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# LEGAL ISSUES RELATED TO THE SHARIAH ADVISORY COUNCIL IN MALAYSIA

## **ABSTRACT**

Malaysia has always aspired to be the hub for Islamic banking and finance. Various measures have been, and are being, carried out to promote Malaysia as an international Islamic banking and financial centre. As the backbone for this, the national Shariah Advisory Council (SAC) has been established under the auspices of the Central Bank of Malaysia Act 1958 (CBMA). Under the CBMA, the SAC has been conferred a statutory function as the authority for the ascertainment of Islamic law for the purposes of Islamic banking, as well as business and other types of Islamic financial businesses. In 2009, the CBMA 1958 was replaced and repealed. With the coming into force of the CBMA 2009, the role and functions of the SAC was reinforced and upgraded in terms of appointments of members and, most importantly, that the Shariah rulings pursuant to any reference made to the SAC by the Civil court or arbitrator concerning Shariah matters shall be binding on the Islamic financial institutions as well as on the court and any arbitrator. The issue of whether or not the SAC is the final arbiter on Islamic banking and finance disputes or, in other words, there is no longer a process of judicial review where it involves Shariah matters, will be the highlight of this paper. To what extent does the post CBMA 2009 solve the binding nature

of the SAC upon the Civil courts of Malaysia as its rulings and directives are only relevant to 'Shariah' issues? What would be the situations if the issues of the Islamic banking and finance cases are deemed not to amount to a 'Shariah' issue, but are purely on banking, land matters or contractual interpretations? Has there any actual legal reform been brought about by this amendment or is it merely a cosmetic changes? If the court were to be bound by the SAC rulings, does this not usurp the independence of the judiciary which is the corner stone of the principle of separation of powers between the executive, the legislature and the judiciary? The above legal issues will be critically explored with the help of cases decided by the Malaysian Civil courts, pre and post CBMA 2009.

Keywords: *The Shariah Advisory Council*, Islamic Banking, Islamic Finance

### **Abstrak**

*Malaysia berkeinginan menjadi pusat utama perbankan dan keuangan Islam. Berbagai tindakan telah dan terus dilakukan untuk mempromosikan Malaysia sebagai sebuah pusat perbankan dan keuangan International. Sebagai pendukung utama, The Shariah Advisory Council (SAC) di Malaysia telah didirikan dibawah naungan Undang-Undang Bank Sentral Malaysia tahun 1958 (Central Bank of Malaysia Act 1958). Dibawah UU ini, SAC telah dinyatakan secara fungsi perundang-undangan sebagai pihak yang berwenang untuk mengawal hukum Islam untuk tujuan-tujuan perbankan Islam dan bisnis serta bentuk-bentuk keuangan Islam lainnya. Pada tahun 2009, Undang-Undang Bank Sentral Malaysia tahun 1958 diganti dengan UU Bank Sentral 2009. Dengan berlakunya UU Bank Sentral 2009, peranan dan fungsi SAC ditingkatkan dalam bentuk pengangkatan anggota dan yang paling penting keputusan-keputusan syariah menurut SAC oleh pengadilan sipil dan arbitrator berkaitan masalah syariah berlaku mengikat terhadap lembaga-lembaga keuangan syariah dan pengadilan serta arbitrator. Masalahnya adalah apakah SAC merupakan arbiter yang bersifat final dalam kaitan dengan keuangan dan perbankan Islam atau dalam kata lain tidak ada proses judicial review yang lebih lama dimana melibatkan masalah-masalah syariah, akan ditekankan dalam tulisan ini. Dalam hal apakah setelah adanya UU Bank Sentral Malaysia 2009 menyelesaikan sifat mengikat SAC terhadap pengadilan-pengadilan sipil Malaysia sebagai keputusan-keputusan dan petunjuk dan hanya relevan terhadap masalah-masalah syariah? Apakah yang akan terjadi jika masalah-masalah keuangan dan perbankan Islam dianggap tidak dijadikan sebuah masalah syariah, tetapi murni masalah perbankan, tanah atau interpretasi kontraktual? Sudahkah ini merupakan reformasi hukum yang aktual yang timbul akibat amandemen ini atau hanya perubahan yang bersifat kosmetik? Jika pengadilan terikat pada keputusan-keputusan SAC, apakah hal itu tidak mengontrol independensi lembaga peradilan yang menjadi pilar utama prinsip separation of powers antara eksekutif, legislatif dan peradilan? Masalah-masalah di atas akan di eksplorasi secara kritis melalui kasus-kasus yang telah diputus oleh pengadilan Malaysia sebelum dan setelah diundangkan UU Bank Sentral Malaysia 2009.*

*Kata Kunci: The Shariah Advisory Council, Perbankan Islam, Keuangan Islam*

## **I. INTRODUCTION**

Malaysia has always inspired to be the global hub for Islamic banking and finance (IBF). Malaysia is the largest centre for IBF in the Asian Pacific region with the IBF assets stood at USD272.5 billion. In 2012, Malaysia accommodates 21 Islamic banks, 17 takaful operators and 16 Islamic fund management companies (Bank Negara Malaysia, 2012). Islamic banking in Malaysia is specifically governed by the Islamic Banking Act 1983 (IBA) 'Islamic banking business' is defined by its Section 2 as "banking business whose aims and operations do not involve any element which is not approved by the Religion of Islam'. This definition forms the basis for the establishment of the Shariah Advisory Council (SAC) of the Central Bank of Malaysia (CBM), (Bank Negara

Malaysia (BNM)), its legal status and functions.

The objective of this paper is to analyse the rationale for establishing the SAC, to explore its legal status and statutory duties as well as other striking legal issues that derive therefrom. The focus will be on the development of the law in the pre and post Central Bank of Malaysia Act (CBMA) 2009. With the passing of the new CBMA 2009, the legal position of the SAC has been upgraded and this is the beginning of the judicial recognition of the binding nature of the SAC within the conventional legal framework of Malaysia.

## **II. DISCUSSION**

### **A. The Establishment of the Shariah Advisory Council (SAC)**

Section 3(5) and (b) of the IBA states that there shall be no recommendation for a licence by the Central Bank and the Minister shall not grant a licence, unless he is satisfied that there is in the proposed Islamic bank's articles of association, provision for the establishment of a Shariah Advisory Body (SAB) to advise the bank on the operations of its banking business in order to ensure that they do not involve any element which is not approved of by the religion of Islam. The need for Shariah compliant supervision is due to the generality of the definition of 'Islamic banking business' and the non-exhaustiveness of the IBA provisions as a whole. For example, Shariah contracts such as Mudarabah, Musyarakah, Ijarah, Murabahah and Wakalah are not mentioned in the IBA. It was only from the official documents of the sole Islamic bank at that time (Bank Islam Malaysia, 1983) that these underlying Shariah contracts were identified (Yasin, 2001:10).

In March 1993, instead of establishing more Islamic banks, Bank Negara introduced interest free banking scheme within conventional banks, it was initially called windows but was upgraded to a division. Many conventional banks set up "Islamic windows" and appointed selected Muslim scholars to be members of their Shariah advisory bodies (Yasin, 1996:296). With the increasing number of banks offering Islamic banking products it was decided to harmonize their Shariah interpretations. As a result of this, section 124 (7) of the Banking and Financial Institutions Act 1989 (BAFIA) was introduced to provide for the establishment of SAC to advise Bank Negara on matters relating to Islamic banking business and Islamic financial business.

In 2003, section 13A was added to the IBA which provides for reference by the Islamic banks to the SAC on Shariah matters and further provides that they shall comply with the advice of the SAC. Section 13A further defines "Shariah Advisory Council" to mean the Shariah Advisory Council established under Section 16B (1) of the Central Bank of Malaysia Act 1958. Section 13A of the IBA must therefore be read together with Section 16(B) (1) of the CBMA 1958. Under Section 16B, the SAC has been conferred with a statutory function that it shall be the authority for the ascertainment of Islamic law for the purposes of Islamic banking business, among others, based on Shariah principles and supervised and regulated by Bank Negara Malaysia. The amendment, which in effect, confers advisory powers to the SAC over the Islamic banks, creates

a common understanding between the Shariah advisory bodies and the SAC.

With the coming into force of the Central Bank of Malaysia Act 2009, the role and functions of the SAC was reinforced whereby it was accorded the status of the sole authoritative body on Shariah matters pertaining to Islamic banking. While the rulings of the SAC shall prevail over any contradictory ruling given by a Shariah body or committee constituted in Malaysia, court and arbitrators are also required to refer to the rulings of the SAC for any proceedings relating to Islamic financial business, and such rulings shall be binding.

### **SAC in the Pre-CBMA 2009**

From the earlier studies on the subject (Yakoob, 2009: 1-29; Yasin, 2007: 99; Yasin, 2001:1; Shariff, 1998: xlv; Yasin, 1997: xii), it was observed that the main legal constraint could be said revolves around the Malaysian legal system in which Islamic banking was operating. There were issues *inter alia* as to which court would try Islamic banking disputes: the civil court or the Shariah court, issues on the qualification of the judges to try Islamic banking disputes and their lack of understanding, which was evident from the approach they took in deciding cases involving Islamic banking and their refusal or reluctance to make reference to the SAC.

Studies have addressed the issues in the context of the following (Yakoob, 2009: 1-29; Yasin, 2001:1; Yasin, 1997: xii):

1. the legal and judicial framework of Islamic finance which lies within the conventional civil framework
2. the application of the common law principles by the civil courts in deciding cases in Muamalat law and
3. reference to the SAC was regarded as optional and not obligatory by the civil courts.

The issues above resulted in legislative and juridical obstacles. Legislative obstacles refers to the existing laws of the country that are applicable to banking are based on common law and some of the provisions of this legislation are inconsistent with Islamic law, therefore making that specific part of the law incompatible with Islamic banking. Juridical obstacles concerns the challenges faced by Islamic banking in Malaysia when the courts that decide Islamic banking cases are the civil courts whose judges are trained in common law and follow the rules and procedures familiar to them under the conventional system rather than Islamic law.

### **Legislative Obstacles**

The IBA is unique in the sense that it is the first Act of Parliament to deal specifically with Islamic banking in a jurisdiction that follows the common law system. The application of the common law of England and the rules of equity, together with statutes of general application and the application of English law in commercial matters in Malaysia are based on Sections 3 and 5 of the Civil Law Act 1956 respectively. Sections 3 (1), a, b, c and Section 3 (2) of the Civil Law Act 1956 (Revised 1972) provide that:

- 1) Save so far as other provision has been made or may hereafter be made by any written law in

force in Malaysia, the Court shall

- a. in Peninsular Malaysia or any part thereof, apply the common law of England and the rules of equity as administered in England on the 7 April 1956;
  - b. in Sabah, apply the common law of England and the rules of equity, together with statutes of general application, as administered or in force in England on 1 December 1951;
  - c. in Sarawak, apply the common law of England and the rules of equity, together with statutes of general application, as administered or in force in England on 12 December 1949, subject however to subparagraph
- 2) Provided always that the said common law, rules of equity and statutes of general application shall be applied so far only as the circumstances of the States of Malaysia and their respective inhabitants permit and subject to such qualifications as local circumstances render necessary.

Section 5 of the Civil Law Act 1956 (Revised 1972) in particular Section 5(1) which provides: “(1) In all questions or issues which arise or which have to be decided in the States of Peninsular Malaysia other than Malacca and Penang with respect to the law of partnerships, corporations, banks and banking, principals and agents, carriers by air, land and sea, marine insurance, average, life and fire insurance, and with respect to mercantile law generally, the law to be administered shall be the same as would be administered in England in the like case at the date of the coming into force of this Act, if such question or issue had arisen or had to be decided in England, unless in any case other provision is or shall be made by any written law.

The passing of the IBA which has managed to expand the role of Islamic law to non-personal and non-matrimonial matters is merely a Federal law (the law of general application-applicable to both Muslims and non-Muslims) to regulate and license Islamic banks in Malaysia. As observed by Suriyadi Halim Omar, J (as he then was), in the case of *Arab-Malaysian Merchant Bank Bhd v Silver Concept Sdn Bhd* (CLJ 8, 2009: 9) stated: “The Islamic banking system, currently co-existing with the civil banking system in Malaysia, is the extraction of the essence of Islamic Jurisprudence or Syariah, sourcing from the al-Quran and Al-Sunnah/ahadith and is here to stay. These two sources are the only God sanctioned sources in Islam. Despite all the unknown fears, bits and pieces have been picked up and pieced together, and finally seeing a wholesome and identifiable Islamic banking system molded from these two sublime sources. It saw statutory reality with the promulgation of the Islamic Banking Act 1983, primarily to provide for the setting up and licensing of Islamic banks, falling within the jurisdiction of the civil law and applying the civil court procedures”

Islamic banking in Malaysia currently has to operate within the purview of the civil court jurisdiction and its procedural rules (Rules of the Courts 2012 as well as the Rules of the Court of Appeal 1994 and the Rules of the Federal Court 1995) and is subject to the existing laws governing *inter alia* the parties’ contractual relationship and in terms of the legislation it is enforced under (Contracts Act 1950, the National Land Code 1965, the Hire Purchase Act 1967, the Sale

of Goods Act 1957 and the Stamp Act 1949), the provisions of which may contain elements which are not approved by the Religion of Islam. The reasons for this problem are as follows:

1. Division of judicial powers between the civil courts and the Shariah courts as defined in the Federal Constitution (FC). This division is provided for under Part VI (Relations between the Federation and the States) Chapter 1 (Distribution of Legislative Power), to be read together with Part IX (the Judiciary) under the FC. Section 74 of the FC deals with Federal and State laws with reference to the three Lists contained in the Ninth Schedule namely:
  - a. the Federal List (List 1);
  - b. the State List (List 2) and
  - c. the Concurrent List (List 3).

The relevant parts are in List 1 and List II. List I: Item 7: Finance including banking, bills of exchange, promissory notes and other negotiable instruments, foreign exchange. Item 8: Trade, commerce and industry including incorporation, registration and winding up of company, insurance. List II (State List) deals with Islamic law and personal and family law of persons professing the religion of Islam except in regard to matters included in the Federal List". It is obvious that List II does not include banking, insurance, companies and contract. These matters come under the Federal List and by virtue of the proviso in List II, Islamic banking matters come under the jurisdiction of the civil courts.

Furthermore, the phrase 'person profesing the religion of Islam' in List II has created another complication for an already difficult situation. The usually cited case in this respect is *Bank Islam Malaysia Bhd. v. Adnan Bin Omar* (Kuala Lumpur High Court, Civil Suit No. S3-22-101-91; Yasin, 2001: 6-7). An issue, which was not reported, was concerned with the jurisdiction of the Shariah court over Islamic banking cases. It was held, *inter alia*, that as BIMB is a corporate body with no religion, the bank was not within the jurisdiction of Shariah Courts as List II only provides for jurisdiction over persons professing the religion of Islam. It is a considered view that the promulgation of the legislation governing Islamic banking and finance as Federal legislation showed the intention of Parliament that matters pertaining to banking and finance were never intended to be dealt with at the State level, where there would be no uniformity in terms of its administration.

2. The general nature and the non-exhaustiveness of the provisions of the IBA. This has been seen as another hurdle to be surmounted. A perusal of the provisions of the Act would show that it is regulatory in nature and does not provide for the substantive law for Islamic banking. It has been further observed that there was not any specific thought of meeting the requirements and expectations of the Shariah, since the clauses used are mainly derived from the conventional banking practices and the repealed Banking Act 1973 which the IBA was modelled from.

It has been pointed out that the IBA overlooked the aspect of conflict between its provisions and other written laws, be they substantive or procedural laws. The provision of Section

55 that does deal with conflict of laws, limits its scope to the application of the Companies Act 1965. There was a hypothetical argument on whether the legal maxim *expression unius alterius* would be applicable. Norhashimah Mohd Yasin urged that the oversight should be rectified immediately and suggested that perhaps a lesson could be taken from Pakistan where their Islamic banking law has been constructed to state: “The provisions of this ordinance shall have effect notwithstanding anything contained in the Companies Act 1913 (VII of 1913), or any other law for the time being in force (Yasin, 2001: 12-13). But this was subsequently answered in the negative by the Malaysian Court of Appeal in *Bank Kerjasama Rakyat Malaysia v Emcee Corporation* (CLJ 1, 2003: 625).

The judgment delivered by Abdul Hamid Mohamad JCA states: “as was mentioned at the beginning of this judgment the facility is an Islamic banking facility. But that does not mean that the law applicable in this application is different from the law that is applicable if the facility were given under conventional banking. The charge is a charge under the National Land Code. The remedy available and sought is a remedy provided by the National Land Code. The procedure is provided by the Code and the Rules of the High Court 1980. The court adjudicating it is the High Court. So, it is the same law that is applicable, the same order that would be, if made, and the same principles that should be applied in deciding the application. The main source of the applicable law is s. 256 of the National Land Code:”

In *Bank Islam Malaysia Bhd v. Lim Kok Hoe & Anor & Other Appeals* (CLJ 6, 2009:22), Raus Sharif JCA (as he then was) stated: “... the law applicable to BBA contracts is no different from the law applicable to loan given under the conventional banking. The law is the law of contract and the same principle should be applied...”. The SAC can play a role to mitigate the constraints in terms of the legislative framework and the general nature of the IBA, essentially to ensure Shariah compliance. However this is subject to the civil court’s willingness to examine the issue at hand from the viewpoint of Shariah and to utilize the expertise of the SAC as a reference. This approach is not impossible and had been done in England in the case of *Glencore International AG v Metro Trading International Inc* (EWHC, 2000: 199; All ER 1, 2001: 103) on which the English judge, Moore-Bick J, was willing to examine the issue at hand from the viewpoint of Shariah with the assistance of experts (Yasin, 2007: 100-104; Norhashimah, 2001, 13-15). What more in Malaysia, where the SAC is conferred with the power to issue rulings on Shariah matters and as been referred to as the authority on matters related to IBF.

However the reported cases indicate that at the inception of litigation concerning Islamic banking cases, the Malaysian courts are reluctant to refer to the SAC. The courts always based their decisions on the current banking laws regime without making any reference to the underlying Shariah principles.

### Juridical Obstacle

From the studies made on this aspect and the reported cases, it can be gathered that the main objections, vis-à-vis reference to the SAC under the repealed Section 16(B) of the CBMA 1958, are premised on the following grounds:

- 1) reference to the SAC's ruling was held to be an abdication of the civil court's judicial functions;
- 2) the ruling of the SAC is not binding on the court and in any case such reference is discretionary; and
- 3) that the issue in a particular case was not one of Shariah compliance but merely the interpretation of its contractual terms. In other words, it was a non-Shariah issue in order to justify a reference to the SAC.

Abdul Wahab Patail J (as he then was), in the case of *Affin Bank Bhd v. Zulkifli Abdullah* (CLJ 1, 2006: 438) was of the view that reference to the SAC was not necessary for the following reasons: "Since the question before the court is the interpretation and application of the terms of the contractual documents between the parties and of the decisions of the courts, thus reference of this case to another forum for a decision would be an indefensible abdication by this court of its function and duty to apply established principles to the question before it. It is not a question of Shariah law."

His Lordship, in his subsequent decision in the case of *Arab-Malaysian Merchant Bank Bhd v Silver Concept Sdn Bhd* (CLJ 8, 2008:522) reiterated his position in terms of reference to the SAC. He further opined that although the resolution of the SAC that Al-Bai' Bithaman Ajil complied with Shariah, section 16(B) of the CBMA 1958 did not make reference mandatory and that it clearly did not intend the SAC to be a judicial authority.

"It was submitted by the plaintiff that the Shariah Advisory Council had determined that the Al-Bai' Bithaman Ajil (ABBA) complied with the shariah and once the determination is made on the issue of shariah compliance by the said Shariah Advisory Council any question on their said determination can be referred to the Shariah Advisory Council. Section 16B of the Central Bank of Malaysia Act 1958 (Act 519) however does not make reference mandatory. It clearly did not intend the Shariah Advisory Council in the executive branch of government to be the judicial authority. Thus, its rulings are binding only upon the arbitrator where reference is made by an arbitrator. In the case of reference by the court, the ruling is not binding but shall be taken into consideration. Given that reference is discretionary and the rulings are not binding, and taking into consideration the issue is not as to the shariah compliance of the ABBA Facility but the interpretation of its terms, the court is of the opinion reference is not necessary."

In the subsequent development, by virtue of the decision of the Court of Appeal in the case of *Bank Islam Malaysia Berhad v. Lim Kok Hoe and Anor and Other Appeals* (CLJ 6, 2009:22) the status of SAC resolutions, such as in this case on the validity of Al-Bai' Bithaman Ajil, has been restored



and that it ought to be referred to by the judges (*Malayan Banking Bhd v. Ya'kup Oje & Anor*, CLJ 5, 2007: 311). The discretionary nature of the reference under Section 16(B) brought another issue to the surface.

Since then some litigants have thought it fit to tender expert opinions or evidence to challenge the resolution of the SAC. In the case of *Tan Sri Abdul Khalid Ibrahim v. Bank Islam Malaysia Bhd & Another Case* (CLJ 4, 2010: 388), counsel for the Plaintiff produced 3 Shariah opinions, which essentially raised issues with the BBA Agreement.

## **B. SAC in the Post-CBMA 2009**

The new CBMA 2009 was passed by Malaysian Parliament and subsequently received the Royal assent on 19<sup>th</sup> August 2009. It came into effect on 25 November 2009. The relevant provisions are contained in Part VII governing Islamic Financial Business. Sections 51 to 58 in Chapter 1, specifically deal with the SAC. While Chapter 2 provides for the power of the BNM as well as promotion of Malaysia as an international financial centre. Section 51 is the authoritative section that confers authority on BNM to establish a SAC on Islamic finance which shall be the authority for the ascertainment of Islamic law for the purposes of Islamic financial business.

The functions of the SAC as stipulated under Section 52(1) are as follows:

- 1) to ascertain the Islamic law on any financial matter and issue a ruling upon reference made to it in accordance with Part VII;
- 2) to advise Bank Negara on any Shariah issue relating to Islamic financial business, the activities or transactions of Bank Negara;
- 3) to provide advice to any Islamic financial institution or any other person as may be provided under any written law; and
- 4) such other functions as may be determined by Bank Negara.

Section 52(2) explains that “ruling” means any ruling made by the Shariah Advisory Council for the ascertainment of Islamic law for the purposes of Islamic financial business. The new law appears to give recognition to the duty of the SAC as the highest authority for the ascertainment of Islamic law for the purposes of Islamic financial business when it provides under Section 53(1) that the Yang di-Pertuan Agong may, on the advice of the Minister after consultation with the Bank, appoint from amongst persons who are qualified in Shariah, or who have knowledge or experience in Shariah and also in banking, finance, law or such other related disciplines as members of the SAC.

This could imply an elevation of the status of the SAC, as under the repealed Act, the appointment would be made by the Minister on the recommendation of the BNM (Section 16(B) (2) of the CBMA 1958). The functions of the SAC under Section 52(1) are reinforced by Section 55 where the law provides for the requirement that BNM shall consult with its SAC on any matter relating to Islamic financial business and for the purpose of carrying out its functions or conduct-

ing its affairs under the CBMA 2009 or any other written law in accordance with the Shariah.

Sub-section 2 of Section 55 governs the relationship between the Shariah Committees of the Islamic financial institutions (IFIs) and the SAC of the Bank Negara. In the new Shariah Governance Framework for Islamic Financial Institutions, the main duties and responsibilities of the Shariah Committee of the IFIs are listed as follows:

- 1) Advise on matters to be referred to the SAC - The Shariah Committee may advise the IFI to consult the SAC on Shariah matters that could not be resolved.
- 2) Provide written Shariah opinions The Shariah Committee is required to provide written Shariah opinions in circumstances where the IFI make reference to the SAC for further deliberation, or where the IFI submits applications to the Central Bank for new product approval

Corresponding to this, Section 55(2) of the CBMA 2009 provides that: (2) Any Islamic financial institution in respect of its Islamic financial business, may (a) refer for a ruling; or (b) seek the advice of the Shariah Advisory Council on the operations of its business in order to ascertain that it does not involve any element which is inconsistent with the Shariah". In the event that a ruling by a Shariah Committee differs from the ruling issued by the SAC, Section 58 of the CBMA provides that the SAC ruling shall prevail and shall bind the Shariah Committee of the Islamic financial institution. The position is reinforced by the provisions of the Guidelines on Shariah Governance Framework for Islamic Financial Institution under Principle 6 (Section 59 of CBMA) which, inter alia, expressly states that: "Members of the Shariah Committee must not act in a manner that would undermine the rulings and decisions made by the SAC or the committee they represent. They are required to respect and observe the published Shariah rulings issued by the SAC and shall not go against the decisions of the committee that they represent in public.

6.3 In cases where there are uncertainties and differences of opinions, the IFI may seek advice and refer for a ruling from the SAC.

6.4 In cases of disputes and court proceedings relating to Islamic financial business or any Shariah issues arising from the IFI's business operations, both the court and the arbitrator shall take into consideration the published rulings of the SAC or refer such issues to the SAC for its ruling. Any ruling made by the SAC arising from a reference made shall be binding on the IFIs and the court or the arbitrator. In the event where the decision given by the IFI's Shariah Committee is different from the ruling given by the SAC, the rulings of the SAC shall prevail. However, the Shariah Committee is allowed to adopt a more stringent Shariah decision."

With the new CBMA 2009, the most significant effect is about the binding nature of the SAC's rulings. Any ruling made by the SAC pursuant to a reference made by any court or arbitrator pursuant to a Shariah matter shall be binding on the IFIS and the court or arbitrator. This is statutorily provided for under Section 57 of the CBMA 2009: "Any ruling made by the Shariah Advisory Council pursuant to a reference made under this Part shall be binding on the Islamic financial institutions under section 55 and the court or arbitrator making a reference under section 56".

### C. SAC and Post-CBMA 2009: Some Critical Analysis

From the foregoing, the passing of the CBMA 2009 marked an important milestone in terms of supervision and monitoring of the implementation of Islamic banking business. The intention of Parliament in passing the Act as far as Islamic banking is concerned, can be deduced from the Parliamentary debate dated on 9 July 2009:

- a. the framers of the legislation intended to give statutory recognition to the existence of a dual banking system in Malaysia, i.e. the Islamic banking system to operate on the same level playing field as its conventional counterpart; and
- b. since the civil court is afforded the jurisdiction to hear Islamic banking disputes and in so far as the disputes are on or related to Shariah issues, such issues must be referred to the experts in Shariah and the experts in Islamic banking. The CBMA 2009 sought to provide the solution by granting the authority to Bank Negara for the establishment of the SAC as the highest authority to be referred to by the civil courts and any ruling made by the SAC would be binding.

At the very least, it could be said that the framers of the legislation had taken note of the issues and constraints faced by the Islamic banking system in operating within the framework of the conventional legal system and the civil court jurisdiction. Whilst the notion and the objective seem ideal, looking at the scenario one would wonder to what extent the binding nature of the SAC's ruling would be receptive to the civil courts in Malaysia. "If the judges are bound to follow the SAC's rulings on Shariah matters, some might argue that it would hinder their independent status to a certain extent. The argument goes further to say that the rulings of the SAC are conclusive and not subject to appeal. This definitely would not be well accepted by lawyers who would like to be able to use the appeal system" (Trakic, 2012: 456-457).

The other aspect that is less importance is how far the CBMA 2009 would solve the fact that the binding nature of the SAC ruling only relates to matters pertaining to Shariah? What would be the situation if the 'banking matter' and not the 'Shariah issue' is raised? It was opined that it could then be argued that sometimes certain Shariah matters might be banking matters concurrently and the line between the two in certain circumstances might be very slim (Trakic, 2012:457). Obviously, how far this argument may be sustained, in light of the earlier decided cases, would depend on how the courts perceive the real issue to be addressed, i.e. 'Shariah issue' or 'banking issue,' in determining the dispute. It is a considered view that avenues are wide open for the judges to rule that any issue before them is not a Shariah issue necessitating reference to the SAC.

This is what occurred in *Mohd Alias Ibrahim v RHB Bank Bhd & Anor* [2011] 4 CLJ 654.) It was held by the Court *inter alia* that the issue of whether the facility is Shariah compliant or not is only one of the issues to be decided. Although the ascertainment of Islamic law as made by the SAC will be binding on the court as per Sections 56 and 57 of the CBMA 2009, it will be up to the Court to apply the ascertained law to the facts of the case. The court still has to decide the

ultimate issues, which have been pleaded. Consequently, it was decided that the final decision remains with the Court.

This case further illustrates the legal challenge arising out of the provisions giving the finality to the SAC's ruling. In this case Sections 56 and 57 of CBMA 2009 (the Impugned Provisions) were challenged on the ground of being *ultra vires* the Federal Constitution. The Plaintiff sought a declaration that the Impugned Provisions be declared invalid and posed the following questions for the determination of the court:

- 1) whether by the Impugned Provisions, the SAC was actually usurping the judicial power of the court in Art. 121(1) of the Federal Constitution;
- 2) whether the Impugned Provisions had in effect delegated the decision-making power of the court relating to matters of Islamic financial business to the SAC and were, on that score, inconsistent with Art. 121(1) of the Federal Constitution;
- 3) whether by the Impugned Provisions making the ruling of the SAC binding on the court, the parties had been deprived of their right to be heard, and in any case whether such deprivation: (a) was in breach of the Constitution; and (b) constituted a breach of natural justice; and
- 4) whether the Impugned Provisions could have retrospective effect on Islamic banking transactions which occurred prior to the date of the coming into force of CBMA 2009.

These questions were answered in the negative and the Court refused the declaration sought, however the Court has made the following important legal pronouncements concerning the role of the SAC:

**1) The role of the SAC is to ascertain the law and not to determine it**

The Court referred to the earlier decisions of *Tan Sri Abdul Khalid Ibrahim v Bank Islam Malaysia Bhd & Another case* (CLJ 4, 2010: 388) and the Court of Appeal decision in the case of *Lim Kok Hoe*, (supra) and decided that it is clear that the SAC was established as the authority for the ascertainment of Islamic law for the purposes of Islamic banking business, takaful business and Islamic financial business. Therefore, if the court refers any question under Section 56 (1) (b) of the CBMA 2009 to the SAC, the SAC is merely required to make an ascertainment, and not determination, of Islamic laws related to the question.

**2) Corollary thereto, the SAC is not in a position to issue a new *hukm Syara'* but to find out which one of the available *hukm* is the best applicable in Malaysia for the purpose of such ascertainment**

In this regard, the Court held that: "(94) The Federal Constitution has given the power to Parliament to make laws with respect to any of the matters enumerated in the Federal List which includes the ascertainment of Islamic law and other personal laws for purposes of federal law (Article 74 and Item 4 (k) in the Federal List of the Ninth Schedule to the Federal Constitution), (95) Act 701 is a federal law and its contents are consistent to the words employed in the Federal

Constitution. In this sense, it can be seen that the SAC is not in a position to issue a new *hukm Syara'* but to find out which one of the available *hukm* is the best applicable in Malaysia for the purpose of ascertaining the relevant Islamic laws concerning the question posed to them.

(96) For example, in a matter where there are differences of opinion regarding the validity of a certain Islamic finance facility, SAC can be referred to ascertain which opinion of the jurist is applicable in Malaysia. This ascertainment of Islamic law will be binding upon the courts as per the Impugned Provisions. It will then be up to the courts to apply the ascertained law to the facts of the case. At the end of the matter, the application and final decision of the matter remains with the court. The court still has to decide the ultimate issues which have been pleaded by the parties. After all, the issue whether the facility is Shariah compliant or not is only one of the issues to be decided by the court.

(97) This is in line with s. 52(2) of Act 701 which provides: (2) For the purposes of this Part, “ruling” means any ruling made by the Shariah Advisory Council for the ascertainment of Islamic law for the purposes of Islamic financial business (emphasis added). (98) Such conclusion may have been different if the word “determine” was used instead as this would create a different function of the SAC which is not provided in the Federal Constitution.”

### **3) The SAC is not a judicial body and the process of ascertainment by the SAC has no attributes of a judicial decision.**

In this regard the following part of the judgment is worth reproducing: “(102) The SAC cannot be said to perform a judicial or quasi-judicial function. The process of ascertainment by the SAC has no attributes of a judicial decision. The necessary attribute of the judicial decision is that it can give a final judgment between two parties which carries legal sanction by its own force. It appears to the court that before a person or persons or a body or bodies can be said to exercise judicial powers, he or it must be held that they derive their powers from the State and are exercising the judicial power of the State. An attempt was made to define the words “judicial” and “quasi-judicial” in the case of *Cooper v. Wilson & Ors* [1937] 2 KB 309.

The relevant quotation reads: “A true judicial decision presupposes an existing dispute between two or more parties, and then involves four requisites: (1) The presentation (not necessarily orally) of their case by the parties to the dispute; (2) If the dispute between them is a question of fact, the ascertainment of the fact by means of evidence adduced by the parties to the dispute and often with the assistance of argument by or on behalf of the parties on the evidence; (3) If the dispute between them is a question of law, the submission of legal argument by the parties, and (4) a decision which disposes of the whole matter by a finding upon the facts in dispute and application of the law of the land to the facts so found, including where required a ruling upon any disputed question of law. A quasi-judicial decision equally presupposes an existing dispute between two or more parties and involves (1) and (2), but does not necessarily involve (3) and never involves (4). The place of (4) is in fact taken by administrative action, the character of

which is determined by the Minister's free choice".

(103) The Court has no hesitation in holding that the process employed by the SAC is not a judicial process at all. The function of the SAC is confined to the ascertainment of the Islamic law on financial matters. (104) There is nothing in the Impugned Provisions from which it could be inferred that the SAC really exercising judicial functions. There are no contending parties before the SAC. The issue relating to Islamic financial business is referred to it by the court or arbitrator. The SAC does not require evidence to be taken and witnesses to be examined, cross-examined and re-examined.

(105) This is not a case where the court transfers part of its judicial powers and functions to the SAC. The court is of the view that the sole purpose of establishing the SAC is to create a specialized committee in the field of Islamic banking to ascertain speedily the Islamic law on financial matters which can command the confidence of all concerned in the sanctity, reliability, quality and consistency in the interpretation and applications of Shariah principles for Islamic finance transactions before the court. (106) It is not an attempt by the executive to take over gradually the judicial power traditionally exercised by the courts under safeguards which ensure the competence, independence and impartiality of the judges, and replacing by persons who have neither a judicial background nor specialized knowledge and by persons who retain lien and loyalty to executive branch."

#### **4) The rulings passed by the SAC are not fatwas within the context of administration of Islamic laws in Malaysia**

The Court observed that according to the States and Federal Territories Administration of Islamic Law Act, Enactment and Ordinance, only States and Federal Territories fatwa committees can issue fatwa which must be in accordance with the enacted procedures and then published in the Gazette. Otherwise the statement would remain as a mere decision/opinion of the Muftis.

#### **5) SAC's rulings are essentially expert opinions.**

The Court held that: "(109) Hence, the ruling issued by the SAC is an expert opinion in respect of Islamic finance matters and it derives its binding legal effect from the Impugned Provisions enacted pursuant to the jurisdiction provided under the Federal Constitution". On this point it is interesting to note that the Court has gone to the extent of making a judicial pronouncement that in the context of Islamic banking, every ruling or resolution made by the SAC, comprising of members who are qualified in Shariah, economics, law and finance and appointed based on standards enunciated in Section 53 of the CBMA 2009, is regarded as a collective ijtihad.

The decision of Mohd Zawawi Salleh J in the *Mohd Alias Ibrahim* case (supra) above, was affirmed by the Malaysian Court of Appeal in *Tan Sri Abdul Khalid Ibrahim v Bank Islam Malaysia Berhad* (Court of Appeal, Civil Appeal No. W-02(IM)-3019-12/2011). In this appeal, a challenge

was made *inter alia* against the constitutionality of Sections 56 and 57 of the CBMA 2009 on the ground that they contravened Part IX and Articles 8 and 74 of the Federal Constitution, in that the SAC is “usurping” the functions of the Courts in ascertaining Islamic law. The Court of Appeal in dismissing the appeal affirmed the position taken in *Mohd Alias Ibrahim (supra)*, and reiterated the law that the statutory function of the SAC is to ascertain Islamic financial business only. It does not hear evidence nor decide cases. The SAC is a statutory expert, as decided by the Court of Appeal:

“S.56 and s.57 contain clear and unambiguous provisions to the effect that whenever there is any Shariah Question arising in any proceedings relating to Islamic financial business before e.g any Court, it is mandatory for the Court to invoke s.56 and refer it to the SAC, a statutory expert, for a ruling. The duty of the SAC is confined exclusively to the ascertainment of the Islamic Law on financial matters or business. The judicial function is within the domain of the Court i.e to decide on the issues which the parties have pleaded. The fact that the Court is bound by the ruling of the SAC under s.57 does not detract from the judicial functions and duties of the Court in providing a resolution to the dispute(s) which the parties have submitted to the jurisdiction of the Court. In applying the SAC ruling to the particular facts of the case before the Court, the judicial functions of the Court to hear and determine a dispute remain inviolate. The SAC, like any other expert, does not perform any judicial function in the determination of the ultimate outcome of the litigation before the Court, and so cannot be said to usurp the judicial functions of the Court. Hence, s.56 and s.57 are valid and constitutional (emphasis added)”.

### III. CONCLUSION

The decision of the Court of Appeal *Tan Sri Abdul Khalid Ibrahim (Supra)*, may be said to have closed the avenue for legal challenge against the constitutionality of Sections 56 and 57 of the CBMA 2009, unless overruled by the Federal Court. It is of a considered view that the judicial pronouncement that the SAC is a ‘statutory expert’, is a form of legal maneuvering to circumvent the otherwise difficult legal questions concerning on one hand the issue of separation of powers of the executive and the judiciary and on the other the exercise of the executive power without being subjected to any review or appeal.

The operation of Islamic banking business in Malaysia is made subject to the relevant existing federal laws governing the parties’ transactions and relationship, and consequently their legal rights and liabilities are made subject to these laws. Thus, any ruling made by the SAC, if it amounts to a decision, may give rise to a right to have it reviewed by the court of law. This is the check and balance process imposed by the law so as not to allow unfettered discretion by the executive to the detriment of the public at large. However, would the judiciary have the capacity to review the decision made by the SAC over matters which, as the courts themselves observed, Islamic scholars (ulama) take years to comprehend?

It was earlier thought that perhaps a form of review of the SAC ruling could be made, perhaps

to an international body to ensure the independence of the SAC's ruling. However, as commented on by Tun Abdul Hamid Mohamad (the former Chief Justice of Malaysia), such an option is impractical due to, among other things, the issue of sovereignty and the issue of interpretation based on school of thought (madhhab).

Tun Abdul Hamid Mohamad has made an interesting commentary when he said: "Those who know civil law do not know Islamic law. Those who know Islamic law do not know civil law. Those who think they know both have never practised law". He added that he did not want a situation where "the religious scholars try to interpret the Constitution and. lawyers try to interpret the Quran". Having stated the above, notwithstanding the binding nature of the SAC's ruling, it remains a fact that it is open for the judges to decide that any issue before them is not a Shariah issue which compels the court to refer to the SAC. As Mohd Zawawi Salleh J in the case of *Mohd Alias* (supra) has made the following significant remarks: "The issue of whether the facility is Syariah compliant or not is only one of the issues to be decided by the court. And although the ascertainment of Islamic law as made by the SAC will be binding on the court..., it will be up to the court to apply the ascertained law to the facts of the case. The court still has to decide the ultimate issues which have been pleaded. Consequently, the final decision remains with the court (emphasis added)".

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