

*In the name of Allah the most
gracious the most merciful*

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Topic of the day

Shariah compliance and
supervision processes

Outline

1. Internal and External Audit on Shariah compliance & supervision processes.
2. Incorporation of audit on Shariah process in conventional banks offering Islamic finance services.
3. Suggestions and recommendations.
4. Conclusion

Internal & External Shariah Audit

Introduction

- General principles governing an audit of F. Ss prepared by a FI which conducts business in conformity with Islamic Shariah Rules and Principles. i.e. **Shariah Review**

Process

- The auditor plan and perform professional audit + competence + due care recognition.
- Evidences to support M. representations & not only assuming that they are correct.

Objective

- To enable the auditor to express an opinion as to whether the F. Ss are in accordance with the Shariah Rs & Ps, the Ac. Ss of the AAOIFI + national Ac. Ss and practices in the country

Shariah Review

➤ Definition and principles of Shariah review

Sh. R. is an examination of the extent of an IFI's compliance, in all its activities, with the Shariah. This examination includes;

- Agreements,
- Contracts
- Policies
- Products
- Transactions
- Memorandum and articles of association
- Financial statements
- Reports (internal audit and central bank inspection)
- Circulars etc. (*two types of Shariah Review*)

Internal Shariah review

1. The internal Shariah review is an integral part of the organs of governance of the IFI and operates under the policies established by the IFI.
2. It shall have a statement of purpose, authority, and responsibility (charter).
3. The charter shall be consistent with Islamic Shariah rules and principles.
4. The charter shall be approved by the SSB and issued by the board of directors.
5. The charter shall be regularly reviewed.

External Shariah review

1. The external auditor is there to review internal procedures and act as support of internal auditor's duties.
2. Advantage of being more independent
3. Access to various F&SSB & IFIs
4. Opportunity to keep us up-to-date with latest industry developments.

Objective of the Shariah review

- The objective of a Shariah review is to ensure that the activities carried out by an IFI do not contravene the Shariah rules and principles, Fatwas, guidelines, and instructions issued by the F&SSB.
- **The achievement of this objective requires** that the Shariah Review (*as defined in previous slides*) is mandatory.
- The internal Shariah review shall be carried out by **an independent division/department.**

Responsibilities

□ **Two types of responsibilities;**

1. The auditor is responsible for forming and expressing an opinion on the financial statements.
2. The management is responsible for ensuring that the financial statements and the IFI's activities comply with Islamic Shariah Rules and Principles as determined by the Shariah Supervisory Board and this is based on Auditor's opinion.

The SSB's report is based on....

Illustrative wording..... *(according to the standard)*

“We conducted our review which included examining, on a test basis of each type of transaction, the relevant documentation and procedures adopted by the Example Islamic Financial Institution.

We planned and performed our review so as to obtain all the Information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Example Islamic Financial Institution has not violated Islamic Shariah Rules and Principles.” **F&SSB trusts on Auditors.**

Hence,

- The main and basic responsibility comes on Shariah Auditors.
 - a) They have to provide facts to the F&SSB
 - b) To prepare F&SSB's report to the Shareholders
 - c) To make sure that IFIs achieved the goal????
- **Request for conducting a general survey.**

AAOIFI Auditing Standards

- What are the criteria / requirement for the Sharia Auditor?
- According to AAOIFI Auditing Standard no 4.

“The auditor shall be knowledgeable about Islamic Shariah Rules and Principles. However, he would not possess the same level of knowledge as that of SSB members and thus the auditor shall not be expected to provide interpretation of these rules and principles”.

➤ Then how can we ensure compliance with Shariah?

AAOIFI Certifications

- **Are CSAA and CIPA adequate qualification?**
 - ✓ No conditions for eligibility and entitlement
 - ✓ No experience and pre-education required
 - ✓ Do not cover the full AAOIFI's Standards
 - ✓ Training's standard & Trainer is question mark. Is it sufficient & competent?
 - ✓ What type of merit required & implementation skills?
 - ✓ How many Auditors are truly qualified?
 - **If a survey conducted to know about the facts.**

Recommendations

We need;

- Proper official training of Sharia Auditors
- Strengthening the Certification's process
- Eligibility for obtaining the AAOIFI's Certificates
- Qualification Standards of Sh. A. to be more strict:

Limiting mainly to existing, new and or prospective professional auditors only.

- Proper control and support by F&SSBs
- Standardisation of Shariah Audit:

Establishment of professional, dedicated and global audit firms with close links to AAOIFI & other standard bodies for quicker and more practical standard creation.

Conclusion

- This is an ongoing process and we need to find ways to improve this.
- Always $-x- = +$ وما ارید الا الاصلاح ما استطعت
- Our respective Shariah scholars planted IFI's tree. To water and take care of it is our religious and ethical responsibility.

هذا مني والله أعلم بالصواب وشكرًا