RESEARCH MONOGRAPH 77
2026

BIBM-INCEIF Joint Research

Shariah Governance in Islamic Banks of Bangladesh: An Evaluation

Research Team

Dr. M. Mahabbat Hossain, CIPA, CSAA, DIB

Associate Professor,
Bangladesh Institute of Bank Management (BIBM)
Email: mahabbat@bibm.org.bd | Phone: +880 1716 373 565

Mezbah Uddin Ahmed, FCCA, MIBF, CIPA, CSAA

Research Fellow, ISRA Institute, INCEIF University, Malaysia
Email: mezbah-isra@inceif.edu.my | Phone: +60 182 786 173

Md. Alamgir, CIPA, CSAA

Professor and Director (Certification)
Bangladesh Institute of Bank Management (BIBM)
Email: alamgirtipu@bibm.org.bd | Phone: +880 1716 061 773

Muhammad Habibur Rahman, CIPA, CSAA

Senior Vice President and Head of Internal Shariah Audit,
Islami Bank Bangladesh PLC
Email: habiburibbl@gmail.com | Phone: +880 1841 026 163

Bangladesh Institute of Bank Management
বাংলাদেশ ইনস্টিটিউট অব ব্যাংক ম্যানেজমেন্ট

INCEIF UNIVERSITY

Shariah Governance in Islamic Banks of Bangladesh: An Evaluation

Research Team

Md. Mahabbat Hossain, Ph.D., CIPA, CSAA, DIB
Associate Professor, BIBM

Mezbah Uddin Ahmed, FCCA, MIBF, CIPA, CSAA
Research Fellow, ISRA Institute, INCEIF University, Malaysia

Md. Alamgir, CIPA, CSAA
Professor and Director (Certification), BIBM

Muhammad Habibur Rahman, CIPA, CSAA
Senior Vice President and Head of Internal Shariah Audit
Islami Bank Bangladesh PLC

Editorial Advisor

Md. Ezazul Islam, Ph.D.
Director General, BIBM

Editor

Md. Shihab Uddin Khan
Professor and Director (Research, Development and Consultancy), BIBM

Support Team

Research, Development and Consultancy Wing
Papon Tabassum, *Assistant Senior Officer, BIBM*
Sk. Md. Azizur Rahman, *Officer, BIBM*

Publications-cum-Public Relations Section
Md. Al-Mamun Khan, *Senior Officer (PPR), BIBM*
Md. Morshadur Rahman, *Officer (PPR), BIBM*

Typeset By

Sk. Md. Azizur Rahman, *Officer, BIBM*

Creative & Design Partner

Fajr Advertising

Published in

August 2026

Published By

Bangladesh Institute of Bank Management (BIBM) and INCEIF University, Malaysia

Copyright ©

BIBM 2026, All Rights Reserved

The views in this publication are of authors only and do not necessarily reflect the views of the institutions involved in this publication.

RESEARCH MONOGRAPH 77
2026

Shariah Governance in Islamic Banks of Bangladesh: An Evaluation

Md. Mahabbat Hossain, Ph.D., CIPA, CSAA, DIB
Associate Professor, Bangladesh Institute of Bank Management

Mezbah Uddin Ahmed, FCCA, MIBF, CIPA, CSAA
Research Fellow, ISRA Institute, INCEIF University, Malaysia

Md. Alamgir, CIPA, CSAA
Professor and Director (Certification), Bangladesh Institute of Bank Management

Muhammad Habibur Rahman, CIPA, CSAA
Senior Vice President and Head of Internal Shariah Audit, Islami Bank Bangladesh PLC

Bangladesh Institute of Bank Management
বাংলাদেশ ইনস্টিটিউট অব ব্যাংক ম্যানেজমেন্ট

INCEIF UNIVERSITY

Foreword

It gives me great pleasure to present this research monograph titled *Shariah Governance in Islamic Banks of Bangladesh: An Evaluation*, jointly undertaken by the Bangladesh Institute of Bank Management (BIBM) and the ISRA Institute of INCEIF University, Malaysia. This publication represents the first research output under the Memorandum of Understanding signed between the two institutions, reflecting our shared commitment to advancing research, knowledge exchange, and professional excellence in Islamic banking and finance. I firmly believe that this collaboration will serve as a foundation for many future initiatives that contribute to the development of the Islamic financial services industry both nationally and internationally.

Islamic banking has become an integral component of Bangladesh's financial system, accounting for a significant share of banking assets, deposits, and financing activities. Over the past four decades, the industry has played an important role in promoting financial inclusion, entrepreneurship development, ethical finance, and socio-economic progress. As the industry continues to expand and become increasingly interconnected with the national and global financial system, ensuring sound governance, effective oversight, and institutional accountability has become indispensable for maintaining public confidence and supporting its long-term sustainability.

The importance of this study has become even more pronounced in light of the recent challenges faced by parts of the banking industry. Governance failures, weaknesses in oversight mechanisms, rising non-performing investments, liquidity pressures, and declining depositor confidence have highlighted the critical need for stronger institutional governance. While these challenges have affected the broader banking sector, their implications are particularly significant for Islamic banks, where stakeholders expect compliance not only with regulatory requirements but also with the principles and objectives of Shariah. These developments have reinforced the need to reassess existing governance practices and strengthen institutional frameworks capable of preserving confidence in the Islamic financial system.

In Islamic banking, Shariah governance serves as a distinctive and additional layer of governance that complements conventional corporate governance mechanisms. Its effectiveness directly influences institutional credibility, stakeholder trust, and the authenticity of Shariah-compliant financial services. More importantly, an effective Shariah governance framework ensures that Islamic banks remain faithful to the principles of justice, transparency, accountability, and ethical conduct that underpin Islamic finance. Therefore, strengthening Shariah governance is not merely a matter of regulatory

compliance; it is essential for preserving the integrity, resilience, and sustainability of Islamic banking institutions while contributing to the realization of the higher objectives (Maqasid al-Shariah) of the Islamic financial system.

Recognizing the strategic importance of this issue, BIBM, in collaboration with the ISRA Institute of INCEIF University, undertook this study to evaluate the existing Shariah governance framework of Islamic banks in Bangladesh. Drawing upon survey responses, Focus Group Discussions (FGDs), Key Informant Interviews (KIIs), and a comprehensive review of international standards, regulatory guidelines, and institutional practices, the study presents an evidence-based assessment of governance structures, the effectiveness of Shariah Supervisory Committees, Shariah compliance functions, internal Shariah audit, disclosure practices, and the prevailing regulatory framework. The study further benchmarks current practices against internationally recognized standards and identifies areas where governance arrangements can be further strengthened.

I would like to express my sincere appreciation to the research team for their dedication, professionalism, and scholarly rigor in conducting this important study. I also extend my gratitude to the ISRA Institute of INCEIF University, participating banks, Shariah scholars, industry experts, and all respondents whose valuable contributions greatly enriched the research. Their collective support demonstrates the importance of collaboration among regulators, academia, and industry in addressing contemporary challenges facing Islamic banking.

I sincerely hope that this research monograph will serve as a valuable reference for policymakers, regulators, researchers, and practitioners and stimulate further research and policy dialogue on Shariah governance. More importantly, I hope it will contribute to strengthening governance practices, enhancing stakeholder confidence, and supporting the development of a resilient, transparent, and globally competitive Islamic banking industry in Bangladesh.

Md. Ezazul Islam, Ph.D.
Director General, BIBM

Message

The sustainable development of Islamic banking and finance depends not only on the growth of institutions and markets but also on the continuous generation of knowledge that strengthens governance, promotes innovation, and enhances public confidence. In an increasingly interconnected world, many of the opportunities and challenges facing Islamic financial institutions transcend national boundaries and require collaborative responses from researchers, practitioners, regulators, and academic institutions.

It is in this spirit that the ISRA Institute of INCEIF University and the Bangladesh Institute of Bank Management (BIBM) entered into a Memorandum of Understanding (MoU) on 22 October 2024 to promote cooperation in research, capacity development, knowledge exchange, and professional development in the field of Islamic banking and finance. The partnership reflects a shared commitment to advancing the industry through evidence-based research, intellectual collaboration, and the dissemination of practical knowledge.

I am pleased to note that this research report, *Shariah Governance in Islamic Banks of Bangladesh: An Evaluation*, represents the first major output produced under this collaborative arrangement. As the inaugural outcome of the MoU, the study demonstrates the value of combining academic rigor, industry insights, and international perspectives to address issues of strategic importance to the Islamic financial services industry.

Shariah governance remains one of the most critical pillars of Islamic finance. While the structures, regulations, and institutional arrangements may differ across jurisdictions, the fundamental objectives of Shariah governance remain universal: to ensure integrity, accountability, transparency, and faithful adherence to the principles of Shariah. As Islamic banking continues to expand globally, strengthening governance frameworks has become increasingly important for preserving stakeholder confidence, enhancing institutional resilience, and supporting sustainable growth.

The significance of this study extends beyond the boundaries of a single country. Although the research focuses on the experience of Islamic banks in Bangladesh, many of the governance issues examined in this report are relevant to Islamic financial institutions across jurisdictions. Questions relating to the effectiveness of Shariah oversight, institutional accountability, governance structures, regulatory frameworks, and assurance mechanisms are matters of common concern for the global Islamic finance industry. Consequently, the lessons and insights generated through this study contribute to a broader body of knowledge that can benefit policymakers, regulators, practitioners, and researchers worldwide.

One of the distinguishing features of Islamic finance is its emphasis on collaboration and collective advancement. The challenges facing the industry today cannot be addressed by

individual institutions or jurisdictions acting in isolation. Rather, they require sustained engagement among regulators, industry participants, scholars, and academic institutions across different regions. Collaborative initiatives such as this research project help bridge knowledge gaps, facilitate the exchange of experiences, and contribute to the development of more effective and harmonized governance practices.

As this publication marks the first milestone under the BIBM–INCEIF partnership, I am confident that it will serve as the foundation for many future initiatives. There remains significant potential to expand cooperation through additional joint research projects, policy dialogues, conferences, seminars, executive education programs, publications, and other knowledge-sharing activities. Such initiatives will not only strengthen the relationship between our institutions but also contribute to the advancement of Islamic banking and finance at both regional and global levels.

On behalf of the ISRA Institute of INCEIF University, I would like to express my sincere appreciation to the leadership of BIBM for their commitment to this partnership and to the members of the research team for their dedication and scholarly efforts. I also extend my gratitude to all regulators, industry practitioners, Shariah scholars, and participants who contributed their valuable insights and experiences to this study.

I sincerely hope that this publication will stimulate further discussion, inspire future research, and support ongoing efforts to strengthen Shariah governance frameworks. More importantly, I hope it will serve as a reminder that the advancement of Islamic banking and finance is a shared responsibility that transcends institutional and geographical boundaries and requires collective efforts for the benefit of the global community.

Said Bouheraoua, Ph.D.
Director
ISRA Institute
INCEIF University, Malaysia

Acknowledgement

The research team expresses its sincere gratitude to Almighty Allah (SWT) for granting us the opportunity, strength, and guidance to complete this study titled *"Shariah Governance in Islamic Banks of Bangladesh: An Evaluation."*

This research has been undertaken as a joint initiative of the Bangladesh Institute of Bank Management (BIBM), Bangladesh, and the ISRA Institute of INCEIF University, Malaysia, under the Memorandum of Understanding (MoU) signed between the two institutions on 22 October 2024. As the first major research output produced under this collaborative arrangement, the study reflects the shared commitment of both institutions to advancing knowledge, research, and professional excellence in Islamic banking and finance.

The research team gratefully acknowledges the institutional support provided by BIBM and INCEIF University throughout the study. We express our profound gratitude to the management of both institutions for their encouragement, cooperation, and unwavering commitment to promoting research and knowledge development in the field of Islamic finance. We are particularly grateful to Dr. Md. Ezazul Islam, Director General of BIBM, and Dr. Said Bouheraoua, Director of the ISRA Institute, INCEIF University, for their continuous support and valuable guidance throughout the research process. We would also like to express our sincere gratitude to Professor Md. Shihab Uddin Khan, Director (Research, Development & Consultancy), BIBM, under whose portfolio this study was undertaken. The research team greatly appreciates continuous support provided by Research, Development & Consultancy wing of BIBM throughout the study.

We would like to convey our sincere appreciation to Bangladesh Bank, particularly the officials of the Islamic Banking Regulation and Policy Department (IBRPD), for their valuable cooperation, insights, and constructive observations. Our heartfelt thanks are extended to the members of the Boards of Directors, Shariah Supervisory Committees (SSCs), senior management teams, Heads of Shariah Secretariat, Heads of Islamic Banking Divisions, internal Shariah auditors, compliance officials, and other banking professionals from Islamic banks and conventional banks operating Islamic branches and windows who participated in the survey, Key Informant Interviews (KIIs), and Focus Group Discussions (FGDs). Their willingness to share experiences, challenges, and professional insights substantially strengthened the empirical foundation of this research.

The research team also extends its appreciation to the distinguished discussants, guests, and participants of the dissemination seminar for their valuable comments, observations, and recommendations. Their constructive feedback contributed significantly to refining the findings and policy recommendations presented in this report.

We acknowledge with gratitude the administrative, technical, and logistical support provided by the relevant divisions and officials and supporting staff of both institutions. Their assistance in coordination, communication, data collection, event management, and document preparation facilitated the smooth execution of the study.

Finally, we express our deepest appreciation to all respondents, participants, scholars, regulators, practitioners, and stakeholders who contributed directly or indirectly to this research. Their cooperation reflects a shared commitment to strengthening Shariah governance, enhancing institutional integrity, and promoting the sustainable development of Islamic banking and finance. We sincerely hope that the findings and recommendations of this study will contribute to informed policy discussions and support the continued advancement of Islamic banking and finance both within and beyond national boundaries.

Md. Mahabbat Hossain, Ph.D., CIPA, CSAA, DIB
Mezbah Uddin Ahmed, FCCA, MIBF, CIPA, CSAA
Md. Alamgir, CIPA, CSAA
Muhammad Habibur Rahman, CIPA, CSAA

Governance is a critical determinant of the stability, integrity, and sustainability of banking institutions. In Islamic banks, governance extends beyond conventional corporate governance arrangements and incorporates an additional layer of oversight through Shariah governance mechanisms. Recent governance failures in several Islamic banks in Bangladesh have raised concerns regarding the effectiveness of existing governance structures, including the role of boards of directors, Shariah Supervisory Committees (SSCs), internal control functions, and regulatory oversight. Against this backdrop, this study evaluates the Shariah governance framework of Islamic banks in Bangladesh and identifies measures for strengthening governance practices within the industry.

The primary objectives of the study are to evaluate the existing Shariah governance framework of Islamic banks in Bangladesh in light of international standards and local regulatory guidelines, examine the effectiveness of institutional arrangements and operational mechanisms relating to Shariah governance, and develop policy recommendations for strengthening governance practices.

The study adopts a mixed-method research approach, drawing on both primary and secondary data sources. Primary data were collected through structured questionnaires, Focus Group Discussions (FGDs), and Key Informant Interviews (KIIs) involving regulators, members of boards of directors, Shariah scholars, senior management, internal auditors, and banking professionals. Responses were received from 20 banks representing more than half of the Islamic banking institutions operating in Bangladesh. Three FGDs were conducted, including one at BIBM involving representatives from 25 banks and two additional discussions with officials of Bangladesh Bank and Islami Bank Bangladesh PLC. Secondary information was collected from international standards, regulatory guidelines, annual reports, academic literature, and relevant publications. The findings were analyzed through a thematic approach.

The study finds that Islamic banking has achieved significant growth in Bangladesh and currently represents a substantial share of the country's banking sector. However, recent events have exposed weaknesses in governance arrangements, highlighting the need for stronger oversight and accountability mechanisms. Survey findings indicate broad agreement among respondents regarding the importance of Shariah governance in ensuring transparency, accountability, stakeholder confidence, and compliance with Shariah principles. At the same time, respondents identified several weaknesses in the existing framework.

The findings reveal concerns regarding the effectiveness of SSCs, particularly in relation to their independence, competency, authority, and level of engagement in institutional decision-making. Variations in governance practices among banks indicate the absence of a sufficiently standardized approach to Shariah governance. The study also finds that Shariah governance functions are not always adequately integrated into broader corporate governance and risk management frameworks.

The assessment further indicates that internal Shariah audit functions vary significantly across institutions in terms of scope, independence, resources, and reporting arrangements. While most

Islamic banks conduct Shariah audits, the quality and coverage of such activities are not uniform. Disclosure practices relating to Shariah governance also differ considerably among banks, particularly in relation to SSC activities, Shariah awareness programs, and audit coverage. These variations limit transparency and reduce comparability across institutions.

The FGDs and KIIs reinforce these observations. Participants emphasized that governance failures experienced by some Islamic banks were influenced not only by weaknesses in Shariah governance but also by broader deficiencies in corporate governance, including ineffective oversight by boards of directors, inadequate accountability mechanisms, ownership concentration, and external influence on institutional decision-making. Participants also highlighted the absence of external Shariah review arrangements and the need for greater alignment between Shariah governance and conventional governance structures.

Based on the findings, the study proposes a number of policy recommendations. These include strengthening board independence and competency; aligning corporate governance and Shariah governance structures; formalizing Shariah compliance functions within the Three Lines of Defense framework; enhancing the independence and effectiveness of internal Shariah audit; increasing the engagement and accountability of SSCs; introducing external Shariah review and fiduciary rating mechanisms; establishing fit-and-proper criteria for SSC members; improving disclosure practices; strengthening stakeholder awareness; promoting principle-based regulatory approaches; and implementing structured capacity development programs for directors, senior management, SSC members, and operational personnel.

The study concludes that effective Shariah governance is essential for maintaining the credibility, integrity, and sustainability of Islamic banking institutions. Strengthening governance arrangements requires a comprehensive approach involving regulators, boards of directors, SSCs, management, and other stakeholders. The recommendations presented in this report are expected to contribute to the development of a more robust and effective Shariah governance framework, thereby supporting the long-term stability and sustainable growth of Islamic banking in Bangladesh.

List of Abbreviations

AAOIFI	: Accounting and Auditing Organization for Islamic Financial Institutions
ASIFI	: Auditing Standards for Islamic Financial Institutions
BB	: Bangladesh Bank
BCBS	: Basel Committee on Banking Supervision
BDT	: Bangladesh Taka
BIBM	: Bangladesh Institute of Bank Management
BoD	: Board of Directors
BRPD	: Banking Regulation and Policy Department
BSEC	: Bangladesh Securities and Exchange Commission
CBS	: Core Banking Systems
CEO	: Chief Executive Officer
CFO	: Chief Financial Officer
CG	: Corporate Governance
COSO	: Committee of Sponsoring Organizations of the Treadway Commission
CPD	: Continuous Professional Development
CRAR	: Capital to Risk-Weighted Assets Ratio
CSB	: Central Shariah Board
CSBIB	: Central Shariah Board for Islamic Banks of Bangladesh
CSR	: Corporate Social Responsibility
ESG	: Environmental, Social and Governance
FGD	: Focus Group Discussion
GCC	: Gulf Cooperation Council
GIFR	: Global Islamic Finance Report
GS	: Governance Standards
GSIFI	: Governance Standards for Islamic Financial Institutions
IB	: Islamic Bank
IBFBD	: Islamic Banking and Finance in Bangladesh Annual Review
IBRPD	: Islamic Banking Regulation and Policy Department
ICBIBL	: ICB Islamic Bank Limited
IBD	: Islamic Banking Division
ICC	: International Chamber of Commerce
ICCD	: Internal Control and Compliance Division
ICT	: Information and Communication Technology
IIA	: Institute of Internal Auditors
IIFS	: Institutions offering Islamic Financial Services

ICD	: Islamic Corporation for the Development of the Private Sector
IFCI	: Islamic Finance Country Index
IFDI	: Islamic Finance Development Indicator
IFI	: Islamic Financial Institution
IFSB	: Islamic Financial Services Board
KII	: Key Informant Interview
KPI	: Key Performance Indicator
LSEG	: London Stock Exchange Group
MoU	: Memorandum of Understanding
NPL	: Non-Performing Loan
OECD	: Organisation for Economic Co-operation and Development
OIFI	: Other Islamic Financial Institutions
PEP	: Politically Exposed Person
PLC	: Public Limited Company
ROA	: Return on Assets
ROE	: Return on Equity
SAB	: Shariah Advisory Board
SG	: Shariah Governance
SMT	: Senior Management Team
S&P	: Standard & Poor's
SSB	: Shariah Supervisory Board
SSC	: Shariah Supervisory Committee
SCU	: Shariah Compliance Unit
SNCR	: Shariah Non-Compliance Risk
TA	: Total Assets
ToR	: Terms of Reference
UAE	: United Arab Emirates
USD	: United States Dollar

Contents

1. Background of the Study	1
2. Objectives of the Study	2
3. Methodology of the Study	3
4. Literature Review	4
4.1 Global Trends and Domestic Dynamics of Islamic Banking in Bangladesh	4
4.2 Literature on Shariah Governance	9
4.3 Governance Structures in Islamic Banks of Bangladesh	11
4.3.1 Traditional Corporate Governance in Banks	12
4.3.2 Additional Components of Governance of IFIs	14
4.3.3 Impact of Good Corporate Governance in IFIs	16
4.3.4 Regulatory Framework for Governance Structure of Islamic Banks	17
5. Findings and Discussion	19
5.1 Survey Findings	19
5.1.1 Role, Effectiveness, and Structural Limitations of SSC	20
5.1.2 Shariah Governance Structure and Institutional Framework	21
5.1.3 Regulatory Framework and Supervisory Effectiveness	22
5.1.4 Shariah Disclosure Quality and Reporting Practices	23
5.1.5 Governance Dynamics and Crisis Interaction	24
5.1.6 External Shariah Assurance and Market Confidence	25
5.2 Findings from FGDs and KIIs	26
5.2.1 Dual Governance Structure and Implementation Gaps	26
5.2.2 Formal Compliance versus Substantive Shariah Implementation	26
5.2.3 Weaknesses in Board Governance and Oversight	26
5.2.4 Independence and Effectiveness of SSCs	27
5.2.5 Fragmented Governance Architecture	27
5.2.6 Weaknesses in Internal Shariah Audit and Compliance	28
5.2.7 Weak Integration of Shariah Compliance into Operations	28
5.2.8 Human Capital and Competency Gaps	29
5.2.9 Technology and System Constraints	29
5.2.10 Political Economy and External Influence	29
5.2.11 Institutional Culture and Behavioral Constraints	30
5.2.12 Policy–Implementation Disconnect	30
5.2.13 Lack of Standardization and Market Discipline	30
5.2.14 Weak Accountability and Stakeholder Representation	31
6. Recommendations	31
6.1 Restoring Governance Integrity through Independent & Competent Board Structures	32
6.2 Aligning Corporate Governance with Shariah Governance	32
6.3 Formalizing the Shariah Compliance Function within the Three Lines of Defense	32
6.4 Strengthening the Scope, Rigor, and Independence of Internal Shariah Audit	33
6.5 More Active Engagement of the SSC	33
6.6 Introduction of External Shariah Review and Fiduciary Rating	33
6.7 Shariah-Based Performance Metrics for Institutions and Employees including SMT	34
6.8 Strengthening SSC Composition through Fit and Proper Criteria	34
6.9 Enhancing Stakeholder Awareness of Shariah Governance	35
6.10 Principle-Based Regulation and Functional Separation in Supervision	35
6.11 Capacity Development and Structured Knowledge Enhancement	35
7. Conclusion	36
References	38

Shariah Governance in Islamic Banks of Bangladesh: An Evaluation

1. Background of the Study

Governance is not merely a regulatory requirement but a critical determinant of institutional integrity. It is a fundamental pillar of banking institutions, as they manage the funds of others. Effective governance enhances transparency, strengthens stakeholder confidence, and supports prudent risk management. Conversely, weak governance can lead to financial mismanagement, increased exposure to fraud, institutional failures, and broader systemic instability. Accordingly, banks are subject to strict regulatory oversight. This importance is even greater for Islamic banks, which must comply with Shariah principles in addition to national regulations. As a result, additional layers of governance are embedded within their institutional framework.

Islamic banks operate under a dual governance structure that ensures the faithful application of Islamic financial principles alongside regulatory compliance. Within this structure, the Shariah governance (SG) framework constitutes an additional and distinct layer of governance, enhancing the overall rigor and integrity of the system. However, the mere existence of such a framework is insufficient. Its effectiveness depends on the sound structuring and proper functioning of its key components.

Islamic banking in Bangladesh began in 1983 with the establishment of Islami Bank Bangladesh Limited, now Islami Bank Bangladesh PLC. Since then, the sector has significantly expanded, with, as of end-2024, 10 full-fledged Islamic banks operating and around 30 conventional banks offering Islamic banking services through dedicated branches or windows. Islamic banking now accounts for about one-fourth of the country's banking sector, reflecting strong demand for Shariah-compliant financial services. This growth has made Islamic banking a key component of Bangladesh's financial system and an important contributor to financial inclusion.

Over time, the industry has demonstrated strong performance across several key financial indicators, often outperforming the conventional banking sector. However, this rapid growth has not been matched by corresponding improvements in governance frameworks, particularly in SG. Consequently, the sector has become exposed to considerable risks, with political influence having become a significant contributor to governance failures.

Recent governance failures across several Islamic banks in Bangladesh have revealed critical shortcomings, including violations of banking norms by boards of directors and senior management, weak oversight by Shariah Supervisory Committees (SSCs), inadequate regulatory supervision, and instances of political interference. These issues

have disrupted the operations of affected banks and exposed deeper structural weaknesses within the system. The lack of robust governance mechanisms and effective accountability has intensified financial instability and uncertainty across the sector.

These issues have impacted the broader assessments of the banking industry. A report published by *The Daily Star* on 15 August 2024 noted that Bangladesh has been assigned the highest risk level in the Banking Industry Country Risk Assessment by *S&P Global Ratings*, with a score of 9 out of 10, where 10 indicates the weakest condition (S&P Global Ratings, 2024). This classification underscores the severity of governance-related shortcomings within the banking sector, particularly among some Islamic banks. Most full-fledged Islamic banks, with few exceptions, are currently facing acute liquidity pressures, rising non-performing assets, and significant erosion of depositor confidence.

The current distress also reflects recurring patterns in Bangladesh's banking history. Governance breakdowns in institutions such as Farmers Bank Limited, National Bank Limited, and BASIC Bank Limited illustrate how weak governance, mismanagement, and regulatory shortcomings can lead to systemic instability. These experiences suggest that governance weaknesses are not isolated incidents but indicative of persistent institutional deficiencies. While external shocks may influence banking outcomes, such events can hinder organizational objectives regardless of the strength of internal control systems (COSO, 2013).

In this context, the effectiveness of governance, particularly SG, has become critically important. In Islamic banks, governance extends beyond conventional oversight to include compliance with ethical and religious principles, introducing an additional layer of accountability. Failures in these governance mechanisms not only affect financial performance but also undermine stakeholder trust and the credibility of Islamic banking as a whole.

Given these concerns, a comprehensive evaluation of the governance framework of Islamic banks in Bangladesh is both timely and necessary. Strengthening governance practices, particularly in Shariah oversight, institutional accountability, and regulatory effectiveness, is essential to restoring confidence and ensuring the long-term sustainability of the sector. This study seeks to assess existing governance structures, identify key gaps, and provide policy-relevant recommendations for enhancing SG in Islamic banks in Bangladesh.

2. Objectives of the Study

The primary objective of this study is to identify and critically assess governance-related issues in Islamic banks in Bangladesh. The specific objectives of the study are:

a. to evaluate the existing SG framework of Islamic banks in Bangladesh in light of international standards and local regulatory guidelines, with the aim of identifying key governance components and clarifying their respective roles;

b. to examine the institutional arrangements and operational mechanisms of SG, including Shariah compliance functions, internal Shariah audits, and the integration of Shariah non-compliance risk (SNCR) into the overall risk management framework; and

c. to develop actionable policy recommendations and reform measures aimed at strengthening SG practices within the Islamic banking sector in Bangladesh.

3. Methodology of the Study

This study adopts a mixed-method research approach, combining qualitative inquiry with descriptive analysis of structured questionnaire responses, to evaluate the SG framework of Islamic banks in Bangladesh, drawing on both primary and secondary sources.

Primary data are collected through Key Informant Interviews (KIIs) and Focus Group Discussions (FGDs) conducted with key stakeholders, including officials of the central bank, members of boards of directors, Shariah scholars serving on SSCs, senior management, internal auditors, and experts in bank governance.

An FGD organized at BIBM was attended by representatives from 25 banks, primarily Heads of Shariah Secretariat or Heads of Islamic Banking. In addition, two further FGDs were conducted at the Islamic Banking Regulation and Policy Department (IBRPD) of Bangladesh Bank and at the Shariah Secretariat of Islami Bank Bangladesh PLC. These engagements generated in-depth insights into governance practices, structural weaknesses, regulatory challenges, and potential reform directions within the sector.

Furthermore, opinions were collected through a structured questionnaire. A total of 20 banks responded, representing more than 50 percent of Islamic banking institutions in Bangladesh, thereby ensuring adequate sectoral coverage and strengthening the reliability of the findings.

Secondary data are obtained through content analysis of relevant international standards, including those issued by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB), as well as regulatory guidelines, published reports, academic literature, and official websites of concerned institutions. This facilitates a structured benchmarking of local practices against global standards and established frameworks. The collected data are analyzed thematically to identify key patterns, gaps, and areas of concern in existing SG practices.

The findings of this study are expected to provide practical, policy-relevant insights for regulators, policymakers, banking executives, and SSCs, thereby strengthening governance frameworks and enhancing the long-term sustainability of Islamic banking in Bangladesh.

4. Literature Review

4.1 Global Trends and Domestic Dynamics of Islamic Banking in Bangladesh

The data indicate a strong and sustained expansion of the global Islamic finance industry, with total assets rising from USD 2.17 trillion in 2015 to USD 5.99 trillion in 2024, and projected to reach USD 9.7 trillion by 2029 (Table 4.1). Islamic banking remains the dominant segment, accounting for over 72 percent of total assets, highlighting the bank-centric nature of the industry. This indicates the strong growth potential of Islamic banking globally; therefore, Bangladesh should align itself with international developments by strengthening its SG framework and ensuring effective implementation of global standards.

Table 4.1: Breakdown & Growth of Global Islamic Finance in the Past Decade

Year	Global IB Assets		Global *Sukuk* Outstanding		Global *Takaful* Assets		Islamic Funds Outstanding		Global OIFI Assets		Total Islamic Finance Assets	
	USD Billion	Growth (%)	USD Billion	Growth (%)	USD Billion	Growth (%)	USD Billion	Growth (%)	USD Billion	Growth (%)	USD Billion	Growth (%)
2015	1,603	11.09	306	(11.56)	47	30.56	71	7.58	143	9.16	2,170	10.97
2016	1,769	10.36	349	14.05	48	2.13	99	39.44	143	0.00	2,408	10.97
2017	1,831	3.50	420	20.34	46	(4.17)	123	24.24	145	1.40	2,565	6.52
2018	1,882	2.79	470	11.90	47	2.17	116	(5.69)	152	4.83	2,667	3.98
2019	2,133	13.34	539	14.68	54	14.89	150	29.31	154	1.32	3,030	13.61
2020	2,453	15.00	626	16.14	63	16.67	183	22.00	162	5.19	3,487	15.08
2021	2,875	17.20	713	13.90	77	22.22	244	33.33	158	(2.47)	4,067	16.63
2022	3,244	12.83	788	10.52	90	16.88	220	(9.84)	167	5.70	4,509	10.87
2023	3,569	10.02	863	9.52	254	182.22	86	(60.91)	153	(8.38)	4,925	9.23
2024	4,318	20.99	1,031	19.47	308	21.26	136	58.14	193	26.14	5,985	21.52
2028 (Projected)	5,248	21.54	1,521	47.53	396	28.57	138	1.47	225	16.58	7,528	25.78
2029 (Projected)	6,897	31.42	1,802	18.47	237	(40.15)	538	289.86	246	9.33	9,719	29.10
Share in 2024 (%)	**72.15%**		**17.23%**		**5.15%**		**2.27%**		**3.22%**		**100%**	

Source: Based on IBFC (2025) and ICD–LSEG Islamic Finance Development Report 2025

Table 4.2 highlights that the global Islamic finance ecosystem in 2024 is supported by a broad and evolving institutional infrastructure. From a governance perspective, while Islamic finance operates in 57 countries, only 23 have central Shariah committees. The sustainability dimension reflects growing alignment with global trends, evidenced by USD 61.5 billion in Environmental, Social, and Governance (ESG) *Sukuk* and continued contributions through corporate social responsibility (CSR) activities. In terms of awareness, the large number of events and news coverage demonstrates increasing global

engagement and market visibility. The knowledge base is also expanding, with significant contributions from education providers, research publications, and academic journals, supporting human capital development and innovation.

Table 4.2: Islamic Finance Industry Supporting Ecosystem in 2024

A	**Governance**	
1	Countries	57
2	Countries with Central Shariah Committee	23
3	Scholars in Shariah Boards	1,617
B	**Sustainability**	
4	Total Value of ESG *Sukuk* Outstanding (USD Billion)	61.5
5	Total CSR Funds Disbursed (USD Billion)	1.7
C	**Awareness**	
6	Number of Islamic Finance In-person Events	1,031
7	Islamic Finance Virtual Events	379
8	Number of Islamic Finance News	9,480
D	**Knowledge**	
9	Islamic Finance Education Providers	1,186
10	Islamic Finance Research Papers Produced	5,291
11	Islamic Finance Journals	379

Source: Based on IBFC (2025) and ICD–LSEG Islamic Finance Development Report 2025

Table 4.3 reflects Bangladesh's gradual yet fluctuating position among the Top 10 countries in the Islamic Finance Country Index (IFCI) over 2015–2024. Bangladesh initially appeared in the lower ranks (around R10) during 2015–2017. Over time, its position improved, reaching mid-tier rankings (around R8–R7) in subsequent years, suggesting progress in market development, institutional growth, and industry recognition. However, the movement is not consistently upward, as it shows fluctuations, including a decline in the most recent year. This pattern indicates that while Bangladesh has established a presence in the global Islamic finance landscape, its progress remains uneven and lacks sustained competitiveness, underscoring the need for structural reforms, stronger governance, and enhanced regulatory and market frameworks to achieve a more stable and higher ranking.

Table 4.3: Islamic Finance Country Index (Top 10 IFCI 2015–2024)

Rank	Y 2015	Y 2016	Y 2017	Y 2018	Y 2019	Y 2020	Y 2021	Y 2022	Y 2023	Y 2024
R 1	Iran	Malaysia	Malaysia	Malaysia	Indonesia	Malaysia	Indonesia	KSA	KSA	Iran
R 2	Malaysia	Iran	Iran	Iran	Malaysia	Indonesia	KSA	Malaysia	Malaysia	KSA
R 3	KSA	KSA	KSA	KSA	Iran	Iran	Malaysia	Indonesia	Pakistan	Sudan
R 4	UAE	UAE	UAE	UAE	KSA	KSA	Iran	Iran	Indonesia	Malaysia
R 5	Kuwait	Kuwait	Kuwait	Kuwait	Sudan	Sudan	Pakistan	Pakistan	Iran	Brunei
R 6	Bahrain	Indonesia	Pakistan	Indonesia	Brunei	Pakistan	Sudan	Sudan	Bangladesh	Indonesia
R 7	Indonesia	Qatar	Indonesia	Pakistan	UAE	Brunei	Brunei	Bangladesh	Sudan	Kuwait
R 8	Qatar	Bahrain	Bahrain	Bahrain	Bangladesh	UAE	Bangladesh	Brunei	Brunei	Pakistan
R 9	Sudan	Pakistan	Qatar	Qatar	Kuwait	Bangladesh	UAE	UAE	UAE	Bahrain
R 10	Pakistan	Bangladesh	Bangladesh	Bangladesh	Pakistan	Kuwait	Kuwait	Kuwait	Kuwait	Bangladesh

IFCI is based on a multivariate analysis. For construction of the index, original dataset included information on several variables, including macroeconomic indicators of the countries. Variables are: (i) Number of Islamic Banks, (ii) Number of IsBFIs, (iii) Shari'ah Supervisory Regime, (iv) Islamic Financial Assets, (v) Muslim Population, (vi) Sukuk, (vii) Education & Culture, and (viii) Islamic Regulation & Law.

Source: Based on IBFC (2025) and Global Islamic Finance Report (GIFR) 2024

Table 4.4 shows that Bangladesh ranks 11th in the Islamic Finance Development Indicator (IFDI) 2025 with a score of 38, reflecting moderate performance. While it demonstrates a strong governance score (80), it lags in sustainability, knowledge, and awareness, which limits its overall position. This suggests that Bangladesh needs to strengthen its broader Islamic finance ecosystem beyond governance to improve global competitiveness.

Table 4.4: Top IFDI Countries and Global Average Score (2025)

Rank	Country	IFDI Score	Financial Performance	Governance	Sustainability	Knowledge	Awareness
1	Malaysia	135	144	98	155	101	200
2	Saudi Arabia	114	136	73	111	48	200
3	United Arab Emirates	92	88	85	56	50	200
4	Indonesia	75	59	76	32	200	49
5	Pakistan	72	40	78	24	88	200
6	Kuwait	67	47	79	29	17	195
7	Bahrain	66	47	84	30	22	173
8	Iran	64	119	55	–	21	6
9	Qatar	40	31	64	27	8	69
10	Türkiye	39	33	65	26	41	15
11	**Bangladesh**	**38**	**31**	**80**	**17**	**13**	**19**
12	Oman	34	17	75	23	15	37
13	Brunei Darussalam	31	9	72	14	22	44
14	Iraq	30	31	59	1	4	20
15	Jordan	29	16	51	41	28	14
	Global Average	**11**	**8**	**20**	**8**	**6**	**11**

Source: Based on IBFC (2025) and ICD–LSEG Islamic Finance Development Report 2025

As of end-2024, Bangladesh's banking sector comprises 61 scheduled banks, including 10 full-fledged Islamic banks. In addition, 30 conventional banks offer Islamic banking services through dedicated branches and/or windows. Table 4.5 illustrates the market share of Islamic banking across major indicators during 2018–2024. The evidence suggests a generally rising but uneven trend in the shares of financing/investment, deposits, assets, and liabilities, with several indicators such as financing, assets and liabilities peaking around 2021–2022 before moderating, while deposits and operating expenses continued rising through 2024, reflecting the expanding role of Islamic banks within the overall banking system.

Table 4.5: Market Share of Islamic Banking in Bangladesh (%)

Particulars	Market Share of IBs in the Banking Industry							
	2018	2019	2020	2021	2022	2023	2024	Trend
Financing/Investment	23.1	23.14	24.0	25.8	26.28	25.93	24.75	
Deposit (*Mudarabah* & Others)	20.1	20.96	21.6	23.5	23.03	22.18	28.15	
Assets	19.1	19.58	20.1	22.1	22.63	22.47	22.1	
Liabilities	19.4	19.85	20.4	22.3	22.93	22.75	22.5	
Equity	15.6	15.57	15.4	17.8	17.73	17.85	16.1	
Off-Balance Sheet Items	10.6	12.08	12.2	12.5	12.95	11.78	12.4	
Profit Income (Interest Income)	34.31	24.32	26.3	28.6	27.58	27.45	26.38	

Particulars	Market Share of IBs in the Banking Industry							
	2018	2019	2020	2021	2022	2023	2024	Trend
Profit (Interest) Paid to Depositor	23.13	23.04	23.2	25.1	25.61	25.16	24.89	
Non-Profit Income	9.25	10.1	7.7	8.8	11.68	10.02	10.38	
Operating Expenses	17.12	18	18.1	19.7	20.07	20.37	20.61	
Net Profit After Tax	38.32	24.01	36.7	40.4	18.14	18.33	5.54	
Remittances	35.38	35.34	40.51	49.18	54.53	54.30	36.76	
Agricultural Credit	7.01	2.57	13.41	16.94	19.85	19.04	17.46	
Number of Bank Branches	12.06	13.05	14.25	19.02	19.75	20.71	15.24	
Number of Employees in IB	18.66	20.06	21.32	23.93	25.42	24.70	24.53	

Source: Based on IBFC (2025) and Financial Stability Report of BB

Table 4.6 compares key performance and stability indicators for Islamic banks with those of the overall banking sector during 2018–2024. Islamic banks generally outperformed the industry in ROA until 2021 and in ROE until 2023, while also showing stronger investment–deposit ratios and income efficiency. However, a sharp decline in profitability and capital adequacy in 2024, coupled with rising classified investments, indicates deteriorating asset quality and increased solvency risk.

Table 4.6: Some Selected Indicators of Banking Sector of Bangladesh (%)

Indicators	2018		2019		2020		2021		2022		2023		2024	
	All	IBs	All	IBs	All	IBs	All	IBs	All	IBs	All	IBs	All	IBs
ROA	0.3	0.6	0.5	0.6	0.3	0.5	0.2	0.5	0.6	0.5	0.6	0.5	0.43	0.12
ROE	4.4	10.7	7.4	11.4	4.3	10.2	4.4	9.9	10.7	11.5	11.1	11.6	8.70	3.18
Net Profit Margin	3.0	2.2	2.1	2.9	1.4	2.4	1.3	2.3	1.4	2	1.6	2.3	1.30	1.89
Interest (Profit) Income to Total Assets (TA)	5.9	7.5	6.1	7.6	4.9	6.4	4.3	5.5	4.4	5.4	4.9	6.0	5.58	6.66
Net Interest (Profit) Income to TA	1.9	2.7	1.9	2.6	1.2	2.1	1.1	2.0	1.2	1.8	1.4	2.0	1.12	1.65
Non-Interest (Profit) Income to TA	1.9	0.9	1.8	0.9	2.0	0.8	2.0	0.8	2.1	1.1	2.0	0.9	2.43	1.14
Advance (Investment) to Deposit Ratio	77.6	90.81	77.3	94.3	81.4	83.3	73.2	84.7	79	91.4	80.4	95.3	81.55	97.06
CRAR	10.5	11.6	11.6	12.4	11.6	12.7	11.1	12.8	11.8	12.7	11.6	12.7	3.08	(4.95)
Classified Loans (Investment) to Advances	9.3	4.8	9.3	4.7	8.1	4.1	7.9	4.0	8.2	4.1	9.4	4.8	20.20	23.18
Classified Loans (Investment) to Capital	52.6	71.9	92.1	71.7	80.7	67.2	80.7	67.2	95	72.1	107.8	81.7	263.04	489.5

Source: Based on IBFC (2025) and Financial Stability Report, BB

Table 4.7 highlights the dissolution and restructuring of boards in seven Islamic banks during August–September 2024. Several of these banks were linked to the S Alam Group, while others faced separate governance and ownership concerns. They faced severe financial distress, with the non-performing loan (NPL) ratios. Given their significant market share, the crisis resulted in systemic implications. Regulatory actions were taken in

response to governance failures, deteriorating asset quality, and ownership concentration, with board restructuring and merger initiatives aimed at restoring stability and oversight.

Table 4.7: Board Dissolution and Restructuring of Islamic Banks in Bangladesh (2024)

S/n	Bank Name	Date of Board Dissolution	Key Reason
1.	Islami Bank Bangladesh PLC	August 22, 2024	S Alam Group control, governance concerns
2.	Social Islami Bank PLC	August 25, 2024	High NPL, planned for merger*
3.	Union Bank PLC	August 27, 2024	High NPL, planned for merger*
4.	Global Islami Bank PLC	August 27, 2024	High NPL, planned for merger*
5.	Export Import Bank of Bangladesh PLC	August 29, 2024	High NPL, planned for merger*
6.	First Security Islami Bank PLC	September 1, 2024	High NPL, planned for merger*
7.	Al-Arafah Islami Bank PLC	September 3, 2024	S Alam Group connection

**The merger of five banks is currently in progress*

Source: Based on IBFC (2025)

A review of the 2024 annual reports of full-fledged Islamic banks reveals notable inconsistencies in SG disclosures (Table 4.8). While six banks reported SSC meetings (averaging 6.3 annually, ranging from 5 to 11), four have not provided such information. Disclosure of Shariah awareness programs is even weaker, with only two banks reporting data. This underscores the need for a standardized reporting framework to ensure consistent, transparent, and year-wise disclosure of SSC activities and awareness initiatives.

Table 4.8: Meetings of SSC in Full-fledged Islamic Banks in 2024

S/n	Name of the Bank (Alphabetical order)	No. of Meetings of SSC	No. of Shariah Awareness Programs
1	Al-Arafah Islami Bank PLC	5	Not disclosed
2	Export Import Bank of Bangladesh PLC	5	Not disclosed
3	First Security Islami Bank PLC	Not disclosed	Not disclosed
4	Global Islami Bank PLC	Not disclosed	Not disclosed
5	ICB Islamic Bank Limited	Not disclosed	Not disclosed
6	Islami Bank Bangladesh PLC	11	5
7	Shahjalal Islami Bank PLC	6	Not disclosed
8	Social Islami Bank PLC	6	Not disclosed
9	Standard Bank PLC	5	1
10	Union Bank PLC	Not disclosed	Not disclosed

Source: Based on IBFC (2025)

In 2024, SSC fees and expenses of most full-fledged Islamic banks in Bangladesh declined markedly compared to 2023 (Table 4.9), although the reasons for this decline cannot be determined from the available data.

Table 4.9: SSC Fee and Expense of Full-fledged Islamic Banks in 2024

S/n	Name of the Bank (Alphabetical order)	2024 (BDT)	2023 (BDT)	Growth (%)
1	Al-Arafah Islami Bank PLC	526,355	491,793	7
2	Export Import Bank of Bangladesh PLC	503,100	624,600	(19)
3	First Security Islami Bank PLC	60,000	307,000	(80)
4	Global Islami Bank PLC	294,476	338,653	(13)
5	ICB Islamic Bank Limited	88,000	152,000	(42)
6	Islami Bank Bangladesh PLC	1,399,774	1,556,000	(10)
7	Shahjalal Islami Bank PLC	808,100	1,073,245	(25)
8	Social Islami Bank PLC	320,132	867,376	(63)
9	Standard Bank PLC	378,229	562,824	(33)
10	Union Bank PLC	358,400	334,800	7

Source: Based on IBFC (2025)

Table 4.10 presents the Shariah audit activities of full-fledged Islamic banks in 2024. Although banks operate wide networks of branches, sub-branches, and agent outlets, audit coverage is either limited or not disclosed in many instances. This suggests uneven compliance oversight across operational units. While some progress is evident in branch-level audits, there remains a clear need to expand audit coverage and ensure consistent, comprehensive reporting across all channels to strengthen Shariah governance.

Table 4.10: Shariah Audit Activities of Full-fledged Islamic Banks in 2024

S/n	Name of the Bank (Alphabetical order)	No. of working units as on 31.12.2024			No. of working units covered under Shariah audit in 2024		
		Branch	Sub Branch	Agent Outlets	Branch	Sub Branch	Agent Outlets
1	Al-Arafah Islami Bank PLC	226	18	100	226	Not disclosed	
2	Export Import Bank of Bangladesh PLC	155	73	9	Not disclosed		
3	First Security Islami Bank PLC	206	177	108	Not disclosed		
4	Global Islami Bank PLC	105	154	20	Not disclosed		
5	ICB Islamic Bank Limited	33	0	0	Not disclosed		
6	Islami Bank Bangladesh PLC	400	265	2783	394	33	147
7	Shahjalal Islami Bank PLC	141	5	120	140	Not disclosed	
8	Social Islami Bank PLC	181	240	370	Not disclosed		
9	Standard Bank PLC	138	0	11	Not disclosed		
10	Union Bank PLC	114	60	0	Not disclosed		

Source: Based on IBFC (2025)

4.2 Literature on Shariah Governance

IFSB defines the SG system in Islamic financial institutions (IFIs) as a set of arrangements that ensure effective and independent oversight of Shariah compliance. This includes issuing Shariah pronouncements, disseminating rulings, conducting internal compliance reviews, and periodic verification by the Shariah board (IFSB, 2009). In practice, regulatory frameworks have further institutionalized these principles. For example, Bank Negara Malaysia introduced its Shariah Governance Framework in 2011 (later revised in

2019), clearly defining the roles and responsibilities of key governance bodies, including the board of directors, Shariah committee, senior management, and control functions. The Shariah board plays a central role in ensuring compliance across all banking operations and in promoting transparency, accountability, and ethical conduct (Alam et al., 2021).

The literature emphasizes that the effectiveness of SG depends significantly on the credibility, independence, and competence of Shariah board members, who serve as key custodians of compliance and ethical assurance (Aziz & Ghadas, 2022). Early work by Grais and Pellegrini (2006) highlights that SG arrangements are primarily internal to IFIs, relying heavily on Shariah Supervisory Boards (SSBs) and internal review mechanisms. While this proximity may facilitate responsiveness and innovation, it also introduces governance challenges, particularly relating to independence, conflicts of interest, and disclosure (Grais & Pellegrini, 2006).

Scholarly works identify core components of SG, including the board of directors, internal and external audit functions, and Shariah review units, which collectively contribute to an integrated governance system (Shah, 2019). These components help ensure that Islamic banks operate efficiently while maintaining compliance with Shariah principles. Moreover, the integration of SG practices has been shown to enhance transparency, fairness, and long-term sustainability in Islamic banking operations.

Empirical evidence further demonstrates that strong SG positively influences the performance of Islamic banks. For instance, adherence to SG principles, particularly those aligned with *Maqasid* al-Shariah, improves service quality, strengthens financial performance, and enhances institutional reputation (Kiranawati et al., 2023). Similarly, Hasan et al. (2022) and Tarihoran et al. (2021) find significant relationships between Islamic corporate governance, Shariah compliance, and financial performance. Additionally, governance structures such as SSBs positively influence CSR disclosures (Kachkar & Yilmaz, 2023). A robust SG framework also plays a critical role in mitigating legal and Shariah risks (Karimah, 2022).

Comparative studies reveal notable variation in governance approaches across jurisdictions. For example, Ulfi (2022) notes that Gulf Cooperation Council (GCC) countries adopt a more minimalist model, whereas many Asian jurisdictions follow a more interventionist approach. Other studies emphasize the need for centralized Shariah advisory mechanisms, harmonization of standards, and stronger institutional coordination (Hailu & Tekdoğan, 2023).

Despite these developments, evidence from Bangladesh suggests that SG frameworks remain underdeveloped and fragmented. The SG system in Bangladesh is predominantly voluntary rather than regulatory, lacking a comprehensive and centralized framework. In

practice, SSBs often function in an advisory capacity with limited enforcement authority, while ultimate responsibility for Shariah compliance frequently rests with the board of directors. This arrangement raises concerns regarding independence, accountability, and effectiveness, potentially leading to inconsistencies in Shariah interpretation and application across banks (Alam et al., 2019).

Furthermore, the absence of a centralized Shariah authority and binding regulatory standards has resulted in heterogeneous governance practices, weak monitoring mechanisms, and potential conflicts of interest within institutional structures. The reliance on self-developed frameworks by individual banks, coupled with limited regulatory oversight, creates scope for divergence in practices and may undermine the credibility of Shariah compliance (Alam et al., 2019).

Despite a growing body of literature, existing scholarship remains largely normative, jurisdiction-specific, and insufficiently attentive to institutional realities in emerging markets such as Bangladesh. Much of the empirical evidence is drawn from relatively mature regulatory environments, particularly Malaysia and GCC countries, where governance infrastructures, supervisory intensity, and Shariah standardization mechanisms are more developed. Consequently, the direct applicability of these findings to Bangladesh is limited.

Moreover, prior studies tend to emphasize formal governance structures while underexploring how these arrangements function in practice, especially in contexts characterized by regulatory constraints, political economy considerations, and institutional weaknesses. In Bangladesh, recent episodes of governance failure, liquidity stress, and erosion of depositor confidence in several Islamic banks underscore a disconnect between formal SG frameworks and their effective implementation. However, there is a lack of systematic, evidence-based research that critically examines these dynamics by integrating stakeholder perspectives, institutional practices, and regulatory effectiveness.

This study addresses this gap by offering a contextually grounded and empirically informed assessment of SG in Bangladesh, focusing on identifying structural deficiencies, implementation gaps, and actionable reform priorities.

4.3 Governance Structures in Islamic Banks of Bangladesh

Corporate governance (CG) is about protecting the interests of all people connected to a company while prioritizing the long-term well-being of the general public. The concept of CG aligns with Islamic teachings, as Islam strongly promotes ethics, good morals, honesty, and integrity. From an Islamic perspective, CG means that IFIs should integrate Islamic moral and ethical values into all their activities and business operations (IFSB, 2023). This implies that every decision—whether strategic or routine—should be guided by these

values, and such ethical principles should become an integral part of the organization's overall culture. Therefore, in Islamic banks, effective governance structures are essential for ensuring accountability, transparency, and strict adherence to Shariah principles. In Bangladesh, the governance framework of Islamic banks encompasses both traditional CG practices and the unique SG mechanisms that distinguish them from conventional banks, as discussed below.

4.3.1 Traditional Corporate Governance in Banks

Generally, CG refers to the fair, efficient, and transparent management of an organization to achieve clearly defined objectives. It includes the framework for structuring, directing, and controlling a corporate entity to attain long-term strategic goals that meet the expectations of shareholders, creditors, employees, customers, and other stakeholders. The World Bank defines CG as the structures and processes for the direction and control of companies that concern the relationships among management, the board of directors, controlling shareholders, minority shareholders, and other stakeholders (World Bank, 1999).

One of the most widely used global definitions is provided by the Organisation for Economic Co-operation and Development (OECD). CG involves a set of relationships between a company's management, its board, its shareholders, and other stakeholders, and it provides the structure through which the company's objectives are set, the means of attaining those objectives are determined, and performance is monitored (OECD, 2015).

The International Chamber of Commerce (ICC) defines CG as follows:

"Corporate governance is the relationship between corporate managers, directors, and the providers of equity, as well as people and institutions who save and invest their capital to earn a return. It ensures that the board of directors is accountable for the pursuit of corporate objectives and that the corporation itself conforms to the law and regulations" (ICC, 2005).

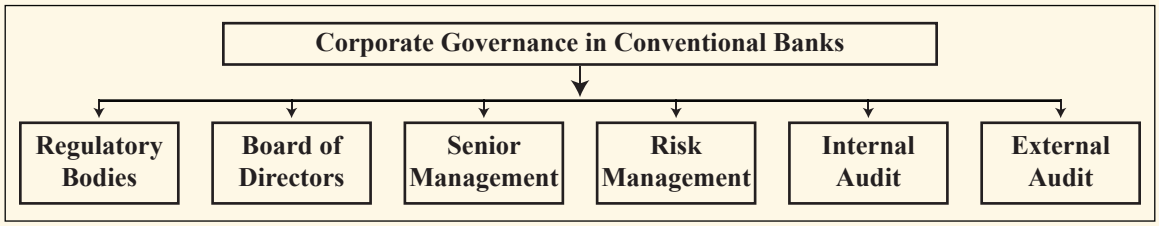
According to the Basel Committee on Banking Supervision (BCBS), CG involves the manner in which the business and affairs of banks are governed by their boards and senior management (BCBS, 2015).

IFSB incorporates SG within the broader framework of CG. According to the IFSB, CG is a set of relationships between a company's management, its board, its shareholders, and other stakeholders that provides the structure for setting the company's objectives, attaining those objectives, and monitoring performance (IFSB, 2023). Therefore, it helps define the way authority and responsibility are allocated and how corporate decisions are made.

Banks, like any other corporate entity, must ensure sound CG. Regardless of their ownership structure, banks function in many respects as public institutions because the

major portion of their funds originates from depositors and the general public. Consequently, the failure of a bank has far-reaching implications, particularly for depositors who are not responsible for the bank's managerial decisions or governance failures. Figure 4.1 presents a CG framework in conventional banks.

Figure 4.1: Corporate Governance Framework in Conventional Banks



Source: Based on Hossain and Ahmed (2025)

The CG framework typically comprises several key components, each playing a crucial role in ensuring transparency, accountability, and efficiency within an organization. The banking sector operates under the supervision and guidance of the country's central bank. A set of regulations is issued to streamline the activities of the banks. Bangladesh Bank, the central bank and apex regulatory body for the country's monetary and financial system, was established as a corporate body vide the Bangladesh Bank Order, 1972 (P.O. No. 127 of 1972) with effect from 16th December 1971. Bangladesh Bank performs all the core functions of a typical monetary and financial sector regulator, as well as several other non-core functions (www.bb.org.bd). All scheduled banks and finance companies are under the monitoring and control of the Bangladesh Bank. It establishes the legal and regulatory framework within which companies operate. Regulatory bodies ensure compliance with regulations, prevent fraud, and maintain the financial stability of the economy.

The Board of Directors (BoD), the highest governing body within a bank, is responsible for overseeing the overall management and strategic direction of the organization. Bangladesh Bank has set forth the role and responsibilities of the BoD in a bank. The board ensures that executive decisions align with shareholder interests, regulatory requirements, and ethical standards. BoD represents the owner and shareholders of the entity. As per the CG code, the board has overall responsibility for the bank, including approving and overseeing management's implementation of the bank's strategic objectives, governance framework, and corporate culture (BCBS, 2015).

The Senior Management Team (SMT), comprising key executives such as the CEO, CFO, and other top managers, is responsible for implementing the board's strategic directives, managing daily operations, and ensuring the organization's financial health. Under the direction and oversight of the board, senior management should carry out and manage the bank's activities in a manner consistent with the business strategy, risk appetite, remuneration, and other policies approved by the board, as recommended by BCBS (2015).

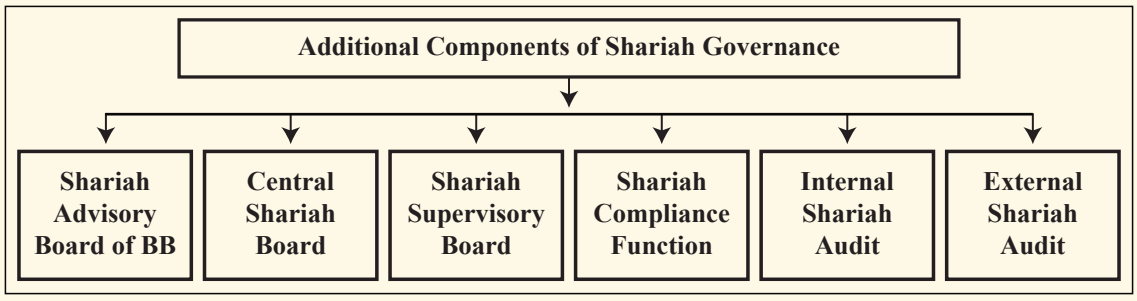
Internal Audit and Risk Management play a critical role in identifying, assessing, and mitigating risks. Internal audits will act independently and without management influence. By contrast, risk management will operate under the guidance and supervision of SMT to keep risks at a tolerable level for the bank. Both internal audit and risk management units will ensure compliance with governance policies, regulatory standards, and financial controls over the activities performed by the bank.

External audits ensure transparency, accountability, and regulatory compliance in a bank's governance framework. They verify financial statements, assess internal controls, and identify risks of fraud or mismanagement. By ensuring adherence to regulations, external audits help banks maintain credibility and avoid legal penalties. Their reports guide decision-making, strengthen risk management, and enhance stakeholder confidence, making them a vital pillar of good governance.

4.3.2 Additional Components of Governance of IFIs

In the case of IFIs, the concept of CG extends beyond the conventional relationships among management, boards, shareholders, and other stakeholders. While the general CG framework is equally applicable to IFIs, these institutions incorporate additional components to ensure Shariah compliance and the proper discharge of fiduciary responsibilities. This expanded framework reflects the unique ethical and religious foundations of Islamic finance, which require institutions to adhere not only to regulatory requirements and stakeholder expectations but also to the principles of Shariah. As such, CG in IFIs embodies a broader ethical and spiritual accountability, encompassing responsibilities not only to stakeholders but also to Allah (SWT). Accordingly, the governance structure of IFIs integrates specific mechanisms designed to oversee and ensure compliance with Shariah principles. Figure 4.2 illustrates these additional components of Islamic CG in IFIs.

Figure 4.2: Additional Components of Shariah Governance



Source: Based on Hossain and Ahmed (2025)

The Shariah Advisory Board (SAB) of Bangladesh Bank, established in 2025, serves as a central authority to ensure that Islamic banking operations in the country adhere strictly to

Shariah principles. Formed under Bangladesh Bank's official policy framework, the board provides expert guidance on Islamic jurisprudence, reviews financial products and regulatory policies for Shariah compliance, and promotes harmonization across Islamic banks. Its formation reflects Bangladesh's commitment to strengthening governance and transparency in Islamic banks, aligning with global standards in countries such as Malaysia and Bahrain.

The Central Shariah Board for Islamic Banks of Bangladesh (CSBIB) is a common forum composed of the Chairmen and Secretaries of the SSCs of the member banks. It provides guidance, rulings, and *fatwas* to ensure uniformity in Islamic finance practices within a country or jurisdiction. The CSBIB primarily focuses on advisory, regulations, and limited supervision. The CSBIB operates at a broader level rather than within a single institution.

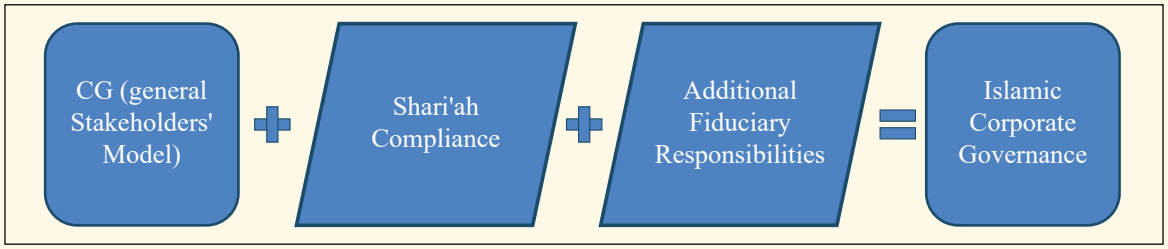
At the institutional level, the SSC serves as an advisory body that guides management on Shariah-related issues, reviews financial products, and ensures compliance with established Shariah principles. The SSC issues *fatwas* and plays a key role in product development, risk assessment, and decision-making to maintain adherence to Shariah. Therefore, the activities of SSC are classified into two levels – ex-ante and ex-post (IFSB 10).

Within IFIs, internal mechanisms such as the internal Shariah audit and Shariah compliance units actively monitor operations, policies, and transactions to detect any Shariah non-compliance. The internal Shariah audit assesses processes, identifies gaps, and recommends corrective actions to ensure all activities remain Shariah-compliant. This audit should be independent of the management's influence. Meanwhile, the Shariah compliance unit works continuously with various departments under its management, offering real-time guidance to prevent any violations. The Shariah compliance function is a part of management.

To enhance credibility and transparency, the external Shariah audit function, as an independent oversight mechanism, verifies whether IFIs maintain compliance with Shariah. The audit reassures shareholders, investors, and regulatory bodies that the institution's financial activities adhere to ethical and Shariah guidelines. At present, there is no external Shariah audit system in Bangladesh.

Together, these components form a comprehensive governance framework to ensure Shariah compliance within IFIs. By fostering transparency, accountability, and ethical financial practices, this framework strengthens stakeholder trust and contributes to the sustainable growth of Islamic banking and finance. Figure 4.3 presents the structure of Islamic CG.

Figure 4.3: Structure of Islamic Corporate Governance



Source: Authors' creation

4.3.3 Impact of Good Corporate Governance in IFIs

One of the most important objectives of CG is the resolution of the principal-agent conflict of interest, with a view to promoting the interests of all stakeholders and the soundness and stability of the financial system (Chapra & Ahmed, 2002).

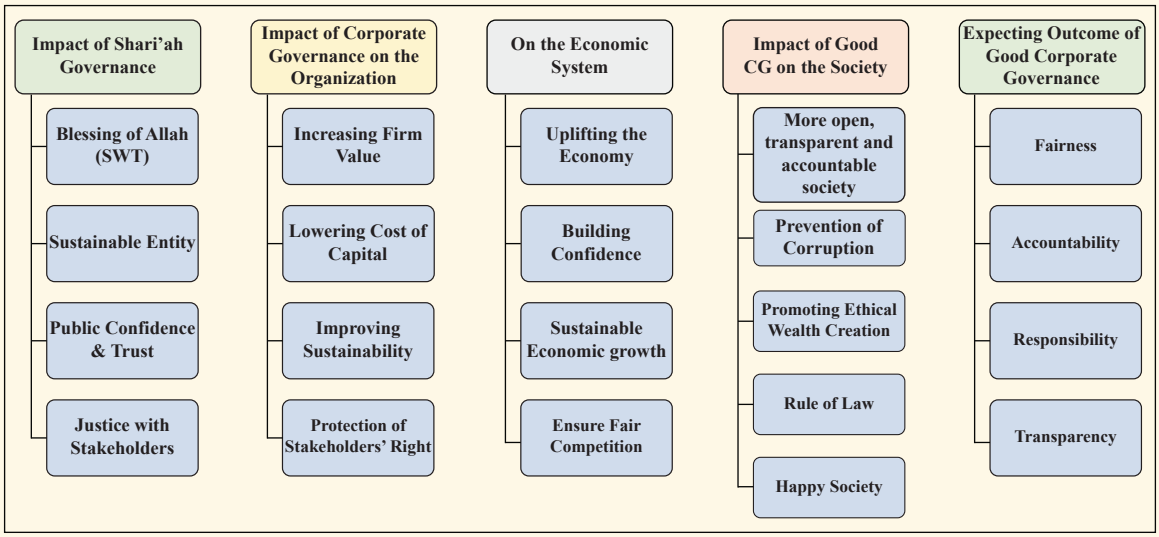
In IFI, stakeholders include capital providers (*Rab al-Maal*) and other capital contributors. Effective governance ensures that practices and policies do not disproportionately benefit owners or equity holders. By promoting an equitable distribution of risks and rewards, it protects the interests of all parties involved, upholds ethical standards, and fosters trust, accountability, and sustainability, ultimately benefiting the broader economy and society.

Stakeholders expect strict adherence to Shariah and require a corporate structure that guarantees compliance across all operations. Effective governance in Islamic banks goes beyond conventional practices, necessitating a deep understanding of Islamic principles and ethics, as well as mechanisms for transparency, accountability, and fairness. Adhering to these principles helps Islamic banks maintain stakeholder trust and confidence, thereby reinforcing their reputation as ethical and reliable institutions. Without effective CG, it may not be possible to strengthen Islamic banks and to enable them to perform their role effectively (Chapra & Ahmed, 2002).

A good corporate and SG culture may bring immense benefits to institutions and society as a whole. A compliant culture plays a crucial role in various aspects of an organization, the economic system, and society. SG, in particular, brings the blessing of Allah (SWT), embedding divine accountability into organizational practices. This spiritual foundation strengthens justice and fairness in dealings with stakeholders. Within an organization, it enhances firm value, lowers the cost of capital, improves long-term sustainability, and protects stakeholders' interests. In the broader economic system, CG revitalizes the economy, builds confidence, promotes sustainable economic growth, and fosters competitiveness through fair competition. At the societal level, it contributes to a more open, transparent, and accountable society, upholds the rule of law, encourages ethical

wealth creation, and ensures social justice, thereby fostering a disciplined life. Figure 4.4 summarizes the impact of the good corporate and SG environment of a country.

Figure 4.4: Impact of Good Corporate and Shariah Governance of IFIs



Source: Hossain and Ahmed (2025)

4.3.4 Regulatory Framework for Governance Structure of Islamic Banks

4.3.4.1 Local Regulatory Framework

The governance structure of Islamic banks in Bangladesh is primarily governed by the Bank Companies Act 1991 and the Companies Act 1994, which provide the fundamental legal basis for the establishment and operation of banks, including Islamic banks. In addition, the Guidelines for Conducting Islamic Banking, issued by Bangladesh Bank in 2009, provide specific operational and governance guidance for Islamic banking activities in the country. Alongside these, CG codes issued by Bangladesh Bank and the Bangladesh Securities and Exchange Commission (BSEC) are applicable to Islamic banks. Moreover, the Prudential Regulations for Banks contain various regulatory requirements designed to strengthen governance, risk management, and accountability within banks.

Besides the above, Bangladesh Bank has issued BRPD Circular No. 02 (February 11, 2024) and BRPD Circular Letter No. 56 (December 30, 2024) outlining specific guidelines regarding the formation of the BoD and clarifying their roles and responsibilities in ensuring effective governance in banks.

Furthermore, the Islamic Banking Regulation and Policy Department of Bangladesh Bank issued Circular No. 01 on 28 September 2025, providing comprehensive guidance on the governance of SSC in banks operating Islamic banking activities. The circular emphasizes that the responsibility for ensuring all deposit, investment, and other banking activities comply with Shariah rests with the bank's BoD, whose members must possess adequate

knowledge of Shariah and Islamic banking principles. The circular also provides that banks—both full-fledged Islamic banks and conventional banks with Islamic banking branches and windows—should constitute an SSC comprising knowledgeable, skilled, and impartial experts in Islamic jurisprudence. While the circular outlines the broad framework for SSC formation, it recognizes that detailed guidance is required on SSC composition, member appointment and removal, tenure, remuneration, duties, responsibilities, selection of chairman and secretary, establishment of Shariah secretariat, decision-making processes, preparation of Shariah compliance reports, annual SSC reports, performance evaluation of members, and maintaining confidentiality. Consequently, banks are expected to follow best practices in structuring their SSCs to ensure effective SG in all Islamic banking operations.

4.3.4.2 International Standards and Best Practices

In addition to domestic regulations, Islamic banks in Bangladesh are guided by international standards developed by institutions such as AAOIFI and IFSB.

In particular, AAOIFI Governance Standards (GS) collectively establish a comprehensive international framework for the governance of IFIs, with a strong emphasis on SG, accountability, and ethical conduct. These standards cover key areas, including the overall SG framework, Shariah review and audit (both internal and external), the independence, appointment, composition, and functioning of SSBs, and the establishment of Shariah compliance functions. They also address governance structures, including audit and governance committees, fiduciary responsibilities, and rating mechanisms, while promoting transparency through disclosure and reporting standards. In addition, the standards incorporate broader dimensions, such as CSR, ethical frameworks, and centralized Shariah oversight through mechanisms such as the Central Shariah Board. Collectively, these standards provide a structured and integrated approach to ensuring that Islamic banks operate consistently, with integrity, effective oversight, and full compliance with Shariah principles, and that governance practices align with international best practices.

Complementing the detailed SG standards issued by AAOIFI, IFSB provides a broader prudential and governance-oriented framework for IFIs. In this regard, the IFSB-10, *Governance Guiding Principles for Institutions Offering Islamic Financial Services (IIFS)* highlights the importance of sound governance structures, clear lines of responsibility, and effective internal control mechanisms, emphasizing that boards must ensure Shariah compliance, ethical conduct, and risk management are embedded in decision-making processes. Building on this foundation, the IFSB-30, *Revised Guiding Principles on Corporate Governance for IIFS,* provides a more comprehensive and updated framework focusing on board accountability, risk governance, transparency, and fiduciary responsibilities toward investment account holders (depositors), while reinforcing the need

for an effective and independent SG framework integrated within overall governance structures. Together, AAOIFI and IFSB standards offer a complementary, holistic approach to governance, combining detailed Shariah-compliance requirements with broader CG and risk management principles.

In addition, Islamic banks in Bangladesh are also guided in their operations and governance by internationally recognized standards and frameworks, such as the Internal Control–Integrated Framework (2013) of the Committee of Sponsoring Organizations of the Treadway Commission (COSO), the G20/OECD Principles of Corporate Governance (2023) of the OECD, and key standards issued by the BCBS. Complementary guidance from the Institute of Internal Auditors (IIA) and the International Federation of Accountants further strengthens internal audit practices and ethical standards. Collectively, these international frameworks enhance accountability, transparency, and stakeholder confidence while ensuring alignment with both prudential requirements and Shariah principles.

4.3.4.3 Implementation Challenges

Despite the presence of both local regulatory frameworks and international standards, significant implementation challenges persist in Bangladesh's Islamic banking sector. In particular, many Islamic banks face difficulties in ensuring the effective functioning of SSCs due to incomplete implementation of governance mechanisms, inadequate Shariah audit systems, and limited oversight of SSC activities. Moreover, Bangladesh currently lacks an independent external Shariah audit framework, which further weakens the overall SG structure. Another critical limitation is the absence of dedicated legislation specifically governing Islamic banking, which creates regulatory ambiguities and allows governance deficiencies to persist.

5. Findings and Discussion

5.1 Survey Findings

This section presents the empirical findings from the questionnaire survey, providing a systematic assessment of the effectiveness of SG in Islamic banks in Bangladesh. The analysis focuses on multiple dimensions, including the role and performance of SSCs, the robustness of governance structures, the effectiveness of regulatory oversight, the quality of Shariah-related disclosures, and the interaction between governance and institutional stability. Drawing on responses from key stakeholders across the banking sector, the findings offer insights into both the formal presence and the practical functioning of SG mechanisms.

The results reveal significant gaps between regulatory expectations and operational realities, highlighting structural weaknesses, capacity constraints, and enforcement

challenges that impact governance outcomes in practice. Together, these findings provide a basis for a critical evaluation of the existing framework and inform the policy recommendations discussed in subsequent sections. The evidence further suggests that SG in Bangladesh is at a critical inflection point. Moving forward requires transitioning from a certification-based model to a governance-driven approach, in which SSCs function not merely as contract validators but as active participants in risk governance, accountability, and value creation. A summary of the questionnaire survey is presented in Tables 5.1–5.6.

5.1.1 Role, Effectiveness, and Structural Limitations of SSC

The survey findings (Table 5.1) reveal a mixed but structurally constrained role of the SSC within Islamic banks in Bangladesh. While a majority of respondents perceive the SSC as formally important, its practical effectiveness appears limited and uneven.

A relatively positive perception emerges regarding the formal role of SSCs in ensuring Shariah compliance, with 60 percent of respondents agreeing or strongly agreeing that SSCs play an effective role (SSC4). Similarly, 65 percent believe SSCs operate independently from management influence (SSC1), suggesting that formal independence is, at least nominally, recognized.

However, deeper analysis reveals significant weaknesses in substantive oversight. A large proportion of respondents (60%) disagree that SSCs effectively scrutinize high-risk and related-party investments (SSC3), and an even higher proportion (70%) believe SSCs are ineffective in preventing questionable investments prior to approval (SSC5). This indicates a reactive rather than a proactive governance function, where SSCs may validate structures ex post rather than shape decisions ex ante.

Moreover, technical capacity concerns are evident. Only 25 percent of respondents agree that SSC members possess sufficient financial and banking expertise (SSC2), while 45 percent disagree. This highlights a critical gap between Shariah knowledge and financial sophistication, limiting the SSC's ability to evaluate complex banking risks.

The findings also suggest a form-over-substance challenge. Half of the respondents remain neutral on whether SSCs evaluate economic substance (SSC6), and 35 percent agree that SSCs primarily serve a marketing function, while half (50%) disagree (SSC9). This aligns with broader critiques in the literature that SG risks becoming symbolic, particularly when certification is detached from real economic outcomes.

Importantly, respondents strongly emphasize accountability. A significant majority (75%) agree that failure to detect major non-compliance constitutes governance negligence (SSC12), and 85 percent support holding SSC members accountable for governance

failures (SSC13). This signals a clear demand for stronger accountability frameworks, moving beyond advisory roles toward enforceable responsibility.

Overall, the SSC in Bangladesh appears to operate within a compliance-oriented, certification-driven paradigm, with limited influence over core risk-taking decisions—raising concerns about the depth of SG.

Table 5.1: SSC Role and Oversight (Response %)

Code	Measurement Item	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
SSC1	The SSC operates independently from management influence.	5.00	25.00	5.00	50.00	15.00
SSC2	SSC members possess sufficient financial and banking expertise.	15.00	30.00	30.00	20.00	5.00
SSC3	SSC scrutinizes high-risk and related-party investments.	15.00	45.00	15.00	25.00	0.00
SSC4	The SSC plays an effective role in ensuring Shariah compliance.	0.00	25.00	15.00	50.00	10.00
SSC5	The SSC is effective in preventing questionable investments before approval.	15.00	55.00	20.00	5.00	5.00
SSC6	The SSC evaluates economic substance in addition to contractual form.	5.00	20.00	50.00	25.00	0.00
SSC7	The SSC considers risk concentration and portfolio quality.	5.00	30.00	20.00	40.00	5.00
SSC8	The SSC adds substantive value to Islamic banking operations beyond formal certification.	10.00	25.00	35.00	30.00	0.00
SSC9	The SSC primarily serves a marketing function rather than strengthening governance.	10.00	40.00	15.00	35.00	0.00
SSC10	Positive Shariah certification does not necessarily reflect high-quality investments.	15.00	20.00	30.00	25.00	10.00
SSC11	Good Shariah performance does not automatically imply sound asset quality.	15.00	15.00	20.00	35.00	15.00
SSC12	Failure of SSC to detect major non-compliance constitutes governance negligence.	0.00	15.00	10.00	45.00	30.00
SSC13	SSC members should be accountable for the governance failures in Islamic banks.	5.00	10.00	0.00	55.00	30.00

Source: Questionnaire Survey

5.1.2 Shariah Governance Structure and Institutional Framework

Table 5.2 indicates that while formal governance structures exist, they lack clarity, transparency, and standardization. Only 40 percent of respondents agree that Islamic banks have clearly defined internal SG frameworks (SGSF1), while 35 percent disagree. More

critically, 60 percent of respondents report that such frameworks are not publicly available (SGSF2), highlighting a transparency deficit that may undermine stakeholder trust.

Alignment with international standards (e.g., AAOIFI and IFSB) is also ambiguous, with 40 percent of respondents remaining neutral (SGSF3). This suggests that standard adoption may be partial, inconsistent, or not well understood by practitioners.

A notable and important finding relates to SSC composition. While 55 percent support scholar-only SSCs (SGSF6), a much stronger consensus (95%) favors a balanced composition combining Shariah scholars and industry experts (SGSF7). This reinforces the earlier finding on technical gaps and supports the argument that interdisciplinary expertise is essential for effective SG. Furthermore, there is overwhelming support (95%) for strengthening fit-and-proper criteria for SSC members (SGSF8), indicating recognition that current qualification and appointment standards are insufficient.

Table 5.2: Shariah Governance Structure and Framework (SGSF) (Response %)

Code	Measurement Item	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
SGSF1	Islamic banks in Bangladesh have clearly defined internal Shariah governance frameworks.	0.00	35.00	25.00	35.00	5.00
SGSF2	Shariah governance structures are publicly available.	15.00	45.00	15.00	25.00	0.00
SGSF3	Shariah governance frameworks align with international standards (e.g., AAOIFI, IFSB).	5.00	15.00	40.00	35.00	5.00
SGSF4	Internal policies clearly define SSC roles and responsibilities.	0.00	30.00	10.00	55.00	5.00
SGSF5	SSC members play their roles independently in practice.	5.00	35.00	20.00	40.00	0.00
SGSF6	The composition of SSCs consisting solely of Shariah scholars enhances the effectiveness of SSC deliberations.	5.00	15.00	25.00	45.00	10.00
SGSF7	A balanced composition of SSCs comprising both Shariah scholars and industry experts enhances the effectiveness of SSC deliberations.	0.00	0.00	5.00	60.00	35.00
SGSF8	The fit-and-proper criteria for SSC members should be strengthened.	5.00	0.00	0.00	65.00	30.00

Source: Questionnaire Survey

5.1.3 Regulatory Framework and Supervisory Effectiveness

The regulatory environment is perceived as incomplete and weakly enforced, despite some recognition of its structural presence, as depicted in Table 5.3. Half of the respondents (50%) agree that the regulatory framework is comprehensive (RFOE1), suggesting that rules may exist on paper. However, this perception sharply contrasts with views on implementation and enforcement.

A striking 85 percent of respondents either disagree or remain neutral regarding the effectiveness of regulatory supervision (RFOE2), and a similar proportion (80%) either disagree or remain neutral on whether enforcement mechanisms are strong enough to deter governance failures (RFOE3). This indicates a significant enforcement gap, where regulatory provisions lack practical impact. Additionally, while 90 percent of respondents agree that coordination between regulators and SSCs would enhance governance (RFOE5), 70 percent state that such coordination is not currently present in practice (RFOE6). This highlights a disconnect between regulatory design and operational reality.

Table 5.3: Regulatory Framework and Oversight Effectiveness (RFOE) (Response %)

Code	Measurement Item	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
RFOE1	The regulatory framework for Shariah governance is comprehensive.	0.00	25.00	25.00	45.00	5.00
RFOE2	Regulators effectively supervise compliance with Shariah governance standards.	5.00	40.00	40.00	10.00	5.00
RFOE3	Enforcement mechanisms are strong enough to deter governance failures.	0.00	40.00	40.00	20.00	0.00
RFOE4	Clear guidelines exist for addressing governance failures.	5.00	35.00	30.00	30.00	0.00
RFOE5	Coordination between regulators and SSCs enhances governance effectiveness.	0.00	0.00	10.00	65.00	25.00
RFOE6	Coordination between regulators and SSCs is currently present in practice.	20.00	50.00	5.00	25.00	0.00

Source: Questionnaire Survey

5.1.4 Shariah Disclosure Quality and Reporting Practices

Table 5.4 points to moderate disclosure practices but insufficient depth and analytical rigor. While a plurality of respondents agree that SSC reports provide meaningful disclosures (40%) and a majority agree that these reports explain the basis of Shariah decisions (55%) (SDQR1–2), concerns remain about substantive transparency. A majority (55%) of respondents believe that disclosure quality reflects governance performance (SDQR4), but this is counterbalanced by 65 percent agreeing that current reports lack sufficient analytical depth (SDQR5). Furthermore, only 40 percent agree that significant non-compliance events are disclosed (SDQR3), suggesting selective or incomplete reporting, which may obscure underlying risks.

Encouragingly, there is strong consensus (85%) that enhanced disclosures would improve depositor trust (SDQR6). This highlights disclosure reform as a high-impact, low-cost intervention for strengthening market confidence. Thus, disclosure practices appear to be compliance-driven and standardized, but not sufficiently insightful, transparent, or decision-useful.

Table 5.4: Shariah Disclosure Quality and Reporting (SDQR) (Response %)

Code	Measurement Item	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
SDQR1	Shariah compliance reports provide meaningful disclosure rather than customary statements.	5.00	30.00	25.00	40.00	0.00
SDQR2	SSC reports clearly explain the basis of Shariah decisions.	5.00	25.00	15.00	55.00	0.00
SDQR3	SSC reports disclose significant non-compliance events.	10.00	30.00	20.00	40.00	0.00
SDQR4	SSC disclosure quality reflects true governance performance.	5.00	30.00	10.00	50.00	5.00
SDQR5	Current SSC reports lack sufficient analytical depth.	0.00	15.00	20.00	55.00	10.00
SDQR6	Enhanced disclosures by the SSCs would improve depositor trust.	0.00	5.00	10.00	60.00	25.00

Source: Questionnaire Survey

5.1.5 Governance Dynamics and Crisis Interaction

The findings of the Table 5.5 strongly establish that SG effectiveness is deeply embedded within broader institutional governance structures. An overwhelming majority of respondents affirm that board commitment (75%) and senior management support (85%) significantly influence SSC performance (GSI1–2). Similarly, 90 percent recognize the importance of internal Shariah audit effectiveness (GSI3), indicating that SSC effectiveness is interdependent rather than standalone. Critically, all respondents agree that weak internal governance structures reduce SSC effectiveness (GSI4), underscoring that SSC limitations are often symptomatic of broader governance failures. The relationship between governance and financial distress is also clearly recognized. A significant majority agree that governance deficiencies contributed to recent defaults (90%) and that liquidity crises expose governance weaknesses (65%) (GSI5–6). This confirms that SG is not merely a compliance function, but a core determinant of financial stability.

Table 5.5: Governance Dynamics and Crisis Interaction (GSI) (Response %)

Code	Measurement Item	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
GSI1	Board-level commitment influences Shariah governance effectiveness.	0.00	10.00	15.00	50.00	25.00
GSI2	Senior management support influences SSC performance.	0.00	10.00	5.00	65.00	20.00
GSI3	Internal Shariah audit effectiveness influences governance outcomes.	0.00	5.00	5.00	75.00	15.00
GSI4	Weak internal governance structures reduce SSC effectiveness.	0.00	0.00	0.00	80.00	20.00
GSI5	Liquidity crises expose weaknesses in governance systems.	5.00	20.00	10.00	35.00	30.00
GSI6	Governance deficiencies contributed to recent defaults.	0.00	0.00	10.00	50.00	40.00

Source: Questionnaire Survey

5.1.6 External Shariah Assurance and Market Confidence

The survey reveals strong and consistent support for external Shariah assurance mechanisms (Table 5.6). A vast majority of respondents support the introduction of external Shariah audits (90%) and ratings (80%) as tools to enhance governance (ESAMC1, ESAMC3). Even more striking is the level of agreement that such mechanisms would improve stakeholder trust, with 95 percent supporting external Shariah audits and 90 percent supporting Shariah ratings (ESAMC2, ESAMC4).

These findings indicate a clear market demand for independent assurance mechanisms, reflecting limited confidence in existing internal governance arrangements. External assurance mechanisms are therefore perceived not only as complementary tools, but as necessary institutional innovations to restore credibility and strengthen discipline in the sector.

Table 5.6: External Shariah Assurance and Market Confidence (ESAMC) (Response %)

Code	Measurement Item	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
ESAMC1	External Shariah audit would enhance Shariah compliance and governance of Islamic banks.	0.00	0.00	10.00	65.00	25.00
ESAMC2	External Shariah audit would enhance stakeholder trust in Islamic banks.	0.00	0.00	5.00	60.00	35.00
ESAMC3	External Shariah rating would enhance Shariah compliance and governance of Islamic banks.	0.00	0.00	20.00	45.00	35.00
ESAMC4	External Shariah rating would enhance stakeholder trust in Islamic banks.	0.00	0.00	10.00	45.00	45.00

Source: Questionnaire Survey

Taken together, the survey findings present a coherent and multi-layered diagnosis of Shariah governance in Bangladesh. Formal structures exist but lack substantive effectiveness, particularly in risk oversight and decision-making influence. Technical and competency gaps within SSCs limit their ability to engage with complex financial realities, while weak enforcement undermines the credibility of the regulatory framework. Disclosure practices are insufficiently transparent and analytical, reducing their usefulness to stakeholders. The findings also suggest that Shariah governance weaknesses reflect broader institutional deficiencies rather than isolated problems. There is therefore strong demand for reform through enhanced accountability, stronger fit-and-proper criteria, and external assurance mechanisms. These findings align with broader concerns in Islamic finance regarding the risk of "form over substance", where compliance structures exist without delivering meaningful governance outcomes. In the Bangladesh context, this challenge is further compounded by institutional weaknesses, regulatory gaps, and recent sectoral crises.

5.2 Findings from FGDs and KIIs

5.2.1 Dual Governance Structure and Implementation Gaps

The findings from the FGDs and KIIs indicate that SG in Islamic banks in Bangladesh is evolving within a dual governance framework increasingly aligned with broader CG structures. While there is no inherent legal conflict between corporate and SG regulations, the main challenge lies in their effective coordination and implementation. Evidence suggests that governance outcomes are significantly influenced by political economy factors, including external pressures, politically exposed persons (PEPs), weak enforcement of regulatory provisions, and institutional capacity constraints, all of which undermine independence and accountability.

Although the regulatory framework is relatively well-established, a persistent gap remains between formal provisions and actual practice. Governance mechanisms are often implemented in a procedural or compliance-oriented manner, with limited focus on ensuring substantive Shariah compliance in transactions and operational activities.

5.2.2 Formal Compliance versus Substantive Shariah Implementation

A recurring theme in the discussions is that SG is largely documentation-driven rather than substance-oriented. While formal processes—such as issuing *fatwas*, preparing audit reports, and maintaining compliance documentation—are generally followed, the implementation of Shariah principles at the operational level is often inconsistent. Although SSCs play a central role in the SG framework, they often engage minimally, relying heavily on management-provided information rather than conducting independent verification. As a result, their role frequently becomes limited to procedural compliance, raising concerns about whether Shariah oversight is genuinely effective or merely symbolic.

A key finding of the study is that compliance is often assessed based on the existence of *fatwas*, audit reports, and supporting documentation, rather than the authenticity and substance of the underlying transactions. Participants noted that documentation is often used to regularize transactions rather than to ensure genuine compliance. Audit processes tend to emphasize form over substance, and reported compliance may not accurately reflect actual practices. These findings indicate a predominance of symbolic or certification-based approaches to SG rather than substantive, governance-driven compliance.

5.2.3 Weaknesses in Board Governance and Oversight

At the institutional level, board governance remains a critical concern. The dominance of the chairman, combined with weak collective decision-making, often limits board effectiveness. Independent directors, despite being formally appointed to provide

oversight, frequently lack genuine independence and, in many cases, operate as affiliates of controlling interests. Similar concerns are evident within SG structures, where SSCs and internal Shariah audit functions struggle to maintain independence due to self-censorship, managerial influence, and structural limitations.

The findings further reveal blurred boundaries between the board, management, and Shariah functions, particularly when boards become involved in operational matters such as credit approvals. This weakens the distinction between governance and management responsibilities and undermines policy-based governance. Additionally, Shariah knowledge among the BoD and the SMT is generally inadequate. Collectively, these weaknesses undermine both corporate and SG, reinforcing a system characterized by discretionary, influence-driven decision-making rather than institutionalized governance practices.

5.2.4 Independence and Effectiveness of SSCs

Although SSCs are formally established within Islamic banks, their practical effectiveness remains limited. The findings indicate a lack of standardized criteria that adequately integrate both Shariah and banking expertise in the appointment of SSC members. In practice, SSCs often have limited involvement in operational verification and rely heavily on management-provided information, limiting their ability to independently assess actual practices. Weak follow-through in implementing SSC decisions further undermines their effectiveness.

As a result, SSCs frequently function as procedural or advisory bodies rather than as active governance institutions. Their role is often confined to issuing opinions and approving documentation, with minimal engagement in monitoring and ensuring substantive Shariah compliance at the operational level.

5.2.5 Fragmented Governance Architecture

The structural arrangement of SG functions poses significant challenges. The findings reveal a fragmented institutional framework with unclear role delineation among SSCs, Shariah secretariats, internal Shariah audit, management, and compliance functions. In dual banking systems, overlapping responsibilities further weaken governance effectiveness and create ambiguity in accountability and oversight.

A major concern is the lack of a clearly defined second line of defense against SNCR. While internal Shariah audit functions exist as part of the third line of defense, there is limited evidence of a dedicated Shariah risk management or compliance function within management to proactively identify and mitigate risks. In several cases, Shariah audit functions are positioned under the Internal Control and Compliance Division (ICCD) or

business units, compromising their independence, and Shariah secretariats often lack sufficient authority and appropriate organizational standing.

These structural weaknesses are compounded by the absence of multi-layered Shariah audit practices, as external and SSC-led reviews are largely missing in practice. Collectively, these deficiencies undermine the effectiveness, independence, and overall integrity of the SG framework.

5.2.6 Weaknesses in Internal Shariah Audit and Compliance

Internal Shariah audit is identified as a critical but structurally weak component of the SG framework. The findings indicate that audit practices are primarily sample-based, creating a significant risk of undetected Shariah non-compliance. Additionally, internal auditors often face management influence and organizational pressure, leading to self-censorship and limiting their willingness to report irregularities or adverse findings objectively.

The effectiveness of the audit function is further constrained by limited independence in reporting and evaluation processes, with audit activities emphasizing post-facto rectification over preventive compliance and early risk detection. Some participants indicated that audit findings may be adjusted, softened, or suppressed, and that Shariah non-compliant income is occasionally regularized through documentation practices, raising serious concerns about the integrity and transparency of the audit.

The findings also reveal a lack of multi-layered Shariah audit mechanisms in practice. External Shariah audits and SSC-led independent reviews are largely absent, reducing the overall robustness and credibility of the Shariah assurance framework.

5.2.7 Weak Integration of Shariah Compliance into Operations

The findings reveal that Shariah compliance is not effectively integrated into operational processes and is often treated as an ex post or documentation-based function rather than an integral component of transaction execution. Several operational deficiencies were identified, including inadequate verification of underlying assets in trade-based contracts, compromised documentation practices in corporate financing, and implicit guarantees in *Mudarabah* deposits.

Additionally, compliance checks at the initiation, approval, and disbursement stages are often weak or inconsistently applied, limiting the effectiveness of preventive controls. These weaknesses indicate a fundamental disconnect between formal SG frameworks and day-to-day banking operations.

5.2.8 Human Capital and Competency Gaps

Another critical dimension concerns competency and knowledge gaps among key stakeholders, including the BoD, SMT, SSC members, and operational staff. The findings consistently highlight inadequate Shariah knowledge at both strategic and operational levels, limiting the effective implementation and oversight of Shariah principles within institutions. A major constraint across the system is the shortage of qualified human capital, particularly trained *Muraqibs* and experienced Shariah professionals, compounded by limited structured training programs and insufficient academic and professional development pathways.

The findings also indicate a significant shift in the evolution of Islamic banking practices. Earlier phases of Islamic banking were characterized by a stronger ethical commitment despite comparatively weaker technical knowledge and institutional capacity. In contrast, the current environment reflects improved technical expertise but a declining ethical orientation. This transformation has contributed to a governance culture in which compliance is increasingly driven by formal and procedural requirements rather than intrinsic ethical and Shariah values.

5.2.9 Technology and System Constraints

Operational challenges are further compounded by technological limitations within the banking infrastructure. The findings indicate a heavy dependence on foreign core banking systems (CBS), many of which were not originally designed to meet the specific operational and compliance requirements of Islamic banking. As a result, banks often face delays in implementing Shariah-compliant system modifications and operational adjustments.

Additionally, the lack of standardized system architecture across Islamic banks contributes to inconsistencies in processes and compliance practices. The technological constraint reduces operational efficiency, and hinder the effective implementation of compliance requirements.

5.2.10 Political Economy and External Influence

The findings strongly suggest that many governance challenges are deeply rooted in broader political economy dynamics. The influence of PEPs, concentrated ownership structures, and family-controlled significantly affects institutional governance and decision-making processes. Participants also highlighted external pressures on both regulatory authorities and institutions, which constrain independent oversight and hinder the implementation of governance standards.

These dynamics undermine institutional independence, reduce the effectiveness of enforcement mechanisms, and create an environment in which governance decisions are often shaped by influence and vested interests rather than by formal regulatory and SG principles.

5.2.11 Institutional Culture and Behavioral Constraints

The discussions further reveal a broader institutional culture characterized by weak professionalism, "yesmanship", and fear-driven behavior. A recurring concern across interviews and FGDs is the reluctance of employees to challenge authority or raise concerns about irregularities. Self-censorship among internal auditors and Shariah personnel appears particularly significant, as many refrain from reporting issues due to fear of professional repercussions, marginalization, or loss of career opportunities.

The lack of effective whistleblowing mechanisms and preventive frameworks further limits transparency and accountability within institutions. Additionally, participants highlighted various operational malpractices, including manipulation of documentation, non-transparent procurement practices, and informal financial arrangements. These findings suggest that governance weaknesses are embedded not only at the strategic and institutional levels but also within routine operational practices, thereby undermining the integrity and effectiveness of the governance framework as a whole.

5.2.12 Policy–Implementation Disconnect

A persistent gap between policy formulation and implementation is evident within the regulatory and supervisory framework. Although Bangladesh Bank and other regulatory bodies have issued multiple circulars, guidelines, and governance frameworks, enforcement remains weak and largely procedural. Inspections and audit processes tend to focus more on documentation and formal compliance requirements than on verifying the substantive compliance of underlying transactions, resulting in a disconnect between reported compliance and actual practices.

The findings further indicate that fragmented regulatory oversight, limited coordination among supervisory departments and regulatory bodies, and broader institutional capacity constraints significantly diminish the effectiveness of governance and enforcement mechanisms. Consequently, governance frameworks often serve as procedural exercise rather than effective systems that ensure meaningful compliance and accountability.

5.2.13 Lack of Standardization and Market Discipline

From an operational perspective, several issues undermine Shariah compliance at the frontline level. The findings reveal significant variations in product structures, contract implementation, and operational practices across institutions, reflecting the lack of

standardized industry practices and guidelines for Islamic financial products. In many cases, Islamic contracts are applied inconsistently, while verification of underlying assets remains insufficient. Compliance processes also tend to rely heavily on documentation without adequately ensuring the underlying economic substance of transactions.

In dual banking systems, these challenges are further exacerbated by manpower shortages, reliance on conventional-oriented CBSs, and structural tensions between business targets and Shariah compliance requirements. Inconsistent application of regulatory requirements across institutions further undermines market discipline and creates confusion among stakeholders. Collectively, these factors contribute to compromised compliance practices, particularly in corporate working capital financing and trade-based transactions.

5.2.14 Weak Accountability and Stakeholder Representation

Accountability mechanisms within the governance framework are found to be weak and fragmented. The findings indicate that responsibility for Shariah non-compliance is often not clearly assigned, creating opportunities for blame-shifting across organizational layers. Although enforcement measures formally exist, their application remains limited and inconsistent, while the lack of a structured punishment system further undermines institutional discipline and deterrence.

Another significant concern relates to the limited representation of depositors within governance structures, despite their central role in Islamic banking under the *Mudarabah* framework. This imbalance raises broader concerns regarding fiduciary responsibility, stakeholder protection, and the overall effectiveness of governance and accountability mechanisms within Islamic banks.

6. Recommendations

The study highlights that SG challenges in Bangladesh are systemic rather than isolated. Addressing these issues requires a comprehensive and coordinated approach that combines regulatory reform, institutional strengthening, cultural transformation, and effective enforcement. Without such efforts, ongoing governance weaknesses may continue to erode public trust and hinder the long-term sustainability of Islamic banking in the country.

The FGDs and KIIs indicate several strategic directions for improvement. A clear preference emerged for principle-based regulatory approaches supported by strong, consistent enforcement mechanisms instead of overly prescriptive rule-based frameworks. Strengthening institutional capacity—particularly within regulatory authorities and Islamic banks—is essential to enhance governance effectiveness and supervisory quality. The findings also emphasize the need for structural reforms, including a clearer separation of policy, compliance, risk management, and audit functions; the establishment of dedicated

Shariah risk management units; and greater independence for SSCs and Shariah secretariats. Additionally, ongoing capacity development through structured training and knowledge-sharing initiatives for members of the BoD, SMT, SSCs, and operational staff is critical to addressing competency gaps and improving the overall quality and integrity of SG practices.

6.1 Restoring Governance Integrity through Independent and Competent Board Structures

Weak board oversight, the replacement of competent and independent directors due to political influence, and the appointment of less qualified Shariah committee members collectively undermine the integrity of governance in Islamic banks. These practices facilitate unethical financing decisions, weaken accountability, and contribute to the breakdown of corporate and SG frameworks, significantly increasing exposure to SNCR. Strengthening fit-and-proper criteria, ensuring genuine independence of the board and Shariah bodies, and integrating SG within the risk management framework are essential to restoring effective oversight, enhancing compliance, and safeguarding institutional integrity.

6.2 Aligning Corporate Governance with Shariah Governance for Effective Institutional Oversight

Without effective CG, proper SG cannot be ensured in a bank. The governance of an Islamic bank encompasses both CG and SG, and it is recognized that a bank with strong CG excels in SG. A distinctive feature of an Islamic bank is its adherence to Shariah, making it crucial for banks to improve their SG. In this context, the BoD, SMT, and SSC should fulfill their roles simultaneously.

6.3 Formalizing the Shariah Compliance Function within the Three Lines of Defense Model

Each Islamic bank in Bangladesh should establish a dedicated and effective Shariah Compliance Unit (SCU) within its management structure, tasked with implementing and monitoring the decisions, rulings, and guidelines of the SSC. Currently, Shariah compliance functions are typically housed within the Shariah Secretariat in full-fledged Islamic banks or within the Islamic Banking Division (IBD) of conventional banks offering Islamic banking services. To address this structural limitation, the proposed SCU should serve as a second line of defense—similar to risk management and compliance units—without any business or profit targets, ensuring independence and objectivity while maintaining operational effectiveness. The unit should effectively implement SSC decisions at all operational levels, continuously monitor Shariah compliance in products

and processes, closely coordinate with business units, identify and mitigate SNCRs, and provide timely reports to both management and the SSC.

6.4 Strengthening the Scope, Rigor, and Independence of Internal Shariah Audit

The effectiveness of the internal Shariah audit depends on the scope, rigor, and independence of its oversight functions. Audit coverage should extend beyond selective sampling to include population-based reviews, ensuring a comprehensive assessment of transactions and processes from a Shariah perspective. The internal Shariah audit must also adopt a system-driven approach that enables real-time identification, rectification, and prevention of Shariah non-compliance. Structurally, the internal Shariah audit function should align with the ICCD, incorporating independent on-site audits by qualified *Muraqibs*, off-site surveillance supported by robust documentation and ICT-based monitoring, and continuous follow-up mechanisms to ensure timely correction and escalation. Auditor competency is a critical factor in effectiveness; *Muraqibs* must possess a skill set that combines Shariah expertise, banking knowledge, and audit proficiency. However, in practice, internal Shariah audit independence is often constrained. Despite formal provisions, pressures such as reassignment or job insecurity discourage objective reporting. Over time, this environment leads to self-censorship, weakening the Shariah audit function and increasing the risk of undetected non-compliance.

6.5 More Active Engagement of the SSC

The effectiveness of SSC is crucial for the overall quality of SG. The SSC should function not only as a reactive body but also as a proactive institution that fosters a Shariah-compliant environment within the bank. This requires a well-composed team with a balanced mix of Shariah expertise and practical knowledge of Islamic finance and banking operations. A clearly defined Terms of Reference (ToR) is essential to outline responsibilities, authority, and reporting structures, ensuring accountability and clarity. Continuous professional development (CPD) must be institutionalized to keep SSC members informed about evolving standards, regulatory expectations, and industry practices. Additionally, regular participation of SSC members in BoD meetings and its committees is necessary to enhance their understanding of operational dynamics and address Shariah issues at the policy level. The effective functioning of the SSC also relies on strong institutional support, particularly from the Board and its Audit Committee, to ensure independence, active engagement, and meaningful contributions to governance and oversight.

6.6 Introduction of External Shariah Review and Fiduciary Rating

The current Shariah assurance framework in Islamic banks relies primarily on internal controls and the SSC, allowing little room for independent external validation. This gap

limits transparency, reduces comparability across institutions, and undermines stakeholder confidence. Additionally, fiduciary risks—especially those affecting *Mudarabah* depositors and unrestricted investment account holders—are not adequately assessed and disclosed. To address these issues, it is crucial to introduce a formal External Shariah Review framework managed by an authorized independent body, along with mandatory annual Shariah assurance reporting subject to external verification. Simultaneously, a comprehensive Fiduciary Rating framework should be developed to evaluate how effectively Islamic banks protect the interests of investment account holders. These initiatives should align with internationally recognized standards, including AAOIFI Auditing Standards for Islamic Financial Institutions (ASIFI) 6, AAOIFI GS 10, IFSB-1, and IFSB-30, to ensure consistency, credibility, and global comparability (Hossain et al., 2025).

6.7 Shariah-Based Performance Metrics for Institutions and Employees including SMT

Current performance assessment systems in Islamic banks focus heavily on business expansion and volume targets, often incentivizing the neglect of procedural discipline and Shariah requirements, which increases the risk of Shariah non-compliance. Additionally, the lack of a unified Shariah-focused key performance indicator (KPI) framework limits accountability and undermines the integration of compliance into daily operations. To address this, Shariah-oriented performance indicators should be included in both institutional and individual evaluation systems. At the institutional level, integrating Shariah parameters into an expanded supervisory framework—such as a CAMELSS-type model—would ensure that compliance is a core component of overall performance assessment, as aligned with Hossain et al. (2025).

6.8 Strengthening SSC Composition through Fit and Proper Criteria

International standards, such as AAOIFI governance standards and IFSB principles, emphasize the appointment of SSC members based on clear fit-and-proper criteria. These criteria focus on ensuring adequate expertise, integrity, and independence for effective Shariah oversight. Sound Shariah decision-making requires not only a strong grounding in Islamic jurisprudence but also a clear understanding of banking operations and business dynamics. An effective SSC should ideally have a balanced composition, with qualified Shariah experts alongside members with relevant financial and operational expertise, facilitating more informed and practical judgments (Hossain et al., 2025). According to international best practices, professional expert members may serve as non-voting members of the SSC.

6.9 Enhancing Stakeholder Awareness of Shariah Governance

Islamic banks in Bangladesh should enhance stakeholder awareness of SG by focusing on both employees and customers to improve implementation and public confidence. Notably, the lack of motivational and awareness programs for employees and customers has been identified as an SNCR in BRPD Circular No. 3/2016, Guidelines on Internal Control and Compliance in Banks, issued by Bangladesh Bank. Therefore, banks should implement structured, ongoing training programs for employees to ensure a solid understanding of Shariah principles, product structures, and compliance requirements, along with customer-focused awareness initiatives through simplified disclosures and educational campaigns. This approach would strengthen internal compliance capacity and external trust, thereby enhancing the overall effectiveness of the SG framework.

6.10 Principle-Based Regulation and Functional Separation in Supervision

In line with international standards, adopting a principle-based regulatory approach is more suitable for strengthening SG, as it promotes flexibility and informed judgment rather than rigid rule compliance. Central bank regulations should focus on overarching principles rather than prescribing detailed processes, allowing banks to design implementation mechanisms based on their size, nature, and operational complexity. From a governance perspective, clear separation between policy formulation and supervisory functions is essential to ensure objectivity and effectiveness in oversight. Furthermore, regulatory development should not be reactionary to isolated incidents within a few institutions; instead, it should prioritize cultivating a strong compliance culture. Greater emphasis should be placed on ethical conduct, institutional discipline, and sustainable governance practices rather than continuously expanding rule-based requirements.

6.11 Capacity Development and Structured Knowledge Enhancement

Concerns regarding the professionalism and effectiveness of SSC members highlight the need for a comprehensive capacity development framework across all governance layers. Targeted training should be provided to operational employees to strengthen practical implementation of Shariah requirements, while structured knowledge-sharing initiatives should be introduced for the BoD, senior management, and SSC to enhance coordination and informed decision-making. SSC members, in particular, should be equipped with foundational knowledge of economics and banking operations, while BoD members should be well-versed in governance standards and relevant domestic regulations. At the same time, a basic level of Shariah knowledge should be ensured across all stakeholders. Institutionalizing CPD for BoD, SMT, and SSC is essential to maintain competency, align with evolving standards, and improve the overall effectiveness of SG.

7. Conclusion

This study provides a comprehensive assessment of the SG practices of Islamic banks in Bangladesh. The analysis reveals a disconnect between formal governance structures and their practical effectiveness. Although the sector has grown significantly since its establishment in 1983, governance arrangements, particularly SG, have not evolved at a comparable pace. This has exposed Islamic banks to reputational risks, financial instability, eroding public trust.

The Islamic banking sector in Bangladesh is at a critical juncture that requires urgent attention to governance effectiveness. The findings indicate that governance practices exhibit a form-over-substance dynamic. SSCs, internal control functions, and regulatory frameworks exist in theory, yet their influence on core decision-making, risk management, and accountability remains limited. In practice, SSCs primarily operate under a certification-oriented approach, with insufficient engagement in assessing economic substance, monitoring high-risk transactions, or preventing governance failures. These limitations are closely linked to capacity constraints, weak independence, and unclear accountability mechanisms.

At a broader level, weaknesses in SG are intertwined with failures in overall CG. The concentration of ownership, erosion of SSC independence, and increasing politicization of banking institutions have weakened oversight. Decision-making is often influenced by informal power structures rather than institutional processes, undermining fiduciary responsibility and professional standards. These patterns reflect deeper institutional challenges where governance mechanisms are shaped more by incentives and power relations than by formal rules.

The study also links governance deficiencies to recent crises in Islamic banks. Liquidity pressures, rising non-performing assets, and declining depositor confidence are manifestations of deeper governance failures.

Addressing these challenges requires strengthening corporate and SG structures. This includes enhancing the capacity of BoD, SMT, and SSC through structured training in risk management, ethical banking practices, and regulatory compliance. Strengthening the independence and technical expertise of SSCs is critical, as they must operate free from management influence and contribute meaningfully to governance and oversight. Similarly, internal Shariah audit functions must be adequately resourced, professionally structured, and protected from undue interference to ensure effective monitoring and control.

Regulatory reforms must focus on improving enforcement, strengthening supervisory effectiveness, and enhancing coordination between regulators and governance bodies.

Adopting international best practices from jurisdictions such as Malaysia and Bahrain can help align local frameworks with global standards and improve governance outcomes. Strengthening disclosure practices and promoting transparency will also be essential for rebuilding stakeholder confidence.

Equally important is embedding a strong ethical foundation within Islamic banks. Promoting Shariah-compliant investments, ensuring transparent reporting, and reinforcing accountability mechanisms will enhance public trust and support the long-term stability of the sector. SG must be positioned not merely as a compliance function but as a central pillar of ethical and sustainable banking.

The revitalization of the Islamic banking sector ultimately depends on the effective implementation of these reforms, supported by strong regulatory oversight and a culture of professionalism and integrity. Political will and strategic support at the national level are essential. Coordinated efforts among regulators, policymakers, and financial institutions will be necessary to address existing governance weaknesses, prevent future crises, and unlock the full potential of Islamic banking as a key contributor to Bangladesh's economic development.

Without a transformation toward substantive, accountable, and ethically grounded governance, the sector risks continued instability despite its strong growth trajectory and societal relevance.

References

Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). (Various years). *Governance standards for Islamic financial institutions (GS 1–21)*. AAOIFI.

Alam, M. K., Rahman, S. A., Mustafa, H., Shah, S. M., & Hossain, M. S. (2019). Shariah governance framework of Islamic banks in Bangladesh: Practices, problems and recommendations. *Asian Economic and Financial Review, 9*(1), 118–132. https://doi.org/10.18488/journal.aefr.2019.91.118.132

Alam, M. K., Islam, F. T., & Runy, M. K. (2021). Why does Shariah governance framework important for Islamic banks? *Asian Journal of Economics and Banking, 5*(2), 158–172. https://doi.org/10.1108/AJEB-02-2021-0018

Aziz, H. A., & Ghadas, Z. A. A. (2022). Corporate governance framework for Shariah compliant corporation. In *Proceedings of the International Joint Conference on Arts and Humanities 2021 (IJCAH 2021)* (Vol. 618). Atlantis Press. https://doi.org/10.2991/assehr.k.211223.092

Bank Negara Malaysia. (2011). *Shariah governance policy document*. https://www.bnm.gov.my/index.php?ch=57&pg=144&ac=836&bb=file

Bank Negara Malaysia. (2019). *Shariah governance policy document*. https://www.bnm.gov.my/index.php?ch=57&pg=137&ac=163&bb=file

Basel Committee on Banking Supervision. (2015). *Corporate governance principles for banks*. Bank for International Settlements.

Chapra, M. U., & Ahmed, H. (2002). *Corporate governance in Islamic financial institutions* (Occasional Paper No. 6). Islamic Research and Training Institute, Islamic Development Bank.

Committee of Sponsoring Organizations of the Treadway Commission. (2013). *Internal control–Integrated framework*. American Institute of Certified Public Accountants.

Grais, W., & Pellegrini, M. (2006). *Corporate governance and Shariah compliance in institutions offering Islamic financial services* (World Bank Policy Research Working Paper No. 4054). World Bank.

Hailu, S. M., & Tekdoğan, Ö. F. (2023). Ensuring the compliance of Islamic finance applications with Shariah principles in Ethiopia: The way forward. *Hitit Theology Journal, 22*(1), 139–168. https://doi.org/10.14395/hid.1247875

Hasan, A., Amilin, A., & Nasaruddin, I. Y. (2022). Does intellectual capital and Islamic corporate governance affect financial performance and earning management on Sharia banking in Indonesia? *AFEBI Islamic Finance and Economic Review, 6*(1), 57. https://doi.org/10.47312/aifer.v6i01.399

Hossain, M. M., & Ahmed, M. U. (2025). Shariah supervisory committees in Bangladesh: Practices, issues, and policy recommendations. *Bank Parikrama: A Journal of Banking & Finance, 50*(2), 55–91. https://doi.org/10.64204/BP1019-7044/50(2)/A20253

Hossain, M.M., Alamgir. M., Karim, R., Khadem, M.A.R.K. and Arefin, M.E. (2025). "Operational Risk Management in Islamic Banks: Best Practices and Evaluation", *Banking Research Series 2025*, Issue 02, pp. 1-69. https://www.bibm.org.bd/publications-read.php?id=157

IBFC. (2025). *IBFBD 2025: Thrive with Shari'ah*. IBFC. https://ibfcbd.com/report/

IFSB. (2009). *IFSB-10: Guiding principles on Shari'ah governance systems for institutions offering Islamic financial services*. Islamic Financial Services Board.

IFSB. (2023). *IFSB-30: Revised guiding principles on corporate governance for institutions offering Islamic financial services (banking segment)*. Islamic Financial Services Board.

International Chamber of Commerce. (2005). *Corporate governance*. ICC.

Kachkar, O., & Yilmaz, M. K. (2023). How diverse are Shariah supervisory boards of Islamic banks? A global empirical survey. *International Journal of Ethics and Systems, 39*(2), 312–341. https://doi.org/10.1108/IJOES-10-2021-0195

Karimah, I. (2022). Between legal risk and sharia risk in Islamic banking: How Shariah governance address the problem. *Diponegoro Law Review, 7*(1), 88–105. https://doi.org/10.14710/dilrev.7.1.2022.88-105

Kiranawati, Y. C., Aziza, S. M., Nasim, A., & Ningsih, C. (2023). Islamic banking governance in Maqashid Sharia perspectives: A systematic literature review. *Share: Jurnal Ekonomi dan Keuangan Islam, 12*(1), 59–74. https://doi.org/10.22373/share.v12i1.15446

OECD. (2015). *OECD principles of corporate governance*. Organisation for Economic Co-operation and Development.

Shah, A. Q. A. (2019). *Exploring the best industry practice of Shariah review function under Shariah Governance Framework 2010* [Unpublished manuscript]. Universiti Teknologi MARA. https://ir.uitm.edu.my/id/eprint/31244/

S&P Global Ratings. (2024). *Banking industry country risk assessment update: July 2024*. S&P Global Ratings.

Tarihoran, A. H., Irfan, I., & Astuty, W. (2021). Effect of Sharia compliance, Islamic corporate governance, Islamic social reporting on financial performance at Islamic commercial banks in Indonesia. *Budapest International Research and Critics Institute-Journal (BIRCI-Journal), 4*(4), 9166–9173. https://bircu-journal.com/index.php/birci/article/view/2917

Ulfi, I. (2022). Comparison of Sharia governance model in Islamic financial institutions between the GCG and Asian countries. *Jurnal Akuntansi dan Manajemen Bisnis, 2*(2), 149–157. https://doi.org/10.56127/jaman.v2i2.248

World Bank. (1999). *Corporate governance: A framework for implementation*. World Bank.

Certified
Islamic Banking and Finance Professional (CIBFP)
[Led by Global & Local Islamic Finance Professionals]

Admission going on for the Next Intake

Two Intakes in a year (January & July)

Background of the Program

Islamic banking and finance industry is growing faster than the conventional counterpart both in global and local context. In line with this, there is huge demand for a set of skilled people with technical and Shariah knowledge for expediting the growth and making the Bangladeshi banking and finance industry sustainable. Besides, all types of key stakeholders should have operational knowledge in Islamic banking and finance for working together for the development of our economy. Moreover, there is no sufficient scope for acquiring relevant knowledge in this area through the existing education system. To meet-up this indispensable need of the economy, BIBM as a national-level apex training institute, is offering a unique certification program designed to develop a competent resource pool.

Summary of the Program

A. Online Module (Duration 8 weeks)

Regulations, websites and reports of different national and international entities are main sources of the study. Expected study duration for this module are 50 hours. Objectives of the module are:

- To familiarize the candidates with the associated entities in local and global context;
- To acquaint the candidates with regulations and market status; and
- To gather primary knowledge for effective participation in the subsequent modules.

B. Classroom-based On-Campus Module (Duration 14 Weeks)

Face-to-face interaction, learning guide and lecture synopses are main sources of the study for this module. Subject matter experts will lead the sessions for 42 hours. Excluding class-room discussion, desirable study duration for this module is 85 hours. Objectives of the module are:

- To accustom the candidates about the operational aspects of Islamic banking and finance;
- To make aware the candidates about the Shariah aspects in process and mechanism of Islamic banking and finance contracts; and
- To inspire the candidates for continuous thinking about a sustainable and compliant banking and finance industry.

C. Virtual Interactive Session Led by Global Islamic Finance Professionals (Duration 6 weeks)

Virtual interactive sessions with global Islamic finance professionals for about 39 hours will upgrade understanding of the candidates. The candidates will achieve following objectives by spending 40 hours, in addition to the interactive sessions:

- To share international regulations and practices related with Islamic banking and finance;
- To equip the candidate for making contribution for the development of Islamic banking and finance industry of the country; and
- To enhance the confidence level of the candidates for working in international market place.

Target Group of the Program

Certified Islamic Banking and Finance Professional (CIBFP) [Led by Global & Local Islamic Finance Professionals] program is structured considering the need of the diversified stakeholders including:

- Professionals working in Islamic banking and finance institutions either full-fledged or dual;
- Professionals working in conventional financial institutions having interactions with Islamic finance entities;
- Executives of the regulatory bodies, academic staffs and researchers of different organizations;
- Job-seekers for widening the expected market.

Maximum 30 Participants per Intake

Evaluation Process:

Assignments, Quizzes, Presentation and Pen-Paper Based Final Examination

Methods:

Self-Study of E-Learning Materials, Lecture, Scenario Based Learning, Group Discussion, Open Discussion

Course Fee BDT 60,000 per participant

For Enrollment

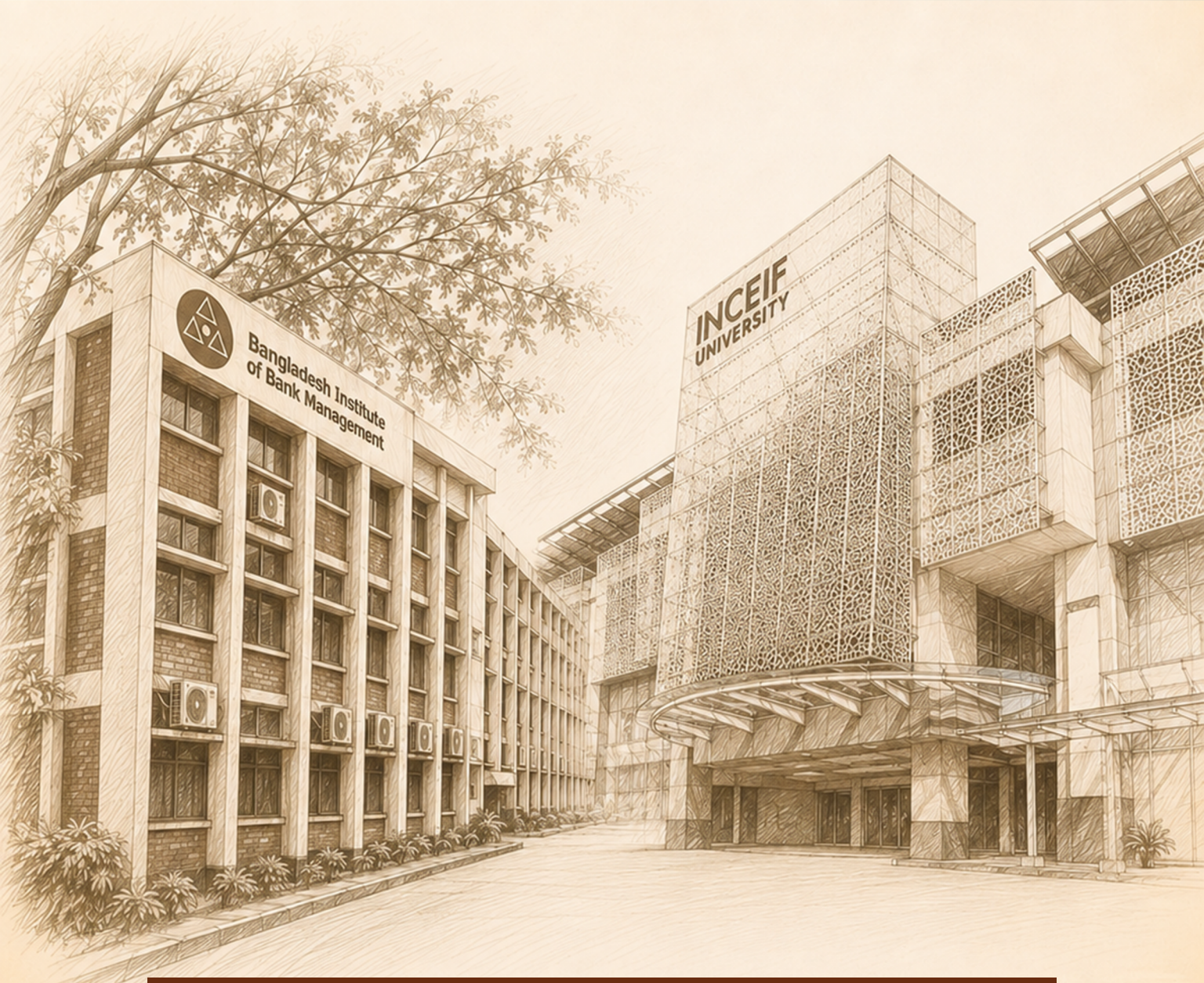
For Objectivs Contents and Rules & Regulations

For More Information

Certification Program Office
Bangladesh Institute of Bank Management
+88(02)48032091-4, +88(02)48032096-8. Ext-103
+8801733339444, +8801716-373565 (Coordinator)
cibfp@bibm.org.bd www.bibm.org.bd, www.bibmcertification.org

Bangladesh Institute of Bank Management

Plot No. 4, Main Road No. 1 (South), Section No. 2 Mirpur, Dhaka-1216



Contact Details

Bangladesh Institute of Bank Management
বাংলাদেশ ইনস্টিটিউট অব ব্যাংক ম্যানেজমেন্ট

Plot No. 4, Main Road No. 1 (South)
Mirpur, Section No. 2
Dhaka-1216, Bangladesh
Phone |+88-02-48032091-4
+88-02-48032097-8
Email | bibmresearch@bibm.org.bd
Web | www.bibm.org.bd

INCEIF UNIVERSITY

University Registration No. DU018 (W)
Blok B, Lot 41, Seksyen 51
Jalan Tun Ismail
50480, Kuala Lumpur, Malaysia
Phone | 03 7651 4000
Fax | 03 7651 4094
Email | enquiries@inceif.edu.my

Creative Partner Fajr ADVERTISING

Price: BDT 300.00
USD 8.00