RIPHAH CENTRE OF ISLAMIC BUSINESS

Journal of Islamic Business and Management
2021, 11(01), 75-89
https://doi.org/10.26501/jibm/2021.1101-006

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PRIMARY RESEARCH

Sharī'ah Governance Framework and Perception of Islamic Banking in Pakistan

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Keywords
Sharī'ah Governance
Public Perception
Sharī'ah Scholar Perception

Received: 22 October 2020
Accepted: 12 February 2021

Abstract.
Purpose: Globally commercialized Islamic Banks were launched in 1970s at Middle East, Africa while in year 2002 at Pakistan. As of 2019, there were 5 full-fledge Islamic Banks operating in Pakistan and nearly all conventional banks have Islamic windows. Islamic Banks captured more than 15.5% share of the total Pakistan's banking market and have far greater potential and capacity to take major share in the market.
Methodology: Researchers have examined State Bank of Pakistan's Sharī'ah Governance Framework and compared it with the Sharī'ah governance framework of Malaysia, in light of IFSB guidelines. Based on key findings, focused group interviews of Sharī'ah scholars were carried out to get their perception about the Sharī'ah compliance and effectiveness of Sharī'ah Governance Framework in Pakistan.
Findings: The study focused on 5 key components of a good governance system, independence of Sharī'ah board, competence, confidentiality, consistency and disclosure requirement. The study revealed that Pakistan's Sharī'ah governance system is compliant with IFSB guidelines and comparable with Malaysian model.
Significance: This study is a unique study in the context of Pakistan. The finding of this research study will provide a comprehensive over view of the Sharī'ah Governance Framework (SGF) and perception of the Sharī'ah Scholars on SGF. The study findings may be useful for Islamic banks and other institutions using Islamic mode of financing.
Limitations: The study was conducted on a limited sample size mainly from Karachi however the study may be replicated on a bigger sample size and including other cities while the number of conducted interviews can be increased if we go for pan Pakistan as they were only 15 dues to limitation of city as Karachi.
Practical Implication: The Sharī'ah scholars have positive opinion and shown satisfaction on Sharī'ah governance system and effectiveness of Sharī'ah controls.The study results can be used to improve public perception about Sharī'ah compliance of Islamic banking system in Pakistan.

KAUJIE Classification: L34, J3
JEL Classification: M48, G15, G18

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INTRODUCTION

Islamic Banking was launched in Pakistan in 2002, with the inception of Meezan Bank. As of 2019, there were 5 full-fledged Islamic Banks and nearly all conventional banks have their Islamic windows. As per the Islamic Finance Bulletin (December, 2018) issued by State Bank of Pakistan (SBP), Islamic Banks have acquired more than 15.5% share of the total Pakistani Banking market. In order to bring control in ensuring Sharī'ah compliance of Islamic Banks, State Bank of Pakistan introduced a Sharī'ah Governance Framework in 2015, which was further revised in 2017. The Sharī'ah Governance Framework is a set of internal control and good governance guidelines to ensure transparency and credibility in the Islamic Banking practices in Pakistan.

The first formal application of the Islamic Banking system can be seen in the form of Savings bank based on "profit sharing" in the Egyptian town of MitGhamr in 1963 (Al-Omar & Abdel-Haq, 1996). These saving banks were of the nature of savings and loan institutions rather than commercial banks. The first commercial bank, Naser Social Bank, was established in 1971 in Egypt but it did not use the name and slogan of Islamic Banking (Al-Suwaidi, 1994). In the 1970's first group of fully declared Islamic commercial banks emerged which included institutions such as the Dubai Islamic banks (1975), the Kuwait Finance House (1977) etc.

Pakistan was created on the basis of Islam as its religion. Since its creation, the people of Pakistan had always demanded for elimination of *ribā* (Usmani, 2005) from the financial system of Pakistan. Muhammad Ali Jinnah, gave a very strong message regarding evolution of country's financial system on the basis of Islamic guidelines, during the inaugural ceremony of State Bank of Pakistan. In Pakistan first practical step towards Islamization of the financial system was taken in 1980s during the era of President Zia ul Haq. He issued a regulatory directive to convert all the financial dealings in lines with Qur'ānic law (Sheikh, 2007). The scholars criticized the steps taken at that time as most of the steps where merely change of nomenclature without changing the real process. On the basis of struggle of scholars, the case of determining the religious status of Pakistani Banking system was brought in the highest court which declared it against the principles of Islam in 1991 (Zaidi, 2003). The Supreme Court also gave a timeline for implementing the Islamic banking system by 2001 but later on the decision was challenged for reconsideration by some banks in year, the fate of which is still pending at Supreme Court of Pakistan (Usmani, 2005).

On the alternate side the State Bank of Pakistan started working on a parallel banking system in the country and launched the first Islamic Islamic Banking Policy in December 2001 (Akhtar *et al.,* 2011). The policy framed a clear and phase wise road map of the gradual implementation of the Islamic Banking system in Pakistan (Akhtar *et al.,* 2011). As a part of the Islamic Banking promotion activity State Bank of Pakistan supported and encouraged the banks to launch their Islamic Banking windows or subsidiaries. In order to present a running and workable model of a full fledge Islamic Banking system there was a need of a full-service Islamic Bank which was fulfilled through launch of Meezan Bank in 2003. As per Islamic Banking Bulletin in 2018 by State Bank of Pakistan, there were 5 full fledge Islamic Banks and 17 Islamic Banking windows of conventional banks with a total Islamic

Banking branch network of 2851 branches and the share of deposits of Islamic banking stood at 15.5% of the total banking deposits.

Although Islamic banking is rapidly expanding in Pakistan, previous studies have found that public concern about "Sharī'ah non-compliance risk" (the risk that an Islamic financing transaction will be challenged on the grounds that it does not comply with Islamic law) remains a major bottleneck (Ahmed & Khan, 2020; Balz, 2008; Bhatti, 2020). Any Islamic financial system's performance in any country is largely determined by stakeholders' assumption that all aspects of the system must adhere to Sharī'ah principles and rules (Ahmed & Khan, 2020) while we have lack of literature in Pakistan's prospectives so this study aims to investigate Sharī'ah scholars' perspectives on Sharī'ah non-compliance risk in order to address public concern and assist in reducing the bottleneck that has slowed the exponential expansion of Islamic banking in Pakistan.

Before the inception of Sharī'ah Governance system in Pakistan there were no formal controls over the authenticity and credibility of operations of Islamic Banks in compliance with Sharī'ah. After the launch of SGF, the Islamic Banks are imposed with several responsibilities, disclosures and control hierarchy. The purpose of this research is to find out the perception of Sharī'ah scholars about various aspects of SGF so that its effectiveness in mitigating Sharī'ah non-compliance risk can be evaluated and to add literature in the context of Pakistan due to scarcity of such valuable literature. The findings of the study will help the policy makers in making improvements to the current Sharī'ah Governance mechanism so that it can be effectively used and monitored for the purpose for which it was established.

LITERATURE REVIEW

Prohibition of Interest in Qur'ān

Islamic Banking is a system of banking that performs its banking functions in line with the guidelines and principles set by Sharī'ah. As expressed in the Qur'ān and Muhammad 's practices (Sunnah), considered binding for all believers; as an ideal Islamic law. The most distinguishing characteristic of Islamic banking system is the prohibition of interest. Sharī'ah strongly prohibits acceptance of interest (known as *ribā* or usury) at any form (fixed or floating) for loans of money (Usmani, 2007). The prohibition of *ribā* is mentioned several times in Holy Qur'ān. At first it was warned that interest deprives from Allah's blessings but no specific prohibition was mentioned. The Holy Qur'ān declared *ribā* as an act which is like inappropriate use of someone else's property. Afterwards the Qur'ān advised Muslims to stay away from interest as this act is more beneficial to them. Finally, through Surah Al-Baqarah verse 275-281, the Holy Qur'ān clearly prohibited interest and gave a ruling on the permissibility of trade transactions... The translation of those verses (275-279) of Sura Al Baqarah are as follows:

> "As for those who devour interest, they behave as the one whom Satan has confounded with his touch. Seized in this state they say: Buying and selling is but a kind of interest, even though Allah has made buying and selling lawful, and interest unlawful. Hence, he who receives this admonition from his Lord, and then gives up

(dealing in interest), may keep his previous gains, and it will be for Allah to judge him. As for those who revert to it, they are the people of the Fire, and in it shall they abide (275)".
"Allah deprives interest of all blessing, whereas He blesses charity with growth. Allah loves none who is ungrateful and persists in sin (276)".
"Truly the reward of those who believe and do righteous deeds and establish Prayer and pay *zakāh* is with their Lord; they have no reason to entertain any fear or grief (277)".
"Believers! Have fear of Allah and give up all outstanding interest if you do truly believe (278)".
"But if you fail to do so, then be warned of war from Allah and His Messenger. If you repent even now, you have the right of the return of your capital; neither will you do wrong nor will you be wronged (279)".

Need for Sharī'ah Governance Framework

Good corporate governance is an essential element towards sustainable growth of any industry. Failures in incorporating proper corporate governance practices have resulted in the famous East Asian crises on late 1990s and the failure of Enron (Sarkar & Sarkar, 2012). Besides any other industry the need for stringent corporate governance is manifolds for a banking company because people gave their funds to banks and any failure in handling those funds would result in losses whose spread is not just limited to the bank itself but are widespread (Levine, 2004). Although Islamic value system itself propagates just and equity but the need for a robust governance system is also there for its correct implementation. The unique nature of Islamic banks differentiates them from traditional banking companies. Hence, according to Brown et al. (2009), its unique risks require dedicated attention; and there is a need to think beyond the traditional models of corporate governance.

Any Islamic financial system's performance in any country is largely determined by stakeholders' assumption that all aspects of the system must adhere to Sharī'ah principles and rules (Haque *et al.,* 2010). The Islamic banking system would fail if stakeholders refused to assume the system as one that complies with Sharī'ah laws, which is known as Sharī'ah non-compliance risk (IFSB1-2005). The impact of Sharī'ah compliance risk is sufficient to trigger a bank's failure because it leads to excessive withdrawals of public deposits (Ginena, 2014). Sharī'ah risk, according to Balz (2008), is "the possibility that an Islamic financing transaction would be challenged on the grounds that it does not comply with Islamic law".. A solid governance framework is essential for controlling the Sharī'ah non-compliance risk and safeguarding the Islamic Banking system. The services of Sharī'ah scholars, working as Sharī'ah Boards (SBs), are used to ensure that all Islamic Bank operations are Sharī'ah-compliant. One of the most essential components of the Sharī'ah governance structure for Islamic banks is the Sharī'ah Board. The Sharī'ah board has a dual duty of supervision and consultation, and through providing advice and opinions, it has a significant impact on the day-to-day practises of Islamic finance and the Bank's activities. The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB) are the international standard-setting bodies for the Islamic banking

industry. According to the AAOIFI, an Islamic bank's Sharī'ah board should include at least three members who have been suggested by the board of directors before being nominated by the shareholders. The goal of the Sharī'ah Governance system, according to IFSB Standards 10 (2009), is to ensure that the Islamic Banking organisation has enough controls in place to assure Sharī'ah compliance in its activities. As a result, Sharī'ah governance refers to a system guided by Sharī'ah principles and overseen by an effective Sharī'ah board to ensure that IFI activities are compliant with Sharī'ah principles and practises (Hassan, 2010). Alman (2012) further emphasised the significance of the Sharī'ah Supervisory Board (SSB) as one of the internal governance bodies tasked with overseeing Islamic banks' actions in conformity with Sharī'ah. According to Rahajeng (2012), the Sharī'ah supervisory board or Sharī'ah compliance unit is the distinguishing characteristic that separates Islamic Bank corporate governance from a worldwide system of governance. Because Sharī'ah governance is a type of corporate governance, it should represent the core features of a good governance system: independence, transparency, accountability, responsibility, and fair (Hashim *et al.,* 2015). In this context, studies by (Grais & Pellegrini, 2006) and (Farook *et al.,* 2011) claimed that the distinctive characteristics of SSB must be understood before SSB can be included in a corporate governance mechanisms framework.

Sharī'ah Governance Models

According to Hamza (2013), there are two types of Sharī'ah governance models:

- De-centralized model
- Centralized model

De-centralized model

Islamic banks, in this method, have their own Sharī'ah Boards that are separate from the Central Bank. Each Islamic Bank in the GCC and other jurisdictions has its own Sharī'ah Board, which decides on the compliance of items offered. Kuwait, Saudi Arabia, Bahrain, Qatar, the United Arab Emirates, Jordan, Yemen, Gambia, and Indonesia are examples. At the central bank level in the GCC, there is no effective national Sharī'ah Board. At the level of the Islamic Bank, there are individual Sharī'ah Boards. Contracts and Sharī'ah-compliant financial products are approved or disapproved at the level of these institutions by their own Sharī'ah Boards.

Centralized model

The centralized system is based on a centralized Sharī'ah Board that is affiliated with the Central Bank and makes decisions on the conformance of all Islamic Banks' products and activities with Islamic principles. Each Islamic Bank has its own Sharī'ah Board in addition to the centralised regulator-based Sharī'ah Board, which gives guidance to the Islamic Bank within the general rules of the central Sharī'ah Board. The creation of a Sharī'ah Board in the Central Bank aids in assuring consistency and standardisation of operations, and its true benefits will become apparent if the Central Bank takes a consultative rather than a directive approach (Hidayah, 2014). Malaysia, Pakistan, and Sudan all have a centralized Sharī'ah governance approach.

Pakistani Sharī'ah Governance Framework

State Bank of Pakistan launched the Sharī'ah Governance framework (SGF) in 2015, further revised in 2017. The major elements of Sharī'ah Governance Framework are:

1. Role of board of directors

The SGF requires Board of Directors to be responsible for ensuring Sharī'ah compliance in Islamic Banks.

2. Role of executive management

The SGF required that is the responsibility of the Executive Management of the bank to ensure compliance with the instruction of Sharī'ah Board in daily operations of the Bank. The executive management is responsible for providing true and factual representations when discussing their proposals and submissions with Sharī'ah Board. Further, the executive Management is also responsible for providing sufficient Islamic Banking training to their staff.

3. Sharī'ah board

The SGF requires each Islamic Bank to have a Sharī'ah Board with minimum three Sharī'ah Scholars. Each Sharī'ah Scholars must fulfill certain specific education criterion about Islamic studies as prescribed in the fit and proper criterion mentioned in the SGF. The Sharī'ah Board is nominated by the Bank and its decisions and instructions are binding on the Bank including the Board of Directors. As per the requirement of the SGF, each and every product, structure, manual, SOP etc. must be approved by the Sharī'ah Board of the Bank.

4. Resident Sharī'ah board member

In order to provide guidance on daily affairs of the Islamic Banks, the SGF required the Sharī'ah Board to nominate one of its members as a Resident Sharī'ah Board member (RSBM) to support the bank in addressing queries about practical implication of SB guidelines.

5. Sharī'ah compliance department

To assist the SB and the RSBM, the SGF requires each and every Islamic Bank to create a Sharī'ah Compliance Department that would primarily serve as a channel between the Bank's management and the Sharī'ah Board. Apart from discussing proposals with the Bank's management on daily basis the Sharī'ah Compliance Department is also entrusted with the duty of carrying out a Sharī'ah Compliance review on annual basis to ensure that the guidelines of the RSBM and SB are being followed in the operations of the Bank.

6. Sharī'ah audit department

To ensure that effective controls for effective Sharī'ah Compliance are in place the SGF requires creation of a separate and independent Sharī'ah audit department/unit reporting to the Board audit committee. The Sharī'ah audit department is entrusted with the duty of performing annual Sharī'ah assessment of the Bank's operations and to highlight any instances of control weaknesses to Sharī'ah Compliance Department for their ratification and resolution.

7. External Sharī'ah audit

Each Bank is required to get an external and independent assessment of their operations with reference to Sharī'ah Compliance from reputable External Audit firms and to publish their report in the Annual report of the Bank.

8. Assessment and supervision by State bank of Pakistan

In order to assess the efficiency of the Sharī'ah Board and to assess their performance, State Bank of Pakistan required each Bank to send the minutes of the Sharī'ah Board meetings to the Islamic Banking Department of State Bank of Pakistan along with detail deliberations and basis of rulings. Apart from this the SBP will also perform Sharī'ah Assessment review of Islamic Banks on random basis.

Comparison between Sharī'ah Governance Frameworks of Pakistan with Sharī'ah Governance Framework of Malaysia

In order to access the differences between different Sharī'ah governance frameworks we have compared Sharī'ah Governance Framework of Pakistan with Sharī'ah Governance framework of Malaysia, in light of necessary elements of Sharī'ah Governance framework as suggested by IFSB. The reason for selecting Malaysian SGF model is that both Pakistan and Malaysia followed a centralized approach and both ran a parallel system of Islamic and conventional banking. The comparison between these two systems in light of IFSB guidelines is given in Table 1.

METHODOLOGY

We have used a semi-structured interview method to find out the perceptions of Sharī'ah Scholars and practitioners about this new SGF. For that purpose, Purposeful Sampling has been done in Karachi because it is a sampling technique that qualitative researchers use to recruit participants who can provide in-depth and detailed information about the phenomenon under investigation (Etikan *et al.,* 2016). The purposive sampling technique, also called judgment sampling, is the deliberate choice of a participant due to the qualities the participant possesses and it is a nonrandom technique that does not need underlying theories or a set number of participants; while simply put, the researcher decides what needs to be known and sets out to find people who can and are willing to provide the information by virtue of knowledge or experience (Bernard, 2017). 15 Participants were approached in person via personal referencing. These participants were working in different Sharī'ah divisions of Islamic banks, takaful divisions and in other Sharī'ah entities. Standard coding techniques are used to find out key themes from these interviews. The reason for choosing Sharī'ah Scholars is that they are the key components of this SGF, as SGF required all Islamic Banks to involve Sharī'ah Scholars at various levels and functions including Sharī'ah Board, Sharī'ah Audit, Product Development and Sharī'ah Compliance (Wardhany & Arshad, 2012).

TABLE 1
Comparison between Sharī'ah Governance Standards of Pakistan and Malaysia in light of IFSB standards

Area	IFSB	SGF Malaysia	SGF Pakistan
Independence	1) No blood or intimate relationship with IFI or any employee who have control over IFI 2) Member of SSB should not be a full-time employee of IFI 3) No immediate family member of the member SSB or member SSB should be and should not have been employed in a senior position in that IFI 4) SSB to have separate and independent access to all the information of the bank which they require.	1) Covered 2) Covered 3) Covered 4) Independent access to information provided	1) Not covered 2) Not covered 3) Not covered (in order to cover the above the SGF Pakistan requires approval of State Bank of Pakistan 4) covered
Competence	1) Fit and proper criterion required for selection of SSB member 2) Detailed guidelines got accessing Good character, honesty, competency, and clarity judgment requirement for SSB and its members. 3) Emphasis on continuous training 4) Mandatory orientation and induction training at the time of joining 5) Performance assessment mechanism 6) Delegation of functions to other SSB members and SCD units allowed	1) Every IFI should have its own fit and proper criterion 2) Not covered in detail 3) Covered 4) No mandatory training 5) Performance assessment mechanism in place 6) Not covered	1) Pre-defined Fit and proper criterion 2) Not covered in detail 3) Emphasis on continuous training 4) No mandatory training requirement 5) No performance assessment mechanism 6) Delegation not allowed No mandatory training 7) Performance assessment mechanism in place 8) Not covered

TABLE 1 continue

Area	IFSB	SGF Malaysia	SGF Pakistan
Confidentiality	1) Confidentiality clauses in terms of appointment 2) Appropriate disciplinary and reporting procedure in case of non- compliance 3) No restriction on number of boards a member may serve	1) Covered 2) Covered 3) A Sharī‘ah board member cannot serve in other Sharī‘ah board of same type of IFI	1) Covered 2) Covered 3) A Sharī‘ah board member may serve on Sharī‘ah board of 3 other IFIs
Consistency	1) Pronouncements backed by evidences and references 2) Consistency of opinions required in similar opinions in other boards	1) covered 2) Not allowed to participate in other boards	1) Covered 2) Not covered
Disclosure	1) Sharī‘ah Board report in annual accounts of the banks	1) Covered 1)	Covered
Additional requirements			1) External Sharī‘ah audit requirement 2) Resignation of SSB member subject to SBP clearance 3) Submission of SSB meeting minutes to SBP

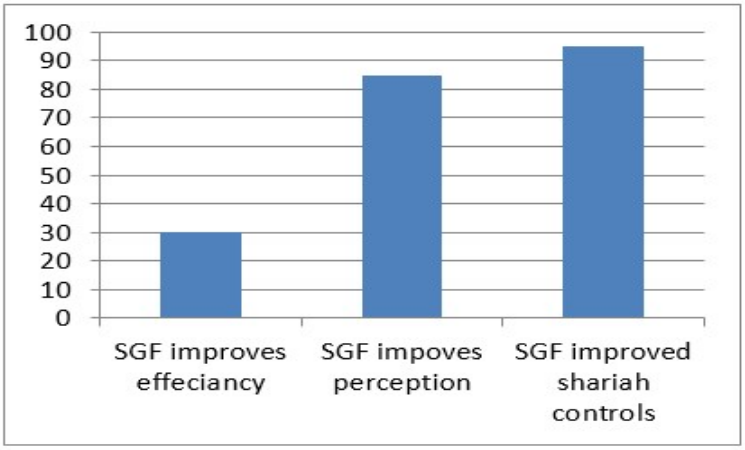

FIGURE 1. Effect of SGF on bank’s operations

FINDINGS

Effect of Sharī'ah Governance Framework on Banks

In the area of impact of SGF on efficiency of Islamic Banks we found mixed views. Almost 70% of the Sharī'ah scholars thought that the current SGF system will not improve the efficiency of the Islamic Banking operations. Almost 80% of the Sharī'ah scholars thought that the public perception will increase as a result implementation of SGF and 95% of Sharī'ah scholars were of the view that internal Sharī'ah controls of the Islamic Banks will enhance as a result of implementation of SGF.

All the Sharī'ah scholars agreed that introduction of Sharī'ah Governance framework have improved internal Sharī'ah controls of the Islamic Banks which resulted in improvement of perception towards Sharī'ah compliance of Islamic banks by the public (Haridan *et al.,* 2018). In the regime of Sharī'ah governance framework each transaction is reviewed by various Sharī'ah control clusters including Product Development Department, Sharī'ah Compliance Department, Sharī'ah Audit Department, Resident Sharī'ah Board member, Sharī'ah Board, External Sharī'ah Audit etc. which resulted in better Sharī'ah compliance of the transactions. It was felt by some scholars that the actual improvement in public perception in post SGF era is much lesser than it was expected and it was mainly attributable towards lack of marketing of the key control clusters introduced by SGF (Alam *et al.,* 2020). It is perceived that masses are, in general, not aware of the mandatory and rigorous Sharī'ah compliance processes enforced on Islamic banks by the regulator through the SGF.

On one hand it was felt that SGF improved the internal Sharī'ah controls but on the other hand the Sharī'ah scholars showed their concerns over the effect some of these stringent controls over the efficiency and performance of the Islamic Banks (Akhtar *et al.,* 2018). It was felt that this framework did not allow any delegation of authority by the Sharī'ah Board and thus every transaction is required to be routed through layers of reviewing authority before execution(Akhtar *et al.,* 2018). These layers of reviewing authorities have impacted the turnaround time in delivering prompt services by Islamic Banks(Akhtar *et al.,* 2018). It was suggested that Sharī'ah board should be allowed to delegate some of its functions for smooth running of operations of the Bank (Sarkar, 2005).

Independency of Sharī'ah Board

Independency of Sharī'ah board and its members is considered to be one of the important factors of any governance mechanism (Alam & Miah,2021). Most of the Sharī'ah scholars are satisfied that Sharī'ah governance framework gave sufficient level of independence to the Sharī'ah board and its members (Aziz,2012). The Sharī'ah scholars felt that even if Sharī'ah Board members are restricted from being employee of the bank, it will not impact their independence and will not create conflict of interest (Aziz, 2012). They considered any such restriction only on Sharī'ah board members as a sign of distrust when there are no such restrictions on other independent functions like internal audit and compliance functions of the bank (Alam & Miah, 2021). On the question of performance evaluation of Sharī'ah Board members there were two opinions. One group was in favour of performance evaluation but strongly felt that such performance evaluation must be done by a body that is competent

enough for this purpose. Some were of the opinion that this condition is unnecessary as no such conditions are applicable to the Board of Directors of the Bank and Sharī‘ah board is also like a board(Alam & Miah, 2021).

In the area of independency of SGF almost 95% of the Sharī‘ah scholars thought that the current SGF system has given sufficient powers to the Sharī‘ah Board. Almost 40% of the Sharī‘ah scholars thought that the powers of Resident Sharī‘ah Board Member are sufficient in SGF. Almost 95% of Sharī‘ah scholars did not agree that there must be any restriction on Sharī‘ah Board member being employee of the Bank. 90% of the respondents agree that there must be any performance evaluation criterion in the Sharī‘ah Governance Framework.

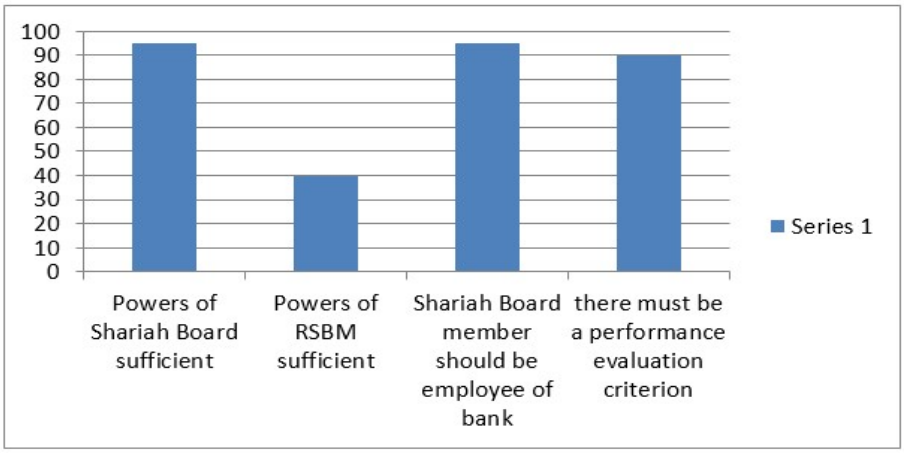

FIGURE 2. Independence of Sharī‘ah board

Consistency and Confidentiality

95% of the Sharī‘ah scholars agree that opinions of Sharī‘ah board members must be consistent in different forums they represent. Almost all the scholars agree that there must be a restriction in Sharī‘ah Board members to serve on more than one Bank as 95% felt that it would create conflict of interest, 90% feels it will sacrifice the confidentiality of information and 90% of the scholars felt that it will create conflicting opinions.

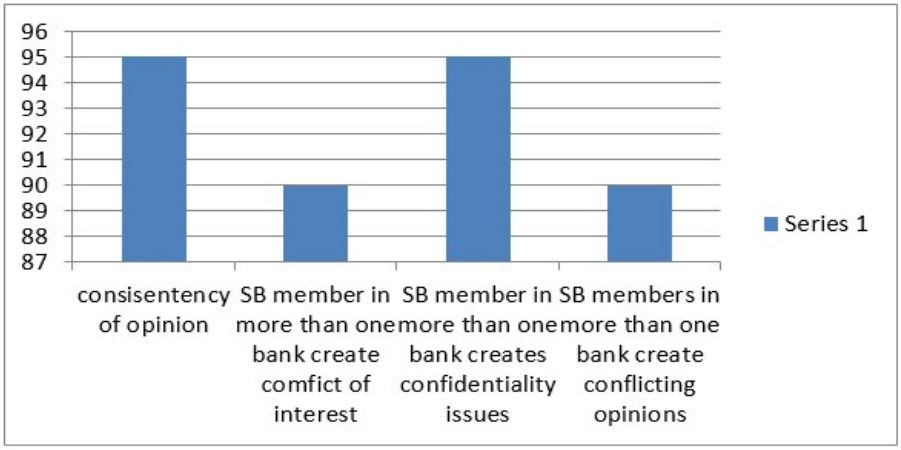

FIGURE 3. Confidentiality and consistency

All the Sharī'ah scholars were unanimous that there should be a measure to ensure that opinions of Sharī'ah Board members are consistent in various bodies they represent (Aziz, 2012). However, they felt that any deviations of opinions in two bodies must not be taken negatively as some material information may have triggered the change in opinion(Aziz, 2012). It was suggested that it should be imposed that whenever there is a change in opinion of any member of Sharī'ah board, they must be required to disclose the factors responsible for the change of opinion (Waris et al.,2008). In Pakistani SGF, it is allowed to a Sharī'ah Board member to serve on more than one Sharī'ah boards of Islamic Banks as against the SGF of Malaysia (Waris *et al.,* 2008).

Although the Sharī'ah scholar's belief that this may result in sharing of information of one bank to other but such sharing of information will not be due to mal intention but it may just be shared unintentionally during discussions. It was strongly felt that these issues can only be avoided is Sharī'ah Board members are restricted to serve in one bank only (Waris *et al.,* 2008).

Delegation of Authority and Disclosure

Almost all (96%) of the Sharī'ah scholars felt that there must be a mechanism for delegation of authority on routine and daily issues. Almost 90% of the scholars felt that restriction of delegation of authority increases turnaround time, 90% felt that it increases Sharī'ah Compliance and 95% felt that it diluted the powers of RSBM. Almost 95% of the Sharī'ah Scholars felt that disclosure requirements are adequately covered in the Sharī'ah Governance Framework.

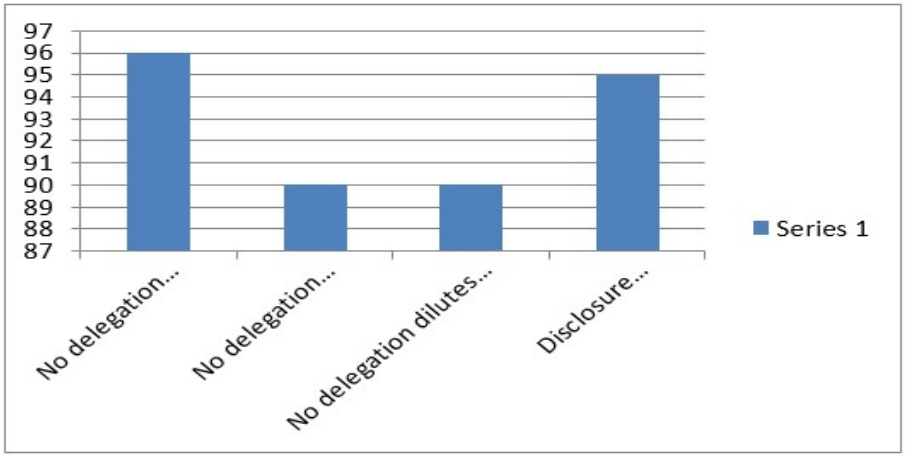

FIGURE 4. Delegation and disclosure

The Sharī'ah scholars were satisfied with the disclosure of information requirement imposed by SGF and considered it as an important element in improving public perception of the Bank. It was suggested that it may be considered by the regulator to require Islamic banks to publish annual Sharī'ah board report in the newspapers so that its ultimate benefit can be reaped. It was also suggested that it should be made mandatory to disclose difference of opinion if any in the annual accounts (Alam *et al.,* 2019).

Conclusion

On the basis of our discussion we can conclude that Pakistani Sharī'ah Governance system is comparable to International standards regarding governance systems. The Sharī'ah scholars are satisfied with the effect of the Sharī'ah governance system over the Sharī'ah controls and perception of Islamic Banks. The system in Pakistan did not mention any evaluation criterion for the performance of Sharī'ah board member, which is an essential element of international practices on Sharī'ah governance framework. In the light of our discussion it was suggested that State Bank of Pakistan should nominate any competent body for such evaluations or self-evaluation approach may also be explored. At one hand the Scholars are in praise of the system yet they feel that in order to bring control the system has been made a bit rigid and less flexible to operating challenges of Islamic Banks which needs to be considered.

Implications

In the event when stakeholders failed to presume the system as a system that complies with Sharī'ah rulings the Islamic banking system would fail and this is referred to as Sharī'ah non-compliance risk (IFSB1-2005). The impact of Sharī'ah compliance risk is enough to cause a failure of the Bank because it leads to excessive withdrawal of deposits from public (Wardhany & Arshad, 2012). The finding of this research study will provide a comprehensive over view of the Sharī'ah Governance Framework (SGF) and perception of the Sharī'ah Scholars on SGF. The study findings may be useful for Islamic banks and other institutions using Islamic mode of financing. While this study results will help in building the confidence of the potential investors on Islamic banking.

Limitations

• The study was conducted on a limited sample size mainly from Karachi however the study may be replicated on a bigger sample size and including other cities.
• The number of conducted interviews can be increased if we go for pan Pakistan as they were only 15 dues to limitation of city as Karachi.

Recommendations

1. There is a need for further studies on the subject to address the frequently asked questions of potential investors in respect of "Sharī'ah non-compliance risk".
2. The awareness campaign on Sharī'ah Compliance of Islamic banking is needed.
3. State Bank of Pakistan also needs to make the Sharī'ah Compliance Risk Mitigation process public to restore the confidence of the general public.
4. Banks need to be open and transparent to educate the potential investors in respect of the process of management of investors' funds and mode of calculation of profits etc.

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