Antecedents of Islamic Corporate Governance: Evidence from Major Cities of Pakistan

Muhammad Awais*[1], Qaisar Ali Malik[2], Naeem Ullah[3]

[1*]HoD/Associate Professor, Department of Economics & Finance, Foundation University Islamabad, Pakistan.

[2]Dean/ Professor, Faculty of Management Sciences, Foundation University Islamabad, Pakistan.

[3]Associate Professor, Department of Business Administration, Foundation University Islamabad, Pakistan.

Corresponding author: m.awais@fui.edu.pk

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Islamic corporate governance is different from conventional corporate governance, as it's purely based on shariah laws. This paper aims to identify the antecedents of Islamic Corporate Governance based on the subjective approach behind taking the interviews of experts from the field. According to the report, Structure, Independence, Heterogeneity, Monitoring, Shareholder Activism, and Disclosure are the main forces behind Islamic corporate governance. The study's theoretical contribution is that it identified several important antecedents for organisations' adoption of Islamic corporate governance. The study's practical implication is that it might now be simple to identify and assess Islamic corporate governance procedures.

1. Introduction

Corporate governance includes a systematic framework for senior managers to answer to shareholders. It is not, however, restricted since it addresses the entire web of official and informal interactions, including those in the business world and the ramifications for society as a whole. It deals with managing and exerting control over various parties by functioning as a corporate charter and promotes collaborative management. To manage jointly, everyone must have a same degree of knowledge, but this can be advantageous or problematic for an organisation depending on the situation. For example, having a high level of education would facilitate better governance, but everyone who is educated would want to be involved in management (Hasan, 2009; Vigoda-Gadot & Mizrahi, 2024). Corporate governance helps investors as well as the organisation since it allows the firm to raise capital and manage its operations without needing to make all of the investments themselves, and it allows investors to participate in the profits without having to do any operational tasks. Because no two businesses can operate under the same rules and principles and because every company has different objectives, corporate governance varies across different locations, areas, sectors, and organisations (Larbsh, 2015; Nguyen et al., 2024).

Conventional corporate governance and Islamic corporate governance have different tenets. According to conventional corporate governance, corporations have a duty to answer to their stakeholders and shareholders. Conventional company governance is infused with a more comprehensive notion of accountability by the Shariah. In addition to shareholders and stakeholders, organisations also have to answer to Allah Almighty. Consequently, this expands and enhances the notion of corporate governance. Thus, increasing the security and confidence of the corporation's stakeholders and shareholders (Muneeza & Hassan, 2014; Zain & Abdullah, 2019). In non-Islamic organisations, both the firm and the investors participate in commercial operations to generate wealth, but in Islamic organisations, the investor is regarded as a business partner based on his share of investment and the benefit and risk are shared. Three main factors make up corporate governance: disclosure, accountability, and transparency. These elements need to be used in tandem; if one is not applied properly, the other determinants won't be able to meet their goals. The goal of Islamic corporate governance is far more sophisticated than that of conventional corporate governance, as these determinants are owed to Allah Almighty before to shareholders and stakeholders. This is in contrast to the former, where these determinants are owed to the company's stakeholders and shareholders. Islamic corporate governance's primary goal is to manage the business while taking Islamic law into account. The proper corporate governance framework is desperately needed by Islamic companies.

The current literature does not identify the antecedents of Islamic Corporate Governance, that maybe because Islamic Corporate Governance have not been adopted by Muslim countries as it should have been. This study aims to clearly identify antecedents of Islamic Corporate Governance. The study is unique in respect to the fact that the antecedents of Islamic Corporate governance has never been properly identified. There is a dire need to identify the antecedents of Islamic corporate governance, this identification will lead to initiation and support of future research on Islamic corporate governance. Therefore, this study intends to investigate some of the major antecedents of Islamic corporate governance.

2. Literature Review

Pakistan's Big Cities Provide Evidence of the Islamic Corporate Governance's Predictors (Fotiuh, 2010; Gul et al., 2024). Corporate governance can be defined as "the way in which boards monitor the functioning of a company by its management, and how board members are accountable to shareholders, stakeholders, and the firm" (Mahdavi & Daryaei, 2016). The idea of corporate governance was endorsed as a result of growing awareness of the importance of protecting the interests of all stakeholders, especially minority shareholders. It has been claimed that effective corporate governance is greater than just a good idea because it encourages investment flow, supports healthy capital markets, and minimizes the cost of capital (Al-Hiyari et al., 2024). The general consensus is that governance allows an organization to set specific objectives and work towards accomplishing them more effectively. In a similar way if properly administered, organizations may effectively fulfill their commercial and financial objectives and aspirations.

According to Lazonick and O'Sullivan (2000), the corporate governance structure is primarily composed of three elements: the allocation of investment returns, the sorts of investments made by organizations, and the individuals who make these decisions. These aspects of corporate governance are well-known to managers and executives in the business world, and Shari'ah-compliant organizations are particularly focused on these ideas. Those in charge of Islamic enterprises need to exercise extraordinary caution because a company's Shari'ah compliance depends on the source of capital, how it is employed, and how the return is distributed. since a company's future can be made or broken by its corporate governance.

To carry out the many responsibilities and goals of the business in a transparent and efficient manner, it is essential to establish good governance at every level of the company. An Islamic corporate governance system accomplishes these objectives in addition to Islamising the idea. A number of countries, including Malaysia, have released guidelines or standards for Islamic financial institutions regarding Islamic governance, along with suggestions for other organizations and institutions (such as AAOIFI and IFSB). However, the difficulty with these regulations or guidelines is that they are not relevant to all Islamic corporations, and they are not binding on the entire world, thus they cannot be uniformly adopted and implemented to all Islamic corporations.

Muneeza and Hassan (2014) stated that because the main point of Islamic corporate governance is to obey Allah. On the other hand, traditional corporate governance frameworks are inadequate for Islamic corporate governance. The following elements must be applied to all Islamic corporations, regardless of geographical locations for better governance.

1. Shareholders, demand depositors, regulators, financial market authorities, the Islamic Economic Community, and, last but not least, the general public are all stakeholders in Islamic enterprises. All of these parties along with their interests should be thoroughly analyzed and cared for by Islamic corporations within the confines of shari'ah.

2. The parties to whom the Shari'ah Committee owes a duty of care must be given a right to sue the Shari'ah Committee's part is proven in case of sheer negligence.

The literature suggests that the following factors should be included as antecedents of Islamic Corporate Governance:

2.1 Shariah Board

Shariah board comprises of Shariah experts having best knowledge and expertise in Shariah jurisprudence. The issues regarding business can be tackled in several ways by different Shariah scholars having diversified knowledge and competencies hence boosting innovations. More clients will be attracted by different Shariah board members or scholars, this can in turn help businesses to enhance their productivity and efficiency (Grassa, 2016; Safiullah et al., 2024).

2.2 Shariah Audit / Review Committee

The Islamic financial institutions comprises of an independent Shariah review or audit committee which act as a governing body to keep track of Shariah activities. The main duty of this committee is to supervise, direct and review the activities and transactions in the light of Islamic jurisprudence. While Shariah board takes care of the Shariah compliance of the financial products and transactions (Echchabi & Abd. Aziz, 2014; Kolsi & Grassa 2017; Tawfik & Elmaasrawy, 2024), role of Shariah audit is assisting the Shariah board in reviewing and monitoring the day-to-day activities. In IB context it has been seen that financial performance of a firm can be increased by quality Shariah audits and reviews (Minaryanti & Mihajat, 2024; Othman & Ameer, 2015).

2.3 Shariah Board Size

Jensen and Meckling (1976) presented the agency theory stating that principal and agents are interconnected in a firm. The company being principal appoint Shariah Supervisory Board (SSB) as an agent that works on company’s behalf. Shariah members are very crucial in the usefulness of Shariah Board. Shariah jurists are members of Shariah boards being aware of the financial markets and having expertise about financial laws of Islam. Each Shariah board must consist of at least three experts having competencies and experiences in relevant domain. (Riyadh et al., 2024). There is a consensus on maximum number of Shariah board members being at most seven (Ben Zeineb & Mensi, 2018).

2.4 Board Independence

The investors being principals of the company appoint Board of Directors (BOD’s) as agents. The management of the company in no way should control the leadership of the board as BOD’s are supposed to efficiently and effectively monitor the day to day activities of the business. If the BOD is independent, there would be an efficient performance, better and unbiased decision making prioritizing the interests of shareholders. In Islamic Banking context, the independent board is thought in aiding in a better performance of the firm (Abdul Rahim et al., 2024; Mollah & Zaman, 2015).

2.5 Chief Executive Officer Duality

CEO acting as a board president refers to CEO duality. The agency theory by Jensen and Meckling (1976) specifies that routine activities of the top management are observed by assigning duties to the agents in order to overcome the agency problems. Agency theory focuses that the CEO must have distinguished responsibilities as compared to the board chairman (Fama & Jensen, 1983; Jensen & Meckling, 1976; Stoelhorst & Vishwanathan, 2024). The responsibility of the CEO is to manage the day-to-day tasks while chairman’s duty is to control and develop policies and strategies for the board (Ben Zeineb & Mensi, 2018).

3. Methodology

The qualitative method was employed in this study to obtain respondents' in-depth responses. It was guaranteed that no information was provided before the participants, and no evaluation of potential rebuttals was exchanged. Furthermore, the interview-based multi-case study approach (Eisenhardt, 1989; Eisenhardt & Graebner, 2007) was employed to obtain comprehensive data and statistics pertaining to Islamic corporate governance. The facts were gathered through semi-structured talks. Several instances provide the opportunity to categorise forms and fundamental issues through in-depth analysis of themes and supporting data. The case study protocol, as outlined in Table 1 (Haddock-Millar et al., 2016).

The primary discussion questions centred on the study's issue, which is discern about Islamic corporate governance and how it contributes to organisations' success. This study's ability to identify several situation-specific perspectives allowed for a proportionate investigation of strategies related to the application of Islamic corporate governance with the goal of accelerating business growth.

The population of this study consisted of consultants on Islamic governance and specialists from Pakistani industry and academia. In-depth information was extracted through semi-structured talks. In addition, nearly 28 interviews with top executives and industry experts were scheduled for this study; 11 of them were conducted in-person, and the remaining 17 used an open-ended questionnaire (Table 2) - but, merely 23 plaintiffs gave comprehensive and sound responses as per the prerequisite of the study.

Table No 1. Case Study Protocol

Steps of the Case Study
1. To determine the study's scope and research emphasis
2. Determining which distinct prosperities are "multiple cases"
3. Supplementary formulation of the research questions
4. To determine the appropriate research instruments and study protocols, using semi-structured conversations and focus groups as approaches for collecting qualitative data.
5. To determine the "appropriate" contributors, a vertical and horizontal slice of the case studies containing expertise in human resource development and environmental management
6. August 2023 is the data gathering period.
7. Data analysis: case-specific analysis at a single subsidiary level 8. Progression of recurrent themes
8. Analysis of cross-cases
9. Coming to a close: the deluge of literature and data obtained
10. Dissemination: writing articles

Table No 2. Respondents of the Discussions

Job role	***Pakistan***
Category	
Islamic Corporate Governance Expert - Industry	16
Islamic Corporate Governance Expert - Academia	12
Total participants	28

Table 2's job roles demonstrate that every contributor possesses a wealth of knowledge about Islamic Corporate Governance and the current company practices. The primary debate topics are drawn from the body of research on Islamic corporate governance and popular governance techniques. The questions for discussion are included in Table 3.

The talks started off with a thorough discussion of the following topics: the industry's concept of Islamic corporate governance; top management's life-shaping decisions; stakeholders' psychosomatic insights; the sensitivity of governance decisions; and businesses' propensity for taking risks. Following that, the conversation shifted to the particular topics identified in the literature as well as the application of shariah-based concepts to governance. The one-to-one discussions sustained among 30 and 50 minutes and up to 55 minutes for each individual.

Table No 3. Discussion Protocol and Queries

Discussion protocol

Showcase the contestant(s) and interrogator(s).

Plan the research procedure

Describe how the research will be determined, together with its aims and objectives.

Talk about the research's potential results, ethical concerns, and get consent.

Draw the interview/focus group's structure.

Themes of the study and explicit queries

The Industry's Concept of Islamic Corporate Governance

1. What are the main controlling factors behind the Islamic corporate governance?
2. May you please share the numerous effects of conventional governance practices on the financial-economic condition of the businesses?

The life-shaping decisions of the Top Management

1. Do you think that shariah based corporate governance decisions are life-shaping decisions of the industry?
2. Why shariah based governance decisions are good as compared to conventional?

Stakeholder's psychological perceptions

1. May you please outline two or three utmost significant spiritual acuities of the Top Management and entrepreneurs at the time of policy making and decisions taking?
2. To how much extent, executives in the market may agree that they will take shariah based governance decisions.
3. What role do you play in order to convince executives for shariah based governance decisions?

Sensitivity of the governance decisions

1. How sensitive is the governance decision for the business?
2. How the level of efficiency (weak, semi-strong & strong) may change in the organization after the implementation of governance decision?

Risk-taking propensity of businesses

1. Do you think that majority of businesses are not interested in Islamic corporate governance practices? If “Yes”, then how you may encourage them towards Islamic corporate governance practices?
2. Conventional businesses may take either high risk or low risk. What do you think?

About you

1. What kind of concepts are vital for you at the time of taking governance related decisions?
2. What do you perceive as the main levers to do rational shariah based corporate governance decisions?

4. Results and Discussion

The program for qualitative analysis was used to analyse the interviews. In the majority of cases, it was observed that Islamic and conventional corporate governance were identical. The stakeholder's perspective and Shariah form the foundation of Islamic corporate governance, which is where the differences reside. Shariah laws and regulations served as the model for Islamic corporate governance. The agency conundrum is resolved by Islamic business governance, as the principle of taqwa supersedes any self-interest or betrayal of trust. Both the board and the management would report to and work for Allah. Therefore, the double accountability method will reduce the possibility of fraud and trust breaches. All the specialists in the area agreed that since the board will not act for its own financial gain, heuristic phenomena will work better in Islamic corporate governance. Protection of the assets and confidence of all parties involved will be their primary goals (Morgado et al., 2018).

According to an expert, the board's efficiency is diminished by duality because two distinct perspectives will each contribute a greater level of competence. Will therefore result in improved business performance. According to a different expert, after leaving the board, board members shouldn't be hired as chairman. Board will become independent and transparent as a result. The family-owned companies need to figure out how to lessen their influence and make the board independent. A combination of controlling and non-controlling shareholders as well as management should be included on the board. There are individuals of all nationalities living in Pakistan, and most enterprises have an impact on them all. Therefore, a true variety of cultures should be represented on the representation board. This will give shareholders a stronger sense of identification and ownership.

The difficulty businesses in Pakistan have is locating real and well-respected leadership. Since reputation is an objective term, a change in the board affects it. The efficacy and efficiency of the board ought to be assessed by an impartial outsider. A 360-degree strategy should be used, meaning that each board member should be assessed separately in addition to as a member of the board. The wealth of the shareholders should always have an impact on the directors' salary. This will act as an internal check on board members to protect the interests of shareholders. Islamic business governance mandates that withholding information that could cause loss is sinful. Only when information is complete and released on time can it be used to inform decisions. Therefore, all information that might be pertinent to the parties involved should be fully and promptly given.

5. Conclusion

The adoption of Shariah legislation and stakeholders' perspectives are the key areas where Islamic business governance and conventional corporate governance diverge. The results of this study may not be applicable to other contexts because the sample was limited to Pakistan. Heterogeneity, Structure, Disclosure, Shareholder Activism, Independence, and Monitoring are the main forces behind Islamic corporate governance. The study's theoretical contribution is that it identified a number of Islamic corporate governance antecedents that support the practice's adoption in organisations. The study's practical implication is that it might now be simple to identify and assess Islamic corporate governance procedures. The study's focus is narrow; further research should expand both the sample size and the study area.

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