

Enhancing the Implementation of Shariah Review Practices in Islamic Banks

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Abstract

Research aim: The aim of the present study is to understand how Shariah review practices are being implemented by gathering the perceptions of Shariah officers at different Islamic banks (IBs). This is done through analysis of similarities and differences of Shariah review practices across different IBs.

Design/ Methodology/ Approach: Data was gathered through semi-structured interviews with six Shariah officers, including managers and executive levels from five different IBs.

Research finding: Utilising an institutional perspective, the findings suggest that coercive isomorphism through comprehensive guidelines on Shariah review practices promote consistent implementation of Shariah review procedures. In addition, the findings reveal that systematic communications of issues in Shariah review findings to the management and reporting the final findings to a Shariah committee is crucial in minimising threats of independence. Finally, timeliness in reporting and leveraging on other functions is proposed to enhance the effectiveness of Shariah review practices.

Theoretical contribution/Originality: This study applies institutional theory in assessing of how Shariah review practices are being implemented in Malaysian IBs. Comparatively, most prior studies utilise agency theory, which considers Shariah review practices as an oversight function in IBs.

Practitioner/Policy implication: Insights from this study underline the importance of comprehensive guidelines on Shariah review practices. This is because they enhance the standardisation of practices which improves the comparability, understandability, and quality of the work performed by Shariah officers. The study also suggests that IBs revisit their leveraging models to ensure efficient coordination of resources and improve reporting to their Shariah committees.

Originality/value: This study contributes to the literature on the establishment of the Shariah review function and internal modules of Shariah review practices through normative, coercive, and mimetic isomorphisms.

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1. Introduction

Malaysia is undoubtedly one of the most well-developed and highly regulated countries in terms of its Islamic finance industry. In fact, the country has been one of the leading global hubs of Islamic finance (BNM, 2022). Since its development more than three decades ago, Islamic finance in Malaysia has developed into a comprehensive and sophisticated marketplace, one that is open to all industry players to collaborate and mutually benefit from a highly conducive business environment of innovation and expertise (BNM, 2022).

Islamic banking is a system that relies on Islamic law in banking business practices (Isamail et. al, 2015). Each of the Islamic laws followed by Islamic banks (IBs) should be derived from the two main primary sources in Islam, which are the Quran and the Sunnah of the Prophet Muhammad (PBUH). There are a variety of products offered by IBs across the globe, such as *wadiah*, *murabahah*, *mudharabah*, and *ijarah muntanhiia bittamlik*. These products differ from one country to another, mainly to meet local demand. IBs are constantly developing and innovating products offered to customers based on the growing need of technology in today's context (Samsudin, 2016). The constant development of products offered by IBs is crucial to ensure the banks' survival and profitability. However, this development must take place within the framework of Islamic law (Al-Salem, 2009). The products, in substance, must genuinely and truly represent the principles and values of Islam.

IBs in Malaysia are highly regulated and governed by Bank Negara Malaysia (BNM). The Islamic banking industry was previously governed by the Shariah Governance Framework (SGF) in 2010, which was later replaced by the Shariah Governance Policy Document (SGPD) in 2019. Shariah governance refers to the internal control systems established within IBs. It is stipulated in the regulatory framework that IBs must establish their own internal control functions to ensure their operations are in compliance with Shariah guidelines and principles. According to Goodwin-Stewart et al. (2006), the effectiveness of an internal control function as a monitoring mechanism is positively dependent on the management commitment and those charged with governance. Their study also shows that company size is strongly associated with internal control functions.

All IBs in Malaysia are financially robust and possess their own internal control functions. According to the SGPD, Shariah governance comprises a Shariah committee that is supported by three other main internal control functions: the Shariah audit, Shariah risk management, and Shariah review

(SGPD, 2019). The SGPD (2019) defines Shariah review as a function for regular assessment of operations, business, affairs, and activities of Islamic financial institutions (IFIs) in compliance with Shariah requirements. The Shariah audit, meanwhile, refers to an independent periodical assessment on quality to ensure the soundness and effectiveness of an IFI's internal controls, risk management systems, and governance processes, as well as improving the overall in compliance with Shariah compliance of its operation, business, affairs, and activities (SGPD, 2019; Aziz et al., 2019; Ab Ghani et al.; 2022).

The Shariah review function, as one of the main internal control functions in IBs, will be the focus of this study. The Shariah review function is an internal monitoring mechanism that supports the effectiveness of Shariah committees in IBs (Ab Ghani et al., 2019; Haridan et al., 2018). As mentioned in the Shariah governance framework, all reports on findings prepared by the Shariah review function are ultimately approved by a Shariah committee. In effect, the Shariah review function acts as the eyes and ears of a Shariah committee. Most prior studies examine Shariah review from the perspective of an oversight function, but few have explored how Shariah review practices are being implemented in IBs.

Concerns have been raised on the consistency of Shariah review practices due to an absence of comprehensive frameworks and guidelines pertaining to the function by relevant authorities (Besar et al., 2009), which has led to various approaches to these practices. Such inconsistencies affect the quality of Shariah review outputs, specifically in reporting findings of Shariah non-compliance. Moreover, findings from prior literature also support the notion that the differences between Shariah audit and Shariah review are unclear (Naysary et al., 2020). It is argued that there are overlapping roles and responsibilities as well as redundancies of work between both. Hence, a proper understanding on the practical realities of Shariah review practices is crucial to differentiate the precise roles and responsibilities of the review and audit functions that act as the second and third lines of defence in IBs. Effective internal control functions in monitoring Shariah compliance are expected to reduce Shariah non-compliance and enhance public trust and confidence in IBs. In short, issues related to the Shariah review function, a critical internal monitoring mechanism supporting the Shariah committee's effectiveness, require an exploration of actual implementation of Shariah review practices. The study aims to address the gaps in identifying the similarities and differences of Shariah review practices in the absence of comprehensive guidelines and clear distinction between the Shariah review and Shariah audit.

This study extends and contributes to the literature in three ways. As noted above, the Shariah review function is one of the internal monitoring mechanisms that support the effectiveness of Shariah committees in IBs. Shariah review has mostly been examined from the perspective of it being an

oversight function (Naysary et al., 2020; Besar et al., 2009), but little attention has been paid to exploring how Shariah review practices are implemented in IBs from an institutional theory perspective. The institutional theory is best suited to examine how the implementation of governance mechanisms of Islamic banks can be improved. In their study of Shariah governance, Karbhari et al. (2020) highlight the importance of institutional theory, as it contributes towards organisational image, achieving religious legitimacy, and inspiring a more robust regulatory environment. This leaves huge impacts on IBs, including in the roles, functions, and powers of various stakeholders. Institutional theory has the requisite depth and flexibility to understand the structure of a society and an organisation (Scott, 1987). It examines the processes of why and how rules, norms, and practices are established by an organisation. Institutional theory can also explain how other Shariah practices resemble each other, even if those organisations face different enablers and challenges. A well-designed Shariah governance framework driven by institutional theory could assist in providing guidelines, strategies, and procedures for IBs to better conduct, monitor, and control their social, religious and accountability obligations (Karbhari et al., 2020). Therefore, this study aims to explore the realities of Shariah review practices in highly regulated Malaysian IBs. Since the Shariah review function reports on the state of Shariah compliance to the Shariah committee of IBs, its performance can directly and indirectly affect the quality of the Shariah committee's oversight function.

Second, there are no specific Shariah review guidelines or frameworks issued by relevant authorities (Besar et al., 2009), which has led to various approaches to Shariah review among IBs and redundancies (Naysary et al. 2020). Therefore, clarity on actual Shariah review practices would be able to improve coordination within control functions. Third, insights from this study can outline best practices for Shariah review based on the similarities and differences of practices implemented by different IBs. Outcomes of this study can serve as a future reference to relevant authorities in improving related regulatory requirements, such as those pertaining to reporting practices, independence, and competencies. In turn, this will enhance the quality of work performed by Shariah review officers who are the second line of defence in IBs.

This study performs preliminary assessments and contributes to the conduct of existing Shariah review practices using insights gathered from practitioners. Semi-structured one-on-one interviews were conducted with six IB officers, including those in managerial and executive positions, directly involved in implementation of Shariah reviews. Such interviews are an effective method for providing reliable and comparable qualitative data with different participants. It allows interviewees a degree of freedom to explain their thoughts and to highlight areas of particular interest and expertise that they feel they have (Horton et al., 2004).

The study findings outline several emerging issues and recommendations that need to be addressed to improve the delivery of Shariah review practices. First, guidelines on Shariah review best practices are expected to improve comprehension and comparability of reports to the Shariah committee. The guidelines can assist domestic and foreign IBs in managing their Shariah review practices based on their respective contexts and nature of operations. Thus, the findings might give insight and future reference to regulators and authorities in improving related regulatory requirements. Second, a clear line of communication for Shariah review findings to management and Shariah committees can address significant issues that could impact the performance of IBs, particularly those pertaining to Shariah non-compliance. Finally, clarification on the roles and responsibilities of Shariah review would reduce the overlaps and redundancies between the Shariah review and Shariah audit functions. At the same time, the guidelines also represent an avenue in which coordination and reliance on work performed by other departments within IBs can be improved.

The remainder of the paper is structured as follows: Section 2 reviews the prior literature. This is followed by an explanation of the research method in Section 3. The results of the analysis and discussion of findings are presented in Section 4, and the paper ends with concluding remarks, highlights the limitations and implications of the study, as well as recommendations for future research.

2. Literature Review

2.1 Shariah governance and Shariah review

The Islamic Financial Services Board (IFSB, 2009) defines the Shariah governance system as “the set of institutional and organisational arrangements through which an IFI ensures that there is an effective independent oversight of Shariah compliance over each of the structures and processes.” Shariah governance refers to a system controlled by an effective religious board to ensure that the activities of IFIs are in accordance with Shariah principles and conduct (Haron et al., 2022). Hence, IFIs have to set up an internal Shariah system to ensure the Shariah compliance of its activities. This internal body can be founded by a simple Shariah board or extended to an internal Shariah system, composed of a Shariah board and an internal Shariah review unit or department to support the board in performing its functions (Hassan, 2010). The Accounting and Auditing Organization of Islamic Financial Institutions (AAOIFI) has also developed a comprehensive framework for corporate governance of IFIs, which is composed of seven governance standards. These standards cover different

areas, including Shariah supervisory board (SSB) composition, Shariah review, internal Shariah review, audit and governance, SSB independence, etc.

Grassa (2013) reviews the diverse steps in the development of the Shariah governance system and its different practices in IFIs around the world, and urges regulatory authorities and the IFSB to standardise the practices of Shariah governance worldwide. The Shariah supervisory system for IFIs differ in the Gulf Cooperation Council (GCC) region from country to country. Bahrain has established a comprehensive regulatory framework governing Shariah supervisory practice at both the national and institutional level, while Qatar, the United Arab Emirates and Kuwait have only adopted a regulatory framework for Shariah supervision at the institutional level. Saudi Arabia has no specific regulation for Shariah supervisory practices, and leaves it to voluntary initiatives of IFIs and the market. Indeed, the development of Islamic finance in Saudi Arabia is considered very distinctive. There is no specific legal framework for IFIs as there is for conventional financial institutions. While GCC countries largely prioritise institutional autonomy, Shariah governance practices in Indonesia are largely based on state guidelines, with strong oversight by the Dewan Syariah Nasional-Majelis Ulama Indonesia (DSN-MUI). Conversely, in Indonesia's dual governance system, blending central regulatory oversight with institutional Shariah boards indicates attempts at consistency, but challenges to harmonise the practices remain.

In Malaysia, a balanced approach is utilised through centralised control by BNM and institutional autonomy in its implementation, which offers operational flexibility. Decentralised governance in Malaysia allows for individual IB autonomy, but this often results in greater variability. Shariah governance in Malaysia refers to the framework, regulations, and guidelines designed by the regulatory body, BNM, to uphold Islamic principles and ethics in the Islamic banking industry. Compared to conventional banks, the Islamic banking industry has a special need to ensure that the operations of the banks comply with Islamic principles. Hence, Shariah governance guidelines serve as instruments to address the distinctive requirements of the Islamic banking sector, as the concepts and structures of conventional corporate governance do not fully align with the principles upheld by IBs (Alam et al., 2019). Having standardised and robust Shariah guidelines that are universally followed and supervised by a regulatory authority is very important. These guidelines should be regularly updated to ensure their practicality and relevance over time, and can enhance accountability, transparency, disclosure, and independence of IBs in implementing Shariah principles.

The SGPD (2019) clearly notes that the presence of a Shariah committee is to observe comprehensive compliance of the operations and products

of IBs to Shariah principles. Compliance to Shariah principles indicate the alignment of IBs' daily operations and practices in accordance with the requirements of the *maqasid al-Shariah*, namely the *maslahah* or public interest (El-Maswi, 2020). A Shariah committee, being the heart of Shariah governance, owes fiduciary and oversight duties towards the IBs and their stakeholders. In order to perform robust monitoring of Shariah compliance, the Shariah committee is highly reliant on a Shariah review function (Haridan et al., 2018). The SGPD (2019) also stipulates that a Shariah review function is one of internal monitoring mechanisms that supports the effectiveness of Shariah committees in IBs. It conducts regular assessments on the compliance of IBs' activities and operations of Shariah principles. An effective Shariah review function comprises a performance of robust methodology by competent Shariah officers (Fatah & Nazer, 2017). Therefore, a Shariah review function is vital, as it is the second line of defence in monitoring any Shariah non-compliance activities or procedures in IBs. It is also critical in assisting the Shariah committee in exercising their oversight duties of ensuring Shariah compliance in IBs.

From a theoretical perspective, a Shariah review function can be supported by the three isomorphisms of institutional theory. DiMaggio and Powell (1983) argue that organisations are subjected to isomorphic pressures, such as normative isomorphism, mimetic isomorphism, and coercive isomorphism. The study underlines that the structures, conducts, and routines of an organisation are largely determined by the characteristics of their environment. Hence, the institutional theory helps explain the behaviour of organisations. In the context of this study, IBs are defined by economic and competitive pressures as well as by the operational characteristics of the respective IBs. First, IBs are largely influenced by normative pressures, for example, through the requirement of the establishment of the Shariah review function, which is outlined in the rulings of the SGPD. Meanwhile, the implementation of Shariah review practices is greatly determined by mimetic pressures due to the absence of a Shariah review framework. Thus, internal practices are dominated and determined individually by Shariah officers and the Shariah committees of IBs, largely contributing to the similarities and differences in practice between them. Thanks to the highly regulated Islamic banking industry, coercive pressure is an inevitable byproduct. The Shariah review function in IBs generally exists within the IFI ecosystem, where it receives the regular support of professional training. Therefore, the current study aims to explain the institutionalisation of the Shariah review function merely as a ceremonial aspect of the formal structure of the monitoring mechanism. The study also intends to clarify how the legitimacy of Shariah review practices is essentially determined by the parties or actors involved within the control functions.

Shariah review practices may differ due to the diversity of operational characteristics of respective IBs, especially in terms of their specific nature and settings. In fact, differences in settings and characteristics are normally observed across full-fledged, foreign, or subsidiary IBs. Thus, the Shariah review function at present works in a context with varying needs and preferences, given the specific characteristics of IBs. In contrast, the use of alternative theories such as resource dependency theory may offer alternate perspectives on how IFIs navigate resource constraints given the limited pool of qualified resources. Stakeholder theory, meanwhile, addresses the diverse expectations between investors, regulators, and customers. Largely, institutional theory is the most relevant to this study as it focuses on convergence of practices in IFIs which are determined by isomorphic pressures, despite the industry being highly regulated.

2.2 Shariah review as an internal control function

An internal control system positively impacts corporate sustainability as it improves operational effectiveness and efficiency, which in turn ensures adherence to legal and regulatory requirements, enhances the reliability of reports and disclosures, and enables stakeholders to evaluate a firm's sustainability (Harasheh & Provasi, 2023). Minaryanti and Mihajat (2024) employ three variables—internal Shariah compliance, Shariah risk, and internal Shariah audit—to gauge how well Shariah principles are being used in IBs. Compliance of IBs to Shariah principles is crucial as it differentiates their operations from their conventional counterparts (Ab Ghani et al., 2019). Hanefah et al. (2020) show that poor internal control systems in IBs significantly contribute towards Shariah non-compliance.

As noted above, the SGPD (2019) outlines three main internal control functions, namely Shariah audit, Shariah risk management, and Shariah review. The Shariah audit refers to periodical assessments of operational and compliance audits. It covers a comprehensive review of both financial and non-financial information within IBs, aiming to confirm Shariah compliance (Ab Ghani et al., 2019). This function reports directly to the audit committee and board of directors. Shariah risk management, meanwhile, manages risk exposure and mitigation in IBs. Ariffin (2022) highlights that Shariah non-compliance risks are similar to other risks, and it is essential to manage the risk exposure involved and to develop a robust risk management framework. This function reports directly to the board of directors' risk management committee. The third internal control function, Shariah review, mainly performs continuous and regular Shariah compliance assessments of the operations, activities, and products offered by IBs. The final report of the Shariah review findings is approved by the Shariah committee. However, little is known on the coordination between these three control functions.

The governance system in IBs is more complex than those found in conventional banks (Karbhari et al., 2020). IBs must ensure that their Shariah review functions work effectively to enhance public confidence in their operations and products (Alam et al., 2021). This is because any non-compliance of Shariah principles by IBs would diminish trust, as well as incur costly fines and penalties from the authorities (Omar & Hassan, 2019). A Shariah review function is crucial in the continuous assessments of Shariah compliance once the implementation of Shariah products and procedures by the business unit is underway. It is clearly stated in the SGPD (2019) that as one of the internal control functions, the Shariah review assists the Shariah committee in performing oversight duties. Hanefah et al. (2020) stipulates that an absence of effective internal control systems in IBs may lead to a higher risk of Shariah non-compliance. Hence, the establishment of a Shariah review function is crucial to reduce such risks (Algabry et al., 2020).

2.3 Shariah review guidelines

Previous studies examine Shariah review from the perspective of an oversight function based on agency theory. However, few explore how Shariah review practices are implemented in IBs. Similarly, there is an absence of a comprehensive methodology framework on Shariah review practices that explains the proper conduct of Shariah review practices by officers. The absence of such a framework may cause inconsistencies in practice, affecting the quality and comprehensiveness of Shariah review outputs to Shariah committees, specifically in reporting findings of Shariah non-compliance. Indeed, without a specific Shariah review guideline or framework issued by relevant authorities (Besar et al., 2009), it may lead to various approaches in the actual work performance of the Shariah review function in IBs.

Since there is a dearth of research on practical realities in relation to the conduct of the Shariah review function by officers in actual practice, it is timely to explore the contemporary practices of the Shariah review and understand the common methodology adopted by most Shariah review functions in IBs in Malaysia. Given that it is a highly regulated industry, standardised practices should improve the comprehension and comparability of Shariah review reports. Alam et al. (2022) and Khatib et al. (2022) argue that the current guidelines are not comprehensive, as they only cover certain areas of IB operations, leading to the birth of various practices. A uniformed guideline is therefore crucial to ensure that consistency of practice is achieved in IBs as expected by regulators (Derigs & Marzban, 2008).

2.4 *Timeliness in Shariah review reporting*

The establishment of a Shariah review function therefore critical to help minimise risks of Shariah non-compliance (Algabry et al., 2020). Despite the greater complexity of the governance system of IBs than their conventional counterparts (Karbhari et al., 2020), there is a need to ensure that the Shariah review function works effectively to enhance the public's confidence in the banks' overall operations and products (Alam et al., 2021).

However, the SGPD (2019) does not specify the process of a Shariah review function, starting from the planning to the reporting phase. It is outlined in the SGPD (2019) that the minimum reporting responsibility of the Shariah review function is to report regularly to the board of directors, Shariah committee, and senior management on issues of Shariah non-compliance. This indicates that there are no standardised timelines for Shariah review officers to adhere to in completing their tasks. Though Ali et al. (2019) reveal that a common timeline to complete one review is two months, this still depends on the risks of the area under review. In fact, most IBs implement a modified Shariah framework for staffing, systems, and processes to ensure Shariah compliance (Aziz et al., 2019).

2.5 *Leveraging on other control function*

In the SGPD, the Shariah review function is positioned vertically on the same level as other governance functions, like the Shariah audit and Shariah risk management. However, unlike the other functions, the ultimate reporting line of the Shariah review function is to the Shariah committee. A final decision on the findings of the Shariah review is highly dependent on the Shariah committee. In line with this, Masruki et al. (2020) underscore the importance of competency for a Shariah committee, as they are the ultimate overseer of the Shariah review function.

Regarding governance mechanisms, banks safeguard their operations with the establishment of three lines of defence model (Bantleon et al., 2021). This model is crucial to ensure the effectiveness of the governance mechanism within an organisation. Based on the reporting structure of SGPD, the Shariah review function represents the second line of defence in IBs. Any form of Shariah non-compliance that might be overlooked by the Shariah review function can be detected by the third line of defence, which is the Shariah audit. Coordination between the monitoring functions of IBs minimises the chance of fraud and error within banks (Johari, 2022). At the same time, communications between both functions also lead to knowledge exchange that helps increase their efficiency in review and audit exercises (Nguyen, 2020).

Furthermore, the business department of IBs is involved in the reporting Shariah findings, whether directly or indirectly, despite the SGPD noting the

presence of a direct reporting line between the Shariah review function and the Shariah committee. This argument is proven by Embi and Shafii (2018), who note that there is a higher percentage of discussions on Shariah findings between the Shariah review function and the business department. Yasoa et al. (2020) indicate that this practice is acceptable, while Alam et al. (2022) is of the view that this represents a lack of independence by the Shariah review function since they need to highlight the Shariah findings to the business department.

3. Methodology

The current study aims to explore how Shariah review practices are implemented by IB officers. A qualitative research approach is therefore relevant in this context, in line with Yin (2009), who states that interviews conducted using a qualitative method can gather deeper and richer information. Hence, the study adopts a semi-structured interview method to solicit views and opinions from relevant participants. Six participants from five different IBs were interviewed to explore contemporary Shariah review practices in order to make preliminary assessments of the practical reality of Shariah review practices. The participants consist of five participants from four domestic IBs (including one full-fledged IB and three IB subsidiaries), and one foreign IB subsidiary. Of these, two interviewees are from the executive level and four from the managerial level. The participants were selected as they are the most appropriate to answer the research question of the Shariah review practices among the diverse categories of IBs in Malaysia.

The participants involved directly in the implementation of the Shariah review practices hence provide a wide span of exposure from executive to managerial perspectives. The various positions represented by the participants are crucial in explaining the views and practices that exist based on the different levels of authority, job autonomy, and various working experiences in different IBs. This shows that the selected participants are the most appropriate respondents for the study to gather first-hand information pertaining to actual practices and issues they encounter in implementing Shariah review practices in their respective IBs.

Data were obtained through semi-structured interviews. The interviewees of the study comprised heads of the Shariah review function or the compliance division, and practitioners directly involve in performing Shariah review practices from various categories of IBs. The inclusivity of all categories is aimed to ensure the richness of the study's findings by providing valuable insights (Creswell & Poth, 2018). Boddy (2016) emphasises that the number of interviewees for a qualitative study is open for debate, as there are no specific guidelines on how to determine the appropriate number. Thus, the inclusion of diverse participants ensures the

study reflects diversity in organisational structures, regulatory environments, and practices within IBs. Insights from foreign IBs highlight similarities and differences between local and global standards. Moreover, a small expert-focused sample is appropriate where the depth and insight outweigh the breadth and data saturation principle, assuming sufficient information has been gathered. For this study, semi-structured interviews were conducted until data redundancy had occurred and data saturation was reached in subsequent interviews.

The interviews were not conducted with strict formality to enhance the openness of the sessions. As stipulated in Table 1, the interviews ranged between one hour and one hour and 20 minutes, and were recorded using an online meeting platform with the consent of the participants. Consent on confidentiality and anonymity was obtained from all participants. Each interview was then transcribed upon completion of the sessions. The qualitative data gathered from the interviews were subsequently validated through a series of procedures, with data collection and data analysis carried out simultaneously, as suggested by Creswell and Creswell (2017). The semi-structured interview questions were developed based on the literature review and tested with a small group of non-participants. The feedback obtained were used to align the questions with research objectives and research questions. The interview protocol was strengthened by doing a pilot study to identify flaws and allow necessary modification (Abdul Majid et al., 2017).

First, the participants were coded for confidentiality and anonymity, as presented in Table 1, with the background of participants. Then, the recorded interviews were transcribed, and their transcriptions were then read and reread to identify common and emerging themes. The themes were then extracted, tabulated, and analysed manually. Multiple coders self-analysed the transcriptions systematically to ensure consistent coding process and to reduce the risk of individual bias. Establishment of clear protocol resolved disagreements and bias through consensus discussions among coders as to improve reliability. The data were analysed based on within-case and cross-case approaches, and the results were summarised based on a pattern code (Hubberman & Miles, 1994) derived from prior studies, guidelines, and emerging themes during the interviews. This method involves reorganisation and condensation of a vast array of initial information into readable output. Subsequently, the three significant themes and patterns are categorised in accordance with the interview questions, which are regarding the absence of guideline or framework, timeliness, and leverage or coordinate work reliance with another department.

Table 1. Background of Participants

Interviewee code	Years of experience	Professional qualification	Shariah background	Type of position	Type of IB	Interview length
IV1	> 10 years	Yes	Yes	Manager	Domestic FFIB	1 hour 20 minutes
IV2	> 10 years	Yes	Yes	Manager	Domestic IBS	1 hour 15 minutes
IV3	< 5 years	Yes	Yes	Executive	Domestic IBS	1 hour
IV4	< 5 years	Yes	Yes	Executive	Domestic IBS	1 hour
IV5	> 10 years	Yes	Yes	Manager	Foreign IBS	1 hour 5 minutes
IV6	> 5 <10 years	Yes	Yes	Middle manager	Domestic IBS	1 hour 15 minutes

Notes: FFIB: full-fledged IB, IBS: IB subsidiaries

4. Findings and Discussion

An exploratory assessment of Shariah review practices in different IBs was carried out to understand the actual practices and their related issues. The study finds that the results and insights gathered from the interviews were aligned with the requirements stipulated in the SGPD (2019), evidence from prior studies, and the emerging themes of the interviews. Hence, three significant themes are identified and discussed in the following subsections: (1) absence of a Shariah review framework; (2) timeliness in reporting Shariah review findings; and (3) leverage or coordinate. Based on the interviews' insights, several implications of the study and recommendations for future studies are then summarised in the conclusion.

4.1 Absence of Shariah review framework

Findings of the study revealed that BNM's current SGPD merely sets minimum requirements on Shariah review practices that should be followed by IBs. The responsibility of BNM is in line with the institutional theory shown by the structure of Shariah governance of IBs in Malaysia. All IBs in Malaysia adhere to the rules and guidelines provided by BNM. As the central bank has the ultimate power to control and monitor all IBs, the isomorphism that suit this case is coercive. The coercive isomorphism is clearly becoming the main isomorphic pressure that influences the presence of the Shariah review function for all IBs. However, there is an absence of a specific framework issued by the regulator on the precise conduct of Shariah

review practices. This is mentioned by IV5 and IV6:

We refer to many guidelines because there are no specific guidelines currently available in the market. We have a lack of guidelines or standards for Shariah reviews. We adopt many guidelines plus best practices. (IV5, Bank E)

Guidelines like SGPD are the basic requirements that banks should follow. But, how to do the tasks were not explained in SGPD. (IV6, Bank B)

The finding is supported by Alam et al. (2022) and Khatib et al. (2022), who find that the available Shariah governance frameworks are not comprehensive enough in explaining standard procedures. According to other respondents, the absence of detailed procedures on the conduct of Shariah review practices forced IBs to internally develop their own methodologies. It was found that the internally developed methodologies by the respective IBs explain detailed procedures on the conduct of Shariah review practices to be followed by staff and was commonly practiced. Most importantly, it designed the procedures of the Shariah review to ensure that the objectives are achieved. These observations are explained by IV1, IV3, and IV4:

We don't have detailed guidelines like the auditing standards. So, it is based on the bank's own initiatives. We call it a methodology. (IV1, Bank A)

We are not really relying directly on available standards like SGPD from BNM because the guidelines issued are too general. We need to rely on our best practices as discussed and instructed internally. (IV3, Bank C)

We are mainly referring to the internal guidelines as the internal guidelines have already been established by the Shariah department. The internal guidelines are based on few standards available in the market. This is because the available guidelines are not comprehensive. (IV4, Bank D)

The findings also outline that the guidelines in use by most IBs are still very general and cannot be used as the main reference by other IBs. There is a need for a common standard to be used as a guideline due to the specific context and different nature of the IBs themselves. For instance, the methodology used in foreign IBs may not be applicable to local IBs. As IV1 states:

We can't adopt 100 percent the methodology of other banks as our business nature is different. So mostly, we will adopt the methodology from the compliance unit and suits it with our Shariah review objectives. (IV1, Bank A)

The absence of a framework places little coercive pressure on IBs, but there are mimetic pressures when the framework is developed internally. In

addition, the study also finds that Shariah review practitioners hop to other IBs and share some practices with each other during trainings. This has led to greater harmonisation of practices through the IBs in the industry. Besides that, the different bases used for internally developed methodologies have resulted in a variation of approaches and conducts of Shariah review practices. Studies by Algabry et al. (2020) and Alam et al. (2021) state that the self-developed methodology in IBs is caused by differences in bank policies, understanding of *madhhab* (school of thought), and inconsistent practices of Shariah governance among IBs. Moreover, the conferences and meetings involving Shariah officers and managers from Malaysia IBs have become a platform to share and exchange best practices. It proves the presence of mimetic isomorphic pressure in the Shariah review function among IBs in Malaysia.

Therefore, as asserted by Derigs and Marzban (2008), the presence of a uniformed, understandable, and standardised guideline on the conduct of Shariah review would enhance the credibility and consistency of IB practices. In the presence of a standardised Shariah review guideline, a more comparable and standardised Shariah review findings report can thus be produced. Without this, approaches towards Shariah compliance becomes varied, and Shariah review teams tend to work in silos within their organisations. Sometimes, overlapping responsibilities between Shariah review and Shariah audit functions often result in duplication of efforts or confusion in accountability. Fragmented communication, inconsistencies, and redundancy between control functions consumes more time and resources, which may cause delays in reporting by the Shariah compliance teams.

4.2 Timeliness in reporting Shariah review's findings

Timeliness in reporting refers to the time taken for the overall process of Shariah review practices, from the planning to reporting stages. At present, many of the respondents assert that there is no stipulated guideline stating the time required to complete Shariah review practices in the absence of a Shariah review framework. In practice, determining the timeline of Shariah review practices largely relies on the scope and complexity of the tasks. This is stipulated by IV2 and IV4:

The review can be around one to two months. It depends on the scope or work done by the officer. (IV2, Bank B)

For a Shariah review officer, we have on average four to six weeks to complete our findings. (IV4, Bank D)

They further state that the expected maximum timeline for Shariah officers to complete their review tasks is two months. The finding is supported by Ali

et al. (2019), who find that Shariah review officers often complete the review tasks in two months, involving two Shariah review officers for every review assignment. However, the complexity and riskiness of the areas under review naturally require a much longer period. The notion is supported by IV5 who responded:

It depends on the review scoping. Higher risk areas will need more time. (IV5, Bank E)

Upon completion of the review process, the findings are discussed among team members, and any Shariah non-compliance issues are brought up to the business department or management for rectification. The majority of the respondents commented that a specific timeline should be allocated for the business department or management to return the rectifications.

Normally two months are adequate for the management to do an appropriate action. Then, they will report back to us. (IV1, Bank A)

When we find (a case of) Shariah non-compliance, we will ask the management to rectify it. For minor issues, we will ask them to amend it in a short period of time, so we will not put it as a finding. But, for major findings, the management needs to amend them after the Shariah committee meeting. The deadline depends on the issues. It can be months. (IV6, Bank B)

There is still a time that the management needs to rectify the findings because we need to report significant non-compliance issues to BNM. So, we will depend on the deadline given by BNM. (IV3, Bank C)

The management needs to revise the Shariah non-compliance (issues) within the deadline given. The deadline depends on how serious the issue is. For sure, more serious issues need more time to be treated. (IV4, Bank D)

As highlighted above, a specific timeline needs to be observed by the management in providing rectifications, as any Shariah non-compliance issues are reported directly to BNM. Indeed, any major, complicated, and difficult issues would require a longer time to be rectified prior to being reported. On the other hand, the management seems to be responding faster in providing rectifications for findings classified as major issues, as highlighted by IV3.

For major and significant issues, normally, the management will investigate them faster. (IV3, Bank C)

Timeliness in reverting rectifications on major issues is crucial as it impacts operations, products, and activities classified as Shariah non-compliance. In fact, IV1 also mentions that stricter compliance procedures are a result of deadline pressure and approval in reverting the rectifications by the top

management and the management's governance team.

If let's say they exceeded the target date, they need to get a CEO approval for the extension of (the) target date for the first time. For the second time, if they required extensions, the board's approval is required. (IV1, Bank A)

Rectifications from the management would come in the form of corrective or preventive actions. Otherwise, the management is obliged to explain the necessary remedial actions to the Shariah review team to prevent the recurrence of Shariah non-compliance issues in the future.

The management will be given time to rectify the issue either with corrective or preventive action. (IV1, Bank A)

In short, observation on timeliness in performing and reporting Shariah reviews' findings as well as in reverting rectifications for Shariah non-compliance is crucial, as some of the issues may indirectly affect business performance. Rectifications often include the provision of corrective and preventive measures to ensure that remedial actions are in place. Delay in the process flow would hinder timely submission of the report on Shariah non-compliance issues to BNM. As such, deadlines set by BNM underline the coercive pressure in enhancing control over the management of Shariah non-compliance issues. The timeline given is highly dependent on the deadline given by the main regulator. This is because the findings of Shariah non-compliance should be reported to BNM as soon as they are approved by the Shariah committee. In order to achieve effective governance practice, those charged with governance should assist in exercising stricter oversight duties in monitoring the conduct of Shariah review procedures and rectification processes.

4.3 Leverage or coordinate

According to BNM (2019), Shariah review involves regular assessments on the compliance of operations, businesses, and activities of IFIs with Shariah requirements. Indeed, it is possible that the scope of works for a Shariah review function to overlap with other control functions. Therefore, the current study aims to examine the possibilities for the Shariah review function to coordinate or leverage on other departments or control functions in IBs. In addition, the study also intends to further explore the possibilities of the Shariah review function relying fully or partially on other control functions. Rationally, given the possibilities are achieved, the Shariah review function should be able to manage resources and mitigate risks more efficiently.

Interestingly, there are findings in relation to work coordination by the Shariah review function with other control functions are found to be implemented by some IBs. Indeed, the findings indicate that the coordination of the function depends on the area and its level of risk, as well as how its resources are efficiently managed. IV1, IV4, and IV5 note that:

We are not relying on other departments in terms of findings. (Shariah) Audit will have their own assessment and (Shariah) review will have our own assessment. This is because when we conclude that this area is high-risk, we would review the area no matter if other functions already did an assessment on the same area. (IV1, Bank A)

We are not really depending on each other. We have our own scope, and internal audit has their own scope. If we scoped a high-risk area which is also being scoped as high-risk by them, we both will proceed for an assessment on the same area. (IV4, Bank D)

We have only four team members in the Shariah review department, including myself. If all of us are needed to cover all Shariah review-related job scopes, it is (simply) not possible. We are always coordinating with other departments' officers to ensure efficiency. (IV5, Bank E)

It is apparent that there is no coordination between the Shariah review function with other control functions for Bank A and Bank D. In fact, each function performs its work independently, assessing identified high-risk areas, although the (overlapped) scope has been reviewed by other functions.

Meanwhile, the Shariah review function of Bank E was found to be the only one coordinating with other departments as one of its mechanisms to efficiently manage its resources. The study believes that coordination between the different Shariah functions would encourage a more efficient use of resources given similar scopes are covered by other functions. This could overcome the shortage of staff issue; in turn, the coordination with other functions is mostly covered the low-risk areas. Notably, subsequent findings are supported by prior studies that outline the importance of inter-departmental communications and exchange of information to minimise the chance of fraud or error, specifically on matters of Shariah non-compliance (Johari, 2022; Nguyen, 2020). By addressing these coordination challenges, IBs can enhance the efficiency of resources management, reliability of their Shariah review practices, as well as ensuring timely and consistent reporting.

5. Conclusion

The present study examines the current practices of a Shariah review function across various settings of IBs which include full-fledged IBs, as well as foreign and local subsidiaries of IBs. Notably, variations in governance processes can undermine uniformity in practices and introduce systemic risks. This fragmentation could potentially confuse stakeholders and

jeopardise public trust and confidence in IFIs. Thus, to gather views from subject matter experts, the respondents of the study are mainly represented by Shariah review officers of diverse backgrounds and positions including executive and managerial positions. The findings outline the absence of a comprehensive Shariah review framework, which has resulted in non-uniformity of Shariah review practices despite being in a highly regulated industry. The findings further highlight that internally developed modules are being applied by the existing Shariah review function in respective IBs, resulting in inconsistencies in Shariah review practices. This, in turn, produces Shariah review reports that are not standardised and comparable to each other.

Without the presence of comprehensive framework on Shariah compliance, approaches towards Shariah compliance are varied and Shariah review teams tend to work in silos. Moreover, timeliness in reporting the findings of Shariah reviews largely relies on the management's responsiveness in reverting rectifications on any Shariah non-compliance issues. In fact, the study finds that close monitoring by those charged with governance would assist in complying with the strict timeline. Indeed, timely reporting is important as it improves the information value of the reports. On another note, the findings also reveal that coordination and reliance on other Shariah control functions would minimise the issues of overlapping work scopes and shortage of staff, though this was found not to be practiced by all IBs.

With regards to its practical implications, insights from this study will assist in outlining best practices based on the similarities and differences of Shariah review practices found across IBs in Malaysia. In addition, it would serve as a future reference for relevant regulators and authorities in improving related regulatory requirements. Regulators can facilitate knowledge sharing forums in exchanging best practices and strengthen the capacity building initiatives through training and certification programs. Periodic reviews would ensure the relevance of the Shariah review practices in adapting to market dynamics. Eventually, the absence of a Shariah review framework globally rooted in differences of Shariah interpretation across jurisdictions and complexity in balancing diverse stakeholders' expectations. Indeed, foreign IBs often deal with diverse Shariah interpretations particularly in catering to international markets and global practices. Whereas domestic IB in Malaysia mainly adhere to BNM guidelines and local requirements. Malaysia as an Islamic financial hub could serve as a model for others to leverage. In line with the mimetic pressures, establishment of regional or global working groups could harmonise differences in interpretation and Shariah review practices based on the insights gathered from the study. Regulators can facilitate knowledge sharing forums in exchanging best practices and strengthen the capacity building

initiatives through training and certification programs. Periodic reviews would ensure the relevance of the Shariah review practices in adapting to market dynamics.

Theoretically, this study contributes to the subject matter through its application of institutional theory, while prior studies utilise agency theory in examining the role of the Shariah review function as one of the internal monitoring mechanisms in a Shariah governance framework. The findings indicate that normative pressure outlines the presence of a Shariah review function. However, mimetic pressures, thanks to the various backgrounds and movements of Shariah officers and Shariah committees from one IB to another, assist in the development process of an internally developed guideline of Shariah review practices within respective IBs. It is believed that proper harmonisation of differences in the Shariah practices could further enhance the quality of Shariah review reporting into a more standardised and comparable manner. In addition, from the compliance and risk management perspective, lack of standardised practices complicates monitoring Shariah compliance, which in turn leads to potential breaches and unrecognised Shariah non-compliance risks which may escalate reputational and financial risks. In short, the overall control and monitoring mechanisms within IBs are aimed to minimise Shariah non-compliance and strengthen the reputation of the IBs at large.

The present study contains several limitations. For example, the study only focuses on Shariah review practices in the context of IBs as part of IFIs as a whole. Institutional theory has its limitations, as its analytical focus is primarily on the behaviour of IBs, rather than on the individual actors within IBs. Future research could integrate stakeholder theory and resource dependency theory by offering broader lens to analyse the interplay of resources, stakeholders' pressures, and institutional structures. These theories deal with the scarcity of resources and inconsistencies in expectations among stakeholders. The application of institutional theory is more prevalent in studying the coercive, mimetic, and normative pressures within this context of this study, as it aims to examine the inconsistencies in Shariah review practices.

In addition, future studies can examine Shariah review practices in other parts of IFIs, such as takaful institutions. Comparisons on implementation aspects within different settings could outline best practices for the Shariah review. In a similar vein, the findings of current study have limited applicability in international contexts mainly due to differences of regulatory frameworks (such as SGPD and AAOIFI) that govern IFIs across different jurisdictions. Moreover, variation in *ijtihad* (independent reasoning) among scholars across different jurisdictions has further contribute to a diversity of practices. Thus, future studies could explore how specific regulatory frameworks and *ijtihad* approaches shape Shariah review practices. Finally,

Shariah review could expand its scope into other aspects, including risk management, ethics, and sustainability. A holistic assessment approach through the integration of risk perspectives, ethical principles, and socially responsible practices in the conduct of Shariah reviews could further enhance its contributions.

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