

# Compliance of Islamic Financial Institutions in Pakistan with the Principles of Islamic Commercial Law: An Illusion or Reality (Views of Islamic Law Scholars)

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## Abstract

*Sharī'ah* compliance of Islamic financial institutions is one of the most important aspects of research in these days. In Pakistan, *Sharī'ah* compliance is made essential for Islamic Banking Institutions (IBIs) by the regulatory body, the State Bank of Pakistan (SBP). To comply with the *Sharī'ah*'s rules and regulations, SBP, therefore, introduced a comprehensive *Sharī'ah* Governance Framework (SGF) in 2015. It is the duty of *Sharī'ah* board to ensure that transactions of the IBIs fall under the ambit of Islamic commercial law. This study, primarily, discusses two dimensions regarding the compliance of the IBIs' business, i.e., whether it is an illusion or reality. Discussion in 'Focused Group', an important technique of qualitative research method has been adopted. While following this, data has been collected through one-on-one interviews. A sample size of fourteen (14) Informants (7 *Sharī'ah* advisors associated with Islamic banks and finance institutions, and 7 *Sharī'ah* scholars) was drawn; covering, mainly, two major cities of Pakistan i.e., Lahore and Karachi. Moreover, *Sharī'ah* Advisors have been selected from the Securities and Exchange Commission of Pakistan (SECP) registered list. *Sharī'ah* scholars, on the other hand, have been taken from recognized educational institutes of HEC. Interview questions, of the present work, are directly related to *Sharī'ah* compliance of IBIs in Pakistan. The findings reveal that Islamic banks are *Sharī'ah* compliant in Pakistan. Majority of *Sharī'ah* advisors and *Sharī'ah* scholars have an opinion in favor of reality practice regarding function and operation of the IBIs like profit maximization, CSR, sustainable development, products, services, working environment and supervision. However, some of them indicated illusionary practices, too.

**Key Words:** *Sharī'ah* Board, *Sharī'ah* Compliance, Islamic Banking Institutions, Islamic Commercial Law.

**KAUJIE Classification:** B0, S5

**JEL Classification:** G21, G30, Z12

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## Introduction

Islamic banking and finance are emerging as an alternative to conventional interest-based banking and financing (Samad, Gardner, & Cook, 2005). The basic objective of Islamic finance is to lead to redistribution of wealth for improving the financial health of the needy in line with the requirements of *Sharī'ah*. The teachings of Islam, of course, are comprehensive in nature; covering all aspects of life. Moreover, there are clear instructions even for aspects like *Halāl* and *Harām*. It emphasises universal faith, promoting brotherhood, social equality, and fairness in economic activities for the welfare of the mankind. Moreover, Islamic commercial law provides comprehensive guidelines for sustainable economic growth. Islamic banks and other financial institutions contribute to economic growth by performing different activities as per precepts of Islamic law. One important feature of IFIs is to share the risk among different investors as per these rules. These institutions focus on freedom and fairness; as universal principles as per the instructions of Allah almighty. (Abbasi et al., 2012; A. Ahmad, Malik, & Humayoun, 2010; A. Ahmad, ur Rehman, & Saif, 2010). A strong and well-functioning Islamic financial system paves a way for regional financial integration worldwide. It also contributes to the uplifting economy, social development and in creating job opportunities (El Qorchi, 2005).

*Sharī'ah* compliance, while having the above discussion in mind, plays a crucial role in IFI governance. It's mandatory for all IFIs, as per the SBP's guidelines, to ensure that their activities and operations are *Sharī'ah* based or at least *Sharī'ah* compliant – under any stretch of explanation. The regulatory body in this respect comprises the *Sharī'ah* advisors of financial institutions. In view of Hamza (2013) members of *Sharī'ah* board are remunerated and appointed by Islamic banks. They just play the role of advisory, and do not have the necessary authority to make the decision.

To undertake Islamic banking operations, *Sharī'ah* boards are appointed represented by at least 3 Shariah scholars. State Bank of Pakistan (SBP) has introduced the criteria for such *Sharī'ah* scholars. This criterion is, apart from the usual aspects of honesty and integrity, based on a person's qualifications both in terms of experience and qualification in understanding Islamic banking and finance transactions. These *Sharī'ah* scholars are chosen by the banks, approved by the SBP and appointed by the banks to oversee their Islamic banking operations. They, therefore, serve as SBP's eyes at the operational level of Islamic banking operations in the country. Their independence and neutrality are, of course, indispensable for *Sharī'ah* compliance of Islamic banks and other Islamic financial institutions (Akhtar, 2006).

As per Islamic Banking Bulletin, assets of the Islamic banking industry, while recording quarterly growth of 4.9%, increased by Rs. 132 billion to reach Rs. 2,790 billion by the end of March 2019. The market share of Islamic banking as on that date constituted a share of 15% in assets and 15.6% in deposits of the overall banking industry in the country (SBP, 2019). .

Although we might be discussing the Islamic financial institutions in general, but for this study, we are focusing on Islamic banking institutions (IBIs) operating in Pakistan. Respondents' view expressed for this study is also about the IBIs in general. The IFIs are operating in many countries and have been offering substantial *Sharī'ah*-compliant products and services in the last thirty years (Gait & Worthington, 2007b). Islamic finance is practiced, predominantly, in the Muslim world throughout the middle ages.

Later on, European financiers and businessmen adopted different modes, techniques, and instruments of Islamic finance – keeping in view the beneficial nature of such banking. Moreover, Islamic finance can contribute to economic growth and development. Financial intermediation motivates individuals and business entities to save, as well as, offering them a range of instruments to fulfill their financial needs by sharing risk and reward (Mohieldin, Iqbal, Rostom, & Fu, 2012). Besides, Islamic financial institutions are the first to come up with the idea of interest-free transactions. In Malaysia, for instance, a pilgrimage fund was established in the late 1950s; accumulating the savings of those people intending to make the pilgrimage to Makah.

As Johan, Dali, Suki, and Hafit (2017) mentioned that Islamic banks are in “between a hammer and the anvil” situation as they are facing challenges of producing competitive products. While having the importance of Islamic finance law in mind, the main objective of this study is to investigate whether the Islamic banks and other Islamic financial institutions in Pakistan are *Shari’ah* compliant or not. This study, in other words, explores whether *Shari’ah* compliance in IBIs is reality or illusion.

## Literature Review:

There are many reasons to introduce Islamic banking for Muslim customers. The main, among these is that conventional banking follows an interest-based system while interest is strictly prohibited by *Shari’ah*.<sup>2</sup> Muslims, therefore, need such institutions, as alternatives to conventional banking, that provide an opportunity to carry out transactions as per the precepts of *Shari’ah*. There are some issues with the IBIs. For instance, it is felt that customers do not have exact knowledge about IBIs’ operations or the return on their investment (Alam, Arslan, Saleem, Raziq, & Aleem, 2011; Gait & Worthington, 2007a).

Hunjra, Akhtar, Akbar, and Niazi (2011) affirmed that customers felt barriers to the adoption of the Islamic banking system for getting services. In addition, the IBIs have a small network branch system, inconvenient location of branches. Furthermore, *Shari’ah* principles are not implemented properly (Alam et al., 2011).

To comply with *Shari’ah* rules and to uphold customers’ satisfaction, IFIs have to constitute a *shari’ah* board (SB). It works independently for monitoring the activities of Islamic financial institutions in the light of Islamic commercial law. The SB’s duty is to monitor and regulate the ongoing activities of the IBIs in accordance with the Islamic commercial laws in line with regulations introduced by the SBP time to time.

This study works on two perspectives of the IBIs in Pakistan in terms of *Shari’ah* compliance i.e., it’s a reality or an illusion. Reality means anything that exists

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<sup>2</sup> *Shari’ah* strictly prohibits interest based loans. There are many verses of the Holy *Qur’ān* and *Hadith* of the Holy Prophet (SAW) that confirms this prohibition. For instance, in the Holy *Qur’ān* *Allāh*, the exalted, says “O Ye Who Believe! Fear *Allāh*, and give up what remains of your demand for usury, if ye are indeed believers. If ye do it not, take notice of war from Allah and His apostle. But if ye turn back ye shall have your capital sums: deal not unjustly and ye shall not be dealt unjustly. (*Qur’ān* 2:278-279). In another verse the Lord of Universe says “That they took *Ribā* (usury), though they were forbidden and that they devoured men’s substance wrongfully. We have prepared for those among men who reject faith a grievous punishment”. (*Qur’ān*4:161) From Jābir, may *Allāh* be pleased with him, said: “The messenger of *Allāh* (SAW) has cursed one who charges *Ribā*, he who gives it, one who records it, and the two witnesses; and he said, “They are equal” (*Muslim Sahīh*, Chapter on *Ribā*, *Hadīth* no.1598).

- an event that has actually happened or a thing which really exists (Oxford University Press, 2005). Moreover, in physical terms, it is the totality of a system, known and unknown (Saridakis, 2016). Illusion, according to Bach and Poloschek (2006) is something that deceives or misleads intellectually or perception of something objectively existing in such a way as to cause misinterpretation of its actual nature.

### **Compliance of IBIs with the Principles of Islamic Commercial Law: A Reality**

Aim of Islamic financial institutions, as mentioned earlier, is to provide *Sharī'ah* compliant alternative to conventional banking. These IFIs, or more specifically the IBIs are working according to *sharī'ah*'s principles; contributing to the economy in different ways. Many customers think that *Sharī'ah* compliance of IBIs is a reality as these institutions are offering pure *Sharī'ah* based transactions. In addition, these institutions need to work in removing the inequalities and improving the general standard of living. This aspect (*Sharī'ah* based) of IBIs has been discussed by many scholars in their scholastic works. The following lines would clarify it further.

In view of Kaleem and Ahmed (2010), Islamic microfinance institutions are socially and financially sustainable and based on the concepts of volunteer services among community members, and brotherhood. Charity based Islamic microfinance provides money for production and consumption to the needy and thus, targets social and economic social needs of the poorest segments of the society. Furthermore, it can help to reduce indebtedness and the unequal distribution of wealth in society (Ahmed, 2006). Moreover, the Islamic financial institutions strictly follow *Sharī'ah* compliant features, principally, the prohibition of taking or giving interest. In these institutions, the actual profit is distributed after the completion of actual business transaction and no profit is given in the form of any predefined amount. Likewise, IBIs are restricted from lending money to customers that contradict *sharī'ah* principles (Amin & Isa, 2008b). Farook, Kabir Hassan, and Lanis (2011) posit that customers are more satisfied with Islamic banking compared to conventional banking. It shows that Islamic Banking is purely based on *Sharī'ah*'s principles; whereas conventional banking is entirely based on profit maximization through interest-based borrowing and lending. Moreover, operations of IFIs are arguably better than conventional banking, though conventional banking has an advantage in terms of technical efficiency (Shahid, Rehman, Niazi, & Raoof, 2010). Additionally, Islamic banking has emerged as a strong financial system; based on financing, assets, profitability, effectiveness, etc.; while maintaining consistent growth (Awan, 2009). In terms of funds, deposits, and assets, (Akram, Rafique, & Alam, 2011) have examined the degree of satisfaction and customer awareness towards the products and services of the IBIs, in line with the principles of Islamic commercial law. Khan (H. N. Khan & Asghar, 2012) also have the same opinion in this connection.

*Sharī'ah* advisors ensure compliance with rules and regulations of all the products and services; enforcing policies, procedures, and agreements as per principles of Islamic commercial law. They also prepare a report on the bank's annual financial statements in respect of its *sharī'ah* compliance. They review compliance while having access to all accounts, documents, and records. Moreover, they also view operations of the institution periodically, along with the coordination of employees who are responsible for *Sharī'ah* compliance (SBP, 2008).

## **Compliance of IBIs with the Principles of Islamic Commercial Law: An illusion**

Islamic financial institutions are operating, according to Iqbal, far below their potential as they cannot take root in the absence of other necessary components of the Islamic financial system (Iqbal, 1997). Customer satisfaction, of course, is an important factor for any IBI as it is for other financial institutions. Owing to this fact, a study is conducted for customer satisfaction through six different variables, namely reliability, tangibles, empathy, assurance, compliance, and responsiveness based on the CARTER model. This study, in the very first instance, compares the service quality and customer satisfaction of Islamic and conventional financial institutions. It found that compliance with Islamic principles is the most significant criteria for the potential customer to choose Islamic banks, predominantly, in Islamic countries. Malaysia is one of the top-ranked countries under compliance attributes. (HALAKE; Othman & Owen, 2001).

IBI's customers have the perception that *Sharī'ah* bodies are only concerned with the validation of transactions and not monitoring operations. Moreover, there is a lack of prescribed global standards for Islamic banking and finance institutions to establish product lines globally (Arman, 2013). Unfortunately, there is no single well-organized financial center, for instance, that claims to be instituting and monitoring operations in accordance with pure Islamic principles. Besides, the stock markets in Muslim countries, namely Pakistan, Egypt, Jordan, etc. are not fully compatible with Islamic rules and regulations. Stock markets of Sudan and Iran are probably the closest to function in compliance with Islamic principles, but the secondary markets for IFIs are extremely non-liquid and shallow (Iqbal, 1997).

## **Methodology:**

Descriptive research, as a matter of fact is taken from words and pictures rather than numbers. It, of course contains quotations said by the participants to illustrate and present the findings. Descriptive data include; field notes, photographs, transcripts, audios recordings, and documents (Bogdan & Biklen, 1997). It is simply used to describe the various aspects of the phenomenon in minute detail. Moreover, it supports to uncover new facts and meanings through observation, description, and documents (Graneheim & Lundman, 2004). In addition, a descriptive type of research uses three methods of data collection; including questionnaires, interviews (open-ended), and observations. This is done, usually, through focused group techniques. In the present work the same research technique of qualitative research has been followed. Interviews have been conducted with fourteen (14) informants (7 *Sharī'ah* advisors associated with banks and 7 *Sharī'ah* scholars); exploring whether the IBIs in Pakistan are *Sharī'ah* compliant, in their perception or not (Smith, Flowers, & Larkin, 2009).

These scholars are primarily related to two major cities of Pakistan i.e., Karachi and Lahore. *Sharī'ah* advisors, on one hand, are selected from the SECP's (Securities and Exchange Commission of Pakistan) registered advisor's list (also associated with Islamic banks) and *Sharī'ah* scholars on the other hand are selected from recognized educational institutes of HEC. In addition, interview questions are related to the "reality" and "illusion" aspects of *Sharī'ah* compliance of IFIs in Pakistan.

Data analysis is established through an inductive approach, guided by the available literature. Convenience and purposive sampling techniques are used too, which is appropriate for the selection of a relevant and most useful sample from a population (Marshall, 1996). Moreover, interview sessions are held through telephonic sources –

as this is the easiest way for the collection of data. Furthermore, semi-structured interviews have been carried out, recorded in audio, and subsequently transcribed. The data obtained from the interviews are thematically analyzed at the later stage; a method of analyzing, identifying, and recording the data from participants (Steely et al., 2006).

## Results and Discussion:

Demographics of *Sharī'ah* advisor i.e., their length of service, gender, age, and registration numbers can be calculated from the following table with minute details.

Table: 1 Demographics Sharī'ah Advisors (SA) SECP Register List 2017

S. No	Informants	Length of Service	Gender	Age	Registration No.
1	Informants (SA.1)	8	M	38	SECP/IFD/A1
2	Informants (SA.2)	6	M	35	SECP/IFD/A2
3	Informants (SA.3)	11	M	37	SECP/IFD/A3
4	Informants (SA.4)	10	M	34	SECP/IFD/A4
5	Informants (SA.5)	10	M	36	SECP/IFD/A5
6	Informants (SA.6)	09	M	37	SECP/IFD/A6
7	Informants (SA.7)	6	M	34	SECP/IFD/A7

All seven informant's (*Sharī'ah* advisors) interviews have been analyzed with the two basic objectives. Firstly, during analysis, all-important themes are mentioned with the utmost care for the purpose not to miss any important theme derived from the interview. At this phase, extracted emerging themes, related to prescribed themes, were carefully analyzed. There are total 20 emerging themes, in total. One from *Sharī'ah* advisor No.1, 10 from *Sharī'ah* advisor No.2, 13 from *Sharī'ah* advisor No.3, 11 from *Sharī'ah* advisor No.4, 10 from *Sharī'ah* advisor No.5, 08 from *Sharī'ah* advisor No.6 and 09 from *Sharī'ah* advisor No.7 respectively. The detailed list of total emerging themes of all informants (*Sharī'ah* advisors) is given in the following table

**Table: 2 Themes by Participants**

<b>Informant (SA.1)</b>	<b>Emerging Themes</b>	<b>Informant (SA.2)</b>	<b>Emerging Themes</b>
Maximization of Profit	4	Maximization of Profit	2
Sustainable Development	3	Sustainable Development	3
Supervision	5	Supervision	2
Product and Services Quality	4	Product and Services Quality	2
Working Environment	4	Working Environment	1
<b>Total</b>	<b>20</b>	<b>Total</b>	<b>10</b>
<b>Informant (SA.3)</b>	<b>Emerging Themes</b>	<b>Informant (SA.4)</b>	<b>Emerging Themes</b>
Maximization of Profit	3	Maximization of Profit	3
Sustainable Development	3	Sustainable Development	3
Supervision	3	Supervision	1
Product and Services Quality	2	Product and Services Quality	2
Working Environment	2	Working Environment	2
<b>Total</b>	<b>13</b>	<b>Total</b>	<b>11</b>
<b>Informant (SA.5)</b>	<b>Emerging Themes</b>	<b>Informant (SA.6)</b>	<b>Emerging Themes</b>
Maximization of Profit	3	Maximization of Profit	2
Sustainable Development	2	Sustainable Development	1
Supervision	2	Supervision	2
Product and Services Quality	2	Product and Services Quality	1
Working Environment	1	Working environment	2
<b>Total</b>	<b>10</b>	<b>Total</b>	<b>08</b>
<b>Informant (SA.7)</b>	<b>Emerging Themes</b>		
Maximization of Profit	2		
Sustainable Development	1		
Supervision	2		
Product and Services Quality	2		
Working Environment	2		
<b>Total</b>	<b>09</b>		

#### **4.1. Maximization of Profit**

As per Askari, Iqbal, and Mirakhor (2011), Islamic banks use the interest-free system, risk-sharing techniques, and profit maximization for their investors. The response received from *Shari'ah* advisors, regarding the same fact can be elaborated as under.

“Being a *Shari'ah* Advisor, in my point of view earning of IFIs is really based on principles of *Shari'ah*” (SA.1)

“yes, Islamic bank offers interest-free profit”. (SA.7)

“In my view, I always care about investors’ interest”. (SA.1)

“In my view, IFIs keep an eye on investor’s interests to build up their trust”. (SA.2)

“I follow Sharī‘ah rules and regulations in their procedure as per guidelines provided by the State Bank of Pakistan”. (SA.3)

“I try my best for the interest-free earning; based on profit and loss mechanism policy”. (SA.4)

“Definitely, IBIs operate in the best interest of investors and they are managing their transactions as per rules of Islamic commercial law. (SA.5)

“Yes, IBIs are presenting their best efforts to promote Islamic banking and finance according to the principles of Islamic commercial law”. (SA.6)

#### **4.2. Sustainable Development**

In view of Furqani and Mulyany (2009), Islamic banks and financial institutions play an effective role as financial intermediaries; facilitating growth, savings, and sustainable development. The following details may clarify *Sharī‘ah* advisor’s opinion regarding the same characteristics.

*“In my opinion, as a Sharī‘ah Advisor, Islamic banks are actively involved in sustainable development as per guidelines of Islamic finance laws”. (SA.1)*

*“We have real economic activities as per principles of Islamic commercial law. These economic activities, predominantly, include sustainable development”. (SA.2)*

*“During my service as a Sharī‘ah Advisor, I have noticed that Islamic banks and other Islamic financial institutions are actively involved in sustainable development – though the process is a little bit slow””. (SA.3)*

*“I think Islamic banks and financial institutions target sustainable development as a major factor in their policies.”(SA.4)*

*“Of course, Islamic banks care about sustainable development in their commercial activities”.(SA.5)*

*“Yes, to some extent”. (SA.7)*

*“Yes, Islamic bank offers transactions having sustainable development as a major part”. (SA.7)*

#### **4.3. Social Welfare:**

Hassan and Salma Binti Abdul Latiff (2009) contend that IFIs contribute to society’s development in the shape of corporate social responsibility. Islamic banks in Pakistan play the same role. The following point may reveal it as contended by the *Sharī‘ah* advisors selected for the sample.

*“Absolutely, we focus on corporate social responsibilities through charitable activities”. (SA.1)*



“Yes, we actively participate and extend our hands to help the needy and poor persons”. (SA.2)

“Practically speaking, we can say that Islamic banks are involved (though to some extent) in social development. In some Islamic banks, some separate accounts are opened for the same purpose”. (SA.3)

“Yes, in my opinion, Islamic banks are actively involved in various activities related to social development”. (SA.4)

“Yes, Islamic banks fulfill the obligation of social development to some extent”. (SA.7)

#### **4.4. Supervision**

Abbasi et al. (2012) contend that the IBIs are directed and controlled by a legitimate regulatory body, known as the Shariah Board or the *Sharī'ah* Supervisory Board (SSB). The purpose of the SSB is to ensure that the bank operates in conformity with the principles of *Sharī'ah*. The viewpoint of SSB, regarding the supervision of commercial transactions is as under.

“Yes, Islamic banks’ transactions are closely watched”. (SA.1)

“My role, as Sharī'ah Advisor, is independent in nature. I supervise all sort of commercial activities operated at my bank”. (SA.2)

“Yes, Sharī'ah Advisors watch all types of commercial transactions carried on by their banks”. (SA3)

“Yes, Sharī'ah advisors are independent to supervise each transaction of their corresponding financial institution”. (SA.5)

“To some extent, Islamic banks’ Sharī'ah advisors supervise the commercial activities of their corresponding banks”. (SA.6)

#### **4.5. Product and Services Quality:**

M.M. Khan, Ahmed, and Nawaz (2011) investigated the relationship among products and service quality, customer satisfaction, and performance of Islamic banks. All these aspects, if based on *Sharī'ah*, can play a vital role in the development of Islamic banks. The following details would show whether service quality, customer satisfaction, and performance of Islamic banks are *Sharī'ah* based or not.

“I experienced that the IBIs provide products and services as per principles of Sharī'ah”. (SA.1)

“Practically speaking, products and services of Islamic banks are purely Sharī'ah based; as all the products have been approved by the Sharī'ah advisors. (SA.2)

“Being a Sharī'ah advisor I can say firmly that all products and services of Islamic banks are purely based on Sharī'ah”. (SA.3)

“Of course, all commercial products of Islamic banks are based on the principles of Islamic commercial law”. (SA.4)

“As per my experience, with 98% accuracy, you can say IFI’s products and services are purely Sharī'ah board”. (SA.5)

#### 4.6. Working Environment

M.S. Ahmad (2011) explains that Islamic work ethics support consultation, cooperation, equity, unity, and spirituality at the workplace. Practicing Islamic ethics at the workplace, indeed leads towards creativity, trust, and honesty.

*“Yes, Islamic banks provide an Islamic working environment that promotes cooperation, equity, unity, and spirituality at the workplace.” (SA.1)*

*“Practically speaking, Islamic banks provide a good working environment as per principles of Islamic ethics”. (SA.2)*

*“Yes, as a Shari‘ah advisor I have noticed that Islamic banks offer an environment where equality is always the order of the day ”. (SA3)*

*“Being a Shari‘ah advisor, I have observed that Islamic financial institutions care extensively about the development of Islamic working environment”. (SA.4)*

*“Yes, Islamic banks provide equal opportunities to all in their products, services, employment, etc.”. (SA.5).*

**Table. 3 Phenomenological Reduction: Shari‘ah Advisors taken from SECP Register List 2017**

Categories	Themes	Reality	Illusion
Maximization of Profit	<ol style="list-style-type: none"> <li>1. Real profit</li> <li>2. Profit and loss sharing ratios</li> <li>3. Interest-free profit</li> <li>4. Wealth maximization</li> </ol>	10	1
Sustainable Developments	<ol style="list-style-type: none"> <li>1. Government support</li> <li>2. Economic activities</li> <li>3. Growth</li> <li>4. Renowned projects</li> <li>5. Investor wealth maximization</li> </ol>	8	2
Social Welfare	<ol style="list-style-type: none"> <li>1. Equal distribution of wealth</li> <li>2. CSR</li> <li>3. Poor and needy</li> <li>4. Charity</li> <li>5. Zakat</li> </ol>	8	3
Supervision	<ol style="list-style-type: none"> <li>1. SBP Regulatory system</li> <li>2. Neutral Shariah Board System</li> <li>3. Shariah Governance</li> <li>4. Shariah involvement</li> </ol>	8	5
Product and Services Quality	<ol style="list-style-type: none"> <li>1. Alternative to conventional banking</li> <li>2. Modern technology</li> <li>3. Fairly launched products and services</li> </ol>	12	2
Working Environment	<ol style="list-style-type: none"> <li>1. Good environment</li> <li>2. Cooperative</li> <li>3. Protected environment</li> <li>4. Association</li> </ol>	12	3

	5. Customer care		
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Source: Authors' focused coding for Phenomenological reduction

This tabular & graphical representation aims to describe the most frequent collective themes of all seven informants who are *Shari'ah* advisors of Islamic banks. These are the words or statements which *Shari'ah* advisors have made during face-to-face interviews. This study contains two different directions for *Shari'ah* compliance of IFIs i.e., illusion and reality. Majority of *Shari'ah* advisors emphasize on the maximization of profit with the value of 10. Likewise, sustainable development, social welfare, supervision shows the 8 values respectively; meaning thereby that banks' *Shari'ah* scholars are in support of reality regarding *Shari'ah* compliance of the IBIs. Some *Shari'ah* advisors consider it illusion as the value of maximization of profit is just 1, sustainable development 2, social welfare 3, and supervision 5. For products/services and working environment, the majority of the *Shari'ah* advisors suggested reality because its values are 12 for both. On the other side, it shows only 2 values for product and services quality and 3 values for the working environment. Based on the results, it can be said that the majority of the *Shari'ah* advisors are in favor of reality regarding *Shari'ah* compliance in IFIs.

**Table: 4 Tabular and Graphical Representations of Informants Collective Frequencies**

Themes	Reality (N)
Maximization of profit	10
Sustainable development	8
Social welfare	8
Supervision	8
Product and services quality	12
Working environment	12
Themes	Illusion
	(N)
Maximization of profit	1

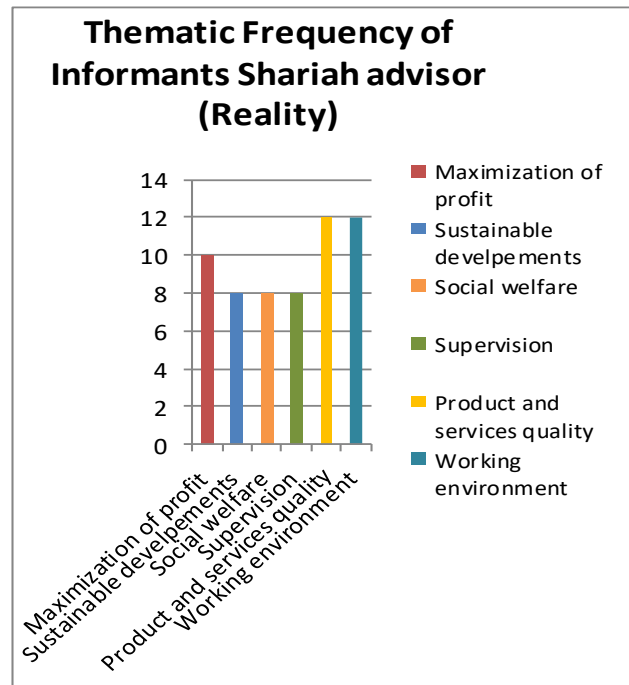


Figure 1: Authors self-created on the basis of informant's (Shari'ah Advisors) view

Sustainable development	2
Social welfare	3
Supervision	5
Product and services quality	2
Working environment	3

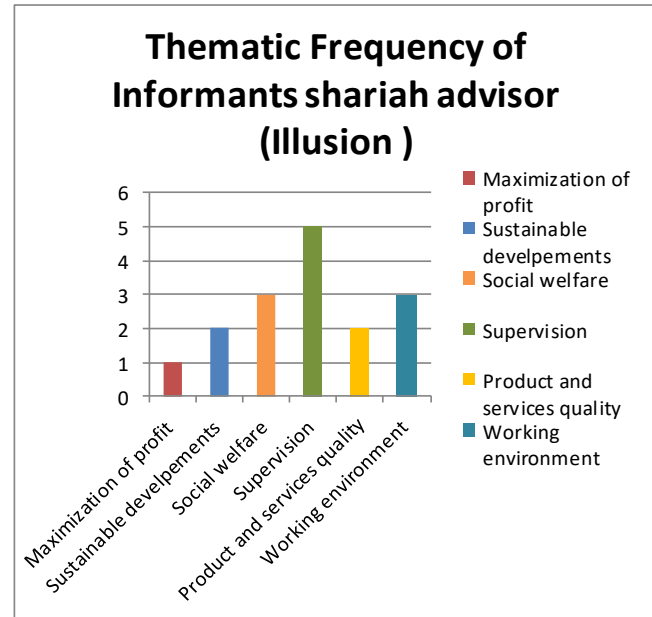


Figure 2: Authors self-created on the basis of informant's (Sharī'ah Advisors) view

**Table: 5: Demographics Sharī'ah Scholar (SS)**

***Sharī'ah* Compliance of Islamic Financial Institutions in Pakistan: Illusion or Reality 5. *Sharī'ah* Scholars' view**

Sr No .	Informants	Length of Service	Gender	Age	HEC Recog. Institutes
1	Informants (SS.1)	05	M	32	A1
2	Informants (SS.2)	04	M	31	A2
3	Informants (SS.3)	09	M	36	A3
4	Informants (SS.4)	10	M	40	A4
5	Informants (SS.5)	11	M	42	A5
6	Informants (SS.6)	09	M	38	A6
7	Informants (SS.7)	5	F	33	A7

All seven informants' (*Sharī'ah* scholars) interviews are profoundly studied. During the analysis, various themes have been developed from the informants' opinions. The following table may clarify the process (of theming) with minute details.

**Table: 6 Themes by Participants**

<b>Informant (SS.1)</b>	<b>Emerging Themes</b>	<b>Informant (SS.2)</b>	<b>Emerging Themes</b>
Maximization of Profit	2	Maximization of Profit	4
Sustainable Development	3	Sustainable Development	3
Supervision	2	Supervision	3
Product and Services Quality	2	Product and Services Quality	3
Working Environment	2	Working Environment	3
<b>Total</b>	<b>11</b>	<b>Total</b>	<b>16</b>
<b>Informant (SS.3)</b>	<b>Emerging Themes</b>	<b>Informant(SS.4)</b>	<b>Emerging Themes</b>
Maximization of Profit	3	Maximization of Profit	2
Sustainable Development	4	Sustainable Development	1
Supervision	1	Supervision	1
Product and Services Quality	0	Product and Services Quality	1
Working Environment	0	Working Environment	2
<b>Total</b>	<b>08</b>	<b>Total</b>	<b>07</b>
<b>Informant (SS.5)</b>	<b>Emerging Themes</b>	<b>Informant (SS.6)</b>	<b>Emerging Themes</b>
Maximization of Profit	1	Maximization of Profit	2
Sustainable Development	1	Sustainable Development	1
Supervision	0	Supervision	1
Product and Services Quality	0	Product and Services Quality	1
Working Environment	1	Working Environment	1
<b>Total</b>	<b>03</b>	<b>Total</b>	<b>06</b>
<b>Informant (SS.7)</b>	<b>Emerging Themes</b>		
Maximization of Profit	2		
Sustainable Development	1		
Supervision	1		
Product and Services Quality	1		
Working Environment	2		
<b>Total</b>	<b>07</b>		

### **5.1 Maximization of Profit:**

IFIs generate profit by using Islamic products, such as, provision of funds and acceptance of deposits. By using Islamic modes of financing, IFIs ensure the maximum level of profit. (Waemustafa & Sukri, 2016).

*“No, Islamic banks do not earn the real profit rather it earns interest like conventional banks”. (SS.1)*

*“Absolutely, yes our Islamic banks do offer interest-free profit”. (SS.2)*

*“I think that IFIs earn true profit as per rules of Islamic commercial law”. (SS.3)*

*“Profit, earned by the Islamic banks, is according to the principles of Islamic law”. (SS.4)*

*“IFIs institutions provide real profit to their customers”. (SS.5)*

*“Absolutely, yes our Islamic banks provide a true profit – the one supported by the principles of Islamic commercial law”. (SS.6)*

*“I do not think so...Islamic banks just change the term ‘interest’ with ‘profit’”. (SS.7)*

## **5.2 Sustainable Developments:**

In the Islamic economic system, investors have to comply with the principles of *Shari‘ah* i.e., to do justice with all stakeholders, protect the economic environment and sustain the development process (Al-Roubaie & Sarea, 2019).

*“No, in my view Islamic banks are not rightly involved in sustainable development as per principles of Islamic commercial law. (SS.1)*

*“Yes, to some extent Islamic banking institutions are involved in sustainable development”. (SS.2)*

*“In my opinion, Islamic banking institutions are supporting social development activities”. (SS.3)*

*“If IFIs work ideally, it can be proved beneficial to our economy and society”. (SS.4)*

*“Yes, our Islamic institutions have a huge role in equal distribution of wealth and sustainable development as per the principles of Islamic law”. (SS.5)*

*“Unfortunately, IFI’s currently working as an alternative to conventional structures and, therefore, are not involved in sustainable development as required by Islamic law. (SS.6)*

*“Every economic circle, of course, contributes to the development of a country. IFIs, too, is very special for the same through sukūk (commercial certificate) and other projects”.(SS.7)*

## **5.3 Social Welfare:**

Islamic financial institutions work under the umbrella of *Shari‘ah* which guides the whole process and social activities. Furthermore, CSR practices need much more attention in Pakistan (Durrani, 2016).

*“In my view, Islamic business ethics, corporate social responsibility of the business organizations and Islamic financial institutions should be seen as a benefit rather than a cost. These institutions are really involved in various activities indispensable for the development of society”. (SS.1)*

*“I believe that the collection of zakāt is not done effectively” (SS.1)*

*“I believe that IFIs are in the process of lining their activities for the social development as required by Islamic law”. (SS.3)*

## **5.4 Supervision:**

*Shari‘ah* supervisory board is one of the important parts of Islamic Financial Institutions, appointed by the board of directors to monitor the rules and regulations.

*Sharī'ah* supervisors monitored the issues related to compliance and other activities (Amin & Isa, 2008a). Furthermore, *they* supervise the banking activities and ensure that products and services are as per the principles of Islamic commercial law (Rao, 2018).

*"In my opinion, Sharī'ah advisors actively supervise all commercial transactions of their corresponding banks". (SS.1)*

*"No, I do not think so. The powers of Sharī'ah advisors are very limited and, therefore, they do not supervise Islamic banks' activities minutely. (SS.2)*

*"No, Sharī'ah advisors do not supervise their corresponding banks' activities; owing to the fact of their limited powers and lack of required knowledge, predominantly, that of contemporary accounting and finance". (SS.3)*

*"In my opinion, Sharī'ah advisers supervise all commercial activities of IFIs – though to a very limited extent". (SS.4)*

*"As a Sharī'ah scholar, I do not think that Sharī'ah advisors can supervise commercial transactions of their corresponding banks as they are not independent. Independent Shariah advisors, indeed, follow the policies of shari'ah in every transaction, whether it is related to the customer or it is related to the investments". (SS.5)*

*"No, in my opinion, most of the Sharī'ah advisors do not have the capacity required for active supervision. I think Madrassa (Religious schools) must follow a proper curriculum which is designed by experts for a Sharī'ah advisor. Moreover, they should be authorized and should be certified by the professional institutions for Sharī'ah advisors. They should understand the basic concepts of the modern economy". (SS.6)*

*"In my opinion, which may be wrong, Sharī'ah advisors do not check commercial transactions properly". (SS.7)*

## **5.5 Product and Services Quality**

IFIs provide *Sharī'ah* compliant products and services to protect the Muslims' interest (Ali & Raza, 2017). Islamic banks are liable to provide Islamic products and services that are in line with *Sharī'ah* rules to protect Muslims from interest.

*"I do not think so that products and service quality of Islamic banks follow principles of Islamic commercial law". (SS.1)*

*"No, products and service quality of IFIs are not up to the level required by Islamic law". (SS.2)*

*"Yes, products and service quality of Islamic banks match the quality required by Islamic law. (SS.3)*

*"I do not think that Islamic banks provide products and service quality according to Islamic principles". (SS.4)*

*"Yes, Islamic banks provide products and service quality as required by Islamic law". (SS.5)*

*"Yes, in my opinion, IFIs follow principles of Islamic law in the provision of products and service quality". (SS.6)*

*"No," (SS.7)*

## 5.6 Working Environment

(Chebab and Zribi (2012)) examine the main elements behind customers moving from a conventional bank to Islamic banks. They find that the quality of the relationship between the customer and the bank influencing customer choice.

*“No, IFIs do not have a working environment proposed by Islamic law. There is always cheating of customers in many respects ...I do not want to go in detail”. (SS.1)*

*“I had a great experience of working with an Islamic bank. Their dealings with the customers are not as required by Islamic finance law. Moreover, their environment is not the one approved by Islamic work ethics. For instance, equal opportunities are not provided to all employees and customers”. (SS.2)*

*“I have experience of working in Islamic banks. Their relationship is fair with the customers and employees. However, there is space for further improvement”. (SS.3)*

*“Alhamdulillah, a good atmosphere is available in Islamic banks but needs improvement, too, in the windows sector”. (SS.4)*

*“No, IFIs do not provide a good working environment envisaged by Islamic commercial law”. (SS.5)*

**Table:7 Phenomenological reductions: Shari‘ah Scholars (SS)**

Categories	Themes	Reality	Illusion
Maximization of Profit	1.Real profit	6	2
Sustainable Development	1. Sustainable growth 2. Megaprojects 3. Economy beneficial	7	3
Social Welfare	1.Equal distribution of wealth 2.Zakat 3.Funds 4.CSR	4	3
Supervision	1.Independent shariah advisor 2.Reporting system 3.Regulatory authority 4.Shariah compliance 5.SBP Supervision	5	4
Product and Services Quality	1.Fair marketing 2.Awareness 3.Alternative to the commercial banks 4.Modern technology	5	2
Working Environment	1.Language 2.Professional behavior	4	2

Source: Author’s focused coding for Phenomenological reduction

This tabular & graphical representation aims to describe the collective themes of all seven informants (*Shari‘ah* scholar). These are the words or statements which they made during face-to-face interviews. This study contains two different directions for *Shari‘ah* compliance of IFIs i.e., illusion and reality. The majority of *Shari‘ah* scholars



emphasised on the maximization of profit. Its dimension shows 06 in both tabular and graph form; meaning thereby that most of *Sharī'ah* scholars are in favor of reality. Only one informant (*Sharī'ah* scholar) considered *Sharī'ah* compliance as an illusion. Likewise, sustainable development, social welfare, supervision show the 7, 4, 5 values respectively; meaning thereby that *Sharī'ah* scholars are in support of reality regarding compliance in IFIs. Some *Sharī'ah* scholars considered it illusion as the value of sustainable development is 7, social welfare 4, and supervision 5. For products/services and working environment, the majority of the *Sharī'ah* scholar opted reality because its values are 5 and 4. It can be said, after having these figures in hands that majority of the *Sharī'ah* scholars are in favour of reality regarding *Sharī'ah* compliance in IFIs.

**Table: 8 Tabular and Graphical Representations of Informants Collective Frequencies**

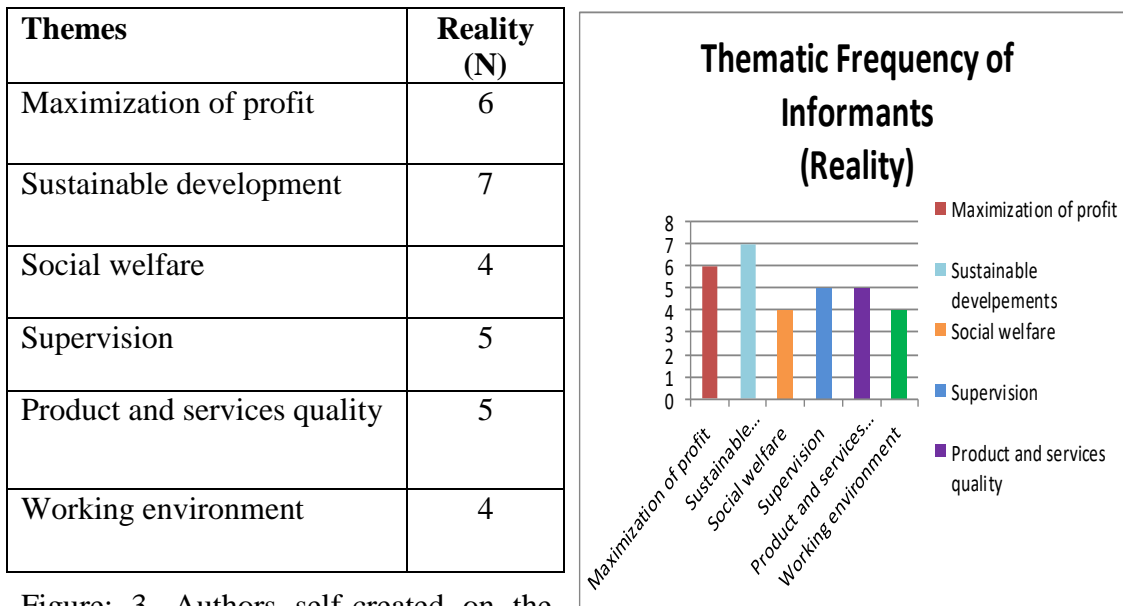
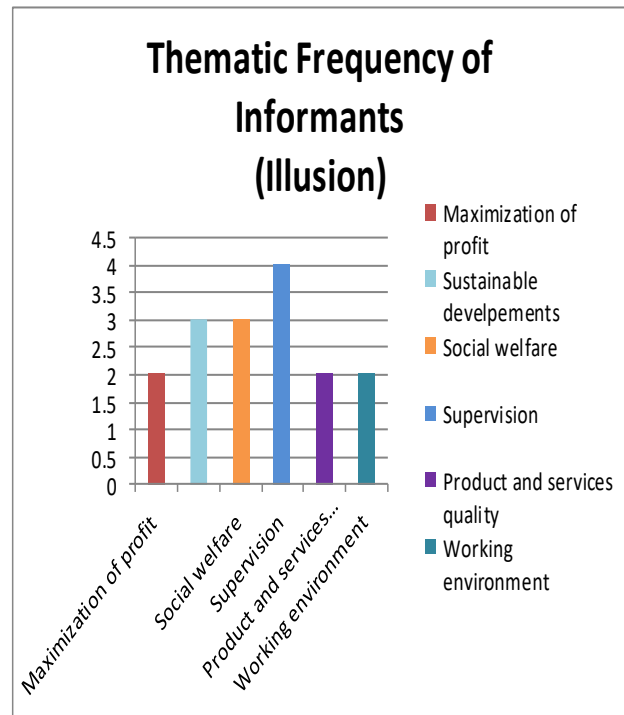


Figure: 3. Authors self-created on the basis of informant's (*Sharī'ah* Scholar) view

Categories	Illusion (N)
Maximization of profit	2
Sustainable development	3

Social welfare	3
Supervision	4
Product and services quality	2
Working environment	2

Figure: 4. Authors' self-created on the basis of informant's (*Sharī'ah* Scholar) view



## 6. Conclusion:

The current research based on the views of selected Shariah advisors associated with Islamic banks in Pakistan and some Shariah scholars graduating from HEC, Pakistan's recognized madaris chains not associated with Islamic banks, tested whether the IBIs' compliance to *Sharī'ah* is a reality or an illusion. Here the term 'reality' means that Islamic banks follow both in letter and spirit, the principles of Islamic commercial law in their business and commercial transactions. The term 'illusion', on the other hand, has a contrary meaning to that of 'reality'.

The *Sharī'ah* advisors and *Sharī'ah* scholars were interviewed regarding *Sharī'ah* compliance of Islamic banks. They were asked various questions – directly and indirectly, related to the commercial activities of IBIs in Pakistan. In addition, they were asked about the working environment offered by the Islamic banks for their customers and employees.

Islamic banks and financial institutions are bound to comply with the rules of *Sharī'ah*. As per the view of the *Sharī'ah* advisors and *Sharī'ah* scholars included in the study, Islamic banks' compliance to *Sharī'ah* is a reality; as they follow the principles of commercial law to the possible extent. But only some *Sharī'ah* advisors and *Sharī'ah* scholars have a contradiction with this opinion by saying that the bank's Shariah compliance is an illusion - they are doing business for their own interest and benefits without giving due weightage to the Shariah.

This study might be helpful to the current and potential customers, who have doubts in their minds regarding *Sharī'ah* compliance. Findings show that IBIs are following the principles of Islamic commercial law in their day to day transactions. The State Bank of Pakistan has taken many initiatives for making the transactions of Islamic banks in line with the rules and regulations of Islamic law. However, still, there is a space for improvement. As a matter of fact, an effective and efficient *Sharī'ah* compliance system enhances the confidence level of the customers. Researchers, in the future may like to include other stakeholders of Islamic finance for assessing the perception of the general public and specific groups in the society about Islamic banking and finance. This ultimately would help in evolving Islamic finance system in the long run on sustainable basis.

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