

# Issues and Challenges Faced by Islamic Financial Institutions in Canada

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## Abstract

Despite the fact that Canada is a major and important host for Muslim individuals, that it has a long history welcoming Muslims and that it generally respects minority rights, religions and cultures, Islamic Finance is still at its infancy stage in the country. This paper aims at studying the reasons of this stagnant stage including the issues and challenges behind these reasons. After a thorough study done with managers of Islamic Financial Institutions in Canada, different issues and challenges emerged. These are connected in some cases and independent in others with the major ones being Government inertia towards Islamic Finance, Muslim community inertia towards asking for their rights as well as the failure of some Islamic Financial Institutions.

**Keywords:** Islamic finance, Canada, Islamic financial institutions, issues and challenges

## 1. Introduction

Canada is the second largest country in the World with a population of 37.59 million of which more than 1.4 million are Muslims (National Household Survey, 2011). According to statistics the Muslim population in Canada doubles every 10 years (Lalani et al., 2015). With this number increasing, the need of Muslims for Islamic finance is increasing as well (Edward, 2011). These Muslims are in need of basic necessities such as houses, cars and deposits; and the majority of them needs to acquire them through Islamic finance in order to remain in line with their religious requirements. However, they can rarely find this type of financing (Tahmina, 2013).

Up to date, no Islamic bank or window exists in Canada and the few Islamic financial institutions that are in the country face different issues and challenges (Tahmina, 2013) resulting in a lack of demand in some cases and in a huge demand with limited offer in other cases. Furthermore, very few studies have been done in the field to find out what are these issues and challenges as well as the reasons behind them. This research has the objective of exploring these latter and to report them as clearly as possible in order to understand the current situation of Islamic finance in Canada.

The conceptual framework of this study can be summarized in this diagram:

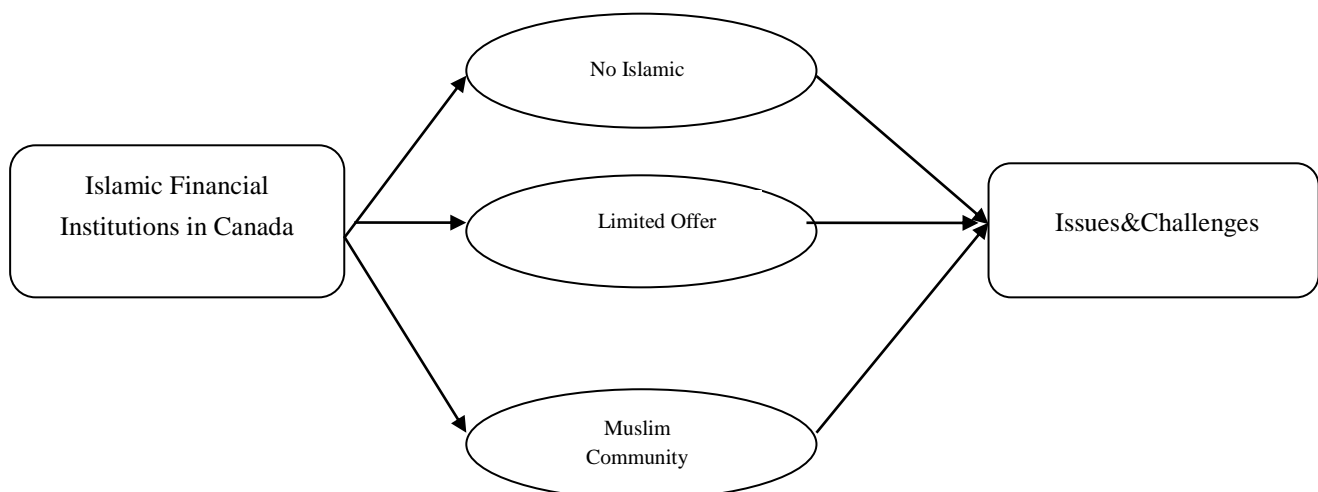


Figure 1. Conceptual framework of the study

## 2. Review of Related Literature

### 2.1 Overview

Islamic finance is a growing industry all over the world; be it in Muslim countries or non-Muslim countries. Even though the market is relatively small compared to its conventional counterpart, Lalani et al. (2015), Chaudhry (2011), Alexakis and Tsikouras (2009) and Lynn (2009) acknowledge that Islamic finance is growing in a faster way than the conventional one. The growth rate of Islamic finance is evaluated at 20% per year until 2016 (Hussain et.al 2015, p.1), which is double the conventional growth rate. Furthermore, the Islamic economic bloc became the fourth largest one after the United States, China and the European Union. McMillen (2010) mentions that even though USA has a smaller Muslim population in terms of percentage, Islamic finance there is better developed than in Canada. Indeed, the investments in Islamic finance by North American and Muslim countries will be beneficial and fruitful for both sides. It would add value and diversification to the Western countries and more capital and investments in the Muslim countries.

McNamara (2009) in the GIFR; Global Islamic Finance Report, and the IFWG; Islamic Finance Working Group (2010) of Toronto emphasize that Islamic Finance can benefit not only Muslims but non-Muslims as well as it is a form of ethical financing. Many investors from Canada and even abroad would be interested to invest in businesses that are ethical and compliant to the Islamic principles. Alternatively, McMillen (2010) states that the success of Islamic finance in America did not stem from the amendments made in its legal and regulatory framework but rather from the flexibility of the Shariah principles. Lalani et al. (2015) mention that several non-Muslim countries have already implemented and used Islamic finance, hence Canada should not be left behind.

Souiden and Marzouki (2015) prove that religiosity of individuals does have an influence on their attitude towards Islamic banks. They further suggest that conventional banks should answer the demand of Muslim customers. Furthermore, Ladhariet al. (2011) argue that Canadian banks' managers need to consider "empathy" as an important element in their service delivery through strategies oriented towards the needs of all customers.

Volk and Pudelko (2016) confirm that the Islamic banking products that are mostly used by Muslim societies are retail-banking products. Alharbi (2015) states that even though some Islamic financial products are available in Canada, they remain limited and scarce. Moreover, it is considerably easier for consumers to choose a bank for deposits instead of a near-bank (Dean &Schwindt 2014, p.33) because only banks can offer deposits in Canada and no other financial institution is allowed to. However, the main problem in Canada is that it is not possible to implement any Islamic deposits in the current legal system since deposits in conventional banking have different mechanisms. Additionally, Hanif (2011) states that an Islamic credit facility cannot be successful without a push from the real sector since all these credits must either be through risk and profit-sharing or asset-backed. He adds that the objective of offering Islamic financial products is not just money but also society's well-being. These traits explain the particularities and features of Islamic banking products and where and why the differences with conventional banking products exist.

A few banks applied for the opening of an Islamic bank next to the Office of the Superintendent of Financial Institutions (OSFI) in Canada in order to offer Islamic banking products (Alharbi, 2015). According to Good (2009), Albassam Inc. also sent its application however, till this date, no response has been received. Goud says that the Ministry of Finance declared that it was studying the case and checking whether Islamic financial products can be offered in the actual regulatory framework. Goud (2009) and Alharbi (2015) mention that Canada Mortgage and Housing Corporation (CMHC), which is a federal institution, has shown interest in the topic by asking for proposals in the objective of providing reports of research about Islamic finance. This demonstrates the non-indifference of the Canadian government however; nothing has been proclaimed from their side since more than a decade.

Although the Islamic finance industry is almost unpracticed by Canadian conventional finance players, Lalani et al. (2015) and Chaudhry (2011) say that some institutions do offer Islamic financial products and services especially mortgages and mutual funds. In fact, Lam (2009) in the Global Finance Report attests that Canada has made a first step toward Islamic finance since S&P, based in Toronto, created an index of equities that are Shariah-compliant on the Toronto Stock Exchange. However, when compared to some other Western countries, Lam (2009) and Lynn (2009) say Canada is taking a very slow pace towards the direction of implementing Islamic finance and in the US even if the growth is slow, it is bigger and steadier than in Canada.

Although Islamic Finance has not comprehensively flourished in the Canadian soil, there are a few Islamic financial products offered by some institutions. These institutions are classified into three categories: institutions that are Canadian and Islamic, institutions that are Canadian and non-Islamic and an institution that is non-Canadian but

Islamic.

## 2.2 Canadian Islamic Financial Institutions

There are nine Islamic financial institutions offering Islamic financial products in Canada. These are:

### 2.2.1 Ansar & Islamic Cooperative Housing Corporation

Ansar & Islamic Cooperative Housing Corporation has opened its doors in 1981 making it the first Islamic Financial Institution not only in Canada but in all of North America. Among its affiliates are Al-Amin Interest-Free RRSP, Ansar Financial Group, Cypress Creek Developments and Ansar Financial and Development Corporation (AFDC). Its objective was to help Muslims in Canada to buy houses in a Shariah-compliant manner. The company invites the Muslim community to invest in Housing Cooperatives, Private Corporations and the Public Company. While investing in private corporations, the share price is fixed; and when investing in the public company where the trading is at the stock exchange, the share price changes on a daily basis. The majority of investments in Ansar Financial group are in real estate properties and projects.

Ansar Housing helps the community in buying houses, leasing equipments and cars as well as realizing business partnerships. The community can also invest their retirement and education savings with tax benefits in Ansar's Public Company shares.

For the purpose of buying a house with Ansar Housing Company, the shares work as an investment where the customers must have shares equivalent to 20% of the first 100,000\$ cost of the house they intend to purchase. They would earn quarterly dividends that are declared annually, until they cover all the shares of the house and own it. Each entity of Ansar Financial Group offers different programs; however, shares of the public and private corporation can both be included in the retirement savings plan.

Ansar offers Takaful as a pilot program for the cooperative members only due to certain regulatory requirements that need to be amended by the Canadian Parliament.

### 2.2.2 Manzil

Manzil is a company based in Toronto that offers financial solutions to Canadian all over Canada except in the province of Quebec which operates under different laws. Manzil offers Mortgages using either Diminishing Musharaka or Murabaha model. Under the Murabaha model, the maximum repayment term is of 25 years. Manzil also offers investment funds using the Mudaraba model wherein the capital is acquired from private retail sources.

### 2.2.3 AlBassam House Inc

AlBassam House Inc is a Saudi family business company based in Calgary in the province of Alberta. Its objective is to promote Islamic Finance in Canada. First of all, AlBassam House offers advisory services, products' structuring and contacts in the Gulf countries for the realization of Islamic financial transactions. Moreover, it offers Real Estate and Commercial services as well as short and medium term funding through reverse Murabaha or Wakala. AlBassam helps in using revolving Murabaha or Murabaha with a fixed profit in the place of floating rate or fixed rate bonds. Instead of using commercial papers, the group insures Sukuk Al Ijara. An example of structured products offered is a Real Estate backed on Ijarah.

### 2.2.4 An-Nur Cooperative Corporation

An-Nur Cooperative Corporation is an Islamic Financial Institution based in Scarborough in the province of Ontario with an office in Mississauga. An-Nur offers its services mainly to the residents within the province of Ontario and has a limited operation in the province of Alberta. The Corporation has the intention to extend its offers to other provinces as well.

The products offered by An-Nur Cooperative Corporation are as follows: Investments in commercial, residential and industrial real estate projects, Shariah compliant Home Purchase Plan and RRSP (Registered Retirement Savings Plan), RESP (Registered Education Savings Plan), TFSA (Tax Free Savings Account) as well as other Retirement and Saving Plans through affiliated companies.

In the Home Purchase Plan, An-Nur Cooperative Corporation uses two methods; the first method being declining partnership in its "HOME" Plan also named "Home Ownership Made Easy" where the customer needs to contribute a minimum of 25% as a down payment. The second plan uses Murabaha but in exceptional cases only. An-Nur uses Musharaka (Partnership) for Residential Real Estate Investments and offers Industrial and Commercial Investments through affiliated corporations.

### 2.2.5 Qurtuba Housing Cooperative

Qurtuba Housing Cooperative was launched in 1991 in the city of Montreal, Quebec responding to the demand of the Quebec Muslim community. It has Jamal Badawi and TaqiUsmani as Shariah advisors; these are two highly respected figures in the world of Islamic Finance. Qurtuba offers investment with dividends and Home financing through Musharaka (Partnership Agreement). The cooperative supports its members to have Takaful insurance for housing and vehicles through the Canadian Cooperators Insurance Company.

### 2.2.6 Al-Ittihad Investments

Al-Ittihad has opened its doors in 1991 at the same time and location of Qurtuba Housing Cooperative. The two institutions work closely together and offer services to Quebec residents. While Qurtuba offers Investments and Home financing, Al-Ittihad uses Murabaha to offer cars, equipment and business investments. Due to some difficulties, Al-Ittihad has closed its doors in 2007 but succeeded to obtain a Certificate of Revival in 2009.

### 2.2.7 Zero Mortgage Canada

Zero Mortgage is a Canadian Islamic financial corporation that operates as a referral institution working with conventional regulated Canadian financial institutions yet with specific terms and conditions. The objective is to offer only Shariah-compliant features helping Muslims all over the country to acquire houses using MusharakaMutanaqisa agreement. Zero Mortgage Corporation is based in Toronto with three branches in Ontario to offer information to interested customers.

### 2.2.8 Salam Financial

Salam Financial is a Canadian Islamic Financial Institution based in Ottawa in the province of Ontario. It was created in 2006 in order to meet the needs of the Canadian Muslim community. Salam Financial offers Shariah-compliant commercial financing with 35% of down payment and investment products to all Canadian residents. The company has a project to offer Home Ownership program under the Murabaha model.

### 2.2.9 Amana Canada Holdings

Amana Canada Holdings is based in Toronto and offer Shariah-compliant commercial loans and investment products. The commercial loans are based on the principle of Murabaha and the Investment products are based on Musharaka. The services are offered to all Canadian residents. Amana Canada Holdings gets its capital from private investors and is affiliated to its Swiss partner, Amana Switzerland Holdings Inc.

## 2.3 Canadian Non-Islamic Institutions

There are two non-Islamic institutions in Canada that offer Islamic financial products, these are:

### 2.3.1 Assiniboine Credit Union

Located in the city of Winnipeg in the province of Manitoba, Assiniboine Credit Union is a Canadian Credit Union company that functions as a financial cooperative and is the largest in the city. The company offers different products and services including an Islamic mortgage using Declining Partnership Agreement and a Promise to buy. The initial contribution for the Islamic mortgage has to be at a minimum of 20% of the Purchase Price and the term for repayment is up to 25 years. The capital used to this matter is the deposits of local members who are the owners of the credit Union. Assiniboine Credit Union is owned by about 120.000 local members.

### 2.3.2 Wealth Simple Investment Portfolio

Wealth Simple Investment Portfolio is an online platform offering investment services to individuals and businesses as well as Savings and Advisory services. It has three head offices in three countries; Canada, USA and UK. Seeing the important number of Muslims in the West including Canada, Wealth Simple offers a Halal Investing Portfolio and uses the MSCI Islamic Index Series methodology in order to exclude Shariah non-compliant securities. This portfolio includes 50 stocks and does not involve in businesses that derive significant income from interest on loans. Furthermore, Shariah scholars are hired to screen the investments for Shariah-compliance.

## 2.4 Non-Canadian Institutions Offering Islamic Financial Products in Canada

In Canada, some foreign financial institutions are allowed to offer their products to Canadian individuals. Islamic financial institutions are not an exception to the rule; however, there is only one American financial institution that offers Islamic retail-banking products; the Ijara Community Development Corporation (IjaraCDC):

### 2.4.1 Ijara Community Development Corporation (IjaraCDC)

Ijara CDC is an American non-profit organization that is based in Michigan, USA. It offers its services to Americans

and Canadians alike, and provides Shariah structuring services for residential and commercial financing based on IjarawaIqtina model. Ijara CDC gets capital from traditional banks, trust companies and credit unions. The minimum down payment that the customer must pay in Canada is 5%. The term payment can go up to 25 years for both residential financing and investment; nonetheless, the down payment for investment must be of a minimum of 25-30%. Most investors in IjaraCDC finance between 100,000 and 2 million dollars.

Concerning commercial financing, the down payment in Ijara CDC varies between 10% and 35% depending on the units requested and the purpose of construction (whether residential or business); and the term payment is between 20 and 26 years. Additionally, it is worth to mention that all these institutions are near-banks and not banks. Near banks in Canada refer to all financial institutions (except banks) that offer financial products.

Vojtech (2015) says that the real reasons hindering the implementation of Islamic Finance are due to the actual legal definitions and implications of deposits and loans. He explains that since Islamic Finance relies on Shariah which is not a codified legal system, then every Islamic financial contract can only rely on Shariah interpretations that need to be detailed. Baharom et al. (2017) maintain that the Canadian regulatory framework needs amendments in order to host the design of Islamic financial products since the latter is quite different from the conventional ones. Dzuljastri and Hanudin (2013) call regulators and policy-makers to consider the different modifications needed for the implementation of an Islamic financial product. These modifications concern different regulations, laws and policies as well as accounting and taxation elements.

A few banks applied for the opening of an Islamic Bank next to the Office of the Superintendent of Financial Institutions in Canada in order to offer Islamic banking products (Alharbi, 2015). AlbassamInc also sent its application however, up-to-date no response has been received (Albassam, 2021). Goud (2009) says that the Ministry of Finance declared that it was studying the case and checking whether Islamic Financial Products can be offered in the actual regulatory framework. Goud (2009) and Alharbi (2015) mention that Canada Mortgage and Housing Corporation (CMHC), which is a federal institution, has shown interest in the topic by asking for proposals in the objective of providing reports of research about Islamic finance. This demonstrates the non-indifference of the Canadian government however; nothing has been proclaimed from their side since more than a decade.

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The IFWG (2010) of Toronto sees that the government has to do some work in order to make Islamic Finance a reality in Canada. One of the crucial steps is to convince the relevant government that the change is needed and desirable. There is also a need in organizing different conferences, symposiums and research. The team emphasizes that once Islamic Finance is well implemented in Canada, it will bring opportunities for investors from the Gulf Region to work with Canada. Lalani et al. (2015) and Sole (2007) see that one of the greatest means for a successful Islamic Finance in Canada is to link investors in the country and the Muslim World, and to attract investors from oil-exporting countries like the GCC and South Asia.

This list of Islamic financial institutions with the products they offer can seem appealing and comprehensive. However, in some cases the demand from the Muslim community is not that important and in others, the offer from these institutions is not that available. All previous studies mention that there are some issues faced by these institutions namely in the Legal and Regulatory Framework and in the Taxation framework; yet no study has approached these institutions in order to analyze what these issues and challenges are. This study delves into the reasons behind these matters in order to intensively explore the issues and challenges faced by Islamic financial institutions in Canada. In fact, knowing these issues would help field players and policy makers to assess the situation of Islamic finance in Canada and enrich the literature related to it.

### **3. Data and Methodology**

This research is qualitative in nature using semi-structured interviews with 11 respondents who are experts in the field including 4 managers of Islamic financial institutions, 6 Banking and Finance lawyers and 1 regulator all based in Canada. The interviews are held in the work site of the participants.

As mentioned in the literature review, there are 12 Islamic financial institutions offering Islamic financial products in

Canada. All 12 managers of these institutions have been contacted through e-mail and asked to participate in the interview. 4 of these managers have agreed to participate and one of them rejected the proposal while the remaining did not respond. Similarly, 11 finance and banking lawyers were contacted and 6 of them responded; 5 regulators were contacted and 1 of them agreed to participate in the interview.

The approach of this study is phenomenological since managers of Islamic financial institutions are individuals who are directly impacted by the issues and challenges faced in Islamic finance in Canada (Adu, 2019). The purpose of this study is exploratory where these issues and challenges are discovered through a thematic analysis of the data.

#### **4. Discussion and Analysis**

The data analysis of this research was done in three parts: transcribing the interviews, coding the data, developing themes from the codes and finally establishing relationships between the themes. The researcher practiced epoché during the whole part of analysis in order to avoid any biases, personal perspectives and preconceptions.

After listening several times to the audio recording of the interviews, the researcher became acquainted with the data and transcribed it herself. The coding was hence done manually using the interpretation-focused coding strategy since the approach is phenomenological and the purpose is to explore the issues and challenges (Adu, 2019). The data was also somehow implicit hence critical review was needed. Then the researcher searched for empirical indicators from the transcriptions. The coding strategy came up with 52 codes assigned to data. These codes were then classified according to their frequency of appearance in the data and in the transcripts starting with the dominant ones.

As for the theme development, the individual-based sorting strategy was used by arranging the dominant codes into clusters, comparing the remaining codes to the dominant ones and to each other and then creating themes according to shared similarities.

The participants; who are mainly founders and managers of their Islamic financial institutions as well as lawyers and regulators, were asked during the interviews questions that aim to underlie the issues and challenges that Islamic financial institutions face in terms of the legal and regulatory framework. The answers were then analyzed and 7 themes emerged. These are the following:

##### ***Theme 1: Strict Legal and Regulatory Framework***

The major challenge faced by the existent Islamic financial institutions in Canada is the legal and regulatory framework. These financial institutions faced tremendous hardship operating under the current laws. As informant IFI4 expressed it:

*The major challenge is to operate within the existing laws*

These difficulties are represented by restrictions on partnership, on equity investment, and on mortgage among many other restrictions. Furthermore, as the Canadian financial framework has been written in the objective of avoiding any high risk, there is nothing out there that would protect Islamic financial institutions in case of hazard in a mortgage transaction, for example. This means that when the financial institution offers a mortgage to a customer and then when any third person comes and faces an accident, this institution will bear the costs and can even be sued because of that. Because of these many restrictions, there is a lack in Islamic retail-banking products diversification. Thus institutions are not able to satisfy the demand of their Muslim customers.

##### ***Theme 2: Structuring Products according to Three Different Laws***

Another important challenge that Islamic financial institutions in Canada face is that they need to structure their products according to three totally different laws. These are the Shariah law, the financial institution law and the taxation law. Furthermore, in order to do that, Muslim managers have to hire a team of lawyers and shariah professionals which requires a lot of time and effort and thus, additional costs. Informant IFI2 declared:

*Regulators did not do anything to allow for these (Islamic) structures to be created without any complications and all products that currently exist are more about work around solution*

Additionally, informants IFI3 and IFI4 said:

*The most challenging thing for us is to comply with three different legislations and to come up with the wording and documentation that will be acceptable for all three laws*

Participants who are Islamic financial institutions managers attest that if there was a framework that considered Islamic financial products in its content would have made tasks much easier not only for them but also for the Canadian Muslim community. They affirm that having one set of rules to respect and follow is much safer than

looking for work around solutions in order to adhere to the crucial shariah law, the taxation law, as well as different financial laws depending on the institution type. As informant IFI2 said:

*It's not that it cannot be done for some products. We have structured some products but it's very complicated and could be simplified if these rules were allowed for*

### **Theme 3: Restrictions for different types of Islamic financial institutions**

As previously mentioned, because of the quasi-impossibility to open an Islamic bank, Islamic financial products were rather offered in Cooperatives, Credit Unions and Private Financial Companies. Again, this did not alleviate all the hurdles that Muslim managers face, since even these types of institutions contain some restrictions that do not allow an easy offering of Islamic retail-banking products. These issues are enumerated below:

- **Provincial Credit Union Acts** in Canada restricts credit unions from offering their products to all Canadians. It is rather restricted to the Province where it is located only. Informant IFI1 said:

*There is a small Credit Union providing diminishing Musharaka financing but that's a credit union and its scope is limited to geographic location.*

Additionally, credit unions in Canada are not allowed to share risk which presents an inhibition for some Islamic financial products that contain risk elements that need to be shared between the customer and the institution. Similarly, the act does not allow that type of organization to create partnership with its customers. Informant IFI1 mentioned:

*Islamic financial institutions do have an issue when it comes to that sense of doing diminishing musharaka and really coming on board as a general partner because that's increasing their risk exposure.*

Finally, even though credit unions are the only institution besides Canadian banks that offer deposits, these cannot be offered through a sharing of profit and loss which is the case of some types of Islamic deposits.

- **The Canada Cooperatives Act** causes some inconveniences for Islamic cooperatives in Canada. The main products that are offered in Islamic cooperatives are home mortgage and equity investments. However, these products contain some challenges since the Act does not allow people who acquire a house through the cooperative to rent any part of the house. Informant IFI4 said:

*In other institutions than cooperatives, some home owners do rent their basement but in our cooperatives' system they cannot; and if one house is rented or partially rented the cooperative can lose its status and that's a challenge*

The reason is that houses financed through a cooperative have a privilege to be tax deductible. Therefore, if in any case people rent the house or even part of it, it will not be considered as a cooperative product and hence the cooperative will need to pay taxes for it. Certainly, renting part of the house is not an obligation; yet, it is a tradition in Canada to rent a basement, for example, in order to pay for the mortgage.

On the other hand, cooperatives cannot allow Muslims to invest in equity. The only possibility is to offer 30% on equity and this only to its members. Additionally, investors in cooperatives cannot get more than 6% in dividends. IFI4 said:

*Cooperatives have restrictions; a cooperative cannot give dividends more than 6% to its members*

Finally, cooperatives wishing to offer insurance policies are obliged to pay interest which goes against the principles of an Islamic institution.

- **Canada Business Corporations Act:** As per this act, a private company cannot have more than 50 shareholders. This does not particularly represent a challenge for an Islamic private company since it applies to all Canadian private companies but Muslim managers state that this does not help Islamic finance since there is an important Muslim community in the country and not enough robust Islamic financial institutions to satisfy their needs. Informant IFI4 mentioned about this point:

*We cannot have more than 50 shareholders in private companies but people are investing with us and we are investing in other projects and other businesses but we cannot take more than 50 shareholders. As the community grew the demand grew so we had to stop taking new members. This is not fair to newcomers. They come to us, we say sorry we can't help you we are a community owned project. We had no choice*

- There was a possibility of creating a mutual fund for the purpose of offering Islamic financial products; however, informants affirm that the system in this type of institutions requires customers to take a high risk which is not the type of products the Canadian Muslim community needs.

**Theme 4: Absence of a Legal Enforcement Body**

Muslim managers of Islamic financial institutions in Canada complain that there is a lack of government support to Islamic finance. Informant IFI2 said:

*Islamic finance is struggling in Canada because there hasn't been, I guess, openness or willingness from the government at all levels*

Because of this lack of support, Islamic finance is not regulated in Canada and hence, there is no enforcement body that verifies the activities of Islamic financial institutions in Canada. Informant IFI2 added:

*In Canada, Islamic finance is not regulated so anybody can put their hand and say that I am halal or have an Islamic financial institution but nobody is there to verify*

This has caused a couple of these institutions to either fail to be Shariah-compliant or to indulge in fraud. As a result, a bad image contaminated all other Islamic financial institutions in Canada and hence, they are paying for the mistakes of the defaulting institutions. Informant IFI2 attested:

*Many claim that the Islamic financial institutions are not even Shariah compliant*

On the other hand, Islamic institutions face a heavy competition next to the big banks that has full support of the government. Among many of the consequences of this inequity is the high price offered by Islamic institutions compared to an affordable one offered by Canadian banks.

**Theme 5: Quasi-impossibility to open an Islamic bank**

The first thing Muslim managers thought about in order to offer their services was to open an Islamic bank. However, the extreme difficulty opening a new bank in Canada discouraged them from achieving this project. First of all, it may take more than ten years before getting a license for any new bank. Then, there is a significant capital requirement that is not often accessible. Additionally, because of the unique nature of Islamic financial products, extra compliance costs would be imposed by policy-makers according to professional lawyers. Informants IFI1 and IFI4 said:

*To be recognized as a bank, there are substantial criteria: the regulatory framework and you have to get substantial capital cash injection that needs to be raised*

Regarding the same, IFI2 stated:

*Setting up a bank takes years of process, millions of dollars of fees, and there's no guarantee that you will get the bank license*

It is worth noting that in Canada, it is lawyers who interpret the law and hence they are the ones that advise financial managers about what they can and cannot do. These lawyers did not get any solution for these managers except to think about non-bank financial institutions such as cooperatives, credit unions, private companies and mutual funds. As a result, Muslim managers followed this advice, opened these financial institutions; yet, they still face some difficulties with financial laws even if these are less than the banking ones.

**Theme 6: Taxation Issues**

For Islamic home financing, the double land transfer tax poses an issue for Islamic financial institutions. Unless these institutions create their products through different structures, they would need to pay a land transfer tax for each transaction in relation to the house ownership. IFI2 said:

*When structuring, let's say in particular a mortgage product that would be under diminishing musharaka or murabaha, we always run into double land transfer tax issues and/or taxation on transferring of ownership over multiple period of times*

Similarly, wherever a product mentions the word 'profit' as its income, the institution has to pay an Income Tax for it creating extra charges for this same institution. Additionally, whenever a product is bought for the purpose to be resold, the bank will need to pay double taxes for it since these are considered as two different transactions. While Islamic financial institutions manage to find bypass solutions, all managers state that it would be much more practical to have tax alleviations in order to perform their activities in a simpler way. In that regard, informant IFI1 said:

*Again the taxation: we don't have the setup right now, for example Musharaka or Murabaha is now being double taxed*



***Theme 7: Other Issues***

In addition to the legal issues faced by Islamic financial institutions in Canada, the managers mention some other issues that they face in their practice. One of the issues is the lack of capital. Muslim managers said that since they are working individually, it is often hard to find the adequate capital to face the demand of the large Muslim community.

On the other hand, some Islamic institutions complain of not receiving enough demand. There are three main reasons for this lack of demand. First, there seems to be a lack of marketing of the Islamic financial products from these Islamic institutions. Then, the Muslim community became skeptical after seeing the bad experience of some other Islamic institutions that seemed to perform with dishonesty and lack of transparency. Third, the prices of the Islamic retail-banking products do not seem to be competitive next to the conventional ones offered by the Canadian big banks.

Finally, the informants declare that the word 'Islamic' poses an issue to the offering of Islamic financial products as well. Many of them try to avoid using this word and give an alternative name to the products.

In fact, the data revealed that the three major issues and challenges that impact Islamic financial institutions in Canada are the government inertia towards Islamic finance, the Muslim community inertia towards asking for their rights of financing their needs through Islamic finance in order to respect their religious requirements in that matter and the failure of some Islamic financial institutions that previously turned out to not comply with Shariah principles related to Islamic finance in their products and/or behaviors.

The themes and sub-themes were further analyzed for the purpose of studying potential connections among them. The relationships found between the themes and sub-themes were either causal, chronological or/and concurrent. One theme was independent and was not related to the other ones according to the data. The following figure clarifies the issues and challenges explored as well as the connections between them:

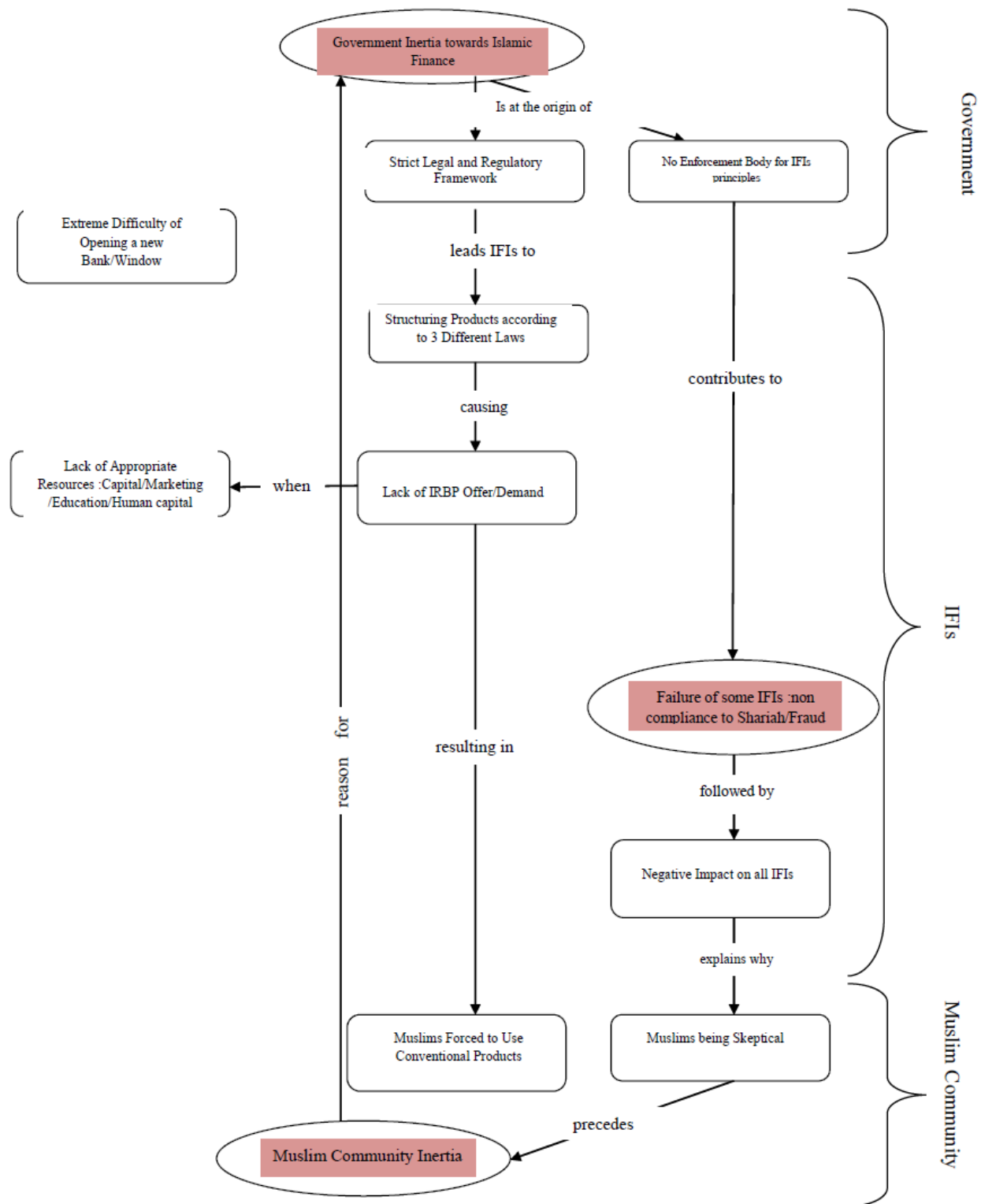


Figure 2. Issues and challenges faced by IFIs in Canada and the connections between them

**5. Findings**

The purpose of this research was to explore the issues and challenges faced by Islamic financial institutions in

Canada. After a thorough qualitative study using semi-structured interviews done with managers of Islamic Financial Institutions, data was analyzed and the issues and challenges generated are as follows:

One of the most important issues and challenges that IFIs face in Canada are the strict legal and regulatory framework of the Canadian banking and financial system. In fact, some of these laws and regulations do not allow for an Islamic bank to open in Canada or for existing banks to open an Islamic window. For this reason, Muslims turn to the solution of opening other Islamic non-bank financial institutions such as cooperatives, credit unions and private companies. The laws and regulations of these institutions are less strict than the banking ones; however, they remain strict since for instance credit unions cannot deal in partnership and have to offer its services in the Province where it is located only; and cooperatives members cannot rent their mortgages.

Because of the restricted legal and regulatory framework, Islamic financial institutions face the challenge of structuring their Islamic financial products according to 3 different laws which are the Shariah law, the Canadian financial laws and taxation laws. This structuring has not always been easy for these institutions and for this reason, not many Islamic financial products could be offered especially when it comes to Islamic retail-banking products (IRBP) that are important for the Muslim community. When this latter does not find the appropriate IRBP that they need, they are forced to turn to conventional financial institutions. The scarcity of IRBP is also explained by the lack of some appropriate resources that are crucial for the success of any financial institution which are the capital and the marketing that is supposed to attract the Muslim community.

Since the government did not set any laws and regulations for Islamic financial institutions including an enforcement body that supervises and verifies the activities of these institutions, some of them fail to adhere to Shariah principles. There was even a case of fraud that negatively impacted the image of all other Islamic financial institutions which resulted in an important part of the Muslim community to be skeptical and questioning the adherence of all of the IFIs in Canada. As a result, many Muslims became reticent to using the products of IFIs.

Last but not least, the major issue that emerged from this research is that the Muslim community inertia towards asking the government for a proper and wide implementation of Islamic finance resulted in the government not taking the matter to an upper level, in the Islamic financial institutions struggling with the existing legal and regulatory framework and thus for Islamic finance to stagnate in Canada creating a sort of a vicious circle. These issues and challenges can be summarized in the following figure:

## **6. Conclusion and Recommendations**

The results of this research meet with the previous few studies that were done about Islamic finance in Canada and that revealed that one of the main issues and challenges faced by Islamic financial institutions were the current Canadian banking and financial laws and regulations that do not fit Islamic finance requirements and principles, marketing issues, lack of capital and taxation (Tahmina, 2013; Edward, 2011; Goud 2009). It also confirms the need of an enforcement body that would ensure the adherence of IFIs to Shariah principles of Islamic finance. However, this paper adds a discovery to the field which is the Muslim community inertia in asking for their rights from the Canadian government. Additionally, the government inertia towards Islamic finance causes the failure of some Islamic financial institutions which then provokes the skepticism of the Muslim community which presents a sort of vicious circle that will not end if action is not taken in order to solve these issues.

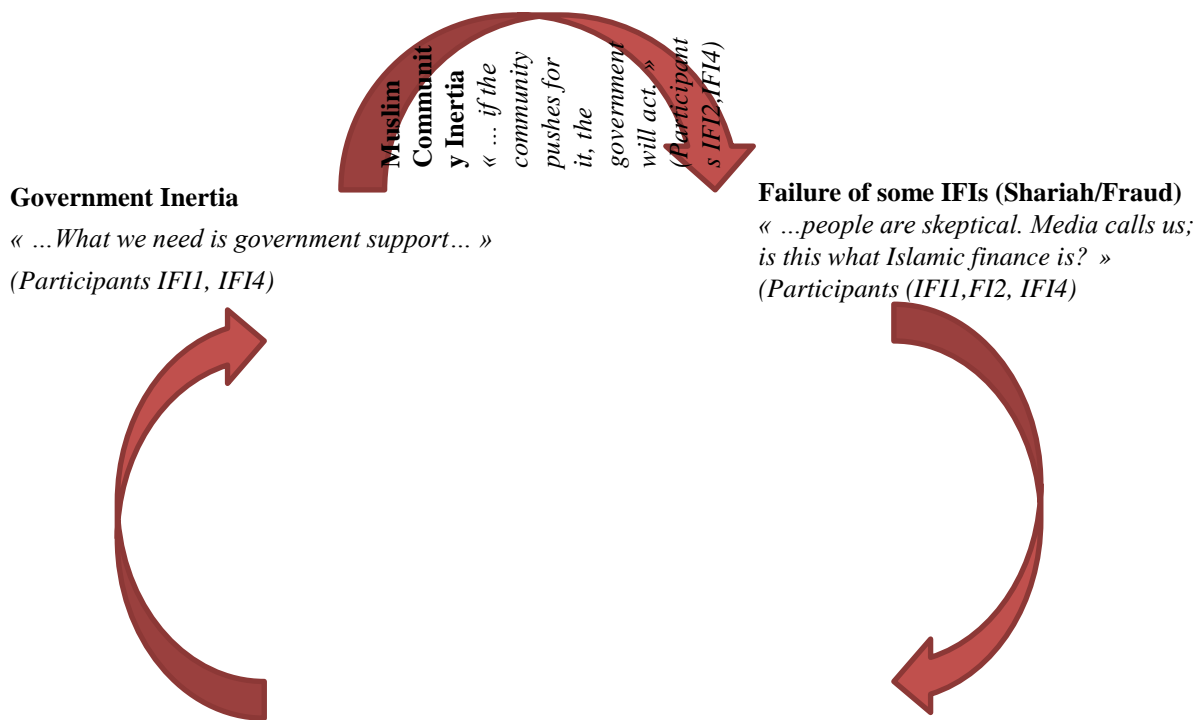


Figure 3. Major issues and challenges faced by IFIs and the causal connections between them

Recommendations that can be done after exploring the results of this research are for the 3 important players for Islamic finance in Canada which are the government, the Islamic financial institutions and the Muslim community.

- For the Muslim community to push the government to satisfy their needs in terms financing since religion is generally of utmost importance to Muslim which explains their needs for Islamic finance.
- For the Canadian government to amend and/or broaden the definitions some of the strict laws and regulations that inhibit the implementation and smooth functioning of Islamic financial institutions in the country.
- For Islamic financial institutions to carefully adhere to Shariah principles related to Islamic finance in order to keep the essence and principles of this type of financing and not to hinder the image of Islam that emanates from greediness, lack of knowledge and/or indifference.

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