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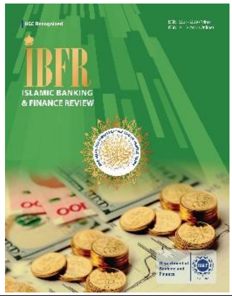

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Author (s):	Rafiullah Sheikh[1], Khalid Hussain[2]
Affiliation (s):	[1]Riphah International University, Islamabad, Pakistan [2]Bahria Business School, Islamabad, Pakistan
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Role of *Shariah* Supervisory Boards (SSBs) in Islamic Financial Engineering: A Critical Review

Rafiullah Sheikh[1*] and Khalid Hussain[2]

[1] Riphah School of Leadership, Riphah International University, Islamabad, Pakistan

[2]Department of Management Studies, Bahria Business School, Islamabad, Pakistan

Abstract

This study aims to review critically the role of *Shariah* Supervisory Boards (SSBs) in Islamic financial engineering. It also strives to explore the similarities between the role of SSBs and that of the Board of Directors (BODs). Based on the content analysis, it was found that the different roles of an SSB, such as a legislator, consultant/advisor, and auditor, are pivotal in Islamic financial engineering in order to improve the efficiency of Islamic financial markets. Moreover, various similarities in the respective roles of SSBs and BODs were found but only to a narrower extent, since SSBs monitor and control only the religious side of the Islamic Financial Institutions (IFIs). This study proposes to incorporate SSBs within the structure of two-tier boards such that SSB might be considered as the supervisory board, whereas the regular BOD needs to be considered as the management board.

Keywords: Islamic banking and finance, Islamic financial engineering, product development, *Shariah* Governance (SG), *Shariah* Supervisory Boards (SSBs)

Introduction

Islamic Financial Institutions (IFIs) have attracted special attention of academics and policymakers worldwide because of their stability and sustainability during the financial crisis of 2007-2008. At that time, the whole economy was crippled (Trad et al., 2017) and various limitations of the conventional banking system, such as poor risk management, lack of disclosure, and lack of regulatory oversight were exposed (Mollah & Zaman, 2015).

* Corresponding Author: rafiullah.sheikh@riphah.edu.pk

Shariah Supervisory Board (SSB) is the most significant governance mechanism of an IFI (Ahmed et al., 2013). Distinct from the Conventional Financial Institutions (CFIs), IFIs provide financial services in conformity with the *Shariah* principles of avoiding *Riba* (interest), *Gharar* (absolute risk and/or uncertainty), *Qimar* (gambling), *Maysir* (games of chance), and other business activities prohibited by Islam (Ayub, 2007). Under these circumstances, the concept of *Shariah* Governance (SG), parallel to Corporate Governance (CG), has evolved to ensure *Shariah* compliance which remains the underlying reason for the existence of IFIs (Al-Amer, 2018). Choudhury and Hoque (2006) argued that SSBs comprise the higher authority in IFIs which should not be bypassed. However, SSBs bring an additional layer of governance which can create a conflict of interest between different stakeholders (Mollah & Zaman, 2015; Neifar et al, 2020).

SG is considered to be the Islamic CG. However, researchers argue that conventional and Islamic CG have different objectives. Conventional CG is more concerned about the protection of stakeholders' rights, while the main aim of Islamic CG is the retention of the Islamic identity of the corporate body (Muneeza & Hassan, 2014). Al-Amer (2018), however, asserted that SG does not completely replace CG but provides additional governance standards to ensure *Shariah* compliance under the supervision of SSBs. SG, as an additional governance mechanism of CG, provides a multi-layer governance structure to IFIs (Mollah & Zaman, 2015).

According to Alam et al. (2021), the expected roles and responsibilities of SSBs are as follows: (a) delivering *Fatwa* (*Shariah* opinion) on contemporary financial issues; (b) developing SG policies and their implementation; (c) approving and developing innovative financial products; (d) monitoring IFIs’ functions; (e) identifying problems and outlining solutions; and most importantly (f) ensuring *Shariah* compliance.

Abbas (2015) argued that financial engineering and product development can either improve the efficiency of financial markets or bring catastrophes, such as the financial crisis of 2007-2008. Although IFIs escaped the said crisis, still, the role of product development is believed to be decisive in determining their future. Furthermore, the general perception in financial markets about product development by IFIs is such that they merely imitate or replicate the existing conventional financial instruments. Therefore, they have failed to bring the desired socioeconomic impact.

The primary aim of this research, which is mainly library based and exploratory, is to undertake a critical review of the role of SSBs in Islamic financial engineering. The aim is to gain an insight into the principles and strategies followed by IFIs in developing innovative Islamic financial instruments that do not only increase their liquidity and improve risk management but also retain their Islamic identity. Following three are the specific objectives of this study:

(i) to explore the distinctive features of Islamic financial engineering;

(ii) to establish a link between CG and Islamic principles; and

(iii)to explore the distinctive role of SSBs in Islamic financial engineering and how it fits into the conventional CG structure.

The rest of the paper is organized as follows: Section 2 discusses financial engineering in Islamic perspective; Section 3 explores CG in Islamic perspective; Section 4 explores the role of SSBs in Islamic financial engineering and the corporate governance structure; and finally, Section 5 concludes the paper.

Financial Engineering in an Islamic Perspective

According to Finnerty (1988), financial engineering is defined as "the design, development, and implementation of innovative financial instruments and processes, and the formulation of creative solutions to problems in finance". However, Al-Suwailem (2007) described financial engineering as "principles and strategies for developing innovative financial solutions". Financial engineering is objectively done to lower transaction costs and achieve better returns.

The Islamic financial industry has been steadily growing worldwide for the last few decades, which has expanded the range of Islamic financial products offered by the IFIs, considerably. It is worth mentioning that with the increase in the financial depth of the Islamic financial industry, the need for more refined Islamic financial products which can increase liquidity, develop secondary markets, and improve risk management, is also increasing (Abbas, 2015; Askari & Iqbal, 2013).

It is important to realize that Islamic financial engineering is subject to the rules defined by the *Shariah*, which makes it more complicated as compared to conventional financial engineering. According to the *Shariah*, any financial instrument is permissible if it does not contain elements prohibited by Islam, such as *Riba*, *Gharar*, *Qimar,* and *lkrah* (coercion) (Sheikh & Khan, 2018; Iqbal, 1999).

The prohibition of *Riba* is a major Islamic belief and among the basic building blocks of the Islamic financial system. A very comprehensive definition of *Riba* is as follows: "*Riba* means and includes any increase over and above the principal amount payable in a contract obligation, not covered by a corresponding increase in labor, commodity, risk or expertise." According to this definition, the term *Riba* includes both usury and interest (Ayub, 2007). The prohibition of *Gharar* is another basic building block of the Islamic financial system. *Gharar* is found in any contract if parties to the exchange lack in the knowledge of the subject matter or there is reasonable doubt regarding the control of either party over the completion of the exchange (Saleh, 1992). The prohibition of *Qimar* is also among the basic building blocks of the Islamic financial system. The term *Qimar* refers to gambling. It is applied to all those contracts whose outcomes are uncertain and one party gains at the cost of the other party. Therefore, Ayub (2007) asserted that *Qimar* resembles *Gharar* because the gambler is uncertain whether he would win or lose. The term *Ikrah* indicates coercion or imposing a contract/condition on a party, forcefully (Iqbal, 1999). It is worth mentioning here that Islam wants people to earn their livelihood through legitimate efforts and should not devour others' property unjustly or forcefully (Saleem, 2013).

Financial engineering in conventional finance relates mostly to derivatives (Al-Suwailem, 2007). According to Chance and Brooks (2015), a derivative is a security and/or a contract and its value is derived from some underlying assets. The underlying assets can be anything like commodities, agricultural products, metals, energy products, financial assets including stocks and bonds, interest rates, and currency rates. Importantly, derivatives are of the following four types: (i) forwards; (ii) futures; (iii) options; and (iv) swaps. It is pertinent to note that forwards and swaps are the most customized contracts, which are executed without any guarantor/moderator. While, options are contracts that give their holders the right, but not the obligation, to buy/sell an underlying asset at a specified 'strike price' by a certain 'expiration date'. Futures contracts, however, are standardized legal contracts concluded in futures exchanges where contracting parties are protected from counter-party risks. Futures contracts obligate the contracting parties to buy/sell an underlying asset at a predetermined price, regardless of the market price at the expiration date (Anwer & Habib, 2019; Ayub, 2003).

The majority of the *Shariah* scholars believe that derivatives have certain prohibited elements, such as *Riba*, *Gharar*, *Qimar*, *Maysir*, and the sale of one debt for another; moreover, derivatives are mere transactions that are devoid of any real/productive activities (Mansuri, 2022; Akhter-Uddin & Ahmad, 2020; Ayub, 2003; Usmani, 1996). Therefore, derivatives are unacceptable according to the *Shariah* principles. However, Kamali (1999) argued that futures and options, whose underlying assets are agricultural products, can be beneficially used for hedging purposes to protect farmers and the food production industry against price risk. He asserted that such futures and options would facilitate risk management, and therefore, are permissible based on *Maslahah* (public interest). Similarly, the Securities Commission Malaysia's (2020) *Shariah* advisory council resolved the permissibility of derivatives based on *Maslahah, Urf Tijari* (common business practice), and avoidance of hardship.

The development and popularity of the *Sukuk* market is another area of Islamic financial engineering. SSBs play an important role to evaluate the legitimacy of *Sukuk*. The approval of SSBs to structure and issue a new *Sukuk* affects its acceptance and hence, its performance in capital market (Ahmed et al. 2019; Utami et al. 2019). Kachkar and Mustafa (2022) argued that the structure, size, and qualification of the SSB members affects the performance of the financial products.

Islamic financial engineering is required for improving the efficiency of the Islamic financial markets. However, it should not come at the cost of *Shariah* compliance, which is considered as the underlying reason for the establishment of IFIs. Iqbal (1999) suggested to use two different approaches, namely reverse engineering and innovation, for Islamic financial engineering. In the case of reverse engineering, an existing conventional instrument is evaluated to find its closest *Shariah*-compliant substitute. A major advantage of this approach is that it gains recognition from conventional finance practitioners; hence, Islamic financial markets can easily be integrated into the conventional financial system, worldwide.

Researchers have argued that reverse engineering or imitation might help the Islamic financial industry in its early developmental stages. Although, in the long run, it has certain drawbacks. Firstly, it shows the preeminence of form over substance and means over ends. Secondly, it gives the impression that the Islamic financial industry always follows the conventional industry. If Islamic financial engineering is only based on replication/imitation, the conventional industry will always remain the leader in this regard. This is against the philosophy of creativity, and therefore, this approach remains in contradiction to the true sense of financial engineering (Al-Suwailem & Hassan, 2011).

The second approach of Islamic financial engineering is innovation, where new financial instruments are innovatively designed by applying *Shariah* principles (Vogel & Hayes, 1998). Resultantly, a new set of Islamic financial instruments, with a unique risk-return profile, emerges. This approach is closer to the true spirit of the Islamic financial system. However, designing new systems in different environments is always challenging and takes time. It is, however, worth mentioning here that the essential requirements of an Islamic financial system, which include efficient markets, information symmetry, *Shariah* compatible property rights, and regulatory laws do not exist in most Islamic countries. This innovative approach demands a high level of understanding of Islamic commercial law, Islamic economics, and that of the conventional financial systems as well (Iqbal, 1999).

Corporate Governance (CG) in an Islamic Perspective

In the early 1990s, CG gained importance in the developed world when the US and UK based corporations dissatisfied their shareholders due to their bad governance practices and poor performance (Hamid & Ginena, 2015). Moreover, the 2007-2008 financial crisis and the failure of several 'too big to fail' financial institutions made CG an important concern for academicians, regulators, and governments, globally (Ginena, 2014). Some other factors that contributed to the increased attention CG received worldwide included institutional investors' growth, globalization of financial markets, and deregulation of the financial sector (Iqbal & Mirakhor, 2004).

Researchers generally do not agree on a common definition of CG (Al-Amer, 2018). According to the Organization for Economic Cooperation and Development (OECD), CG involves relationships between different stakeholders of a company, including its shareholders, board, management, creditors, suppliers, and others. Moreover, CG provides the structure for setting a firm's objectives, the means to attain these objectives, and the ways to monitor performance (Johnston, 2004). Solomon (2020) defined CG as a system of checks and balances which ensures that companies remain accountable to their stakeholders and their business activities are performed in a socially responsible way. Butt (2016) defined CG as "the mechanism used to control and direct the affairs of a corporate body to serve and protect the individual and collective interests of all its stakeholders." In simple words, CG is defined as the system that helps to direct and control companies (Cadbury Report, 1992).

Nordberg (2011) listed the following two issues that CG seeks to address: (i) how corporations are directed and monitored and what are the different mechanisms available to make corporations perform better? and (ii) what are the different mechanisms available to ensure that corporations do not destroy the value for which they were created? In a nutshell, CG is arguably a framework for corporations which is essential to operate them efficiently (Al-Amer, 2018).

Corporations have become a global phenomenon. To establish an ideal framework for their governance, different approaches are used. Different CG theories have evolved, resultantly. The first theory is the agency theory. According to this theory, shareholders and managers are related as principals and agents, where agents (managers) are required to act in the best interest of principals (shareholders) and work towards maximizing their wealth (Solomon, 2020). However, due to the principal-agent relationship there arises agency problems, which are "difficulties financiers have in assuring that their funds are not expropriated or wasted on unattractive projects" (Shleifer & Vishny, 1997). Agency theory assumes that due to the power the managers have, they can be engaged in transactions benefiting themselves and promoting their self-interest, while ignoring the interests of their owners (Letza et al., 2004).

The proponents of the agency theory argue that agency problems can be solved by focusing on the Board of Directors (BOD). The BOD should be composed and structured in a manner that it represents shareholders and balance shareholders' as well as managers' demands, and prevents tensions among them (Nordberg, 2011). To solve the agency problem, a corporation may be viewed as a collection of contracts between individuals. This theory helps to safeguard shareholders' interest by introducing incentives for managers based on a contract that specifies their duties, rewards, and shareholders' right to monitor their performance (Fligstein & Freeland, 1995). This theory aligns managers' interests with shareholders' interests and gives greater importance to shareholders. Moreover, the company is viewed as the BOD's promise to shareholders that their wealth would be maximized (Keay, 2008).

The second most important CG theory is the stakeholder theory. According to this theory, the objective of a corporation is not only to maximize its shareholders' wealth; rather, corporations are responsible for the well-being of all their stakeholders. In a broader context, a corporation has a responsibility towards the whole society (Fligstein & Freeland, 1995; Letza et al., 2004). The logical basis of stakeholder theory is that stakeholders provide the essential resources for corporations. Hence, their interests need to be safeguarded (Keay, 2010).

The third most important CG theory is the stewardship theory which contradicts the agency theory. This theory assumes that managers are not opportunistic and their behavior, as well as decisions, are not based on their personal interests and self-dealing. They simply want to do a good job and be good stewards of the companies they work for. Due to this assumption, shareholders' voice and board representation should not be concerned; rather, the focus should be shifted towards providing a clear and consistent role, expectations, and authorizing and empowering executives to achieve their best performance (Donaldson & Davis, 1991).

The link between CG and Islamic principles has been discussed by many researchers (Al-Amer, 2018). Some researchers have suggested a totally different CG model for Islamic corporate bodies due to their unique characteristics (Muneeza & Hassan, 2014; Choudhury & Hoque, 2006). However, according to Iqbal and Lewis (2009), the parallels between the Islamic approach to CG and the stakeholder and socially responsive corporate paradigms should be examined potentially. Approving this viewpoint, Iqbal and Mirakhor (2004) argued that Islamic principles provide a sound basis for the stakeholder theory. Their viewpoint is basically derived from two important Islamic beliefs concerning property rights. The first belief is that all property belongs to Allah (SWT), while people are custodians or stewards. According to the second belief, the ownership of property belongs to the community as a whole, whereby a property's possession does not give people the right to use it exclusively, rather it remains a priority over others to use it. Under these circumstances, property owners are prohibited to waste or squander it. Moreover, the owners of a specific property are not allowed to use it in a way that possibly affects their neighbors injuriously.

Some researchers consider stewardship theory as more compatible with Islamic CG, since managers are considered as stewards performing their duties following Islamic beliefs (Obid & Naysary, 2014). The self-dealing assumption of the agency theory is not rejected either. From the perspective of the agency theory, obedience to the *Shariah* principles could intensify the agency problem. For example, many investors in IFIs demand *Shariah* compliance of their investments along with returns (Al-Nasser & Muhammed, 2012). Thus, in conventional companies, agency problem arises when managers fail to maximize shareholders' wealth. However, in the case of IFIs, if managers fail to place funds into *Shariah*-compliant investments, an additional source of agency problem is created (Safieddine, 2009).

Islamic CG cannot be separated from conventional CG. Broadly speaking, Islamic ethical system leads to the welfare of an individual and society in general. Seemingly, it is inclined towards the stakeholder theory but can be linked to different CG theories by adding more ethical standards. It is pertinent to note that Islam does not provide a detailed CG mechanism that contradicts modern CG theories and mechanisms. Therefore, Islamic ethical values merged with CG might help in developing an ideal governance structure that minimizes corruption (Iqbal & Lewis, 2009).

Role of SSBs in Islamic Financial Engineering and CG Structure

While SSB is considered as the nucleus of an IFI in the SG context, its framework is, however, alien to CG (Al-Amer, 2018). According to Fatmawati et al. (2022), SG is an exclusive governance mechanism of IFIs in which SSBs play the most important role to ensure *Shariah* compliance. This section critically reviews the role of SSBs in Islamic financial engineering and compares it with the role of BODs. It is pertinent to note that the said comparison would enable SSBs to be recognized in the modern CG structure.

Shariah compliance is the main concern of the CG of IFIs which are required to avoid all *Riba*, *Gharar*, and *Qimar* based transactions, short-selling, and any risk-free return based on a mere financial transaction without making any value addition in the real economy (Ayub, 2019). For this purpose, all IFIs are duty bound to appoint their SSBs to undertake the management, supervision, and auditing of all their transactions (Aribi et al., 2019). The literature, however, lacks a standard definition of SSBs (Garas & Pierce, 2010). According to Al-Khelaifi (2003), the available definitions can be categorized into two different types. The first type of definitions focus on different aspects of SSBs' functions. While, the second type of definitions stress *Shariah* supervision, the task SSBs are entrusted with. The first category is the most common and the one adopted by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and Islamic Financial Services Board (IFSB), the two most prominent Islamic financial standard-setting organizations. According to AAOIFI (2022a), an SSB consists of jurists having a vast experience in *Fiqh Al-Muamalat* (Islamic commercial jurisprudence). These jurists are able to consistently direct, review, and supervise the activities of IFIs in order to ensure their *Shariah* compliance. The definition given by the IFSB (2009) describes SSBs more generally as a group of *Shariah* scholars acting in the capacity of special advisers to the IFIs.

The second type of definitions mainly focus on *Shariah* supervision, objectively. *Shariah* supervision may be defined as the process of controlling, reviewing, and analyzing all business activities of IFIs in order to ensure their *Shariah* compliance and to mitigate the *Shariah* non-compliance risk in order to earn permitted (halal) profits and improve the performance of the IFIs (Garas & Pierce, 2010). SSBs are not exclusively responsible for *Shariah* supervision because other SG mechanisms share the same objective; however, they still remain the dominant source and authority of *Shariah* supervision, while all other mechanisms are linked to them (Al-Amer, 2018).

The main objective of SSBs is to maintain the confidence of the stakeholders of the IFIs regarding the *Shariah* compliance of the financial services offered and other transactions performed by them (Ayub, 2019; Zainal-Abidin et al., 2020). To achieve this objective, AAOIFI (2022a) assigns SSBs the duty to review, supervise, and direct all the activities of their respective IFIs. IFSB (2009), however, classifies an SSB's duties into the following two categories: (a) ex-ante and (b) ex-post. The first set of duties are those performed during the product development stage. These duties include issuing *Fatwa* or *Shariah* standards and checking the compliance of new products before introducing them to clients. The second set of duties are performed afterwards. These duties include a *Shariah* review and *Shariah* reporting. Some researchers also highlight the intermediate-level duties of SSBs. These duties are performed at the time of the offering of new products. These include *Shariah* advisory in different situations arising either due to regulatory constraints or customer demands (Hamid & Ginena, 2015).

In general, SSBs are authorized to consider, decide, and supervise all *Shariah*-related matters (State Bank of Pakistan [SBP], 2018). In SG literature, there also exists a classification of SSB roles depending on their nature, that is, SSB roles are either advisory or supervisory (Garas & Pierce, 2010). Al-Amer (2018) argued that the three main roles of an SSB are that of a legislator, consultant/advisor, and auditor.

Arguably, the role of SSBs as a legislator is very important. If any financial contract is not present in *Fiqh Al-Muamalat*, then SSBs are authorized to interpret the *Shariah*, issue *Fatwa,* and hence, legislate the IFIs' transactions before offering them to the clients (Garas & Pierce, 2010). Moreover, some SSBs are assigned the task of educating the public regarding *Shariah* matters related to Islamic finance. This role is similar to the role of regulatory authorities in educating the general public on matters associated with different regulations (Al-Amer, 2018).

SSBs also perform advisory and/or consultancy roles in which they assist the management of IFIs in *Shariah* compliance. Generally, SSBs ensure the *Shariah* compliance of the IFIs' financial products, financial contracts, and financial services before they are offered to the customers (SBP, 2018). SSBs check new proposals for financial transactions to decide about their *Shariah* legitimacy and recommend any necessary amendments. It resembles the advisory role of lawyers in deciding the legality of a specific transaction. It also bears a resemblance to the non-audit work performed by audit firms to make companies comply with international standards on accounting and auditing. Importantly, the advisory role of SSBs includes discussions on financial product development with the concerned executives for developing *Shariah*-compliant financial instruments and help in mitigating the *Shariah* non-compliance risk (Hamid & Ginena, 2015). IFIs consult their respective SSBs during the implementation stage of new financial products in case any ambiguity related to any *Shariah* aspect arises (Garas & Pierce, 2010). Advisory from SSBs is also required while calculating the *Zakat* of IFIs, disposing of any non-*Shariah*-compliant earnings, and distributing profits among shareholders and Investment Account Holders (IAHs) (Iqbal & Greuning, 2007).

Financial products are audited post-offering to check their *Shariah* compliance. The major aim of auditing is to ensure the *Shariah* compliance of all financial services offered by IFIs (Al-Amer, 2018). SSBs review and audit all procedures for implementing innovative financial products and also their respective IFIs' financial statements (Garas & Pierce, 2010). Afterward, they issue a report regarding their respective IFIs' *Shariah* compliance, which is an integral part of the IFIs' annual reports (Grais & Pellegrini, 2006). According to AAOIFI (2022b), *Shariah* review examines the *Shariah* compliance of all financial activities of IFIs. Internal *Shariah* audit departments are established by IFIs to assess the *Shariah* compliance of all their activities. Moreover, the said department assists SSBs in conducting research, training programs, and performing their auditing duties (Hamid & Ginena, 2015).

All the aforesaid roles of SSBs are crucial for the Islamic financial industry. Regulators need to recognize that a high level of independence is mandatory for both legislative and auditing roles. In case the required level of independence is not ensured, Islamic financial industry would face susceptibility to failure due to lack of general public trust in *Shariah* compliance of its products and activities (Sori et al., 2015). Grais and Pellegrini (2006) identified the lack of independence as a challenge that constrains SSBs' ability to fulfill their responsibilities. It is worth mentioning here that IFIs' profitability is dependent on the trust of the general public in their *Shariah* compliance, which is further linked to the independence of their respective SSBs (Al-Amer, 2018).

To summarize, the various roles of SSBs as a legislator, consultant/advisor, and auditor are pivotal in Islamic financial engineering for developing innovative Islamic financial instruments that not only enhance liquidity and offer risk management tools but also conform to the *Shariah* principles. As a legislator, an SSB issues *Fatawa* regarding its respective IFI's product development. While, as a consultant/advisor, it guides the product developers in developing *Shariah*-compliant products and helps to mitigate the *Shariah* non-compliance risk. Finally, as an auditor, it constantly reviews and audits all procedures related to the implementation of new Islamic financial products.

In the end, the similarities between the various roles of SSBs and BODs are discussed. Importantly, this comparison would help to embed SSBs in the modern CG structure. According to Johnson et al. (1996), the responsibilities of BODs can be categorized into the following three broadly defined roles: (i) control; (ii) service; and (iii) resource-dependence. Control involves BODs' monitoring of management on their shareholders' behalf. In this capacity, BODs are responsible for hiring and firing top management, determining their remunerations, and ensuring that managers do not expropriate the interests of shareholders. Service role involves BODs' consultation with the top level management regarding administrative and other managerial issues. The resource-dependence role of BODs is their responsibility of acquiring resources critical to a company's success.

The similarities between the various roles of SSBs and BODs have been reported by several researchers (Al-amer, 2018). In this context, Nathan and Ribière (2007) argued that SSBs have roles similar to that of BODs but to a narrower extent, since SSBs monitor and control only the religious side of the IFIs. They constantly review and approve all financial transactions of their respective IFIs, their innovative financial products, and their SG related policies. Moreover, SSBs appoint internal *Shariah* auditors. The service role of BODs is presumably similar to SSBs' advisory/consultancy role, where SSBs advise the management of their respective IFIs on all *Shariah*-related matters and train their executives about the implementation of Islamic rules and regulations. Finally, the resource-dependence role of BODs is similar to SSB's right of accessing all information required for making decisions regarding the *Shariah* compliance of IFIs.

A high level of independence is required by SSB members to perform their different roles. They should not be considered as their respective institution's employees, nor should they be influenced by the BOD or management (Warde, 2010). This leads Morrison (2014) to assume a two-tier board system, so that SSBs may be incorporated within the CG structure. For this purpose, Malkawi (2013) suggested that an SSB needs to be considered as a supervisory board, while the regular BOD is expected to operate like a management board. Al-Dohni (2008), however, asserted that an SSB might be considered as a supervisory board only in *Shariah*-related matters. However, in the case of all non-*Shariah*-related matters, the regular BOD has the authority (Al-Amer, 2018).

Conclusion

Shariah supervision holds an extremely important position in the IFIs' corporate governance structure. *Shariah* non-compliance risk arises when an IFI fails to comply with *Shariah* principles in providing financial services. Consequently, the transaction is canceled and hence the income cannot be recognized as *Halal*. Moreover, the reputation of IFIs would be damaged. Resultantly, IFIs would suffer financial losses because their profitability is dependent on the general public trust regarding their *Shariah* compliance. To mitigate the *Shariah* non-compliance risk, IFIs appoint renowned *Shariah* scholars who are well-versed in *Fiqh Al-Muamalat* generally and Islamic financial transactions particularly, on their SSBs.

The major responsibility of SSBs is to ensure that all activities of their respective IFIs are in conformity with the *Shariah*. Furthermore, SSBs develop SG policies and implement them, approve and develop innovative financial products, monitor IFIs' functions, identify problems, and outline solutions. Interestingly, Islamic financial engineering is an important task SSBs are entrusted with. According to one definition, financial engineering is described as "principles and strategies for developing innovative financial solutions". It is worth mentioning here that Islamic financial engineering is required to improve the efficiency of the Islamic financial markets but not at the cost of *Shariah* compliance, which is the underlying reason for the existence of IFIs.

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