

ANALYSIS ON THE PROVISION OF LEGAL REQUIREMENT FOR THE ESTABLISHMENT OF THE *SHARĪAH* COMMITTEE OF ISLAMIC BANKS IN MALAYSIA

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ABSTRACT

The formation of the Sharīah committee in the Islamic banks is crucial in ensuring the Islamic banking business carried out by the Islamic banks comply with Sharīah principles. In Malaysia, the setting up of this committee is a statutory requirement to be observed by Islamic banks. By using legal research methodology, this study seeks to analyse the provision of legal requirement for the establishment of Sharīah committee of Islamic banks in Malaysia. By employing analytical and critical analysis on the relevant legal provision, this study found that, the provision of law is significant which requires the Islamic banking institutions and participating banking institutions offering Islamic banking schemes to establish Sharīah committee in order to ensure the Sharīah compliance in relation to Islamic banking business. However, several legal issues pursuant to the general nature of the respective legal provision need to be attended by the relevant authority. These include the definition, the terminology used and the composition of the Sharīah committee as well as its position in the Islamic banks' organisation structure.

Keywords: Islamic Bank; Islamic Finance; *Sharīah* Committee; *Sharīah* Advisory; *Sharīah* Governance.

Introduction

Since 1983, the implementation of Islamic banking business under the surveillance of Central Bank of Malaysia (hereinafter referred to as 'CBM') is regulated by several statutes passed by the Parliament of Malaysia and the guidelines issued by CBM. Such statutes and guidelines also have provisions which governing the *Sharīah* committee of Islamic banks. At the initial stage, the establishment of the *Sharīah* committee in Malaysia was

a statutory requirement as enshrined in Islamic Banking Act 1983 (Act 273) ([1] which required the Islamic banks to establish their own *Shari'ah* committee.

The statutory requirement for the establishment of the *Shari'ah* committee as stated under IBA 1983 has demonstrated to be effective in governing Islamic banking business in terms of *Shari'ah* adherence as well as standardization[2]. The creation of this committee is varied from one county to another and for some countries, the setting up of such advisory body is considered not obligatory [3]. However, the establishment of the *Shari'ah* committee of financial institutions could provoke certain legal problems [4].

The *Shari'ah* committee is an independent body of dedicated scholars in *al-mu'āmalāt* (Islamic transaction/commercial law) that is entrusted with the responsibility of supervising, directing and revising the business activities of the institutions in order to guarantee that they are conforming with Islamic principles [5]. In relation to the composition, *Shari'ah* committee must consist of Muslim jurists [6] and who exert influence on the running of Islamic banking business of an Islamic bank [7]. Previously, this committee consisted of *Shari'ah* scholars, some of whom had slight information of contemporary banking and who often could not comprehend the language in which transactions were documented. Such problems could be a remarkable handicap to the development of Islamic finance transaction and the growth of new Islamic finance products [8]. Ideally, a *Shari'ah* committee would be constituted of a group of scholars and experts in *Fiqh* (science of Islamic law), banking, economics, accounting and finance [7].

Hence, this study is meaningful and may contribute to the existing literature related to Islamic banking particularly pertaining to the legal aspects of the establishment of *Shari'ah* committee of Islamic banks as has been stipulated by the law in Malaysia.

Legislations Governing the *Shari'ah* Committee of Islamic Banks

In this country, the *Shari'ah* committee of Islamic banks are subject to the legal framework as set out by the laws regulating Islamic banking business since 1983. Over 30 years, enhancements have been made by the authority to reinforce such legal structure via a series of amendments and introducing of new legislations. Apart from that, the legal framework of the *Shari'ah* committee is also pursuant to the guidelines issued by the CBM to govern the Islamic banking business.

During 1983 to 2004, this committee was regulated by IBA 1983 where the regulatory framework existed in the general manner. Islamic banks were required by IBA 1983 to form their own *Shari'ah* committee. Furthermore, the institutions were required to incorporate extra clause for the formation of the *Shari'ah* committee in their Article of Association (hereinafter referred to as 'AoA'). Likewise, the IBA 1983 in a general manner spelled out the function of the *Shari'ah* committee as to advise the Islamic banks regarding the Islamic financial business (IBA 1983, s.3(5)(b))[9].

As a result of the general nature of the legal provisions, matters concerning to the appointment of the *Shari'ah* committee members and its procedures, the number of membership, the qualification and the composition of the committee were subject to the decision of the institutions. The same concerning the responsibilities and duties of the committee. With the amendment of IBA 1983 in year 2003, the regulatory framework has been upgraded. Based on the amendments, the establishment of the *Shari'ah* committee of the Islamic banks shall be approved by CBM (Islamic Banking (Amendment) Act 2003 (Act A1214), s.2). Accordingly, CBM has the final say in this regard.

One thing should be pointed out that, during the period of 1983 to 2013, only IBA 1983 has provision dealing with the *Shari'ah* committee for Islamic banking institutions. No such provision stipulated under Banking and Financial Institutions Act 1989 (Act 372) [10] and Development Financial Institutions Act 2002 (Act 618) (hereinafter referred to as

'DFIA 2002'). Even though both statutes allowed the banking institutions licensed under them to offer Islamic banking facilities. Nevertheless, this is no longer question, since those IBA 1983 is repealed by Islamic Financial Services Act 2013 (Act 759) [10] and BAFIA 1989 is repealed by Financial Services Act 2013 (Act 758) [11][12].

In a nutshell, IFSA 2013 has better legal provisions in administering the matters of the *Shari'ah* committee in contrast to the repealed statute. Meanwhile, FSA 2013 requires participating financial institutions offering Islamic financial facilities to observe the provisions of IFSA 2013 including the requirements pertaining to the formation of *Shari'ah* committee as well as the matters related to it.

Apart from statutes, the *Shari'ah* committee have been regulated by a number of Guidelines issued by CBM. In December 2004, CBM has issued BNM/GPS 1 which shed light on three (3) substantial elements relating to the *Shari'ah* committee as including: (a) the rules, regulations and procedures in the establishment of the committee; (b) the role, scope of duties and responsibilities of the committee; and (c) the relationship and working arrangement between the committee and the *Shari'ah* Advisory Council of CBM.

However, effectively from 1st January 2011, BNM/GPS 1 is replaced with the introduction of *Shari'ah* Governance Framework for Islamic Financial Institutions (BNM/RH/GL 012-3) (hereinafter referred to as 'SGF 2010') [13]. The issuance of SGF 2010 with the following objectives:

(a) Sets out the expectations of the CBM on an Islamic financial institution's *Shari'ah* governance structures, processes and arrangements to ensure that all its operations and business activities are in accordance with *Shari'ah*;

(b) Provides a comprehensive guidance to the board, *Shari'ah* committee and management of the Islamic financial institutions in discharging its duties in matters relating to *Shari'ah*; and

(c) Outlines the functions relating to *Shari'ah* review, *Shari'ah* audit, *Shari'ah* risk management and *Shari'ah* research.

Beginning 1st April 2020, there is new guideline namely *Shari'ah* Governance 2020 issued by CBM to regulate the Islamic financial institutions in Malaysia. Such policy is issued pursuant to s.29(2), 57(2) and 155 of IFSA 2013 and also pursuant to s.33E(2), 41 and 116 of DFIA 2002. This policy document supersedes the SGF 2010

Legal Basis for the Establishment of the Shari'ah Committee

The establishment of the *Shari'ah* committee in Malaysia is a legal requirement since 1983. Islamic banks regulated and supervised by CBM are required to set up their own *Shari'ah* committee to provide advice on *Shari'ah* matters pertaining to Islamic financial business. Prior to the implementation of IFSA 2013 and FSA 2013, the establishment of *Shari'ah* committee of the Islamic banks was pursuant to the legal requirement of IBA 1983 and other Guidelines issued by CBM.

Effectively on 30th June 2013, the establishment of *Shari'ah* committee is pursuant to a provision of IFSA 2013 which provides that:

(1) A licensed person shall establish a *Shari'ah* committee for purposes of advising the licensed person in ensuring its business, affairs and activities comply with *Shari'ah*.

(2) For the purposes of subsection (1), where there is more than one licensed person within a financial group, one of the licensed persons may apply to the Bank for the establishment of a single *Shari'ah* committee within the financial group and the Bank may approve the application in writing if the Bank is satisfied that the *Shari'ah* committee so established is capable of ensuring compliance with *Shari'ah* by all licensed persons within the financial group.

(3) The Bank may require an approved person or operator of a designated payment system to establish a *Shari'ah* committee for purposes of advising the approved person or operator of a designated payment system in ensuring their business, affairs and activities comply with *Shari'ah*.

The above subsection 30(1) explicitly requires a licensed person licensed under section 10 of IFSA 2013 to establish the *Shari'ah* committee. Such licensed person including licensed Islamic bank, licensed international Islamic bank, licensed *takāful* operator and licensed international *takāful* operator¹ are required to establish the *Shari'ah* committee to advise the licensed person in confirming its business, affairs and activities comply with *Shari'ah*.

In the case of more than one licensed person within a financial group, IFSA 2013 permits one of the licensed persons to apply in writing to the CBM for the establishment of a single *Shari'ah* committee to serve within the financial group. In this regard, CBM may approve the application provided that such single *Shari'ah* committee is capable to monitor *Shari'ah* compliance for the entire licensed persons within the financial group.

Apart from the above, for the purpose of the monitoring *Shari'ah* compliance, Central Bank of Malaysia may require an approved Islamic financial adviser, approved issuer of a designated Islamic payment instrument, approved operator of a payment system and approved *takāful* broker to establish a *Shari'ah* committee to give advice to such person pertaining to *Shari'ah* matters. This indicates that not only Islamic banks and *takāful* operators must establish *Shari'ah* committee. In fact it is extended to any person approved by [14] to conduct Islamic financial business subject to the discretion of Central Bank of Malaysia.

Meanwhile, authorized persons and operators of designated payment system governed by FSA 2013 and permitted to carry out Islamic financial business are required to observe the provisions of IFSA as well [14]. This includes the requirement to establish a *Shari'ah* committee pursuant to section 30 of [14]. Hence, a licensed bank, licensed investment bank, an approved person or operator of designated payment system carrying on Islamic financial business shall establish the *Shari'ah* committee respectively.

Similarly CBM may requires an approved insurance broker carrying on *takāful* broking business, an approved financial adviser carrying on Islamic financial advisory business, an operator of a designated payment system or approved operator of a payment system involved in Islamic financial business or an approved issuer of a designated payment instrument involved in issuing a designated Islamic payment instrument pursuant to subsection 30(3) of IFSA to set up a *Shari'ah* committee. In addition, the director of a licensed bank, licensed investment bank, an approved person or operator of designated payment system Islamic shall always have due regard to the advice of its *Shari'ah* committee pertaining to Islamic financial business carried out by such institutions [14].

By putting IFSA 2013 as the legal basis for the establishment of the *Shari'ah* committee, it has standardized the legal requirement to establish the *Shari'ah* committee which should be complied by a licensed person and approved person to offer Islamic financial facilities even if such persons are licensed and regulated by FSA 2013. Previously, inconsistency of statutory requirements occurred when only IBA 1983 required Islamic banks to establish the *Shari'ah* committee. However, no such provision is found in BAFIA 1989 and DFIA 2002.

Inconsistency also occurred when IBA required Islamic banks to incorporate additional clause for the formation of the *Shari'ah* committee in the AoA of the respective institutions. Unlike participating institutions in Islamic Banking Scheme (hereinafter referred to as 'IBS') under BAFIA 1989 and DFIA 2002, no such rule is required. Currently, such requirement

is not stipulated by IFSA 2013 since it becomes a statutory requirement of IFSA 2013 which should be adhered to by such licensed person and approved person involved in Islamic financial business.

Hence, it can be concluded that every licensed person under IFSA 2013 and every licensed person under FSA 2013 which is allowed to conduct certain Islamic financial businesses, are required to establish a *Shari'ah* committee for the purposes of advising the institutions in ensuring its business, affairs and activities comply with *Shari'ah*. Meanwhile, for an approved person or an operator of a designated payment system under IFSA 2013 and FSA 2013, such person is subject to the discretion of Central Bank of Malaysia whether to establish a *Shari'ah* committee or not.

Apart from the statutes, several guidelines explicitly require Islamic banks to establish a *Shari'ah* committee. Guidelines on International Islamic Bank (BNM/RH/GL 002-9) requires International Islamic Bank (hereinafter referred to as "IIB") to appoint the *Shari'ah* committee with the duties and responsibilities to review the institution's operations and activities compliance with *Shari'ah* requirements. In this regard, IIB is given three alternatives in forming *Shari'ah* committee, namely; (a) establishing its own *Shari'ah* committee; (b) leveraging on its parent's or group's *Shari'ah* committee; or (c) appointing an external *Shari'ah* advisor.

The SGF 2010 which superseded BNM/GPS 1 has retained the provision that requires every Islamic financial institutions regulated and supervised by the CBM to establish *Shari'ah* committee. Accordingly, [15]an Islamic bank licensed under IBA 1983, a financial institution licensed under the BAFIA 1989 and a development financial institution prescribed under the DFIA 2002 that participates in the IBS are required to establish a *Shari'ah* committee to provide advice on Islamic financial business.

Pertaining to a financial group, SGF 2010 allows them either to form a *Shari'ah* committee for each institution within the group or to form a single *Shari'ah* committee to provide advisory service to the entire group. In applying the second alternative, each licensed institutions within the financial group may request for an exemption from the CBM and the exemption shall only be granted to the Islamic financial institutions if the CBM is satisfied that the group *Shari'ah* committee is able to prove that it is adequately competent of serving the needs of the whole financial group. Otherwise, each licensed institutions is subjected to the first requirement.

To sum up, the above discussion explains that the formation of the *Shari'ah* committee is a legal requirement as contained in IFSA 2013, FSA 2013, SGF 2010, *Shari'ah* Governance 2020 and also several other Guidelines. All licensed institutions carrying on Islamic financial business are required to establish *Shari'ah* committee. Meanwhile CBM may require an approved Islamic financial adviser, approved issuer of a designated Islamic payment instrument, approved operator of a payment system and approved *takāful* broker to establish a *Shari'ah* committee to advise such person in certifying that their business, affairs and activities parallel with *Shari'ah*.

Legal Analysis on the Definition of the Shari'ah Committee

The *Shari'ah* committee refers to the *Shari'ah* committee of an institution established pursuant to section 30 [15]. Meanwhile the FSA 2013 states that the *Shari'ah* committee has the same meaning as interpreted in subsection 2(1) of the IFSA [4]. Prior to the implementation of the IFSA 2013 and the FSA 2013, there is no legal interpretation given to the *Shari'ah* committee established by the Islamic banks. The IFSA 2013 has improved such shortage by providing the legal interpretation to such committee.

However, such interpretation seems too general and has yet to simplify the suitable interpretation of “*Sharī‘ah* committee”. The provided interpretation is pertaining to the requirement for the establishment of *Sharī‘ah* committee for licensed person to conduct Islamic financial business pursuant to s.30 of IFSA 2013. It does not reflect the important characteristics of the *Sharī‘ah* committee.

More precise legal interpretation is needed by inserting the important characteristics to define this committee. For instance, *Sharī‘ah* committee can be legally interpreted as an independent body established pursuant to the law, have a number of qualified members as may be prescribed by the law and have the duties and responsibilities as may be specified by the law [13]. Thus, it is suggested that the amendment be made to IFSA 2013 by incorporating more precise interpretation in defining the *Sharī‘ah* committee.

Legal Analysis on the Terminology Used for the *Sharī‘ah* Committee

In referring to the *Sharī‘ah* committee established by the Islamic banks, various terms have been used by the statutes. “*Sharī‘ah* advisory body” was a terminology used by IBA 1983 and Central Bank of Malaysia Act 1959 (Revised 1994). Meanwhile, Central Bank of Malaysia Act 2009 (Act 701) (hereinafter referred to as ‘CBMA 2009’) termed it as “*Sharī‘ah* body” and “*Sharī‘ah* committee” (CBMA 2009, s.58). IFSA 2013 and FSA 2013 termed it as “*Sharī‘ah* committee”. According to the Guidelines issued by BNM, “*Sharī‘ah* committee” is the most frequently used by the Guidelines in representing *Sharī‘ah* committee. For examples, *Sharī‘ah* Governance 2020, SGF 2010; Guidelines on Financial Reporting for Licensed Islamic Banks (BNM/RH/GL/002-2); [16] Guidelines on Financial Reporting for Islamic Banking Institutions (BNM/RH/CP 022-1); Guidelines on Corporate Governance for Licensed Islamic (GP1-i) (BNM/RH/GL 002-1); Guideline on *Ibrā’* (Rebate) for Sale-Based Financing (BNM/RH/GL 012-5); Guidelines on Financial Reporting for Development Financial Institutions (BNM/RH/GL 005-16); and Guidelines on Fit and Proper for Key Responsible Persons for Development Financial Institutions (BNM/RH/GL 005-13). In the meantime several Guidelines alternately use “*Sharī‘ah* advisory”, “*Sharī‘ah* advisory body” and “*Sharī‘ah* committee” such as Guidelines on International Islamic Bank (BNM/RH/GL 002-9).

Only BNM/GPS 1 and Guidelines on the Governance of *Sharī‘ah* Committee for Development Financial Institutions (BNM/RH/GL/005-6) have specified that a *Sharī‘ah* committee established by the Development Financial Institutions to be known as a “*Sharī‘ah* Committee”. However, both Guidelines were superseded by SGF 2010. Thus, there is no longer any reference from Guidelines which provide specific terms to be used. “*Sharī‘ah* Committee” is a preferred noun used by SGF 2010. Nevertheless SGF is silent in specifying that a *Sharī‘ah* committee established by the Islamic banks shall be known as a “*Sharī‘ah* Committee”. Similarly *Sharī‘ah* Governance 2020.

Due to the absence of legal provisions which require that specific terminology should be given to the *Sharī‘ah* committee established by Islamic banks, several names have been given by Islamic banks to the *Sharī‘ah* committee. Among the terminologies used by Islamic banks are as follows:

(a) *Sharī‘ah* Committee – Alliance Islamic Bank Berhad (Annual Report of Alliance Islamic Bank Berhad, 2020); Deutsche Bank (Malaysia) Berhad (Financial Statements of Deutsche Bank (Malaysia) Berhad, 2019), Bank Pembangunan Malaysia Berhad (Annual Report of Bank Pembangunan Malaysia Berhad, 2019); and AmlInvestment Bank Berhad (Annual Report of AmlInvestment Bank Berhad, 2020).

(b) *Shari'ah* Supervisory Council – Bank Islam Malaysia Berhad (Annual Report of Bank Islam Malaysia Berhad, 2019).

(c) *Shari'ah* Advisory Committee – Standard Chartered Saadiq Berhad (Financial Statements of Standard Chartered Saadiq Berhad, 2019).

(d) *Shari'ah* Board – Al Rajhi Banking & Investment Corporation (Malaysia) Bhd. (Financial Statements of Al Rajhi Banking & Investment Corporation (Malaysia) Bhd, 2019).

A research conducted by [17] reveals that the majority of respondents are more comfortable with the term *Shari'ah* committee as a proper terminology to be used since such a term has been used by financial institutions for several years. On the other hand, some respondents opine that the given name should be flexible. The most important thing is that such body is capable of ensuring *Shari'ah* compliance and is distinguishable from the SAC of CBM.

Despite the diversity of terminologies, the duties and responsibilities of this body are similar pursuant to IFSA 2020 (IFSA 2020, s.32) and *Shari'ah* Governance 2020. For consistency and uniformity of the terminology, it is suggested that CBM should determine a specific terminology to be used by Islamic banks. In addition, it would avoid any confusion and misconception from stakeholders due to the diversity of terminology used by Islamic banks. Hence, it would be good if there is a legal provision provided that the specific terminology such as *Shari'ah* Advisory Board or *Shari'ah* Committee should be given to the *Shari'ah* committee established in the Islamic banks.

Legal Analysis on the Composition of the *Shari'ah* Committee

Referring to statutes, there is no stipulation pertaining to the composition of the *Shari'ah* committee established by the Islamic banks. However, such a stipulation has been laid down by *Shari'ah* Governance 2020 which should be observed by Islamic banks. Regarding the number of members, prior to SGF 2010, the *Shari'ah* committee shall consist of a minimum of three members. Then, the minimum number has been increased to five persons pursuant to the requirement of SGF 2010 (Hussain, 2020). The same now requires by the *Shari'ah* Governance 2020. However for the banking institutions participating in IBS, the *Shari'ah* committee, at minimum, comprise at least three (3) *Shari'ah* committee members.

The Islamic banks are allowed to appoint more than five persons since the *Shari'ah* Governance 2020 does not specify the maximum number of membership to be appointed. It depends on the decision of the institutions in ensuring the effectiveness of *Shari'ah* supervision carrying out by their *Shari'ah* committee. For instance, the Islamic bank expands its Islamic financial business by offering new Islamic financing facilities/products or upon opening new branches locally or abroad. What is more important is the output and the effectiveness of the work done by five members compared with the work done by more than five members but who failed to perform the duties and responsibilities effectively.

Apart from that, *Shari'ah* Governance 2020 requires that majority of its *Shari'ah* committee members are *Shari'ah* qualified persons; and the chairman of the *Shari'ah* committee must be a *Shari'ah* qualified person. The *Shari'ah* qualified persons to be assessed by the following requirements:

(a) holds, at minimum, a bachelor's degree in *Shari'ah*, which includes study in *Usul Fiqh* (principles of Islamic jurisprudence) or *Fiqh Muamalat* (Islamic transaction/commercial law);

(b) possesses solid knowledge in *Shari'ah* with reasonable Islamic finance knowledge and experience of the relevant industry; and

(c) demonstrates strong proficiency and knowledge in written and verbal Arabic, with good command in the preferred language of the Islamic financial institutions, either Malay language or English language.

The above requirements of *Shari'ah* Governance 2020 are the improvement made to the SGF 2010. Previously, SGF 2010 also allows the Islamic banks to appoint experts from relevant backgrounds such as finance and law as a member of the *Shari'ah* committee provided that such members must not form the majority of the *Shari'ah* committee. Those experts could provide input on related areas and support the depth and breadth of the *Shari'ah* deliberations. It would be of advantage if all the members of the *Shari'ah* committee besides being experts in the field of *Shari'ah*, are also experts in the fields related to finance, economics and law. For example, Islamic banks may appoint person who holds a bachelor's degree with the combination of study in the field of *Shari'ah* and Law, *Shari'ah* and Economic or *Shari'ah* and Finance from recognized universities. Even though there is no provision stipulated by *Shari'ah* Governance 2020, the author of opinion that, the Islamic banks are not barred to appoint the member of *Shari'ah* committee from other academic background. The most important is the majority of the members are *Shari'ah* qualified person.

In addition, the Islamic banks should also consider the level of knowledge and language proficiency of a member in forming the composition of the *Shari'ah* committee. The requirement regarding this as required by *Shari'ah* Governance 2020 is something good. In line with the duties of the *Shari'ah* committee to deliberate the *Shari'ah* issues based on references which are mostly in Arabic, majority of members should be able to demonstrate strong proficiency and knowledge in Arabic both written and verbal. At the same time, they must also have good understanding of Malay Language and English.

Based on the above discussion, it can be summarized that the Islamic banks merely should not appoint at least five members in forming *Shari'ah* committee, but should also take into consideration the composition of such committee as laid down by the *Shari'ah* Governance 2020 including academic qualification, knowledge and proficiency of languages, expertise and relevant background of the members.

Legal Analysis on the Secretariat to the *Shari'ah* Committee

Shari'ah Governance 2020 requires Islamic financial institutions to establish a secretariat to serve the *Shari'ah* committee. The functions of such a secretariat includes: (a) coordinating communications and disseminating information among the *Shari'ah* committee, the board and senior management; (b) performing in-depth research and studies on *Shari'ah* issues; (c) providing day-to-day advice to relevant parties within the Islamic financial institutions on *Shari'ah* matters based on the rulings of the SAC and decisions or advice of the *Shari'ah* committee; (d) ensuring proper dissemination of decisions or advice of the *Shari'ah* committee within the Islamic financial institutions; and (e) undertaking administrative and secretarial functions to support the *Shari'ah* committee.

This is the new improvement made by *Shari'ah* Governance 2020 compared to SGF 2010. In addition *Shari'ah* Governance 2020 requires that an officers who perform the responsibilities as Secretariat to the *Shari'ah* Committee also to possess a *Shari'ah* qualification. The secretariat also has the responsibility to plan and coordinate *Shari'ah* committee meetings in a manner that promotes sound decision-making by the *Shari'ah* committee.

Legal Analysis on the Position of the *Shari'ah* Committee in the Islamic Banks' Organisation Structure

In discussing the establishment of the *Shari'ah* committee, the position of such committee within the Islamic bank's organizational structure is also essential to be scrutinized. Undoubtedly every Islamic bank has its own organizational structure and may vary from other Islamic banks. However, the *Shari'ah* committee should exist in the organizational structure of the Islamic bank which will clarify its position, to whom they are accountable as well as will reflect their role in the institution.

Previously, SGF 2010 clearly provides that the *Shari'ah* committee shall functionally report to the Board of Directors of Islamic bank (hereinafter referred to as 'BoD'). Accordingly, they are responsible to the BoD. This is also consistent with the appointment of members of the *Shari'ah* committee by the BoD (Guidelines on Corporate Governance for Licensed Islamic Banks BNM/RH/GL 002-1). At the same time, one of their duties is to advise the BoD and the Islamic bank on the *Shari'ah* matters as specified by SGF 2010. However, according to *Shari'ah* Governance 2020, there is no clear stipulation on this matter. This situation leads to the question, where is the appropriate position of *Shari'ah* committee within the Islamic bank's organizational structure.

If the position of *Shari'ah* committee is higher than BoD in the organization structure, it will illustrate that the *Shari'ah* committee is the ultimate power in driving the business direction of the Islamic bank. In fact, it is beyond the roles and functions of BoD. If placed under the BoD, it will illustrate that the *Shari'ah* committee board is controlled by the BoD. Hence the issue on the independence of *Shari'ah* committee in discharging its duties is questionable.

The author of opinion that, the best position is by putting *Shari'ah* committee parallel to the BoD in the organization structure that has the capacity to advise the BoD and Islamic bank in ensuring *Shari'ah* compliance. For consistency, it would be appropriate if *Shari'ah* Governance 2020 may prescribe the position of *Shari'ah* committee in the Islamic financial institution's organizations structure. It would be good as well if *Shari'ah* Governance 2020 provides an illustration on the proper position of the *Shari'ah* committee within the Islamic bank's organizations structure.

Conclusion

Based on the above discussion, it can be seen that IFSA 2013 and the Guidelines are complementary to each other in the requirement for the establishment of *Shari'ah* committee by Islamic banks and participating banks in IBS. It can be seen that, the new *Shari'ah* Governance 2020 has improve the previous provision of SGF 2010 pertaining to the composition of *Shari'ah* committee and the secretariat to the *Shari'ah* committee. Although the above provisions of IFSA and Guidelines are very good in dealing with the establishment of *Shari'ah* committee, the study reveals that there are several deficiencies which still need to be improved. Firstly, the legal interpretation of the *Shari'ah* committee. The interpretation given by s.2(1) of IFSA 2013 is too general and fails to describe the essential features of the *Shari'ah* committee. Secondly, the establishment of the *Shari'ah* committee. The legislation is silent on the specific terminology to be used by Islamic banks. Thirdly, the position of the *Shari'ah* committee in the organizational structure is not stipulated by the law.

Hence, this study suggests that improvements should be made to the following the legal aspects involving the legal interpretation, terminology as well as the position of the *Shari'ah* committee. More specific legal interpretation should be given to the *Shari'ah* committee which may describe the essential features of such body. In addition, specific

terminology to be used should be determined for consistency. Finally, the position of the *Shari'ah* committee within the Islamic bank's organizational structure should be specified. Improvement is needed to strengthen the legal framework of the *Shari'ah* committee as a key person in ensuring the *Shari'ah* compliance of Islamic banks in Malaysia.

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