Corporate Governance in the Islamic Banking System in Pakistan: The Role of the Shari’ah Supervisory Boards

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ABSTRACT:
Since it was launched commercially in the 1970’s, Islamic finance has grown at a rapid rate. Today Islamic banks are operating in nearly all Muslim countries and many non-Muslim countries. To ensure that Islamic financial institutions comply with the religious requirements, banks are required to utilise the services of a Shari’ah Supervisory Board (SSB). These SSBs consist of a number of Shari’ah (Islamic law) scholars who conduct internal religious audit in Islamic financial institutions and are required to approve the Shari’ah compliance of new financial products before they are launched commercially. This study addresses the issues of accountability and governance in Islamic financial institutions in Pakistan, and investigates the roles and responsibilities of the SSBs and Shari’ah advisors. For the purpose of this study, the field-based case study method was applied and primary data was collected using semi-structured face-to-face interviews that were conducted over a period of five years with individuals from the Pakistani banking sector. Additional information was sourced from historical documents, State Bank of Pakistan directives and relevant court cases that involved the Pakistani Islamic Banking sector.

Thematic analysis of the data reveals that there is a worldwide shortage of competent Shari’ah advisors in the Islamic finance sector. The training of new Shari’ah advisors in Pakistan is affected by the lack of educational infrastructure and the lengthy time period required for training in Islamic jurisprudence. This has resulted in banks hiring individuals as Shari’ah scholars who are members of SSBs in more than one banking institution, thereby raising concerns about conflict of interest. The findings also detail the process by which SSBs and Shari’ah advisors ensure that Islamic financial institutions are accountable for their Shari’ah operations. The SSBs are required to verify that the operations of the banks are in conformity with religious law, and to impose the suggested penalties in case of non-compliance. Finally, in comparison with existing national Shari’ah governance models in the Middle East and South-East Asia, the study evaluates the new Shari’ah governance and application model for Islamic financial institutions that has been enforced by the State Bank of Pakistan. This model is seen as the first step towards the implementation in Pakistan of the Shari’ah governance requirements put forth by the Accounting and Auditing Organization of Islamic Financial Institutions (AAOIFI), the global regulatory body for Islamic financial institutions.
DECLARATION:
This work contains no material that has been accepted for the award of any other degree or diploma in any university or other tertiary institution to Hussain Gulzar Rammal and, to the best of my knowledge and belief, contains no material previously published or written by another person, except where due reference has been made in the text.

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