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Conference Proceedings Report

Shariah Audit Conference 2020

Mainstreaming Shariah Audit in Islamic Finance 1st - 2nd December 2020 Tuesday - Wednesday















Conference Overview

Over the years, the global Islamic finance industry has consistently registered double-digit growths, buoyed by sturdy economic activities among major jurisdictions such as Malaysia. Robust government investment and spending on infrastructure development have underpinned the growth of Islamic finance. On the back of this phenomenal growth, market players must ceremoniously ensure that Islamic finance practices pivot around the essence of Shariah requirements, which includes areas related to governance and compliance.

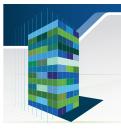
As evident in Malaysia's case, the trajectory of Islamic finance has been propelled by a solid regulatory landscape as well as a robust Shariah governance framework. There is an urgent need for all market players to embrace the importance of Shariah Audit in ensuring proper governance and compliance culture to navigate the opportunities and challenges in the Islamic finance industry. Latest updates on Shariah Audit and its importance as a key building block are the main highlights of the conference.



Attendees

The conference recorded 241 international and local attendees from the industry and academia, among others comprising the following:

- Academicians
- Accountants
- Consultants/Advisors
- External and Internal auditors
- Risk Managers/Officers
- Shariah Advisors
- **Shariah Auditors**
- **Shariah Compliance Officers**
- Shariah Researchers
- Undergraduate and Post-graduate students



About the Organisers



Established under the Accountants Act 1967, MIA is the national accountancy body that regulates, develops, supports and enhances the credibility status and interests of the profession in Malaysia. MIA accords the Chartered Accountant Malaysia or "C.A. (M)" designation. Presently, there are more than 35,500 MIA members making their strides in businesses across all industries, public practices, public sector and academia in Malaysia and around the world.

MIA international presence and connections are reflected in its membership of regional and international professional organisations such as the ASEAN Federation of Accountants (AFA), and the International Federation of Accountants (IFAC). MIA is a leading provider of continuing professional education for the accounting fraternity. MIA won the Human Resource Minister Award under the Training Providers category for its exceptional contribution and role in the human resources development sector of Malaysia.



IBFIM is a lifelong learning institution which aims to be the global reference centre for Islamic finance (IF). Our programmes are designed to ensure attainment of technical proficiency levels to fulfill job requirements and support professionalisation of the IF industry. IBFIM key programmes are developed based on IBFIM Qualifications Framework and are accorded Full Accreditation by the Finance Accreditation Agency (FAA) to maintain the quality of the programmes.

IBFIM has also been providing business and Shariah advisory services to the industry, since 2001. IBFIM scope of advisory services extends to other sectors beyond the banking industry namely cooperatives, Islamic fund management companies, takaful operators, government-linked companies and technology-based companies.

IBFIM has scaled up its capacity and capability in offering its virtual services. IBFIM's clients (locally and globally) have the options to engage either face-to-face or virtual training to fulfill their learning needs through IBFIM Centralised Learning System (ICLASS) and virtual webinar platforms.

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Dr. Veerinderjeet Singh

President, Malaysian Institute of Accountants (MIA)



Keynote Address by

YBhg. Tan Sri Abdul Wahid Omar

Non-Executive Chairman, Bursa Malaysia & Chairman, Universiti Kebangsaan Malaysia (UKM)











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Session 1 Leaders' Forum on Shariah Audit





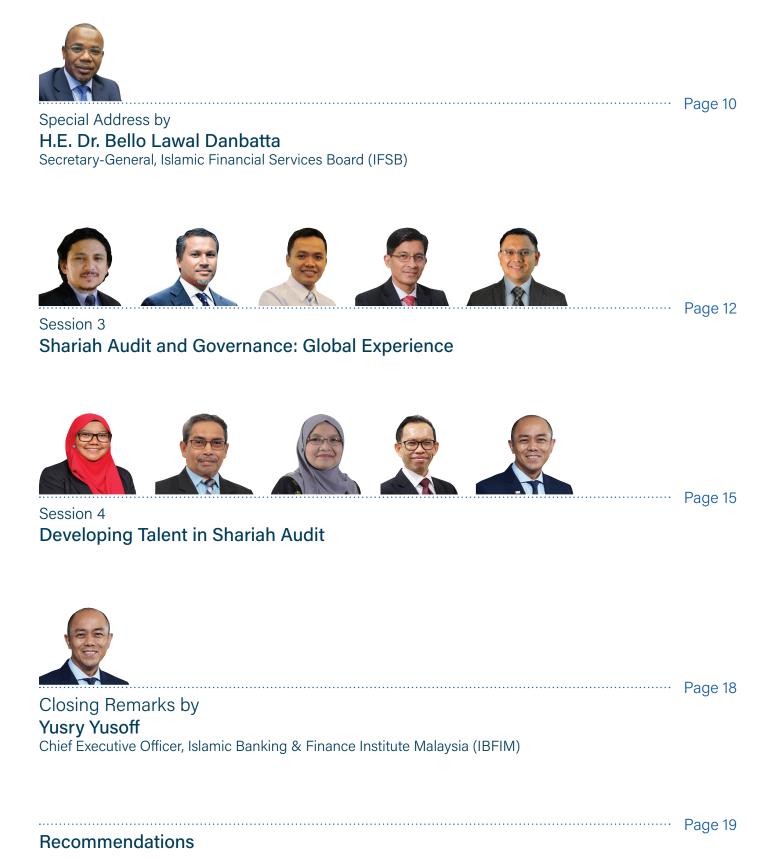






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Session 2 Institutional Integrity through Shariah Audit



Welcome Remarks by Dr. Veerinderjeet Singh President Malaysian Institute of Accountants (MIA)



- YBhg. Tan Sri Abdul Wahid Omar, Non-Executive Chairman, Bursa Malaysia & Chairman, Universiti Kebangsaan Malaysia (UKM)
- **Distinguished Guests**
- Ladies & Gentlemen

Good morning and welcome to the Shariah Audit Conference 2020, a joint initiative by MIA and the Islamic Banking & Finance Institute Malaysia (IBFIM). Thank you all for attending.

Today's Conference is an important initiative for nation building, as it seeks to develop talent in Shariah auditing to meet the needs of the Islamic finance sector. We have more than 150 participants attending today.

This Conference is also aligned with Bank Negara Malaysia's policy document on strengthening Shariah governance implementation within Islamic Financial Institutions.

As a Shariah audit is considered a new competency area, the number of qualified Shariah auditors is relatively small. MIA as the regulator and developer of the accountancy profession is delighted to work together with IBFIM, as IBFIM aims to produce qualified Shariah auditors with an integrated knowledge of Shariah, accounting, auditing, risk and governance via its certified professional Shariah auditing qualification.

MIA members who are auditors are well qualified to take up professional qualifications in Shariah audit, as both financial and Shariah audits draw upon the similar underlying skillsets and expertise. Shariah auditors are required to be equipped in the following areas - shariah, governance and auditing, accounting and reporting for Islamic finance transactions, shariah risk management and internal controls, shariah audit planning, shariah audit fieldwork and communications¹.

MIA members who are auditors are well qualified to take up professional qualifications in Shariah audit, as both financial and Shariah audits draw upon the similar underlying skillsets and expertise.

https://ibfimonline.com/programmes/qualification/ cpsa/#1459420092425-29dd0662-7a34

Therefore, MIA's collaboration with IBFIM could potentially produce a pool of competent Shariah auditors who will uphold Shariah governance within Islamic Financial Institutions (IFIs) and play an integral role in strengthening the risk management, stability and integrity of the Islamic financial system. This in turn will protect stakeholders and is aligned well with upholding good governance and the public interest, which is MIA's top priority as the regulator of the accountancy profession.

We are also pleased to note that this Conference adds another dimension of value to MIA's advocacy for strengthening Islamic finance, supporting our nation building purpose. Earlier this year, we launched the Islamic finance textbook for applying Malaysian Financial Reporting Standards (MFRS) for Islamic finance transactions. This textbook addresses the reporting complexities and challenges faced by IFIs in order to bridge the current knowledge gap and has been very well received. It can also be highly useful for Shariah auditors who must be well-versed in accounting, reporting and auditing of Islamic finance transactions. MIA has also just concluded the second year of the multi-stakeholder Islamic Finance Mini Pupillage Programme, which seeks to train a larger pool of Islamic finance professionals and address the shortage of financial experts in Islamic finance.

Ladies and gentlemen, before I conclude my remarks, I wish to thank IBFIM as our co-organiser and all our distinguished speakers and panellists for making time to be here.

We are honoured to have YBhg Tan Sri Abdul Wahid Omar, Non-Executive Chairman, Bursa Malaysia who is recognised for his championship of corporate governance to deliver the keynote address in just a few moments.

Going forward, MIA will continue to improve our capacity and competency building efforts for Islamic finance. Our collaborative initiatives in the pipeline include upcoming publications on Shariah audit, specifically best practice guides on shariah audit, which we believe will help strengthen the development and regulation of Islamic finance, not only in Malaysia but in the global Islamic finance markets.

Before we end, I would like to take this opportunity to thank our sponsors: Platinum sponsors - Finance Accreditation Agency, FWD Takaful, MBSB Bank, AIA Public Takaful, SME Bank and Bank Pertanian Malaysia (Agrobank). Gold sponsor - AFFIN Islamic Bank, CIMB Bank, Bank Islam Malaysia Berhad and Bursa Malaysia. Silver Sponsors - Ernst & Young (EY), Islamic Markets.Com, The Malaysian Institute of Certified Public Accountants (MICPA) and The Malaysian Insurance Institute (MII) and all our supporters.

On that note, I wish you a productive conference. Thank you!

Keynote Address by YBhg. Tan Sri Abdul Wahid Omar Non-Executive Chairman, Bursa Malaysia & Chairman, Universiti Kebangsaan Malaysia (UKM)



Bismillahirahmannirrahim Assalamu'alaikum warohmatullahi wabarakatuh.

Distinguished Speakers

Ladies and Gentlemen,

It is indeed an honour to be able to share my thoughts with you today.

Let me start by thanking the Malaysian Institute of Accountants and Islamic Banking & Finance Institute of Malaysia for co-organising this conference, as well as the event sponsors for the contribution towards the growth of Islamic finance.

Convening at the first Virtual Shariah Audit Conference 2020, I am encouraged to see the strong line-up of panellists, all highly respected leaders in the industry. I certainly look forward to hearing their valuable insights, developments and opportunities in Shariah audit, governance and compliance.

For today, allow me to cover three areas in my address. Before we discuss "Mainstreaming Shariah Audit in Islamic Finance", let me first give my view on the promising growth of Islamic Finance in the Post-COVID-19 world.

Promising Growth of Islamic Finance

The COVID-19 pandemic has resulted in challenges to people's livelihoods and the economy.

According to the Sustainable Development Goals Report 2020²:

- An estimated 71 million people are expected to be pushed back into extreme poverty;
- Some 1.6 billion workers in the informal economy would have seen their income fallen by 60% in the first month of the crisis;
- More than 1 billion slum dwellers worldwide are acutely at risk from the effects of COVID-19, suffering from lack of adequate housing, overcrowding and limited access to formal healthcare facilities.

Many now realise that without drastic action, adapting to such unprecedented impact in the future will be more difficult, expensive and have a significant effect on our climate, health and biodiversity.

As policies slowly shift towards ensuring sustainable development, Sustainable and Responsible Investments, or SRI, will help broaden the reach of Islamic finance, due to the close alignment and high degree of overlap.

Hence, the long-term potential for Islamic finance remains promising globally.

²https://www.un.org/development/desa/en/news/sustainable/sustainable-development-goals-report-2020.html

Malaysia is widely acknowledged as being at the forefront of Islamic finance, mainly due to a conducive ecosystem, effective regulatory framework and strong human capital development.

We achieved some noteworthy milestones with several industry "firsts" and innovations for the Islamic fund management resulting in a wide array of Islamic products introduced in the market. Today, Malaysia is the largest global Islamic fund in terms of Asset under Management.

In the equity market, Bursa Malaysia's Shariah-compliant investing platform, or Bursa Malaysia-i, positions the Exchange as a global marketplace for Shariah listing and investments.

As at October 2020, 718 out of 937 listed companies, or 77% are Shariah-compliant, which also makes up about 72% of total market capitalisation.

Getting Shariah Audit into the Mainstream

Ladies and Gentlemen,

It is easy to see the appeal of Islamic finance, due to its principles of inclusivity and the potential to promote financial stability. However, the high increase in demand for Shariah-compliant financial products has raised the importance of more refined investment screening process and audit.

Some of the issues faced are the inconsistencies in screening methods across different countries and organisations. Having too many different methodologies adds cost, and in the long run, could hamper the growth of Islamic finance.

Non-compliance with Shariah principles pose an area of risk that could translate into legal, image and reputational risks, which have far-reaching consequences for the Islamic financial system.

Stakeholders also want to ensure that companies in which they have an interest in are complying with the Shariah requirements and are managed responsibly.

There is growing awareness, especially among Islamic institutions, of the importance of Shariah audit in contributing towards achieving the objectives of the *Maqasid Al-Shariah*.

Getting Shariah audit into the mainstream is an initiative that ensures compliance and maintains the credibility of Islamic finance among stakeholders. It will provide stakeholders with greater independence of Shariah assurance.

Moreover, the scope of conventional financial audit is inadequate to fulfil the needs of stakeholder when it comes to adhering to Shariah principles in business transactions and operations. They will also lack the skills to audit large numbers of transactions for Shariah compliance.

The assurance of Shariah compliance, through the audit function, is fundamental in upholding the integrity of any institutions at large. It also promotes a diverse role in improving the competitiveness of the institutions through effective mitigation of Shariah non-compliance risk and embracing Shariah culture within the institution itself.

Shariah audit is conducted with the purpose to add value and improve on the governance, risk management and compliance with business operations, mainly focusing on the objective of ensuring a sound and effective internal control system. In this instance, the Shariah Supervisory board and Shariah auditor plays a significant role in ensuring the institution operates in accordance with Shariah rulings.

It has been argued that the role of financial reporting and auditing should not be confined to the needs of investor decision-making but should be viewed with more focus on corporate governance.

With Shariah governance being the bedrock of Islamic finance, it upholds the principles of good corporate governance. It can universally extend beyond Islamic finance to all industries to ensure best practices are adopted in the management and operations of companies, whether sole proprietorship, cooperatives, GLCs, PLCs or financial institutions alike.

As a next step, introducing an appropriate Shariah audit framework will help in creating robustness in the industry. It is crucial for external Shariah auditors for the financial Islamic institutions to remain independent and transparent and avoid internal Shariah auditors auditing their own products and operations.

Increasing Talent in Shariah Audit

Ladies and Gentlemen,

Despite the importance of Shariah audit, there has been little understanding of its implementation towards an effective and efficient Shariah audit from the human capital perspective. This brings me to the third part of my address, on the need to increase talent in Shariah audit.

In Malaysia, the current focus is primarily on internal Shariah audit, which has raised several debates on its independence. Numerous challenges, including the limited availability of qualified resources, have prevented the successful implementation of external Shariah audits

In terms of industry experience, a 2013 study highlights that only 5.9% of auditors are qualified in both fields of Shariah and accounting. Out of these Shariah auditors, only 69% practise Shariah auditing in Islamic Financial Institutions³.

The scarce resource of both shariah and auditing qualifications as well as the lack of experience poses a threat to Shariah audit independence which may adversely affect the integrity of organisations. Moreover, the competency requirements for Shariah auditors have yet to be fully developed.

3http://www.m-hikari.com/ref/ref2018/ref1-4-2018/p/ref14-2018.pdf

With this regard, the call to fulfilling this gap needs to gain more attention. In Malaysia, there are only a few local universities that offer Shariah Audit as part of the subject in accounting courses. More notably, only Universiti Sains Islam Malaysia offers a course specialised in Shariah Audit.

On top of that, professional training is scarce since there are only a few local training agencies that provide professional certification to the Shariah audit practitioner.

Professional qualifications, such as the Certified Professional Shariah Auditor (CPSA) offered by IBFIM is essential in developing the required pool of Shariah auditors, in line with the aspirations of meeting the regulatory requirements.

Such certification does not only augment the existing skillsets of the auditors but has the potential to professionalise the role into a new profession. Since its launch, CPSA has produced 36 certified holders to serve the industry.

The recognition of CPSA as a professional programme by the Ministry of Education through its Graduate Employability (GE) initiative has yielded significant results. Through this initiative, over 300 final year undergraduates from 13 public universities throughout the nation have enrolled for the certification.

The Islamic finance industry has also played a commendable part towards upskilling and reskilling talent within the Islamic financial institutions. Currently, more than 100 personnel from 11 Islamic banks in Malaysia are enrolled in the certification. It is important that the Malaysian Institute of Accountants help facilitate the implementation of a comprehensive and integrated Shariah auditing framework in order to cater for the ever increasing number of Islamic financial institutions in Malaysia.

CPSA has also received full-accreditation from the Finance Accreditation Agency in efforts to ensure the certification meets industry and quality professional learning and development in the financial services industry.

Closina

Ladies and Gentlemen,

There is a considerable growth potential for firms to offer Shariah auditing services to institutions outside of Malaysia as part of the country's Islamic finance ancillary services.

However, issues in terms of Shariah auditing standards, qualifications and independence needs to be resolved for the smooth development of the Islamic finance industry.

I certainly look forward to hearing the deliberations and invaluable insights that will be shared by our respected panellists in these areas.

On that note, I wish everyone a productive conference ahead.



Synopsis

Shariah audit has a vital role in assuring compliance and governance of Shariah-based institutions, particularly in its operations as well as the offering of its Shariah-compliant products and services to the mass market. Through the forum, the leaders and decision-makers will share insights on the importance and potentials of Shariah audit towards best practices in IFIs. This session provided valuable insights on Shariah audit roles and deliberation of prevailing issues and mitigation efforts in addressing Shariah non-compliance and simultaneously enhancing Shariah governance within the IFIs in line with the new requirements of the Shariah Governance Framework.

Session Insight

The moderator, Ibrahim Sani, Producer/Executive Editor, Astro Awani, began the session by highlighting the key issues raised by Tan Sri Abdul Wahid Omar during his Keynote Address, specifically the presence of inconsistencies across the board of various industries and companies pertaining to Shariah audit; and talent depravity wherein the industry is severely deprived of qualified talents to execute Shariah audit. A point was also raised as to whether companies should consider offering services in terms of Shariah audit.

What comes first? Do we create the methodology, or do we create more talents?

Ibrahim Sani

In solving these problems, the moderator raised an interesting question of "What comes first? Do we create the methodology, or do we create more talents?"

The panellists, in their respective roles as leaders and decision-makers, shared their valuable insights on the significance, potentials and persistent challenges towards addressing Shariah non-compliance and how best to enhance Shariah governance in line with the new Shariah Governance Framework.

Datuk Nik Mohd Hasyudeen Yusoff, Group Managing Director and Chief Executive Officer, Lembaga Tabung Haji, started the session by stating that in order for an institution to achieve *Maqasid Al-Shariah*, the adoption of Shariah principles must be in its entirety. He explained that individuals and institutions will be able to experience the beauty of Shariah principles by fully supporting Shariah-compliant products and the conduct of Shariah audit.

Notwithstanding this, due to the issue of inconsistencies in screening methods and views adopted by different institutions, it was therefore important to look at certain scope and parameters that could be agreed upon by all parties.

Individuals and institutions will be able to experience the beauty of Shariah principles by fully supporting Shariah-compliant products and the conduct of Shariah audit.

Datuk Nik Mohd Hasyudeen Yusoff

He highlighted several crucial factors to be considered in the process of doing so, such as competency, broadness of knowledge, and experience in dealing with emerging ideas and concept.

Although different institutions use a variety of methodologies in their auditing process, at the end of the day, the same standards will be referred to. This was especially important in the context of Shariah auditing, as the compliance with *Maqasid Al-Shariah* will ultimately ensure overall effectiveness.

One of the main reasons why there has been a constant challenge in getting Shariah audit into the mainstream was that it has always been an after-thought, according to Dato' Hj Mohd Redza Shah Abdul Wahid, Chairman of The Board, Lembaga Amanah Yayasan Pembangunan Ekonomi Islam Malaysia (YaPEIM). As opposed to the organised structure of conventional audit, Shariah audit has yet to have one. He went on to say that the growing awareness amongst institutions has led to the significance of structuring Shariah audit. By doing so, every institution would then be able to play specific roles towards achieving the objectives of the Shariah principles.

In stating his views, Nazlee Khalifah, Chief Executive Officer, Affin Islamic Bank Berhad, then explained how crucial it was for customers and distributors to first have a common understanding of a bank's compliance procedures pertaining to Shariah principles.

With regard to this, particularly, in banks, it was not just an understanding on the method and manner of selling Shariah-compliant products or the conduct of Shariah audit, rather, it was to provide a platform where customers and distributors could be given clarifications as to how such principles work, whilst at the same time ensuring that the bank achieves its deliverables and desired outcomes.

It is crucial for customers and distributors to first have a common understanding of a bank's compliance procedures pertaining to Shariah principles.

Nazlee Khalifah

He went on to explain that there must be clarity in this matter to avoid banks from facing risks of Shariah non-compliance. With regard to the methodology that should be referred to by Shariah auditors, he felt that it was vital to look at an organisation's overall objectives, alignment and direction, to ensure that the context was in its proper place.

On top of this, every institution plays a role in gearing up towards Shariah audit, and once this has been successfully internalised, only then will it eventually grow into the mainstream.

In sharing his opinions, Mr. Nik Shahrizal Sulaiman, Partner/Islamic Finance Leader, PwC Malaysia, stressed the importance of fully comprehending the expectations of shareholders on the concept and application of Islamic finance, as these expectations have evolved throughout the years.

On top of having strict compliance with the principles of Shariah, the perspective has now been more aligned towards the integration of the Environmental, Social and Corporate Governance (ESG) factors within an organisation. For this reason, it was significant for Shariah auditors to embrace the strategy of making Islamic Finance 'tayyiban', in addition to upholding halal virtues.

The moderator then queried the panellists on the challenges in increasing Shariah audit talents towards creating a vibrant industry. To this question, Datuk Nik Mohd Hasyudeen Yusoff responded that although it was necessary to have a rise in Shariah audit talent, the demand for Shariah auditors should come naturally. An example of this was the incorporation of Lembaga Tabung Haji, where Shariah principles have been embedded in the culture from the very beginning of its set-up.

Because of this, over the years, Shariah auditing has been integrated as part of its overall annual audit and internal audit process. He noted the increasing demand for qualified Shariah auditors; however, it was his strong view that the concept of nurturing Shariah audit within the industry should happen at a gradual pace.

A more crucial focus should instead be on the institution's capabilities, and the required skill sets of Shariah auditors, as these he believed, will eventually lead to a more all-encompassing Shariah profession.

The growth of Shariah audit has reached a point where it was timely for external auditors to also enhance their skills on the subject matter.

Dato' Hj. Mohd Redza Shah Abdul Wahid

In opposing, Dato' Hj Mohd Redza Shah Abdul Wahid said that having a proper set of regulations was the best way forward to ensure proper adherence to Shariah principles, and in his view, this would then be the solution to complement the increased demand of Shariah auditors within the industry. He also noted that the growth of Shariah audit has reached a point where it was timely for external auditors to also enhance their skills on the subject matter.

Nazlee Khalifah added that at the moment, Shariah auditors, with specific reference to banks, were only focused towards functions revolving around processes and reviews of contractual documents. A crucial step that organisations and Shariah talents need to take in order to create more vibrancy in the Islamic finance industry was to ensure that they take on bigger roles in order to get further validation from third parties.

In analysing the issue, Nik Shahrizal Sulaiman strongly felt that there were two important issues to consider, firstly, due to the different components within an institution, the articulation and alignment of strategic objectives should be looked into to ensure that there was a common understanding of the role of Shariah auditors. Secondly, was to find the best techniques towards getting more efficiency out of these processes. With regard to the former, it was vital for discussions to take place amongst the board, Shariah Committee and Shariah auditors to ensure that the strategic objectives of all parties were aligned.

In terms of efficiency, Shariah auditors must make continuous efforts to ensure their improved competencies through the use of technology, for example Artificial Intelligence (AI), as this would be the best method to apply in order to save their time and energy. These factors, coupled with enhanced training and qualifications will then allow Shariah auditors to play a more effective role in the industry. In response to a question from the floor as to the scope of modern Shariah auditors, Nik Shahrizal Sulaiman quoted an example of a financial statement review, where it goes back to the objective of reviewing the financial statements.

He explained that whereas an external auditor would be in a better position to ensure that the financial statements were in compliance with international financial standards, Shariah auditors on the other hand, will look into elements that might indicate Shariah noncompliance.

As to whether templates and checklists were integral in an audit procedure, he continued by saying that auditors would not be able to conduct holistic audit if they did not have sufficient skills and knowledge of the said industry.

Templates and checklists were useful for specific audit checks and consistency, however an over reliance on them could lead to some form of confusion and misrepresentation, which could eventually affect the entire Islamic finance fraternity. Therefore, rather than solely depending on these documents, auditors – external, internal and Shariah – should focus on making sure a holistic view was given during the conduct of audit.

Auditors would not be able to conduct holistic audit if they did not have sufficient skills and knowledge of the said industry.

Nik Shahrizal Sulaiman

He noted the current challenges faced by auditors during the COVID-19 pandemic situation. However, he believed that Shariah auditors could strengthen their roles by working towards obtaining information via digital means, and to employ the best approaches in facilitating their clients during an audit exercise on how the burdens of their clients could be eased.

When asked whether Shariah auditing will be the superseding authority in all circumstances, Nazlee Khalifah was of the view that Shariah auditors formed part of an internal audit team who were responsible to ensure that all processes and documents were Shariah-compliant. Due to the fact that external auditors will conduct their audit based on the findings made by the Shariah auditors, having sufficient skills in Shariah auditing will enable the external auditors to conduct their audit more effectively. Dato' Hj Mohd Redza Shah Abdul Wahid added that notwithstanding the prevalence of the external auditor's role, eventually the role of Shariah auditors too will be strengthened. In order for Shariah auditors to have a better standing in the market, they need to be able to provide assurance that they are qualified, and have the relevant skill sets. He believed that professional bodies could look into raising the standards of Shariah auditors within the market, specifically in the Islamic financial institutions.

The moderator concluded the session by highlighting several key factors to ensure that *Maqasid Al-Shariah* is respected and achieved in its entirety, and that the integrity of Shariah assurance is effectively managed. Amongst others, there has to be a common understanding on the clarity of scope, definition setting, and skill sets of Shariah auditors. Simultaneously, Shariah auditors need to be fit for purpose and take on their respective functions in adding value to the governance of an institution, particularly in assisting the institutions towards complying with Shariah principles. To avoid further confusion in the industry, regulators, professional bodies and associations all play significant roles in setting these standards and in developing talent management to address the needs of the industry.



Synopsis

The assurance of Shariah compliance through the Shariah audit function is crucial in upholding the integrity of Islamic Financial Institutions (IFIs). Hence, an effective Shariah audit function ensures an efficient internal control system for Shariah compliance in IFIs. This session discussed institutional arrangements and requirements that need to be considered to ensure effective implementation of Shariah audit in enhancing the integrity of IFIs.

Session Insight

How do Shariah based institutions embrace the directives of Shariah assurance and audit within internal governance? This was the first issue elaborated at length by Dr. Hurriyah El Islamy, Executive Board Member, Foreign Investment and International Relations, Badan Pengelola Keuangan Haji & Member of Awqaf Properties Investment Fund Supervisory Committee, Islamic Development Bank, where she explained that with regard to its implementation in Malaysia, the matter can be executed using either an assimilation approach or by having a dedicated unit within an audit function.

By having a clear Shariah auditing framework, there will be a comprehensive set of guidelines, policies and SOPs to differentiate between the roles and functions.

Dr. Hurriyah El Islamy

Using assimilation as an approach has proven to be rather challenging for most institutions. She clarified that the reason behind this was the difficulty in acquiring internal auditors with the requisite Shariah knowledge and necessary qualifications to undertake their functions. Because of the disparity that exists in such a situation, staff needed to be trained and retrained, which ultimately led to a slow-moving process of Shariah implementation within the said institution. On the other hand, institutions that have invested in a new unit to specifically handle Shariah audit functions were ultimately faced with the need of having to increase more headcounts and new hires. This in turn meant that the new staff required more time to adapt to their new functions.

She then shared several highlights of her experience in the process of institutionalising Shariah audit through internal control functions amongst the financial institutions in Bahrain. Whilst compliance with Shariah principles was merely a separate part of the audit process and only conducted on a consultancy basis pre-2007, it had significantly progressed until 2017 onwards where Shariah was then seen in a holistic approach within an institution's business processes and operations. Based on the evolution of the implementation of Shariah in the respective institutions, she was of the strong view that a full-fledged Shariah institution could avoid any forms of potential gaps and mismatch.

The moderator, **Ibrahim Sani**, then invited the next panellist to share how institutional integrity could be attained with the implementation of Shariah audit, based on his personal experiences and insights on the matter.

Datuk Dr. Mohd Daud Bakar, Chairman, Shariah Advisory Council Bank Negara Malaysia, Securities Commission of Malaysia & The Labuan Financial Services Authorities, expressed his delight at the industry's progress pertaining to the acceptance of, and compliance with the Shariah principles. He was of the view that in addressing challenges such as inconsistency in the screening of Shariah talents and talent depravity within the industry, there has to be an understanding that the progress was in relation to the behaviour of people. He quoted that there was a need "to move away from terminologies and mechanical compliance, and instead,

to look at substantive compliance and emerging trends of potential non-compliance".

When technology is applied, there will be transparency and unambiguity, which have always been the key factors affecting the effectiveness of Shariah audit.

Datuk Dr. Mohd Daud Bakar

He gave an interesting account as to how technology could be maximised in Shariah audit, where he clarified that it should not merely be used to analyse on a periodical basis, but rather for it to be utilised it to the extent that auditors could make audit assessments on a real-time basis, thus simplifying the processes involved. He also emphasized that when technology is applied, there will be transparency and unambiguity, which have always been the key factors affecting the effectiveness of Shariah audit.

Shaikh Muhammad Abdul Mubeen, Shariah Board/Committee Member for Standard Chartered Bank Pakistan & Malaysia, then shared some updates on the implementation of the Shariah Governance Framework in Pakistan. He pointed out that it was crucial for integrity to be achieved at all times throughout Shariah auditing, and mentioned two significant processes that were involved, namely during the pre-launching and post-launching of a product.

Prior to any product launch, the Shariah Committee will be heavily involved in the structure development, and this would mean that Shariah assurance, compliance processes and policies will start from this point forth. He further explained that once the product has been launched in the market, it falls within the purview of the Management. The processes will henceforth be regulated, depending on the frequency of reviews and audits.

In response to a question from the floor, he further explained that there was a necessity for the laws to be changed in order for Shariah to be fully implemented by the Islamic financial institutions. Notwithstanding this, due to the existence of numerous jurisdictions, a full and immediate implementation would not be easy, therefore an option would be either to have a minimum number of Shariah requirements to be fulfilled, or for Shariah scholars to make their opinions on the basis of *ijtihad!*

As the process of Shariah audit was to provide independent assessment and assurance, internal auditors should not work in fear or favour. In view of this, Mohd Khaidzir Shahari, Board of Governor, Institute Internal Auditors Malaysia/Head of Risk Consulting KPMG, suggested that Shariah auditing should not be done simply on an ad-hoc basis, rather, it has to be properly planned and periodically conducted.

Critical thinking skills should be cultivated in all audit processes, and in any given circumstances, Shariah auditors and internal auditors should work together in providing a new audit perspective. It was timely and crucial for auditors to evolve if they need to reach a certain standard within the industry, and to attain this, it was

necessary for them to be equipped with in-depth industry knowledge and a diversified set of skills. He added that the internal audit delivery model must be revisited to contain four key elements, quoting, "the positioning of the internal audit", "people that the internal audit is resourced with", "process", and "perception". It was also important for audit to have a change management programme.

When questioned by the moderator as to the overlapping functions of Shariah review and audit, the panellists were unanimous in that there should be a clear distinction between the roles, and gave their suggestions on how to approach the matter with clarity. Dr. Hurriyah El Islamy said that by having a clear Shariah auditing framework, there will be a comprehensive set of guidelines, policies and SOPs to differentiate between the roles and functions.

In concurring, Mohd Khaidzir Shahari said that the clarity of such a framework can warrant an all-encompassing Shariah audit process. He added however, that it also depended on the maturity, proactiveness and effective communication of the Head of Internal Audit in ensuring that the functions of respective personnel do not overlap. He also thought that adding more personnel to solve problems of such nature was not considered as a key success factor. On this matter, Shaikh Muhammad Abdul Mubeen felt that the presence of Shariah scholars in the Shariah auditing team was vital as they could offer guidance and expertise on certain subject matters, as and when required of them.

To reach certain standard within the industry, it is necessary for auditors to be equipped with in-depth industry knowledge and a diversified set of skills.

Mohd Khaidzir Shahari

The panellists, however, had separate views as to whether there was a necessity to have a new set of laws to address inconsistencies pertaining to Shariah across all countries. Dr. Hurriyah El Islamy felt that despite consistency being the key issue to address such variances in the industry, establishing new laws would not immediately resolve any problems. She shared the success story of Bahrain's corporate governance implementation, where institutions were required to comply with a set of standards, with the option of providing an explanation, should there be a peculiarity or a special condition.

In concurring, Datuk Dr. Mohd Daud Bakar shared the same sentiments that it was unnecessary for the establishment of more laws on Shariah audit. He was of the view that to do this would only cause a state of unpreparedness as a large number of Shariah talents were still lacking in the capabilities and skills required of them, citing that only 5.9% of auditors in the industry were Shariah qualified. He admitted that there was a pressing need for a proper implementation of Shariah audit in Islamic financial institutions, notwithstanding this, the creation of talent and/or training programmes were still not up to mark. In order to establish a stronger system within the industry, some time would be required to ensure that the talents become better qualified and equipped in their areas of expertise. He suggested HR policies to include rewards and compensations as a form of assurance to the auditors that they should not work in fear or favour.

In his opposing views, Shaikh Muhammad Abdul Mubeen said that the best way forward was to have a set of laws. In order to ensure the effectiveness of its implementation, the industry requires a reasonable timeframe for the industry players to prepare themselves. Mohd Khaidzir Shahari commented that although Malaysia's Shariah Governance already has a set of laws for Islamic financial institutions to adhere to, requirement to include Shariah scholars as members of the Shariah Review is yet to be imposed. He was of the view that in order to complement the current framework, it was therefore necessary for a new set of Shariah laws to be established, whether for internal audit or accounting.

In summarising her thoughts, Dr. Hurriyah El Islamy quoted that "for Islamic finance, it takes 'three to tango', i.e., for the regulators, the industry and the public to play their role" and emphasised that all parties should continuously work together towards having a unified framework and approach. She reiterated that regulators and standard setting bodies should collaborate in developing standards which were unique to their respective countries. More importantly, the functions of Shariah auditors must be empowered and not only being a sub to the functions of internal audit.

Knowledge, expertise and talent are very important in this industry, otherwise we cannot maintain the Shariah assurance in the industry for the Islamic financial institutions.

Shaikh Muhammad Abdul Mubeen

Datuk Dr. Mohd Daud Bakar reiterated the importance for Shariah auditors to infuse smart technology in the way they work in order to stay ahead of the game, and to execute their tasks efficiently and effectively. In addition, Shaikh Muhammad Abdul Mubeen talked about how public trust was to be valued and upheld at all times, and that the only way to achieve this was by ensuring Shariah assurance on the products and services of every financial institution. He closed his statement by stating that "knowledge, expertise and talent are very important in this industry, otherwise we cannot maintain the Shariah assurance in the industry for the Islamic financial institutions".

In the context of the expertise and skills required of auditors, Mohd Khaidzir Shahari commented that "the worst nightmare for the auditor is when the clients tell the auditor that the auditor is wrong". To avoid such an occurrence, auditors should be guided by Bank Negara Malaysia's Shariah Governance and the Institute of Internal Auditors framework, and to take initiatives for them to be equipped with the necessary expertise and skill sets required of them. He was positive that in due time, this will eventually lead to the achievement of standards expected of the Shariah auditors within the financial services industry.

In closing, the panel agreed that once the adoption of appropriate systems towards instilling good Shariah governance are in place throughout all organisations, institutional integrity through Shariah audit can then be achieved.

Special Address by H.E. Dr. Bello Lawal Danbatta Secretary-General Islamic Financial Services Board (IFSB)



- All respected prominent speakers,
- Ladies and gentlemen.

Assalamualaikum warahmatullahi wabarakatuh, and very good morning to all of you.

It is a great pleasure for me to give a special address remarks in this reputable Shariah Audit Conference 2020 organised by Islamic Banking & Finance Institute Malaysia (IBFIM) and Malaysia Institute of Accountants (MIA) with the topic of "Promoting Soundness and Stability of the Islamic Financial System through Shariah Audit".

I am pleased to see that the development of Islamic financial industry has been progressing very well in many frontiers including asset size, products and services, and also financial sectors despite the challenging time of COVID-19 pandemic.

I wish that the conference would be a strategic platform for the relevant stakeholders to discuss and deliberate the latest issues of Shariah audit and its impacts to the Islamic financial industry's governance.

Shariah Audit at Glance

Ladies and gentlemen,

Shariah audit can be defined as the examination practices of the Institutions offering Islamic Financial Services (IIFS) to comply with Shariah principles in all of its activities, particularly the financial statements and other operational components that are subjected to the risk of compliance.

Since Shariah is the cornerstone of the Islamic financial products and services, the absence of Shariah value prepositions in the IIFS products and services offered to the customers would undermine the confidence in the Islamic financial services industry as a whole.

I am pleased to see that the development of Islamic financial industry has been progressing very well in many frontiers including asset size, products and services, and also financial sectors despite the challenging time of COVID-19 pandemic.

Shariah audit is paramount for the Islamic financial industry development as it is an additional governance mechanism of IIFS in conforming to their Islamic financial accountability and stakeholders' interest.

In this light, Shariah audit is part of Shariah governance mechanism of the IIFS. Due to that reason, the establishment of Shariah audit framework and an effective Shariah audit program in IIFS may be able to reduce the Shariah non-compliance risk and assist the harmonization of Shariah practices across IIFS.

Therefore, Shariah audit practices strengthen Shariah-compliance and enhance the integrity of the IIFS.

According to the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), the objective of auditing in IIFS is to enable the auditor to express an opinion on the financial statements and all material aspects according to and in compliance to the fatwas, rulings and guidelines issued by the Shariah Supervisory Board (SSB) of the respective IIFS, the accounting standards of AAOIFI, national accounting standards and practices, and relevant legislations and regulations applied in the jurisdiction where the IIFS is operating.

AAOIFI has issued internal Shariah audit standard with the objective of providing a comprehensive guideline on independent assessment of IIFS adherence with Shariah principles and rules to those charged with governance and the Shariah Supervisory Board (SSB), thereby helping in managing the Shariah non-compliance risk and ensuring a sound internal control system.

Through the issuance of the standard, it is expected that internal accountability and transparency of the IIFS can be enhanced, and the confidence of all its stakeholders can be gained.

Role of IFSB for Shariah Audit through Promoting Financial Stability

IFSB has the mandate to develop the standards tailored for the Islamic financial industry to promote the stability and soundness of the Islamic financial industry. Currently there are two standards that can relate to the Shariah audit practices, which are:

 a. IFSB-3: Guiding Principles on Corporate Governance for IIFS:

this standard sets out that Shariah pronouncements/ resolutions issued by the Shariah boards should be strictly adhered to. The internal Shariah review would therefore be assigned to someone adequately trained in Shariah compliance review/audit, so that he or she would have a competent grasp of the process.

 IFSB-10: Guiding Principles on Shariah Governance Systems for IIFS;

in this standard, Shariah audit is part of wide Shariah governance systems in which while an internal Shariah compliance review/audit for verifying that Shariah compliance has been satisfied, any incidents of non-compliance should recorded and reported throughout the process, and as far as possible should be addressed and rectified by the IIFS.

IFSB does not issue standard specifically to the Shariah audit issue as our standard mainly focuses on the risk and governance aspects in promoting the stability and soundness of the Islamic financial industry.

In this regard, we view that Shariah audit is part of the Shariah governance mechanism to promote the financial stability. With regard to the IFSB-10 Shariah Governance standard, we are now collaborating with AAOIFI to produce a joint standard for the enhancement of the standard and look at the Shariah issues in more comprehensive manner based on the current state of the Islamic financial industry.

We hope that in a couple of years we can publish that joint standard with AAOIFI in accommodating the industry's needs.

IFSB has the mandate to develop the standards tailored for the Islamic financial industry to promote the stability and soundness of the Islamic financial industry.

The Importance of Shariah Audit for Promoting Financial Stability Ladies and gentlemen,

Let me draw your attention to the main topic regarding the Shariah Audit in relation to the financial stability. In our views as international standard setting body, Shariah audit can play pivotal role in promoting financial stability from three perspectives:

First, Curbing excessive risk taking behavior that could impede the stability of the Islamic financial industry.

Through the professional practices of the Shariah audit, excessive risk taking behavior in IIFS from the top-management to the officers level can be detected and rectified accordingly.

This is in line with the macro-prudential policy objective to maintain the financial stability in limiting the excessive risk taking behavior within the financial system.

Second, Promoting the confidence of the Islamic financial

As I mentioned before, the Shariah value prepositions of the products and services of IIFS offered to the customers is detrimental for the customers' confidence in the Islamic financial industry.

In this regard, the customers' confidence would pave the way to the stability of the Islamic financial industry.

Third, Assuring the effective financial intermediation that adhere to the Shariah norms.

Well-functioned financial intermediation is a central point for enhancing the value of the stakeholders. Their stability, financial performances, and ability to intermediate resources will depend on stakeholders' confidence.

Besides, it could also enhance the safety-net of the Islamic financial industry as a whole by observing a proper risk governance framework set by the regulators.

Hence, based on those three points of perspective, assurance of the Shariah compliance for the IIFS through Shariah auditing process is pivotal for promoting the stability of the Islamic financial industry.

There is an urgency for the Shariah audit to complement the current mechanism of governance Islamic financial industry as part of efforts in preserving the Islamic financial stability.

Closing Remarks

As a concluding remark, there are still many challenges ahead for the credible Shariah audit process in promoting the stability for the Islamic financial industry, such as talent gaps for conducting the Shariah audit, developing a comprehensive Shariah auditing programs and procedures, Shariah auditing education, and so forth.

Based on those challenges, the stakeholders need to work handin-hand to overcome the challenges ahead for effective Shariah governance implementation in the IIFS.

There is an urgency for the Shariah audit to complement the current governance mechanism of the Islamic financial industry as part of efforts in preserving the Islamic financial stability.

Finally, please allow me to wish you all a fruitful discussion and deliberation in this important event. I am sure that we can achieve significant outcomes that are beneficial to promote development in this particular area of Shariah audit.

Thank you very much for your kind attention.



Synopsis

Shariah audit is unique to Islamic Financial Institutions (IFIs) due to its requirement to ensure that all business activities and operations of IFIs adhere to Shariah precepts. This session provided a global perspective to the Shariah audit practices of practitioners in different jurisdictions who are involved directly or indirectly in the process of Shariah auditing with a focus on issues of standards, qualifications, and independence.

Session Insight

Moderated by Associate Prof. Dr. Mohamed Eskandar Shah Mohd Rasid, Associate Dean, School of Graduate & Professional Studies INCEIF, Financial Sector Specialist Consultant of World Bank, the session explored the enlightening perspectives of leaders from global and domestic Islamic finance institutions as well as international standard setters and practitioners, through the sharing of their experiences and overall views of the global shariah audit and governance.

Based on his observations and personal experiences, Dr. Aznan Hasan, Chairman, Shariah Committee, Maybank Islamic Berhad; Member, Shariah Board, Accounting and Auditing Organisation of Islamic Financial Institutions (AAOIFI); Chairman, Shariah Advisory Board; Barclays Capital (DIFC, Dubai), was of the view that Malaysia was still not in the position to have laws pertaining to Shariah auditing.

Shariah governance is exceptionally important in Islamic finance and there must be continuous development in this area until best practices become the norm.

Dr. Aznan Hassan

Notwithstanding this, he recommended all Islamic financial institutions to have their own internal Shariah auditors, as this could gear them towards the application of best practices in relation to Shariah audit.

He shared several insights based on his engagements with various parties both locally and abroad that when such laws were applied, non-conformity with Shariah principles will cause Islamic financial institutions to be subjected to heavy penalties, and even as far as having their services discontinued.

Every financial institution faces reputational risk, and such will be the case if the laws of Shariah were not adhered to. In his point of view, rather than focusing on the application of such laws, all control functions involving Shariah risk, review and audit must first be in place in order for Shariah audit to work in its entirety.

His quote, "governance is like salt, you cannot under do or over-do it; striking the right balance for governance is important" referred to how each country had a distinct method of practising and applying their governance framework, hence prior to imposing any form of law on the Islamic financial institutions, it was the role of regulators to ensure a ready infrastructure and that a pool of Shariah talents have been accordingly trained. He added that a useful tool to ensure an effective implementation was to establish a solid framework for the internal auditors, and to ensure proper adherence to it.

Dr Muhammad Iman S Mihajat, Head of Shariah, Al Yusr Islamic Banking - Oman Arab Bank, then shared Oman's perspective on Shariah governance and Shariah audit. Prior to the implementation of Shariah auditing laws in Oman, the industry was already guided by the Islamic Banking Regulatory Framework (IBRF) which required all Islamic banks to operate with the key elements of Shariah.

Oman's Shariah auditing model was developed pursuant to the establishment of the Central Shariah Board in 2013, which has strengthened Shariah governance requirements. An example of such a requirement was that those who sit in the Shariah Supervisory Board must have the relevant Shariah background expected of them.

In Oman, one of the main challenges was the difficulty in acquiring qualified local Shariah scholars. Notwithstanding this limitation, continuous training programmes have been offered to upskill local Shariah talents.

With regard to ensuring that there was an alignment of objectives, Shariah meetings were conducted amongst the financial institutions on an annual basis.

In response to the moderator as to what makes Oman's approach unique relative to the other models adapted by other countries, he was of the view that Oman has always been careful in avoiding disputes pertaining to regulatory issues raised in other jurisdictions. He cited an example of this where the Central Shariah Board of Oman did not allow the implementation of Tawarrug in order to avoid criticisms amongst Shariah scholars and other senior iurisdictions.

Proper communication and good relationship with top and senior management, providing proper training to the three-layer of audit functions, and engaging with the external audit are very necessary.

Dr. Muhammad Iman S Mihajat

"The bar has in fact been raised in terms of the expectations of what are the baseline requirements when it comes to Shariah compliant products and processes". This was the opinion of Mr. Muhammad Syarizal Rahim, Partner, Ernst & Young PLT Islamic Financial Services, when asked to elaborate on the role of statutory auditors, and their considerations of Shariah auditing and governance as part of their role.

He said that because there was enhanced transparency, initiatives towards minimising any litigation of data dispute to challenge the validity of Shariah contracts will be present. He went on to explain that there were different levels of alignment between internal policies, nonetheless considerations will be given on additional 'hot-spot' areas such as Shariah governance, new product development process, practise of late-payment charges and process comprehensiveness of how an organisation monitors and reports its non-compliance issues.

Regardless of banking or Takaful, auditors are now in the position to challenge certain decisions made should any of them has any indication of not meeting the baseline requirements. However, to do that they must be well versed with rules and regulations, and have a good grasp of product knowledge and the respective baseline requirements.

The bar has in fact been raised in terms of the expectations of what are the baseline requirements when it comes to Shariah compliant products and processes.

Muhammad Syarizal Rahim

He further explained that in order for baseline requirements to be considered during crucial decision-making processes by the Shariah Committee, it was the role of the Secretariat, which is the Management, to provide timely escalation of critical issues for the Committee's attention and deliberations.

The Secretariat also plays a supporting role by ensuring that thorough research has been done prior to the decision-making processes, so that every critical issue has been identified and presented to aid in the deliberations, and consequently, the decisions of the Shariah Committee.

When asked to elaborate on Bank Islam's regulatory perspective and practises, Muazzam Mohamed, Chief Executive Officer, Bank Islam Malaysia Berhad, said that in Bank Islam, Shariah auditors look into the adherence towards the conduct, practices and rulings of the Shariah Council of Bank Negara Malaysia and other guidelines issued by Bank Negara Malaysia, Securities Commission Malaysia, and the bank's internal guidelines on Shariah compliance.

He explained that Bank Negara Malaysia's policy document on Shariah Governance 2019, which superseded the Shariah Governance framework 2010, had placed more burden on the board, Shariah Committee and key organs involved in Shariah governance in the Islamic financial institutions to comply with Shariah principles.

This has reinforced the robustness of internal control functions in the management of Shariah non-compliance risks, and has also clearly specified the roles of the three layers of control, namely Shariah risk management, Shariah review, and Shariah audit.

In response to the moderator as to how a Shariah governance ecosystem should be, **Dr. Aznan Hasan** stressed on several key factors that could lead to the establishment of a solid ecosystem, which include, ensuring that there was no shortage of Shariah scholars in the industry, the development of a solid infrastructure, continuous engagement between the two main organs, i.e., the board and the Shariah Committee, and enhanced clarity with regard to the audit function within an institution.

On this note, he commended IBFIM's efforts in offering certified professional Shariah qualifications, which was vital for the Shariah governance ecosystem as a whole.

To a question by the moderator as to how a conflict of interest could be avoided, **Dr. Muhammad Iman S Mihajat** quoted that as it was a challenge in getting qualified Shariah auditors in Oman, therefore "proper communication and good relationship with top and senior management", "providing proper training to the three-layer of audit functions, and "engaging with the external audit" were very necessary.

In this circumstance, where there was a shortage of qualified auditors, in order to attain better clarity and to avoid any form of conflict of interest, all layers of control were made to report directly to the Head of Shariah, and the latter will bear the accountability and responsibility to maintain all forms of communication with the Shariah Committee.

In Malaysia, the competency of the auditors is crucial and this has proven to be a challenge amongst Shariah auditors when making decisions on strategic matters.

Muazzam Mohamed

Muazzam Mohamed agreed that, similarly in Malaysia, the competency of the auditors was crucial and this has proven to be a challenge amongst Shariah auditors when making decisions on strategic matters.

In avoiding any potential conflict of interest, the pool of professionals must be broadened, and in this regard, he applauded the efforts of IBFIM, INCEIF and ASAS in offering the relevant training and certifications to develop the skills of compliance officers.

To a question by the moderator, **Dr. Aznan Hasan** responded that based on his own experience and practise in Malaysia and several countries, it was his strong belief that Malaysia currently has the best practise of Shariah audit and Shariah governance.

In summing up, he stressed the utmost importance of Shariah governance in Islamic finance and that there must be continuous development in this area until best practices become the norm.

In concurring, **Dr. Muhammad Iman S Mihajat** reiterated that an authoritative framework should at least be imposed in order to implement Shariah governance. He was delighted to share that Indonesia was currently at its second stage in the development of a Shariah Governance Framework.

Muazzam Mohamed echoed the other panellists that a strong Shariah governance would enable Islamic financial institutions to protect and uphold the reputation of the Islamic financial services industry, and that the current pandemic situation should be taken as an opportunity to "push forward the beauty of Islamic finance which is different from conventional finance".



Synopsis

Despite the importance of Shariah auditing, there have been, however, little understanding of how to implement an effective and efficient Shariah audit from the human capital perspective. The scarcity of qualified auditors with both Shariah and auditing qualifications and the issue of self-review is posing a threat to its independence and may affect the integrity of Islamic Financial Institutions (IFIs). Moreover, competency requirements for Shariah auditors have yet to be fully developed even though there is a need for it. This session discussed the opportunities and challenges in nurturing talent for Shariah audit practices.

Session Insight

The moderator, Prof. Dr. Zurina Shafii, Shariah Committee Standard Chartered Saadiq Berhad & Shariah, Advisor for Khadijah International Waqf Fund (Labuan), started off the final session of the conference by giving an overview on the significance of continuing the growth of talent in Shariah audit, specifically with regard to having it mainstreamed in various Shariah-based industries.

She shared a comment made by Tan Sri Abdul Wahid Omar during his Keynote Address in which it was mentioned that 70% of companies listed in Bursa Malaysia were Shariah compliant. She said that other establishments such as cooperatives, public entities, brokerage and credit companies have also benefited from the best practices of Shariah governance and Shariah assurance.

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Prof. Dr. Zurina Shafii

Due to existing regulatory aspects, there has been a diverse practise of Shariah governance and Shariah assurance, hence she invited the panellists to share their views on the current state of these practices in their respective sectors.

Dr. Nurmazilah Dato' Mahzan, Chief Executive Officer, Malaysian Institute of Accountants (MIA), started off the session by providing a brief description of MIA's processes and activities, which include regulating Chartered Accountants and public practise firms.

With regard to Shariah audit, she explained that for institutions other than Islamic financial services institutions; the purpose, intent and objectives in carrying out Shariah auditing will particularly be looked into.

...the ability to make judgements, to understand the business and regulatory framework of that business, to have independence, professional scepticisms, characteristics and skill sets of being an auditor.

Dr Nurmazilah Dato' Mahzan

An example of this was in the situation of auditors for a cooperative, who will be co-regulated by MIA as they were also members of MIA. A co-regulatory engagement of such nature was an example of how MIA offers support in assisting towards the mainstreaming of Shariah audit and in providing overall assurance to the Islamic financial services industry.

As part of their adherence to the ethical code, auditors who provide any form of auditing must be competent and highly skilled, which include, she quoted, "the ability to make judgements, to understand the business and regulatory framework of that business, to have independence, professional scepticisms, characteristics and skill sets of being an auditor".

Prof. Dato' Dr. Mustafa Mohd Hanefah, Professor, Universiti Sains Islam Malaysia (USIM), then shared interesting highlights of his experience in the area of developing talents in the university. He said it began with the kick-off of a Shariah auditing course in Arabic in 2010, and eventually the publication of the first textbook in Shariah auditing in 2012.

There are now opportunities to work together with the industry, regulators, professional bodies and accreditation bodies.

Prof. Dato' Dr. Mustafa Mohd Hanefah

Continuous engagements with various stakeholders had eventually led the university to take on various initiatives including obtaining a research grant from Bank Muamalat Malaysia Berhad for Islamic accounting and reporting, and participation in the Knowledge Transfer Programme, where they were able to develop Shariah modules.

He expressed his delight that the Shariah Audit Training under the Knowledge Training Programme was the first Shariah training programme to be accredited by FAA; and that collaboration with other financial institutions and associations, including MBSB and IBFIM had also taken place thereafter.

He encouraged other industry players and stakeholders to be involved in such initiatives, as this was key towards developing qualified Shariah audit talents within the industry. Although the development had not been easy, teaching and learning initiatives have grown in the last decade, and this was made possible through continuous engagement with the industry and the auditors.

Mr. Yusry Yusoff, Chief Executive Officer, Islamic Banking & Finance Institute Malaysia (IBFIM), then went on to provide a background of how IBFIM had initially embarked on its initiative towards fostering the growth of Shariah talents in the financial services industry. He explained that IBFIM commenced its Certified Professional Shariah Auditor (CPSA) programme due to concerns highlighted by the Shariah fraternity upon the introduction of the Islamic Financial Services Act, specifically on the imposition of hefty penalties for non-compliance on Shariah matters.

The programme, he explained, acted as a tool that could be leveraged on, specifically in managing issues and challenges faced by the industry. Upon the launch of the CPSA programme in 2019, the numbers of intake increased from a modest 50 to 450 professionals in 2020. With CPSA, professionals who lacked the necessary talent and skill sets when undertaking internal audit functions were now able to develop their skill sets and qualifications.

Eventually, due to its universal application, not only can CPSA become a tool to produce more talents for the local and global markets, but it can be well suited to develop skill sets and basic competencies for Shariah auditing in other Shariah-based situations, and not just for Islamic banks and Takaful operators.

Malaysia will be recognised as a centre of excellence on Shariah audit in terms of policy, research and talent development.

Yusry Yusoff

Speaking from the perspective of an accrediting body, Khairul Nizam Md Som, Chief Executive Officer, Finance Accreditation Agency (FAA) then provided an outlook for talent development in relation to Shariah audit. Based on the accreditation of USIM's accounting programme and IBFIM's professional programmes, he said that a significant lesson learned from the exercise was that learning programmes need to be outcome-based and benchmarked. Without doubting the crucial presence of competencies, it was also vital to establish the levels and specific outcomes that were required from any learning programmes which have been anchored into the competency framework.

With regard to his opinion as to how Artificial Intelligence (AI) technology would shape the future of Shariah auditors, he shared the quote "AI will not replace auditors, but auditors using AI will replace those not using AI" and stressed that IT innovations and technology advancements were competency domains that should be explored and fully utilised by auditors, as part of their talent and learning development process.

To a question posed by a member of the floor on how AI technology can shape the future of Shariah audit, Dr. Nurmazilah Dato' Mahzan first shared the findings of an experimental research conducted by them in 2012 on internal auditors. Data collected from the research has shown the low level of their Shariah knowledge; however, there has been significant improvement on this matter over the years.

Notwithstanding this, she felt that auditors were still challenged by the fact that they were neither multi-knowledgeable nor multiskilled. In concurring with the other panellists, she said that through the use of AI technology, auditors can then quickly and effectively enhance their skills, specifically in the area of data analysis and decision-making, which will in turn put them in a much better position during the conduct of an audit.

Yusry Yusoff echoed the views that technology was an enabler within an audit process, as its application will give better focus to the auditors to place better emphasis in making better deliberations and decisions, and avoiding issues which were mundane and routine in nature. He also agreed with a suggestion from a member of the floor, that a fintech application could enhance the capabilities of Shariah auditors.

"There are now opportunities to work together with the industry, regulators, professional bodies and accreditation bodies" according to Prof. Dato' Dr. Mustafa Mohd Hanefah, and he looked forward

to more collaborations in the near future including opportunities in Shariah risk management and Shariah research.

Khairul Nizam Md Som reiterated the significance of internal auditing and responsibility of all stakeholders in producing a set of qualified and competent Shariah talents for the benefit of the industry as a whole. He then touched on the "value-based intermediation guidelines and initiatives that have been rolled out by Bank Negara Malaysia to the financial services institutions", especially in the areas of sustainability audit and sustainability review, and added that this was a pertinent area of Shariah audit for the industry partners and financial institutions to join forces on.

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Mr. Khairul Nizam Md Som

"There are now opportunities to work together with the industry, regulators, professional bodies and accreditation bodies" according to Prof. Dato' Dr. Mustafa Mohd Hanefah, and he looked forward to more collaborations in the near future including opportunities in Shariah risk management and Shariah research.

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In his concluding words, Yusry Yusoff shared his hopes that in the near future, "Malaysia will be recognised as a centre of excellence on Shariah audit in terms of policy, research and talent development". Dr. Nurmazilah Dato' Mahzan, in concurrence to his view, reiterated the importance of focusing on the right skill sets for auditors, and to ultimately uphold the purpose of Magasid Al-Shariah. She encouraged more collaborations, dialogues and forums to ensure that this objective can be achieved. On a final note, she reminded auditors to focus on their continuing education in order for them to be kept well-informed on the continuous development, skills and technologies.

Closing Remarks by
Yusry Yusoff
Cheif Executive Officer
Islamic Banking & Finance Institute Malaysia
(IBFIM)



Bismillahirahmannirrahim
Assalamu'alaikum warohmatullahi wabarakatuh.

Distinguished Speakers

Ladies and Gentlemen,

It is indeed an honour to be given the opportunity to conclude the inaugural Shariah Audit Conference today. The 2-day virtual conference has seen all experts from diverse backgrounds come together to share their insights on Shariah audit from all angles.

For today, allow me to conclude with the key takeaways from this conference.

First, let me touch on the universal acceptance of Shariah audit.

Notably, the Islamic finance fraternity, regulators, practitioners, professional bodies and other entities beyond, acknowledge the importance of Shariah audit despite the diversity in practises and standards as applied in different jurisdictions.

Notwithstanding, these diverse players have one underlying objective in common which is; Shariah audit is integral in adding value and simultaneously enhances governance, risk management and compliance.

The diverse players in Islamic finance have one underlying objective in common which is; Shariah audit is integral in adding value and simultaneously enhances governance, risk management and compliance.

Coming to my next point, getting the Shariah audit into the mainstream involved efforts by all stakeholders to provide greater independence of Shariah assurance.

All in all, the deliberation in each session of the conference have strongly underlined the importance of Shariah Audit, hence, echoing the emphasis by the regulator that industry players and practitioners alike, carry the responsibility to collectively collaborate in executing effective Shariah audit function towards the assurance of Shariah governance.

Realizing the need for the concerted effort, the role of industry training institutions like IBFIM and higher learning institutions alike unquestionably have to complement such effort as they are entrusted with the responsibility to disseminate and transform the Shariah audit knowledge into the applicable know-how for learners. This will be critical in providing solutions to address the competency issues in Shariah audit.

This brings me to the final key takeaway of the conference, setting the skillset baseline for Shariah audit. The industry has to play a commendable part towards upskilling and reskilling current talent and it is important that relevant professional bodies facilitate the implementation of an integrated Shariah auditing competency framework. Hence, in the long run, it will have a direct impact as it drives the scalability of the industry further, which will ultimately contribute to Islamic finance sustainability.

Ladies & Gentlemen,

IBFIM envisages for the conference to be a game changer to the future Islamic financial landscape, particularly in Shariah audit and Shariah governance assurance.

Therefore, it is our fervent hope that, the conference may form a contribution by IBFIM and MIA in realizing the agenda of mainstreaming Shariah audit.

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On behalf of the organisers, MIA and IBFIM would like to record our special thanks to the panellists for their valuable insights on the development and opportunities in Shariah audit, governance and compliance.

We also wish to thank our conference supporters:

- Association of Islamic Banking and Financial Institutions Malaysia (AIBIM)
- ASEAN Federation of Accountants (AFA)
- The Institute of Internal Auditors Malaysia (IIAM)
- Malaysian Takaful Association (MTA), and
- Universiti Sains Islam Malaysia (USIM)

Our heartfelt thanks also go to the event sponsors:

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We hope to see you again! Thank you & Wassalamu'alaikum WBT.



Recommendations

The following were the observations and recommendations made based on the deliberation in all the sessions of the conference:

▶ Roles of Regulators & Financial Institutions

- Regulators, professional bodies and associations to undertake the role of setting professional standards pertaining to the scope, definition setting and skill sets of Shariah auditors.
- The need to have a solid framework for internal audit and for regulators to check on a consistent basis that the pool of Shariah talents have been accordingly trained. Regulators to ensure that adequate infrastructure is in place prior to enforcement of any form of regulation pertaining to Shariah audit and governance.
- A set of incentives offering by the regulators is essential to attract financial institutions in applying these best practices.
- Best practices in external Shariah audit in the financial institutions to be imposed, whilst at the same time ensuring that internal Shariah auditors play their relevant roles with necessary supervision of the regulators.
- Islamic financial institutions to have their own Shariah internal auditors.

► Skillsets and Innovation in Shariah Auditing

- Internal auditors to have proper qualifications and certifications to increase their dual capabilities, where they will be able to conduct mainstream auditing, and also specialise in Shariah auditing.
- Internal auditors to diversify their skills and activities, and to become more pro-active in their respective roles.
- The need for the current internal audit delivery model to be re-assessed to contain key elements necessary in elevating the standards of auditors as business partners.
- Necessity for an audit change management programme to be developed, which includes data management, IT systems and regulatory requirements.
- Auditors to embrace new technologies to improve the quality of audit.

▶ Roles of Professional Bodies & Associations

- Professional bodies and associations to undertake the role of developing talent to address the needs of the industry, for example via the offering of professional Shariah certification courses and training programmes.
- Professional bodies and associations to continuously offer professional Shariah qualifications and training programmes to equip them with professional skills and the requisite Shariah understanding and knowledge.
- Industry and stakeholder engagements are needed in the development of Shariah audit talents.







