



**Supplementary Information**  
**Appendix SG-1**  
**Independent Assurance Report and**  
**Management's Report on**  
**Control Procedures Relating to**  
**Shari'a Compliance and Governance**  
**Structure**



**XYZ BANK  
INDEPENDENT ASSURANCE REPORT  
AND  
MANAGEMENT'S REPORT ON  
CONTROLPROCEDURES RELATING TO  
SHARI'A COMPLIANCE AND GOVERNANCE STRUCTURE  
31 DECEMBER 20XX**



- 1. INDEPENDENT ASSURANCE REPORT**
- 2. MANAGEMENT'S REPORT ON CONTROL PROCEDURES RELATING TO SHARI'A COMPLIANCE AND GOVERNANCE STRUCTURE**
- 3. CONTROL PROCEDURES RELATING TO SHARI'A COMPLIANCE AND GOVERNANCE STRUCTURE**
  - 3.1. Overview
  - 3.2. Shari'a Governance
    - 3.2.1 Structure for Shari'a coordination and implementation and oversight
    - 3.2.2 Shari'a framework
  - 3.3. Control environment
  - 3.4. Transaction level controls
  - 3.5. Product specific controls
  - 3.6. Investment level controls
  - 3.7. Hiring process, employee training and awareness
  - 3.8. Other controls
- 4. CONTROL OBJECTIVES**
  - 4.1. Overall control objective
  - 4.2. Specific control objectives



**1. INDEPENDENT ASSURANCE REPORT TO THE BOARD OF DIRECTORS OF XYZ BANK ON CONTROL PROCEDURES RELATING TO SHARI'A COMPLIANCE AND GOVERNANCE STRUCTURE**

We have been engaged by the Board of directors of XYZ Bank (the 'Bank') to perform an independent reasonable assurance engagement on the management's report on control procedures relating to Shari'a compliance and governance structure and management's assertion on the design and operating effectiveness of these controls (together the "Management Shari'a compliance and governance report"), as set out on pages X to XX, of the Bank for the year ended 31 December 20XX.

***Management's responsibility***

The Bank's management is responsible to provide an assertion about the fairness of the presentation of the Management Shari'a compliance and governance report, which is aimed to ascertain the suitability of the design and operating effectiveness of controls to achieve the related control objectives stated in the Management Shari'a compliance and governance report, and to ensure the Bank's compliance with relevant provisions of Volume 2 of the Rulebook ('Rulebook') issued by the Central Bank of Bahrain and the guidelines and directives issued by its Shari'a Supervisory Board ('SSB'). The Management of the Bank is responsible to ensure that the Bank's activities comply with Islamic Shari'a Rules and Principles as determined by the SSB as set out in Accounting and Auditing Standards for Islamic Financial Institutions 1 and 2. Management is also responsible for the prevention and detection of fraud, error and non-compliance with the laws and regulations applicable to the activities of the Bank.

***Practitioner's responsibility***

Our responsibility is to express an independent conclusion on the Shari'a compliance and governance report and on the design and operating effectiveness of these controls, based on our procedures. We conducted our engagement in accordance with International Standard on Assurance Engagements 3000, *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information*, issued by the International Auditing and Assurance Standards Board. This standard requires that we comply with ethical requirements and plan and perform procedures to obtain reasonable assurance about whether, in all material respects, the Shari'a compliance and governance report is fairly presented and the controls are suitably designed and operating effectively. The engagement is also in compliance with the applicable AAOIFI standards. An assurance engagement to report on the Shari'a compliance and governance report, design and operating effectiveness of the controls involves performing procedures to obtain evidence about the controls stated therein, and the design and operating effectiveness of these controls.

The procedures selected depend on the practitioners' judgment including the assessment that the Management Shari'a compliance and governance report is fairly presented, and that controls are suitably designed and operating effectively. An assurance engagement of this type also includes evaluating the overall presentation of the Management Shari'a compliance and governance report, and the suitability of the criteria described therein.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.



**1. INDEPENDENT ASSURANCE REPORT TO THE BOARD OF DIRECTORS OF XYZ BANK ON CONTROL PROCEDURES RELATING TO SHARI'A COMPLIANCE AND GOVERNANCE STRUCTURE (continued)**

***Limitation of Shari'a Compliance and Governance Report***

The Management Shari'a compliance and governance report is prepared to meet the needs of a range of users and may not, therefore, include every aspect of the control procedures that each user may consider important in their own particular environment.

Our procedures regarding adequacy of systems and controls relating to the Bank's compliance with the SSB guidelines and directives are subject to inherent limitations and, accordingly, errors or irregularities may occur and not be detected. Furthermore, such procedures may not be relied upon as evidence of the effectiveness of the systems and controls against fraudulent collusion, especially on the part of those holding positions of authority or trust.

The conclusion relates only to the year ended 31 December 20XX. The conclusion does not provide assurance in relation to any future periods as changes to systems or controls may alter the validity of our conclusion.

***Work performed***

Our work mainly included:

- 1) Discussion with the Bank's management on the Shari'a compliance and governance structure of the Bank;
- 2) Review of documentation and systems established by the Bank to develop Shari'a compliance and governance framework, in order to develop an understanding of the Shari'a compliance and governance framework and an understanding of the related internal controls. This includes:
  - a. Review of minutes of meetings of Shari'a Supervisory Board and Board of Directors;
  - b. Review of policies and procedures;
  - c. Review of selected job descriptions;
  - d. Review of reports prepared by the Shari'a Supervisory Board;
  - e. Review of reports prepared by the Internal Shari'a Auditor;
  - f. Any other reports relevant for the purpose.
- 3) Assessing the risks that Management's assertion on the description of controls may be materially misstated;
- 4) Performing further procedures on the identified risks, as deemed appropriate, using a combination of inspection, observation, confirmation and inquiry;
- 5) On a sample basis testing of transaction level controls listed in the Management Shari'a compliance and governance report;
- 6) On a sample basis testing of product specific controls listed in the Management Shari'a compliance and governance report;
- 7) Review of pool management and profit distribution system of the Bank;
- 8) Checking of compliance with employee training procedures of the Bank; and
- 9) On a sample basis testing of other controls listed in the Shari'a compliance and governance report.

The scope of our work is also in compliance with 'scope of the auditor work' as outlined in AAOIFI Auditing Standard No. 4 regarding 'Testing for compliance with Shari'a Rules and Principles by an External Auditor'.



**1. INDEPENDENT ASSURANCE REPORT TO THE BOARD OF DIRECTORS OF XYZ BANK ON CONTROL PROCEDURES RELATING TO SHARI'A COMPLIANCE AND GOVERNANCE STRUCTURE (continued)**

***Conclusion***

In our opinion, the management's assertion that internal controls relating to Shari'a compliance and governance and the design and operating effectiveness of those controls is effective, in all material respects, based on criteria laid down in the Management Shari'a compliance and governance report, is fairly stated.

***Intended users and purpose***

In accordance with the terms of our engagement, this independent reasonable assurance report on the Bank's Shari'a compliance and governance framework and its compliance with the relevant provisions of the CBB Rulebook and guidelines and directives issued by its SSB, has been prepared for the Board of Directors of the Bank and for the Central Bank of Bahrain, solely to assist the management to meet the requirement of clause XXXX of the Rulebook and circular no. XXXXX dated XXXXX issued by the Central Bank of Bahrain, and for no other purpose or in any other context. This report should not be regarded as suitable to be used or relied upon by any third party, for any purpose or in any context. Any third party that obtains access to this report or a copy thereof and chooses to rely on this report (or any part thereof) does so at their own risk; and we accept no responsibility or liability to any third party. Our report is not to be copied, referred to or disclosed, in whole or in part, to any third party, other than the Central Bank of Bahrain, without our prior written consent.

XX XXX 20XX



## **2. Management's Report on control procedures relating to Shari'a compliance and governance structure**

XYZ Bank (the "Bank") was established in the Kingdom of Bahrain to carry out banking and other financial activities in accordance with Islamic Shari'a Rules and Principles. The Bank operates under an Islamic banking license granted by the Central Bank of Bahrain ("the CBB") on [Date]. The management of the Bank, under authorization from the Board of Directors ("BoD") of the Bank, is responsible for establishing and maintaining adequate internal controls to ensure Shari'a compliance at all times. These controls are designed and implemented under the supervision of the Shari'a Supervisory Board ("SSB") to provide assurance regarding compliance with respect to Islamic Shari'a Rules and Principles.

As per objectives listed in section 4, the following are the broad categories in which the above mentioned control procedures are designed:

- a. Shari'a Governance
  - Structure for Shari'a coordination and implementation and oversight
  - Shari'a framework
- b. Control environment
- c. Transaction level controls
- d. Product specific controls
- e. Investment level controls
- f. Hiring process, employee training and awareness
- g. Other controls

Details of each category are provided in sections 3.2. to 3.8.

Based on the control objectives listed in section 4, we believe that:

- a) The control procedures listed in section 3.2 to 3.8 fairly present the Bank's controls designed and implemented throughout the period from 1 January 20XX to 31 December 20XX;
- b) The control procedures listed in section 3.2 to 3.8 were suitably designed throughout the period from 1 January 20XX to 31 December 20XX; and
- c) The controls procedures listed in section 3.2 to 3.8 operated effectively throughout the period from 1 January 20XX to 31 December 20XX.

Approved by the management of the Bank on \_\_\_\_\_

**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

### 3. Control procedures relating to Shari'a compliance and governance structure

#### 3.1 Overview

This report provides information about the control procedures (points 3.2 to 3.8) which are designed, implemented and maintained by the Bank to achieve the Shari'a compliance objectives (point 4) during the period from 1 January 20XX to 31 December 20XX. These control policies and procedures are regularly reviewed by the management, and accordingly may, from time to time, be modified with a view to achieving the control objectives. No representation is made to any parties that future control policies and procedures will reflect current practice.

All control systems have inherent limitations and cannot guarantee the totally effective operation of systems, nor the total completeness and accuracy of the records. Also, they cannot necessarily prevent fraudulent collusion.

#### 3.2 Shari'a Governance

##### 3.2.1 Structure for Shari'a coordination and implementation and oversight

- a) Articles of Association permit the Bank to carry out all commercial and investment banking business activities.
- b) The Shari'a governance framework of the Bank is in line with CBB's regulations, resolutions and directives and market best practices. The Shari'a governance framework of the Bank includes:
  - i. Shari'ah Supervisory Board (SSB);
  - ii. Internal Shari'a coordination and implementation Function;
  - iii. Internal Shari'a Audit Function; and
  - iv. Independent External Shari'a Compliance Audit.
- c) The SSB of the Bank comprises of at least three (3) scholars specialized in Fiqh Al Mu'amalat. These members have extensive experience in the field of Islamic banking and finance and meet the fit & proper criteria specified by the CBB. The structure of the SSB is as follows:

S. No.	Name of the Scholar	Qualification	Position in the board	Nationality
1	[Name of scholar 1]	[Qualification]	[Position]	[Country]
2	[Name of scholar 2]	[Qualification]	[Position]	[Country]
3	[Name of scholar 3]	[Qualification]	[Position]	[Country]

- d) The appointment of SSB members is formally documented by the Bank via a formal offer letter duly signed by the respective SSB member;
- e) The appointment of the SSB has been approved by the BoD of the Bank;



**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

- f) A charter for the SSB has been approved by the Board defining the scope of work for the SSB. The charter includes, at a minimum, the following:
- i. Purpose of the charter;
  - ii. Authorization of the charter;
  - iii. Membership of the SSB;
  - iv. Composition of the SSB;
  - v. Chairperson;
  - vi. Secretary;
  - vii. Possible cause/course of removal and replacement of a Member;
  - viii. Authority of the SSB;
  - ix. Responsibilities of the SSB;
  - x. Meetings;
  - xi. Voting and decisions;
  - xii. Amendments to the charter; and
  - xiii. Relationship with the BoD and Management of the Bank and its various departments.
- g) The roles and responsibilities of the SSB include the following:
- i. To supervise the Bank's operations and activities to ensure compliance with the Islamic Shari'a, and also monitor and review transactions to ensure full compliance with Shari'a rules and principles and SSB pronouncements;
  - ii. To ensure, with the cooperation of the independent external Shari'a compliance auditor (IESCA), the existence of an appropriate and functioning internal Shari'a control framework for compliance with Islamic Shari'a rules and principles;
  - iii. To approve the internal Shari'a audit annual plans;
  - iv. To notify the CBB in case of any failure by the Board of directors to effectively deal with any major Shari'a non-compliances of the Bank;
  - v. To approve all relevant documentation for new products and services, including contracts, agreements, marketing and promotional materials or other legal documentation used in the Bank's business transactions must be approved by the SSB;
  - vi. To review and approve the Bank's annual Zakah calculations on behalf of the shareholders;
  - vii. To put on record, in written form, any opinion that it gives on Shari'a-related issues;
  - viii. At least one SSB member be present at the AGM to respond to any enquiries from the Banks' shareholders during the discussion of the end of year financial results;
  - ix. To review the reports and observations of the Shari'a coordination and implementation function and internal Shari'a audit function and provide advice on such reports and observations;
  - x. To approve the profit/loss allocation to the investment account holders;
  - xi. To specify the means of disposal of earnings that have been realised from sources or by means prohibited by Shari'a rules and principles;

**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

- xii. To approve the appointment and removal of the Shari'a Officer and the head of internal Shari'a audit function and supervise their work;
- xiii. To develop its own operating procedures;
- xiv. To report administratively to the Board of directors;
- xv. To meet with the Board of directors of the Bank at least once a year to discuss issues of common interest. Such meeting must have a clear and specific agenda including the difficulties faced by both parties and ways to resolve them;
- xvi. To submit the SSB report, as part of the annual report, to the shareholders with a copy to the Board of directors and the CBB as per AAOIFI, on the Bank's Shari'a compliance, provided that the SSB report includes any non-compliance issues to the Shari'a rules and principles; and
- xvii. To ensure that information obtained in the course of their duties is kept confidential as per Article (117) of the CBB Law.

### **3.2.2 Shari'a framework**

- a) Shari'a Officer has been included in the organizational structure of the Bank;
- b) Shari'a coordination and implementation function is governed by the relevant policies and procedures prepared by the management, vetted by the SSB and approved by the BoD;
- c) Shari'a Officer is a full time employee of the Bank heading the Shari'a coordination and implementation function of the Bank, appointed by the Management in consultation with the SSB and the approval of the CBB. Shari'a Officer reports to the SSB independently from the Management;
- d) Shari'a Officer or the Head of Internal Shari'a Audit function has the added role of secretary to the SSB;
- e) Shari'a coordination and implementation function facilitates the Management in ensuring compliance with Shari'a (as manifested by the guidelines and Fatawa issued by the SSB) and Islamic banking stipulations of the CBB on a day to day basis in all its business activities, operations and transactions. This is achieved through the review and evaluation, before any product is offered to a customer, the contracts, agreements, fees, charges, policies, procedures, product manuals, product transaction structures, complete offering documentation including, promotion and marketing materials, advertisements and other communications to general public, memorandum and articles of association, and any other matter which can potentially impact the Shari'a compliance of the Bank or influence the perception of its Shari'a compliance. Subsequently, the Shari'a Officer submits his report, along with all the relevant documentation, to the SSB for their review and decision;
- f) Shari'a coordination and implementation function is involved in the testing and implementation of new products / services to ensure full Shari'a compliance under the relevant Fatawa. The function also assists the relevant staff in dealing with any Shari'a non-compliance issues arising from the implementation stage;

**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

- g) Shari'a Officer participates in and arranges, in conjunction with the Human Resources Training Department training the Bank's employees by holding regular meetings, courses and seminars. He also disseminates knowledge by publishing and distributing pamphlets, brochures, etc., explaining principles of Fiqh al-Muamalat in general, and in particular the Fatawa, guidelines and instructions issued by the SSB about the products and services offered by the Bank;
- h) The Bank has in place an Internal Shari'a Audit function reporting to the audit committee. The Head of the function is appointed by the management subject to the approval of the audit committee in consultation with the SSB and the approval of the CBB. The function is adequately resourced with proficient staff having the relevant qualification and experience;
- i) Internal Shari'a Audit function is governed by the relevant policies and procedures prepared by the management, vetted by the SSB and approved by the BoD;
- j) The Internal Shari'a Audit staff have no executive authority or responsibility for the activities they audit;
- k) The Head of Internal Shari'a Audit function is a full time employee of the Bank and is responsible for examining and evaluating the extent of the Bank's compliance with the following:
  - Shari'a principles;
  - The SSB's Fatawa, guidelines, pronouncements and instructions / recommendations;
  - Shari'a related regulations, resolutions and directives issued by the CBB;
  - Shari'a standards issued by AAOIFI; and
  - Shari'a related policies and procedures of the Bank.
- l) The Head of Internal Shari'a Audit function expresses his opinion to the SSB on the extent of Shari'a compliance of the Bank's operations through an actual audit of the business transactions;
- m) The Head of Internal Shari'a Audit function reviews and examines the adequacy and effectiveness of the Bank's Shari'a compliance system, covering all aspects of the Bank's business operations and activities;
- n) The Head of Internal Shari'a Audit function has direct and regular communications with all levels of Management, SSB, Audit Committee, Shari'a Officer and Independent External Shari'a Compliance Auditor. No scope limitation and/or restriction of access to documents, reports, etc. is placed on Internal Shari'a Audit staff;
- o) The Head of Internal Shari'a Audit function prepares periodic reports to the Audit Committee, based on the audit plan, for consideration and appropriate action. A copy of such reports is also presented to the SSB and the CEO;
- p) The Head of Internal Shari'a Audit function follows up to ascertain that appropriate action is taken on his reported findings and recommended corrective actions. In addition, any other recommendations relating to Shari'a matters made by the SSB, the Independent External Shari'a Compliance Auditor and/or the CBB are also followed up;
- q) In case of any difference of opinion between the Management and the Head of Internal Shari'a Audit function on matters relating to Shari'a interpretation, the issue is referred to and decided by the SSB;

**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

- r) The internal Shari'a audit plan is in place which is approved by the SSB on an annual basis;
- s) The internal Shari'a audit planning process includes, at a minimum, the following:
  - Developing an Internal Shari'a audit Program
  - Obtaining background information about the activities to be audited, such as locations, products/services, branches, divisions, etc.;
  - Establishing internal Shari'a audit objectives and scope of work;
  - Obtaining SSB Fatawa, guidelines, instructions, prior year internal and Independent External Shari'a Compliance Audit results, relevant correspondence including with the CBB;
  - Determining the resources necessary to perform internal Shari'a audit;
  - Communicating with all the individuals at the Bank who need to know about Internal Shari'a Audit; and
  - Performing, as appropriate, a survey to become familiar with activities, risks and controls to identify areas of Internal Shari'a Audit emphasis, and to invite comments and suggestions.
  - Establishing a risk-based Shari'a audit plan
- t) Internal Shari'a Audit report is submitted to the audit committee within the required time frame;
- u) During the [year ended] [period from XXXX to] 31 December 20XX the SSB has conducted XX meetings to review and approve key decisions relating to Shari'a matters. Minutes of the meetings are prepared and circulated to SSB members within X days of the meeting. The SSB members sign off the minutes to confirm the matters addressed therein. Decisions taken in SSB meetings are reflected in policies and procedures and operations of the Bank;
- v) The Independent External Shari'a Compliance Auditor is appointed and approved by the CBB.
- w) Roles and responsibilities for Shari'a Officer and Internal Shari'a Audit functions are appropriately defined and documented;
- x) All new products and services are reviewed and approved by the SSB before being offered to customers. Such information is appropriately documented.

**3.2.3 SSB quorum, minutes etc.**

- i) SSB meets at least on quarterly basis and each member of SSB attends at least three fourth of the meetings during a calendar year. Further, in addition to the regular meetings, the SSB Chairperson may convene SSB meetings as and when he deems it necessary;
- ii) All meeting are chaired by the SSB Chairperson and in his absence, by the vice-Chairperson;
- iii) The quorum of SSB meetings is majority of its members. SSB decisions are made through majority vote of SSB members;
- iv) The agenda of the SSB meetings along with sufficient details is sent to the SSB members well in advance, enabling them to come prepared in the meetings. The specific timelines for submission of the agenda is set by the SSB itself;

**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

- v) All the SSB approvals taken through circulation are made part of the minutes of the next SSB meeting;
- vi) The minutes of meetings are prepared and circulated to the SSB members. The SSB ensures that the minutes of its meetings have necessary details of all the decisions made and / or Fatawa issued along with the detailed rationale (Fiqhi or other) and difference of opinion or dissenting note, if any. Further, the minutes are signed by all the SSB members who attended the meeting to confirm the matters addressed therein, no later than in the next meeting;
- vii) The decisions taken in SSB meetings are reflected, as appropriate, in policies and procedures and day to day operations of the Bank as applicable

### **3.3 Control environment**

We are committed to maintaining a control conscious environment throughout the Bank in order to ensure that the operations of the Bank are conducted in a Shari'a compliant and controlled manner. This is achieved through the following policies and procedures:

- a) A management and organization structure is maintained by the Bank;
- b) An appropriate Shari'a governance framework in compliance with CBB regulations, resolutions and directives, AAOIFI governance standards and guidelines and directives issued by SSB is maintained;
- c) Key duties and functions are segregated. An independent executive is designated with the responsibility for Shari'a coordination and implementation; another independent executive is designated with the responsibility for internal Shari'a audit;
- d) Policies and procedures manuals and documentation in relation to Shari'a products, operations, compliance, trainings, and internal controls are maintained and available to all relevant staff;
- e) Business monitoring and risk assessment are in place to obtain reasonable assurance that the business is operating in compliance with Shari'a, regulatory and internal control requirements;
- f) Shari'a coordination and implementation and audit reports are submitted to the relevant authorities in line with the agreed annual plan;
- g) Procedures are in place on delegation of authority from senior Management;
- h) New business initiatives and products are fully considered and approved by the Management taking into account the relevant risks and benefits, Shari'a compliance and internal control requirements; and
- i) Documents are properly controlled and retained in accordance with established policies and procedures and in line with CBB's regulations, resolutions and directives.

### **3.4 Transaction level controls**

- a) All the products and services offered by the Bank are approved by the SSB;
- b) Adequate segregation of duties is in place for review and approval of transactions. The IT system does not post transactions that have not been approved by an assigned individual;
- c) Documents provided by customers are verified to ensure their authenticity. Individuals verifying such documents are required to stamp, initial and date the documents to evidence verification;

**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

- d) Only standard templates approved by the SSB are used for initiating and executing transactions;
- e) The income statement and sources of income including contracts made with counterparties are periodically reviewed by Internal Shari'a Audit. The review is conducted to:
  - i) Ensure that the Bank is operating within the parameters defined and approved by the SSB; and
  - ii) Determine whether any portion of income generated is Shari'a non-compliant and perform corrective actions (such as setting aside such income for charity purposes);
- f) All templates of agreements/contracts/forms are reviewed by Shari'a Officer prior to execution. This may include templates to be used for employee contracts, rental agreements, account opening forms, etc.
- g) All transactions are concluded with maker checker concept ensuring segregation of duties.

### **3.5 Product specific controls**

Before a product is launched to the general public, the Bank develops detailed product programs including but not limited to process flows, product features, product accounting treatment, IT system interaction, underlying contract templates and advertising material, which are approved by the SSB and other relevant authorities. Controls relating to the products currently being offered by the Bank are as follows:

#### **Murabaha:**

- a) The Bank has developed a Murabaha contract template which is approved by the Shari'a Supervisory Board and is used for Murabaha transactions;
- b) Staff executing Murabaha transactions are required to enter the following information before a transaction can be processed:
  - i) Purchase price of the underlying asset and associated costs;
  - ii) Sales price of the asset; and
  - iii) Bank's profit margin.
- c) The Bank is undertaking Murabaha transactions for [types of Murabaha], which is approved by the SSB;
- d) Documents that confirm legal title and ownership of underlying asset in the name of the Bank are obtained and maintained on file;
- e) Where the standard Murabaha contract template is not used, the amended contract is reviewed and approved by the Shari'a Officer to confirm inclusion of appropriate clauses necessary for a Shari'a compliant transaction.

#### **Diminishing Musharaka:**

- a) The Bank has developed a Diminishing Musharaka contract template which is approved by the Shari'a Supervisory Board and is used for Diminishing Musharaka transactions;
- b) Activities/projects/sectors where the Bank's equity under Diminishing Musharaka transactions can be invested are approved by the SSB and made available to the Bank's employees;



**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

- c) Documents that confirm legal title and ownership of the underlying asset in the name of the Bank are obtained and maintained on file;
- d) Where the standard Diminishing Musharaka contract template is not used, the amended contract is reviewed and approved by the Shari'a Officer to confirm inclusion of appropriate clauses necessary for a Shari'a compliant transaction.

**Ijarah (example if a product is not offered):**

- a) Currently Ijarah is not being offered as an independent product. However, Ijarah contract template is in place and approved by the SSB;

**Unrestricted Investment Accounts (URIA):**

- a) Funds are accepted under the Mudaraba model which has been approved by the SSB;
- b) The savings account and term deposits are obtained on the basis of Mudaraba, whereas inter-bank placements are done under Wakala;
- c) The deposits obtained by the Bank from URIA are invested in activities/projects/sectors/products which are approved by the SSB;
- d) Weightings are communicated to the depositors before the start of the pool period and are displayed on the Bank's website and notice boards in the branches in line with the relevant CBB regulations,, resolutions and directives;
- e) The profit rates are announced every month in the form of circulars which are displayed at the branches.

**3.6 Investment controls**

- a) Investments are executed only after being approved by the Shari'a Supervisory Board;
- b) To obtain approval from the SSB the Management submits information in various forms to provide the SSB with a clear picture of the potential investment. Matters subject to review and approval may include:
  - i) Preliminary deal analysis;
  - ii) Deal structuring and financing;
  - iii) Legal documentation;
  - iv) Private Placement Memorandum; and
  - v) Deal exit strategy (should be reviewed and approved by SSB members).
- c) For each investment, the SSB issues a certificate of approval which is signed off by the members of the SSB. The certificate evidences the review and approval by the SSB. It also indicates the SSB's satisfaction that the investment structure and associated documentation are in compliance with Shari'a principles;
- d) Investments are reviewed by the Internal Shari'a Audit function post acquisition to ensure they adhere to investment structure approved by the SSB;
- e) Site visits, meetings and discussions are conducted as and when deemed appropriate depending on the type of investment.

**3.7 Hiring process, employee training and awareness**

- a) The senior Management of the Bank including the CEO has adequate knowledge, qualification and experience in Islamic banking and finance;

**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

- b) Hiring processes are well defined. Required competence in Shari'a matters is defined in the hiring criteria;
- c) The Shari'a Officer oversees the Shari'a training plans and schedule for the Bank. He spends a significant percentage of his time, on an annual basis, in training the Management and the staff of the Bank.
- d) The Bank has developed a comprehensive training plan for the year 20XX identifying the areas where training is required and ensuring relevant subjects are covered;
- e) Various department and unit heads from within the Bank impart the training along with utilizing external expertise and the Shari'a resources within the Bank;
- f) A log of time spent on training is maintained by the training department of the Bank in an ERP based HR system;
- g) Induction training sessions are conducted for new staff (especially client facing employees) on the Bank's products and Shari'a principles;
- h) Seminars are conducted for employees to keep them up to date on:
  - New products and services approved by the Bank; and
  - Amendments to existing products and services.
- i) Annual training budget is in place for employees;
- j) A database containing Fatawa and Shari'a guidelines issued by the Bank's SSB is in place on the Bank's website and the internal portal of the Bank that is accessible to all staff members who are engaged in the Bank's operations as well as any other employee who asks for it. The database is kept up to date with new Fatawa issued from time to time.

**3.8 Other controls**

- a) The Bank has developed a code of conduct/ethics which is approved by the SSB to ensure compliance with Shari'a principles; and
- b) Tools for obtaining customer feedback and complaints are implemented (suggestion drop box, email, phone, etc.). The Shari'a Officer reviews customer feedback/complaints received to ensure matters relating to Shari'a compliance are adequately addressed.



**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

#### **4. Control Objectives**

The Bank's control objectives as approved by the Bank's SSB are provided below:

##### **4.1 Overall control objective:**

Ensure that the Bank's activities are conducted in a Shari'a compliant manner. Achievement of this objective requires compliance with Shari'a guidelines/directives issued by the Bank's SSB (referred to as the Bank's Shari'a principles) and other relevant authorities.

##### **4.2 Specific control objectives:**

Ensuring that:

- a) The Bank's transactions, contracts and earnings are in accordance with the Bank's Shari'a principles;
- b) Employees are appropriately and adequately trained to possess knowledge on Shari'a products/services offered by the Bank;
- c) Revenues, collections and income that do not comply with the Bank's Shari'a principles are adequately segregated and appropriately treated;
- d) Allocation of profit and charging of losses to investment accounts conform to the basis approved by the SSB; and
- e) Management does not override or compromise the Bank's Shari'a principles to enhance the Bank's performance.

**[Minimum Control Procedures Provided for illustrative purposes only, each IFI will have its own policies and procedures]**

**2. INDEPENDENT ASSURANCE REPORT TO THE BOARD OF DIRECTORS OF XYZ BANK ON CONTROL PROCEDURES RELATING TO SHARI'A COMPLIANCE AND GOVERNANCE STRUCTURE (QUALIFIED)**

We have been engaged by the Board ....

***Management's responsibility***

The Bank's management is responsible to provide an assertion about the fairness of the.....

***Practitioner's responsibility***

Our responsibility is to express an independent conclusion on the Shari'a compliance ....

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit conclusion.

***Basis for qualified opinion***

The Management's Shari'a compliance and governance report did not include product specific controls with respect to Murabaha and Musharaka, thereby failing to ensure the Bank's compliance with the CBB's regulations, resolutions and directives and the Shari'a rules and principles expressed in the rulings of its SSB.

***Qualified opinion***

In our opinion, except for the effects of the matter described in the Basis for qualified opinion paragraph, the management's assertion that internal controls relating to Shari'a compliance and governance and the design and operating effectiveness of those controls is effective, in all material respects, based on criteria laid down in the Management Shari'a compliance and governance report, is fairly stated.

***Intended users and purpose***

In accordance with the terms of our engagement, this independent reasonable assurance report.....