

Ensuring The Compliance of Islamic Finance Applications with Shariah Principles in Ethiopia: The Way Forward

Etiyopya'da İslami Finans Uygulamalarının Şer'i İlkelere Uyumunun Sağlanması: İzlenecek Yol

SUADIQ MEHAMMED HAILU

suadiq1434@gmail.com
orcid.org/0000-0003-3270-1357

ÖMER FARUK TEKDOĞAN

Dr. Öğr. Üyesi, Ankara Sosyal Bilimler Üniversitesi, İslami Araştırmalar Enstitüsü, İslam Ekonomisi ve Finansı Bölümü, Ankara, Türkiye

Asst. Prof. Social Sciences University of Ankara, Institute for Islamic Studies, Department of Islamic Economic and Finance, Ankara, Türkiye

tekdogan82@gmail.com
orcid.org/0000-0002-4397-1718

MAKALE BİLGİSİ / ARTICLE INFORMATION

Makale Türü /Article Types: Araştırma Makalesi / Research Article

Geliş Tarihi /Received: 9 Şubat 2023

Kabul Tarihi/Accepted: 9 Haziran 2023

Yayın Tarihi/Published: 30 Haziran 2023

ATIF/CITE AS:

Hailu, Suadiq Mehammed – Tekdogan, Ömer Faruk, "Ensuring The Compliance of Islamic Finance Applications with Shariah Principles in Ethiopia: The Way Forward", *Hitit İlahiyat Dergisi*, (Haziran/June 2023) 22/1, 139-168. <https://doi.org/10.14395/hid.1247875>

Yazar Katkıları: %50 - %50

Değerlendirme: Bu makalenin ön inceleme iki iç hakem (editörler- yayın kurulu üyeleri) içerik inceleme ise iki dış hakem tarafından çift taraflı kör hakemlik modeliyle incelendi. Benzerlik taraması yapılarak (turnitin) intihal içermediği teyit edildi.

Etik Beyan: Bu çalışmanın hazırlanma sürecinde bilimsel ve etik ilkelere uyulduğu ve yararlanılan tüm çalışmaların kaynakçada belirtildiği beyan olunur.

Etik Bildirim: ilafdergi@hitit.edu.tr <https://dergipark.org.tr/tr/pub/hid>

Çıkar Çatışması: Çıkar çatışması beyan edilmemiştir.

Finansman: Bu araştırmayı desteklemek için dış fon kullanılmamıştır.

Telif Hakkı & Lisans: Yazarlar dergide yayınlanan çalışmalarının telif hakkına sahiptirler ve çalışmalarını CC BY-NC 4.0 lisansı altında yayımlanmaktadır.

Author Contributions: %50 - %50

Review: Single anonymized - Two Internal (Editorial board members) and Double anonymized - Two External Double-blind Peer Review

Ethical Statement It is declared that scientific and ethical principles have been followed. while conducting and writing this study and that all the sources used have been properly cited.

Complaints: ilafdergi@hitit.edu.tr - <https://dergipark.org.tr/tr/pub/hid>

Conflicts of Interest The author(s) has no conflict of interest to declare.

Grant Support: The author(s) acknowledge that they received no external funding to support this research.

Copyright & License Authors publishing with the journal retain the copyright to their work licensed under the CC BY-NC 4.0.

Ensuring The Compliance of Islamic Finance Applications with Shariah Principles in Ethiopia: The Way Forward

Abstract

The notion behind Islamic finance is providing alternative Shariah-compliant financial services and products for those who do not willingly access conventional finance as it contravenes Shariah principles. Currently, Islamic finance is expanding throughout Muslim and non-Muslim countries. One of the most critical challenges of the Islamic financial sector is the extent of the compliance of Islamic finance practices with Shariah principles. Therefore, there should be a control mechanism for ensuring the compliance of products and services provided by Islamic financial institutions with Shariah principles. Scholars argue that institutions engaged in Islamic finance should apply the Shariah governance framework in countries where Islamic finance is being practiced. The Shariah governance framework is mainly categorized into two main approaches: centralized and decentralized Shariah governance frameworks. The availability of a centralized Shariah governance framework is essential to ensure the application of Islamic finance in accordance with Shariah principles. Ethiopia is one of the countries that accommodated the application of Islamic finance through exclusively interest-free banking windows by conventional banks in 2011 and fully-fledged interest-free banks in late 2019. However, the National Bank of Ethiopia (NBE) did not specify any Shariah governance framework in its legislation. The unavailability of an established Shariah governance framework may expose the sector to the risk of Shariah non-compliance. This study investigates how to ensure compliance of Ethiopia's Islamic finance applications with Shariah principles. Document studies and semi-structured interviews were conducted with 15 respondents, including experts in Islamic finance, Shariah scholars, and Islamic finance practitioners, to collect the needed data for this endeavor. The findings indicate that interest-free banks, especially interest-free banking windows, do not give the necessary attention to the issue of the Shariah governance framework. The presumed manifestations of Shariah compliance in Ethiopia are having a Shariah advisory committee, using Arabic words and names for their products and services, declaring they are following the Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and Islamic Financial Services Board (IFSB) standards, and participating in corporate social activities. However, these claims are insufficient to argue that their products and services are Shariah-compliant as long as an authorized external body oversees and controls their application. In addition, the results indicate that adapting the AAOIFI standards to the extent of industry development is recommended to ensure Shariah compliance in Ethiopia. Besides, considering responsible stakeholders in ensuring Shariah compliance, the government/NBE and financial institutions engaged in Islamic finance are identified as primary stakeholders. On the other hand, the Ethiopian Islamic Affairs Supreme Council (EIASC), religious scholars and

institutional Shariah advisors, interest-free professional associations, academicians in Islamic economics and finance, and educational institutions are considered secondary stakeholders. In addition, the findings also indicate that the policymakers' approaches of Türkiye, Malaysia, Kenya, and South Africa to the Islamic finance industry could be the best model for policymakers in Ethiopia. Establishing a centralized Shariah advisory committee under the NBE is recommended to ensure the compliance of interest-free finance applications with Shariah principles in Ethiopia. To this endeavor, all stakeholders such as government/NBE, financial institutions engaged in the Islamic finance industry, EIASC, religious scholars and institutional Shariah advisors, interest-free professional associations, academicians in Islamic economics and finance, and educational institutions should play a significant role by fulfilling their respective responsibilities.

Keywords: Islamic finance, Ethiopia, National Bank of Ethiopia, Shariah governance, Shariah compliance, interest-free banking

Etiyopya'da İslami Finans Uygulamalarının Şer'i İlkelere Uyumunun Sağlanması: İzlenecek Yol

Öz

Geleneksel finansın ürünleri ve operasyonları İslam'ın ilkelerini ve yasalarını dikkate almamakta ve bunlara uymamaktadır. Bu nedenle, geleneksel finansın sunduğu hizmetlere erişmeye istekli olmayanlar için İslam'ın ilkelerine ve yasalarına uygun alternatif finansal ürünler ve hizmetler sunmak İslami finansın arkasındaki temel fikirdir. İslami finans halihazırda İslam İşbirliği Teşkilatı üyesi ülkelerde olduğu kadar gayrimüslimlerin çoğunluk olduğu ülkelerde de büyüyen bir sektördür. İslami finans sektörünün karşılaştığı en kritik zorluklardan birisi, İslami finans uygulamalarının Şer'i ilkelerle ne kadar uyumlu olduğudur. Bu nedenle, İslami finans kuruluşlarının sunduğu ürün ve hizmetlerin Şer'i ilkelere uygunluğunu sağlamaya yönelik bir kontrol mekanizması olmalıdır. İslami finansın uygulandığı ülkelerde, İslami finans sektöründe faaliyette bulunan kurumlar tarafından uygulanması gereken bir Şer'i yönetim çerçevesinin olması gerektiği savunulmaktadır. Şer'i yönetim çerçevesi esas olarak merkezileştirilmiş ve merkezi olmayan Şer'i yönetim çerçevesi olmak üzere iki yaklaşıma ayrılmaktadır. Merkezi bir Şer'i yönetim çerçevesinin mevcudiyeti, İslami finansın Şer'i ilkelere uygun olarak uygulanmasını sağlamak için esastır. Etiyopya, 2011'de faizsiz bankacılık pencereleri aracılığıyla geleneksel bankalar tarafından ve 2019'un sonlarında ise tam teşekküllü faizsiz bankalar tarafından İslami finans uygulamalarını devreye alan ülkelerden biridir. Ancak, Etiyopya Ulusal Bankasının (NBE) belirlediği yasal düzenlemelerde Şer'i yönetim çerçevesine dair herhangi bir hüküm veya ibare bulunmamaktadır. Yerleşik bir Şer'i yönetim çerçevesinin bulunmaması, İslami finans sektörünü Şer'i uyumsuzluk riskine maruz bırakabilir. Bu çalışma, Etiyopya'nın İslami finans uygulamalarının Şer'i ilkelere uygunluğunun nasıl sağlanacağını araştırmaktadır. Bu çaba için gerekli verileri toplamak amacıyla İslami finans uzmanları, İslam alimleri ve İslami finans uygulayıcıları da dahil olmak üzere 15 katılımcı ile yarı yapılandırılmış görüşmeler ve belge çalışmaları yapılmıştır. Bulgular, faizsiz bankaların, özellikle faizsiz bankacılık pencerelerinin, Şer'i yönetim çerçevesi konusuna gerekli ilgiyi göstermediğini işaret etmektedir. Etiyopya'da Şer'i uyumluluğunun varsayılan unsurları arasında Şer'i danışma komitesine sahip olmaları, ürün ve hizmetleri için Arapça kelimeler ve isimler kullanmaları, İslami Finansal Kurumlar için Muhasebe ve Denetleme Kurumu (AAOIFI), İslami Finansal Hizmetler Kurulu (IFSB) standartlarını takip ettiklerini beyan etmeleri ve kurumsal sosyal faaliyetlere katılmaları yer almaktadır. Ancak bu unsurlarla birlikte dışarıdan yetkili bir kuruluş tarafından İslami finans kurumlarının uygulamalarını gözetlenmesi ve denetlenmesi gereği göz önüne alındığında, İslami finans kurumlarının ürün ve hizmetlerinin Şer'i açıdan uygun olduğunu iddia etmek için yeterli zemin olmayacaktır. Bununla birlikte, Etiyopya'da Şer'i uyumluluğu sağlamak için, İslami finans sektörünün

gelişimi ölçüsünde AAOIFI standartlarının uyarlanmasının önerildiği çalışma kapsamında elde edilen bulgularda görülmektedir. Ayrıca, Şer'i uyumluluğun sağlanmasındaki sorumlu paydaşlar dikkate alındığında, İslami finans sektörüyle ilgili hükümet organları, Etiyopya Merkez Bankası (NBE) ve finansal kuruluşlar birincil paydaşlar olarak tanımlanmaktadır. Öte yandan, Etiyopya İslami İşler Yüksek Konseyi (EIASC), İslam alimleri ve kurumsal Şer'i danışmanlar, faizsiz finans meslek kuruluşları, İslam ekonomisi ve finansı alanında çalışan akademisyenler ve eğitim kurumları ikincil paydaşlar olarak değerlendirilmektedir. Ayrıca, elde edilen bulgular Türkiye, Malezya, Kenya ve Güney Afrika'daki politika yapıcılarının İslami finans sektörüne yaklaşımlarının Etiyopya'daki politika yapıcılar için en iyi örnek olabileceğini de göstermektedir. Etiyopya'da faizsiz finans uygulamalarının Şer'i ilkelere uygunluğunu sağlamak için NBE bünyesinde merkezi bir Şer'i danışma komitesi kurulması tavsiye edilmektedir. Bu doğrultuda, hükümet, NBE, İslami finans sektörüyle uğraşan finans kurumları, EIASC, İslam alimleri ve kurumsal Şer'i danışmanlar, faizsiz finans meslek kuruluşları, İslam ekonomisi ve finansı alanında çalışan akademisyenler ve eğitim kurumları gibi tüm paydaşlar sorumluluklarını yerine getirerek önemli bir rol oynamalıdır.

Anahtar Kelimeler: İslami finans, Etiyopya, Etiyopya Merkez Bankası, Şer'i yönetişi, Şer'i uyumluluk, faizsiz bankacılık

Introduction

Ethiopia is a country located in East Africa. It is Africa's second most populous country after Nigeria, and its total population is expected to reach 122 million in 2022. With this population, Ethiopia is ranked as the 12th most populous country globally.¹ The Ethiopia Population Census Commission reported that, according to the 2007 census, 34% of the Ethiopian population practices Islam.²

In 1991, the communist system was dismantled and replaced by the Ethiopian Peoples' Revolutionary Democratic Front (EPRDF). The EPRDF changed the economic philosophy from a planned economy to a market-driven economy. The EPRDF started the economic transformations by declaring proclamations on the Monetary and Banking sectors. Proclamation No. 83/1994 on Monetary and Banking and Proclamation No. 84/1994 on Licensing and Supervision of the Banking sector are the best examples of EPRDF's financial sector reform efforts. These proclamations permit the establishment of private banks in Ethiopia. Consequently, Awash International Bank, the first private bank in Ethiopia, was established in 1994 as a share company.³

The financial system of Ethiopia consists of banking institutions, insurance companies, microfinance institutions, and capital goods or lease companies. As of December 2022, there were 30 banks, 18 insurance companies (including one state-owned and 17 private insurance companies), 40 microfinance institutions, and six private capital goods finance/lease companies providing services under the National Bank of Ethiopia (NBE) supervision.⁴

1.1. The History of Islamic Finance in Ethiopia

Ethiopian Muslims have engaged in numerous personal and collective efforts to obtain permission to establish Islamic financial institutions (IFIs). As an illustration, one of the inquiries presented by representatives of the Ethiopian Muslim diaspora community to the late Prime Minister Meles Zenawi in 2007 pertaining to the authorization of launching Islamic financial institutions in Ethiopia.⁵ A significant milestone in Islamic finance in Ethiopia was achieved by a group of individuals who conceived the idea of

¹ United Nations Department of Economic and Social Affairs, Population Division, *World Population Prospects 2022: Summary of Results* (United Nations, New York, 2022).

² Federal Democratic Republic of Ethiopia Population Census commission, *Summary and Statistical Report of the 2007 Population and Housing Census Results* (Addis Ababa, Ethiopia, 2008).

³ Charles Harvey, *Banking Reform in Ethiopia* (Brighton: Institute of Developing Studies, 1996). 25-26.

⁴ National Bank of Ethiopia (National Bank of Ethiopia, "Financial institutions", 2022).

⁵ Dereje Feyissa, "The Transnational Politics of the Ethiopian Muslim Diaspora", *Ethnic and Racial Studies* 35/11 (Kasım 2012), 1893-1913.

establishing a comprehensive interest-free institution called ZamZam Bank. Furthermore, they endeavored to raise awareness about Islamic finance and persuade parliamentarians, ministers, and government officials regarding the importance of interest-free finance in Ethiopia.⁶

On June 28, 2008, a significant development took place as the Banking Business Proclamation of Ethiopia, Proclamation No. 592/2008, included the implementation of interest-free finance for the first time. Within this proclamation, Article 22 (2) stipulates that the Central Bank has the authority to issue directives to govern banking operations on mobilizing non-interest-bearing deposits.⁷ Following the issuance of this proclamation, the founding members of ZamZam Bank initiated the sale of shares. They undertook other essential preparations to establish Ethiopia's first fully-fledged interest-free bank. However, despite fulfilling all the requirements for launching the bank, the NBE ultimately issued Directive SBB/51/2011 in September 2011, which allowed exclusively interest-free banking services to be conducted through windows within a conventional bank.⁸ This directive halted the progress toward establishing a fully-fledged interest-free bank and paved the way for introducing interest-free windows within traditional banks. Following the issuance of this directive, the state-owned Commercial Bank of Ethiopia and the privately-owned Oromia Bank obtained permission from the NBE in 2013 to offer interest-free banking services through the window system.⁹ Furthermore, by the end of 2021, 12 traditional banks began offering interest-free products and services through the window system.¹⁰

Even though the undertaken journey to establish a fully-fledged interest-free bank was closed by directive No. SBB/51/2011, the Muslim communities continued to ask the government permission to launch a fully-fledged interest-free bank until 2019. During this period, the founders of ZamZam Bank carried out different activities regarding the consent of a fully-fledged interest-free bank, including sending a letter to new Prime Minister Dr. Abiy Ahmed Ali and the newly appointed Governor of NBE, Dr. Yinager Dessie.¹¹

⁶ Nassir Dino, "Islamic Banking in Ethiopia: A paradigm Shift", *ISFIR Review* 12/5 (2022).

⁷ Banking Business Proclamation (BBP), Federal Negarit Gazeta 14th Year No 57. (25 August 2008), Proclamation No. 592/art.22/3,p.4216.

⁸ Licensing and Supervision of Banking Business (SBB): Directives to Authorize the Business of Interest Free Banking, National Bank of Ethiopia (2011), Directive No. SBB/ 51/ art.2/3,p.2.

⁹ Suadiq Mehammed HaiLu - Ibrahim Bushera, "Interest Free Banking in Ethiopia: Prospects and Challenges", *International Journal of Islamic Economics and Finance Studies*, 2 (July 2020), 119-137.

¹⁰ Suadiq Mehammed Hailu - Nissar Ahmad Yattoo, "Islamic Finance In Ethiopia: Current Status, Prospects And Challenges", *International Journal of Islamic Banking and Finance Research*, (30 August 2021), 1-18.

¹¹ Dino, "Islamic Banking in Ethiopia: A paradigm Shift", 35-43.

Finally, in 2019, the struggles of Ethiopian Muslims gave fruit, and Dr. Abiy Ahmed Ali, the current prime minister, declared permission to establish a full-fledged interest-free financial institution on May 22, 2019.¹² Consequently, the NBE issued a proclamation called “Proclamation No: 1159/2019”¹³, which permits the establishment of a full-fledged interest-free bank. In line with the authorization to establish fully-fledged interest-free banks in Ethiopia, four banks, namely ZamZam, Hjira, Shabelle, and Rammis, have commenced operations to provide comprehensive interest-free banking services and products.

IFIs must ensure that their products and procedures follow Shariah principles. Failing to comply with these principles poses a risk of Shariah non-compliance for such institutions. As a result, IFIs may face potential failures, which can subsequently impact the Islamic finance industry as a whole.¹⁴ Therefore, an efficient and sound Shariah governance system can be vital in tackling the collapse of IFIs, business scandals, and potential Shariah non-compliance risks.¹⁵

Until 2009, there was no shared definition for Shariah governance in the Islamic finance industry. The IFSB then defines the Shariah governance system as a collection of institutional procedures through which IFIs ensure effective and independent oversight of Shariah compliance over issuing relevant Shariah provisions and their distribution to the relevant bodies of the IFI. The observation of Shariah compliance is performed through the internal Shariah review and the annual Shariah review. Therefore, according to IFSB-10, the Shariah governance system comprehends three main functions: governance, control, and compliance.¹⁶

1.2. Standardization in Islamic Finance

Standardization is defined from various perspectives across different disciplines. For example, ISO characterizes standardization as the process

¹² Addis Getachew, “Ethiopian PM Attends Iftar with Muslim Community: Abiy Ahmed Promises Grand Mosque, Interest-Free Banking for Muslims”, Anadolu Agency, (15 December 2022).

¹³ Banking Business Proclamation (BBP), Federal Negarit Gazeta 25th Year No 88. (9 September 2019), Proclamation No. 1159/art.59/1,p.11689.

¹⁴ Rihab Grassa, “Shariah Supervisory System in Islamic Financial Institutions: New Issues and Challenges: A Comparative Analysis between Southeast Asia Models and GCC Models”, *Humanomics* 29/4 (2013), 333-348.

¹⁵ Aznan Hasan - Ruslan Sabirzyanov, “Optimal Shari’ah governance model in Islamic finance regulation”, *International Journal of Education and Research* 3/4 (2015), 243-258.

¹⁶ Islamic Financial Services Board (IFSB), Guiding Principles on Shari’ah Governance Systems for Institutions Offering Islamic Financial Services (Malaysia: Islamic Financial Services Board, Acceptance December 2009, IFSB-10) .

of establishing or formulating a standard for a particular subject.¹⁷ The standardization process ends by developing a standard for the subject matter of the process. ISO also defines a standard as a guideline issued by a recognized organization through mutual consent and approval for a specified activity to achieve the optimal degree of the intended objective".¹⁸

Like its conventional counterpart, the Islamic finance sector also needs profound standards for its product and service. However, since the inception of modern Islamic finance, studies like Iqbal, Ahmad and Khan,¹⁹ Khan,²⁰ Smolo and Habibovic,²¹ Yaacob and Abdullah²² identified that lack of standardization has been among the main hindrance to the Islamic finance sector development. Furthermore, Shanmugam and Zahari²³ stated that the absence of standardization might lead to ambiguity, misunderstanding, and discomfort among scholars and investors. Therefore, this issue affects the expansion of the Islamic finance sector significantly.

To resolve the lack of standardization problem in the Islamic finance industry, internationally recognized standard-setter institutions such as Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), Islamic Financial Services Board (IFSB), International Islamic Financial Market (IIFM), and International Islamic Rating Agency (IIRA) are issuing standards for IFIs.

AAOIFI has released 117 standards across five categories: Shariah, accounting, auditing, ethics, and governance. These standards are adopted by different countries and IFIs at varying levels, including full adoption, partial adoption, and guidance. For instance, based on the 2022 AAOIFI Footprint Report, 39 countries have fully adopted the Shariah standards, 48 have fully adopted the accounting standards, and 48 have fully adopted the governance

¹⁷ T.R.B. Sanders (ed.), *The Aims and Principles of Standardization* (United Kingdom: International Organization for Standardization (ISO), 1972), 17.

¹⁸ Sanders, "The Aims and Principles of Standardization", *The Aims and Principles of Standardization*, 18.

¹⁹ Munawar Iqbal et al., *Challenges Facing Islamic Banking* (Jeddah, Kingdom of Saudi Arabia: Islamic Development Bank, Islamic Research and Training Institute, 1998), Occasional Paper, no. 1.

²⁰ M. Fahim Khan, "Setting Standards For Shariah Application in the Islamic Financial Industry", *Thunderbird International Business Review* 49/3 (Mayis 2007), 285-307.

²¹ Edib Smolo - Elmin Habibovic, "Barriers to Growth of Islamic Finance: Issue of Standardisation", *Islamic Banking and Finance: Principles, Instruments and Operations*, 2012, 715-737.

²² Hakimah Yaacob - Apnizan Abdullah, "Standards Issuance for Islamic Finance in International Trade: Current Issues and Challenges Ahead", *Procedia - Social and Behavioral Sciences* 65 (Aralık 2012), 492-497.

²³ Bala Shanmugam - Zaha Rina Zahari, *A primer on Islamic finance* (Charlottesville, Va: Research Foundation of CFA Institute, 2009), 93.

standards. Additionally, the Shariah, accounting, and governance standards of AAOIFI have been adopted by 45, 55, and 51 regulatory jurisdictions, respectively, at different levels of adoption.²⁴

As an international regulatory and supervisory agency to promote prudent and transparent IFIs, IFSB issues 37 standards, guiding principles, and technical notes. As of June 2022, IFSB has 188 members consisting of 81 regulatory and controlling bodies, ten international inter-governmental organizations, and 97 market players (financial institutions, professional firms, associations, and stock markets) in 57 jurisdictions.²⁵

1.3. Statement of The Problem

SBB/72/2019²⁶ describes interest-free banking as a banking institution involved in mobilizing and advancing funds in line with Shariah rules. Considering regulatory and supervision issues, article 7(1) of SBB/72/2019 states that an interest-free bank should fulfill all regulatory and oversight requirements of NBE for conventional banks except for interest rates. Further, regarding compliance with Shariah principles, Article 7(2) of SBB/72/2019 states that the board of directors of an interest-free bank shall postulate a detailed rule and guide on Shariah compliance control mechanisms. However, this directive does not provide any information regarding the controlling mechanism or the Shariah control framework. Therefore, it has not yet been determined how and by whom the practices of licensed interest-free banks will be checked and supervised and whether they comply with Shariah principles. For this purpose, this study examines how Islamic banks in Ethiopia can ensure the compliance of their products and services with Shariah principles.

1.4. The Objective of the Study

The primary objective of this paper is to explore potential strategies for interest-free banks in Ethiopia regarding complying their products and services with Shariah principles.

The specific objectives of this study are:

- I. Exploring the most suitable type of Shariah governance model for Ethiopian IFIs.

²⁴ Auditing Organization for Islamic Financial Institutions (AAOIFI), AAOIFI Footprint Report 2022 (Kingdom of Bahrain: AAOIFI Secretariat, 2022), 49.

²⁵ Islamic Financial Services Board (IFSB), "About IFSB -Background" (Accessed 20 December 2022).

²⁶ Licensing and Supervision of Banking Business (SBB): Directives to Authorize the Business of Interest Free Banking, National Bank of Ethiopia (2019), Directive No. SBB/ 72.

- II. Examining whether Ethiopia can develop its own Islamic financial standards.
- III. Investigating whether adopting international Shariah standards or developing a new local Shariah standard is the best approach for Ethiopian IFIs.
- IV. Identifying the stakeholders in ensuring the compliance of Islamic finance applications with the Shariah principle in Ethiopia.

1. Literature Review

There are many studies regarding ensuring the compliance of Islamic finance applications with Sharia principles. However, to our knowledge, no research has been done about how IFIs in Ethiopia can ensure their products and services conform with Shariah principles except Oumer.²⁷ He forwarded a recommendation for policymakers in Ethiopia to establish a centralized Shariah Supervisory body that is mandated to control and oversight whether institutions are working within the line of Shariah principles.

Researchers in Islamic finance suggest various ways of ensuring Shariah compliance. For instance, Khan²⁸ stated that there is a need for a global self-regulatory body organized by Shariah experts worldwide to develop the highest Shariah standard and control the application of for Islamic finance industry. In addition, Grassa²⁹ recommended both local and global Shariah governance mechanisms and stated that national Shariah authorities are crucial in monitoring and ensuring Shariah compliance. Alkhamees³⁰ argued that regulatory bodies should enact a sound Shariah governance framework to safeguard the robustness of the Islamic finance industry and stakeholders’

²⁷ Kamil Abdu Oumer, *A Critical Appraisal of the Regulatory Regime of Islamic Banking in Ethiopia* (Hamad Bin Khalifa University (Qatar), 2021), 60.

²⁸ Khan, “Setting Standards For Shariah Application in the Islamic Financial Industry”, 306.

²⁹ Grassa, “Shariah Supervisory System in Islamic Financial Institutions: New Issues and Challenges: A Comparative Analysis between Southeast Asia Models and GCC Models”, 346.

³⁰ Ahmad Alkhamees, “The Impact of Shari’ah Governance Practices on Shari’ah Compliance in Contemporary Islamic Finance”, *Journal of Banking Regulation* 14/2 (Nisan 2013), 134-163.

confidence. Alam et al.³¹, Bhatti and Maria³², Hussain³³, and Shafii et al.³⁴ assert that an efficient and effective Shariah governance framework is essential to ensuring Shariah compliance, minimizing Shariah non-compliance risk, and eliminating the confusion among stakeholders of IFIs.

From the perspectives of regulatory bodies, Hasan³⁵ classified the Shariah governance models of that time into five types: reactive approach, passive approach, minimalist approach, proactive approach, and interventionist approach. Considering factors such as legal or regulatory framework, regulatory requirements for Shariah Supervisory Board (SSB), National Shariah Authority, and organizational SSBs, Ahmed³⁶ identified four Shariah governance regimes, namely legally constructed Shariah governance, robust Shariah governance, passive Shariah governance, and market-driven Shariah governance system. Further, Hamza³⁷ classified the Shariah governance models into decentralized and centralized ones. Similarly, Hasan and Sabirzyanov³⁸ categorized the Shariah governance practices into three main modes: centralized, laissez-faire or self-regulation, and hybrid model. In the hybrid model, there is a passive centralized SSB with active institutional SSBs. Besides, Fatmawati et al.³⁹ examined 11 countries' Shariah governance framework. Then, they categorized these frameworks into strict, moderate, or flexible Shariah governance framework approaches.

³¹ Md. Kausar Alam vd., "Why Does Shariah Governance Framework Important for Islamic Banks?", *Asian Journal of Economics and Banking* 5/2 (11 Ağustos 2021), 158-172.

³² Maria Bhatti, "Managing Shariah Non-Compliance Risk via Islamic Dispute Resolution", *Journal of Risk and Financial Management* 13/1 (18 Aralık 2019), 1-9.

³³ Mohammad Azam Hussain, "The Duties and Responsibilities of Shariah Committee in Ensuring Shariah Compliance of Islamic Financial Business in Malaysia", *Selected Legal Issues in Indonesia and Malaysia* (UNISSULA PRESS, 2020), 1-18.

³⁴ Zurina Shafii vd., "Integrated Internal-External Shariah Audit Model: A Proposal towards the Enhancement of Shariah Assurance Practices in Islamic Financial Institutions", *The Islamic Research and Teaching Institute* 1436 (2015).

³⁵ Zulkifli Bin Hasan, "Regulatory Framework of Shari'Ah Governance System in Malaysia, GCC Countries and the UK", *Kyoto Bulletin of Islamic Area Studies* 3/2 (2009), 82-115.

³⁶ Habib Ahmed, "Shari'ah Governance Regimes for Islamic Finance: Types and Appraisal - I regimi di governance conformi alla shari'ah nella finanza islamica: tipologia e valutazione", *Economia Internazionale/International Economics* 66/4 (2011), 393-412.

³⁷ Hichem Hamza, "Sharia Governance in Islamic Banks: Effectiveness and Supervision Model", *International Journal of Islamic and Middle Eastern Finance and Management* 6/3 (23 Ağustos 2013), 226-237.

³⁸ Hasan - Sabirzyanov, "Optimal Shari'ah Governance Model in Islamic Finance Regulation", 243-248.

³⁹ Dewi Fatmawati vd., "Shariah Governance in Islamic Banks: Practices, Practitioners and Praxis", *Global Finance Journal* 51/100555 (2020).

Considering the efficient and effective Shariah governance approaches, Hamza⁴⁰ examined the decentralized and centralized Shariah governance models. He states that reaching a consensus on Shariah interpretation and managing disputes in the decentralized Shariah governance model is challenging. Additionally, it creates differences in the application of Islamic finance within the same country and harms the credibility of the Islamic Finance Industry. However, the centralized Shariah governance model creates consistency in an Islamic finance application, reduces disputes on Shariah interpretation, and creates good competition between institutions. Ahmed⁴¹ argues that the centralized or national SSB can reduce the Shariah compliance, reputation, and legal risks arising in IFIs and generate stability in the industry. In addition, Grassa⁴² stated that the centralized SSB is the more efficient and practical approach to control and oversight of the compliance of financial institutions' operation with Shariah principles than the decentralized SSB or institutional SSB. On the other hand, COMCEC⁴³ recommends the national or centralized Shariah governance approach with institutional SSB under a robust control of central SSB to ensure the compliance of Islamic finance application with Shariah principles.

2. Research Methodology

A qualitative research method is applied to examine how Islamic banks in Ethiopia can ensure the compliance of their products and services with Shariah principles. According to Busetto et al.⁴⁴, the most commonly applied qualitative data collection methods are semi-structured interviews, observations, document studies, and focus groups. This study used semi-structured interviews and document studies from these qualitative data collection methods. Document studies or analysis refers to a review by the researcher for documents like reports, directives, proclamations, guidelines, archives, and letters.

To conduct semi-structured interviews, identifying the potential respondents who can respond to research questions is the primary task.

⁴⁰ Hamza, "Sharia Governance in Islamic Banks: Effectiveness and Supervision Model", 226–237.

⁴¹ Ahmed, "Shari'ah Governance Regimes for Islamic Finance: Types and Appraisal", 393–412.

⁴² Grassa, "Shariah Supervisory System in Islamic Financial Institutions: New Issues and Challenges: A Comparative Analysis between Southeast Asia Models and GCC Models", 346.

⁴³ Standing Committee for Economic and Commercial Cooperation (COMCEC) COMCEC, *Improving Shariah Governance Framework in Islamic Financ* (2020), 29.

⁴⁴ Loraine Busetto vd., "How to Use and Assess Qualitative Research Methods", *Neurological Research and Practice* 2/1 (Aralik 2020), 14.14., "plainCitation": "Loraine Busetto vd., "How to Use and Assess Qualitative Research Methods", *Neurological Research and Practice* 2/1 (Aralik 2020)

Accordingly, the authors tried to conduct semi-structured interviews with Experts in Islamic finance, Shariah scholars, and Islamic finance practitioners. As a result, the details of the respondents who participated in the interview are presented in the following table.

Table 1. Backgrounds of the semi-structured interview respondents

No.	Types of Respondents	Number
1	Experts in Islamic finance	9
2	Shariah scholars and practitioners	3
3	Islamic finance practitioners	3
	Total	15

There are no hard and fast rules regarding the sampling of interviewees. However, Crabtree and Miller⁴⁵ indicated that five to eight respondents for the homogeneous sample and 12-20 respondents for the non-homogenous sample are sufficient. Therefore, the sample size of this study is satisfactory, with 15 respondents.

All interviews are recorded with mobile and computer devices and converted to text in line with the research questions. Galletta and Cross⁴⁶ stated that transcription is the preliminary step before analyzing semi-structured interview data. The interview was conducted in the Amharic language (the official language of Ethiopia). Accordingly, the interview records of all respondents were typed out in English. Consequently, the transcription was analyzed using methods such as coding (finding essential themes of the responses), identifying patterns using codes (frequency, magnitude, type, process, and structure), and selecting them based on patterns. Finally, the result is presented descriptively using tables, figures, and charts.

3. Results and Discussion

The collected data results through interview questions are presented through five main themes. The first theme encompasses interview questions one and two, and the main subject of these questions is the current situation of the Shariah governance framework in Ethiopia. The second theme includes only interview question three, and its topic is the presumed manifestations that products and services offered by interest-free banks are Shariah-compliant. The third category comprises interview questions four, five, and six, and its primary premise is the approaches of standardization, either local

⁴⁵ Benjamin F. Crabtree - William L. Miller , Benjamin F. Crabtree - William L. Miller (ed.), *Doing qualitative research* (Thousand Oaks, Calif: Sage Publications, 1999).

⁴⁶ Anne Galletta - William E. Cross, *Mastering the Semi-Structured Interview and Beyond: From Research Design to Analysis and Publication* (NYU Press, 2013).

or international. Model countries' approaches to Islamic finance are discussed under the fourth team with interview question seven. Finally, the fifth theme comprises interview questions eight, nine, and ten. The subject of the fifth team is the main stakeholders in ensuring the compliance of Islamic finance applications in Ethiopia with Shariah principles.

3.1. The Current Situation of the Shariah Governance Framework in Ethiopia

The banking business directive of Ethiopia does not include anything about the controlling mechanism or Shariah governance framework. Therefore, it has not yet been determined how and by whom the practices of licensed interest-free banks will be checked and supervised and whether they comply with Shariah principles. Therefore, the first two interview questions were forwarded to the respondents to know the availability of efforts and invitations regarding the Shariah governance framework and standardizing the application of Islamic finance in Ethiopia by NBE and other stakeholders. Unfortunately, the results indicated no action or invitation regarding the Shariah governance framework and standardizing the application of Islamic finance in Ethiopia by NBE and other stakeholders. Therefore, the issue of the Shariah governance framework and standardization of Islamic finance practice in Ethiopia is still left to the institutions' discretion independently.

3.2. Presumed Manifestations that Products and Services Offered by Interest-free Banks are Shariah Compliant

The interest-free banking business has been applied in Ethiopia through two models: interest-free windows by conventional banks and stand-alone interest-free banks. Accordingly, respondents were asked about the presumed manifestations that products and services offered by a window or fully-fledged interest-free banks are Shariah compliant. The respondent's answer to presumed manifestations that products and services offered by interest-free banks are Shariah compliant is presented in the table below.

Table 2. Presumed Manifestations of Shariah Compliance in Ethiopia

No.	Presumed Manifestations of Shariah Compliance	Frequency
1	Having Shariah advisory committee	15
2	Using Arabic words for their products and services	4
3	Saying they are following AAOIFI or IFSB	3
4	Participating in corporate social activities	1

The above table shows that all respondents presumed that the primary manifestation of Shariah compliance by interest-free banks, especially interest-free windows, is having a Shariah advisory committee. However, unless the operations of interest-free banks are oversight and checked by an independent central Shariah advisory board, having an institutional Shariah advisory committee is not enough to prove to be Shariah compliant. According to AAOIFI governance standards, an Islamic financial institution shall have Shariah supervisory board, internal Shariah review, and audit and governance committee at the institutional level.

3.3. Standardization Approaches

All IFIs in Ethiopia, either conventional windows or fully-fledged interest-free banks, apply Islamic finance without a common reference point. Therefore, the absence of a shared standardization of Islamic finance is one of the sector's main challenges. The standardization problem can be solved by either issuing local Islamic finance standards or adopting international ones. Considering this, we asked respondents about the suitable strategy for Ethiopia from issuing local standards and adopting international standards. The findings indicated that adapting international standards is the best strategy for Ethiopia.

Several reasons are mentioned by respondents why issuing local standards is not a suitable approach to Ethiopia's Islamic finance sector. The first reason cited by all respondents is the lack of skilled human resources in Islamic finance. Therefore, to issue local standards, the availability of scholars

specialized in Fiqh Al-Muamalat (Islamic commercial jurisprudence) with knowledge of Islamic finance is critical. Unfortunately, the reality in Ethiopia is that there are specialized jurists in Fiqh Al-Muamalat without expertise in Islamic finance. In addition, some scholars specialize in Islamic finance without enough knowledge of Fiqh Al-Muamalat. The second reason is the unavailability of education and research institutions specializing in Islamic finance. Islamic finance is not included in the Ethiopian education system, even as a single subject. Therefore, to issue local standards, education and research institutions' availability is vital. The third and last reason is that no responsible body can take this initiative from the regulatory body and the market. Consequently, respondents claimed that issuing local standards should not be a short-term strategy for the Islamic finance sector in Ethiopia.

Respondents were asked which international Islamic finance standards, such as AAOIFI or IFSB, are preferable to adopt by the Islamic finance sector in Ethiopia and to what extent. The interviewee's responses indicated that adopting AAOIFI standards is a preferable standard Islamic finance sector in Ethiopia. However, some respondents recommended IFSB standards for capital adequacy and risk management. The main reasons for the preference for AAOIFI standards are that AAOIFI standards are developed depending on Fiqh, and Ethiopia is geographically near Gulf countries. Therefore, there are different levels of adoption, such as full adoption, partial adoption, use as guidance, and develop local standards based on AAOIFI. Considering this, respondents indicated that as the Islamic finance sector in Ethiopia is at the infant level, adapting only visible or applicable standards in Ethiopia with contextualization is a preferable approach.

3.4. Model Countries' Approaches to Islamic Finance

Countries follow different approaches regarding providing a suitable legal framework environment and specific supervision and control mechanisms for the Islamic finance industry. Consequently, we asked respondents which countries' approach could be Ethiopia's best model. Respondents stated the approaches of countries that adhere to a liberal economic system and Muslim minority countries in terms of number and capacity could be a model to Ethiopia. Specifically, the respondents' recommendation for a model country is demonstrated in the following figure.

Figure 1. The approaches of interviewees to different country models

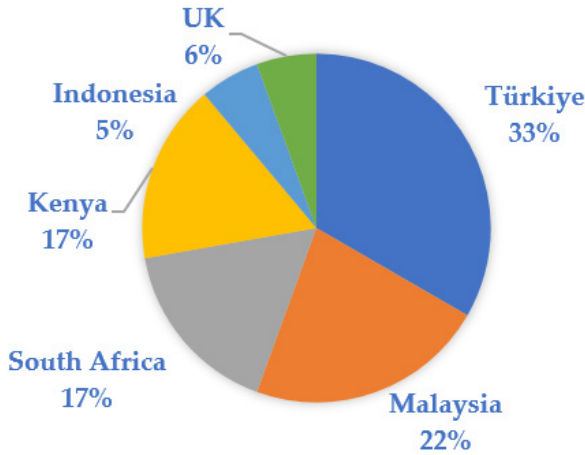


Figure 1 indicates that 33% of respondents recommend that Türkiye's approach can be the model for Ethiopia. Further, Malaysia, South Africa, and Kenya's models are also recommended by respondents. The efforts of the recommended countries by respondents, in terms of accommodating Islamic finance in their financial system and their initiatives regarding the Sharia governance framework, are discussed in the subsequent paragraphs as a potential model for Ethiopia.

Türkiye

One of the exemplary approaches of Türkiye's regulatory body to the Islamic finance sector is the establishment of the current Participation Banks Association of Türkiye (TKBB) by Banking Law No.2001/3138. Product development, improving corporate management, developing skilled human resources, and defending the rights and interests of participation banks are among the objective of the association. All banks that received a license as participation banks should be a member of this association. Further, the Directorate of Participation Banking under the Central Bank of Türkiye (TCMB) was established in February 2021 to strengthen the relationship between the central bank and participation banks, to support the development and stability of the sector, and monitor the relationship of the industry with the international organization in Islamic finance.⁴⁷ These two measures of Türkiye regarding the Islamic finance sector are among the best approaches that can be the model for the regulatory bodies of Ethiopia.

⁴⁷ Türkiye Katılım Bankaları Birliği (TKBB), "Hakkimizda", (Accessed1 January 2023).

Malaysia

Malaysia is unique in giving special attention to the Islamic finance industry. Ladin⁴⁸ stated that Malaysia's approach to the Islamic finance industry could be a model for other countries in developing the sector. Malaysia has been applying a dual banking system following the enactment of the Islamic Banking Act (IBA) in 1983. IBA gave the Central Bank of Malaysia a mandate named Bank Negara Malaysia (BNM) to regulate, license, and supervise Islamic banks alongside conventional banks.⁴⁹ Regarding Shariah governance, BNM launched the National Shariah Advisory Council (NSAC) in 1997 as the highest Shariah authority on Islamic banks and insurance. Besides, to solve the knowledge gaps in Islamic finance and develop talented experts in Islamic finance, BNM established INCEIF University in 2005.⁵⁰ To sum up, the efforts of BNM on providing suitable legal formwork, Shariah governance, and developing experts for the Islamic finance industry can be the best model for NBE.

Kenya

Besides being a minority Muslim country, Kenya accommodated Islamic finance in its financial system before Ethiopia in 2005. However, with the Central Bank of Kenya (CBK) taking a positive approach towards the Islamic finance industry, the Islamic banking law was revised in 2007, leading to the licensing of two Shariah-compliant banks by the CBK.⁵¹ Furthermore, in 2010, CBK amended section 45 of the financial act that permits the CBK to recognize the payment of return in place of interest on government securities. This amendment aims to open opportunities for Shariah-compliant investment in Kenya.⁵² According to Casablanca Finance City (CFC)⁵³, the government of Kenya is playing a significant role in the development of the Islamic finance industry and is planning to be a hub for Islamic finance in East Africa. CBK provides continuous support to the Islamic finance industry by issuing a

⁴⁸ Mohamad Akram Ladin, "Islamic Financial System: The Malaysian Experience and the Way Forward", *Humanomics* 24/3 (29 August 2008), 217-238.

⁴⁹ Saleh Ali Hussein vd., "Islamic Banking Revolution in Malaysia: A Review", *Humanities & Social Sciences Reviews* 7/4 (2019), 267-275.

⁵⁰ Sulaiman Abdullah Saif Al Nasser, Datin, "Introduction to History of Islamic Banking in Malaysia", *Humanomics* 29/2 (2013), 80-87.

⁵¹ Kabir Hassan et al. (ed.), Kabir Hassan vd. (ed.), *Islamic Finance in Africa: The Prospects for Sustainable Development* (Cheltenham, UK ; Northampton, MA, USA: Edward Elgar Publishing, 2022), 3-4.

⁵² Enrique Gelbard et al., "Islamic Finance in Sub-Saharan Africa: Status and Prospects", International Monetary Fund, IMF Working Paper, WP/14/149 (2014), 10-12.

⁵³ Casablanca Finance City (CFC), CFC Africa Insights Islamic Finance in Africa: The Upcoming Frontier. (Toronto: Thomson Reuters, 2019), 24.

detailed master plan. Therefore, Kenya's government's effort to become a hub for Islamic finance can be a model for the Ethiopian government.

South Africa

South Africa, with a relatively small Muslim population, is the first Sub-Saharan African country to have Islamic finance in its financial system. In 2010, the government of South Africa amended the taxation law to recognize Murabaha, Diminishing Musharaka, and Mudharaba. Further, in 2011 another amendment was carried out to introduce Sukuk by the government only. The Shariah governance framework is among the problems facing the Islamic finance sector in South Africa. There is no centralized Shariah advisory body. Despite the Shariah governance challenges, the South African government's effort to amend the taxation act at different times to provide a suitable situation for Islamic finance can be a model to Ethiopia.⁵⁴

3.5. Stakeholders in Ensuring the Compliance of Islamic Finance Applications in Ethiopia with Shariah Principles

The last three interview questions are concerned with identifying the stakeholders responsible for ensuring the compliance of Islamic finance applications with Shariah standards. Respondents listed out the following stakeholders.

Table 3. Stakeholders in Ensuring Shariah Compliance in Ethiopia

No.	Stakeholders	Frequency
1	Government/NBE	14
2	Financial institutions engaged in Islamic finance	11
3	EIASC	10
4	Institutional Shariah advisors	8
5	Religious Scholars	8
6	Academicians in Islamic Economics and Finance	7
7	Educational institutions	7

It is possible to categorize the stakeholders mentioned by respondents as primary and secondary stakeholders. The primary stakeholders are the government/NBE and financial institutions engaged in Islamic finance. Conversely, the secondary stakeholders include Institutional Shariah advisors, EIASC, religious scholars, Interest-free professional associations, Islamic economics and finance academicians, and educational institutions. In the subsequent paragraphs, we summarized the roles of these stakeholders

⁵⁴ CFC, CFC Africa Insights Islamic Finance in Africa: The Upcoming Frontier, 28-29.

in ensuring the compliance of Islamic finance applications in Ethiopia with Shariah principles depending on respondents' feedback.

The mandate to issue a directive related to banking business engaged in non-interest bearing deposit mobilization and utilization is given to NBE by article 22(2) of Banking Business Proclamation No 592/2008 Article. However, the directive of NBE that permits the establishment of interest-free banking does not say anything about the Shariah Governance framework and leaves it at the institutional level. Accordingly, considering the responsibility of the Government/NBE, all respondents stated that the NBE should issue a directive regarding Shariah governance and the oversight mechanism on interest-free banks.

Although the government/NBE is an important stakeholder, the responsibility of ensuring that their products and services align with Shariah principles lies exclusively with conventional interest-free windows and fully-fledged interest-free banks. All respondents stated that the institutions should provide the Islamic finance sector's challenges in Ethiopia and their recommended solutions to NBE. Therefore, conventional interest-free windows and fully-fledged interest-free banks are liable for pushing the NBE to take the necessary measures to solve the sector's problems. Specifically, the institutions also should force NBE to issue a directive regarding the Shariah governance framework to supervise and control the industry. Besides, they should strive to provide Shariah-compliant products and services for their feature endeavor without expecting any controlling mechanizing from NBE.

The EIASC is Ethiopian Muslims' highest central organizing body regarding religious issues. In normal conditions, it is expected that EIASC to facilitate and support the NBE regarding ensuring the compliance of Islamic finance applications with Shariah principles. In addition, the EIASC can push the NBE to provide a Shariah governance framework for the Islamic finance industry. Regarding the role of EIASC, respondents raised two different suggestions. Most respondents suggested that the current status of EIASC is not affordable to facilitate and support the NBE in the Shariah government. In addition, they said that EIASC has many institutional problems that should solve by them.

On the contrary, the minority of respondents stated that EIASC could work with the NBE to ensure Islamic finance's application aligns with Shariah principles. EIASC is the principal institution in finding solutions for Muslim communities' common requests. Therefore, EIASC can play a significant role

in informing the NBE on the importance of having a Shariah governance framework for the Islamic finance industry. At the 2nd regular meeting of EIASC on February 8, 2023, nine different committees were formed under the EIASC structure. One of these committees is the Interest-free Banks Supervision Committee, which aims to collaborate with the NBE and interest-free banks for Shariah supervision.⁵⁵ This initiative by EIASC regarding the Shariah supervision of interest-free banks is commendable.

Religious scholars are responsible for teaching the community about right and wrong according to Islam. Therefore, if the applications of Islamic finance are not compliant with Shariah principles, they should inform the institution and communities regarding the incompliant applications. For example, all prominent religious scholars in Ethiopia have become Shariah advisors for interest-free windows in conventional banks. However, almost all respondents indicated that their role in the bank is for marketing purposes to show customers they have a Shariah advisory board. Hence, in contrast to other religious scholars, those who assume the role of Shariah Advisors ought to fulfill their duty of playing a vital part in ensuring that the products and services offered by their institutions adhere to Shariah principles.

From a conventional perspective, bankers' associations significantly influence the central bank on bank-related issues as they know the sector well, and their recommendations to central banks are significant. In the same way, interest-free banker associations can also play the same role as traditional banker associations. For example, in Ethiopia, the Ethiopian Interest-Free Finance Professionals Association (EIFFFPA) was established in 2021. Assisting policymakers regarding interest-free finance is one of the main objectives of EIFFFPA. Respondents stated that EIFFFPA is among the stakeholders in ensuring the compliance of Islamic finance applications with the Shariah principle in Ethiopia by providing recommendations to regulatory bodies and creating awareness about the Shariah governance framework.

Respondents also indicated that academicians specialized in Islamic economics and finance are responsible for researching to identify the prospects and challenges of the sector. They should provide recommendations to policymakers on necessary measures to assist the expansion and development of interest-free finance applications in line with Shariah principles.

⁵⁵ Ethiopian Islamic Affairs Supreme Council (EIASC), “የኢትዮጵያ እስልምና ጉዳዮች ጠቅላይ ምክር ቤት የዐ-ሎግዎች ጉባዔ በቀጣይ የሚተዳደርበትን ደንብ በሙሉ ድምፅ አፀደቀ [The Ulema Assembly of the Ethiopian Supreme Council for Islamic Affairs has unanimously approved its governing laws]”, Facebook, (11 March 2023,10:05).

Educational institutions are responsible for producing skilled human resources. However, in Ethiopia, state-owned universities have not started giving Islamic economics and finance as a department, even as a single subject. Private universities and colleges have a slight initiation to provide Islamic economics and finance. However, Education and Training Authority (ETA) is not giving accreditation to the Islamic Economics and finance department. When the Ethiopian government authorized the implementation of Islamic finance, it should have also incorporated Islamic economics and finance into the education system. Islamic economics and finance encompass more than just religious education; they represent an alternative economic and financial system based on Shariah principles as an alternative to conventional practices. Moreover, Islamic economics and finance education are accredited and taught in various Western countries such as the USA, the UK, and Australia. Therefore, it is recommended that ETA should accredit the subject as its role is significant to the development and expansion of Islamic finance in Ethiopia.

Conclusion

This study examines how interest-free banks in Ethiopia can ensure compliance with Islamic finance applications with Shariah principles and the way forward. For this purpose, qualitative data collection methods such as semi-structured interviews and document studies were applied to this study. Semi-structured interviews were conducted with 15 respondents, including experts in Islamic finance, Shariah scholars, and Islamic finance practitioners.

Islamic banking in Ethiopia is applied through a separate window within conventional and stand-alone interest-free banks. There is no common Shariah governance framework in Ethiopia to be adopted by IFIs. The finding indicated that interest-free banks, especially interest-free windows, do not give the issue of the Shariah governance framework problem the necessary attention.

Financial institutions providing interest-free banking products and services are marketing themselves as Shariah-compliant financial institutions. Therefore, we asked respondents about the presumed manifestations of their claims. The result indicated that appointing Shariah advisory committee, using Arabic words for their products and services, saying they are following AAOIFI or IFSB standards, and participating in corporate social activities are the main presumed manifestations of Shariah compliance in Ethiopia.

Standardization of the application of Islamic finance can play a significant role in the development of the expansion of the sector. Considering this, the study's outcome shows that adopting the international Islamic finance standard is a suitable approach for Ethiopia compared to developing local standards. Additionally, the finding indicated that adapting the AAOIFI standards depending on the extent of development of the sector in Ethiopia is preferable.

The approaches of countries for the Islamic finance industry are different to a significant extent. Nevertheless, the finding of this study indicated that the policymakers' approaches of Türkiye, Malaysia, Kenya, and South Africa could be the best model for Ethiopia.

Considering the responsible stakeholders in ensuring the compliance of Islamic finance applications with Shariah principles, the result shows that there are primary and secondary stakeholders. The primary stakeholders are the government/NBE and financial institutions engaged in Islamic finance. On the other hand, the secondary stakeholders are the EIASC, religious scholars and institutional Shariah advisors, interest-free professional associations, academicians in Islamic Economics and Finance, and educational institutions.

Recommendations

The main objective of this study is to investigate how to ensure the compliance of Islamic finance applications with the Shariah principle in Ethiopia. The following recommendations are forwarded to the respective stakeholders, depending on the study's findings.

The NBE is the primary stakeholder in the Islamic finance industry as the government gave the mandate to issue directives related to the industry. First, the NBE should create a suitable and competitive infrastructure for the Islamic finance industry by amending directives that tackle Islamic finance applications. Second, the NBE should establish a centralized Shariah advisory committee that can control and oversight the application of Islamic finance by institutions. Third, it is recommended that the NBE adapt AAOIFI standards to be followed by Islamic finance institutions in Ethiopia to the necessary extent. Finally, the Government/NBE of Ethiopia should follow the global Islamic finance development by establishing an independent body under the NBE or Ministry of Finance.

The financial institutions that offer Islamic finance products and services should work together for their common interests. They should enforce the

NBE by providing inputs regarding the challenges facing. Specifically, they should collectively ask the NBE to follow or adapt a Shariah governance framework that will apply to all institutions in the sector.

The EIASC, religious scholars, and institutional Shariah Advisors should work together to ensure that interest-free financial institutions align with Shariah principles. Further, they should expose non-Shariah compliance applications in the sector and ask policymakers to take necessary measures regarding the Shariah controlling and oversight mechanisms.

Interest-free professional associations, academicians in Islamic Economics and Finance, and educational institutions should work together to create awareness about Islamic finance and develop skilled human resources on Islamic finance. In addition, they should support policymakers by providing necessary inputs that enforce to issue directives to solve challenges facing the sector.

References

- AAOIFI. "AAOIFI Makes All Its Standards Accessible on Its Website on a Complimentary Basis". Accessed December 20 2022. <https://aaoifi.com/announcement/aaoifi-makes-all-its-standards>
- AAOIFI, Auditing Organization for Islamic Financial Institutions, AAOIFI Footprint Report 2022. Manama: AAOIFI Secretariat,2022. <https://aaoifi.com/aaoifi-footprint-2022/?lang=en>
- Abdullah Saif Al Nasser et al. "Introduction to History of Islamic Banking in Malaysia". *Humanomics* 29/2 (2013), 80–87. <https://doi.org/10.1108/08288661311319157>
- Ahmed, Habib. "Shari'ah Governance Regimes for Islamic Finance: Types and Appraisal - I Regimi Di Governance Conformi Alla Shari'ah Nella Finanza Islamica: Tipologia e Valutazione". *Economia Internazionale/International Economics*, 66.4 (2011), 393–412
- AI-Abdullatif, Sultan Abdullah. *The Application of the AAOIFI Accounting Standards by the Islamic Banking Sector in Saudi Arabia*. Durham: Durham University, Ph.D. Dissertation, 2007. http://etheses.dur.ac.uk/2594/1/2594_605.pdf
- Akram Laldin, Mohamad. "Islamic Financial System: The Malaysian Experience and the Way Forward". *Humanomics* 24/3 (2008), 217–38. <https://doi.org/10.1108/08288660810899377>
- Alam, Md. Kausar et al. "Why Does Shariah Governance Framework Important for Islamic Banks?". *Asian Journal of Economics and Banking* 5/2 (2021), 158–72. <https://doi.org/10.1108/AJEB-02-2021-0018>
- Alkhamees, Ahmad. "The Impact of Shari'ah Governance Practices on Shari'ah Compliance in Contemporary Islamic Finance". *Journal of Banking Regulation* 14/2 (2013), 134–63. <https://doi.org/10.1057/jbr.2012.12>
- BBP, Banking Business Proclamation (Proclamation No. 592). *Federal Negarit Gazeta* No 57. (August 25 2008). Accessed March 31 2023. <https://nbebank.com/wp-content/uploads/2019/04/BANKING-BUSINESS-592.pdf>
- BBP, Banking Business Proclamation (Proclamation No. 1159/art.59/1), *Federal Negarit Gazeta* No 88. (September 9 2019). Accessed March 31 2023. <https://nbebank.com/wp-content/uploads/pdf/directives/bankingbusiness/banking-business-proclamation-1159-2019.pdf>
- Bhatti, Maria. "Managing Shariah Non-Compliance Risk via Islamic Dispute Resolutio". *Journal of Risk and Financial Management* 13/2 (2019),1-9. <https://doi.org/10.3390/jrfm13010002>
- Busetto, Loraine et al. "How to Use and Assess Qualitative Research Methods" *Neurological Research and Practice* 2/1 (2020). <https://doi.org/10.1186/s42466-020-00059-z>
- CFC, Casablanca Finance City, *CFC Africa Insights Islamic Finance in Africa: The Upcoming Frontier*. Toronto: Thomson Reuters, 2019.
- COMCEC, Standing Committee for Economic and Commercial Cooperation. *Improving Shariah Governance Framework in Islamic Finance*. Ankara: COMCEC Coordination Office, 2020 2020 <<http://ebook.comcec.org>

- Crabtree, Benjamin F.- William L. Miller, eds. *Doing Qualitative research*, 2nd ed. Thousand Oaks, Calif: Sage Publications, 1999.
- Dino, Nassir. "Islamic Banking in Ethiopia: A Paradigm Shift" *ISFIR Review* (October 5 2022), 35-43. <https://zamzambank.com/wp-content/uploads/2022/11/05-IS-FIRE-October-2022-Web-Version.pdf>
- EIASC, Ethiopian Islamic Affairs Supreme Council, "የኢትዮጵያ ስልጠና ጉዳዮች ጠቅላይ ምክር ቤት የዕለተኛ ጉባዔ በቀጣይ የሚተዳደርበትን ደንብ በሙሉ ድምፅ አፀደቀ [The Ulema Assembly of the Ethiopian Supreme Council for Islamic Affairs has unanimously approved its governing laws]", Facebook. 11 May 2023,10:05. Accessed 11 May 2023. <https://www.facebook.com/eiasc/>
- Fatmawati et al. "Shariah Governance in Islamic Banks: Practices, Practitioners and Praxis", *Global Finance Journal*, 51 (2020), 100555.<https://doi.org/10.1016/j.gfj.2020.100555>
- FDRE-PCC, Federal Democratic Republic of Ethiopia Population Census Commission. *Summary and Statistical Report of the 2007 Population and Housing Census Results*. Addis Ababa: United Nations Population Fund, 2008. [https://www.ethiopianreview.com/pdf/001/Cen2007_firstdraft\(1\).pdf](https://www.ethiopianreview.com/pdf/001/Cen2007_firstdraft(1).pdf)
- Feyissa, Dereje. "The Transnational Politics of the Ethiopian Muslim Diaspora", *Ethnic and Racial Studies*, 35.11 (2012), 1893–1913. <https://doi.org/10.1080/01419870.2011.604130>
- Galletta, Anne. *Mastering the Semi-Structured Interview and Beyond: From Research Design to Analysis and Publication*. Epub:NYU Press, 2013. <https://doi.org/10.18574/nyu/9780814732939.001.0001>
- Gelbard, Enrique et al. "Islamic Finance in Sub-Saharan Africa: Status and Prospects". *International Monetary Fund*, IMF Working Paper, WP/14/149 (2014).
- Getachew, Addis. "Ethiopian PM Attends Iftar with Muslim Community: Abiy Ahmed Promises Grand Mosque, Interest-Free Banking for Muslims", *Anadolu Agency*, (December 15 2022) <https://www.aa.com.tr/en/africa/ethiopian-pm-attends-iftar-with-muslim-community/1484949>
- Grassa, Rihab. "Shariah Supervisory System in Islamic Financial Institutions: New Issues and Challenges: A Comparative Analysis between Southeast Asia Models and GCC Models", *Humanomics*, 29/4 (2013), 333–48.<https://doi.org/10.1108/H-01-2013-0001>
- Hailu, Suadiq Mehammed - İbrahim Bushera. "Interest Free Banking in Ethiopia: Prospects and Challenges", *International Journal of Islamic Economics and Finance Studies*, 2 (July 2020), 119-137. <https://doi.org/10.25272/ijisef.678972>
- Hailu, Suadiq Mehammed - Nissar Ahmad Yatoo. "Islamic Finance In Ethiopia: Current Status, Prospects, and Challenges", *International Journal of Islamic Banking and Finance Research* 6/1, 1-18(2021), 1–18. <https://doi.org/10.46281/ijibfr.v6i1.1317>
- Hamza, Hichem. "Sharia Governance in Islamic Banks: Effectiveness and Supervision Model" *International Journal of Islamic and Middle Eastern Finance and Management* 6/3 (2013), 226–37. <https://doi.org/10.1108/IMEFM-02-2013-0021>

- Harvey, Charles. "Banking Reform in Ethiopia". *Institute of Development Studies*, 37 (1996)
- Hasan, Aznan - Ruslan Sabirzyanov. "Optimal Shari'ah Governance Model in Islamic Finance Regulation", *International Journal of Education and Research*, 3/4 (2015), 243–58.
- Hasan, Zulkifli Bin. "Regulatory Framework of Shari'ah Governance System in Malaysia, GCC Countries and the UK"., *Kyoto Bulletin of Islamic Area Studies* 3/2 (2009), 82–115
- Hassan, Kabir et al. (ed.). *Islamic Finance in Africa: The Prospects for Sustainable Development*, Studies in Islamic Finance, Accounting, and Governance. Cheltenham, UK ; Northampton, MA, USA: Edward Elgar Publishing, 2022.
- Hussain, Mohammad Azam. "The Duties and Responsibilities of Shariah Committee in Ensuring Shariah Compliance of Islamic Financial Business in Malaysia", *Selected Legal Issues in Indonesia and Malaysia*. ed. Mohammad Azam Hussain et al.1-18. Indonesia: UNISSULA PRESS, 2020..
- Husseini, Saleh Ali et al. "Islamic Banking Revolution in Malaysia: A Review". *Humanities & Social Sciences Reviews* 7/4 (2019), 267–75. <https://doi.org/10.18510/hssr.2019.7434>
- IFSB, The Islamic Financial Services Board. "About IFSB -Background". Accessed December 20 2022. <https://www.ifsb.org/background.php>
- Iqbal, Munawar et al. *Challenges Facing Islamic Banking*, Occasional Paper, no. 1, 1st ed. Jeddah, Kingdom of Saudi Arabia: Islamic Development Bank, Islamic Research and Training Institute, 1998.
- IFSB, Islamic Financial Services Board. *Guiding Principles on Sharî`ah Governance Systems for Institutions Offering Islamic Financial Services*. Malaysia: Islamic Financial Services Board, Acceptance December 2009, IFSB-10.
- Khan, M. Fahim. "Setting Standards For Shariah Application in the Islamic Financial Industry". *Thunderbird International Business Review* 49/3 (2007), 285–307. <https://doi.org/10.1002/tie.20145>
- NBE, National Bank of Ethiopia. "Financial Institutions". Accessed December 20 2022. <https://nbe.gov.et/banks/>
- Oumer, Kamil Abdu. *A Critical Appraisal of the Regulatory Regime of Islamic Banking in Ethiopia*. Doha: Hamad Bin Khalifa University, Master's Thesis, 2021.
- Sanders, T. "The Aims and Principles of Standardization". International Organization for Standardization (ISO), 1972.
- SBB, Licensing and Supervision of Banking Business: Directives to Authorize the Business of Interest-Free Banking. Ethiopia: National Bank of Ethiopia (2011). Accessed March 31 2023. <https://nbebank.com/wp-content/uploads/pdf/directives/bankingbusiness/sbb-51-11.pdf>
- SBB, Licensing and Supervision of Banking Business: Directives to Authorize the Business of Interest Free Banking. Ethiopia: National Bank of Ethiopia (2019). Accessed March 31 2023. <https://nbebank.com/wpcontent/uploads/pdf/direc>

- tives/bankingbusiness/Interst%20free%20banks.pdf
- Shafii, Zurina. "Integrated Internal-External Shariah Audit Model: A Proposal towards the Enhancement of Shariah Assurance Practices in Islamic Financial Institutions". *The Islamic Research and Teaching Institute* 1436-7, 2015.
- Shanmugam, Bala - Zaha Rina Zahari. *A Primer on Islamic Finance*. Charlottesville, Va: Research Foundation of CFA Institute, 2009.
- Smolo, Edib - Elmin Habibovic. "Barriers to Growth of Islamic Finance: Issue of Standardisation". *Islamic Banking and Finance: Principles, Instruments and Operations*, ed. Adnan Trakic and Hanifah Haydar Ali Tajuddin. 715–37. Malaysia: JCL Publication, 2012).
- TKBB,Türkiye Katılım Bankaları Birliği. "Hakkimizda". Accessed January 1, 2023. <https://tkbb.org.tr/sayfa/detay/hakkimizda/tarihce-856934>
- UN, United Nations. *World Population Prospects 2022: Summary of Results*. New York: United Nations Publication, 2022. https://www.un.org/development/desa/pd/sites/www.un.org.development.desa.pd/files/wpp2022_summary_of_results.pdf
- Yaacob, Hakimah - Apnizan Abdullah, "Standards Issuance for Islamic Finance in International Trade: Current Issues and Challenges Ahead", *Procedia - Social and Behavioral Sciences*, 65 (2012), 492–97.<https://doi.org/10.1016/j.sbspro.2012.11.154>

