

Shariah Supervisory Board Report - 2019

الحمد لله رب العالمين، والصلاة والسلام على خاتم الأنبياء والمرسلين، محمد المصطفى الأمين، وعلى آله وأصحابه أجمعين، وبعد:

All praises to Allah (ﷻ). This was the eighteenth year of Islamic commercial banking for Meezan Bank which is under review. During the year, the Shariah Supervisory Board (SSB) of Meezan Bank held five meetings to review various matters referred to them by the Bank.

Meezan Bank has a team of professionals in the Shariah Compliance Department (SCD) working under the guidance of SSB. The main objective of this department is to facilitate and ensure Shariah-compliance in all the new processes, procedures and products, refine existing products and procedures, manage Islamic banking trainings and awareness sessions and conduct Shariah-compliance reviews of transactions. The SCD also serves as secretariat to the Bank's Shariah Supervisory Board.

In addition to the above, a separate Shariah Audit Department (SAD) is working under the Board of Director's Audit Committee to review Shariah-compliance in the Bank's activities. This department submits its Audit report to the Resident Shariah Board Member (RSBM) and Shariah Supervisory Board for their information, review and determination of appropriate corrective actions.

We appreciate the efforts of the staff of Shariah Compliance Department and Shariah Audit Department for their efforts in promoting and strengthening the environment of Shariah compliance in the Bank.

It gives us comfort to observe high level of commitment of the staff, management and the Board members of the Bank. It is also encouraging to know that there are more than 11,500 staff members in the Bank who are a source of halal income for their families.

We are pleased to share the major achievements of Meezan Bank towards the cause of Islamic banking during the year ending December 31, 2019.

Research and New Product Development

The SSB recognizes the efforts of the SCD for conducting around 225 customer and industry visits to understand the business model and reviewing more than 3,000 different types of transactions as per the guidance of RSBM/SSB.

During the year, more than 23 Shariah-compliant syndicated transactions involving various structures such as Ijarah, Diminishing Musharakah and Running Musharakah were executed by the Bank under the supervision of RSBM/SSB. These transactions provided Shariah-compliant financial solutions to various Government and private entities such as National Power Parks Management Company (Private) Limited, Hub Power Company, Engro Powergen Thar (Private) Limited, Sindh Engro Coal Mining Company (SECMC). These syndicated transactions provided support to various needs including infrastructure development, capital expansion and project financing.

SSB is pleased by the Bank's efforts towards the execution of Rs 200 billion Pakistan Energy Sukuk which not only helped in reducing the issues of circular debt but also supported the liquidity deployment needs of the Islamic Banking Industry. It is also to be noted that during 2019, the Sukuk was also listed in Pakistan Stock Exchange and can be traded by institutions as well as individuals.

In line with the UNDP's Sustainable Development Goals and Meezan Bank's commitment to promote and lead Shariah-compliant Green Banking initiatives, the Bank provided Green Islamic syndicated financing solutions for five projects based on wind power generation plants to its customers NASDA

Green Energy (Private Limited), Metro Wind Power Limited, Gul Ahmed Electric Limited, Artistic Wind Power (Private Limited), and Din Energy Limited.

The Bank has actively supported the State Bank of Pakistan for adoption of various AAOIFI Shariah Standards in Pakistan and for resolution of numerous issues faced by the Islamic Banking Industry.

During the year, the Bank conducted Islamic Banking awareness programs for religious scholars, Parliamentarians, Bureaucrats and Government officials, both independently and in collaboration with IBA CEIF. The Bank's staff also met various Government officials to discuss and promote Islamic banking in Pakistan.

During the year, the SSB provided guidance for different matters, most noteworthy of them being:

- Approval for Shariah Structure of GoP Ijarah Sukuk on Jinnah International Airport Karachi
- Development of Product manuals for three Shariah-compliant refinance schemes namely Islamic Financing Facilities for Renewable Energy, Storage of Agricultural Produce and Modernization of SMEs
- Development of guidelines for development of a digital platform for providing FinTech financing solutions to its retail customers
- Development of guidelines for dealing with Fintechs under Electronic Money Institutions (EMI) regulations that are involved in facilitating payments and settlement related needs of the customers
- Approval for tailor made specialized low-cost housing finance product based on Diminishing Musharakah for the under-privileged segment of the society

Training & Development

SSB is pleased to note that the year 2019 was highly productive in terms of training and awareness of Islamic Banking Products. A special training session was also arranged for members of the Board of Directors of the Bank which was delivered by Dr. Imran Ashraf Usmani and Sheikh Esam M. Ishaq.

During the year, 100 training sessions comprising more than 1,450 man-hours were organized for staff members across the country catering to more than 3,800 employees of the Bank. This number includes orientation and batch trainings for new joiners, refresher programs like Asset Refresher, Deposit Refresher, Trade Finance & Treasury Operations and certification programs in Islamic financial products. Two Islamic Banking e-Learnings were launched covering 4,900 staff.

In order to create awareness of Islamic banking in the general public, the Bank conducted 143 seminars in major cities such as Karachi, Islamabad, Lahore, Peshawar, Rawalpindi, Faisalabad, Multan, Hyderabad, Azad Jammu & Kashmir, Hazara, Abbottabad and DG Khan which were attended by more than 13,800 participants representing customers, general public, professionals, Ulema, Muftian-e-karam and students of various universities.

During the year, the Bank developed various learning videos on Islamic banking concepts and has disseminated them through an internal learning management system for their optimal use and effectiveness. During the year, around 32 members of the senior management and executives of the Bank were given training on Islamic banking.

The Bank also arranged 5 special workshops for its corporate customers in major cities of Pakistan in collaboration with IBA CEIF. We are hopeful that the Bank will continue such initiatives in the future.

It is heartening to observe that in order to disseminate the teachings of Holy Quran, 12 Quran learning sessions on 7 topics were held for Head Office staff.

Shariah Advisory and Industry Support

SSB is also pleased to share that the Bank is actively supporting the Islamic finance industry across the globe by providing tailor-made Shariah advisory solutions. Following are the notable advisory services provided by the Bank during the year:

- Advisory services to Islamic Co-operative Finance, Australia related to Takaful services in Australia
- Capacity building & training session in Australia and Bahrain on Islamic banking & finance
- Technical services and support to Akhuwat Islamic Microfinance for Islamic housing finance product development along with training to their senior team members
- Representation in Capital Market session of AAOFI-World Bank Conference held in Bahrain in November, 2019
- Facilitation of Bank's capital market clients for launching various Shariah-compliant funds and plans; bringing the total number of funds and plans under its advisory to more than 60 which covers a major share of the Islamic mutual funds industry

Review of Assets

During the year, the Bank primarily used Diminishing Musharakah, Running Musharakah, Istisna, Ijarah, Murabaha, Musawamah, Salam – Bills, Wakalah Tul Istithmar, Tijarah, Salam – Commodity, Musharakah and Bai Muajjal for its financing activities.

We appreciate that the Bank is keenly focused on promoting Green and Sustainable banking products by financing alternative energy projects to reduce Carbon footprint.

The Bank has moved towards diversification in the usage of various financing products and has reduced the reliance on Murabaha, as is evident from the Bank's financing portfolio. There is a growth of 16.79% in Diminishing Musharakah from previous year. Bank has mainly focused on financing through Musharakah modes, including Diminishing Musharakah and Running Musharakah and these modes of financing constitute 53% of the Bank's total financing. The Bank's total financing portfolio reached Rs 507 billion (gross) as of December 31, 2019.

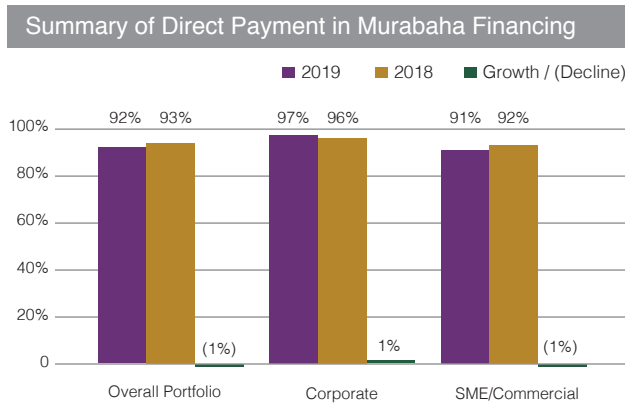
Financing Modes	2019 % in total portfolio	2018 % in total portfolio	Growth / (Decline)% in total portfolio
Diminishing Musharakah	22.58	18.75	3.83
Musharakah & Running Musharakah	30.48	30.50	(0.02)
Istisna	11.52	14.06	(2.54)
Ijarah	10.91	10.57	0.34
Murabaha	3.27	3.82	(0.55)
Musawamah	5.42	7.63	(2.21)
Salam - Bills	1.47	1.10	0.37
Wakalah Tul Istithmar	8.06	7.82	0.24
Tijarah	2.57	2.57	0.00
Salam - Commodity	2.07	1.82	0.25
Other	1.65	1.36	0.29

We have noted that as per our guidelines, the Bank reversed the financing of Rs 648 million provided to its customers under Murabaha & Musawamah without any profit as those transactions could not be converted into real trade due to genuine business reasons. Similarly, in Ijarah financing, the Bank being the owner of asset bore the loss of Rs 0.58 million resulting from shortfall in Takaful claims.

Summary of Direct Payment in Murabaha Financing

During the year, direct payment for Murabaha financings to Corporate and SME/Commercial customers was 92%. It is highly recommended that efforts be continued to increase this percentage of direct payment of Murabaha transactions.

	2019 %	2018 %	Growth/ (Decline)%
Overall Portfolio	92	93	(1)
Segment wise			
Corporate	97	96	1
SME/Commercial	91	92	(1)



It is worth mentioning that to strengthen the Shariah-compliance control, physical inspection of delivery of goods was carried in almost all the Istisna and Tijarah transaction.

Liquidity Management

For the purpose of the liquidity management, the Bank invested Rs 85 billion in Pakistan Energy Sukuks. Also, due to lack of availability of venues for Shariah-compliant investments, Bai Muajjal transactions worth Rs.222 billion were outstanding at the year end.

Review of Deposits

The Bank continued to offer deposit products based on Shariah-compliant modes such as 'Mudarabah' & 'Qard'. It is heartening to see deposits grow by 19% to reach a sum of Rs 933 billion as on December 31, 2019. During the year, the process of allocation of assets and funds to various deposit pools, announcement of overall profit sharing ratios for Mudarabah-based deposits, monthly allocation of weightages, and distribution of income to deposit accounts was monitored and reviewed in accordance with the respective pool management guidelines of SBP and Meezan Bank Limited.

During the year, the Bank continued to develop and revamp its deposit products. COII of 1.5 Years with monthly profit payment option was introduced during the year for those depositors who seek high yielding monthly income products.

Shariah Audit

The Shariah Audit function plays a key role in ensuring Shariah-compliance by evaluating adherence to Shariah guidelines in each and every activity undertaken by the Bank.

In compliance of the Shariah Governance Framework, issued by the State Bank of Pakistan (SBP), a separate Shariah Audit Department reporting to the Board of

Directors' Audit Committee is in place. This department ensures Shariah compliance by evaluating adherence to Shariah guidelines prescribed by Shariah Supervisory Board, Resident Shariah Board Member and Shariah guidelines of Islamic Banking Division of SBP. The Shariah Audit function keeps a continuous check on all activities starting right from the time of opening of a branch and goes hand in hand at each step of product offering till the stage of final profit distribution to the customers.

During the year under review, Shariah Audit of 615 branches, Area offices, Consumer and Corporate hubs and Head Office departments was conducted as a part of the Bank's efforts to strengthen the internal Shariah control mechanism. These audits not only cover the assessment of financial transactions and operational activities that the branches and departments undertake but also include an evaluation of Islamic finance knowledge of staff.

Charity

During the year, an amount of Rs 64.2 million was transferred to the Charity Payable Account. This includes Rs 5.27 million to eliminate the non-compliant income portion which was identified during Shariah audits, Rs. 9.8 million to purify the dividend income earned from the investment made in Shariah-compliant stocks by the Bank and Rs 49.11 million transferred to Charity Payable Account in the normal course of business on account of non-timely payments by customers in various financial transactions. An amount of Rs 49.85 million was disbursed from the Charity Account after approval of the RSBM/SSB.



Details of Charity Account are available in note # 20.4 of this Annual Report.

Suggestions

For the purpose of further improving the Bank's business, the SSB suggests the following:

- In line with the vision of an Islamic welfare state, the Bank should approach the Government for creation of a high power committee for elimination of Riba from society.
- As a socially responsible organization, the Bank should focus on providing green financing solutions that have a positive effect on the energy sector and also ensure environmental preservation.
- The Bank should explore new avenues for providing solutions to various business needs of small entrepreneurs, youths and startups.
- Government has taken the initiative of providing low cost housing schemes for the low income group of society. The Bank should coordinate and collaborate with SBP and Government of Pakistan to maximize the financing of this project through Islamic mode of finance.
- It is suggested that the Bank should launch innovative and user-friendly digital banking products to promote financial inclusion and well-being in the banking ecosystem.
- It is suggested that public-private sector partnership be encouraged for issuance of Sukuk to support financing requirements of the Government.
- The Bank should collaborate with SBP for implementation of IFSB standard on Capital Adequacy for Islamic Financial Institutions.
- The Bank is encouraged to work with the SBP for introduction of Shariah-compliant alternatives for Discount Window and Liquidity Management Framework.
- Government has undertaken several infrastructure projects like Dams, Motorways etc. The Bank should pursue the Government to generate maximum financing for these projects under Islamic modes of finance.
- It is suggested to explore the possibility of launching welfare Sukuk for uplifting the underprivileged segment of the society.

Recommendations

Based on the review of various transactions, reports of Internal and External Shariah Audit and Shariah Compliance of the Bank, it is recommended that:

- The Bank should work on modernizing and upgrading the controls and oversight mechanism based on digital technology, to create efficiency.
- Proper measures should be adopted with regards to commitment and mind-set of the resources in the hiring process.
- The Bank should work on developing learning and awareness programs to disseminate religious, moral and ethical values among its staff.

- For liquidity management purposes, the Bank should use Bai Muajjal when other avenues like Musharakah placement and Sukuk are not available.
- The Bank should continue to focus on creating awareness regarding misconceptions of Islamic banking by conducting seminars / programs and awareness sessions for the masses at public level.
- The Bank, in collaboration with academia, Higher Education Commission and educational text boards, should take initiatives to design the courses or chapters related to the benefit of Islamic financial system on society.
- Training should be conducted for relevant departments to update them regarding current practices, manuals and guidelines prescribed by Shariah Supervisory Board and SCD.
- Conventional insurance is not permissible from Shariah perspective. Therefore, it is again recommended to convert more clients to Islamic Insurance i.e. Takaful as soon as possible

Conclusion

It is mandatory on the Management and employees to ensure application of Shariah principles and guidelines issued by the Shariah Supervisory Board and Resident Shariah Board Member and to ensure Shariah compliance in all its activities. The prime responsibility for ensuring Shariah-compliance of the Bank's operations thus lies with the Board of Directors and Executive Management.

Based on the extensive reviews of sample cases for each class of transaction, related documentations, processes, profit distribution mechanism for the depositors by SCD, review of Internal Shariah Audit and External Shariah Audit reports and Management's representation made in this regard, the Bank, in our opinion, has complied with the rules & principles of Islamic Shariah in light of the guidelines and directives given by the Shariah Supervisory Board, Resident Shariah Board Member of Meezan Bank and guidelines issued by Shariah Supervisory Board of SBP related to Shariah-compliance. The non-compliant income identified during the review is being transferred to Charity Account through a well-defined system and being utilized properly in accordance with the instructions of SSB.

Based on the strength and capacity of the full-fledged SCD and policies and guidelines for Shariah-compliance issued at the Bank, we are of the opinion that an effective mechanism is in place to ensure Shariah compliance in overall operations of the Bank.

May Allah (ﷻ) bless us with the best Tawfeeq to accomplish His cherished tasks, make us successful in this world and in the life hereafter and forgive our mistakes.

Wassalam Alaikum WaRahmat Allah Wa Barakatuh.



Mufti Muhammad Naveed Alam
Resident Shariah Board Member



Sheikh Esam Mohamed Ishaq
Member Shariah Supervisory Board



Dr. Muhammad Imran Ashraf Usmani
Member Shariah Supervisory Board



Justice (Retd.) Muhammad Taqi Usmani
Chairman Shariah Supervisory Board

Dated: 3rd Jamadi us Sani 1441 H / January 29, 2020

اللہ ﷻ سے دعا ہے کہ وہ ہماری رہنمائی ان راہوں کی طرف کرے جو اس کی رضا کا باعث ہوں، ہمیں دنیا اور آخرت میں کامیابیوں سے نوازے اور ہماری غلطیوں اور خطاؤں سے درگزر فرمائے۔ آمین۔

والسلام علیکم ورحمۃ اللہ وبرکاتہ



مفتی محمد نوبید عالم
ریزیڈنٹ شریعہ بورڈ ممبر



شیخ عصام محمد اسحاق
ممبر شریعہ سپروائزری بورڈ



ڈاکٹر محمد عمران اشرف عثمانی
ممبر شریعہ سپروائزری بورڈ



جسٹس (ریٹائرڈ) محمد تقی عثمانی
چیئر مین شریعہ سپروائزری بورڈ

۳ جمادی الثانی ۱۴۴۱ ہجری مطابق ۲۹ جنوری ۲۰۲۰