



# **SHARI'AH GOVERNANCE FRAMEWORK**

**FOR**

## **ISLAMIC BANKING INSTITUTIONS**

**ISLAMIC BANKING DEPARTMENT  
STATE BANK OF PAKISTAN**

April 2014

# TEAM

<b>NAME</b>	<b>DESIGNATION</b>	<b>CONTACT</b>
Saleem Ullah	Director	<a href="mailto:saleem.ullah@sbp.org.pk">saleem.ullah@sbp.org.pk</a>
Zulfikar Ali Khokhar	Additional Director	<a href="mailto:zulfikar.khokhar@sbp.org.pk">zulfikar.khokhar@sbp.org.pk</a>
Nighat Tanveer	Sr. Joint Director	<a href="mailto:nighat.tanveer@sbp.org.pk">nighat.tanveer@sbp.org.pk</a>
Muhammad Wasim Khan	Joint Director	<a href="mailto:wasim.betanni@sbp.org.pk">wasim.betanni@sbp.org.pk</a>
Ghulam Shabbir	Joint Director	<a href="mailto:shabbir@sbp.org.pk">shabbir@sbp.org.pk</a>
Ashfaq Ahmed	Joint Director	<a href="mailto:ashfaq.iba@sbp.org.pk">ashfaq.iba@sbp.org.pk</a>

## ACRONYMS

AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
AGM	Annual General Meeting
BAC	Board Audit Committee
BOD	Board of Directors
CEO	Chief Executive Officer
EM	Executive Management
FAPC	Fit and Proper Criteria
FAQs	Frequently Asked Questions
HR	Human Resources
IAH	Investment Account Holder
IBB	Islamic Banking Branches (of Conventional Banks)
IBD	Islamic Banking Department (of SBP)
IBI	Islamic Banking Institutions-(includes both full-fledged and Islamic Banking Divisions of Conventional banks)
ICAP	Institute of Chartered Accountants of Pakistan
ISA	Internal Shari'ah Audit
ISAU	Internal Shari'ah Audit Unit
PBUH	Peace be upon Him
PLS	Profit and Loss Sharing
RSBM	Resident Shari'ah Board Member
SB	Shari'ah Board of IBIs
SBP	State Bank of Pakistan
SCD	Shari'ah Compliance Department of IBIs
SECP	Securities and Exchange Commission of Pakistan
SGF	Shari'ah Governance Framework
SOP	Standard Operating Procedure
TOR	Terms of Reference

## Table of Contents

	Page No.
Introduction .....	1
1. Role of Board of Directors (BOD).....	1
2. Role of Executive Management.....	2
3. Shari’ah Board .....	3
4. Resident Shari’ah Board Member (RSBM) .....	5
5. Shari’ah Compliance Department .....	6
6. Internal Shari’ah Audit.....	7
7. External Shari’ah Audit .....	7
8. Conflict Resolution .....	8
9. Competence of the Organs dealing with Shari’ah Governance Framework.....	9
10. Report of Shari’ah Board.....	10

# **SHARI'AH GOVERNANCE FRAMEWORK FOR ISLAMIC BANKING INSTITUTIONS**

## **Introduction**

Complying with the principles of Shari'ah as enshrined in the Holy Quran and the Sunnah of the Prophet (PBUH) is the essence and raison d'être of Islamic banking industry. A sound and effective Shari'ah compliance framework is thus critically important to give confidence to the general public about Shari'ah conformity of Islamic Banking Institutions (IBIs)' products and services. State Bank of Pakistan (SBP) endeavors to ensure that the operations of IBIs remain in conformity with the rules and principles of Shari'ah. Accordingly it has been issuing regulations, instructions and guidelines on Shari'ah compliance since the re-launch of Islamic banking in 2001.

In 2008, SBP issued detailed set of instructions and guidelines for Shari'ah compliance vide IBD Circular No. 2 of 2008. However, keeping in view the developments taken place in the Islamic banking industry over the recent years, some of the instructions and guidelines have been revisited and a comprehensive Shari'ah Governance Framework (the framework) has been developed. The framework shall be applicable to all IBIs i.e. full-fledged Islamic banks, Islamic banking subsidiaries and Islamic banking division of conventional banks. The primary objective of the framework is to strengthen the overall Shari'ah compliance environment in the IBIs and explicitly define the roles and responsibilities of various organs of IBIs including the Board of Directors (BOD), executive management (EM), Shari'ah Board (SB), Shari'ah Compliance Department (SCD) and internal and external auditors towards Shari'ah compliance.

The Shari'ah Governance Framework (SGF) of an IBI shall, at the minimum, cover the following:

- i. An effective mechanism for the BOD oversight of the IBI's Shari'ah compliance environment
- ii. Accountability of executive management in implementation of the framework
- iii. An independent and effective Shari'ah Board appointed as per Fit and Proper Criteria (FAPC) of SBP with one of its Shari'ah Scholar members working as Resident Shari'ah Board Member (RSBM) to advise the bank on day to day and routine Shari'ah issues
- iv. A Shari'ah Compliance Department to assist the SB and to serve as conduit between the SB and the management of the IBI
- v. Shari'ah compliance review mechanism to assess the operative effectiveness of the Shari'ah governance and compliance framework introduced by the SB and BOD
- vi. An independent Internal Shari'ah Audit Unit (ISAU) which may be a part of internal audit department or an independent unit depending on the size of the IBI
- vii. External Shari'ah Audit to be undertaken along with the annual audit of the IBI

## **1. Role of Board of Directors (BOD)**

- i. The BOD shall be ultimately responsible and accountable for ensuring full conformity of IBI's operations with Shari'ah principles. Like other risks faced by an IBI, the BOD needs to be fully cognizant of Shari'ah non-compliance risk and its potential implications on the reputation and business of the IBI. Towards this end, the BOD shall introduce effective mechanism including diligent oversight over the functioning of the framework and compliance with the fatawa, instructions, and guidelines of the SB.
- ii. The BOD should also be fully aware of their fiduciary responsibility particularly towards the Investment Account Holders/Profit and Loss Sharing depositors (IAHs/PLS depositors) who

accept the risks that are almost similar to those of the shareholders but without having any voting rights and forums like Annual General Meeting (AGM) to express their concerns on IBI's performance. The IAHS expect IBIs to not only exercise prudence in deployment of their funds in different avenues but also ensure Shari'ah conformity of the returns to be earned and distributed to them. The BOD is thus expected to introduce necessary mechanism and risk management system to safeguard the interest of the IAHS and also to ensure Shari'ah conformity of the returns etc being paid to them.

- iii. The BOD shall appoint a Shari'ah Board (SB) to advise it on all Shari'ah related matters and assist in introducing and implementing an effective Shari'ah compliance framework. It shall also approve the Terms of Reference (TOR) of the SB and fix remuneration of the SB members. In case of foreign banks having Islamic Banking Branches (IBBs), the appointing authority shall be the Country Manager/CEO.
- iv. The BOD shall meet the SB<sup>1</sup> at least on half yearly basis to a) have a detailed briefing on the Shari'ah compliance environment, the issues/ weaknesses, if any, and recommendations to improve Shari'ah compliance environment, and b) ensure timely and effective enforcement of the SB decisions/observations/ recommendations.

## **2. Role of Executive Management**

- i. The executive management of the IBI shall be responsible for implementing of the framework. Every executive shall ensure that all the procedure manuals, product programs, checklist etc as approved by the SB, are made available to and understood by everyone working in his/her respective group/ functional area. Moreover, every executive is responsible for imparting adequate training to his/her group employees in coordination with Training Department and Shari'ah Compliance Department.
- ii. Every group Head and executive shall also be accountable and responsible for implementation of the SB decisions/ fatawa relating to his group/ functional area. Executive management needs to show zero tolerance for the Shari'ah non-compliance and take appropriate actions against the employees who failed to ensure compliance with the Shari'ah rules and principles in their respective area of responsibility. The Shari'ah non-compliance instances shall also have strong bearing on their performance appraisals, promotions, bonuses etc.
- iii. Whenever the management refers a matter to SB for fatwa/ opinion/ guidance, it shall ensure that complete information is submitted to the SB enabling it to give opinion based on complete information and understanding of the proposal/product.
- iv. The decisions/fatawa of the SB shall be binding on the IBI. In case of disagreement between the SB and the management, the matter shall be resolved as per the conflict resolution mechanism given in the later part of this document.
- v. IBIs should arrange trainings and orientation programs on Islamic banking and finance for the BOD members and the senior executives to improve their understanding and general acumen on Islamic finance.
- vi. The management is also expected to take initiatives on regular basis for orienting and sensitizing the BOD and the key executives about the business utility and importance of an enabling Shari'ah compliance environment and the key distinguishing features of Islamic finance products.

---

<sup>1</sup> The quorum of SB meeting with BOD shall be at least two Shari'ah Scholar members.

### **3. Shari'ah Board**

#### **A. Constitution of the SB and Appointment of SB Members**

- i. Every IBI shall have a Shari'ah Board comprising at least three Shari'ah Scholars appointed as per the Fit and Proper Criteria (FAPC) notified by SBP.
- ii. The SB Chairperson shall have at least 05 years experience of working as Shari'ah Advisor or a member of Shari'ah Board of an IBI. The other Shari'ah Scholar members of the SB shall have at least 03 years experience as Shari'ah Advisor/Member of Shari'ah Supervisory Board (SSB) of an IBI or has served as a deputy to Shariah Advisor or as a member of Shari'ah team of an IBI. However, SBP may allow some relaxation in the FAPC requirements of the Chairman or the SB member on sufficient cause being shown.
- iii. The appointment of the SB members and Chairperson shall be subject to prior written approval of SBP.
- iv. IBIs may, in consultation with the SB, also engage professionals like lawyers, accountants, economists to assist and advise the SB on banking, legal, financial and economic matters. The nature of engagement of such members shall however be advisory for the SB and they shall not have voting rights in the SB meetings.
- v. The SB members shall be appointed for a term of 03 years and shall be eligible for reappointment. The Shari'ah Scholars working in IBIs as Shari'ah Advisors at the time of issuance/effectiveness of this framework may be reappointed as SB member or Chairperson as the case may be and their term would start from the date of reappointment.
- vi. The SB members except the Resident Shari'ah Board Member (RSBM) can serve at the SBs of up to three IBIs in Pakistan; the IBIs shall add a confidentiality clause in the contract of SB members for maintaining secrecy and confidentiality of IBI's non-public information/matters.
- vii. The SBP shall be informed about the reappointment of the SB members/Chairperson for another term at least two months prior to the expiry of their term. In case of any adverse feedback about the SB member/Chairperson, SBP may advise the IBI to reconsider this decision.
- viii. The IBIs not offering another term to the SB members shall also inform the SBP about their decision along with the rationale at least three months before the expiry of the term. In case of observations/reservations on the decision, the SBP may revert back to the IBI for reconsidering the decision.
- ix. Removal or termination of any SB member before expiry of his/her term shall be subject to prior approval of SBP. For the removal of the SB member, the IBI shall seek SBP approval by submitting the detailed rationale to SBP along with the documentary evidence, if any, to support its proposal.
- x. The SB members resigning before the expiry of their term shall submit the resignation to the BOD in case of domestic banks and country manager in case of foreign banks along with a copy to Islamic Banking Department of SBP. The resignation shall state the reasons and background that forced the SB member(s) to resign.
- xi. Any vacancy in Shari'ah Board arisen on account of resignation, removal or termination of any SB member shall be filled within three months.

#### **B. Role of Shari'ah Board**

- i. The SB shall advise the BOD and the executive management of the IBI on all Shari'ah related matters. All the SB decisions/ rulings/ fatawa shall be binding on the IBI whereas the Shari'ah Board shall be responsible and accountable for all its Shari'ah decisions.

- ii. The SB shall cause to develop a comprehensive Shari'ah compliance framework for all areas of operations of the IBI and shall approve all products/services to be offered and/or launched by the IBI.
- iii. The SB shall ensure that all the IBI's products and services and related agreements/ contracts, structure, process flows, product manuals, marketing advertisements, sales illustrations and brochures etc are in conformity with the rules and principles of Shari'ah. The executive management while seeking the SB decision on any proposal shall ensure provision of all the necessary information, details and documents enabling the SB to have adequate understanding of the product, its process flows, business and economic outcomes and Shari'ah permissibility or impermissibility.
- iv. The Shari'ah Board shall have unhindered access to all records, documents and information from all sources including professional advisors and IBI's employees in discharge of its duties.
- v. Considering the importance of the SB decisions and their binding nature, the SB shall rigorously deliberate on the proposals before giving any decision/fatwa; all such deliberations and rationale for allowing or disallowing a particular product/ service etc shall be duly recorded and documented.
- vi. All the reports of internal Shari'ah audit and Shari'ah compliance reviews shall be submitted to the SB for prescribing appropriate enforcement action. SB shall take up the unresolved issues with the management and if warranted shall include the outstanding issues in their annual Shari'ah compliance report. Moreover, SB/ Head of SCD shall discuss all the significant and unresolved issues with SBP inspection team during on-site inspection.
- vii. The SB shall also specify the process/procedures for changing, modifying or revisiting fatawa/rulings/ guidelines etc already issued by SB.

Notwithstanding anything contained herein, all the decisions/rulings/ fatawa of SB shall be in conformity with the instructions, guidelines and directives issued by SBP from time to time.

### **C. Shari'ah Board Meetings, Quorum, Minutes etc**

- i. Shari'ah Board shall meet at least on quarterly basis and each member of SB shall attend at least three fourth of the meetings during a calendar year. Further, in addition to the mandatory quarterly meeting, the SB Chairperson may convene SB meetings as and when he deems it necessary.
- ii. All meetings shall be chaired by the SB Chairperson and in his absence one of the Shari'ah Scholar members shall be elected as the acting Chairperson to preside over the meeting.
- iii. The quorum of SB meeting shall be at least two Shari'ah Scholar members. The SB decisions should preferably be made through consensus of the Shari'ah Scholar members; however in case of difference of opinion, the decisions may be taken through majority vote of Shari'ah Scholar members.
- iv. The agenda of SB meeting along with sufficient details shall be sent to the SB members well in advance enabling them to come prepared in the meetings; the specific timelines for submission of the agenda shall be set by SB itself.
- v. SB may hold half of its meetings through video-conferencing subject to recording of proper minutes of the meeting.
- vi. All the SB approvals taken through circulation shall be made part of the minutes of the next SB meeting.
- vii. The SB shall ensure that the minutes of its meetings have necessary details of all the decisions made and/or fatawa issued along with the rationale and difference of opinion or



dissenting note, if any. Further, the minutes shall be signed by all the SB members who attend the meeting.

- viii. The minutes of the meetings shall be submitted to Islamic Banking Department of SBP within 45 days of the meeting for information and record. Further, the minutes shall be made available to the BOD, SBP inspection teams, internal/external auditors on request enabling them to have a feel of the SB proceedings and appreciate/understand the rationale and background of the SB opinions/decisions.

#### **D. Independence of Shari'ah Board (SB)**

The SB shall discharge its duties independently and objectively. The members of the SB shall continuously assess their relationships with their respective IBIs to identify any situation where the issue related to independence may arise or can reasonably be inferred. The BOD shall ensure that the SB is not subject to any undue influence and pressures of conflicting interests of the management and/or its own members. Toward this end, IBI shall inter alia comply with the following:

- i. The appointment letter of each SB member shall clearly state the role and responsibilities of the SB and shall be duly accepted by him.
- ii. The members of SB shall neither involve nor be responsible in any manner for the operational responsibilities and functions of IBI.
- iii. SBP prudential regulation G-2 shall also be applicable on the members of SB.

#### **E. Report of Shari'ah Board**

The SB shall, based on the work of internal/external Shari'ah audit, Shari'ah compliance review, prepare a report on IBI's Shari'ah compliance environment and conditions. The minimum requirements for the report are given in Annexure – A of this document. The report shall be signed by all the members of SB. The report shall be discussed in the BOD meeting and published in the IBI's annual report.

### **4. Resident Shari'ah Board Member (RSBM)**

The SB of an IBI shall in consultation with the management designate one of the SB members other than the Chairperson as RSBM to provide guidance/advice in day to day Shari'ah related operational matters. Like other Shari'ah Scholar members of the SB, the role of RSBM shall be advisory in nature. Moreover, keeping in view the nature of RSBM's job, he/she shall be resident and generally available in Pakistan. Further, RSBM of an IBI shall not be part of SB of any other IBI in Pakistan. The RSBM will have the following role:

- i. Provide guidance on a day-to-day or routine Shari'ah related issues raised by the management and the staff of IBI.
- ii. Provide post product approval clarifications on various Shari'ah related issues and queries of management, staff, and approve routine documents, process flows etc.
- iii. Facilitate and provide guidance to the IBI's product development function regarding the Shari'ah aspects of new products/ideas.
- iv. Guide, advise and lead the SCD in conducting Shari'ah compliance reviews of key business areas on sample and test check basis.
- v. Respond to the Shari'ah related queries of IBI's present/prospective clients regarding IBI's products, services and Shari'ah practices received through SCD.
- vi. Supervise the preparation of Shari'ah training material and collaborate with SCD and Training Department in designing and delivery of Shari'ah related trainings.

- vii. Respond to all Shariah related queries made to him through SCD by different departments of the IBI.
- viii. Submit a quarterly report to the SB of all the material clarifications, opinions etc given on routine/operational nature Shari'ah issues including guidance provided to the executive management to get all such opinions etc ratified by the SB.

## **5. Shari'ah Compliance Department**

Every IBI shall have a Shari'ah Compliance Department (SCD) which may be headed by a full-time<sup>2</sup> RSBM or a suitably qualified, trained and experienced officer recommended by the SB. The department shall have dedicated adequate staff as per the advice of the SB, enabling it to discharge its responsibilities in a proper manner. Further, SCD shall work under the overall guidance and supervision of the SB and its Head shall report to the SB and his/her performance appraisal etc shall be finalized by the SB. The department shall be responsible for the following:

### **i. Secretariat of Shari'ah Board**

It shall serve as the secretariat to the SB with the responsibility to provide all the necessary secretarial support to the SB including timely provision of meetings' agenda, proposals, working papers, recording minutes and approvals/fatawa issued thereof by the SB members, and maintaining proper record of agenda items, minutes and fatawa along with the rationale issued by the SB.

### **ii. Conduit between Management and the Shari'ah Board**

The department shall act as conduit between the SB and the management of the IBI. It shall review all the proposals and related agreements, contracts, manuals, process flows, checklists etc submitted by management before presenting them to the SB for approval. The RSBM will also help and advise SCD in review of the proposals to be submitted to the SB.

### **iii. Facilitation of Management**

The department shall provide necessary support to the IBI's product development department, business units, branches and its Head Office departments in their day to day Shari'ah related issues, queries etc under the guidance/advice of the RSBM. The Shari'ah opinions and advice on the routine/day to day operational matters shall be given by the RSBM and not by the SCD. The department however, shall in no way be engaged in operational functions including product development etc.

### **iv. Shari'ah Compliance Review**

The department shall keep continuous watch on IBI's Shari'ah compliance environment and shall ensure that all the organs of Shari'ah Governance including the BOD oversight mechanism, internal Shari'ah audit, and enforcement of SB directives by executive management etc are operative and effectively undertaking their respective functions as defined in the SGF. In order to monitor and ensure compliance of IBI's operations with rules and principles of Shari'ah, SBP instructions and SB fatawa/ guidelines on an ongoing basis, the department under the lead and supervision of RSBM shall, on sample basis, conduct Shari'ah internal control review of the IBI's business units, branches, and other Head Office departments. Based on these reviews and other mechanism introduced by SCD for assessing the Shari'ah conformity of IBI's operations, the RSBM shall periodically submit a report to the SB on overall Shari'ah compliance environment in the IBI, the ownership and commitment of BOD and executive management in building the necessary Shari'ah compliance infrastructure, key areas of improvement etc. The periodicity of this report shall be decided by the SB.

---

<sup>2</sup> The RSBM not available to the IBI on full-time basis will not head SCD.

#### **v. Enforcement of Shari'ah Audit Reports**

All the reports of internal Shari'ah audit, external Shari'ah audit and extract of SBP's inspection report on Shari'ah compliance shall be sent to SB for information and for prescribing appropriate enforcement actions. The SCD shall be responsible for execution and implementation of the enforcement actions prescribed by the SB, follow-ups with the management and for keeping record of all the unresolved issues. SB shall take up the unresolved issues with the management and if warranted shall include the outstanding issues in their annual Shari'ah compliance report. Moreover, SB/ Head of SCD shall discuss all the significant and unresolved issues with SBP inspection team during on-site inspection.

#### **vi. Trainings on Shari'ah Compliance**

The SCD in collaboration with Training Unit of Human Resources Department of IBI shall develop the training material and provide Shari'ah trainings as per training plan approved by management and SB. Moreover, the SCD shall be responsible for ensuring that necessary training has been imparted to all the bank staff and that periodic refresher courses are also organized to keep the staff updated on developments in the field. The management shall provide all the required facilities for the purpose and the SCD shall report its concerns in this regard, if any, to the SB.

#### **vii. Others Functions**

- i. The department shall prepare a comprehensive procedure manual including checklists and standard operating procedures (SOPs) to assist its staff in discharging their duties.
- ii. The department shall ensure that IBI's website gives brief introduction of SB members, disclosures required by SBP, key features of all the products offered, frequently asked questions (FAQs) and the contact details of the department.
- iii. The department shall liaison with Islamic Banking Department of SBP on Shari'ah compliance related issues.

### **6. Internal Shari'ah Audit**

- i. Every IBI shall have an Internal Shari'ah Audit Unit (ISAU) which may be a part of internal audit department or an independent unit depending on the size of the bank. Moreover, Head of ISAU shall report to Head of Internal Audit or Board Audit Committee (BAC) in case of independent unit.
- ii. IBI shall ensure that staff of ISAU is appropriately qualified and trained to perform their duties. Shari'ah audit staff shall be dedicated to Shari'ah audit only; however, Shari'ah and regular audit of a branch or a function can be performed simultaneously.
- iii. The scope, methodology, checklists/work programs, Shari'ah audit manual and format of internal Shari'ah audit report shall be reviewed and approved by the SB.
- iv. ISAU shall prepare a separate Shari'ah audit plan which, after review by the SB, shall be approved by the Board Audit Committee.
- v. The final Shari'ah internal audit report shall be submitted to SB for prescribing appropriate enforcement actions.
- vi. The final report along with the enforcement/corrective actions prescribed by SB shall be sent to the BAC for information and ensuring compliance with the SB directives on the report.

### **7. External Shari'ah Audit**

In order to have an independent assessment of Shari'ah governance and compliance environment of an IBI, the scope of external audit of IBIs shall also include an independent and

objective assessment of conformity of IBI's operations with Shariah rules and principles. The external auditor's assessment of IBI's Shariah compliance environment shall be published in annual audited accounts; the SBP shall prescribe the format of this report in consultation with Institute of Chartered Accountants of Pakistan (ICAP). The audit firms shall have the capacity i.e. the HR and methodology etc. to conduct the Shari'ah audit.

For the purpose of this Shariah governance framework the scope of external Shari'ah audit shall be limited to assessing compliance of an IBI's financial arrangements, contracts, and transactions with Shariah rules and principles. The Shariah rules and principles for the purpose of the external Shariah audit shall comprise of the following, in the sequence provided below:

- i. Essentials, Regulations, Instructions, Guidelines and Shari'ah Compliance Framework issued by the State Bank of Pakistan (SBP) including the Shari'ah Standards issued by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), as adopted by SBP (with suitable modifications);
- ii. The rulings of the Shari'ah Board of the SBP;
- iii. Requirements of the applicable Islamic Financial Accounting Standards as notified by the Securities and Exchange Commission of Pakistan (SECP);
- iv. Approvals and rulings given by the Shari'ah Board of the IBI (or the Shari'ah Advisor of the IBI prior to constitution of the Shari'ah Board) in line with the principles defined by SBP; and

The external auditors shall also prepare a report for the BOD giving their assessment on: a) compliance with SBP instructions on Shari'ah compliance, b) compliance with the Shari'ah compliance framework approved by the SB, c) the Shari'ah compliance environment, d) the risks associated with Shari'ah non-compliance and the capacity/quality of the risk management system to measure and manage/mitigate this risk, e) the level of awareness and sensitization of the executive management and BOD in appreciating this risk.

## **8. Conflict Resolution**

- i. The decisions and fatawa of the SB are binding on the IBI. However in case of difference of opinion between the SB and the IBI's management on any Shari'ah related matter, the fatwa/opinion of the SB etc, the issue shall be referred to the SBP Shari'ah Board for decision.
- ii. In case any difference of opinion between an IBI and the SBP inspection team regarding Shari'ah conformity of IBI's products/ services/ transactions, the matter shall be referred to SBP Shari'ah Board for decision.
- iii. Similarly in case of difference of opinion between the Islamic Banking Department of SBP and IBI on Shari'ah conformity of any existing or proposed new product or service of the IBI, the structure, process flows, underlying agreements etc of such products shall be referred to SBP Shari'ah Board for decision on the Shari'ah permissibility or otherwise of such products<sup>3</sup>.
- iv. The SB may also refer Shari'ah issues to SBP for consideration of SBP Shari'ah Board. The case shall be sent to SBP along with its arguments based on Shari'ah. The SBP Shari'ah Board shall provide guidance in such cases at its earliest convenience.

---

<sup>3</sup> The IBIs are required to submit the salient features, product structure, process flows, underlying agreements, reporting in books of accounts and financial statements and Shari'ah Advisor's certificate (SB's certificate after issuance of the SGF) of all new products and services to IBD of SBP at least 30 days before the launch of the product.

## **9. Competence of the Organs dealing with Shari'ah Governance Framework**

- i. The BOD and executive management are expected to have a reasonable knowledge of Shari'ah principles and their broad application on Islamic finance. IBIs shall ensure that the members of the Board of Directors and the executive management are exposed to orientation sessions/trainings on Islamic banking on regular basis which apart from their professional development would also facilitate in effective implementation of the Shari'ah governance framework.
- ii. Similarly the members of the SB shall be exposed to the training sessions, orientation programs related to legal and regulatory framework, banking, finance, treasury operations etc to improve their understanding of legal and regulatory framework and banking and finance.
- iii. The IBI shall also ensure that all its key executives including credit, marketing, operations and risk Heads, the branch managers, the relationship managers and other front line staff have adequate understanding of Islamic banking and finance and are able to appreciate and understand Shari'ah non-compliance risk. The IBIs shall also ensure to expose such officials to various training sessions, seminars, and workshops for their continued professional development. This would lend confidence to the public that the IBI they are dealing with is manned by professionals having adequate skill and expertise.

X...X...X

## Report of Shari'ah Board

(Period)

In the name of Allah, the Beneficent, the Merciful

1. While the management of (name of the IBI) is solely responsible to ensure that the operations of the bank are conducted in a manner that comply with Shari'ah principles at all times, we are required to submit a report based on review of the overall Shari'ah compliance environment conducted by the bank's Shari'ah Compliance Department.

2. To form our opinion as expressed in this report, the Shari'ah Compliance Department carried out reviews, on test check basis, of each class of transactions, the relevant documentation and process flows etc. Further, we have also reviewed the work carried out by internal/external Shari'ah audit. Based on above, we are of the view that:

***(SB's opinion at least on the following may be given)***

- i. The IBI has complied with Shari'ah rules and principles and also with the specific fatawa, rulings, guidelines issued by SBP and by SB from time to time.
- ii. Whether or not the bank has a comprehensive mechanism in place to ensure Shari'ah compliance in their overall operations.
- iii. Whether or not the bank has a well-defined system in place which is sound enough to ensure that any earnings realized from sources or by means prohibited by Shari'ah have been credited to charity account and are being properly utilized.
- iv. Whether or not the bank has complied with the SBP instructions on profit and loss distribution and pool management.
- v. The level of awareness, capacity and sensitization of the staff, management & the BOD in appreciating the importance of Shari'ah compliance in the products and processes of the bank.
- vi. Whether or not the Shari'ah Board has been provided adequate resources enabling it to discharge its duties effectively.

Signature

Name

Chairman Shari'ah Board

Signature

Name

Member Shari'ah Board

Signature

Name

Member Shari'ah Board

Date of Report: \_\_\_\_\_