



## External Relations Department

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### **SBP issues instructions to enhance the Stability and Soundness of Islamic Banking**

State Bank of Pakistan (SBP) has issued exclusive instructions on Shariah Non-Compliance Risk (SNCR) management, aimed at enhancing the stability and soundness of Islamic banking. The foundation of Islamic Banking lies in compliance with Shariah rules and principles in all its business activities and operations. SNCR is a unique risk faced by Islamic Banking Institutions (IBIs) and must be managed proactively. The increasing size of the industry in terms of assets and deposits, diversified operations, products and services make focused management of SNCR a necessity. In addition, the adoption of uniform practices will help in maintaining consistency over time and across IBIs.

To improve SNCR management, instructions issued by SBP require the Board of Directors (BoD) and senior management of IBIs to approve and ensure implementation of SNCR as a part of overall risk management framework in line with the size and complexity of their business. The SNCR management framework will be developed using SBP's instructions on Shariah principles and decisions in conjunction with rulings and fatawa of the Shariah Board of the IBI as key reference points. These will allow for the identification of risks and controls in different products, services and business activities. As per SBP's instructions, IBIs should take necessary steps to ensure that relevant members of BoD and senior management possess requisite knowledge and understanding of the risk management of SNCR.

SBP's instructions require IBIs to have an appropriate reporting mechanism, including frequency and thresholds for reporting of SNCR events to the BoD or its sub-committee. IBIs will also be required to maintain proper record of Shariah non-compliant events or transactions and furnish to SBP, on a quarterly basis, the details of actual losses incurred.

Issuance of current instructions coupled with existing comprehensive Shariah Governance Framework will help to achieve targets laid down in the third strategic plan for Islamic banking recently issued by SBP.

SBP's Circular on SNCR can be accessed at <https://www.sbp.org.pk/ibd/2021/C1.htm>

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