

Challenges Faced by Malaysian Islamic Banks in Treating Shariah Non-compliance Events

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Keywords: Shariah Non-compliance, Shariah Non-Compliance Event, Shariah Non-compliance Reporting, Islamic Banks, BNM Guidelines.

Abstract: Islamic finance in Malaysia has been growing rapidly in the past 30 years and continues to thrive in many countries. In 2019, a total of 16 Islamic banks (IBs) is listed and supervised by Bank Negara Malaysia (BNM) with 5 banks being foreign entities. In view of the rivalry with the conventional banking sector, Islamic banks (IBs) offer new innovative Islamic products and financial projects which may lead to greater risk of Shariah non-compliance (SNC) exposure to the Islamic Financial Institutions (IFIs) in its effort to stay competitive. This study intends to review the challenges faced by IBs in treating the SNC and propose recommendations for the existing policy to enhance the treatment of SNC. This study adopts qualitative research method by conducting semi-structured in-depth interviews with Islamic banking professionals targeting five IBs. Both the primary and secondary sources are used for data collection. The finding shows that there are a lot of minor concerns and challenges faced by IBs in managing SNC events in the industry. The finding of this study would contribute positively in terms of facilitating policy makers and regulators on enhancing the regulations and practices in ensuring zero SNC events. Simultaneously, enriching and contributing to the existing literature on the SNC practices by IBs so that more researchers can have larger resource of reference to diversify the topics related to this study.

1 INTRODUCTION

The push for innovation to fulfil commercial purposes has led many Islamic financial institutions (IFIs) to adopt conventional principles and instruments. However, this may expose the IFIs towards the risk of Shariah Non-compliance (SNC), as all financial transaction, projects and activities must comply with the law of Shariah. BNM has issued a Shariah Governance Framework in 2011 to be complied by all IFIs that include established core functions that would guide the Islamic Banks in achieving effective operational excellence and concurrently adhering to the Shariah principles.

Nonetheless, despite the BNM framework and guidelines, SNC risks can potentially arise when there is a mistake made in the documentation process in dealing with a certain contract. Apart from that, conflicts appear when the Islamic products are improperly managed although the terms and conditions in place have already been stipulated to be in line with Shariah. According to Islamic Financial Services Board (IFSB), SNC risk is defined as “The

risk that arises from the bank’s failure to comply with rules and principles determines by the relevant Shariah regulatory councils”.

Shariah compliance is the core element and the most predominant factor in operations of the Islamic banking and finance business. Failure to adhere to Shariah principles and values in carrying out the financial activities, business and operations may lead the Islamic bank to be exposed to the risk of non-compliance. SNC risk is considered as the unique risk of Islamic banks and IFIs compared to the conventional counterparts.

Management of non-compliance issue is crucial in ensuring customers’ faith and confidence in the Islamic banking and finance. Hence, monitoring of SNC events has to be on continuous basis and transparent in establishing credibility of the banks in their transactions. Therefore, this study intends to explore the concerns and challenges of SNC issues faced by Islamic banks. Subsequently, this study will take the current practices into consideration to propose recommendations on how to improve and

enhance the treatment of Malaysian Islamic Banks towards SNC events.

The significances of this study include enriching the existing literature on this topic and increasing the awareness among the beneficiaries and the regulators to better improve the policy and guidelines on SNC event in Malaysia. The scope of this study is limited to Malaysian Islamic banks practices on SNC treatment, which is regulated by Bank Negara Malaysia (BNM).

This study is structured as follows: Section two discusses the overview of Islamic banking industry in Malaysia, Shariah Governance Framework, and Statutory requirement on Shariah Non-compliance (SNC) event; Section three describes briefly about the methodology used; Section four presents the analysis and findings; Section five provides conclusions.

2 LITERATURE REVIEW

2.1 Islamic Banking Industry in Malaysia

Islamic finance and banking industry in Malaysia has been rapidly growing and increasing remarkably since more than 30 years ago. Malaysian model of Islamic banking today is one of the most advanced Islamic banking systems in the world (Marimuthu et al, 2010). In order to differentiate Islamic from conventional banking, we should begin by defining Islamic banking. According to Bank Negara Malaysia (BNM), Islamic banking is a banking system that complies with Islamic law. The underlying principles that govern Islamic banking are mutual risk and profit sharing between parties involved, the assurance of fairness for all and the transactions involve an asset and ownership or an underlying business activity that does not contradict with Shariah. Islamic banks offer facilities with a various financing arrangement with the contractual terms used between the bank and the customers as partners, buyer and seller, *wakil* (agent), fund provider and entrepreneur. Meanwhile conventional banks offer facilities based on loan arrangement and interest with the contractual term used between the bank and the customers are as borrower and lender.

The first Islamic commercial bank in Malaysia, Bank Islam Malaysia Berhad (BIMB) was established and started its operations in July 1st 1983. BIMB operated as the only Islamic bank in Malaysia for 10 years before the government allowed Islamic Windows Operation, also known as ‘Window’ to be offered by other conventional banks. Islamic Financial Board Services (IFSB) defined Islamic

Window Operation as “A part of a conventional financial institution (which may be a branch or dedicated unit of that institution) that provides both fund management (investment accounts) financing, and investment that are Shariah compliance, with a separate fund” (IFSB, 2017). Window operation has contributed to the growth of Islamic banking and finance in Malaysia as the conventional banks started offering Islamic financing product to the customers. The numbers of Islamic banks in Malaysia keep growing and currently there are a total of 16 Islamic banks that are supervised by Bank Negara Malaysia including several foreign owned entities. Table below shows the latest list of all Islamic banks in Malaysia retrieved from BNM website.

Table 1: List of Islamic Banks in Malaysia.

Name	Ownership
Affin Islamic Bank Berhad	Local
Al Rajhi Banking & Investment Corporation (Malaysia) Berhad	Foreign
Alliance Islamic Bank Berhad	Local
AmBank Islamic Berhad	Local
Bank Islam Malaysia Berhad	Local
Bank Muamalat Malaysia Berhad	Local
CIMB Islamic Bank Berhad	Local
HSBC Amanah Malaysia Berhad	Foreign
Hong Leong Islamic Bank Berhad	Local
Kuwait Finance House (Malaysia) Berhad	Foreign
MBSB Bank Berhad	Local
Maybank Islamic Berhad	Local
OCBC Al-Amin Bank Berhad	Foreign
Public Islamic Bank Berhad	Local
RHB Islamic Bank Berhad	Local
Standard Chartered Saadiq Berhad	Foreign

Sources: Bank Negara Malaysia (BNM) 2018.

2.2 Shariah Governance Framework

In 2010, Shariah Governance Framework (SGF) was introduced by Bank Negara Malaysia and being implemented starting on January 1st 2011 by IFIs. The Shariah Governance Framework plays an important role in supporting the robust development of the Islamic finance industry and promoting end-to-end Shariah compliance in Malaysia (BNM, 2017). The objectives of Shariah Governance Framework are, firstly to provide the guidelines on Shariah governance structures, processes and arrangements for all Islamic banks and IFIs to ensure the Shariah compliance in the entire business operations and activities. Secondly to provide comprehensive guidance of Shariah Committee and the management of IFIs in their business conduct or, anything related to Islamic financial matters. Lastly, to highlight the four (4) Shariah Governance Framework key functions such as Shariah risk management, Shariah review, Shariah research and Shariah audit.

Figure 1 below shows the reconstructed illustration adapted from Shariah Governance Framework policy document published by BNM on the model structure of roles, functions and relationships between the key organs in the governance framework of IFIs:

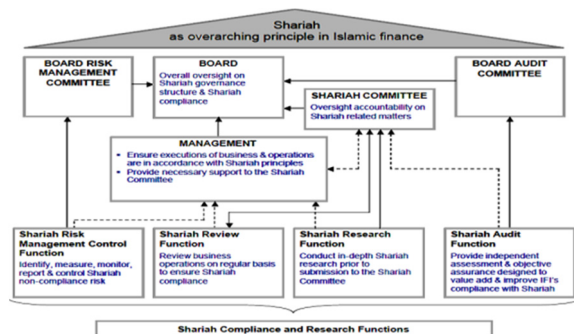


Figure 1: Model of Shariah Governance Framework for Islamic Financial Institutions.

Source: Bank Negara Malaysia (BNM), 2018

The IFIs shall ensure that the reporting on Shariah matters is carried out effectively in an orderly manner on regular basis. The Shariah Committee of IFIs shall report to the Board of Directors on Shariah related matters. The Shariah review function shall simultaneously report to the Shariah Committee and the IFIs management. Meanwhile, the Shariah audit function shall report to the Shariah Committee and Board Audit Committee on the Shariah matters. All SNC events that have been identified via several channel by any means with sources shall be reported to the Board of Directors and also the Bank (BNM). Shariah Governance Framework's core functions Shariah risk management, Shariah review and Shariah audit are required to be performed on continuous basis to ensure an effective management within the bank

2.3 Statutory Requirement on Shariah Non-compliance Event

In Malaysia, there are comprehensive regulation made to ensure IFIs do not contradict the Shariah principles in overall business activities. The regulation is Islamic Financial Services Act (IFSA) that came into force in 2013 as an omnibus act, consolidating the Islamic Banking Act 1983 & Takaful Act 1984 and repealing both. IFSA 2013 introduces end-to-end Shariah compliance regulatory framework for IFIs. The act was enacted to provide:

- i. The comprehensive regulation and supervision of Islamic financial institutions, payment systems

and other relevant entities in Malaysia to ensure all the activities, product and services offered complies with Shariah

- ii. The oversight of the Islamic money market and Islamic foreign exchange market
- iii. To promote financial stability and IFIs compliance with Shariah laws and principles (IFSA 2013)

The important provisions of IFSA on Shariah Requirement for Islamic Banks and IFIs are Section 28 (1) & (2) of IFSA 2013. It states that IFIs shall ensure that its aims and the entire operations, business, and activities are in accordance with Shariah rules at all times. Compliance with any ruling and decision made by the Shariah Advisory Council (SAC) in respect of any particular aim and operation, business, affair or activity by shall be deemed to be Shariah compliance. It shows that starting from the beginning until the end of the agreement, the requirements of Shariah must be fulfilled (Kunhibava, 2015).

Should there be any disregard on Shariah principles or any breach of contract with regards to the Shariah compliant requirement or it contains any standards against BNM guidelines, the Islamic banks and IFIs will be exposed to the risk of SNC. BNM also provides guidelines on the reporting process of SNC event in Operational Risk Integrated Online Network (ORION) revised policy document published in 2018. The guidelines include the reporting types and timeline on SNC event. The financial institutions or Islamic Banks that are exposed to SNC will be required to undergo the rectification process in accordance with Section 28(3) of IFSA 2013.

ORION policy document explains the process of SNC reporting that has to be adhered by IFIs starting from how the issue is reviewed by Qualified Shariah Officer (QSO) before confirming that it is a Potential SNC or non-SNC. IFIs have to report the issue in ORION system within 1 working day after the QSO confirmation. If QSO confirms the issue as non-SNC related, then it will be reassess to find out if it is related to operational risk. If the issue is operational risk related, it will be reported in ORION system as a general operational risk loss event.

Meanwhile, if QSO confirms it as a Potential SNC, then it will be reported in ORION system as Potential SNC (PSNC) and IFIs will have to get the SC decision on the issue. SC will decide the previous confirmed PSNC as an SNC or non-SNC in the meeting within 14 working days. The Potential SNC label in ORION will be updated to Actual SNC

(ASNC) when SC decides it as an SNC event and rectification plan is required. In the case of SC deciding it as a non-SNC, then IFIs have to update SNC field in ORION and reassessment is needed to find out whether the issue is an operation risk related or non-operational risk related.

IFIs are required to propose a rectification plan but members of SC and Board of Directors have to give their approval before the plan being submitted in ORION within 30 calendar days. (*ORION Policy Document*, 2018)

In addition, Section 28 (3) IFSA 2013 stipulates that, when IFIs becomes aware of the SNC event in any of its business or activity or any disregard towards the advice and ruling of Shariah committee or Shariah Advisory Council, they shall:

1. Immediately notify its Shariah committee about the event
2. Immediately notify Bank Negara Malaysia of the event
3. Immediately stop the non-compliant act and cease from carrying on or taking on any other similar business, affair or activity
4. Immediately come up with a rectification plan within 30 days after becoming aware of such non-compliance, and submit the plan to the Bank Negara Malaysia for the rectification process

Meanwhile, Section 28 (4) IFSA 2013 states that the bank may be put through an assessment as it thinks necessary to determine whether the institution has rectified the non-compliance events or not, referred to the subsection (3).

Failure to resolve and rectify the non-compliance issue will result them subject to punishment either under Section 59 (3) of Central Bank Malaysia Act 2009 or Section 28(5) or 29(6) of IFSA 2013. Any person who contravenes or disregards the subsection (1) or subsection (3) of Section 28 of IFSA 2013, commits an offence and shall, on conviction, be liable to imprisonment for a term not more than eight years or a fine not more than twenty-five million ringgit or be subject to both penalties. But this does not render the transaction becomes void under Malaysian Law and in fact it is still enforceable (Lee, 2017).

2.4 Methodology

A qualitative method is more suitable and appropriate for a research that explores the variation and diversity in any aspect of social life (Kumar & Ranjit, 2011). Qualitative method is concerned with subjective assessment of opinions, attitudes and focuses more on naturalistic setting. This methodology is not subjected to rigorous quantitative analysis, therefore

the data is generally expressed in words rather than numerical analysis. The result generated will be in non-quantitative form as it cannot be measured and counted accurately.

As for this study, a qualitative method is deemed to be more efficient and suitable compared to quantitative method because the exploratory way of acquiring information through interview will fulfil the research objectives more comprehensively. Therefore, qualitative research methodology that comprises interview and document analysis is adopted. Semi-structured interviews conducted with the respondents aim to explore the management and treatment of Islamic Banks towards SNC. Additional data collected through sources such as journal articles and web pages; complement the findings from the interviews.

Adopting a convenience sampling method, five (5) Islamic banks were chosen to represent the total of 16 existing Islamic institutions supervised by BNM. There are twelve (12) respondents that contributed to the findings of this study. The following table lists out the related information about the respondents for semi-structured interviews.

Table 2: List of Respondents for Semi Structured Interviews.

Bank	Positions	Nationality
Bank A	Head of Shariah Review and Assurance, Group Shariah Business Compliance	Malaysian
Bank A	Section head, Shariah Review and Assurance, Group Shariah Business Compliance	Malaysian
Bank B	Manager, Shariah Supervisory	Malaysian
Bank B	Assistant Manager, Shariah Supervisory	Malaysian
Bank C	Shariah Risk Management	Malaysian
Bank D	Director, Islamic Banking Compliance, Group Compliance	Malaysian
Bank D	Assistant Manager, Group Compliance	Malaysian
Bank E	Head of Shariah Compliance Review	Malaysian
Bank E	Shariah Advisory	Malaysian
Bank E	Shariah Advisory	Malaysian
Bank E	Shariah Review	Malaysian
Bank E	Shariah Risk Management	Malaysian

All the respondents have the experience of working in the Islamic banking industry ranging from 2 years to 10+ years. The respondents are willing to participate in the interview and give an accurate and relevant data to contribute to the topic of this study via their hands-on knowledge and vast experience in the industry to support the findings.

3 RESULT AND ANALYSIS

Each of the Islamic banks has developed its own internal Shariah governance framework to ensure the effectiveness of management within the bank and stay in line with BNM and IFSA requirement. There are no standardization on who should be appointed as Qualified Shariah Officer (QSO) by each Islamic bank. Each bank appoints different Qualified Shariah Officer (QSO) that holds the responsibility to confirm any Shariah issue detected. QSO appointed by Bank A is the Head of Group Shariah Business Company. For Bank B, the QSO is the Head of Shariah and Shariah Review function. The QSO of Bank C is the Chief Shariah Officer (CSO). Meanwhile, Bank D and Bank E both have Shariah review function as their QSO.

Furthermore, they also have different internal timeline for QSO to give the confirmation on Potential SNC. BNM only provides the reporting timeline after the QSO confirmation until the rectification plan. It has been revealed by the respondents that the internal timeline for Bank A is 10 working days. Meanwhile, Bank B and E are 14 working days, Bank C is 2 working days and Bank D is 7 working days (minimum internal timeline). The Potential SNC event that has been confirmed by QSO of the respective bank will be tabled to Shariah Committee meeting within 14 working days after the date of confirmation. If there is no pre scheduled meeting that is held within the 14 days period, Islamic banks are required to conduct an ad-hoc meeting to discuss specifically on the Potential SNC matter. The ad-hoc meeting may consist of a minimum required quorum. Shariah Committee will then decide if the event is SNC or non-SNC.

In the event when Shariah Committee confirmed it as SNC, the actions must be stopped immediately and cease from carrying on or taking on any other similar business, affair or activity. The respective business unit or the business owner shall immediately come up with the rectification plan within 30 days. The plan must be approved by Shariah Committee and Board of Directors before being submitted in ORION system. In the revised ORION policy document, the circular resolution is no longer allowed. All the Shariah Committee meeting and board meeting must be a physical meeting.

Hence, some respondents said they will try to ask for QSO confirmation for the SNC event before being tabled to Shariah Committee and get the approval for the rectification plan from Board of Directors, as close as possible to the pre scheduled meetings. This is one of the strategies to avoid calling the Shariah

Committee and Board of Directors for an inevitable ad-hoc meeting to get their approval for the rectification plan. This way, they may reduce the time gap and immediately do the rectification processes instead of stopping the whole activity after the declaration of Actual SNC.

All the respondents said the business unit or, the respective process owner will be responsible to prepare the rectification plan. It will be presented along with the evidence and documents related to justify the event in the SC meeting. However, the plan will be reviewed by Shariah Review to make sure it tackles the root cause before being tabled in the meeting. The SC and Board of Directors have to approve the rectification plan before being submitted to ORION within 30 calendar days after the reporting date of Actual SNC. If, there is no pre scheduled board meeting held within the 30 days' period, Islamic banks are required to conduct an ad-hoc meeting to get the approval on the rectification plan. The ad-hoc meeting may also consist of the minimum required quorum.

Any income derived from the activity that is declared as Actual SNC will be channelled to charity or any other means as prescribed by Shariah Committee for purification purposes.

3.1 Challenges Faced by Islamic Banks

Through the interviews, the researcher concluded that there are no major challenges in managing the SNC event in a full-fledged Islamic Bank. All new financial products and services will be reviewed and approved by Shariah Division of the bank and Shariah Committee respectively. Subsequently, the policy, documents, terms and conditions, agreements, and contracts with the respective products, services and processes must be reviewed. As such, they are able to manage the SNC from the beginning. In addition, periodic review is done by Shariah Review and Shariah Audit team to detect any SNC risk.

Unfortunately, there are many minor concerns and challenges faced in managing SNC events in the industry. Some banks gave the same concerns with the other. Therefore, the researcher compiled all the challenges as follows:

1. The Business Unit or, the 1st line of defence (management or internal control measures), did not admit any SNC risks detected, and only reported the detection as an operational risk event.
2. Lack of knowledge and skills
 - a. Working level: Lack of knowledge and competency to detect SNC, analysing and articulate the issues. The working level should

- have the knowledge and understanding in the Shariah matters. Not only the knowledge on BNM guidelines and standards.
- b. Shariah Committee: Full understanding in the technicality of the project and transaction before they come up with a decision.
3. Lack of independency on the working level and Shariah Committee.
 - a. Working level: Working level such as Shariah functions must be seen as independent as possible, not wavered and being influenced in their engagement and review. That way, the Shariah functions of IFIs may function at the maximum capacity.
 - b. Shariah Committee: Shariah Committee member is being appointed based on their qualification whereby the remuneration is paid by the bank management. They should not be influenced being in favour of the bank management or to secure the contract. They should have been clearer and firm in decision making whether to agree or disagree.
 4. *'Uruf Tijari* or more known as common industry practice is a practice which is accepted by the community and does not contradict with Shariah. An example is the credit card. Shariah Committees of Bank A already decided that credit card is not allowed due to leading a non-shariah transaction and purchases of non halal items, such as liquor and entertainment. But, the SC decision has been revised and credit card is allowed because of *'Uruf Tijari*. The concern here is how the common industry practices became the *dalil* of a certain decision instead of *dalil* from *quran* and *sunnah*. The Shariah Committee and Islamic banks have the power to control the customer from doing such transactions. They should be firmer in giving decision on a strong reason and *hujjah*. It is due to their decisions that will play a big role in ensuring the activities of Islamic banks in line with the Shariah principles.
 5. The business owner must fully understand the product and compliance culture to follow the Shariah rules. For example, disbursement of *tawarruq* facility. To avoid any mistakes that lead to SNC event, the process owner must understand that *tawarruq* transaction must require an *aqad* and additional terms and conditions compared to conventional disbursement facility.
 6. BNM did not provide a clear definition of SNC. Therefore, the Shariah Committee can be too rigid or too lenient with decision-making. For example, the customer has forgotten to complete a form in one of Islamic transaction. By the conduct, the contract is not void, it does not affect the transaction but it does not follow the requirement and procedure. With the consideration of the Shariah Committee, it can be decided as SNC or just an operational risk event. If the same issues raise again in the future, the Shariah Committee may decide it as SNC. This may lead to an inconsistency in the decision.
 7. System constraint is another issue that could compromise SNC management. Business unit is responsible and will have to take action on the rectification plan of the SNC, but in the case when the SNC arises because of the system error, the rectification plan will be delayed until it is fixed.
 8. Circular resolutions, or passing resolutions without meetings is no longer allowed in the new revised ORION policy document published in 2018. Bank C revealed they did not agree with the new requirement to have physical meetings for Shariah Committee and Board of Directors. This is a concern to them because it is not easy to schedule an ad-hoc physical meetings especially the meeting to get the approval for the rectification plan from the Board of Directors.
 9. Challenge faced by the banks to retain the right talent such as a Shariah professional that understand and embrace the full concept of Shariah in Islamic banking. For example, Bank D failed to retain a talent, who is a Shariah professional and a branch manager. He is trusted to handle the Shariah matters but unfortunately, he transferred to another bank after getting the job offer.
 10. The bank has to keep up with BNM new issuance of policy requirements, SAC new requirement process and the additional requirements. They have to manage in understanding those requirements as it can impact the product, documentation, and the system that may lead to SNC.

3.2 Recommendations to Enhance the Existing Policy and Regulations

All respondents from the five (5) Islamic banks agreed that the existing regulations and guidelines are very comprehensive and the best but the problems are in the implementation process. IFIs have the liberty to decide the level of adherence whether to be stringent or less. The Islamic banks can be more stringent than BNM but should not be less than that of BNM. Therefore, the respondents come up with the recommendations based on standardization to better improve the current policy. The Islamic banks will

have a clearer guide to decide on the status of SNC. The recommendations will be listed as follows:

1. BNM shall come up with the Shariah non-compliance (SNC) definition.
2. BNM shall come up with clear criteria of SNC. The Shariah Committee and QSO will consider the criteria in making a decision.
3. BNM to come up with the parameters to resolve the Shariah issues.
4. Some Shariah Committee being too lenient or too stringent with deciding process, as there are a lot of *khilaf* in *fiqh muamalat*. SAC of BNM should decide and publish which opinion should be followed by all Islamic banks for the purpose of standardization.
5. The SNC events reported by Islamic banks should be discussed in the meeting of Shariah Advisory Council (SAC) of BNM and the decision shall be published. As the ruling and decision of SAC is binding to all IFIs Shariah Committee, including the court and arbitrator. This will give a clear reference for Shariah Committee to give a decision on SNC event.
6. The respondents from Bank C and E agreed that BNM shall provide a clear timeline during event investigation and the process of being confirmed by the QSO to decide whether it is a Potential SNC or not. Each bank has their own internal timeline, ranging from 2 working days to 1 year or limitless (based on the complexity of the issue) but BNM should impose a clear maximum timeline for the QSO to come up with a decision before reporting in ORION system.
7. Respondent from Bank C recommends the BNM to re-allow circular resolution to get Shariah Committee decision on SNC event and the approval by Board of Directors on rectification plan.

4 CONCLUSIONS

As Malaysia adopts a dual banking system, Islamic banking industry continuously grows and pushes for new innovation for commercial satisfaction to attract interest of Muslim customers. This may lead many IFIs to develop the products and services adopted from conventional counterparts that can result in a greater exposure towards SNC risk, as the products, financial transaction, and overall activities of IFIs must comply with Shariah principles.

SNC event is usually a case-to-case basis and it does not focusing on the financial transaction only, it goes beyond documentation, terminology and

transaction. It may also arise because of the related governance and process. For instance, failure to uphold Shariah governance and fail to get the agreement of Shariah Committee on a certain deal may also lead to SNC. The Islamic banks must manage SNC risk as a pre-event control measure. They must ensure all the arrangement, terms and condition do not contradict with Shariah before the execution with continuous review done for measuring purpose

The legal regulations and framework is one of the biggest factors to the robust growth of the Islamic finance in Malaysia. The existing policy and requirements by BNM are the most comprehensive and effective in the global Islamic financial industry. However, it still needs be improved especially the SNC event aspects. Both the policy makers and Islamic banks hold the important role in enhancing the SNC treatment of Malaysia.

Conclusion that can be drawn from the five (5) Islamic banks interviewed to represents all sixteen (16) Islamic banks of Malaysia is that they faced some minor challenges in the treatment of SNC. Each bank treats SNC differently based on different factors. For instance, some banks will decide certain events as SNC but, the other bank may consider the same event as operational risks, which are the non-SNC events. It may lead to inconsistency in the SNC decision on Islamic financial industry. Therefore, the banks shall comprehend the difference between operational risk event and SNC event. The researcher supports the recommendation that has been put forward by the respondents. Firstly, the regulators shall provide a clear definition of SNC and the parameters to resolve the SNC issues. This is important to enhance the SNC treatment as the regulators or the policy makers are the only with the ability to either amend or add new guidelines and requirements for the aspects.

Secondly, the policy makers shall provide a maximum internal timeline to get the QSO confirmation on the Potential SNC after the issue detection. This is to give a clear guide for IFIs that none of them should take advantage and turn a blind eye on the issue for a while. Without the maximum internal timeline, they will procrastinate in giving a confirmation after the issue detection to have enough time to report in ORION system and completing the next requirement within the timeline. They will simultaneously hold pre-scheduled SC and Board of Directors physical meeting to get the decision and approval of the rectification plan without the need to arrange an ad-hoc meeting. From the Shariah perspective, this is definitely not allowed, as the

essential foundation of Islamic finance is the Shariah compliance with overall operations and activities. If any possible of non-compliance is detected, they should resolve it as quickly as possible to avoid disobedience of Allah's commands.

For Islamic banks, they must strengthen the competency and independency of employees in order to increase professionalism in managing the business conduct and activities. This is essential since these employees are the one who are responsible to manage the operations of IFIs and any possible SNC events. The Shariah Committee members also must be genuine based on the qualification requirement provided by BNM before a person is appointed as a member of Shariah Committee for a certain IFIs. They must be dependable, consistent and firm on their decision.

Next, the Islamic banks should increase the level of awareness on SNC risks among the business unit and employees of the banks. This enables identification of any SNC risk, monitoring and systematically controlling their respective area, and may decrease the risk of SNC. The bank must also ensure the working level is educated on the reporting requirement of SNC event and stay alert to new guidelines and requirements published by BNM as it can affect the existing documentation or system on certain products.

In addition, it is recommended to include all BNM guidelines, the reporting process and the actual SNC events in the syllabus of Islamic banking lesson for students. This is to increase the level of awareness for students on the actual practice in the industry.

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