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Duties and Decision-Making Guidelines for *Sharī‘ah* Committee: An Overview of AAOIFI

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Muhammad Amanullah****

Abstract: The *Sharī‘ah* ‘Committee is a board which is independent in directing, reviewing and supervising an Islamic Financial Institution (IFI). It consists of those who are specialised in *Fiqh Mu‘amalāt* or those who know it with expertise in other fields. In conjunction with IFIs emergence, the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) was established and has issued numerous standards on accounting, auditing and also governance for IFIs. The researchers intend to review the duties and decision-making guidelines of the *Sharī‘ah* Committee prescribed by the AAOIFI in 2010. The review undergoes a thorough search and critical analysis of any related content about the topic throughout the whole standard. Some important results are: AAOIFI mentions directly the duties of the *Sharī‘ah* Committee along with the definition of this *Sharī‘ah* Committee. These duties are directing, reviewing and supervising. On the other hand, decision-making guidelines are indicated indirectly and they are scattered throughout the AAOIFI governance standards.

Key words: AAOIFI, *Sharī‘ah* Committee, duties, decision-making, guidelines

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Abstrak: Jawatankuasa Syariah adalah lembaga yang bebas untuk mengarah, menyemak dan mengawasi Institusi Kewangan Islam (IFI), terdiri dari mereka yang mengkhususkan diri dalam *Fiqh Mu'āmalat* atau mereka yang mempunyai pengetahuan tentangnya dengan kepakaran dalam bidang lain. Selain itu, seiring dengan perkembangan IKI, Organisasi Perakaunan dan Pengauditan untuk Institusi Kewangan Islam (AAOIFI) telah ditubuhkan dan telah mengeluarkan banyak piawaian mengenai perakaunan, pengauditan dan juga tadbir urus IFI. Penyelidik telah menyemak Piawaian Tadbir Urus dan Etika yang dikeluarkan oleh AAOIFI pada tahun 2010, mengenai tugas dan garis panduan membuat keputusan oleh Jawatankuasa Syariah. Semakan tersebut dijalankan secara menyeluruh dan kritikal untuk mencari apa-apa kandungan berkaitan mengenai topik tersebut di dalam piawaian tersebut. Hasilnya, AAOIFI hanya menyebut secara langsung tugas Jawatankuasa Syariah dalam definisinya mengenai Jawatankuasa Syariah, iaitu mengarah, menyemak dan menyelia, sementara garis panduan membuat keputusan pula didapati secara tidak langsung secara berselerak sepanjang piawaian tadbir urus AAOIFI .

Kata Kunci: AAOIFI, Jawatankuasa Syariah, tugas, membuat keputusan, garis panduan

Introduction

The Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) is a non-profit autonomous international corporate body that prepares the accounting, auditing, governance, ethics and *Shari'ah* standards for IFIs and the Islamic finance industry. AAOIFI, within the *Shari'ah* rules and principles, aims to improve the quality and uniformity of auditing and governance practices related to IFIs through the introduction of Accounting, Auditing and Governance Standards for IFIs (AAGSIFI). The researcher will examine the duties and decision-making guidelines from the AAGSIFI; whether they are constructive and well-elaborated for practitioner uses.

From the researcher's knowledge, there is not a single study yet that has been made on this topic which is focusing on the duties and decision-making guidelines issued by AAOIFI. However, the researcher was successful in finding some related studies. Among them is an article wrote by Al-Shubayli (2011) which mentions that the roles of the *Shari'ah* Supervisory Board are to set up the *Shari'ah* guidelines toward IFIs and confirm its application in the IFIs. There is also a comparative study by Nawal Kasim, Htay and Syed Ahmed Salman

(2013) which did an analysis of AAOIFI, IFSB and BNM *Sharī'ah* governance guidelines. However, this study did not touch on the duties and decision-making guidelines directly but compared the whole of AAOIFI's guidelines with the other guidelines. Other than these, the researcher did not find any other related works of literature on decision-making guidelines for the *Sharī'ah* Committee.

As an international autonomous body of standards, AAOIFI's guidelines for the *Sharī'ah* Committee on its duties and decision-making processes should be examined to ensure that it is compatible internationally. Besides, the absence of previous literature on this topic necessitates a need to conduct a critical and thorough study towards it.

The Chronological Development of AAOIFI

The modern record of accounting was first issued in Italy by Luca Pacioli in 1494 by using double-entry bookkeeping (Lauwers & Willekens, 1994, p. 302). In the nineteenth century, accounting shifted from local expert organisations in England to establish the Institute of Chartered Accountants in England and Wales in 1880 (Perks, 1993, p. 16). However, long before Pacioli pioneered his book, the Muslim world had already instituted the *Bayt al-Māl* system which is a monetary institution that serves as the treasurer of the state and also safeguards social welfare. Muslims also had their *Kitābāt al-Amwāl* which means cash recordings.

These *Kitābāt al-Amwāl* manuscripts can be traced back to the late first century of the Islamic era, which corresponds to the early eighth century C. E., which was much earlier than what was issued by Pacioli in the 15th century. Among the works that contributed to *Kitābāt al-Amwāl* manuscripts are *Kitāb al-Kharāj* by 'Abū Yūsuf Ya'qūb ibn 'Ibrāhīm (d. 182/799), *Kitāb al-Kharāj* by Yaḥyā ibn 'Ādam (d. 203/819), *Kitāb al-Amwāl* by 'Abū 'Ubayd al-Qāsim ibn Sallām (d. 224/839), *al-Kharāj wa Ṣinā'at al-Kitābah* by 'Abū al-Faraj Qudāmah ibn Ja'far al-Kātib (d. 320/932), *Kitāb al-Amwāl* by 'Abū Ja'far Aḥmad ibn Nasr al-Dāwūdī (d. 402/1011) and *Kitāb al-Istikhrāj li 'Aḥkām al-Kharāj* by 'Abū al-Faraj 'Abd al-Rahmān ibn Rajab al-Ḥanbalī (d. 795/1393).

Kitāb al-Amwāl by al-Dāwūdī, for example, is one of the significant works on the revenue administration of the early phase of Islam. It contained verdicts of the disputes related to problems of settlement of lands and administration of properties. It was being used for a practical

purpose in the fourth/fifth centuries of Hijrah in North Africa, Spain and Sicily. The manuscript remained in demand for even five hundred years after the death of al-Dāwūdī. All of these precious manuscripts are concrete evidence of progressive accounting history in Islamic civilisation (al-Dāwūdī & Abu'l Muhsin, 1784, p. 2).

Furthermore, accounting or accountancy is the measurement, processing, and communication of financial information about economic entities such as businesses and corporations (Needles, Powers, & Susan V. Crosson, 2014, p. 4). It evaluates the results of the commercial activities of any organisation. The term 'accounting' is used habitually as a synonym of the term 'financial reporting.' Its practitioner is known as an accountant.

Accounting organisations such as standard-setters, accounting firms, and professional bodies facilitate accounting practices by announcing the financial statements which are prepared by accountants following generally accepted accounting principles (GAPP) (Horngren, Datar, & Rajan, 2015, p. 25). Various standard-setting organisations set GAPP such as the Financial Accounting Standards Board (FASB) in the United States and the Financial Reporting Council in the United Kingdom.

Besides that, the word audit is derived from a Latin word "*audire*" which means "to hear" (Ajao, Olamide, & Ayodejitemitope, 2016, p. 33). During the medieval times, auditors in Britain used to hear the accounts read out for them and checked that the organisation's personnel were not negligent or fraudulent at a time when manual book-keeping was prevalent (Matthews, 2006, p. 6). An audit is a "systematic, independent and documented process for obtaining audit evidence (records, statements of fact or other information) which are relevant and verifiable" as defined in ISO 19011:2011—Guidelines for auditing management systems (ASQ, "What is auditing?"). Through the audit, a set of policies, procedures or requirements are fulfilled. The practitioner of auditing is called an auditor. The auditing process has three different stages of different types of auditors in conventional practice.

The process of conducting accounting and auditing of conventional financial institutions is well-established. However, its establishment is based on following the framework of the traditional system which was based on usury in their transactions. Meanwhile, the emergence of IBF needed accounting and auditing organisations that could provide

standards for IFIs. Therefore, after a working paper presented by the Islamic Development Bank during the annual meeting of its board of governors in Istanbul in March 1987, some committees were formed to examine and formulate the appropriate methods of accounting standards for IFIs. They made intensive effort and conducted several studies to provide a basis for the rules. They placed these studies in five volumes and deposited them in the library of the Islamic Research and Training Institute of the Islamic Development Bank in Jeddah. These studies led to the establishment of the Financial Accounting Organization for Islamic Banks and Financial Institutions (FAOIBFI) in 1991 which was signed by IFIs by the Agreement of Association in the State of Bahrain, as an international autonomous non-profit corporate body (Bucheery, 2001, p. 58).

After four years of work, the:

“[r]ecognition of the importance of auditing led the FAOIBFI to change its name in 1995 to the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), to include a specific reference to auditing (Archer & Karim, 1997, p. 100).”

The renaming of the organisation has resulted in a new organisational structure. The new arrangement is headed by the Secretary-General (AAOIFI, «Introduction», 2002, pp. 2-3).

Nowadays, AAOIFI is an international organisation primarily responsible for the development and issuance of standards in the areas of *Sharī'ah*, accounting, auditing, ethics and governance for the global Islamic finance industry. AAOIFI is also responsible for secondary objectives which are:

- i. Spreading accounting and auditing concepts relevant to IFIs and their applications through training, seminars, publication of a periodical newsletter, carrying out and commissioning of research and other means,
- ii. Preparing, promoting, and interpreting accounting and auditing standards for IFIs, and
- iii. Rechecking and revising accounting and auditing standards for IFIs (AAOIFI, “Objectives”).

Karim claims that the reasons behind AAOIFI’s issuance of accounting standards for Islamic banks are:

- i. The fear that the regulatory agencies might intervene to regulate the financial reporting of these institutions using conventional supervision in the countries in which Islamic banks operate, and
- ii. To achieve an appropriate degree of comparability between these banks' financial statements (Karim, 1990, pp. 299–305).

AAOIFI started the process of producing Islamic accounting and auditing standards by developing a statement of the objectives and concepts of financial accounting for Islamic banks, in a way similar to that of its Western counterpart, FASB (Financial Accounting Standards Board) in the USA (Karim, 1994, pp. 53-59). It started with the objectives and the concepts set forth by international accounting standards-setting bodies, tested them against *Sharī'ah* principles and accordingly accepted standards which are in agreement with *Sharī'ah* and rejected those that are not.

AAOIFI follows a due process which provides interested parties with the opportunity to express their opinion on the standards before they are finally approved by the Accounting and Auditing Standards Board and the *Sharī'ah* Board (Karim, 1994, pp. 53-59). Moore says:

“Each accounting and auditing standard undergoes a rigorous process of scrutiny and revision before issued as an exposure draft. Each exposure draft is subject to extensive debate at a public hearing before being promulgated as a standard (Moore, 1997, p. 99).”

Gambling et al. described AAOIFI as an organisation which has been set up with a remit to produce a set of standards, but its remit does not extend to enforcing the implementation of them. AAOIFI is expected to work very closely with the current regulatory agencies in the countries where the Islamic banks operate, to gain their support in encouraging Islamic banks under their supervision to implement AAOIFI's standards (Gambling, Jones, & Karim, 1993, pp. 195-207). Karim further explains:

“...so as long as important stakeholders perceive AAOIFI's role as a private self-regulatory body within the context of setting morally governed standards, this might help AAOIFI to have its standards at least voluntarily implemented by Islamic banks” (Karim, 1996, p. 132).

The Structure of AAOIFI

Every organization, whether profit or non-profit based, political or NGO, international or national, has its vision and objectives, which are achieved through task allocation, a grouping of expertise, a hierarchy of conduct which together are called an organizational structure. A suitable, realistic and significant arrangement is needed to achieve the organization's vision in a periodical timetable. There are many types of corporate structures depending on the kind of image being aimed for.

AAOIFI is an international non-profit organisation primarily responsible for the development and issuance of standards for the global Islamic finance industry. At the beginning of its establishment, AAOIFI used the name of FAOIBIFI. At that time, the structure was slightly different from the current organisational structure. FAOIBIFI comprised of the Board of Trustees, the Financial Accounting Standards Boards, the Executive Committee and the *Sharī'ah* Committee.

After four years of progressing, FAOIBIFI changed its name to AAOIFI and consequently also changed its organizational structure. After that, the new corporate composition comprised of the General Assembly, the Board of Trustees, the Accounting and Auditing Standards Board, the Executive Committee, the *Sharī'ah* Boards, and the General Secretariat to be headed by the Secretary-General (Bucheery, 2001, p. 58). The upper hierarchy changed, some additional boards added and standardization of the structure occurred.

The change was substantial for the democratization process of the organization's structure. This process was indicated when the Board of Trustees, which comprised of a limited number of committees as the organization's highest decision maker, changed to the General Assembly, which involved all members including ordinary members. This change proves that the AAOIFI significantly expanded and became more democratic for its general purpose.

The AAOIFI has a constructive hierarchical structure and an inter-linked connection between boards. The ultimate authority over the organization is the General Assembly which convenes at least once a year. The General Assembly has the power to approve, amend AAOIFI's statute, appoint the Board of Trustees which situates under the General Assembly in the hierarchy, and adopt the annual financial statements (AAOIFI, "General Assembly").

Besides that, the General Secretariat is responsible for the rapporteur and secretarial work. The AAOIFI's Secretary General heads the General Secretariat. This secretariat combines all of the secretaries on all Boards in AAOIFI for administrative and operational purposes. It is responsible for, amongst others, day-to-day operations, preparation of standards (in coordination with AAOIFI's standards' Boards) and carrying out standards-related activities (AAOIFI, "General Secretariat").

The AAOIFI also comprises of committees that support the Board of Trustees. There are three of them: the Executive Committee, Audit Committee, and Nominating Committee. All the committees are founded functionally with their job scopes. The Executive Committee is responsible for, amongst others, discussing the work plan, the annual budget, and annual report (AAOIFI, "Executive Committee"). Meanwhile, the Audit Committee upholds the integrity, transparency, disclosures, and risk management (AAOIFI, "Audit Committee"). The Nominating Committee is the one who nominates, selects and appoints the technical boards which consist of the *Shari'ah* Board, the Accounting and Auditing Board, and the Governance and Ethics Board (AAOIFI, "Nominating Committee").

Furthermore, the three technical boards similarly aim to come up with a set of standards relevant to their functionality, such as the Governance and Ethics Board came up with the AAOIFI Governance and Ethics Standards. The compositions of the boards are multi-disciplined, profession-based individuals from among practitioners in the industry and also from among academicians in respective fields. The researcher's concern is on the Governance and Ethics Board as it is the one that drafted the roles and decision-making guidelines for the *Shari'ah* Committee.

The AAOIFI Governance and Ethics Board (AGEB) held its first meeting on the 25th of April 2016. A few months earlier, the General Assembly of AAOIFI approved its establishment next to the former two boards that were already founded. Dr Hameed Merah, the Secretary-General of AAOIFI said that the purpose of AAOIFI's foundation is:

“[i]n continuation of AAOIFI's pioneering efforts to serve the global Islamic finance industry through the development of its governance and ethical standards, and in its keenness to enhance governance within the industry (Merah, 2016).”

Moreover, to preserve the diversity of the board, its members are recruited from many different sectors within IBF as follows:

- i. At least five members are representing IFIs (commercial banks, investment banks, insurance, financing companies, etc.).
- ii. Up to five members representing accounting and auditing firms, and professionals in the field of governance, risk management, and compliance (GRC).
- iii. Up to three members representing central banks, regulatory authorities, and international or multilateral organisations (such as the World Bank, International Monetary Fund (IMF), the Islamic Financial Services Board (IFSB), etc.).
- iv. At least one member who is a *Sharī'ah* scholar (and does not serve at the same time on AAOIFI *Sharī'ah* Board).
- v. At least one member is representing academicians (universities and educational institutions) (AAOIFI, “Composition”).

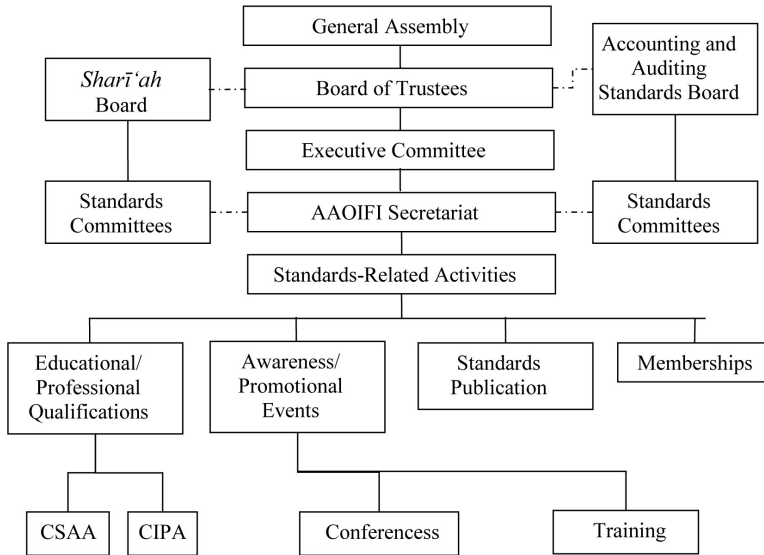
The composition is also involving stakeholders outside IBF. It shows the commitment of AAOIFI to make its standards as relevant as possible worldwide. The table below shows the persons who are involved in AGEB:

Table 3.1 Members of AGEB (aaoifi.com, “AGEB Members”)

Name	Position	Status
Mr Jamil Darras	Head, Central Accounting Section, Finance Department, Islamic Development Bank, Saudi Arabia.	Chairman
Sheikh Essam Mohammed Ishaq	Shari'ah Advisor & Board Member, Discover Islam Centre, Bahrain.	Member
Dr Hussein Said Saifan	Assistant General Manager, Jordan Islamic Bank, Jordan	Member
Mr Oliver Agha	Managing Partner, Agha & Co, United Arab Emirates	Member
Mr Qudeer Latif	Partner, Clifford Chance LLP, Dubai, United Arab Emirates.	Member
Dr Hatim El-Tahir	Director, Islamic Finance Group, Deloitte & Touch, Kingdom of Bahrain	Member
Dr Hamed Hassan Merah	Secretary-General, Accounting and Auditing Organization for Islamic Financial Institutions	Member

The structure of AAOIFI is illustrated in the chart below:

Figure 3.1 The Structure of AAOIFI (aaoifi.com, "Structure")



Duties of *Sharī'ah* Committee According to AAOIFI

A duty is a moral or legal obligation (Oxford dictionaries, "Duty"). It is derived from an old French word, '*deu*', a past participle of '*devoir*' from a Latin word which means "debt." Therefore, '*deu*' itself means 'that which is owing' (Encyclopædia Britannica, "Duty"). Thus, duty is the combination of words that consist of a sense of morality added to accomplishing legal obligations. The commitment comes as a sense of belonging, like someone who is in debt with another.

The Muslim world is familiar with the concepts of '*al-'amānah*,' '*farḍ al-kiḥāyah*' and '*al-dayn*'. '*Al-'Amanah*' is an act of completing or state of being completed or finished (*al-Mu'jam al-Wasīt*, 2004, p. 28). Every Muslim must accomplish their religious obligations as stated in the verse no. 72, *sūrah al-Aḥzāb*:

"We did indeed offer the Trust (*al-'amānah*) to the Heavens and the Earth and the Mountains; but they refused to undertake it, being afraid thereof: but man undertook it;- He was indeed unjust and foolish;- " (*Qur'ān*, 33:72).

'*Al-'Amānah*' here is all the religious obligations according to the majority of scholars' opinions (al-Qurtubī, 1996, p. 254).

This duty is the effect of the personal vow by all mankind in front of Almighty as captured in the Holy *Qur'ān*:

“When thy Lord drew forth from the Children of Adam - from their loins - their descendants, and made them testify concerning themselves, [saying]: “Am I not your Lord [who cherishes and sustains you]?”- They said: “Yea! We do testify!” [This], lest ye should say on the Day of Judgment: “Of this, we were never mindful” (*Qur'ān*, 7:172).

This vow shows the promise humans made in front of the Almighty which makes it justified for humans to keep the obligation of fulfilling all the Almighty's orders.

All obligations are not the same for every person. It is only according to their level of knowledge and ability as Allah doesn't burden His servant beyond their limitations. The different stages of responsibility can be reflected through the *farḍ al-kifāyah* concept in Islam, i.e. things of public interest, whether for religion or material purposes, without which a society cannot be organised and sustained. If someone capable does it, all others are liberated from committing a sin (Al-Zarkashī, 1992, p. 251). However, if none of them does it, the society as a whole will bear the sin collectively. Therefore, every aspect of *farḍ al-kifāyah* should be assigned to a specialist to accomplish it. Allah said:

“Indeed, Allah commands you to render trusts to whom they are due and when you judge between people to judge with justice. Excellent is that which Allah instructs you. Indeed, Allah is ever Hearing and Seeing” (*Qur'ān*, 4:58).

The deed of putting a specialised person in the right position is the nearest way to achieving fairness in a society. Islam teaches us to establish a sustainable and independent religious society with sufficient statesmen and qualified personnel in every section of human life since the time of the Prophet (S.A.W).

Therefore, the *Sharī'ah* scholars who are *Sharī'ah* Committee members, perform their responsibility for the interest of a society by contributing and supervising the IFIs; if they are not there, most of the public will remain in *Sharī'ah* non-compliant transactions. Their effort

contributes to preserving both the religion and a prosperous society in this world. It is an additional '*amānah*' from Allah (S.W.T.) given to this committee for the benefit of the Muslim society, besides the common duties that they are obliged to perform individually like other Muslims.

The AAOIFI, in its Governance Standards, has assigned the *Sharī'ah* Committee a few entrusted job scopes for the accomplishment of the activities of IFI (AAOIFI, "Governance", 2010, pp. 4-5). They are as follows:

- i. Directing.
- ii. Reviewing.
- iii. Supervising.
- iv. Reporting.

All these roles are to fulfill the requirement of *Sharī'ah* -compliance of an IFI.

These roles of the *Sharī'ah* Committee have been inserted in the duties of the *Sharī'ah* Supervisory Board in the AAOIFI Governance Standards as follows:

"The *Sharī'ah* Supervisory Board is entrusted with the duty of directing, reviewing, and supervising the activities of the Islamic financial institution to ensure that they comply with Islamic *Sharī'ah* Rules and Principles (AAOIFI, "Governance", 2010, pp. 4-5)."

It is understandable that the *Sharī'ah* Committee also needs to make sure that the report is in-line with standards and accurate with the activities although its secretariat usually prepares it.

Moreover, to ensure that an IFI is *Sharī'ah*-compliant, the *Sharī'ah* Committee needs to direct the Board and other stakeholders towards it, as the AAOIFI entrusts this committee to do so. The *Sharī'ah* committee has to address the issues related to instructions, regulations, forms of contract, and development of *Sharī'ah* principles. In case of any inquiries and questions, from any stakeholder, they need to give *fatwās* that answer and direct those questions (Malek Marwan, Mohamad Sabri, Rashila, & Raghad, 2016, p. 29).

Sharī'ah review is a screening process of all IFI activities including but not limited to contracts, agreements, policies, products, transactions, memorandums and articles of association, financial statements, reports

(especially internal audit and central bank inspection), and circulars. It aims to create a parallel situation between IFI activities and *Sharī'ah* teachings (AAOIFI, "Governance", 2010, p. 14). This review is the most crucial part in converting a conventional institution to an Islamic one. The *Sharī'ah* Committee has a duty to participate in this review.

Observing the execution of *fatwā* pronouncements and compliance of IFI activities with them is the supervising process that needs to be carried out by the *Sharī'ah* Committee directly or indirectly. This supervision includes the method of preventive, remedial and, complementary control. The preventive process is an early review of an end user product before an IFI markets it. The remedial method is in charge when IFI markets the product through the auditing process. Then the *Sharī'ah* internal auditor's report is reviewed for complementary control as a certainty of *Sharī'ah* compliance (Garas & Pierce, 2009, p. 395).

The three main roles of the *Sharī'ah* Committee of directing, reviewing and supervising complement each other. Directing is essential in the early processes, while supervising is a process in the execution period of a *fatwā*. The *Sharī'ah* executive in the office plays a vital role in ensuring that this period is a success. The reviewing is then a startup and complementary looking-back process in converting conventional products to Islamic products and also in the post-mortem process; later, if some loops are found, the *Sharī'ah* Committee can put an instant remedy to them.

Decision-Making Guidelines for *Sharī'ah* Committee Issued by AAOIFI

Decision-making is an integral part of daily processes, especially in modern corporate governance in a company. The right decisions from the Board of Directors will direct all the activities of the organization towards a fruitful outcome. However, a contrary result will appear, if an improper decision is made from the decision maker. This situation puts any decision-making job at high-risk in the corporate environment. Consequently, the risk will increase if it involves the *Sharī'ah* as the main subject of decision-making.

The Oxford Dictionary defines decision-making as the action or process of making important decisions (Oxford dictionaries, "Decision-making"). Meanwhile, Trewatha & Newport define the decision-making

process as follows: “Decision-making involves the selection of a course of action from among two or more possible alternatives in order to arrive at a solution for a given problem” (MSG, “What is Decision-making?”). If both definitions are merged, then we can prescribe that decision-making is the selection of a course of action from among two or more options in a significant problem.

However, when the *Sharī‘ah* Committee members decide on a *Sharī‘ah* matter, it is called ‘*ijtihād*’. ‘*Ijtihād*’ is a traditional practice of Muslim scholars for any decision on *Sharī‘ah* matters, since the Prophet’s (S.A.W) time. Hence, the Prophet (S.A.W) himself made ‘*ijtihād*’ at certain times. ‘*Ijtihād*’ is not poor decision-making since the scholars refer a *Sharī‘ah* matter to the sources of revelation to an extraordinary extent. The person who makes ‘*ijtihād*’ is called a ‘*Mujtahid*’. There is a list of criteria or requirements in order to be a ‘*Mujtahid*’. And the process to conduct any ‘*ijtihād*’ is also systematically done.

The AAOIFI in its Governance Standards didn’t mention directly any decision-making standards for *Sharī‘ah* Committee in *Sharī‘ah* matters. However, the researcher has extracted some points related to the decision-making process from AAOIFI’s governance standards. They are as follows:

- i. To ensure the independence of the *Sharī‘ah* committee (AAOIFI, “Governance”, 2010, pp. 44-45).
- ii. To determine that the management has brought all principal transactions and dealings requiring the review of the *Sharī‘ah* committee to the *Sharī‘ah* Committee and to ensure the accuracy of the information (AAOIFI, “Governance”, 2010, p. 66).
- iii. The *Sharī‘ah* Committee shall consist of at least three members, and the involvement of consultative expertise is encouraged (AAOIFI, “Governance”, 2010, p. 4).
- iv. The *Sharī‘ah* team then provides a report for any decree or *fatwā* following AAOIFI’s standards of reporting (AAOIFI, «Governance», 2010, pp. 5-8).

Based on the above points, the researcher divides the decision-making process issued by AAOIFI into three, i.e. pre, current and post decision-making processes. The first step is in the pre-decision-making process. The second step is the current decision-making in action,

while the last level is in the post decision-making process period. Also, he concludes that the first step is continuously needed by a *Sharī'ah* Committee, not only at the beginning of the process.

Among the first step is to ensure the independence of the *Sharī'ah* Committee members. Independence, in AAOIFI's Governance Standards, is mentioned as follows:

“[a]n attitude of mind which does not allow the viewpoints and conclusions of its possessor to become reliant on or subordinate to the influences and pressures of conflicting interests. It is achieved through organizational status and objectivity” (AAOIFI, “Governance”, 2010, p. 44).

Objectivity is an independent mental attitude which *Sharī'ah* Committee members should maintain in performing *Sharī'ah* supervision. The standard mentions that a *Sharī'ah* Committee member should not be an employee of the same institution, and he shouldn't be involved in any operational or managerial responsibilities in the system. He also can't subordinate the judgment of any *Sharī'ah* supervision to that of others. The *Sharī'ah* Committee also must not be in any engagement with any officer or employee in his supervision institution for at least three years in the preceding period of his contract (AAOIFI, “Governance”, 2010, pp. 44-45).

This principle, therefore, necessitates *Sharī'ah* Committee members to be just, intellectually sincere and impartial by avoiding any conflict of interest. A lack of independence and conflict of interest can occur in the following examples:

- i. Financial involvement with, or in the affairs of, clients such as shares ownership, guarantees, etc.
- ii. Personal and family relationships between *Sharī'ah* Committee members and any member of the Board of Directors, or any executive in the management team of the institution.
- iii. The recurrent fees' bill of the IFI shows a broad representation of the proportion of the total gross payments of a *Sharī'ah* Committee and also the due payments for prior periods.
- iv. When IFI make contracts to pay the fee of the *Sharī'ah* Committee with the contingency fee method.
- v. If any of the *Sharī'ah* Committee members is offered a performance-related bonus.

- vi. If IFI gifts the *Sharī'ah* Committee members any goods or services or provides them with undue hospitality out of common courtesy of social life.
- vii. Any actual or threatened litigation has occurred between the IFI and a *Sharī'ah* Committee member.
- viii. Long association of the *Sharī'ah* Committee with the IFI which has exceeded five years (AAOIFI, "Governance", 2010, pp. 47-48).

The *Sharī'ah* Committee's independence is important since it will affect the decisions made by this committee. Any selfish and non-independent decision-making from the *Sharī'ah* Committee will result in lousy decisions being made towards the community. Which will ultimately lead to the tarnishing of the image trying to be portrayed by *Sharī'ah* Committee among the public. This situation will bring a high-level of risk towards Islamic Finance and will take a long time to rectify and re-convince the public about it.

Furthermore, the *Sharī'ah* Committee needs to assure that all matters related to the *Sharī'ah* in IFI's activities are discussed in the *Sharī'ah* Committee meetings, and the most important thing is that the information must be accurate and comprehensive. For that purpose, the *Sharī'ah* Committee should have complete and unrestricted access to all records, transactions, and data from all sources including professional advisers and the IFI's employees. Therefore, *Sharī'ah* Committee shall appoint someone from its members, or any other person, as a supervisor to help it in performing its duties. The accuracy of any information brought by any stakeholder will affect the decision that will be taken by the *Sharī'ah* Committee.

The researcher observes that in AAOIFI's Governance Standards, there is no statement that indicates a specific methodology or medium through which the *Sharī'ah* Committee can decide on any *Sharī'ah* matter. There is also no explanation about how any ruling or *fatwā* by *Sharī'ah* Committee is reached, either by a simple majority or otherwise. Moreover, the AAOIFI hasn't mentioned in its standards whether the *Sharī'ah* Committee needs to appoint a leader from among them or not.

However, in AAOIFI's standards there is indirect guidance to form a *Sharī'ah* Committee for the decision-making process in a meeting. The standard states that an IFI shall consist of at least three *Sharī'ah*

Committee members and they may seek assistance of consultants who have expertise in business, economics, law, accounting and other fields. The members should not include directors or significant shareholders of the IFI. The committee can also have members who are not specialized in *Fiqh al-Mu'āmalāt* but have expertise in IFIs.

Lastly, the *Sharī'ah* Committee, after pronouncement of a *fatwā* or ruling is obligated to prepare a report following the format set by AAOIFI's standards. The *Sharī'ah* Committee's report should contain the following essential elements:

- i. "Title;
- ii. Addressee;
- iii. Opening or introductory paragraph;
- iv. Scope paragraph describing the nature of the work performed;
- v. Opinion paragraph containing an expression of opinion on the compliance of the IFI with Islamic *Sharī'ah* rules and principles;
- vi. Date of report; and
- vii. Signature of the members of *Sharī'ah* supervisory board (AAOIFI, "Governance", 2010, p. 5)."

Conclusion

After three years of research since 1987, the AAOIFI was established to provide accounting standards for IFIs. During its early establishment, FAOIBFI (the first name of AAOIFI) only focused on accounting standards. However, after the awareness of the importance of auditing four years later, it made a change to its name, which emphasizes both accounting and auditing. In its later progress, AAOIFI also strengthened its view on contributing to the governance and ethics' standards.

The current structure of the AAOIFI is well-established with a definite composition, hierarchy, and objective. However, currently, the AAOIFI's standards are not binding for IFIs to follow. In order to make its standards more beneficial and effective, the AAOIFI is suggested to make these standards as binding law for all IFIs worldwide. This can be done by creating a memorandum of understanding between the AAOIFI and the countries that have Islamic finance institutions.

The duties and functions of the *Sharī'ah* Committee issued by the AAOIFI consist of three roles, which are directing, reviewing and

supervising. Despite their importance, these functions in the AAOIFI standards are only stated in the definition of the *Sharī'ah* Supervisory Board without any particular subtopic for them.

The decision-making guidelines provided by the AAOIFI are scattered in various parts of its governance standards without a proper subtopic discussing them. The silence of the AAOIFI standards in some decision-making processes, such as the methodology for reaching a decision will open a chance for misconduct. Therefore, robust and more specific standards are needed from the AAOIFI for the decision-making process by the *Sharī'ah* Committee in *Sharī'ah* matters.

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