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State Bank Issues Instructions & Guidelines for Shariah Compliance in IBIs

The State Bank of Pakistan today issued Instructions & Guidelines for Shariah Compliance in Islamic Banking Institutions (IBIs) to further strengthen the Shariah compliance framework in Islamic banking industry.

These 'Instructions and Guidelines for Shariah Compliance' have been finalized in consultation with various stakeholders as well as reviewed and approved by the SBP Shariah Board.

It may be pointed out that these Instructions and Guidelines for IBIs are in addition to current Prudential Regulations, guidelines and other directives issued by the SBP.

The 'Instructions for Shariah compliance in IBIs' cover various areas related to appointment, removal and working of Shariah Advisors (SAs); conflict resolution in Shariah rulings; Shariah compliant modes; use of charity fund, introduction of new products and services and schedule of service charges etc. It may be pointed out that essentials of Islamic modes of financing, issued by SBP in April 2005, have now been augmented and made part of these instructions.

According to these instructions, every IBI will be required to appoint a Shariah Advisor in line with a clear set of instructions issued by the SBP including that the appointment of Shariah Advisor will be approved by the Board of Directors; Shariah Advisor will be required to meet the 'Fit and Proper Criteria for Shariah Advisors' notified by the SBP; the *Fatawa* and rulings of the Shariah Advisor in all financial matters shall be binding on the IBIs etc.

In terms of duties & responsibilities of the Shariah Advisor (SA), the SA will be responsible to review operations of the IBI on periodic basis in coordination with officials responsible for Shariah compliance to ensure that all the products and services being offered by the IBI conform to the injunctions of Shariah. If any income is declared as non-Shariah compliant by the SA, the same shall be credited to Charity Account opened for this purpose. According to the instructions, the SA will also be required to prepare a report on the IBI's annual financial statement in respect of its Shariah compliance.

These instructions also deal with Conflict Resolution in Shariah rulings wherein in case of any difference of opinion arising between the SA of an IBI and the State Bank's inspection staff or other SBP departments regarding Islamic Banking practices, the State Bank may refer the case to the SBP Shariah Board and the decision of SBP Shariah Board will be final.

The State Bank has also introduced a complete new set of Shariah-compliant modes of Banking and Financing for IBIs that include Mudaraba; Musharaka; Diminishing Musharaka; Equity participation in the form of shares in a corporate entity; Ijarah or Ijarah wa Iqtina; Murabaha; Musawamah; Salam; Istisna; Tawarruq; Qard; Wakalah; Assignment of Debt and Kafalah.

These instructions also prescribe essentials of Islamic modes of financing as minimum requirement for Shariah compliance in respect of products developed on the basis of such modes. For the Islamic modes for which essentials have not been prescribed, Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI) Shariah standards may be used as guidelines by IBIs in consultation with their Shariah Advisors.

The 'Guidelines for Shariah compliance in IBIs' are meant for providing guidance in areas like Shariah compliance, internal Shariah audit, investment in shares, policy for profit distribution with PLS account holders and financial reporting and general disclosure etc. Necessary flexibility has been provided in these guidelines and IBIs can set up the suggested systems and procedures keeping in view the size and scope of their operations.

It may be mentioned here that the State Bank is promoting and developing Islamic banking industry in Pakistan as a parallel system and this sector has witnessed tremendous growth. Currently, total assets of Islamic banking industry have exceeded Rs 200 billion and the branch network of 18 Islamic banking institutions (i.e. 6 full-fledged Islamic banks and 12 conventional banks having Islamic banking branches) has expanded to 47 cities all over Pakistan.
