

POLICY RECOMMENDATIONS OF THE 14TH MEETING OF THE COMCEC FINANCIAL COOPERATION WORKING GROUP

The COMCEC Financial Working Group (FCWG) has successfully held its 14th Meeting on September 15th, 2020 in virtual-only format with the theme of “Improving the Shariah Governance Framework in Islamic Finance”. During the Meeting, FCWG made deliberations on improving shariah governance framework in Islamic finance sector in the OIC Member Countries. Room Document, prepared in accordance with the main findings of the analytical study conducted for the 14th Meeting of FCWG and the answers of the Member Countries to the policy questions, was the main input for the discussions. Accordingly, the participants have come up with some policy recommendations.

Policy Advice 1: Developing a comprehensive legal and regulatory framework for the Shariah Governance processes and arrangements to ensure that all the operations and business activities in Islamic Finance are in accordance with Shariah.

Rationale: Islamic banking and financial market laws should contain the definitions of all currently known and approved Islamic finance products and services as well as instruments. The concerned law should stipulate the general rule of prohibiting trade in pure risk and debt. The law may also authorize the regulator to add new products once they are approved.

Furthermore, a special standard for the listed companies and Islamic financial instruments should be attached to the law with a stipulation of an annual review. Such standards would set the required conditions for ensuring Shariah compliance. Besides, a handbook on Islamic finance products and instruments should be issued by the regulators to support and facilitate the implementation of the respective law.

Policy Advice 2: Encouraging the establishment of national Shariah Supervisory Boards (SSBs) supervising the institutional SSBs.

Rationale: National Shariah Supervisory Boards (SSBs) have various important functions. They can play a very significant role in resolving the disputes between Islamic Financial Institutions (IFIs) and customers. Furthermore, approving new products, supervising IFIs on proper income purifications, reviewing yearly accounting of profit and zakat calculations and their distribution, assessing and regularly reporting Shariah non-compliance risks to shareholders and investment account holders are among the other major functions of National SSBs. The National SSBs are very instrumental in securing the interests of all stakeholders, not just shareholders.

Policy Advice 3: Developing guidelines for ensuring/facilitating the active involvement of Investment Account Holders (IAHs) in IFIs' management in accordance with their contribution to the mudaraba pool.

Rationale: Comprehensive guidelines about Shariah Governance Framework can be developed to enable all stakeholders (i.e. customers, management, shareholders, supervisory authorities) perform their roles in accomplishing the Shariah Governance objectives, and to promote soundness and stability of IFIs. In this regard, the following mechanisms, among others, might be taken into consideration during the preparation of the concerned guidelines:

- Voting in the general assembly and board of directors should be distributed between shareholders and IAHs in proportion to their resources,
- The resources provided by IAHs might be measured as of the beginning of the financial year,
- IAHs might be allowed to assign their representatives in the general assembly of IFIs,

- BoD seats might be assigned to the IAHs with the largest accounts, in a proportion of their resources.

Policy Advice 4: Encouraging talent development through training and professional certification programs and increasing the awareness of stakeholders about Shariah Governance.

Rationale: In many cases, there might be a need for improving the qualifications of SSB's members and a shortage of qualified Shariah experts. The practice of assigning SSBs membership exclusively from among Shariah specialists without identifying the necessary qualifications such as academic degree, research and teaching experience etc. is a major challenge. In this respect, a set of criteria may be identified for the appointment of the SSB members. In addition, training and professional certification programs can be conducted for talent development in this crucial area.

Policy Advice 5: Promoting the integration of Islamic Finance sector into whole economy with a view to making monetary policy more inclusive.

Rationale: In order to integrate the Islamic finance sector into the macro-economy and make monetary policy more inclusive, monetary authorities are advised to do the following:

- To issue Central Deposit Certificates (CDC) in proportion to the ratio of total Islamic finance assets to the total financial assets in the whole economy, against their cash value which would be placed as Central Deposits in IFIs. Accordingly, the monetary authority may wish to reduce money supply by the same amount or any amount that would make such issue non-inflationary, by increasing the legal reserve ratio.
- The monetary authority would set the instructions to control the investment of central deposits.
- The monetary authority can issue more CDC's and make them available for sale to the public, including IFIs. Their profits would be added to the Central Deposits in IFIs.
- The monetary authority may allow trading of CDC's in money market.
- The monetary authority can change the rate of growth of money through: (1) Adding to or subtracting from its Central Deposits balances with IFIs, (2) using open market operations in CDC's to adjust the rate of growth of the money supply.

Instruments to Realize the Policy Advices:

COMCEC Financial Cooperation Working Group: In its subsequent meetings, the Working Group may elaborate on the above-mentioned policy areas in a more detailed manner.

COMCEC Project Funding: Under the COMCEC Project Funding, the COMCEC Coordination Office issues calls for project proposals each year. With the COMCEC Project Funding, the member countries participating in the Working Groups can submit multilateral cooperation projects to be financed through grants by the COMCEC Coordination Office. For realising above-mentioned policy recommendations, the member countries can utilize the COMCEC Project Funding facility. These projects may include the organization of seminars, training programs, study visits, exchange of experts, workshops and preparation of analytical studies, needs assessments and training materials/documents, etc.