

**Speech of His Excellency the Governor of the Central Bank of Kuwait,  
Dr. Mohammad Y. Al-Hashel,  
on the Occasion of the Opening Ceremony of  
The 5<sup>th</sup> Conference of the Islamic Financial Institutions,  
Arranged by Shura Sharia Consultancy Company  
(Kuwait, 16 - 17 December 2013)**

**In the Name of Allah, Most Gracious, Most Merciful**

Praise be to Allah, Lord of the worlds. Peace and blessings be upon His Honest Messenger, His family, His companions and His followers until the Day of Judgment.

**Distinguished Scholars,  
Esteemed Attendees,**

**Assalamo Alaykom,**

It gives me great pleasure to welcome you all in this august forum, and to express my overwhelming happiness that the State of Kuwait is hosting the Fifth Conference of the Islamic Financial Institutions, and the attendance of distinguished Islamic scholars, experts and specialists in the field of Islamic finance industry. I wish you all a pleasant stay in Kuwait, your second

homeland, and thank you for your participation and travel. I would like to express gratitude and appreciation to Shura Sharia Consultancy Company for their notable efforts in the good organization of this conference, and I am thankful to Professor Dr. Ajeel Jasem Al-Nashmi, President of the Conference, for the kind invitation extended to me to participate in this distinguished forum. I am confident that this event will enrich the dialogue and discussions about cases/issues related to the Sharia-compliant banking and financial business and in discussing methods of developing Sharia supervision of Islamic financial institutions, determining the nature of challenges that face the Islamic financial industry, and considering ways to overcome these challenges in order to support the Islamic banking business and establish it on a strong basis.

**Dear Brothers,**

Let me take this opportunity to briefly underline some points that I believe could be of importance as we all are concerned about establishing a suitable environment for developing practical mechanisms for the Islamic financial industry. I will cover these points under four main themes. The first one pertains to the real increasing importance and significance of the Islamic financial industry and the need to develop it. The second theme presents a vision of some challenges and risks that face this industry and the ways to overcome them. The third will shed light on a subject that I think is gaining attention from all of us which is governance of Sharia supervision activities and its development. Finally, I will briefly elaborate upon the experience of the State of Kuwait in the field of Islamic financial industry.

**Distinguished Attendees,  
Esteemed Guests,**

The global banking and financial map shows the worldwide spread of the Islamic Finance Industry which has traversed local and regional boundaries. In fact, this industry has entered a new phase of real maturity, whether in the vision and objectives or strategies and methodologies. The Islamic financial industry has become an integral part of the global financial and economic reality. This is evident in the remarkable growth of Islamic financial industry through the last years in terms of the growing volume of assets managed under Islamic business, issues of sukuk and Islamic investment funds, in addition to the ongoing growth of the number of the Sharia-compliant financial institutions.

Estimates indicate that the global market of Islamic financial services, measured by the size of Sharia-compliant assets, has reached above US\$ 1.7 trillion by now, recording a quantum leap from a paltry US\$ 150 billion in mid 1990s. In the same manner, the number of Islamic financial institutions has increased in parallel to more than 600 institutions operating in more than 75 countries around the world. Moreover, the Islamic sukuk market has achieved prominent growth. Issues have reached about US\$ 140 billion in 2012, hitting historic highs. While these developments are indeed encouraging and reflect the solid fundamentals of Islamic banking globally, it remains below our ambitions, taking into account that the Islamic finance is still merely 1% of the global financial system - a very modest share.

We have all noticed that interest in the Islamic financial industry is becoming less confined to Muslim countries or Muslims. As a matter of fact, it has become interesting to all players in the financial field all over the world. This mainly arises from the fact that the controls governing the Islamic Finance Industry are based on ethical methodologies, particularly sharing profits and losses, and focusing on the real economy away from speculation. These methodologies attract and expand the demand for Islamic financial services. In light of this development, it is time for all who are connected to this industry to cope with the quantitative and qualitative changes in the activities of the Islamic banking and financial business. This can be achieved by establishing an environment that can develop and uphold the capabilities and resources of the Islamic financial institutions. Only then, can they undertake their vital role in establishing strong/effective bases for new banking and financial systems that will have diversified instruments and activities, and will be capable of supporting such base within the global financial system.

Here, I should underline that the call for development is not limited to growth in size or number of institutions, but more importantly, it should be planned growth established on sound foundations that guarantee suitable success and progress.

**Distinguished Attendees,**

I do not want to elaborate upon the status of the Islamic financial industry and its increasing importance especially as it is becoming evident to everyone. So, I would like to turn to the second theme regarding the

challenges and risks that confront this industry and the means to overcome them.

Sharia-compliant financial transactions go hand in hand with the need for a Sharia opinion which has to be aligned to the essence and nature of the financial transaction. It should emerge from a clear knowledge of its characteristics and outline, and from a broad and deep Sharia perspective to finally devise the Sharia opinion. Arguably, it is not a simple task. Taking the responsibility of Sharia supervision in Islamic financial institutions needs distinguished scholars and specialists with deep background in the jurisprudential and Sharia rules, as well as being familiar with the changes and occurrences in financial transactions, instruments in general and those operating in accordance with Islamic Sharia in particular. This difficult equation might embody the most prominent challenge confronting the Islamic financial industry. That is, the availability of a qualified human capital for Sharia supervision in the Islamic financial institutions - especially with the rapid growth of the number of the Sharia-compliant banking and financial institutions and the increase in the diversity of its instruments, products and transactions.

Moreover, it is clear now that the underlying risks in banking and financial transactions are becoming much larger, whether the institution is conventional or Islamic, which cannot be overlooked, especially with the frequent recurrence, severity and the increasing possibility of being hit by crises that strike the global financial system - At this point I would like to confirm that the Sharia-compliant banking and financial entities are not only facing risks such as those faced by their counterparts of conventional

entities, but in addition, these entities are also facing other risks related to diversified Islamic financial instruments which should be Sharia-compliant. Moreover, risks may be more severe and detrimental for Islamic banking and financial entities, due to the relatively high concentration of activities of many Islamic financial institutions. These risks may become more severe due to the relatively limited number of risk-hedging instruments that are Sharia compliant, which is also one of the main challenges facing the Islamic financial industry. In this context, I would like to mention that the operational practices have uncovered that the main factor associated with the success of Islamic financial institutions is related mainly to their ability to manage these risks with the highest levels of performance proficiency and efficiency.

In general, therefore, there is a need for programs to improve the level of governance and to develop financial markets that can embrace a range of Sharia-compliant financial instruments, and to exert more effort to invent/design and develop diversified and effective Sharia-compliant risk-hedging instruments.

**Esteemed Guests,**

My third theme will focus on the issue of governance of Sharia supervision activities and the means to develop it. I know that the fifth Jurisprudential Conference of Islamic Financial Institutions addresses many events and issues that may be mostly centered on the subject of Sharia supervision of Islamic financial institutions, which is in fact the focus of the supervisory and oversight authorities and all those who are involved in this industry.

Certainly, Sharia supervision has become a science having its own fundamentals, mechanisms and intermingling techniques among the conventional audit precepts and the Sharia requirements. These in essence emerge from the fundamental importance of Sharia rules and controls and aim at specifying the general framework of the organizational plans and the adopted methodologies and mechanisms in the process of auditing. This in effect bolsters the capacity of the management of each institution at making decisions in order to protect its assets and face different types of risks and challenges.

The concept of supervision, whether conventional or Islamic, does not differ considerably in terms of target and goals. However, the concept of Sharia supervision has its unique features that emerge from the type of transactions that characterize Islamic financial institutions, which are different in their nature to typical transactions performed by conventional banking institutions. Undeniably, that unique feature of Islamic finance poses different kinds of challenges that necessitate the presence of a strong Sharia supervision governance fundamentals to consider all risks facing Islamic financial institutions, especially in an environment where conventional and Islamic banking services co-exist, and to provide appropriate regulatory frameworks that suit their activities.

**Distinguished Attendees,**

The theoretical concepts related to Sharia supervision on Islamic financial institutions are clear to all. So, I would like to highlight the work mechanisms of Sharia supervision authorities in accordance with the main

four principles of governance, i.e. fairness, accountability, transparency and specification of responsibility. However, the functional practices have uncovered a handful of challenges that should be prudently and efficiently dealt with so that the work of the Sharia supervision authorities can proceed on sound grounds. It will not be an exaggeration if I concede that one of the most prominent challenges is that not sufficient attention is paid to make sure of compliance with Islamic Sharia rules or what is known as the subsequent Sharia audit. Usually, the responsibility for fatwa and subsequent Sharia audit are assigned to the Sharia supervisory authority maintained by most Islamic financial institutions. This practice is by no means in line with the Sharia supervision governance fundamentals. So, while we are trying to develop the work of Sharia supervision and face the present challenges, I believe that there should be clear and specific professional frameworks for the duties and responsibilities of Sharia authorities and Sharia internal audit. In this context, we can refer to the history of development of the audit profession to be considered as a role model and to benefit from conventional guidelines regarding this matter. This should be undertaken in cooperation with competent regional and international authorities which will save much effort and time. Furthermore, I believe that we can consider the idea of establishing an independent legal entity that will take the responsibility for the regulation and development of the work of Sharia audit and supervision.

**Esteemed Guests,**

I would like to point out another equally important element, which is the independent nature of the Sharia supervision authority in Islamic financial



institutions. As a matter of fact, the Sharia authority should have free reign for issuing fatwas and Sharia rules in accordance with the precepts of due diligence and conditions of fatwa without any interference from top management of the institution in question. This will enhance confidence of stakeholders and clients in the soundness of transactions from Sharia perspective.

Possibly you will all agree with me that one of the most visible challenges that face the Islamic banking and financial business is the limited number of Sharia scholars who are specialized in jurisprudence of transactions, and are consequently qualified for membership of Sharia supervision authorities in the Islamic financial institutions, especially when one takes into account the rapid increase of the number of Sharia-compliant banking and financial institutions. With this relatively limited number of Sharia scholars, we notice that the members of Sharia supervision authorities in Islamic financial institutions can be associated with many authorities, which, of course, carries an element of pressure in terms of time and effort necessary for conducting their duties in the most efficient manner.

If we consider that the knowledge, and literature of conventional finance economies has developed over several decades, so as to cover the theoretical aspects of finance in a comprehensive manner - unlike Islamic finance economies. That said, there is an urgent need for strengthening the role of educational institutions and research entities to represent the main source of knowledge, contribute to the establishment of theoretical foundations, and to qualify members as Sharia scholars through studying modern methodologies in financial and economic sciences together with Sharia studies. Also,

attention should be paid to improving the practical experience through intensive training courses and imparting experiences among Islamic financial institutions. This would result in members of Sharia supervisory authorities acquiring the necessary jurisprudential skills to perform their duties. He would be able to issue jurisprudential opinions or assess conditions for emerging financial issues and transactions based on scientific grounds that are derived from the Sharia science and financial and economic sciences.

### **Distinguished Attendees,**

As we are trying to face these growing challenges, it is necessary to establish initiatives for broad dialogue and to open communication channels between stakeholders and scholars in Sharia supervision on one side, and concerned supervisory institutions on the other. I believe that such initiatives may greatly contribute to reaching agreement on a road map that could be drawn up by experts and specialists in scientific and theological authorities. The objective of such a road map would be to develop Sharia supervision and to achieve a distinguished and effective professional position which will assist in achieving the developmental objectives of the financial and economic sectors.

### **Esteemed Guests,**

The experience of the State of Kuwait in terms of Islamic financial industry will be the last theme. As you know, the State of Kuwait is one of a handful of countries throughout the globe that witnessed the inception of Islamic

financial industry, and which then became a main part of its banking and financial sector. The first Islamic financial institution in the State of Kuwait was established in the year 1977. That was followed by successive establishments of a number of Sharia-compliant financial institutions. Presently, there are five Sharia-compliant national banks registered with the Central Bank of Kuwait (CBK), in addition to a branch of a Non-Kuwaiti Islamic bank and fifty one Islamic investment companies.

Ever since the dawn of Islamic financial activities, the CBK has believed that it was necessary to work within a regulatory and supervisory framework that guarantees the soundness and efficiency of these activities. This belief has been incarnated in passing the Law No. 30 of the year 2003. The law has added a new section concerning Islamic banks to the third part of Law No. 32 of the year 1968 concerning Currency, the Central Bank of Kuwait and the Organization of Banking Business. The law has vested in the CBK the responsibility of laying down and the execution of prudent regulatory and supervisory controls for the work and activities of the Islamic banks operating in the State of Kuwait, providing that these policies and controls should be in line with the best international standards and practices in this field. The importance of the supervisory and oversight role of the CBK on Islamic banks emerges from the fact that it guarantees the soundness and strength of the activities, liquidity and solvency of these banks, and ensures that they have robust financial positions. In addition, it preserves the rights of their customers and business counterparts.

The responsibility for Sharia supervision is assigned to the Sharia supervisory authority at each Islamic bank. The Sharia supervisory authority

is charged with submitting an annual report to the General Assembly of the bank. This report should include the opinion of the Authority about the level of compliance of the banks' works to the rules of Islamic Sharia together with any additional observations in this regard.

**Distinguished Attendees,**

Lastly, I should like to express my opinion that the Islamic financial industry has really achieved a remarkable progress through the last decade. It has, in fact, exceeded the phase of being an emergent industry and has now become a prominent part of the global financial system. In order to uphold this ongoing progress and growth, it requires concerted efforts from all the parties involved in this industry to create an integrated institutional system, to ensure the provision of the necessary regulatory and legal structures and frameworks that are necessary for undertaking the operations and activities of the Islamic financial industry on sound grounds and supporting/upholding the role of the supervisory authorities and the activities of the Sharia supervision, and to pay attention to issues such as education and training as well as enhancing the professional competence of people employed in this industry.

Undoubtedly, the rapid development of matters relating to financial activities in general, and the Islamic financial industry in particular, pose more challenges to us which call for boosting morale and the combining of efforts to deal with them counting on our capabilities, resources and our awareness of the requirements of this age while committing to the path of Allah and the Sunna of his Chosen Prophet (May Allah bless him). I believe

that this conference with such distinguished attendees creates an inspiring environment for dialogue and initiatives which will contribute to the progress and prosperity of the Islamic financial industry.

I wish you all success and a comfortable stay in the country and our final prayer is Praise be to Allah, Lord of the worlds.

Assalamo Alaykom.