

## **The Role of Fatwa (Islamic Legal Opinion) to Islamic Banks and Other Financial Institutions: A Myth or Reality in the Nigerian and Malaysian Contexts?**

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**Abstract.** Nowadays, Islamic banking having succeeded in guaranteeing the safety of customer's wealth worldwide has stepped into tackling the arising issues within the banking sector. The main objective of the banking system is to ensure the true compliance with the principles of Islamic commercial jurisprudence through the effective means of supervision. The supervision is supposed to have been carried out by Islamic experts in a manner which effective and binding verdicts could be issued but a lot of challenges have been faced. The Islamic advisory board in an Islamic financial institution has been used for long as a collective fatwa issuing body saddled with the responsibility of ensuring the shari'ah compliance. However, involvement of technocrats therein coupled with some bureaucracies; and as well as lack of a suitable legal framework and enabling environment in support of its operation, have been causing a grievous injury to the system in recent times most especially in the Modern Muslim countries where shari'ah is applied side-by-side with other legal systems. In fact, such factors have resulted to lack of an effective legal framework on Islamic financial activities. It is against this backdrop that the paper has been jointly looked at the practices in Nigeria and Malaysia with a view to ascertaining the level playing ground for the performance of their shari'ah advisory bodies. In the end, the paper revealed that the Malaysian Islamic financial model is a reality compared to other countries in the world. Hence, the Malaysian model is expected to be suitable and relevant to the Nigerian system. Thus, the paper suggests among other things that generally, the Federal Government of Nigeria should adopt the Malaysian model of Islamic financial system; specifically, the paper suggests that the Government in collaboration with Central Bank (CBN) should facilitate the amendment of the relevant legislation such as the Constitution of Nigeria, Bank and Other Financial Institution Act (BOFIA) and CBN Act/Regulations in order to pave way for enacting a suitable Islamic financial regulatory framework; and the Government should therefore enact a distinctive Islamic financial regulatory framework that can independently regulate for the Islamic financial activities in the country.

## 1. Introduction

Fatwa is an Islamic ruling on a point of Islamic law that is issued by a recognized scholar based on sound evidence.<sup>1</sup> However, in Islamic finance, such rulings are issued by a competent body to be known as “shari’ah advisory board”.<sup>2</sup> Fatwa plays a very important role in Islamic financial institutions as it serves as a life (*Ruh*) to the institutions for its sustainability. Different countries have different approach to shari’ah governance in Islamic financial institutions, depending on the nature and peculiarity of each country. There are countries with a complete and independent Islamic banking regulations due to nature of their legal systems and financial administrative set up, other countries do not operate under a full-fledged Islamic financial system due to the pluralistic nature of their legal systems. However, among them, some have a distinct legal framework for Islamic banks and other financial institutions. It is obvious that having a distinct legal framework on Islamic financial activities would certainly have impact on their shari’ah governance. Thus, the paper has deliberately combining the two countries (Nigeria and Malaysia) in order to ascertain individually the implication and merit of having a distinct legal frame work on Islamic finance. In doing that therefore, the paper would at the beginning look at the concept of Islamic finance from the early period of Islam. Thereafter, a discussion will be followed on the nature of Islamic financial institutions and their shari’ah advisory boards in both Nigeria and Malaysia. This will enable the paper to ascertain the level attained and the gap realized from each country’s legal framework on Islamic finance and shari’ah supervision. Finally, the paper ends with conclusion.

## 2. The Concept of Islamic Finance from the early period of Islam

The idea about commercial contracts generally is not a new phenomenon in Islamic law. It has been reported that the Prophet (PBUH) was a merchant and a trader since before his Prophet hood. He carried caravans from Mecca (*Makkah*) to Syria (*Sham*).<sup>3</sup> In fact, this practice was traceable from the convention and occupation of his tribe (*Arab-Quraish*) and his clan (*Banu- Hashim*). The main economy and occupation of *Quraish* as at that time (before the *Hijrah* [the Prophet migration] to Madinah) centered on trade and trade –related activities. Among their practices was that a caravan which belongs to someone would be entrusted and accompanied by a different person other than the owner.<sup>4</sup> This indicates by implication, that the concept of contemporary *mudarabah* (limited partnership) and *musharakah* (partnership) were rooted from such practices. It has continued until the time when the Prophet (PBUH) migrated to Madinah. After the Prophet (PBUH) migrated to Madinah, where it was used to be the center of Agriculture, he legalized the practice of *Muzara’ah* (partnership in relation to crop cultivation) and *Musaqah* (partnership in relation to orchard farming).<sup>5</sup> This signifies how important the concept of partnership was since that time. To further buttress the genesis of Islamic financial contracts, it was also reported in a Hadith narrated by Aishah (RA), that the Prophet (PBUH) bought some food (another *riwayah* [version] of the Hadith said: he bought thirty (30) *Sa’i* of Baley) from a Jew, and in return, the Prophet (PBUH) gave the Jew his mail (armored iron cloth) as a security for the commodity.<sup>6</sup> This practice has also been confirmed as the root genesis of mortgage (*rahn*) and other related transactions that have been practiced in modern Islamic banking.

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<sup>1</sup> Ahcene Lahsasna, *Introduction to Fatwa, Shari’ah Supervision and Governance in Islamic Finance*, (Kuala Lumpur: Malaysia, CERT Publication, 2010), 5

<sup>2</sup> Ibid

<sup>3</sup> Ali Adnan Ibrahim, “The Rise of Customary Business in International Financial Market: An Introduction to Islamic Finance and Challenges of International Intergretion”, *AM. U. INT’L. L. REV.* (2008) 23:661, P 673

<sup>4</sup> Monzer Khaf and Tariqullah Khan, *Principles of Islamic Jurisprudence: A Survey*, Research Paper No. 16, (Jeddah: Kingdom of Saudi Arabia, Islamic Research and Training Institute, Islamic Development Bank, 1992), 11-12

<sup>5</sup> Ibid

<sup>6</sup> Muhammad Ibn Isma’il, *Sahih Al- Bukhari*, Vol. 3, P15 and 231

However, history has shown that during the life time of the Prophet (PBUH), there was no institution that primarily responsible for money transaction as practiced by the contemporary Islamic banks and other financial institutions. But it has been narrated that prior to 8<sup>th</sup> century, there was system similar to the contemporary banking which reflects some group of people called “*Sarraffeen*” or “*Sayarifah*” or “*Jahabidha*” who acts like a *bureau de change* in modern days time. Usually, such people confine themselves in a particular place called *Diwan al-jahabidha*, which is similar to what is now called as “bank”, in order to run the financial activities. After the 8<sup>th</sup> century, it has changed to another dimension more similar to modern banking functions but with slides different to modern banking system. It was interest-free business transaction unlike the modern banking.<sup>7</sup>

The concept of the Islamic commercial transactions based on the principles of *mudarabah* (limited partnership) and *musharakah* (partnership) originated from the early stage of Islam.<sup>8</sup> Such principles have indeed acquired the legal basis from the Qur’an and Sunnah. The existence of fatwa in Islamic financial institution is to make clarification of issues that are not explicitly provided for in the Qur’an and Sunnah. Fatwa plays much better role in the modern Islamic financial institutions due to emergence of new developments in the sector.<sup>9</sup> For instance, fatwa played an important role in addressing the controversial issues in a banking sector such as the legality of the concept of *tawarruq* (money liquidity or monetization) in Islam and the concept of *sukuk* (Islamic bonds) in the Islamic finance.<sup>10</sup>

In recognizing the significance of fatwa, Muslim societies have also continued to formalize the pre modern jurisprudence with a view to reviving the classical Islamic jurisprudence. Some of the contemporary jurists like Al-Qardawi, were among the people who made efforts in that directions, towards making the role of fatwa in the contemporary society a reality. The agitation for collective *ijtihad* started immediately after the fall of the Ottoman Empire, in which the Hanafi jurisprudence was codified in 1876 AD/1293 AH as “*Majallat Al- Ahkam Al- Adliyya*” and later became obsolete when the Empire collapsed after the World War I.<sup>11</sup> Various Islamic countries began to establish organizations that would be responsible for issuing a collective *ijtihad*. In 1961, Cairo has established the Institute of Islamic Research (*Majma’ A-Buhuth Al- Islamiyyah*), Saudi Arabia has established the Islamic Jurisprudence Council of the World Muslim League (*Majma’ Al- Fiqh Al- Islami*) in 1979 which is based in Makkah. Similarly, the Organization of Islamic Corporation (OIC) has established the *Fiqh Academy* (*Majma’ Al- Fiqh Al- Islami*) in 1984 with the Headquarters at Jeddah, Saudi Arabia. As a result of the efforts made by such organizations whereby making a jurisprudential thinking to be in line with the modern developments, the issue of the contemporary Islamic finance started gaining ground in 1970s. Thereafter, it was recorded another development, when some banks’ sponsored institutions such as the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) were established to oversee the

<sup>7</sup> Abdelkader Chachi, “Origin and Development of Islamic Banking operations”, Journal of the King Abdul- Aziz University *J.KAU: Islamic Econ.*, (2005 A.D/1426 A.H) Vol. 18, No. 2, pp. 3-25 at 9-12

<sup>8</sup> Ibid

<sup>9</sup> Ibid, 685-686

<sup>10</sup> Aleshaikh, Nourah, Mohammad, *Jurisprudence on Tawarruq: Contextual Evaluation on Basis of Customs, Circumstances, Time and Place, Durham theses*, ( UK: Durham University, 2011) Available at Durham E-Theses Online: <http://etheses.dur.ac.uk/3188/>, accessed on 22/11/2013, see also Nagaoka Shinsuke, “Critical overview of the History of Islamic Economics: Formation Transformations and New horizons”, *Asian and African Area Studies*, (2012)11 (2): 114-136 at 127-129

<sup>11</sup> Nagaoka Shinsuke, “Critical overview of the History of Islamic Economics: Formation Transformations and New horizons”, *Asian and African Area Studies*, (2012)11 (2): 114-136 at 127-129

shari'ah activities in the banks; then after that, followed by proliferation of the shari'ah advisory boards in various Islamic financial institutions (IFIs).<sup>12</sup>

The relationship between fatwa and financial institution is something that is traceable from the history of Islam. Of course, in the present time, the fatwa committee in Islamic financial institutions is not just a mere fatwa issuing body, but it has become an engine room for the sustainability and developments in such institutions. In fact, it played a vital role to the growth of the Islamic finance.<sup>13</sup> Fatwa and the Islamic financial institutions are inter-dependable and inseparable phenomena. Hence the latter cannot function without the former.<sup>14</sup> Issuance of fatwa in Islamic financial institutions has been carried out by the shari'ah advisory board. And as such, it is limited and confined to passing *fatawa* only on the issues referred to it by the financial organizations.<sup>15</sup> Once a fatwa is issued, it can only be utilized by such financial institutions. That is to say, every financial institution can stick to the ruling of its shari'ah advisory board.<sup>16</sup>

In recent times, the Islamic Financial Services Board (IFSB) in line with its mandate, has developed and approved<sup>17</sup> some guiding principles that can assist and strengthen the day to day running of the Islamic financial services industry (IFSI) in a particular region. Such guiding principles can promote soundness and stability of Islamic financial system whereby facilitation of better understanding of shari'ah governance issues.<sup>18</sup> *Fatawa* issued by the shari'ah advisory boards in Islamic financial institutions have been used to elaborate the practice adopted previously by the classical jurists. Although, it is certain that not all the rulings of the classical jurists are classical in nature, but generally, it has been affirmed that *fatawa* issued by Islamic advisory board in the financial institutions can amend the classical *fiqh* doctrines so that they become relevant in meeting the sophisticated financial needs of the contemporary Muslim *ummah*.<sup>19</sup> Virtually, muftis have adopted different approaches to achieve the advisory objectives, but the fundamental one among them is advocating the innovation of new Islamic financial products based on the adaptation of various medieval contracts. Advocates of this approach are normally the scholars who work closely with the Islamic financial institutions. They try to understand the problems faced by the practitioners and then suggest possible solutions according to the principles of Islamic jurisprudence. Hence, their work focuses mainly on how to apply the *fiqh* doctrines in creating financial instruments that are compatible with conventional products in all aspects.<sup>20</sup>

The establishment of Islamic advisory boards in Islamic financial institutions is an example of a collective fatwa. Thus, any matter related to the aspect of Islamic finance practices would be brought to them for a legal opinion or judgment.<sup>21</sup> The Islamic advisory board will deliberate on the

<sup>12</sup> Mahmoud A. El- Gamal, *Islamic Finance, Law, Economics and Practice*, (UK: Cambridge University Press, 2006), 27-35

<sup>13</sup> Ibid

<sup>14</sup> Murat Cizakca, *Finance and Economic Development in Islam, Historical Perspective*, MPRA paper No. 42046 (Kuala Lumpur, INCEIF, 18<sup>th</sup> October, 2012), 1-26

<sup>15</sup> Abdur-Razaq Abdul-Majid Alaro, "Shari'ah Board in Islamic Banks: A Frontage of Contemporary Ijtihad" International Conference on Ijtihad and Ifta' in the 21<sup>st</sup> Century: Challenges and Prospects, Volume 1, English and Malay Papers, Organized by Department of Fiqh and Usul al Fiqh & International Institute for Muslim Unity, International Islamic University Malaysia, 10<sup>th</sup>-12<sup>th</sup> Sha'aban, 1429 AH (12<sup>th</sup>-14<sup>th</sup> August, 2008 AD), 217-233

<sup>16</sup> Amalia Zomeno, "The Stories in the fatwas and the fatwas in History", in *Narratives of truth in Islamic law*, Boudouin Dupret, Barbara Drieskens, Annelies Moors (eds), (UK: London, I.B. Touris & Co. Ltd., 2008), 25

<sup>17</sup> The approval was made during the ninth meeting of the Board in Jeddah, Saudi Arabia

<sup>18</sup> Islamic Financial Services Board, *Guiding Principles on Shari'ah Governance Systems for Institutions offering Islamic Services*, (Islamic Financial Services Board, 2009)

<sup>19</sup> Habib Ahmed, "Islamic law adaptability and financial Development", *Islamic Economic Studies*, (February 2006) Vol. 13, No. 2, p 87

<sup>20</sup> Ibid

<sup>21</sup> Ahcene Lahsasna, *Introduction to Fatwa, Shari'ah Supervision and Governance in Islamic Finance*, (Kuala Lumpur: Malaysia, CERT Publication, 2010), 236

issue and come out with a resolution irrespective of whether the resolution would be considered as binding fatwa or not. The board is responsible for ensuring that day to day operations of financial institutions always conform to the principles of shari'ah. But not only that, the board is also responsible for revising the structure of the financial product and as well as implementation of the shari'ah recommendations. Other responsibilities of the board include: advising the financial institutions on shari'ah matters in its dealings; and providing written shari'ah opinion especially when circumstances so demand.<sup>22</sup>

However, in making such functions of the advisory boards effective and viable, there should be a need to have board members who are qualified to issue fatwa as required by Islamic *corpus juris*. Thus, there are some laid down rules under shari'ah for a person to be fitted in the board, namely: he must have a good methodology of issuing fatwa after understanding the case presented to him; he must be liberal in such a way that he may put into consideration of his audience (*mustafti*) and the contemporary developments; he must not compromise the basic principles of shari'ah; and he must be one that is conversant with the basics of the schools of Islamic jurisprudence other than his own.<sup>23</sup> The relationship between fatwa and the Islamic financial Institutions is so paramount to an extent that such institutions cannot function without a competent body that would be responsible for an effective supervision in line with the principles of shari'ah.<sup>24</sup>

### 3. Nature of Islamic Financial Institutions and Shari'ah Advisory Board in Nigeria

Generally speaking, countries in the world are differed according to the nature of their Islamic legal framework on Islamic finance. Thus, there are some countries that have an Islamic Banking Act (as a legal framework for Islamic banking). Such countries include: Malaysia, Iran, Sudan, Gambia, Syria and Yemen. Other countries do not have a specific legal framework but have some provisions that allow for the establishment and running of Islamic banking under their conventional banking Act. Example of such countries is: Nigeria, Indonesia, Pakistan, Kuwait and Turkey. Other category involves countries that do not have specific provisions for regulation of Islamic banking under their conventional banking Act but the Islamic banking system is presumed to have been covered by the general regulations concerning the shari'ah compliant products within their legal framework. Countries under this category include: Singapore, Kenya, and UK.<sup>25</sup>

The regulations on financial institutions in Nigeria are dependent on the model used by the conventional banking system. The Central Bank of Nigeria (CBN) is the main regulatory and supervisory body of all banks in the country.<sup>26</sup> It regulates all banking activities in Nigeria including Islamic banks and micro-finance. Apart from the CBN, there are also some subsidiary regulatory bodies such as the Security and Exchange Commission (SEC);<sup>27</sup> Corporate Affairs Commission

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<sup>22</sup> Mughees Shaukati, General perception of Fatwa and its Role in Islamic Finance, INCEIF Islamic Jurisprudence and Legal Maxims (Kuala Lumpur: Malaysia, INCEIF, the Global University in Islamic Finance, 2009), 17-20

<sup>23</sup> Ibid

<sup>24</sup> Ibid

<sup>25</sup> Regulations and Supervision of Non Interest Bank in Nigeria, A Presentation of Financial Policy and Regulation, Department of Central Bank of Nigeria at the two-day NDIC FICAN Workshop, 2011, held at Dutse, Jigawa state capital, November 28, 29, 2011

<sup>26</sup> Part 1, Section 1, of the Central Bank of Nigeria Decree No. 24 of 1991 Act, CAP C 4, Laws of the Federation of Nigeria LFN (2004)

<sup>27</sup> Part 1, Section 1 of the Investments and Securities Act (ISA), Decree No. 45 (1990) Act, Laws of the Federation of Nigeria (LFN), CAP I 24, 2004. The section provides for the establishment of the Securities and Exchange Commission (SEC).

(CAC);<sup>28</sup> and the Nigerian Deposit Insurance Company (NDIC).<sup>29</sup> All are Federal Parastatals established under the Enactments and Laws of the Federation of Nigeria.<sup>30</sup>

Islamic financial system in Nigeria is not really a new phenomenon. It has been practiced since the pre-colonial Nigeria, as far back as the 19<sup>th</sup> century. It has been rooted and effectively practiced since the period of the Fulani jihad of Reformation (*Tajdid*) that took place in the Sokoto Caliphate (now the largest part of Northern Nigeria and some parts of the West and Central African States).<sup>31</sup> When the British colonial administrators came, the larger part of the system including the commercial practices based on the Islamic commercial jurisprudence was gradually modified.<sup>32</sup> After so many decades, Nigeria became an independent state. Since then, Muslims have been trying to revive the suspended Islamic affairs including the banking system but to no avail.<sup>33</sup> Fortunately, during the military era (around early 1990s) an attempt was made by the then military administration to consider the yearning and aspirations of the Muslim majority in the country thereby promulgating Decrees that suit the interest of the Muslim majority. The regime promulgated a Decree which established a Statute called: “Banks and Other Financial Institutions Decree BOFID” No. 25, 1991 as amended.<sup>34</sup> Such Statute has attempted to revive Islamic banking thereby given it opportunity to breathe in. The Decree recognizes the establishment of banks based on profit and loss sharing.<sup>35</sup> The Decree also recognized the establishment of 'specialized' banks such as non-interest banking and such other banks as may be designated from time to time.<sup>36</sup> Hence, the designation of non-interest banks as specialized banks was based on the provisions of the Banks and Other Financial Institutions Decree (BOFIA now).<sup>37</sup> In fact, from 1993 to 1995 investors started applying for banking license in order to operate Islamic banking but their application did not materialize due to non-compliance with and non fulfillment of the Central Bank requirements. However, in 1996, Habib Bank Plc as it then was (Keystone Bank Plc now) opened a non-interest banking window offering a limited number of shariah-compliant products, yet, the attempt did not register a significant success but ended up with only window licensed operation.<sup>38</sup> Furthermore, in same 2004, following the demands for the establishment of full-fledged non-interest banking from interested investors, an approval-in-principle (AIP) was granted to *Ja'iz* International Plc to establish *Ja'iz* Bank Plc upon meeting mandatory capital requirement.<sup>39</sup> The year 2010 has marked the beginning of the full-fledged Islamic financial system in the country. Thus, in April 2010, the first full-fledged Microfinance known as “*Albarka* Microfinance” started operation.<sup>40</sup> Similarly in

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<sup>28</sup> Part 1, Section 1 of the Companies and Allied Matters Act (CAMA), Decree No. 1 (1990) Act, Laws of the Federation of Nigeria (LFN), CAP C 20, 2004. The section provides for the establishment of the Corporate Affairs Commission.

<sup>29</sup> Section 1, of the Nigerian Deposit Insurance Corporation Act, CAP 301, Laws of the Federation of Nigeria (1990), Act CAP N102 Laws of the Federation of Nigeria, (2004). The section provides for the Establishment of the Nigerian Deposit Insurance Corporation (NDIC)

<sup>30</sup> See Laws of the Federation of Nigeria LFN, (2004)

<sup>31</sup> Abdul Gafoor, A. L. M; *Islamic Banking*, (Chapter 4 of his book, *Interest-free Commercial Banking*), (1995) P 22

<sup>32</sup> Mannan, M. A; *Islamic Economic Theory and Practice*, (Delhi, 1980), P. 161

<sup>33</sup> Erico, L. and Farahbaksh, M. Op cit Pp 6-8 see also Khaf, M., Ahmad A. and Homud, S; *Islamic Banking and Development: An alternative banking concept?* (IRTI, 1998) Pp 21-22

<sup>34</sup> The Decree has now been renamed as BOFIA after been ratified by the Act of the National Assembly

<sup>35</sup> Section 23 of the BOFIA

<sup>36</sup> Section 61 of the BOFIA

<sup>37</sup> Sanusi, L. S; ‘Islamic Finance in Nigeria: Issues and Challenges’, lecture delivered at Markfield Institute of Higher Education (Mihe), (UK, Leicester, June 17, 2011), Pp. 6-7

<sup>38</sup> Shehu Usman Rano Aliyu, *Islamic Banking and Finance in Nigeria: Issues, Challenges and Opportunities*, international Institute of Banking and Finance, Bayero University Kano, 26/Oct/2012, Munich Personal RePEc Archive (MPRA), Paper No.42573, available at <http://mpra.ub.uni-muenchen.de/42573>. accessed on 9/10/2013, p 4

<sup>39</sup> Sanusi, L. S; ‘Islamic Finance in Nigeria: Issues and Challenges’, lecture delivered at Markfield Institute of Higher Education (Mihe), (UK, Leicester, June 17, 2011), Pp. 6-7

<sup>40</sup> Shehu Usman Rano Aliyu, 4

August 2010, The CBN released the new banking model which designated non-interest banks among the specialized banks as contained in the Statute.<sup>41</sup> As a result of that, the *Ja'iz Bank Plc* was given license to start operations in 2012.<sup>42</sup>

Fatwa remains a valuable phenomenon in the Islamic financial sector, to an extent that, no any Islamic financial institution can breathe in without a fatwa body, which is termed as “shari’ah advisory board” in present days. It is an engine room of an Islamic financial institution. It also assists even the conventional financial institutions in taking decisions related to Islamic law. This fact has been supported by Shaykh (Dr) Muhammad Abubakar in an interview conducted with him on the role of fatwa to some institutions in Nigeria.<sup>43</sup> He said; fatwa plays a role not only to Islamic financial institutions but also to conventional institutions. It serves as a fundamental pillar in the Nigerian financial institutions whose background is conventional. It assists the institutions in demarcating the lawful transactions from the unlawful ones. It harmonizes the controversial issues that may likely arise in the system especially in its inter-relationship with the conventional banks. He reiterated that, Islamic banking basically and fundamentally relies on fatwa.<sup>44</sup> In strengthening the foregoing idea, Dr. Ibrahim Umara has went further to make reference to the provision of Qur’an *Al Baqarah* 2: 275 (on prohibition of *riba* -interest), where he stated that, without prejudice and unreasonable compromise to the standard laid down by the principles of shari’ah, the provision should be interpreted in line with the contemporary development. Of course, it can be done by fatwa institution<sup>45</sup>

As for the shariah supervision and governance over Islamic banking in Nigeria, experience has shown that even prior to the full-fledged operation, the Central Bank of Nigeria has been the mother of all banks. It regulates and monitors the activities of all banks including Islamic banks and all other commercial banks. Thus, the CBN has designed a regulatory framework for Islamic banking in the country with a view to running the affairs of the Islamic bank and its shari’ah advisory council whose name was later amended to “the CBN Council of Experts”.<sup>46</sup> Such amendment happened as a result of criticisms made by some people (especially non Muslims) in the country.<sup>47</sup> According to them, the establishment of the “CBN shari’ah council” contravened the provisions of the 1999 constitution<sup>48</sup> which provides that the government should at all times adhere to the

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<sup>41</sup> Ibid

<sup>42</sup> Abdul-Razzaq A. Alaro, "Sharia Supervision as a Challenge for Islamic Banking in Nigeria" in: Oloyede I.O. (ed.), *Al-Adl (The Just): Essays on Islam, Islamic Law and Jurisprudence*, Ibadan, Nigeria, 2009, pp. 53-72 at 1

<sup>43</sup> Muhammad Alhaji Abubakar (PhD in Shari’ah (Fiqh) Islamic University of Madinah Saudi Arabia, an Imam al Mufassir, a lecturer at University of Maiduguri, Nigeria), Interview by the author, Maiduguri: Borno state, Nigeria, 16<sup>th</sup> July, 2013

<sup>44</sup> Ibid

<sup>45</sup> Ibrahim Umara (PhD and H.O.D of Political Science Dept. University of Maiduguri, Nigeria), Interview by the author, Maiduguri: Nigeria, 14<sup>th</sup> July, 2013

<sup>46</sup> A mere change of name is not supposed to affect the constitution, membership and functions of the Board. There is this maxim in equity that says: “Equity looks at the intent rather than the form”. However, some people may hide under it to bring confusion in respect of the constitution of membership of the Council, thinking that the phrase “Advisory Council of experts” may include everybody.

<sup>47</sup> Paul Tempus Temitope, Nigerian factor: Between reality and Islamic Banking, available at [http://igbofocus.co.uk/html/islamic\\_banking.html](http://igbofocus.co.uk/html/islamic_banking.html), accessed on 08/12/2013

<sup>48</sup> See for instance section 16 1(d) of the 1999 Constitution of the Federal Republic of Nigeria (as amended) which states as follows: “without prejudice to the right of any person to participate in areas of the economy within the major sector of the economy, protect the right of every citizen to engage in any economic activities outside the major sectors of the economy”. Also Section 14(3) of the Constitution which states that “The composition of the Government of the Federation or any of its agencies and the conduct of its affairs shall be carried out in such a manner as to reflect the federal character of Nigeria and the need to promote national unity, and also to command national loyalty, thereby ensuring that there shall be no predominance of persons from a few State or from a few ethnic or other sectional groups in that Government or in any of its agencies”. Also section 39 (1) (a) of the BOFIA stipulates that “Except with the written consent of the Governor, no bank shall, as from the commencement of this Decree, be registered or incorporated

principle of “making recourse to federal character” of the nation in its affairs.<sup>49</sup> Similarly, they have also lamented to the extent that the name “shari’ah” within the phrase “CBN shari’ah council” is Islamic and contrary to the provision of BOFIA. Hence it was an attempt to Islamize the country contrary to the provision of the Constitution.<sup>50</sup> They have further said that the establishment of Islamic banking generally, was an attempt to impose Islam on unbelievers contrary to the provision of the Constitution.<sup>51</sup>

Furthermore, among other challenges faced by Islamic banking activities in Nigeria was inability to have a standard; specific; and independent legal frame work on Islamic financial institutions. This is due to the fact that Nigeria falls under countries that have plural legal system with no distinctive legal framework on Islamic finance.<sup>52</sup> The Islamic finance was operating under the supervision of the CBN through non-interest banking (NIB) services.<sup>53</sup> Generally, issues concerning the Islamic financial activities always require people who are fit and proper to spearhead.<sup>54</sup> This includes their qualification, expertise and exposure to be fitted in their respective duties. In the case of Islamic banking, the experts should fulfill most if not all the requisite qualifications for them to be appointed as members of the shari’ah board in Islamic financial institutions. In fact, they should not be hand-picked by the bank management themselves just as errand boys. So that it may not be resulted to forming incompetent and incredible board members.<sup>55</sup> In Nigeria, sometimes even if the board has been rightly constituted with credible and competent scholars as members, still their roles remain largely advisory due to inability of having the enforcement power on any decision to be made.<sup>56</sup> Another serious lacuna bedeviling the system in Nigeria also lies with the *modus operandi* of the shari’ah advisory board. Their duties are mostly dependents on the bank authorities, to an extent that they do issue *fatawa* only on matters referred to them.<sup>57</sup> This is contrary to the convention of an ideal fatwa issuing body in an idle Islamic financial institution which ordinarily is

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with a name which includes the words “Central” “Federal,” “Federation,” “National”, “Nigeria”, “Reserve”, “State”, “Christian”, “Islamic”, “Moslem”, “Quranic”, “Biblical”

<sup>49</sup> Section 14 (3) of the 1999 constitution as amended

<sup>50</sup> Section 10 of the 1999 constitution as amended, the section provides: “The Government of the Federation or of a State shall not adopt any religion as State Religion”.

<sup>51</sup> Section 38 (1) of the 1999 constitution as amended, the section provides: “every person shall be entitled to freedom of thought, conscience and religion”

<sup>52</sup> Regulations and Supervision of Non Interest Bank in Nigeria, A Presentation of Financial Policy and Regulation, Department of Central Bank of Nigeria at the two-day NDIC FICAN Workshop, 2011, held at Dutse, Jigawa state capital, November 28, 29, 2011 With respect to regulation on Islamic banking, countries differ from each other; there are countries with 100% Framework. Such countries are purely Islamic country. Example of such countries is the Islamic Republic of Iran and Sudan; there are also countries with plural legal system but with distinct regulations for Islamic banking. Such countries include: Malaysia, Pakistan, Brunei and Gambia; the last category revolves around the countries with plural legal system but with distinct regulation for Islamic banking products. Example of such countries is UK, Singapore and Kenya.

<sup>53</sup> Abdul-Razzaq A. Alaro, 53-72

<sup>54</sup> CBN Inaugurates Council of Experts on Islamic banking, available at <http://forum.ipaidabribenaija.com/business-news/item/14431-cbn-inaugurates-council-of-experts-on-islamic-banking>, accessed on 08/12/2013

The CBN has inaugurated the Financial Regulation Advisory Council of Experts (FRACE) on 14/01/2013, which comprises: Shaykh Sharif Ibrahim Saleh Al-Husain (as chairman). Other members include: Sheikh Adam Idoko; Dr. Ibrahim Jalo; Dr. Abdulrazaq Alaro; Dr. Bashir Aliyu Umar; Executive Director of the International Shariah Research Academy of the Bank Negara Malaysia, Dr. Mohammad Akram Laldin; and Secretary-General of the Shari’ah Supervisory Board of the Central Bank of Sudan, Dr. Ahmad Ali Abdallah

<sup>55</sup> Muhammad Alhaji Abubakar (PhD in Shari’ah (Fiqh) Islamic University of Madinah Saudi Arabia, an Imam al Mufassir, a lecturer at University of Maiduguri, Nigeria), Interview by the author, Maiduguri: Borno state, Nigeria, 16<sup>th</sup> July, 2013

<sup>56</sup> Shaykh Muhammad Ibn Uthman (an International Scholar and the Imam of the Sahaba Mosque Kano.), Interview by the author, Kano: Nigeria, 19<sup>th</sup> August, 2013

<sup>57</sup> Ibid



operated in two modes, namely: as a research committee (*Lajinat al Bahth*) and as a supervisory committee (*Lajinat al Ishraf wal Raqaabah*).<sup>58</sup>

Progressively, in order to enhance shari'ah governance in Islamic financial institutions, the CBN in collaboration with some Institutions in Nigeria have made effort in establishing other strong supervision units in order to render effective supervision and services to the Islamic financial institutions in the country. The collaborated institutions include: Bayero University Kano (BUK) which has established an International institute of Islamic banking and finance (IIIBF) for graduate degrees and professional training programmes for Islamic finance practitioners. Similarly, there are also established centers for Islamic banking and finance training in some departments of economics in some institutions in the country for the purpose of strengthening the Islamic financial institutions.<sup>59</sup>

#### 4. The Nature of the Islamic Financial Institutions and Shari'ah Advisory Board in Malaysia

The history of the Malaysian modern Islamic financial institutions can be traced as far back as early 1960s (precisely 1963) when the Muslims Pilgrims Corporation Fund (*Tabung Haji*) was established to control and coordinate the pilgrims fund and other related matters.<sup>60</sup> The establishment of such body marked as the beginning and foundation of an Islamic financial institution in the country. After two decades of its establishment, the Islamic Banking Act (IBA) and the *Takaful* (Islamic insurance) Act were enacted so as to pave way for establishment of Islamic banking and *Takaful* institutions respectively. Thus, in 1983 and 1984, the first Islamic bank and *Takaful* institutions were established by virtue of the aforementioned Acts respectively.<sup>61</sup> Close to a decade that was around early 1990s, the *sukuk* (Islamic bonds) markets in Malaysia have started gaining ground with huge number of companies participating in the investment. From that period henceforth, Malaysia has continued to recognize its success in the Islamic financial sector. Amongst the successes recorded were: the establishment of the Shari'ah Advisory Council (SAC) by the Central Bank of Malaysia (*Bank Negara Malaysia* [BNM]) and Securities Commission (SC) under their respective Acts (CBA 2009 and Securities Commission Act 1993); and setting up the Malaysian International Islamic Financial Centre (MIFC) in 2006 was also an achievement.<sup>62</sup> The shari'ah board which is otherwise known as the "Fatwa Board or Shari'ah Committee" in Malaysia, is heavily regulated and less dynamic compared to other countries in the world. It has given the Islamic financial institutions in the country a proper direction towards enhancement of the Islamic financial sector, and that has consequently made the country to recognize its success in economic and socio-political developments.<sup>63</sup>

The main function of the shari'ah advisory board is to issue fatwa on matters related to the going concern of Islamic financial institutions. However, the boards are prevented from using the *fatawa* which were issued by other Islamic financial institutions' advisory committee.<sup>64</sup> This is in order to

<sup>58</sup> Mufti Hassaan Kaleem, Meet the scholar,

[http://www.deloitte.com/view/en\\_XD/xd/viewpoint/2064992d33587210VgnVCM200000bb42f00aRCRD.htm](http://www.deloitte.com/view/en_XD/xd/viewpoint/2064992d33587210VgnVCM200000bb42f00aRCRD.htm) accessed on 9/10/2013

<sup>59</sup> Shehu Usman Rano Aliyu, Islamic Banking and Finance in Nigeria: Issues, Challenges and Opportunities, international Institute of Banking and Finance, Bayero University Kano, 26/Oct/2012, Munich Personal RePEc Archive (MPRA), Paper No.42573, available at <http://mpra.ub.uni-muenchen.de/42573>. accessed on 9/10/2013, pp 11-12

<sup>60</sup> Mohammad Zaid Mohd Zain et al, "Growth and Prospect of Islamic Finance in Malaysia" *International Conference on Social Science and Humanity IPEDR* Vol.5 (2011), P 182

<sup>61</sup> Ibid

<sup>62</sup> Price Water House Coopers, *Malaysia Asia's Islamic Finance Hub*, (PWHC, 2008), 15

<sup>63</sup> Ahmad Hidayat Buang, Personal Communication Via E-Mail, 28<sup>th</sup> October, 2013

<sup>64</sup> Mughees Shaukati, 17-20

forbid the practice of “*talfiq*”<sup>65</sup> within the Islamic banking sector.<sup>66</sup> In strengthening the function of the shari’ah advisory committee in Malaysia, the *Bank Negara Malaysia* BNM (Central Bank of Malaysia) issued out a framework known as “the Shari’ah Governance Framework 2011” so as to give the shari’ah advisory boards much powers for overseeing the Islamic banks in the country. The BNM mandated all the Islamic banks in Malaysia not only to comply with the *fatawa* issued by their boards but to also seek for their opinions in respect of any issue.<sup>67</sup> Similarly, in furtherance to ensure the effective shari’ah compliance in Islamic financial sector, the BNM has amended the Central Bank of Malaysia Act 1958 in order to improve the the functions of its shari’ah advisory council (SAC). The amendment has given the SAC the sole responsibility of overseeing all matters related to Islamic finance including settlement of disputes pertaining to shari’ah issues within the Islamic financial institutions.<sup>68</sup>

In addition, several laws were also amended in Malaysia in order to make shari’ah governance in Islamic financial institutions successful. For instance, it has recorded the amendments of Banking and Financial Institutions Act (BAFIA) 1984 and the Securities Commission Act 1993. To this effect, the Central Bank of Malaysia Act 2009 confirms the status of National *Shari’ah* Advisory Council (SAC) to be the sole authoritative body in Islamic finance. The Bank has also issued a guideline known as BNM/GPS1, for the purpose of effective governance of the shari’ah committee in the Islamic financial institutions. To complement this, the Securities Commission of Malaysia also issued the registration of *Shari’ah* Advisers Guidelines 2009 whose function is to set up the registration criteria of a *shari’ah* adviser in the capital market sector.<sup>69</sup>

The development of Islamic banking industry in Malaysia has been achieved and recorded, most especially between the periods of 1983 to 1993. Within that interregnum, Malaysia has liberalized on implementation of Islamic finance, thereby facilitating the enactments/amendments of some Acts, such as the Islamic Banking Act (IBA) 1983, the *Takaful* Act 1984, the Banking and Financial Institution Act (BAFIA) 1989, the Securities Commission Act 1993 and the Central Bank of Malaysia Act 2009.<sup>70</sup> The establishment of IBA has created an avenue for the establishment of the first shari’ah advisory board in 1983. Other shari’ah boards were subsequently established simultaneously together with their banks. As the time went on, in 1993 the Central Bank has also given the conventional Banks, a window operation for establishing the Islamic banking in the country.<sup>71</sup> By 1<sup>st</sup> May 1997, the BNM has established a highest and coordinating shari’ah body known as “Shari’ah Advisory Council SAC” under the BAFIA that is responsible for the shari’ah supervision of all the Islamic financial activities in BNM. This implies that other shari’ah committees (SC) of IFIs are to be considered as the shari’ah advisory bodies for their respective banks. Notably, the shari’ah committees (SC) are established under the BNM/GPS1 Enactment. Thus, the roles, duties (under its section 20) and scope of SC, and as well as their relationship with SAC have been also spelt out in same Enactment.<sup>72</sup> The provisions of the Enactment shall regulate

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<sup>65</sup> *Talfiq* is refer to as picking and choosing opinion and patching them together to pursue shari’ah exemption without observing their relevant controls or their context and circumstances, and consequently leads to adoption of irrelevant *fatawa*. See Amir Shaharuddin et al, Fatwa on Islamic Capital Market: A Comparative between Malaysia and Gulf Co-operation Council (GCC) Countries, ISRA Research Paper, (No. 40/2012), 6-7

<sup>66</sup> Amir Shaharuddin et al, Fatwa on Islamic Capital Market: A Comparative between Malaysia and Gulf Co-operation Council (GCC) Countries, ISRA Research Paper, (No. 40/2012), 6-7

<sup>67</sup> Ibid

<sup>68</sup> BNM/RH/GL/012-2, Islamic Banking and Takaful Department, Resolutions of Shari’ah Advisory Council of Bank Negara Malaysia, Pp 1-37 see also Zulkifli Hassan, Regulatory Framework of Shar’ah governance System in Malaysia, GCC Countries and UK, Kyoto Bulletin of Islamic Area Studies, 3-2 (March 2010), Pp 82-115

<sup>69</sup> Ibid

<sup>70</sup> Ibid

<sup>71</sup> Ibid

<sup>72</sup> See section 5 of the BNM/GPS1

only the Islamic financial institutions recognized by the law concern.<sup>73</sup> Similarly, the Enactment has provided for the qualification of the SC members; such as possession of at least a requisite knowledge, and having expertise or experience in Islamic jurisprudence or Islamic law of transaction (*Mu'amalat*).<sup>74</sup>

Most importantly, in the year 2003, the Central Bank of Malaysia Act 1958 was amended and to the effect that the amendment enhances the role of SAC. It attained the role of a sole authority committee that handles the shari'ah matters in Islamic finance in the banking sector generally. Meanwhile, the amendment stipulates that the BNM may establish an advisory council which shall regulate the Islamic banking business, *takaful* business, Islamic financial business, Islamic development financial business, or any other business which is based on the principles of Islamic law. The SAC can make any pronouncement related to banking and other related matters, and once it makes a pronouncement, it is binding upon the arbitration panel but not the courts. This position of the Act (as it then was) seems to be inactive in proffering solution to disputes in the financial sector. Consequently thereafter, the CBA has been further amended in July 2009 to incorporate all the lacunas identified.<sup>75</sup> Thus, in the New CBA, the framework for the governance of the SAC has been laid out in detail;<sup>76</sup> the status of the SAC as the highest and sole authoritative body in the Islamic financial sector remains intact, and the legal implication of the decisions (*fatawa*) deliberated upon by the SAC has been amended to an extent that it binds both the arbitration panel and the courts of law. In fact, the rulings of the SAC have binding force on the arbitration panels, courts of law, Islamic banking and *Takaful* (Islamic insurance) institutions. Similarly, the rulings of the SAC have also binding force on the shari'ah boards in the Securities Commission.<sup>77</sup>

Due to the significance of the shari'ah committees in Islamic finance, the Islamic banking Act (IBA) makes it a requirement for securing a license, by any financial institution that is willing to operate based on Islamic model, to make provision for shari'ah board in its article of association.<sup>78</sup> Similarly, the BAFIA also provides for the establishment of the SC to advise the bank on matters relating to Islamic financial business.<sup>79</sup> In respect of *Takaful* (Islamic Insurance), the *Takaful* Act provides that the Director General shall also refuse to register an applicant unless he is satisfied:

“(a) that the aims and operations of the *Takaful* business which it is desired to carry on will not involve any element which is not approved by the *Shari'ah*; and  
(b) that there is in the Articles of Association of the *Takaful* operator concerned provision for the establishment of a *Shari'ah* advisory body, as may be approved by the Director General, to advise an operator on the operations of its *Takaful* business in order to ensure that it does not involve in any element which is not approved by the *Shari'ah*.”<sup>80</sup>

Apart from the institutions established under the IBA 1983, the BAFIA 1989 and *Takaful* Act 1984, Shari'ah Committee (SC) is also established under some other enactments such as the Development Financial Institutions Act 2002.<sup>81</sup>

<sup>73</sup> See section 6 of the BNM/GPS1

<sup>74</sup> See section 11 of the BNM/GPS1

<sup>75</sup> Zulkifli Hassan, Regulatory Framework of Shar'ah governance System in Malaysia, GCC Countries and UK, Kyoto Bulletin of Islamic Area Studies, 3-2 (March 2010), 82-115

<sup>76</sup> See Chapter VII, Sections 51-58 of the CBA

<sup>77</sup> See the Registration of Shari'ah advisers Guidelines (2009) under section 377 of the Markets and Services Act 2007.

The section provides for the registration of advisers in matters regulated and supervised by the Securities Commission

<sup>78</sup> Section 3 (5) (b) of the IBA, 1983, the section provides: “The BNM shall not recommend the grant of a license, and the Minister shall not grant a license, unless he is satisfied that there is, in the articles of association of the bank concerned, provision for the establishment of shari'ah board.”

<sup>79</sup> Section 124 (7) of the BAFIA, 1989

<sup>80</sup> Section 8 of the *Takaful* Act 1984

<sup>81</sup> Zulkifli Hassan, Regulatory Framework of Shar'ah governance System in Malaysia, GCC Countries and UK, Kyoto Bulletin of Islamic Area Studies, 3-2 (March 2010), 82-115

To sum up the discussion, the shari'ah advisory boards in Malaysia have been statutorily backed up in such a way that they can perform same role as idle state fatwa committee. Both the SC and state fatwa committee are primarily responsible for the issuance of fatwa. However, the *fatawa* to be issued by the former should be limited to matters related to transactions/contracts (*Mu'amalat*). In a similar vein, while the SAC was established to deal with and oversee any matter related to Islamic finance within Islamic financial institutions established under the IBA, CBA and *Takaful* Act, the National fatwa Committee was established to issue fatwa for the country on all matters referred to it by the conference of Rulers (*Malis Raaja-Raja*). While the SAC has been placed under BNM and IFIs, the National fatwa Committee is under the supervision of the Department of the Islamic Affairs (*Jabatan Kemajuan Islam Malaysia JAKIM*)<sup>82</sup> Furthermore, a decision of the shari'ah advisory boards binds only their respective IFI, whereas, the fatwa committees' decision, if assented and published in the Gazette, shall bind everyone in the country.<sup>83</sup>

## 5. Conclusion

The role of fatwa and fatwa issuing bodies in Islamic financial institutions has been understood generally as a pillar to their survival. Development of Islamic banking industry and their shari'ah advisory bodies in Malaysia has been successfully recorded due to the enactment, amendment and liberalization of legal framework on Islamic finance. This has made the financial institutions and their regulatory bodies to function and operate freely and autonomously. However, in Nigeria the legal framework on Islamic finance is not distinctive and autonomous. Their regulatory framework on shari'ah governance is always subjective to the Central Bank Act and Guidelines; it is based on that fact that the legal basis for establishment and governance of the Islamic financial institutions in Nigeria *per se* revolves around the Central Bank Act and Guidelines. In fact, the real challenge faced by the institutions nowadays is, how to ensure absolute and uninterrupted compliance of its products with the provisions of shari'ah. Of course, this must be attained only if there is an independent legal framework and effective shari'ah supervision in place. To this end, the paper suggests as follows:

- (1) In general sense; the Federal Government of Nigeria should adopt the Malaysian model of Islamic financial system, since both countries mostly share common features;
- (2) In specific sense; the Government in collaboration with CBN should do the following:
  - (a) Facilitate the amendment of the relevant legislation such as the constitution of Nigeria, BOFIA and CBN Act/Regulations in order to pave way for enacting a suitable Islamic financial regulatory framework;
  - (b) Enact a distinctive Islamic financial regulatory framework that can independently regulate for the Islamic financial activities in the country;
  - (c) Establish an independent and competent shari'ah supervisory body that can supervise and advise Islamic financial institutions in the country;
  - (d) And any other things that it's deemed fit necessary for enhancing the governance of Islamic financial institutions within the realm of the law.

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