

## SHARIA GOVERNANCE IN ISLAMIC FINANCIAL INSTITUTIONS: A COMPARATIVE REVIEW OF MALAYSIA AND INDONESIA

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### Abstract

*As important participants in Sharia governance, Malaysia and Indonesia emphasize the importance of a Sharia supervisory board at the institutional level to ensure compliance with Islamic principles. This study provides a comparative analysis of Sharia governance practices in Indonesia and Malaysia, focusing on the key differences and similarities between the Sharia governance frameworks in Malaysia and Indonesia. The method adopted in this study was document research. This method allows researchers to access a wide range of information and perspectives from various sources such as books, academic journals, government reports, and online databases. The findings reveal that both Malaysia and Indonesia have implemented Sharia governance frameworks in their Islamic financial institutions. However, their structures and regulatory frameworks differ from each other. Malaysia follows a two-tier structure with a comprehensive framework, whereas Indonesia follows a decentralized model with dispersed regulations. Both countries require the establishment of a Sharia committee at the institutional level to ensure compliance with the Sharia principles. Therefore, this comparative analysis enhances the understanding of Sharia governance in Islamic banking and finance, shedding light on the strengths and weaknesses of Malaysia and Indonesia's frameworks.*

**Keywords:** *Sharia Governance; Islamic Banking; Islamic Finance; Sharia Supervisory Board*

### Abstrak

Malaysia dan Indonesia sebagai negara yang menerapkan tata kelola syariah di sektor perbankannya menekankan pentingnya dewan pengawas syariah di tingkat institusi untuk memastikan kepatuhan terhadap prinsip-prinsip Islam. Tujuan utama dari penelitian ini adalah untuk melakukan analisis komparatif praktik tata kelola syariah di Indonesia dan Malaysia. Laporan ini berfokus pada perbedaan dan persamaan utama antara kerangka tata kelola syariah di Malaysia dan Indonesia. Metode yang



digunakan adalah penelitian dokumen kualitatif. Metode ini memungkinkan peneliti mengakses berbagai informasi dan perspektif dari berbagai sumber seperti buku, jurnal akademik, laporan pemerintah, dan database online. Temuan ini mengungkapkan bahwa Malaysia dan Indonesia telah menerapkan kerangka tata kelola syariah di lembaga keuangan Islam mereka; namun, terdapat perbedaan dalam struktur dan kerangka peraturannya. Malaysia menganut struktur dua tingkat dengan kerangka komprehensif, sedangkan Indonesia menganut model desentralisasi dengan peraturan yang tersebar. Kedua negara mewajibkan pembentukan komite Syariah di tingkat institusional untuk memastikan kepatuhan terhadap prinsip-prinsip Syariah. Oleh karena itu, analisis komparatif ini akan meningkatkan pemahaman tentang tata kelola syariah dalam perbankan dan keuangan Islam, serta menjelaskan kekuatan dan kelemahan kerangka kerja perbankan syariah di Malaysia dan Indonesia.

**Kata kunci:** Tata Kelola Syariah; Perbankan Syariah; Keuangan Syariah; Dewan Pengawas Syariah

## INTRODUCTION

Sharia governance plays a pivotal role in Islamic banking and finance by guaranteeing the adherence to Islamic principles. The primary goal of Sharia governance is to ensure adherence to, and enhance public trust in, the ethical standards, administration, and business activities of IFIs (Sori et al., 2015). It encompasses a series of structural measures employed by Islamic Financial Institutions to establish robust supervision, accountability, and adherence to Shariah principles in their activities (SAMA, 2020; Jan & Ismail, 2023). Islamic Financial Institutions (IFIs) implement Sharia governance frameworks to ensure effective oversight, accountability, and compliance with Sharia principles in their operations (Shafii et al., 2014; Rahajeng, 2013; Wijayanti & Setiawan, 2023). The main components of these frameworks typically include the following. (1) The establishment of a Sharia Supervisory Board (SSB) or Sharia committee comprising a minimum of three legal experts is tasked with verifying that the activities and offerings of IFIs adhere to Islamic principles. They provide guidance on Sharia-related matters, verify operations, and certify products. (2) Sharia review: This function involves reviewing the operations of IFIs to ensure compliance with Sharia principles. (3) Sharia audit: The Sharia committee engages in Sharia audits to verify that the institution's activities align with the Sharia principles. (4) Sharia risk management: This assists in mitigating the risks linked to deviations from Shariah principles in the operation of IFIs. Hence, IFIs have implemented Sharia governance frameworks to ensure compliance with Islamic principles in their operations.



Sharia governance frameworks typically involve the establishment of a Sharia Supervisory Board (SSB) or Sharia Committee at the institutional level. The SSB, also known as the Sharia committee, consists of a minimum of three legal experts who receive compensation from the bank, but function as autonomous advisors. Their responsibilities encompass offering guidance to the bank's staff, providing recommendations on charitable contributions (zakat), scrutinizing operations, and endorsing products (International Monetary Fund, 2002). Apart from the SSB or Sharia committee, Sharia governance frameworks may encompass other vital roles or entities such as Sharia review, Sharia audit, and Sharia risk management. These roles play a crucial role in guaranteeing that the objectives and activities of IFIs consistently align with Sharia principles (Shariah Governance Framework for Islamic Financial Institutions, 2010).

Sharia governance frameworks can differ among nations and institutions, shaped by local regulatory conditions and particular requirements of IFIs. For instance, Malaysia possesses an extensive Sharia Governance Framework established by the Central Bank of Malaysia, whereas in Indonesia, regulations are spread across multiple laws, statutes, guidelines, and circulars (Ulfi, 2022).

Typically, these frameworks include forming a Sharia Supervisory Board or committee within the institution, along with other key functions, such as Sharia review, Sharia audit, and Sharia risk management. The specific structure and implementation of Sharia governance frameworks may vary across countries and institutions depending on the local regulatory environments and needs of the IFIs.

As significant participants in the Islamic finance sector, both Malaysia and Indonesia adopted Sharia governance frameworks in their Islamic financial institutions. However, their design and regulatory structures are distinct. Malaysia has a two-tier structure with a comprehensive framework, whereas Indonesia has a more centralized model with dispersed regulations (Aziz et al., 2019; Meutia & Adam, 2021). Despite these differences, both countries emphasize the importance of a Sharia committee or board at the organizational level to guarantee adherence to Islamic principles.

The primary aim of this study is to conduct a comparative analysis of Sharia governance practices in Indonesia and Malaysia. It focuses on the key differences and similarities between the Sharia governance frameworks in Malaysia and Indonesia. Hence, the results of this comparative analysis will enhance the comprehension of Sharia governance in Islamic banking and finance and offer perspectives on the advantages and disadvantages of the current frameworks in Malaysia and Indonesia.



Sharia governance holds significant importance in Islamic banking and finance, as it ensures the adherence of financial institutions to Islamic principles and regulations. Research in this area has been conducted to cover various topics, including the examining the impact of Sharia governance mechanisms on the performance of Islamic banks, the functions of Sharia Supervisory Boards, and the evolution of Sharia governance frameworks across diverse nations (Al-Suhaibani & Naifar, 2014; Alnasser & Muhammed, 2012; M. Bhatti & Bhatti, 2009; Grais & Pellegrini, 2006; Grassa, 2013; Ridwan & Mayapada, 2022; Uyob et al., 2022). Research carried out in Bangladesh revealed that the caliber of the Board of Directors, Sharia Supervisory Board, management, and Sharia executives had both positive and negative effects on the quality of Sharia compliance, the bank's reputation, goodwill, and overall performance within Islamic banks (Alam et al., 2022). Another study examined Sharia governance in Islamic banks across 11 countries by comparing international and national Sharia governance codes (Fatmawati et al. 2022).

Several books and case studies have been published on the subject, such as "The Edinburgh Companion to Shari'ah Governance" (Ali et al., 2020), "Shariah Governance in Islamic Banking Institutions" (S. andan & Ismail, 2023), and "Case Studies in Islamic Banking and Finance" (Kettell, 2011). These resources provide in-depth analyses of Sharia governance in various contexts, including the roles of Sharia supervisory boards, fatwas, and Shariah decisions. Research on Sharia governance in Islamic banking and finance has been conducted in various countries including Indonesia and Malaysia. These studies focus on the development of Sharia governance frameworks, the role of Sharia supervisory boards, and the influence of Sharia governance mechanisms on Islamic bank performance (Aziz et al., 2019; Laldin & Furqani, 2018; Rahajeng, 2013; Wijayanti & Setiawan, 2023).

In Indonesia, research has introduced a novel framework for Sharia governance within Islamic banks by juxtaposing Sharia governance concepts rooted in accounting, audit entities specializing in Islamic financial institutions, the Islamic Financial Services Board, and PBI No. 11/33/2009 (Meutia & Adam, 2021). Another study focused on the role of the Sharia Supervisory Board in Islamic banks in Indonesia, Malaysia, and Iran, examining their responsibilities and authority (Arsyanti, 2010).

A comparative analysis of the Sharia governance frameworks in Indonesia and Malaysia revealed several similarities and differences between their practices (Masruki et al. 2020). Abdullah (2017) compared the Islamic banking sectors in Malaysia and Indonesia by examining aspects such as legal structures, court authority, capital expansion, product portfolios, and Sharia governance. The findings suggest that each of these nations possesses



strengths and weaknesses in the Islamic banking sector. To realize their ambition as Islamic banking hubs, they must address their shortcomings while leveraging their respective strengths. In Malaysia, research has been dedicated to investigate Sharia governance practices in Islamic financial institutions (Masruki et al. 2020). In this study, content analysis was used to assess the compliance practices of Malaysian Islamic banks. A separate research endeavor explored the distinctions between the current Sharia governance frameworks in Malaysia and Pakistan, investigating how they mutually reinforce one another (Ahmad et al. 2023).

Studying Sharia governance in Islamic banking and finance is imperative. By exploring how Sharia governance mechanisms shape the sector, the functions of Sharia Supervisory Boards, and the evolution of Shariah governance frameworks across various nations, researchers can make valuable contributions to the continual advancement of Islamic banking and financial practices that are not only in harmony with Islamic principles but also sustainable in the long term.

## **LITERATURE REVIEW**

Sharia governance framework is integral to Islamic banking and finance, as it ensures that all operations align with Islamic law and Sharia principles. The primary function of the Sharia Board within this framework is to verify compliance with financial transactions and operations (Alam et al., 2021). This framework fosters transparency, accountability, and ethical practices that are crucial to the credibility and trust of stakeholders and depositors. The adoption of a transparent and responsible corporate governance system in Islamic banking is essential for preserving the reputation and trustworthiness of Shariah compliant banking. It helps build trust among stakeholders and depositors as it demonstrates the commitment of Islamic financial institutions to uphold Sharia principles in their operations. Sharia Board members must possess the credibility to instill confidence in stakeholders and depositors (Aziz & Ghadas, 2022). The Sharia governance framework within the realm of Islamic banking and finance is an indispensable element of this sector, promoting the values and ethics of Islamic finance, and providing stakeholders with confidence in the integrity of institutions. Moreover, the significance of the Sharia Governance Framework in Islamic banking and finance is magnified due to the growing intricacy of Islamic financial transactions. The establishment of the Sharia Governance Framework and Sharia Board is pivotal in guaranteeing that Islamic financial institutions function in accordance with Islamic laws and principles.



The primary objective of the Sharia governance framework is to establish a comprehensive framework that delineates the roles and responsibilities of all the parties engaged in Islamic banking. Shah (2019) mentions that the Sharia Governance Framework includes key components, such as the board of commissioners, internal auditors, and the Sharia internal external review unit. These components collaborate to establish a strong system of corporate governance within Islamic banks, guaranteeing their efficient and effective operations in accordance with the Sharia compliance principles. These studies underscore the significance of integrating Sharia governance practices to ensure transparency, fairness, and long-term sustainability in Islamic banking. Abbasi (2020), Mihajat (2019), and Takaloo et al. (2022) argue that the integration of the Sharia supervisory board and governance arrangements within Islamic banks is vital for establishing credibility and fostering trust among stakeholders and depositors. Hence, this framework not only promotes the ethical and transparent functioning of Islamic financial institutions, but also assures stakeholders and depositors regarding adherence to Shariah principles in the operations of these institutions.

Previous studies have shown the advantages of good sharia governance. Kiranawati et al (2023) discussed on the impact of Sharia governance on the performance of Islamic banks, particularly emphasizing the principles of Maqashid Sharia. They highlight how adherence to Sharia governance principles can enhance service quality, increase financial performance, and improve the overall reputation of Islamic banking institutions. Hasan et al (2022) discussed in the summaries analyze the relationship between intellectual capital, Islamic corporate governance, financial performance, and earning management in Sharia banking in Indonesia. They find that intellectual capital and Islamic corporate governance have a direct impact on financial performance, which in turn affects earnings management. While intellectual capital positively influences Return on Assets (ROA), Islamic corporate governance has a negative effect. These studies emphasize the importance of good corporate governance for the sustainability and performance of Islamic banks. Similarly, Tarihoran et al. (2021) focus on the impact of Sharia compliance, Islamic corporate governance, and Islamic social reporting on the financial performance of Islamic Commercial Banks in Indonesia from 2015 to 2019. The findings revealed that while sharia compliance and Islamic corporate governance positively influenced financial performance, factors such as profit-sharing ratio, zakat performance ratio, and Islamic social reporting did not have a significant effect. This finding is supported by Kachkar and Yilmaz (2023), who found a positive significant correlation between Shariah supervisory boards and corporate social responsibility disclosure, diversity on corporate boards,



characteristics of Shariah supervisory boards, and the relationship between board demographic diversity and corporate philanthropic giving in Islamic banks. Moreover, the Sharia governance framework in Islamic banking and finance contributes to an industry's overall stability and sustainability. The Sharia governance framework in Islamic banking and finance is instrumental to ensuring adherence to Sharia principles, promoting ethical practices, enhancing transparency, and fostering accountability in Islamic financial institutions (Alam et al., 2020; Saad, 2020).

Karimah (2022) delves into the legal and Sharia risks faced by Islamic banking in Indonesia, emphasizing the significance of Sharia governance in mitigating these risks. They underscore the role of the Sharia Supervisory Bodies and National Sharia Boards in ensuring compliance with Sharia principles and regulatory frameworks. This finding is supported by Khairunnisak and Purba (2023), who analyze Good Corporate Governance (GCG) practices in Sharia banking in Indonesia. They emphasize the legal responsibility of Islamic banks to adhere to GCG principles of transparency, accountability, professionalism, and fairness in their operations. The implementation of the GCG principles in Sharia banking is crucial for improving performance, securing cheaper financing, restoring investor confidence, and satisfying shareholders.

However, the diversity of Sharia governance approaches represents a significant challenge for the Sharia financial industry. Research conducted by Ulfi (2022) identified notable differences in the approach between the two regions. GCC countries have adopted a minimalist model, whereas Asian countries have implemented an interventionist model. The regulatory framework, status of the Sharia board, and appointment processes for Sharia board members vary significantly between the two regions, demonstrating the significance of Sharia corporate governance in Islamic finance.

The importance of standardization, governance, and stakeholder involvement in the development of the Islamic finance sector is another crucial issue. Hailu and Tekdoğan (2023) emphasize the need for a centralized Sharia advisory committee, adaptation of international standards, collaboration with stakeholders, and incorporation of Islamic economics and finance into the education system. Kasi and Mahmood (2019) examine the challenges faced by Islamic banking in Bahrain due to the lack of standardization in Sharia rulings, despite efforts towards standardization through regulatory involvement.

Furthermore, the study examines the constitution, composition, and functioning of Sharia Boards within Islamic banks in Bahrain, identifying inconsistencies in practices related to reporting, training programs, and disclosure of information. Sharia governance is of utmost importance for



maintaining the honesty and conformity of Sharia principles in Islamic banking operations (Al Rahahleh et al., 2019; Khalid, 2020). Empirical studies have demonstrated that the characteristics of Sharia Supervisory Boards have a significant impact on Islamic bank performance. This finding highlights the need to implement improved governance practices. Furthermore, the presence of a strong and effective Sharia governance framework enables Islamic banks to differentiate themselves from conventional banks by offering financial products and services in line with Sharia principles, thereby attracting a niche market of customers seeking ethical and religiously compliant financial solutions. In addition, studies have indicated that the efficiency of Sharia Supervisory Boards can exert a positive influence on the performance of Islamic banks.

A fundamental aspect of Sharia governance is its compliance framework, designed to ensure Islamic financial institutions adhere to Sharia principles and standards in all activities. Sharia governance compliance mechanisms include the establishment of a Sharia Supervisory Board, regular audits and inspections, internal control systems, and training programs for employees. These mechanisms collaborate to ensure that Islamic banks' activities align with Sharia's principles and standards, thereby safeguarding stakeholders' interests and maintaining customer trust. Sharia governance provides a structured framework for all parties involved in Islamic banking and finance to fulfill their roles and responsibilities in upholding Sharia compliance (Mohamad et al., 2019). With a comprehensive Sharia governance framework, Islamic banks can demonstrate their commitment to uphold the value of Islamic finance and provide religiously compliant financial solutions to their customers.

To conclude, the establishment of a robust Sharia governance framework, complemented by efficient monitoring and enforcement mechanisms, empowers Islamic banks to preserve Sharia compliance throughout their operations and sustain their reputation as providers of Islamic financial services. Therefore, a comprehensive governance framework for Sharia is imperative for Islamic financial institutions. It guarantees conformity to Sharia principles and standards through vital frameworks and protocols for the effective monitoring of Sharia compliance.

## **METHODOLOGY**

This study employs a qualitative approach to investigate a subject in its natural setting (Patton, 2014). A qualitative research design is crucial for gaining a thorough and nuanced understanding of the subject. By focusing on an insider's perspective, qualitative research allows a deeper understanding of complex phenomena.





This research relied on secondary data from journals, government websites, and other organizations, collected using documentation and observational methods. In this study, library research plays a key role in enabling a systematic exploration and analysis of existing literature and documents. This method provides access to a diverse range of sources, including books, academic journals, government reports, and online databases, and offers a comprehensive overview of current knowledge, theories, and research findings (Farr, 2008). This approach helps establish a solid knowledge foundation, identify key concepts and theories, and uncover gaps in the existing literature. It also offers a historical perspective, illustrating how understanding of the topic has evolved over time.

Employing technical data analysis, this study examined and interpreted technical documents such as reports, manuals, and scientific papers. This method helps identify patterns, trends, and correlations in the data and provides key insights to inform the research findings. We used QDA Miner Lite, a qualitative data analysis software. QDA offers a methodical and rigorous approach to analysing and interpreting the abundant data obtained from interviews, ensuring a thorough exploration of the research topic (Lorenzetti et al., 2020).

## **RESULTS AND ANALYSIS**

Islamic banking and finance operate in accordance with Islamic legal principles (Zaini et al., 2019). Islamic banking must work in accordance with Islamic business principles and ethics by implementing transparent and accountable corporate governance (Morrison, 2015). This ensures that the bank operates in a manner that is in line with the principles of Islamic law, promoting ethical conduct, and responsible practices (Moqbel & Ahmed, 2020).

Islamic banks employ a distinct form of corporate governance, referred to as Sharia corporate governance, in addition to governance models employed in traditional banking. This distinction arises from the unique features of Islamic banks, notably, the inclusion of a Sharia supervisory board. According to Hasan, the establishment of a Sharia supervisory board represents a significant step toward the effective implementation of Sharia governance in Islamic banking (Yadiati et al., 2022). This board assumes a vital function in verifying that the bank's operations and procedures align with the Islamic principles. The presence of a Sharia supervisory board allows Islamic banks to strengthen their corporate governance standards and offer stakeholders and investors confidence that their activities adhere to Islamic principles (Jan et al., 2021). Furthermore, the directors of Islamic banks are subject to oversight from both the board of



directors and Sharia board. Members of the Sharia board must establish trustworthiness in the bank and in all stakeholders, including depositors (Uyob et al. 2022).

This comparative analysis focuses on the key differences and similarities between the Sharia governance frameworks in Malaysia and Indonesia, particularly in three aspects: (1) structure, (2) regulatory framework, and (3) Sharia committees/boards. Thus, the output of this comparative analysis will contribute to a better understanding of Sharia governance in Islamic banking and finance and provide insights into the strengths and weaknesses of the existing frameworks in Malaysia and Indonesia.

### **Structural approach**

Sharia governance frameworks in Malaysia and Indonesia differ in terms of their approach and effectiveness. Malaysia and Indonesia, both key participants in the Islamic finance sector, have established Sharia governance frameworks within their Islamic financial institutions (IFIs) to ensure adherence to Islamic principles. However, the framework structures of the two countries differ. Malaysia adopts a two-tier Sharia governance structure, which includes a central Sharia council at the national level and a Sharia committee at the institutional level (Sharia Governance Framework for Islamic Financial Institutions, 2010). Notably, the Sharia Committee is mandatory for all Islamic financial institutions (IFI) (Ali et al. 2018). The Central Bank of Malaysia, also known as Bank Negara Malaysia, has issued an extensive Sharia governance framework applicable to Islamic financial institutions. This framework delineates the duties and obligations of essential parties, including the board of directors, Sharia committee, management, and internal and external auditors. The centralized Sharia governance structure in Malaysia has demonstrated greater effectiveness in assuring the autonomy of the Sharia supervisory board in its function of oversight and maintaining the uniformity of Islamic rulings, as corroborated by studies conducted by Yadiati et al. (2022). It allows for more standardized and independent oversight of Sharia compliance at the national level for Islamic financial institutions, promoting transparency, accountability, and the ability to effectively address Sharia compliance issues.

On the other hand, Indonesia employs a decentralized model comprising a national fatwa council at the national level and a Sharia board within the industry. The nation has promulgated multiple regulations that delineate facets of Sharia governance; however, these regulations are spread across various laws, statutes, guidelines, and circulars. Within Indonesia's Sharia



governance framework, the central component is the Sharia supervisory board (SSB) of Islamic financial institutions (Rahajeng 2013). However, Indonesia's decentralized Sharia governance framework presents several challenges. The decentralized system in Indonesia has led to inefficiencies in Sharia governance, stemming from a lack of coordination and consistency in monitoring and enforcing compliance among Indonesian Islamic banks. This hinders the effectiveness and credibility of Islamic banks in Indonesia (Ulfi 2022).

To overcome these challenges, Islamic banks in Indonesia must enhance their compliance with the Sharia governance standards (Yadiati et al., 2022). Implementing a more centralized Sharia governance framework, similar to Malaysia, proves to be more effective in mitigating Sharia compliance risks and improving transparency in Islamic banking and finance in Indonesia (Meutia & Adam, 2021). Moreover, development of the Sharia governance framework in Malaysia has advanced. Indonesia can draw insights and lessons from Malaysia's experience and adapt these to suit its context.

### **Regulatory framework**

The regulatory structures governing Sharia in Islamic banking and finance differ significantly between Malaysia and Indonesia. The level of regulatory oversight and enforcement varies between the two countries, with Malaysia adopting a more centralized approach through the Central Bank of Malaysia, while Indonesia employs a more decentralized model with Sharia boards operating at the institutional level.

In Malaysia, the Shariah governance framework has matured into an essential component of the country's legal framework, overseeing Islamic banking and finance systems (Laldin & Furqani, 2018). In Malaysia, the regulatory framework for Sharia governance is thorough and organized. The Central Bank of Malaysia has introduced an extensive Sharia governance framework that delineates the duties and obligations of crucial participants, including the board of directors, Sharia committee, management, and internal and external auditors. This framework offers explicit directives and anticipations for Islamic financial institutions to ensure their adherence to Islamic principles. This integrative approach in Malaysia makes Sharia governance enforceable, and demonstrates the country's commitment to upholding Sharia principles in the Islamic finance industry (Ulfi, 2022; Meutia & Adam, 2021). Overall, the regulatory framework for Sharia governance in Malaysia is more comprehensive and structured than in Indonesia, which has a more decentralized and dispersed framework.



On the other hand, Indonesia's regulatory framework for Sharia governance is decentralized and dispersed across various legislation, acts, guidelines, and circulars. The dispersed regulatory framework of Indonesia makes it challenging for Islamic financial institutions to navigate and comply with these requirements.

Disparities in regulatory frameworks between Malaysia and Indonesia can affect the efficiency and uniformity of Sharia governance. The regulatory structure of Sharia governance in Islamic banking and finance plays a pivotal role in confirming the adherence to Islamic principles. This provides a clear framework and guidelines for Islamic financial institutions, thereby promoting transparency, accountability, and trust in the industry. Furthermore, a robust Sharia governance framework is essential for minimizing the Sharia compliance risk and ensuring the independence of the Sharia Board in their supervision (Aziz et al., 2019; Rethel, 2018).

### **Sharia Committees/Boards**

The function of a Sharia committee or board to guarantee compliance with Islamic principles within financial institutions is important in both Malaysia and Indonesia. These committees or boards bear the responsibility of supervising the activities and offerings of institutions to verify their alignment with the Islamic principles.

In Malaysia, the Sharia committee is central to the governance framework and plays a crucial role in ensuring compliance of Islamic banks with the Sharia principles. In Indonesia, the Sharia board is also established at the institutional level, but operates within a decentralized framework, with multiple Sharia board members from different backgrounds and institutions having the authority to issue fatwas (Zaini & Bin Shuib, 2021).

The Shariah governance structure in Malaysia is regarded as more proficient in safeguarding the autonomy of the Sharia Supervisory Board in its oversight and upholding the consistency of Islamic rule. This centralized framework facilitates a more efficient and standardized approach to Sharia governance, engendering increased trust among stakeholders in the Islamic banking sector. Additionally, Malaysia's centralized Sharia governance framework demonstrates stronger Sharia disclosure requirements than Indonesia's decentralized framework. These differences in Sharia governance frameworks between Malaysia and Indonesia highlight the importance of a centralized approach to ensure the independence and consistency of Sharia rulings in Islamic banking institutions (Aziz et al., 2019; Laldin & Furqani, 2018; Rahajeng, 2013). Malaysia's incorporation of an all-encompassing



strategy in which Shariah governance is an integral component of the nationwide legal framework that oversees the Islamic banking and finance system has played a role in enforcing Shariah governance in the country's Islamic banking sector.

The centralized Sharia governance system in Malaysia, which encompasses the formation of a Sharia committee or board within institutions, has proven to be more effective in ensuring adherence to Sharia principles and providing guidance in Islamic banking operations than the decentralized framework in Indonesia, ensuring compliance of Islamic banks with Sharia principles, and promoting transparency in Islamic banking operations. The centralized Sharia governance framework in Malaysia, which includes the establishment of a Sharia committee or board at the institutional level, has proven to be more effective in ensuring the consistency of Sharia rulings and addressing conflicts of interest in Islamic banking operations (Ulfi, 2022). The centralized Sharia governance framework in Malaysia, with its integrated strategy and formidable regulatory supervision, has played an indispensable role in the advancement and expansion of the Malaysian Islamic banking and finance sector (Aziz et al., 2019). It has helped build trust and confidence among stakeholders, both domestically and internationally, by providing clear guidelines and regulations for compliance with Islamic law.

Overall, the Sharia governance framework in Malaysia is more effective than that in Indonesia because of its centralized approach, stronger independence of the Sharia Supervisory Board, and stricter Sharia disclosure requirements. It provides a more robust and comprehensive system for ensuring compliance with Sharia principles and promoting transparency in Islamic banking and finance operations than the decentralized framework in Indonesia.

The future of Sharia governance in Islamic banking and finance hinges on continual enhancement and assimilation of best practices. This involves increasing compliance with Sharia governance standards, adopting robust oversight mechanisms, and advocating transparency in decision-making procedures. Regulatory bodies in the realm of Islamic banking and finance, such as the Central Bank of Indonesia and Central Bank of Malaysia, play a pivotal role in fostering collaboration and exchanging knowledge and expertise. Nonetheless, it is vital to recognize that the effectiveness of a Sharia governance framework ultimately relies on its implementation and the commitment of all stakeholders, encompassing Islamic financial institutions, regulators, scholars, and customers.



## CONCLUSION

The differences in Sharia governance frameworks between Malaysia and Indonesia significantly impact the efficiency and credibility of Islamic banking. In structural terms, Malaysia has implemented a two-tier Sharia governance system, comprising a central Sharia council at the national level and a Sharia committee at the institutional level. Conversely, Indonesia employs a more centralized approach featuring a national fatwa council at the national level and an industry-based Sharia board. In addition, the regulatory framework for Sharia governance varies between Malaysia and Indonesia. Malaysia boasts a comprehensive Sharia governance framework issued by the Central Bank of Malaysia, while Indonesia's regulations are distributed across various legislations, acts, guidelines, and circulars, which serve as a guide for Islamic financial institutions.

Malaysia has a more structured and centralized approach, Indonesia's framework is more fragmented. The centralized Sharia governance system in Malaysia has demonstrated greater efficacy in ensuring the autonomy and uniformity of Islamic rulings within Islamic banking and finance. These differences in structural and regulatory frameworks reflect the various approaches taken by Malaysia and Indonesia to implement Sharia governance in Islamic financial institutions. Despite these differences, both countries emphasize the importance of establishing a Sharia committee or board at an institutional level. The Sharia committee or board plays a crucial role in ensuring compliance with the Sharia principles and providing guidance to financial institutions. Additionally, more research is imperative to gain insight into the influence of Sharia governance frameworks on Islamic bank performance and sustainability.

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