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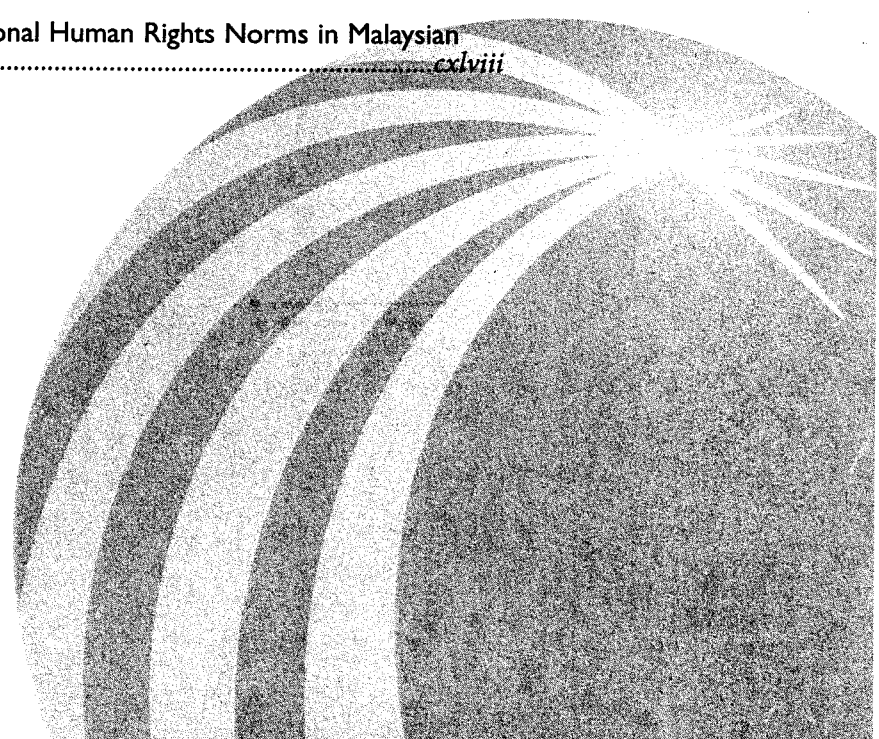
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SHARIAH COMPLIANCE PROCESS IN MALAYSIAN ISLAMIC BANKING

by

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Abstract

It should be understood that the Muslims worldview which sees Islam as a set of the rules of conduct for the overall areas of life including the economic sphere, is a driving force for the birth of Islamic banking. As a faith based financial institution, the Islamic banking business is therefore, strictly dictated by religious tenets, namely the Quranic and prophetic teachings. Accordingly one of the most important aspects in Islamic banking is the regulation on the Shariah compliance. In this context, the issue on the shar'iah assurance in the product offering is relevant to be considered. The paper seeks to analyse the process and procedures for Shariah assurance in the product offering in Islamic banking in Malaysia. The theoretical overview of the shar'iah assurance, the regulatory frameworks designated to cater such process and procedures are then mapped and evaluated in the context of the practical implementation of some of the Islamic banking products. Lastly, valuable suggestions are then presented to be proportionally adopted for the purpose of achieving better process and procedures in the Shariah assurance in the product offering in Islamic banking in Malaysia.

INTRODUCTION

Shariah compliance plays a significant essence of the Islamic financial institutions ('IFIs')'s governance. It is the duty of the institutions to ensure that all of its activities and operations are Shariah compliant. The body that is

final reference of Shariah issues on financial matters, the CBA 2009 provides that the appointment of members to SAC is made by the Yang di-Pertuan Agong, on the advice of the Minister after consultation with the Central Bank.²

Unlike the SAC, which is governed by the Central Bank Act 2009, the SC is established by virtue of the guidelines on the Governance of Shariah Committee for the Islamic Financial Institutions (BNM/GPS1) which has now been replaced by the Shariah Governance Framework of Islamic Financial Institutions 2011. The SC facilitates the SAC in advisory duties, as it is impossible for the council to advise all Islamic and conventional financial institutions conducting Islamic banking business. In Malaysia, Islamic banking business is conducted by two different financial institutions, namely a full fledged Islamic bank and conventional bank offering Islamic banking business. The former is within the ambit of the Islamic Banking Act 1983 ('IBA') and the latter is governed by the Banking and Financial Institutions Act 1989 ('BAFIA'). The regulations on the SC apply to both types of financial institutions equally. It is provided under s 3(5) of the IBA 1983 and s 124 of the BAFIA respectively; that any bank conducting its business based on Islamic principles shall establish a Shariah Advisory Body to ensure Shariah compliance. In fact, the establishment of the SC is a requirement for granting license for the institutions carrying out Islamic banking business. The license will not be granted unless there is a provision for the establishment of a Shariah Advisory Body in the articles of association of the respective IFIs.³

METHODOLOGY FOR SHARIAH COMPLIANCE

There are some methods and procedures of the process which Shariah advisors undertake to examine and ascertain Shariah compliance of the product and operation of Islamic banking. These methods and procedures are termed as 'instrument for supervision', which according to 'Abd al-Hamid al-Ba'li, there

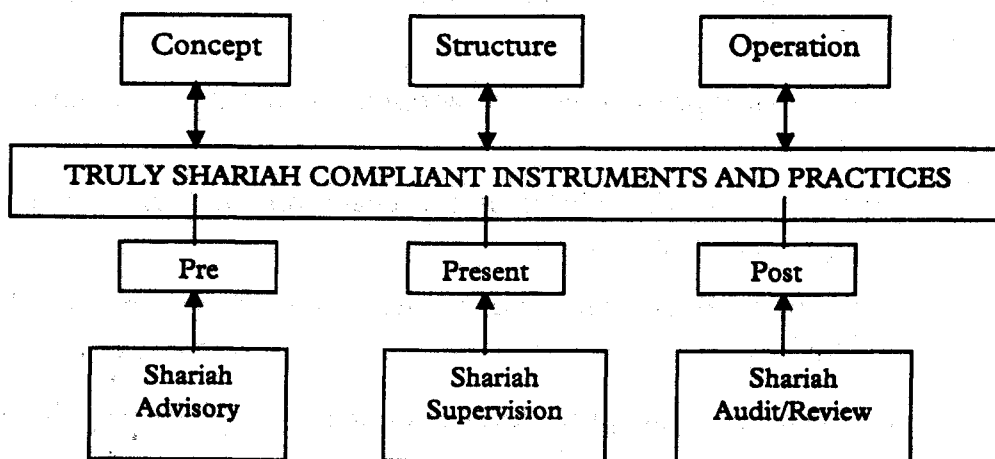
2 Section 33 of the Central Bank of Malaysia Act 2009. It is interesting to note that the authority of the SAC is not only confined to Islamic banking business, but extends to takaful business, Islamic development financial business, or any other business which is based on Shariah principles and is supervised and regulated by the Central Bank. This is the unique nature of the Islamic finance industry in Malaysia whereby the Islamic banking, takaful and Islamic capital market are considered different industries. Thus, a financial institution that operates banking business and takaful is legally required to establish SC for each business respectively.

3 Section 5(a) and (b) of the IBA 1983.

are three instruments for supervisory activities:⁴

- (1) researching and evaluating the operation of the bank;
- (2) issuing decisions relating to the product and operation which may be periodically, daily, weekly, monthly, annually, etc; and
- (3) withdrawing or cancelling decisions and operations which are not in line with the Shariah principles.

To achieve the effectiveness in Shariah supervision on compliance, it is an urgent task for the Shariah advisors to examine the whole aspects related to the operation of the bank, as the responsibility of the board is to ensure that the whole aspects are conducted on the basis of Shariah principles. The Shariah supervision is not limited solely in giving Shariah opinions or issuing fatwas or advices before certain products are launched by the bank, rather, reviewing and auditing exercises after the products or schemes are launched are indeed compulsory. For such reason, there are three stages of the supervision method that may be adopted — pre-supervision (*qabliyyah/sabiqah*), ongoing supervision (*athna' al-'amal*), and post-supervision (*ba'diyyah/lai'qah*).⁵ The following diagram (Diagram 1) illustrates the three-tier Shariah compliance method.



Adapted from Rusni Hassan, *Fundamentals of Islamic Banking Products and Instruments*,

4 'Abd al-Hamid al-Ba'li, *Taqnin Amal al-Hai'ah al-Shar'iyyah: Mu'amalah wa Aliyatuh* at p 63 (a paper presented in al-Mu'tamar al-Thalith li al-Hai'at al-Shar'iyyah li al-Mu'assasat al-Maliyah al-Islamiyyah, 5-6 October 2003, Bahrain).

5 'Abd al-Sattar Abu Abe Ghuddah, 'Al-Asas al-Fanniyyah li al-Riqabah al-Shar'iyyah wa 'Ilaqatiha' in *Hauliyah al-Barkah, Majallah Mutakhassisah bi Fiqh al-Mu'amalat wa al-'Amal al-Masraf al-Islamiy* (2002) 4 at p 22. Also refers to 'Abd al-Hamid al-Ba'li, *Taqnin* at p 64.

THE PROCESS OF ASSURING SHARIAH COMPLIANCE

The process in assuring Shariah compliance in Islamic banking may involve a long chain of activities which are interconnected to each other. The process involves various parties and covers various activities from the initial formation of the products until after such products are marketed to the customers. In a nutshell, there are five steps for the Shariah compliance process adopted by Islamic banking practitioners in Malaysia. First of those is establishing measures of the product offered, and the second is advisory or supervisory activities. The next step is issuing a Shariah opinion or fatwa of a new product and then, taking necessary action towards the case of non-compliance towards *fatwas* or decision. The last step is issuing Shariah opinions in the annual report of the bank to be presented in the shareholders' general meeting. Deliberation of each step will be presented in the following discussions.

Establishing specific measures for product offering

The first and most important stage in ascertaining Shariah compliance is defining the product. The details of the products in Islamic banking business are not clearly stated in the existing legislations, neither in the Islamic Banking Act 1983 ('IBA') nor the Banking and Financial Institutions Act 1989 ('BAFIA'). Guidelines for product offering however, have been enumerated in the SPTF (*Skim Perbankan Tanpa Faedah*) or Interest Free Banking Scheme Guidelines,¹⁰ which is initially designated for conventional banks offering Islamic banking business, instead of Islamic banks.¹¹ Setting up clear measures of the products is a step that the bank shall undertake before the application of the product into a real financial contract. The measures are made in such a way that enables both the bank and the customers to understand very clearly, the nature of the contract (product) and its legal effect.

Under the guidance of Shariah Committee ('SC') members, the bank formulates the structures of the products according to the specific measures (terms of product). The terms of the product is a brief description on every product offered that provides an easy and simple process of execution of the

10 Bank Negara Malaysia Guidelines on Skim Perbankan Tanpa Faedah (SPTF) for Finance Companies 1993.

11 The absence of a specific legal provision concerning the features of the product for Islamic banks, may be due to the fact that Islamic banks were incorporated based on the IBA 1983, in which the Shariah Committee (SC) is required to ascertain that any product offered does not infringe Islamic tenets. The Shariah Committee (SC) members together with the management of the bank are capable of deciding a list of products which are compliant with Shariah principles.

contract in the respective product. *Bay' bithaman ajil* ('BBA') financing is a good example to illustrate the point. According to the SPTF Guidelines 1993, it is, 'the sale of goods on deferred payment basis at a price which includes a profit margin agreed by both parties'.¹² Based on the definition, an Islamic bank then defines it in a way that eases the customers to clearly understand the product. Accordingly, the BBA product terms in this context may be defined as 'deferred payment sale whereby the bank will finance customers who wish to acquire an asset but to defer the payment for the asset for a specific period or to pay by installment'.¹³ This product then is formulated into a specific applicable term and thus, in the BBA facility agreement, the following provisions are normally adopted: 'Under this facility (BBA), the Bank shall first purchase the asset concerned. The Bank subsequently sells the relevant asset to the Customer at a selling price which comprises of the actual cost of the asset to the Bank and the Banks margin at profit.'¹⁴

As the terms are initiated by the industry, hence there is non-uniformity of the features of the product terms, as it is depends on the Islamic financial institutions themselves. For instance, another Islamic bank has adopted a slight different definition of the BBA. It is defined in short as: '*Bay bithaman ajil* or Deferred Payment Sale refers to the sale of goods on a deferred payment basis at a price that includes a profit margin agreed upon by both the buyer and the seller.'¹⁵ This definition, even though not in verbatim with the other banks' definition, seems to be sufficient to describe the essential aspects of the product.

There could be different terms used by the banks, to refer to the products, but, as it is apparent from the two terms from two different banks, that the difference in delivering such terms is merely in the wordings, while substantially they are similar to each other. The additional features may be given by the banks in their terms of the products, as this is a matter of the banks' policy, however, these must all the time be Shariah compliant.

Advisory or supervisory activities

Basically, there are two kinds of supervisory or advisory activities that the Shariah Committee (SC) undertakes; they are periodical meetings with the management, and ad hoc meetings in resolving urgent issues. The rigorous

12 SPTF Guidelines 1993 at p 4.

13 Refer to Bank Islam Malaysia Bhd at: <http://www.bankislam.com.my>.

14 *Ibid.*

15 Maybank at: <http://www.maybank2u.com.my>.

Islamic banking activities requires frequent meeting to be conducted with the Shariah advisors to resolve the issues faced by the bank. Periodical meetings are set out to evaluate the operation and products of Islamic and conventional banks conducting Islamic banking business. Usually, this mode of supervisory or advisory activity is conducted through the meeting with the management of the bank. Since this meeting is a matter of internal policy, the frequency of it may be different among banks. However, monthly meetings are most common.¹⁶ However, when issues relating to Shariah arise and are considerably urgent, the members of the Shariah Committee (SC) are then invited to a meeting.¹⁷ Certain departments within the bank, from which the Shariah issue arose from, either because of a new product or due to other issues, have to provide paperwork pertaining to the context of the issue and a proposed possible solution. Based on this, the members of the Shariah Committee (SC) have to resolve the issue immediately and thus an ad hoc meeting needs to be held. This ad hoc meeting is on a case to case basis but this is indeed part of the duty of the members of the Shariah Committee (SC) to solve such problems when needed.

Issuing Shariah opinion or *fatwas*¹⁸ relating to the products of Islamic banking

The issuance of Shariah opinions relating to Islamic banking products is one of the most important roles of the Shariah Committee (SC). Shariah opinion or fatwas can be divided into two stages. First, the issuing Shariah opinions relating to the products or issues which their basic contracts has been resolved by the Shariah Advisory Council (SAC). Second, the issuing of fatwas relating to the product or new issues which no resolution of the Shariah Advisory Council (SAC) has been found.

In the case where there is ready resolution on the respective product, issued by the SAC, the product development of the bank will prepare the proposal to

16 In this case, the BIMB has meetings once in every two months. Source: interview with the head of Shariah Department who is also the secretary of the Shariah Committee in the BIMB, Ustadh Nasrudin Yaakub on 28 February 2007. Also, interview with Dr Abdul Halim Muhammad, Vice Chairman of the SAC, 22 February 2007.

17 Interview with the Head of Shariah Department who is also the secretary of the Shariah Committee in the BIMB, Ustadh Nasrudin Yaakub on 28 February 2007; interview with Dr Abdul Halim Muhammad, Vice Chairman of the SAC, 22 February 2007; interview with Dato Md Hasyim Hj Yahya, a member of the SAC, 7 March 2007.

18 Though scientifically, there is no sharp difference between Shariah opinion and *fatwa*, as these two are actually similar in nature, technically, a Shariah opinion is a specific term to call the opinion given by Shariah Board within the industry. In contrast, a *fatwa* usually refers to the decision delivered by the higher Shariah body, namely the SAC.

be submitted and discussed with the Shariah Committee. Shariah Committee (SC) members, despite listening to the presentation, may also request to the Shariah department to conduct necessary research pertaining to various aspects relevant to the proposed product. This committee members, taking the proposal and result of the research into account, then analyses the issue and resolves the problem in a clear statement in the form of a Shariah opinion. However, when Shariah Committee (SC) members are unable to resolve the issues, they shall consult the Shariah Advisory Council (SAC), and when necessary, obtain a formal approval.

The procedure is more rigorous in the case where there is no resolution made on the product to be developed. The respective bank, through the Shariah Committee (SC), requires confirmation and approval from the Shariah Advisory Council (SAC) in the Central Bank. It is the duty of the Shariah Committee (SC) to prepare the proposal and adequate Shariah opinion to justify the product. The proposal (with justifications) is to be submitted to the Islamic Banking and Takaful Department of the Central Bank of Malaysia for deliberation by the SAC. At this level, the process of the issuance of fatwas or decisions has to follow the following process:¹⁹

Firstly, the bank sends an application to obtain a *fatwa* from the Central Bank of Malaysia (Islamic Banking and Takaful Department) whereby proper explanation of the proposed product must be provided together with Shariah justification on the product.

Secondly, the Islamic Banking and Takaful Department of the Central Bank, in response to the above application and proposal, undertakes necessary research and provides a detailed analysis on the proposal. The analysis is then tabled and discussed by the members of the Shariah Advisory Council (SAC) for the purpose of getting the *fatwa* pertaining to the product.

Thirdly, the Central Bank may invite the product owner (bank) and the Shariah Committee (SC) of the respective bank for a meeting designated to resolve the issue. The proposal forwarded by the respective bank, together with the paperwork is then presented in the meeting. The aim behind the involvement of various related parties in this meeting is to analyse the product

19 This process of the issuance of fatwas is based on some sources of information: (i) interview with Mr Hamzah Kamaruzzaman, staff of Department of Islamic Banking and Takaful, the Central Bank of Malaysia; (ii) interview with Dr Abdul Halim Muhammad, Vice Chairman of SAC, 22 February 2007; and (iii) interview with Dato Md Hasyim Hj Yahya, a member of SAC, 7 March 2007.

related problems in all aspects, to ensure that the *fatwa* is made with full understanding of the concept of the product.

Fourthly, the process involves resolving the issue. Having reviewed the whole aspect of the proposal, the Shariah Advisory Council (SAC) then conducts a meeting or even a series of meetings to deliberate and analyse problems and issues relating to the proposal. Having undertaken such procedures, the Shariah Advisory Council (SAC) may then resolve the problem or issue and grant the approval accordingly. The result is then formulated in the form of a *fatwa* or resolution of this Council.²⁰ The *fatwa* or resolution shall be circulated by the Central Bank to all the banks conducting Islamic banking business and not specifically to the bank from which the Shariah issue was raised.

Considering the few stages of the process that needs to be undertaken, it is understandable that the issuance of a *fatwa* or resolution may be delayed. The duration needed for the issuance of a *fatwa* mostly depends on whether or not the problem is complicated. From the experience of the Shariah Advisory Council (SAC), the longest time taken to resolve an issue may extend to three months.²¹

Ever since the Shariah Advisory Council (SAC) was established in 1997, no less than 21 *fatwa* or resolutions have been issued, ranging from banking to *fatwa* issues,²² minus Islamic securities, since the Securities Commission of Malaysia (under the Securities Commission Act 1993) has its own Shariah Committee with its resolutions.²³ The *fatwas* or resolutions of Shariah Advisory Council (SAC) range from those which are pursuant to the application or request from the industry, and also other relevant *fatwas* or

20 The official term to call such products of the Shariah Advisory Council (SAC) is 'decision'; see BNM/GPS1, Guidelines on the Governance of Shariah Committee for the Islamic Financial Institutions, December 2004. Whereas for the product of the Shariah Advisory Council in the Securities Commission, for comparison, the term referred to is 'resolution', see Securities Commission, Resolutions of the Securities Commission Shariah Advisory Council (Kuala Lumpur, 2006). However in the in the publication issued by the Central Bank of Malaysia pertaining to the decisions of this Council, the terms used is also resolution: Central Bank of Malaysia, Shariah Resolutions in Islamic Finance (Kuala Lumpur, 2007).

21 Interview with Dr Abdul Halim Muhammad, a member of the SAC for the appointment tenure 2004–2006 and 2006–2007 (22 and 27 February 2007). Prior to the appointment he was a member of the SAB in various Islamic financial institutions, such as, the Malaysian Development Bank, RHB Bank, Bank Rakyat, Bank Muamalat and Bank Bumi.

22 Central Bank of Malaysia, *Shariah Resolutions in Islamic Finance* (Kuala Lumpur, 2007).

23 For the resolutions issued by Shariah Committee of the Securities Commission, see Securities Commission, *Resolutions*.

resolutions relating to Islamic banking and finance which are independently initiated by the Central Bank of Malaysia, particularly by the Department of Islamic Banking and Takaful.²⁴

Enforcement of *fatwas* or decisions

The non-compliance towards issued fatwas is perceived as ignorance and infringement towards Islamic tenets. It is reasonable therefore, that specific actions are to be taken on the relevant institutions which do not comply with the fatwas. In this regard, respective bodies which have the authority, namely the Shariah Committee (SC) and the Central Bank, shall ensure the enforcement of the fatwas. To ascertain such implementation, in certain banks for instance, a dedicated department is established to monitor the implementation of Shariah compliance. In Bank Islam Malaysia Bhd ('BIMB'), as a case in point, is the Department of Audit and Shariah Risk that is designated to do the monitoring work. Periodically, a team is appointed to monitor the bank's operation to ensure if there are Shariah issues or cases of non-compliance. Normally, the audit exercise is conducted once every two months. When the department finds a Shariah issue or case of non-compliance, a report of the findings then must be presented to the Shariah Committee (SC) to be resolved.²⁵

In the Malaysian structure of financial authority, ensuring the enforcement and compliance towards *fatwas* falls on the Central Bank. It is the Supervision Department in the Central Bank of Malaysia which is responsible for any non-compliance and ignorance.²⁶ Through certain methods of supervision, this department will bring any non-compliance cases to the Central Bank, and the Central Bank will then take the necessary actions.²⁷ In the case of non-compliance, the Central Bank may conduct an investigation at any time without prior notice and if the case of non-compliance is found, it will be subject to the respective punishment.²⁸ This is part of the authority of the Central Bank to control banks in Malaysia, as the provision below states:

24 Interview with the staff of Shariah Unit, Islamic Banking and Takaful Department, Bank Negara of Malaysia, Mr Hamzah Kamaruzzaman.

25 Interview with the Head of Shariah Department of BIMB, Ust Nasrudin Yaakub (28 February 2007).

26 Interview with the staff of Shariah Unit, Islamic Banking and Takaful Department, Bank Negara of Malaysia, Mr Hamzah Kamaruzzaman.

27 Islamic Banking Act 1983 ('IBA'), s 37(a)-(b).

28 The punishment ranges from administrative penalties, such as letter of reminder till petition for winding up the bank. See the IBA, s 37(a)-(b).

The Central Bank shall from time to time investigate, under condition of secrecy, the books, accounts and transactions of each Islamic bank and of any branch, agency or office outside Malaysia opened by an Islamic bank.²⁹

It is also stated in the BAFIA 1989, that the Central Bank holds similar authority over conventional banks conducting Islamic banking business. It is stipulated that the Central Bank shall, from time to time, examine various documents and transactions of the licensed financial institution.³⁰

Apart from this, it is again legally stated that the Central bank also, with the directive from the Minister, may conduct certain or special investigation if there is reason to believe that the Islamic bank is carrying on its business in a manner that contravenes the act.³¹ Thus, the power of the Central Bank over Islamic banks or banks conducting Islamic banking business is clearly noticeable here.

In the case of infringement towards the standing legal framework, or towards Shariah compliance, there are a few types of penalties of which shall be imposed on any institution which is proven to infringe the *fatwas*. In short, the penalties range from requesting banks to take certain steps to rectify the infringement as what is determined by the Ministry of Finance or the Central Bank, the revocation of the license, to presenting a petition to the High Court for termination of the bank by the court.³² These provisions, again, indicates that the compliance of the bank towards Shariah principles is mandatory.

Issuing Shariah opinions in the annual report

The annual report is an expression of the responsibility of the institution to the shareholders and to the public. For this reason, a complete performance of the bank and a comprehensive audit should be clearly presented in this annual report. In this regard, Islamic banks, or any banks conducting Islamic banking business, are obliged to provide different presentations compared to the banks operating under interests system. Despite the presentation on a prudential aspect, they shall also present the Shariah compliance aspect. Thus, the annual report of Islamic banks and conventional banks conducting Islamic banking business must contain the prudential audit³³ and Shariah audit.

29 IBA, s 31.

30 Banking and Financial Institution Acts (BAFIA) 1989, s 69.

31 IBA, s 32.

32 IBA, s 37(f); BAFIA, s 73

33 Prudential audit is the audit based on the measures which shows the fitness of financial aspects, such as capital adequacy ratio ('CAR') and non-performed Loan ('NPL').

As the prudential aspect is mandatory of the corporate governance for the banking industry, Islamic banks are also subject to the fulfilment of this aspect. In this regard, Islamic banks are treated equally with those of conventional banks. There are no differences between Islamic banks and banks conducting Islamic banking business compared to their conventional counterparts in terms of this prudential presentation. Variables which are used to review the prudentiality of conventional banks are also applicable here.

This is the distinctive feature which differentiates the Islamic banking business compared to that of the conventional. Having audited in their prudential aspect, the next audit is the Shariah audit, as the bank has to comply to Shariah principles in the operations and products. For the purpose of the annual report, the Shariah Committee (SC) members must conduct a comprehensive audit for a period of one year, and issue the Shariah opinion with regards to the compliance of the products and operations of the bank according Shariah principles. In the annual report, the statement of Shariah opinion must be included.

Based on the above process and procedures, the issuance of Shariah opinion in the annual report is the last stage of the whole process conducted in ascertaining Shariah compliance of Islamic banking.

ISSUES IN SHARIAH ADVISORY OR SUPERVISORY AND THE WAY FORWARD

Problem of Shariah Advisory or Supervisory

Shariah Advisory or Supervisory is a relatively new profession and hence further effort to enhance this profession is much demanded. This is a new area where Shariah scholars can play a significant role. Being a new area of profession, there may be some problems which need solutions. The authority of the body and its independence are cases in point. In turn, these problems affect the efficiency of board members in performing their duties. In specific reference to the operations of Islamic banking in Malaysia, there are some problems faced in Shariah Advisory/Supervisory:

The rapid development of the product

Banking industries are marked with continuous change and development of the products. In addition, product innovation is a main concern of the industry. The new products are sometimes formulated in the form of a mixture between or among the existing products, as well as in a form which is totally

new and novel.³⁴ Since the contract principles in Islamic law are well established, therefore, to accommodate a new product and fit it in the Islamic contracts, there is a need for a complicated contractual engineering.

Whilst the backgrounds of the members of the Shariah Committee (SC) are mostly from Shariah or *fiqh muamalah* expertise, they may find problems and difficulties to fit new banking products into the Shariah context. The adjustment between classical *fiqh* and modern financial products is far from easy.

The conflict of law (ikhtilaf)

It is a matter of fact that in various matters pertaining to *fiqh* (jurisprudence), there are subjects which are considered as the area of *ikhtilaf* (disagreement) among jurists, especially among the *imam* of *madhhab* (school of laws). Malaysia, which so far holds onto Shafie *madhhab*, needs to reconsider its stance. It seems that Shariah opinions which are solely based on this *madhhab* cannot be accepted globally. The application of *bai' al-'inah* is a case in point. In addition to this legal controversy, the problem is increasingly complicated due to the expansion of foreign financial institutions into Malaysia, as such institutions sometimes are still bound by the *fatwas* of Shariah Boards in their country which is confined to a different *madhhab* from that of Malaysia. The Al-Rajhi Bank is a case in point.³⁵ Hence, Malaysian practitioners are now considering more globally acceptable *fatwas*. It is the *fatwa* board such as the AAOIFI and IFSB, Majma al-Fiqh, and any other international standard boards that are significant to be considered in the harmonisation of *fatwas*.

The way forward

For the purpose of addressing the existing problems, there are plans and actions which may be taken. As explained below, part of the problems has been

34 For instance, the new product may be in the form of 'three in one' means three contracts in one product, or 'two in one', means two contracts in one product, as has been stated by Dato Md Hasyim Hj Yahya, a member of the SAC in the interview 7 March 2007.

35 The initiative for globally acceptable *fatwas* just in conform to the observance that international boards relating to Islamic banking may significantly play a role in bridging the gap in the Islamic legal aspect. As stated by Abdul Kadir Thomas, 'This body of 22 scholars represent broadly all members of the Organization of Islamic Conference (OIC), assuring that the Malaysian and other East Asian voices are heard on a peer basis with scholars from West Asia, South Asia and Africa. It is at AAOIFI and the IFSB that the convergence of East and West Asia is slowly but surely being hammered out into proper accounting and governance guidelines': Abdul Kader Thomas, *Islamic Finance Goes Global* at Far Eastern Economic Review, March 2007.

responded while the rest are still in the plans for action:

Advancing expertise

In order to overcome the difficulties in resolving cases pertaining to the new product, training is then provided. In addition to this, the composition of the members of the Shariah Committee (SC) is also a mixture of fresh scholars and experts in the field of finance. Consequently, the appointment of the members of the board who are mostly academicians from the universities may seem to be a suitable solution for the moment. They are in possession of the ability to do research, an ability which is very essential for doing Shariah Advisory.

Converging with the globally acceptable Shariah fatwas

For the purpose of introducing *fatwas* which are acceptable globally, various legal opinions from some major *madhhab* in the Muslim society need to be considered. Fatwas issued by the AAOIFI, IFSB, Majma al-Fiqh and other international standard bodies for Islamic financial business are to be considered as reference for the Shariah Advisory Council (SAC) in issuing *fatwas* or resolution. Apart from this, the establishment of some foreign Islamic banks has brought about implications to the fatwas that they follow. In this regard, being a licensed company, they naturally have to follow the Shariah Advisory Council (SAC)'s decisions, however, they may adopt another opinion that is different from the Malaysian standard with the approval of the Shariah Advisory Council (SAC) within the Central Bank.³⁶ This process enhances the standardisation of fatwas and Shariah opinion which is globally acceptable.

It is observed from the deliberation above that the existing framework has provided clear duties and responsibilities of all parties involved. Accordingly, the process of assuring Shariah compliance can be undertaken properly. However, in regard to the proposal for creating globally acceptable *fatwas* and resolution on Shariah matters pertaining to Islamic banking business, Malaysia needs a concerted effort to accommodate various opinions from different *madhhabs* without losing their step on the Shafie *madhhab*, which has been their view for centuries.

CONCLUSION

36 An example is when the Al-Rajhi Bank is willing to use a scheme under the *musharakah mutanaqisah in lieu of the bay' bithaman ajil*, and this bank did the above mentioned procedure: interview with Dr Abdul Halim Muhammad, Vice Chairman of the SAC, 27 February 27 2007.

The process of assuring Shariah compliance in Islamic banking is one of the substantial aspects in shaping the practice of Islamic banking business to be truly parallel with Islamic principles. It is a significantly meticulous process undertaken by the Shariah advisors and the management of the banks to ensure that Shariah compliant is enforced and maintained in the overall operations of the bank. However, more often than not, the Shariah advisors are facing constraints to provide intensive monitoring on the activities of the bank due to lack of knowledge on the practical operations of the banking activities and the limited time spent by them in the bank for the above purpose. As such, the proposal of having a permanent office of the Shariah advisors at the bank may be considered towards providing a more efficient method of supervision.

The function of this Shariah officer is to check and review all products and related documentations. This enables the board members, by assistance of an administrative officer in charge for the job, to monitor the activities of the bank. In addition to this, another method is also possible, namely, by conducting periodical (regular) meetings to answer and respond to all queries raised by the management of the bank. This method, however, is more formal, and may, to a certain extent, put the management of the bank in an uncomfortable situation. Indeed, this highly formal situation also means that the board members may not obtain the information directly. Another possible method for supervision is that the Shariah advisors undertake duties by checking samples of the banking documentations and other relevant issues.³⁷

It should be understood that the existence of the Shariah advisors is essentially needed by the bank, in spite of it being created to merely fulfil the requirements for obtaining a license. Therefore, the ignorance of Shariah advisors towards issues of Shariah compliance of the bank may be deemed as a failure of them to accomplish its basic mission. On the other hand, it seems to be difficult for the members of the Shariah advisors to closely understand the practical operation of the Islamic banking business when certain methods of monitoring are not provided.

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Interview

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