Developing a Corporate Governance Disclosure Index for Islamic Financial Institutions

Norakma Abd Majid[1]
Maliah Sulaiman[2]
Noraini Mohd Ariffin[3]

Despite the heightened discussion on the importance of good governance in the development of Islamic Financial Institutions (IFIs), the type of governance indicators that may be applied to IFIs has rarely being discussed. More importantly, the need to measure the quality of corporate governance (CG) using a disclosure index is undeniably pertinent. Accordingly, this study attempts to develop a CG disclosure index from a stewardship perspective for IFIs. Specifically, the disclosure index is developed using the guidelines issued by the Central Bank of Malaysia (BNM), the standards on CG promulgated by the Accounting and Auditing Organization of Islamic Financial Institutions (AAOIFI) and the framework introduced by the Islamic Financial Services Board (IFSB). The comprehensive index developed in this study highlights a "best practice" model of CG disclosure for IFIs.

Keyword(s): corporate governance quality, index disclosures, Islamic Financial Institutions.

1 Introduction

The uniqueness of Islamic banking brings about a number of interesting features in the governance structure of Islamic financial institutions (IFIs) since equity participation, risk and profit-and-loss sharing (PLS) arrangements formed the basis in its financing system. Consequently, IFIs is deemed to have an extremely high level of accountability in order to protect the rights of its stakeholders. This poses an important challenge for IFIs to improve on all the crucial aspects of its corporate governance (CG) (Chapra, 2007: 338). The aim of CG in IFIs is primarily to increase corporate accountability by broadening the scope of disclosure beyond a financial focus. This is to ensure that the rights of an array of stakeholders are met. Given that the annual report is a tool where management communicates firm performance and governance matters to stakeholders (Healy and Palepu, 2001), in discharging its accountability, IFIs should specifically include governance related information in their annual reports.

More importantly, issues concerning CG of IFIs need to be aligned with matters concerning the PLS system. The application of the PLS system in IFIs create a complex accountability framework which would attract special scrutiny from its stakeholders. Essentially what this means is the need for IFIs to have a better *Shariah* compliance structure.

[1] Email: norakma.amajid@gmail.com Department of Accounting and Finance, Faculty of Management and Economics Universiti Malaysia Terengganu, 21030 Kuala Terengganu, Malaysia
[2] Corresponding author: Email: maliah@iium.edu.my, Department of Accounting, Kulliyyah of Economics and Management Sciences
International Islamic University Malaysia Jalan Gombak, 53100 Kuala Lumpur, Malaysia
[3] Email: norainima@iium.edu.my, Department of Accounting, Kulliyyah of Economics and Management Sciences International Islamic University Malaysia, Jalan Gombak, 53100 Kuala Lumpur, Malaysia

Theoretically, high CG quality is dependent on the competence and integrity of the decision makers in IFIs. Subsequently, this will strengthen the trust stakeholders have in IFIs. This will then ensure its sustainability. More significantly, CG quality of IFIs provides a benchmark that can be used to differentiate each IFI. To determine CG quality of IFIs, a CGD index is pertinent. Essentially, our study contributes to the existing literature on CG and IFIs in that it establishes a "best practice" code tailored specifically for IFIs. The index was developed by consolidating 3 guidelines/standards issued by the Central Bank of Malaysia (BNM), the Islamic Financial Services Board (IFSB) and the Accounting and Auditing Organization of Islamic Financial Institutions (AAOIFI). This would greatly enhance the governance structure of the Islamic banking industry and subsequently ensuring its sustainability. The rest of the paper is organized as follows. The following section discusses corporate governance in IFIs while section 3 focuses on the 3 guidelines used to develop the CGD index namely, the "Guidelines on Corporate Governance for Licensed Islamic Bank" (GP1-i) issued by the Central Bank of Malaysia (BNM), the "Guiding Principles on Corporate Governance for Institutions Offering Only Islamic Financial Services (IFSB-3) issued by the Islamic Financial Services Board and the "Governance Standards for Islamic Financial Institutions" or (GSIFI) issued by the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). Section 4 describes the development of the index while section 5 concludes.

2 Corporate governance and Islamic financial institutions (IFIs)

Corporate governance (CG), broadly defined, is a set of processes, policies and laws affecting the way an organization is directed, administered and controlled. Bansuch, Pate and Thies (2008) defined CG as a set of formalised values and procedures implemented by the owners, directors and the management of the business in its various operations as well as its interactions with stakeholders. Holder-Webb, Cohen, Nath and Wood, (2008) defined CG as the provision of effective boards, strong shareholder rights, and broad disclosures in managing a business. From the perspective of IFIs, governance specifically addresses issues pertaining to the role and conduct of the *Shariah* Supervisory Boards (SSB). More specifically, CG of IFIs should include the following:

i. Safeguarding interests of Investment Account Holders
ii. Compliance with the *Shariah*
iii. Governance and risk management of *Mudarabah* and *Musharakah* contracts and
iv. Establishment of a comprehensive CG framework articulating the fiduciary responsibilities of the board and senior management.

A focus on all the above will lead to an improvement in the level of trust and confidence in the Islamic finance industry (Iqbal and Greuning, 2008). More importantly, AAOIFI claims that strong governance practices will win public confidence and thereby promote trust amongst their equity holders, investors and other parties dealing with them. Subsequently, this would enhance *Shariah* compliance.

In order to examine if indeed there exists differences between CG of IFIs and other organizations, it is important to understand what are the unique characteristics of IFIs in the first place. The uniqueness of IFIs emanates from its fundamental principle to conduct its operations in accordance with Islamic *Shariah*, the primary issue being the prohibition of the receipt and payment of *riba* (interest). A pre-determined fixed rate of return on capital where one party bears the risk while the other party receives a reward irrespective of the outcome of the use of the borrowed amount would mean an uneven distribution of risk and reward in the transaction. More importantly, *riba* also leads to the concentration of wealth by transferring wealth from the poor to the rich. This is primarily why *riba* is prohibited. The alternative to avoid dealing with interest is the various forms of profit-sharing contracts that are peculiar to Islamic banking. These contracts are said to enhance justice and equitable distribution of profits and risks in investment (Bashir, 1984).

Given these unique characteristics of IFIs, one question that may be raised is: How do we ensure that IFIs are actually discharging its accountability satisfactorily? Additionally, how do we determine the quality of CG information disclosed by IFIs? The use of self-developed indices to determine disclosure quality has been commonly used in prior studies examining the quality of environmental and corporate social responsibility disclosure. Similarly, an index may also help researchers determine the quality of CG information disclosed by IFIs. A disclosure index is defined as "a qualitative based instrument designed to measure a series of items which, when the scores for the items are aggregated, gives a surrogate score indicative of the level of disclosure in the specific context for which the index was devised" (Hooks, Coy and Davey, 2002: 38).

Thus, in the context of this study, the Guidelines-based checklist of the index was developed to arrive at the overall rate of the IFI's corporate governance quality. The development of the index as a proxy for governance quality is in line with prior studies (e.g., Hamid and Sigit, 2005; Hassan and Christopher, 2005; Qu and Leung, 2006; Parsa, Chong, and Isimoya, 2007 and Florou and Galarniotis, 2007). The derivation of the governance items in the index are centered on the suggestions of 'best practices' that are commonly referred to within the sphere of governance disclosure measurement debate. The focus of this study is specifically on IFIs.

The establishment of best practice codes, tailored specifically to IFIs, would help the Islamic financial industry to improve its governance structures and procedures. There are several regulatory bodies that promulgate governance guidelines and standards to encourage the disclosure by IFIs of CG related information. Such bodies include the Central Bank of Malaysia (BNM), the Islamic Financial Services Board (IFSB) and the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). With an introduction of the codes from these bodies, good governance practices in IFIs would be fairly simple to design and the likely cost to implement them would also be low.

3 The "Guidelines"

As mentioned earlier, the comprehensive CGD index is derived from three prominent guidelines/standards. These are:

(1) The "Guidelines on Corporate Governance for Licensed Islamic Banks", known as GP1-i issued by BNM in 2007 (the extended version of GP1 in 2005),

(2) The "Guiding Principles on Corporate Governance for Institutions Offering Only Islamic Financial Services (Excluding Islamic Insurance (Takaful) Institutions and Islamic Mutual Funds)" or IFSB-3 issued by IFSB in 2006, and

(3) The "Governance Standard for Islamic Financial Institutions" or GSIFI nos. 1 to 6 issued by AAOIFI in 2008.

The choice to base the index on these three (3) guidelines is made because it effectively encapsulates all of the governance disclosure envisaged for IFIs. The first source, issued by the Central Bank of Malaysia, dictates the main reference source to form the checklist of governance disclosure. It was thought to be a reasonable starting point to refer to as it contains the governance items disclosure requirements, which are applied to all licensed IFIs in Malaysia. While the second and third referred guidelines form the basis for identifying other governance items that are not covered and sometimes overlap with that recommended in the first.

For our purpose, the Guidelines on Corporate Governance for Licensed Islamic Banks (BNM/ GP1-i) is regarded as a primary reference in the development of the CGD Index used in this study, while the other two (IFSB/ IFSB-3 and GSIFI/ AAOIFI) are complimentary sources of input for the index. Details of each guideline are discussed in the following sub-sections.

GP1-i

According to the Central Bank of Malaysia (BNM, 2007: 1), all banks in Malaysia need to observe the recommendations stated in the "Guidelines on Corporate Governance for Licensed Islamic Banks", also known as GP1-i, since this initiative is to encourage the adoption of effective and high standards of corporate governance practices by Islamic banks and Islamic bank holding companies.The Guidelines are divided into three sections consisting of broad principles of CG, the minimum standards and the specific requirements for sound CG. It covers several important sections of board matters, management oversight, accountability and audit and transparency. For the purpose of developing the CGD Index, this study has focused on the minimum components of CG disclosure, which are laid down in Principle 13 and listed in Paragraph 2.110 of the Guidelines. The Paragraph forms an essential part in the CG indicators used for this study. It comprises eleven (11) dimensions; *Board as a whole* (renamed as *Board structure and functioning* in the index), *Nominating Committee, Remuneration Committee, Risk Management Committee, Audit Committee, Shariah Committee, Risk Management, Internal Audit and Control Activities, Related Party Transactions, Management Reports and Non-Adherence to Guidelines.* In reference to these dimensions, this study summarises its requirements relating to governance matters in Column 1 in Appendix I.

A thorough examination of the Guidelines reveals that it used a well-known definition of CG by the OECD (revised April 2004), in its Paragraph 1.04. Specifically, CG is defined as a process and structure used to direct and manage the business and affairs of the institution towards enhancing business prosperity and corporate accountability with the ultimate objective of realising long-term shareholders value, whilst taking into account the interests of other stakeholders. Thus, the meaning denotes that the guidelines attempt to govern the relationships between the institution's management who are responsible to set the direction and manage the business, the boards whose accountability is to strategically actualise the purpose of existence of an institution for the benefit of all –the shareholders who contribute the resources and other stakeholders.

The Guidelines on CG for Licensed Islamic banks (BNM/ GP1-i) is an extension of the "Guidelines on CG for licensed institutions" (BNM/ GP1) issued in 2005. The Guidelines were issued in September 2007 and incorporate the unique features of IFIs. Moreover, the focus of the subsequent publication was to provide an increasingly comprehensive set of CG guidelines, rather than to revise prior guidelines. The peculiarities of IFIs have been recognised in the newer CG Guidelines issued by the BNM in 2007. The comparison of BNM/ GP1 to BNM/ GP1-i indicated that the latter provides extra dimensions to cater for the specificity of IFIs. The results of the review are tabulated in Table 1 as follows:

Table 1
The differences between BNM/ GP1 and BNM/ GP1-i

Feature	Clauses in BNM/GP1	Clauses in BNM/ GP1-i
1	The usage of the term “licensed institutions” throughout the Guideline (**Para. 1.01**).	The term “licensed institutions” is replaced by “licensed Islamic Bank”, which is used throughout the Guideline (**Para. 1.01**).
2	The definition of Bank Holding Company, Financial Holding Company and Licensed Institutions provided by Banking Financial Act 1989 (BAFIA) are included in the Guideline (**Para. 1.01**).	No definition of such institutions or company in the Guidelines since there is no provision to define such issues in the Islamic Banking Act 1983 (IBA).
3	The guidelines should be read together with Banking Financial Act 1989 (BAFIA), the Companies Act 1965 and other relevant regulations, guidelines or circulars relating to CG that BNM may issue from time to time (**Para. 1.08**).	The guidelines should be read together with Islamic Banking Act 1983 (IBA), the Companies Act 1965 and other relevant regulations, guidelines or circulars relating to CG that BNM may issue from time to time (**Para. 1.08**).
4	The applicability of the guideline is for; - Licensed institutions - Bank Holding Company and Financial Holding Company (**Para. 1.09**).	The applicability of the guideline is for; - Islamic bank licensed under Islamic Banking Act 1983 (Excluding International Islamic Bank). - Islamic Bank Holding Company (**Para. 1.09**).
5	From a legal perspective, these guidelines are issued pursuant to section 56, 57 and 126 of the Banking Financial Act 1989 (BAFIA) (**Para. 1.13**).	From a legal perspective, these guidelines are issued in pursuant to section 53A of the IBA 1983 (**Para. 1.13**).
6	The guidelines outlines nine (9) major responsibilities of the board of Licensed institutions (**Para 2.10**).	Addressing the specificity in Licensed Islamic banks, another two (2) additional clauses are added to the responsibilities of the board. The additions of the board’s responsibilities are stated in: **Para 2.10 (vi)**: to institute comprehensive policies, processes and infrastructure to ensure *Shariah* compliance in all aspects of the Islamic bank’s operations, products and activities. **Para 2.10 (ix)**: to ensure protection of the interest of the depositors, particularly investment account holders (IAHs).
7	The board committee consists of four (4) committees (of Nominating committee, Remuneration committee, Risk management committee and Audit committee) (**Para 2.18**).	On top of the four committees listed in GP1 Guidelines, the Guidelines require the establishment of a *Shariah* committee to assist the board (**Para 2.19**).

With reference to Table 1 above, the last two identified extra features are significant to this study. By referring to feature no. 6, the BNM/ GP1-i specifically mentions the two (2) additional responsibilities on top of the nine (9) listed in the previous Guidelines (BNM/ GP1). In particular, the Guidelines require the board to give due consideration relating to *Shariah* compliance matters in all aspects of IFIs’ operations, products and activities. The Guidelines also specify that the responsibility of the board is to ensure the protection of the interests of depositors, especially investment account holders (IAH) in IFIs. Another is feature no. 7 where the Guidelines require a special committee to assist the board in administering the IFIs, with the suggestion to establish a *Shariah* committee.

Following this development, the CGD Index used in this study, to surrogate as a governance indicator in IFIs, acknowledges the specific issues highlighted by BNM's guidelines to capture three items of: (1) *Shariah* compliance, (2) Customers or IAHs, and (3) *Shariah* Committee to become specific governance disclosures in IFIs. For analysis purposes, the finding of no existence on these specific governance dimensions: *Shariah* Committee (D6), Customers/IAHs (D12) and *Shariah* compliance (D14) among these IFIs would likely signal that there is room for improvement for the IFIs to undertake the suggestion to incorporate the unique features of themselves. However, the finding of its existence signals the capability of the banks to both meet the economic objectives and to provide a decision making process that incorporates non-economic factors, such as fairness and equality as suggested in Islamic values, thus promoting the trust from stakeholders in the decisions undertaken by them.

In developing the index, we have also included the guidelines issued by the IFSB (refer to Column 2 in Appendix I) and AAOIFI (refer to Column 3 in Appendix I). These are discussed next.

IFSB-3

The IFSB issued the "Guiding Principles on Corporate Governance for Institutions Offering Only Islamic Financial Services (Excluding Islamic Insurance (Takaful) Institutions and Islamic Mutual Funds, IFSB-3)" in 2006. The Guidelines specially focus on 2 (two) areas that are unique to IFIs; namely, the protection of investment account holders (IAHs) and compliance issues in IFIs that relate to *Shariah* rules and principles. IFSB-3 consists of two (2) parts: the Guiding principles (GP) and the Rationale and Objectives of the principles (RO). Its GP consists of seven (7) principles assigned into four (4) major parts: general governance approach of IFIs; rights of investment account holders (IAH); compliance with Islamic *Shariah* rules and principles and transparency of financial reporting in respect of investment accounts. The purpose of the Guidelines is to strengthen the corporate governance of IFIs, which complements the existing international corporate governance standards set by the Organization for Economic Co-operation and Development (OECD), and the Basel Committee on Banking Supervision (BCBS). The extracts of the requirements set by this organization is summarised in Column 2 in Appendix I. One governance mechanism, which is unique to IFSB (2006), is the recommendation for BODs to establish a governance committee (GC). The following is the rationale set by the guidelines for the establishment of a governance committee in IFIs;

"GC whose functions are distinctly different from a conventional audit committee is made particularly because IFIs operate investment accounts which are not in the form of debt contract (as in the case of conventional fixed deposits), thus raising governance issues which have so far been overlooked. Conceptually, Mudharib in the investment account contract comprises both the IFIs' management and shareholders, not alone the management".

Additionally,

"the significance of investment accounts as a source of funds for IFIs, and the unique fiduciary duties that come with them under the principle of Mudharabah, certainly merits the establishment of a special organ of governance such as the GC" (IFSB-3:18).

According to IFSB-3, the minimum number of members in the GC is three. The GC should include a member of the audit committee (AC); a *Shariah* scholar preferably appointed among the IFIs' *Shariah* supervisory board (SSB) and a non-executive director (NED). The guidelines also require that any increment in the GC membership should be filled by independent non-executive directors (INEDs).The GC is to work closely with the management, the AC and the SSB to coordinate, oversee and monitor the implementation of the governance policy framework and to periodically report to the BODs of findings and recommendations resulting from the functions delegated to the GC. The establishment of the GC is, to some extent, complementary to other governance mechanisms. Its existence brings about the effectiveness of the AC since the tasks performed by GC may lighten the demanding mandate placed on the AC. It is also a complementary governance organ in the sense that should there be conflicts of interest between shareholders and the IAHs (especially when the funds are commingled), it is then necessary to establish a special committee to reconcile the needs of these two main contributors of funds. Accordingly, the role of the GC becomes pertinent. While the AC deals with interest of shareholders, the GC stands to safeguard the interest of IAHs. Such an arrangement is expected to help both the AC and the GC to have a clear and focused scope of responsibilities, thus reducing any ambiguity that may arise.

GSIFI

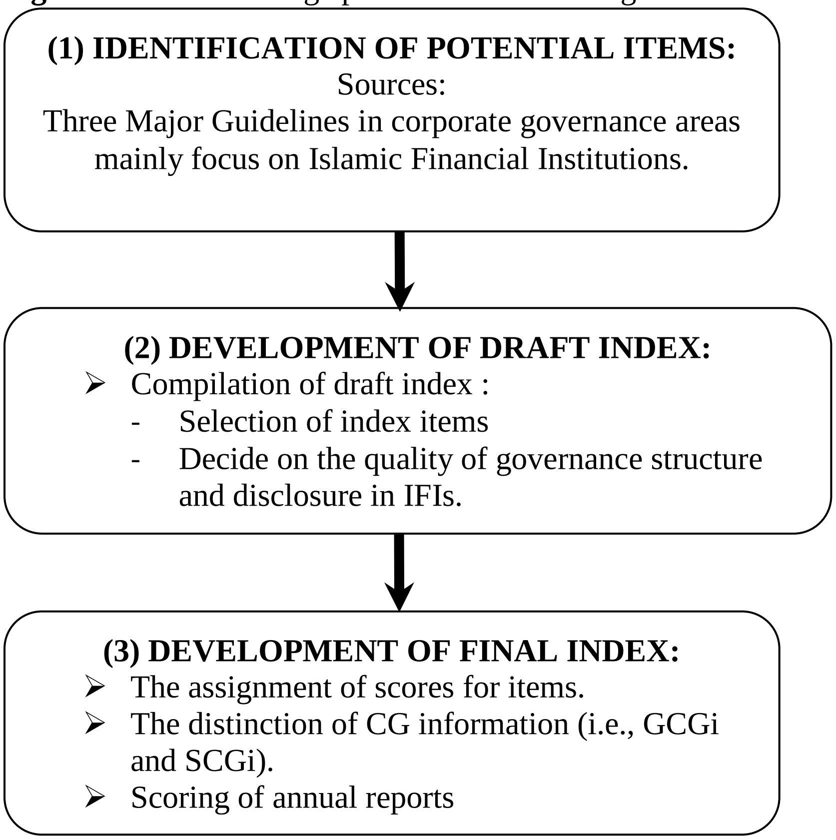
The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), established in 1991, issued "Governance Standards for Islamic Financial Institutions (GSIFI)" in 2008. Altogether AAOIFI issued six (6) standards addressing governance matters. These are GS1 on *Shariah* Supervisory Board, GS2 on *Shariah* review, GS3 on Internal *Shariah* review, GS4 on Audit and governance committee, GS5 on independence of *Shariah* supervisory board, and GS6 on Statement of governance principles. All the six standards will be examined in developing the index.

4 Developing the index

As indicated earlier, the three (3) Guidelines above were chosen because these guidelines effectively encapsulate all of the governance disclosure envisaged for IFIs. GP1-i issued by the Central Bank of Malaysia, dictates the main disclosure requirements applied to all licensed IFIs in Malaysia while the second and third were the basis in identifying other items which are not covered in the first. In developing the CGD index, we have used stewardship theory. Essentially, the stewardship model advocates that managers are persons of trust and that they will act in the best interests of the principal (Mills and Keast, 2009). On this basis, one can conclude that the steward will always strive for enhanced performance and this will become the intrinsic long term non-financial objective of a steward (Gupta and Parua, 2006). Thus, as stewards, managers of IFIs are motivated to work towards achieving the "best practice" model of CG disclosure. Accordingly, IFIs will incorporate the governance attributes that maximizes returns as well as other relevant non-financial attributes.

The themes in the index were determined based upon the suggestions in the Guidelines. It has been summarised into 14 main dimensions, with 123 sub-items, as presented in Table 2. The index is crafted to suit the accountability issues of IFIs that are pertinent to discharge the steward's obligations. For this reason the CGD Index is divided into 2 themes; general-governance related information (i.e., 10 dimensions) and specific-governance related information (i.e., 4 dimensions). These parameters are expected to be disclosed in the corporate governance section or elsewhere in the annual report of IFIs. All these recommendations made by AAOIFI and IFSB are reconciled with those suggested by the Central Bank of Malaysia. Any redundancies are merged to become an item while unique items of IFIs stand as new items in the index. The reconciliation process between these Guidelines to become a comprehensive CGD Index is detailed in the next part. The process of the construction of the disclosure index is presented in Figure 1 below.

Figure 1: The three-stage process in constructing the CGD Index.



As illustrated, there were three phases in the construction of the CGD Index for this study.
*Phase 1:*Identification of potential items made in reference to the recommendations in the three (3) major Guidelines; GP1-i (2007), IFSB-3 (2006) and GSIFI (2008).

The approach we have taken here (that is to select the items for the index from the three Guidelines) is to limit and focus on governance regulations meant specifically for IFIs. This, however, constitutes a limitation of the current study as it will restrict the opportunity to seek other useful recommendations that may come from alternative sources, including company laws and the Bursa Malaysia Listing Requirements, which might be applicable in the context of IFIs. This inherent limitation is a concern of prior studies as well (see Florou and Galarniotis, 2007).

The selection of potential items for the governance disclosure index starts with a list of items of CG information drawn from the suggestions of the GP1-i. In addition, a careful review of two other guidelines (i.e., IFSB-3 and GSIFI) was undertaken to select items of CG information not included in the checklist of the GP1-i. There is no theory to provide specific guidance on the inclusion of the items in a governance quality index (Florou and Galarniotis, 2007: 982). Therefore, consistent with Florou and Galarniotis (2007), the current study uses the same approach and only includes governance items that can be verified through annual reports in the CGD Index. Adherence to the rule will disqualify certain non-observable elements to become part of the developed index. The results of the independent review of each Guideline are presented in Table 2.

Phase 2: Development of the draft index.

The initial process of drafting the index begins with the examination for quantifiable governance items in all three guidelines. This process led to the inclusion of 147 items of CG disclosure items in the initial list: 79 items from the GP1-i checklist, 49 items from the GSIFI checklist and 29 items from the IFSB-3 checklist. As the relevant literature shows that there is no commonly used theory to determine the number of items in the disclosure index (Hooks, Coy and Davey, 2002: 43; Florou and Galarniotis, 2007: 982), this study assumes that neither rules nor restrictions are imposed on the amount of governance items in the index. Accordingly, all the recommendations from the selected standards that are quantifiable from annual reports are listed at this stage. It is regarded as an advantage to include a range of 29 items (IFSB-3) to 79 items (GP1-i), as this is deemed appropriate to discharge the accountability of banks,which have a wide range of stakeholders. Therefore, without taking an approach to direct at any specific stakeholder group, an extensive list of items is favoured to cater for the needs of the wide-ranging users in IFIs.

Table 2

The Draft Index: Themes of CG Disclosures laid down in GP1-I, IFSB-3 and GSIFI.

Dimension	**Governance Disclosures Theme**	**GP1-i**	**IFSB-3**	**GSIFI**
1	Board structure and functioning	√(19)		√(7)
2	Nominating committee	√(8)		
3	Remuneration committee	√(7)		√(2)
4	Risk management committee	√(8)		
5	Audit committee/Audit and governance committee	√(9)	√(9)	√(6)
6	*Shariah* committee/*Shariah* Supervisory Board	√(8)	√(1)	√(13)
7	Risk management	√(9)		√(2)
8	Internal audit and control	√(6)		√(2)
9	Related parties transaction	√(2)	√(1)	
10	Management report	√(1)		√(1)
11	Non-adherence to Guidelines	√(2)		
12	Customers/Investment Account Holders (IAHs)		√(11)	√(3)
13	Governance committee		√(6)	
14	*Shariah* Compliance		√(1)	√(3)
	TOTAL ITEMS	**79**	**29**	**39**

In reference to Table 2, the initial list of 147 governance items were then assigned to the 14 dimensions as was suggested in the Guidelines. The first eleven (11) dimensions of governance items in the index are derived from Principle 13: Para 2.110 of GP1-i. Due to specific requirements made by IFSB and AAOIFI, many of their suggested items cannot be simply put under the existing dimensions. Subsequently, another three (3) new dimensions were created to cater for the requirements provided by them. This yielded 14 dimensions in total. It is worth mentioning here, that there are a few cases where assigning the items to the dimensions is not without ambiguity (Florou and Galarniotis, 2007: 983). As indicated in Table 2, the independent assessment on the three guidelines resulted in the production of three (3) independent initial lists, which are significant in the study of governance information of IFIs. The first list is developed in reference to BNM/ GP1-i (2007), (labelled as GP1-i), which produced 79 items across eleven (11) categories; the review based on IFSB/ IFSB-3 (2006), (labelled as IFSB-3) provided 29 items across six (6) categories considered as the second list and the third list was in reference to AAOIFI/ GSIFI (2008), (labelled as GSIFI), which produced 49 items across eleven (11) categories. Interestingly, only two (2) dimensions: *Audit committee* (the term used in GP1-i and IFSB-3) *or Audit and governance committee* (the term used in GSIFI) and *Shariah* committee (the term used in BNM/GP1-i) or *Shariah* supervisory board (the term used in IFSB-3 and GSIFI) are common to all the Guidelines under review. Meanwhile, GSIFI (2008) and GP1-i (2007) shared another five (5) categories: *Board structure and functioning; Remuneration Committee; Risk management, internal audit and control* and *Management report*.

Both of the international standard-setting organizations in the Islamic finance industry, AAOIFI and IFSB, have recognised the growing need for more specific governance issues in their guidelines to address two (2) governance disclosure items, namely, the protection of *Investment Account Holders (IAHs)* and *Shariah compliance.* The *governance committee* is exclusively a recommendation of IFSB-3. However, the disclosure requirements for these items, which constitute the specific kind of governance information, have yet to be included in the minimum requirements of BNM/ GP1-i. Consequently, these results in the creation of new dimensions are included in the CGD index. The themes, together with the items extracted from the Guidelines, are tabulated in Table 2 along with an indication of which authoritative guidelines consider which themes and the quantity of items recommended by them.

Phase 3: Development of the Final Index

Having ensured that all the recommendations in the guidelines were taken into account, the next step was to trace any duplication among the identified items and assign those selected and relevant items under the relevant dimension of appropriate governance themes to become the final index.In the process to include the relevant items of governance disclosure to the final index checklist, the fine-tuning of the index through the elimination of overlapped items in the three Guidelines was undertaken. This procedure was pertinent in order to avoid any duplication and provide some kind of consolidation among the three Guidelines. Any item that was found to overlap with an item in BNM/ GP1-i was consolidated to be a single governance item under the dimension in which it was recorded.

At the point of refinement, the authors produced a final comprehensive index which consists of 123 items of governance disclosure divided unevenly across fourteen (14) dimensions (Ds);D1: *Board structure and functioning;* D2:*Nominating committee;* D3:*Remuneration committee;* D4:*Risk management committee;* D5:*Audit committee* or *Audit and governance committee;* D6:*Shariah committee* or *Shariah Supervisory board;* D7:*Risk management;* D8a and 8b:*Internal audit and control;* D9: *Related parties transaction;*D10:*Management report;* D11:*Non-adherence to guidelines;* D12:*Customers/Investment account holders;* D13:*Governance committee* and D14:*Shariah compliance.*

The distinction of CG information: Between GCGi and SCGi.

In the final process, the distinction between the GCGi and SCGi is guided by the policies and recommendation made in the guidelines. The CG information, commonly practiced in generic firms,is regarded as general whilst, the CG information is regarded as specific when it is specially suggested in the guidelines to address the specific nature of the operation of IFIs. The final comprehensive CGD index consists of 123 items divided unevenly across fourteen (14) dimensions. Ten dimensions were classified as general corporate governance (GCGi) dimensions while four were categorized as specific corporate governance information (SCGi). The former consists of the following:

D1: *Board structure and functioning;*
D2:*Nominating committee;*
D3:*Remuneration committee;*
D4:*Risk management committee;*
D5:*Audit committee* or *Audit & governance committee;*
D7:*Risk management;*
D8:*Internal audit and control;*
D9: *Related parties transaction;*
D10:*Management report* and
D11:*Non-adherence to guideline.*

The SCGi comprises the following:
D6:*Shariah committee* or*Shariah Supervisory board;*
D12:*Customers/Investment account holders;*
D13:*Governance committee and*
D14:*Shariah compliance.*

Additionally, this study has sub-classified D8 (*Internal audit and control) into* D8a and D8b. This was necessary as two items in this dimension, performance of internal *Shariah* review by internal audit department and a charter of internal *Shariah* review, are specific to IFIs. Accordingly, authors are of the opinion that these two items should be indicated in a sub-category, D8b. Table 3 summarises the CGD Index.

Table 3
Categorization in CG Disclosure Index

Dimension (s)	Sub –items
Board structure and functioning. (24- sub items numbered as D1-1: 24).	Total number of board members, the mix and number of executive and non-executive directors on the board, shareholding of directors and its restrictions, the role of Chairman and Chief executive Officer (CEO), the board meeting in terms of frequency and attendance, the qualification and experience of directors, performance assessment of board as a whole, individual directors and CEO, resignation, criteria of appointment of members on the board and *Shariah* advisors, and remuneration policies and payment to BODs, directors and management.
Nominating committee (NC). (8 sub-items numbered as D2-25: 32).	The presence of NC, its composition, the frequency and quorum for meetings, the role and responsibilities of NC. The note indicates the assessment done by NC in relation to the mix of skills and experience of directors to balance the resources pooled.
Remuneration committee (RC). (8 sub-items numbered as D3-33: 40).	The existence of RC, its composition, the frequency and quorum for RC meetings, the role and responsibilities of RC, remuneration structures and policies set for management and *Shariah* committee.
Risk management committee (RMC). (8 sub-items numbered as D4-41: 48).	The presence of RMC, its composition, the frequency and quorum for meetings, the role and responsibilities of RMC. The notes on risk management.
Audit committee (AC)/ *Audit and governance committee* (AGC). (12 sub-items numbered as D5-49: 60).	The existence of AC, its composition, the frequency and quorum of AC meetings, the role and responsibilities of AC. The charter for internal and external auditor to regulate their functions and relationship.
Shariah committee/ Shariah supervisory board. (16 sub-items numbered as D6-61: 76).	The presence of SC/SSB, the composition of its members, key information on the members' qualification and experiences, the frequency and quorum for meetings, the role and responsibilities of SC/SSB. The endorsement of IFIs' activities, policies and procedures of the appointment and dismissal as well as the policy on rotation, the remuneration scheme, *fatwas* and rulings during the year, *Shariah* review performance, and issuance report by SC.

Table 3: Continued

Dimension (s)	Sub –items
Risk management. (9 sub-items numbered as D7-77: 85).	Discussion on the nature of risks and types of activity giving rise to such risks, the composition of risk exposure, method to manage the risk including its identification, monitoring, management and controlling of risk items in banks, the presence of *Shariah* risks and the failure of managing it could bring material impairment of meeting the corporate objectives, the evaluation and assessment of risk items, the findings and recommendations derived from the assessment done, the comparative figures of the exposures of risk composition and the development programme and succession planning in banks to help deal with the risk elements in bank.
Internal audit and control. (8 sub-items divided into sub-a numbered as D8-86: 91 and sub-b of D8-92:93).	This area represents the independent source of information available to the BODs. It consists of the scope of internal audit, a review of the effectiveness of the key internal control policies and procedures, area of focus during the performance review, the changes of internal control policies and procedures, its reporting procedures, the remuneration policy for internal auditor, the performance of internal *Shariah* review (ISR) by internal auditors and the charter for ISR in bank.
Related parties' transactions (RPTs). (2 sub-items numbered as D9-94: 95).	The definition of RPTs and their policies and procedures governing such transactions undertaken by banks. The nature and extent of such transaction in banks.
Management reports. (2 sub-items numbered as D10-96: 97).	The system and procedures of reporting to BODs to allow them to assess the performance of banks. The disclosure and responsibility of management for establishing a system and maintaining compliance with *Shariah* requirements.
1.1.1 *Non-adherence to guidelines.* (2 sub-items numbered as D11-98: 99).	Any breach of guidelines needs to be disclosed and the alternative measures to address the breach or any limitations that arise.
Customers/investment account holders (IAHs). (14 sub-items numbered as D12-100: 113).	The risks and rights of IAHs upon entering the contract and on liquidation, the application of IAHs' fund, its investment strategies, the mechanics of income smoothing by banks, issues on reserves; Profit equalization reserve (PER) and Investment risks reserve (IRR) and their distribution, profit calculation methods, the changes in policies in investment and asset allocations, smoothing returns and profit calculation, issues of commingling of funds, rights of unrestricted IAHs upon *Mudharib*'s failure to perform and *Shariah* consideration on the basis of profit allocation to ensure the fairness among the dealing parties.

Table 3: Continued

Dimension (s)	Sub –items
Governance committee (GC). (6 sub-items numbered as D13-114: 119).	The composition of the GC, the role and responsibilities of the GC and chairman of the GC.
Shariah compliance (4 sub-items numbered as D14-120: 123).	Matters relating to *Shariah* requirements. The mechanism in place, such as the existence of a *Shariah* Manual to provide structured procedures and rules in ensuring all *Shariah* requirements are observed. The banks' treatment on prohibited earnings earned during the course of business, the statement of the sources and uses of zakat funds and method of calculation of its amount, as well as the uses and sources of charity funds.

5 Conclusion

Major corporate scandals in recent years have resulted in increased attention on CG disclosure. Similarly, considerable attention has been given to improving CG practices in the Islamic financial services industry. In an effort to enhance the quality of CG in the financial services sector, regulatory bodies have promulgated governance guidelines to improve the governance practices and transparency. Of particular concern is the need for IFIs to conform to the requirements of *Shariah* in all aspects of their operations. More importantly, there is a need to develop a comprehensive CG disclosure index for IFIs in order to evaluate CG disclosure quality of IFIs. This is primarily what we have done.

The CG index developed here is based on three pertinent guidelines/standards issued by various regulatory bodies: the Central Bank of Malaysia, GP1-i (2007), the Islamic Financial Services Board, IFSB-3 (2006), and AOIIFI, GSIFI (2008). The final CGD index consists of fourteen dimensions split into two areas of governance–general-governance related information (GCGi), commonly applied in generic-companies and specific-governance related information (SCGi), which addresses the peculiarities of IFIs. The ten dimensions of GCGi are board structure and functioning, nominating committee, remuneration committee, risk management committee, audit/audit and governance committee, risk management, internal audit and control, related parties transactions, management report and non-adherence to guidelines while the 5 dimensions of SCGi consist of the *Shariah* Supervisory Board, the specific part of internal audit and control, the Investment Account Holders, the governance committee and issues pertaining to *Shariah* compliance. Altogether, there were 123 items across 14 dimensions. The segregation of governance information into the general and specific governance in the comprehensive index is an extension of prior studies in examining CG disclosure quality of IFIs (e.g., Hamid and Sigit, 2005; Hassan and Christopher, 2005).

The use of a comprehensive list of disclosure items aggregating all three relatively recently released governance guidelines available to IFIs (the BNM, IFSB and AAOIFI) is a primary contribution of the study. More importantly, the index developed here can be used as a benchmark to determine the CGD quality of IFIs, perhaps globally. The use of an index in exploring the narrative disclosure in annual reports represents a dominant method applied in prior studies. To have a set of common indicators to qualify as the "best practice" CG of IFIs could enrich and strengthen the industry characteristics. This would, inevitably, trigger the intrinsic capability of IFIs all over the world, as well as emphasize and uphold their strength and specificities as a competitive advantage to propagate the Islamic finance market.

The diffusion of CG reporting practices, which is common to all IFIs, could make possible the increased willingness to disclose specific kinds of CG information by IFIs as the preparers are more certain of their choice of CG information (thus, higher quality CG reports) that eventually strengthen stakeholders' knowledge of the industry for them to gain trust in the decision making undertaken by the IFIs. Finally, the index developed here focuses on the "desirable"---- on what IFIs *ought* to disclose. This constitutes the first stage of the study. The next stage is to examine what IFIs are actually disclosing. This would give rise to the gap between the "ideal" and the "actual". Identifying the gap may well enable regulators to determine the steps that need to be taken to address such a gap.

References

AAOIFI (2008), Accounting, Auditing and Governance Standards for Islamic Financial Institutions No.1 to 6. Bahrain: Accounting and Auditing Standards for Islamic Financial Institutions.

Bandsuch, M., Pate, L. and Thies, J., (2008), "Rebuiding stakeholder trust in business: An examination of principle-centered leadership and organizational transparency in corporate governance", *Business and Society Review*, Vol. 113, No.1, pp. 99-127.

Bank Negara Malaysia (2007), "Guidelines on Corporate Governance for Licensed Islamic" (GP1 – i), Bank Negara Malaysia, Kuala Lumpur.

Bashir, B.A., (1984), "Successful development of Islamic Bank", *Journal of Research in Islamic Economics*, Vol.1, No.2, pp. 63 – 71.

Chapra, M.U. (2007), Challenges facing the Islamic financial industry. In Hassan, M.K. and M.K. Lewis (Eds.), *Handbook of Islamic Banking* (pp.338 – 357). Cheltenham, UK: Edward Elgar Publishing Limited.

Florou, A.and Galarniotis, A., (2008), "Benchmarking Greek corporate governance against different standards", *Corporate Governance: An International Review*, Vol. 15, pp. 979 - 998.

Gupta, Arindam and Parua, Anupam, (2006) "An Enquiry Into Compliance of Corporate Governance Codes By the Private Sector Indian Companies" (December 18, 2006). 10th Indian Institute of Capital Markets Conference Paper. Available at SSRN: http://ssrn.com/abstract=962001.

Hameed, S.M.I and Sigit, P. (2005), "Analysis of Corporate Governance Disclosure in Islamic Commercial Banks' Annual Reports: A Comparative Study of Islamic Commercial Banks in Malaysia and Indonesia", Presentation at The Accounting, Commerce and Finance : The Islamic Perspective Conference, 29 to 31 March 2005, Jakarta. Available at http://www.scribd.com/doc/9882916/Sigits-Paper-for-Prof-Omar-Conference

Hassan, S. and Christopher, T., (2005), "Corporate Governance Statement Disclosures of Malaysian Banks and the Role of Islam", *Asian Review of Accounting*, Vol. 13, No. 2, pp. 36 - 50.

Healy, P.M. and Palepu, K.G., (2001), “Information asymmetry, corporate disclosure, and the capital markets: a review of the empirical disclosures literature”, *Journal of Accounting and Economics*, Vol.31, pp. 405-440.

IFSB (2006), Guiding Principles on Corporate Governance for Institutions Offering Only Islamic Financial Services (Excluding Islamic Insurance (Takaful) Institutions and Islamic Mutual Funds). Kuala Lumpur: Islamic Financial Services Board.

Iqbal, Z. and Greuning, H.V., (2008), “Banking and the risk environment: corporate governance”, Islamic Finance News, 15 February, 2008.

Mills, David E. and Keast, Robyn L. (2009) *Achieving better stewardship of major infrastructure assets through configuration of governance arrangements utilising stewardship theory.*In: 13th International Research Society for Public Management Conference (IRSPM XIII), 6-8 April, Fredericksberg, Denmark.

Parsa, S., Chong, G. and Isimoya, E., (2007), “Disclosure of governance information by small and medium-sized companies”, *Corporate Governance*, Vol. 7, No. 5, pp. 635-648.

Qu, W. and Leung, P., (2006), “Cultural Impact on Chinese Corporate Disclosures – A Corporate Governance Perspective”, *Managerial Auditing Journal*, Vol. 21, No. 3, pp. 241 -264.

Appendix I

The checklist of disclosures items extracted from three guidelines

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 1: Board structure and functioning	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D1-1	Total number of board members	Para 2.20		
D1-2	Board of directors (BODs) consist of both executives and non-executives.	Para 2.22		
D1-3	Total number of non-executive directors	Para 2.22		
D1-4	Independent directors own ≤ 5 percent equity interest directly or indirectly in the bank or in its related companies.	Para 2.27		
D1-5	The Chief Executive Officer is the Only executive director on board.	Para 2.28		
D1-6	Independent non-executive directors are ≥ 1/3 of the total board size.	Para 2.29		
D1-7	Total number of independent non-executive director	Para 2.29		
D1-8	Split between the Chairman and CEO roles.	Para 2.38		
D1-9	The chairman of the board is non-executive director.	Para 2.38		
D1-10	The board meets at least 6 times in a year.	Para 2.73		
D1-11	The attendance of every board member.	Para 2.73		
D1-12	A minimum attendance of an individual director at board meeting throughout the year achieved 75 percent.	Para 2.73		
D1-13	The roles and responsibilities of the board.	Para 2.110(1)(ii)		GS6 Para 48 GS6: Appendix C
D1-14	The qualifications and experiences held by each director in office.	Para 2.63		
D1-15	The information on shareholding of directors in office at the date of annual report	Para 2.110(1)(v)		
D1-16	The performance criteria to assess effectiveness of the board as a whole.	Para 2.84 Para 2.110(1)(v)		GS6 Para 52

Appendix I: Continued ..

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 1: Continued	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D1-17	The performance criteria to assess effectiveness of the individual director on board.	Para 2.84 Para 2.110(1)(v)		
D1-18	The performance criteria to assess effectiveness of the CEO.	Para 2.85		
D1-19	Resignation of members during the year.	Para 2.110(1)(vii)		
D1-20	The management structure of the bank.			GS6 Para 50 GS6: Appendix C
D1-21	Predefined set of criteria upon the selection of member of BODs			GS6 Para 46
D1-22	Predefined set of criteria upon the selection of member of SSBs			GS6 Para 46
D1-23	A statement of the remuneration policy of BODs.			GS6 Para 63 GS6: Appendix C
D1-24	Remuneration paid to directors and management			GS6 Para 63 GS6: Appendix C
	Dimension 2: Nominating committee (NC) *			
D2-25	The bank has a Nominating Committee	Para 2.18(i)		
D2-26	NC consists at least five (5) members	Para 2.110(2)(i)		
D2-27	A minimum of four (4) non-executive directors are on NC.	Para 2.110(2)(i)		
D2-28	The Chairman of NC is an independent director	Para 2.110(2)(i)		
D2-29	The functions and responsibilities of NC.	Para 2.110(2)(iii)		
D2-30	The full NC meets minimum once a year.	Para 2.110(2)(iv)		
D2-31	The attendance of every committee member.	Para 2.110(2)(iv)		
D2-32	A statement on the committee’s assessment on the mix of skills, experience and other qualities of directors.	Para 2.110(2)(v)		

Appendix I: Continued ..

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 3: Remuneration committee (RC)	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D3-33	The bank has a Remuneration Committee.	Para 2.18(ii)		
D3-34	RC consists of a minimum of three (3) members.	Para 2.110(3)(i)		
D3-35	All members on RC are non-executive directors.	Para 2.110(3)(i)		
D3-36	The Chairman of RC is an independent director.	Para 2.110(3)(ii)		
D3-37	The full RC meets once a year to review the remuneration packages.	Para 2.110(3)(iv)		
D3-38	The attendance of every committee member.	Para 2.110(3)(iv)		
D3-39	The functions and responsibilities of RC.	Para 2.110(3)(iii)		
D3-40	A remuneration structure and policies of management.			GS6 Para 63 GS6: Appendix C
	Dimension 4: Risk management committee (RMC)*			
D4-41	The bank has a Risk Management Committee.	Para 2.18(iii)		
D4-42	RMC consists of a minimum of three (3) members.	Para 2.110(4)(i)		
D4-43	All members on RMC are non-executive directors.	Para 2.110(4)(i)		
D4-44	The Chairman of RMC is an independent director.	Para 2.110(4)(ii)		
D4-45	The RMC holds regular meetings 2-3 times per year.	Para 2.110(4)(iv)		
D4-46	The attendance of every committee member.	Para 2.110(4)(iv)		
D4-47	The functions and responsibilities of RMC.	Para 2.110(4)(iii)		
D4-48	A statement on the risk management framework.	Para 2.110(4)(v)		
	Dimension 5: Audit committee (AC)* or Audit &Governance Committee (AGC)***			
D5-49	The bank has an Audit Committee	Para 2.18(iv)	RO Part 1 (89)	GS6 Para 53
D5-50	AC consists of a minimum of three (3) members.	Para 2.110(5)(i)	GP Part 1 (19)	GS4 (No.12b)
D5-51	All members on AC are non executive directors.	Para 2.110(5)(i)	GP Part 1 (19)	GS6 Para 54 GS4 (No.11)
D5-52	Majority of member in AC are independent directors.	Para 2.110(5)(i)		

Appendix I: Continued ..

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 5: Continued	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D5-53	ONE member of AC is financially literate (i.e. having a qualification in accounting/ or experience in the field of finance).	Para 2.110(5)(i)		
D5-54	The Chairman of AC is an independent director	Para 2.110(5)(ii)	GP Part 1 (19)	
D5-55	The functions and responsibilities of AC.	Para 2.110(5)(iii)	GP Part 1 (19) GP Part 3 (51)	GS6 Para 54 GS4 (No.11b)
D5-56	The AC holds regular meetings 2-3 times a year.	Para 2.110(5)(iv)		
D5-57	The attendance of every committee member.	Para 2.110(5)(iv)		
D5-58	Adequate written rules governing the external audit functions		RO Part 1 (89)	
D5-59	Adequate written rules governing the internal audit functions.		RO Part 1 (89)	
D5-60	AC closely worked together with the external and internal auditor to perform routine review of the bank's risk exposures and accounting procedures		RO Part 1 (89)	
	Dimension 6: *Shariah* Committee (SC)* or Shariah Supervisory Board (SSB)***			
D6-61	The bank has a SC/ SSB.	Para 2.17		GS1 (No.3)
D6-62	SSB consists of a minimum of three (3) members.	Para 2.110(6)(ii)		GS1 (No.7)
D6-63	The key information and background of members in SC/ SSB (including name, qualification and experience)	Para 2.110(6)(i)	RO Part 3 (53)	GS1 (No.2)
D6-64	The functions and responsibilities of SC/ SSB.	Para 2.110(6)(iii)		GS6: Appendix C
D6-65	The frequency of SC/ SSB meeting during the year.	Para 2.110(6)(iv)		
D6-66	The attendance of every member of SC/ SSB.	Para 2.110(6)(iv)		
D6-67	An endorsement by SC/ SSB on the conformity of the Islamic bank's operations in accordance with *Shariah* principles.	Para 2.110(6)(v)		GS6: Appendix C
D6-68	Directors or significant shareholders of the banks are not on SSB			GS1 (No.7)
D6-69	The policies and procedures relating to the appointment of SSB.			GS6 Para 45
D6-70	The policies and procedures relating to the dismissal of SSB.			GS1 (No.7)
D6-71	The remuneration paid of SSB.			GS1 (No.3)

Appendix I: Continued ..

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 6: Continued	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D6-72	A report of Shariah Supervisory Board			GS1 (No.25)
D6-73	The fatwas, rulings and guidelines issued by SSB during the year.			GS1 (No.25)
D6-74	A performance of Shariah review by SSB.			GS2 (No.1)
D6-75	The practice of SSB rotation in every five (5) years			GS5: Appendix A
D6-76	A remuneration structure and policies of *Shariah* Supervisory Board (SSB).			GS6 Para 63
	Dimension 7: Risk management (RM)			
D7-77	The nature of risk faced by the bank.	Para 2.110(7)(i-a)		
D7-78	The activities within the bank which give rise to the risk.	Para 2.110(7)(i-a)		
D7-79	The composition of the risk exposures (i.e low, medium, high).	Para 2.110(7)(i-a)		
D7-80	The methods to identify, monitor, manage and control the risk.	Para 2.110(7)(i-b)		GS6: Appendix C
D7-81	The presence of any other risk that could materially impair the bank's ability to meet its corporate objectives and business strategies.	Para 2.110(7)(i-c)		
D7-82	The nature and frequency of review/ assessment in respect of the bank's risk management system.	Para 2.110(7)(i-d)		
D7-83	The key recommendation of the review/ assessment of risk management system.	Para 2.110(7)(i-d)		
D7-84	A comparative analysis of previous year's data relating to risk exposures composition.	Para 2.110(7)(ii)		
D7-85	An establishment of a programme for succession planning and leadership development on the subjects related to bank's business.	Para 2.10(iii)		GS6 Para 58

Appendix I: Continued ..

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 8a: Internal audit and control *	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D8-86	The scope of internal audit in bank.	Para 2.99		
D8-87	A review of effectiveness of the key internal control policies and procedures established for managing daily activities.	Para 2.110(8)(i)		
D8-88	The focused areas of internal audit during the review.	Para 2.110(8)(ii)		
D8-89	The changes in the policies and procedures of the internal control during the year.	Para 2.110(8)(i)		
D8-90	The procedures of reporting any of the deficient and breach on part of internal control.	Para 2.110(8)(iii)		
D8-91	The performance and remuneration package of Internal auditors are evaluated and decided by Audit Committee	Para 2.101		
	Dimension 8b: Internal audit and control *			
D8-92	The performance of internal *Shariah* review by internal audit department.			GS3 (No.5)
D8-93	A charter of internal *Shariah* review.			GS3 (No.3)
	Dimension 9: Related parties transaction			
D9-94	The policies and procedures relating to the related party transactions (RPTs) (i.e. the definition of related party, the limits applied, terms of transactions and procedures for approving and monitoring RPTs)	Para 2.95		
D9-95	The nature and extent of transactions with affiliates and related parties.	Para 2.110(9)(i)	GP Part 4 (59)	

Appendix I: Continued ..

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 10: Management report	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D10-96	The systems and procedures facilitating the communication to directors to enable them to assess the performance of bank against its plan (i.e. the types and frequency of reports).	Para 2.110(10)(i)		
D10-97	A statement of management's responsibility on the compliance with the *Shariah* .			GS1 (No.14)
	Dimension 11: Non-adherence to Guidelines *			
D11-98	Any non-adherence to the Guidelines.	Para 2.110(11)(i)		
D11-99	Explanation of alternative measures taken by bank to comply with the principles of the Guidelines.	Para 2.110(11)(ii)		
	Dimension 12 : Customers / Investment Account Holders (IAHs)			
D12-100	The contractual risks and right of IAHs.		GP Part 2 (26)	
D12-101	The investment and asset allocation strategies		GP Part 2 (26)	
D12-102	The rights and liabilities of IAHs in the event of liquidations.		GP Part 2 (32)	
D12-103	The mechanics of smoothing the returns by bank.		GP Part 4 (58)	
D12-104	Notes related to the utilization of Profit Equalization Reserve (PER).		GP Part 4 (63)	
D12-105	Notes related to the use of Investment Risks Reserves (IRR).		GP Part 4 (63)	
D12-106	The treatment for the distribution of PER in the event of liquidation.		GP Part 2 (38)	
D12-107	The method of profit calculation and its share of profit earned attributable to IAHs for the year.		GP Part 4 (58)	
D12-108	The changes of the policies in respect of profit calculation		GP Part 4 (64)	

Appendix I: Continued ..

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 12: Continued	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D12-109	The changes of the policies in respect of investment and asset allocation strategies.		GP Part 4 (64)	
D12-110	The changes of the policies in respect of the mechanics in returns smoothing during the year.		GP Part 4 (64)	
D12-111	The legal right due to the unrestricted IAHs as a result of commingled funds.			GS6: Appendix C
D12-112	The legal right due to the unrestricted IAHs in the event of *Mudharib*'s failure.			GS6: Appendix C
D12-113	A report on the appropriateness of *Shariah* basis of allocation of profit between the equity holders and the investment account holders.			GS1 (No.17)
	Dimension 13: Governance committee (GC) **			
D13-114	GC consists a minimum of three (3) members.		GP Part 1 (13)	
D13-115	ONE member in GC is a member of Audit Committee		GP Part 1 (13)(i)	
D13-116	ONE member in GC is a *Shariah* scholar elected from the bank's SSB.		GP Part 1 (13)(ii)	
D13-117	ONE member in GC is an independent non-executive director.		GP Part 1 (16)(iii)	
D13-118	The roles and functions of the GC.		GP Part 1 (15)	
D13-119	The Chairman of GC is an independent non-executive director		GP Part 1 (16)(i)	

Appendix I: Continued ..

	GOVERNANCE REQUIREMENTS IN THE STANDARDS	REFERENCES IN THE STANDARDS		
	Dimension 14: *Shariah* Compliance	(1) BNM/ GP1-i	(2) IFSB-3	(3) GSIFI
D14-120	Mechanism for monitoring Shariah compliance (i.e. how bank obtain rulings from *Shariah* scholars and how it apply fatwa).		GP Part 3 (49)	
D14-121	A report of the treatment of all earnings realised from the source or means prohibited by Islamic *Shariah.*			GS1 (No.18)
D14-122	A statement of sources and uses of zakat and charity funds.			GS1 (No.19)
D14-123	The method of *zakat* calculation which is in compliance with Islamic *Shariah*.			GS1 (No.19)