

## **SHARIA GOVERNANCE OF ISLAMIC FINANCIAL INSTITUTIONS: A COMPARATIVE STUDY AMONG MALAYSIA, BAHRAIN AND SRI LANKA**

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### **ABSTRACT**

*Islamic finance industry has been widely developing not only in Muslim countries such as Malaysia and Bahrain but also in non- Muslim countries such as Sri Lanka. At the same time, the Shari'ah governance is one of major requirements for Islamic financial institutions to be recognised by the Shariah and the Muslim customers. As such, the Shari'ah governance plays a significant role in the industry to ensure that it meets the objective for the establishment of the Islamic financial institutions. Thus, the purpose of this paper is to investigate the level of Shari'ah governance of Islamic financial institutions in Sri Lanka, Malaysia and Bahrain. Hence, this is a comparative study among three countries. The research paper adopts a qualitative method and content analysis in order to accomplish the objective of the study. The data for the study is based on the primary and secondary sources that could be collected from Parliamentary Acts, books, articles, magazines, online materials and annual report of Islamic financial institutions available in the above three countries. The findings of the study are expected to be greatly useful for the Islamic financial institutions in Sri Lanka and similar countries where there is no proper legislation on Shariah governance.*

**Keywords:** Shari'ah governance, Islamic finance industry, legislation, Shariah-compliance

### **1. INTRODUCTION**

Islamic financial institutions have the duty to ensure the compliance with Shariah principles in all aspects of their products, instruments, operations, practices and management which will be achieved by the establishment of a proper Shariah governance framework. Thus Shariah supervision plays an

essential role in the governance of Islamic financial institution and forms part of the principal component of the Shariah governance framework.<sup>1</sup>

The Islamic Finance Services Board (IFSB) defines the *Shari'ah governance* system as “a set of institutional and organizational arrangements through which Islamic financial institutions ensure that there is effective independent oversight of *Shari'ah* compliance over the issuance of relevant *Shari'ah* pronouncements, dissemination of information and an internal *Shari'ah* compliance review.”<sup>2</sup>

The Shariah governance which refers to all the elements about the active role of the Shariah board and compliance with Shariah is fundamental to Islamic banks in particular and the implementation of Shariah governance is encouraged by international institutions of regulations like Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI) and IFSB.<sup>3</sup>

This research paper critically evaluates Shari'ah governance in Islamic financial institutions in three different countries, Malaysia, Bahrain and Sri Lanka. Malaysia aspires to transform the country into becoming an Islamic banking and finance hub and one of the efforts is strengthening the Shariah governance in the Islamic finance sector.<sup>4</sup>

*Shariah* governance for Islamic Financial Institutions (IFIs) in Malaysia is governed by the *Shariah* Governance Framework for the IFIs 2010 (SGF 2010) that was developed and introduced by Central Bank of Malaysia (BNM)<sup>5</sup>

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<sup>1</sup> Hamza, H. (2013). Sharia governance in Islamic banks: Effectiveness and supervision model, International Journal of Islamic and Middle Eastern Finance and Management, Vol. 6 No 3, 226-237.

<sup>2</sup> Hasan, Z., Islamic science university of Malaysia (university sins Malaysia).

<sup>3</sup> Hamza, H. (2013). Sharia governance in Islamic banks: Effectiveness and supervision model, International Journal of Islamic and Middle Eastern Finance and Management, Vol. 6 No 3, 226-237.

<sup>4</sup> Zulkifli Hasan (n.p), Faculty of Shariah and Law Islamic Science, University of Malaysia, page no:1

<sup>5</sup> Othman, A., Hassan R., Omar MN, Napiah D.M., Ariffin1, M., Yusoff A, Nuraini khatimin & Azami zaharim, (n.p). *Shariah* Governance for Islamic Financial Institutions in Malaysia on the Independency of *Shariah* Committee and Efficiency of Its *Shariah* Decisions, P.1.

According to Bahrain, the Central Bank of Bahrain (CBB) Rule Book Volume 2, Islamic banks, Part A, High Level Control, section 1.3.15 provides that the CBB requires all banks to establish an independent *Shari'ah* board complying with AAOIFI's Shariah Standards for IFIS No. 1 and No.2..<sup>6</sup>

In Sri Lanka unlike Malaysia and Bahrain the Sharia governance is regulated by the Shariah boards established voluntarily by the IFIs. The Shariah is based on primary sources of Islam that will be implemented by way of Shariah boards.<sup>7</sup>

## 2. OBJECTIVES OF THE STUDY

To investigate the level of compliance with Shariah governance of Islamic financial institutions in Malaysia, Bahrain and Sri Lanka and suggest necessary changes to Sri Lankan regulatory authority for adoption of best practices followed by Islamic financial institutions in Malaysia and Bahrain which are pioneers in Islamic finance industry.

## 3. LITERATURE REVIEW

### THE DEVELOPMENT OF SHARIAH GOVERNANCE IN ISLAMIC FINANCIAL INSTITUTION

According to Zulkifli Hasan, Dynamic and good Shariah governance is very important. The ultimate purpose of the establishment of the SC in Islamic financial institutions is to ensure Shariah compliance with its operations and products. All banks and Takaful operators must have provision regarding the establishment of the SC in their Articles of Association and Memorandum of Association.

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<sup>6</sup> Zulkifli Hasan\*(n.p),Regulatory Framework of *Shari'ah* Governance System in Malaysia, GCC Countries and the UK,. Kyoto Bulletin of Islamic Area Studies, 3-2 (March 2010).Pp-89-91.

<sup>7</sup> Nafees S.M. And Habeebullah M.T(2016), Enhancement Of Islamic Banking Industry: A Sri Lankan Perspective. International Conference Proceeding 2016 organised by the Faculty of Islamic Studies and Arabic language, South Eastern University of Sri Lanka, PP-1-4.

The term Shariah Committee or Shariah Advisory Body or Shariah Advisory Council has been used interchangeably for the past 21 years. The term Shariah Committee has been introduced by Central Bank of Malaysia (CBM) in section 3 of the Guidelines and Procedures for Shariah Committee (BNM/GPS1) issued in December 2004. With the issuance of these Guidelines and Procedures, all Shariah Advisory Council of Islamic financial institutions and Takaful operators will be recognized as Shariah Committee and the term National Shariah Advisory Council (hereinafter referred to as “the SAC”) will be used by CBM.

Ahmad Ibrahim 1997 said that the first Shariah Committee was set up in 1983 by Bank Islam Malaysia Berhad (BIMB). BIMB started its operations as Malaysia’s first Islamic bank on 1st July 1983, set up with an initial authorized capital of RM600 million and a paid-up capital of RM 79.9 million. The bank has gradually increased its authorized and paid-up capital to RM 2 billion and RM 563 million respectively, to accommodate the growth of its assets and to better position itself in meeting future expansion and growth. With that policy, many conventional banks set up their Islamic windows and at the same time they appointed selected Muslim scholars to be members of Shariah Committee. (<http://www.bankislam.biz>).

Nik Norzrul Thani (2001) refers on 1st October 1999, a second Islamic bank, namely Bank Muamalat Malaysia Berhad (BMMB) commenced operations. The establishment of BMMB was the effect of the spin-off following the merger between Bank Bumiputra Malaysia Berhad (BBMB) and Bank of Commerce (Malaysia) Berhad. As part of the effort to streamline and harmonize the Shariah interpretations among banks and Takaful companies, National Shariah Advisory Council of CBM was established on 1st May 1997 under BAFIA 1984. This Council is the highest Shariah authority on Islamic banking and Takaful in Malaysia (<http://www.bnm.gov.my>).

It is important to note that the SC’s duties and responsibilities with other *fatwa* institution such as the National Fatwa Committee and the State Fatwa

Committee differ in several aspects. In selecting the subject matter of *fatwa*, the latter is subject to three occurrences for example in section 34 of the Administration of Islamic Law (Federal Territories) Act 1993 provided that *fatwa* will be issued if it is ordered by the Yang Dipertuan Agong (YDPA) or if it is upon the request of the general public or on accord of the Mufti himself. The scope of *fatwa* is general and wide and limited to the inquiries of the ruler or the public. Furthermore, any *fatwa* issued will only bind the state if it is gazzeted.

The SC on the other hand has a rather active approach in selecting the subject matter of any issue and its decision will be considered as the SC resolution rather than naming it as a *fatwa*. The SC has to scrutinize the *Shariah* principles, evaluating product features and in many instances they have to suggest for alternatives. The nature of studying and analyzing the fiqh in the Islamic finance industry is also technical, complicated and in depth. In addition, the SC will only issue resolution based on the inquiries and needs of its respective Islamic financial institutions and not from the public at large.

As a conclusion therefore, effective *Shariah* 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 and lawyers.

The SC plays very important role in ensuring good *Shariah* governance. The role of the SC is to include advising board of directors on *Shariah* matters to ensure that the operations comply with *Shariah* principles at all time, endorsing and validating relevant documentations pertaining to the products and services, as well as the internal policies and manuals and marketing advertisements, assisting related parties, advising on any *Shariah* matters arising before referring the same to the SAC, assisting the SAC on reference for advice and ensuring all its decisions are properly implemented.

The recent development on setting up a special High Court in the Commercial Division or the Muamalah bench and also the amendment of section 16B of the CBA 2003 shows positive indication by the government in providing more comprehensive and effective Shariah governance in Islamic finance sector. The Muamalat bench in the High Court provides special focus by the respective judges on the disputes on Islamic finance and it also can be considered as an approach of harmonizing the civil and Islamic law in Malaysia. Shariah governance is unique to Islamic system of financial management. It can be considered as vital corporate governance for Islamic financial institutions. Good Shariah governance assures a tremendous growth of the Islamic banking and finance industry.

According to HMA. Hilmy & SMM, Mazahir, Today Islamic banks are operating in nearly all Muslim countries and many non-Muslim countries since 1970s. Unlike conventional banking industry, Islamic banking industry provides only the *halal* financial services for their customers because of its Shari'ah *compliant* system.

Therefore, the *Shari'ah governance* is the essence and vehicle for a comprehensive regulatory and supervisory infrastructure of Islamic banking system and it is the key feature of Islamic banking industry which distinguishes it from the conventional financial system. The overall compliance of Islamic banking and financial business is solely depending on the adequacy and efficiency of the Shari'ah governance.

To ensure that Islamic banking system is complying with the religious requirements, it is required to utilize the service of *Shari'ah* supervisory board (SSB). These SSB consist of number of *Shari'ah* scholars who Conduct internal religious audit in Islamic financial Institutions and are required to approve the *Shari'ah Compliance* of new financial products before they are launched commercially.

## 4. METHODOLOGY

The research will be exploratory study in selected countries using Case Study approach. Due to the wide scope of study mostly secondary sources of data will be used. Besides, conventional secondary data sources, various database and analytical tools used for data collection. To analyze the data, we were critically evaluating the sharia governance of Islamic financial institutions in three Islamic countries by applying content analysis technique.

### 4.1 RESEARCH QUESTION

- How to improve sharia governance of Islamic financial institutions in Sri Lanka?
- Why sharia governance is essential for Islamic finance?
- How to operate sharia governance in Islamic financial institution in Sri Lanka as like Malaysia and Bahrain

## 5. RESULT AND DISCUSSION

Shari'ah governance system as defined by The IFSB Guiding Principles on *Shari'ah* Governance System in Institutions Offering Islamic Financial Services (IFSB-10) refers to a set of institutional and organizational arrangements to oversee *Shari'ah* compliance aspects in Islamic Financial Institutions (IFIs). In this regard, majority of IFIs have established their own *Shari'ah* board and some of them even have set up a dedicated internal *Shari'ah* review unit or department to support *Shari'ah* board in performing its function. This indicates a positive development on the aspect of *Shari'ah* governance system in IFIs. Looking at the different framework and style of *Shari'ah* governance in various legal environment and diverse banking models, it is worth examining the regulatory framework of *Shari'ah* governance system in different jurisdictions. As such the Shariah governance of Islamic financial institutions in Malaysia, Bahrain and Sri Lanka is discussed.

### Malaysia

Malaysia has a very unique legislative framework consisting of mixed jurisdictions and mixed legal systems namely common law and *Shari'ah*. The common law principles are applied in the civil court in almost matter of jurisdiction.

The BNM has issued the BNM/GPS 1 that regulates the governance of SC of Islamic financial institution. Apart from that, the BNM has also issued the Guidelines on the Disclosure of Reports and Financial Statements of Islamic Banks known as BNM/GPS8-i. The BNM/GPS1 consists of 10 parts with 24 sections and one appendix. The contents include objectives, scope of application, establishment of the SC, membership, restrictions, duties and responsibilities of the SC and Islamic financial institutions, reporting structure, effective date and secretariat of the SAC.

The objective of BNM/GPS 1 is to set out the rules, regulations and procedures in the establishment of the SC to define the role, scope of duties and responsibilities of the SC and to define relationship and working arrangement between the SC and the SAC (Section 5). The BNM/GPS1 shall only be applicable to a licensed Islamic bank which participates in the Islamic Banking Scheme, a development financial institution prescribed under the DFIA which carries on Islamic Banking Scheme; and a Takaful operator registered under the Takaful Act 1984 (Section 6). The Board of Directors (BOD) shall appoint the members of the SC and the tenure shall be valid for a renewable term of two years but subject to the approval of the BNM (Section 8). The member of the SC shall at least either have qualification or possess necessary knowledge, expertise or experience in Islamic jurisprudence or Islamic law of transaction (Section 11). With purpose of mitigating the risk of potential of conflict of interest and confidentiality issues, IFIS are not allowed to appoint any member of the SC in another IFI of the same industry (Section 19).

To ensure that the SC would be able to function effectively, the SC shall at least consisting of a minimum three members in which will be coordination by the *Shari'ah* secretariat of the respective IFIS (Section 15). The SC members may be disqualified if he fails to meet the requirements or breach of corporate governance such as he has acted in a manner which may cast doubt on his fitness to hold the position, has been failed to attend 75 percent of meetings in a year without reasonable excuse, has been declared a bankrupt, or a petition under bankruptcy laws is filed against him, was found guilty for any serious criminal offence, or any other offence punishable with imprisonment of one year or more, or subject to any order of detention, supervision, restricted residence or banishment (Section 16).



As regard to roles and responsibilities, section 20 provides clear duties and responsibilities of the SC and it includes *inter alia* to advise the BOD on *Shari'ah* matters in its business operation, to endorse *Shari'ah* Compliance Manuals, to endorse and validate relevant documentations, to assist related parties on *Shari'ah* matters for advice upon request, to advise on matters to be referred to the SAC, to provide written *Shari'ah* opinion and to assist the SAC on reference for advice. Besides, the IFIs must assist the SC as well as possible in providing sufficient relevant information and these include referring all *Shari'ah* issues to the SC, to adopt the SC's advice, to ensure that product documents be validated, to have a *Shari'ah* Compliance Manual, to provide access to relevant documents, to provide sufficient resources and to remunerate the members of the SC accordingly (Section 21).

The SC is legally required to produce a *Shari'ah* report expressing their observation on IFIs' compliance with *Shari'ah* principles. In this aspect, the Guidelines on Financial Reporting for Licensed Islamic Banks (BNM/GP8-i) specifies minimum requirement of the *Shari'ah* report. The BNM/GP8-i requires content of the *Shari'ah* report to be at least declaration of *Shari'ah* compliance endorsed by the *Shari'ah* committee members. In term of the reporting structure, the SC will report functionally to the BOD as this reflects the status of the SC as an independent body of the IFIs. The BOD is bound by any decision of the SC and they have to consider the SC's views on certain issue related with operational matters, policy or business transactions.

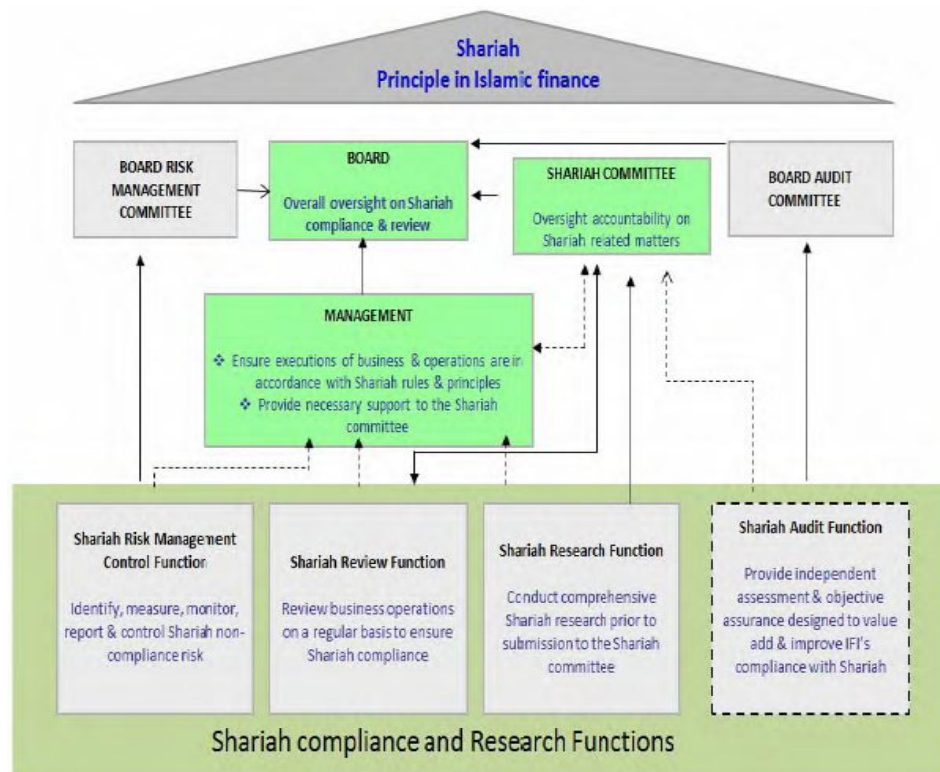
The amendment to the Central Bank of Malaysia Act 1958 in 2003 enhances the role of the SAC. Now, the SAC is accorded to be the sole authoritative body on *Shari'ah* matters pertaining to Islamic finance. The amendment provides that the BNM may establish an advisory council which shall be the authority for the ascertainment of Islamic law for the purposes of Islamic banking business, *Takaful* business, Islamic financial business, Islamic development financial business, or any other business which is based on principles and is supervised and regulated by the BNM. The decision made by the SAC nevertheless is only binding upon the arbitration and not the court.

Due to several controversial court cases involving IFIs, with the initiative of the BNM, the CBA was passed in July 2009. Chapter VII sections 51-58 specifies the

*Shari'ah* governance framework of the SAC. This new Act confirms the status of the SAC as the highest authority in matters pertaining to Islamic banking, finance and *Takaful*. In addition, it clarifies the position of *Shari'ah* pronouncement and the SAC's deliberation to be binding upon the court as well as arbitration. To demonstrate the significance of the SAC's authority, the appointment of the SAC members then will be made by the Yang Di Pertuan Agong or the King of Malaysia with the advice of finance minister. This important amendment finally clarifies the status of the *Shari'ah* ruling to have binding force upon Islamic banking, finance and *Takaful* matters.

Despite of the recent legal development, it is worth noting that the CBA has jurisdiction to only in matters fall under the auspices of the BNM, so as to exclude the *Shari'ah* board in the Securities Commission. In August 2009, the Securities Commission of Malaysia issued the Registration of *Shari'ah* Advisers Guidelines under section 377 of the Capital Markets and Services Act 2007. This Guideline specifically provides rules and procedures for registration of *Shari'ah* advisers in matters regulated and supervised by the Securities Commission (SC, 2009).

BNM Shariah Governance Framework (2011) proposed the model of Shariah governance framework for IFIs operating in Malaysia



The Acts are following: Which are the central bank of Malaysia act 2009 and the Islamic financial service act 2013.

### **The Central Bank of Malaysia Act 2009 (Act 701)**

The Act was passed to provide for the continued existence of the Central Bank of Malaysia and for the administration, objects, functions and powers of the Bank, for consequential or incidental matters. The most significant provision of the newly passed legislation is Part VII under the heading "Islamic financial business". Part VII is divided into 2 chapters i.e. Chapter 1 Shariah Advisory Council (Section 51 to 58) and Chapter 2 (Section 59 -60) Powers of the Bank. Part VII directly provides for the Islamic financial business which is defined under section 2 as any financial business in Ringgit or other currency which is subject to the laws enforced by the Bank and consistent with the Shariah.

### **The Islamic Financial Services Act 2013**

The rule relating to Shariah governance is provided under section 30 until section 36 of IFSA 2013 whereby the existence of these provisions highlighted the intention of the law maker, in focusing to the matters pertaining to appointment and qualification of the Shariah committee's members in Islamic financial institution. Unlike the central bank of Malaysia Act 2009 which merely touched the surface of the matter by highlighting the general requirement for financial institution to have a Shariah committee, the current provision provides a more specific requirement under section 30 of IFSA 2013 which requires an institution to apply directly to the central bank for the establishment of Shariah committee. This will enable the Central Bank to have direct information as to the members of the Shariah committee in an Islamic financial institution, which at the same time, to ensure a proper supervision towards the activities conducted.

Another major point being made available under the new Shariah governance legal provision is the criteria of the members of Shariah committee. A clear standard of requirement pertaining to the appointment of such committee is highlighted under section 31 which is to be crossed referred with section 29 (2) (a) which states only those who is really fit and qualified may be appointed as the Shariah committee members. This leads to the notion that members of Shariah committees in every

financial institution must be chaired by those who met the requirements as stated by the Central Bank. Availability of such clause would be vital in ensuring the products and services introduced by the Islamic financial institution complied with the Shariah principles via the supervision of competent members.

Section 32 of IFSA 2013 contributes to the significance of Shariah committees in every institution through the introduction of the Shariah governance which not only set out the duties of the Shariah committees in the institution, but rather blends into the structure of the company itself. By extending the powers of Shariah governance into certain aspects in a company such as matters involving the board of directors and internal Shariah compliance, one can understand that Shariah governance would be one of the integral parts in an institution up to the point that Shariah committee may no longer be treated as a minor part or division of a company.

### **Bahrain**

Al-Suwaidi, 1993 said that, Bahrain was exposed to the English system more as compared to other GCC countries. However, after independence in 1971, Bahrain has developed several substantive and procedural laws and at the same time put *Shari'ah* as a main source of legislation as stated in the Article 2 of the Constitution of Bahrain. This position creates difficulties for commercial sectors particularly financial institutions because the interest-based transactions would have been declared illegal. In view of this, Bahrain developed its own laws such as the Law of Civil and Commercial Procedure of 1971, the Law on the Establishment of the Bahrain Monetary Agency of 1973, the Companies Registration Act of 1983 and the Commercial Law of 1987 which are based mainly on the Egyptian code. Article 76 of the Commercial Law of 1987 clearly allows interest charges in commercial loan but subject to the rate determined by the Bahrain Monetary Agency. As such, the Civil Court of Bahrain has comprehensive jurisdiction over civil and commercial matters except those relating to *Shari'ah* disputes.

Hasan, A., 2007 refers that, The CBB Rule Book Volume 2, Islamic Banks, Part A, High Level Control, section 1.3.15 provides that the CBB requires all banks to establish an independent *Shari'ah* board complying with AAOIFI's governance standards for IFIs No. 1 and No.2. This section provides with a clear legal requirement for the establishment of the *Shari'ah* board in IFIs in Bahrain in which failure to do that will constitute non-compliance with the CBB's directive. Unlike the other GCC countries, Bahrain has established National *Shari'ah* Advisory Board of

the CBB with purpose to serve and to verify the *Shari'ah* compliance. *Shari'ah* board of the CBB nevertheless is different with the other national *Shari'ah* board as in the case of Malaysia, Sudan, Indonesia, Pakistan and Brunei as it does not have authority upon the other IFIs. As regard to the *Shari'ah* governance system, Bahrain follows the AAOIFI governance standards where it requires all IFIs to establish *Shari'ah* Supervisory board. Section 1.3.16 of the CBB Rule Book requires IFIs to adopt the standards as well as having a separate function of *Shari'ah* review for a purpose of ensuring *Shari'ah* compliance as stipulated in the standards No.3. To address this issue, the practice of the IFIs shows that the *Shari'ah* review or audit is carried out by the existing internal audit personnel. This legal requirement for the adoption of the standards reflects the role of Bahrain as the host of the AAOIFI since its establishment in 2001.<sup>8</sup>

### **Sri Lanka**

The Islamic banking industry is regulated by the Shariah and positive laws. The Shariah is based on primary sources of Islam that will be implemented by way of Shariah boards whereas positive law is promulgated by the Central Bank of Sri Lanka to safeguard public interest. In this sense, Banking Act No.30 of 1988 and the Banking (amendment) Act No. 2 of 2005 play an important role in regulating the Islamic banking industry.

The All Ceylon Jammiyyathul Ulama (ACJU) plays a significant role in mitigating the shortcoming of the legislation on Shariah governance (Mubarak, 2009). It is a non-governmental organization that was established in 1924 has been incorporated under the Act No. 51 of 2000 of Parliament of Sri Lanka. It is not a statutory body whose ruling is not considered legally binding. It has several divisions for different issues including a division for Islamic banking and finance. This service is voluntarily rendered by the ACJU in the interest of Muslim community in Sri Lanka. Although it is not mandatory for IBIs to comply with its ruling, they follow it in general for the purpose of convincing customers. Meanwhile, it is to be noted that Amāna Bank is a member of AAOIFI and it complies with its ruling in terms of Shariah compliance. However, it is suggested for IBIs to adopt voluntarily its ruling in order to constitute a consistency in the application of Shariah principles governing Islamic banking. Nevertheless, Shariah governance must be legislated in due course for the

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<sup>8</sup> Zulkifli Hasan\*(n.p),Regulatory Framework of *Shari'ah* Governance System in Malaysia, GCC Countries and the UK., Kyoto Bulletin of Islamic Area Studies, 3-2 (March 2010),PP.89-91

sustainability of the industry. In some countries, the role of the Shariah has been recognized significantly. Malaysia is a good example and it has done a commendable job with regard to the regulation of the Islamic banking industry pertaining to the role of the Shariah. Accordingly, all Islamic banking institutions are bound to appoint Shariah advisory boards that would consult the Shariah Advisory Council (SAC) in the case of conflict of opinion. The SAC has been set up under the Central Bank of Malaysia. The courts and arbitral tribunals are instructed to consult the SAC whose opinion is binding on them (see sections 27-38 of the Islamic Financial Services Act 2013 of Malaysia).<sup>9</sup>

## 5. RECOMMENDATION

- The Islamic financial institutions which are operating their services in Sri Lanka may follow proper sharia governance in all their activities.
- All Islamic financial institutions should have proper sharia boards in all their branches and these sharia boards should be regulated by the main sharia board. So, all Islamic financial institutions which are in Sri Lanka, they have to build up main sharia board to deal with their every financial activity.
- Every Islamic financial institution should provide proper sharia knowledge to all their employees as they are lack of sharia knowledge.

## 6. CONCLUSION

Based on the foregoing discussion, it is concluded that there is good sharia governance in Malaysia and Bahrain. In this sense, Malaysia is a good example and it has done a commendable job with regard to the regulation of the Islamic banking industry pertaining to the role of the Shariah governance. Accordingly, all Islamic banking institutions are bound to appoint Shariah advisory boards that would consult the Shariah Advisory Council (SAC) in the case of conflict of opinion. The SAC has been set up under the Central Bank of Malaysia.

In case of Bahrain, the CBB requires all banks to establish an independent *Shari'ah* board complying with AAOIFI's Shariah standards for IFIs No. 1 and No.2. This section provides a clear legal requirement for the establishment of the *Shari'ah*

<sup>9</sup> Nafees S.M. And Habeebullah M.T.(2016)., Enhancement Of Islamic Banking Industry: A Sri Lankan Perspective. International Conference Proceeding 2016 organised by Faculty of Islamic Studies and Arabic language, South Eastern University of Sri Lanka.

board in IFIs in Bahrain in which failure to do that will constitute non-compliance with the CBB's directive. Unlike the other gulf co-operation countries (CGG), Bahrain has established National *Shari'ah* Advisory Board of the CBB with purpose to serve and to verify the *Shari'ah* compliance.

As noted earlier, in Sri Lanka there isn't proper sharia governance in all Islamic financial institutions. Amana is only the full fledged Islamic bank that is concerned about the good sharia governance. When a comparison is made among Malaysia, Bahrain and Sri Lanka one may find that there is a big gap with regard to Sharia governance.

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