

EVOLUTION OF SHARIAH STANDARDS AND GUIDELINES FOR AAOIFI, IFSB AND BANK NEGARA MALAYSIA

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When Islamic banks were established in the 1970s, they were confronted with a major challenge: how to assure users that their services and transactions were in compliance with the cardinal rules and principles of Shariah — which was the *raison d'être* of their establishment.

To fulfill this objective, Islamic banks established a new governance organ, the Shariah Board or Shariah Supervisory Board (SSB). The SSB usually comprises of three members. However, the terms of reference of the SSB in the form of the process of appointment, termination, and composition tend to differ among Islamic banks. The rulings issued by different SSBs with regard to similar transactions may also be inconsistent, resulting in these transactions not being comparable in terms of their basis in Shariah. The resulting proliferation of different variants of such transactions increases transaction costs for Islamic banks and their customers, and this is likely to have hindered the growth of the industry.

These differences in Shariah rulings by SSBs have concerned not only similar transactions across different jurisdictions but also those within the same jurisdiction. In the early years of Islamic banks, their boards of directors were the ones to set the terms of reference of the SSBs; however this has changed in a number of jurisdictions where it is now regulated by the central bank or another central authority, although to varying degrees depending on the legal frameworks that govern the operations of Islamic banks.

ROLE OF ACCOUNTING & AUDITING ORGANIZATION FOR ISLAMIC FINANCIAL INSTITUTIONS (AAOIFI)

The initial thought behind the establishment of the Shariah Board of AAOIFI was to provide a degree of harmonization to its accounting standards, which was its initial mandate. However, the need to harmonize the differing Shariah rulings of Islamic banks has become more pertinent, becoming the main objective of the AAOIFI Shariah Board.

The AAOIFI Shariah Board therefore adopted a due diligence process similar to that of the AAOIFI Accounting Board for the issuance of Shariah standards. This includes issuing an exposure draft of the standard and holding of a public hearing, allowing the public to inquire about aspects of the standard. This was a major development as almost no Shariah scholars were used to the process. Furthermore, the standards included a section on the “Basis of Standard” to enable users of the standards to ascertain the basis on which the Board had arrived at the content of its standards.

It is worth noting that the standards were issued without any dissent or minority opinion being published, so as not to confuse the public, given the prominence of the Shariah scholars who sat on the inaugural AAOIFI Shariah Board. In addition, the standards were not considered *fatawa* (Islamic legal edicts) so as not to be attributed to any particular member of the Shariah Board, but rather as a collective ruling of the Board.