A critical assessment of the Islamic Banks governance under English law: legal pioneering or pragmatic adaptation?

Dr. Nehad Khanfar
Islamic College-Middlesex University, London-UK

Abstract:

In the last ten years Islamic banking and finance became part of the British financial market debate. More, financial, academic, consultancy firms, and individuals showed interest in Islamic banking, financial products and transactions. Based on unprecedented interest and demand, the British government and regulatory bodies were urged to regulate Islamic banking to comply with English law and regulations. In other words, the government would not afford losing the potential adding value of Islamic banking and finance, and needed to have Islamic banking activities law compliant. Despite the fact that Islamic banking comes from different legal theory and adopts different law philosophy from English law, the government was required to regulate Islamic banks and Islamic financial activities, governance included, to comply with the law of land. To some extent, the Financial Conduct Authority (FCA) previously called FSA (Financial Services Authority), gradually, succeeded to develop regulation of Islamic financial activities in order to incorporate it within the English legal system. This paper, will critically examine to what extent the UK regulatory bodies succeeded to create clear rules of Islamic bank's governance. It also aims to critically assess how creative the legislators were in establishing legal rules combining two different legal philosophies. Furthermore, this paper will analytically investigate whether Islamic bank's governance is crafted and positioned using a pioneering legal approach or was pragmatically adapted as a response to the circumstantial necessity.

Introduction:

Islamic finance and banking started to attract serious attention of the UK's regulators in mid-90s. This was part of the rapid and significant growth of Islamic banking and finance on global financial arena. On one hand, there was high interest in providing a platform for Islamic finance in London as part of its tradition in 'competitive innovation', on the other hand, knowing that Islamic finance and banking by nature radically differ from conventional ones, regulatorsneeded to deal with specific issues in order to incorporate Islamic finance into English legal/financial systems.

"As banking regulators, the Bank of England and, from 1998, the FSA (Financial Services Authority) have been open to the development of Islamic finance in the UK for some time. The first important signal was given in a speech by Lord Edward George, then Governor of the Bank of England, in September 1995 at a conference organised by the Islamic Foundation. In this, he recognised the 'growing importance of Islamic banking in the Muslim world and its emergence on the international stage' as well as the need to put Islamic banking in the context of London's tradition of 'competitive innovation'." (www.fsa.gov.uk, 2003, p8). As a side note, FSA (Financial Services Authority) has been replaced by FCA (Financial Conduct Authority) after April 2013. It acts as the regulatorof financial firms who wish to operate in the UK.

In the meantime, the Islamic finance continued to develop in the UK and witnessed the founding of the Islamic Finance Council in Scotland in 2005. This was followed by establishing the special sub group in 2007 to build a strategic plan to promote UK as an international hub of Islamic financial services.

This positive development further enhances the growth of Islamic finance industry in the UK and put it as one of the main growing trends in banking and financial sectorin the country. For the regulators, it becomes a necessity to pave the way forward for Islamic banking and finance to settle into the banking system of the country. As concept of the Islamic banking is imported

from different Islamic religious/legal philosophy, the English law maker, and as such the regulator needed to be as creative and pragmatic as possible to be able to incorporate Islamic banks into the UK banking industry.

In this paper, there would be an attempt to critically analyse the trend of the UK regulators in dealing with Islamic bankingand its legal/financial requirements with corporate governance to be mainly considered in this discussion. Furthermore, it will also critically examine whether the UK regulators, regarding Islamic corporate governance, pioneered legal solution or adopted a pragmatic approach. Thus, Sharia board and its role in corporate governance of Islamic banks will be one of the key elements of the paper's discussion.

1.1 An induction to a pragmatic approach

In 2000, HM Treasury and the Bank of England launched a working group to investigate the viability of Islamic finance in the UK. Sir Edward Georgewas the initiator of this group which included the Governor of the Bank of England, members representing the Treasury, the Council Mortgage Lenders, the Muslim Council of Britain, banks and Financial Services Authority (Briault, 2007, p48).Sir Howard Davies, as a chairman of the FSA (Financial Services Authority) in 2003, announced that 'he had no objection in principle to the idea of an Islamic bank in the UK'. (FSA, 2003, p9).

Showing more pragmatic signs and flexible approach Sir Edward George argued that UK had 'a cleareconomic interest in trying to ensure that the conditions for a flourishing Islamicmarket are in place in London'. He went on saying that introducing Islamic finance would benefit the Muslim consumers and support the concept of 'innovation anddiversity' in London market and promote it'as an international financial centre' (Ibid, p9).Translating this practicality and pragmatically, it did not take much longer to get the Islamic Bank of Britain authorised and operating as

a whole and independent bank in 2004(www.islamic-bank.com, 2007). It has been followed by authorising the European Islamic Investment Bank in 2006 with a balance sheet of £302m. (www.eiib.co.uk). Then the authorising and launching of the Bank of London and the Middle East came in 2007, 'with a start-up capital of £175m (www.blme.com). This continued, relatively, in rapid track to authorise 'Islamic hedge fund manager' and Islamic Takaful provider (www.amiricapital.com).

Currently the UK, particularly the City of London, gained its prominent position to set as the 'third largest market of Islamic finance after the Gulf Co-operation Council states (GCC) and Malaysia' (Ercanbrack, 2011, p27). It is worth highlighting that the attempt to present Islamic financial services launched in 1980s in the UK. In 1982 Al Barakah Bank being the first full-fledged Islamic bank. Failing to comply the regulators' requirements the bank was closed down by the Bank of England in 1993 (Housby, 2005, p73).

As a matter of fact, this impacted on the UK regulators when dealing with Islamic financial institutions in the UK. The financial authorities become more vigilant when it comes to corporate governance in Islamic banks operating in the UK. Having said that, it is also important to note that the financial authorities granted more licences for more Islamic banks to work in UK, such as Islamic bank of Britain (currently taken over by Al Rayan Bank and working under this name). In addition to other Islamic financial retailers who offer Islamic financial products in the market since 1990s(HM Treasury, 2008). Keeping the door open to authorise more Islamic banks after a negative experience would be translated as part of the pragmatic legal approach adopted by the UK regulators. As mentioned earlier, when Al Barakah Islamic bank failed to comply or meet the legal requirements and good governance, it did not prevent the governments and regulators from attracting and promoting the UK to serve as an international hub for Islamic finance and banking.

1.2 Governance under English Law

Protecting the stakeholders' interests stands at the core concerns of the governance. The protection goes beyond the financial interests to other intangible elements that concern the stakeholders such as beliefs, morality or ethics, and religion (Grais and Pellegrini, 2006, p2).The Organisation for Economic Co-operation and Development (OECD), considered the corporate governance to be a set of rules to control and directthe companiesin order to protect the interest of shareholders and other stakeholders aiming on sustaining and enhancing value(Stanley, 2008, p46).

The UK, derives and designs its laws and regulations based on theNeo-Liberalpolitical and economic philosophy,where common law is the core of its legal system, which heavily and steadily relies on precedents. This forms the solid foundation of pragmatic tradition of the English law (Atiyah, 1987, p59).As for financial and economic matters, it makes the government intervention in capital markets at low level. This is a self-explanatory instance for presenting a pragmatic method of tackling legal and regulatory aspects in connection to finance, and consequently, Islamic banking. Hence, there is an evident tendency, usually, that shareholders are given protection more than other parties(Cook and Deakin, 1999, p5).

1.2.1 Agency Theory

One of the main models of governance is adopted in the UK is agency theory. The theory was established and developed to answer the questions that are risen in relation to governance in the event 'of separation of ownership' (shareholders) and control (management)in industrial corporations (Al-Sadah, 2007, p2). Mainly, the theory is built on contractual basis between the management that is qualified to manage the corporate, and the investors or shareholders in order to run the business rationally and professionally on behalf of the latter party (investors). That is to

say that the investors may not be equipped with the managerial skills or do not have the time that arenecessary to carry out the business operations and activities (Chowdhury,2004, p27).

According to this theory, governance standards, are structured to separate between the ownership and management which is commonly known as the 'agency problem. In the meantime, some assurance standards should be placed to ensure that the management's actions are taken to preserve the interests of both shareholders and stakeholders (Stanley, 2008, p45).This seems not always the case, where it has been an argument that agents may not always carry out their managerial duties in the best interest of the shareholders or investors. This is due to the fact that there might be a tendency from the agents to pay more attention to their interest rather the shareholders' (Smith, 2011, p35).It is worth noting that there is no real mechanism (legally or otherwise) that could provide an assurance to have the management acting to achieve the best results on behalf of the investors (Fontrodona and Sison, 2006, p13).

1.2.2 Anglo Saxon Model

"This model is well known as market based model and used by United States of America in addition to United Kingdom of Britain. This model concerns about the maximization of shareholder value and just looks after the shareholder interests through increasing profitability and efficiency". (Hasan, 2009, p22).

Looking into governance systems in different countries including Germany, USA, Japan, and UK (Shleifer and Vishny, 1997, p81) concluded, through their survey, United Kingdom enjoyed a distinctive system that provides the investors with a strong legal protection.

Due to the legal nature and philosophy of the English law and regulations which rely more on precedents and case law, in which, the legal structure is more elastic. Based on that, it would

be clearly noted that the regulatory framework of governance in UK is considered to be a self-regulated system.(Chowdhury, 2004,p119).This automatically means that although the government and related departments enforce specific rules to regulate financial and banking institutions there is a wide room for flexible and adaptable structure for governance.

As it was noted by the international Chamber of commercethe model of Anglo Saxon concentrates the ownership in hands of few people who, through executive chairman, enjoy an influential powers and authorities over the management, this has been led by the "ideas of shareholder primacy"(Schnyder, 2010, p13). This leaves minority investors in a vulnerable position against the owners and the management (http://www.iccwbo.org).

2.1 Islamic Model of Corporate governance:

It is a must requirement that any financial institution introducing Islamic financial or banking services or products comply with Sharia rules and principles. Compliance in this instance should come through corporate governance by which the Islamic financial industry would achieve stability and confidence (Grais and Pellegrini, op.cit, p6).

In this context the Sharia principles which are mainly derived from Quran and prophetic traditions (Sunnah) would not be on different stands from good governance as in conventional financial institutions. That is to say, morality, ethics, transparency, honesty, accountability, and documentation would stand at the heart of Islamic financial entities and banking operations (Farouk, 2015, p14). Hence, there would be no contradiction or harm by imposing conventional corporate governance on Islamic bank and its operations. It is rather a positive element and a strengthening factor to get Islamic finance incorporated in the global financial market (Stanley, op. cit).

Due to the special nature of Islamic banking, where the bank

does not deal with interest, neither charging nor paying. Instead, the relation between Islamic bank and the depositors built on a profit-loss sharing. This impacts seriously on the Islamic bank's corporate governance. Therefore, in this instance, a special consideration should be given to "the corporate governance implications of the obligation of an Islamic bank to operate in accordance with the rules and principles of the Shariah" (Al-Sadah, 2007). Corporate governance model in Islam encompasses exceptional elements and offers characteristic features compared to the Anglo-Saxon corporate governance concept and models. It contains the element of tawhid (Islamic Principle of monotheism) where Allah (God) is always watching and observing over us, shura (the Principle Consultation) where decisions are taken after going through discussion process (Hassan, 2009, p57).Applying these rules on commercial and financial transactions entails that Islamic corporate governance must be established with morals, fairness and honesty (Hafeez, 2013, p100).

From Islamic perspective the corporate governance has a specific objective which is mainly to preserve or protect the rights of stakeholders to mitigate the risks that might occur because of the actions of organisation(Iqbal and Mirakhor 2004, p66). It has to be stated that the main mission of the Islamic corporate governance is providing a protection for stakeholders as they are to be considered the weaker party in the financial equation (Toufik, 2015, p113). This comes by creating the balance between the interests among the different groups who represent them. This protection would be based on Sharia principles (Hafeez, 2013).

Adding more elements to corporate governance in Islamic finance (Haqqi, 2014, p29) argued that this kind of corporate aims to enhancing disclosure and transparency, encouraging and improving professionalism, and decreasing the mistakes and strengthening the good practice functionality of governing bodies in Islamic banks. It is about establishing and strengthening the confidence and trust among investors and stakeholders (Ibid,

p114). The Sharia supervisory board sets at the heart of corporate governance and plays a crucial role in the Islamic banks' governance. Thus, it shapes and is considered to be one of the main principal constituent of the Sharia governance framework (Hamza, 2013, p12).

The role of Sharia board which refers to an active supervision of implementation of Islamic law principles in Islamic banks is encouraged and supported by "international institutions of regulations like Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI) and Islamic Financial Services Board (IFSB)" (Miskam, Nasrul, 2013, p456). This comes in light of the fact that, in the UK, there is no particular governing legislation to guide or direct Sharia governance framework where regulators would just step in case of serious misconduct that may impact on the industry badly (Hasan, 2010, p83)

As far as structure is concerned the model of Islamic corporate governance tends to be dependent on the stakeholder one. The stake which is classified to be a property rights that 'might be at risk' because of bank conducts. Hence, it is the duty and responsibility of the bank to protect, equally, the stakeholders' property rights in addition to shareholders. According to Iqbal and Mirakhor (2003; 2004) stakeholders may include either individuals or groups who enjoy an 'explicit or implicit contractual obligations' with the corporate or company. The legal power of Sharia board would be taken/given by different sources, and mainly by regulators (Wilson, 2009, p74).However, Sharia supervisory board, under shareholders of Islamic bank, would be given supreme position in governance structure compared to other elements that form the governance system. Based on that, Sharia board has the authority to decide over its own internal ruling policies, tasks, responsibilities, and also concerning its relations with other governance aspects and parts within IFI (the Islamic financial institutions) (Garas and Pierce, 2010, p69).

2.2 English law approach towards the governance of Islamic bank

The Islamic banks in Britain are established and registered as public companies limited by shares. They are structured based on a two-tier board or Dual Board systemwhich comprises'a management board and a Shariah Board'. Having mentioned that, in one hand, there is no indication in The Companies Act 2006 ('the 2006 Act') if the company in UK required one or two boards; on the other hand, in (s 155) of the same act stated that 'Companies required to have at least one director who is a natural person'. Also there is no indication, whatsoever, if directors could play a role as board members or not. This gives a direct and indisputable evidence that the structure of Dual Board and non-executive directors (Shariah Board) in Islamic financial banks and institutions is legally accepted and functional under English law(Morrison, 2014, p51).

Unlike the UK, different approach can be found in a country like Jordan asIslamic banking is well established, where Banking Code Art. 58(a) states that the Sharia board should encompass at least three members with a binding authority on the Islamic bank.The same situation applies to Bahrain as theyadopt 'The AAOIFI Principles on Corporate Governance' (AAOIFI, Governance Standard for Islamic Financial Institutions No. 1, sec. 2.).

As an evidence of the pragmatic legal approach, it is not obligatory under English regulatory law for the Islamic banks to establish a Sharia board. It is worth noting, there is a legal freedom given to Islamic banks to decide what arrangement fits their structure and better for their functionality in one hand.Furthermore, in the otherhand, regulators even have no concern or interest in regard to Sharia compliance, instead, all related issues are delegated to every individual Islamic bank to select the best suitable framework to fit their structure, 'but subject to proper disclosure to its Stakeholders' (Khan et al, 2015, p636).

Moreover, the Financial Services Authority (FSA), currently known as FCA (Financial Conduct Authority) requires Islamic banks to prove that Sharia board, if it took place, does not have executive roles or interference in the bank management. In other words, the bank has to show clear evidence that Sharia board role is restricted within its supervisory or advisory position(FSA, 2007, p13).By observation, it seems to be that Islamic financial institutions in UK strictly committed to the advisory role of Sharia boards with no indication or report to imply otherwise (Wilson, 2007, p66).

This certainly comes in the same line of the pragmatic methodadopted by English law where it gives a room for the Sharia board to be part of the Islamic banks' structure but with no executive involvement. It does also show, to some extent, how English regulator can be innovative to adapt itself with other legal systems and law philosophies who do not share similar values. Pragmatism is the key point here, with no compromise of law enforcement and implementation.

It is important to note that English courts would not be able to implement or refer to Sharia (Islamic law) when ruling over Islamic financial transactions or deals (Foster and Neo, 2013, p31).It has been justified that there is no unified interpretation of Islamic law to act upon as a reference under English judicial system. Even for who argue that Islamic law relies on precedents as much as English law, it would prove that precedents are not really strictly binding as much as they would in its English counterparts (Morrison, 2014, p29).

3.1Non-discriminatory regimeisa pathway to a pragmatic adaptation

It is fair to say that when FCA (Financial Conduct Authority), previously (FSA), authorises a financial institution to operate in the UK it has to fully comply with standards introduced by the authority and other relevant regulators (HM Treasury, 2011, p51).

There is no special consideration or treatment to any institution based on its financial speciality, or religious/faith principles, or its country of origin. “This approach is fully consistent with FSMA’s six Principles of Good Regulation, in particular, facilitating innovation and avoiding unnecessary barriers to entry or expansion within the financial markets” (www.fsa.gov.uk).

‘There is, a level playing field’ in dealing with applications from conventional and Islamic firms’. This by itself is a vibrant proof that English law and legal system altogether enjoying a high level of pragmatism in giving an equal chance to Islamic banks to function and offer financial products which are totally initiated and belong to other religious legal/economic philosophy (FSA Annual Report, 2008/09, p32).

The ‘level playing field’ “have aimed at enacting legislative changes to ensure a level playing field for Islamic finance products, while not necessarily incorporating Shariah elements in the substantive law of the land” (Mejía, 2014, p13). Being willing and determined to initiate and carry out a process of legislative modifications to include taxation, legal and regulatory rules in order to ensure ‘a level playing field’ between Islamic and non-Islamic finance elaborate on the pragmatic inclination of English legislatorstowards other legal systems (https://auscifwp.files.wordpress.com, 2013, p34).

In doing so, English law paves the road to positively interact and flexibly absorbing legal rules and principles imported from other legal arenas. In addition, the FSA (Financial Services Authority) showed a serious interest in seeing Islamic financial industry developing in the UK(Dar, 2004, p18). Nonetheless, in his speech on September 2003 in Bahrain, Sir Howard Davies rightly said, that ‘it would not be appropriate, nor would it be legally possible, to vary its standards for one particular type of institution’. Reflecting on that, the FSA’s adopted undisputed pragmatic rule which says ‘no obstacles, but no special favours’ (FSA, 2003, p11). Once again, this rule is a reflection of pragmatic principles

and shouts loudly that English law is rationally capable and prepared to creatively deal with new legal/financial developments even if they are derived from a system who does not share religious or ideological roots with English law and its philosophy.

Although these standards have to be met by any kind of firms, but there might be a need to comply with a specific requirements of different sectors. For instance, the adequacy of financial resources such as capital would differ from what is required to be met by the bank. It is important to reconfirm that the rule of capital requirement would equally apply for both conventional and Islamic banks(Kammer, et al, 2015, p18). One more example to elaborate upon, and also falls under pragmatic approach of English law, that is the businesses are required to install 'reasonable systems and controls' 'to manage the type of business it wishes to undertake'. The threshold and the rules governing its arrangement 'are flexible enough to be as readily applied to an Islamic firm as to a conventional provider, whatever sector the firm is operating in' (Bank of England, 2014, pp7-8).Even when applying the rules of Financial Services and Markets Act (FSMA) to Islamic financial institutions, it would still need more work to be done in order to clarify some unclear areas. Nonetheless, no obstacles have occurred or presented that could not be tackled. Overcoming the obstacles is left and related to the corporation between the FCA (Financial Conduct Authority)and the institution to create pragmatic mechanism and design solutions (Belouafi and Chachi, 2014, p61).

3.2 Shari'ah Governance and the clear reflection of legal pragmatism of English law

As a starting point on Sharia governance in the UK, in addition also, to all what have been mentioned and discussed above, which come on the same line with what was 'highlighted by the Managing Director of the UK Financial Services Authority (FSA) while speaking at a conference in the Middle East:

1. protection of customers of Islamic Banks;
2. transparency (including issues relating to Corporate Governance);
3. professional competition (in differential and distinct aspects of Islamic banking in addition to competence in the conventional aspects of banking)'. (FSA, 2007, p62).

Despite the fact that Islamic banking, relatively, is a recent sector and still in need for more development in the UK, it appears to havea well-structured governance framework.There is, as discussed earlier, an announced clear policy by the UK authority in which conventional and Islamic finance receive equal legal treatment (Kammer, et al, 2015, p17). Therefore, IFIs,legally, are not required to establish Sharia board as part of corporate governance, regardless whether we are talking about banks branches or banks working on national level. However, in case of establishing this kind of bodies (Sharia board) as one of the governance elements the main concerns of the UK authorities would be from financial and operational side. This is in order to assure that the role of Shari'ah board in the IFIs is advisory and not executive. (Briault, 2007, p9).

Taking a close look into the practice of the working Islamic financial institutions (IFIs) in the UK market gives a clear example of the pragmatic legal position of the UK regulators towards Islamic banks. This is evident from the fact that Islamic banks in the UK are individually allowed to arrange their own Sharia governance without being obliged to adopt or adhere to a specific Islamic uniform national board or committee (Solé, 2007, p49). This could be logically predicted as the UK government is not expected to follow the Shari'ah governance approach since the UK adopt secular law and regulations not religious ones(Agnélio and Pita, 2014, p26).

There is an actual reflection of the freedom given to every indi-

vidual Islamic bank in forming its own Sharia board with no obligation to refer to a uniform governmental reference (Ercanbrack, 2011, p74).This was also translated into the number of the members of Sharia board, whereAl Rayan Bank, previously(Islamic Bank of Britain) and the European Finance House consist of three scholars.On the other hand, the European Islamic Bank and the Bank of London and the Middle East have four Shari'ahscholars. At the extreme opposite the Gate House Capital has just one scholar. This also would entail that the government would not intervene in choosing or appointing the board, or even defining who they are(HM Treasury, 2008, p19) apart from applying the rules of 'Approved Persons' rules, which equally applies to conventional banks.

Again, the variation of the structures of Shari'ah board in Islamic financial institutions in the UKshowsa flexible legal policy followed by the FCA (Financial Conduct Authority)and other UK regulators. Hence, in addition to this flexibility that is given to the IFIs in the UK to create and form the Sharia governance, proves to far extent the pragmatic response of the British legal system and the openness towards other legal systems and approaches.

This pragmatic approach might attract some serious criticism on confidentiality and the availability of Sharia scholars (HM Treasury, 2008, p26). This comes out of the fact that some Sharia scholarsact in three boards of different banks in the same time. Therefore, there would be a certain level of concerns in relation to conflict of interests and the question of confidentiality(Garner, 2013, p34). But it has to be pointed out that the criticisms would be raised as the concept of good governance under Islamic Financial law is ambiguous. In other words, there is no particular characteristics to be defined or uniformly identified by an official body or framework.(Ercanbrack, 2011, p127). To elaborate on this point, under English law, the Sharia scholar is not required to disclose that he/she sits on other boards of other banks. In order to avoid any kind of expected or unforeseen conflict of inter-

ests, it would be highly recommended, as part of good practice of good governance to get the scholars disclosing their multiple positions on Sharia boards. This comes out of the fact that Sharia board itself would be usually examining whether the bank adopting a good policy of disclosing facts about its activities (Sulaiman, 2015, p71). Based on this, without any shadow of doubt, disclosure would be part of good corporate governance exercised by those who are enjoying multiple membership of Sharia boards in the same time. More importantly, it should be supported by a specific regulation to enhance the transparency measures within Islamic finance institutions.

Due to the fact that there are no specific standards to be followed, every Islamic financial institution would need to deal with Sharia governance based on internal arrangement (Morales and Shiblaq, 105, p54). But generally this does not mean that Islamic banks are exempted from good governance rules and practices. They have to pay attention as much as any other financial institution by complying 'with its duties under the FCA's Principles for Businesses (PRIN) to take reasonable care to organise and control its affairs responsibly and with adequate risk management systems' (Ibid). Islamic banks usually, as any conventional bank, have to carry out an "internal and external audits are performed on a regular basis to confirm compliance with Islamic principles. Lastly, if the generation of interest is suspected, 'purification' systems have been put in place, mainly as donations to the poor" (Novethic, 2009, p11).

3.3The role of Sharia board under English law, legal pragmatism is the key!!

When the FSA (Financial Services Authority),currently called FCA (Financial Conduct Authority),studied and assessed the capability of the UK legal/financial system in absorbing the Islamic financial firms in the market, it 'has identified three main areas of potential difficulty which are common toIslamic applications'.

One of which is the role of Shariascholars (Ercanbrack, 2011, p20).

This role of the Sharia Supervisory Board (SSB) is defined by theindustry by its kay aims. One of which is, that the board members(scholars)have to make sure thatthe structure, and mechanism in processing the products and transactions are Sharia compliant (Sasan, et al, 2014, p24).In practical term, after a thorough examination and assessment of a new designed transaction or product introduced in the bank, and when Sharia board is satisfied of itsSharia compliance, the approval will be issued(Morrison, 2014, p104).

As the regulator, though, is not religiousand supposed to bea secular body. Therefore, it has no role, and it would be out of its capacity,to adopt or give an opinion over 'different interpretations of Sharialaw' (Global Islamic Finance Report (GIFR), 2010). Holding this clear position by the UK regulators, once again establish the idea of the legal pragmatic attitude held regarding Islamic banking. This simply introduces Islamic banking "to be an acceptable financial innovation whose presence further promotes that jurisdiction's standing as an international financial center"(Song and Oosthuizen, 2014, p7).Nevertheless, there is a legal requirement for theregulators to exactly know, from a practical and financialstandpoint, about the role of the Sharia Supervisory Board (SSB)and its functionality in Islamic banks. More importantly, to make sure to keep it within supervisory contribution (Hasan, 2010, p83).As a practical translation to what has been mentioned above, the UK regulators strictly 'imposed a principle of strict separation between the role of the Shari'ah committee and bank governance'. (FSA, 2007, p13)

As far as the regulator is concerned, mainly,to make sure that the position of Sharia board in the governance structure is restricted within the advisory or supervisory role rather an executive one (Casper, 2012, p6). Two clear reasons stand behind this emphasis.Firstly, according to regulations in the UKif any per-

son wishes or ought to be appointed as a director in afinancial firmhas to go through certain procedures and seek an approval from the regulators FCA(Financial Conduct Authority). In its legal capacity (FCA) would carry out a suitability assessment as part of specific process in order to register the approved seeker or applicantbased on a set of "standards known as the 'Fit and Proper test forApproved Persons' (www.handbook.fca.org.uk, 2016).

Taking an academic measure into one of the assessment factors 'competence and capability' would imply that for a person to be appointed as a director, they would need to meet some expectations of relevant expertise. The question to be raised is, that if Sharia scholars wanted to get an executive directorshipposition would they have the required standards of competency and capability? (Dewar and Hussain, 2014, p39).Practically and realistically speaking, many of them would not be able to meet this kind of requirements as religious studies and experiences would not necessarily provide them with the technical and professional skills in economics and finance, let alone accounting and auditing knowledge.

Secondly, assuming, for academic and practical argument, that Sharia board's members are holding director's positions, their role would likely beinvolved in an executive matterrathera non-executivewhere this might lead them toan active contribution in running the actual business (Al-Sadah, 2007, p72).If this happens, which is likely to be the case, the legal and practical situation would be rather complicated as to the high possibility of having a member of Sharia board in one Islamic bank/financial institution sitting on another board of another one. As mentioned earlier, this might lead to a serious situation of conflict of interest. This would be occurring as there is a serious shortage of qualified Sharia scholars with proper skills facing the Islamic financial industry in the UK (Saidi, 2009, p39).It is the responsibility of the Islamic financial firm towards the FCA (Financial Conduct Authority)to prove that the SSB is not being involved in the manage-

ment or other executive tasks. As mentioned above, so far, it was not reported that any of the working Islamic banks and financial institutions failed to show that the Sharia board is exceeding its supervisory role (Casper, 2012, p56).

Findings and Conclusion:

It is notable that despite the UK government accepted, attracted, and supported the development of Islamic finance and banking,law makers and regulators have not adopted or initiated a particular concept or model of Islamic corporate governance. It seemed as if the UK regulators have been avoiding any involvement to introduce its own version of Islamic corporate governance. In doing so, the door kept open to wider spectrum of Islamic finance providers to choose UK as a platform to establish and promote Islamic financial products to the wider world. As part of its pragmatic traditions, the UK legislator and regulators have not tried to create new remarks on the definition of Islamic corporate governance. The remarks were made by leaving Islamic corporate governance as a floating concept, especially with regard to Sharia supervisory board and its position in the corporate governance of the Islamic financial institutions.

It has been shown, how UK regulators adopted a clear methodology to pragmatically adapting the legal/financial rules to incorporate Islamic banking within its system. This happened as an element ofa real legal innovative method adopted by the UK rules and regulations. This reflection has been presented by the pragmatic interaction that has been originated or innovated by the UK regulators withIslamic law that represents different legal traditions and philosophyand do not share similar legal/economic values. Bearing this in mind, adopting a pragmatic approach when dealing with Islamic financial institution and its governance, did not lead, by any means, to compromise the law enforcement and implementation.

To sum up, in focussing on two main elements of the UK regulations “Level playing field, and no obstacles no favouritism”in relation to corporate governance of Islamic finance, would shed a clear light on the pragmatic legislative policy that has been embraced by the UK regulators when dealing with Islamic finance and its corporate governance. This flexibility has been established by delegating the interpretation of corporate governance of every individual bank, mostly, to its Sharia board. In doing so, the regulatorsavoidthe burden of direct involvement in providing any religious opinion, and keep their secular identity untouched. Corporate governance of Islamic banks in the UK benefited greatly from the pragmatic legal tradition that is deeply rooted in English law. This keeps the door open for further development to boost Islamic finance industry, particularly in the UK and generally in Europe.

References:

Books and Journals:

- AAOIFI, Governance Standard for Islamic Financial Institutions No. 1, sec. 2.
- Agnélio, M., Pita, C. (2014). Some Issues to Consider when Regulating Islamic Banking Business in Secular Countries, Journal of Islamic Banking and Finance, Vol. 2, No. 1, pp. 389-405.
- Al-Sadah, A. K. (2007). Corporate Governance of Islamic Banks, Its Characteristics and Effects on Stakeholders and the Role of Islamic Banks Supervisors, School of Management, University of Surrey.
- Alwyni, F.A. (2015). Corporate governance in global Islamic financial institutions, Islamic Finance News.
- Atiyah, P. S. (1987). Pragmatism and Theory in English Law. Stevens and Sons, London.
- Belouafi, A., Chachi, A. (2014). Islamic Finance in the United Kingdom:
- Casper, M. (2012). Sharia Boards and Sharia Compliance in the context of European Corporate Governance. Preprints and Working Papers of the Center for Religion and Modernity. Münster.
- Chowdhury, D. (2004). Incentives, Control and Development: Governance in Private and Public Sector with Special Reference to Bangladesh. Dhaka Viswavidyalay Prakashana Samstha, Dhaka.
- Chowdhury, N. T. (2015). Shariah Governance Framework of the Islamic Banks in Malaysia, International Journal of Management Sciences and Business Research, Vol-4, Issue 10. Pp115-124.
- Cook, J. and Deakin, S. (1999). Stake holding and Corporate Governance Theory and Evidence on Economic Performance, ESRC Centre for Business Research, University of Cambridge.

- Dar, H. A. (2004). Demand for Islamic Financial Services in the UK: chasing a mirage? Loughborough University, Institutional Repository. Economic Research Paper, No 04-11.
- Ercanbrack, J.G. (2011) The Law of Islamic Finance in the United Kingdom: Legal Pluralism and Financial Competition. PhD Thesis, SOAS (School of Oriental and African Studies), University of London.
- Ercanbrack, J. (2011). The Regulation of Islamic Finance in the United Kingdom. Ecclesiastical Law Journal, 13 (1). pp. 69-77.
- Factors Behind its Development and Growth. Islamic Economic Studies, Vol. 22, No. 1, Pp37-78.
- Fontrodona, J., Sison, A. J. (2006). The Nature of the Firm, Agency Theory and Shareholder Theory: A Critique from Philosophical Anthropology. Journal of Business Ethics 66: 33–42.
- Foster, N., Neo, D. (2013). Dispute Resolution and Insolvency in Islamic Finance: Problems and Solutions, Centre of Islamic and Middle Eastern Law (CIMEL), SOAS Law of Islamic Finance Working Papers Series Report of Proceedings.
- Garas, S.N., Pierce, C. (2010). Sharia supervision of Islamic financial institutions, Journal of Financial Regulations and Compliance, Vol. 18 No 4, Pp 386-407.
- Grais, W. Pellegrini, M. (2006). Corporate Governance and Stakeholders' Financial Interests in Institutions Offering Islamic Financial Services, World Bank Policy Research Working Paper 4053.
- Garner, J. M. (2013). A Critical Perspective on the Principles of Islamic Finance Focusing on Sharia Compliance and Arbitrage. Leeds Journal of Law & Criminology • Vol. 1 No. 1. Pp 69-90.
- Hamza, H. (2013). Sharia governance in Islamic banks: Effectiveness and supervision model, International Journal of Islamic and Middle Eastern Finance and Management, Vol. 6 No. 3, Pp226-237.
- Hasan, Z. (2010). Regulatory Framework of Shari'ah Gover-

nance System in Malaysia, GCC Countries and the UK, Kyoto Bulletin of Islamic Area Studies, 3-2. Pp. 82–115).

- Haqqi, A. R. (2014). Shariah Governance in Islamic Financial Institution: An Appraisal, US-China Law Review, Vol. 11, 112. Pp 112-133.
- HM Treasury, (2008). The Development of Islamic Finance in the UK: the Government's perspective.
- Iqbal, Z, and Mirakhor, A. (2004). Stakeholders Model of Governance in Islamic Economic System, Islamic Economic Studies, Vol. 11. No. 2, Pp 43-64.
- John Dewar, J., Munib Hussain, M. (2014). Islamic Finance & Markets in 10 jurisdictions worldwide. Law Business Research Ltd.
- Kammer, A., Norat, M., Marco Piñón, M., Prasad, A., Towe, C., Zeidane, Z., and an IMF Staff Team. (2015). Islamic Finance: Opportunities, Challenges, and Policy Options. International Monetary Fund.
- Khan, A., Tanveer, S., Shah, Q. A., and Jamil, R. A. (2015). Comparative Analysis of Regulatory and Supervisory System of Islamic Banks: Evidence from Pakistan, Malaysia, Bahrain and United Kingdom, Mediterranean Journal of Social Sciences, MCSER Publishing, Rome-Italy. Vol 6, No, 6 S2. Pp 629-640.
- Maliah Sulaiman, M., Et al. (2015). Corporate Governance of Islamic Financial Institutions in Malaysia. Asian Journal of Business and Accounting 8(1). pp 65-93.
- Malik M. Hafeez, M. M. (2013). An Analysis of Corporate Governance in Islamic and Western Perspectives, International Journal of Business, Economics and Law, Vol. 2, Issue 3. Pp98-103.
- Miskam, S., Nasrul, M.A. (2013). Shariah Governance in Islamic Finance: The Effects of the Islamic Financial Services Act 2013 (IFSA 2013) - Proceeding of the World Conference on Integration of Knowledge, WCIK 2013. 25-26 November

2013, Langkawi, Malaysia. (e-ISBN 978-967-11768-2-5). Organized by WorldConferences.net.

- Mejía, A. L., Aljabrin, S., Awad, R., Norat, M., and Song, I. (2014) Regulation and Supervision of Islamic Banks, International Monetary Fund.
- Morales, R.A., Shiblaq B. (2015). Islamic Finance & Markets In 14 jurisdictions worldwide. 2nd Ed, Law Business Research Ltd, London.
- Morrison, S. (2014). Shariah Boards and the Corporate Governance of Islamic Banks in the United Kingdom, Journal of Islamic Economics, Banking, Vol-10, No1. Pp 96-109.
- Novethic, (2009). Islamic Finance and SRI: any Crossover? Novethic.
- Saidi, N. (2009). Corporate governance in Islamic finance, Islamic wealth. Hawkamah, the Institute for Corporate Governance, Chapter 33.
- Sasan, M., Moradi, M., and Eskandar, H. (2014). Corporate Governance: Convergence v.s Divergence. British Journal of Economics, Finance and Management Sciences, Vol. 9 (1).
- Schnyder, G. (2010). Varieties of Insider Corporate Governance: Centrer-right Preferences and the Determinants of Reform in the Netherlands, Sweden, and Switzerland. Centre for Business Research, University of Cambridge, Working Paper No. 406.
- Shleifer, A., Vishny, R. W. (1997). A survey of corporate governance, Journal of Finance. Vol. LII. No2. pp 737-732.
- Smith, T. R. (2011). Agency Theory & Its Consequences. Master Thesis at Copenhagen Business School, Programme: M.Sc Finance & Strategic Management. Under the supervision of Sven Junghagen, Department of Management Politics & Philosophy.
- Solé, J. (2007). Introducing Islamic Banks into Conventional Banking Systems, International Monetary Fund.

- Song, I., Oosthuizen, C. (2014). Islamic Banking Regulation and Supervision: Survey Results and Challenges. International Monetary Fund.
- Stanley, M. (2008). Corporate Governance: Playing Catch-Up. New Horizon, (169), 46.
- Toufik, B.B. (2015). The Role of Shari'ah Supervisory Board in Ensuring Good Corporate Governance Practice in Islamic Banks. International Journal of Contemporary Applied Sciences, Vol. 2 No. 2. Pp109-118.
- Wilson, R. (2007). Islamic finance in Europe. European University Institute for MUSMINE. RSCAS Policy papers. No. 2007/02.
- Zulkifli, H. (2009). Corporate Governance: Western and Islamic Perspectives. International Review of Business Research Papers Vol.5 No. 1.Pp. 277-293.

Websites and Electronic Sources:

- www.fsa.gov.uk/Pages/Library/Communication/Speeches/2003/SP118.shtml. Retrieved at 10/03/2016
- FSA, (2007). Islamic Finance in the UK: Regulation and Challenges, www.fsa.gov.uk/pubs/other/islamic_finance.pdf. Retrieved at 03/03/2016
- www.islamic-bank.com/imagesupload/IBBINTERIMREPORTJUNE2007.pdf. Retrieved at 10/03/2016
- www.eiib.co.uk/documents/eiib_interim_rep_a4(2).pdf. Retrieved at 08/03/2016
- www.blme.com/pdf/BLME_launch_press_release.pdf. Retrieved at 08/03/2016
- www.amiricapital.com/about/ami_gro.php. Retrieved at 06/03/2016
- www.biih.co.uk/Press01.asp. Retrieved at 04/03/2016
- FSA, Islamic Finance in the UK: Regulation and Challenges, November 2007, www.fsa.gov.uk/pubs/other/islamic_finance.pdf,

- Briault, C. (2007). Centre of Islamic Finance, FSA Industry Forum, London. http://www.fsa.gov.uk/pages/Library/Communication/ Speeches/2007/1018_cb.shtml. Retrieved at 17th March, 2016.
- Prudential Regulation Authority, (2014). Bank of England, Occasional Consultation Paper. CP5/14. Available at: http://www.bankofengland.co.uk/pra/Documents/publications/policy/2014/ocp5-14.pdf. Accessed on 19/03/2016.
- Wilson, R. (2009). The development of Islamic finance in the GCC Working Paper, Kuwait Programme on Development, Governance and Globalisation in the Gulf States. Available at: http://eprints.lse.ac.uk/55281/1/Wilson-2009.pdf. Accessed on 16/03/2016.
- https://auscifwp.files.wordpress.com/2013/10/islamic-finance-publication.pdf. Accessed on 19/03/2016.
- Global Islamic Finance Report (GIFR 2010). Legal & Regulatory Issues in Islamic Finance from a UK Perspective. Pp 206-219. Available at: http://gifr.net/gifr2010/contents/ch_21.pdf. Accessed on 20/03/2016.
- www.handbook.fca.org.uk, (2016). The Fit and Proper test for Approved Persons. Release 4. Available at https://www.handbook.fca.org.uk/handbook/FIT.pdf. Accessed on 22/03/2016.
- HM Treasury, (2011). Available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/81411/consult_newfinancial_regulation170211.pdf. Accessed on 13/03/2016.
- http://www.fsa.gov.uk, (2008/09). FSA Annual Report, Promoting efficient, orderly and fair markets, Section two. Pp29-36. Available at: http://www.fsa.gov.uk/static/pubs/annual/ar08_09/section2.pdf. Accessed on 10/03/2016.

Table of Contents