

**A Study on  
Risk Management in Islamic Banking**

دراسة حول اداراه المخاطر في البنوك الاسلامية

by

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## **ABSTRACT**

Risk management is an integral part of banks' activities and the banking industry is generally considered one of the riskiest types of businesses. Therefore, the present study aims to examine the risk management practices in Islamic banking, using Ajman bank as the case study. The methodology used in this study is qualitative based on structured interview. The analysis is based on face-to-face interviews with five heads of departments including Retail Banking Department, Internal Control Department, Sharia Department, Compliance and Risk Management (liquidity) Department. The results show that Ajman bank has effective risk management practices. The Risk Management department displays proper control for risk mitigation and the bank is in accordance with the Sharia compliant. In addition, the findings reveal that the bank complies with Basel requirements and UAE Central Bank regulations.

## ملخص

إدارة المخاطر هي جزء لا يتجزأ من أنشطة البنوك وتعتبر الصناعة المصرفية عموماً واحدة من أخطر أنواع الأعمال التجارية. لذلك، تهدف هذه الدراسة إلى دراسة ممارسات إدارة المخاطر في الخدمات المصرفية الإسلامية، باستخدام مصرف عجمان كدراسة حالة. المنهجية المستخدمة في هذه الدراسة نوعية تستند إلى مقابلات منظمة. ويستند التحليل إلى مقابلات وجهاً لوجه مع خمسة رؤساء الإدارات بما في ذلك إدارة الخدمات المصرفية للأفراد، وإدارة الرقابة الداخلية، وإدارة الشريعة، وإدارة الامتثال وإدارة المخاطر (السيولة). وتظهر النتائج أن بنك عجمان لديه أنشطة فعالة لإدارة المخاطر. قسم إدارة المخاطر يعرض الرقابة المناسبة للتخفيف من المخاطر والبنك وفقاً للأحكام الشرعية. بالإضافة إلى ذلك، تكشف النتائج أن البنك يمثل متطلبات بازل ولوائح مصرف الإمارات العربية المتحدة المركزي

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## **CHAPTER ONE: INTRODUCTION**

This chapter discusses the background and research of the topic questions. It covers the main concepts and aims of the study, and it outlines the objectives, and research questions. It also demonstrates the significance of the study in the context of previous experience and research.

Risk involves both susceptibility of asset values and chances of income growth. A significant element of management of risk is to comprehend the risk–return trade-off of different assets and investors. Investors can expect a higher rate of return only by increasing their exposure to risks. As the objective of Banks is to create value for the shareholders by obtaining assets in multiples of shareholder-owned funds, treatment the subsequent risks confronted by the equity converts an significant function of these institutions. As Islamic banking is comparatively new, the risks inherent in the instruments used are not well understood. Islamic banks can be predictable to face two types of risks risks that are similar to those faced by out-dated financial mediators and risks that are sole due to their compliance with the Shari'a. Likewise, Islamic banks are constrained in using some of the risk mitigation instruments that their conventional counterparts use as these are not allowed under Islamic commercial law. Will be discusses some of the unique risks that arise due to compliance with the shari'a and the special nature of risk mitigation obligatory on Islamic Bank by the shari'a mandate.

### **1.1 BACKGROUND**

The worldwide budgetary emergency of 2007, the Islamic fund industry has picked up

Significance as it gives another choice to broaden investible assets. The Islamic fund

Industry developed from having USD 150 billion in resources under administration in the mid-1990s to USD 1.3 trillion out of 2011. Around half of the absolute resources of the Islamic account industry is topographically focused, with an expected 47.06% of complete resources being held in Islamic banks in Middle East.

Islamic finance is developing inside worldwide fund. In its cutting edge structure, Islamic banking began with spearheading tests in the 1960 in Egypt. The Mit-Ghamr Islamic Saving Associations (MGISA) activated the reserve funds of Muslim speculators, giving them restores that didn't violate the laws of the Shari'ah. The MGISA pulled in a whirlwind of stores, which developed at the pace of in excess of 100 percent for each year in the initial three years of tasks. Afterward, the Pilgrims Fund Corporation (PFC) empowered Malaysian Muslims to spare continuously and put resources into Shari'ah-agreeable instruments, to help their uses during the Hajj time frame (journey). The Islamic finance industry has gained importance as it provides another alternative to diversify investible funds. The Islamic finance industry grew from having USD 150 billion in assets under management in the mid-1990s to USD 1.3 trillion in 2011. Around half of the total assets of the Islamic finance industry is geographically concentrated, with an estimated 47.06% of total assets being held in Islamic banks in the Middle East and Asia. Beginning in the mid-2000s, regulatory authorities in different jurisdictions started introducing and amending legislation to make the legal systems more supportive of the Islamic banking industry's growth. Besides, following the financial crisis, the increased interest surrounding Islamic banking has increased the level of awareness among investors, regulators and other stakeholders. As a result, assets under Islamic bank management and Islamic banking windows have grown at a compound annual growth rate (hereafter CAGR) of 40.3% between 2004 and 2011 reached USD1.1 trillion. The average return on equity for the top 20 Islamic banks was 12.6%, which is comparable to the 15% ROE of conventional banks. COMCEC, (2014).

In 2012, the PFC had 8,000,000 record holders and stores of more than \$12 billion. Officially, Islamic banking began in the late 1970s with a bunch of organizations and immaterial sums, however it has progressively become in the course of recent decades, with all out resources coming to about \$2 trillion at end-2014. Hussain, (2015).

The foundation of the Islamic Development Bank (IsDB) in 1975 was a turning point for Islamic banking, coming soon after the foundation of the primary major Islamic business bank—the Dubai Islamic Bank in the United Arab Emirates. The achievement of the last prompted the foundation of a progression of comparative banks, including Faisal Islamic Bank (Sudan) and Kuwait Finance House (Kuwait) both in 1977. As right on time as the late 1970s, steps were taken in Pakistan for making the money related framework agreeable with Shari'ah standards. Hussain, (2015).

The legitimate system was then changed in 1980 to take into consideration the activity of Shari'a compliant benefit sharing financing organizations, and to start bank money through Islamic instruments. Also, Iran authorized another financial law in August 1983 to supplant customary saving money with premium free banking. The law gave banks a window of three years for their tasks to get consistent with Islamic standards. Sudan's endeavours to adjust its whole financial framework to Shari'ah standards started in 1984. The monetary framework, including guidelines setting and administrative organizations, has additionally been getting up to speed with the quick development of Islamic financing. Global standard-setting organizations were built up to guide the tasks of the business around the globe, in spite of the fact that institutionalization of Islamic items crosswise over various nations stays a test. Since 1991, the Accounting and Auditing Organization for Islamic Financial Institutions, Hussain, (2015).

(AAOIFI), situated in Bahrain, has been giving bookkeeping, reviewing, and Shari'ah models for budgetary detailing at Islamic money related establishments. The Islamic Financial Services Board (IFSB), built up in 2002 in Malaysia, is answerable for giving supervisory and regularity IMF, models and rules. It additionally advances the appropriation of these models and rules by significant administrative specialists. In 2001, the International Islamic Financial Market (IIFM) in Bahrain was ordered to create rules for the issuance of Islamic budgetary instruments

and to empower dynamic optional market exchanging. Most as of late in 2010, the Malaysia-based International Islamic Liquidity Management Corporation (IILM) began giving present moment Shari'ah-agreeable money related instruments to encourage cross-outskirt Islamic liquidity the board. Hussain, (2015).

This paper is for the most part expected to give a review of key arrangement issues and difficulties confronting professionals and strategy producers. It gives a review of Islamic account, examines key macroeconomic ramifications from its extension over the globe, and gives an expansive point of view on key components of Islamic fund and banking. Rather than investigating profoundly a couple of questionable issues or acquainting new arrangements with current difficulties in Islamic fund, it attempts to give a general diagram of the Islamic money industry which, as a moderately new part of account, is frequently hard to comprehend and inclined to being misconstrued. While Islamic money has extended past Muslim-larger part nations, arriving at Europe and Sub-Saharan Africa, Shari'ah-consistent budgetary resources stay amassed in Iran, Malaysia, and a couple of Gulf Cooperation Council (GCC) nations, where it has gotten fundamental. The paper raises various strategy related inquiries, yet much of the time, it will concede the gritty responses to other, companion papers.

The primary objective of the research is to examine the risk management practices in Islamic banks with reference to Ajman Bank. Risk management practices is not only one of the crucial areas in finance but also one of the least studied areas especially in Islamic finance. The operational risk plays an important role in the profitability of the banks (Vanini and Leippold, 2005) due to the avoidance of any withdrawal risk and reputational risk. The Islamic banks that have better operational risk management are able to avoid any unexpected loss due to failure in operations, internal control and systems. Well-developed internal control procedures enable the Islamic banks to efficiently process the financing to generate more profits.

Ajman Bank is a keystone in Ajman's economic development strategy and in a position to benefit from the Emirate's growth and potential like no other. Ajman Bank is committed to becoming a sustainable organization in its truest sense, balancing care for the community and employees with the business of delivering value to its shareholders and customers. Ajman Bank growth in the profit from year to year since the bank opened ([www.ajmanbank.ae](http://www.ajmanbank.ae)).

## **1.2 AIM AND OBJECTIVES OF THE STUDY.**

The purpose of this study is to examine the nature of the risk management practices of Islamic banks, and aim to avoid any and all excessive risk. The case of Ajman Bank. This study likewise discovers the differences in risk management practices as per the Islamic finance products provided by Ajman Islamic Bank. The study will effort to achieve the resulting objectives:

Objective 1: Identify the various types of risk management and type of risk in Islamic banks.

Objective 2: Analyse the bank's products risk such as Murabaha , Mudaraba, Ijarah, Trade Finance, Sharia , Compliance , Liquidity. Operational, Price, Credit, Market. Price , Settlement , profit with risk of loss ,Investment , Salam , Istisna'a , Sukuk ,Financial Crime and money laundry risks

Objective 3 : To investigate the relationship between the risk management and performance of in the banks.

Objective 4: Provide recommendations for the bank to mitigate risk

Objective 5: Assist the bank to avoid regulatory impact and losses

## **1.3 SIGNIFICANCE AND MOTIVATION OF THE STUDY**

There is lack of studies that examine risk management practices in Islamic banks in the UAE.

And to provide the banks Management with the information in which risk affect the

Organization and the requirements of avoiding and mitigate risk The research structure will be including the research as the literature review which will provide the different views and research results from the previous study, moreover, to identify the process of the research that it will be taken in consideration. Then the part of the research methodology which will describe the research methodology in details., and to discuss the risk with the bank department head and to analysis the results based on the interview. The last chapter will be writing the recommendation for the research and conclusion to how we mitigate and avoiding the risks in bank.

## **1.4 GLOBAL INDUSTRY OUTLOOK**

First Islamic Bank in world started in Dubai in 1975. Nearby more than 500 Islamic Financial Institutions around the global

Global industry size around \$1.5 trillion.

Expected to double in in just five years.

The global Sukuk market-Sukuk outstanding around —\$324.7bn.

Global assets under management (AUM) in Islamic funds currently stand at US\$60 Billion with more than 800 funds.

## **1.5 UNITED ARAB EMIRATES OUTLOOK**

UAE is the second largest Islamic banking market after Malaysia. Expected to reach \$262 billion worth by 2019. Islamic banking dissemination in the UAE currently stands around 20 per cent. Represents a 14 per cent portion of the global market. The industry in the UAE is growing at over twice the rate of conventional banking.

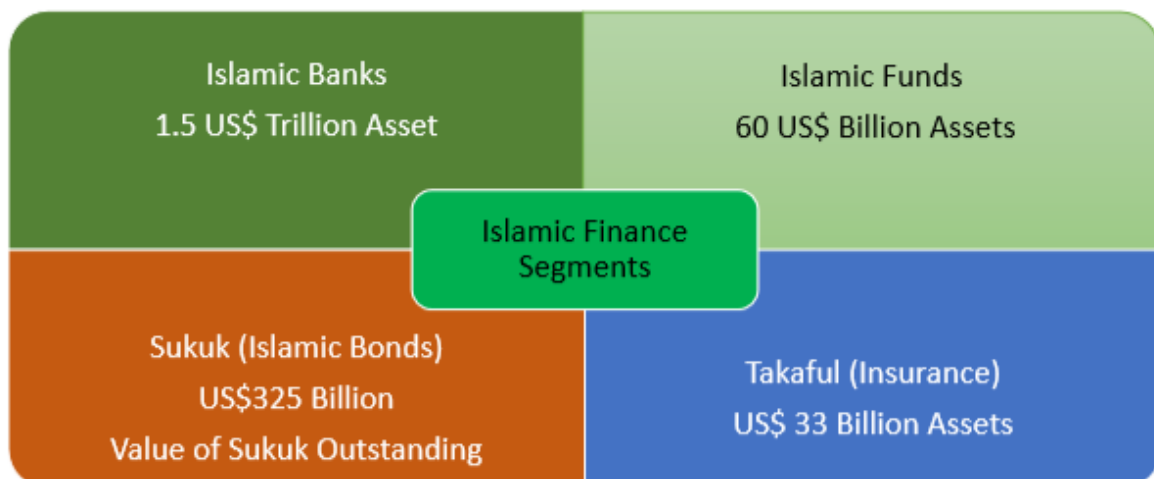
Both the Islamic finance and conventional banking industries in the United Arab Emirates

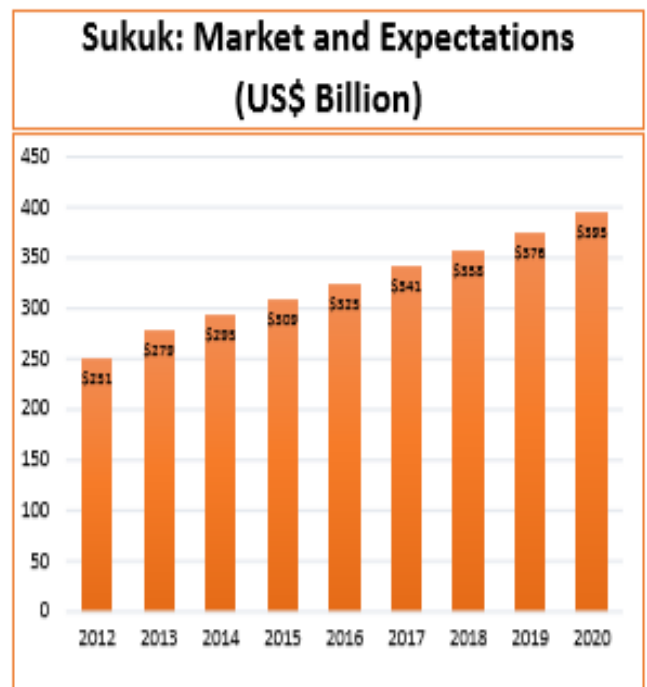
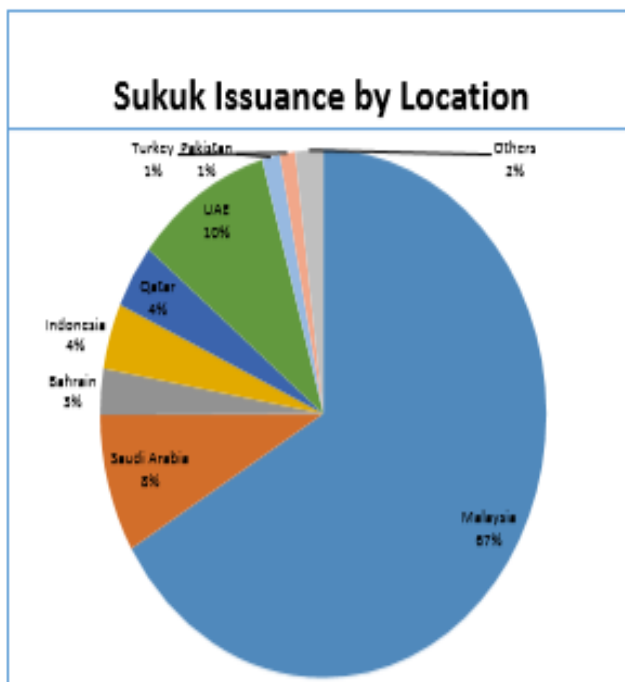
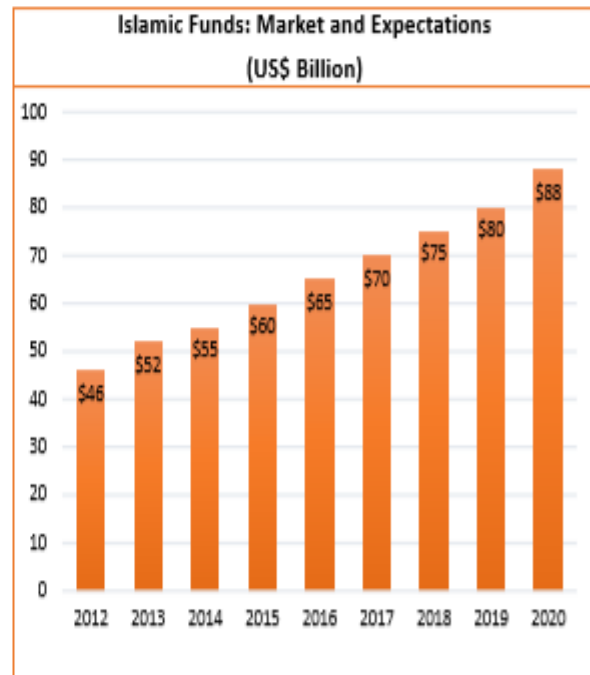
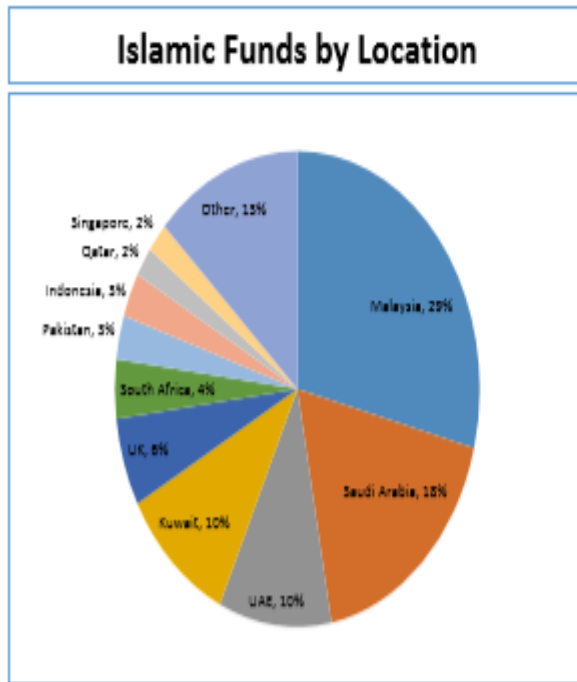
(UAE) are governed by the Central Bank of United Arab Emirates (CBUAE), established by the Central bank under the Union Law No.10 of 1980. In addition, Islamic financial institutions in the U.A.E. are required to comply the following laws:

Islamic Banking Federal Law No.6 of 1985, which establishes the legal foundations for Islamic banks  
Capital Market The Federal Law No.4 of 2000

## **TAKAFUL**

The Federal Law No. 6 of 2007. After which, a new insurance/Takaful Law was passed in 2010 to regulate the Takaful industry further.





**IFSB:** The Islamic Financial Services Board is a universal standard-setting association that advances and improves the sufficiency and strength of the Islamic money related administrations industry by giving worldwide prudential gauges and core values for the



business, comprehensively characterized to incorporate banking, capital markets and protection segments. **IFSB , 2018**

**IIFM:** Universal Islamic Financial Market is a standard-setting body of the Islamic Financial Services Industry (IFSI) concentrating on institutionalization of Islamic budgetary agreements and item formats identifying with the Capital and Money Market, Corporate Finance and Trade Finance portions of the IFSI. **IFSI, 2018.**

## **1.6 ISLAMIC BANKING REGULATION- THE UAE LEGAL FRAMEWORK: -**

The Religious Supervisory Board, or “Shari’ah Board” contain of scholars of the Islamic law, who achieve the purpose of independent advisors in advising Islamic banks on whether their transactions are in accordance with shari’ah rules. The role of the Board includes but not limited to the following: Supervise the shari'ah compliance of all the transactions in the bank. Analyse, advise and direct the bank on day-to-day emerging situations reported by different departments, branches or customers to safeguard Shari'ah compliance. Supervise and approve the development of Shari’ah compliant procedures. Certify Shari'ah compliance of bank's product documents, contracts and agreements. Islamic Finance A UAE Legal Perspective, 2019.

## **1.7 THE DIFFERENCE BETWEEN ISLAMIC AND CONVENTIONAL BANK.**

One key qualification is that regular banks get their money by charging premium and costs for organizations, however Islamic banks obtain their money by advantage and incident sharing, trading, leasing, charging charges for organizations rendered, and using other sharia understandings of exchange. Albeit Islamic business banks have various things like those

offered by standard banks, the two components differ sensibly. One key difference is that standard banks gain their money by charging premium and costs for organizations, while Islamic banks secure their money by advantage and adversity sharing, trading, leasing, charging costs for organizations rendered, and using other Sharia understandings of trade (Jamaldden, (2019)).

In Islamic banking source of the fund Current Accounts; deposits are guaranteed by the bank but earn no income. Profit Sharing Accounts: Depositors share the risk and return with the bank. Returns are not guaranteed; depends on the bank's performance. And the uses of fund The bank shares the earning risk in equity-based contracts and take credit and transaction risks on other contracts, without the use of conventional hedging instruments. While in conventional bank The bank takes all the risks and guarantees the deposits and a pre-specified return. And the Financing is debt-based.

The object must be lawful from the Sharia's perspective. The object must be legally owned by the parties to a contract. The object must be either in existence at the time of contract or deliverable. The object must be determined precisely as to its essence, its quantity, and its value. Deception is not allowed The price must be lawful in nature The price is known to both the parties to avoid any dispute. The subject of sale must be in the possession of the seller at the time of sale. (Jamaldden, (2019)).

## **1.8 RESEARCH QUESTIONS**

- What risks identify belong to the bank department?
- What is the level of risk identification, assessment, analysis and monitoring and controlling within the short time?
- What is the recommendation to be the bank in line with the regulation to avoid the department risks?

## **CHAPTER TWO: LITERATURE REVIEW**

The issuance of the amended Basel II system for bank capital ampleness not just improves the risk affectability and precision of the criteria for evaluating capital sufficiency, yet it is on a very basic level about more grounded and increasingly successful risk the executives grounded in sound corporate administration and upgraded budgetary divulgence. I ought to recognize that the exceptional highlights of Islamic banking may not generally be enough tended to by wide universal benchmarks for traditional banking contained in the Basel II structure. In any case, the IFSB considers cautiously the worldwide financial benchmarks that have been and are being produced for traditional banking. The IFSB's capital ampleness standard, for example, attracts to a huge degree on Pillar 1 of the Basel II system (the base capital sufficiency prerequisites). It has likewise discharged a presentation draft on the supervisory survey process (steady with the standards of Basel's Pillar 2) and another on revelation and market discipline (Pillar 3). Knight, (2007).

Al Tamimi (2002) investigated the degree to which the UAE commercial banks use risk management techniques in dealing with difference types of risks, and The study found that the UAE commercial banks were mainly facing credit risk. The study also found that inspection by branch managers and financial statement analysis were the main methods used in risk identification. The main techniques used in risk management according to this study were establishing standards, credit score, credit worthiness analysis, risk rating and collateral; the study also highlighted the willingness of the UAE commercial banks to use the most sophisticated risk management techniques, and recommended the adoption of a conservative credit policy as per Ayub , 2007 in regards to the area specific tools (deposit, investment and other products), there are multiple uses of an Islamic mode to meet different banking needs (summarized mainly from Ayub 2007; Kettell, 2011).

In regard to deposit products of Islamic banks, generally, no return is given on current accounts (based on Al-Wadeeah principle) on the grounds that such deposits take the form of current deposits given to Islamic banks and the idle deposits cannot carry any return. They are kept as Amanah; but if the proceeds of such accounts are used by banks in their business, bank has to take permission of the depositor, and then they are treated as investments of the bank which has no bearing on any increase or decrease. All remunerative deposits in Islamic banks, including saving deposits against which banks provide checking facility, is accepted on Mudaraba or a profit and loss sharing (PLS) basis. The profit distribution ratio between the bank and the depositor shall be agreed upon at the time of account opening subject to the condition of the Sharia.

As per the case study According to El-Gamal (2001), the central concept in Islamic banking and finance is justice, which is achieved mainly through the sharing of risk; and stakeholders are supposed to share profits and losses. While justice stems usually from a religious or ethical basis, ethical finance is not a new concept. As Subbarao (2009) noted, people often forget that the godfather of modern capitalism, and often called the first economist, Adam Smith was not an economist, but rather a professor of moral philosophy. Smith had a profound understanding of the ethical foundations of markets and was deeply suspicious of the “merchant class” and their tendency to arrange affairs to suit their private interests at public expense. In short, Smith emphasized the ethical content of economics, something that got eroded over the centuries as economics tried to move from being a value-based social science to a value-free exact science (Subbarao (2009)).

An effective internal control system requires that the material risks that could adversely affect the achievement of the bank's goals are being recognised and continually assessed. This assessment should cover all risks facing the bank and the consolidated banking organisation (that is, credit risk, country and transfer risk, market risk, interest rate risk, liquidity risk, operational risk, legal risk and reputational risk). Internal controls may need to be revised to appropriately address any new or previously uncontrolled risks , Basle, (1998).

Effective risk assessment identifies and considers internal factors (such as the complexity of the organisation's structure, the nature of the bank's activities, the quality of personnel, organisational changes and employee turnover) as well as external factors (such as fluctuating economic conditions, changes in the industry and technological advances) that could adversely affect the achievement of the bank's goals. This risk assessment should be conducted at the level of individual businesses and across the wide spectrum of activities and subsidiaries of the consolidated banking organisation. This can be accomplished through various methods. Effective risk assessment addresses both measurable and non-measurable aspects of risks and weighs costs of controls against the benefits they provide Basle, (1998).

According to (Khalid & Amjad, 2012) The risk management theory describes the term 'risk management' as "a method through which decisions are made; a process conducted on two steps: (1) to identify the origin and causes of risks, and (2) to develop ways to assess risks by means of mathematical models" (Khalid & Amjad, 2012)

Linbo Fan (2004) found that profit efficiency is sensitive to credit risk but not to insolvency risk or to the mix of loan products. Hahm (2004) argues that it is necessary to improve banking supervision and banks' risk management to ensure successful financial liberalization. This is based on a study of interest rate and exchange rate exposure of Korean banks before the 1997

Asia Pacific economic crisis, which found that the performance of commercial banks was significantly associated with their pre-crisis risk exposure. Fatemi and Fooladi (2006), after investigating the current practices of credit risk management in the largest US-based financial institutions, report that identifying counterparty default risk is the single most important purpose served by the credit risk models utilized. However, it should be noted that these results are based on a very low response rate, i.e. 21 responses to questionnaires sent to 100 banks.

As enthusiasm for Islamic money develops, the significance of the IFSB's job increments. The significance of the key components of banking - traditional or Islamic - can't be accentuated enough. Subjects, for example, corporate administration, hazard the executives and capital sufficiency are key components that support sound monetary practices. The direction gave by the IFSB in these zones guarantees that there are strong monetary market frameworks and hearty center money related foundations working as per free from any potential harm hazard the board rehearses. It is significant that a similar level of supervisory oversight is applied to Islamic monetary organizations, to guarantee the proceeding with acknowledgment of their instruments and administrations in global markets and traditional financial frameworks. Furthermore, the core values and gauges created by the IFSB are helping managers all-inclusive to all the more likely comprehend and oversee organizations giving Islamic money related administrations. Knight, (2007).

However, that as it may, there is developing piece of the pie and rising local fundamental significance of Islamic money which underscores the significance of creating solid administrative structures for prudential guideline and supervision in Islamic account locales, upheld by proactive pressure testing and an upgraded set of capacities for macro prudential observation. In accordance with its order, the IFSB has reacted on a number of fronts to such worldwide advancements with a progression of cutting edge prudential norms what's more, core values that adjust worldwide administrative structures with the specificities of Islamic

fund. Beside Standards and Guidance/Technical Notes, the IFSB Work Plan as of late has additionally included working papers on various subjects of rising issues in Islamic money including budgetary wellbeing nets, customer security, Shari'ah resistance risk, goals and recuperation systems, fundamental connections and macro prudential issues, etc. Going ahead, alongside fortifying its measures execution program by including effect and consistency evaluation measurement, the IFSB will keep on creating new guidelines and core values for covering all divisions of IFSI. IFSB , (2018).

risk is characteristic in any business undertaking, and great risk management is a fundamental part of maintaining a fruitful business. An organization's administration has changing levels of control as to risk. A few dangers can be legitimately overseen; different dangers are to a great extent outside the ability to control of organization the executives. Here and there, the best an organization can do is attempt to foresee potential dangers, evaluate the potential sway on the organization's the same old thing and be set up with a plan to respond to unfriendly occasions. There are numerous approaches to order a bank money related dangers. One approach for this is given by isolating money related chance into four general classifications market risk, credit risk, liquidity risk, and operational risk. Maverick , (2019).

Market risk includes the risk of changing conditions in the particular bank where an organization seeks business. One case of market risk is the expanding propensity of buyers to shop on the web. This part of market chance has displayed critical difficulties to customary retail organizations. bank that have had the option to cause the essential adjustments to serve an internet shopping open to have flourished and seen significant income development, while organizations that have been delayed to adjust or settled on awful decisions in their response to the changing market place have fallen by the wayside. This model likewise identifies with another component of market chance the risk of being defeated by contenders. In an undeniably aggressive worldwide commercial center, frequently with narrowing overall revenues, the most



monetarily fruitful organizations are best in offering a remarkable incentive that makes them stand apart from the group and gives them a strong commercial center personality. Credit risk is the hazard organizations acquire by stretching out credit to clients. It can likewise allude to the organization's own acknowledge chance for providers. A business goes for broke when it gives financing of buys to its clients, because of the likelihood that a client may default on instalment. An banks must deal with its very own credit commitments by guaranteeing that it generally has adequate income to take care of its records payable tabs in a convenient manner. Something else, providers may either quit stretching out credit to the organization, or even quit working with the organization inside and out. Maverick , (2019).

Liquidity risk incorporates resource liquidity and operational financing liquidity chance. Resource liquidity alludes to the relative simplicity with which an organization can change over its advantages into money ought to there be an unexpected, generous requirement for extra income. Operational financing liquidity is a reference to day by day income. General or occasional downturns in income can display a considerable risk if the organization abruptly ends up without enough money close by to pay the essential costs important to keep working as a business. This is the reason income the executives is basic to business achievement—and why examiners and financial specialists take a gander at measurements, for example, free income when assessing organizations as a value speculation. Operational Risk allude to the different risk that can emerge from an banks customary business exercises. The operational risk classification incorporates claims, extortion chance, work force issues, and plan of action chance, which is the risk that an organization's models of showcasing and development plans may demonstrate to be erroneous or deficient. Maverick , (2019).

In 2001 Banque du liban (BDL) gave handouts that manage the methods by which banks and money related establishments control their tasks with their clients so as to stay away from any contribution in activities identified with money laundry or fear based oppressor financing.

Executing the idea of the risk based methodology, BDL expects banks to receive a risk based approach in characterizing clients and activities as per the hazard levels (low, medium or high dangers), considering the nation dangers, client dangers and administrations risk. It additionally mentioned the foundation of risk based control measures and systems. In the extent of risk the executives, the stage was set through setting up chance strategies and checking. Charafeddine, (2015).

In 2011, each bank working in Lebanon was mentioned by BDL to set up consistence and risk. The executive's units and to select autonomous individuals in their Board of Directors. These units incorporate an AML and Countering Financing of Terrorism (CFT) Special Committee, an AML/CFT Compliance Unit (accountable for confirming consistence with AML/CFT systems, laws, and guidelines in power), and an AML/CFT Branch Official in every one of the bank's offices accountable for controlling the activities. Also, BDL requires banks and budgetary organizations working in Lebanon to carefully actualize the Regulations for the Control of Financial and Banking Operations for Fighting Money laundry and Terrorist Financing, especially with clients who demand the lead of cross border tasks by method for reporter banks and monetary establishments. It stipulated that banks what's more, monetary foundations ought to pursue a hazard based methodology by checking the personality of people or on the other hand organizations engaged with the exchange and those that have financial proprietorship, just as by creating methods to constantly screen the related activities and records. Inside this extension, banks and budgetary organizations must receive the most extreme exactness and due persistence to the character of

the monetary right proprietor in the activities directed. Banks are mentioned to refresh their database identified with AML/CFT data and to inform the SIC about suspicious exchanges. So as to further heighten the lawful part of consistence and hazard the executives, BDL have

mentioned in 2013 banks and money related foundations working in Lebanon to set up a Legal Compliance Unit that is in charge of recognizing and averting legitimate dangers, taking the necessary measures to alleviate these risk. Charafeddine, (2015).

The Basel Committee's Standards Implementation Group, through its Operational risk Subgroup (SIGOR), has concentrated on the functional difficulties related with the improvement, usage and upkeep of an operational risk (OR) the board and estimation structure that meets the necessities of Basel II,<sup>1</sup> especially as they relate to the Advanced Measurement Approaches (AMA). The SIGOR's command incorporates Recognizing and taking part in settling the useful difficulties related with the Effective advancement, usage and support of an AMA system. BCBS, (2011).

Predictable with this command, this paper distinguishes supervisory rules related with the advancement and support of key inward administration, information and demonstrating structures hidden an AMA. Since operational risk is a developing order, this paper is proposed to be an evergreen report, and as further issues are recognized and desires for assembly towards a smaller scope of proper practices are built up, these too will be added to this record. This paper doesn't decrease or override the watchfulness of national directors to act in a way that is reliable with their specific administrative methodologies. All things considered, the production of this paper is planned to encourage a combination of training by banks as well as national directors. BCBS, (2011).

Project Risk Management isn't a discretionary movement it is basic to fruitful undertaking the executives. It ought to be applied to all tasks and subsequently be remembered for venture plans and operational reports. Along these lines, it turns into a basic piece of each part of dealing with the task, in each stage and in each procedure gathering. Project Management Institute, (2009). Huge numbers of the task the board forms address arranging the project, from

idea to final plan and from acquisition through every day the executives of execution and close-out. These procedures regularly expect a ridiculous level of sureness about the task and, in this way, they have to incorporate treatment of undertaking risk. Project Management Institute, (2009). Project Risk Management tends to the vulnerability in project appraisals and suppositions. Along these lines, it expands upon and broadens other task the board forms. For example, venture planning gives dates and basic ways dependent on action term and asset accessibility thought to be known with conviction. Quantitative chance examination investigates the vulnerability in the assessed length and may give elective dates and basic ways that are progressively practical given the risk to the project. Project Management Institute, (2009). Project Risk Management is definitely not a substitute for the other undertaking the board forms. Despite what might be expected, Project Risk Management necessitates that these venture the board forms (for example planning, planning, and change the executives) be performed at the degree of the accepted procedures accessible. Project Risk Management includes the point of view of task risk to the yields of those different procedures and adds to their incentive by considering. For example, chance administration gives the premise whereupon to gauge the measure of cost and calendar possibility saves that are expected to cover chance reaction activities to a necessary degree of confidence for meeting project targets. PMI, (2009).

The European Central Bank's Banking Supervision arm has distributed the 2020 supervisory needs of the Single Supervisory Mechanism and a risk assessment for 2020. ECB Banking Supervision has recognized the accompanying dangers to the euro banking part: monetary, political and obligation support ability challenges in the euro territory; plan of action manageability; digital wrongdoing execution chance identified with banks' procedures for non-performing advances; facilitating loaning principles; repricing in budgetary markets; offense,

illegal tax avoidance and fear mongering financing; Brexit; worldwide standpoint and geopolitical vulnerabilities; response to guideline; and environmental change related risk.

Bank Prudential Regulation & Regulatory Capital, (2019).

Risk management involves assessing and quantifying business risks, then taking measures to control or reduce them. Risk is seen as the probable loss of income and assets' value. Only unexpected losses are included and expected losses are not included in the definition of risk.

Besides common risks encountered by the conventional banks Islamic banks exposed to some additional types of risks: investment return risk shari'ah compliance risks. Reputational risk; failures in governance, business strategy and process.

## **2.1 TYPE OF RISK:**

Following the Type of risk definition and taken from different resources covering the bank risk.

## **2.2 RISK ASSESSMENT**

Examiners assess risk via its impact on capital and income for managing viewpoint, chance is the conceivable that procedures, expected or unforeseen, may affect the account organization's capital or income. The basic presence of hazard isn't really explanation behind concern. To place hazards in context, inspectors ought to choose if the dangers an account organization is attempted are justified. For the most part, dangers are justified when they are reasonable, quantifiable, controllable, and inside the fund bank ability to promptly withstand unfriendly execution. In the event that inspectors decide dangers are ridiculous, these are consolidated in the assessment report and the fund organization's administration is in like manner encouraged to relieve or dispose of the baseless dangers. Fitting activities for the account organization may incorporate decreasing exposures, expanding capital, or reinforcing hazard the executives

forms. Finding out the degree of characteristic hazard is an informed decision in the wake of surveying and gauging all the variables and assessment criteria for every one of the inalienable dangers. For instance, if the advantage quality

of the advance portfolio being evaluated has weakened to a not exactly acceptable rating with a significant level of grouped credits, the degree of natural credit hazard will presumably be appraised as high.

## **2.3 INHERENT RISK**

Inherent risk is the risk presented by a mistake or oversight in a budget summary because of a factor other than a disappointment of inside control. In a money related review, innate risks are destined to happen when exchanges are mind boggling, or in circumstances that require a high level of judgment with respect to monetary evaluations. This sort of hazard speaks to a most dire outcome imaginable in light of the fact that every single interior control set up has in any case fizzled.

Intrinsic chance is one of the dangers examiners and investigators must search for while inspecting fiscal summaries, alongside control hazard and location chance. When leading a review or investigating a business, the evaluator or investigator attempts to increase a comprehension of the idea of the business while inspecting control dangers and intrinsic dangers. In the event that characteristic and control dangers are viewed as high, an inspector can set the location hazard to an acceptably low level to keep the general review chance at a sensible level. To bring down identification chance, a reviewer will find a way to improve review systems through focused review determinations or expanded cases sizes.

Tuovila, (2019).

Organizations working in profoundly directed areas, for example, the budgetary division, are bound to have higher characteristic hazard, particularly if the organization doesn't have an

inward review office or has a review office without an oversight advisory group with a money related foundation. A definitive hazard presented to the organization likewise relies upon the money related introduction made by the inalienable hazard if the procedure for representing the presentation fizzles. Complex monetary exchanges, for example, those embraced in the years paving the way to the money related emergency of 2007-2008, can be hard for even the keenest budgetary experts to get it. Resource sponsored protections, for example, collateralize obligation commitments (CDOs), got hard to represent as tranches of differing characteristics were repackaged over and over. This intricacy may make it hard for an inspector to make the right assessment, which thusly can lead speculators to believe an organization to be more monetarily stable than in fact. Tuovila\_, (2019).

#### **2.4 MARKET RISK:**

Market risks the plausibility of a speculator encountering losses due to variables that influence the general execution of the monetary markets where the individual in question is included. Market chance, likewise called "methodical risk," can't be killed through enhancement, however it tends to be supported against in different manners. Wellsprings of market risk incorporate downturns, political unrest, changes in loan costs, cataclysmic events and psychological oppressor assaults. Deliberate, or advertise chance will in general impact the whole showcase simultaneously. Chen , (2018)

This can be appeared differently in relation to unsystematic risk, which is interesting to a particular organization or industry. Otherwise called "nonsystematic chance, "explicit chance, diversifiable risk or residual risk, with regards to a venture portfolio, unsystematic risk can be diminished through broadening. Chen , (2018).

#### **2.5 RATE OF RETURN RISK:**

Rate of return risk emerges due to surprising changes in the market pace of return, which antagonistically influence a company's income. In a traditional monetary establishment, returns are fixed; both the firm and store suppliers know ahead of time what their profits will be. In Islamic firms, returns are questionable and financial specialists share the two profit and loss with the bank. Jamaldeen, (2019).

## **2.6 LIQUIDITY RISK:**

liquidity is a bank's capacity to meet its money and collateral commitments without supporting inadmissible misfortunes. Liquidity chance alludes to how a bank's powerlessness to meet its commitments (regardless of whether genuine or saw) compromises its money related position or presence. Liquidity risk the board incorporates the procedures and systems a bank uses to Survey its capacity to meet its income and guarantee needs (under both typical and focused on conditions) without negatively affecting everyday tasks or its general money related position. Alleviate that risk by creating procedures and taking fitting activities intended to guarantee that fundamental assets and security are accessible when required. Hronec, (2019).

## **2.7 OPERATIONAL RISK:**

Operational risk is the risk of misfortune upcoming about because of insufficient or bombed inner procedures, individuals, and framework or from outer occasions. Operational hazard is related with human blunder, framework disappointments and deficient strategies and controls. It is the risk of misfortune emerging from the potential that deficient data framework; innovation disappointments, ruptures in inner controls, misrepresentation, unanticipated fiascoes, or other operational issues may bring about sudden misfortunes or notoriety issues. Operational chance exists in all items. BCBS, (2011).



## **2.8 REPUTATION RISK:**

Is a risk or threat to the great name or remaining of a business or element. reputational risk can happen that legitimately, as the aftereffect of the activities of the organization itself. By implication, because of the activities of a worker or representatives. Extraneously, through other fringe parties, for example, joint endeavor accomplices or providers. Kenton, (2019).

## **2.9 LEGAL RISK:**

Legal risk chance the board as a control is a moderately better approach for deduction for some in-house lawful groups. The developing desire in the money related administrations industry from different offices and controllers is that Legal gets expressly associated with formal risk the board forms. When characterizing legitimate risk which has been surrounded as reputational sway, working or monetary misfortunes and issues influencing the association's capacity to work together unmistakably Legal needs to accomplish more than the "normal everyday employment" to distinguish, oversee and moderate lawful risk. Guerra, (2019).

## **2.10 STRATEGIC RISK:**

strategic risk the executive's system reliable with the direction set down in the module, and guarantee that their structure is comparable with the nature, size and intricacy of their business and is proper for their individual conditions and needs. AIs won't be blocked from embracing elective methodologies on the off chance that they can fulfil the Hong Kong Monetary Authority (HKMA) that such approaches satisfy comparative hazard the board purposes. Perceiving that improving vital hazard the executives is a progressing procedure, the HKMA won't require existing AIs to meet all prescribed hazard the board rehearses following the

module is given. In any case, they are relied upon to distinguish regions where such practices ought to be applied to their vital hazard the executive's system, and gain consistent ground towards applying them inside a sensible time span. The HKMA will screen their advancement in improving such structure and consider the advancement accomplished in deciding its supervisory needs. HKMA, (2007).

## **2.11 COMPLIANCE RISK:**

Is the risk of legitimate or administrative approvals, material monetary misfortune, or misfortune to notoriety a bank may endure because of its inability to conform to laws, guidelines, rules, related self-administrative association norms, and sets of accepted rules pertinent to its financial exercises. Then again, a viable procedure would distinguish consistence chances in every business line, item and procedure, and devise approaches to relieve such chances. The procedures and prerequisites ought to be appropriately reported with a rundown of do's and don'ts going with the equivalent. The examples of inability to hold fast to appropriate direct ought to be changed over into contextual investigations and dispersed among the staff for instruction and entrenchment of wanted frames of mind.

Banks ought to shun the inclination to treat consistence just as cost and ought to perceive that appropriate lead spares the bank from conceivable reputational misfortune and punishments subsequently, creates shrouded profit which most banks don't evaluate, and thus don't understand. A poor consistence culture may prompt substantial expenses to the banks. All inclusive, from the earliest starting point of the money related emergency and until 2020, punishments and fines on banks is are relied upon to top USD400 bn. Quinlan and Associates, a Hong Kong-based budgetary administrations consultancy assessed that terrible conduct had eradicated \$850 billion in benefits for the best 50 worldwide banks since the 2008 money related emergency as compose downs, exchanging misfortunes, fines and higher

consistence costs<sup>3</sup>. From June 2018 to July 2019, the Reserve Bank has forced money related punishments on 76 events adding up to ₹ 122.9 crore on different business banks working in India. Notwithstanding, dread of fines and punishments won't be sufficient to stay aware of the advancing idea of guidelines. However, a budgetary administration framework with worked in charge makes consistence an ordinary practice that empowers the association to work at more prominent effectiveness. What's more, stable administration makes favorable condition for the estimations of consistence, uprightness, trust, and regard for the law; to flourish in the association's way of life. Thus, a bank can enable its whole association to work with obligation while keeping up the adaptability important to remain in front of consistently advancing guidelines and business challenges.

## **2.12 FOREIGN EXCHANGE RISK/CURRENCY RISK:**

The risk characteristic in remote trade business, especially in running open outside trade positions, have been elevated lately by the expanded insecurity of trade rates. Therefore, the checking of these dangers has become a matter of expanded enthusiasm to supervisory specialists. BIS, (1980). The motivation behind this note is to think about the prudential parts of banks' outside trade exercises. It isn't straightforwardly worried about the limitations that nations may put on their banks' outside trade business for trade control, financial or other full scale monetary reasons. In practicing prudential power over this zone of banks' exercises, nonetheless, supervisory specialists need to consider the job of the banks as "showcase producers" in remote trade. This job has two viewpoints. Right off the bat, banks need to cite rates to their clients (counting different banks) at which they stand prepared to purchase and sell monetary forms. Furthermore, independent from anyone else taking open situations in monetary standards, banks (just as non-banks) help to guarantee that the remote trade markets

are adjusted anytime of time without over the top and unpredictable conversion scale changes. At the end of the day, administrators need to weigh prudential contemplation against the need to empower the banks to have their influence in the smooth and productive working of the trade markets. Whatever might be the definite parity struck between these contemplation's, supervisory specialists must look to guarantee that the dangers expected by banks in their outside trade tasks are never so enormous as to establish a critical risk either to the dissolvability and liquidity of individual banks, or to the wellbeing and security of the financial framework overall. BIS, (1980).

### **2.13 PROFIT WITH RISK OF LOSS**

Profit and Losses Sharing (PLS) includes specificities in the Islamic bank liquidity issue. Utilizing hypothetical-deductive strategy, this paper attempts to look at whether the participative intermediation is answerable for high composition to liquidity deficiency or prompts less article to liquidity hazard. Seeing development change, we presume that PLS between intervention prompts a more piece to liquidity hazard since Islamic banks regularly use short-term stores to permit financing of Musharaka and Mudarabah at long haul. Be that as it may, for the hazard change, the PLS instrument between the banks and its contributors from one viewpoint and the bank and business people then again, allows less composition to liquidity chance. The participative entomb intercession appears to produce a constrained liquidity work and is portrayed by less cash creation. This suggests it is basic to fortify the obligation the executives of liquidity chance. By and by, the effect of PLS between intervention on liquidity hazard is impacted by the level of advancement of Islamic currency advertise and the presence of Islamic loan specialist finally resort. Hamza, (2014).

## **2.14 CREDIT RISK**

During the era of conventional bank practice, various credit risk alleviation strategies and instruments have been created and the procedure of their development, because of consistent changes in the financial business, is proceeding. Islamic banks, be that as it may, have not yet figured out how to create bona fide, Sharia adequate credit hazard the board procedures to the degree adequate to address their issues. In this way, they are frequently compelled to utilize ordinary systems, whose predictable application in Islamic banking, because of the Sharia rebelliousness of specific procedures or the manner by which they are executed in regular banking, is very restricted. In this paper, we will break down the ordinary credit chance administration and relief methods and their pertinence in Islamic banking, the credit hazard the board rehearses in Islamic banks, the accomplished outcomes and variables that impact the development and force of credit risk in Islamic banking. Lekpek, (2018).

## **2.15 INVESTMENT RISK:**

To make an incentive for their members, senior administration and sheets of chiefs at Islamic monetary establishments must find a way to deal with their novel dangers. Islamic monetary establishments face a few hazards that ordinary money related firms don't, including value venture chance, uprooted business chance, pace of return hazard, and sharia resistance risk. Islamic budgetary firms offer instruments dependent on value speculations. The two agreements for the most part utilized for these instruments are mudaraba (organization) and Musharaka (joint endeavor association). Value speculation chance emerges due to a potential abatement in the reasonable estimation of the value position held by the Islamic firm. A company's value interest can go from direct interest in undertakings or joint adventure organizations to roundabout sharia-agreeable speculation, for example, in stocks. On the off

chance that the firm faces a decrease in the estimation of its value position, it can lose any potential profit for its ventures and may even lose its contributed capital. This circumstance can trigger extra issues, for example, credit risk and liquidity risk. The Islamic firm can attempt to lessen value chance by examining certain key elements, including the accompanying, before entering an agreement: The foundation and marketable strategy of the overseeing accomplice or supervisory group The anticipated lawful and financial condition wherein the task will happen. Jamaldeen ,(2019).

## **2.16 MURABAHA**

Murabaha is a type of offer where the expense of the products to be sold just as the benefit on the deal is known to the two gatherings. The buy and selling cost and the overall revenue must be unmistakably expressed at the hour of the deal understanding. Installment of the Murabaha cost might be in spot, in portions or in singular amount after a specific timeframe. Murabaha has been received as a method of premium free financing by an enormous number of Islamic banks to back the acquisition of the purchaser merchandise, middle person or capital products, land, crude materials, apparatus and hardware. It might likewise be utilized for exchange financing needs, for example, import of merchandise or pre-shipment send out fund. In any case, the subject of Murabaha must exist and be in the responsibility for bank at the hour of offer in a physical or helpful belonging structure; and these benefits must be something of significant worth that is delegated property in Islamic law and must not be illegal wares. Obligation instruments and financial units that are dependent upon the standards of Bai' al Sarf can't be sold through Murabaha. Hussain , (2015).

Islamic banks are required to go out on a risk between the acquisition of the benefit from the dealer and the clearance of the resource for the individual requiring the products. The bank is

made up for the time estimation of its cash as the net revenue. Nonetheless, it isn't made up for the time estimation of cash outside of the contracted term. Truth be told, the bank can't charge extra benefit on late installments; the advantage stays as a home loan with the bank until the Murabaha is forked over the required funds; and there must not be any reference to the hour of installment by the purchaser to keep the exchange free from interest. Hussain, (2015).

## **2.17 IJARAH:**

“In principle, Ijarah may be effected directly on the asset without any requirement of a preceding master agreement. However, it is permissible requirement of a preceding master agreement. drawn up covering a number of Ijarah transactions between the Institution and the customer, setting out the general terms and conditions of agreement between the two parties. In this case, there may either be a separate lease contract for parties. or alternatively the two parties may exchange notice in offer and acceptance by referring to the terms and conditions contained in the customer master agreement. AAOIFI , (2017).”

## **2.18 MUSHARAKAH**

“This standard covers the Murabahah transaction and its different stages, This standard covers the Murabahah exchange and its different stages, the issues identifying with ensures before finishing up a Murabahah arrangement such the issues identifying with ensures before closing a Murabahah arrangement, for example, guarantee, as guarantee, Hamish Jiddiyyah Hamish Jiddiyyah (security store) and issues identifying with (security store) and issues identifying with ensures for recuperation of the obligation made by the Murabahah exchange. ensures for recuperation of the obligation made by the Murabahah exchange, AAOIFI, (2017).

as long as following Shari’ah standard to avoid & mitigate risk and loss for the bank so AAOIFI prefer the following to be conduct Murabaha contract The Institution must ensure that the party from whom the The Institution must ensure that the party from whom the item is bought is a

third party other than customer or his item is bought is a third party other than customer or his agent. For example, it is not permitted for a customer to sell agent. For example, it is not permitted for a customer to sell an ordered item to the Institution and then repurchase it through an ordered item to the Institution and then repurchase it through a Murabahah transaction. Nor may the party that is a Murabahah transaction. Nor may the party that is supplying supplying the item be wholly, or by way of majority [more than 50%], the item be wholly, or by way of majority [more than 50%], AAOIFI, (2017).”

## **2.19 SALAM:**

“This standard covers Salam and Parallel Salam transactions, whether This standard covers Salam and Parallel Salam transactions, whether the Institution is the buyer or the seller, and issuing Salam Sukuk. This the Institution is the buyer or the seller, and issuing Salam Sukuk. This standard does not cover Istisna’a (manufacturing or supplier contract) standard does not cover Istisna’a (manufacturing or supplier contract) because the latter is covered by a separate standard. because the latter is covered by a separate standard.” AAOIFI,(2017)

“ It is permissible to initiate through negotiations several Salam, It is permissible to initiate through negotiations several Salam contracts (with different parties). Each operation will end at its contracts (with different parties). Each operation will end at its due date. It is also permissible to draw up a general framework due date. It is also permissible to draw up a general framework or a master agreement that consists of an understanding to or a master agreement that consists of an understanding to conclude successive Salam contracts, each of which will take conclude successive Salam contracts, each of which will take place at an appropriate time. In this latter case, the transaction place at an appropriate time. In this latter case, the transaction involved shall be concluded on the basis of a memorandum of involved shall be concluded on the basis of a memorandum of understanding in which the contracting parties determine the



understanding in which the contracting parties determine the framework of the contract and the intention of the parties to framework of the contract and the intention of the parties to buy and sell. The parties shall also determine the quantity and buy and sell. The parties shall also determine the quantity and specifications of the goods, the manner of their delivery, the specifications of the goods, the manner of their delivery, the basis for determining the price, and the manner of payment. basis for determining the price, and the manner of payment. The types of guarantees and other prospective arrangements The types of guarantees and other prospective arrangements shall also be specified in the memorandum. The execution shall also be specified in the memorandum. The execution of each Salam contract may then take place separately at the of each Salam contract may then take place separately at the appropriate date. appropriate date. If the Salam contract is concluded on the basis of what was If the Salam contract is concluded on the basis of what was initially agreed in the memorandum of understanding, the initially agreed in the memorandum of understanding, the contents of the memorandum become part and parcel of the contents of the memorandum become part and parcel of the contract. This will hold true unless the parties agreed contract. AAOIFI,(2017).”

## **2.20 ISTISNA’A.**

“The standard covers Istisna’a and parallel Istisna’a transactions whether the Institution is acting as an ultimate purchaser or is acting as a manufacturer Institution is acting as an ultimate purchaser or is acting as a manufacturer or as a builder for construction. or as a builder for construction. moreover for avoiding a risk in Istisnaa transaction bank must adhering of the Istisna’a Contract, Conclusion of an Istisna’a contract at the time of contracting or Conclusion of an Istisna’a contract at the time of contracting or after the bilateral promise after the bilateral promise . It is permissible that the Institution and a customer conclude an Istisna’a contract before the Institution assumes title to the an Istisna’a contract before the Institution assumes title to the subject-matter to be sold to the customer or to the materials subject-matter to be sold

to the customer or to the materials from which the subject-matter will be produced (manufactured from which the subject-matter will be produced (manufactured or constructed). or constructed). It is permissible for the Institution to benefit from any price offers or quotations that the customer has obtained from other offers or quotations that the customer has obtained from other dealers or suppliers to assist it in the evaluation of expenses dealers or suppliers to assist it in the evaluation of expenses and the computation of prospective profit. and the computation of prospective profit. It is not permissible that the Institution's role in the Istisna'a be that of a financial intermediary between a buyer and a third that of a financial intermediary between a buyer and a third party, especially if the buyer has become unable to meet his party, especially if the buyer has become unable to meet his obligations toward such a third party, and this prohibition obligations toward such a third party, and this prohibition applies whether such a role would take place before or after applies whether such a role would take place before or after the commencement of the work. AAOIFI,(2017).”

## **2.21 SUKUK**

The aim of Sharia'a standard is to elaborate the Shari'ah rules for the issuance and trading of investment Sukuk (certificates) as well as the elaboration of and trading of investment Sukuk (certificates) as well as the elaboration of their types, characteristics, Shari'ah regulations and the conditions for the their types, characteristics, Shari'ah regulations and the conditions for the issuance of Sukuk and dealings in them for trading by Islamic financial institution of Sukuk and dealings in them for trading by Islamic financial institutions (institution/institutions). Investment Sukuk are certificates of equal value representing undivided Investment Sukuk are certificates of equal value representing undivided shares in

ownership of tangible assets, usufruct and services or (in the shares in ownership of tangible assets, usufruct and services or (in the ownership of) the assets of particular projects or special investment ownership of) the assets of particular projects or special investment activity, however, this is true after receipt of the value of the Sukuk, the activity. (AAOIFI, 2017).

However, this is true after receipt of the value of the Sukuk, the closing of subscription and the employment of funds received for the closing of subscription and the employment of funds received for the purpose for which the Sukuk were issued. purpose for which the Sukuk were issued. In this standard, Sukuk have been designated as Investment Sukuk in this Sharia'a standard, Sukuk have been designated as Investment Sukuk in order to distinguish them from shares and bonds. order to distinguish them from shares and bonds. Investment Sukuk are of different types, and among these are: Investment Sukuk are of different types, and among Certificates of ownership in leased assets Certificates of ownership in leased assets These are certificates of equal value issued either by the owner of These are certificates of equal value issued either by the owner of a leased asset or a tangible asset to be leased by promise, or they a leased asset or a tangible asset to be leased by promise, or they are issued by a financial intermediary acting on behalf of the owner are issued by a financial intermediary acting on behalf of the owner with the aim of selling the asset and recovering its value through with the aim of selling the asset and recovering its value through subscription so that the holders of the certificates become owners of subscription so that the holders of the certificates become owners of the assets. AAOIFI, 2017).

## **2.22 TRADE FINANCE:**

Islamic trade finance, import trading through the bank as a guarantee for the buyer and seller. based Murabaha requires move of possession all the while from provider to lender and from

agent to the recipient of advance. Thus, risk the board practices would be like traditional loaning. Resource sponsored Murabaha, then again, requires holding responsibility for products financed and offers ascend to certain risk to be overseen. This paper features the risk territories for resource based backed Murabaha and proposes techniques to deal with the risk related with forms molded by the hidden Islamic trade finance contract. Gundogdu, (2017).

“The stage of requesting the opening of credit: At this stage the buyer requests the bank to open the credit so that the seller buyer requests the bank to open the credit so that the seller can be notified The stage of issuing credit and notifying the seller: At this stage, The stage of issuing credit and notifying the seller: At this stage, the bank issues and sends the letter of documentary credit to the bank issues and sends the letter of documentary credit to the buyer, either directly or through an intermediary bank. the buyer, either directly or through an intermediary bank. AIIOFI, (2017).

“The stage of executing the credit: At this stage, the beneficiary presents the documents stipulated in the letter of credit to the presents the. The bank examines them in accordance with the credit bank. If the documents conform to instructions, the bank conditions., the bank accepts them, executes the credit and delivers the documents to accepts them, executes the credit and delivers the documents to the buyer, in case it is not the institution itself, after the receipt the buyer, in case it is not the institution itself, after the receipt of partial or full payment of the value or receives a deed of partial or full payment of the value or receives a deed of commitment to pay on the date of maturity so that the buyer is commitment to pay on the date of maturity so that the buyer is able to receive the goods represented by the documents. If the able to receive the goods represented by the documents. If the documents do not conform to instructions, the bank reserves documents do not conform to instructions, the bank reserves the right to accept, reject or seek amendment of the documents. the right to accept, reject or seek amendment of the documents. Coverage by correspondents: If more than one bank participates Coverage by

correspondents: If more than one bank participates in the execution of credit, the accounts are settled in accordance in the execution of credit, the accounts are settled in accordance with the terms of coverage agreed upon between the banks. with the terms of coverage agreed upon between the banks. Types of documentary credit Types of documentary credit Basic classification Basic classification Documentary credit is classified, according to the strength of the undertaking into two types; namely revocable the undertaking into two types; namely revocable credit, which can be amended or cancelled without consulting it, which can be amended or cancelled without consulting the beneficiary, and irrevocable credit, which cannot be the beneficiary, and irrevocable credit, which cannot be amended or cancelled without the consent of the parties. amended or cancelled without the consent of the parties. Other classifications There are other classifications of documentary credit.” AAOIFI (2017).

“There are other classifications of documentary credit. These include the following: include the following: Transferable documentary credit: This credit entitles the benefit transferable documentary credit: This credit entitles the beneficiary to request the executing bank to make the credit available, carry to request the executing bank to make the credit available, partially or totally, to another beneficiary. Revolving or renewable credit, which means the beneficiary can Revolving or renewable credit, which means the beneficiary can repeatedly submit new documents for new operations within the repeatedly submit new documents for new operations within the limits of the credit amount and during its limits of the credit amount and during its permissibility. however, the seller (beneficiary) does not have a right to request payment seller (beneficiary) does not have a right to request payment from the buyer as long as the credit subsists and is valid. If the form the buyer as long as the credit subsists and is valid. If the credit expires before the submission of the documents, the seller credit expires before the submission of the documents, the seller has the right to claim payment directly from the buyer, because has the right to claim payment directly from the buyer, because expiry of the credit in itself does

not amount to revocation of expiry of the credit in itself does not amount to revocation of the sale contract. The bank is obliged to pay the value of the credit to the beneficiary when the latter presents the documents that conform efficacy when the latter presents the documents that conform to instructions, except upon proof of fraud or forgery of the to instructions, except upon proof of fraud or forgery of the documents, or in the case of a court decision declaring the sale documents, or in the case of a court decision declaring the sale contract null and void. AIIOFI, (2017).

### **2.23 INSURANCE RISK**

The risk of reductions in earnings and/or value through financial or reputational loss due to fluctuations in the timing, frequency and severity of underwritten insurance events and/or the fluctuations in the timing and amount of claim settlements. This includes fluctuations in profits due to customer behavior. GSM , (2019).

### **2.24 OPERATIONAL RISK**

The risk of reductions in earnings and/or value through financial or reputational loss, from inadequate e or failed internal processes and systems or from people related or external events. GSM , (2019).

### **2.25 COMPLIANCE & LEGAL RISK**

The risk of reductions in earnings or value through financial or reputational loss due to the Group's failure to respond appropriately to regulation, laws or recognized industry standards that are relevant to the Group's business activities, strategy and objectives.

Legal Risk is the risk to delivery of business objectives, reductions in earnings and/or value due to legal challenge, adverse judgements or unenforceable contracts. GSM , (2019).

## **2.26 CUSTOMER RISK:**

The risk of reductions in earnings or value through financial or reputational loss due to inappropriate or poor treatment of customers. GSM , (2019).

## **2.27 INFORMATION TECHNOLOGY RISK**

The risk of reductions in earnings or value through financial or reputational loss due to IT service design and delivery not supporting the Group's strategic objectives, or not being compliant with relevant regulation or legislation. GSM , (2019).

## **2.28 PEOPLE RISK**

The risk of reductions in earnings or value through financial or reputational loss due to inappropriate behavior, industrial action or health and safety issues. Loss can also be incurred through failure to recruit, retain, train, reward and incentivise appropriately skilled staff to achieve business objectives and through failure to take appropriate action as a result of staff underperformance. GSM , (2019).

## **2.29 PRODUCT RISK**

The risk of reductions in earnings or value through financial or reputational loss due to product design failing to meet customer, legal or regulatory expectations and requirements. This includes product implementation and management. GSM , (2019).

## **2.30 SUPPLIER & OUTSOURCING RISK**

The risk of reductions in earnings or value through financial or reputational loss due to the failure of any supplier or outsourcer; and/or the actions of any third party being in breach of regulation or legislation. GSM , (2019).

### **CHAPTER THREE: METHODOLOGY**

The purpose of this study is to examine the risk management practices in Islamic bank using Ajman bank as case study. The study has assumed a qualitative research. The research enterprise improved in this study is descriptive research design. The descriptive research is used to acquire the information based on the current interview feedback was conducted with the respective members in the Banks. Similarly, this study has adapted the sampling in Ajman Bank the risk in several department and when researchers use this covering the risk in the banks product along with the mitigation of avoiding loss or any kind of reputational risk The sampling units are the following sample of Ajman Bank by conducting interviews to the respondents using open ended questionnaires at their corresponding work place without violating research ethics. The purpose for selection of Ajman Bank is that it is the first Islamic bank in the Emirate of Ajman and the bank was established after the 2008 financial crisis. Ajman bank is relatively considered a small bank compared with other Islamic banks in the United Arab Emirates (UAE) such as Abu Dhabi Islamic Bank and Dubai Islamic Bank. Most of the previous studies focused on large banks in UAE and ignore small banks such as Ajman Bank. Therefore, this study will attempt to shed the light on the risk management practices of small Islamic banks taking Ajman Bank as a case study.

Ajman Bank is a youthful, coordinated Islamic business bank based on the estimations of trustworthiness, trust and straightforwardness. The principal Islamic bank joined in the Emirate of Ajman, the Bank was set up in 2007. Its offers were recorded on the Dubai Financial Market in February 2008 and the Bank opened authoritatively and began activities in 2009 from two branches in Ajman. The bank presently has branches and ATMs over the UAE. With our system of focusing on the quickly extending Shari'ah money related administrations advertise, Ajman Bank gives a wide scope of significant worth driven financial administrations in the UAE for individual, business and government customers, all



in consistence with Shari'ah standards. Ajman Bank searches out the market's best items, individuals and innovation so as to convey what clients need, how they need it, conveying genuine worth and reproducing that human touch lost in current banking. Headquartered in Ajman, the Bank is emphatically bolstered by the Emirate's Government, which possesses 25 percent ([www.ajmanbank.ae](http://www.ajmanbank.ae)).

### **3.1 ADVANTAGES OF QUALITATIVE METHOD**

As it was referenced before that the research methodology was utilized right now subjective strategy. Meetings should be possible in various manners, for example, via telephone, Emails, and up close and personal. A few people who don't have time they favor through messages or telephones and others incline toward eye to eye. There are numerous focal points of eye to eye talk with, similar to it very well may be recorded without a doubt with the authorization of the interviewee. Likewise, questioner can get favorable position of meaningful gestures, instances of expressive gestures are sound, non-verbal communication, and voice which can offer questioner increasingly verbal responses to the inquiries. Besides, the end of this sort of meeting is simpler contrasting with others since it shows when the questioner rearranging the paper and turning of the recorder (Opdenakker, 2006). Also, it can give open new theme territories that are not at first considered and itemized picture about the subject can develop (The advantages and disadvantages of qualitative and quantitative research methods), O'NEILL, R. (2008).

### 3.2 DISADVANTAGES OF QUALITATIVE METHOD.

Further to of advantage of qualitative method there are weaknesses too. A portion of these drawbacks are assortment the information for this sort of technique is additional tedious contrasting with quantitative information assortment. Also, it relies for the most part upon the abilities of the analyst. Some of the time it is hard to make precise examination all things considered when individuals give reactions that are profoundly free. What's more, it is normally difficult to arrive at high number of individuals since less individuals are examines this subject for instance (Advantages and Disadvantages of Qualitative Data Analysis, O'NEILL, R. (2008).

### 3.3 TABLE SUMMARY OF PRIMARY DATA SOURCES

These interviews were conducted to obtain complete information on bank department risk views the researchers used a purposive sampling method in conducting the interview technique by interviewing experienced and knowledge respondents about the problems of the risk study along with the preventive control and sharia complaint

Participant	Qualification	Age	Years of experience	Interview Type.	positions
Retail Banking	MBA	45	21	Face-to-face at the office. Along with the recording session	Head of products

Compliance	MBA	46	22	Face-to-face at the office.  Along with the recording session	Head of Compliance
Sharia'a	MBA	50	26	Face-to-face at the office.  Along with the recording session	Head of Sharia Audit
Internal Control	MBA	38	16	All the communication was through email.	Head of Internal Control
Risk Management	Bachelor	40	18	Face-to-face at the office.  Along with the recording session	Senior Manager Risk Middle Office

### **3.4 INTERVIEW QUESTIONS**

- What risks identify belong to the bank department?
- How can analysis and manage the risk within the short time?
- What is the recommendation to be the bank in line with the regulation to avoid the department risks?

## **CHAPTER FOUR: RESULTS and DISCUSSION**

In terms of interview result with the bank department heads they agreed that all the area in the banks there is a risk and against those risks there is a certain control which can be mitigate the control following results

### **4.1 INTERVIEW OUTCOME WITH RETAIL BANKING: -**

The interview conduct with Head of retail product based in the risk related to retail finance product and its worth mentioned that the risk behind based on the interview analysis.

The retail banking customers can be having a different finance facility such as, Credit Card, Personal Finance, Auto Finance & Home Finance; being a Ajman bank financing customer

Customer name will be in the due diligence stage via checking his or her name in the black list via the internal and international systems. And based on the result the action will be taken that if the customer eligible borrowing or not, Here the banks have a secured finance (Home and Auto Finance) and non-secured finance (Personal & Credit Card finance). The Islamic bank offering the finance based on the equity investment, Murabaha contract signed by the customer and the bank officer. And all the requirements such as salary certificate, bank statement if the customer have another account in other banks. The risk will be determining in case the department team ignored the following of the policy and producer and not follow the delegation of authority approved by the management member. In the home and personal finance customer must transfer the salary to the bank and the instalment will be debited on monthly basis as agreed in the Murabaha contract. In case the customer defeater and not payback the instrument amount bank will come to know within the short time through the unpaid instrument report, so if customer defaulter bank will determine the risk and will take an action asap to know that the reason behind that the customer not settled the finance instrument, customer will be contacted via the concern department team to provide the justification on the delay of the settlement and

why the salary not credited to his or her account. Collection department will follow up by calling the customer. Customer account will be blocked with the certain instrument amount.

The case will be shared with the insurance department to ensure the finance cover by bank insurance policy.

Customer name will be updated in the black list to avoid any relationship in future. Customer name will be reported in al Etihad Credit Bureau (AECB).

#### **4.2 INTERVIEW OUTCOME INTERNAL CONTROL DEPARTMENT:**

While conducting Head of Internal Control below feedback obtain and for avoiding the risks as well. Internal Control Department (ICD) is an integral part from the bank department independent, objective assurance and consulting activity designed to add value and improve the organization operations. It also helps the organization to accomplish its objectives by bringing a systematic and disciplined approach in monitoring and improving the effectiveness of risk management, control and governance processes.

Internal Control system is designed to ensure that day-to-day actions are consistent with established plans, objectives and regulations (ICD provides a reasonable assurance not an absolute assurance. the Operations Objectives Operation control pertain to the effectiveness and efficiency of the bank in using its assets and other resources for protecting the bank from loss. And the Information Objectives address the preparation of timely and reliable reports needed for decision. making within the banking organization and Compliance Objectives to ensure that all banking business is conducted in compliance with applicable laws and regulations. On daily basis the department team conducting the control via the internal exceptional reports to ensure all monitoring transaction are complying with the supporting

documents. The ICD team verifying the transaction in the reconciliation system and in case and findings as discrepant the same will be communicate to the concern department for their action.

All the regulation received from Central bank taking in consideration and shared with the relevant department for their necessary action. Monthly report shared with the Head of relevant department to show all the risk during the previous month and show the result if the discrepant closed by concern unit or still opened and need for rectification.

Ensure that all functions in the Bank are complying with the laid down internal and regulatory policies, procedures, rules and regulations to safeguard the Bank's interest. Certify that staff are made aware of their roles and responsibilities in line with the documented Policies and Procedures (P&P), Job Descriptions (JDs) and Service Level Agreements (SLAs) - Ensure that the Bank achieves its long term profitability and sustained growth. Establish an accurate and timely reporting mechanism within each unit / department.

Ensure accuracy and reliability in the accounting and operating data.

Identify & rectify internal control issues on a timely basis.

Evaluate the level of performance in all departments & units of bank.

#### **4.3 INTERVIEW OUTCOME SHARIA DEPARTMENT: -**

After the interview conduct with Head of Sharia and conduct the following interview questions

Found the risk belong to Sharia department and the control mitigation as well.

we found the following risk might have affected the Islamic Bank. Risk of Non-compliance with Sharia regulatory requirements (including product development, transactions, proposals and other activities) Risk that contracts and agreements does not comply with Sharia rules and principles – with regard to formation, termination or any other rights or obligations. Risk of non-compliance or delay in implementation of AAOIFI standards lead to Central Bank

penalties. Risk that the Sharia audit findings and observations may not be addressed timely by stakeholders lead of open audit items.

While analysing the bank loss might have happened due to the bank not following the process as per the Sharia compliant meaning that suppose if the customer auto finance request and after sharia audit checked the customer file and founding the process and documentation not in sequence will due to the profit loss because in regular such case Sharia will request the department and finance to move the profit from the profit and loss account and credited to charity account. Meanwhile for the credit card customer late payment, will due for charges and the charges will be moved to charity account as well as so banks have to ensure no such fund will credit to PL account and to avoid any reputational and regularity impact.

Post launch of product Sharia audit will audit the executed transactions on sample base to identify any non-adhering dimensions or scenarios. Pre-launch product design, structuring, legal contracts & documents, PPGs, BRDs, process flows, marketing materials, etc. are reviewed by Sharia review unit. Executed Transaction review process is in place by Sharia Audit (Quarterly sample-based Sharia audit occurs each year) to identify any deviation from established and approved Sharia guideline for all products and services.

Pre-Execution Sharia review provides one-time approval for applications documents and contract documents at product launching stage for Standardized Products. Where unstandardized transaction has to be reviewed case to case basis for its Sharia approval from the structure, process flow to the agreements prepared by external / internal Lawyers. All policies and product & services programs must be reviewed by Sharia Compliance Division. In case of changes / amendments the concerned division has to insure Sharia Compliance Division review and approval on that.



Post Transaction Execution review process is in place by Sharia Audit (Periodic sample sharia reviews occur each year). Marketing materials must be submitted to Sharia for Sharia reviewed by the concerned authority. Marketing materials shall be reviewed internally and in case of new concept or in case where decision by Sharia team will be difficult, ISCC opinion must be taken. Reported incidents reviewed by Sharia Audit to ensure reversal of repugnant income where decided by ISCC.

Post launch of product Sharia audit will audit the executed transactions on sample base to identify any non-adhering dimensions or scenarios from the ISCC guidelines and AAOIFI Sharia standards. Policies, Procedures (PPGs), new products/concepts & structures, legal documents & agreements, process flows, marketing materials are reviewed by Sharia before launch to verify and to ensure sharia compliance in light of the ISCC injunctions & guidance's if needed a further guidance will be obtained from ISCC.

Sharia compliance division ensures that approval on transactions is according to ISCC approval only. Sharia Review function ensures all amendment or changes in products, process flows, accounting entries, etc, are in compliance with AAOIFI Sharia Standards and the ISCC pronouncements.

The interpretation of all form of documents is that all documents of the bank including but not limited to all kind of Concept papers, Contracts, Process Flows, Memos, PPGs, Marketing material, Internal & External documents prepared by internal lawyers or external law firms. For the implementation of the article, All business and supporting departments shall arrange to provide the documents for Sharia review and Sharia Review Unit post review of the material shall send the new concepts and documents to ISCC to obtain ISCC Fatwa or Resolution which shall be communicated to the concerned department via Sharia Compliance Division under cc to the management for implementation. Timeframe will be decided by stakeholders for action

or rectification of open Sharia audit findings, which will be reviewed by Sharia audit team after the collapse (completion) of allocated time period. The rectified Sharia audit findings will be reviewed and marked as closed while the report/MIS will be prepared for non-rectified and open Sharia audit items accordingly.

#### **4.4 INTERVIEW OUTCOME COMPLIANCE DEPARTMENT:**

While conducting the Head of Compliance and conduct the following questions, determine that the risk and control mitigation as well.

While analysing the risk might bank risk might have affected the bank in case the control not in place. Compliance is following the UAE-Central Bank regulation and in line with the international rules and standard.

The customer new to bank conducting the due diligence and the compliance check list Such as the World Check System, Internal customer black list, know your customer (KYC) and In case the customer from high risk nationality the customer service officer will check send the document to the compliance department team for their approval or reject before the customer open any kind of relationship with the bank. might having the Risk that fines/penalties are imposed due to money laundering and wrong practices. Risk that clients on boarding is not inline bank internal policies and procedures Risk that approval or decision has been taken by Compliance is not in line with policy of 100% mitigation Financial Crime Risks (FCR) for existing customer. Unable to ensure appropriate governance around regulatory requirements and risk around SARs which lead to AML alert overdue for WBG/CBG/ TCM/ Investments. Inadequate compliance procedures and controls leading to regulatory sanction, increased supervisory intrusion and significant reputational damage to the bank. Incomplete, inaccurate and/or untimely reporting of required financial and operating information to regulatory agencies may expose the bank to reputation loss or legal action. Non-compliance with customer

requirements, bank's policies and procedures or laws and regulations may result in lower quality, higher costs, lost revenues, unnecessary delays, penalties, or fines. Unable to perform due diligence before entering into an agreement or a transaction with another party. Such as investigating the party before entering into relationship agreement or conducting a transaction with Ajman Bank. Suspicious Transaction Report (STR) cases are not reported to C.B on timely basis lead to reputational and legal impact / loss. AB customer become part of black list after Opened the account.

The ultimate goal is to ensure that the compliance with all applicable regulatory requirements. And the objective of this update is to clarify and simplify the process, periodic reporting and roles & responsibilities Compliance team should maintain a book of record for all received regulatory requirements. And should send regulatory requirements to all concerned departments. Any department that receives any regulatory requirement(s) should send these immediately to the department Head in order to start the process.

AML alerts to be reviewed by Compliance team are approved along with the required supporting documents (on sample basis); and to safeguard the bank against any threat of money laundering. To ensure all the know your customer (KYCs) reviewed by Compliance team are approved along with the required supporting documents (on sample basis); and to safeguard the bank against any threat of money laundering. The black listed customers are updated in System immediately to avoid any reputational or legal impact and loss. To ensure no relationship with the Sanctioned Country without Compliance approval and should be investigated and declined. In case customer received from any terrorism or tourist organization are mandate to freeze the transaction /account and promptly inform the relevant regulatory authorities in writing.

#### **4.5 INTERVIEW OUTCOME RISK MANAGEMENT DEPARTMENT /LIQUIDITY:**

While conducting the Head of Treasury Middle Office, and conduct the interview questions the department analysis as following:

The risk identification that The liquidity risk Identifying the sources of reputation risk involves focusing on those activities that are perceived as most likely to affect the Bank's reputation, thus enabling it to enhance its controls over such activities. As such risk owners should consider the key risks faced from each of the Bank's stakeholders, and identify any other risks that may be specific to the country/region taking into account strategy and business focus.

Stakeholders are individuals and groups with multitude of interests, and demands as to what the Bank should provide to society. For the purpose of formalized Stakeholder Management, classifying key stakeholders those individuals or groups whose interest in the Bank must be recognized into groups is a useful tool, and allows management strategies for like groups to be developed and implemented. The following matrix matches each stakeholder with the type of reputation risk brought to the Bank. On daily basis the risk middle office team reconcile all the transaction between the Treasury Capital Market and Treasury operations departments to ensure the transaction already proceed and in case any outstanding the same will be communicate to the concern department for their rectification and action.

Treasury remains responsible for action/providing execution to the plans way forwards discussed in the framework. Liquidity Risk Management Framework Liquidity represents the ability of Ajman Bank to accommodate decreases in liabilities and to fund increases in assets. Liquidity exposure can stem from both internal and external factors. External liquidity risks can be geographic, systemic or instrument specific. Internal liquidity risk relates largely to the perception of Ajman Bank in its various markets, local, regional, national and international.

General Liquidity Guideline's Surplus liquidity / cash will be invested to earn optimal return while keeping the risk at minimum. Money Market operations will be undertaken to facilitate handling of normal commercial and financial transactions. Money Market operations will be conducted within the limits approved as per the delegation of authority. Repo/reverse repo transactions will be conducted against the eligible securities. Sensitivity Analysis: examines the impact of change in some variable(s) (e.g. profit rates, FX rates, quoted prices) on the value of a portfolio/financial position. Potentially, a number of variables can be collectively stressed or different sensitivity tests can be combined to form a multifactor stress test. While the simplicity of sensitivity analysis makes it easier to use and understand, at best, it provides an approximation of the impact of a risk factor on a portfolio. Sensitivity analysis is often used in market risk stress testing models wherein the risk sensitivities stressed using the relevant risk factors. Scenario analysis assesses impact of extreme but plausible scenarios on a given portfolio/financial position of an institution, using sophisticated modelling techniques and typically incorporating macroeconomic variables. Scenarios could be historical or hypothetical. Scenario analysis takes into account correlations between risk factors, including macroeconomic variables. Shocks assumed are recommended to be closer to real life as other factors are not supposed to be held assumption under simple sensitivity test. Stress tests addressing credit risk and liquidity risk related concerns on the bank balance sheet are better modelled using the scenario based approach. Stress Testing Governance in terms of BIS principles for sound stress testing practices and supervision, stress testing should form an integral part of the overall governance and risk management culture of a bank. The Board of Directors of Ajman Bank shall therefore take complete ownership of the stress testing framework and ensure that the same is fully embedded in Banks risk management. Secured or unsecured basis. Ajman bank already maintains an active presence within markets relevant to

its funding strategy and we need to ensure we invest adequately in infrastructures, processes and information collection.

Ajman Bank currently already has a number of credit lines from local institutions, examples are: Sharjah Islamic Bank, Emirates Islamic, Bank Noor Islamic Bank iv) Dubai Islamic Bank, Abu Dhabi Islamic Bank, Abu Dhabi Commercial Bank.

Banks ought to have sufficient arrangement of internal controls to system the honesty of their loan charges chance administration process and to advance powerful and proficient activities, dependable money related and administrative detailing, and consistence with significant laws, guidelines, and institutional strategies. A compelling arrangement of inward control for loan fee chance incorporates a satisfactory procedure for recognize and assessing risk and having adequate data frameworks to help these. The framework would likewise build up arrangements and techniques and their adherence are persistently explored. These intermittent surveys would cover the amount of loan cost risk, yet additionally the nature of financing cost chance administration. Care ought to be taken that there is satisfactory division of obligations of risk estimation, observing and control capacities.

Finance loss provision ratio is the amount set aside for potential loss of the total lend amount or finance and advances. Higher provision banks maintain here lower fund it has to utilize as these also includes provision for good loan which is just hold and unutilized. so lower loan loss provision is preferred in financial institutions. Everest bank has the lowest loan loss provision giving average of study at. bank limited has lowest limit loan loss provision set at and highest as giving average.

## **CHAPTER FIVE: CONCLUSION**

The dissertation study has conduct a several main topics that the risk belongs to the Islamic banking and how the bank defines the risk belong to each department, moreover bank have a several controls to avoid and mitigate the impacted risk.

Below summary related to each chapter in the dissertation.

### **chapter one:**

Provided a main several information in the bank and the objective, problem statement, significant and motivation of the study and research questions.

### **Chapter Two:**

In this chapter related to the other previous study through the literature review and type of risk belong to the Islamic banking.

### **Chapter Three:**

In chapter three shows the data and methodology in Ajman Bank and the bank department conduct through the interview to define the risk belong into each department. Advantage and disadvantage of research method, and Limitation of the Methodology.

### **Chapter Four:**

The interview result for the for how the banks department define the risk for Retail banking, Internal Control, Compliance and Sharia departments, along with the control mitigations to avoid any regulatory impact and loss. The analysis show clear responsibilities of the relevant department.

## **Chapter Five:**

Chapter Five will be shows the conclusion and recommendation of the dissertation moreover the discover of the risk practise in Islamic banking and the recommendation based on the interview result to show the risk mitigation based on the control approbation to avoid and mitigate the risk in the bank, and further research will be conduct to close the gap of the risk.

The main purpose of this study is to discover the risk management practices in Islamic banking and to classify the specific risk in Ajman Bank through the interview and based on the qualitative research method. The detailed review of previous literature assisted in the preparation of the interview guide and in conducting interviews with five department heads Ajman bank. The risk might reach huge risk if the department not follow the bank policy and procedure, moreover bank might face a reputational risk due to the relationship with the black listing customer and liquidity risk. The Bank Corporate Governance forms the foundation of an effective reputation risk management and provides a basis for guiding Bank's conduct and actions in achieving its vision, values, goals and strategies. Board of Directors and Senior Management should lead the good practices in line with Bank's Corporate Governance Code. Some examples of good Corporate Governance infrastructure and practices are effective Employment Sourcing and Selection Policy, robust framework for succession planning, clear authorities and responsibilities of all employees, effective process for monitoring performance, open and empowering corporate culture to encourage responsible and ethical behaviour, risk awareness of employees, effective systems and controls, adequate policies and procedures in place to ensure that all disclosures to stakeholders are clear, accurate, complete, relevant, consistent and timely. Risk is the indecision that must be considered carefully, as banks deal with future uncertainties. Some of these risks are similar to those of the conventional banks. Studies on various countries and banks report that credit risk, operational risk, mark up risk,



and liquidity risk are the major financial risks affecting banks. The magnitude of the impact of each of these risks varies across the type of financing contracts the banks engage in. For instance, Mudarabah, Musharakah and Murabahah are the financing modes mostly influenced by these risks, when compared to, Salam, Ijarah and Istisna. This study is aimed at exploring the dimensions and determinants of efficient risk management. The study reports that operating risk is the most important risk for the banks in the sample. By operating risk, we mean the lack of system, human capital and wounding advantage technology in handling customers' demands. Credit risk is the second most important risk. Credit risk is the doubt that the customer would not come to pay their loan payments back to the bank, due to a number of economic and social issues. The additional two significant risks are liquidity risk and mark up risk. Liquidity risk has always been a threat for banks. The services offered by Islamic money markets to resolve the liquidity delinquent are extremely limited to certain countries. Among the modes of financing, these risks influence the three primitive levels of Islamic contracts more than the modern contracts. Mudarabah, Musharakah and Murabahah are the three partnership contracts that are severely affected by the four categories of risk. In addition, mark up risk has special implications for Murabahah. A lack of understanding, limited use of technology, limited or no diversification across various products and areas, among others, are the major problems identified by the bank managers. Also, bank managers recognised limited securitization and the inaccessibility of Islamic money market instruments as barriers to well-organized liquidity management. The Islamic regulatory system is insufficient to decrease problem loans. Banks have already established risk reporting systems. However, country risk was not analyzed and reported, as many banks are not globally diversified. Bankers haven't use technology to manage risks. Many of the modern tools were unknown to Banks. Operating risk was reported very poorly. Most of these banks have used AAOIFI risk management guidelines and the guidelines suggested locally by the central banks. Since many countries did not have sufficient

Islamic banking regulations, a portion of these banks opted to use other globally accepted standards of risk management and reporting systems. Two thirds of the bankers had active engagement in research and development in order to recognise problems earlier. Bankers do believe that Basel regulations are only partly applicable to banks. Hence, there is need for full-fledged Islamic regulation of risk management and control. This study proposals a risk management framework viewing that banks are the strongest institutions in risk management if they make use of the Shari'ah-based banking system. Islamic Sharia's is the core risk management system, which is also supported by internal and external control mechanisms. Many of these controls are absent in conventional financial system. This study proposes capitalising in the training of employees, investment in education and technology, investment in relationship structure with other banks and customers, and modification of banking operations among concurring neighbouring countries. Risk management operations must be healthy and robust to the changes in banking operations. Eventually, the constancy of banking operations should be given higher importance than the size of operations.

## **5.1 RECOMMENDATIONS**

Based on the findings we I Key Risk Indicators (KRIs) must be established in order to effectively monitor the reputation risk profile and identify any changes that may impact the achievement of objectives.

Internal Audit, Internal Control and Sharia 'a department must continue their checking and evaluation to ensure in case any risk define to be escalated for rectification and further action.

It is recommended that the stress testing exercise as well as the framework is independently validated at some point in time, depending including all its scenarios, parameters and assumptions. This validation is suggested to ensure soundness and consistency of the stress

testing framework. For each of the aforementioned risk (credit risk, market risk, liquidity risk, reputational risk and legal risk, outstanding proposed actions that have not been implemented for any reason should be escalated to the senior management including the Operational Risk Management in a timely manner for further action.

The role of Chief Risk Officer (CRO) are an important role by providing the quality assurance to the Senior Management and board director so the he is area responsible by ensuring that the banks are covering all the risk and control scenarios and in line with the Central Bank regulation

And policy and producer are covering for all the bank department to avoid any lack off process due to the error and impact, loss.

Ajman Bank very small bank comparing with the large bank in UAE such as ADIB, DIB, so will consider that the risk appetite will very minimal to the bank otherwise the impact will be huge and affected hall organization. As well as the following recommendation also for the International Financial Institutions (IFIS).

IFIs must certify appropriate training for their staff on various updated technologies that IFIs have to rely on for better analysis of the issues pertinent to risk management in IFIs. IFIs should increase investment in examination and growth activities to find challenges beforehand; partnership with international organizations might proposal valued visions into challenges from various scopes. In the non-appearance of a robust secondary market, banks can form a podium within themselves to resolve liquidity issue. This caring of association will also support in preparing a strong risk reports. In order get improved projections and communication updates, IFIs must invest in new technologies to ensure that the staff is getting the right information at the right time. Meanwhile the rudimentary setup of the risk management system is by now recognised, IFIs need to upgrade their systems using wounding edge technology. Even though

it is not entirely possible for many years to come, IFIs must stop competing with the conventional banks. Conventional banking risks and those of IFIs are never the same. Many IFIs are working in dual banking systems and are chiefly endangered by financial systems. Progressively, IFIs necessity have a plan to go back to Shari'ah based risk management systems. As illustrated in Shari'ah based financial operations is the first line of defines. If IFIs detriment in the first line of defence, the rest of the system will failure. Hence, the most significant element of risk management in IFIs is to bring back the insight of Shari'ah into operations. IFIs are still stressed to expand their portfolio of operations across countries, sectors and industries. Perhaps it is easier to diversify across industries and sectors. However, IFIs have to ensure that there exist experts on those sectors and industries among the staff who can guide the risk management process for that specific sector. In fact, IFIs should have experts on each sector or industry they are dealing with. This returns to the idea of having successful training to employees. Understand that the risk the executives division exists exclusively with the end goal of operational maintainability. It may not yield any social worth expansion in the prompt term. Islamic banks are more intently attached to social improvement objectives than ordinary banks.

In any case, the goal of the hazard the executives division is to make IFIs fit for social improvement. Consequently, there ought not be any job struggle between the general target of the IFIs and the particular destinations set for the risk management division. In a portion of these instructive organizations are spent significant time in banking and budgetary segment training. IFIs may offer cases to talk about in colleges so as to fabricate mindfulness about hazard the board rehearses and Systems. As the Islamic money related framework is moderately new, there is a requirement for an integrative methodology between the banks and the controllers so as to bring a proactive, long haul change in the manner in which we see hazard the executives today. Banks are fortunate in the event that they are in a framework that

doesn't endure ongoing defaulters. Banks must help the administration and the administrative expert in presenting a sound lawful environment for all. In numerous nations, there is no Islamic financial law to manage the IFIs. Notwithstanding the conventional lawful framework, IFIs must work out a working practice that submits to the laws of Shari'ah. Screen the general risk profile and the executive's ability, writing about its discoveries to the Ensure that chance proprietorship, and a proper culture, is set up and that chance administration data to encourage its utilization in supporting choice making. Monitor the budgetary and non-monetary risk profile of their business work, and guarantee exposures are overseen inside the parameters concurred and set by the Board.

## **5.2 FURTHER RESEARCH**

In fact, the bank enhancing a proper and strong policy and producer to enhance the bank department activity, further the research is to identify the criteria of adding the risk and control for the department wise and how the risk team conduct the testing of the control to see the result and ensuring the controls are efficient or not and based on that to check what is the best way to adding the risk and control or how to add other control for the existing risk if the risk and control testing failure. Further research should be directed to decide if the flexibility of the Islamic banks was really because of the standards whereupon Islamic money depends upon, or different variables, for example, the lesser level of combination of Islamic account foundations with the worldwide economy and following will be discovered the further research.

## **5.3 CONTROL RATING CRITERIA.**

Control Rating Criteria is the weight of the quality assurance that each risk linked with the proper control to provide the management the result of these testing of the control and ensure there's no breach otherwise to define the corrective action to cover all the gap of the risk as per the below criteria

Rating	Description	Definition
1	Satisfactory	Control is well designed, and meets its objective(s). It is effective and reliable at the current time, subject to periodic monitoring and review.
2	Need improvement	The control is somehow incorrectly designed and/or is not entirely effective. Accordingly, more work to be done to improve these deficiencies / weaknesses / gaps.
3	Unsatisfactory	Significant control deficiencies / weaknesses / gaps. Either the control does not meet its objective(s), it does not operate effectively, or does not exist.

#### 5.4 CORRECTIVE ACTION PLANS

- An assigned action owner.
- Expected target date for implementation.
- A documented acknowledgment by process and action owners, agreeing to the corrective action plans and / or agreed upon recommendations

The diagram below also indicates the suggested risk response to Accept, Reduce, Transfer and Avoid the risk.

<b><u>ACCEPT THE RISK</u></b> Risk are considered not be significant. The cost of dealing with the risks is greater than perceived benefit. Risk should remain under review in case the business environment changes.	<b><u>REDUCE THE RISK</u></b> This is an area where management should take immediate action to reduce frequency of losses. Management should consider the need for risk control measures, such as self-insurance to deal with frequency of loss.
<b><u>TRANSFER THE RISK.</u></b> Risks in this area should be transferred or minimized through insurance, hedging, or contingency planning. Reduction of the impact of the risk will minimize insurance premiums.	<b><u>AVOID THE RISK.</u></b> Need to take immediate action to reduce the impact or Likelihood of the risk. An extreme form of business risk avoidance is to terminate the operation

## **5.5 LIMITATION OF THE STUDY**

Actually the limitation for the primary source of data which was difficult due to research in other organization and the question were given and provided by only one organization Ajman Islamic Bank. However we conducted more than one interview for different department, meanwhile the limitations of a study are its flaws or shortcomings which could be the result of unavailability of resources, small sample size, flawed methodology, etc. No study is completely flawless or inclusive of all possible aspects. Therefore, listing

The limitations of study reflects honesty and transparency and also shows that you have a complete understanding of the topic. Generally the limitations of a study basically discusses any unanswered questions that your study did not address. Could have used another means or method of data collection and could the research design have been better acknowledging the study's limitations will give the impression that you are aware of what the study was not able to cover. Moreover, it would prevent the peer reviewer from pointing them out.

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