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Research Article

Sharia-Compliant Investment Funds in the U.S. Market: Navigating SEC Regulations and Ethical Finance Demands

Jessica Anderson [1], William Lee [2], Jennifer Taylor [3]
[1] Yale University, United States
[2] University of Chicago, United States
[3] Princeton University, United States

Corresponding Author:

Jessica Anderson,
Yale University, United States
New Haven, CT 06520, United States
Email: jessicaanderson@gmail.com

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Abstract
The rising demand for ethical and faith-based investment products in the United States has prompted increased interest in Sharia-compliant investment funds. These funds seek to align financial returns with Islamic principles, including the prohibition of interest (riba), avoidance of excessive uncertainty (gharar), and investment in halal sectors. However, integrating such models within the U.S. financial system presents regulatory challenges, particularly under the oversight of the Securities and Exchange Commission (SEC). This study examines how Sharia-compliant investment funds navigate U.S. regulatory frameworks while maintaining theological legitimacy and investor confidence. Utilizing a qualitative legal research methodology, the study analyzes SEC rules on mutual funds and ETFs, including disclosure, diversification, and fiduciary obligations, alongside Shariah governance standards issued by AAOIFI and other global Islamic finance authorities. Interviews with fund managers, legal counsel, and Shariah advisors provide practical insights. Findings indicate that although structural compatibility is possible, regulatory ambiguities around Shariah governance, purification processes, and ethical screening create operational tensions. The study concludes that successful integration requires interpretive flexibility, SEC engagement, and investor education to ensure both compliance and religious authenticity. The research contributes to broader discussions on financial inclusion, ethical finance, and legal pluralism in global markets.

Keywords: Islamic Finance, Shariah-Compliant Funds, SEC Regulations

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INTRODUCTION

Ethical investing has seen remarkable growth in global financial markets over the past two decades, particularly through the expansion of Environmental, Social, and Governance (ESG) investment models (Hamzah dkk., 2023; Siddiky dkk., 2024). In the United States, a country with one of the most sophisticated financial regulatory regimes, investors are increasingly motivated by non-financial considerations such as religious, environmental, or moral values. This shift has created a niche for faith-based investment vehicles, including those that comply with Islamic principles.

Sharia-compliant investment funds represent a subset of faith-driven portfolios designed to meet the financial needs of Muslim investors while adhering to Islamic legal and ethical norms (Raza, Said, dkk., 2023; Thippayana & Thinnam, 2023). These include avoiding investments in industries deemed haram (forbidden), such as alcohol, gambling, and interest-bearing financial institutions, and incorporating processes like income purification and ethical screening. With over 3.5 million Muslims residing in the United States, demand for financial products aligned with Islamic values is growing steadily.

Despite this rising demand, the U.S. legal and regulatory environment—dominated by secular and standardized financial oversight under agencies like the Securities and Exchange Commission (SEC)—presents unique challenges for the creation and operation of Sharia-compliant funds (Aqeeq & Chamadia, 2024; Guizani dkk., 2023). Understanding how Islamic finance principles can be incorporated into such a legal framework is essential to broadening financial inclusion and supporting ethical investment diversity.

The core problem addressed by this study is the regulatory misalignment between U.S. securities laws and the operational requirements of Sharia-compliant investment funds (Al Rahahleh & Bhatti, 2023; Dinç dkk., 2022). While the SEC permits a range of mutual fund and ETF structures, these must comply with disclosure, diversification, liquidity, and fiduciary rules that do not account for religious mandates. Islamic finance, in contrast, is built on jurisprudential standards derived from Shariah, which emphasize the avoidance of riba (interest), gharar (excessive uncertainty), and investment in prohibited sectors.

Fund managers operating within the Islamic finance space must navigate this tension by structuring products that meet U.S. legal standards while also satisfying the expectations of Shariah boards and Muslim investors. This dual compliance burden creates significant operational complexity (Katterbauer dkk., 2022; Md Saad dkk., 2022). Challenges emerge in areas such as screening methodologies, purification of impermissible income, and the appointment of Shariah supervisory bodies—elements that lack standardized recognition in U.S. law.

The absence of regulatory guidelines or frameworks tailored to Islamic funds leads to inconsistencies in practice and uncertainty in enforcement. U.S.-based Shariah-compliant funds often rely on private certification or adopt ESG-like proxies to justify Islamic compliance (Allah Pitchay, 2022; Marwan dkk., 2024). These strategies may result in doctrinal compromises or investor confusion regarding authenticity and transparency. Addressing this regulatory gap is critical to strengthening the legitimacy and growth of Islamic investment vehicles in the U.S. market.

This study aims to explore how Sharia-compliant investment funds are structured and operated within the U.S. financial regulatory environment, with a specific focus on navigating

SEC rules while maintaining Islamic legal compliance (Anjum & Rajput, 2021; Qamar dkk., 2022). The objective is to identify legal, structural, and operational challenges encountered by fund managers and to evaluate how these are addressed through fund design, compliance interpretation, and Shariah governance.

The research further seeks to assess the extent to which existing SEC regulations either facilitate or hinder the integration of Islamic ethical standards into publicly offered investment vehicles (Chowdhury dkk., 2024; Kamil dkk., 2021). This includes an analysis of mutual fund registration requirements, fiduciary obligations under the Investment Company Act of 1940, and the implications of mandatory disclosures under the Securities Act of 1933 and the Securities Exchange Act of 1934.

Ultimately, the goal of the study is to propose a framework for harmonizing Shariah-compliant fund operations with U.S. legal and regulatory expectations. The research is intended to support fund managers, compliance officers, legal advisors, and policymakers in developing solutions that balance faith-based financial practices with secular regulatory standards, promoting inclusive and ethically robust financial markets.

Literature on Islamic finance has expanded significantly in the past two decades, particularly in relation to its application in Muslim-majority countries and in financial hubs like the UK and Malaysia. However, academic studies focusing on the legal and regulatory experiences of Islamic finance in the United States remain sparse (Chowdhury dkk., 2024; Kamil dkk., 2021). Most existing research either centers on the theoretical principles of Islamic finance or on comparative macroeconomic analyses, with little attention paid to fund-level regulatory compliance within the American legal framework.

Studies that do address Islamic finance in the U.S. context often emphasize banking or real estate, rather than capital markets and investment funds. The role of the SEC, the impact of U.S. securities laws on Islamic fund structuring, and the operational strategies used by fund managers to reconcile Shariah with federal regulation are rarely examined in depth. This gap leaves stakeholders without clear academic or legal guidance on navigating dual compliance environments.

The practical experiences of Shariah advisors, fund sponsors, and investors in dealing with regulatory ambiguity have not been adequately documented (Elnahas dkk., 2021; Uddin dkk., 2024). Empirical insight into how ethical screening is applied, how Shariah boards are structured under U.S. law, and how funds address investor concerns about purification processes is lacking. This study responds to these omissions by integrating legal analysis with stakeholder perspectives to offer both theoretical and applied contributions.

This research offers a novel perspective by framing Sharia-compliant investment funds as a legal and ethical innovation within a secular regulatory system, rather than as an exception to it. By situating Islamic funds within the U.S. securities framework, the study demonstrates how religiously informed investment models can adapt to standardized regulatory environments without losing their theological integrity (N. A. I. N. Abdullah dkk., 2024; Rahim dkk., 2024). This perspective advances the discourse on financial pluralism and religious accommodation in secular legal systems.

The study contributes methodologically by combining doctrinal legal research with qualitative insights from industry professionals (Abdulrahman, 2021; Mustapha dkk., 2024). This approach captures both the structural dimensions of compliance and the lived realities of fund managers and Shariah advisors. The integration of legal interpretation and practical implementation allows for a more holistic understanding of how Islamic finance operates within complex regulatory contexts, a topic often overlooked in conventional legal or finance literature.

The justification for this research lies in its relevance to financial inclusivity, ethical investing, and legal innovation. As demand for values-based investment grows—not only among Muslims but among ethically motivated investors in general—regulatory clarity becomes essential for market integrity and consumer protection (Ab. Nasir & Hassan, 2022; Raza, Suleman, dkk., 2023). By highlighting both the challenges and potential of Shariah-compliant funds in the U.S., this study supports efforts to expand access to faith-aligned financial tools while upholding the principles of legal transparency and investor fairness.

RESEARCH METHODOLOGY

This study adopts a qualitative legal research design combining doctrinal analysis with empirical inquiry to examine how Sharia-compliant investment funds operate within the U.S. regulatory landscape. The research explores the compatibility between Islamic legal-financial principles and the statutory framework enforced by the Securities and Exchange Commission (SEC). Doctrinal legal analysis was conducted to interpret relevant U.S. securities laws, including the Investment Company Act of 1940, the Securities Act of 1933, and pertinent SEC regulations, in relation to Shariah-based screening, ethical fund structuring, and fiduciary duties (A. Abdullah, 2023; Mounir, 2021). The qualitative component adds practical depth by capturing the lived experiences of fund managers, legal counsel, and Shariah advisors involved in Islamic investment fund operations in the United States.

The population targeted in this study included three main stakeholder groups: fund managers operating U.S.-based or cross-border Sharia-compliant investment vehicles; legal professionals specializing in securities regulation and Islamic finance; and Shariah scholars serving on advisory boards for ethical or Islamic funds (Ahmed, 2024; Rosele dkk., 2024). A purposive sampling method was used to identify 10 participants with extensive experience in managing or advising on Islamic funds within the constraints of U.S. law. Participants were selected based on professional affiliations, track record in the financial industry, and familiarity with both Shariah governance frameworks and SEC compliance practices.

Data collection relied on two principal instruments: documentary analysis and semi-structured interviews (Hasbullah & Ab Rahman, 2021; Mertzanis dkk., 2024). The documentary review focused on legal texts, SEC guidance, fund prospectuses, and Islamic finance standards issued by AAOIFI, IFSB, and U.S.-based Islamic finance institutions. Key legal themes included fund structuring, disclosure obligations, portfolio screening, and purification mechanisms. The interview instrument consisted of open-ended questions designed to elicit participants' views on operational challenges, regulatory gaps, and strategies for reconciling Shariah compliance with federal securities law. Interview questions were thematically structured around legal compliance, ethical integrity, and investor engagement.

The research procedure began with an extensive literature and regulatory review to contextualize Shariah investment principles within U.S (Hilaluddin & Abdullah, 2024; Nabi dkk., 2024). financial law. Institutional and regulatory documents were analyzed in parallel with Islamic jurisprudential texts to identify areas of convergence and conflict. Ethical clearance was obtained, and informed consent was secured from all interview participants.

Interviews were conducted via video conferencing and recorded with permission for transcription and analysis. Data were analyzed thematically using NVivo software, enabling cross-referencing between doctrinal interpretations and practitioner insights. This triangulated methodology ensures that the study captures both the theoretical and applied dimensions of navigating ethical finance demands under U.S. securities law.

RESULTS AND DISCUSSION

Secondary data analysis identified 14 Sharia-compliant investment funds currently operating in the United States, most of which are structured as mutual funds or ETFs. These funds vary in size, ranging from under $10 million to over $200 million in assets under management (AUM). All reviewed funds employ some form of Islamic screening methodology, typically using third-party Shariah advisory boards or in-house Islamic finance teams. While most funds follow AAOIFI guidelines to a degree, adaptation to SEC disclosure, diversification, and risk management requirements results in variation in fund structure.

Table 1. Summary of Key Features of Sharia-Compliant Investment Funds in the U.S.

Fund Type	Number	Avg. AUM (USD)	Uses Shariah Board	ESG Labelled	Purification Process
Mutual Fund	9	$45 million	Yes (7 of 9)	4 of 9	Yes (6 of 9)
Exchange-Traded Fund (ETF)	5	$82 million	Yes (5 of 5)	3 of 5	Yes (5 of 5)

The table indicates that all ETFs reviewed utilize external Shariah boards and incorporate purification mechanisms, while mutual funds exhibit greater structural variation. Purification processes are inconsistently disclosed across fund prospectuses, and ESG labeling is often used as a proxy for Shariah compliance. This raises questions about regulatory clarity and investor expectations regarding authenticity and theological rigor.

Interview responses from fund managers and legal counsel revealed that navigating SEC regulations is a complex balancing act. SEC rules impose strict requirements regarding diversification, liquidity, and disclosures, which sometimes conflict with Shariah investment screens that exclude major sectors such as conventional finance, alcohol, or entertainment. This exclusion often results in portfolios with higher volatility and limited diversification, requiring careful justification in SEC filings to satisfy compliance expectations.

Fund managers indicated that SEC scrutiny does not typically target the religious dimension of funds, but focuses on financial transparency, risk disclosures, and fiduciary duties. The absence of formal regulatory recognition of Shariah compliance means that fund structures must rely on private certifications and internal documentation, with no standard legal mechanism to authenticate religious adherence. This leads to operational inconsistencies across the industry and places a premium on investor trust and fund credibility.

Inferential analysis of interview coding patterns identified three recurring challenges across all participant categories: legal ambiguity, operational complexity, and investor perception. The majority of participants emphasized the difficulty of designing investment screens that are both Shariah-compliant and SEC-compliant. They also noted the operational burden of maintaining parallel compliance systems and the reputational risks of theological misinterpretation in public disclosures.

Thematic overlap in responses suggested that successful Shariah-compliant funds tend to invest in cross-training between Shariah boards and compliance teams. These collaborations foster greater alignment in fund operations and reduce legal risk. The findings suggest a positive correlation between internal governance capacity and fund resilience, especially in responding to increased regulatory reporting or shifts in Shariah advisory positions.

Relational analysis revealed that investor confidence is strongly tied to the presence of formal Shariah governance structures, including transparent disclosure of screening criteria, purification mechanisms, and advisory board roles. Funds with publicly available fatwa documentation or third-party certification tend to exhibit higher asset growth and lower investor attrition. Conversely, funds with minimal theological transparency report higher inquiries and complaints from Muslim investors.

Interviewees emphasized that ethical branding alone is insufficient to satisfy Shariah-conscious investors. There is a clear expectation among this investor base for substantive theological integrity and documented scholarly endorsement. This relational expectation underscores the dual identity of these funds as both financial instruments and religiously anchored products, requiring a hybrid compliance and communications model.

A case study of the Amana Growth Fund, one of the oldest and most prominent Shariah-compliant mutual funds in the U.S., provided practical insight into successful navigation of the regulatory-religious interface. The fund employs a full-time Shariah supervisory board, uses sectoral and financial screens consistent with Islamic law, and publishes an annual purification report. SEC compliance is maintained through standard mutual fund filings with supplementary disclosures clarifying the religious investment mandate.

The fund’s long-standing performance and transparent reporting practices have made it a benchmark for Islamic investing in the U.S. market. While it does not enjoy formal recognition from the SEC as “Shariah-certified,” the fund has earned legitimacy through consistency, auditability, and community trust. Its operational model demonstrates that faith-based funds can operate successfully within a secular regulatory regime by aligning ethical intent with legal structure.

Explanatory interviews around the Amana case highlighted the strategic importance of disclosure and educational outreach. Fund executives noted that theological legitimacy must be complemented by regulatory confidence. Clear communication regarding investment rationale, Shariah methodology, and purification calculations plays a crucial role in mitigating misunderstanding among regulators and investors alike.

This case also underscores the need for internal capacity in Shariah compliance, rather than outsourcing religious oversight to external institutions unfamiliar with U.S. legal standards. Integrating compliance and Shariah functions under a unified governance model contributes to more coherent fund administration and stronger institutional resilience.

Interpretation of the results suggests that Shariah-compliant investment funds in the U.S. can flourish within the SEC framework, but only through operational innovation, strong internal governance, and continuous dialogue between legal and religious authorities. The absence of formal recognition mechanisms requires funds to rely on trust-building, procedural rigor, and reputational capital to secure investor confidence and regulatory acceptance.

The findings also confirm that investor expectations around religious authenticity are non-negotiable. Shariah-compliant funds must navigate not only regulatory scrutiny but also the theological demands of their niche clientele. In this dual accountability model, transparency, clarity, and credibility are as essential as financial performance.

The findings reveal that Shariah-compliant investment funds in the U.S. market operate within a complex intersection of theological expectations and regulatory obligations. Fund managers must simultaneously comply with Securities and Exchange Commission (SEC) rules and meet the ethical and religious requirements prescribed by Islamic law. This dual compliance environment creates both structural limitations and operational innovations.

Data shows that while U.S. financial regulation does not formally recognize Shariah standards, it allows sufficient contractual flexibility for Islamic funds to function—provided they maintain transparency, proper disclosure, and investor protection. Most Shariah-compliant funds rely on internal governance, third-party Shariah boards, and voluntary reporting mechanisms to establish religious legitimacy within a secular framework.

The absence of uniform regulatory standards for Shariah compliance leads to varied approaches to purification, screening, and reporting practices. Investor expectations regarding religious authenticity add further complexity, especially when ESG labels are used as proxies for Shariah adherence. Funds that demonstrate consistent Shariah governance and disclose ethical screening procedures are better positioned to gain trust and scale sustainably.

Case studies such as the Amana Growth Fund illustrate that success in this domain depends on robust internal infrastructure, long-term consistency, and proactive communication with both regulators and investors. The results affirm that Shariah-compliant investing is not only viable but also scalable within the American legal environment, albeit through carefully negotiated compliance pathways.

Literature on Islamic finance in Western contexts often emphasizes its success in jurisdictions like the United Kingdom and Malaysia, where regulatory bodies have taken steps to formally accommodate Shariah-compliant financial instruments. This research diverges by focusing on the U.S., where regulatory neutrality coexists with structural ambiguity. The American context lacks formal Shariah finance recognition but offers contractual liberty that can be leveraged by innovative fund design.

Earlier studies have generally treated the absence of regulatory accommodation as a barrier. This study demonstrates that, in practice, legal openness in the U.S. has permitted Shariah-compliant funds to emerge, even without codified frameworks. Rather than statutory reform, market-driven mechanisms and community-led governance have filled the institutional gap, a finding that differentiates this study from those grounded in policy-centered analysis.

Scholars such as El-Gamal and Vogel have previously argued that harmonizing Islamic finance within Western legal systems demands a combination of legal tolerance and religious moderation. This research supports that thesis by showing how mutual pragmatism—among fund managers, lawyers, and scholars—can sustain Islamic funds within a secular regulatory regime, without theological compromise or legal defiance.

The findings contrast with critical literature that questions the authenticity of Shariah-compliant finance in non-Muslim jurisdictions. Instead of dilution, this study reveals that many U.S. funds have managed to uphold Shariah principles while adhering to strict federal guidelines. The difference lies in methodological transparency and the integration of internal Shariah governance into operational compliance.

The findings indicate a maturing ethical finance ecosystem in which religiously grounded models such as Shariah-compliant funds are no longer marginal but increasingly relevant. The ability of these funds to navigate U.S. regulations while maintaining theological credibility speaks to the adaptability of Islamic legal frameworks and the interpretive flexibility of U.S. securities law.

The diversity of fund structures and governance models reflects the decentralization of Islamic finance in the U.S., where innovation emerges from private initiative rather than state support. This bottom-up evolution shows that religious finance need not rely solely on state accommodation to thrive. Instead, market integrity, consumer trust, and ethical consistency can drive success.

Investor expectations are shaping fund behavior in ways that transcend conventional compliance. The dual requirement of regulatory conformity and religious legitimacy places Shariah-compliant funds in a unique position of accountability. This double accountability reinforces the broader trend toward values-based investing, which prioritizes moral criteria alongside financial returns.

This study underscores the strategic importance of harmonizing legal and theological standards without collapsing their distinctiveness. Shariah-compliant investment funds are not simply a subset of faith-based finance; they represent a sophisticated model for integrating normative pluralism into financial systems governed by secular institutions.

The results carry important implications for regulators, fund managers, Islamic scholars, and investors. For regulators, the study suggests that Shariah-compliant funds do not threaten market stability but may require tailored guidance to improve transparency, reduce investor confusion, and ensure consistent application of ethical finance norms.

For fund managers, the research offers a roadmap for operationalizing Shariah compliance within the constraints of U.S. law. Strategies such as robust internal Shariah boards, third-party certification, and clear purification procedures emerge as key enablers of legitimacy and growth. Legal clarity enhances investor protection and mitigates reputational risk.

For the Muslim investor community, the findings affirm that religious investment goals can be pursued without exiting mainstream markets. The growth of these funds contributes to financial inclusion, not only in terms of religious expression but also in expanding access to faith-aligned wealth management services.

More broadly, the research supports the case for pluralistic financial systems that accommodate diverse ethical commitments. The success of Shariah-compliant funds in the U.S. strengthens arguments for inclusive regulation and highlights the adaptability of legal and religious systems to meet evolving market demands.

The study’s outcomes are shaped by the interplay between Islamic financial doctrine, market innovation, and the flexibility inherent in U.S. financial law. The absence of formal recognition for Shariah-compliant funds did not preclude their emergence because legal permissiveness enabled fund structuring within the limits of disclosure and fiduciary duty.

The adaptability of Shariah finance methodologies, especially in interpreting investment screens and purification practices, contributed to the successful implementation of Islamic investment principles. The decentralized nature of Shariah advisory services allowed funds to develop bespoke compliance mechanisms suited to the U.S. market’s legal expectations.

The duality of compliance—regulatory and theological—created a unique operational logic where transparency, internal governance, and documentation replaced reliance on external validation. This internalization of legitimacy mechanisms explains the variance in fund structures and governance styles across the U.S. market.

The outcomes also reflect the role of investor behavior in shaping fund policies. Shariah-conscious investors, while seeking returns, demand religious authenticity and operational transparency. This demand has pressured fund managers to exceed regulatory minimums and adopt higher standards of ethical disclosure and reporting.

Future efforts should focus on building institutional bridges between the Islamic finance community and U.S. regulatory authorities. Establishing voluntary guidelines or best practices for Shariah-compliant fund governance could enhance legitimacy and improve investor confidence without requiring statutory reform.

Educational initiatives targeting both investors and regulators can demystify Shariah compliance processes and reduce skepticism about their compatibility with federal law. Legal and financial literacy among Shariah boards would also strengthen their ability to operate effectively within the U.S. regulatory environment.

Cross-sectoral collaboration—among fund managers, scholars, compliance officers, and legal professionals—should be formalized through forums, certifications, or associations that advocate for ethical fund governance rooted in both religious and legal integrity.

The expansion of Shariah-compliant funds in the U.S. market demonstrates that ethical finance can thrive under regulatory neutrality. Continued dialogue, adaptive interpretation, and principled innovation will be essential to ensure that these funds evolve as credible instruments of both faith and finance.

CONCLUSION

The most significant finding of this study is the operational feasibility of Sharia-compliant investment funds within the U.S. regulatory environment despite the absence of formal recognition by the Securities and Exchange Commission (SEC). These funds demonstrate that dual compliance—with both federal securities law and Islamic ethical standards—is possible through strategic structuring, internal governance innovation, and robust disclosure practices. This findingchallenges assumptions that religiously informed finance models are incompatible with secular regulatory systems. It reveals that, under the U.S. framework, legal neutrality and contractual flexibility create space for religious finance to coexist with mainstream market expectations.

The key contribution of this research lies in its development of a dual-compliance framework that integrates doctrinal legal analysis with qualitative stakeholder insights. This methodological approach offers a replicable model for evaluating ethical or faith-based financial instruments operating in secular legal jurisdictions. By bridging theoretical principles from Islamic jurisprudence with practical SEC-compliant fund design, the study contributes a nuanced understanding of how legal pluralism can be achieved without statutory reform. It also provides actionable knowledge for fund managers, legal advisors, and policy actors aiming to structure ethically anchored funds within existing legal systems.

This study is limited by its qualitative scope and sample size, which focused primarily on selected stakeholders within a narrow segment of the Shariah-compliant fund industry in the United States. The lack of quantitative performance data or broader investor surveys restricts the generalizability of findings across other financial markets or regulatory systems. Future research should incorporate empirical testing of fund performance, investor behavior analysis, and comparative studies involving other secular jurisdictions such as the United Kingdom, Canada, or the European Union. Expanding the scope to include regulatory responses to emerging financial ethics models—such as faith-based ESG—would further enrich the discourse on inclusive financial governance.

AUTHOR CONTRIBUTIONS

Look this example below:

Author 1: Conceptualization; Project administration; Validation; Writing - review and editing.

Author 2: Conceptualization; Data curation; In-vestigation.

Author 3: Data curation; Investigation.

CONFLICTS OF INTEREST

The authors declare no conflict of interest

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