The task of standard setters such as the Islamic Financial Services Board (IFSB) is to provide the guiding principles that enable regulators to require, or force, “firms to talk” in the public interest. This applies in particular to financial sector regulators who must oversee institutions whose failure could have cascading or system-wide impacts. Moreover, because financial institutions often have cross-border operations and are highly interconnected, there is value to an international language, or benchmark, for the standards and guiding principles used by regulators. In contributing to the development of internationally consistent, robust supervisory regimes, the IFSB’s standards are benchmarked against those of our international comparators, with whom we work closely: the Basel Committee for Banking Supervision, the International Association of Insurance Supervisors, and the International Organization of Securities Commissions. This function has become more prominent in recent years with the rapid growth and internationalization of Islamic finance, which has resulted in the emergence of Islamic banking sectors that are of domestic systemic importance—in that they exceed 15 percent of total banking sector assets—in a number of key jurisdictions (IFSB 2016a).

Standards must be embedded in the legal and regulatory framework that underpins supervisory and regulatory functions, and which plays a critical role in supporting the stability and resilience of financial systems. However, the key challenges to Islamic finance, from the perspective of stability and resilience, are not all located within the legal and regulatory frameworks per se, but rather fall within the broad span of the financial infrastructure that supports markets and

Jaseem Ahmed was the Secretary-General of the Islamic Financial Services Board (IFSB) from 2011 to 2017. He thanks Dr. Volker Nienhaus and Mr. Peter Casey. He also thanks Mr. Zahid ur Rehman Khokher and Mr. Esam Osama Al-Aghbari, Assistant Secretary-General and Member of the Secretariat, respectively, of the IFSB, for their very helpful suggestions and comments. Any remaining errors and omissions are those of the author.

1 The phrase is adapted from Admati and Pfleiderer 2000.
intermediaries, and of which the legal and regulatory framework are constituent parts. Thus, while the legal and regulatory frameworks are rightly viewed as central to financial infrastructure, two observations will point toward an interconnected set of issues that have made policy more complex in Islamic finance.

First, Islamic banks will need to be able to manage their liquidity through access to a regular supply of high-quality liquid assets. For a conventional bank, this is provided by government bonds that carry a rate of interest and are hence not permitted in Islamic finance. It has been a challenge for many countries to develop Shari‘ah-compliant government securities, primarily in the form of Sukūk, that provide this key liquidity management function.² The issue is that it has proved challenging to find the Islamic law basis for a tradable security that is based on general government revenues, in which a specific rate of return, linked to a concrete project, is not easily identified (Sundararajan, Marston, and Shabsigh 2011). Second, central banks will want to be able to provide emergency liquidity support to an Islamic bank in crisis times. Again there are technical and Shari‘ah issues that have resulted in a relatively slow progress in this area, at least in some if not in all jurisdictions.

These key aspects of the liquidity management infrastructure will need to be addressed at the very outset of decision-making and planning for the introduction of Islamic finance, in parallel with other measures that directly focus on building the legal and regulatory framework. In view of this, the IFSB has stressed over the years the importance of the liquidity management infrastructure and the way it interconnects with the development of government securities, the development of a Shari‘ah-compliant interbank market, and the further development of risk-management capabilities within financial institutions and at the macroprudential level (IFSB 2008).

Since the global financial crisis, the IFSB has if anything raised the importance it has accorded to this issue. This is especially relevant, in the postcrisis environment, in the light of the recognition that this issue is related to a more general one: that of the absence of a sufficient supply of safe assets, which is characteristic of a crisis environment. Islamic finance is not in crisis, but neither is it necessarily immune to it. For this reason, it will be imperative to take up as the highest priority the development of safe assets—assets that have high liquidity and tradability.

Two other medium-term issues that the IFSB raised shortly after its establishment, and which now feature as key elements of the postcrisis integrated approach to financial stability, were Shari‘ah-compliant deposit insurance schemes and insolvency and resolution regimes to facilitate rapid and timely restructuring and/or recapitalization of failing or insolvent institutions. These

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² Sukūk are certificates that represent a proportional undivided ownership right in tangible assets, or a pool of tangible assets and other types of assets. These assets could be in a specific project or specific investment activity that is Shari‘ah-compliant. See the IFSB “Glossary” at http://www.ifsb.org/terminologies.php.
latter issues are getting important attention in the IFSB’s research program, which is often a leading indicator of standards and guiding principles to come.3

The rest of this chapter will address the following issues. First, in what sense is Islamic finance distinctive, thereby requiring a different approach to regulation and supervision? Second, what are the key legal and regulatory challenges it faces? Third, how have IFSB standards been shaped to respond to these challenges? Fourth, what further progress in the implementation of IFSB standards has been made? Finally, what further work on the standards do we expect to develop in the near future?

WHAT IS DISTINCTIVE ABOUT ISLAMIC FINANCE?

Islamic finance derives its legitimacy from principles embedded in Islamic law. These principles require that Islamic financial transactions must serve a higher purpose, that is they must serve the goals of social justice, to be achieved through economic transactions that achieve shared prosperity. Financial transactions must be geared toward promoting the real sector. They should be based upon risk-sharing and partnership to the extent possible. The earning of returns in the absence of risk—in a word, “interest”—is forbidden. There are prohibitions against gambling. There are restrictions on excessive leverage, excessive speculation, and excessive complexity. Together, these constitute a distinct system of ethics that can be described as the “embedded governance” of Islamic finance in which the emphasis is on the real sector, ethical conduct, and social impact.4

These are essential aspects of Islamic finance that contributed to its resilience during the crisis. Thus, Islamic financial institutions were largely unexposed to the toxic financial assets that were at the heart of the global crisis. The toxic assets did not, in general, pass the Shari‘ah test (at least in relation to complexity). That they did not pass the Shari‘ah test was aided by an innovation introduced by modern Islamic finance: the Shari‘ah Advisory Board, which is unique to Islamic finance and provides Islamic financial institutions with additional audit and governance mechanisms.

Addressing Differences

Islamic finance has some distinctive features that mean the standards developed for conventional finance often do not fit it in an adequate or satisfactory manner. To give three key examples:

• The profit-sharing investment accounts offered by Islamic banks are (or should be) risk-bearing rather than equivalent to deposits;

3 For example, IFSB 2014 and 2016b.

4 Islamic Financial Services Board, Islamic Development Bank, and Islamic Research and Training Institute 2010. See also Ahmed 2016.
Islamic mortgages are often based on a leasing structure that involves the bank holding title to the assets; and

Islamic insurance—Takaful—involves principles of risk-sharing rather than conventional risk transfer.

These represent real differences with conventional finance. Yet it is also true that finance, whether Islamic or conventional, serves a broad set of common or overlapping functions and needs. It is not surprising, therefore, that some of the solutions look somewhat similar. However, in view of the differences there is a risk that the distinctiveness will be lost if Islamic finance is required to be regulated within a framework of conventional standards and guiding principles. That would be a great loss, not least for the wider inclusion in the financial system of people who are currently self-excluded for religious reasons but who look for confirmation that Islamic finance really is different and meets their requirements and aspirations.

THE KEY LEGAL AND REGULATORY CHALLENGES

Three key considerations in law, among others, provide an overview of issues faced in jurisdictions seeking to introduce and appropriately regulate Islamic financial institutions. First, a fundamental issue in law, which applies to all Islamic finance, is under what conditions a firm, or an instrument, can claim to be “Islamic.” If a bank says, “This is an Islamic mortgage,” what concern does the regulator, or the law, have in that claim? If a customer believes that claim has been made falsely, can they sue? This issue of Sharī'ah governance is approached in different ways in different places. Some regulators have their own boards of scholars to decide ultimately what can and cannot be claimed. In other places, the emphasis is on the firm having its own arrangements and a proper basis for making the claim. Others rely mainly on disclosure. But there needs to be clarity about the approach.

At the same time, it should be stressed that there is a rich body of Islamic law on which scholars have drawn in providing solutions that have expanded the range of Islamic finance transactions in recent times. And while the principle of precedent, or stare decisis, which is a key feature of common law, does not have a parallel in Islamic law, we can nevertheless observe movement toward greater consistency in recent times. Modern approaches to information dissemination, and dialogue between different jurisdictions, are leading to greater transparency and understanding of the basis for differences in approach, as well as to convergence on many issues.

The second key consideration is the ability of the legal system to provide transparency and predictability to the enforcement of Islamic finance contracts. Here, it is relevant that Islamic finance transactions involve both Islamic and secular law. We can distinguish between Shari’ah-incorporated jurisdictions and purely secular jurisdictions. In a Shari’ah-incorporated jurisdiction, Islamic finance contracts will be enforced in accordance with Shari’ah, because the
governing law has already incorporated Sharīʿah. However, in a secular jurisdiction that does not give cognizance to Sharīʿah, enforcement will take place as a matter of contract enforcement in accordance with the governing law of the land without reference to Islamic law. The contract will be enforced in relation to its provisions, in the light of national law, and not the Sharīʿah. From this perspective, the contract is simply a form of private law, which different kinds of legal systems are able to enforce (DeLorenzo and McMillen 2011). The courts in such secular jurisdictions as the United Kingdom and the United States have been willing and able to enforce Islamic finance contracts despite being secular jurisdictions. We have also seen a number of recent cases in which the US Bankruptcy Court has supported complex bankruptcy restructurings in a chapter 11 filing on a Sharīʿah-compliant basis (McMillen 2016).

And third, it is important to bear in mind that countries that promote Islamic finance are at markedly different stages of economic, market, and institutional development. Reflecting these differences, these countries are also at different phases of legal and regulatory development for Islamic finance. Their source of law varies, with common law prevalent in some jurisdictions whereas others rely predominantly on civil and commercial codes. Some common law jurisdictions in Asia give formal cognizance to Sharīʿah, whereas others do so through secular provisions inherited from colonial times, but these may be restricted to personal law and have no applicability to financial transactions.

A different context is provided by Arab-speaking countries that have inherited commercial codes from Ottoman times—codes that have subsequently been refined and modernized. These jurisdictions have constitutional frameworks that typically also recognize Sharīʿah as a source of law. There are differences in the hierarchy of laws in these jurisdictions, where customary law, the commercial codes, and Islamic law are all sources of law. Despite these differences, however, each jurisdiction faces a common set of issues, and there is an international dialogue on good practices. Broadly speaking, unity in principle and diversity in practice would be a good characterization of the approaches to the regulation and supervision of Islamic finance.

Against this background of institutional and historical diversity, the common goal for the establishment of Islamic finance on a sound legal and regulatory basis has been pursued in diverse ways. While some countries have opted to have separate laws for Islamic finance, others have chosen to amend existing laws, sometimes through a minimal set of changes to the laws in place for conventional finance; this is the route taken in the United Kingdom (Ainley and others 2007). Clarity and transparency in the legal framework are vital to ensure a level playing field among financial institutions and to foster consumer confidence, but this can be achieved in different ways depending on the national institutional setting. The IMF’s important cross-country survey on the legal and regulatory framework identifies and sheds light on many such differences (Song and Oosthuizen 2014).

Additional perspective can be provided through the recognition of the policy alternatives and the factors that shape the choices made in different national
settings. Thus, whether a jurisdiction opts for exemptions from existing laws, seeks amendments to them, or decides to draft altogether new laws for Islamic finance represents a set of forward-looking decisions in which the scope of the central bank’s powers can be a key determinant. Where the central bank has wide powers, the authorities may well decide to anchor the introduction of Islamic finance on its current powers, while setting in motion the needed longer-term adjustments to the legal framework. Many countries address this challenge by developing a road map that targets minimum, necessary changes needed to provide an initial legal framework, while more comprehensive legislation is being drafted and discussed with appropriate stakeholders, such as national legislative bodies.

Other issues bear upon the underlying legal framework. One, for example, involves regulation and supervision for an environment where conventional and Islamic finance coexist, with Iran and Sudan being the two exceptions in which only Islamic financial transactions are recognized. Another issue is the appropriate choice of distribution channel for Islamic financial products to reach consumers, and whether this is to be done through stand-alone Islamic banks, or some combination of subsidiaries and window operations. These are live issues today across jurisdictions and continents.

**LEGAL AND REGULATORY ASPECTS OF THE IFSB’S STANDARD SETTING**

Turning to the supervisory and regulatory framework, as Figures 12.1 and 12.2 indicate, a key question, and the first focus of the IFSB when it was established, was on how capital adequacy and liquidity standards were to be applied to Islamic banks. In particular, how should the distinctive character of profit-sharing investment accounts be recognized? The IFSB initially issued several Standards and Guidance Notes on the effective measurement and disclosure of these accounts, and on making transparent their effective rates of return. Among other issues addressed through the “first generation” of IFSB standards prior to the global financial crisis, the following featured prominently:

- Guiding principles on the design of effective credit registries, recognition of external credit-rating agencies, and the measurement of nonperforming financing;
- The principles on which conduct of business and transparency and market discipline in Islamic banks should be based; and
- *Shari’ah* governance principles and corporate governance issues.

To date the IFSB has issued 26 standards, guiding notes, and technical notes covering the banking, capital markets, and *Takaful*, or Islamic insurance sector. The focus of the initial standards was principally on the banking sector, as this represented about 80 percent of assets under management globally, but since 2007 the scope has expanded to include both *Takaful* and Islamic Capital
Markets. A joint paper with the International Association of Insurance Supervisors led in 2007 to the launch of a series of standards on the Takaful sector, which is ongoing.

The IFSB has directed a major work program into these technical areas over the years. It will need to further redefine the work program to keep up with the changes in the Basel standards. A significant effort has been made since 2012 to adapt to the Basel III framework, which has posed some challenges. A considerable effort is underway both to reflect the specific risk factors that apply to Islamic finance and to provide a frame of reference to the global architecture for financial sector stability with a view toward achieving greater consistency.

Challenges posed by Basel III Capital and Liquidity Framework. The Basel-mandated increases in banks’ capital quality, consistency, and transparency have raised issues for Islamic finance. In general, the capital structures of the significant majority of Islamic banks are dominated by Tier 1 capital in common equity form. In addition, most have capital adequacy ratios significantly higher than those seen in the conventional banking sector. The reasons for this can be explained by strict Shari’ah prohibitions on what constitutes the capital for Islamic financial institutions. Thus, the prohibition of Gharar (conditionality and uncertainty) has had an impact in terms of the absence—or presence only in limited forms—of Islamic subordinated debt, preference shares, and hybrid and callable capital structures.

Note: The Expected New Standards were approved and issued in December 2016 and April 2017, respectively. Three additional standards were issued in December 2018, bringing the total issuances to 22 Standards and Guidance Notes, and 2 Technical Notes.
As a result of these considerations, the capital structures of Islamic financial institutions and their above-average capital ratios put them in a favorable position relative to many of their conventional counterparts. Nevertheless, some areas require attention. In raising Tier 2 capital, for instance, the issue is how institutions offering Islamic financial services will meet *Sharī’ah* requirements before meeting the regulatory requirements for instruments such as subordinated debt, hybrid capital, convertible contingent capital, and *Sukūk* that can be considered as capital. These issues are addressed in the IFSB’s Revised Capital Adequacy Standard, which required, among other features, upfront specification of the conditions under which one type of capital converts into another, as a bank goes from being a “going concern” to a “gone concern.” In addition, the IFSB has felt it appropriate to provide a set of requirements comparable to Basel in terms of its capital conservation, countercyclical, and other buffers.

Liquidity is an area where Islamic banks are impacted to a significant extent by Basel III, principally due to the lack of liquid Islamic financial instruments. For example, Basel III stresses the need for banks to maintain a stock of assets that can easily be turned into cash at reliable values, either through markets or central banks’ cash from a “discount window.” In fulfilling the liquidity requirement of Basel III via the discount window, much work remains to be done to ensure an adequate supply of *Sukūk* that can provide assets that qualify for discount window access.
A key issue is limited availability of Sharī'ah-compliant instruments/Sukūk that can meet Basel III’s requirements. In particular, it is difficult for many such instruments to meet the market-related characteristics such as “active and sizeable market,” “presence of committed market makers,” “low market concentration,” and “flight to quality.” Availability of Level 1 assets is not adequate in most jurisdictions. Also, a repo market is not available in most jurisdictions; therefore, the expectation of being “traded in large, deep and active repo or cash markets” is not applicable to many Sharī'ah-compliant assets.

Despite the challenges, various options are available for the application of the liquidity framework to Islamic banks, and these are addressed in detail in IFSB’s most recent standard on liquidity management issued in 2015 (IFSB 2015c). Basel III had suggested three alternative treatments in jurisdictions where sufficient liquid assets are not available. The IFSB’s Quantitative Impact Survey provided the feedback that the majority of both supervisory authorities and banks were agreeable to these proposals, which include committed facilities from the central bank and the use of additional Level 2 assets with a higher haircut, when Level 1 assets are not available in sufficient volume.

**PROGRESS IN IMPLEMENTATION OF STANDARDS**

A significant effort is underway to strengthen implementation through workshops and surveys. The IFSB Implementation Surveys were launched in 2011 and were designed not only to assess progress made, but also to identify the requirements, intentions, and plans of our members over the medium term (Figure 12.3). The initial survey focused on 11 standards issued by the IFSB, whereas that of 2015 covered 17 standards. The surveys, which are now annual, indicate a strengthening and widening process of standards implementation (Figure 12.4). Progress, in terms of movement across the four-fold classification used by both the IFSB and the Financial Stability Institute, requires closer examination.

**Figure 12.3. IFSB Standards Implementation Surveys**

The survey captures:
- The breadth of implementation (for example, the number of countries implementing standards)
- Challenges being faced by the member RSAs in the implementation of standards
- The support expected from the IFSB Secretariat

The information collected from implementation surveys has aided the IFSB’s efforts to fine-tune its standards development as well as IFS initiatives to suit the needs and constraints faced by its member jurisdictions.

Source: IFSB 2015b.
Note: IFSB = Islamic Financial Services Board; RSA = regulatory and supervisory authority.
The first survey in 2011 indicated that the earliest IFSB standards featured more frequently across jurisdictions as having been fully or partially completed. The 2015 survey indicates a new dimension, that the most recent standards touching upon the updated capital and liquidity framework now feature prominently as being planned or under implementation. This is brought out in Figure 12.5. Thus, it can be seen that the first IFSB standard, issued in 2005, is recorded as having been fully implemented by 42 percent of survey respondents, 10 years later in 2015. In contrast, IFSB 15, which refers to the new capital adequacy framework and was issued in 2013, has in a short space of two years been fully implemented by 26 percent of respondents in 2015. (The “take-up rate” in Figure 12.5 is defined as the implementation rate divided by the number of years since issuance). This could be an indication that the pressure of Basel III is spilling over to early implementation of comparable IFSB standards, which of course remain voluntary. On the other hand, IFSB-10—the standard on Sharī‘ah governance, which was issued in 2010 and initially had a slow take-up—now is the most frequently cited standard planned for implementation. The take-up of this standard is likely to be linked to a growing policy focus on an expanding Islamic finance sector, as well as stronger capabilities for planning and implementing reforms.

The preconditions for successful implementation, identified by the surveys, have remained broadly consistent over the years (Figure 12.6). The top-ranked issues and constraints remain those related to having in place a strong legal and regulatory framework, and staff capabilities. In terms of addressing the key constraints, the surveys indicate consistency in the importance given to technical assistance from the IFSB in translating its standards into more meaningful and practical guidance notes and reports. The scope of the identified needs for technical assistance includes an enhanced program of customized train-the-trainers

<table>
<thead>
<tr>
<th>Stage of Implementation</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Final rule in force</td>
<td>30%</td>
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<tr>
<td>Final rule published</td>
<td>1%</td>
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<tr>
<td>Complete</td>
<td></td>
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<tr>
<td>In progress</td>
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<tr>
<td>Planning</td>
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<tr>
<td>Not planned</td>
<td></td>
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<tr>
<td>Draft regulations published</td>
<td>0%</td>
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<tr>
<td>Regulation in drafting stage</td>
<td>8%</td>
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</tbody>
</table>

Within 1 year: 4%
1–3 years: 23%
3–5 years: 13%

Source: IFSB 2015b.
Note: Based on a total of 39 respondents.
workshops for supervisory agencies, known as Facilitating the Implementation of the IFSB Standards. The key priority, therefore, is to find the resources and organizational modes and partnerships that help committed jurisdictions meet the challenges they face and their desire for assistance in addressing these challenges. These are issues that the IFSB has elaborated on in its Strategic Performance Plan 2016–18, through an expanded capacity to be provided by its Implementation Unit.

To paraphrase the chairman of the Basel Committee, standards and principles, if not implemented, are like a lighthouse in which the light is not turned on. In respect of Islamic finance and the standards of the IFSB, while much remains to be done, we can safely conclude that the light in the lighthouse is being turned on across an increasing number of jurisdictions.

The IFSB’s Medium-Term Agenda

The following specific sets of issues provide the medium-term framework for the IFSB’s work program. First, to complete by fine-tuning the body of standards related to the new international standards for financial stability. These include a new technical note on stress testing, which was submitted to the IFSB Council in December 2016, and further revision to capital adequacy issues as needed. A new standard is targeted for completion in the area of transparency.
and market disclosure for the banking sector, to reflect the recent Basel paper on this subject. 5

Second, we will be paying increasing attention to Takaful and the development of Islamic capital markets, both in terms of new standards and in terms of research and knowledge products. Because banking is the largest sector in Islamic finance, it was our initial priority in standard-setting, but in our recently published Strategic Performance Plan for 2016–18 we intend to put more effort than hitherto on capital markets, Takaful and also on financial inclusion. A new Standard for Transparency and Disclosure on Islamic Capital

5 This Standard was approved and issued as IFSB-22 in December 2018.
Markets is under preparation and was submitted to the IFSB Council in early 2017 and a standard on the Supervisory Review Process for Takaful was launched in 2016.6

Third, we have launched a program for the preparation of Core Principles for Islamic Finance Regulation, which aims to achieve greater consistency and focus of implementation efforts for both Islamic and conventional parts of the financial system in all jurisdictions. The first set of Core Principles for the banking sector were issued in 2015, and in 2016 we launched the preparation of Core Principles for ICM (IFSB 2015a). Core principles for Takaful are expected to be launched in 2018, once the International Association of Insurance Supervisors has concluded its ongoing review of its own core principles.

The development of the core principles by the IFSB is in response to the existence of gaps in the regulatory and supervisory framework in many countries. The Core Principles assist supervisory authorities that are regulating and supervising Islamic finance to identify applicable principles and benchmarks, to fill the gaps in the existing policies and regulations in their jurisdictions. The Core Principles can be used by both advanced and emerging market jurisdictions.

Fourth, the heightened importance of legal and regulatory reforms that promote greater resilience has been incorporated into a new program that aims to promote cooperation among our members on stability issues. In this context, a specific set of activities is the Islamic Financial Stability Forum, where we are working to develop greater cross-border understanding of crisis management and resolution issues, as well as those related to the development of the financial safety net. The IFSB Stability Forum focused on anti-money laundering and provided the background for the launch of a working paper on this subject in 2017.

Finally, we also have a research program intended to lay the groundwork for possible future standards. Our work in that area will include, among others, macroprudential issues and resolution and recovery frameworks. The resolution of Islamic banks, in particular, raises challenging issues, some of which are addressed in a joint publication by the IFSB and World Bank (2011). One important area is the treatment of profit-sharing investment accounts, which are a key product of Islamic banks. Should investors in these be treated like depositors who are owed a debt or as fully risk-bearing investors? Can an order of priorities be established between creditors, as would normally be done in conventional insolvency law, given that Shari‘ah would normally rank all creditors equally? Where banks do business with each other, for example, in the Islamic money market, can obligations be set off against each other, even if the contractual bases are different?

Issues like these are important even in resolution short of insolvency, as the Financial Stability Board has taken the view that resolution arrangements should respect the hierarchy of claims, and that no creditor should be worse off.

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6 These standards were approved in April 2017 and December 2018, respectively. See http://ifsb.org for a list of all issued standards.
than if the institution had been allowed to become insolvent (Financial Stability Board 2014). There are other unexplored issues, some of which connect with other safety-net issues, especially lender of last resort and deposit insurance, on which the IFSB has published research papers.

CONCLUSION

A modern financial sector, including for Islamic finance, is highly dependent on a legal and regulatory framework that ensures transparency, consistency, and predictability. The diversity noted across countries in the legal and regulatory frameworks for Islamic finance reflects a variety of factors, including differences in source of law and in stages of economic and institutional development. The IFSB aims to accommodate this diversity, while also providing a consistent basis for promoting financial stability through the implementation of its standards. This is challenging, not least because of the rapid pace of growth and internationalization that is transforming the face of Islamic finance. These developments, however, are taking place in the context of sustained scrutiny and dialogue involving regulators and policymakers. The scrutiny underpins a dynamic process of recalibration, revision, and strengthening of the legal and regulatory framework across many jurisdictions.

Overall, these developments indicate that the supervisory and regulatory framework for Islamic finance faces challenges not unlike those faced in conventional financial systems at a similar stage of development. But in specific areas the challenges are daunting in terms of what is needed to articulate solutions consistent with Islamic law. In this environment, the stability of the financial system, and the orderly development of Islamic finance, will be aided by the parallel and joint implementation of Basel Core Principles and the standards and guiding principles of the IFSB.

The stronger postcrisis emphasis on the key objective of financial stability, and the larger role of Islamic finance in many jurisdictions, pose challenges that are relevant from a wider perspective. The first challenge is how to strengthen the national regulatory and supervisory framework, in a way that is consistent across borders, to enhance the stability and resilience of Islamic finance. A second challenge is how to facilitate the integration of Islamic finance into the surveillance framework that monitors the stability of the global financial system. It will be important for a wider international engagement, including in particular by the IMF in tandem with the IFSB and other institutions, to address these issues.

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