

# SHARIAH ADVISORY COUNCIL OF THE IFI IN MALAYSIA



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## Objective of the lesson

- To ensure that the students understand
- the legal framework,
- the roles and functions
- and related issues
- of the Syariah Advisory Council of the IFI

## Learning Outcome

- the students shall understand the development of syariah corporate governance in term of its legal framework, roles and functions and related issues of the Syariah Advisory Council of the IFI.
- the students shall know the qualifications of a member of the Syariah Advisory Council.

## References

- Central Bank of Malaysia Act 2003. the IBA 1983, the BAFIA 1989 and BNM/GPS1 .
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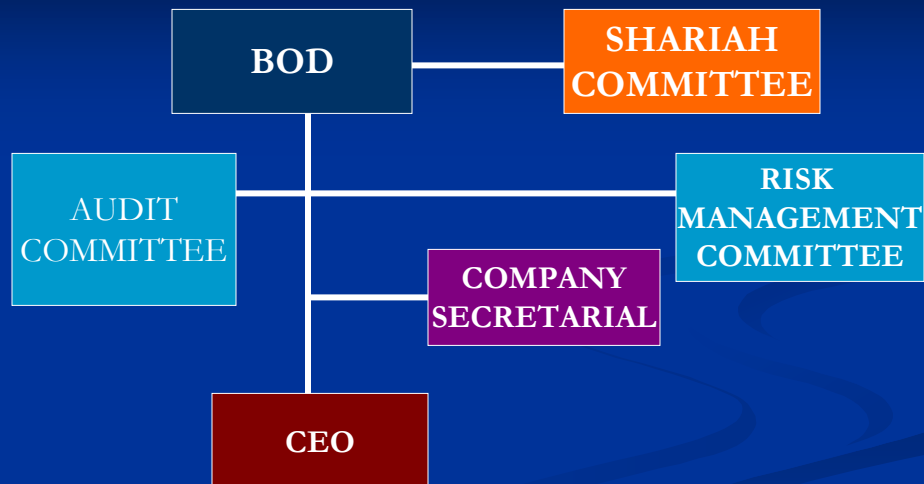
## BACKGROUND

- With 24 years of experience in regulating and developing the Islamic financial system, Malaysia has been recognized as having in place a good foundation to become one of the effective Islamic financial hubs.
- Malaysia is now having 12 Islamic banks, 3 are foreign Islamic financial institutions, 7 are Islamic subsidiaries of banking groups and several Islamic windows of conventional banking institutions. For Islamic capital market, Malaysia has 89 Islamic unit trust funds, 85 percent of Bursa Malaysia's counters are Shariah approved counters and 46 percent of the corporate bond markets are Islamic bonds or sukuku.

## INTRODUCTION

- Dynamic and good shariah corporate governance is the very essence in the development of Islamic banking and finance sector in Malaysia.
- In Islamic financial institution shariah corporate governance mostly refers to the management, establishment and affairs of the SAC.
- The establishment of the SAC is a statutory requirement to all IFI.

## Shariah Corporate Governance



## Definition

- The SAC is a committee set up either in Islamic financial institutions or takaful operators with a purpose to ensure Shariah compliance to its operations and products. It is a statutory requirement provided under the Central Bank of Malaysia Act 2003, the Islamic banking Act 1983, the Banking and Financial Institutions Act 1984 and the Takaful Act 1984.

## Cont.....

- The term Shariah Committee or Shariah Supervisory Council or Shariah Advisory Council has been used interchangeably for the past 21 years. IBA 1983 used the term Shariah Supervisory Council while BAFIA 1984 used the term Shariah Advisory Council. The term Shariah Committee has been introduced by Bank Negara Malaysia in the Guidelines and Procedures for Shariah Committee issued in December 2004.

## Objective

- The main objective of the establishment of the SAC is to advise the Islamic financial institutions on any Shariah matter and also to ensure compliance with the Shariah tenets and requirements in their operations

## The SAC and National Fatwa Committee

- The National Fatwa Consultative Committee for Islamic affairs was established in 1970 and now is under the administration of JAKIM, Prime Minister's Department.
- This body has the authority to issue fatwa at national level to any matter referred by *Majlis Raja-raja*. *Majlis Fatwa Kebangsaan* consist of Chairman of the committee, Mufti for each state, five persons knowledgeable in Islamic law appointed by Majlis Raja-raja and a member of legal profession or judiciary appointed by Majlis Raja-raja
- The SAC is under the IFI's management.

## The SAC and State Fatwa Committee

- The functions of the Fatwa Committee are to develop the Islamic law within the jurisdiction involving Muslim only.
- It has to advise the Ruler in all matters of Shariah and Mufti will be the chief authority in Islamic law matters in that state. The only recognized fatwa is legal rulings published by state Mufti with the consent of rulers and it has been gazzetted.
- The SAC's Resolution only binds their respective IFI.

## The Differences between SAC and Fatwa Committee

- Committee Members
- State Fatwa Committee has their own members specifically provided in the Administration of Islamic Law whereby National Fatwa Committee consist of representatives of mufti from all states including selected members appointed by YDPA. State Fatwa Committee will be chaired by Mufti and National Fatwa Committee will be chaired by selected appointed person by YDPA.
- Open policy for the IFI to choose and appoint their members of the SAC

## Advisory Jurisdiction

- National Fatwa Committee and State Fatwa Committee will discuss any matter which falls within the jurisdiction provided under the State List of Federal Constitution. This includes in the matter of Islamic family law such as marriage, divorce, ruju' maintenance, hadhanah, Islamic criminal offences and Islamic law of property.
- The SAC mainly issues resolution on muamalat and certain matters on ibadah.

## Enforcement of Fatwa

- A Fatwa of National Fatwa Committee and State Fatwa Committee is not binding and enforceable unless and until it is published in the state's gazette.
- The SAC's resolution does not bind the court to follow its decision.



## Subject Matter

- In selecting the subject matter of fatwa, the former is subject to three occurrence, namely if it is ordered by the YDPA or if it is upon the request of the general public or on accord of the Mufti himself.
- The SAC will issue resolution upon request made by the IFI, customer, lawyers and etc. It concerns more on the parties involved in the banking business.

## Cont...

- The SAC plays an active approach in selecting the subject matter of *fatwa*.
- Working hand in hand with the secretariats of respective banks, the SC has to scrutinize the Shariah principles, suiting it to the proposed product, and in many instances they have to suggest for alternatives.
- The nature of studying the fiqh in the Islamic banking and takaful industry is also technical and in depth

## The SAC's members of BNM

- Datuk Syeikh Ghazali Abdul Rahman,
- Datuk Md. Hashim Yahaya,
- Datuk Dr. Abdul Monir Yaacob,
- Datuk Hassan Ahmad.
- Datuk Dr. Abdul Halim Ismail,
- Dato' Abdul Hamid Haji Mohamad
- Dr. Mohd. Daud Bakar.
- Prof. Madya Dr. Abdul Halim Muhammad,
- Dr. Mohd. Ali Baharum
- Dr. Mohd. Parid Sheikh Ahmad

## THE DEVELOPMENT OF SHARIAH CORPORATE GOVERNANCE

- The ultimate purpose of the establishment of the the SAC is to ensure shariah compliance to its operations and products.
- The first SAC that has been set up was in 1983 by Bank Islam Malaysia Berhad.
- As part of the effort to streamline and harmonise the Shariah interpretations among banks, National Shariah Advisory Council of Central Bank of Malaysia was established on 1st May 1997. This Council is the highest Shariah authority on Islamic banking in Malaysia

## BNM/GPS 1

- This guideline consists of 10 parts with 24 sections and one appendix.
- The objective is to set out the rules, regulations and procedures in the establishment of a Shariah Committee; to define the role, scope of duties and responsibilities of a Shariah Committee; and to define relationship and working arrangement between a Shariah Committee and the SAC of Bank Negara Malaysia

## Qualification to be the SAC's members

- The Board of Directors of an Islamic financial institution shall appoint the members of the Shariah Committee the term shall be valid for a renewable term of two years
- The proposed member of the Shariah Committee shall at least either have qualification or possess necessary knowledge, expertise or experience in Islamic jurisprudence (*Usul al-Fiqh*); or Islamic transaction/commercial law (*Fiqh al-Mucamalat*)
- Practically additional qualifications are really being needed such as prudent and competent in syariah and legal aspects of Islamic finance and also proficient in English and Arabic

## Cont...

- Islamic financial institutions are not allowed to appoint any member of the SAC in another Islamic financial institution of the same industry.
- For example, X is appointed as the SAC member of Maybank Berhad. A is still eligible to be appointed as a member of Takaful Nasional. This is to avoid any element of conflict of interest and also for reasons of confidentiality within their respective institutions.

## DUTIES AND RESPONSIBILITIES

- The primary objectives of the establishment of the SC are to advise Islamic financial institutions on any shariah matter such as to its operation, to analyse and evaluate Shariah aspects of new products/schemes so as to ensure compliance with the shariah tenets and requirements in their operations.
- Guidelines on the Governance of SC for the Islamic Financial Institutions (BNM/GPS1)

## Concept and Structure of the Products

- The SC will evaluate the concept and structure of the new product and will review the existing products.
- For example, Home financing under the concept of *Bay' Bithaman Ajil*.
- From observation, Islamic banking products under the concept of “*Al Bay*” or contract of exchange are the biggest contributor in terms of growth and profit to the Islamic financial institutions in Malaysia.

## Documentation

- The SC will vet meticulously and endorse all products documentation.
- Section 20 (b) and (c) of BNM/GPS1 expected the SC to endorse and validate all relevant documentations and this includes the term and condition, the product manual, marketing advertisement, sales illustration and brochures used to describe the product.

## Business Operations

- The SC will monitor the Islamic banking operations from time to time.
- Section 20 (a) of BNM/GPS 1 provides that they shall advise the bank on shariah matters in order to ensure that the business operations of the Islamic financial institutions comply with shariah principles at all times. It includes the procedures for transaction, actual business operations, and system applicable to the banking operations.

## To Advice Related Parties On Shariah Matter Upon Request

- The related parties of Islamic financial institution such as its legal counsel, auditor or consultant, branches or even customer may seek advice on Shariah matters from the SC.
- There will be a syariah unit which administer of all request for the SC's deliberation.

## To Provide Written Shariah Opinion.

- Section 20 (f) of BNM/GPS 1 requires the SC to record any opinion given.
- In particular, the SC through its secretariat shall prepare written Shariah opinions.
- This written shariah opinion shall consist of issues, product structures and features, the SC's opinion together with their reasoning from sources of Islamic law.

## To endorse Shariah Compliance Manuals

- Section 20 (b) of BNM/GPS 1 states that the manual will specify the manner in which a submission or request for advice be made to the SC, the conduct of the SC's meeting and the manner of compliance with any Shariah decision.
- Islamic financial institution shall have a Shariah Compliance Manual which shall be regarded as a standard operational procedure for shariah governance.

## To assist the SAC of Central Bank of Malaysia on reference for advice.

- Section 20 (e) of BNM/GPS 1 requires the SC to assist the SAC of CBM on any matters referred by Islamic financial institution.
- If any institution refers the SAC on certain products and fiqh issues, the SC must explain the shariah issues involved upfront and they have to provide recommendations for a decision.
- The explanation and recommendation must be supported by relevant shariah jurisprudential literature from the recognized sources.

## General Tasks and Duties

- The SC also will deal with certain general duties and tasks relevant to their job scope and this includes to assist the related parties on shariah matter and to determine the zakat policy of the banks.
- Zakat is compulsory to every Muslim and Islamic institutions such as a bank.



## Procedures

- Receive inquiries from respected departments
- Syariah Secretariat will confirm the issues and documents to be presented to the SAC.
- Prepare memo to the SAC to seek Syariah views on the matter.
- The SAC's meeting
- Resolution of the SAC
- Endorsement by the SAC
- Circular to all departments and branches for notification.

## Statutory and Shariah Requirements

- The guideline provides that the SAC member will be appointed by the board of directors of an Islamic financial institution upon recommendation of its nomination committee.
- The appointment of the SAC member shall obtain prior written approval of BNM and the term of appointment shall be valid for a renewable term of two years.

## Cont....

- To ensure that the SAC would be able to function effectively, the composition of the Shariah Committee consist a minimum of three (3) members and their affairs will be managed by a shariah secretariat of the respective Islamic financial institutions

## Legal Framework

- The establishment of the SC is a statutory requirement to all banks which offer Islamic banking products pursuant to section 3 (5) (b) of the Islamic Banking Act 1983 for Islamic banks, section 124 (7) of the Banking and Financial Institution Act 1989 for Islamic banking scheme banks, section 8 (5) of the Takaful Act 1984 and section 16B of the Central Bank Act (Amendment) 2003.

## Cont....

- Central Bank of Malaysia has issued BNM/GPS 1 that regulates the governance of Shariah Committee.
- The parliament has amended section 16B of the Central Bank of Malaysia Act (Amendment) 2003 whereby the National SAC will be the sole authorities to be referred by the civil courts pertaining to Islamic banking and finance.

## Administration of Justice

- BNM with a cooperation of judicial body has agreed to set up a special High Court in the Commercial Division known as the Muamalah bench.
- According to Practice Direction No.1/2003, paragraph 2, all cases under the code 22A filed in the High Court of Malaya will be registered and heard in the High Court Commercial Division 4 and this special high Court will only hear cases on Islamic banking.

## Court's Jurisdiction

- Islamic banking and takaful could not be interpreted under the ambit of 'personal' but under the item 'finance' in the Federal Constitution. Therefore, it falls under the purview of the Civil court.
- List I Schedule 9 Federal Constitution

## Cases under Muamalat Bench

- Cases Registered from 1.3.2003 – 1.12.2005=656
- Settled Cases from 1.3.2003-1.12.2005=497
- Balance of Cases up to 1.12.2005=388
- Percentage of Settled Cases from 1.3.2003 – 1.12.2005=75.7%
- The statistic shows a remarkable amount of cases settled by the court from the year 2003 to 2005. However, all of the cases are concerning defaulters of facilities payment taken action by the respective banks. None, from the statistics, is challenging the decisions of the Syariah Committees.

## To What Extent The Legal Framework Works?

- From 1983 until 2006 the Islamic Banking assets in Malaysia amounted to RM113.5 billion, accounting for 11% of total banking asset. In 2010- Target 20%.
- The implementation of muamalat bench shows a positive result on the increasing numbers of settled cases. From the statistic, it shows that more than 75% out of 656 cases has been settled by the court from year 2003 to 2005.

## CONCLUSION

- The SC plays very important roles in ensuring good syariah governance.
- The setting up of a special High Court in the Commercial Division, the issuance of BNM/GPS1 and also the amendment of section 16B of the CBA shows positive indication by the government in providing more comprehensive and effective syariah governance.
- An effective syariah governance framework requires involvement of the Shariah Committee as the key player, the government as the regulatory body, the Islamic financial institutions as the implementer and also to other persons relevant to the business such as auditors, accountants, lawyers.

## Cont....

- Any resolution or fatwa either issued by National Fatwa Committee or State Fatwa Committee or the SC on *mucamalat* should be circulated and published by the mass media
- The SC must not only act merely as an advisory unit whereby its resolution or opinion may be rejected but it should be regarded as a decision and policy maker.

Thank You



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