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# From Constitutional Prohibition to Regulatory Architecture: Riba Regulation in Pakistan and Malaysia and the Design of a Transition Law for Islamic Banking

**Bushra Urooj[1], Saira Naheed[2]**

*[1]LLM Student at school of law and policy, University of Management and Technology, Lahore, Email: f2024144001@umt.edu.pk*
*[2]Lecturer at School of Law and Policy, University of Management and Technology, Lahore, Email: saira.naheed@umt.edu.pk*

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***Corresponding Author:***
*Saira Naheed*
***Email:***
*saira.naheed@umt.edu.pk*

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## ABSTRACT

*Pakistan and Malaysia both see Shariah compliance as important for Islamic banking but they have created very different legal systems to control riba. Pakistans system is based on a promise in the constitution to remove riba the rulings from the Federal Shariat Court and rules from the State Bank of Pakistan. Malaysias system is based on laws, a special Shariah Advisory Council at Bank Negara Malaysia and clear guidelines for how things should be done. This article uses that difference to make a case, for change. It looks at riba not as a religious rule but as an issue involving the order of laws, who is responsible how courts should handle it, who needs to be held accountable and how changes should be made. Using methods that look at the ideas and how things work the article examines Pakistans court system Malaysias rules about Shariah compliance and the guidelines set by both regulators. The article says that Pakistan has a constitution but less strong laws that go along with it. Malaysia on the hand has clearer ways to make sure things follow Shariah rules. Malaysia also has ways to report when things do not follow Shariah and has good teamwork between courts and regulators. The article says Pakistan should not just copy what Malaysia does. Instead Pakistan should take the parts of Malaysias system and make them fit for Pakistan. This should be done through a law about stopping interest and building an Islamic financial system. This law should explain what interest is make it required by law to follow Shariah rules create a group to handle Shariah finance set up a way for courts to refer to this group write down how to deal with cases where Shariah rules are not followed protect people who use financial services and plan a step-, by-step change before the 2028 deadline set by the constitution.*

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## Introduction

The ban on interest is one of the clear-cut rules of Islamic business ethics but putting it into practice in a modern bank system is challenging. A country cannot stop interest by changing names. It has to say what kinds of returns are not allowed allow ways to get money watch over how Islamic law is followed help the courts, control government debt protect people who use the banks and make sure there are penalties when banks treat following Islamic law as just a formality. The legal problem therefore is not whether Islamic law says interest is bad, in theory. The bigger question is how a modern legal system can turn that ban into banking laws. (Qur'an 2:275-279; Usmani, 2002; Islamic Financial Services Board, 2009).

Pakistan and Malaysia are an example to look at because they both have a big Islamic banking part and they both think following Shariah rules is very important for Islamic finance to be real.. The way they do things is very different. Pakistan starts with what the constitution says and the Federal Shariat Court has a lot of power and the State Bank of Pakistan makes the rules. Malaysia does things a bit differently they use laws about money. They have a group called the Shariah Advisory Council of Bank Negara Malaysia and they have rules that everyone has to follow.

This comparison is very important for Pakistan because they have a deadline to get rid of riba before January 1 2028 as it is written in Article 38(f) of the Constitution of Pakistan. The Constitution of Pakistan which was made in 1973 has this rule. It was also talked about in the Constitution Twenty-sixth Amendment Act in 2024. Malaysia also has some laws like the Central Bank of Malaysia Act from 2009 and the Islamic Financial Services Act, from 2013. Pakistan and Malaysia and their Islamic banking sectors are very important to look at.

The main point of this article is easy to understand but really important. Pakistan has a system that is very strong in theory but it is not working well in practice because it is not organized properly. On the hand Malaysias legal system is not as flashy but it works better in real life. This does not mean Pakistan should just copy Malaysias system. That would be an idea because Pakistan has its own unique legal system, including the Federal Shariat Court, the Council of Islamic Ideology and its own history of dealing with riba lawsuits.

A better way to do things would be for Pakistan to pick and choose the parts of Malaysias system that work well. Pakistan should keep its constitutional and judicial system but also use some of Malaysias good ideas, such as making sure companies follow Shariah law having a central authority to oversee Shariah finance and having procedures in place to handle cases where companies are not following the rules. Pakistan should also have ways to report when companies are not complying hold board members accountable and discipline those who are not doing their job properly as noted by Watson in 1974 Legrand in 1997 Nelken in 2001 and JRI Resources, in 2019.

This article helps finance law in three ways. First it looks at riba regulation as a problem with how thingsre governed and set up rather than just arguing about interest. Second it compares Pakistan and Malaysia by looking at what their laws do not just how they seem similar on the surface. Third it suggests what should be in a law for Pakistan that prohibits riba and helps the country move to a financial system that follows the constitution and can be enforced by banks. So this article is for people who study finance and also for people who make laws regulate, judge and work with moving from a system based on interest to one that follows Shariah rules like Islamic finance experts and bankers in Pakistan and other places and Islamic finance law is a big part of this. Islamic finance law is what this article is, about. (Ahmad et al., 2023; Uddin, 2024; Jamil, 2024).

## Conceptual Framework and Methodology

This article looks at things in a few ways. It is a study because it looks at what the constitution says and also at laws, court decisions, rules and standards for following Shariah. The article is qualitative which means it tries to understand what these things mean than just looking at numbers, like how well banks are doing or if customers are happy. It is also comparative which means it compares Pakistan and Malaysia to see what each country does and what Pakistan can learn from Malaysia without forgetting its constitution and how things work there. The article compares Pakistan and Malaysia to see what things each country does and how Pakistan can use what it learns from Malaysia. Pakistan can learn from Malaysia. Use those lessons to make things better as long as it remembers its own constitution and how things are done in Pakistan. (Hutchinson, 2018; Creswell & Poth, 2018).

The way things work is important. We should not just compare things on paper. For example we should not ask if Pakistan has the Shariah Advisory Council as Malaysia. This is not the question to ask. A better question is how Pakistan and Malaysia make sure that the Shariah rulings are consistent for financial business. It is also not enough to ask if Pakistan has a law that's exactly the same as Malaysias Islamic Financial Services Act 2013. A useful question is whether Pakistan has a law that requires Islamic financial institutions to make sure they follow the Shariah rules in everything they do including their goals, operations, business and activities. The Shariah compliance is what matters for financial institutions. Pakistan needs to have something in place to ensure this happens just like Malaysia does with the Islamic Financial Services Act 2013 and the Shariah Advisory Council. The goal is to have consistency in Shariah rulings for financial business, in Pakistan. (Legrand, 1997; Nelken, 2001; Central Bank of Malaysia Act 2009, ss. 56-57; Islamic Financial Services Act 2013, s. 28).

The basic idea of banking is based on four main concepts. The first concept is Maqasid al-Shariah. Maqasid al-Shariah is about being fair and just. It is about protecting peoples money and making sure they are not taken advantage of. Maqasid al-Shariah also makes sure that people are treated fairly when they buy or sell things. This idea helps us make sure that we do not just change the name of something to make it sound Islamic. We actually change the way it works.

The second concept is about who's in charge. This is called governance. We need to know who makes the decisions, who checks to make sure everything is okay who looks at the accounts, who reports any problems and who is responsible if something is not according to Shariah rules.

The third concept is about trust. This is called legitimacy. People need to believe that Islamic banks are really following Shariah rules. They need to know that the banks are not just using words to make their products sound good but they are actually different from regular banks.

The fourth concept is, about making sure the rules work in countries. This is called adaptation. We can learn from countries but we need to make sure that the rules work with the laws and customs of our own country. Maqasid al-Shariah and these concepts are important for Islamic banking to work properly. (Auda, 2008; Chapra, 2008; Islamic Financial Services Board, 2025; Watson, 1974).

The main materials include parts of the Quran that talk about interest; Pakistans Constitution, cases about interest and documents from the State Bank of Pakistan; the Central Bank of Malaysia Act 2009 the Islamic Financial Services Act 2013 and documents from Bank Negara Malaysia; and rules created by groups like the Islamic Financial Services Board and the Accounting and Auditing Organization for Islamic Financial Institutions. Other materials include books, articles from experts and studies about Islamic finance law, Shariah control and how laws change in different places. Explanations that are not from experts have not been included in the list of references to make the article stronger, for sending to a journal. (Hutchinson, 2018; Islamic Financial Services Board, 2009, 2025; AAOIFI, 2024).

## Riba as a Legal and Governance Problem

The Quran says that taking riba is not allowed. This rule is based on an idea: it is okay to buy and sell things but it is not okay to take extra money just because someone owes you money. The Quran says this in Surah al-Baqarah, where it says that buying and selling is allowed. Taking riba is not. It also tells people who take riba to stop doing it. It says that people who are having a hard time paying back money they owe should be given more time.

A time ago some important Islamic scholars figured out that there are different kinds of riba. One kind is called riba al-nasi'ah, which's when someone takes extra money just because they waited a long time to get their money back. The other kind is called riba al-fadl, which's when someone takes extra money when they trade certain things.

Nowadays Islamic banks are mostly worried about the kind of riba because when they lend people money they want to get some money back after a while just because some time has passed. This is basically the same, as taking riba, which is not allowed in the Quran. Islamic banks want to follow the Qurans rules so they have to figure out ways to lend money without taking riba. (Qur'an 2:275-280; Usmani, 2002; Vogel & Hayes, 1998).

The law has a lot to say about this idea. People often get it wrong. Islamic law does not have a problem with making money buying and selling things or lending money. It is okay to make a profit from selling something renting it out working with someone acting for someone owning something taking a risk or investing money. What Islamic law says is wrong is when someone lends money and gets money back just because time has passed, without taking any risk themselves. This is important when making rules because just using the right words from Islamic law does not make a contract valid. The law has to look at things, like who owns what who has control, who takes the risk how much things cost, if people are told everything they need to know and what happens if someone cannot pay back the money. (Usmani, 2002; Chapra, 2008; El-Gamal, 2006).

Governance is really important here. Islamic banks have a lot of products like murabaha, ijara, mudarabah, musharakah, diminishing musharakah, salam, istisna and wakalah-based products.. Just because a product has a certain name it does not mean that is what it really is. For example a murabaha facility needs to be a sale. An ijara structure needs to be a lease. A musharakah or mudarabah arrangement needs to share risks in a way that's consistent with the contract. Islamic banks cannot just charge a penalty for payments that is really just interest, in disguise. So the regulator has to watch everything, including how productsre approved how they are actually used how documents are written how audits are done how income is purified what customers are told and what happens when a transaction does not follow Islamic law or Shariah requirements of the Islamic bank and its murabaha, ijara, mudarabah, musharakah, diminishing musharakah, salam, istisna and wakalah-based products. (AAOIFI, 2024; State Bank of Pakistan, 2024; Islamic Financial Services Board, 2009).

A serious framework for riba must answer some questions. What is considered riba in the laws of the land? Who has the power to make decisions about Shariah finance that everyone must follow? How do courts deal with Islamic finance issues? What should institutions do when they do not follow Shariah rules? How can the system change without causing problems in the market or just pretending to comply with the rules? Pakistan and Malaysia have ways of answering these questions about riba and comparing them shows what is good and bad, about each way of doing things regarding riba. (Islamic Financial Services Board, 2025; Laldin & Furqani, 2018; Uddin, 2024).

## Pakistan: Constitutional Strength and Statutory Fragmentation

Pakistans interest framework starts with the Constitution. Article 38(f) as changed by the Constitution (Twenty-sixth Amendment) Act 2024 says the State must get rid of interest completely by 1 January 2028. This gives Pakistan a constitutional base, than many places that have Islamic banking systems. It also brings a sense of urgency. A constitutional deadline can help control the regulatory process but it can also bring legal and market risks if it is not supported by clear transition laws. (Constitution of Pakistan, 1973, art. 38(f); Constitution (Twenty-sixth Amendment) Act, 2024; Jamil, 2024).

Pakistan has a layer which is the judicial system. The issue of riba has gone through court cases in the Federal Shariat Court and the Supreme Court. The Federal Shariat Court looked at the laws about interest. Said they go against what Islam teaches in the case of Dr. Mahmood-ur-Rehman Faisal versus the Secretary of the Ministry of Law.The Shariat Appellate Bench also said that interest is not allowed in the case of Dr. M. Aslam Khaki versus Syed Muhammad Hashim.The United Bank Ltd versus M/s Farooq Brothers case was sent back to a court and earlier decisions were set aside but the court did not give a clear plan for Islamic banking laws.The Federal Shariat Court made another decision in the M/s Farooq Brothers, versus United Bank Ltd case, which is reported as PLD 2023 FSC 47. This decision strongly said that interest is not allowed and told banks to stop using interest-based systems. (Dr. Mahmood-ur-Rehman Faisal, PLD 1992 FSC 1; Dr. M. Aslam Khaki, PLD 2000 SC 225; United Bank Ltd, PLD 2002 SC 800; M/s Farooq Brothers, PLD 2023 FSC 47).

The judicial material is really powerful because it talks about the question directly: whether the interest that banks charge is considered riba. The courts in Pakistan have looked at this as a question that affects the whole country and its laws not just a problem between banks and their customers. This is why the Pakistani way of doing things is important. At the time what the courts say is not enough to make new laws. The courts can make decisions explain what the laws mean and give directions. They cannot make all the rules for things like managing money paying off debts, taxes and how banks should follow Shariah laws. The courts cannot do all of this on their own for the banking system. The judicial material and the Pakistani model are important because they deal with the question of riba. The Pakistani model is an example because the courts in Pakistan have made decisions about riba. These decisions are important for the country.

The courts in Pakistan have said that riba is not allowed. This is a deal because it affects the whole banking system. The judicial material is helpful because it explains what the courts have said about riba. It is also helpful because it talks about the model and how it works. The Pakistani model is not about the courts. It is also about the laws and rules that govern the banking system. The judicial material is important because it helps us understand these laws and rules. It is also important because it talks about the role of Shariah laws, in the banking system. The judicial material and the Pakistani model are connected to the question of riba. They are also connected to the banking system and the laws that govern it. The judicial material is helpful because it explains all of these things and how they work together. (M/s Farooq Brothers, PLD 2023 FSC 47; Uddin, 2024; Mansoori, 2022).

The third layer is about rules and regulations. The State Bank of Pakistan has made a set of rules for banking. They have a framework called the Shariah Governance Framework for Islamic Banking Institutions. This framework was sent out through IFPD Circular No. 08 Of 2024. It started being used from 1 January 2025. It applies to banks that only do banking, banks that have Islamic banking departments and regular banks that have Islamic banking branches. It explains what the jobs are of the people in charge the managers, the Shariah boards the Shariah experts who work at the banks the departments that make sure everything is okay with law the people who create new products and the people who check to make sure everything is being done correctly. The Islamic banking rules also say that if the banks do not follow the rules they might get in trouble with the law. The State Bank of Pakistan Islamic banking rules are very important, for banking. (State Bank of Pakistan, 2024; Islamic Financial Services Board, 2025).

Market data supports the need for rules. The State Bank of Pakistans Islamic Banking Bulletin for March 2026 showed banking assets of about PKR 14.7 trillion. The same report showed deposits of about PKR 11.3 trillion. It also showed financing of, about PKR 5.6 trillion. Islamic banking made up 23.0 percent of banking assets. Islamic banking made up 28.5 percent of deposits. Islamic banking made up 38.2 percent of financing. These numbers show that Islamic banking is no longer an ethical area. It is an important part of Pakistans banking industry. (State Bank of Pakistan, 2026).

The main problem is not that there are no rules. Pakistan has a constitution, legal guidelines, central bank instructions, Islamic law requirements and international standards. The problem is that everything is spread out. The constitution, court decisions, bank instructions, Islamic rules, regular banking laws, court procedures and public debt documents do not yet work under one combined law. This split can cause confusion, for courts, officials, banks and people at a time when Pakistan needs the opposite. (Uddin, 2024; Jamil, 2024; Islamic Financial Services Board, 2025).

## Malaysia: Statutory Shariah Compliance and Centralised Authority

Malaysia does things differently when it comes to law. Malaysias legal technique is different. It does not start with a rule like Pakistans, where they have to get rid of riba by a date. In Malaysia they made sure the financial laws follow the Shariah rules from the beginning. The Central Bank of Malaysia Act 2009 is a law that created the Shariah Advisory Council of Bank Negara

Malaysia. This council is in charge of figuring out what Islamic law says about financial business. The law has sections, like sections 56 and 57 that say if a court or an arbitrator has a question, about Shariah they have to ask the Shariah Advisory Council. The councils answer is final so the courts and arbitrators have to go by what the Shariah Advisory Council of Bank Negara Malaysia says about Shariah questions and this is how Malaysias Shariah compliance works for financial business.(Central Bank of Malaysia Act 2009, ss. 51, 56-57; Bank Negara Malaysia, 2019; Islamic Financial Services Act 2013).

The Islamic Financial Services Act 2013 takes a step by making it a law that Islamic financial institutions must follow Shariah rules. The Islamic Financial Services Act 2013 says that Islamic financial institutions have to make sure they do everything according to Shariah rules. This includes what they want to achieve how they operate, their business what they do and all their activities must follow Shariah rules. The law also says that if Islamic financial institutions do not follow Shariah rules it is a problem that needs to be fixed. If an Islamic financial institution realizes it is doing something that does not follow Shariah rules it has to tell Bank Negara Malaysia and its Shariah committee away. Then it has to stop doing that thing and come up with a plan to fix the problem within the time the law says. This means that following Shariah rules is not something that Islamic financial institutions should do to look good but it is something they have to do by law. The Islamic Financial Services Act 2013 makes Shariah compliance a legal requirement, for financial institutions. (Islamic Financial Services Act 2013, s. 28; Laldin & Furqani, 2018).

Bank Negara Malaysia has a plan called the Shariah Governance Policy Document that was made in 2019. This plan makes sure that everyone knows what they have to do. It tells the people in charge like the board and the senior management what is expected of them. It also tells the Shariah committee what they need to do. The good thing about this plan is that it makes things very clear. It is like a list of jobs. The law says what has to be done. Then the central bank says how it should be done. The Shariah committee gives the say on what is right and wrong. The banks and other places have to follow these rules.. If there are any problems the courts know what to do. This is different from what they do, in Pakistan. Bank Negara Malaysias plan is very clear and easy to understand. It helps everyone know what they have to do. The Shariah Governance Policy Document is a help. Bank Negara Malaysias Shariah Governance Policy Document is very important. (Bank Negara Malaysia, 2019; Hussain et al., 2015).

Malaysian case law shows how this structure came into being. Early cases like Bank Islam Malaysia Berhad v Adnan Omar tended to treat financing documents as regular contracts. Later cases like Affin Bank Berhad v Zulkifli Abdullah and Arab Malaysian Finance Bhd v Taman Ihsan Jaya raised questions about recovering profit and the fairness of certain BBA structures. The Court of Appeal in Bank Islam Malaysia Bhd v Lim Kok Hoe brought back certainty while also acknowledging that Islamic finance cases need proper Shariah analysis. The later SAC-reference cases Mohd Alias Ibrahim v RHB Bank Bhd and JRI Resources Sdn Bhd v Kuwait Finance House (Malaysia) Berhad, made it clear that the SAC determines Islamic law, for Islamic financial business while the court still has the power to decide the case. (Bank Islam Malaysia v Adnan Omar, 1994; Affin Bank v Zulkifli, 2006; Arab Malaysian Finance v Taman Ihsan Jaya, 2008; Bank Islam Malaysia v Lim Kok Hoe, 2009; Mohd Alias, 2011; JRI Resources, 2019).

Malaysias way of doing things is not perfect either. People are talking about the power of the SAC rulings. How they affect the courts, the independence of institutions and the problem of giving too much power to interpret things. Some experts are also wondering if some Islamic finance products are really that different from loans. These are points to think about but they do not mean Malaysias model is bad. They just show that we need to make sure the laws are clear and that we have supervision and transparency. For Pakistan Malaysia is useful because it shows how to make sure things follow Shariah law through laws, an authority, ways for courts to get help and good governance. Malaysias model is not perfect. It is helpful, in showing how to get things started. (Laldin & Furqani, 2018; JRI Resources, 2019; El-Gamal, 2006).

**Table 1. Comparative legal architecture of riba and Shariah governance regulation**

| Dimension | Pakistan | Malaysia | Comparative finding |
|---|---|---|---|
| Primary legal driver | Constitutional mandate, Federal Shariat Court jurisprudence and SBP regulatory instruments. | Financial legislation, especially the Central Bank of Malaysia Act 2009 and Islamic Financial Services Act 2013. | Pakistan has stronger constitutional direction; Malaysia has clearer statutory implementation. |
| Central Shariah authority | FSC for constitutional Shariah review; SBP and institution-level Shariah boards for Islamic banking governance. | BNM Shariah Advisory Council as statutory authority for ascertainment of Islamic law in Islamic financial business. | Pakistan needs a technical Shariah finance reference mechanism that does not displace FSC jurisdiction. |
| Institutional governance | SBP Shariah Governance Framework defines duties of boards, management, Shariah boards, compliance and audit functions. | BNM SGPD defines board, Shariah committee, senior management and control-function responsibilities. | Both systems recognise multi-actor governance, but Malaysia has stronger statutory backing. |
| Court handling of Shariah finance questions | Ordinary courts decide disputes; no equally detailed statutory reference route for technical Islamic finance questions. | Courts or arbitrators refer Shariah questions to the SAC under CBA 2009 where needed. | Malaysia offers an adaptable model for judicial coordination. |
| Shariah non-compliance | Regulatory treatment exists through SBP governance rules, but statutory codification remains incomplete. | IFSA 2013 directly regulates notification, cessation and rectification duties. | Pakistan should codify non-compliance as a legal event, not merely an internal governance matter. |

| Dimension | Pakistan | Malaysia | Comparative finding |
|---|---|---|---|
| Transition challenge | Fixed 2028 deadline requires conversion of banking, public debt, liquidity, documentation, taxation and court-decree practices. | Mature statutory Islamic finance market with ongoing governance and enforcement challenges. | Pakistan needs phased transition legislation rather than symbolic prohibition. |

## Comparative Findings

### *Legal hierarchy matters*

The first thing we found out is that having a constitution and clear laws are two different things. The deadline set by Pakistans constitution makes the reform project important. Something that needs to be done quickly. In Malaysia the laws give people in charge organizations and courts an idea of what they need to do. A constitution can show us the way. A law must explain what people have to do how they have to do it what happens if they do not follow the rules what they have to report and what role each organization plays. So Pakistans next step should be to make all the laws work together not just say again that riba is not allowed. (Constitution of Pakistan, 1973; Islamic Financial Services Act 2013; Central Bank of Malaysia Act 2009).

This point is really important because Islamic banking is involved in things like deposits, financing, investments and sovereign instruments. It also deals with interbank liquidity, recovery litigation and consumer protection. The rules of the country cannot decide everything on their own such as whether a court decision should be changed, how government savings schemes should be rearranged what to do with income that does not follow the rules or how tax law should handle documents, for selling assets. If we do not have laws to guide the system it may take a time to do things or people may only pretend to follow the rules. Islamic banking is a part of this and we need to think about how it will work. Islamic banking needs to be considered in all these areas to make sure everything runs smoothly. (State Bank of Pakistan, 2026; Islamic Financial Services Board, 2025).

### *Central authority must be carefully designed*

The second thing is about Shariah authority. In Malaysia they have something called the SAC which helps reduce confusion by giving courts and institutions a point to refer to Pakistan is different because it has a different system in place. Pakistan has the Federal Shariat Court which checks if laws go against what Islam says and the SBP is in charge of banking institutions. You cannot just take the SAC and put it in Pakistan without figuring out how it will work with the Federal Shariat Court, the Supreme Court, the SBP and the regular banking courts. Shariah authority is a deal in Pakistan and it needs to be handled carefully. The SAC in Malaysia is an idea but it may not work in Pakistan because of the different Shariah authority setup. Shariah authority in Pakistan has to be considered when trying to implement something, like the SAC. (Central Bank of Malaysia Act 2009, ss. 56-57; JRI Resources, 2019; Constitution of Pakistan, arts. 203B-203G).

The solution is separation based on function. A central Shariah Finance Council inside or connected to SBP should give rulings on Islamic finance products, contracts and operational questions. Banking courts and civil courts should be able to send technical Shariah finance questions to that group when there is no binding ruling. However constitutional questions, about whether a law goes against the rules of Islam should stay under the control of the Federal Shariat Court and the constitutional appeal system. This keeps Pakistans structure intact while taking on Malaysias coordination function. (Mohd Alias, 2011; JRI Resources, 2019; M/s Farooq Brothers, PLD 2023 FSC 47).

### *Shariah non-compliance needs legal consequences*

The third finding is that when something does not follow Shariah rules it has to be taken seriously by the law and the people in charge. If a product or a way of making money is found to not be following the rules we cannot just ignore it. Deal with it in a casual way. We need to have a system in place that says what to do in this situation. This system should include telling the people inside the company getting the Shariah board to look at it informing the people who make the rules stopping what is wrong away if necessary making things right cleaning up the money treating the customers fairly if they are affected getting the board to say everything is okay and then checking to make sure everything is still okay. The way Malaysia does it with the IFSA model is an example because it makes sure that people take not following the rules very seriously. Pakistans SBP framework is trying to do the thing but it needs stronger support, from the law to really work. (Islamic Financial Services Act 2013, s. 28; Bank Negara Malaysia, 2019; State Bank of Pakistan, 2024; Islamic Financial Services Board, 2025).

This point is also good for the customers of banking. Customers of banking usually trust the Islamic banking institutions Shariah representation. If this Shariah representation is not done properly the Islamic banking customers should not have to deal with a private problem. The law should make sure that Islamic banking institutions tell the customers everything treat income in a clear way and make sure that the people in charge are responsible, for what they do. If this is not done, following the Shariah rules becomes something that the Islamic banking institution does to look good than something that the law requires. (Islamic Financial Services Board, 2025; Laldin & Furqani, 2018).

### *Substance must prevail over labels*

The fourth finding is that Pakistan should not just focus on making things look like they are following rules. There is a problem with Islamic finance, which is that it can be very similar to regular loans. This does not mean that Islamic finance is not possible. It means that the law needs to look at what's really going on. Just because someone calls a deal murabaha, ijara, musharakah or wakalah it should not be considered valid. The people, in charge and the courts should check if the deal really involves selling, leasing, owning, taking risks being an agent or being a partner, when it comes to finance like murabaha, ijara, musharakah or wakalah. (El-Gamal, 2006; AAOIFI, 2024; Affin Bank v Zulkifli, 2006; Arab Malaysian Finance v Taman Ihsan Jaya, 2008).

Pakistans reform law should have a rule that stops people from getting around the law. This rule should say that a business deal is not okay with Shariah if it uses words but it is really just a loan or debt that gets bigger over time without actually doing any real business providing a service owning something taking a risk or investing in something. This rule would make sure that the rules about riba are in line with what Shariah's trying to achieve and it would help people trust Islamic banking. The rule is important, for banking because it would make sure that business deals are really Shariah-compliant. Islamic banking should follow this rule to be fair and to follow the principles of Shariah. (Auda, 2008; Chapra, 2008; Usmani, 2002).

### *Transition must be phased, not improvised*

The fifth finding is that Pakistan needs to make a plan for what they want to do by 2028. If they just stop using the arrangements they have now it could cause a lot of problems with the law people might take them to court and it could be bad for the whole system.. If they just keep putting it off they will not be following what the constitution says they should do. A better way to do this would be to make a law that says they have to do things in steps they have to report on how they're doing every year and they have to make sure that the institutions that are following the plan are safe from getting in trouble. Pakistans 2028 deadline is very important. They need to make sure they are ready, for it. (Constitution (Twenty-sixth Amendment) Act, 2024; Jamil, 2024).

The change needs to be about more than banking for individuals. It has to look at things like when governments borrow money how the treasury works, the ways the State Bank of Pakistan helps with money government programs to help people save markets for sukuk laws about taxes and registration how companies get money what happens when someone does not pay back a loan charges, for not paying old rules and how accounting works.

If we only change the products that banks offer it will not be enough because the government still uses things that are based on interest to manage its money and make sure there is money moving around. The change needs to be bigger. Include public finance and how money moves around. (State Bank of Pakistan, 2026; Islamic Financial Services Board, 2025).

**Table 2. Selected landmark cases and their legal relevance**

| Jurisdiction | Case | Legal relevance |
|---|---|---|
| Pakistan | Dr. Mahmood-ur-Rehman Faisal v Secretary, Ministry of Law, PLD 1992 FSC 1 | Early Federal Shariat Court decision treating interest-related provisions as repugnant to Islamic injunctions. |
| Pakistan | Dr. M. Aslam Khaki v Syed Muhammad Hashim, PLD 2000 SC 225 | Shariat Appellate Bench decision upholding broad anti-interest reasoning and giving transformation directions. |
| Pakistan | United Bank Ltd v M/s Farooq Brothers, PLD 2002 SC 800 | Review decision remanding the riba matter and delaying final implementation. |
| Pakistan | M/s Farooq Brothers v United Bank Ltd, PLD 2023 FSC 47 | Fresh Federal Shariat Court judgment reaffirming the prohibition of riba and directing transition from interest-based banking. |
| Malaysia | Bank Islam Malaysia Bhd v Lim Kok Hoe [2009] 6 MLJ 839 | Restored commercial certainty in BBA disputes while recognising the Shariah dimension of Islamic finance litigation. |

| Jurisdiction | Case | Legal relevance |
|---|---|---|
| Malaysia | Mohd Alias Ibrahim v RHB Bank Bhd [2011] 4 CLJ 654 | Clarified that the SAC ascertains Islamic law for Islamic finance and does not decide the entire dispute. |
| Malaysia | JRI Resources Sdn Bhd v Kuwait Finance House (Malaysia) Berhad [2019] 3 MLJ 561 | Federal Court decision affirming the constitutional validity and binding effect of SAC rulings on referred Shariah questions. |
| Malaysia | Pan Northern Air Services Sdn Bhd v Maybank Islamic Bhd [2020] MLJU 2206 | Illustrates practical court handling of ta'widh and SAC-reference issues. |

## A Pakistan-Specific Reform Model

The comparison shows that there needs to be a law: a Riba Prohibition and Islamic Financial System Transition Act. The name of the law is not as important, as what it does. The law should not be a symbolic statement because Pakistan already has constitutional and legal statements. The law should work in practice. It should explain what riba is, put duties in place give power to people work with courts and regulators say what will happen if rules are broken and handle the change. (Uddin, 2024; Jamil, 2024; Islamic Financial Services Board, 2025).

### *Definition of riba and protection of lawful profit*

The law should explain what riba is in a way that includes any amount added to the original loan or debt. This means it should cover all kinds of situations like when the extra amount's fixed or when it changes or when it is added on top of another amount. It should also include cases where the extra amount is hidden as a fee for a service that is not really provided or when it is part of a plan that's just a way to charge interest. At the time the law should make it clear that making a profit from buying and selling things renting something out working together with someone acting on behalf of someone providing a service or investing in something that involves some risk is okay. We need an explanation of what riba is because if it is not clear it can lead to problems. Either people will be stopped from doing things that are actually allowed. They will find ways to get around the rules. The law must make it clear that it is not allowed to guarantee that someone will owe money than they should without making it seem like it is wrong to make a legitimate profit from doing business with riba. The law should protect people from riba. Make sure that people can still make a profit from legitimate business activities, like trade, lease, partnership, agency, service and risk-based investment without being accused of riba. (Usmani, 2002; M/s Farooq Brothers, PLD 2023 FSC 47; AAOIFI, 2024).

The law should also let the State Bank of Pakistan make rules for banking products and contracts that everyone has to follow. These rules can be made by the State Bank of Pakistan itself or by using rules that are already accepted like the rules made by the Accounting and Auditing Organization for Islamic Financial Institutions. Only after they have been checked to make sure they work in our country. This is necessary because Islamic banking uses kinds of contracts and each contract has its own set of technical rules. The law should make sure that these rules are seen as requirements that must be followed than just good ideas that people can choose to follow if they want to. Islamic banking needs this because it is based on finance principles and these principles are very important for Islamic finance to work properly. The State Bank of Pakistan and Islamic finance experts should work together to make sure that the rules, for banking products and contracts are clear and fair. (AAOIFI, 2024; State Bank of Pakistan, 2024).

### *Statutory Shariah compliance duty*

Pakistan needs to have a law that's similar to what Malaysia has with the IFSA 2013. Every single Islamic. Every part of a bank that does Islamic banking and every other company that does Islamic finance should make sure they are doing things according to Shariah rules. They should also follow the rules set by the State Bank of Pakistan and the decisions made by the Shariah finance authority. This rule should apply to the company, the people, in charge of the company and the top managers of the Islamic bank, Islamic banking subsidiary, Islamic banking window and other companies that do Islamic finance. (Islamic Financial Services Act 2013, s. 28; Laldin & Furqani, 2018; State Bank of Pakistan, 2024).

The job of making sure something is okay with Shariah rules should not just be about saying yes or no to a product. Shariah rules need to be followed from start to finish: when we are thinking about the product, when we are writing down the details when we are buying things for the product when we are actually doing the work when we are keeping track of money when we are talking to customers, when things are not going well when we are trying to fix problems when someone wants to stop when we are getting money back and when we are closing everything down. A product can seem okay at first. Then it can become not okay when we are actually doing it. So the law should say that we need to keep checking if something's okay with Shariah rules all the time and that we need to look carefully at everything not just say it is okay, at the beginning. Shariah compliance is very important. Shariah compliance needs to be checked all the time to make sure the product is following Shariah rules. (Bank Negara Malaysia, 2019; Islamic Financial Services Board, 2009, 2025).

### *Central Shariah Finance Council*

The law needs to set up a Central Shariah Finance Council either connected to the State Bank of Pakistan. The group should have people who are trained in Shariah law experts in finance law banking professionals and others who know about rules and solving arguments. This Council must give decisions on questions, about Islamic finance agree on or create Shariah rules give advice to the State Bank about products and changes keep a public list of its decisions and help train courts and the people who watch over the financial system. (Central Bank of Malaysia Act 2009, ss. 51, 56-57; Hussain et al., 2015).

The Council should not take the place of the Federal Shariat Court. This has to be very clear. The main job of the Council should be to check and make sure that Islamic financial businesses are following the rules and to set standards for them. The Federal Shariat Court should still have the power to decide if laws are against the teachings of Islam. If we keep these two separate it will prevent problems between institutions. Make the changes safer, in terms of the constitution. The Federal Shariat Court and the Council should have their roles the Federal Shariat Court should deal with laws that go against Islam and the Council should deal with Islamic financial business. (Constitution of Pakistan, arts. 203B-203G; M/s Farooq Brothers, PLD 2023 FSC 47).

### *Court-reference mechanism*

Banking courts and civil courts and also arbitral tribunals should have the power to send Shariah finance questions to the Central Shariah Finance Council. They should have to do this when there is no decision already made on the issue. The Central Shariah Finance Council should only get questions about Shariah finance. They should not get questions about what happened or who is at fault.

The court is still in charge of using the decision, from the Central Shariah Finance Council and applying it to the situation. The court has to figure out what the contract means. If someone did not follow the contract. The court also has to calculate what the punishment should be and make sure the punishment is enforced. Banking courts and civil courts and also arbitral tribunals have to do this with Shariah finance questions. (Central Bank of Malaysia Act 2009, ss. 56-57; Mohd Alias, 2011; JRI Resources, 2019).

This system uses an idea from Malaysia. Makes it work for Pakistan. It knows that regular judges may not be experts, in business law but it still gives them the power to make decisions. This system helps reduce decisions makes things faster and makes people trust the decisions made about Islamic finance. This system should have rules that say how long judges have to make decisions when they have to publish their decisions and what to do with cases that are still waiting to be decided. (Mohd Alias, 2011; Pan Northern, 2020).

### *Shariah non-compliance reporting and rectification*

The law should include a way to handle situations where something is not following Shariah rules. When an organization finds out about a problem it should quickly tell its Shariah board or committee and also let SBP know within a certain time. If the problem is proven the organization should stop the activity that is causing the issue make a plan to fix it find the customers who are affected get rid of any income that is not allowed fix any mistakes, in papers or how things were done and then make sure the top leaders of the organization say it is all fixed. (Islamic Financial Services Act 2013, s. 28; Bank Negara Malaysia, 2019; State Bank of Pakistan, 2024).

The protocol needs to know the difference between problems with documents, mistakes when putting plans into action situations where money is made in a way that is not allowed and situations where the rights of customers are not respected. Each of these problems needs to be handled in a way. Some problems can be fixed inside the company. The protocol should be able to tell the difference, between technical documentation defects, execution failures, unlawful income events and customer-rights events. Some problems need to be told to the customers. The company may need to give them their money back. In some cases the company may need to give money to a charity because they made money in a way that is not allowed or they may need to pay a penalty to the government. The law should allow the SBP to create rules and it should also say what the minimum responsibilities are so that everyone knows what they have to do and the SBP can make sure that these responsibilities are followed. (Islamic Financial Services Board, 2025; AAOIFI, 2024).

### *Anti-circumvention and substance review*

The law should have a part that stops people from finding ways around it. This part should say that a business deal is not okay with Shariah just because it uses words or Islamic finance papers.

The people in charge and the courts should look at what's really going on including things like how assets are connected who owns what who has control, how risks are shared how prices are set what happens when someone does not pay how people are treated if they pay off their debt early and if someone is acting for someone else. The law should make sure that the deal is not a way to guarantee that someone will make more money from debt. The people, in charge and the courts should check if the deal is really Shariah-compliant or not. Shariah-compliant deals should be fair and honest. The law should help make sure of that. The law should look at the Shariah-deal and see if it is really what it says it is. (El-Gamal, 2006; Usmani, 2002).

This part is really important for Islamic banking to be legitimate. If people think that Islamic banking is like regular banking but with more complicated papers then people will start to question the integrity of the whole system. When we look at the details of a deal it does not mean that judges should be able to change the terms of finance agreements just because they think it is not fair. It means that judges should make sure that Islamic finance agreements are real and follow the rules and they should not allow agreements that are basically just hiding the fact that they are charging interest, which's against the principles of Islamic banking and this is what is known as riba, in Islamic finance. (Dusuki & Abozaid, 2007; Islamic Financial Services Board, 2025).

***Public debt, liquidity and tax neutrality***

A banking system without interest cannot work if the governments financial system still uses interest. The law should ask for a plan to change debt. This plan should cover things like government bonds how the government borrows money, how the public sector gets money, government savings programs and ways to manage money. It should tell the Ministry of Finance the central bank and other groups to create options that follow Islamic rules. These options could include things, like sukuk and other methods that help manage money without using interest-based loans. (Jamil, 2024; State Bank of Pakistan, 2026; Islamic Financial Services Board, 2025).

The law should also make sure that taxes and documents are treated the same. Islamic finance usually needs to have sales contracts, rental agreements or partnership papers. Regular finance just uses one loan contract. If taxes are not the same for everyone and it is hard to register and pay fees for documents Islamic finance might become more expensive than loans. This would make it tougher for people to really switch to finance. The law must not punish people for following the rules of Shariah when it comes to the way they do business. Islamic finance needs to be treated so people can choose it without worrying about extra costs. The goal is to make Islamic finance just as easy to use as finance and that means the law should not favor one over the other. Islamic finance should be given the treatment, as regular finance when it comes to taxes and documents so people can use Islamic finance without any problems. (Laldin & Furqani, 2018; Usmani, 2002).

***Consumer protection, disclosure and judicial capacity***

Consumer protection is really important when we talk about riba reform. We need to make sure that customers get all the information they need about the contract they are using. This means they should know the sale price or how the rental works, how the profit is calculated what happens if they default and what the rules are for ibra or getting a rebate. They should also know about ta'widh. How risks are shared and what happens if they want to settle early. Just because we give customers this information does not mean that the bank is following Shariah rules.. It does help to avoid confusion and arguments.. It stops banks from saying they are doing the right thing because of their religion when really they are not being clear with customers, about what they have to do. Consumer protection and riba reform go hand in hand. Clear disclosures are a big part of that. (Islamic Financial Services Board, 2025; Pan Northern, 2020).

The people who work in the courts like the judges who deal with banking and civil cases and the judges who hear appeals need to know about finance. They need to understand things, like Shariah governance and Islamic finance contracts. The court staff and the lawyers who work with banks also need this training. They have to know about riba and sukuk and ta'widh and ibra. They need to know what to do when someone does not follow the Shariah rules. If the courts do not apply the law in the way every time it will not work. So the law should say that the people who work in the courts have to get training. They should also have books and materials to help them make good decisions when they are dealing with Islamic banking problems. This way the courts can handle these cases in an consistent way. The judges who deal with banking cases should get the training they need to do their job well. Islamic finance contracts and Shariah governance are things for them to know about. (Mohd Alias, 2011; JRI Resources, 2019).

**Table 3. Recommended contents of a Pakistan Riba Prohibition and Islamic Financial System Transition Act**

| **Recommended provision** | **Purpose** | **Expected effect** |
|---|---|---|
| Definition of riba | Covers stipulated excess over loans or debts while protecting lawful trade, lease, partnership and investment profit. | Reduces ambiguity and closes disguised-interest loopholes. |
| Statutory Shariah compliance duty | Requires Islamic financial institutions and windows to ensure end-to-end Shariah compliance. | Makes compliance enforceable beyond internal certification. |
| Central Shariah Finance Council | Creates a recognised technical authority for Islamic finance rulings and standards. | Improves consistency and supports regulators and courts. |
| Court-reference mechanism | Allows courts and arbitrators to refer technical Shariah finance questions. | Reduces inconsistent judicial treatment while preserving judicial power. |
| Shariah non-compliance protocol | Requires reporting, cessation where needed, rectification, purification and board certification. | Strengthens accountability and customer trust. |
| Anti-circumvention rule | Tests substance rather than Islamic labels alone. | Protects Maqasid and market legitimacy. |
| Public debt and liquidity transition plan | Covers sovereign borrowing, SBP liquidity tools, sukuk and public savings schemes. | Makes the constitutional deadline operational. |

| Recommended provision | Purpose | Expected effect |
|---|---|---|
| Tax and documentation neutrality | Removes extra legal costs caused by Shariah-compliant documentation. | Encourages genuine conversion. |
| Consumer disclosure rules | Explains contract type, pricing, default charges, ibra and risk allocation. | Reduces disputes and protects customers. |
| Annual parliamentary reporting | Requires public progress reports against the 2028 deadline. | Creates accountability and transparency. |

## Discussion: Why Adaptation Is Better Than Transplantation

Comparative law is only helpful when we think about the situation it is being used in. We should not look at Malaysias experience as something we can just copy and use. Pakistan has its Federal Shariat Court that has the power to make decisions based on the constitution and it has its own rules about riba that have to be followed by a certain time. The court system in Pakistan is also different from the one in Malaysia and the banking system is changing to follow rules. The SAC in Malaysia works within a system of laws and rules. If we copy what Malaysia does without making changes to fit our country it could cause problems about who has the power to make decisions especially between a new group that deals with Shariah finance and the Federal Shariat Court. Comparative law like this can be useful, for Pakistan. Only if we use it in a way that makes sense for our own country. We need to think about how Malaysias experience can help us with Shariah finance and how we can use it to make our own system better. (Watson, 1974; Legrand, 1997; Nelken, 2001).

Pakistan should take a look at how things work in other countries like Malaysia. Malaysia has a system that makes sure the laws about finance are actually followed. This is because the laws have to be enforced and people have to do what they are supposed to do. The courts need a way to figure out if the laws are being followed. If something goes wrong there has to be a way to report it and fix it. This means that the people in charge not the Islamic scholars have to be responsible for what happens. These are things that Pakistan can learn from. However Pakistan should make sure that the way it does things is its own and not just a copy of someone System. Pakistan should find a way to make these ideas work in its country. The Islamic finance laws, in Pakistan should be enforced in a way that makes sense for Pakistan. (Islamic Financial Services Act 2013; Central Bank of Malaysia Act 2009; Bank Negara Malaysia, 2019; Islamic Financial Services Board, 2025).

The biggest counterpoint is that laws cannot fix the money problem of changing the way public money and banking works. That point makes sense. A law by itself cannot start markets teach judges change how the government borrows money or adjust how organizations work.. Without laws these jobs stay broken and easy to change. The suggested law should be seen as the support needed. It won't finish the change, on its own. It can set up the power, plans and responsibility needed for the change to really happen. (Jamil, 2024; Uddin, 2024; Islamic Financial Services Board, 2025).

Another thing people might say against a central Shariah authority is that it could reduce the number of different opinions in Islamic jurisprudence. This is a concern. Islamic law has different views and if one group has too much control it could get rid of the good differences. The solution is not to get rid of authority completely. The solution is to make sure the people in charge explain their decisions clearly publish their rulings talk to scholars and people who work in the field and make it clear what rules are set in stone for the banking system and what is an idea, for discussion. Banking law needs to be clear. That does not mean it has to stop people from learning and discussing Islamic law. Islamic jurisprudence and Shariah authority are important. Shariah authority should be careful not to reduce pluralism in Islamic jurisprudence. (Legrand, 1997; Nelken, 2001).

A third thing people might say against this is that looking into anti-circumvention might make Islamic finance lawsuits really hard to predict. We should not let judges cancel contracts just because they do not like how things turn out financially. The solution is to define what we mean by substance review. The law needs to point out things to look for: who owns something, who has it, who takes the risk how assets are connected, who is, in charge how prices are set what happens when someone defaults and whether the deal creates debt that is not allowed. When we review something to see if it is real we need to be careful and follow rules not go by what we think. Islamic finance needs this to be fair and clear so we can trust the process. Know what to expect from Islamic finance litigation. (El-Gamal, 2006; AAOIFI, 2024).

## Conclusion

The control of interest is not a religious statement. It is a project to build a system. Pakistan has a constitutional and legal background especially after the updated decision from the Federal Shariat Court and the constitutional deadline to remove interest before 1 January 2028. It also has progress, in regulation through the Shariah Governance Framework of the State Bank of Pakistan. The missing part is connection: a law that can turn legal promises into something that can be used in the financial system. (Constitution of Pakistan, 1973, art. 38(f); M/s Farooq Brothers, PLD 2023 FSC 47; State Bank of Pakistan, 2024).

Malaysia has shown that following Shariah rules by law is a thing. They have one group that makes sure everyone is following these rules. They also have a way for courts to get help when they need it and a way to report when people are not following the rules. The people, in charge of banks have to make sure they are doing things too. Pakistan can learn from this. They should not just copy what Malaysia is doing. Use these lessons to make their own way. Pakistan needs to make sure the Federal Shariat Court is still a part of their system. At the time they need to create a special way to handle Islamic finance questions when they come up in regular bank cases. Islamic finance questions should have a pathway. This will help Pakistan make sure they are doing things with Islamic finance. Malaysias experience with statutory Shariah compliance is very important. Pakistan should really look at what Malaysia has done with their Shariah authority and court-reference mechanisms. (Islamic Financial Services Act 2013; Central Bank of Malaysia Act 2009; Bank Negara Malaysia, 2019; JRI Resources, 2019).

The Riba Prohibition and Islamic Financial System Transition Act is a deal. It should clearly say what riba is. The Riba Prohibition and Islamic Financial System Transition Act should also make sure that people who do business in a way can still make a profit. The Riba Prohibition and

Islamic Financial System Transition Act has to make sure that everyone follows the rules of Shariah.

The Riba Prohibition and Islamic Financial System Transition Act needs to create a Central Shariah Finance Council. The Riba Prohibition and Islamic Financial System Transition Act should have a way for courts to ask for help when they need it. The Riba Prohibition and Islamic Financial System Transition Act has to say what happens when someone does not follow the rules of Shariah.

The Riba Prohibition and Islamic Financial System Transition Act should have a rule that prevents people from finding ways around the law. The Riba Prohibition and Islamic Financial System Transition Act needs to have a plan for when the country owes money and needs money to keep things running. The Riba Prohibition and Islamic Financial System Transition Act should make sure that taxes are fair. The Riba Prohibition and Islamic Financial System Transition Act has to protect the people who buy things. The Riba Prohibition and Islamic Financial System Transition Act requires that the government tells the public what is going on every year.

This plan would help Pakistan because it gives them a way to do things. It is between two choices: stopping everything all, at once which can cause big problems or just changing the name of things which does not really help. The Riba Prohibition and Islamic Financial System Transition Act is a choice because it is not too extreme. (Jamil, 2024; Uddin, 2024; Islamic Financial Services Board, 2025).

The main goal is not just to take interest out of documents. We want to create a system that is fair and follows the law. In this system people should make money from work not from taking advantage of others. We also want to make sure that people who borrow money are treated fairly and that banks are honest about what they're doing. The rules of the Shariah should be. People should know the difference between trading and riba. This is what Pakistans next step in changing banking should be based on. Pakistans next phase of banking reform should be judged by this standard. Islamic banking reform, in Pakistan should follow these rules to make sure it is really Islamic. (Qur'an 2:275; Chapra, 2008; Auda, 2008; Usmani, 2002).

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