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The Role of Shariah Board in Islamic Banks: Evidence from Pakistan, Bahrain, Qatar and Bangladesh

Dr. Talat Hussain

Department of Islamic Banking, University of Management and Technology, Lahore

Abstract

This study theoretically explains *Shari'ah* role in supervising the Islamic banks in countries including Bahrain, Pakistan, Qatar and Bangladesh. This study will discuss the roles and responsibilities of the Islamic banks working under their central banks. The criteria of this study is appointment of the *Shari'ah* board, qualification of the *Shari'ah* board, role of the *Shari'ah* board and *Shari'ah* governance, legal structure and remuneration of the *Shari'ah* board members. This study is qualitative study and in this we have explained individually country wise their role and comparison between them. At the end it is suggested that *Shari'ah* board in Bangladesh is not strong enough, there should be more defined rules and responsibilities of *Shari'ah* board and also there should be proper defined criteria for hiring of *Shari'ah* board.

Key Words: Shariah Board, Islamic Banks Pakistan, Bahrain, Qatar, Bangladesh



I-Introduction

Islamic finance is growing day by day and people are gaining interest in Islamic finance. People are discussing Islamic finance and want to have more knowledge regarding Islamic finance. People are gaining more information regarding how does shari'ah rules affect and work in Islamic banks. Islamic finance is based on the roles and regulations of the Quran and Ahadith. Quran has given all the necessary guidelines to follow Islamic contracts in practical life, whereas Ahadith shows us how to practice those in our life. Islamic Banks follows complete guidelines and all their products are shari'ah compliant and approve.¹ When people will ask more about shari'ah rules, they are more interested about shari'ah rules and how banks are implementing these rules in daily transaction? To answer this question it is important to study the role of the shari'ah board.

The shari'ah board members have unique features; they consist of different individuals from different field who have vast experience in their profession. They will help each other to form a framework in bank and provide their expertise on shari'ah related issues and guidelines will be given by them how to practice the shari'ah rules.²

The shari'ah board plays very important role in any organization; they help to evaluate the daily transactions in banks. They monitor day to day transactions and provide solutions if any shari'ah related issues arise. In this article we have discussed different roles and sharia'ah governance framework of four countries Pakistan, Bahrain, Qatar and Bangladesh.³

2-Research Questions

Islamic banking and finance is growing day by day, and it is important to examine the role of shari'ah board in these institutions. Sharia'ah board provides complete guidelines to be follow and practices are made by these institutions should be fully compliant with board guidelines. We have to evaluate the role of shari'ah board in Bangladesh, Qatar, Bahrain and Pakistan. And to compare what are the differences between them.

3-Research Objective

- Our Research objective is to check what are the role of shari'ah board in Qatar, Bahrain, Bangladesh and Pakistan?

- What are the differences between sharia'ah board of Qatar, Bahrain, Bangladesh and Pakistan?
- Which is the weakest and need improvement in their shari'ah board roles?

4.2-Qualification Of Shari'ah Board:

The board of directors must check following details before hiring of the Shari'ah board members;

- i) Should have a good character and clean background and have good professional reputation while dealing in professional business.
- ii) Have good judgment, and capable and have good sense of due diligence.
- iii) Have bachelor degree in Islamic finance/ Shari'ah.
- iv) Have good background of Shari'ah and should have fluent in Arabic language.
- v) Have a degree in Fiqh ul Muamalat
- vi) Have strong knowledge of accounting and Islamic finance.
- vii) Have a minimum of seven year experience in Shari'ah related teaching and research.

4.3-Product Development Process Flow

The new product will be launched after the critical evaluation by the shari'ah officer, the shari'ah officer must check the details and procedures and other relevant documents regarding new product and then present it in front of the shari'ah supervisory board. The product will also be assessed by the shari'ah internal and external auditors that product does not include anything which is not complaint to shari'ah, including documents, marketing and process and procedure of the product.⁺

4.4-The Role Of Shari'ah Board

- i) The shari'ah supervisory board must have all the necessary powers and responsibilities to ensure shari'ah compliance in all transactions and procedure of the Bahraini Islamic banks.
- ii) The shari'ah supervisory board must evaluate the transactions, rulings and fatwas of the shari'ah supervisory board must be bound on the Bahraini Islamic banks.

- iii) It is the duty of the shari'ah supervisory board to check and approve the annual programs of the internal shari'ah audit.
- iv) In case of the launching of new product it is the role of the shari'ah supervisory board to check and validate all the documents related to product like promotion, advertisement, contracts etc.
- v) The shari'ah supervisory board must review and submit report of annual zakah contribution on behalf of the shareholders.
- vi) The shari'ah supervisory board must submit written consent in shari'ah related issues.
- vii) One member of the board must be present in the annual financial meeting to answer the issues or queries of the shareholders.
- viii) Profit allocation to the investment account holders must be done by the shari'ah supervisory board.
- ix) The shari'ah supervisory board must disclose the ways through which the income earned by non-sharia ways can be disbursed.

4.6-Legislative Infrastructure

Islamic banks of Bahrain consist of the article 38 of the central bank of Bahrain and financial institution law of 2006. Further amendment was made in August 2017 in the module for Islamic banks volume 2. In this volume specifically all matters and guidelines are provided regarding shari'ah board, its roles and responsibilities, appointment and reporting etc.

4.7-Remuneration

The remuneration must be finalized by the general assembly. The remuneration paid by the Islamic banks in Bahrain must be disclosed by their final report. (www.cbb.gov.bh, 2017).

5-The Role Of Shari'ah Board In Pakistan

Islamic banking services offered in Pakistan are through i) full-fledged Islamic banks, ii) Islamic banks as subsidiary of conventional banks, iii) Islamic windows working under conventional banks.⁵

5.1-Appointment of Shari'ah Board:

Appointment of the Shari'ah board in Pakistan has been detailed described by regulatory bank, State bank of Pakistan. Every Islamic banking Institution must appoint three Shari'ah scholars, appointed by the board of directors. These appointments are subject to prior approval from central bank after

appointed by the board of directors. The board must include lawyer, accountants and economists, these people will help Shari'ah board members to assist them and advise them in regulatory matters, but these people will not have the power to give vote in Shari'ah board meeting, they will only provide their expert opinions to assist the board.⁶ The board members must be appointed by the Islamic banks for the period of three years, and these years will be start after the approval of the Central bank (SBP).⁷

5.3- Product Development Process Flow

The product development flow will be in two phases, one main phase is that Shari'ah board will review the product and its marketing and complete process flow, and if they found that product a as per shari'ah rule, they will then go for the second phase. In second phase the product will be referred to SBP for their approval, after obtaining approval from SBP, product will be launched.⁸

SBP has provided complete guidelines for product development to the Islamic Banks, as they should have a department for research and development and that staff should be qualified to provide guidelines to the Shari'ah board committee.⁹

5.5- Shari'ah Governance

State bank of Pakistan have revised the governance framework in 2015 after 2008. This framework has designed for all the Islamic banks, like full-fledged Islamic banks, Islamic banks subsidiaries and Islamic bank operations working under conventional banks. The main objective of the framework is to provide a strong environment for all the Islamic banking institutions, and provide guidelines for the roles of different organs, including board of director, executive management, product development department, Shari'ah Board, Shari'ah compliance department and internal and external audit departments. The framework should cover minimum points which are;

- i) Accountability of the staff and executive management for implementation of the framework as per shari'ah guidelines.
- ii) an effective and independent Shari'ah board appointed as per guidelines provided by SBP, in which one member working as resident Shari'ah board member to check whether the products and procedures are implementing as per Shari'ah guidelines.

- iii) There should be a Shari'ah compliance department to work as medium between management and Shari'ah board.
- iv) There should be an internal Shari'ah audit department.
- v) It should include a product development department for development of new products and ideas.
- vi) An external audit department for annual audit of the operations of the Islamic banking institutions.

5.6- Legislative Infrastructure

In November 2002, amendment was made in banking companies' ordinance 2001 to establish or convert bank to Islamic banks. These amendment described detailed criteria and legal requirement for establish of Islamic banks as per guidelines provide by Quran and Hadith.¹⁰

5.7- Remunerations

The remuneration will be fixed by the board of the directors and management. The remuneration will be disclosed by the bank to the Shari'ah board. There is no fix amount disclosed by the central bank or commercial banks in Pakistan.

6- The Role Of Shari'ah Board In Qatar

Islamic banking services are being offered by in Qatar is through stand-alone Islamic banks.

6.1 Appointment Of The Shari'ah Board

The appointment of the Shari'ah supervisory board will come in two steps. On first step the Islamic banks should final the supervisory board as proposed by the BOD of the bank. And then they sent their final approved list to Qatar central bank for their no objection certificate. After obtaining no objection certificate from Qatar central bank, they appoint the Shari'ah board.¹¹ The Shari'ah board can be re-appointed by the bank after getting approval from Qatar central Bank.¹²

6.2 Qualification Of The Shari'ah Board

The person appointed by Islamic banks in Qatar must have following qualifications:

- i) A person must have proper knowledge and should be capable of providing adequate solutions and judgment of Shari'ah related

matters. And shari'ah member must be fit and proper to exercise function of shari'ah board members.

- ii) The person should have good character, and honest and have integrity.
- iii) The person should be capable of passing sound judgment and should be competent and have sound mind.

6.3 Product Development Process Flow

Product development covers both aspects, pre-approval and post approval, pre-approval involves approval of the product within the Bank from the executive management or from BOD. And post approval involves approval from the central bank for the product.¹³

6.4 Role Of Shari'ah Board

The shari'ah board has following rules as mentioned in banking regulations 2015 by Qatar central Bank.

- i) Check daily routine transactions and procedures are to be followed as prescribed by shari'ah board.
- ii) Provide opinion on shari'ah related issues and submit annual, semiannual and quarterly reports and any noncompliance found, should be mentioned in that report.
- iii) Prepare shari'ah guidelines for all working departments to which they follow, also provide guidelines for working with other conventional and financial institutions.
- iv) shari'ah board should form a sound control on all banking regulations and make necessary arrangements for shari'ah compliance.
- v) shari'ah board should form and validate different contracts with other banks and organizations.
- vi) shari'ah board should give proper training to the bank staff regarding shari'ah issues and board should ensure that no activity carried out against shari'ah rules.
- vii) shari'ah board should define rules regarding income earned from non-compliant shari'ah methods.

6.5 Shari'ah Governance

The Shari'ah governance framework consists of the Shari'ah supervisory board, internal audit. The Shari'ah supervisory board will be looking after rules and regulations approved by board of directors. The Shari'ah board will

be free from the board of directors or management or any other department of the bank. They will carried out the reports and evaluate the process and procedure of the daily transactions of the Bank. The board will have full access to every transaction and file and will conduct audit as per their rule book and no other department will interfere in their matters.¹⁴ Internal Shari'ah audit will be conduct on daily basis to check day to day transactions. The internal Shari'ah auditor will implement the policies procedures defined by the Shari'ah board.¹⁵

6.6 Legislative Infrastructure

The Islamic banks incorporated through company's regulation act 2005 and Islamic investment Bank incorporated through Companies regulations 2005.

6.7 Remunerations

The remunerations will be decided by the general assembly and assembly can delete board of directors. The remunerations are fixed at the time of the appointment of the board member. The remunerations can be a fixed amount monthly or it can as per number of meetings. Once the remuneration is decided it cannot be changed, it will not change at the time of renewal of the contract.¹⁶

7-Shari'ah Board Role In Bangladesh

Islamic banking in Bangladesh has been growing in last few years. In Bangladesh Islamic banking is practicing through full-fledged Islamic banks and through Islamic banking services offered by the conventional Banks.

7.2 Qualification Of The Shari'ah Board

The Shari'ah board should fit and proper in all respects as defined by the Bank of Bangladesh. The fit and proper criteria consist of the following conditions;

- i) The board of director must have a kamil, dawa or have post graduate degree in Islamic finance, Arabic or in Islamic economics. They must have sufficient experience in Islamic banking.
- ii) The board must have at least 3 years' experience in Islamic banking or have experience in research and development related to Islamic banking and finance. .
- iii) The member should have three year experience in fatwa board in giving rulings on Islamic trade related issues.

- iv) Must have three publications in any recognized journal or book related to Islamic finance and economics.
- v) Must have good track record in professional dealings.
- vi) Must have a good reputation and should be honest and have integrity.

7.3 Role Of Shari'ah Baord

The role of Shari'ah board is to make sure that all activities carried out by the bank must be Shari'ah compliant. And no activities should be against Shari'ah rules and regulations. It is the duty of the Shari'ah board to report the activities that are non-complaint to Shari'ah to board of directors of the Islamic Bank. Board of director is ultimately responsible for the miss conduct if any found in transactions or any non-compliant Shari'ah activity found in Bank transactions.¹⁷

7.4 Shari'ah Governance

The Shari'ah governance framework is designed by the Bangladesh Bank. This framework includes the Shari'ah committee which will be appointed by the board of directors. The Shari'ah committee will make sure that all activities carried out by the Islamic banks are Shari'ah compliant. There is no mention of internal or external Shari'ah auditor by the Bangladesh Bank. The committee will form and issue rules and regulations to be followed and carried out by the bank.

7.5 Product Development Process Flow

Bangladesh Bank has defined all the products related to deposits and credits. Bangladesh bank also have mentioned all products details which to be followed like products related to import and export. Like waeeda, mudarba, musharka, salam and istisna all related Islamic products have been defined by the Bangladesh Bank. It has also defined the import related products and export related. Bangladesh bank has also designed the framework of rate of return.

Bangladesh bank has not only just defined the import and export related contracts but it has also defined the refinance related framework.

7.6 Legislative Infrastructure

The banks are formed according to the banking companies Act 1991. The revision was made in 1994 in companies. Banking prudential regulations have also provided for guidance of the Banks in Bangladesh.¹⁸

7.7- Remuneration

There are no details provided by the Bangladesh bank regarding the remuneration of the Shari'ah committee, as the board of directors can also form a shari'ah committee of their own, so there is no specific mentioned of remuneration of the shari'ah committee.¹⁹

8-Comparative Analysis Of Pakistan, Bahrain, Qatar And Bangladesh On Issues Of Shari'ah Board

8.1 Appointment And Independence Of Shari'ah Board

The appointment process in these four countries is alike with small changes except Bangladesh. In Bahrain the central bank has given authority to the banks to hire the board and there is specific mention of the prior approval from Bangladesh Bank. Whereas Both Pakistan and Qatar Central Banks have mentioned that after finalizing the list of board members, both list should be approved from the regulatory Bank, without their approval no appointment can be final. Whereas Bangladesh Bank has mentioned that the board members can be consists of the shari'ah board, there is no bounding on them to create separate department for it.

8.2 Qualification Of The Shari'ah Board And Competency

The qualification have also been defined the regulatory banks of the four countries. Bahrain regulatory bank have also defined in detail about the qualification of the board, that he must have a degree in Fiqh ul Muamalat and have seven year experience in teaching and research related to Islamic finance. Pakistan central bank have also defined that board members should have 5 year experience in Islamic banking and finance and also have minimum 3 years' experience in Shari'ah advisory board. Bangladesh have also defined a proper criteria for hiring of Shari'ah board members, that they must have 3 years' experience in Islamic banking and have experience in fatwa board also. Whereas Qatar have not mentioned any criteria for having adequate experience or any degree. Person should have proper knowledge and have capability of passing judgment on Islamic issues.

8.3 Product Development Process

Product development in Pakistan and Bahrain are same, in both countries the product will be evaluated by the Shari'ah department and then after their approval product will be referred to their regulatory Bank. After regulatory

approval product will be finalized. Bahrain bank have defined further that product will not only be approved by the Shari'ah board but the internal and external Shari'ah department also. Qatar regulatory bank have defined the product process flow as internal approval from their Board of directors and after that approval from their central Bank. Whereas Bangladesh has not defined any process for product development, Bangladesh bank has pre-defined all products related to deposits, import and export.

8.4 Role Of Shari'ah Board

According to the AAOIFI standards there are two different opinions of the people regarding Shari'ah review and Shari'ah audit, but some people take it in same ways. We have evaluated the Shari'ah role in four countries, in three countries Pakistan, Qatar and Bahrain the role of Shari'ah board is almost same and well defined that Shari'ah board will be responsible for the daily transactions and will be responsible for any misconduct done by the banks. They are also responsible for handling of income if earned by the non-compliant Shari'ah ways. Whereas Shari'ah board in Bangladesh is not ultimately responsible, as their duty is to check the transactions as per Shari'ah rules, but board of directors of the bank are responsible if any miss conduct found in their transactions.

8.6 Legislative Infrastructure

Islamic banks in Bahrain consist of the article 38 of the central bank of Bahrain and financial institution law of 2006. Pakistani Islamic banks consist of the banking ordinance 2001, which was further amended in November 2002. Qatar Islamic banks are incorporated through banking companies' regulation 2005. Bangladesh banks are formed as per companies Act 1991 which was amended further in 1994.

8.7 Remuneration

The remuneration to the Shari'ah board in Pakistan, Qatar and Bahrain is explained by the regulatory banks and remuneration will be paid by the Islamic banks not by the central Bank. Whereas in Bangladesh where remuneration can be paid to the board of directors as Shari'ah board can be consists of board of directors if they are eligible as per criteria described by the Bangladesh bank.

9-Conclusion

Quran and Sunnah are the main sources of the Shari'ah. Muslims are provided complete guidelines to be follow by these principles. But we have to make sure their implications in our practical life. To implement these rules requires the exercise of Ihtihad. In these exercise religious scholars plays a vital role. This exercise can arise many solutions to many different problems. The role of Shari'ah board is to check those problems and give solutions to these problems as per their guidelines. The Shari'ah board consists of many filed experts; this expert can include economists, accountants, and researchers. These people must have educational qualification as well as professional to deal with such issues.²⁰

The role of the Shari'ah board in four countries are same, they have to evaluate the problems, and transactions in daily routine and give proper solutions and provide guidelines if any issue arise. We have evaluated qualifications, and role and remunerations of the Shari'ah board in these countries. Role of shari'ah board is same all countries except there are few changes in their framework as Bangladesh Banks do not have any internal or external auditors except Shari'ah board, which can be consist of Board of directors. Bangladesh banks do not have such strong Shari'ah board and does not provide proper guidelines regarding role and responsibilities of the Shari'ah board. They should define proper guidelines which Shari'ah board is to follow and there should be an external and internal audit teams for evaluation of the performance of the Shari'ah board. In this article we have only selected four countries; further work can be made on other countries and can include banks in those countries and their practical implications which regulatory bank gives them.

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