

Emily Fuller, Deborah Low, Ellen McGinnis, Emma Russell in PrivateEquityWire: Shariah in the Spotlight III: Understanding Governance in Shariah Law and ESG

November 5, 2020 Deborah Low, Ellen McGinnis

PRACTICES Fund Finance, Finance, Environmental, Social and Governance

Governance is perhaps the least talked about component of 'ESG,' but is based on concepts of fairness, transparency and accountability that form the basis of good corporate governance.

Good corporate governance looks at the relationship among the company and its employees and shareholders, focusing on issues such as the balance of power among the managers, executives and directors of a company, compensation structures, quality control in product generation, transparency in decision making and accountability for corporate action. Good corporate governance structures have long been a factor that investors will consider when making investment decisions as poor corporate governance will expose the company and by extension, its investors to risks, such as shareholder, employee or consumer litigation, penalties for labor law or sanctions violations, lack of approval or authorisation for projects and investment schemes from governmental authorities and regulators, or other punitive actions for violations of applicable law.

However, while all companies may be subject to certain governance laws and regulations, such as accounting standards, mandated governance structures including independent directors, employee hiring and benefits and compliance with law, an ESG evaluation will seek to measure the effectiveness of a company's protocols for compliance with these regulations, and whether the company is taking additional steps to promote fairness and transparency.

Similarly, Islamic financial institutions are subject to additional rules and regulations which have been developed to ensure good corporate governance and compliance with Shariah. For example, the Accounting and Auditing Organisation for Islamic Financial Institutions sets governance, accounting, and ethical standards for Islamic financial institutions, equivalent to the International Financial Reporting Standards. Islamic financial institutions themselves will also have a Shariah Supervisory Board ("SSB") whose job it is to review transactions and report as to whether they are Shariah-compliant.

Excerpted from *PrivateEquityWire*. To read the full article, click [here](#).

This article is the third part of a series