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Nor Fadilah Bahari¹, Zurina Shafii², Mustafa Mohd Hanefah³

Optimizing Shariah Governance Practices in Ar-Rahnu Cooperatives: Insight into Structure, Guideline Adherence, and Challenges

ABSTRACT

This paper aims to examine Shariah governance practices in Ar-Rahnu cooperatives. It would also analyse the challenges encountered by Ar-Rahnu cooperatives in implementing effective Shariah governance, including regulatory constraints, and operational complexities. The study employed multiple case studies and selected four different categories of Ar-Rahnu cooperatives as a sample. Data collection strategies were based on interviews with Ar-Rahnu cooperatives' key governance organs and documents. The data was analyzed using thematic analysis and content analysis. The study's results indicate that the Ar-Rahnu cooperatives have progressively strengthened their Shariah governance. However, a few areas, like Shariah risk and audit, demand greater focus from Ar-Rahnu cooperative management. The recommended strategies that may bolster Shariah governance and compliance procedures are to entrench Shariah culture, enhance awareness, improve Shariah competency within the management of cooperatives and regulators' duties to reinforce the current Shariah legal elements for cooperatives. Also, together with positive support from regulators who provide a comprehensive Islamic legal and regulatory system. This study provides valuable insights for practitioners, policymakers, and researchers working in the Islamic pawn broking industry and cooperative studies. Furthermore, it would propose potential future directions and innovative solutions to improve Shariah governance and assurance in Ar-Rahnu cooperatives.

Keywords: Shariah Governance, Ar-Rahnu, Cooperatives, Challenges

Ar-Rahnu Kooperatiflerinde Şer'i Yönetişim Uygulamalarının Optimizasyonu: Yapı, Kılavuzlara Uyum ve Zorluklara İlişkin Bir Bakış

ÖZ

Bu makale, Ar-Rahnu kooperatiflerindeki Şeriat yönetişim uygulamalarını incelemeyi amaçlamaktadır. Ayrıca, etkili Şeriat yönetişimini uygulamada Ar-Rahnu kooperatiflerinin karşılaştığı düzenleyici kısıtlamalar ve operasyonel karmaşıklıklar gibi zorlukları analiz etmektedir. Çalışma, birden fazla vaka çalışması yöntemi kullanmış ve örneklem olarak dört farklı kategoriye ait Ar-Rahnu kooperatiflerini seçmiştir. Veri toplama stratejileri, Ar-Rahnu kooperatiflerinin temel yönetişim organlarıyla yapılan görüşmeler ve belgeler üzerine dayandırılmıştır. Veriler tematik analiz ve içerik analizi yöntemleriyle incelenmiştir. Çalışmanın sonuçları, Ar-Rahnu kooperatiflerinin Şeriat yönetişimlerini giderek güçlendirdiğini göstermektedir. Bununla birlikte, Şeriat risk yönetimi ve denetim gibi birkaç alan, Ar-Rahnu kooperatifi yönetiminin daha fazla odaklanmasını gerektirmektedir. Şeriat yönetişimi ve uyum prosedürlerini güçlendirebilecek önerilen stratejiler

¹ Phd., Universiti Islam Selangor (UIS), Department of Economics, Accountancy and Management, norfadilah@uis.edu.my, ORCID: [0000-0001-5792-195X](https://orcid.org/0000-0001-5792-195X) Asst. Prof., KTO Karatay University, Department of Islamic Economics and Finance, karjief@karatay.edu.tr, ORCID: [0000-0000-0000-0000](https://orcid.org/0000-0000-0000-0000))

² Professor.Dr., Universiti Sains Islam Malaysia (USIM), Faculty of Economics and Muamalat, zurina.shafii@usim.edu.my, ORCID: [0000-0002-1476-1199](https://orcid.org/0000-0002-1476-1199)

³ Professor Dato', Dr., Universiti Sains Islam Malaysia (USIM), Faculty of Economics and Muamalat, mustafa@usim.edu.my, ORCID: [0000-0002-0880-6856](https://orcid.org/0000-0002-0880-6856)

arasında Şeriat kültürünün yerleşik hale getirilmesi, farkındalığın artırılması, kooperatif yönetimi içinde Şeriat yeterliliğinin geliştirilmesi ve düzenleyicilerin kooperatifler için mevcut Şeriat hukuki unsurlarını güçlendirme görevleri yer almaktadır. Ayrıca, düzenleyicilerden gelen kapsamlı bir İslami hukuki ve düzenleyici sistem desteğiyle pozitif katkı sağlanması önerilmektedir. Bu çalışma, İslami rehin finans sektörü ve kooperatif çalışmaları alanında çalışan uygulayıcılar, politika yapıcılar ve araştırmacılar için değerli bilgiler sunmaktadır. Ayrıca, Ar-Rahnu kooperatiflerinde Şeriat yönetişimini ve güvencesini iyileştirmeye yönelik potansiyel gelecek yönelimleri ve yenilikçi çözümleri önermektedir.

Anahtar Kelimeler: Şer'i Yönetişim, Ar-Rahnu, Kooperatifler, Zorluklar

1. INTRODUCTION

Since the flourishing growth of Islamic finance sectors in Malaysia, Shariah governance has been the utmost priority and consideration in creating the Islamic finance ecosystem in Malaysia. The Malaysian government has been at the forefront of embarking on the industry's growth with structured regulatory systems, frameworks, legislation, guidelines, and a holistic Islamic finance ecosystem. These efforts aim to ensure that the Islamic finance sector complies with Shariah laws in all aspects of legal, prudential, operational, and governance matters.

In recent years, there has been extensive research on Shariah compliance and Shariah governance, especially in the Islamic banking sectors (IBs). Despite this, there are still few studies focusing on the Shariah governance aspects of Ar-Rahnu cooperatives. Ar-Rahnu must conduct its business and activities in accordance with Shariah principles, prioritizing the economic and social dimensions. As an Islamic financial sector, Ar-Rahnu business's fundamental principle is to achieve *maqasid al-shariah*.

The five common dimensions of *maqasid al-shariah* based on Al Ghazali 1937, as cited in Chapra (2008), are: i) safeguarding their faith (*din*), ii) their self (*nafs*), iii) their intellectual ('*aql*), iv) their posterity (*nasl*), and v) their wealth (*mal*). Shariah governance is one of the special elements that distinguish the Islamic financial sectors from their conventional counterparts. Ar-Rahnu cooperatives not only focus on the material elements, but they are also obligated to adhere to Shariah rules.

The absence of a solid Shariah governance structure and insufficient laws might lead to Shariah risk, thereby tarnishing Ar-Rahnu's reputation as one of the country's most respected Islamic pawnbrokers. The roles of key Shariah governance organs in the Ar-Rahnu cooperative are important to assure that all aspects of the cooperative's business are in line with Shariah rules, which indirectly strengthens Shariah governance in Ar-Rahnu cooperatives.

Ar-Rahnu, an Islamic pawn broking institution in Malaysia, contributes significantly to the country's economy. Various institutions, such as banking institutions, government link companies (GLCs), credit cooperatives, state link companies, and other private companies, have served Ar-Rahnu operators up to this day. The number of Ar-Rahnu operators keeps increasing over the years, and cooperatives are among the pioneers in the business of Ar-Rahnu.

According to the Malaysia Co-operative Commission Societies (MCSC), in 2022, out of 15,315 registered cooperatives, 595 conduct credit activities and *takaful*, or insurance services, which have recorded RM 140.76 billion of assets with 2.4 million members. Furthermore, Ar-Rahnu's operations generated revenue of RM37.6 million, involving over 100 cooperatives and disbursing a total funding of RM369.9 million (SKM, 2022).

Along the growth, it undeniable that the business of Ar-Rahnu was exposed to Shariah non-compliance issues. Shariah non-compliance may happen if the Ar-Rahnu business is improperly conducted from beginning to end and there are elements such as *riba*, *gharar*, and *maysir*. The business process and operation of Ar-Rahnu and must be clear from unlawful items or any elements contradicted with the rules of Shariah.

Previous studies Md. Yusuff (2015), Musa et al. (2018), Rasmin and Markom (2014), and Shah et al. (2018), have claimed that the absence of specific regulations and a lack of control and supervision, coupled with minimal Shariah governance practices, contribute to the emergence of Shariah issues in the business of Ar-Rahnu.

Meanwhile, Nik Azman and Kassim (2017), remarked on the issues of pricing practice and the criticisms of the application of Shariah contracts in Ar-Rahnu discussed by Fairouz and Khir (2012) and Mohamad et al. (2008). Significant changes occurred when the SC's of BNM announced their intention to restructure the former Ar-Rahnu scheme to a new Ar-Rahnu scheme due to the non-Shariah compliance factor. The implications of these issues prompted BNM to enforce the restructuring of the former Ar-Rahnu scheme into the new Ar-Rahnu scheme for all Islamic Financial Institutions (IFIs) under its purview, which became effective in February 2020.

In conjunction with the enforcement, the regulatory body of cooperatives, the MCSC, announced the enforcement of the new alternative of the Ar-Rahnu scheme on May 1, 2021, for all cooperatives. In June 2021, the MCSC streamlined the Ar-Rahnu scheme into a new Shariah scheme. Therefore, one of the ways to minimise Shariah issues in Ar-Rahnu cooperatives is to strengthen the implementation of Shariah within the Ar-Rahnu cooperatives. The application of the new scheme is still in its early stages, and proper conduct is required to prevent any potential Shariah issues. For those reasons, the study aims to examine the current Shariah governance practices in Ar-Rahnu cooperatives, including their perspectives on the available guidelines and acts, and further identify the challenges faced by the cooperatives.

2. LITERATURE REVIEW

In Malaysia's financial system, the demand for Ar-Rahnu was influenced by the Muslim community, which needs Shariah-compliant pawn broking services. Studies by Amin et al. (2007) and Abdul Hamid et al. (2014) proved that the Shariah element is one of the factors that influenced the community's request for Ar-Rahnu. Besides, Ar-Rahnu provides an attractive alternative to the local banking system and best credit alternative for customers to overcome their financial difficulties. Flexible services, minimal credit evaluation, and fast credit approval were 32 factors that made Ar-Rahnu the best choice for its customers (Skully, 1992).

For Islamic credit cooperatives that served Rahnu micro-financing, the jurisdiction of cooperatives in Malaysia is under the supervision of *Suruhanjaya Koperasi Malaysia* (SKM). In the early stages of its establishment, Ar-Rahnu operators were governed by the Pawn Broking Act of 1972. However, the existence of certain sections that allow the permissible practise of charging interest on the loan was inconsistent with Islamic rules (Abu Bakar et al., 2018; Rasmin & Markom, 2014). The practice of interest, or *riba*, is not practicable for Ar-Rahnu and is absolutely *haram*, thus must be avoided.

In 2013, the SKM introduced GP 25 - *Garis Panduan Aktiviti Pajak Gadai Islam* (Ar-Rahnu). The introduction of this guideline acts as guidance to all cooperatives to conduct the business of Ar-Rahnu in an orderly and prudent manner. Nevertheless, the guideline was cancelled by SKM in 2020 for the restructuring of a new Ar-Rahnu scheme. For Islamic banks that serve Ar-Rahnu scheme, they are guided by *Rahn* Policy document by BNM.

To date, the development of Shariah governance has increased demand not only for Islamic banking sectors but also for other non-banking sectors that are currently active in serving Islamic financing products. Following the growing effort to embark on the practice of Shariah governance in Islamic banking sectors in the country, the regulators of the cooperatives have taken similar actions and continue to make an effort to strengthen the Shariah governance practice within Islamic cooperatives. The Shariah governance guideline was established in 2015

to strengthen Shariah governance and assurance practices in Ar-Rahnu cooperatives. However, issues related to Shariah compliance continue to arise. Therefore, this study examines the Shariah governance and assurance practices within Ar-Rahnu cooperatives. The findings provide significant contributions to the cooperatives, policymakers, and society as a whole, ensuring that the business operations of Ar-Rahnu cooperatives align with Shariah principles.

2.1. SECOND-LEVEL HEADING IN THE TEXT

GP28 Shariah Governance Guideline for cooperatives is applicable to Islamic cooperatives that conduct banking activities, offering credit, financing, and Ar-Rahnu. The introduction of the GP 28 guideline aims to enhance the effective responsibility and accountability of the members in the organization, including the board of directors, management, and Shariah Committee, to lead to business according to Islamic rules.

Besides, it aims to strengthen the identity and development of each component of governance in order to form more competitive and competent cooperatives that operate with integrity (Hassan et al., 2018). The GP 28 contains the framework and roles of each governance organ in cooperatives to achieve the completion of five aspects of Maqasid Shariah, particularly in the aspect of governance. The enforcement of this guideline able to empower the regulatory functions of SKM against cooperatives in conducting business and Shariah compliant activities. This effort was in line with the aims of Malaysia's government to strengthen Shariah compliant practice within the Islamic financial sector.

In addition, GP 28 stipulates that all related cooperatives must at least appoint their own Shariah officers, having a Shariah secretariat that carry out an audit function that includes aspects of Shariah compliance. According to GP 28, implementing of Shariah compliant practice in Islamic cooperative are the responsibilities and duties of each component, including:

1. Cooperative Boards,
2. Shariah Committee,
3. Cooperative Management,
4. Internal Audit Committee.

This guideline automatically effective to all cooperatives including Ar-Rahnu cooperatives. Number of previous research emphasizes the need for a Shariah governance framework for Islamic cooperatives. Studies by Issyam et al. (2016) suggested the establishment of a Shariah Committee as a mechanism to ensure Shariah compliance in the business and operation of the Islamic cooperative and Shariah Advisory Council of Bank Negara as a reference/consultation body. This is in line with Section 26(1) of the Malaysia Cooperative Societies Commission Act 2007, which stipulated that SKM consult the SAC of BNM on any matters related to Shariah for advice.

3. METHODOLOGY

The multiple case study approaches employed were to obtain the perspective of industry practitioners and observe the real practices within the selected cooperatives. The sampling methodology was based on purposive sampling. The study's scope was limited to four categories of Ar-Rahnu cooperatives. The cooperatives involved were:

- i. Cooperative bank (ABC)
- ii. Cooperative by state link company (ACM)
- iii. Cooperative under Islamic bank's subsidiaries (ACK)
- iv. Cooperative by foundation company (ACY)

All selected cooperatives are currently active in serving and conducting Ar-Rahnu businesses. The study excluded Ar-Rahnu providers from Islamic commercial banks and private companies. The exclusion of these two categories of institutions was due to certain limitations, including time constraints and the readiness of the institutions to be involved in the study. The respondents involved in the study were the key governance organs in the cooperatives, which include board members, the Shariah Committee, senior management, and the branch manager. All the selected samples and respondents were selected based on their willingness to participate in the study.

The interview session began by inquiring about the cooperative's present implementation of Shariah governance, specifically their compliance with Shariah governance guideline GP 28, their perspective on the existing legal frameworks in Ar Rahnu cooperatives, and the obstacles encountered by the cooperatives in upholding Shariah governance. The study employed two methods of conducting interviews: face-to-face and online. The online interview was carried out using the Zoom platform. The interview ran between one and two hours. Each participant received a semi-structured question that aligned with the specified objectives. Each level of key governance organs received a different set of questions.

After the interviews were conducted, the researcher transcribed the data, and the transcripts were submitted to the respondents via two approaches: email or face-to-face checking for validation purposes. If the information recorded was different from what was said during the interview sessions, respondents are free to comment on or correct the data. Furthermore, if the information is incomplete and uncertain, the researcher will make a telephone call to the respondents to obtain or reconfirm it. The respondents were previously apprised of these matters. The details of interviews conducted with key organs of four Ar-Rahnu cooperatives are illustrated in Table 1.

Table 1: Details of the Interviewees

No.	Interviewees Profile	
1.	Interviewee1 (I1ACM)	General Manager Cooperative ACM (GM_ACM)
2.	Interviewee 2 (I2ACM)	Shariah Committee Members/ BOD ACM
3.	Interviewee 3 (I5ACM)	Internal Auditor ACM
4.	Interviewee 4 (I1ABC)	Branch Manager Cooperative ABC, Bangi Branch
5.	Interviewee 5 (I1ACY)	Branch Manager ACY
6.	Interviewee 6 (I2ACY)	Head of Shariah Department/ Shariah Secretariat ACY
7.	Interviewee 7 (I1ACK)	Head of Division/ BOD Cooperative ACK
8.	Interviewee 8 (I2ACK)	General Manager Cooperative ACK

Source: Authors

Also, to verify the absence of Shariah governance organs and structures in the Ar-Rahnu cooperatives, data was also collected from related documents such as their annual report and official website. The individuals who were interviewed validated the accuracy of this material.

Data obtained from both sources was further refined and analysed based on content analysis and thematic analysis. The study employed ATLAS.ti-22 to perform qualitative data analysis.

3. DISCUSSION AND FINDING

According to the findings, the study deduces three themes from the data. The first theme is the organizational Shariah structure in each cooperative; the second theme is the adherence and relevancy of the available guidelines and acts in Ar-Rahnu cooperatives; and the third theme is related to constraints faced by the Ar-Rahnu cooperatives in conducting Ar-Rahnu businesses in accordance with Shariah.

ROI: The current practices of Shariah governance within the Ar-Rahnu cooperatives

The study examined the existing organisational framework of Ar-Rahnu cooperatives to achieve its first objectives. One of the elements of Shariah governance is the presence of Shariah governing bodies within cooperatives. The study obtains information from their financial reports, official websites, and other pertinent documents. The results are as follows:

Table 2: Shariah Organizational Structure of Ar-Rahnu Cooperatives

Internal Shariah Governance Organs	ABC	ACY	ACM	ACK
Internal Shariah Committee	√	√	√	√
Number of SCs	5	5	3	3
Shariah Audit	√	n/a	n/a	n/a
Shariah Review	√	n/a	n/a	n/a
Shariah Risk	√	n/a	n/a	n/a
Shariah Secretariat	√	√	√	√

Source: Authors.

Based on the information in Table 1, each of the four Ar-Rahnu cooperatives has its own internal Shariah Committee (SC), which is responsible for overseeing and monitoring all Shariah-related activities within the firms. The main function of the Shariah Committee (SC) in the cooperative is to issue guidance and advice regarding Shariah matters internally. With regards to the SC compositions, each institution abides by the guidelines outlined in GP 28, where the composition of the Shariah committee should consist of at least three members. This minimum standard is determined by the complexity and size of the cooperatives. Comparatively, the composition of SCs in GP 28 is less than the requirements imposed in SGPD 2019 by BNM.

For IFIs, the composition of SC members, as stated in Paragraph 13.2 of SGPD 2019, requires at least five SC members. For cooperative banks, ABC allocates five SC members as per the guidelines set by BNM, which exceeds what is required in GP 28. For the other cooperatives, ACY, ACM, and ACK, the SC compositions typically consist of three individuals. Nevertheless, ACY went beyond the GP 28 standard when they assigned five SC members to their company. Cooperative ACY relies on the SC in their company. This has been acknowledged by their Head of Shariah or Shariah Secretariat officer at ACY:

“Based on the standard in GPS 28, the required number of members is 3, but in our foundation, we have a total of 5 Shariah Committee members to make sure that every activity runs smoothly.” (I2ACY)

Furthermore, the branch manager of ACY also added that Shariah governance was emphasised by the management. She commented:

“Yes, Shariah governance was emphasised.” (I1ACY)

Meanwhile, both ACM and ACK cooperatives have three SCs, which are in line with the requirements of GP 28. The ACM relies on the SCs in its corporation, whereas ACK has its own SCs and Shariah Officer or Secretariat in its cooperative. It was confirmed by the Head of Ar-Rahnu Division and Deputy Chairman of ACK as follows:

“We have appointed a Shariah officer, and we already have a Shariah Advisor.” (IACK)

In addition, the study also identifies the implementation of a Shariah control function in each cooperative. Only ABC completes the components of Shariah advisors: Shariah audit, Shariah risk, Shariah review, and Shariah secretariat. This was in line with the SGPD 2019 requirement. While for other cooperatives that are not under the bank cooperative category, the functions of Shariah control functions such as Shariah audit, Shariah review, and Shariah risk are not mandatory, and the enforcement is not effective for them. The cooperatives are not required to have these three Shariah-compliant control functions. However, GP 28 stipulates that the cooperatives must designate at least one Shariah officer to act as the Shariah committee's secretary.

In summary, all the Ar-Rahnu cooperatives possess a Shariah Secretariat and only the cooperative bank possesses all four components of the Shariah control function; Shariah audit, Shariah risk, Shariah review, and Shariah secretariat. This was in line with the SGPD 2019 requirement. For other cooperatives that do not fall under the bank cooperative category, the functions of Shariah audit, Shariah review, and Shariah risk are not mandatory, and their enforcement is not effective. However, GP 28 stipulates that the cooperative must designate at least one Shariah officer to act as the Shariah committee's secretary.

Although the requirement stipulated in GP 28 does not require cooperatives to have complete Shariah advisors, a few Ar-Rahnu cooperatives have taken the initiative to conduct Shariah reviews and Shariah audits. A Shariah review was conducted by the internal Shariah unit. Meanwhile, some cooperatives seek Shariah certification on the products by ANGKASA and ISRA upon MCSC's approval. Similar findings were reported by Mahmud Sabri et al. (2023).

RO2: The perspectives of cooperatives on available acts and guidelines.

The second objective of the study was to examine the perspectives of the key governance organs on the available guidelines regarding Ar-Rahnu business and Shariah aspects. Table 2 illustrates the findings from the interviews.

Table 2: Perspectives on the available guideline and Act for Ar-Rahnu cooperatives

Interviewees	Quotations.
Ar-Rahnu Guideline & Act	

11ACY	“For me, so far, it's been good. The current regulations and legislation in Ar-Rahnu provided by MCSC are good and do not interfere with the operation.”
11ABC	“For me, it's good. The current rules and laws make things easier.”
11ACM	“It’s good so far. It's just that if there are a lot of regulations and laws in place, they restrict the business that is conducted to some extent.” (I4ACM)
12ACK	“Ar Rahnu’s regulation is still lame. The qualification allowed is only RM 50,000, but our cooperatives offered up to RM 500,000. So, the guideline and the standard are no longer suitable.
11ACK	“Current regulations are highly retrograde and prevent cooperatives from implementing Shariah governance. I also would like to comment regarding GP25 <i>Garis Panduan Pajak Gadai Islam</i> ; it no longer suits the current market situation because when <i>tawarruq</i> was introduced as the current Shariah contract in Ar-Rahnu, there was no guideline to be referred to. GP 25 is lame and does not suit the current market at the moment.
I2ACM	“We do not yet have a specific act for Ar-Rahnu. Previously, we used the Pawn Broking Act of 1972. If it is an Islamic banking institution, they refer to IFSA 2013, but for Ar Rahnu cooperative, if there is a dispute, it will be taken to the tribunal, and I am not sure which act to refer to. So, this is something that needs attention.”
Shariah Aspects	
12ACY	“For the first question, we have complied with the Shariah governance elements prior to the establishment of GP 28.
11 ABC	“Alhamdulillah, we have obeyed. We have made sure from the beginning that we comply with the guidelines of GP 28.
11 ACK	“The implementation of Shariah has already been done.”

Source: Authors

The findings led to the expression of diverse perspectives on the current legal system in Ar-Rahnu. Some of them are satisfied with the existing laws, as they are perceived as fair and do not restrict the ability of Ar-Rahnu cooperatives to conduct business. It makes it easier for cooperatives to move and manage their businesses. Most of them demonstrate that they comply with MCSC's guidelines: GP 25 *Garis Panduan Pajak Gadai Islam* and Shariah Governance Guideline GP 28 in their operations. Nevertheless, two interviewees asserted that the existing laws and regulations in the Ar-Rahnu and cooperative sectors were antiquated and unable to support the present needs and competitive environment. One of the participants expressed concerns about the appropriate act to use in the event of a dispute in Ar-Rahnu's business.

RO3: Challenges in strengthening the Shariah governance practices

The cooperatives faced a few challenges in maintaining the Ar-Rahnu business. The main issue was the absence of guidance on the new Ar-Rahnu scheme. The available guidelines are not applicable to the present situation. The SKM has cancelled GP 25 *Garis Panduan Pajak Gadai Islam* and has not yet proposed any new guidelines. The need for a new guideline is vital, and responses received from the interviewees claimed that they lacked expertise and guidance on how to conduct the new Ar-Rahnu scheme, which was one of the obstacles to immediately streamlining their Ar-Rahnu product.

The interviewees remarked:

“GP25 should be amended to be consistent with the concept of tawarruq.” (I2ACK)

“GP25 Garis Panduan Pajak Gadai Islam; it no longer suits the current market situation because when tawarruq was introduced as the current Shariah contract in Ar-Rahnu, there was no guideline to be referred to.” (I1ACY)

“There are still no guidelines on tawarruq from the MCSC. However, we already conduct internal research and bring it to our Shariah committee and fatwa council for approval.” (I1ACM)

Most of them suggested that the MCSC, as the main regulator that supervises the cooperatives, should play a proactive role in providing guidelines that match the current situation and environment. The execution of the *tawarruq* contract in the Ar-Rahnu scheme must be conducted in proper arrangement, and the elements in the contract should be conducted properly to avoid the risk of non-Shariah compliance.

The second challenge was financial scarcity. To simultaneously engage in Ar-Rahnu business and adhere to Shariah, cooperatives are required to keep a consistent stream of income. The issues also mentioned by Othman et al., (2013) and Maslinawati et al., (2013). The cooperatives having a problem in getting and having sufficient capital to fund their activities and to sustain in the market. The majority of cooperatives rely on their internal capital resources; share capital, fees, and accumulated profit.

Shariah governance aspects can be efficiently implemented if cooperatives have complete Shariah advisors, including Shariah review, Shariah risk, Shariah audit, and Shariah secretariat, especially for the cooperatives under the categories of "premier" and "100 best cooperatives." But some responses from the interviewees claimed financial constraints were the main obstacles for cooperatives. The description is as follows:

“In cooperatives, the issue is that when they want to establish a Shariah control function in the cooperatives, the cost is high.” (I1ACK)

“We must tighten our operational process to ensure its accordance with Shariah and further refine our practices. However, in achieving this purity, it is a fact that the cost will increase.” (I2ACM)

Last but not least, there is the Shariah competency challenge. Ar-Rahnu business necessitates ability and understanding in both Ar-Rahnu and Shariah matters to all cooperative members. Few of the interviewees admitted that Shariah knowledge is still minimal among cooperative managers and Shariah training was needed. The interviewees revealed:

“I just have basic knowledge of Shariah.” (I1ACK)

“My position is currently as an accountant and member of the team for internal audit. I don't have experience with Shariah auditing.” (I5ACM)

“We do not yet have a Shariah audit certificate. However, the bank provides training, and they give a brief on the Shariah audit function for front-line officers.” (I2ABC)

In a cooperative setting, the appointment was also influenced by political considerations, which were based on voting rather than abilities and knowledge. The interviewees mentioned:

“As far as I’m concerned, some of the management members do not have high qualifications. A branch manager only requires experience and certain training to become qualified to become a branch manager. However, I am not sure how soon it will be. I heard that they would like to strengthen their academic qualifications.” (I2ACY)

“However, there’s an issue where the designation of the board corporation is based on votes. So, there’s a political game, and there are people who want to be designated but are not skilled and have no expertise.” (I1ACK)

Furthermore, with regard to the qualifications and expertise of Shariah Committee members, the majority of respondents disclosed that the appointment process for their SCs adhered to the stringent requirements set forth by the SKM. Nevertheless, the support of a Shariah control function is required to assist the roles of SCs thus to ensure effective implementation of Shariah governance and assurance within the cooperatives. This was claimed by interviewee;

“But SC in the cooperative itself is still not ready to run a business based on Shariah. It does not have a complete Shariah advisor, and they just follow the Central Bank rules. Unlike a bank, a bank is an intermediary institution between depositors and customers, so it has a greater responsibility to take care of customers.” (I2ACM).

The absence of a solid Shariah governance structure and insufficient laws might lead to Shariah risk, thereby tarnishing Ar-Rahnu’s reputation as one of the country’s most respected Islamic pawnbrokers. Findings indicates that, the Shariah governance practices has improve and majority Ar-Rahnu cooperatives were adhered to the GP 28 Shariah governance guideline imposed by SKM. Most Ar-Rahnu cooperatives started to have their own internal Shariah committees. Nevertheless, diverse perspectives were expressed on the current legal system in Ar-Rahnu. Some of them are satisfied with the existing laws, and several said current regulations are less relevant to the current context and must be revised.

To sustain competitiveness and ensure long-term viability, Ar-Rahnu cooperatives encounter various challenges that require collaborative efforts from both internal and external stakeholders. The holistic Shariah awareness and culture should be instilled in the management of cooperative’s management at all level. Besides, the management of Ar-Rahnu cooperative can improve its competency by implementing effective strategies. Regulators play a crucial role in establishing a comprehensive legal and regulatory framework that promotes adherence to Shariah principles and ensures sound governance within Ar-Rahnu cooperatives.

5.CONCLUSION

Strengthening Shariah governance is crucial for maintaining adherence to Sharia rules, enhancing the integrity and credibility of Ar-Rahnu cooperatives. The growing number of Ar-Rahnu providers demands greater attention from regulators and the institutions themselves to ensure they uphold a good reputation and image as Islamic pawn-broking providers. A robust Shariah governance framework ensures compliance with Islamic principles, distinguishing Ar-Rahnu from conventional pawn-broking and building trust and confidence among stakeholders. By upholding these standards, Ar-Rahnu can continue to serve as a reliable and ethical financial solution, contributing positively to the Islamic financial ecosystem and society as a whole.

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