

Islamic Banking and Finance- Where are we

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Abstract:

The Islamic financial industry is presently growing at a very fast pace in comparison to past. While appreciating this, however, there are still a lot of challenges ahead to get a fully Shariah compliant Islamic financial industry which can get complete satisfaction of Muslim Ummah being a matter of faith. Presently a primary Shariah frame work in the shape of standards, Shariah supervisory boards and “*Fatawa*” exist but the core problem is with the implementation. Then there are major issues of independence and authority of Shariah supervisory boards. They may be made a part of top management and responsible for implementation. Acute manpower shortage is another factor preventing Islamic financial industry to become truly Shariah compliant. Moreover there is an urgent need to develop a fully complaint accounting and auditing framework for Islamic financial industry. The IFSB and AAOIFI can play a major role in this respect. As a start all the Islamic financial institutions should adopt completely all the standards of these institutions. Simultaneously the shortage of required Shariah compliant professionals should be met on war footings through establishment of more and more educational and training institutions.

Keywords: Shariah framework, Standards, Shariah compliant professionals, Shariah education training.

1- Introduction (Shorten)

A significant trend in global finance over the last 15 years has been the rapid growth of Islamic banking and finance (IBF), which has gathered momentum to become a significant feature of the financial landscape in the twenty-first century (Pollard & Samers, 2007) “However, a complete Islamic financial system with identifiable instruments and markets is still at an early stage of evolution. Many problems and challenges relating to Islamic instruments, financial markets, and regulation must be addressed and resolved” (Zaheer & Hassan, 2001). The recent economics and financial crises also attracted western countries towards this unique system which create real economies instead of bubble economies. “The world economy is still suffering from the severe global financial crisis that caused the failure of several banks. This has encouraged economists worldwide to consider alternative financial solutions and attention has been focused on Islamic banking and finance as an alternative model” (Rosman et al, 2013).

Today at a time of economic and financial crises, it is high time that it will be revamped present business and management theories, principles and practices completely in line with Islamic principles in order to end the sufferings of world masses and to mend our severed relationship with Allah. The love and fear of Allah is the foundation of all wisdom and this should be the basis for all business theories and principles, that seek to guide human endeavor.

The present financial system based on interest is largely responsible for the economic and financial crises which the world has faced from time to time. Interest should not be considered merely as a fixed addition to the principal amount; rather it includes all unjustified increments arising out of transactions prohibited under the teachings of Islam. The present financial system by nature promotes speculative business. This is mainly facilitated through creation of money by financial institutions and investment in stock markets without any reference to creation of value through producing more and more goods and services. This results in bubble economies which in

turn lead to economic crises such as it has been witnessed recently. The concept of “*riba*” is very comprehensive and as such is strictly prohibited in all its forms. It is the main difference between Islamic Banking and Finance and conventional banking and finance. In Islamic Finance, “Riba or Usury is a foundational concept that differentiates Islamic Banking from conventional banking. Among other principles of Islamic banking and finance, Riba needs a thorough understanding as it has many types and unless a careful analysis is done” (Yurizk, 2013). Present era is of revival of Islam in all over the world. The desire of Muslim Ummah for Islamization for society is increasing day by day. In addition to Muslim Ummah, the non-Muslim are also keen to study Islam. Their interest has specially been increased after the event of 9/11.

Islamic financial industry has made land mark achievements in terms of growth and creating awareness generally among the masses of the world and in particular in Muslim population in the last few years. According to Global Islamic Finance Report 2012, the size of Islamic banking industry has grown to 1.35 trillion US. Dollars with an annual growth of 20%. (GIFR, 2012). Presently 430 Islamic Banks financial Institutions and around 191 conventional banks having Islamic banking windows are operating in more than 75 countries .

Unfortunately our efforts so far, have been devoted to develop some unlawful/undesirable western commodities making their acceptability through Islamic coating. It is the main reason for the failure (Amer, 2007).It is not wise to reshape the present conventional financial system based on *riba* as Islamic through coating instead of evolving a financial system of our own following the teachings of the Quran and Sunnah. The Almighty Allah advised us in “*Surah*” Al-Hajj, Verse 78 of the Quran as “And strive hard in Allah's cause as you ought to strive (with sincerity and with all your efforts that His Name should be superior).

2- Literature Review

It is a matter of disappointment that so far it has failed to win the full confidence of the majority of Muslims that the Islamic financial industry is meeting 100 percent criteria of Shariah compliance. Justice Muhammad Taqi Usmani (2000), one of top most internationally known scholar on Shariah and Islamic Finance has pointed out the following weakness in the Islamic banks.

- Firstly, the basic philosophy of Islamic banking seems to be totally neglected.
- Secondly, by ignoring the instrument of “*musharakah*” the Islamic banks are forced to use the instrument of “*murabaha*” and “*Ijarah*” and these too, within the framework of the conventional benchmarks like Libor etc. where the net result is not materially different from the interest based transactions.
- Thirdly, when people realize that income from in the transactions undertaken by Islamic banks is dubious akin to the transactions of conventional banks, they become skeptical towards the functioning of Islamic banks.
- Fourthly, if all the transactions of Islamic banks are based on the above devices it becomes very difficult to argue for the case of Islamic banking before the masses especially, before the non-Muslims who feel that it is nothing but a matter of twisting of documents only.
- Fifthly, the Islamic banking is based on principles different from those followed in conventional banking system. It is therefore, logical that the results of their operations are not necessarily the same in terms of profitability.
- Sixthly, according to the Islamic principles, business transactions can never be separated from the moral objectives of the society.

- Lastly, the Islamic banks should develop their own culture. Obviously, Islam is not restricted to the banking transactions. It is a set of rules and principles governing the whole human life.

The above discussion not only reflect the present status of Islamic banking and finance in terms of accounting, auditing and governance issues within the frame work of Islamic Shariah but also highlight the need of rigorous efforts in this respect.

“Islamic Financial institutions (IFIs) all over the world are generally using the similar modes of Islamic finance and products, with minor differences of nomenclature according to their regional, legal and other conditions. The commonly used modes are “*Murabaha*”, “*Ijarah*”, “*Musharaka*”, “*Mudarabah*”, Diminishing “*Musharaka*”, “*Salam*”, “*Istisna*”, “*Wakalah*” and “*Kafalah*” etc. There is no difference of opinion among Shariah scholars of the world about permissibility of these modes. However, there are certain differences in application and modus-operandi of the transactions based on some of the above modes in different countries” (State Bank of Pakistan, 2013). Presently there are different Muslim regulating bodies which are not only responsible for making rules, regulations, procedures and standards for Islamic banking and finance under Islamic Shariah but also suppose to regulate the Islamic financial business.

Accounting and Auditing organization for Islamic Financial Institutions is responsible for accounting, auditing, Shariah and governance standards. The Islamic Financial Service Board is mainly responsible for Risk management and governance aspect of Islamic financial industry. “The Islamic Financial Services Board (IFSB) is an international standard-setting organization that promotes and enhances the soundness and stability of the Islamic financial services industry by issuing global prudential standards and guiding principles for the industry, broadly defined to include banking, capital markets and insurance sectors” (IFSB, 2013). In this respect IFSB has issued 15 Standards and 1 exposure draft.

The Accounting and Auditing Organization for Islamic Financial Institutions prepares accounting, auditing, Shariah and governance standards for Islamic financial industry. “The Accounting and Auditing Organization for Islamic Financial Institutions(AAOIFI) is an Islamic international autonomous non-for-profit corporate body that prepares accounting, auditing, governance, ethics and Shariah standards for Islamic financial institutions and the industry” (AAOIFI, 2013).

The basic modes of Islamic finance are “*Musharakah*” and “*Mudarabah*”. “*Salam*” and “*Istisna*” can also be used as mode of finance and simultaneously as mode of sale in certain situations with certain conditions. In addition “*murabahah*” and “*Ijarah*” are not mode of Islamic finance but can be used as financing the business activities.

Most of the Islamic financial institutions largely used “*murabahah*” as financing the business activities. Similarly “*Ijarah*” is also widely used by the Islamic financial institutions as financing the business activities. Mostly audit and Shariah compliance issues are related to “*murabahah*” and “*Ijarah*” as these are not mode of Islamic finance and therefore, a lot of “*Shariah*” injunctions are involved in implementing these in financing the business activities by Islamic financial institutions.

Every Islamic financial institution has a Shariah board or advisor who validate the modes of financing and deposits. They also supervise these activities generally. Then there is “*Shariah*” audit, both internal and external. However, mostly the Shariah non compliance issues arises at the time of executing the transactions by the employees of the Islamic financial institutions as by and large they are not capable to handled these. The Islamic financial industry Shariah boards or advisor are not a part of management and board of directors. They issue “*fatawa*” to validate different schemes, carry out Shariah review audit and issue reports. By default they don't take the responsibility of implementing their fatawa. Further in most of the cases the members of

these boards are handicapped either due to lack of knowledge of accounting & auditing or Shariah.

The law making and regulating agencies of the countries like central banks and corporate law or security commission or authority are presently are the main icons to supervise, monitor and regulate the Islamic financial industry. On the one hand they are playing a positive role in the context. But on the other hand these are hazards in adopting the rules, regulations, procedures and standards of specialized international organizations like IFSB and AAOIFI to get purity in the Islamic financial services to win the hearts of Muslims in terms of their satisfaction and 100 percent Shariah compliance.

Another important issue in terms of audit and Shariah compliance is related to general state of affairs of accounting profession which is presently itself under severe criticism. Its lacks the Islamic concept of accountability, '*Amanah*', '*Shahadat*', '*Shura*', '*Al-adal*' and '*Al-Ihsan*'.

The points as discussed above are some of the very crucial issues for getting truly hundred percent "Shariah" complaint Islamic financial industry. Without addressing these points the audit and "Shariah" issues in Islamic banking and finance cannot be addressed. It should remember that even a drop of "*riba*" in any manner in business transactions can make these "*haram*".

The following are some basic differences between Islamic Banking and Conventional Banking. (Ahmed & Hassan,)

Conventional banking	Islamic banking
1. The functions and operating modes of conventional banks are based on man-made principles.	1. The functions and operating modes of Islamic banks are based on the principles of Islamic <i>Shariah</i> .
2. The investor is assured of a predetermined rate of interest.	2. In contrast, it promotes risk sharing between provider of capital (investor) and the user of funds (entrepreneur).
3. It aims at maximizing profit without any restriction.	3. It also aims at maximizing profit but subject to <i>Shariah</i> restrictions.
4. It does not deal with <i>zakah</i> .	4. In the modern Islamic banking system, it has become one of the service-oriented functions of the Islamic banks to collect and distribute <i>zakah</i> .
5. Lending money and getting it back with interest is the fundamental function of the conventional banks.	5. Participation in partnership business is the fundamental function of the Islamic banks.
6. Its scope of activities is narrower when compared with an Islamic bank.	6. Its scope of activities is wider when compared with a conventional bank. It is, in effect, a multi-purpose institution.
7. It can charge additional money (compound rate of interest) in case of defaulters.	7. The Islamic banks have no provision to charge any extra money from the defaulters.
8. In it very often, bank's own interest becomes prominent. It makes no effort to ensure growth with equity.	8. It gives due importance to the public interest. Its ultimate aim is to ensure growth with equity.
9. For interest-based commercial banks, borrowing from the money market is relatively easier.	9. For Islamic banks, it is comparatively difficult to borrow money from the money market.
10. Since income from the advances is fixed, it gives little importance to	10. Since it shares profit and loss, Islamic banks pay greater attention to developing

developing expertise in project appraisal and evaluations.	project appraisal and evaluations.
11. Conventional banks give greater emphasis on credit-worthiness of the clients.	11. Islamic banks, on the other hand, give greater emphasis on the viability of the projects.
12. The status of a conventional bank, in relation to its clients, is that of creditor and debtors.	12. The status of Islamic bank in relation to its clients is that of partners, investors and trader.
13. A conventional bank has to guarantee all its deposits.	13. Strictly speaking, an Islamic bank cannot guarantee all its deposits.

On the basis of above comparison, in addition to our faith as a Muslim, it can be easily concluded that Islamic banking and finance entirely different from conventional banking and finance. There are several dimensions of these differences. Importantly some of these include:

- 1-Basic Philosophy
- 2- Operation
- 3- Governance
- 4- Laws, Rules, Regulations and Procedures.
- 5- Accounting
- 6- Auditing.

And most importantly the bench mark is Shariah approval and compliance. Actually this aspect is directly related to our faith as a Muslim. It is a matter of life and death for a Muslim. The success in this world and hereafter depends on this. The “*Riba*” in all its forms is “haram” a great sin. (e.g. Quran “*aya*” Surah/Chapter 002 - Al-Baqarah. Verse 275, Surah/Chapter 002 - Al-Baqarah. Verse 276, Surah/Chapter 002 - Al-Baqarah. Verse 278, Surah/Chapter 002 - Al-Baqarah. Verse 279, Surah/Chapter 003 - Al-Imrân. Verse 130, Surah/Chapter 004 - An-Nisâ. Verse 161 and Hadith Bukhari :: Book 3 :: Volume 48 :: Hadith 841, Bukhari :: Book 8 :: Volume 82 :: Hadith 840 and Dawud :: Book 22 : Hadith 3327.

Shariah should be our bench mark for evolving a financial system. Unfortunately, so for the focus of our efforts are to make some how the conventional financial system acceptable through Islamic coating. So there is a need to change our direction. “This situation needs serious consideration of the players in the field and of the Shariah scholars who oversee the new products for Islamic financial Institution. Many conferences and seminars are being held frequently to consider various aspects of Islamic finance. I think it is high time now to find out ways and means to make our products not only compliant with, but also founded on Shariah” (Usmani,2013).

3- Shariah Framework for Islamic Banking and Finance

Presently Islamic financial intuitions are trying to follow a set of accounting, auditing, governance, risk management, rules, regulations, procedures, guide lines and standards etc. to make its operations Shariah compliant. Prominently these include the following:

3-I Issued by the Central Banks/Regulatory Authorities. of a Country.

These are the guide lines which are issued by the central bank and regulatory authority of a Muslim country. For example State Bank of Pakistan (2008) has issued “Guidelines for Shariah Compliance in Islamic Banking Institutions (IBIs)”. Which deals with Shariah compliance, Shariah Internal Audit, Investment in shares, Policy for Profit Distribution, Guidelines for Islamic Micro Finance, which deals with Murabaha Facility Agreement, “*Musawamah*”

Facility Agreement, Lease Agreement, Salam Agreement, Musharaka Investment Agreement, Istisna Agreement, Agreement for Interest free Loan, Mudarabah Financing Agreement and Syndication “*Mudarabah*” Agreement. Other documents include Guidelines on Islamic Financing for Agriculture, Islamic Export Refinance Scheme, Guidelines for **Islamic** Microfinance Business by Financial Institutions, Risk Management Guidelines for Islamic Banking Institutions and Instructions and Guidelines for Shariah compliance.

The Security Exchange Commission of Pakistan (SECP) has issued Mudarabah Companies and Mudarabah (Floatation and Control) Ordinance, 1980, Mudarabah Companies and Mudarabah Rules, 1981, Guidelines for Issue of Certificate of Musharakah for Mudarabah, Takaful Rules, 2005 and Private Equity & Venture Capital Fund Regulations, 2008.

Similarly the Bank Negara Malaysia, the central Bank of Malaysia, has issued 2nd edition of “Shariah Resolutions in Islamic Finance” which deals in all respect of Islamic finance like “*Ijarah*”, “*Istisna*”, “*Mudarabah*”, “*Musharaka*”, “*Qard*”, “*Rahn*”, “*Takaful*”, Financial Derivative Instruments, Islamic Credit Card and “*Shukuk*”.

Likewise other Muslims countries have their own monetary and regulatory authorities to deal the business of Islamic finance. Some of these details are as under :.(More details are at Table-1)

Bahrain	Regulated by the Bahrain Monetary Agency (BMA)
Gambia	Regulated by the Central Bank of Gambia(CBG)
Indonesia	Regulated by the Central Bank of Indonesia (Bank Sentral Republik Indonesia –BSRI)
Iran	Regulated by the Central Bank of Iran (Bank Jamhuri Islami Iran)
Jordan	Regulated by the Central Bank of Jordan (CBJ) ♦Separate regulatory bodies for banks and securities firms
Kuwait	Supervised by the Central Bank of Kuwait (CBK)
Qatar	Regulated by the Central Bank of Qatar (CBQ)
Sudan	Regulated by the Central Bank of Sudan (CBS)
Turkey	Regulated by the Central Bank of Turkey (Turkeyi Cumhuriyet Merkez Bankasi –TCMB) ♦ Banks and securities firms regulated by separate bodies
UAE	Regulated by the Central Bank of UAE
Yemen	Regulated by the Central Bank of Yemen (CBY)

3.2 International Regulating Bodies

In addition to countries own Islamic finance laws making and regulation agencies there exist a few International Institutions who are made responsible by the Islamic countries jointly to make, standards, rules, regulations and procedures for enforcing and regulating Islamic financial services in the Islamic countries. Let us discuss these institutions in some details:

3.2.1 Islamic Financial Service Board (IFSB)

“The Islamic Financial Services Board (IFSB), which is based at Kuala Lumpur, Malaysia was officially inaugurated on 3rd November 2002 and started operations on 10th March 2003. It serves as an international standard-setting body of regulatory and supervisory agencies that have vested interest in ensuring the soundness and stability of the Islamic financial services industry, which is defined broadly to include banking, capital market and insurance. In advancing this mission, the IFSB promotes the development of a prudent and transparent Islamic financial services industry through introducing new, or adapting existing international standards consistent

with “*Shariah*” principles, and recommend them for adoption. To this end, the work of the IFSB complements that of the Basel Committee on Banking Supervision, International Organization of Securities Commissions and the International Association of Insurance Supervisors. As at December 2012, the 184 members of the IFSB comprise 55 regulatory and supervisory authorities, eight international inter-governmental organizations and 121 market players, professional firms and industry associations operating in 41 jurisdictions” (IFSB)

IFSB has so far issued 15 Standards, 5 Guidance Notes and 1 Technical Note (Technical Note on Issues in Strengthening Liquidity Management of Institutions Offering Islamic Financial Services: the Development of Islamic Money Markets). The details are given at Table-4. The standards mainly relate to risk management and governance issues as applicable to Islamic Financial Institutions. The standards are both available in Arabic and English.

The IFSB is a highly profile Institution which prepare these standards aiming to fulfill Shariah criteria and ensuring compliance over financial transactions in terms of risk management and governance in Islamic financial Institutions. The organization is comprised of a council, a technical committee, working groups, task forces and editing committee. The IFSB has a fully functioned secretariat. (Details at Table 2&3)

On the face of it can be said that IFSB provide a strong Shariah frame work in terms of risk management and governance for Islamic financial institutions. However, there is a need to ensure the enforcement and compliance aspects of these standards.

3.2.2 Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI)

The Accounting and Auditing Organization for Islamic Financial Institutions was established on 27th March, 1991 in the State of Bahrain. It has a commendable strength of 200 members from 45 countries. The Accounting and Auditing Organization for Islamic Financial Institutions is responsible for preparing Shariah, accounting, auditing and governance standards for Islamic financial institutions. According to AAOIFI web site these standards has been adopted in the Kingdom of Bahrain, Dubai International Financial Centre, Jordan, Lebanon, Qatar, Sudan and Syria. The countries like Indonesia, Malaysia, Pakistan, Kingdom of Saudi Arabia, and South Africa have issued guidelines based on these standards and pronouncements. Another notable contribution of the institution is human resource development in the Islamic finance.

So far AAOIFI has issued 48 Shariah, 26 accounting, 5 auditing, 7 governance and 2 ethics standards. These standards are both in Arabic and English. The organization provides a comprehensive Shariah, accounting, auditing and governance frame work for Islamic financial institutions. Ideally the Islamic financial institutions should formulate and adopt the accounting and auditing policies, procedures and practices in lines and compliance with these standards instead of conventional standards. However, the state of affairs in this respect is different.

3.3 Institutions Based Supervisory “*Shariah*” Board/Advisor

Every Islamic bank or financial institution has supervisory board or an advisor to guide and supervise the business. “The Islamic banks are distinct from other banks by several characteristics; perhaps most notable is its compliance with Shariah and its principles in all banking operations and activities. This commitment can be translated by the establishment of Shariah supervisory system in Islamic banks” (Kuwait Finance House, 2014). It is the most important characteristic of Islamic banks that distinguishes them from conventional banks. Their main functions of are listed below:

1. Making the Islamic products/investments Shariah compliant.
2. Issuing fatawa to satisfy stakeholders that the products/investments are Shariah compliant.

3. Guiding and supervising the institution to ensure Shariah compliance.
4. Training the employees of the institution.
5. Carrying out inspection to ensure Shariah compliance.
6. Issuing review reports.

A few issues are related to the composition and functioning of such boards. First of all normally the board members either have the knowledge of '*Shariah*' or finance. In rear cases the board members have the complete knowledge of both of these two.

Further as a common issue of corporate governance, such boards may lack independence. "Banks commonly appoint prestigious scholars to their Shariah boards and pay them handsome fees and retainers. This has left the system vulnerable to charges of conflict of interest: the scholars are being paid by the institutions which they are supposed to be supervising impartially (Arabian Gazette, 2011).

In my opinion there is also a structural and organizational issue of such boards which isolate them from the core management stream and therefore, they have no control or grip over the operation of the Islamic financial institutions. In this way the Shariah compliance may not be achievable up to 100 percent level which is mandatory as per Islamic teachings. The Shariah Board normally issued Fatawa as a degree to validate an investment or deposit or Islamic finance scheme as Shariah compliant. It is important to note that in such Fatawa normally it is said that "this approval is subject to implementation of the transaction in strict compliance with the above approved structure, documentation and the process as explained to us (Table-5).

Implementing the fatwa is the main essence of an Islamic financial transaction. However, there may be a big question mark in respect of implementing the fatawa as approved. This may be a great challenge. Simply inspection or periodic review by the Shariah boards cannot fully serve the purpose. In order to overcome such issues it is suggested that the Shariah Board or Advisor may be made a constituent part of Board of Directors so that it can be a part of management and also responsible for implementation of modes of Islamic finance.

Here the experience of an external Shariah auditor and inspector (Ansari, 2013) is shared which leaves a big question mark on the effectiveness and independence of Supervisory Shariah Board/Advisor.

As External Auditor

1. Management is of the view that it has nothing to do in respect of Shariah compliance (Even if I feel that it has something to do with the Objects of the Bank / Mudarabah).
2. Even if it has some evidences in hand, coupled with some sort of research work, it is told that the Shariah Advisor is the final authority. It has been independent, and without any disregard, he is a paid employee and a party to the transaction as he approved it).
3. Top management and Shariah Advisor, are on my side, but the middle level management makes all efforts to fail the exercise.
4. All are bound to follow the advice of the Shariah Advisor, without any opportunity of being heard at any independent forum.

As '*Shariah*' Compliance Inspector

1. Management of the bank under inspection makes all efforts that either no inspection be carried out or if an inspection is inevitable, then it should remain limited to whatever Shariah Advisor has approved.
2. Shariah Advisor becomes a party along with the management, as he has approved the transactions and issued a clean Shariah review report.

3. SBP's management is not sure as to what extent it may interfere into the matters of the Bank with respect to Shariah compliance.
4. SBP's management changes its decisions with regard to the scope of inspection and the responsibility for inspection within various departments.
5. SBP's Shariah board includes a member who was the Government's advocate in the case against the declaration of bank's interest as Haram, and another member, who is on a number of Shariah boards and Shariah Advisor of a Bank whose independence from this perspective is not ensured.

4- Findings

There is no doubt that a primary Shariah frame work in the shape of standards and Fatawa of Islamic financial institutions exist but there is a problem with its implementation. In the first instance these standards are not being applied by all the Islamic financial institutions. A few countries like Sudan, Syria and Bahrain have adopted the Shariah Standards issued by the AAOIFI. Mostly the Islamic financial institutions have their own Supervisory Shariah Advisory Boards or Advisors who oversee and responsible for audit and Shariah compliance. In many cases the members of these boards have not the knowledge of both '*Shariah*' and finance. Then such boards are not a part of management of Islamic financial Institutions. As a common governance problem, such board may lack independence in their decisions.

The Accounting and Auditing Organization for Islamic financial institutions has introduced a complete set of international accounting and auditing standards for Islamic financial Institutions. As a policy these standards should replace National Standards, IFRS and Standards based on GAAP. However, except for a few countries, these have not been adopted.

The third issue is that there is no accounting theory based on Islamic teachings. The present conventional accounting is its self under fire, which as it has been seen, is in conflict with Shariah. Non existence of accounting theory and non adoption of AAOIFI standards plays a big question mark on Shariah compliance by the Islamic financial institutions.

The same is the case with the auditing procedures and auditing standards adopted by the Islamic financial institutions. Most of the financial institutions have not adopted the auditing procedures and standards issued by AAOIFI. Then the in-competence in Shariah and audit by both internal and external auditors carries a big question mark.

Then the Islamic financial industry is facing a cute shortage of manpower in all areas including finance, accounting, auditing, management, marketing, human resource development & management, banking, governance, commercial laws, regulating, master training, capacity building and institutional development etc. Without "Shariah' compliant professionals" in these areas, the issues in auditing and Shariah in Islamic financial industry cannot be resolved completely.

There is a lack of confidence and coordination between international and national law makers and regulating authorities. For example it was the duty of central banks to prevail upon the Islamic financial intuitions to adopt all the standards issued by AAOIFI as now State Bank of Pakistan has adopted a policy to impose Shariah Standards on Islamic banking slowly and gradually. For this purpose necessary amendments in relevant laws should be made. However, it appears that the central banks don't want to forgo their supremacy. Actually the affairs of Islamic financial institutions should be made 100 percent 'Shariah" complaint. In Islam there is no concept of less or more haram. In '*Shariah*' a thing is 100 percent haram (not permissible) or '*halal*' (permissible).

5- Conclusion and Recommendations

A big question in front of Muslim *‘Ummah’* is that why we do not take our own start through copying Sahabah (Razi Allahu un-huma) and Caliphs. As have said in earlier submissions (August, 2007), “Our aim should be to develop different disciplines which ultimate replace present theories and practices in the “exploitation oriented business world” so that the non Muslim may also be benefited. It may not use the words like Islamic finance, Islamic accounting, Islamic marketing, Islamic trade and management etc. Our work should be of such nature that the non- Muslim world should be obliged to embrace these disciplines similar to present situation that we have adopted their theories and practices”.

So our first step in this respect should be to develop a complete accounting and auditing framework for Islamic financial industry totally based on Islamic teachings. The IFSB and AAOIFI can play a major role in this respect. As a start all the Islamic financial institutions should adopt completely all the standards of these institutions.

Secondly necessary legislation may be done by the Muslim countries to make it binding by all the parties. Riba based transactions may completely be banned in the Muslims countries. For international transactions with the non- Muslim countries a workable mechanism can be evolved in the light of Shariah.

Thirdly side by side it should produce such professional who carry out different business assignments as discussed earlier. Especially the managers, accountants and auditors should be completely Shariah compliant professional.

Fourthly the Shariah board should be made a constituent part of management and board of directors.

As final words here it can be reminded followers of Quran to lead the depressed humanity to a prosperous future through Its guidance and practice as being ordered:

“And strive hard in Allah's Cause as you ought to strive (with sincerity and with all your efforts that His Name should be superior). He has chosen you (to convey His Message of Islamic Monotheism to mankind by inviting them to His religion, Islam), and has not laid upon you in religion any hardship, it is the religion of your father Ibrahim (Abraham) (Islamic Monotheism). It is He (Allah) Who has named you Muslims both before and in this (the *Qur'an*), that the Messenger (Muhammad SAW) may be a witness over you and you be witnesses over mankind! So perform AsSalat (Iqamat-as-Salat), give Zakat and hold fast to Allah [i.e. have confidence in Allah, and depend upon Him in all your affairs] He is your Maula (Patron, Lord, etc.), what an Excellent Maula (Patron, Lord, etc.) and what an Excellent Helper!”

(Surah Al-Hajj:: Verse 78)

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----- Appendices

Appendix Table # 1. Summary of Salient Features of Islamic Banking and Supervisory Systems in Some Member Countries

Country	Salient Features of Islamic Banking Supervisory Systems
Bahrain	Regulated by the Bahrain Monetary Agency (BMA) ♦ BMA regulates both commercial banks and investment banks (securities firms); insurance companies are under separate regulatory authority ♦ Dual banking (Islamic and conventional) banking system; Basel capital requirements and core principles adopted for both groups, ♦ Four Islamic banking groups: a) Islamic commercial banks, b) Islamic investment banks, c) Islamic Offshore banks, and d) Islamic banking windows in conventional banks ♦ Consolidated supervision ♦ International Accounting Standards adopted, ♦ Each Islamic bank must have a <i>Sharī'ah</i> board ♦ Compliance with AAOIFI standards under active consideration ♦ Investment deposits, current accounts and capital allocation for assets must be declared, ♦ Mandatory liquidity management by adopting the standardized
Gambia	Dual system ♦ Separate <i>Sharī'ah</i> board required ♦ Compliance with Basel capital requirements and core principles and International Accounting Standards not clear
Indonesia	Regulated by the Central Bank of Indonesia (Bank Sentral Republik Indonesia –BSRI) ♦ Separate regulatory bodies for banks and securities firms ♦ Separate Islamic banking law does not exist; Islamic (<i>Sharī'ah</i>) banking is covered by added section in the banking law (Act No. 10 1998 and Act No. 23 1999) ♦ Separate <i>Sharī'ah</i> board required ♦ Islamic windows allowed ♦ Consolidated supervision ♦ Basel capital requirements and core principles adopted ♦ International Accounting Standards adopted ♦ Major financial transformation in process to strengthen bank capital and solvency ♦ Active <i>Sharī'ah</i> bank development strategy in place by them government.
Iran	Regulated by the Central Bank of Iran (Bank Jamhuri Islami Iran) ♦ All banks in the public sector with a plan for minority privatisation ♦ Bank regulation and supervision is strongly effected by monetary as well as fiscal and other government policies ♦ Single (Islamic) banking system under the 1983 Usury Free Banking Law ♦ Modes of finance are defined by this Law ♦ Recent policy orientation towards adopting the Basel capital and supervisory standards and International Accounting Standards

	<p>◆No <i>Sharī'ah</i> board for individual banks ◆Onsite and offsite supervisory methods and objectives defined and applied ◆ Banks and insurance companies are supervised by different regulatory authorities.</p>
Jordan	<p>Regulated by the Central Bank of Jordan (CBJ) ◆Separate regulatory bodies for banks and securities firms◆ Islamic banking law exists ◆ Dual system ◆ Separate <i>Sharī'ah</i> board required ◆ Consolidated supervision◆ Basel capital requirements and core principles adopted ◆ International Accounting Standards adopted.</p>
Kuwait	<p>Supervised by the Central Bank of Kuwait (CBK) ◆ CBK regulates both commercial banks and investment banks (securities firms); insurance companies are under separate regulatory authority ◆ Dual banking system ◆ Two Islamic banking groups: a) Islamic commercial banks, and b) Islamic investment banks. Conventional banks not allowed to have Islamic banking windows. ◆ Consolidated supervision ◆ Basel capital requirements and supervisory standards adopted ◆ International Accounting Standards adopted ◆ Separate Islamic banking law under active consideration ◆ Separate <i>Sharī'ah</i> board for each bank necessary</p>
Malaysia	<p>Regulated by the Central Bank of Malaysia (Bank Negara Malaysia – BNM) ◆Insurance companies and banks under same regulatory authority; securities firms under separate authority ◆ Private banks ◆ Dual banking system ◆ Islamic windows allowed in conventional banks ◆ Consolidated supervision◆ Basel capital requirements and core principles adopted ◆ International Accounting Standards adopted ◆ CAMELS rating system adopted ◆ Onsite and offsite supervision well defined with clear objectives ◆ Separate <i>Sharī'ah</i> boards at institutional level in the BNM and Securities Exchange Commission ◆Islamic money market and liquidity arrangement exists ◆ Ministry of Finance closely associated with the supervision of Islamic banks.</p>
Pakistan	<p>Regulated by the Central Bank of Pakistan (State Bank of Pakistan-SBP) ◆Securities firms, and Insurance Companies are regulated by separate regulatory bodies ◆ Major banks in the Public Sector; bank regulation and supervision effected by government policies ◆ Islamic banking law does not exist ◆<i>Mudārabah</i> Companies Law exists ◆<i>Sharī'ah</i> board concept does not exist ◆Islamic banks are not identified distinctly ◆ Basel capital requirements and supervisory standards adopted ◆ Bank merger is on cards to strengthen capital ◆Concept of onsite and offsite supervision exists ◆ Major financial transformation is called for by the Supreme Court of Pakistan to introduce Islamic banking and financial system; a Financial Services Transformation Committee has been established by the SBP.</p>
Qatar	<p>Regulated by the Central Bank of Qatar (CBQ) ◆ Dual banking and separate regulatory system ◆No separate Islamic banking law exists ◆Islamic banks supervised by special directives of CBQ ◆ Separate <i>Sharī'ah</i> boards for banks required ◆ Standardised transparency requirements for Islamic banks exist</p>
Sudan	<p>Regulated by the Central Bank of Sudan (CBS) ◆ Single (Islamic) system ◆Islamic banking law in place◆Separate <i>Sharī'ah</i> boards for banks required, also the Central Bank has a <i>Sharī'ah</i> Supervisory Board◆</p>

	Substantial public sector control; supervision and regulation is effected by other government policies ♦ Evolution of financial instruments underway ♦ Compliance with the capital adequacy and supervisory oversight standards of the Basel Committee not clear ♦ Major bank merger is planned to strengthen bank capital
Turkey	Regulated by the Central Bank of Turkey (Turkeyi Cumhuriyet Merkez Bankasi –TCMB) ♦ Banks and securities firms regulated by separate bodies ♦ Law about Special Finance Houses covers Islamic banks ♦ Dual system; no Islamic windows allowed ♦ Basel Committee capital adequacy requirements and supervisory standards recently introduced ♦ Major financial transformation underway ♦ Onsite and offsite supervision concepts and methods exist
UAE	Regulated by the Central Bank of UAE ♦ Islamic banking law exists ♦ Dual system ♦ Islamic banking windows allowed ♦ Separate <i>Sharī'ah</i> boards required ♦ Basel Committee capital adequacy requirements and supervisory standards in place ♦ International Accounting Standards in place
Yemen	Regulated by the Central Bank of Yemen (CBY) ♦ Islamic banking law exists ♦ Dual system ♦ Islamic banking windows allowed ♦ Separate <i>Sharī'ah</i> board required ♦ Major policies and standards set by the CBY are equally applicable to all banks ♦ Separate supervisory office for Islamic banks inside the CBY under active consideration ♦ Compliance with the Basel standards not clear

Source-(Chpra&Khan, 2000)

Table : 2. Islamic Financial Service Board : List of Full Members

No.	Organisation	Country	Membership Type
1.	Autoriti Monetari Brunei Darussalam	Brunei	Full Member
2.	Bangladesh Bank	Bangladesh	Full Member
3.	Bank Al-Maghrib	Morocco	Full Member
4.	Bank Indonesia	Indonesia	Full Member
5.	Bank Negara Malaysia	Malaysia	Full Member
6.	Bank of Mauritius	Mauritius	Full Member
7.	Banque Centrale De Djibouti	Djibouti	Full Member
8.	Capital Market Authority	Oman	Full Member
9.	Capital Markets Authority	Kuwait	Full Member

10.	Central Bank of Bahrain	Bahrain	Full Member
11.	Central Bank of Egypt	Egypt	Full Member
12.	Central Bank of Jordan	Jordan	Full Member
13.	Central Bank of Kuwait	Kuwait	Full Member
14.	Central Bank of Nigeria	Nigeria	Full Member
15.	Central Bank of Sudan	Sudan	Full Member
16.	Central Bank of the Islamic Republic of Iran	Islamic Republic of Iran	Full Member
17.	Central Bank of the United Arab Emirates	United Arab Emirates	Full Member
18.	Dubai Financial Services Authority	United Arab Emirates	Full Member
19.	Insurance Authority	United Arab Emirates	Full Member
20.	Islamic Corporation for the Development of the Private Sector	International Inter Governmental Organizations	Full Member
21.	Islamic Corporation for the Insurance of Investment and Export Credit	International Inter Governmental Organizations	Full Member
22.	Islamic Development Bank	International Inter Governmental Organizations	Full Member
23.	Maldives Monetary Authority	Maldives	Full Member
24.	Monetary Authority of Singapore	Singapore	Full Member
25.	National Insurance Commission	Nigeria	Full Member
26.	Qatar Central Bank	Qatar	Full Member
27.	Saudi Arabian Monetary Agency	Saudi Arabia	Full Member
28.	Securities and Exchange Organization	Islamic Republic of Iran	Full Member

29.	Securities Commission of Malaysia	Malaysia	Full Member
30.	State Bank of Pakistan	Pakistan	Full Member

Source IFSB (2013)

Table --- 3. Islamic Financial Service Board Council Members

Chairman H.E. Sheikh Abdulla Saoud Al-Thani Governor Qatar Central Bank	Deputy Chairman H.E. Dato Mohd Rosli Sabtu Managing Director Autoriti Monetari Brunei Darussalam
H.E. Rasheed M. Al-Maraj Governor Central Bank of Bahrain	H.E. Dr. Atiur Rahman Governor Bangladesh Bank
H.E. Djama Mahamoud Haid Governor Banque Centrale De Djibouti	H.E. Hisham Ramez Abdel Hafez Governor Central Bank of Egypt
H.E. Dr. Darmin Nasution Governor Bank Indonesia	H.E. Dr. Mahmoud Bahmani Governor Central Bank of the Islamic Republic of Iran
H.E. Dr. Darmin Nasution Governor Bank Indonesia	H.E. Dr. Mahmoud Bahmani Governor Central Bank of the Islamic Republic of Iran
H.E. Dr. Ahmad Mohamed Ali President Islamic Development Bank	H.E. Dr. Ziad Fariz Governor Central Bank of Jordan
H.E. Dr. Mohammad Y. Al Hashel Governor Central Bank of Kuwait	H.E. Abdellatif Jouahri Governor Bank Al-Maghrib
H.E. Dr. Zeti Akhtar Aziz Governor Bank Negara Malaysia	H.E. Dr. Fazeel Najeeb Governor Maldives Monetary Authority
H.E. Rundheersing Bheenick Governor Bank of Mauritius	H.E. Sanusi Lamido Aminu Sanusi Governor Central Bank of Nigeria
H.E. Yaseen Anwar Governor State Bank of Pakistan	H.E. Dr. Fahad Al-Mubarak Governor Saudi Arabian Monetary Agency
H.E. Ravi Menon Managing Director Monetary Authority of Singapore	H.E. Dr. Mohamed Khair Ahmed Elzubeat Governor Central Bank of Sudan
H.E. Sultan bin Nasser Al Suwaidi Governor Central Bank of the United Arab Emirates	

Source IFSB Website (2013)

----Table --- 4. Islamic Financial Service Board Issued Standards

No	Title of Standard	Date of Issue
1	Guiding Principles of Risk Management for Institutions (other than Insurance Institutions)	December 2005
2	Capital Adequacy Standard for Institutions (other than Insurance Institutions)	December 2005
3	Guiding Principles on Corporate Governance for Institutions offering only Islamic Financial Services (Excluding Islamic Insurance (Takâful) Institutions and Islamic Mutual Funds)	December 2006
4	Disclosures to Promote Transparency and Market Discipline for Institutions offering Islamic Financial Services (excluding Islamic Insurance (Takâful) Institutions and Islamic Mutual Funds)	December 2007
5	Guidance on Key Elements in the Supervisory Review Process of Institutions offering Islamic Financial Services (excluding Islamic Insurance (Takâful) Institutions and Islamic Mutual Funds)	December 2007
6	Guiding Principles on Governance for Islamic Collective Investment Schemes	December 2008
7	Capital Adequacy Requirements for Sukûk, Securitisations and Real Estate investment	January 2009
8	Guiding Principles on Governance for Takâful (Islamic Insurance) Undertakings	December 2009
9	Guiding Principles on Conduct of Business for Institutions offering Islamic Financial Services	December 2009
10	Guiding Principles on Sharîah Governance Systems for Institutions offering Islamic Financial Services	December 2009
11	Standard on Solvency Requirements for Takâful (Islamic Insurance) Undertakings	December 2010
12	Guiding Principles on Liquidity Risk Management for Institutions offering Islamic Financial Services	March 2012
13	Guiding Principles on Stress Testing for Institutions offering Islamic Financial Services	March 2012
14	Standard On Risk Management for <i>Takâful</i> (Islamic Insurance) Undertakings	<i>December 2013</i>
15	Revised Capital Adequacy Standard for Institutions Offering Islamic Financial Services [Excluding Islamic Insurance (<i>Takâful</i>) Institutions and Islamic Collective Investment Schemes]	<i>December 2013</i>
Guidance Notes		
1	Guidance Note in Connection with the Capital Adequacy Standard: Recognition of Ratings by External Credit Assessment Institutions (ECAIs) on Sharî'ah-Compliant Financial Instruments	March 2008
2	Guidance Note in Connection with the Risk Management and Capital Adequacy Standards: Commodity Murâbahah Transactions	December 2010
3	Guidance Note on the Practice of Smoothing the Profits Payout to Investment Account Holders	December 2010
4	Guidance Note in Connection with the IFSB Capital Adequacy Standard: The Determination of Alpha in the Capital Adequacy Ratio	March 2011

	for Institutions (other than Insurance Institutions) offering only Islamic Financial Services	
5	Guidance Note on the Recognition of Ratings by external Credit Assessment Institutions (ECAIS) on Takâful and ReTakâful Undertakings	March 2011

Source IFSB Website (2014)

-----Table --- 5. Mashreq Al Islami Fatwa Resolution Extract

بسم الله الرحمن الرحيم
الحمد لله رب العالمين والصلاة والسلام على سيدنا محمد وعلى آله وصحبه أجمعين، وبعد ،،،

Mashreq Al-Islami
Shari'ah Supervisory Board Resolution Extract

المشرق الإسلامي
قرار هيئة الرقابة الشرعية

Subject: Murabaha Share Finance

الموضوع: [تمويل الأسهم بالمرابحة]

The Shari'ah Supervisory Board of Mashreq Al-Islami convened on the 6th of August 2006 corresponding to the 12th of Ragab 1427 H, in Dubai, United Arab Emirates and discussed the {Murabaha Share Finance Product} as presented by the Product Manager of the bank and duly reviewed by the bank's Shari'ah Governance Unit.

اجتمعت هيئة الرقابة الشرعية للمشرق الإسلامي في يوم 6 أغسطس 2006م الموافق 12 رجب 1427 هـ بمدينة دبي بدولة الإمارات العربية المتحدة وناقشت منتج [تمويل الأسهم بالمرابحة] الذي قدمه مدير المنتجات وراجعته وحدة الرقابة الشرعية بالبنك.

Now, therefore, in light of the detailed presentation on the product along with its underlying structure, documentation and the relevant supporting example, we the Shari'ah Supervisory Board of Mashreq Al-Islami, after carefully reviewing the case as presented have approved the product via Resolution No. [4]

إطلعت الهيئة على المقترح المقدم من إدارة البنك مصحوباً بالعقود التي تضبط المنتج، وبعد النقاش المستفيض والمراجعة من قبل أعضاء الهيئة؛ أجازت هيئة الرقابة الشرعية المنتج وفق قرارها رقم [4]

The product is bound under the Islamic transaction documents as follows:

على ان يستند تنفيذ المنتج على العقود الموضحة أدناه:

1. Agency Agreement to purchase shares
2. List of Shariah Compliant shares issued by Dow Jones or local industry committee
3. Master Murabaha agreement
4. Murabaha sale agreement

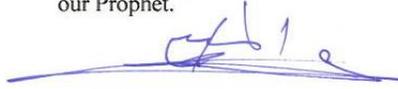
- 1- الوكالة لشراء الأسهم.
- 2- قائمة الأسهم المتوافقة وأحكام الشريعة الإسلامية التي تنشرها داو جونز أو لجنة المصارف.
- 3- عقد المرابحة الإطارى.
- 4- عقد البيع بالمرابحة

This approval is subject to implementation of the transaction in strict compliance with the above approved structure, documentation and the process as explained to us.

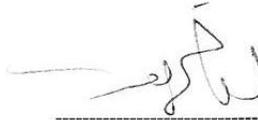
وقعت الهيئة على هذا القرار على أن يتقيد البنك في تنفيذ عمليات هذا المنتج بالشروط والأحكام والعقود الموضحة أعلاه.

May Allah help us all and prayer and peace be upon our Prophet.

والله المستعان وصلى الله على محمد وعلى آله وصحبه وسلم .



Sheikh Abdullah Al Mance
Chairman



Sheikh Nizam Yaquby
Member



Sheikh Dr. Mohammed Elgari
Member

Source- Mashreq Al Islami Fatwa Resolution Extract-Website(2013)