

# A COMPREHENSIVE SHARIAH GOVERNANCE FRAMEWORK FOR ISLAMIC EQUITY CROWDFUNDING: A QUALITATIVE ANALYSIS

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## Abstract

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This paper explores the significant role of the Shariah governance framework in Islamic equity crowdfunding. Unlike Islamic financial institutions, the current regulatory requirements for Shariah aspects appear lenient (Haniff et al., 2019). Indeed, the absence of a proper Shariah monitoring process could result in serious issues regarding public trust, the status of funds, and the outcome of crowdfunding practices. This study applies a qualitative method as the data were gathered through semi-structured interviews with several experts, including crowdfunding practitioners, financial institutions, Shariah scholars, and entrepreneurs. It is found that the comprehensive Shariah governance framework is vital in ensuring that all of its activities follow Shariah rulings and principles. The crowdfunding philosophy is already in line with Shariah's spirit in encouraging wealth distribution, improving transparency, and promoting socio-justice. This unique alternative finance could support Islamic finance to the extent that its processes comply with Shariah. In this regard, the study proposes a comprehensive Shariah governance framework for Islamic crowdfunding in Malaysia. Since this study is based on qualitative, its findings may not be able to be generalized. However, it still provides valuable contributions in terms of proposing a practical Shariah governance framework of Islamic crowdfunding in Malaysia.

**Keywords:** Crowdfunding, Islamic Crowdfunding, Shariah Governance

**Authors' individual contribution:** Conceptualization — H.S.R.; Methodology — M.S.I.I.; Investigation — N.S.M.N.; Resources — M.S.I.I.; Writing — H.S.R.; Supervision — M.S.I.I.; Funding Acquisition — M.S.I.I.

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## 1. INTRODUCTION

Despite worldwide recognition, modern Islamic finance is criticized by some parties that it does not contribute enough to socioeconomic development. As a result, this so-called alternative finance is identical to its conventional counterpart (Marzban et al., 2014). Islamic financial institutions are claimed to prioritize high-net-worth individuals and large-scale companies rather than assisting the poor and micro businesses. Nevertheless, many efforts have been promoted to ensure Islamic financial institutions to re-orient its objective, one of them by introducing value-based intermediation (VBI). VBI, provided by Bank Negara Malaysia (BNM), serves as a guideline for Islamic financial institutions to realize the outcome of Shariah in their practices by initiating a positive and sustainable impact on the economy, society, and environment (BNM, 2018).

While modern financial institutions, including Islamic institutions, are still far from significantly supporting socioeconomic development, crowdfunding seems to be a new hope. To begin with, crowdfunding acts as a platform to link society and project initiators. It operates based on a fundraising concept and has been widely recognized as alternative finance to support start-up businesses, micro-enterprises, and welfare-based projects over the period. Unlike investors or depositors in banking institutions, funders in crowdfunding directly channel their money to the project launched in a crowdfunding platform, so they are aware of any project they support. Another fact to mention, crowdfunding is designed in various forms of donation, reward, equity, and lending. Thus, it becomes more community-based support rather than profit orientation (Wahjono et al., 2017).

Regardless of their model, all crowdfunding practices must comply with the Shariah rulings and its principles to attract Muslims. In more detail, the funding projects must be *halal* (permissible) in terms of their status, as well as financial instruments offered must be Shariah compliant. In general, donation-based and reward-based crowdfunding may not pose any serious Shariah issues (Saiti et al., 2018). Nonetheless, some equity and lending crowdfunding instruments must be improved to avoid *riba* (interest) (Hendratmi et al., 2019). Thus, a special body is needed to monitor the Shariah aspects since any practice against them could significantly affect public confidence among Muslims. The case of sukuk sales dropped 50%, and their prices fell at an average of 1.51% in 2008 could prove this point. Despite the fact that many factors are blamed for this drop, it was believed that the main one was because of the statement issued by a popular Muslim scholar, Muhammad Taqi Usmani (as cited in Ahmad & Ishak, 2020), that the majority of sukuk in the Gulf countries are non-Shariah compliant.

Unlike Islamic financial institutions that are strictly monitored by the BNM, the crowdfunding industry is more lenient. For example, in terms of the Shariah monitoring process, there was no specific requirement for Islamic equity crowdfunding platforms to appoint Shariah advisors, which makes their power, if appointed, less authoritative (Haniff et al., 2019). Meanwhile, some platforms, for example, Ata Plus, are not formally

registered as Shariah compliant platform but prefers to declare that it is a Muslim-focused crowdfunding platform that actively supports Shariah compliant businesses (Hasan, 2021). Even though the crowdfunding philosophy is in line with the spirit of Shariah in terms of promoting wealth distribution, encouraging transparency, and supporting socio-justice, it may result in different outcomes due to the absence of a proper Shariah governance entity. In other words, a project run could possibly involve non-Shariah elements that could threaten the status of the fund. For example, a project that supports the charity of lesbian, gay, bisexual, and transgender (LGBT) groups or non-*halal* businesses based on non-*halal* items like alcohol or pork.

In this regard, this paper aims to propose a comprehensive framework of Shariah governance for Islamic equity crowdfunding in Malaysia. Since this is a qualitative study, the data is based on literature and semi-structured interviews. The former includes articles, theses, books, and non-academic materials like internet websites. However, since literature related to Islamic crowdfunding may be limited in regards to this study, data from semi-structured interviews with Shariah experts and crowdfunding practitioners are adequate to explore the issue and propose a special framework of Shariah governance for Islamic crowdfunding in Malaysia.

The structure of this paper is organized as follows. The introduction is presented in Section 1, which is followed by the concept of Islamic crowdfunding and Shariah governance in Section 2. In Section 3, the research methodology that applied in this study is explained while its findings are presented in Section 4. As for Section 5, it provides a special discussion on the findings, before Section 6 comes up with the conclusion.

## 2. LITERATURE REVIEW

### 2.1. Islamic crowdfunding: An overview

Crowdfunding is designed to link society and the project so the project can be funded by the society through fundraising. This unique practice has been widely recognized as alternative finance to support start-up businesses, small and mid-size enterprises (SMEs), and welfare-based projects. Its root could be the practice of micro-finance and crowdsourcing (Kit, 2021). Since crowdfunding is designed in the form of donation, reward, equity, and lending, it is more community-based support rather than profit orientation (Hervé & Schwienbacher, 2018).

In this regard, crowdfunding can be categorized into non-financial return forms, for example, donation-based crowdfunding, in which a funder donates his/her money without expecting anything in return (Jamaludin et al., 2020). Another example would be reward-based crowdfunding which is a part of the donation, except project initiators would provide special gifts for their funders as a token of appreciation or reward (Wan Mohamad Nazarie & Williams, 2021). The second category is financial return-based crowdfunding which includes lending and equity based. The lending-based crowdfunding, sometimes, is referred to as peer-to-peer (P2P) lending, operates

based on credit contracts. In the end, funders would receive their money back with interest or without interest, depending on the platform (Aderemi & Ishak, 2023). While equity-based crowdfunding is in the form of investment based on specified terms in the campaign whereby funders or investors obtain a percentage of ownership and future earnings from the project, but also high risks (Moritz et al., 2015).

From the Shariah perspective, crowdfunding activities generally seem to be in line with its spirit. In more detail, crowdfunding supports the so-called *maqasid al-Shariah* (objective of Shariah) in terms of encouraging wealth distribution, promoting transparency, and supporting socio justice. However, any practise of Shariah requires to compliance not only in terms of its objective but also with its technical rulings (Ishak et al., 2022). Firstly, all crowdfunding, regardless of their model, must not support any project that is against Shariah, such as non-*halal* businesses. In terms of instruments, while two crowdfunding models: donation based and reward-based, may have no Shariah concerns, equity-based and lending-based need to be revised to ensure that they are free from *riba* (interest), *gharar* (uncertainty) and *maisir* (gambling) (Ishak & Rahman, 2021). Alternatively, many Shariah compliant contracts can be implemented as crowdfunding instruments as the following:

**Table 1.** Crowdfunding models and their alternative Islamic contract

<i>Crowdfunding model</i>	<i>Shariah-compliant contract</i>	<i>The nature of instruments</i>
Donation based crowdfunding	<i>Sadaqah</i> <i>Infaq</i> <i>Zakat</i> <i>Waqf</i>	Charity
Reward-based crowdfunding	<i>Hibah</i>	Charity
Lending-based or debt-based crowdfunding	<i>Murabahah</i> <i>Tawaruq</i> <i>Qard Hassan</i>	Loan and sale
Equity-based crowdfunding	<i>Mudharabah</i> <i>Musharakah</i>	Investment

Sources: Author's compilation.

According to Table 1, many Shariah-compliant contracts can be utilized as crowdfunding instruments regardless of their models. As for donation and reward-based crowdfunding, *sadaqah* and *infaq* can be adopted with the condition that both the fund and the project must be *halal*. Nevertheless, as for *zakat* and *waqf*, despite the fact that they are part of charitable instruments, both have special technical rulings that must be considered before they can be applied as crowdfunding instruments (Khairuddin & Ishak, 2023). For example, *zakat* has its own fixed beneficiaries, while the application of *waqf* must ensure its original fund must remain perpetual. As for equity and lending crowdfunding instruments, they must ensure free from *riba* (Hendratmi et al., 2019). Thus, contracts like *mudharabah* and *musharakah* can be a practical alternative for equity-based crowdfunding instruments (Jamaluddin et al., 2022; Ishak & Rahman, 2021). Meanwhile, *Qard Hassan* can be adopted as a lending instrument (Aderemi & Ishak, 2023).

In regard to Malaysia, crowdfunding has become a new part of the financial sector as well as

charitable activities. Equity-based crowdfunding and lending-based crowdfunding, known as P2P lending, are recognized as alternative financing instruments for entrepreneurs. Several popular platforms, such as Ethis.co, Ata Plus, Pitchin, and Fandaztic are regulated by the Securities Commission Malaysia (SC, 2015). Meanwhile, for charitable activities, several crowdfunding platforms are run by non-government organizations (NGOs) like *kitabantu* or social enterprises like *kitafund*. In addition, due to the introduction of VBI, several donation-based crowdfunding platforms have been established by Islamic banks. For instance, Jariah Fund (Bank Muamalat Malaysia Berhad), Maybankheart (Maybank), Sadaqah House (Bank Islam Malaysia Berhad), and MyWakaf (Association of Islamic Banking and Financial Institutions Malaysia) encourage Islamic financial institutions to actively support the needs of the society (Eldersevi & Muhammad, 2021).

In terms of Shariah compliant, there is no special regulation for donation, and reward-based crowdfunding, except it, must be noted that in Malaysia, *zakat* and *waqf* are exclusively administrated under the State Islamic Religious Council (SIRC) (Kamaruddin & Hanefah, 2021). As for equity-based crowdfunding, Ethis.co is the only platform in Malaysia that declares its Shariah status. It is headquartered in Singapore, and its investment platforms have received regulatory approval in Malaysia, Indonesia, and Dubai. Ethis.co is widely regarded as the world's first investment Islamic crowdfunding platform, and SC Malaysia granted it the first Malaysia Shariah-compliant equity crowdfunding license in 2020 (Faudzi et al., 2021). As a result, Islamic crowdfunding in Malaysia is vital to sustaining the momentum of the Shariah-compliant industries (Ramli et al., 2022).

## 2.2. The Malaysian legal system for equity crowdfunding

Since 1982, it has been commonly known that Malaysians have actively participated in community-based fundraising, directly or indirectly. This country is claimed to be the first country in the Association of Southeast Asian Nations (ASEAN) area (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam) that enact a special law and regulatory framework regarding public crowdfunding (Cheah, 2015).

The SC issued the Guideline on Recognised Markets (GRM) SC-GL/6-2015 (R10-2023) on December 11, 2015. This guideline recognizes a particular market as an alternate trading venue, marketplace, or facility connecting sellers and purchasers. It has been claimed that this guideline that serves as a regulatory framework facilitates equity crowdfunding which went into effect on May 2, 2016 (Ramli et al., 2022). In addition, GRM is issued by the SC according to section 377 of the Capital Markets and Services Act 2007 (CMSA), read together with subdivision 4, division 2 of Part II CMSA (SC Malaysia, 2015).

Furthermore, SC amended its crowdfunding program in 2019 by creating the Malaysia Co-Investment Fund (MyCIF), which incorporates equity and lending crowdfunding. As for now,

Malaysia has been recorded to allow the operation of nine equity crowdfunding platforms and ten lending-based crowdfunding platforms (Kamaruddin et al., 2023). Under the MyCIF initiative, the Malaysian government has already reserved RM180 million for co-investment with private investors on both equity and lending crowdfunding platforms. More than RM357 million has been invested through over 16,000 crowdfunding campaigns, benefiting 2280 micro, small and medium-sized enterprises (MSMEs) in Malaysia. Besides, private investors have contributed more than RM1.36 billion in total.

GRM consists of eleven parts, further divided into chapters. These guidelines provide the requirements for registering a person as the recognized market operator (RMO) for equity crowdfunding and others (Ramli et al., 2022). The four salient features of the guideline are as follows:

1. Requirements for platform operators' registration.
2. Requirements for reporting and disclosure.
3. Requirements for Shariah compliance.
4. Anti-money laundering.

It can be learned that the current regulatory require every registered Islamic crowdfunding to ensure Shariah compliance in its operation. Thus, it is necessary to establish Shariah governance in its practice to ensure all activities would be monitored in terms of Shariah compliance. As a conclusion, this country seems to be seriously promoting the development of equity-based crowdfunding including Islamic crowdfunding as an alternative viable finance by facilitating its legal and regulatory requirement.

### 2.3. Shariah governance and its requirement for Islamic financial institutions

Shariah governance can be broadly defined as the structure and the process applied by Islamic financial institutions to ensure their operations comply with Shariah rulings and its principles. According to the Islamic Financial Services Board (IFSB, 2009), Shariah governance reflects the set of an institutional arrangement whereby Islamic financial institutions must ensure an effective independent oversight of Shariah compliance in terms of issuing relevant Shariah pronouncements, dissemination of information, and an internal Shariah compliance review. Thus, Shariah governance represents a comprehensive framework including specific roles and responsibilities for management, and Shariah supervisory board independently oversees the whole financial activities that must be carried out (Karbhari et al., 2020).

In 2009, IFSB introduced a special guideline for industry-related Shariah governance for Islamic institutions. This includes ensuring Shariah governance system processes are proportionate, complex, and natural to the business. Thus, the Shariah supervisory board must be well-defined regarding the procedures, reports, and reviews. Moreover, they must be competent in terms of reasonable expertise, proper criteria, professional development, and performance in overseeing the Shariah governance system through a formal assessment (IFSB, 2009).

Islamic banking industry has experienced a dramatic growth in the recent period, as its revenues and assets have significantly increased because of the demand, especially after the global financial crisis (Awwad, 2018). In regard with Malaysia, since the first establishment of Islamic banking institutions in 1983, this country has experienced rapid progress in the Islamic finance industry (Ishak, 2019). As a result, it is claimed to be one of the major Islamic countries that have developed a Shariah governance framework (Kayadibi & Güçlü, 2021). The most recent framework is Shariah Governance Policy Document (SGPD) 2019 issued by BNM on September 19, 2019, which is widely recognized as the most comprehensive guideline for Shariah governance (Ahmad & Ishak, 2021). The key components of SGPD 2019 are categorized into six: 1) the board of directors (BOD), 2) the SC, senior management, 3) the control function, 4) Shariah compliance, 5) culture and remuneration, transparency, and 6) disclosure. Moreover, the SGPD 2019 has strengthened the oversight of the board, Shariah supervisory board, and senior management's accountability (Kamaruddin et al., 2020).

Nevertheless, this development is only limited to Islamic banking sectors and the Takaful industry. As for the non-banking financial sector, it is still left behind in this aspect. This includes Tabung Haji (saving fund), Islamic cooperatives, the Employees Provident Fund (EPF), and the Rahn industry. However, it is found that Islamic non-banking financial institutions have applied Shariah governance within their limited mandate, especially in appointing Shariah committees as well as internal Shariah functions for the sake of monitoring the Shariah aspect in their activities. Therefore, it is argued that non-banking sectors may not urgently and necessarily need a standard Shariah governance framework since they have different functions and roles (Ahmad & Ishak, 2021).

Likewise, as for the crowdfunding industry, especially equity-based crowdfunding, which is a part of non-banking financial sectors, its Shariah requirement is lenient. For example, in terms of the Shariah monitoring process, there was no specific requirement for crowdfunding platforms to appoint Shariah advisors, which makes their power, if appointed, less authoritative (Haniff et al., 2019). Therefore, this study aims to explore issues related to Shariah governance in Islamic equity crowdfunding before a special framework can be proposed for this sector.

## 3. METHODOLOGY

### 3.1. Research design

A qualitative research design is a social science research technique that focuses on gathering information through open-ended, informative, and conversational communication. As a consequence, it varies depending on the method used in any study, such as participant observation, depth interviews, and focus groups (Opdenakker, 2006). The primary goal of using a qualitative research design is to gain a richly detailed understanding of a specific issue, topic, or experience related to the study. For example, this study aims to explore issues

related to Shariah governance in crowdfunding before a special framework can be proposed. In this regard, the qualitative research design becomes a preferred method for the initial development model, which includes a critical review and confirmation (Legewie, 2013).

### 3.2. Data collection

Interviews are one of the most important sources for qualitative studies. This study applies semi-structured interviews to obtain the data. In fact, semi-structured interviews are effective for identifying previously unknown qualitative themes and issues, as well as for exploring new areas of study interest and delivering all of the information

studies require. This could be used to confirm previously collected data, and the interview method is a popular data collection tool that has been used in a number of social movement research projects (Rahman, 2019).

Therefore, based on their positions and knowledge, this study has selected interviewees who have knowledge regarding Islamic crowdfunding platforms in Malaysia either as practitioners or experts. The first group represents the main crowdfunding platforms in Malaysia, followed by the Shariah experts in fintech for the second group, who have a background in Shariah and experience in Islamic crowdfunding. The interviewees are listed in Table 2.

**Table 2.** List of interviewees

<i>Participant</i>	<i>Position</i>	<i>Category</i>	<i>Purpose</i>
Interviewee 1 (IV1)	Shariah department	Practitioner	To provide necessary information related Islamic crowdfunding industry.
Interviewee 2 (IV2)	CEO	Practitioner	To provide necessary information related Islamic crowdfunding industry.
Interviewee 3 (IV3)	Shariah expert	Expert	To share experience and knowledge of Islamic financial industries and Shariah governance information.
Interviewee 4 (IV4)	Shariah committee	Expert	To provide expertise in Shariah knowledge and focusing on the Shariah advisory sector.
Interviewee 5 (IV5)	Shariah expert	Practitioner/expert	To share experience and knowledge of Islamic financial industries and Shariah governance information.
Interviewee 6 (IV6)	Board of director	Practitioner	To share experience and necessary information related Islamic crowdfunding industry and Shariah governance information.
Interviewee 7 (IV7)	Shariah consultant	Expert	To provide necessary information related Islamic crowdfunding industry and Shariah governance information.

### 3.3. Data analysis

During the interview process, permission from all interviewees is requested to record their words, in which the salient information was cited in handwritten notes to avoid any misinterpretation to avoid unintentional errors, alongside ensuring the validity and reliability of this study. All facts mentioned by the interviewees were confirmed. Prior to the interview, to ensure that all interviewees were well-prepared, a copy of the questions was submitted a week earlier. Each question is standardised for the sake of the reliability of this study. Following that, the transcription and data gathered would be analysed using the thematic method, which allows researchers to segment, precise, review, as well as restructuring the data into key concepts. This study adopts the six steps of thematic data analysis as suggested by Braun and Clarke (2006). These include familiarising with the data, generating the initial codes, searching for themes, reviewing the themes, defining and naming the themes and writing up the report.

### 3.4. Alternative research method

The objective of this study can also be achieved through focus group discussion (FGD) research method in which it is a part of qualitative analysis. Since this study proposes Shariah governance model, it can be presented in front of expert panels through FGD to obtain their feedback. Nevertheless, FGD requires time and cost to gather all participants. Moreover, since this study is an exploratory study,

semi-structured interview could be the practical method for this stage.

## 4. RESEARCH FINDINGS

Based on the data analysis, this study presents several themes in Table 3. All interviewees were asked for their opinions and thoughts regarding the Islamic crowdfunding industry in Malaysia as well as the need for a Shariah governance framework for these industry players. The findings are divided into three themes as the following:

**Table 3.** List of themes

<i>No.</i>	<i>Theme</i>
1	A bright future for Islamic crowdfunding.
2	Shariah governance is vital in terms of public confidence.
3	The flexibility of Shariah governance.

### 4.1. A bright future for Islamic crowdfunding

All interviewees showed a positive response to a new trend of Islamic crowdfunding in Malaysia. From the industry perspective, IV1, IV2, and IV3 agreed that this unique fundraising could be an alternative source of funds for start-ups like micro-enterprises and NGOs. Through crowdfunding, it enables project owners to fundraise by pooling their money either for business profit or social projects. As mentioned by IV1:

*"The understanding trend of Islamic crowdfunding upsurged. Basically, according to SC Malaysia statistics, the Islamic financial industry is on*

the rise, and one of the main reasons is that the Malaysian government has been matching funding for crowdfunding platforms since last year, which has boosted the Islamic financial industry” (personal communication, January 4, 2022).

The progress of Islamic crowdfunding became better when the SC introduced the GRM SC-GL/6-2015 (R10-2023). This guideline enables the equity crowdfunding industry to grow, especially in the good governance aspect. The effort from SC has allowed Islamic crowdfunding to expand vibrantly in parallel with the digital adoption in fintech, where Malaysia recorded the highest number in ASEAN after Singapore in 2016 (Organisation for Economic Co-operation and Development [OECD], 2020).

In terms of non-financial return crowdfunding, the majority of social projects, such as community social responsibilities (CSR) based projects, have utilized the instrument of crowdfunding as a tool for fundraising campaigns to attract potential funders. IV2 emphasized that digitalization has transformed the crowd into a smart and simple way to donate:

*“This digitalization process in Islamic crowdfunding means that access is widespread, and anyone can click to donate. Also, definitely, yes, it will continue to grow faster”* (personal communication, January 6, 2022).

At the same time, good copywriting is among the factors to attract prospects, as it can influence the funders’ emotions and ultimately make prospects interested in funding. In promoting a crowdfunding project, copywriting plays a crucial part for people to understand about the project in terms of its benefits (Sheriff et al., 2018). IV3 added that the copywriting contributes strength in promoting a campaign that has a potential target of a huge amount:

*“When the proposal of the project comes with good copywriting and the campaign is explicit with the manifest, the rate for fund success is higher. Effectively the funders will attract, which is a good insight for the project enhancement”* (personal communication, February 4, 2022).

Nevertheless, the majority of interviewees are concerned about the positive trend of this industry and the risk of undertaking it. There are extensive precautions that need to be preserved as this industry is ultimately growing faster than the regulatory framework, and the highlight of blockchain technology is still vigorous enough to look somewhat ahead. As mentioned by IV2:

*“We can say it has very good potential and goes beyond the rules. Our platform is currently running on donation crowdfunding, but I can address the risk. Maybe it will be more complicated, or other parties will trust it more because the blockchain has this system in which the contract is more transparent and has higher security”* (personal communication, January 6, 2022).

Hence, the application of blockchain technology indicates a new chapter to reach respected funders by raising money through an online platform in the future. Moreover, their positive potential to reduce administrative and legal complexities could support a project’s cause, which helps entrepreneurs and start-up businesses gain capital globally. This surely enhanced the bright future of the Islamic crowdfunding industry.

#### 4.2. Shariah governance is vital for monitoring and public confidence

Based on semi-structured interviews, it is crucial to provide comprehensive Shariah governance in this industry in order to eliminate all the assumptions and unethical issues regarding the Shariah aspects of public trust in terms of the status of funds and the outcome of crowdfunding practices. IV4, IV5, IV6, as well as IV1, shared their thoughts when Islamic crowdfunding was recognized as having comprehensive Shariah governance. It was assumed this might assure the most success and profit. On the bright side, Islamic crowdfunding appreciates the value of customer trust and credibility, as stressed by IV4:

*“Shariah governance is indeed required because if we want to operate an Islamic product without proper Shariah governance, it may become apparent later in the product’s operation that it is not Shariah compliant, posing a trust risk among the public”* (personal communication, January 5, 2022).

According to the statement, the issues of operating process, inefficiency as well as fraud may be at risk, which could lead to a negative perspective among the funders. However, most of these responsibilities must be accomplished with strong Shariah governance that will provide a good solution to meet the objectives set in the project. Afterwards, the fundraisers have the potential to avoid any Shariah issues by taking the initiative to practice the Shariah guidelines discussed.

IV5 shared his interesting point that the needs of Shariah governance for Islamic crowdfunding should be provided not only for equity but also for the donation to be considered:

*“The importance of Shariah governance is crucial because crowdfunding has many divisions, such as donation, investment, new project development, or CSR, each with its own purpose. For example, investment, whether it is mudharabah or musharakah, should see profit as the main basis. On the other hand, donation crowdfunding also should maintain the transparency of collections from any fraud”* (personal communication, June 16, 2022).

At the same time, the originality of Islamic crowdfunding is similar to the Islamic financial philosophy, which is in line with the Shariah spirit to promote wealth distribution, encourage transparency as well as support socio justice (Ramli & Ishak, 2022). Therefore, the effort to regulate must begin with a proper Shariah governance framework, as Islamic financial institutions in Malaysia are needed due to the nature of their function as financial intermediaries. IV6 stressed:

*“Shariah governance is where you govern the whole institution in a good manner, followed by the Shariah guidelines that the regulator provided. For example, all Islamic financial institutions’ activities must be in line with the Shariah principle. Plus, in the meantime, for risk management it is important to look up the view from a broader perspective such as Shariah audit, Shariah review and Shariah risk management. In this context, Islamic crowdfunding needs its own Shariah governance as an Islamic financial institution as well”* (personal communication, June 9, 2022).

It is noted that Shariah governance is the formalization of how Islamic financial institutions (IFIs) implement the Shariah

requirements set by the regulator. It is a subjective reference based on the Malaysian situation and may be different from other countries. Nevertheless, the representative agreed that the standardization of Shariah government frameworks, such as in IFIs, will increase the potential in the Islamic crowdfunding industry, whether for social or commercial projects.

Public confidence is one of the most critical issues in crowdfunding, where successful participation in online marketplaces and trust is essential. Fundraisers in crowdfunding attempt to gain the trust of potential supporters so that they will contribute to their projects. IV1 stated:

*“In doing charity, there needs to be additional trust because even in Malaysia, we know every now and then that there is corruption. We are very concerned about this, so when it comes to crowdfunding, it’s all about giving more information and transferring information so that the investor and donors have more trust”* (personal communication, January 4, 2022).

It is a subjective reference based on the Malaysian situation and may be different from other countries. Nevertheless, the representative agreed that the standardization of Shariah government frameworks, such as in IFIs, will increase the potential in the Islamic crowdfunding industry, whether for social or commercial projects. Public confidence is one of the most critical issues in crowdfunding, where successful more updates that can be provided, the more funders will be compatible. In order to boost public confidence, all agreements and transactions must be carried out honestly and transparently (Khairuddin & Ishak, 2023). Additionally, institutions encouraging them to help should be a sign of financially empowering the project initiator. Moreover, with comprehensive monitoring from a proactive regulator and periodic campaign awareness to build trust, it could make Islamic crowdfunding accessible for all, especially for those who face financial constraints.

### 4.3. The flexibility of Shariah governance

According to the important part, Shariah governance is a set of core principles for ensuring Shariah compliance through the Islamic crowdfunding structure. Hence, the issuance must follow the specific requirements of the Shariah standard to appropriate the originality of *halal* income. IV1 stated:

*“When it comes to ensuring halal income, a Shariah governance framework is required. What I can share, there must be a Shariah advisory for the issuer because the Shariah screening is initial”* (personal communication, January 4, 2022).

The data show that among those who agreed with the proposal for this institution, there is some flexibility in Shariah governance which emphasizes the issue of transparency for universal benefit. IV3 stated:

*“Shariah governance in the initial phase wants to control donations or equity so that there is no fraud in managing the project through purpose, for example: crowdfunding for society. Enactment about donations already exists through religious councils. Perhaps Shariah governance can refer to religious councils to see the crowdfunding donation structure that has been released again in the case of equity crowdfunding. This is because the element of*

*transparency in crowdfunding is the most important to avoid any annoyance because equity and transactions (muamalat) use customary contracts that require the consent of the public”* (personal communication, February 4, 2022).

Nevertheless, both representatives disagreed with the idea of the Shariah governance framework for Islamic crowdfunding because it gives sluggish growth to the development of an industry that is just getting started in search of economic stability. IV2 stressed:

*“If we want well-regulated Shariah governance, on one hand, it looks disciplined and faster in management. On the other hand, over-regulation will slow down innovation in Islamic finance, so if there is a lot of regulation, then it will be difficult for the development process and space”* (personal communication, January 6, 2022).

In this regard, IV7 supported it, which will drag the innovation of Islamic crowdfunding while other countries will grow the market even faster as follows:

*“I don’t see the need for governance to regulate the beginning process because being more lenient will accelerate the growth of this industry. As we can see, the size of the market is still new, in which, we need more collaboration to expand the understanding and participation in Islamic crowdfunding”* (personal communication, January 7, 2022).

It might be a flexible Shariah governance framework for Islamic crowdfunding for those who agree and disagree. Nevertheless, the structure and content of governance in organisations vary among nations and are a reflection of the institutional context (Arslan et al. 2019). Still, there is a positive reason to be confident while proposing the comprehensive Shariah governance framework for Islamic crowdfunding is crucial. From the interview data above, it is clear that the purpose is to support more conducive and proactive progress in Islamic financial industries. Furthermore, among other satisfactory consequences, this Shariah governance will help in nurturing a society of general cultural and economic reliability as well as well-being in a specific community.

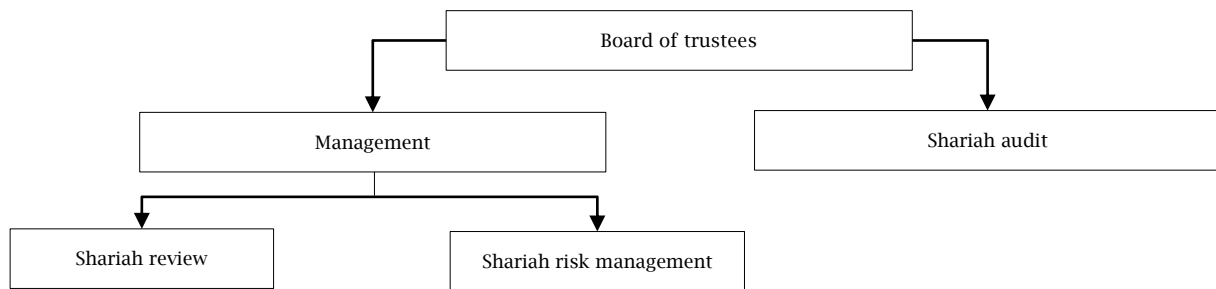
## 5. DISCUSSION

Islamic crowdfunding must ensure a project from the beginning until the end is in line with Shariah. In addition, another aspect needs to be considered, including the potential of fraud, project sustainability, or any risk of loss undertaken in the future.

In this regard, a Shariah governance framework for Islamic crowdfunding in Malaysia is proposed, which comprises an entire structure, process, and other aspects of Shariah governance. This seems in line with the progress of crowdfunding in Malaysia, whereby this industry is expected to become another part of the Islamic financial system that will benefit society (Hilmy & Hassan, 2019).

While there are four types of crowdfunding, this study focuses on equity crowdfunding, in which there are many potential Shariah issues in comparison to other models. Therefore, the structure Shariah governance framework for Islamic equity crowdfunding can be proposed as follows:

**Figure 1.** The structure of Shariah governance framework for Islamic equity crowdfunding



Source: Authors' compilation.

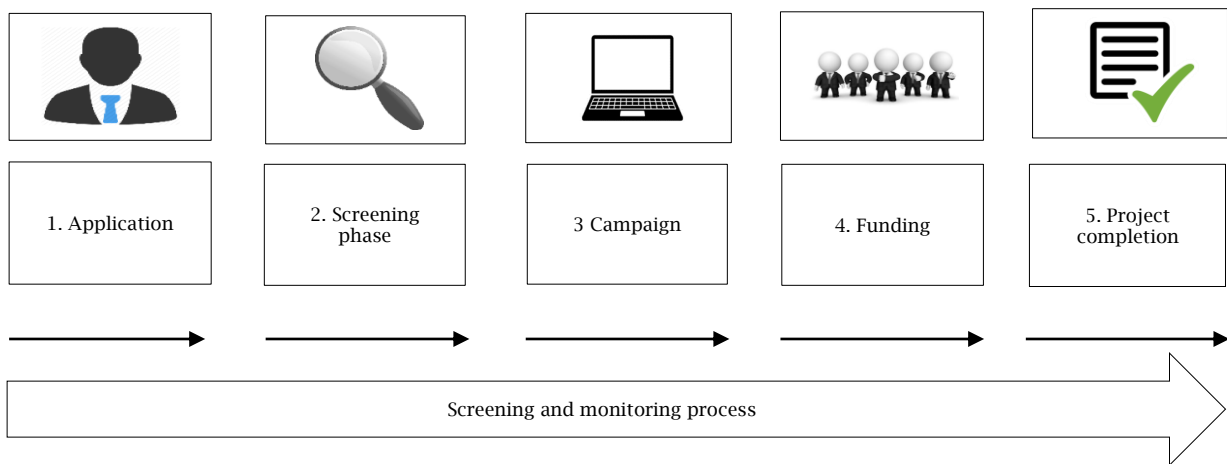
Figure 1 illustrates the structure of the Shariah governance framework proposed for Islamic equity crowdfunding operators as it can be explained as the following:

1. *Board of trustees* plays a role in supporting Shariah compliance in crowdfunding operations through Shariah review, Shariah risk management, as well as Shariah audit.
2. *Shariah review* ensures operation and structures of investment are compliant with Shariah principles.
3. *Shariah risk management* mitigates the element of Shariah non-compliance risk that may be faced from the beginning to the end of the project.
4. A special function that provides an independent *Shariah audit* is needed. Thus, a Shariah audit is suggested, either internal or

external, in screening and auditing the crowdfunding project to ensure it is in line with Shariah.

Even though it is crucial for any Islamic equity crowdfunding platform to provide a proper structure of Shariah governance framework as proposed, this industry is still new and needs flexibility to grow. Therefore, it is suggested not to require the platform with a strict structure like other Islamic financial institutions. As far as there are screening processes for Shariah review, Shariah risk management and Shariah audit, it is sufficient for the time being. At the same time, it is strongly recommended for the platforms to provide Shariah screening and monitoring process for the sake of trust among all involving parties. Hence, the process of Shariah-compliant screening and monitoring can be illustrated as follows:

**Figure 2.** Screening and monitoring process



Source: Authors' compilation.

**Explanation:**

1. *Application*. The project initiator would apply for funding through the crowdfunding platform. He/she must provide a proposal for the project to be evaluated. The background of the project initiator must be screened to ensure he/she never involves in controversial and illegal activities.
2. The pre-campaign *screening* is conducted to ensure the eligibility of the project. The project must adhere to Shariah, which must be free from the elements of prohibition and fraud, as well as it should consider ethics. The project must not engage in selling pork, alcohol, tobacco, gambling, betting, conventional banks, LGBT groups, and non-Shariah

compliant advertising and media. At the same time, the manner of the campaign should be in line with ethics, which expects it to be clean without any element of fraud, trick, or manipulation. In this regard, Shariah management, including Shariah review and Shariah risk, would play their roles.

3. Once the first screening phase is approved, the *campaign* is launched. The project initiator must aggressively promote his/her project to attract investors or funders. This process would be monitored by Shariah review management to ensure it is in line with Shariah and ethics.

4. If the campaign is successful, the platform provider will channel the *fund* to the project



initiator. In this stage, Shariah management would play its role to ensure the project is carried out in line with Shariah.

5. Once the *project is completed*, the profit generated will be distributed in the form of a dividend to the funders, depending on the structure of the investment. The process also must be monitored by Shariah management.

Islamic crowdfunding is typically independent and challenging to locate due to its genuine and pure intentions of giving. However, the next generation of Islamic financial institutions must introduce and investigate crowdfunding elements that could provide more benefits and profit in the future (Wahjono et al., 2017). Islamic crowdfunding may be perceived as a replacement for traditional funding provided by banks, finance companies, private equity, and venture capital. Still, it can also serve as a supplement that allows others to benefit from its value. Adopting a unique standard would unquestionably encourage responsibility, openness, disclosure, and impartiality which is closer to the spirit of Islam (Muneeza & Hassan, 2014). After all, a comprehensive Shariah governance is critical to emphasising and obtaining the blessing hereafter for every component, thereby making Islamic finance relevant in the world.

## 6. CONCLUSION

The objective of this research is to develop a comprehensive Shariah governance framework for Islamic equity crowdfunding in Malaysia. Crowdfunding has gained widespread acceptance as a viable alternative fund for entrepreneurs to launch their early-stage businesses. Crowdfunding has evolved into a mechanism for pooling resources from person to person without the use of financial intermediaries due to the rapid global development of the internet. As a result, Islamic crowdfunding has the potential to be one of the most significant game changers in the financial industry in terms of assisting beneficiaries. Given that the Islamic crowdfunding philosophy already promotes wealth

distribution, encourages transparency, and supports socio justice, this alternative finance could intrinsically support Islamic finance as its practices are Shariah compliant.

The comprehensive Shariah governance framework for Islamic crowdfunding may be of great assistance to any Islamic crowdfunding users in reaching out to the potential in their industries. This Shariah governance framework and Shariah screening timeline will provide a better standard and salient mark to embed generalisation in Islamic crowdfunding practices. Moreover, one of the strengths of Islamic financial institutions is the evolving presence of Shariah teams in the industry. The strength would be used for Shariah matters in order for the Islamic crowdfunding industries to comply with Shariah principles at all times. Nevertheless, the effort towards a Shariah workforce can interact with more Muslim participants and can be used to leverage the effectiveness of Islamic crowdfunding. This study found that it is essential to develop a comprehensive Shariah governance framework for Islamic crowdfunding to ensure that all of its activities adhere to Shariah rulings and principles. This includes forming Shariah review, Shariah audit, and Shariah risk management committees.

Despite the fact that Islamic crowdfunding is not a new research topic, empirical studies in this area are still limited, particularly qualitative approaches. In addition, this study contributes to proposing a comprehensive Shariah governance framework for Islamic equity crowdfunding in Malaysia. More specifically, without a proper Shariah governance framework, it could lead to different outcomes, in which the project may include non-Shariah elements that could endanger the fund's status. At the same time, future studies are crucially needed to broaden this topic, either through quantitative research or mixed-method research approaches. In addition, it is recommended to conduct case studies method on this topic by selecting the case of Asia, Europe, or Middle Eastern countries.

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