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**The 15th International Conference on
Islamic Economics and Finance (ICIEF 2024):
Driving the Agenda
for a Sustainable Humane Economy**



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Transliteration Table: Consonants

Arabic	Roman		Arabic	Roman
ب	b		ط	ṭ
ت	t		ظ	ẓ
ث	th		ع	‘
ج	j		غ	gh
ح	ḥ		ف	f
خ	kh		ق	q
د	d		ك	k
ذ	dh		ل	l
ر	r		م	m
ز	z		ن	n
س	s		ه	h
ش	sh		و	w
ص	ṣ		ء	’
ض	ḍ		ي	y

Transliteration Table: Vowels and Diphthongs

Arabic	Roman		Arabic	Roman
اَ	a		أَ، آَ، إِيَّ	an
أُ	u		أُوَّ	un
إِ	i		إِيَّ	in
آَ، آِ، إِيَّ،	ā		أُوَّ	aw
أُوَّ	ū		إِيَّ	ay
إِيَّ	ī		أُوَّ	uww, ū (in final position)
			إِيَّ	iyy, ī (in final position)

Source: ROTAS Transliteration Kit: <http://rotas.iium.edu.my>

Social Welfare Provision within an Integrated Three-Sector Economic Framework

Bushra Abu Saïd*
Mohd Nizam Barom**

Abstract: Despite its apparent contributions to social welfare, the third sector is still not properly recognised and integrated into mainstream macroeconomic models and statistics. With the aim of enhancing social welfare in Muslim economies, this article firstly seeks to conceptualise an integrated framework of social welfare provision within a three-sector economy. This article uses an integrative review and synthesis of Western and Islamic literatures on the concept and experience of the third sector and social welfare provision and subsequently presents a modified circular flow model that represents a comprehensive social welfare provision framework that actively involves all economic sectors, including the third sector which is largely neglected in traditional macroeconomic framework. Secondly, this article proposes the establishment of an Islamic Third Sector Commission (ITSC) as a tool to enhance efficiency of resource allocation and social welfare provision. It represents a systematic approach to identify priority areas, assess their needs, and allocate resources accordingly, promoting greater efficiency, transparency, and effectiveness in social welfare provision. In sum, this article offers conceptual framework and practical tools that have the potential to enhance the well-being of individuals and communities, while also promoting collaboration and synergy among economic sectors. This integrated approach accentuates the fundamental values of cooperation, solidarity, and justice which are at the core of Islamic economic principles.

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Keywords: Social welfare provision, Traditional macroeconomic framework, Integrated three-sector economic framework, third sector, Islamic economics.

Abstrak: Walaupun sumbangannya terhadap kebajikan sosial ketara, sektor ketiga masih belum diiktiraf dan disepadukan dengan sewajarnya dalam model dan statistik makroekonomi arus perdana. Dengan tujuan untuk meningkatkan kebajikan sosial dalam ekonomi Muslim, makalah ini pertamanya berhasrat untuk membina satu kerangka kerja bersepadu bagi peruntukan kebajikan sosial dalam ekonomi tiga sektor. Makalah ini menggunakan kaedah kajian integratif dan sintesis terhadap literatur Barat dan Islam berkenaan konsep dan pengalaman sektor ketiga serta peruntukan kebajikan sosial, seterusnya membentangkan model aliran pusingan yang diubahsuai yang mewakili kerangka peruntukan kebajikan sosial yang komprehensif dengan penglibatan aktif semua sektor ekonomi, termasuk sektor ketiga yang sering diabaikan dalam kerangka makroekonomi tradisional. Kedua, kertas ini mencadangkan penubuhan Suruhanjaya Sektor Ketiga Islam (SSTI) sebagai satu alat untuk meningkatkan kecekapan agihan sumber dan peruntukan kebajikan sosial. Ia mewakili satu pendekatan sistematik untuk mengenal pasti bidang keutamaan, menilai keperluannya, dan mengagihkan sumber secara sewajarnya, seterusnya mempromosikan tahap kecekapan, ketelusan dan keberkesanan yang lebih tinggi dalam peruntukan kebajikan sosial. Kesimpulannya, makalah ini menawarkan kerangka konsep dan wahana praktikal yang berpotensi untuk meningkatkan kesejahteraan individu dan komuniti, di samping menggalakkan kolaborasi dan sinergi dalam kalangan sektor ekonomi. Pendekatan bersepadu ini menekankan nilai asas kerjasama, solidariti dan keadilan yang merupakan teras prinsip ekonomi Islam.

Keywords : peruntukan kebajikan sosial, Kerangka ekonomi makro tradisional, Kerangka ekonomi sektor ketiga bersepadu, Sektor ketiga, Ekonomi Islam.

Introduction

In contemporary economics, the public and private sectors command the spotlight, while the third sector often remains in the shadows. Typically, we view the public and private sectors as responsible for producing, consuming, and distributing resources in an economy. The two-sector economic framework, however, has its flaws, leading to challenges in achieving socio-economic goals and sustaining development, both in developed (Kendall & Knapp, 2000; Steinberg, 2006; Weisbrod, 1988) and developing economies (Arshad & Haneef 2016; Molla & Alam,

2013). The public sector is often seen as inefficient, while the private sector can contribute to income inequality and leave certain social needs unmet due to their lack of profitability. Moreover, there's a notable absence of ethical or value considerations in this two-sector economic framework (Arshad & Haneef, 2016; High, 1985; Westall, 2009).

On the other hand, the third sector remains somewhat overlooked. This lack of attention may stem from limited information about its scope and contributions, making it 'invisible' in comparison to the other sectors. The term 'third sector' is often used interchangeably with phrases like 'voluntary sector,' 'non-profit sector,' 'charitable sector,' the 'community sector,' the 'philanthropic sector,' the 'intermediary sector,' the 'citizen sector,' the 'civil society,' the 'social economy,' or even simply the 'third way.' It includes a wide array of institutions like NGOs, charities, cooperatives, and social enterprises, among others. In the Islamic context, it also encompasses practices like *zakāt*, *ṣadaqah*, and *waqf*.

Despite its importance in social welfare provision, the third sector is often seen in isolation, and its potential is not fully realised. One reason is the misconception that it competes with the public sector (Evans & Shields, 2000). Furthermore, it has been largely viewed as a traditional charity sector, rather than an active participant in the economy. Legal and organisational challenges further complicate its integration into modern economic frameworks (Salamon, 2010). For instance, depending on the nature of third sector organisations (TSOs) and their sources of support, TSOs are often categorised in national statistics and accounts under the private or public sectors or even the household sector (Salamon, 2010), especially since there are many complex hybrid organisations that overlap between economic sectors. Non-profits, for instance, are categorised under the private sector, acting as social welfare organisations correcting market imperfections, while the public sector regulates and balances income flows in the economy in the form of redistributive measures and social protection. Consequently, the third sector is not recognised as a distinct sector, and its balance of flows and interaction with other sectors are not depicted in mainstream macroeconomic model. Recognising and including the third sector within income flow models has become increasingly important due to the significant flow of income and non-monetary social welfare resources flowing through the third sector to benefit society.

From an Islamic viewpoint, the third sector naturally aligns with Islamic principles, values, and objectives (Alterman & Hunter, 2006; Salih, 2002; Zaenal & Ismail, 2014). It has a rich history of social and economic contributions. Resources from the third sector play a significant role in promoting social welfare in various sectors such as supporting the poor, education, health care, water, and other public amenities (Hamdani et al., 2004). However, it has waned over time as the state and the private sector took precedence (Bremer, 2004; Bikmen, 2008). In recent times, it is making a comeback, but its role and scope vary across regions. Unfortunately, despite the strong emphasis on the social welfare concept within Islam, the social welfare systems in Muslim societies lag behind their Western counterparts. Instead, they often exhibit characteristics inconsistent with Islamic precepts such as 'adversary' relationships and weak partnerships between the third and other sectors of the economy (OIC Outlook Series, 2014). Considering the historical significance, the status given by Islam, and the inherent role of third-sector activities in Islamic economic systems, questions about its role, status, and relevance in contemporary Islamic economies arise.

It is apparent that the third sector, both in Western and Islamic contexts, play an essential role in social welfare provision. This raises questions about how the third sector fits into the economy alongside the public and private sectors, especially considering the considerable resources it handles. Why is it not represented as a distinct sector in the mainstream macroeconomic framework such as the circular income flow model? How do welfare resources, in the form of income, goods and services, circulate through the economy? This article aims to delve into these questions and explore the intricate interactions between sectors in the context of social welfare provision, shedding light on the often overlooked but crucial role of the third sector.

Numerous studies have emphasised the limitations of the traditional two-sector economic model, highlighting its inability to sustain socio-economic development without the integration of a well-established third sector (Weisbrod, 1988; Dollery & Wallis, 2002; Molla & Alam, 2013; Arshad & Haneef, 2016). The third sector is seen as a crucial player capable of complementing the public and private sectors and addressing the shortcomings of the standard two-sector economy. Since the sector has so far been regarded as a side player without proper

institutionalisation, studies like Kolin (2009) call for the need for an integrative system with all three sectors of the economy participating under the welfare system. The concern of inadequate resource distribution and mobilisation through the third sector has also been observed as one of the major drawbacks of contemporary third-sector practices, both in the Western sphere in relation to third-sector failures (Salamon, 1987) and in Muslim societies who face ineffective allocation of philanthropy among welfare sectors (GIFR, 2012; Ismail & Shaikh, 2017). This acts as a hindrance to enhancing the sector's potential and sustaining better social welfare provision in an economy. Hence, a three-sector economy including the third sector offers the potential for a more efficient allocation of resources (Ahmed et al., 1983). Formalising the third sector can also open opportunities for greater sustainability and fundamental economic objectives, addressing the ethical and value components often overlooked in the current two-sector economic framework.

This article, therefore, addresses a critical gap, aiming to understand how the third sector can be effectively integrated with other sectors to enhance overall social welfare provision. It explores the interaction of the third sector with the public and private sectors in social welfare provision particularly in an Islamic economic context, proposing an integrated framework of social welfare provision within a three-sector economy. This integrated three-sector economic framework essentialises the emphasis of Islam on the concept of cooperation, shared responsibility, and solidarity in pursuing the Islamic economic objectives of establishing socioeconomic justice and overall human well-being.

To achieve this objective, sections two and three survey the concept and experience of social welfare provision from the Western and Islamic perspectives respectively. Subsequently, section four presents a framework that describes the interactions among different economic sectors to facilitate social welfare provision. This framework introduces a modified circular flow of income, explaining and illustrating the movement of social welfare income transfers and the exchange of goods and services within an integrated three-sector setting. Furthermore, it offers a comprehensive insight into the intricate relationships between these economic sectors. It also proposes the establishment of an Islamic Third Sector Commission (ITSC) for the efficient allocation of third-

sector resources and overall social welfare provision in an Islamic economy. The final section, section five, concludes the article and discusses some implications of the study.

The Western Social Welfare Concept and Experience

In Western literature, the concept of social welfare stands as a fundamental pillar of a just and united society. Social welfare, in its broadest sense, encompasses the well-being and interests of individuals within a society. It extends beyond merely meeting individual wants, as it considers socially defined needs and common interests, which may sometimes conflict or require individuals to bear costs for the benefit of others (Spicker, 2013). It therefore encompasses a systematic framework of policies, programmes, and institutions designed to assist individuals and groups in achieving satisfactory standards of life and health. Essentially, it aims to tackle the multitude of problems in society and provide support to disadvantaged segments of the population who face various barriers, including physical, mental, economic, and social challenges, preventing them from accessing societal services (Bharadwaj, 2015).

Social welfare thus encompasses a broad spectrum of services aimed at diverse groups, including children, youth, women, the elderly, scheduled castes, scheduled tribes, other backward classes, minorities, disabled individuals, drug addicts, and the economically underprivileged, including destitute and unemployed individuals. Effective social welfare programmes require competent administration to enhance well-being and achieve societal objectives. These objectives include addressing individual needs, promoting personal development, and providing a safety net against uncertainties such as old age, disability, or poverty (Bharadwaj, 2015; Spicker, 2013).

Welfare provision across different economic sectors has evolved over time. Historically, the non-state sectors—market, voluntary, and informal sectors—played the main role in social well-being. However, in the post-World War period, welfare states emerged, and the public sector took on a more prominent role, such as in countries like the UK and Australia (Wright, Marston & McDonald, 2011). For instance, Australia today employs a mixed welfare economy with the third sector as the primary welfare source, supported by various entities including the state, local governments, private market organisations, and informal

groups. The share in welfare contributions varies among different states, with some led by the public sector and others by private and voluntary sectors. This reflects a mixed welfare economy approach, recognising that no single sector can solely address social welfare challenges, prompting consideration of a three-sector solution. (Butcher, 2017; Ghilchrist & Butcher, 2016).

Similarly, Europe exhibits a mixed welfare economic system, where the state, third-sector organisations (TSOs), local municipalities, private volunteer work, and community philanthropy contribute to social well-being (Evers and Laville, 2004). This has given rise to a welfare-mixed economy, recognising the plurality of resources contributing to social welfare (Evers and Laville, 2004).

As sectors intertwine and decentralise services, hybrid organisations have emerged, bridging sectoral boundaries (Evers, 2004). Defourney & Pestoff (2014) emphasise the third sector's complementary role in basic welfare provision, highlighting hybrid organisations that overlap sectors. These hybrids, including mutual aid organisations, informal self-help groups, cooperatives, quasi-public organisations, and third sector-government partnerships, play pivotal roles in social welfare.

Salamon (1987) accentuates that the increased partnerships between the third and public sectors in welfare service provision are one of the driving influences of the evolution of the modern welfare state. Collaboration between the public and third sectors is essential, and it benefits both. Governments provide resources more consistently and ensure they are more equitably distributed, while the third sector specialises in providing welfare services tailored to the needs of society (Salamon, 1987). The third sector also contains a rich resource of volunteers and financial donations which can be maximised through the support of the public sector (Feiock & Andrew, 2006). The collaborative model between the public and third sector can be found worldwide, including the US (third-party government), the UK (third-sector compact with the government), Germany and Scandinavian countries (third-sector subsidiary relationship with the government) (Young, 2000; Gilchrist & Butcher, 2010). According to Anheier (2002), the most advanced third sectors today can be found in these very countries whose third sectors formed a complementary relationship with their governments.

In fact, there has been a shift from public sector dominance to a closer partnership with the third sector, responsible for a significant portion of welfare services (Third Sector, 2005). Such partnerships have proven beneficial, resulting in cost-efficiency, trusted services, flexibility, sustainability, skill development, and improved societal welfare (Butcher, 2017; Productivity Commission, 2010).

According to Bridge et al. (2009), there are four primary sources of funding for the third or welfare sector; commercial sources (including equity finance, bank loans, venture capital, and stocks), private sources (involving TSO founders, individuals, and corporations), earned income (from goods and services, fees, and dues), and special sources (such as personal fundraisings, donations, grants, and endowments). The public sector plays a predominant role in social welfare services in most European countries, particularly in the Western region such as Netherlands, Ireland, and Belgium which boasts some of the world's largest third sectors (Salamon et al., 1999). In Canada as well, public sector transfers are the primary income source for the charitable sector, followed by earned income, with households and businesses providing a smaller share (Emmett and Emmett, 2015).

Conversely, the US primarily depends on commercial sources and private philanthropy contributions (donations and earned income (fees and dues)), with additional support from government funding, grants, and contracts (Bridge et al., 2009). Earned income is also a dominant source of social welfare provision in other parts of the world like Australia, Japan, Latin America, and Central and Eastern Europe (Salamon et al., 1999). In the UK, welfare services rely predominantly on individual private contributions, followed by government welfare funds (NCVO, 2015).

Regarding specific welfare sectors in the US, education, healthcare, and human services rely heavily on earned income (fees), while arts, culture, and environmental welfare depend on private donations (Sherlock and Gravelle, 2009). Government support, though varying in extent, is particularly concentrated in fields like health, education, and social services. Private philanthropy, from both corporations and households, is important but seldom the primary source of welfare funding in most regions. Exceptions include international aid welfare

and religious congregations, where significant private donations are prevalent (Salamon et al., 1999).

Reflecting on the experience of social welfare practices highlighted above reveals the apparent variations in welfare systems according to the way the three different sectors interact and which sector has a prevalence in the provision of social welfare. Regardless of these potential variations, it is clearly seen that a closer partnership between the public and the private sector with the third sector can only lead to better provision of social welfare for the population.

Social Welfare in an Islamic Economy

Social Welfare is undoubtedly a fundamental part of an Islamic economy, starting with the individual, family, society, and then the Ummah as a whole. From the Islamic stance, ideally all the main economic sectors—the state, market, household, and third sector—converge to create what can be termed “an economy devoted to welfare.” This socio-economic order aims to foster a welfare-oriented society where these sectors harmoniously complement one another, thereby enhancing the performance of welfare provision across all sectors.

While the Western social welfare remains morally neutral, rooted in capitalist or socialist ideologies, and founded on principles of social solidarity, the concept of social welfare in Islamic economics is firmly grounded in an Islamic moral philosophy that integrates spiritual and material well-being. Recognising the central roles played by all economic sectors in social welfare provision, this section provides a concise overview of the Islamic perspective on social welfare, outlining how each sector shares that responsibility as well as the experiences of social welfare in practice.

Akhtar (1995) posits that the government plays a key role in providing social welfare in collaboration with the market and non-market sectors while voluntary organisations remain the most significant source of public welfare goods and services. Siddiqi (1991) emphasises the voluntary sector’s role in facilitating income transfers to impoverished households, as well as directly delivering private welfare goods and services to those in need. The family and community sectors, often considered part of the voluntary sector, actively engage in various informal activities and income transfers. Wealth transfers,

both obligatory and voluntary, within immediate and extended family structures, are considered a crucial part of social welfare systems and are identified as being much more extensive in Muslim societies than experienced in their Western counterparts (Mannan, n.d.).

Scholars like Faridi (1983), Ariff (1991), and Siddiqi (1991) highlight the critical roles of all sectors in an economy, particularly in allocation, distribution, and stabilisation – crucial aspects of effective social welfare provision. In terms of allocation, an Islamic economy adheres to a mix of resource allocation among the public, private, and voluntary (including the informal sector) sectors based on social norms and Islamic values. The public sector plays the role of rectifying resource allocation problems by educating and informing society of the needs of its disadvantaged or poor people, expanding its resources as needed, and determining the distribution of *zakāt*, *ṣadaqah* and other wealth transfers. It effectively redistributes income with the help of the voluntary sector. It also provides direct social welfare services and supports other welfare programmes in the economy. At the same time, it regulates and mitigates conflicts between sectors for the social well-being of society. The voluntary sector supplements social welfare resources and services as per the needs of the community with the informal household sector being significantly involved in contributions to the third sector and its welfare services. The distribution function entails the transfer of resources and wealth from higher-income groups to lower-income segments of society.

Current resources of social welfare provision are shared among economic sectors in various ways. For instance, *zakaat* collection and distribution may primarily fall under the purview of the public sector, as seen in Pakistan, Sudan, and Malaysia, or under the community or voluntary sector, as observed in Morocco, Jordan, and Oman (Hasan, 2007). *Zakāt*-based transfers are considered foundational for social welfare, serving as the primary redistribution tool, whether administered by the government or the private voluntary sector. Dogarawa (2008) emphasises the role of *zakāt* within the family system as a sustainable and enduring mechanism for wealth transfer, forming the bedrock of social welfare accomplishments. Chapra (1979) highlights *zakāt* as a primary income source in an Islamic welfare state. Additionally, the sectors collectively perform a stabilising function, eliminating destabilising elements in the economy, with *zakāt* itself acting as a natural fiscal

stabiliser. This function strives to remove any impediments to social welfare and ensure overall societal well-being.

After the decline of the third sector during the Ottoman era, the public sector assumed much of the social welfare provision, with limited roles played by the private and voluntary sectors. However, in recent decades, the transition from authoritarian regimes to more democratic governance in Muslim nations, influenced by a blend of historical, modern, and international practices, has led to a shift in welfare provision from the public to the private sector (Bremer, 2004). Presently, it is common to find a mix of democratic and autocratic governance influencing welfare provision, with countries like Turkey, Indonesia, Bangladesh, Malaysia, Jordan, and Morocco embracing increasingly democratic regimes.

Nevertheless, in many Muslim countries, there remains a noticeable gap compared to developed Western nations in terms of robust collaboration between the third sector and the public sector. While the harmonious relationship observed between these sectors in various Western regions aligns with the Islamic concept of a social welfare system, it is not as widely applied or embraced in Muslim societies. On the contrary, several OIC (Organisation of Islamic Cooperation) countries exhibit an “adversary” relationship between these sectors, sometimes even rivalling each other (OIC Outlook, 2014). The OIC report on civil society concludes that instead of fostering the growth and institutionalisation of the third sector by creating a conducive environment, some governments hinder their third sectors due to concerns about loss of power, political corruption, policy abuse, and limited tolerance for civil society authorities. The extent of conflict between sectors in social welfare provision varies among different OIC countries, with marked disparities between nations. Those regions with smaller third sectors, resulting from poor intersectoral interactions, have much to learn from other Muslim countries with more robust third sectors established through collaborative relationships, as well as from exemplary Western societies that have excelled in social welfare provision.

Interaction of Sectors in Social Welfare Provision

This section explains the intricate interactions inherent to an Islamic economy, where a distinct third sector plays an important role in the provision of social welfare. Given the substantial magnitude of welfare

resources—comprising funds, goods, and services—that flow to the third sector and around the economy through all economic sectors, this study presents a model depicting the flow of income and the exchange of goods and services, for the purpose of societal well-being. It identifies the sources of welfare and the intersectoral interactions that facilitate the realisation of social welfare. It finally presents a holistic framework wherein all economic sectors seamlessly interact within the context of a three-sector economy.

A Modified Model of the Circular Flow of Income in an Economy

This section proposes a basic model that illustrates the interplay of the third sector with other sectors within an economy, facilitating the movement of welfare goods and services. The model depicts the balance of welfare income transfers and welfare goods as the major exchanges and flows in an economy. It is relevant because firstly, it adequately depicts the flow of welfare provision within an economy. Secondly, it recognises the interdependent relationship between the sectors and between economic exchanges as there can be no social welfare goods and services without sources of social welfare provision. Lastly, like the conventional circular flow of income model, it portrays the perpetual nature of the social welfare system through the continual flow of wealth and goods in an economy from a social welfare economic context.

Figure 1 offers a modified depiction of the circular flow of income model, showcasing the sources of social welfare and their movement within an economy featuring a distinct third sector. In a typical economy, formal sectors include the public, private, and third sectors, while the informal sector comprises households. The most significant source of welfare emanates from factor income payments—wages, rents, and profits—that the private sector disburses to households in exchange for factor inputs, including land, labour, capital, and entrepreneurship. For the majority of society, the primary source of social welfare is derived from income earnings and subsequent consumption in resource and product markets, either directly as earners or indirectly through family members' earnings. Consequently, the private (market) sector serves as the largest source of welfare provision within an economy.

Within the household sector, income earnings serve diverse welfare purposes. The higher-income group (rich) extends welfare support (depicted by the red downward arrow) to the lower-income group

(poor) through direct wealth transfers (donations, gifts, *sadaqah*) or informal charitable services and volunteer work. Social welfare within this sector may also encompass community-wide initiatives, societal groups, or informal activities conducted within family structures, such as free tuition classes and community security efforts. The household sector also constitutes the primary source of welfare provision for the third sector within an economy. It provides wealth transfers, donations, goods, and services, as well as non-monetary contributions in the form of time and effort, to pure TSOs such as traditional charitable organisations, orphanages, elderly care homes, and refugee organisations. In the Islamic context, pure TSOs also include *zakāt* or *waqf* institutions.

The private sector (firms) indirectly contributes to the third sector by providing factor income payments to the household sector, which then channels wealth transfers and welfare services to the third sector, as previously described. Furthermore, the private sector directly offers private income transfers such as sponsorships and welfare services in the form of free goods and services or Corporate Social Responsibility (CSR) initiatives for pure TSOs. At the same time, the private sector directly extends private income transfers and welfare goods and services to the household sector, which may manifest as CSR activities benefiting entire communities or voluntary aid targeting specific societal groups. Private contributions also include the time and effort dedicated to social welfare purposes. Lastly, the private sector pays taxes to the public sector, which are crucial for financing public goods, welfare services, and public transfers and grants to the household and third sector organisations.

The public sector (government) serves as another key source of welfare provision for both the household and third sectors. It directly channels welfare goods and services to the informal household sector, either catering to entire communities (e.g., healthcare, education, defence) or specifically focusing on lower-income groups. Moreover, the public sector provides direct transfer payments (e.g., social security, and social welfare programs) to lower-income or disadvantaged groups (e.g., impoverished individuals, single mothers, widows) within the household sector. The public sector is also responsible for extending income transfers and social welfare goods and services directly to pure TSOs in the third sector. Public welfare provision is facilitated through

the collection of resources from taxes and charitable contributions sourced from the household and private sectors.

Finally, the third sector, at the centre of the diagram, is a significant source of welfare provision and well-being, both for pure TSOs within it and for the household sector. Pure TSOs directly transfer income to the lower-income group (poor) in the household sector (as indicated by the red arrow in Figure 1). They also provide goods and services to the entire household sector or specific target groups. Pure TSOs within the third sector receive transfer funds and welfare services from all sectors of the economy—public, private, and household.

Additionally, each sector in the economy—private, public, and household—comprises hybrid TSOs that are major sources of social welfare provision. These organisations overlap with the third sector due to their shared social welfare objectives, thus making them part of the third sector of the economy. For example, social enterprises, cooperatives, and community or ethical-based financial institutions straddle the line between the private and third sectors. Similarly, various other organisations may find themselves at the intersection of the public and third sector or between the informal household and third sector. Irrespective of their placement, all these organisations, directly or indirectly, contribute to social welfare within this integrated three-sector economy, either by extending income transfers and welfare goods to the third sector or directly to underprivileged individuals in the household sector.

Among the myriad sectors of social welfare in society, key areas that receive income transfers and welfare goods from all sectors include education, health, food/clothing, shelter/housing, disaster relief, social care, childcare/orphanages, elderly care, counselling and domestic support, religious organisations, and environment/animal protection. Often, the public sector directs the bulk of welfare support toward fulfilling basic needs (education, health, food, shelter, human services) and increasingly collaborates with the third sector in delivering social welfare services. Meanwhile, private philanthropy from the third and household sectors usually contributes more to social care, disaster relief, counselling, environmental conservation, and religious organisations. International aid (not included in the model) also plays an important role in welfare support in some countries, particularly for disaster aid, social care, and basic human services.

The diagram does not show all the flows as typically found in traditional circular flow of income models. For example, it excludes household sector expenditures on goods and services from the private sector (domestic and abroad), factor inputs from households to businesses, or public subsidies, goods and services received by the market from the government. The purpose is to simplify the diagram, as the objective is to solely focus on the movement of social welfare provision around the economy.

The Framework of Interaction in a Three-Sector Economy

Within a three-sector Islamic economic framework, all sectors collaborate towards the realisation of Islamic economic goals by fostering a conducive and sustainable environment rooted in principles of brotherhood, cooperation, and solidarity. These sectors operate within the rules of the game of Islam – the framework of Islamic principles drawn from the divine sources of the Qur'an and Sunnah. Acknowledging the substantial value and benefits offered by the third sector, both the public and private sectors demonstrate their support through resource contributions. This support can take the form of direct assistance, such as grants, sponsorships, and in-kind resources, or indirect support, like tax concessions and environmentally friendly practices. While each sector independently allocates resources, they also complement one another, with the third sector playing a central role in resource reallocation across the economy, primarily through its numerous social welfare organisations and activities, as depicted in Figure 2.

The household sector predominantly serves as the primary source of volunteers and philanthropists for the third sector. It further contributes by alleviating the third sector's burden through individual and collective social welfare activities and environmentally friendly behaviours. Given that the majority of resources in the economy stem from the household sector—serving as the primary source of labour, clients, and customers for the public and private sectors—these sectors may find themselves in competition for household resources. As the principal resource provider, the household sector significantly influences the overall economic landscape or the 'natural environment' and the function of the third sector particularly through its informal family and community institutions.

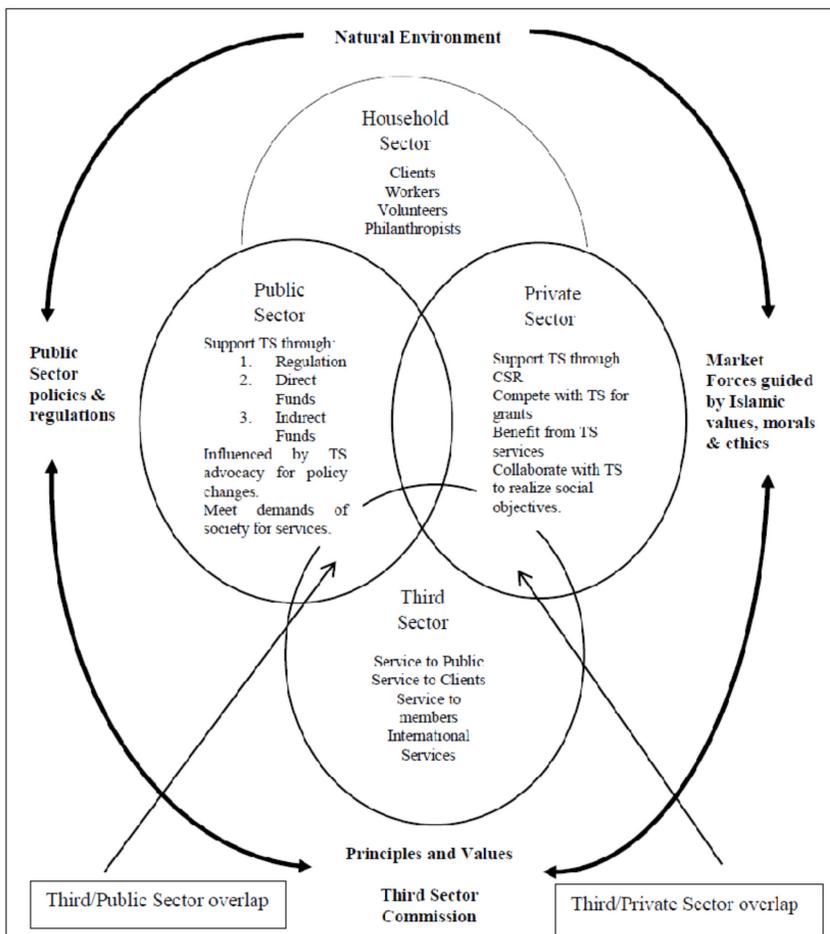


Figure 2, which has been adapted from the Productivity Commission Report (2010), illustrates the interplay among the public, private, household, and third sectors within a collaborative socio-economic framework. These sectors operate under the guidance of various principles: market dynamics, values, and practices rooted in Islamic ethics and morals; regulations from the public sector; policies defined by the state; the cultural values of the third sector and civil society; and the presence of a Third Sector Commission. This collaborative environment is a product of a complex blend of historical, cultural, religious, political, and economic factors, collectively referred to as the natural environment. These factors have the potential to undergo changes, thus influencing the overall socio-economic landscape.

Figure 2: Interactions between Third Public, Private and Household Sectors

The public sector, guided by state legislation and policies based on an Islamic legal and judicial system, assumes the role of overseeing and creating a well-regulated environment. It not only directly funds the third sector but also encourages other sectors to contribute to social welfare by offering tax incentives or concessions. The public sector also fulfils its customary governmental roles, including providing essential public facilities and welfare services, ensuring the satisfaction of basic needs for all citizens, and redistributing funds, wealth, and resources throughout the economy. Overall, it monitors the welfare of all sectors, ensuring their security, stability, and cooperation, intervening when necessary, in cases of deficiencies, shortcomings, or violations of codes of conduct, and maintaining equilibrium between all sectors, individuals, and society.

The private sector, guided by market rules, values, and practices rooted in Islamic values, morals, and ethics, strives to minimise market imperfections and inefficiencies. In doing so, it lightens the burden on the third sector and advances social welfare by adhering to socially responsible behaviour. This includes avoiding practices like interest (*ribā*) and profiteering, supporting CSR initiatives, participating in fundraising projects, and providing low-cost services for the underprivileged. Furthermore, the private sector increasingly intersects with the third sector by establishing cooperatives, social enterprises, and other for-profit social organisations, thereby blurring the lines between these two sectors.

The third sector does not exist merely to fill the gaps left by the public and private sectors but operates in harmony with them while maintaining its autonomy. This reflects the concept of an “inherent social compact that exists in a country” (Productivity Commission, 2010, p.24). The size, scope, and role of the third sector are influenced by the socio-economic environment, as well as the level of cooperation, competition, and complementarity among economic sectors. It is also influenced by the societal demands for TSOs and activities that the third sector can efficiently provide while facing competition for obtaining resources and providing services. To regulate the third sector effectively, maintain codes of conduct among TSOs, and document the activities and institutions within the third sector in each country, the establishment of a ‘third sector commission’ is advisable.

Hybrid organisations within the third sector that overlap with other sectors constitute a crucial component of the third sector. These organisations operate under market rules and conditions or state regulations while aligning with some of the principles and objectives of a TSO. Organisations heavily funded by the government may fall into the ‘public-third sector overlap’ category, while those that operate similarly to private entities but with a clear social benefit focus fall under the ‘private-third sector overlap.’ Regardless of their characteristics, their ultimate aim is to enhance community well-being. These hybrid TSOs play an increasingly significant role in socio-economic development in the modern era. Depending on the collaborative socio-economic environment, some areas may have more of these ‘hybrid’ TSOs than others.

Proposition of an Islamic Third Sector Commission (ITSC)

The establishment of a national, independent third-sector governing body is imperative within the framework of a three-sector economy. This authoritative body would be responsible for overseeing and regulating standard operating procedures through the development of a comprehensive code of conduct and regulatory framework. Such an entity is essential to ensure transparency and optimise the performance of the third sector. Proposed as the Islamic Third Sector Commission (ITSC), this body would produce annual reports detailing the performance, impacts, objectives, and other critical information about the country’s third sector, making it accessible to the public. This transparency initiative is expected to raise awareness of the sector, encourage the establishment of more TSOs, foster enhanced collaboration among economic sectors in social welfare provision, promote community involvement, and stimulate increased volunteering and contributions to the sector. Moreover, it would serve as a valuable source of information for the government and policymakers.

The ITSC would undertake several key roles, including but not limited to:

1. **Registration:** The commission would facilitate the formal registration of all TSOs, capturing essential organisation features such as objectives, social welfare goals, funding sources, service allocation targets, and potential areas of contribution. This information would be recorded in a national registrar.

2. **Evaluation:** The ITSC would be responsible for assessing the contributions of TSOs in terms of resources, activities, direct welfare costs and benefits, and long-term implications. It would gauge the extent to which a country's socio-economic goals are being achieved. To conduct evaluations effectively, the commission would develop a standardised evaluation framework and collect relevant data from TSOs. Additionally, it may establish reward schemes to incentivise organisational growth and improve performance through both monetary (funds) and non-monetary (awards) support.
3. **Regulation:** In its regulatory capacity, the ITSC would ensure TSOs adhere to the code of conduct established for the third sector. It would monitor and prevent cases of over-funding, underfunding, or any form of discriminatory behaviour that favours or discriminates against certain segments of society. The commission would also verify the credibility of registered TSOs, ensuring they genuinely pursue social objectives rather than engaging in fraudulent activities to exploit tax exemptions, grants, or sponsorships. Overall, its role would be to safeguard the sector against corrupt practices and act against deviations from social objectives.
4. **Allocation:** The ITSC would play a critical role in optimising resource distribution. After identifying priority areas requiring third-sector resources, services, and social welfare transfers, the commission would inform TSOs and other economic sectors, guiding them in the allocation of their resources to targeted welfare sectors. This is expected to enhance efficiency, credibility, and transparency.
5. **Intermediation:** Serving as a bridge between the third sector and other sectors, particularly the government, the ITSC would play a crucial role. This role is especially significant in countries where the government provides substantial funding to the third sector and engages in partnerships with the public sector. The commission would collaborate with the government to direct welfare resources to critical areas of society and promote the establishment of additional TSOs.

6. Identification of Barriers: The ITSC may also be tasked with identifying barriers that hinder the effective operation of the third sector. These barriers could be legal, financial, cultural, or of other types. Once identified, the commission would work in collaboration with the government and other sectors to overcome these barriers. For example, in some countries, legal requirements for registering formal organisations may be challenging to meet, resources may be inequitably distributed among welfare sectors due to a lack of information on priority zones, or shortages of funds may impede organisational operations. Additionally, a lack of awareness or cultural norms may limit citizen involvement in volunteering and contributing to TSOs. The ITSC's role in identifying and addressing such unique barriers would be crucial in strengthening and expanding the third sector.

Conclusion and Implications

This article has highlighted the essential position of the third sector within an integrated three-sector economic framework of an Islamic economy, specifically focusing on social welfare provision. It presents a modified income flow model within an integrated three-sector economy that demonstrates social welfare provision in terms of the flows of income and goods and services. The article illustrates the complementary relationship of sectors in a collaborative socio-economic environment within the social welfare provision model that actively involves all sectors, including the third sector which is largely neglected in the traditional macroeconomic framework. The establishment of an Islamic Third Sector Commission (ITSC) is proposed as an important component of this framework. The ITSC serves as an authoritative body overseeing TSOs, ensuring compliance with codes of conduct, and fostering collaboration among sectors.

The article emphasises the interdependence of economic sectors, emphasising the need for enhanced coordination and collaboration among public, private, and third sectors to create a more effective social welfare system. This can inspire innovative approaches to social welfare programs and initiatives, identifying new ways to leverage the interactions between sectors. Increased public awareness of the complexity and significance of all sectors for social welfare provision

can lead to greater support and participation in welfare initiatives, expanding their reach and impact. By understanding how resources flow between sectors, policymakers can make more effective decisions to ensure resources are optimally distributed for maximum societal impact.

The article recognises the significant influence of the household sector in the economic landscape, informing policies to harness its potential for societal well-being. It underlines the role of the public sector in creating a well-regulated environment and encouraging resource contributions to social welfare, emphasising the importance of aligning policies with Islamic legal principles. It also highlights the private sector's responsibility to advance social welfare through ethical business practices, promoting ethical and sustainable economic operations. The article can thus serve to encourage Islamic banks and financial institutions to strengthen their social responsibility roles, optimise resource allocation, seek collaboration opportunities, and advocate for regulatory structures that support their involvement in social welfare provision within an integrated three-sector economy.

Most importantly, the article stresses the critical role of the third sector in resource reallocation and acknowledges the evolving nature of the third sector, with organisations overlapping multiple sectors, reflecting the changing socio-economic landscape. Policymakers and researchers might want to adapt to this shift and acknowledge these hybrid organisations' contributions. Additionally, the proposal for a 'third sector commission' offers a significant policy recommendation that can enhance the third sector's efficiency and accountability.

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(ii) indirect quotation, write as Qur'ān, 30:36

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Ḥadīth

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(i) Al-Bukhārī, 88:204 (where 88 is the book number, 204 is the ḥadīth number)

(ii) Ibn Hanbal, vol. 1, p. 1

Reference:

(i) Al-Bukhārī, M. (1981). *Ṣaḥīḥ al-Bukhārī*. Beirut: Dār al-Fikr.

(ii) Ibn Ḥanbal, A. (1982). *Musnad Aḥmad Ibn Ḥanbal*. Istanbul: Cagri Yayinlari.

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