

# Development and perspectives of ethical finance in Iran

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*Abstract*— Iran has a rich and old tradition of ethical finance and economics. Well before the Islamic Revolution, institutes and initiatives were active in encouraging an inclusive vision of economy. Although re-elaborated under a different light, these concepts survived in the current Constitution, which defines economy using a “social” approach (art.43). Under this light, the legality of capitalism and that of the use of private investment are one of the pillars of economy itself (art.44) only if subordinated to religiously inspired ethical principles of justice and equity and in a way that makes of them a mere complement to State or to the corporative actors. Religious guidance is therefore immanent even in the very own definition of economy as a mean, and not as an end, to get social purposes like, *inter alia*, welfare, elimination of poverty and abolition of deprivation of means of self-sustainment. State-driven economics was nevertheless a prominent concept in original Iranian constitutional thought. Starting from the Nineties, financial and economic reforms have been leading the system from a corporatist vision that characterised the first fifteen years of existence of the Islamic Republic to a more actual social market, putting in discussion and somewhat re-inventing the relationship between the public and the private.

**Keywords:** Iran, Islam, Bonyad, Ethics, Finance, Law.

## I. INTRODUCTION

We can not make a net distinction between the market, that makes up the life of the Companies and constitutes the environment where the business lives, and the general characteristics of the human society hosting and, somewhat, governing that market. Instruments like Corporate Social Responsibility or Health, Safety and Environment are social

tools, extremely important ones to understand the nature of this coexistence given they represent the way the business dialogues, communicates and introduces itself to the public. In the history of modern Iran, we can clearly distinguish two different phases of development of the relationship between business and ethics: that of before the Revolution, and modern revolutionary Iran. In turn, each of these periods may be divided into different phases, with often very different characteristics the one to the others: the first period of the Pahlavi kingdom (first industrialisation) and the period following the economic crisis of the ‘50es by one side; the first decade after the Revolution and the current era, by the other.

A reference has been done to the first period of Pahlavi ruling, an historical moment dating prior to the first samples of ethical finance and of other tools like Corporate Social Responsibility in Western world. That would qualify the experiences of “attention to social issues” belonging to the first half of the 20<sup>th</sup> Century’s Iran as a separate matter. However, we shall not forget that responsibility and ethics in business and finance, as a concept, has lived a continuous process of transformation, and that every specific contest may witness a different experience. Ethics is defined as a systematic approach to moral judgements based on reason, analysis, synthesis, and reflection. In the West, tools like CSR were born as a philanthropic tool in an environment where capitalism, free market and a scarce presence of the State in public life and workers protection. Iran represented (and still represents) a

deeply different context, characterised mainly by Islam, under the light of the Ja'fari doctrine.

Ja'fari Islam is, by a social point of view, an extremely important presence given it makes of business ethics a religious matter, making of ethics an immanent concept in the whole system. We should not forget that Islam overcomes the concept of “faith” as we commonly understand in the Western world, and that it constitutes the very shape of the Law itself [1]. Law, under this light, is not in fact a human product but the manifestation of the will of God. It is, therefore, eternal and not liable to err. Islam is, at the end, the entire system and Islamic legal systems are completely correspondant to it. The Islamic faith is itself a social matter where big attention is given to fairness in contracts, balance between the counterparts, and where a specific attention is given to the wellness of the Community over the wellness of the individual. Finance is, of course, the most significant and meaningful part of business by the point of view of fairness in contracts and lawfulness of transaction, given its very nature of trading services with no provision of material goods.

## II. THE INDUSTRIALISATION: THE BEGINNING OF THE 20<sup>TH</sup> CENTURY

During the time of Reza Shah Pahlavi, Iran witnessed a deep transformation of its society and of its economy. The Iran left him by the Qajars, the House that ruled the Country prior to the Pahlavis and up to 1925, was a rural society mostly unequally distributed in a vast land with few big cities, no linguistic cohesion and even less industrial development [2]. In that moment, the idea of a modern State itself was lacking in Iranian identity. Sophisticated financial activities were absent in Iranian market and almost all of them belonged to the most traditional trade activities, already perfectly regulated by the religious authorities through their interpretation on, and personal effort (*ijtihad*, اجتهاد) in understanding the Law in every single case. Therefore, traditional trading activities (by which almost the entire economy was made up by) was considered conform to religious lawfulness (*halal*, حلال), which made of them “ethical” by definition. That conformity left no possibility to have a further need for a room to be enhanced. The first Parliament (*Majlis*, مجلس) of the Country, created after a constitutional revolution seeking a European-styled development plan for Iran, had to fulfil the most challenging

event for a Country *en route* to a deep transformation: that of the promulgation of a Civil and of a Commercial Code. That happened in 1928, bringing with it the need to regulate and accept into Iranian system some financial institutes and tools coming mainly from the West world, therefore proposing to then Iranian legislator the challenge to consider them licit or not.

Iran took an extremely sophisticated choice while deciding to adopt the Code system while completely adapting it to the Islamic Ja'fari orientation, therefore proposing a “new” model of codification. That model, differently from other Countries of the area, would not choose to print a mere copy of a European legal text, translating it into Persian and adding a Personal Status Code (*ahwal shakhsiyya*) for familiar and personal issues, but would build its entire civil system harmonizing it *in toto* with the Islamic system [3].

With this experience, Iran faces for the first time the ethical dilemma of the lawfulness of adopting financial tools which very origin is unrelated to the islamic world but rather belonging to the Western system.

## III. FINANCE AND ETHICS IN THE IRANIAN CIVIL CODE OF 1928

The very fact that Iran was facing a true revolutionary historical period while adopting the Civil and Commercial Codes was clear since the beginning of the parliamentary debate over the issue. In a famous statement at the Majlis in 1927, the then Representative Dr. Mohammad Mossadegh made clear in front of the Assembly that his being a “Persian and a Muslim” would not let him accept Iran to just absorb a mere translation of a European code and make of it a source of its Law.

In particular, Mossadeq stressed the necessity for his Country to always keep its Islamic foundation, even in moments when the foundation of the Country was “*mistakenly*” identified with “*the concept of modernisation*” itself. Mossadeq, therefore, qualified the modernisation as “false”, stressing the need of not passively accepting it, as it would (to his vision) destroy the Country. A clear stance against a school of thought that would have wanted Iran in the line of those Countries accepting to merely adopt the Western system, but in line with

those underlying the idea of a need to reform welcoming many orientations and ideas of Western origin.

In the first Book of the Code this orientation is made clear while the Legislator addresses the issue of gambling and betting, which are both to be considered not conform to Islam given the well-known prohibition of aleatory enrichment. Therefore, such juristic acts do not find any legitimation in the Law. Art.645 of the Code statutes that gambling and betting are not valid juristic acts, unproductive of effects and for which no legal action shall be admissible. The same norm shall be applied with reference to all obligations produced by illicit juristic acts.

#### IV. THE ISLAMIC REVOLUTION AND THE CURRENT CONSTITUTIONAL ASSET OF ECONOMICS AND FINANCE

The Constitution seeing the light after the Revolution of 1979 gives economics and finance a completely new definition and reads them under the light Islam provides them with. Current Constitution does not actually make any difference between financial activities and pure economic ones, such as trade of goods. Although in Islamic Law fair trade is considered a highly valuable activity in the life of a Muslim (Mohammad used to be a commercial arbiter for a long period of his life), finance presents some difficulties given it is related to production and interchange of services whose value may be determined, in some cases, in an arbitrary way. That is the case of some financial tools, such as derivative obligations, whose output (given market value) may effectively be dependent on factors independent to one's efforts or work and therefore to deserve his own enrichment. That may make of their profit an illicit (haram, حرام) one.

Art.2, 3 and 4 of the Constitution are the main guidance for the exegesis of the Iranian Legal System wishing to study its main sources and constitute the cornerstone of the entire fundamental Chart. Art.2 states that all sources of the law shall be consistent with Islam (*"divine revelation and its fundamental role in setting forth Laws"*), therefore giving it the qualification of a super-constitutional norm. As we read in the preamble of the Constitution itself, *"in the view of Islam, government does not derive from the interests of a class, nor does it serve the domination of an individual or a group. Rather, it represents the fulfilment of the political ideal of a people who bear a common faith and common outlook, taking*

*an organized form in order to initiate the process of intellectual and ideological evolution towards the final goal, i.e., movement towards Allah"*.

After a few lines, the preamble addresses the problem of the qualification of the term "economics" (اقتصاد, eqtesad). It states that while strengthening the foundations of the economy, whose fundamental consideration will be that of fulfilling the material needs of man in the course of his overall growth and development, the new order of the State (which means the Islamic Republic) will fix a principle in contrasts with other economic systems. The aim would be that of the *"concentration and accumulation of wealth and maximization of profit. In materialist schools of thought, the economy represents an end in itself, so that it comes to be a subversive and corrupting factor in the course of man's development. In Islam, the economy is a means, and all that is required of a means is that it should be an efficient factor contributing to the attainment of the ultimate goal"*.

Art.3 of the Constitution recalls what held in the previous one and, while compiling a list of the duties of the State. The twelfth point reports the *"planning of a correct and just economic system, in accordance with Islamic criteria, in order to create welfare, eliminate poverty, and abolish all forms of deprivation with respect to food, housing, work, health care, and the provision of social insurance for all"*.

Art.43 of the Constitution opens the Chapter IV, dedicated to "Economy and financial affairs". It obviously recalls the content of Art.2, considering the vision Islam has of economy and its main objectives and characteristics. The first paragraph puts, as its objectives, *"achieving the economic independence of the society, uprooting poverty and deprivation, and fulfilling human needs in the process of development"*. These objectives are to be reached through very social means and are driven by a social and ethical vision: *"ensuring conditions and opportunities of employment for everyone, with a view to attaining full employment"*. The action of the State is present especially while placing the means of work at the disposal of everyone able to work and lacking the means. The most interesting thing of this article is that it provides the aforementioned means in the form of cooperatives, through granting interest-free loans or *"recourse to any other legitimate means that neither results in the concentration or circulation of wealth in the hands of a few individuals or groups, nor turns*

the government into a major absolute employer". It also states that these steps must be taken with due regard for the requirements governing the general economic planning of the country at each stage of its growth.

A Constitution is not usually required to specify or regulate in detail its provisions, neither to name expressly the institutions that will be called to make those provisions reality. At the moment of the writing of the Constitution, many religious foundations were working in social issues in order to provide the people with an alternative way of development out of Shah's revolutionary means. These foundations were found on one of the very basic principles of Islam as a religious system, that of the cooperation towards the realisation of the Ummah as a perfect human organisation [4].

As a consequence of the Revolution, the entire banking system was turned into a interest-free one, and at the same time a huge reform on capital and financial operators was implemented [5].

## V. BONYAD

*Bonyad* (foundation, بنیاد) is the term that mostly embodies the concept of ethical finance in Iran given it represents the most typical and particular juridical form of a financial actor in the Islamic Republic's legal environment [6][7].

Founded under the revolutionary process of islamization of the entire Imperial Iran's system, bonyads took over the role the Shah had given to institutions such as the Pahlavi Foundation, and their assets were entitled to the Revolutionary Councils all around the Country, keeping them therefore separated from the State's patrimony (*ghanimat* system).

This has constituted the prodromal act of a series of legislative reforms that would implement the actual structure of the Islamic Republic's administration. Sundering the public into two spheres, the one of which would be under the strict control of the religious guidance, somewhat escaping from the classical tools of administrative and financial control by the State, is a juridical instrument in full conformity to the principles of "Guardianship of the Jurisconsult" (*velayat-e faqih*), regulating the constitutional asset of the Islamic Republic [8].

Bonyads therefore enjoy a wider degree of independence and administrative freedom, being free to manage, hold and

constitute business active in almost all possible markets with the exception of the oil one.

By a theoretical and legal point of view, Bonyads shall operate as charity organizations: that would mean, called to address their activities in order to redistribute incomes and not to pursue a profit orientation.

Nevertheless, the specificity of the institution and the fact that Bonyad has become a true *nomen juris* distinguished from the simple concept of non-profit organisation has made of it a reality difficult to measure, to define and to tailor a specific management regime for.

Another important aspect of the Bonyads is that, competing in market against private business, are often blamed on contributing to the insufficient development and transparency of the market itself, impeding an harmonious development of the Country's economy.

Bonyads are not subject to the general accounting laws and are not required to pay taxes, while their actual monetary consistence remains substantially impossible to be defined. Unaccountable to the Central Bank governor as well, there is a lack of proper oversight and control of these foundations.

There is no doubt that the current system has awakened many criticism from inside and outside the Country: a particularly interested eye on the issue has been put by the incumbent Iranian executive, following the steps of the previous reformist Khatami government of the '90es.

A structural reform of the entire Iranian economic law, in light of a long-awaited liberal revolution would help the Country to address in a better way the challenges the Country is facing and to diversify its way of developing a truly wider economy. That may allow an actual opening to modern experiments of ethical finance, today still restricted into the Bonyad system and the provisions of art.3, 43 of the Constitution.

## CONCLUSION

The Ethical Finance in Iran is witnessing the last stage of development started around one hundred years ago: as a Country, Iran always featured very advanced characteristics of social development and attention to the needs of a society in evolution. By the other side, belonging to Ja'fari school made the Country a centre for a "national" school of thought in this sense and the Constitutional provisions of social justice and

protection were, of course, seen as to boost to the development of such a perspective, but the challenge now seems to be that of sustainability. More than being a pure economic issue, we shall now understand how the paradigm of a state-driven economics can coexist with a mixed system of state + market and who is the one who is in charge of that

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