

## SHARIAH COMPLIANCE OF BANGLADESHI ISLAMIC BANKS: DOES IT DIFFER ACROSS BANK MODALITIES?

Syed Mohammad Khaled Rahman<sup>1</sup>, Mohammad Ashraful Ferdous Chowdhury<sup>2</sup>,  
Md. Mofazzal Hossain<sup>3</sup>, Fakrul Islam<sup>4</sup>, Tanvin Hossin Mim<sup>5</sup> and  
Nazmul Alam Nirjon<sup>6</sup>

<sup>1</sup> Department of Business Administration, Shahjalal University of Science and Technology, Bangladesh, kr15sust@gmail.com

<sup>2</sup> Department of Business Administration, Shahjalal University of Science and Technology, Bangladesh, ashraful\_ferdous@yahoo.com

<sup>3</sup> Department of Business Administration, Shahjalal University of Science and Technology, Bangladesh, hossaintipusust@gmail.com

<sup>4</sup> Department of Business Administration, Shahjalal University of Science and Technology, Bangladesh, fakrul70@student.sust.edu

<sup>5</sup> Department of Business Administration, Shahjalal University of Science and Technology, Bangladesh, hossintanvin45@gmail.com

<sup>6</sup> Department of Business Administration, Shahjalal University of Science and Technology, Bangladesh, nazmul20@student.sust.edu

### ABSTRACT

This study assesses the degree of Shariah compliance of different Islamic banking modalities in Bangladesh from the perspectives of investment clients, depositors, and bankers. It adopts a structured questionnaire developed based on AAOIFI standards to gather data from 392 respondents. ANOVA tests and t-tests are applied to identify significant Shariah non-compliance areas and differences in Shariah compliance scores among different Islamic bank modalities. From investment clients' perspective, it is seen that in every mode of investment except Ijarah, Shariah is explicitly violated throughout the Islamic banking industry. Significant Shariah non-compliance is seen in Bai-Murabaha, Bai-Muajjal, cash memos, and receipt and disbursement of goods, while Shariah is complied with in contract documents and client dealings. Bankers view all aspects except financial charges for delay to be Shariah compliant. From the depositors' perspective, Shariah non-compliance is observed in the non-disclosure of information. There is no significant difference in Shariah compliance level between full-fledged and non-full-fledged Islamic banks. These findings should prove useful as a reference point for Bangladesh Bank, Islamic banks, policymakers, depositors, investors, and regulators to address Shariah non-compliance areas to ensure adherence to Shariah standards.

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## I. INTRODUCTION

Islamic finance has attracted interest in the last few decades as a system that potentially resolve problems of the conventional and interest-based financial systems (Komijani & Taghizadeh-Hesary, 2018) and hence as an alternative banking model to the world economy (Hunjra et al., 2022). The Islamic finance and banking system has gained significant attention especially after the global financial crisis because of its stability in absorbing financial and external economic shocks (Baber, 2018). While Islamic banks are noted to be more stable and resilient than conventional banks during financial shocks (Tekdogan & Atasoy, 2021), they are not fully immune to the financial crisis and shocks (Uddin et al., 2017). Fundamentally, the Islamic banking industry offers Shariah-compliant financial services to Muslims who would alternatively be unable to do business with traditional interest-based finance owing to religious commitments. The performance of the Islamic banking industry is astonishing, with a year-on-year growth of 6.9% of assets in 2022 despite the downturn in the global economy (IFSB, 2023). The motivation of Muslims to participate in the Islamic banking system is that the Islamic banks follow the Islamic Shariah- Quran and Sunnah. The appeal of Islamic Banking, however, is not confined to Muslims only; rather, it become attractive to the non-Muslims as well because of the transparency and stability of Islamic financial institutions (Saiti et al., 2022). Contrary to popular perception, religious belief is not even a factor in some cases when choosing Islamic banking services (Rahman et al., 2021); rather, the perception of customers regarding relative advantage and risk management lead the way. Since Islamic banking is fundamentally operated on the basis of transparency, full disclosure, and ethical considerations, these factors are crucial for determining Islamic banks' Sharia compliance level (Komijani & Taghizadeh-Hesary, 2018).

Islamic banks benefit in several ways from being shariah compliance. Compliance with Shariah standards helps Islamic financial institutions to perform financially in a better way, which subsequently results in their stable financial condition (Bugshan & Bakry, 2023; Nidyanti & Siswanto, 2022). The financial stability of Islamic banks, which is achieved through shariah compliance, allows banks to absorb external financial shocks (Baber, 2018; Banna et al., 2022). Similarly, Shariah compliance contributes to fostering customers' satisfaction with the products and services of Islamic banks and the Islamic financial system through the channel of trust and loyalty (Ahmed et al., 2022; Kaakeh et al., 2019). Furthermore, the Shariah compliance of Islamic banks is crucial for economic development of a country. Compliance with Shariah principles makes the banks financially sound, which ultimately impacts economic performance (Daly & Frikha, 2016; Jawad & Christian, 2019; Anwar et al., 2020; Mensi et al., 2020). Therefore, to avoid any controversy, debate, or ambiguity, as well as to uphold the values and principles of finance, Islamic banks should comply with the Islamic Shariah in both governance mechanisms and operating activities.

The fundamental philosophy of Islamic finance is to provide deposit and investment products free of interest, ambiguity, and excessive uncertainty in transactions and financial contracts (Hassan et al., 2013). Despite the fact that the sector has expanded exponentially in its short lifespan, the practice of the product and service offerings has come under criticism (Abbas & Ali, 2019; Ahmed, 2014;

Karim & Shetu, 2020; Majeed & Zainab, 2017; Ullah, 2014). Some of the targets of the critiques are that the Islamic financial products gradually resemble those of traditional finance (Uddin, 2022). The argument is that by doing so, Shariah conditions are blurred, resulting in types of agreements that are met but not the essence or intent of Islamic law. It is also argued, however, that Islamic banks are offering financial products that resemble conventional products, and the products are indifferent to complying with Islamic Shariah regulations (Mustafa, 2019). In addition to the criticism of the Islamicity of the financial products offered by Islamic banks and institutions, it is also evident that the level of Shariah compliance varies among the countries (Abbas & Ali, 2019; Chowdhury et al., 2020; Karim & Shetu, 2020; Majeed & Zainab, 2017; Mustafa, 2019; Ullah, 2014).

Narrowing down to the Islamic banking industry in Bangladesh, Islamic banks are also under criticism regarding their shariah compliance (Ullah, 2014). The inability of current Islamic financial practices to meet Shariah standards has resulted in misleading views and statements regarding the sector. Since the motivation of the customers to participate in Islamic banking is primarily faith-based, it is crucial to maintain the Shariah compliance level to retain their trust and loyalty. As Bangladesh is the second largest Muslim country, and the Islamic banking industry is growing exponentially in Bangladesh (11.7% in 2022) over the years (Bangladesh Bank, 2022), it is crucial to understand the dynamics of shariah compliance of Islamic banks in Bangladesh. Several studies have examined the level of Shariah compliance of Islamic banks in Bangladesh (Ahmad et al., 2014; Karim & Shetu, 2020; Uddin, 2022; Ullah, 2014). Though these studies are pioneers in determining the shariah compliance level of Bangladeshi Islamic banks, all focus on providing shariah scoring from bankers' perspectives, and no study considers from clients' perspectives. While bankers are the primary know-how persons in the banking industry, the opinions of clients could also make differences as the perception between the bankers and clients varies in terms of the shariah governance of the Islamic banks (Oladapo et al., 2019). Contrary to that, some studies have also documented no significant difference in the perception among various stakeholders regarding Islamic banking (Khan & Ramzan, 2015) and its services (Shamsudheen et al., 2021). Therefore, it is still inconclusive whether the level of Shariah compliance varies from different stakeholders' perspectives. Addressing this unsettled issue, this study investigates the level of shariah compliance of Islamic banks in Bangladesh from the perspective of bankers, investment clients, and depositors. While the Islamic banks in Bangladesh have become the alternative banking in the economy and the conventional banks are also operating some Islamic branches and windows, it is also crucial to investigate if there is any variation in shariah compliance among the full-fledged banks and non-full-fledged Islamic banking operating units under conventional banks.

Using descriptive and inferential statistical approaches, the study finds the shariah compliance level of Islamic banks, irrespective of their sub-category belonging, to be heterogeneous. Additionally, the Shariah score varies among bankers, investment clients, and depositors. While investment clients are largely dissatisfied and perceive that the Islamic banks are violating Shariah rules significantly, the bankers conclude that they always put Shariah first. Still, it is noted that the level of Shariah compliance varies among different types of activities.

It is worth noting that there is no significant difference between the banking sub-categories in the level of Shariah compliance, indicating that the entire Islamic banking industry is operating similarly, and the full-fledged banks are not in a pioneering position regarding Shariah compliance.

Despite there are several studies examining the level of Shariah compliance of Islamic banks in Bangladesh (Ahmad et al., 2014; Karim & Shetu, 2020; Uddin, 2022; Ullah, 2014), this study contributes to the understanding of shariah compliance of Islamic banks in Bangladesh in two ways. First, to the best of the authors' knowledge, this study is the pioneer in documenting the disparity in the level of Shariah compliance from different stakeholders' perspectives. Second, we extend the existing literature on the shariah compliance of Islamic banks by uncovering how the level of shariah compliance of full-fledged and non-full-fledged varies in the Bangladeshi Islamic banking industry. The insights from this study have practical implications for stakeholders, government, and regulatory bodies. The study recommends that Islamic banks in all categories effectively conduct Shariah audits and improve the Shariah governance framework to improve the level of Shariah compliance in banks. Further, this study also suggests that government and regulatory bodies employ effective Shariah supervision through the country's central Shariah board.

The rest of the paper is structured as follows- section 2 contains a literature review, section 3 outlines the methodology, section 4 discusses the results and findings, and finally, section 5 concludes the study with recommendations and policy implications.

## **II. LITERATURE REVIEW, RESEARCH GAP, AND HYPOTHESES DEVELOPMENT**

In recent years, the Islamic finance industry has gained significant growth and attention worldwide. However, it is essential for IFIs to maintain Shariah to differentiate it from its conventional counterpart. Several studies have criticized the Shariah compliance practice of IFIs (Abbas & Ali, 2019; H. Ahmed, 2014; Karim & Shetu, 2020; Majeed & Zainab, 2017; Ullah, 2014) and doubted their Islamicity. Ahmed (2014) discovers that in some situations, Islamic banks opt for debatable financing modes as they are only feasible options under the existing legislative framework. The study also adds that, in some cases, inferior modes are chosen due to their economic benefits, and in Bangladesh, Islamic banks lack proper audit and governance committees and are not fully compliant with AAOIFI's Shariah governance framework (Ahmed & Khatun, 2013). Moreover, sometimes, even management uses Shariah boards to maximize their financial benefit in an unethical manner (Alam et al., 2020), causing significant non-compliance in Shariah governance. Karim and Shetu (2020) demonstrate that most Islamic banks have a Shariah scheme; they set a profit limit, which is Shariah non-compliant. In a Shariah-based annual audit, the highest degree of non-compliance is discovered. The authors find some reasons for non-compliance, such as lack of Shariah knowledge among officials, the nonexistence of penalty for non-compliance, etc. Similarly, it is also argued that the Shariah compliance position of IBs in Bangladesh is in jeopardy due to a lack of expertise, a lack of seriousness

in adhering to Shariah, a lack of emphasis on Shariah audit and research, and a lack of a strong SSB with knowledgeable scholars (Ullah, 2014). It is also crucial to mention that Shariah compliance is significantly associated with the quality of Shariah governance mechanisms of the Islamic banks (Alam et al., 2022), and Bangladesh lacks separate and comprehensive Shariah governance guidelines (Alam et al., 2020), which subsequently result in the ambiguity and misconception about the shariah governance and image of Islamic banks. This ambiguity causes Islamic banks to deviate from the Shariah principles and guidelines in their practices (Tabash et al., 2022).

The Islamic banking industry is growing tremendously around the world, and conventional banks are also operating Islamic banking branches and windows. Generally, customers perceive full-fledged Islamic banks to be more Shariah-compliant than their non-full-fledged counterparts (Ratnasari et al., 2021). Though there are some exceptions, such as non-full-fledged Islamic banks outperforming full-fledged banks in digital service offerings, the full-fledged banks still remain competitive in clients' perceptions. However, Ratnasari et al. (2021) have neither empirically investigated if there are discrepancies in being Shariah compliant in practice nor revealed if the variations are statistically significant. In contrast, Islamic banks are not different in the disclosure of Shariah non-compliant income regardless of their banking modalities (Puneri et al., 2020). However, the level of disclosure is not enough to comprehend the level of overall Shariah compliance of the Islamic banks and windows. Interestingly, Majeed and Zainab (2017) study both full-fledged and non-full-fledged Islamic banks to assess the level of Shariah compliance, but they do not record any notable insight regarding the discrepancies between Islamic banks and Islamic branches of conventional banks. Since the empirical insights in the literature are inconclusive, this study hypothesizes that there are differences in the level of shariah compliance between full-fledged and non-full-fledged Islamic banks in Bangladesh.

$H_0-1$ : There is no difference in the level of shariah non-compliance between full-fledged and non-full-fledged Islamic banks in Bangladesh.

The difference in the level of shariah compliance is also prevalent in Islamic banks' deposit products. It is commonly perceived that the products and services offered by Islamic banks resemble those of conventional banks (Ahmad et al., 2014). The investment return of clients' deposits may not completely adhere to the profit and loss sharing concept (Hamza, 2016). Additionally, the management of investment deposits and profit and loss sharing (PLS) assets exhibit moral hazard behavior and excessive risk-taking, which is not in conformance with Shariah principles. Karim and Shetu (2020) also reveal that the level of Shariah compliance in deposit products of Islamic banks is not satisfactory. However, the discrepancies might have resulted from the differences in the Shariah governance mechanisms among the countries (Fatmawati et al., 2022), and despite the products resembling those conventional, the products may not be Shariah non-compliant (Mustafa, 2019).

$H_0-2$ : There is Shariah non-compliance in the deposit schemes offered by Islamic banks.

Since the Islamic banking system fundamentally focuses on investment activities, perhaps there might be elements of Shariah non-compliance in different

types of investment mechanisms. Ullah (2014) finds a significant non-compliance of Shariah standards in investment activities. However, the level of non-compliance varies among different investment activities. Karim and Shetu (2020) note that the Musharakah contract has a high degree of shariah non-compliance, which is also supported by Majeed and Zainab (2017). Their study also finds that Islamic banks moderately comply with the shariah in Mudarabah, Ijarah, and Qard-Al-Hassan contracts. In contrast, Majeed and Zainab (2017) reveal significant non-compliance in Qard-ul-Hassan contracts. The practice of the Shirkah-tul Milk investment mechanism is criticized by Uddin (2022). The study demonstrates that Shariah conformity in apartment purchases could not be rigorously maintained by Islamic banks due to a lack of awareness and comprehension of the goals and philosophies of the banks, a weak Shariah board, poor audit, a weak regulatory agency, and a supervisory issue. Ironically, Islamic banks often choose contentious financing modes due to the unavailability of Shariah-compliant alternatives (Ahmed, 2014). However, Ahmed (2014) argues that the inclination toward Shariah non-compliance in investment activities is induced by the erroneous conception of bank officials and clients of Islamic banks.

$H_0-3$ : There is Shariah non-compliance in the practice of different investment modes by Islamic banks.

As Shariah compliance is the cornerstone for Islamic banks, it is essential for the banks to uphold Shariah principles in every aspect of banking. Along with the deposit products and investment activities, unfortunately, the Shariah non-compliance practices in operational activities is also prevalent. In ensuring the operating activities of Islamic banks to be shariah compliant, the shariah disclosure plays a pivotal role by providing necessary information to the stakeholders. However, the level of Shariah disclosure varies between full-fledged and non-full-fledged Islamic banks, whereas the full-fledged group is more compliant in Shariah disclosure than its non-full-fledged counterpart (Bibi et al., 2023). However, despite some voluntary disclosure, significant numbers of Islamic banks do not maintain proper Shariah disclosure practices (Amin et al., 2021). Moreover, the financing rates of Islamic banks are influenced by the conventional policy rate, which is perhaps due to the economic and legal environments of the banks (Saeed et al., 2023).

$H_0-4$ : There is Shariah non-compliance in performing the operational activities by the Islamic banks.

Since the findings are still inconclusive regarding Shariah compliance in different activities, the study aims to investigate the level of Shariah compliance of Islamic banks in investment mechanisms, deposit products, and operational activities from different stakeholders' perspectives.

### **III. METHODOLOGY OF THE STUDY**

#### **3.1. Data and Sample**

Primary data are used in this study, which are collected through structured questionnaires from three categories of respondents- (i) depositors, (ii) investment clients, and (iii) Islamic bankers. The total number of respondents surveyed is 392, comprising 180 depositors, 162 Islamic bankers, and 50 investment clients.

Similar to Oladapo et al. (2019) and Khan & Ramzan (2015), we focus on different stakeholder groups to better understand how each group perceives the Shariah compliance level of Islamic banks in Bangladesh. Typically, bankers are accessible through organizational channels, while investment clients have varying levels of willingness to participate in the survey due to privacy concerns and their time limitations, resulting in a smaller number of respondents. However, the Islamic banking sector shares approximately 27% of investment in the entire banking industry in Bangladesh (Bangladesh Bank, 2022). Therefore, we calculate<sup>1</sup> the sample size of an unspecified population for the investment client's sub-group with a 10% margin of error at a 90% confidence interval and determine the sample size to be 54. After calculating the sample size and considering the fact that the non-full-fledged Islamic banking branches and windows have a few numbers of investment clients among all clients, we select a 50-clients' representative group to fulfil our objective. Moreover, as deposit and investment products are uniformly offered throughout the country so, bankers, depositors, and investment clients of Sylhet division represents these stakeholders of Bangladeshi Islamic banking industry. we use the purposive sampling method for selecting the sample. The reason is that the bankers are involved in Islamic banking activities and hence are knowledgeable about internal affairs of Islamic banking. Most of the chosen depositors are Mudaraba savings account holders. Likewise, most investment clients in the sample are from Bai-Murabaha and Bai-Muazzal mode as these two are most predominantly offered by Islamic banks in Bangladesh. Shariah non-compliance is evaluated from the perspective of each category of respondents. For developing the content of the questionnaire, at first, the common contentious Islamic banking practices and features of deposit and investment products are identified through personal observation, a pilot survey of respondents, a product dossier, brochures, and previous research articles. The practices and features are then compared with AAOIFI (2017) standards to judge whether those are compatible with Shariah.

**Table 1.**  
**AAOIFI Shariah Standards**

No. of Shariah Standards	Contents
SS-2	Debit card, charge card, and credit card
SS-9	Ijarah and Ijarah Muntahia Bittamleek
SS-10	Salam and Parallel Salam
SS-11	Istisna'a and Parallel Istisna'a
SS-12	Sharikah (Musharakah) and modern corporations
SS-13	Mudarabah
SS-14	Documentary credit
SS-19	Qard
SS-20	Sale of commodities in the organized market
SS-28	Banking services in Islamic banks
SS-47	Rules for calculating profit in the financial transaction

1  $n = \frac{Z^2 \hat{p}(1-\hat{p})}{\epsilon^2}$ , where Z is the z score,  $\hat{p}$  is population proportion, and  $\epsilon$  is margin of error.

Table 1 illustrates the number of AAOIFI shariah standards and the corresponding contents. The existing banking practices' corresponding Ss are segregated into different dimensions and expressed in the form of negative statements in the questionnaire. A five-point Likert scale ranging from +2 to -2 is used to judge the degree of Shariah compliance by banks, where a lesser value indicates more Shariah compliance and vice-versa. Shariah compliance score is determined after compiling the responses and taking the arithmetic mean for each category. The scores are compared among different types of banks. Both open and close-ended questions are used in the questionnaire.

### 3.2. Descriptive Statistics

Table 2 shows that among the three stakeholders of Islamic banks, respondents from full-fledged banks share the highest percentages across all these groups: 76% investment clients, 84.4% depositors, and 82% bankers. On the other hand, branches and windows account for less than 25% of all stakeholders. Business (80%) is the most common occupation among investment clients, followed by workers (10%) and housewives (4%). Additionally, Muajjal (42%), Murabaha (28%), and Ijarah (10%) are the three most popular investment modes in the Bangladeshi Islamic banking sector, whereas Bai-salam and Musaraka are comparatively less popular. The depositors are 70% from Mudaraba (savings) holders and 30% from the mix of Mudaraba (investment) and Al-Wadiah account holders. For the bankers' sub-group, we survey the bankers who are in middle-level managerial positions (51.2%), operational level (42%), and the remaining are at strategic level.

**Table 2.**  
**Demographic Profile of the Respondents**

Indicators	Categories	Investment Clients (%)	Depositors (%)	Bankers (%)
Bank Types	Full-Fledged	76	84.4	82.1
	Branch	4	3.9	5.6
	Window	20	11.7	12.3
Gender	Male	86	90	98.1
	Female	14	10	1.9
Occupation	Business	80	38.3	N/A
	Worker	10	27.2	
	Housewife	4	6.7	
	Others	6	20	
Investment Mode	Murabaha	28	N/A	N/A
	Muajjal	42		
	Bai Salam	4		
	Musaraka & Mudaraba	6		
	Ijarah	10		
	Murabaha & Muajjal	6		
	Muajjal & Ijarah	4		



**Table 2.**  
**Demographic Profile of the Respondents (Continued)**

Indicators	Categories	Investment Clients (%)	Depositors (%)	Bankers (%)
Managerial Position	Top-level		N/A	6.8
	Middle level	N/A		51.2
	Operational level			42
Account Type	Al-Wadiah	N/A	18.9	N/A
	Mudaraba (Savings)		70	
	Mudaraba (Investment)		2.2	
	Both Al-Wadiah & Mudaraba		7.8	
	All		1.1	

Source: Field survey, 2022

## IV. RESULTS AND DISCUSSIONS

### 4.1. Shariah non-Compliance from Investment Clients' Perspective

#### 4.1.1. Comparing the Shariah Compliance Scores among Different Banking Systems

**Table 3.**  
**Mean Shariah Compliance Scores of Investment Modes and Operational Activities**

	Full-fledged Mean	Islamic Branch Mean	Islamic Window Mean
<b>Bai-Murabaha</b>			
In the Bai-Murabaha transaction, the cost and profit markup are not disclosed by Islamic banks to the clients	1.13		-1.00
The specification of the asset to be procured under the Bai-Murabaha contract is not given in detail and is not known to the client	.25		2.00
The bank doesn't acquire the physical or constructive possession of the asset before entering into the Murabaha sale contract	.31		-1.00
Instead of providing goods/commodities, a cash facility is provided	.57		2.00
Islamic bank appoints its customer as its purchasing agent under Murabaha financing	1.56		2.00
<b>III. Average</b>	0.764		0.8
<b>IV. Bai-Muajjal</b>			
The seller (bank) receives a commitment fee for providing the credit period from the purchaser	.18	2.00	.14
Instead of providing goods/commodities, cash facility is provided	.72	1.00	.57
Entire payment for purchased goods is not deferred	.47	-1.00	1.00
<b>V. Average</b>	0.456	0.67	0.57
<b>VI. Bai-Salam</b>			
The price is unknown to the parties to the contract and not fully paid to the seller at the time the "Bai Salam" contract is signed.	1.50		

**Table 3.**  
**Mean Shariah Compliance Scores of Investment Modes and Operational Activities**  
**(Continued)**

	Full- fledged Mean	Islamic Branch Mean	Islamic Window Mean
Selling of Bai Salam products via the client while not appointing him as a sales representative	1.50		
Profit is charged at agreement stage	.50		
Commodities to be procured under 'Bai Salam' are not specified properly to the seller	2.00		
<b>VII. Average</b>	1.37	-	-
<b>Musharaka and Mudaraba</b>			
In Musharaka and Mudaraba, the partners are entitled to a lump sum profit, or the profit is determined as % of capital	1.50	2.00	
In Musharaka and Mudaraba, the profit % is deferred until the realization of profit	1.00	.00	
<b>VIII. Average</b>	1.25	1.00	
<b>IX. Ijarah</b>			
In HPSM, delivery of the asset to the client is either delayed or not made	-.25		-1.67
Before the asset is ready to generate money, the "gestation period" of rent is levied.	1.00	-1.00	1.00
When lease rental is variable, the minimum and maximum rent is not fixed up by the lessor	-.25		.67
Asset is not transferred to lessee in Ijarah Muntahia Bittamleek via a different agreement from Ijarah.	-.75		.33
In the event that the lessee is late with a payment, the lessor (bank) will mandate an increase in the rental amount payable.	1.25		2.00
Sometimes rent on rent is charged	-.75		-1.33
When Bai-Muajjal and Bai-Murabaha Investment are converted to Hire Purchase, rent is levied without demonstrating the bank's proprietorship of the asset.	-.75		1.00
<b>X. Average</b>	-0.071	-1.00	0.52
<b>XI. Operational Activities</b>			
<b>a. Cash Memos</b>			
Cash memos for product purchases are made in the clients' names rather than the banks'.	1.11	2.00	.00
The amount written in the cash memo is not equal to the amount of investment	.69	1.00	.00
Undated/Postdated/Backdated cash memos are taken	.34	.00	-.40
Prior to and following the investment, cash memos are obtained.	.21	-2.00	-1.25
Cash memos are not signed by the vendor and are not sourced from the real vendor.	.18	-1.00	-.10
Cash memo is signed by bank employees as sellers	-.08	1.00	1.80
<b>XII. Average</b>	0.40	0.14	0.008
<b>b. Charging of profit</b>			
Prior to purchasing and selling, a profit is levied.	.42	-1.50	1.13

**Table 3.**  
**Mean Shariah Compliance Scores of Investment Modes and Operational Activities**  
**(Continued)**

	Full- fledged Mean	Islamic Branch Mean	Islamic Window Mean
A new rate of profit is applied after executing the contract with the customer	.08	-1.00	.50
Instead of charging with the cost price at the sale stage, profit is charged at the adjustment stage to compensate profit for the additional period of investment recuperation.	.26	2.00	.22
If there is any postponement, non-receipt, or lesser amount of receipt of profit against the sales revenue of the export L/C, profit is charged by forming Bai-Muajjal investment.	.00	.00	.00
<b>XIII. Average</b>	0.19	-0.12	0.46
<b>c. Contract Documents</b>			
Blank Agreement form(s) are being filled out with the client's signature.	-.38	-1.00	-.80
The branch managers' signature is not included in the agreements.	-.66	-1.50	-1.00
The investment client applies for TT/DD/PO by himself rather than through branch officials.	-.16	.00	-1.00
For the purpose of selling the items under the dealership or Murabaha Post Import Investment (MPI), client's letter of authorization is not required.	.03	.00	.00
<b>XIV. Average</b>	-0.29	-0.625	-0.7
<b>d. Receipt and Disbursement of goods</b>			
In place of the bank officer, the investment client receives commodities.	1.55	.50	.40
The existence of the supplier of goods/commodities is not found	-.14	2.00	.30
There is no proof that the client got items from the branches	.86	.50	.20
There is no proof that the branch got any products from the suppliers	1.05	.50	.40
Without sending representatives to the location to receive, and examine (in case of a buying agency) the products, these are passed to the customer	.47	.00	-.20
<b>Average</b>	0.78	0.7	0.22
<b>e. Client Dealings</b>			
Investment is given in the Shariah-prohibited items	-1.67	-2.00	-1.20
In order to make up for the clients' past debts, fresh investment is made, displaying shady purchasing and selling.	-.34	-2.00	-.60
The client and the branch do not bargain about the price of the items	-.23	-1.00	-.50
<b>XV. Average</b>	-0.75	-1.67	-0.76
<b>f. Financial Charges for Delay</b>			
In credit card transactions, the bank charges the customer an extra amount in the event of a delay in payment of the Qard amount.	.29	1.00	.88
The date for the client's payment is extended by the bank in exchange for an additional charge.	-.26	1.00	-.60

**Table 3.**  
**Mean Shariah Compliance Scores of Investment Modes and Operational Activities**  
**(Continued)**

	<b>Full- fledged Mean</b>	<b>Islamic Branch Mean</b>	<b>Islamic Window Mean</b>
When a client delays sending a product or paying the Qard amount, a penalty clause is incorporated.	.70	2.00	.50
<b>XVI. Average</b>	0.24	1.33	0.26

Source: Field survey, 2022

It is evident from Table 3 that the Islamic banking industry is Shariah non-compliant in every investment mode. In Bai-Murabaha investment, full-fledged banks are non-compliant in all aspects, while Islamic windows are non-compliant with Shariah rules in disclosing asset specifications, providing cash facilities, and employing clients as purchasing agents. However, they strictly follow the rules for disclosing profit and possessing rightful asset authority for investment. In Bai-Muajjal, all banks are Shariah non-compliant except for Islamic branches that do not defer payment. Full-fledged banks have Shariah non-compliance in Bai-Salam transactions. In partnership mode, Islamic banks are found to be significantly non-compliant with Shariah in Musharaka and Mudaraba transactions. The Shariah compliance level regarding Ijarah-related transactions of Islamic banks is heterogeneous. Full-fledged banks are Shariah compliant for most aspects except charging rent during gestation and incremental rent for delayed payment, while Islamic windows are non-compliant in every aspect except for assets delivery under HPSM ( $M = -1.67$ ) and charging rent on rent ( $M = -1.33$ ).

All bank types consistently violate Shariah rules in charging profit, except for Islamic branches that charge profit before trading and charge a new profit rate after executing contracts with clients ( $M = -1.00$ ). All banking groups adhere to Shariah regarding contract document maintenance except for taking the letter of authority for selling goods under the MPI contract ( $M=0.03$ ). Banks are sensitive in maintaining customer relationships and strictly comply with Shariah rules in every aspect of client dealings. However, Islamic branches significantly violate Shariah rules by imposing financial charges for delays in credit card payment, Qard amount, and commodity delivery. Full-fledged banks and Islamic windows comply with Shariah rules regarding extending payment deadlines in exchange for excess payment.

**4.1.2. Differences in Shariah compliance levels among different banking systems:  
a. Differences in Shariah compliance scores in Bai Murabaha, Mudaraba and Musharaka**

**Table 4.**  
**Independent Samples t-test to Compare Shariah Compliance Scores**

Bank Modalities	t-test for Equality of Means							Decision About $H_0-1$
	t	df	Sig. (2-tailed)	Mean Diff.	Std. Error Diff.	95% C. I. of the Difference		
						Lower	Upper	
Mode: Bai Murabaha								
Full-fledged and Islamic window	-.049	15	.962	-.038	.771	-1.681	1.606	accepted
Mode: Mudaraba & Musharaka								
Full-fledged & Islamic branches	.577	1	.667	.250	.433	-5.251	5.752	accepted

Data processed in SPSS

According to t-test, there is no significant difference ( $p = 0.962 > 0.05$ ) in Shariah compliance level between full-fledged and Islamic windows regarding Bai Murabaha investment. The same holds true between full-fledged and Islamic branches regarding partnership mode of investment ( $p = 0.667 > 0.05$ ). Hence,  $H_0-1$  is not rejected.

**b. Differences in Shariah Compliance Scores in Bai Muajjal and Ijarah**

**Table 5.**  
**ANOVA test to Compare Shariah Compliance Scores in Bai Muajjal and Ijarah**

Mode	Source of variance	Sum of Squares	df	Mean Square	F	Sig.	Decision About $H_0-1$
Bai Muajjal	Between Groups	.179	2	.090	.087	.917	accepted
	Within Groups	23.838	23	1.036			
	Total	24.017	25				
Ijarah	Between Groups	1.300	2	.650	3.732	.089*	accepted
	Within Groups	1.045	6	.174			
	Total	2.345	8				

\* $p < 0.1$ , Data processed in SPSS

ANOVA test results show that there is no significant difference between the full-fledged banks, Islamic branches, and Islamic windows in terms of compliance with Shariah rules for the Bai-Muajjal and Ijarah investment modes. Hence,  $H_0-1$  is not rejected.

*c. Differences in Shariah compliance scores in operational activities among bank types*

**Table 6.**  
**ANOVA Test to Identify Differences in Shariah Compliance Scores in Operational Activities**

		Sum of Squares	df	Mean Square	F	Sig.	Decision About $H_0-1$
Cash Memos	Between Groups	.744	2	.372	.753	.477	accepted
	Within Groups	21.752	44	.494			
	Total	22.496	46				
Charging of Profit	Between Groups	1.181	2	.590	.977	.384	accepted
	Within Groups	28.389	47	.604			
	Total	29.569	49				
Contract Documents	Between Groups	1.875	2	.937	2.445	.098*	Accepted
	Within Groups	18.017	47	.383			
	Total	19.892	49				
Receipt and disbursement of goods	Between Groups	2.412	2	1.206	2.104	.133	Accepted
	Within Groups	26.944	47	.573			
	Total	29.357	49				
Client Dealings	Between Groups	.670	2	.335	.532	.591	Accepted
	Within Groups	29.608	47	.630			
	Total	30.278	49				
Financial charges for delay	Between Groups	1.176	2	.588	.697	.503	Accepted
	Within Groups	36.249	43	.843			
	Total	37.425	45				

Table 6 shows that there are no significant differences in Shariah compliance level of operating activities across different banking categories as p values are greater than 0.05 in all cases. Hence,  $H_0-1$  is not rejected.

**4.1.3. Identifying Significant Shariah non-compliance Areas**

As shown in Table 7, the mean Shariah compliance score for all types of Islamic banks in investment mechanisms, including Bai-Murabaha (BM) and Bai-Muajjal (BMu), is much above the neutral value of 0, which indicates that the Shariah non-compliance in both investment mechanisms is significant. Similarly, Shariah's non-compliance in maintaining cash memos (CM), receipts, and disbursement of goods (RD) and imposing financial charges for delay (FC) is also found to be significant. However, in maintaining contract documents (CD) and client dealings (CID), banks are significantly Shariah compliant. Moreover, the Shariah non-compliance in charging profit (CP) ( $M= 0.1333$ ) is not significant despite the existing Shariah non-compliance condition in this dimension.

**Table 7.**  
**One Sample t-test for Testing the Level of Significance of Shariah non-compliance**

	Test Value = 0							Decision about $H_0$
	t	Mean	df	Sig. (2-tailed)	Mean Difference	95% C. I. of the Difference		
						Lower	Upper	
BM_Avg	4.352	.7647	16	.000*** (.1757)	.76471	.3922	1.1372	$H_0$ -3 accepted
BMu_Avg	2.401	.4615	25	.024** (.1922)	.46154	.0656	.8574	$H_0$ -3 accepted
CM_Avg	3.052	.3113	46	.004*** (.1020)	.31135	.1060	.5167	$H_0$ -4 accepted
CP_Avg	1.214	.1333	49	.231 (.1098)	.13333	-.0874	.3541	$H_0$ -4 rejected
CD_Avg	-5.124	-.4617	49	.000*** (.0901)	-.46167	-.6427	-.2806	$H_0$ -4 rejected <sup>a</sup>
RD_Avg	5.865	.6420	49	.000*** (.1094)	.64200	.4220	.8620	$H_0$ -4 accepted
CLD_Avg	-6.896	-.7667	49	.000*** (.1111)	-.76667	-.9901	-.5433	$H_0$ -4 rejected <sup>a</sup>
FC_Avg	1.940	.2609	45	.059* (.1344)	.26087	-.0099	.5317	$H_0$ -4 rejected

Std. Error in parenthesis. \*\*\*p<0.01; \*\*p<0.05; \*p<0.1; <sup>a</sup> p<0.05 of t-statistic with negative value indicates significant Shariah compliance

## 4.2. Shariah Compliance from Bankers' Perspective

### 4.2.1. Comparing the Shariah Compliance Scores among Different Banking Systems

**Table 8.**  
**Mean Shariah Compliance Scores of Investment Modes and Operational Activities**

	Full-fledged Mean	Islamic Branch Mean	Islamic Window Mean
<b>Shariah Noncompliance in Investment Mechanisms (INV)</b>			
In Bai-Murabaha transaction, the cost and profit markup are not disclosed by Islamic banks to the clients (purchasers of the product)	-.59	.17	-.71
The specification of the asset to be procured under the Bai-Murabaha contract is not given in detail and is not known to the client	-.65	-.50	-1.00
Bank doesn't acquire the physical/constructive possession of assets before entering the Murabaha sale contract with the purchaser	.59	1.50	.47
Under Bai Murabaha and Bai-Muajjal, monetary facilities are offered in place of products	-.07	1.00	-.75
The price is unknown to the parties to the contract and not fully paid to the seller at the time the "Bai Salam" contract is signed	-.21	.00	.00
Selling of Bai Salam products via the client while not appointing him as a sales representative	-.19	.00	-.50

**Table 8.**  
**Mean Shariah Compliance Scores of Investment Modes and Operational Activities**  
**(Continued)**

	<b>Full- fledged Mean</b>	<b>Islamic Branch Mean</b>	<b>Islamic Window Mean</b>
An Istisna contract's object is an identifiable existing capital asset rather than identified raw materials that can be altered	-.27	.00	-.13
In the Istisna contract, the vendor may state that it is exempted from liability for flaws	-.17	.00	-.33
Asset is not transferred to lessee in Ijarah Muntahia Bittamleek via a different agreement from Ijarah	-.07	.00	-.14
Investment is given in Shariah-prohibited items	-1.43	-1.89	-1.33
In order to make up for the clients' past debts, fresh investment is made, displaying shady purchasing and selling	-.79	-1.56	-1.50
<b>Average</b>	-0.35	-0.11	-0.54
<b>Shariah Noncompliance in operational activities</b>			
<b>Cash Memos (CM)</b>			
Cash memos for product purchases are made in the clients' names rather than the banks	-.23	.44	-.40
The amount written in the cash memo is not equal to the amount of investment	.02	.11	-.65
Undated/Postdated/Backdated cash memos are taken	-.33	1.00	-.25
Prior to and following the investment, cash memos are obtained.	-.33	.00	-.32
Cash memos are not signed by the vendor and are not sourced from the real vendor	-.37	-1.43	-1.05
The cash memo is signed by bank employees as sellers	-.30	-1.11	-.75
Branches do not keep cash-memo of the bought-goods	-1.25	-1.13	-.89
<b>Average</b>	-0.39	-0.30	-0.61
<b>Charging of profit/rent (CP)</b>			
Before purchasing and selling, profit is levied (during the agreement stage in the case of Bai Salam)	.59	.00	.35
A new rate of profit is applied after executing the contract with the customer	-.36	-1.56	-.65
Profit is charged at the adjustment stage to compensate profit for the additional period of investment recuperation.	-.14	.00	-.25
If there is any postponement, non-receipt, or lesser amount of receipt of profit against the sales revenue of the export L/C, profit is charged by forming Bai-Muajjal investment.	-.31	-.40	-.64
Before the asset is ready to generate money, "gestation period" rent is levied	-.51	-.22	.80
Sometimes Rent on rent is charged	-1.28	-1.25	-1.12
When Bai-Muajjal and Bai-Murabaha Investment are converted to Hire Purchase, rent is levied without demonstrating the bank's proprietorship of the asset	-.16	.00	-.27
In Musharaka and Mudaraba, the partners are entitled to a lump sum profit, or profit is determined as % of capital	-.21	-1.50	-.86
In Musharaka and Mudaraba, the profit % is deferred until the realization of profit.	-.10	.00	.08



**Table 8.**  
**Mean Shariah Compliance Scores of Investment Modes and Operational Activities**  
**(Continued)**

	<b>Full- fledged Mean</b>	<b>Islamic Branch Mean</b>	<b>Islamic Window Mean</b>
Average	-0.27	-0.54	-0.28
<b>Contract Documents (CD)</b>			
Blank Agreement form(s) are being filled out with the client's signature.	-1.02	-1.50	-.25
The branch managers' signature is not included in the agreements.	-1.31	-1.75	-1.55
The investment client applies for TT/DD/PO by himself rather than through branch officials	-.34	-1.57	-1.10
There is no branch-generated post-purchase inspection report	-.49	-.44	-.37
Average	-0.79	-1.31	-0.82
<b>Receipt and disbursement of goods (RD)</b>			
In place of the bank officer, the investment client receives commodities	.60	1.43	.80
The client and the branch do not bargain about the price of the items	-.46	-.14	-.21
Islamic bank appoints its customer as its purchasing agent under Murabaha financing	1.07	1.50	-.72
Buying agent involvement in items not allowed by the bank	-1.22	-1.43	-.80
Existence of the supplier of goods/commodities is not found	-.72	.00	-.05
There is no proof that the client got items from the branches	-.06	-.33	.37
There is no proof that the branch got any products from the suppliers	-.17	.25	.11
Without sending representatives to the location to receive and examine (in the case of a buying agent) the products, these are passed to the customer	.20	.56	.35
For selling the items under the dealership or Murabaha Post Import Investment (MPI), the client's letter of authorization is not required.	-.73	-.80	-.85
For HPSM, the client did not get the asset	-.97	-1.00	-.56
Average	-0.246	0.004	-0.17
<b>Financial charges for delay (FC)</b>			
In borrowing by credit card, the bank charges the customer an extra amount in the event of a delay in payment of the Qard amount	.23	1.83	.56
The date for the client's payment is extended by the bank in exchange for an additional charge.	-.20	-.38	-.13
A penalty clause is included for the client's delay in the delivery of the commodity or in payment of the Qard amount	.61	1.14	-.07
In the event that the lessee is late with payments, the lessor will stipulate an increase in the rent that is payable	.00	-.20	.00
<b>Average</b>	<b>0.16</b>	<b>0.59</b>	<b>0.09</b>

Source: Field Survey 2022

The above table shows that among the three banking groups, the average Shariah scores for investment mechanisms are heterogenous. The study reveals that full-fledged Islamic banks and Islamic windows adhere to Shariah rules in all investment mechanisms, except for asset ownership, as banks do not have prior ownership of assets either physically or constructively. However, they follow Shariah rules when disclosing asset specifications, avoiding prohibited items when making investment decisions, and falsifying trading for default investors. Interestingly, none of the Islamic branches have Bai-Salam, Bai-Istisna, and Ijarah Muntahina Bittamleek modes of investment. Islamic branches are not complying with Shariah regarding cost disclosure in Murabaha and providing goods instead of cash.

In terms of cash memos, full-fledged banks, and Islamic banking windows are found to be Shariah compliant in all aspects, except for charging profit at the agreement stage in Bai-Salam transactions. Banks are found to be Shariah non-compliant in receiving goods by unrightfully parties, appointing their own customers as purchasing agents in Murabaha financing, and indifferent in non-complying Shariah in physical inspection and handing over goods to clients. Banks are Shariah non-compliant when charging delayed payments, except for undue extensions of payment deadlines for additional payments. Some Islamic windows are complying with Shariah rules in 'sanctioning penalty clauses for delayed payment of commodities and Qard amounts. However, full-fledged banks and Islamic banking windows are neutral in the stipulation of rental due in case of delayed payment by the lessee, while Islamic branches are complying.

Overall, full-fledged banks outperform Islamic branches in investment mechanisms and both Islamic branches and windows in receipt and disbursement of goods. Islamic branches comply with the Shariah better than the other two in charge of profit and contract documents. On the other hand, Shariah compliance of Islamic windows in investment mechanisms, cash memos, and financial charges for the delay is better than the other two modalities of Islamic banks.

#### 4.2.2. Difference in Compliance among Different Banking Systems:

**Table 9.**  
**ANOVA Test to Identify the Difference in Shariah Compliance Scores among Different Banking Systems**

Banking aspects		Sum of Squares	df	Mean Square	F	Sig.	Decision about $H_0-1$
Investment Mechanisms	Between Groups	1.964	2	.982	1.916	.151	accepted
	Within Groups	80.950	158	.512			
	Total	82.914	160				
Cash Memos	Between Groups	.864	2	.432	.679	.509	accepted
	Within Groups	100.576	158	.637			
	Total	101.441	160				
Charging of Profit/Rent	Between Groups	.780	2	.390	.574	.564	accepted
	Within Groups	107.959	159	.679			
	Total	108.739	161				

**Table 9.**  
ANOVA Test to Identify the Difference in Shariah Compliance Scores among Different Banking Systems (Continued)

Banking aspects		Sum of Squares	df	Mean Square	F	Sig.	Decision about $H_0$ -1
Contract Documents	Between Groups	2.627	2	1.313	1.817	.166	accepted
	Within Groups	114.176	158	.723			
	Total	116.802	160				
Receipt & Disbursement of Goods	Between Groups	.389	2	.194	.399	.672	accepted
	Within Groups	76.508	157	.487			
	Total	76.897	159				
Financial Charges for Delay	Between Groups	.984	2	.492	.469	.627	accepted
	Within Groups	156.504	149	1.050			
	Total	157.489	151				

Source: SPSS output

This ANOVA test result reveals an interesting insight into the Shariah practice in different activities. Irrespective of the banks' categories, whether they are full-fledged or non-full-fledged, they have similar practices, and there is no significant variation in Shariah compliance level since the p-value between groups for every variable is greater than the 5% level of significance.

#### 4.2.3. Identifying Significant Shariah Non-compliance Areas

**Table 10.**  
One Sample t-test for Testing the Level of Significance of Shariah Practice

	Test Value = 0							Decision about $H_0$
	t	Mean	df	Sig. (2-tailed)	Mean Difference	95% C. I. of the Difference		
						Lower	Upper	
INV_Avg	-9.694	-.550	160	.000*** (.05673)	-.55000	-.6620	-.4380	$H_0$ -3 rejected <sup>a</sup>
CM_Avg	-6.605	-.414	160	.000*** (.06275)	-.41451	-.5384	-.2906	$H_0$ -4 rejected <sup>a</sup>
CP_Avg	-6.893	-.445	161	.000*** (.06457)	-.44506	-.5726	-.3176	$H_0$ -4 rejected <sup>a</sup>
CD_Avg	-11.96	-.805	160	.000*** (.06734)	-.80590	-.9389	-.6729	$H_0$ -4 rejected <sup>a</sup>
RD_Avg	-4.332	-.238	159	.000*** (.05498)	-.23817	-.3468	-.1296	$H_0$ -4 rejected <sup>a</sup>
FC_Avg	1.231	.102	151	.220 (.08284)	.10197	-.0617	.2656	$H_0$ -4 rejected

Std. Error in parenthesis. \*\*\*p<0.01; \*\*p<0.05; \*p<0.1; <sup>a</sup> p<0.05 of t-statistic with negative value indicates significant Shariah compliance

Compared to the Shariah non-compliance by banks from the investment client's perspective, table 10 shows quite the opposite results. Bankers have responded in a way that they are vigilant of Islamic Shariah practice, and they strictly obey the Shariah rules. Except for imposing financial charges for the delay, banks are significantly complying with the Shariah rules in performing banking activities. Only in the case of charging financial penalties and compensation for delay are banks violating Shariah rules on average, which is not significant in practice.

### 4.3. Shariah non-compliance from Depositors' Perspective

#### 4.3.1 Comparing mean Shariah Compliance Scores in Deposit Schemes among Different Types of Banks

**Table 11.**  
**Comparing mean Shariah Compliance Scores in Deposit Schemes**

	Full- fledged Mean	Islamic Branch Mean	Islamic Window Mean
<b>Shariah Noncompliance in Providing Profit (PP)</b>			
Profit (not hibah) is provided against the Al-Wadiah deposit account	-.49	-.75	-.64
The profit rate is fixed in the Mudaraba deposit account	-.15	-.17	.00
The profit rate is fixed in a long-term/investment deposit account	-.18	.00	-.46
The profit rate of Islamic banks resembles the interest rate of conventional banks	-.51	-1.29	-.10
Average	-0.332	-0.552	-0.3
<b>Shariah Noncompliance in Information Disclosure (ID)</b>			
Depositors are not well informed about the terms and conditions of the contract with the Islamic bank while opening a deposit account	.19	.86	.67
Islamic banks do not disclose the bearing of loss, if any, by the depositors.	.77	1.14	1.14
Islamic banks do not disclose to clients all the available deposit product offerings that fit clients' financial goals.	-.01	-.43	.10
Average	0.32	0.52	0.64
<b>Shariah Noncompliance in Lending Principles (LP)</b>			
In borrowing against an Al-Wadiah deposit account through an overdraft facility, account holders are charged an extra amount over the principal amount borrowed	.09	.00	.80
In borrowing against Mudaraba deposit account, customers can get advances which are to be repaid in an extra amount over the principal amount borrowed	-.15	.00	.57
In case of borrowing through a credit card, the bank charges the customer an extra amount in the event of a delay in payment of the Qard amount.	.16	1.00	.29
Average	0.03	0.33	0.55
<b>Shariah Noncompliance in Deposit Principles (DP)</b>			
Al-Wadiah deposit account holders have to bear losses	-.11	.50	-.38
Mudaraba savings/ investment deposit account holders don't bear any loss in spite of the net operating loss of the Islamic banks.	1.02	.83	1.05

**Table 11.**  
**Comparing mean Shariah Compliance Scores in Deposit Schemes (Continued)**

	Full- fledged Mean	Islamic Branch Mean	Islamic Window Mean
Islamic shows negligence in distributing profits from closed Mudaraba accounts.	-14	-17	.50
Islamic bank offers Lakhopoti, Kotipoti, Double Benefit, etc. scheme	-.50	-.86	.29
Average	0.067	0.075	0.365
Grand Average	-.0007	0.04	0.27

Source: Field survey, 2022

Table 11 shows the mean scores of full-fledged Islamic banks, Islamic bank branches, and Islamic windows. Banks are not providing profit against Al-Wadiah accounts, Mudaraba savings, and long-term investment accounts and do not disclose all terms and conditions of contracts. They do not disclose bearing losses by depositors. Islamic branches do not charge extra amounts over principal borrowed, while Islamic windows are non-compliant and charge extra profit. Full-fledged and Islamic windows comply with Shariah rulings regarding bearing losses by Al-Wadiah deposit account holders, but Islamic branches are non-compliant in this. Depositors agree that Mudaraba savings/investment deposit account holders do not bear any loss despite the net operating loss of Islamic banks. Negligence in distributing closed Mudaraba accounts' profit is shown for Islamic windows only. Full-fledged banks and non-full-fledged Islamic branches do not offer Lakhopoti, Kotipoti, and Double Benefit schemes and comply with Shariah in this regard, while Islamic windows are found to be Shariah non-compliant in scheme offering.

Overall, full-fledged banks outperform Islamic branches or windows in Shariah compliance in information disclosure, lending principles, and deposit principles. On the other hand, Islamic branches outperform full-fledged banks and Islamic windows in Shariah compliance in providing profit to depositors.

## 4.3.2. Difference in Shariah Compliance Scores in Deposit Schemes

**Table 12.**  
ANOVA Test to Compare the Difference in Shariah Compliance Scores among Different Banking Systems

Banking aspects		Sum of Squares	df	Mean Square	F	Sig.	Decision about $H_0-1$
Providing Profit	Between Groups	3.505	2	1.752	2.213	.112	
	Within Groups	139.351	176	.792			accepted
	Total	142.856	178				
Information Disclosure	Between Groups	2.353	2	1.177	1.049	.352	
	Within Groups	198.458	177	1.121			accepted
	Total	200.811	179				
Lending Principles	Between Groups	4.343	2	2.172	2.493	.091*	
	Within Groups	56.629	65	.871			accepted
	Total	60.972	67				
Deposit Principles	Between Groups	5.946	2	2.973	3.608	.029**	
	Within Groups	142.564	173	.824			rejected
	Total	148.511	175				

\*\*p<0.05; \*p<0.1

The ANOVA test result shows that except for deposit principles, there is no significant difference in Shariah compliance scores in deposit schemes among different banking systems as  $p > 0.05$ .

## 4.3.3. Identifying Significant Shariah non-compliance Areas

**Table 13.**  
One Sample t-test for Testing the Level of Significance of Shariah non-compliance

Test Value = 0								
	t	Mean	df	Sig. (2-tailed)	Mean Difference	95% C. I. of the Difference		Decision about $H_0-2$
						Lower	Upper	
PP_Avg	-5.819	-.3897	178	.000*** (.06696)	-.38966	-.5218	-.2575	rejected <sup>a</sup>
ID_Avg	4.363	.3444	179	.000*** (.07895)	.34444	.1887	.5002	accepted
LP_Avg	-.021	-.0025	67	.983 (.11568)	-.00245	-.2334	.2285	rejected <sup>a</sup>
DP_Avg	.409	.0284	175	.683 (.06944)	.02841	-.1086	.1655	rejected

Std. Error in parenthesis. \*\*\*p<0.01; <sup>a</sup>p<0.05 of t-statistic with a negative value indicates significant Shariah compliance

In paying out profit for depositors' accounts, banks comply significantly with Islamic Shariah, as per depositors, while the banks are violating Shariah in disclosing relevant information to the depositors. However, neither compliance with loan principles nor non-compliance with deposit principles is significant in practice.

Overall, the Shariah compliance level of Islamic banks, irrespective of their category, is heterogeneous. On average, Shariah compliance varies among the respondent groups and among different investment and deposit schemes. It is worth noting that there is no difference among the bank types in the level of Shariah compliance, and the full-fledged banks are not in a better position regarding Shariah compliance.

#### **4.4. Discussion of Findings**

Analyzing the survey responses, this study documents some interesting and insightful findings. Responses regarding areas where the banks violate Islamic Shariah substantially vary among bankers and clients. Bankers perceive Islamic banks as Shariah-compliant, while the view is opposite in the case of clients. Most bank officials regard the clients as having insufficient knowledge and awareness about Shariah principles, which is also reflected by our experience surveying the clients. The majority of the time, the clients attempt to exploit cash facilities similar to those offered by traditional banks. Perhaps this practice is a result of improper and weak Shariah governance. The Islamic banking system is thought to be well-organized by certain bank executives, and some banks work to uphold shariah compliance. However, the bankers' negligence and lack of shariah knowledge make it difficult to comply with the shariah.

The Bai-Muajjal and Bai-Murabaha are found to be the vulnerable modes, as per the opinion of bankers, which is also supported by Ullah (2014). The assets acquired through these contracts are not in physical or constructive custody of the banks. According to bankers, small investment clients are unable to provide cash memos. In that case, bankers prepare cash memos based on clients' information. Investment modes are crucial since they are the places where all non-compliance is discovered. This occurs as a result of the banks' decision to emphasize profit over shariah compliance in order to compete with conventional banks by serving profit-driven clients. This insight is in line with Saeed et al. (2023) that banks facilitate clients' profit-making tendencies.

The existing Islamic banking system is thought to be similar to the conventional banking system. The public trust in this banking system has declined over time despite the financial success and stability of the banks compared to their conventional counterparts. The central bank has to form a separate body and provide strong guidelines to supervise the activities of Islamic banks, branches, and windows to ensure shariah compliance.

## **V. CONCLUSION AND POLICY IMPLICATIONS**

Islamic banking, an alternative banking system, aims to maximize social and economic welfare by minimizing income and wealth inequality. It operates under

the Islamic law, making Shariah compliance crucial for banks to maintain their status, customer loyalty, and financial stability. This study assesses the level of Shariah compliance in Bangladesh's Islamic banking industry in three categories.

The study's findings have significant policy implications for a variety of stakeholders, including banks' management, regulatory bodies, and policymakers. The management of Islamic banks can play an influential role in ensuring banks' Shariah compliance by tightly monitoring banks' operations through effective Shariah audits and control mechanisms. Additionally, banks' management can improve the independence and effectiveness of the Shariah supervisory board, which could consequently result in improved Shariah governance for the banks. At the regulatory bodies' end, the urge for a separate Islamic banking law is crucial, and the central bank can work with policymakers to develop a dedicated Islamic banking law to alienate Islamic banks from the conventional banking rules. Moreover, the government can employ effective Shariah supervision through the country's central Shariah board. This study also suggests policymakers and other stakeholders initiate awareness and training programs for both bankers and clients to fill the knowledge and expertise gap in maintaining shariah rules in banking activities. Furthermore, policymakers should acknowledge the need for the establishment of academic and knowledge-creation institutions and act accordingly to develop proper knowledge in innovating novel shariah-compliant banking products that can facilitate customers' needs. However, this study is not out of limitations. Similar to the previous studies, the small sample size is one of the major shortcomings of this study. Therefore, future research should consider large sample size data with the broader perspectives of shariah compliance issues.

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