



EVOLUTION OF *SHARĪ'AH* GOVERNANCE PRACTICES IN *SHARĪ'AH* RISK MANAGEMENT FUNCTION FROM THE INSTITUTIONAL THEORY PERSPECTIVE

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ABSTRACT

This research aims at elucidating the evolution of *Sharī'ah* governance practices in a Malaysian *Islāmic* bank by examining the progression toward institutionalization through the lens of Institutional Theory. A qualitative research approach was employed, drawing on existing literature, case studies, and interviews with experts in *Sharī'ah* risk management function. An explanatory case study was done to deeply understand the institutionalization of *Sharī'ah* governance practices due to the evolution of framework and policy from Shariah Governance Framework (SGF) 2010 to the latest Shariah Governance Policy Document (SGPD) 2019. This research delves into the development of *Sharī'ah* governance from SGF 2010 to SGPD 2019, with a particular focus on the institutionalization of the *Sharī'ah* risk management function in an *Islāmic* bank. Analyzing the outcomes through the framework outlined by Burns and Scapens in 2000 within the context of Institutional Theory, the research highlights how this evolution has fortified *Sharī'ah* governance practices over time, indicating a shift toward greater alignment in an *Islāmic* bank with *Sharī'ah* governance. However, a notable limitation persists in ensuring the competency and expertise of *Sharī'ah* officers, particularly in their adaptation to institutional and actionable realms in routinizing the rules. This research paper enriches understanding of institutionalization, emphasizing its pivotal role in fostering trust, providing support, and enabling optimal performance among *Sharī'ah* officers. It highlights the importance of continuous learning and skill development for *Sharī'ah* officers, asserting that competency and expertise can evolve progressively. Consequently, the *Sharī'ah* governance practices in *Islāmic*

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banks have exhibited increased robustness, effectively mitigated *Sharī'ah* non-compliance risks, and demonstrated heightened adherence to *Sharī'ah* governance and compliance.

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1. INTRODUCTION

The evolution of regulated *Sharī'ah* compliance in Malaysia commenced 40 years ago with the enactment of the Islamic Banking Act 1983 (IBA). Malaysia, aspiring to become a global *Islāmic* finance hub, has indeed set a benchmark in the field, particularly in *Sharī'ah* governance. It is now ahead of the world in regulating its *Islāmic* finance industry. The regulatory bodies, notably Bank Negara Malaysia (BNM), have consistently enhanced the framework for *Islāmic* finance since the enforcement of the Islamic Banking Act. BNM's issuance of *Sharī'ah* governance-related guidelines, such as the Shariah Governance Framework (SGF) in 2010 (SGF 2010) and its subsequent revision in 2017, stands as a testament to this commitment. Scholars such as Shafii, Salleh, and Hj Shahwan (2010) emphasize that robust *Sharī'ah* governance is pivotal in establishing the procedures for *Islāmic* products and services offered by Islamic Financial Institutions (IFIs) as it contributes significantly to their financial and economic stability. Malaysia leads the global *Islāmic* finance market, evidenced by its substantial share in the sukuk market, which is approximately 67% globally. The BNM proactive measures through SGF and introduction of the Islamic Financial Services Act (IFSA) in 2013 have further fortified *Sharī'ah* governance practices within IFIs. This step catalyzed the growth of IFIs across the country.

Continuous efforts by BNM were reflected in the issuance of the Shariah Governance Policy Document (SGPD) in September 2019, aimed at enhancing the roles of the board, management, and the *Sharī'ah* committee (SC). Moreover, an increasing number of national and international conferences and programs focusing on *Sharī'ah* governance in IFIs have not only engaged academia but also experts, amplifying societal awareness and understanding in this domain (Mohd Hanefah and Kamaruddin, 2019). Amidst these advancements, however, unresolved concerns and challenges persist in *Sharī'ah*

governance within IFIs, primarily centered around the competence and availability of *Sharī'ah* scholars and practitioners, and the capabilities of IFIs in executing *Sharī'ah* functions (Kamaruddin and Mohd Hanefah, 2017; Shafii, Mohd Ali, and Kasim, 2014). Addressing these issues is crucial as failure to adhere to good *Sharī'ah* governance may jeopardize the *Islāmic* bank operational compliance.

This paper aims at elucidating the evolution of *Sharī'ah* governance practices in a Malaysian *Islāmic* bank within the framework of Institutional Theory, examining the evolution between SGF 2010 and SGPD 2019, with a specific focus on the *Sharī'ah* risk management function. Institutional Theory examines how organizations interact with their environments, respond to societal expectations, and integrate these influences into their practices including rules and routines (Dillard et al., 2004). This study focused on the institutionalization of rules, norms, and behaviors within *Islāmic* banks, recognizing their dynamic nature (Ahmed and Scapens, 2000; Burns and Scapens, 2000; Scapens, 1994). Institutional Theory in this study is aligned with the approach outlined by Karbhari, Alam and Rahman (2020). Their conceptual paper used Institutional Theory to explore institutional development and *Sharī'ah* governance practices in the *Islāmic* banking sector. Analyzing the outcomes through the framework outlined by Burns and Scapens (2000) focused on old institutional economics, this study identified *Sharī'ah* risk management as a key system of rules. Meanwhile, routines are tolerated in existing institutions and institutional norms and values (environment).

The comparative analysis accentuates the strengthening of *Sharī'ah* governance practices, which serves as an isomorphic mechanism for Malaysian *Islāmic* banks to align more rigorously with *Sharī'ah* governance, especially noting the greater institutionalization in SGPD 2019 compared to SGF 2010 in ensuring the legitimacy of Malaysian *Islāmic* banks.

Moving forward, this study will briefly explain the distinction of corporate governance with *Sharī'ah* governance and delve into an overview of *Sharī'ah* governance evolution in Malaysian *Islāmic* banks including the *Sharī'ah* governance practices and *Sharī'ah* risk management function in Section 3, followed by theoretical insights rooted in the Institutional Theory elucidated through Burns and Scapens' framework (2000) in Section 4. Section 5 will detail the research methodology. The analysis and result as well as findings and discussion from the interview with *Sharī'ah* officers in *Sharī'ah* risk

management function are illustrated in Section 6. Section 7 presents the concluding reflections and recommendations for future research.

2. CORPORATE GOVERNANCE AND *SHARĪ'AH* GOVERNANCE

Corporate governance encompasses a set of processes, policies, and laws that influence the governance, direction, management, and control of an organization (Sulaiman, Abd Majid, and Mohd Ariffin, 2015). This framework extends to the governance structure involving key actors in the institutional process. *Sharī'ah* governance, while sharing similarities with corporate governance, is distinct in its unique responsibility for ensuring compliance with *Sharī'ah* principles in all aspects of products, operations, practices, and management within *Islāmic* banks. Grassa and Matoussi (2014) highlight that *Sharī'ah* governance requires IFIs, especially *Islāmic* banks, to conduct their activities exclusively on the basis of *Sharī'ah*, setting it apart from conventional corporate governance. *Sharī'ah* governance, a term employed by researchers to signify the governance system of IFIs, is also known as *Islāmic* corporate governance (Mizushima, 2014; Wilson, 2009).

For the purpose of this research, however, the preferred terminology is *Sharī'ah* governance. Similar to corporate governance, *Sharī'ah* governance is concerned with the objectives of the corporation and its stakeholders. It extends the discourse to delineate how the governance system should operate to ensure *Sharī'ah* compliance within the corporation, addressing gaps in corporate governance theories related to entities offering *Islāmic* products and services. Moreover, *Sharī'ah* governance serves as a system that safeguards all activities and business transactions of *Islāmic* banks from non-permissible features such as *ribā'*, *gharar*, *maysir*, and other similar elements (Venardos, 2010). It acts as a guideline for ensuring the operational practices of *Sharī'ah* officers in *Islāmic* banks are aligned with the *Sharī'ah* compliance mission. Non-compliance with *Sharī'ah* is considered a reputational risk, impacting market and public confidence in credibility of *Islāmic* banking. The significance of *Sharī'ah* compliance in the growth of *Islāmic* banks is stressed by customer preference for *Sharī'ah*-compliant products and services. Ullah and Lee (2012) assert that to achieve better growth, *Islāmic* banks must offer competitive and *Sharī'ah*-compliant products. This aligns with research by Abdullah and Mohd Kassim (2015), which identified *Sharī'ah* compliance as a key factor contributing to *Islāmic* bank growth. Such growth is contingent on the degree of *Sharī'ah*

compliance in offered products and services, and this element as a whole influences customer demand and institutional growth (Khatun, 2013). The establishment of infrastructural institutions supporting the *Islāmic* banks led to the standardization of framework and regulation that enhanced *Islāmic* bank growth in the 2000s (Mat Ghani, 2020)

3. OVERVIEW OF *SHARĪ'AH* GOVERNANCE EVOLUTION IN MALAYSIAN *ISLĀMIC* BANKS

The evolution of *Sharī'ah* governance is seen as a positive development, introducing more stringent regulations, especially concerning *Sharī'ah* compliance in *Islāmic* banks. In the early stages of *Islāmic* banking in Malaysia, matters related to *Sharī'ah* governance were addressed by the BNM guidelines on *Sharī'ah* Committee (BNM/GPS 1), introduced in December 2004. During this period, the *Sharī'ah* Committee played a central role as the primary governance mechanism to ensure *Sharī'ah* compliance in *Islāmic* banks. Recognizing the need for comprehensive *Sharī'ah* compliance, BNM subsequently introduced the Shariah Governance Framework in 2010, effective from January 1, 2011. SGF 2010 significantly enhanced the roles and functions of *Sharī'ah* control, including *Sharī'ah* review, *Sharī'ah* audit, *Sharī'ah* risk management, and *Sharī'ah* research functions. It introduced a systematic approach for *Islāmic* banks to manage *Sharī'ah* non-compliance risks and ensure continuous operations and activities of *Islāmic* banks.

Introduction of the Islamic Financial Services Act 2013 (IFSA 2013) by BNM further solidified *Sharī'ah* governance practices by making them mandatory for *Islāmic* banks (Muneeza, 2014). IFSA 2013 upheld the SGF 2010 and other guidelines, giving them statutory force. The act emphasized the importance of compliance with internal policies and procedures to implement specified BNM standards, with severe statutory punishments for non-compliance.

A subsequent development in Malaysian *Sharī'ah* governance occurred in 2019 with the issuance of the Shariah Governance Policy Document (SGPD) to replace the 2010 version. SGPD 2019 introduced additional obligations and enforcement actions for non-compliance, emphasizing transparency and disclosure. It refined the *Sharī'ah* control functions to focus solely on *Sharī'ah* compliance, excluding *Sharī'ah* risk management and *Sharī'ah* research. Notably, both SGF 2010 and SGPD 2019 included a distinct section on transparency and disclosure to provide detailed guidelines for forming opinions in the *Sharī'ah* Committee.

The evolution of *Sharī'ah* governance between 2004 and 2019 reflects a continuous effort to strengthen *Islāmic* bank regulations and address *Islāmic* banking sector complexities. This evolution has been driven by recommendations from *Sharī'ah* scholars, responding to unresolved *Sharī'ah* governance issues. The emphasis on a *Sharī'ah* compliance culture and penalties for non-compliance has prompted *Islāmic* banks to adapt their activities, contributing to the ongoing evolution of *Sharī'ah* governance. Table 1 summarizes the key milestones in the evolution of *Sharī'ah* governance in Malaysian *Islāmic* banks.

3.1 SHARĪ'AH GOVERNANCE PRACTICES IN MALAYSIAN ISLĀMIC BANKS

The evolution of *Sharī'ah* governance practices has witnessed substantial enhancements following the enforcement of key regulatory frameworks such as SGF 2010, IFSA 2013, and SGPD 2019. These developments have been prompted by a combination of challenges and ongoing institutional structure refinement of reporting lines, disclosure mechanisms, as well as accountability and responsibility frameworks. Notably, these regulatory milestones have played a pivotal role in reshaping the *Sharī'ah* governance landscape within *Islāmic* banking institutions.

Shafii et al. (2014) asserted that expansion of *Sharī'ah* Committee roles and responsibilities, coupled with the integration of *Sharī'ah* control functions, has brought significant value to *Islāmic* bank operational dynamics. This positive impact on operations has been particularly pronounced in the decade since the issuance of SGF 2010. The comprehensive *Sharī'ah* control functions, as stipulated in SGPD 2019, include the *Sharī'ah* review (compliance) function, *Sharī'ah* risk management function, and *Sharī'ah* audit function, all of which continue to play integral roles in ensuring *Sharī'ah* compliance.

One noteworthy adjustment introduced by SGPD 2019 is the consolidation of the *Sharī'ah* research function under the umbrella of the *Sharī'ah* Division. This restructuring aims at streamlining and enhancing the efficiency of *Sharī'ah* governance practices. Consequently, the *Sharī'ah* Division has assumed the role of the secretariat for the *Sharī'ah* Committee, focusing on elevating the quality of decisions and advice provided by the committee. This strategic move underlines a deliberate effort to refine the governance structure and maximize effectiveness of *Sharī'ah* oversight.

TABLE 1
Summary of the *Sharī'ah* Governance Evolution

GPS 1/ 2004	SGF 2010	IFSA 2013	SGPD 2019
<ul style="list-style-type: none"> ▪ To set the rules, regulations, and procedures in forming a <i>Sharī'ah</i> Committee. ▪ To define the <i>Sharī'ah</i> Committee roles, scope of work, and responsibilities. 	<ul style="list-style-type: none"> ▪ To structure a framework that provides <i>Sharī'ah</i> governance structures, processes, and arrangements to ensure that all its operations and business activities align with <i>Sharī'ah</i> principles. ▪ To provide the board, <i>Sharī'ah</i> Committee, and the management with a comprehensive guideline to discharge its duties in <i>Sharī'ah</i> - related matters. 	<ul style="list-style-type: none"> ▪ Effective establishment of <i>Sharī'ah</i> Committee based on qualification, appointment, duties, cessation, and information. ▪ Appointment of a person by institution to conduct audit on <i>Sharī'ah</i> compliance. ▪ Appointment of a person by the bank to conduct an audit on <i>Sharī'ah</i> compliance. 	<ul style="list-style-type: none"> ▪ More active roles and guidelines are expected of the board, <i>Sharī'ah</i> Committee, the senior management, and key institutional members. ▪ The <i>Sharī'ah</i> Committee aims to reinforce robust decision-making processes and internal control functions for optimal <i>Sharī'ah</i> non-compliance risk management
<ul style="list-style-type: none"> ▪ To outline IFIs' duties and responsibilities. 	<ul style="list-style-type: none"> ▪ To outline the newly created functions entailing <i>Sharī'ah</i> review, <i>Sharī'ah</i> audit, <i>Sharī'ah</i> risk management, and <i>Sharī'ah</i> research. 	<ul style="list-style-type: none"> ▪ To enforce <i>Sharī'ah</i> compliance status on the market and drive the IFI toward more <i>Sharī'ah</i> compliance activities via close monitoring and penalties. ▪ To impose strict and severe penalties following the failure to comply with <i>Sharī'ah</i> principles. 	<ul style="list-style-type: none"> ▪ To outline the functions entailing <i>Sharī'ah</i> compliance, <i>Sharī'ah</i> audit and <i>Sharī'ah</i> risk management.

In the context of this research, the examination specifically delves into the evolution of *Sharī'ah* governance practices with a targeted focus on the *Sharī'ah* risk management control function. By scrutinizing the developments in this specific domain, we aim at contributing valuable insights into the ongoing evolution of *Sharī'ah* governance, shedding light on how institutions manage and mitigate *Sharī'ah* non-compliance risks. This focused exploration is expected to yield a nuanced understanding of the advancements and challenges associated with *Sharī'ah* risk management, thereby enriching the broader discourse on the continuous refinement of *Sharī'ah* governance practices within the *Islāmic* banking sector.

3.2 SHARĪ'AH RISK MANAGEMENT FUNCTION

The concept of *Sharī'ah* risk management within the framework of Islamic Financial Institutions (IFIs) has evolved significantly between SGF 2010 and SGPD 2019, underscoring its critical role as a compliance and control function. According to BNM's definition, *Sharī'ah* risk management in SGF 2010 is characterized as a function that systematically identifies, measures, monitors, and controls *Sharī'ah* non-compliance risks to avert potential non-compliance events. *Sharī'ah* risk management is still an important *Sharī'ah* function in the SGPD 2019 to ensure effective risk management of *Sharī'ah* non-compliance (Mohd Ariffin, 2022).

SGPD 2019 further elaborates this function, emphasizing its role in systematically identifying, measuring, monitoring, and reporting *Sharī'ah* non-compliance risks across IFIs' operations, business affairs, and activities. The *Sharī'ah* risk management functions in accordance with the SGPD 2019 requirements to perform risk management processes so that *Islāmic* banks can mitigate any possible events that could create *Sharī'ah* non-compliance risk.

This evolution highlights the growing emphasis on *Sharī'ah* risk management as an independent function within IFIs, dedicated to managing and mitigating the associated non-compliance risks. Kasim et al. (2013) support this idea by emphasizing that a distinct *Sharī'ah* risk management function is pivotal in managing *Sharī'ah* non-compliance risks and preventing potential issues. The systematic approach adopted in addressing these risks ensures the seamless continuation of operations within *Islāmic* banks.

Sharī'ah risk management officers, equipped with expertise in *Sharī'ah* requirements and practices, play a crucial role in this function. They are tasked with reporting directly to the risk

management committee, Board of Directors, and management via the *Sharī'ah* Committee, ensuring effective oversight and control. The *Sharī'ah* risk management function under SGF (2010) requires a comprehensive approach involving identification, measurement, monitoring, and control of such risks. This includes understanding inherent risks in IFIs, evaluating the effectiveness of existing controls, assessing the potential impact of non-compliance on IFIs, and implementing controls to track and prevent non-compliant events. Additionally, developing policies and guidelines for *Sharī'ah* non-compliance risk management and fostering awareness of these risks among IFI staff are the key aspects of a robust risk management framework.

SGPD 2019 further emphasizes the monitoring of *Sharī'ah* non-compliance risk exposures and the effectiveness of mitigation measures. The function mandates reporting to the board, *Sharī'ah* Committee, and senior management regarding such exposures, and contesting decisions that elevate non-compliance risks. This becomes an integral part of IFIs' integrated risk management framework. The effective management of *Sharī'ah* non-compliance risks relies on robust processes within the *Sharī'ah* risk management function, including identification, measurement, monitoring, reporting, and control. By ensuring optimal governance practices within this function, IFIs can consistently align their activities and operations with *Sharī'ah* principles. Notably, *Sharī'ah* compliance is a fundamental aspect of operational risk for *Islāmic* banks. Hence, to mitigate this risk, banks must maintain unwavering adherence to *Sharī'ah* principles in all their operations and product offerings (Izhara, and Asutay, 2010).

4. INSTITUTIONAL THEORY

The Institutional Theory plays an important role in enhancing institutional structure and performance by balancing stakeholders' roles. The theory helps deliver a structure for recognizing how existing practices and standards among similar institutions influence how that regulation (i.e. in this case, *Sharī'ah* governance) is both interpreted and implemented in *Islāmic* banks. Thus, this research is motivated to consider Institutional Theory as the leading theory as it best illuminates the operational guidelines and procedures for IFIs. The few studies that attempt to show the importance of applying Institutional Theory in *Sharī'ah* governance of *Islāmic* banks include a study in terms of institutionalization of norms into *Sharī'ah* finance

(Hasanuddin and Hakim, 2017), institutionalization of *Islāmic* banking practices through specific work of key actors (Siti Nabiha and Adib, 2020) and the adaptation of new Institutional Theory in explaining the differences in *Sharī'ah* governance practices in a concept paper by Alam, Karbhari, and Rahman (2021).

This research, therefore, further adds a novel dimension to literature. First, the contribution to prior literature on *Sharī'ah* governance as it provides valuable insight on why Institutional Theory is more pronounced (as compared to the other theoretical frameworks) in the formation and discharge of the roles, powers, and functions by the different governance organs (such as regulators, the board of directors, management and *Sharī'ah* supervisory boards) operating in this unique corporate governance landscape. Second, by highlighting that the structures, procedures and rules of *Sharī'ah* governance are better represented by Institutional Theory and therefore, more relevant in ensuring accountability, independence, competence, confidentiality and transparency and disclosure especially in mitigating the *Sharī'ah* non-compliance risk, resulting in robust *Sharī'ah* governance and compliance.

Institutionalization involves movements from old to new possibilities (new structure, new policies, new behaviors, new actions, new patterns, new methodologies, new products or new market ideas) based on the reconceptualized patterns in the institution (Kanter, Stein and Jick, 1992). The architecture of institutionalization involves the design and construction of new patterns, or the reconceptualization of old ones, to make new, and hopefully more productive actions possible. Recent literature (Kanji and Moura, 2003; Lycke, 2003), state that changes can be various and could also include changes to procedures, structures, rules and regulations, technology, training and knowledge development within institutions. Therefore, it can be considered as the shift in behavior of the whole institution (Kanter et al., 1992), including the shift in people behavior, their activities, and the relationship of both elements in an institution.

An institution intending to institutionalize the new practices will need to be supported by intense pressure, various force factors, or broad influences to successfully implement the new practices (Norhayati and Siti Nabiha, 2009). Two types of factors influence institutionalization, namely internal and external environmental pressure (Cobb, Helliar, and Innes, 1995). The influence of intense pressure would move from the regulator to the institution level and next, to the internal level in the institution (Wanderley et al., 2011). This institutionalization will need more time to routinize the rules.

Institutionalization is also seen as an important part of evolution involving expansion and improving the systems, rules, and routines.

4.1 BURNS AND SCAPENS FRAMEWORK (2000)

The Burns and Scapens (2000) framework serves as a comprehensive guide in understanding the implementation of *Shari'ah* governance practices within the *Shari'ah* risk management control function. This framework delineates the stages of encoding, enacting, reproduction, and institutionalization, offering a thorough explanation of how these practices become embedded within *Islāmic* bank operations. Importantly, it views institutionalization as an ongoing process, recognizing that it evolves over time rather than being a singular event. This framework's flexibility extends beyond *Shari'ah* governance practices, encompassing various practice types, including the institutionalization of management accounting practices in specific establishments. Its adaptability and inclusivity make it an apt tool for explaining the institutionalization of *Shari'ah* governance practices in this research paper.

What sets Burns and Scapens' framework apart is its acknowledgment of the contribution of culture and values in the institutionalization process. Recognizing the significance of these elements in shaping institutional practices within *Islāmic* banks, the framework emphasizes the role of culture and values in facilitating the embedding of *Shari'ah* governance practices. While other frameworks exist, such as DiMaggio and Powell's (1983) framework of institutional isomorphism, Meyer et al.'s (1990) framework of institutionalized organizations, and Scott's (2008) framework of institutions and organizations, the Burns and Scapens framework stands out given its comprehensiveness, dynamism, and practical applicability. Its ability to encapsulate the complexities of institutionalization, coupled with its adaptability across various practice domains, makes it a fitting choice for elucidating the institutionalization of *Shari'ah* governance practices in *Islāmic* banks within this research context.

5. METHODOLOGY

This explanatory case study was conducted in a Malaysian *Islāmic* bank. This method adds valuable insight and allows for a comprehensive understanding on changes of rules and routines in the current practices in accordance with changes in the *Shari'ah*

governance practices guidelines and procedures from SGF 2010 to SGPD 2019. This research uses a qualitative research methodology. Table 2 lists the three *Sharī'ah* risk management officers, based on work experience (up to 2021 end of data collection period), qualification, and duration of interview for each interview session. The identified interviewees are knowledgeable and have experienced the evolution of *Sharī'ah* governance practices in the *Islāmic* bank. The Head of Shariah risk management function as well as the other two *Sharī'ah* risk management officers could address the questions and reflect the changes in the evolution that occurred from SGF 2010 to SGPD 2019 during the interview. In this single case study, three participants are sufficient since the data is rich, detailed, and saturated in achieving the objective of the study.

TABLE 2
Participants Profile

Position	Working experience with EMERALD (up to 2021)	Qualifications	Reporting to	Duration of interview
Head of <i>Sharī'ah</i> Risk Management Function	10 years	Master in Islamic Economy CIFPs	Chief Risk Management Officer	1 hour 20 minutes
<i>Sharī'ah</i> Risk Management Officer 1	7 years	Degree in Islamic Banking CIFPs	Head of <i>Sharī'ah</i> Risk Management Function	1 hour 25 minutes
<i>Sharī'ah</i> Risk Management Officer 2	3 years	Degree in <i>Fiqh</i> and <i>Usul</i> CIFPs	Head of <i>Sharī'ah</i> Risk Management Function	1 hour 16 minutes

The interview data collected through semi-structured interviews with three *Sharī'ah* risk management officers in an *Islāmic* bank later on named as EMERALD, were transcribed. The transcript data were further analyzed using thematic analysis, content analysis, and discussed based on the Burns and Scapens (2000) framework focused on old institutional economics (OIE) to explain the institutionalization of *Sharī'ah* governance practices in the *Sharī'ah* risk management process at EMERALD. The Burns and Scapens framework provides a valuable lens for better understanding this process (Karbhari et al., 2020). This research explained why and how

Islāmic banks institutionalize their *Sharī'ah* governance practices. Thus, the main theme was developed based on the research question, “Why and how do the *Sharī'ah* governance practices institutionalize in *Islāmic* banks?”. In answering the question, this study considers the current process under SGPD 2019 of *Sharī'ah* risk management control function at EMERALD. The sub-theme was developed earlier from the document reviewed on SGPD 2019, which focused on the *Sharī'ah* risk management process. The transcript data was then extracted and matched with the sub-theme, and at the same time, the codes were identified and developed. This process is called ‘coding’.

This interpretive case study established good rapport between the researcher and EMERALD members during their interactions to gauge “how things should be done” (rules) and “how things are actually done” (routines) in daily operations (Ahrens et al., 2007). As social phenomena are the key focus of interpretive case study and OIE (Burns and Scapens, 2000), this approach complemented the theoretical framework in this study. Four processes fall within the rules and routines, namely encoding, enacting, reproduction, and institutionalization that move in a reciprocal manner. The first process involves encoding the existing institution and taking for granted assumptions and meanings into the new rules, routines and procedures which embody institutional values. The new rules or procedures are usually interpreted in terms of the current norms and values of the group using the system. The second process is enacting routines and rules, which encode the institutional principles through the day-to-day activities performed by institutional members. The third process represents the ‘reproduction’ of the rules and routines over time, through their repeated use in practice (Scapens et al., 2003). The last step refers to ‘institutionalization’ of routines and rules which have been reproduced through the behavior of individual institutional members. The key attribute of the Burns and Scapens framework is that it describes the processes of change over time and remains relatively stable (Cameron and Quinn, 1999).

Table 3 summarizes explanations of the four processes in institutionalization by Burns and Scapens (2000). Institutionalization of the *Sharī'ah* governance rules and routines may be applicable to *Islāmic* banks, in relation to this research, because the introduction of *Sharī'ah* governance into *Islāmic* banks has resulted in great changes to the institution in doing business (Kasim et al., 2013). Accordingly, routinization of rules has coincided with the *Sharī'ah* governance evolution.

TABLE 3
Four Processes of Institutionalization

Process	Transform rules and routines
Encoding	Process of encoding existing rules, routines and procedures which embodied institutional value such as existing accounting standards adopted.
Enacting	The new rules and routines performed by institutional members on daily activities become enactment within the institution. Resistance normally exists at this stage especially when new rules and routines challenge existing understanding.
Reproduction	Process of reproduction of new rules and routines continuously happens in a reciprocal manner through repeated use in practice over time.
Institutionalization	Large collective members within an institution agree to accept the new set of rules and routines.

Source: Burns and Scapens' Framework (2000)

6. ANALYSIS AND RESULTS

The interview data and reviewed documents (SGPD 2019) in this research were further analyzed and discussed according to the Burns and Scapens (2000) framework, with an emphasis on OIE to explain the institutionalization of *Sharī'ah* governance practices in *Sharī'ah* control functions at EMERALD. This framework, which provided a sound understanding of this process, underscored the significance of encoding, enacting, reproduction, and institutionalization in institutionalizing *Sharī'ah* governance practices. Table 4 summarizes the processes under *Sharī'ah* risk management function as stated in SGPD 2019. The first analysis was document-review to understand the routinization of rules or the institutionalization of *Sharī'ah* governance practices. Essentially, SGPD 2019 on the *Sharī'ah* control functions section was reviewed to identify the keywords or themes and further analyzed to address the main research question: "Why do *Islāmic* banks institutionalize their *Sharī'ah* governance practices and how does the institutionalization of *Sharī'ah* governance practices take place in the *Islāmic* bank?"

Parallel to the analysis results, the institutionalization of *Sharī'ah* governance practices was identified under the *Sharī'ah* risk management function, which involved encoding a *Sharī'ah* non-compliance risk management framework. The description in Table 4, which is "To integrate between *Sharī'ah* non-compliance risk with

conventional risk management”, exemplifies encoding. This activity involved integrating this framework with that of conventional risk management used by the Risk Management Division at EMERALD. This integration would ensure effective management of *Sharī'ah* non-compliance risk.

TABLE 4
Processes under *Sharī'ah* Risk Management Functions by
SGPD 2019

<i>Sharī'ah</i> control function	Process
<i>Sharī'ah</i> Risk Management	<ul style="list-style-type: none"> ● To integrate <i>Sharī'ah</i> non-compliance risk with conventional risk management. ● To identify potential <i>Sharī'ah</i> non-compliance risk exposures. ● To assess and measure the potential impact of <i>Sharī'ah</i> non-compliance risk exposures. ● To develop appropriate risk mitigation measures. ● To closely monitor both <i>Sharī'ah</i> non-compliance risk exposures and the effectiveness of risk mitigation measures. ● To report to the BOD, <i>Sharī'ah</i> Committee, and senior management on <i>Sharī'ah</i> non-compliance risk exposures. ● To develop constructive decisions that may prevent escalation to <i>Sharī'ah</i> non-compliance risks.

Source: Bank Negara Malaysia, SGPD 2019

The enacting process involved implementing the *Sharī'ah* non-compliance risk management framework in deterring *Sharī'ah* non-compliance events. The description in Table 4, which is “To identify potential *Sharī'ah* non-compliance risk exposures”, exemplifies enacting. This process involved identifying the potential *Sharī'ah* non-compliance risk exposures by reviewing the documents on new products to identify and assess the risk exposure. This identification would ensure that the management or business unit is aware of the risk exposure and undertakes risk mitigation measures. Reproduction involved the continuous monitoring of *Sharī'ah* non-compliance events. The description in Table 4, which is “Assess and measure the potential impact of *Sharī'ah* non-compliance risk exposures”, exemplifies reproduction. The process involved repetitive

actions in assessing and measuring the potential impact of the identified *Sharī'ah* non-compliance risk exposures. Implementing good assessment tools and mechanisms, such as RCSA, independent risk investigation, and risk notification proved useful in ensuring awareness about the potentiality of *Sharī'ah* non-compliance risks hence prompting risk mitigating actions.

Institutionalization involved embedding practices of deterring and mitigating *Sharī'ah* non-compliance risk as a routine. The description in Table 4, which is “To develop appropriate risk mitigation measures”, exemplifies institutionalization. This process involved developing appropriate risk mitigation measures to counter the identified *Sharī'ah* non-compliance risk exposures. Potential *Sharī'ah* non-compliance events could be mitigated with preventive, corrective, and rectification plans. The enacting process implies “To closely monitor both *Sharī'ah* non-compliance risk exposures and effectiveness of the risk mitigation measures” as described in Table 4. This process involved the close monitoring of *Sharī'ah* non-compliance risk exposures and the effectiveness of risk mitigation measures. At this stage, potential *Sharī'ah* non-compliance events were closely reviewed to ensure no resistance to the risk-mitigating measures and effective enactment of the *Sharī'ah* non-compliance risk management framework. This framework would be updated over time to validate the potential risk exposures identified. The description in Table 4, which is “To report to the BOD, the *Sharī'ah* Committee and senior management on the *Sharī'ah* non-compliance risk exposures”, exemplifies reproduction. This process involved reporting *Sharī'ah* non-compliance risk exposures to the BOD, *Sharī'ah* Committee, and senior management and ensuring that the management, other control functions, and business units are aware of the risks and actions taken to mitigate the risks involved. Initiatives on development of RCSA tools, independent investigation, and risk notification added value to the institutionalization of *Sharī'ah* governance practices in *Sharī'ah* risk management function at EMERALD.

Table 5 provides the sub-theme and codes for Theme 3, *Sharī'ah* risk management function. The cross-sectional content analysis for the interview transcripts was performed with NVivo 14, a computer-aided qualitative data analysis software as per Figure 1. The relevant information was extracted from the transcribed interview data and was deduced to match the sub-theme while simultaneously having the codes identified and developed through the coding process. The final (exploratory) stage of analysis summarized the results derived from the cross-sectional content analysis using NVivo 14 as shown in

Table 6. This final-stage analysis facilitated identification of coded activities under each sub-theme in line with the Burns and Scapens (2000) framework. The routinization of rules elaborated the encoding, enacting, reproduction, and institutionalization in *Sharī'ah* risk management function.

TABLE 5
Document Review and Coding for Theme - *Sharī'ah* Risk Management Function (SGPD 2019)

Sub-theme	Description
<i>Sharī'ah</i> non-compliance Integration	Integrate <i>Sharī'ah</i> non-compliance risk considerations with enterprise-wide risk management.
<i>Sharī'ah</i> non-compliance identification	Identify <i>Sharī'ah</i> non-compliance risk exposures in business operations and activities.
<i>Sharī'ah</i> non-compliance assessment and measurement	Assess <i>Sharī'ah</i> non-compliance risk and measure the potential impact of risk exposures.
Develop mitigation measures	Establish appropriate risk mitigation measures according to the identified risk types and levels.
Monitor <i>Sharī'ah</i> non-compliance	Closely monitor both <i>Sharī'ah</i> non-compliance risk exposures and the effectiveness of risk mitigation measures.
Reporting of <i>Sharī'ah</i> non-compliance	Report to the board, <i>Sharī'ah</i> committee and senior management on the <i>Sharī'ah</i> non-compliance risk exposures.
Developing constructive decisions	Constructively challenge decisions that may give rise to <i>Sharī'ah</i> non-compliance risks to identify and assess <i>Sharī'ah</i> non-compliance.

Source: Bank Negara Malaysia, SGPD 2019

Overall, the encoding stage was manifested in integrating *Sharī'ah* non-compliance risk management with conventional risk management within EMERALD. This integration aimed at ensuring a cohesive and effective approach toward managing *Sharī'ah* non-compliance risk. While implementing the enacting process, it is evident that EMERALD implemented the *Sharī'ah* non-compliance risk management framework to identify potential risk exposures, enabling proactive risk assessment and mitigation.

FIGURE 1
Summary of Content Analysis Performed using NVivo 14–
Theme *Sharī'ah* Risk Management Function

Node Name	Files	Re
THEME 3		
○ SNC assessment	0	0
○ assessment tools	1	2
○ investigation	3	6
○ RCSA tools	1	12
○ risk notification	1	1
○ risk control assessment	3	7
○ SNC challenge	0	0
○ challenges	3	15
○ validation of SNC	1	2
○ SNC identification	0	0
○ document review	2	9
○ risk exposure	2	3
○ SNC Integration	0	0
○ Risk management division	2	5
○ SNC mitigation measures	0	0
○ corrective action	2	4
○ preventive action	2	6
○ rectification plan	2	4
○ SNC monitoring	0	0
○ review SNC	3	5

Moving to the reproduction phase, as observed in the continuous monitoring of *Sharī'ah* non-compliance events, involved routine assessments and measurements of potential risks. This entailed employing robust assessment tools such as RCSA and independent risk investigation to maintain awareness and undertake prompt mitigating actions. Lastly, institutionalization involved embedding risk mitigation practices into routine operations. This stage focused on developing effective measures to counter the identified *Sharī'ah* non-compliance risks, aiming for preventive, corrective, and rectification plans to address potential non-compliance events. Additionally, the ongoing enacting process of closely monitoring non-compliance risk exposures and the effectiveness of mitigation measures emphasized the importance of consistent surveillance. This constant vigilance ensured no resistance to risk-mitigating measures and allowed for updates to the *Sharī'ah* non-compliance risk management framework, validating potential risk exposures over time. Furthermore, the reproduction aspect extended to reporting these risk exposures to the BOD, *Sharī'ah* Committee, and senior management, ensuring comprehensive awareness among management, control functions, and business units. Initiatives such as the development of RCSA tools,

independent investigations, and risk notifications significantly contributed to enhancing the institutionalization of *Sharī'ah* governance practices within the *Sharī'ah* risk management function at EMERALD. This detailed analysis provides a clear understanding of the stages and activities involved in institutionalizing *Sharī'ah* governance practices within the *Sharī'ah* risk management function, demonstrating how these practices are encoded, enacted, reproduced, and institutionalized within EMERALD's operations.

6.1 FINDINGS AND DISCUSSION

The inception of EMERALD in Malaysia signifies a pivotal moment in the development of a robust *Islāmic* financial system within the country (Al Nasser and Muhammed, 2013). Establishing a bank operating within the *Islāmic* framework, however, poses inherent challenges. The early stages of EMERALD's establishment emphasized the crucial role of practitioners, their backgrounds, and philosophies in shaping product and service development (Kitamura, 2020). The commitment of the Malaysian government and Bank Negara Malaysia (BNM) as the regulator, particularly with the introduction of the Islamic Banking Act of 1983 (IBA 1983), significantly influenced the growth of *Islāmic* banking. Despite the regulatory foundation provided by the Act mandating formation of a *Sharī'ah* advisory council, it proved insufficient for efficient management, where the guidelines issued by the regulator- on *Sharī'ah* governance lacked specificity. In response, EMERALD appointed a *Sharī'ah* officer from the outset to ensure institutional reputation and distinguish *Islāmic* banking from conventional practices.

Interview data from EMERALD illustrated the evolution from SGF 2010 to SGPD 2019 and the institutionalization of *Sharī'ah* governance practices within the institution. EMERALD navigated complexities during this evolutionary process, implicitly strengthening *Sharī'ah* governance practices. Initially adopting a self-regulated system aligned with its conditions, EMERALD found the government-issued *Sharī'ah* principles overly general. Intense pressure from various stakeholders, including the public, *Sharī'ah* Committee, renowned scholars, institutional members, and regulators, led EMERALD to ensure *Sharī'ah* compliance across transactions, products, activities, and programs, over time.

TABLE 6
Part of the Cross-sectional Content Analysis for Codes under Theme 3 *Sharī'ah* Risk Management Function

Main Theme - <i>Sharī'ah</i> Risk Management Function							
	Sub theme -SNC integration	Sub theme - SNC identification	Sub theme - SNC assessment	Sub theme - SNC mitigation	Sub theme - SNC monitoring	Sub theme - SNC reporting	Sub theme - SNC challenge
Coded activities under each sub theme identified from data by HO <i>Sharī'ah</i> Risk Management Function	<i>Sharī'ah</i> non-compliance risk is actually part of opportunity risk. Opportunity risk is under the Risk Management Division. So, we work together under the same division. The difference is that we are responsible for <i>Sharī'ah</i> non-compliance risk.	In the EMERALD Annual Report, we report excessive events related to <i>Sharī'ah</i> issues that we have identified, along with the factors that caused these excessive risks.	So, we use the same tool as opportunity risk management to assess SNC events. In fact, <i>Sharī'ah</i> non-compliance risk is a subset of opportunity risk.	The rectification plan is to rectify the SNC events occurring in the bank's current operations. The SNC risk is actually the important thing that we need to identify because we want to mitigate the SNC risk.	Perhaps among other things, we can hold a town hall. The town hall is a training session that we hold with all branch managers to provide exposure to SNC events and risks. This is important so that monitoring of SNC events can be improved.	Previously, under SGF 2010, our reporting line went directly to the <i>Sharī'ah</i> committee. Under SGPD 2019, however, our reporting line goes directly to the management risk committee.	It is difficult to differentiate between opportunity risk events and SNC events. Because there are some scenarios where we feel that "this thing is indeed <i>Sharī'ah</i> , and it is also Opportunity risk", or vice versa.

TABLE 6 (continued)

Main Theme - <i>Sharī'ah</i> Risk Management Function							
	Sub theme - SNC integration	Sub theme - SNC identification	Sub theme - SNC assessment	Sub theme - SNC mitigation	Sub theme - SNC monitoring	Sub theme - SNC reporting	Sub theme - SNC challenge
Coded activities under each sub theme identified from data by <i>Sharī'ah</i> Risk Management Officer 1	<p>Whether under SGF 2010 or SGPD 2019, SNC risk is a subset of opportunity risk.</p> <p>When the organizational structure was changed under SGPD 2019, we were placed under the risk management division.</p> <p>We align our daily tasks or processes with operational risk.</p>	<p>We have <i>Sharī'ah</i>-compliant guidelines that we use to identify SNC risk or to determine whether a case in EMERALD is related to a <i>Sharī'ah</i> non-compliance event.</p>	<p>After the SNC event is identified, the next step is to control the SNC event so that the risk from this event can be reduced or mitigated. Therefore, the SNC event will go through the risk control self-assessment (RCSA) process to identify and evaluate the associated risk.</p>	<p>If a loss event from SNC has been identified, corrective and preventive actions must be implemented to ensure that the SNC risk that occurred does not happen again.</p>	<p>We conduct monthly monitoring and reporting of rectification progress.</p> <p>We keep track of the rectification progress in the bank every month, and it can sometimes take up to a year to resolve SNC events. This means that we keep track of the progress every month and then present on the progress to the <i>Sharī'ah</i> committee and the operational committee.</p>	<p>Initially, under SGF 2010, we had two reporting lines: we reported to the Chief Risk Officer and the Chief <i>Sharī'ah</i> Officer.</p> <p>However, after BNM issued SGPD 2019, we only report directly to the Chief Risk Officer.</p>	<p>When we find a risk or <i>Sharī'ah</i> issue, we will argue whether or not it is a <i>Sharī'ah</i> issue, because the requirement in the <i>Sharī'ah</i> division does not mention the related issue, and there is no internal precedent.</p> <p>Therefore, before we confirm it as SNC, if the issue is in doubt, we call for a meeting with the Head of Shariah, Head of SRM, Head of Audit, and Head of Shariah Compliance. They can constructively challenge that decision.</p>

TABLE 6 (continued)

Main Theme - <i>Sharī'ah</i> Risk Management Function							
	Sub theme - SNC integration	Sub theme - SNC identification	Sub theme - SNC assessment	Sub theme - SNC mitigation	Sub theme - SNC monitoring	Sub theme - SNC reporting	Sub theme - SNC challenge
Coded activities under each sub theme identified from data by <i>Sharī'ah</i> Risk Management Officer 2	<p>The requirements that the SNC risk management team uses to identify SNC risk are <i>Sharī'ah</i> requirements.</p> <p>The tools, procedures, and processes that the team uses, however, are the same as those used by the risk management division.</p>	One of the tools that the team uses is document review. The team reviews internal and external documents to identify potential SNC events.	Once the team has identified a potential SNC event, they conduct a risk control self-assessment (RCSA) to assess the SNC risk from the perspective of gaps. For example, if there is a loss event, the team will include the loss event or findings in the RCSA to identify ways to mitigate the risk.	Corrective actions are important to fix what is wrong. For example, if a customer has not signed the <i>aqad</i> form, the corrective action would be to call the customer to the bank to sign the form. This is one way to mitigate SNC risk.	We need to review the existing products and highlight the related risks based on the applicable guidelines. For example, from the <i>tawarru'</i> perspective, we need to highlight the risks associated with <i>tawarru'</i> for <i>Ar-Rahnu</i> . For example, non-execution of <i>tawarru'</i> commodity trading. This is when we do <i>tawarru'</i> , but we do not actually execute the <i>tawarru'</i> trading. This is not <i>Sharī'ah</i> - compliant. This is one of the ways we monitor bank products.	Based on the RCSA results, we will highlight the five major risks to present to the <i>Sharī'ah</i> Committee, top management, and board committee.	Not executing or, in other words, not following the procedures given for one's work process is also one of the challenges that can lead to SNC events.

6.1.1 INSTITUTIONALIZATION OF *SHARĪ'AH* RISK MANAGEMENT FUNCTION

Sharī'ah risk management, as one of EMERALD's internal control functions, systematically identifies, measures, monitors, and reports *Sharī'ah* non-compliance risks to manage potential events. The Head of Shariah risk management function highlighted the practice's existence since the issuance of GPS 1 in 2004, predating SGF 2010. Introduction of SGF 2010, however, prompted adjustments in the reporting structure. While EMERALD initially reported solely to the Chief Shariah Division, post-SGF 2010, it also reported to the Chief Risk Officer, introducing a dual reporting system. Despite SGF 2010 not explicitly outlining *Sharī'ah* risk management under the Shariah Division, this structure was already in place at EMERALD. With the issuance of SGPD 2019, all control functions, including *Sharī'ah* risk management, became independent. Consequently, institutionalization in EMERALD underwent organizational restructuring, relocating *Sharī'ah* risk management under the Chief Risk Officer.

The Head of Shariah risk management function interviewed revealed that before SGPD 2019, *Sharī'ah* risk management guidelines were integrated with operational risk management, merging as 60% of the *Sharī'ah* risk management guidelines resembled those of organizational risk management. Post-SGPD 2019, the guidelines were merged into a single tool for both *Sharī'ah* and operational risk management functions. EMERALD is effective in their risk management practices. Risk monitoring was the most significant process that affected the bank's risk management practices.

According to the Head of Shariah risk management function, “*Sharī'ah* non-compliance risk is now a part of Operational Risk, which is the reality, so when we merged, we use the same one tool only, which is the merged guideline to perform our function, either *Sharī'ah* or operational risk management. This merger is considered another new measure undertaken following the issuance of SGPD 2019.”

Sharī'ah risk management officer 1 further added that, “...except in executing the function, we have our own *Sharī'ah* requirement compulsory with a penalty to be complied with as per IFSA 2013.

The internal requirement from EMERALD's management itself is another factor that could influence the harmonization of *Sharī'ah* governance practices. Good corporate governance practices must be seamlessly incorporated into EMERALD. Meanwhile,

EMERALD members must maintain optimal governance practices to elevate the institution's image and sustainability. The Head of Shariah risk management function perceived that, "Sometimes when there is an issue on *Sharī'ah* matters, it is quite impossible to maintain the best corporate governance practices in terms of reporting the findings. So, there will be no independence in this case when the gap is closed without any further investigation. So, to harmonize the culture, EMERALD should restructure its *Sharī'ah* control function and the reporting line."

As the key performance indicators of *Sharī'ah* risk management team members are determined by the Shariah Division, the members were considered Shariah Division officers even before the issuance of SGF 2010 and should report to the Head of *Sharī'ah* division. Nevertheless, the *Sharī'ah* risk management officers, other control function *Sharī'ah* officers, and Shariah Division officers were 'stuck', as mentioned by Head of Shariah risk management function, when each time BNM questioned the independence of the *Sharī'ah* control function while reviewing the *Sharī'ah* process and suggested that EMERALD change the single reporting line into a double reporting line. In other words, the officers could not transition from a single to double reporting line given the harmonized practice and culture already in place, which allowed the Head of Shariah Division to easily monitor the *Sharī'ah* development progress. As the internal control functions (including *Sharī'ah* risk management function) are overseen by the Head of Shariah division, they may share their *Sharī'ah* knowledge, experiences, and technical skills in managing *Sharī'ah*-related matters, specifically *Sharī'ah* non-compliance issues. Head of Shariah risk management function deemed it unnecessary to report to the Chief Risk Officer of the Risk management division, as their functions emphasize operational risk management over the *Sharī'ah* risk management function. As the *Sharī'ah* control function, which includes *Sharī'ah* risk management function, at the same time, still requires reporting to the Head of the *Sharī'ah* division, this independence issue raised by BNM during the review process remained unresolved. Nonetheless, the 'stuck' situation was harmonized following BNM's issuance of SGPD 2019, where all the *Sharī'ah* control functions must be independent of the Shariah Division with a single reporting line.

Ensuring the competency of *Sharī'ah* professionals is imperative for the effective passage and execution of *Sharī'ah* judgments and assessments during the evolution of *Sharī'ah* governance practices. The professional application of *Sharī'ah*

knowledge, skills, and experiences forms the cornerstone of successful *Sharī'ah* governance practices within EMERALD. Notably, individuals involved in the Shariah Division and control functions must embody knowledge, qualifications, and experience to adeptly address *Sharī'ah*-related issues. According to the General Manager in EMERALD, the head of any *Sharī'ah*-focused function should serve as the "river of knowledge." This emphasizes accountability in managing and deciding upon *Sharī'ah* matters based on one's *Sharī'ah* expertise. *Sharī'ah* competency is seen as reflective of EMERALD's image, and any deficiency in managing *Sharī'ah* matters could adversely impact the institutionalization of *Sharī'ah* governance practices.

Nevertheless, it is highlighted that having qualifications in *Sharī'ah* alone does not guarantee competency in the *Sharī'ah* risk management function. Previously, under SGF 2010, minimal qualifications for *Sharī'ah* risk management officers were unspecified, leading to challenges for newcomers in understanding their tasks. The current SGPD 2019 mandates that risk officers involved in *Sharī'ah* risk management must possess knowledge of *Sharī'ah* requirements applicable to *Islāmic* financial businesses. Initiative and independent learning are crucial for *Sharī'ah* competency. Emphasizing the importance of self-driven learning, the *Sharī'ah* risk management officer 1 and 2 mentioned that they underwent a one-year training program focusing on Professional Shariah Auditor certification, which included modules on *Sharī'ah* risk management. Training becomes a key avenue for gaining knowledge, exposure, and enhancing *Sharī'ah* competency, preventing deviations from *aqad* (contractual agreements). Both of the *Sharī'ah* risk management officers emphasized the importance of continuous learning and the sharing of knowledge among the Heads of Shariah control function and Branch management. Challenges and resistance are acknowledged, especially in instances where non-Muslim individuals are appointed as superiors. Adherence to BNM requirements, even when faced with challenges, however, is deemed necessary for the institution to maintain *Sharī'ah* governance practices.

Competency in *Sharī'ah*-related matters is not just limited to qualifications; it extends to the capability of the Head of Shariah risk management and the *Sharī'ah* risk management officers to perform the institutionalization of *Sharī'ah* governance practices in the control functions effectively. EMERALD's commitment to *Sharī'ah* competency has been sustained since its inception. However,

challenges arose during the implementation of double reporting for control functions after SGF 2010, especially when a non-Muslim Chief Risk Officer was appointed. The competency of this non-Muslim Chief Risk Officer was initially lacking, leading to divergence from managerial requirements. Subsequent Chief Risk Officer, also non-Muslim, sought guidance from *Sharī'ah* professionals, indicating a shift toward developing competence to handle *Sharī'ah* matters.

The *Sharī'ah* risk management officer 1 perceives EMERALD to be secure, citing the latest Chief Risk Officer's development of competence through guidance from *Sharī'ah* professionals. This emphasizes the importance of leadership competence in ensuring continuous improvement in *Sharī'ah* compliance culture and the mitigation of *Sharī'ah* non-compliance events. Despite religious differences, the Chief Risk Officer's commitment to learning and collaboration with *Sharī'ah* professionals highlights EMERALD's ability to navigate and enhance the evolution of *Sharī'ah* governance practices.

Sharī'ah risk management officer 2 mentioned a few examples of the translation of routines into rules or the transformation of existing rules or routines into new rules or routines in *Sharī'ah* risk management. The first example entails the Potential *Sharī'ah* Issue term.

As the *Sharī'ah* risk management officer 2 explained, "Potential *Sharī'ah* Issue is not stated or required under SGPD 2019. We only have Potential *Sharī'ah* non-compliance events and Actual *Sharī'ah* non-compliance event terms only. But, it is common for us in the *Sharī'ah* risk management function to determine the Potential *Sharī'ah* non-compliance event term since the issuance of the SGF 2010. And until now, after the issuance of the SGPD 2019, we try to embed this routine of determining Potential *Sharī'ah* non-compliance event terms into our *Sharī'ah* risk assessment work process in *Sharī'ah* risk management. The term is now being used as one of the guidelines in our *Sharī'ah* risk management policy". He added that, "The term is not used in SGPD 2019 and not in other *Islāmic* banks, but exclusively used in EMERALD, which is validated by us (*Sharī'ah* risk management)."

Changes in the process or procedure to execute certain tasks depends on either the internal requirement in EMERALD itself or external requirement, typically by the regulatory body of BNM. Other divisions or control functions could similarly influence the transformation of existing rules or routines into new ones. Based on an interview with *Sharī'ah* risk management officer 1, identifying a

new risk in the *Sharī'ah* division or other control functions necessitates a new procedure in *Sharī'ah* risk assessment. Occasionally, the documentation itself needs to be updated. This internal process only requires approval from either the Head of *Sharī'ah* risk management function or the Chief Risk Officer.

Another example addressed by *Sharī'ah* risk management officer 2, "...is when we make a plan for next year". This annual planning, which is not reflected in any *Sharī'ah* risk management guideline or EMERALD policy, served to review the *Sharī'ah* contract policy document. New risks were identified and included under the Risk and Control Self-Assessment (RCSA) result following this review. Despite not being a requirement by GPS 1 2004, SGF 2010, or SGPD 2019, the *Sharī'ah* risk management in EMERALD has executed this yearly planning.

How routines within *Sharī'ah* risk management are translated or transformed into new rules or procedures (institutionalization) was highlighted during the interview. One such instance is the incorporation of the term "Potential *Sharī'ah* non-compliance event," a step introduced by the *Sharī'ah* risk management function to assess whether a loss event or *Sharī'ah* risk may potentially lead to *Sharī'ah* non-compliance. Although not explicitly outlined in SGPD 2019 or other *Islāmic* financial standards, this term has been embedded into EMERALD's *Sharī'ah* risk assessment process since SGF 2010, now an integral part of their *Sharī'ah* risk management policy. The use of this term, exclusively within EMERALD, is validated and utilized by the *Sharī'ah* risk management team despite its absence in standard regulations. Transformations in procedures are influenced by both internal demands within EMERALD and external requirements, particularly stipulations from regulatory bodies such as BNM. *Sharī'ah* risk assessments are often adapted or updated in response to identification of new risks within the *Sharī'ah* division or other control functions, requiring revised procedures and documentation.

Annual planning, another uncodified practice, serves EMERALD in reviewing the *Sharī'ah* contract policy document and identifying new risks for inclusion in the Risk and Control Self-Assessment (RCSA) results. Despite lacking specific mandates from regulatory frameworks such as GPS 1 2004, SGF 2010, or SGPD 2019, EMERALD has consistently executed this yearly planning initiative as part of its *Sharī'ah* risk management practices. Regarding product introduction or enhancement, EMERALD maintains its workflow and standard operating procedures without changes. Each product, however, undergoes a rigorous assessment for potential risks,

especially related to *Sharī'ah* compliance. Strict control measures are enforced until the products meet *Sharī'ah* requirements and are deemed suitable for the market. This practice ensures a high level of control over products to prevent *Sharī'ah* non-compliance issues.

7. CONCLUSION

The journey of EMERALD, in a Malaysian *Islāmic* financial landscape, serves as a compelling case study in the evolution of *Sharī'ah* governance practices. From its inception, EMERALD faced the challenge of establishing an *Islāmic* bank operating within the *Sharī'ah* framework and navigating the nuances of compliance. The commitment of the Malaysian government and BNM as a regulator, evident in the IBA 1983, laid the foundation for *Islāmic* banking's growth, but the generic guidance provided by the Act underlined the need for more specific *Sharī'ah* governance practices. EMERALD's response to this challenge was marked by a self-regulated system, adapting *Sharī'ah* principles from government-issued guidelines. As the institution evolved, however, so did the complexities it encountered, leading to a more robust approach to *Sharī'ah* governance. Pressure from various stakeholders, including the public, *Sharī'ah* Committee, scholars, and regulators, played a pivotal role in driving EMERALD toward a more comprehensive *Sharī'ah* compliance approach. A crucial component of this evolution was the institutionalization of *Sharī'ah* risk management, a control function aimed at identifying, measuring, monitoring, and reporting *Sharī'ah* non-compliance risks.

In EMERALD, the *Sharī'ah* risk management function was not a mere response to regulatory requirements; it existed even before the issuance of SGF 2010. This early adoption positioned EMERALD uniquely but presented challenges during regulatory reviews. The subsequent issuance of SGPD 2019 triggered a restructuring, aligning the *Sharī'ah* risk management function with the Risk Management Division. The integration of *Sharī'ah* risk management with operational risk management, as guided by SGPD 2019, exemplifies EMERALD's commitment to effective risk mitigation. The use of ORION, a reporting system detailing regulation under SGF 2010, IFSA 2013, and SGPD 2019, emphasizes the meticulous approach to compliance. The institutionalization journey, however, faced challenges during leadership transitions. Nevertheless, proactive measures, including training, guidance-seeking, and ensuring the competence of control function heads, demonstrated EMERALD's

dedication to maintaining *Sharī'ah* governance standards.

The EMERALD case study offers valuable insights into the institutionalization of *Sharī'ah* governance practices. To further enhance *Sharī'ah* compliance and risk management, to comply with the dynamic nature of *Sharī'ah* governance practices, regular training programs for *Sharī'ah* officers and control function heads should be conducted. These programs should focus on emerging *Sharī'ah* requirements, risk management methodologies, and evolving regulatory frameworks. Establishing clear and standardized qualifications and competencies for *Sharī'ah* risk management officers besides aligning these qualifications with the specific requirements of the *Sharī'ah* risk management function are essential to ensure a consistent and competent approach to *Sharī'ah* compliance. Awareness of the pivotal role of leadership in the institutionalization process by providing specialized training and mentorship programs is also important to ensure a deep understanding of *Sharī'ah* requirements and effective *Sharī'ah* governance practices. Technological advancements also need to be utilized to streamline *Sharī'ah* risk management processes. Implementing advanced risk assessment tools, automated reporting systems, and digital platforms can enhance efficiency and accuracy in managing *Sharī'ah* non-compliance risks. And lastly, periodically reviewing *Sharī'ah* governance practices is desirable, and in line with regulatory changes and emerging industry standards. This is vital to ensure that EMERALD remains at the forefront of *Sharī'ah* compliance and adapts swiftly to evolving requirements.

Nevertheless, generalizability was identified as one of the single case study's limitations. The study outcomes may not be generalizable to other *Islāmic* banks with similar intricacies, size, and operational activities. Another limitation is on *Sharī'ah* officers' skills gap in routinization of rules. This is because routinization requires a strong understanding in *Sharī'ah*. This study might not be relevant to *Islāmic* banks in other countries because of different regulations and standards used. The last limitation to consider in this study is the lack of existing research that applies the Burns and Scapens (2000) framework to the context of *Islāmic* studies, where it shows the lack of references related to institutionalization in *Sharī'ah* governance practices.

In conclusion, EMERALD's journey provides a rich tapestry of experiences in institutionalizing *Sharī'ah* governance practices. By embracing these recommendations, EMERALD can continue to serve as a benchmark for IFIs, contributing to the broader evolution of

Sharī'ah governance in the dynamic *Islāmic* banking landscape. Future research based on the findings and insights gleaned from the analysis of EMERALD's *Sharī'ah* governance practices could be done by conducting a comparative study of *Sharī'ah* governance institutionalization in various IFIs as well as analyzing how different institutions approach the institutionalization of *Sharī'ah* governance practices, considering variations in size, geographical location, and regulatory frameworks. By addressing these research areas, scholars and practitioners can contribute to a deeper understanding of the dynamics, challenges, and innovations in *Sharī'ah* governance, fostering continuous improvement in IFIs. By pursuing research along these lines, scholars can contribute significantly to the ongoing evolution and enhancement of *Sharī'ah* governance practices in IFIs.

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