Deanship of Graduate Studies

Al – Quds University

The Extentof Basel Accord implementation on Islamic Banks in Palestine

The case of Palestine Islamic Bank

Raneen Abdaljaleel Mohammad Ayyad

Master Thesis

Jerusalem – Palestine

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Dedication

I *dedicate my dissertation to my family and friends. A special thank you goes to my parents who never hesitated to show support, care and love for me since my childhood days.*

For his words of encouragement and the continuous support he gave me throughout my journey in this program, my beloved Husband I am very thankful to have you

My brothers and my sister, where the source of unlimited happiness and comfort when I was down, and for this I don't have enough words to thank you

I also dedicate this dissertation to my many friends and who have supported me throughout the process. I will always appreciate all they have done.

I am now about to end the road I am on, and I will start a new one, which will not be difficult with all of you by my side

My sincere regards to all of you

Declaration:

I certify that this thesis submitted for the degree of master, is the result of my own research, except where otherwise acknowledged, and that this study (or any part of the same) has not been submitted for a higher degree to any other university or institution.

signed: .....

Raneen Abdaljaleel Mohammad Ayyad

Date: 08/06/2020

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Abstract:

The main aim of this study is to demonstrate the implementations of Basel II accord in Islamic banks in Palestine (a case study of Palestine Islamic Bank). In order to achieve the aim of the study, the researcher used the descriptive analytical approach, where the researcher distributed a sample on (145) from the employees of the Palestine Islamic Bank in all branches in Palestine. and the study tool was represented in the questionnaire, which consisted of six axes with (36) paragraphs.

The main result reached in the study is that there is an implementation of the Basel II Accord in the Palestine Islamic Bank with a high mean of (4.45), the supervisory review field according to the Basel II Accord got the highest mean of (4.51), market discipline according to Basel II Accord with a mean of (4.48) followed by the tasks undertaken by risk management in Palestine Islamic Bank with a mean of (4.477), principles on which risk management in Palestine Islamic Bank is based on a mean of (4.47), then the minimum capital area and methods of measuring risks in accordance with the Basel II Accord with a mean of (4.399). The last field was the application of the Basel III Accord with a mean of (4,296), all of which came in a high degree.

Based on the results if this study, the researcher had some recommendation in which the most important ones are: strengthening and qualifying human resources to supervise the various risks and develop their capabilities, develop tools and systems for measuring risk according to internal evaluation methods and to commit to the Islamic rules and regulations in the Islamic banks in order to sustain the competition level in the market with the traditional banks.

مدى تطبيق اتفاقية بازل في البنوك الاسلامية في فلسطين

دراسة حالة البنك الإسلامي الفلسطيني

اعداد: رنين عبد الجليل محمد عياد

اشراف: د. عروبة البرغوثي

ملخص

هدفت الدراسة التعرف إلى مدى تطبيق اتفاقية بازل (2) في البنوك الإسلامية ، دراسة حالة على البنك الإسلامي الفلسطيني، ومن أجل تحقيق أهداف الدراسة عملت الباحثة على استخدام المنهج الوصفي التحليلي، وبلغت عينة الدراسة (145) موظفاً وموظفة من موظفي البنك الاسلامي في جميع الفروع العاملة في فلسطين، وتمثلت أداة الدراسة في الاستبانه والتي تكونت من ست محاور بواقع (36) فقرة.

وتوصلت الدراسة الى نتائج أهمها أن هناك تطبيق لاتفاقية بازل(2) في البنك الاسلاميالفلسطيني، وجاءت النتيجة بدرجة عالية (4.45)، وحصل مجال المراجعة الاشرافية وفق اتفاقية بازل (2) على أعلى متوسط حسابي (4.51)، ومن ثم مجال انضباط السوق وفق اتفاقية بازل (2) بمتوسط حسابي (4.48)، يليه مجال المهملم ليتا تقوم بها إدارة المخاطر في البنوك الاسلامية بمتوسط حسابي (4.477)، يليه مجال المبلدئ ليتا تقوم عليها إدارة المخاطر في انبلوك الاسلامية بمتوسط حسابي (4.47)، ومن ثم مجال الحد الأدنى لرأس المال وأساليب قياس المخاطر وفق اتفاقية بازل (2) بمتوسط حسابي (4.399)، يليه مجال تطبيق اتفاقية بازل (3) بمتوسط حسابي (4.396)، وجميعها جاءت بدرجة عالية.

وأوصت الباحثة بتوصيات أهمها تقوية وتأهيل الموارد البشرية للإشراف على المخاطر المختلفة وتنمية قدراتها وتطوير أدوات ونظم قياس المخاطر وفقاً لطرق التقييم الداخلي للاستفادة من مزايا هذه الطريقة من قبل البنوك الإسلامية، بالاضافة إلى التزام البنوك الاسلامية بالقواعد الإسلامية لتحمل البنوك التقليدية.

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List of Abbreviation:

CAR	Capital Adequacy Ratio
PMA	Palestinian Monetary Authority
RWA	Risk Weighted Assets
CR	Credit Risk
MR	Market Risk
OR	Operational Risk
AAOIFI	Accounting and Auditing Organization for Islamic Financial Institutions
CB	Conservation Buffer
BIS	Bank International Settlement
VaR	Value at Risk
IFSB	Islamic Financial Service Board

Chapter One

1.1 Introduction

The banking system in general includes various risks that require taking precautions and adequate procedures to manage and control these risks according to the international best practice in order to mitigate potential risk exposures or avoid them. As a result of the increasing financial crisis in countries around the globe that resulted in the collapse of many reputable international banking institutions, which was a result of the inadequate managing and controlling their risks. In this context, the Basel II accords was introduced in the year 2006 as a framework for risk management considering early warning system that enable regulatory authorities to concentrate and pay attention on problematic banks instead of all banks. Although major differences exist between Islamic and conventional banks regarding the nature of capital, it is required for Islamic banks to comply with international banking standards and provide viable and safe banking grounds Bohaidar, Roukia; Laraba, Mouloud (2010).

However, it is not altogether clear whether the imposition of capital requirements actually reduces risk-taking incentives. It is extraordinarily difficult - if not impossible – for regulators and supervisors to set capital standards that imitate those that would be demanded by well informed, undistorted private-market participants. For instance, banks may respond to regulatory pressure by increasing their risk exposure. Moreover, actual capital requirements may increase risk-taking behavior. In a guarded assessment, Thakor (1996) shows the conditions under which risk-based capital requirements increase credit rationing, with negative implications for economic growth. Also, Thakor and Wilson (1995) argue that higher capital requirements may induce borrowers to shift to capital markets and in the process impair capital allocation, while Gorton and Winton (1999) show that raising capital requirements can increase the cost of capital. Thus, theory provides conflicting predictions on whether capital requirements curtail or promote bank performance and stability. The Basel Committee on Banking Supervision was established as the Committee on Banking Regulations and Supervisory Practices by the central-bank

Governors of the Group of ten countries at the end of 1974 in the aftermath of serious disturbances in international currency and banking markets. The first meeting took place in February 1975 and meetings have been held regularly three or four times a year since. (Swaan, 2009)

Islamic finance, as an industry, has been witnessing substantial growth in the past decade. From the business side, the sector has mainstreamed within the global financial system, developing as an effective tool for financial development. The mechanism of Islamic banking has its own nature and is different from that of conventional banking in some key ways. For example, traditional banks are based on debt and allow the transfer of risk, whereas Islamic banks are linked with the real economy (materiality) and promote risk sharing so they are less prone to risks. Conventional banks charge interest and fees for loans and other services. Meanwhile, Islamic banks prohibit interest-based transactions and eliminate debt contracts, yet they earn their money by profit and loss sharing, trading and using other Sharia contracts of exchange. Though the principles underlying Islamic finance are as old as the religion itself, modern banks did not start offering *sharia*-compliant products until the mid-1970s. Since then it has grown into a global industry, with total assets of around $2 trillion. Most of that (nearly 80%, according to Malaysia's central bank) is entrusted either to Islamic banks or to the Islamic units of conventional banks. The rest takes the form of *sukuk*, Islam's answer to bonds (15%); Islamic investment funds (4%) and *takaful*, the Islamic version of insurance (1%). In 2012 Iran accounted for 43% of the world's Islamic banking assets, with Saudi Arabia (12%) and Malaysia (10%) ranking second and third**.** (Islamic Financial Services Board report,2016).Western firms are also beginning to use sukuk to raise money. SociétéGénérale and Bank of Tokyo-Mitsubishi UFJ, French and a Japanese bank respectively, have issues in the works; Goldman Sachs is reportedly considering a $500m offer.Such rows have led to calls for greater international standardization for Islamic finance.

The International Standards of Banking Supervision, issued by Basel Committee in the first and second version, has not taken into account Islamic banks, but the Islamic Financial Services Board (IFSB) in Malaysia -which is considered a reference framework institution that most Arab central banks ratify the standards and instructions it issues regarding Islamic Banks- develops special standards for Islamic Banks in the field of good governance rules, capital adequacy and transparency, but the crisis proved the importance

of having sufficient risk-based capital according to the requirements of Revised Basel Framework for capital adequacy. The Islamic banks dependency on principals that are deeply-rooted in the Islamic economy and built on doctrine, the ethical factor and real basis, does not devalue the importance of institutional governance in the management of risks that are higher than those of traditional banks due to subjective reasons which lay in the nature of Islamic investment instruments, and to objective reasons because the institutional, legal and regulatory environment of Islamic banks has not completed yet, in addition to the problems of the market imperfections such as the information asymmetry that leads to moral hazard and adverse selection problems. Moral hazard, in which the borrower uses the loan in risky business and adverse selection as a result of the reality that most bas business needs money and ask for loans which entails the existence of solid risk management framework to handle these issues. Islamic banks not only face the conventional bank risks, but they also are confronted with "new and unique risks as a result of their unique asset and liability structure". According to Khan and Ahmad, these new type of risks are an immediate outcome of their compliance with Sharia law.

The study of the minimum capital requirements of Islamic banks is relevant due to the principle of risk and profit sharing that could, in turn, reduce the overall risk incurred by the bank (Pellegrina, Dalla, 2007).The Islamic banking system, mainly the investment loss and profit sharing, foster the investor's participation in equity, which promotes the assiduity in the investment management and proper monitoring. Furthermore, the other Islamic financial mechanisms (such as Murabaha, Ijara and Istisna) require the involvement of investors in the real economy; as a result, financial transactions are fully backed by real assets. This feature enables Islamic banks to have a clearer view on the allocation of funds and reduce their exposure to speculative behavior (Khediri, Charfeddine& Ben Youssef, 2015). Siddiqui (2006) argues that equity-based Islamic contracts will reduce adverse selection and moral hazard problems, which thereafter, downplays the credit risk of these Islamic financial institutions. Actually, Islamic finance requires information symmetry and transparency in their transactions since Islam prohibits excessive uncertainty (gharar). Moreover, the case of Islamic Banks in Palestine is important to study to the increase of dependency on Islamic banks and the great expansion in their branches that we are visualizing nowadays.

Traditional capital adequacy standards (Reserve bank of New Zeland), 15 May 2006):

Ratio of Capital to Deposits standard: it is one of the most commonly used standards to measure capital adequacy. It has been widely used by American banks till early 1940s; they relinquished it in 1942 in the light of purchasing government bonds by banks and creating deposits for the purpose of funding the American military efforts in the World War II. This standard is based on controlling the risks arising from the increase of total deposits over a certain ratio to the capital. It is worth mentioning here that central banks adopted the 10% as a suitable capital adequacy measurement, i.e. deposits are equal to ten times the capital.

Ratio of Capital to Assets standard (leverage):according to which banks are rated in five ratings; the book value, however, is the basis in calculating the leverage ratio, which is the basis in evaluating a bank's capital adequacy.

1- The leverage ratio > 5%: the bank is well capitalized.
2- The leverage ratio >= 4%: the bank is adequately capitalized.
3- The leverage ratio < 4%: under capitalization degree.
4- The leverage ratio < 3%: the bank is not capitalized.
5- The leverage ratio <= 2%: the bank is in a critical situation regarding its capital composition.

If the leverage ratio comes to 1%, it becomes necessary for the supervisory authority to intervene to correct the situation although relying on the leverage as a capital adequacy measurement has several weaknesses:

Risk-weighted capital standard: (Capital Adequacy ratios basic course on evaluating financial performance and portfolio risk , 2004) in 1993, Basel Accord 1 included credit risks in the capital adequacy measurement; in 1998, the Accord was amended by adding market risks; in 2006, in the Revised Basel Capital Framework or Basel 2, operational risks were added to the capital requirements; credit risks assessment was increased compared with those defined in Basel Accord of 1993 alongside with distinguishing between credit risks of the different items of on- and off-balance sheet's assets when calculating the capital adequacy ratio, i.e. assets are weighted by risks according to specific ratios and weights defined in Basel 2, that's for assets; and regarding the capital, distinction has been made in calculating capital adequacy ratio between two main tiers: the first is the core capital and the second is the supplementary or secondary capital. In addition to the

two tiers, some supervisory authorities request the existence of a third tier as a supplementary capital to be used in contingencies. Basel committee in its final version (adjusted frame work for risk based capital adequacy) fix minimum ratio 12% for capital adequacy in the context of pillar one , and supervisory review for this ratio in pillar two , as the supervisory authority will have the right to check the situation of capital of the bank , to be sure that it is adequate according to the risks have been taken by the bank , with the right for supervisory authority to ask the bank to raise the capital if necessary , and according to pillar three of Basel two , the disclosure is necessary for market discipline , in this issue the participant of the market will know the capital of the bank , and it's risks and the quality of its assets .

The main difference between Basel 1 principles and those of Basel 2 is the necessity for banks to have a capital to face a wider range of risks that are not confined to market and credit risks, but adds to them operational, interest rate, exchange rates and liquidity risks.

Basel Revised Capital Framework (Basel 2) (Methods for calculating international Capital Adequacy ratios (update Jan. 2006): this standard is not new; it had been used in America and Britain. It is not just a relationship between the regulatory capital and the assets weighted by different risks; an in-depth look at it would lead to the following:

1- It faces the invisible and difficult to calculate risks through different risk measurement approaches, i.e. capital becomes like a protection cushion when the bank faces risks.
2- Shareholders' funds are the basis in facing risks. If shareholders in banking benefit from depositors' funds, their contribution to the bank should be no less than the level that protects depositors' funds in the face of risks.
3- The relationship between the capital and the risky assets is a continuous one. The more risky assets increase, the more capital is needed. That is to say the capital is no longer the specific amount required to establish a project at the beginning of its work; there is a continuous need for capital in parallel with the growth of risky assets.
4- The major risks by which the assets are weighted are the credit, market and operational risks. On the level of countries, Basel standard distinguished between the weights used for assets risks; it gave the assets in which the debtor is an OECD

member-state a risk weight of zero, whereas it may be up to 100% for other countries.

5- As for the exchange rates risks, the standard distinguished between the weights of assets risks in local currencies and their equivalent in foreign currencies due to the risks implied in the exchange rates of foreign currencies. Regarding market risks; risks are calculated according to time contracts; a contract's value estimation according to the rate used when the ratio is calculated means the inclusion of market risks.

6- The standard has not taken into consideration the collaterals the banks get in return for the credit given, except in the case of real estate collaterals for residential properties; it gave them risk weights of 35% and 75% if the real estate is commercial, due to the liquid nature of the personal residence loans, which are securitized in the developed countries; also, they are easy to sell and insurance companies guarantee their settlement. The standard gave a zero risk weight for loans secured by cash assets.

7- The standard takes the comprehensive capital concept on the basis that everything provided by shareholders and anything generated inside the bank is for their interest, provided that those funds can be used without barriers or reservations to face the losses before they reach creditors' funds. Therefore, the capital concept is not limited to the capital paid, reserves and retained profits, but also includes the general allocations, the undeclared reserves and the differences in the assessment of fixed assets, securities, and subordinated loans that the bank gets from its shareholders and the loans offered by others that have capital characteristics in terms of bearing risks.

Regarding the denominator used when calculating the capital adequacy ratio including the market risks, we calculate the assets and items on- and off-balance sheet to be weighted by credit risks, then we add to them the market and operational risks, so that when the assets are weighted by risks, we take into consideration the body with which the bank deals according to the standard rating developed by Basel Committee that includes five categories of weights (10%, 20%, 40%, 50%, 100%). The bank's level of development and complexity of its operations determine the approach used to calculate each of the market and the operational risks, as the Supervisory authority may rely on the bank's internal assessments in case it finds the bank ready for that, or may rely on external rating organizations' ratings, taken into consideration that the developing countries face a big

problem in the absence of developed and reliable classification organizations to rate their risks, that makes the supervisory authorities focus on the necessity for banks to enhance the role of external auditor, and the necessity to have an internal competent auditor whose work is risk-based rather than inspection-based.

1.2. Statement of problem

The existence of risk management framework in Islamic banks is the necessary and adequate condition for maintaining a strong, safe and transparent Islamic banking sector for objective considerations related to the external environment and subjective considerations related to the business environment of the bank, sothe researcher wanted to know the extent of Basel Accord implementation on Islamic Banks in Palestine, the case of Palestine Islamic Bank.

1.2.1. Subjective consideration:

1. Considerations related to the Islamic Bank's balance sheet on its both side's assets and Considerations related to the principles of Islamic banking, which involve the sharing of profit and loss that requires transparent control to preserve the interests of deposit holders whose relationship with the bank build on absolute confidence as customers accept profit and loss, the investor holds "bank" risk is one of the fundamentals of Islamic banking Based on the rule of "AlgonmbelGorm " derived from the talk of "Alkheragbel Daman", and therefore no investment treatment is based on the separation of Algonm and Al gorm, that guarantee the bank receives a return without bearing risk, any contract includes the guarantee of the capital invested or profit contract forbidden Shar3an , However, risk mitigation or avoidance is legitimate only if it is done in accordance with the legal formulas and mechanisms. Islamic banks have risks such as traditional banks with different nature, uniqueness and diversity, with diversified Islamic financing and investment tools from debt-based instruments to asset-based instruments.

liabilities, on the asset side, fund uses have a privacy that makes them different from that in conventional banks. They are not debt-based, as in conventional banks, but rather are equity based and asset- Asset-base .

On the liabilities side, the bank's responsibility for deposits and capital is "limited liability", unlike conventional banks where the bank's responsibility towards deposits and capital is unlimited. The bank is obliged to pay an interest rate to depositors regardless of whether the bank makes profits or did not.

2.Resent experience of Islamic banks in comparison with conventional banks

3. Incomplete structure and modeling as in conventional banks.

4. The great experience of Islamic banks and their achievements in a relatively short time necessitating a great and qualitative effort to preserve them.

1.2.2. Objective considerations

1. In the regulatory aspect of the Islamic banks, the absence of a unified regulatory body with more than one regulator for the work of Islamic banks with a difference in Ijtihad where some tend to indulge and another tighten, which leads to weakening the link of Islamic finance to the real economy which is the essence of Islamic finance and the basis of its strength and integrity and ability to confronting crises.

2.The high sensitivity in the area liquidity risk management in Islamic banks is either due to difficulty in obtaining liquidity through borrowing **(funding liquidity risk)** or asset liquidation**(asset liquidation risk)**. The liquidity risk faced by the bank as a result of the inability to obtain the necessary liquidity from one of the exporters is very important because Islamic banks may face serious problems related to liquidity risk for several reasons:

3.(high restriction) constraints resulting from compliance with Islamic law, which prohibits the securitization of the assets of the bank to obtain liquidity, these assets often take the nature of the debt (debt-based assets).

4.slow development somewhat in the Islamic modes of finance, Islamic banks are still not able to provide the necessary funding from market in the suitable image and the right speed, this problem becomes more serious and urgent because of the absence of interbank or overnight lending between banks (money market), which is an important source for banks to obtain liquidity in the short and in a timely manner and appropriate quantity.

5. There is no lender of last resort (lender of last resort) as a gateway to access liquidity in Islamic banks like the situation in conventional banks, which rely heavily on this port to obtain the necessary liquidity as needed through the Central Bank to justify due to the reason for the prohibition of interest in banks Islamic and which prevents access to the Central Bank to obtain liquidity in case of emergency, which requires good management of liquidity risk in Islamic banks and thus the need for a high degree of transparency and clarity in the bank's liquidity risk management and other at appropriate times without affecting the continuity of the bank in the market.

6. There is a lot of privacy and individuality and diversity in forms of Islamic finance, and to preserve the rights of depositors require a high degree of disclosure that the applicant applied to him the principle of participation in the profit and loss, the work requires special accounts for each type of financing different accounting rules and to verify the bank's prudent to invest sources of funds available to it, which is the Bank's commitment towards the owner's manual is about as limited Unlike traditional banks, where is the Bank's commitment towards the owners and depositors unlimited nature of the deposits in Islamic banks and sustainability in line with the examples of Islamic finance, which imposes the length of the nature of funding and the fact that an important part sources of funds the bank creates a complementary relationship between the owners of deposit accounts and owners, the fact that investment funds are placed on the principle of profit and loss, to the extent that some schools of law, tend to name depositors silent partners.

7. The sensitivity of the work of Islamic banks to make sure the public is necessary and sufficient condition to preserve the Islamic banking industry an efficient, effective and safe and sound, capable of performing the role assigned to him in the side of the Economic and Social Council include consideration of moral and religious dimension is required in this type of banks

*** Risks in Islamic banks**

Generally speaking risks of moral hazard and adverse selection are result of asymmetric information in the markets , before lending process adverse selection problem exists when bad business ask for loan ,banks handle this problem by credit rationing and raising the interest rate , moral hazard problem happen after lending process when creditors use funds in bad business .

The risks faced by Islamic banks are similar to the risks faced by conventional banks. However, the risks of Islamic banks are the different and varied as a result of diversified forms of investment in which Islamic banks invest their money such as Moshrakeh, Modarabeh and others. Each of these formulas has risks associated with thenature of the formulas used. The risk of Mosharakeh is concentrated in administrative and marketing risks, and the risk of Modarabeh is concentrated in the extent of the honesty and efficiency of Al shareek al Modareb and in the market risk and the difficulty of auditing, evaluation and follow-up of the project by the bank. The risks associated with Murabaha include non-compliance with the specifications of the purchase order. The risk of Istisna'a is the risks involved in transportation, storage, fluctuations in prices and non-payment. The risks of Al (Ejara el montaheyabeltamleek) includedefault, non-payment and bad use of the tenant. In general, we say that the administrative risks, market risks, guarantees and risks related to the customer, the nature of the operation financed, the currency used, and the repayment risk surround the various financing and investment formulas. Accordingly, each financing or investment formula should be examined separately to determine the risks surrounding them.

The Islamic Financial Services Board (IFSB) in Malaysia and AOFE in Bahrain considered a reference framework institution that most Arab central banks ratify the standards and instructions it issues regarding Islamic Banks- develops special standards for Islamic Banks in the field of good governance rules, capital adequacy and transparency. butthe crisis proved the importance of having sufficient risk-based capital

Basel framework for risk – based capital adequacy ratio has not only focused on developing banks 'sensitivity to risk and thus more accurately in banks' capital adequacy risk assessment criteria. Rather, it has created a solid platform for effective risk management in banks by stimulating financial disclosure to achieve Transparency in banks to the realization of the system of institutional governance, which in turn strengthens the elements of accountability and disclosure, applying basel 2 standards in Islamic banks achieves effective risk management in Islamic banks through an internal rating process and appropriate control systems.

It is easier for Islamic banks to apply the Basel International standards if separate capital criteria for investment deposits and demand deposits to ensure the protection of demand deposits on the one hand and the transfer of investment deposits to specialized investment

funds Which in turn will set international standards for Islamic banks that expand the acceptance of this type of investment and strengthen its competitive position at the global level.

There is a need, therefore, to establish a unified organizational or regulatory body to set regulatory standards and a suitable framework for supervision of Islamic banks, with the need to create a class of regulators and observers to strengthen the capacity of banks to carry out internal classification and to build effective systems of control and risk management in Islamic banks, And to achieve more efficient use of capital and stimulate growth and stability, in line with the principles of Islamic finance.

"No obstacles- no special favors" This statement describes the view of regulators in Britain on the subject of supervision of Islamic banks, where the application of Basel International standards on Islamic banks should not be subject to any controversy or debate As Islamic banks achieved rapid growth over the past two decades expected to continue in the coming decades**(Islamic Financial Services Board report , 2016)**(estimated assets of Islamic banks 500 milliard predicted to jump to 1 trillion by the end of 2017), so applying Basel 2 standards in Islamic banks will lead to positive effect on international financial markets stability**.**

The additional burden required to apply Basel 2 standards in Islamic banks does not justify the failure to provide the necessary data and information, because this is a violation of the professionalism of the Islamic banks governed by set of controls are characterized by continuity and stability in the religious, moral, social and economic sides. Compliance of Islamic banks to Shariah rules and the fact that their references to the Qur'an, Sunnah and Ijtihad does not prevent the application of the Basel standards to make these banks a strong, safe, healthy and efficient financial institution capable of playing a role in providing the real economy with the amount of credit required to finance its activities. (MalcolmKnight, 2015)

1.3 Questions &hypotheses

The Purpose of this research is to check the reality of applying basel international standards for banking supervision on Islamic banking with special reference to Islamic Bank of Palestine (IBP) , to achieve this purpose We have analyses the content IBP annual reports and interviewed a senior executive , and the head of compliance department and

risk management department to determine the extent of the implementation of basel2 international standards in IBP bank and to identify the issues and to answer these questions:

The first question

What is The Extent of Basel Accord Implementation on Islamic Banks in Palestine?

And emerged from this question the following sub-questions.

1. What is the level of implementations of Risk principles exposed over Islamic banks?
2. What is the level of implementations of Risk management tasks in Islamic banks?
3. What is the level ofMinimum capital and risk measurement methods in accordance with Basel II in Islamic banks?
4. What is the level ofSupervisory review according to Basel II in Islamic Banks?
5. What is the level Market discipline in accordance with Basel II in Islamic Banks?
6. What is the level of Implementation Basel III in Islamic Banks?

The second question

Is there any differences in level of The Extent of Basel Accord Implementation on Islamic Banks in Palestine according to the variables(gender, Job title, educational qualification, years of experience, age)?

To achieve this Question, the following hypotheses will be answered:

1. The first hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in the Extent of Basel Accord implementation on Islamic Banks in Palestine due to the gender variable"

2. The Second hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in the Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Job title variable"

3. The third hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in the Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Educational qualifications variable"

4. The fourth hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in the Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Years of experience variable"

5. The fifth hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in the Extent of Basel Accord implementation on Islamic Banks in Palestine due to the age variable"

1.4 Importance&Objectives of Study

The importance of this study is to determine how to apply the international regulatory standards to Islamic banks, which can enable us to understand the strengths and weakness of the management of risks, and to provide the appropriate solutions. Furthermore, it is also important to understand the extent of Basel Accord implementation in Islamic banks regardless of the differences they encounter when it comes to financial instruments' trading..

1.5 Study Population:

The study population consisted of all Islamic bank employees in Palestine, where a questionnaire was distributed over 150 individuals from the 9 different branches. The questionnaire was distributed electronically due to the current situation.

1.6 The study Sample:

A questionnaire was distributed over 145 individuals from both genders between the Mid of March until the Mid of April.

1.7 Study Limitation:

Furthermore, as of the 3rd of March 2020, the Palestinian monetary authority announced that the 6th law published in 2015, that took into consideration the implementation of Basel II in Islamic banks was no longer valid, and the PMA decided to establish the framework according to Basel III criteria and increase the CAR percentage to 13% according to the 9th law of the year 2018. However, this research took into consideration the long period of implying Basel II in the Islamic banking sector in Palestine, and the resources that we found were mostly in regards of this topic.

1.8 Objectives of the study:

- To understand the risks of Islamic banks in Palestine
- Understanding how to calculate the risk – based capital adequacy ratio
- To ensure that Islamic banks are implementing Basel standards in Palestine
- To answer the question: how can the Basel standards be applied to Islamic banks in Palestine?

1.9 Research plan

In order to achieve the purpose of this paper we will present in first section an overview of Islamic banking history and improvements, in the next section we will present an overview of Basel II. Section 3 will be consecrated to the presentation of IFSB and its standards which are related to Basel II. In section 4 we discuss the guidelines issued by PMA in relation with the implementation of Basel II. In section 5 we carry out the investigation of the implementation of Basel II by IBP and the related issues. The conclusion will constitute the final section.

1.10 literature review

A. HABIB AHMED (2014) in his paper discussing risk management is central in operations of financial institutions, both from business and regulatory perspectives. Risk management is not only about identifying and mitigating risks, but involves a strong risk management system that includes establishing appropriate risk management environment, maintaining an appropriate risk management process, and instituting adequate internal controls. This paper provides a measurable tool to assess the risk management framework in Islamic banks. The structured assessment methodology provides indices that gives a quantitative assessment of not only the overall risk management system of a financial institution, but also indicates the strengths and weaknesses of various aspects of this system. The assessment process can be used by Islamic banks and regulatory authorities to identify the weaknesses and improve upon the risk management framework. The paper provides examples of how the assessment method outlined can be used to estimate the status of risk management system for two Islamic banks. The paper provides a framework to assess the RM system of an Islamic bank. Given the importance of RM in

contemporary financial institutions, it is important to assess the RM system and identify its strengths and weaknesses. For any bank to have a comprehensive RM system, some basic elements should be present. The RM system is divided into three components under common and Islamic factors. The latter factors are unique to Islamic banks due to compliance with Sharah rules. The paper identifies items that can be used in different components under the two factors. These are quantified to produce indices of the RM system and its components. Risk management is going to be increasingly important for financial institutions in the new regulatory and business environments. With a quantified index of the RM system, the regulators would be able to identify the risks inherent in different banks and propose remedial guidelines and policies. While the RM system of individual financial institutions will depend on the nature of activities and the size and sophistication of an institution, the framework outlined here can be a basis to build and expand on. The modified version of the RM system assessment framework can be used by both, regulators and Islamic banks, to ensure that a comprehensive RM system is in place.

B. Nico P. Swartz (2013) in his paper discussing that Islamic banking and finance has become a US$100 billion industry and is estimated to grow at a rate of 15% per annum. The essential feature of Islamic banking is that it is interest-free. As a result of this, the Islamic financial system is primarily equity-based. Islamic banks therefore conduct business on a profit-/ loss-sharing principle. Under this arrangement, the provider of capital and the entrepreneur share in the risks and rewards of a ventures to remain competitive, it is important for Islamic banks to find out what their risks are, control them, and monitor them routinely. The objective of this paper is to overview the guidelines for risk management in Islamic banking. Issues related to the nature of risks arising from the use of funds of Islamic financial institutions and their implications on the banking book of Islamic financial institutions are also to be considered in this paper.This paper addressed the objective stated in the abstract. It enabled the reader to know what the risks are for the Islamic economic model. With this knowledge to his/her disposal, the reader will be able to control the risks which hindered the Islamic finance model. As a result thereof, monitoring the Islamic model becomes much easier so that guidelines for risk management can be effective. It must though be Shariah-compliant, in order for the profit and loss sharing principle, which underlies the

Islamic model, to materialize. Under the profit and loss sharing principle, the Islamic system redistributes the consequences of uncertainty over all parties to a business. Debt-financing of the conventional system, in contrast, relieves the financier from uncertainty by shifting it on the real investor, who then alone bears the entire risk of the enterprise. By spreading the same risk over more heads, the Islamic economic system would promote stability. From the standpoint of financial stability, it appears that the Islamic interest-free system does have merit and deserves more serious attention from academics and policymakers alike, especially in view of the recent crisis and rampant bank failures in contemporary economics. On the strength of its stability, Islamic banking is in fact less risky in terms of external shocks, liquidity risks and insolvency risks than conventional banks. These characteristics made Islam banks less vulnerable to risk than conventional banks. Due to its conservative characteristic, Islamic banks have limited access to liquidity, so that it enables investor's stable and competitive returns. On these grounds, investors are given a greater incentive to exercise tight oversight over bank management, since they share risks.

C. Monzer, Kahf (2012) in his study Basel II: Implications for Islamic Banking concluded the following:

1. Islamic bank have qualitatively similar credit risk to conventional banks, therefore the processes of the calculation of minimum equity requirement for credit risk exposure should not be different from the methodologies proposed for conventional banks. This means that the Islamic Banks can go along with this part of the Basel II Proposed Accord and the supervisory authorities would be fair in asking them to abide by these proposals.

2. In Islamic banks, equity must be interpreted to include the equity of shareholders and the equity of the owners of unrestricted deposits because the latter carry their share of the risk of losses by virtue of the Mudhaarabh contract.

3, Elements of fairness must be taken into consideration in distributing the losses as well as in distributing equity charges between the shareholders and owners of unrestricted deposits.

4. The portion of operational-risks minimum capital charges to shareholders in Islamic banks is apparently lower than their counterpart in the conventional banks. Here again the reason is the Mudarabah contract that does not charge the Mudarabah for losses not-

resulting from negligence, fraud or violation of contract including violation of normal and customary professional standard practices. This means that while the parameters of operational risk weighing and minimum equity calculation in Islamic banks may be the same as in their conventional counterpart, the capital burden on shareholders should be lower than that in conventional banks.

5. Trading book risks, in their literal sense, rarely exist in Islamic banks but quasi-trading book risks are much higher in Islamic Banks than in the conventional banks. Here again, capital charges should be carried by both shareholders and owners of unrestricted deposits.

6. Although the supervisory authorities in countries where there are Islamic banks did not yet fully apply the review procedures suggested in Pillar 2 of the New Basel Accord, the application of these proposals does not pose any theoretical or practical impediment to Islamic banking or to Islamic modes of financing.

7. The same also applies to the disclosure requirements of Pillar 3 since whatever the existing level of disclosure in Islamic bank may be, the additional information and their standardization do not pose any theoretical or practical difficulties more than they do for conventional banks.

D. Kayed and Hassan (2011) have described a financial crisis as an event that includes sovereign default, stock markets crashes, and currencies crises. The two authors argued that in 2007–2008 the banking and financial crisis resulted in the accumulation of excessive liquidity, irresponsible lending policies, and the excessive use of complex financial products by banks, along with the quasi-absence of regulatory and supervisory authorities. This so-called diversification of risk between different financial parties did not minimize bank risk exposure as regulators believed that it encouraged financial institutions to benefit from financial derivatives. This led to more risk exposure and resulted in rapid contagion and the spread of losses when indications of financial distress started to appear.

E. Mohammad Bitar (2014) attempt to examine whether banking regulations have the same impact on the stability and the efficiency of Islamic than for conventional banks. We benefit of Basel III recommendations to investigate the impact of bank capital, liquidity and leverage requirements on the stability and the efficiency of Islamic banks compared to conventional banks. A first exploratory study uses

Principal Component Analysis, Logit and Profit methods, and OLS regressions and shows that Islamic banks have higher capital, liquidity, and profitability, but that they are less stable than their conventional counterparts. A second empirical study examines the stability of Islamic banks using conditional quintile regressions and proves that Islamic banks are less stable than conventional banks. It also shows that higher capital and lower leverage improve the adjusted profits of small and highly liquid Islamic banks. Liquidity is positively associated with the stability of large Islamic banks while an opposite effect is detected when small Islamic banks are examined. Finally, we study the efficiency of Islamic banks using Data Envelopment Analysis (DEA) and find that Islamic banks are more efficient than conventional banks. We also find that higher capital and liquidity requirements penalize the efficiency of small and highly liquid Islamic banks, while the opposite is true for financial leverage. These results show that concerning capital requirements for small and highly liquid Islamic banks, a possible trade-off could be found between stability and efficiency.

F. Adam Ja'far (2015), The study aims to identify the standard capital adequacy adapted by the Islamic Council of service standards Financial and its role in reducing the impact of bank credit risk. the study problem that banking risks pose Mahdda ً a significant in the face of the banking system, and specifically credit risk banking because they represent the largest proportion of Total banking risks. In order to create a favorable financial banking environment, these risks must be avoided or reduced. The impact of the study has been formulated in the following questions: Does the application of the Adequate Capital Adequacy Standard in accordance with the standards of the Islamic Financial Services Board reduce the effects of the risk risks? Can it protect, maintain, and stabilize deposits? Is banking safety in number possible due to the presence of banking risks when applied? Used the study descriptive and analytical approach and some statistical methods, the study found a group of the most important results: that the application of the standard capital adequacy adapted according to the Council of service standards for Islamic financial result in the identification and control granted funding ratios for clients, which reduces the risk of bank credit, and lead to the protection of depositors and increase Customer confidence, the study concluded a set of recommendations, including: addressing some of the negative aspects Dah in standard capital adequacy, such as

discriminatory nature towards the governments of developing countries, and the entry of new credit rating agencies to raise the principle of competition.

G. ZuabiTahani, (200).The study examined the analysis and evaluation of the capital adequacy assessment framework in accordance with the Basel Convention and its applicability to Islamic banks especially in light of international banking claims to apply the decisions of the Convention on the new Basel where facing these banks, regarding how to measure the solvency of their capital, which is due mainly to where problems they do not require constant returns as banks, the special nature of traditional sources of such funds as they can Theoretically, it will bear the loss, in addition to the different nature of the financial instruments used. Bring them away from traditional financial instruments.

H. Abu- Elez, Ali (2014), the main aim of this research was: Establishing and highlighting the legal rules and foundations on which capital adequacy calculation is based. Knowing the extent to which Islamic banks adhere to the international financial solvency standards (Basel), and the extent of their compatibility with the special nature of Islamic banks. Seeing the pioneering Islamic attempts to issue Islamic standards for the adequacy of the capital of Islamic banks, and discussing them with a scientific discussion to see which ones are more in line with the Sharia standards, provisions and principles.

Finally, this humble search is nothing more than a human effort that is immune from error and forgetfulness, and perfection of God and unity, and the infallibility of his prophets, and we welcome any purposeful scientific discussion, and any suggestion to improve the research, whether by deletion, addition or amendment, and we hope that this research will benefit in promoting a wider discussion On the main points of the methodology for calculating capital adequacy in Islamic banks.

Chapter two (Literature review)

2.1 An Overview of Islamic Banking

2.1.1 History of Islamic Banking and Finance:

First of all, in order to understand the history of Islamic Banking, we first need to understand and comprehend its definition. The Islamic banking, which is also recognized as the non-interest banking, is a system used by banks that bases its principles to the laws and regulations of the Islamic economic definition. The Islamic banking differ from the normal banking system in two fundamental issues, the first being the shares of profit and loss between the bank and its client, and the second is the non-existing collection of interest profit from lenders and investors as it opposes the laws of Islamic economy[1].

The Islamic banking system saw lights and recognition during the last 40 years, and that is due to the term of Riba spread throughout the normal banking systems and operations, which is totally against the laws of the Islamic economy, thus was the birth of the Islamic banking system to avoid such prohibitions. The term Riba in the Islamic Shari'a is considered as a sin, and is defined as a concept in (Islamic banking) that refers to the action of charging interest, as well as " placing unreasonably and high charges of the interest rates"[2]. There is also another form of Riba, which is the action of exchanging goods that are unequal in worth and quality. Therefore, and as mentioned above, the Islamic banking system came to deny such actions and operations that will lead to unblessed profit in the terms of Shari'a. Accordingly, certain reports on the global Islamic finance illustrated that the number of Islamic banking has been increasing drastically over the world, as they reached approximately 500 banks by the end of 2017[3].

However, the existence of Islamic banks in the banking sector was considered to be a threat to interest banks and commercial banks. In order to avoid countless potential losses, these banks developed a system called the Islamic window. The Islamic window is a

[1]Investopedia, a brief History on Islamic Bank
[2] Characteristics of Islamic banking, Investopedia
[3]Traver 2019, Investopedia

system offered by commercial banks to their clients who are wishing to deal according to the laws and the terms of Islamic finance, thus through certain sections and departments of the bank, these services are offered(Errico&Farahbaksh, 1998).

Since the early 2000s, the global Islamic capital market has been growing in depth and size across jurisdictions, with numerous entities across sectors raising capital in ways that comply with Islamic principles. Nowadays, the global Islamic capital market is a multisector segment that includes holistic financial instruments, including Sukuk Islamic equities, Islamic funds, and other Islamic structured products, such as real estate and investment trusts (REITs) and exchange traded funds (ETFs). The Islamic equity sector is nowadays considered as a key global jurisdiction, as the world's major financial index providers, "Dow Jones, Standard & Poor's, and the FTSE", all established Shariah-compliant equity listings, allowing the Shariah-compliant equity and fund markets to blossom. As an example, the Dow Jones Islamic Market indices cover market capitalization of more than $10 trillion in over 40 countries. These developments have enhanced the attractiveness of Islamic financial markets as an asset class for investment (Davies, 2004)

(**Development of the Islamic Banking and Its Principles and Profit Generation:**

The development of Islamic banking was clearly increasing and cannot be denied, especially after the profit made by the banks in different areas of Islamic banking sectors(World bank, 2012). The Islamic Banking system (IB) achieved a huge advancement globally as illustrated a visible growth in four different categories being Islamic Banking, Sukuk, Takaful, and Islamic Funds. By the end of 2011, the IBs managed to generate 1.1 Trillion USD, 178.2 Billion USD, 15.2 Billion USD, and 60 Billion USD from these four categories respectively according to the world Bank development data group (2012). Therefore, it became obvious to the banking sector that IBs are accomplishing the tasks they aimed for, and their target is growing much bigger than before. The Islamic banks became important on global level, especially since the expansion of the Islamic religion in all cotenants, as demonstrated below, a table to show the number of Islamic banks headquarters globally to show their expansion.

table (2.1): show the number of Islamic banks headquarters globally to show their expansion.

Europe	North America	South America	Asia	Africa
Turkey (1) UK (6)	USA (4)	None	Pakistan (6), Bangladesh (3), Bahrain (9), Iran (14), Jordan (2), Kuwait (2), Lebanon (1), Qatar (3), KSA (6), UAE (4), Brunei (3), Philippines (1), Malaysia (17), Thailand (4)	Algeria (1), Gambia (1), South Africa (1), Sudan (4)

However, and despite the huge and rapid growth of the Islamic Bank on global terms, they are highly concentrated in Asia and that is due to the majority of Muslims that resides in Asian countries and in the Middle East. Furthermore, Islamic Banks are also getting attention from none majority Muslims countries as the likes of Thailand that contains has four institutions offering Islamic banking products (Haron & Yamirudeng, 2003).

- **Principles of Islamic Financial Systems and Profit Generation.**

When it comes to the Islamic economy, it is supposed to reflect and adhere to all Islamic principles and moralities. The main source of such principles is extracted from the holy Quran setting all bylaws and values for the Islamic banking and economic trading. The main Shariah rules with regard to banking and finance include the following (Komijani,2018)**:**

1. Money does not have any intrinsic value and is used merely as a medium of exchange and a tool for preserving and assessing the value of goods, services, and properties.

2. Emphasizing that the bank and well as the customer should carry on all potential losses or profit by shares.

3. prohibited activities with unmoral social values, such as trading alcoholic drinks, betting, and gambling, are off the banking service list.

4. Riba (interest) is prohibited.

5. Gharar (ambiguous and risky transactions) is prohibited.

The development of the Islamic Banking system led them to adapt their own operation methodology to fulfill their needs and these of the customers in accordance to the laws of Islam as per according to many Islamic thinkers, the Islamic Banks has to generate their profits within the boundaries set. The generated profit in the stage of development and the operation system were divided into three different stages being (Public Funds Acquiring, Render of Chargeable Services, and the usage of the acquired funds in profitable).

1. The Acquiring of public funds: This stage of profit-making concentrates on funding the bank's activity from customers' funding like share-holding customers. However, the bank can also use different prospects to accumulate funding like customer current accounts and saving accounts. This type of funding allows the bank to use the deposits without any return payments for the customers. Nevertheless, there is also a different method where the bank is supposed to pay return amount (Profit share) or deducted a certain amount from the customer as (Loss share). This method concentrates on encouraging the customers to deposit amounts in their bank accounts, and in the cases of commercial banks, these deposits have a return of interest rate and no loss value, unlike the case of the Islamic banking (Komijani, 2018).

2. Chargeable Services: These are services which the bank could render on fee, commission or fixed charges which are not tantamount to interest charges. These include (Haron&Yamirudeng, 2003):

1. Safeguarding jewelry and other valuables.

2. Transferring funds.

3. Acting on behalf of clients to purchase or deliver goods.

4. Offering advice and consultancy services.

These are the least profit generating kind of investment, but still require huge cash and other liquid holdings (e.g. balances with clients and other banks). These holdings henceforth, are referred to as "funds for bank services) (Islamic International Rating Agency, 2006).

3. Profitable Business A bank's real investment activities constitute the main source of its profits. There are three kinds of short-term investments which are usually of medium return and risk:

1. Investments on commodities and stocks, where they are not subjected to monopoly speculation or any form or prohibition investment.

2. Financing to customers on a participation or profit-sharing basis. "Profit-sharing ratios are usually contractually predetermined, and the higher portion of return goes to the partner who undertakes management of the business"[1].

3. Long-term investments, which are usually the bank's own projects or other long-term joint projects between the bank and the customersthatcould also be undertaken with financial institutions. These require enormous funds and may be the most profitable, greater risk is also involved.

To guard against any hidden form of interest or other unlawful transactions (or even any possible problem of moral hazard), in any type of business mentioned above, Islamic banks may establish supervisory banks to ensure conformity with principles of Islamic Shari'a (as is the case with FIBS and other Islamic banks)[2].

- **The Reasons behind the Success of Islamic Banking:**

A conducted survey on customers of Faisal Islamic Bank of Sudan (FIBS). Where the special questionnaire was designed to determine the factors that affect supply of funds of Islamic banks was distributed to 1200 customers and 496 (41%) replies were obtained. To conclude the results from the survey, the answers showed that the (any fast flow of funds to Islamic banks that is directly leading to their success is mainly caused by four factors). These factors are the building blocks, and act as a chain. It is identified that funds supplied to current and saving accounts are mainly determined by volume of bank services and volume of funds that the bank invested on a participation basis (AAOIFI,2001).). However, when it comes to the funds supplied to deposit and investment accounts, they are clearly affected by the expected return to depositors as well to the level of risk involved. Return to

[1]Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services WafikGrais and MatteoPellegrini World Bank Policy Research Working Paper 4054, November 2006.
[2] Corporate Governance and Shariah Compliance in Institutions Offering Islamic Financial Services WafikGrais and MatteoPellegrini

depositors are of course determined by the profitability of the bank; and in the case of the Islamic banking system (profit-sharing ratio). These findings reveal that the effective reasons for the success of Islamic banks are:

1. High and efficient bank services.

2. Cheap and less risky advances on a participation basis.

3. Higher return to customers on their investments.

4. Low risk in returns.

These factors seem similar to the usual expectations of any bank's customers. The only difference between the two (Islamic and conventional) is related to the kind of loans to customers. While interest-based banks offer loans on a fixed return (interest), since it is prohibited, Islamic banks offer funds on participation basis. Although this might be more expensive than the fixed interest, (in case of high profitable uses of the loan), it is much safer and less risky than the interest loans (AAOIFI,1999). The customers' objectives are similar but the Islamic banks have a better chance of offering higher returns. The fact that they have to "invest in real investments gives them the chance of obtaining more profits and hence pay greater returns to their customers. This might be at the cost of higher risk. but the risk can be substantially reduced through diversification. Having these high returns at a reasonably low risk would enable the Islamic bank to generate higher volumes of funds and hence to render more hank services, which will in turn attract more funds" (FIBS, 1979).

The success mentioned above, was not only customer opinion or the bank's profiting policy, but it also included the advancement and the development, which is the main topic of this section. The success in developing the commercial Islamic banking system can be the variation between the profit and the risk of loss they have as they try to maximize the returns for the share-holders and achieve a better off return to the depositors while minimizing the risk of loss to all investors and share-holders. Such a policy demonstrates the seriousness of the bank's ideology in attracting depositors searching to increase their equity (Long-term investors). Covering all types of customers was a key player in the expansion the Islamic baking lived after the year 2000 as mentioned above, and was also an important roller in the huge profit by the end of 2011.

2.1.2 General Regulations on Islamic Banking:

The effective prudential regulation of banks is as necessary and desirable in Islamic banking as it is in conventional banking. Therefore, the risks exposed from the market on Islamic banks are similar to those on conventional and commercial banking. Accordingly, the reason of applying those prudential regulation and serious supervision on Islamic banking and its financial activities are the same as the case of conventional banks: mainly to establish and maintain financial stability of the bank. This is achieved by ensuring the safety and soundness of banks, thereby preventing problems from having systemic repercussions.

An important objective underlying the regulatory framework for Islamic banking should be to avoid undermining the stability of the financial system. Key elements to achieve this objective tackles three different fundamental issues: (understanding the nature of Islamic banking activities, making appropriate changes to the existing regulatory framework for Islamic banking, and leveling the playing field between Islamic banking and conventional banking). Current trends indicate that specific elements relating to Islamic banking are being increasingly encapsulated into the regulatory framework (Song,2014).

In addition to what is mentioned above, the recent national and international reforms and regulations implemented in bank regulation and supervision, such as Basel II regime, developed an extensive list of best practices that includes implications for Islamic banks. Islamic banking risks come within the recognition of Basle II pillar covering credit risk, market risk, operational risk and the pillar covering governance, capital management, liquidity risk. However, the challenge for Islamic banks is how should other Islamic banking risks, such as Shari'a compliance risk, fiduciary risk and the rate of return risk, be deal with in an overall Basel II framework to improve the safety and soundness of the system. The compliance with the international and local banking laws as well as those of the Islamic Shari'a increases the difficulty of the Islamic banking mission. Therefore, a new regulatory entity emerges to ease this task, which concentrates on the Islamic banking practices and their adherence to the Islamic bylaws (Oosthuizen, 2014).

The supervision task is not easily recognized among the Islamic banking entities, as there are two different approaches about the accommodations of IBs, where most of the Islamic bank suggests that the central bank and the ministry of finance supervise their

activities. This was not the case for the Islamic bank found in Turkey and the United Kingdom, as they claim the existence of a separated organization outside the central bank and the ministry of finance to supervise and guide the bank's activities(Song, 2014).

4. Shari'a Board of Directors: the task of this board is crystal clear, which is to guide, supervise, and ensure that all tasks and activities done by the bank follows the Islamic laws. However, some of these boards are considered as a part of central banks, which means they work as one unit in order to establish the stability. Therefore, we can see that the regulatory supervision can be divided or united between both corporations. Yet again, within this separation of roles, we still find another branching fact about the legislative and adjudicative roles of the Shari'a board. In some cases, the Shari'a board is given legitimate powers over the decision making regarding the Islamic laws' regulations. In other cases, like Syria, this board is not granted any legitimacy, but is required to be consulted in regards of such issues[1].

2.2 Basel Accord, Brief Summarization and Main Characteristics

Much of the modern risk management framework applied by any financial institution like banks, has been influenced by the work and the frames imposed by Basel banking supervision committee, mainly referred to as BCBS, which is also comprises 27 countries each with a representative whether it is the central bank or another regulatory institution like in the case of the Palestinian Authority. Due to Paris protocol signed in 1993, the Palestinian Authority are not allowed to have a central bank, but instead they have the Palestinian Monetary Authority (PMA), taking several characteristics from central banks and act as the main supervisor and regulator to all banks in Palestine(FIBS, 1979).

Nevertheless, the BCBS meets at the office of the bank international settlement (BIS), based in the city of Basel in Switzerland. These meetings all have the same aim in mind, which is to improve the quality of banking supervision globally, and that usually happens through the co-operation between the central banks in the respective countries and all banks in the area. The global forum issued by the BCBS is considered to be the guidelines and the supervisory standards. Such standards consist of regulations like (Capital adequacy

[1]DadangMuljawan, A Capital Adequacy Framework for Islamic Banks: The Need to Reconcile Depositors' Risk Aversion with Managers' Risk Taking

ratio for bank and the cross borders banking supervisory system), which will be discussed on further part of this chapter.

Therefore, and in other words, the Basel committee has been the main responsible line to introduce the "global minimum standards for the banks' capital to be hold as a 'cushion' against unexpected losses caused by the banks' business activities of lending and trading. One of the accord's key objective is to level the playing field amongst internationally active banks' considering the prudent and different levels of capital risk. The role of the capital requirements was clearly seen in the shining era of Japanese investing banks in the London and their competitive abilities in the financial sector in the mid*1980s(Kahf, 2005).

Therefore, we can see that the role of Basel Accord in general can be explained in two main points being (Investopedia on Basel Accord, 2019):

5. The Basel Accords are three series of banking regulations set by the BCBS.
6. The accords are designed to ensure that financial institutions have enough capital on account to meet obligations and absorb unexpected losses.

The Basel accord consists of three different levels: Basel I, II, and III, the latest was signed in 2010. The upcoming section will discuss the differences between the three levels in the accord and the characteristics of each one.

2.2.1 Basel I, 1988:

The first Basel accord was signed in 1988, and it provided the implementation of what is now called 'credit risk measurement framework', and that is calculated using a minimum capital standard of 8% of the banks' risk weighted assets. The capital standard works as the bank in-case liquidity cushion against unexpected changes in the market or in the banks situation as it prevents the possible default. The risk weighted asset design had in purpose to reflect the creditworthiness of a particular class of obligors. The RWA and as explained by the corporate finance institution "refers to an asset classification system that is used to determine the minimum capital that banks should keep as a reserve to reduce the risk of insolvency[1]. However, the need of these assets is to hold the bank stable against any fall of the other side of the activity whether it is a counterparty or a client regardless of the type of activity 'lending or borrowing'.

[1] CFI official Website: https://corporatefinanceinstitute.com/resources/knowledge/finance/risk-weighted-assets/

7. I.e. on Basel I calculation: if the loan to (counterparty X) has been given by bank A, and the loan's value was 100 million USD, the minimum capital requirement to give such a loan is calculated by: ***Loan value * 8%*** the minimum capital standard provided by the accord, which equals to ***8 million USD*** to be held by the bank to avoid capital risk.

This method used by Basel I managed to cover both conventional on-balance sheet banking assets as well as off-balance sheet instruments as derivatives and guarantees [1].

1. The Risk Weighted Assets in Basel I

The risk weighting of the assets consists of five different categories, and the rang of these categories is between 0%-100%, and the assets are classified into these categories based on the nature of the debtor as demonstrated below[2]:

table (2.2): the assets are classified into these categories based on the nature of the debtor

0% Risk Category	10% Risk Category	20% Risk Category	50% Risk Category	100% Risk Category
This contain: Cash, government debt, central bank debt, and the debt of the governmental organizations	This contains: Central bank debts of countries with high inflation rates	This contains: Development banks Debt, Organization for Economic Co-operation and Development debts.	This contains: Residential mortgages	This contains private sector debt, non-OECD bank debt, real estate, plants and equipment, capital instruments issued at other banks

2. The benefits of Basel I Implementation:

- Significant increase in Capital Adequacy Ratios of internationally active banks.
- Competitive equality among internationally active banks.
- Augmented management of capital.

[1] ACI dealing Certificate syllabus.
[2] CFI official Website: https://corporatefinanceinstitute.com/resources/knowledge/finance/basel-i/

- A benchmark for financial evaluation for users of financial information
- Worldwide Usage
- Greater discipline in managing capital

However, regardless of the benefits and the pros of having the correct application of Basel I on the banking systems, there are some limitations that the accord did not cover. These limitations are the different types of risks besides the capital risk of the bank, I.e. Market Risk, Operational Risk, and Liquidity Risk, were not taken in serious consideration by Basel I and that caused a problem, as banks' main concentration drifted to the Capital risk only. One more problem caused by Basel I, was the evaluation of the assets that was evaluated by their book value, rather than using the 'mark to market' method and evaluate them according to their market value(Helmy, 2012).

Moreover, the Basel I accord consisted of two tier that makes up the capital of the bank. These capitals have to be assigned to the RWA and thus creating what we call (Capital to Risk Weighted Assets Ratio) CRAR. The CARA tier is defined as the following (DebajyotiGhosh Roy, 2013):

3. **Tier One:**

- Paid-up capital
- Statutory Reserves
- Disclosed free reserves
- Capital reserves representing surplus arising out of sale proceeds of assets

4. **Tier-II Capital**

- Undisclosed Reserves and Cumulative Perpetual Preference Shares
- Revaluation Reserves
- General Provisions and Loss Reserves
- Hybrid instruments (these instruments must be unsecured and fully paid up)

- Subordinated debts (Maximum 50% from tier one, 5 years, and traded at discount for short-term maturities).

2.2.2 Basel II, 2006:

Basel II was first introduced at different timing in different countries, nearly starting in to 2006. This developed accord represented a new banking framework to substitute this proposed by Basel I due to its different disadvantages. The effect of Basel II took off in 2008, and regarded different types of risk added to the original credit risk plan. Basel II highlight remains in its concentration on credit risk, market risk, and operational risk. Moreover, the concentration went beyond the different types of risks, as this accord proposed three different aspect (Minimum capital requirement, supervisory review by the central or the monitor bank in the country, and finally regarded the aspect of market discipline by effective disclosure) (Bank of International Settlement, 2001).

The minimum recommended ration in Basel II of the CRWA (capital to risk weighted assets), remained unchanged and was held to be 8%. However, the changes were majorly focusing on the calculation of credit risk capital, as well introducing a new method for a capital charge for operational risk. This new framework was a result of several financial outcome that took place during the last years before its designing, and that is why the plan started in 1999, six years before launching the accord. Just like Basel I was formed by assembling twodifferent Tiers, Basel II creation came with three different pillars each dealing with a certain aspect (Manuel Chavez, 2007). These pillars were the main guideline for banks in order to avoid the exposure caused to them by different types of risk, whether they were conventional or Islamic.

8. Pillar I – Capital Adequacy Requirements.

This pillar of the accords had defined the minimum capital requirement as the eligible capital and methods for calculating risk-weighted assets for credit, market, and operational risk. Moreover, a key objective of the new accord was to make thee capital requirements more risk sensitive, thus aligning regulatory capital to be closer to the economic capital of the bank. In order to measure these new requirements, there are two different approaches to be used: The Standardized approach, and the Internal Rating Based (IRB)approach (BIS, 2006).

1. **The standardized approach:**

It's the same as the previous accord in Basel I, but it is more sensitive as the banks main task now is the allocation of all of their risk weighted assets and their off-balance sheet positions and instruments. Therefore, and according to this approach, an RWA of 100% describes that the exposure of this asset is included in the calculation thus, the capital charge here will be 8%. Nevertheless, this accord does not base the individual risk weighted asset according to the broad category of the counterparty, but it uses an external source of credit assessment (Bank of International Settlement,2001). These sources were defined by Basel II as rating agency, and that came in handy for the banking system.

In Basel I, the corporate lending mechanism had only one RW category of %, but under Basel II, three more RW categories were created (20% - 50% - 150%). This will make the calculation of the CARA more accurate in Basel II than it was in the first edition of this accord (Louati, 2015).

2. **The Internal rating-based approach (IRB)**

In this approach, the bank will not be using an external rating agency, but rather its own internals in order to determine the creditworthiness of the client and then assess it in their portfolio. The minimum capital required by the bank will be calculated by the internal departments using this methodology, and that is by estimating the potential losses or exposures for each of their clients. According to the BIS, banks work to estimate the probability of defaulting that is associated with each borrower, and then the supervisors will supply the other inputs, and thus any bank that is able to provide the minimum capital will also have the ability to be a supplier for other developing banks.

Furthermore, the Internal Raking Based Approach, introduce three different definitions that can estimate the expected loss of the bank.

- Probability of Default (PD): designed to measure the probability that the borrower will default over a certain timeline, and will not be able to fulfill his obligations towards the other party.

- Loss Given Default (LGD): designed to measure the proportion of the borrower's exposure that will be lost if any default occurs in the future

- Exposure at Default (EAD): designed to estimate and measure the outstanding amount in a commitment if any future default occurs.

3. The Calculation of Minimum Regulatory Capital.

As mentioned above, the Basel II mechanism differs from Basel I in the considered types of risk. Therefore, there was an amended version to calculate the "Minimum Regulatory Capital" used by Basel II (BIS, 2006).

Total CRAR = [Eligible total capital funds]/ [Credit RWA + Market RWA +Operational RWA]

The eligible capital funds described in the formula above, consists of (Tier I core capital + Tier II additional or supporting capital). The reason behind this combination between the capitals is due to the fact that, Tier I capital are considered to be more stable and more risk absorbing than those of Tier II (Bank of International Settlement, 2001).

9. Pillar II – A Supervisory Review Process.

This pillar was designed in order to discuss the key principles of the supervisory review, transparency, and accountability. Moreover, there are four main principles of supervisory review as stated in the accord (Bank of International Settlement, 2001).

1. Banks are required to design a process that assess their overall capital adequacy, and their risk portfolio. They are also required to form a strategy for maintaining their capital levels. This principle led to the development in banks of an internal Capital Adequacy Assessment Process (ICAAP).

2. Supervisors, like the local regulators and central banks, should review and evaluate banks' internal capital adequacy assessments and strategies. The regulators are required to test the banks' ability in order to monitor and ensure their compliance with the regulatory capital ratio. However, if the bank showed any lack of compliance the supervisor is required to take actions towards this bank.

3. Supervisors should expect banks to operate above the minimum regulatory capital ratios, and therefore, they should have the ability to require any bank to hold a capital in excess of the minimum.

4. The supervisors should seek to intervene at an early stage to prevent capital from falling below the minimum required to support the risk characteristics of a particular bank, and should require rapid remedial action if the capital was not maintained.

However, the second pillar of Basel II was not only designed to ensure the banks' adequate capital (DebajyotiGhosh, 2013), but it also aimed to demonstrate a better risk management and measurement to encourage banks to monitor and manage all of their risk techniques associated with their business. Moreover, in order to fulfill the first task mentioned by pillar II, the all bank mast form a group of five in order to fully accomplish the process. The main five feature are as below:

- Board of senior management oversight.
- Sound capital assessment
- Comprehensive assessment of risk
- Monitoring and reporting risk associated activities
- Internal control review

10. Pillar 3, The Encouragement of Market Discipline

The accord stipulated the requirements for all public disclosures of a bank's risk activities, and that was in order for the key shareholders to understand the firm's risk exposures. Nevertheless, this mechanism caused banks to include a large section of their annual reports to explain and elaborate on these different types of exposure to the shareholders, as well as their risk management methodologies. Thus, we can say that the creation of the Pillar III, was in order to complete what came in the previous two pillars of the accord. This section of the accord is usually done internally and that is because internal measurement gives the bank more discretion in the task of assessing all of their capital requirements (BIS, 2006).

Banks are always looking to follow the guidelines mentioned above, especially those that are related to disclosure. However, the board of directors understand that the supervisor has all powers to require them to disclose information at times, and to provide updated reports about their disclosure at some other times. All of this combined, can cause the bank

to operate safely and on solid grounds, which is what the supervisor requires to do. In other words, the effect of this pillar on the banking market as a whole is "this is designed to allow the market to have a better picture of the overall risk position of the bank and to allow the counterparties of the bank to price and deal appropriately (Manuel Chavez, 2007)".

Moreover, the third pillar disclosures are set to cover several aspects from both a qualitative and quantitative point of view. These aspects are the below:

- Scope of application of the capital adequacy framework.
- Capital structure and capital adequacy
- Credit risk
- Securitization
- Market risk
- Equities
- Interest rate risk in the banking book
- Operational risk (using the Advanced Measurement Approach AMA).

Therefore, we can see that the types of risk, and yet again are more than those covered by Basel I. they also included the securitization of the bank's assets, and the equity effect is to be calculated[1].

[1]www.BIS.org: Basel III : A global Regulatory framework for more resilient banks and banking systems 65,December 2010 (rev June 2011) .

11. Comparing between the three pillars of Basel II [1]

table (2.3): Comparing between the three pillars of Basel II

Pillar I	Pillar II	Pillar III
1. Risk management incentives 2. New operational risk capital charge 3. Risk weighted assets (RWA) for credit more risk sensitive 4. Market risk largely unchanged	1. Solvency reports 2. Regulatory review 3. Capital determination 4. Regulatory intervention 5. Addresses risk that are not captured by Pillar I like, IR risk and liquidity risk	1. Minimum disclosure requirements 2. Capital transparency 3. Capital adequacy 4. Risk profiling 5. Risk measurement and management

2.2.3 Basel III, 2010:

Basel III was formed to effectively amend and add criteria to Basel II, but on the contrary it does not replace it. This amended accord was derived in response to the global credit crisis that took place in 2008, and it some way economists and financials found it more sophisticated and extensive when it comes to apply the main philosophy of Basel I, rather than being considered as an extension to the second draft of the accord. Basel III focused explicitly on reducing the systematic risk in the banking systems, and produced new features to be included in the risk analysis. Therefore, Basel III and as the BIS regarded it "reforms to strengthen global capital and liquidity rules with the goal of promoting a more resilient banking sector (BIS, 2010)".

As mentioned above, the Basel III saw its birth after the great depression on 2008. One of the main reasons the famous economic and financial crisis, which began in 2007, became so severe was due to the excessive off and on-balance sheet leverage built up by different banking sectors in many countries. Combining this, with the limited amount and

[1]Tamer Bakiciol. Website: https://www.princeton.edu/~markus/teaching/Eco467/10Lecture/Basel2_last.pdf

insufficient stock of liquidity buffers banks had during that period, the problem started to become more and more serious, and this caused several banks to be unable to absorb the resulted losses nor to cope with the exposures produced by the on and off-balance sheet trading (Bank of International Settlement, 2001).

For most of the crisis timeline, the market was not as confidant in its liquidity or solvency as it uses to be, and many banking institutions started to show signs of weakness. The weaknesses were rapidly reflecting on the remaining financial systems, on the countries real economic situation resulting in a massive lack of credit and liquidity. One of the main reasons the famous economic and financial crisis, which began in 2007, became so severe was due to the excessive off and on-balance sheet leverage built up by different banking sectors in many countries. Combining this, with the limited amount and insufficient stock of liquidity buffers banks had during that period, the problem started to become more and more serious, and this caused several banks to be unable to absorb the resulted losses nor to cope with the exposures produced by the on and off-balance sheet trading.

For most of the crisis timeline, the market was not as confidant in its liquidity or solvency as it uses to be, and many banking institutions started to show signs of weakness. The weaknesses were rapidly reflecting on the remaining financial systems, on the countries real economic situation resulting in a massive lack of credit and liquidity. Therefore, this Basel III and in rapid words aims to strengthen the bank-level, its micro-prudential, and its regulations to be able to monitor and work during the period of stress (BIS, 2006).

Basel III also introduced new rules that were approved in 2010, and that targeted the mission. These rules are divided into five different parts being (BIS, 2010):

- The new definition of capital
- More stringent capital requirements
- Leverage ratio
- Counterparty credit risk
- Liquidity coverage ratio

Each of these rules had its own unique role and features to help the bank do their job regardless of the market situation.

12. The new definition of capital

The Basel III accord significantly restricted the eligibility of certain instruments to count towards a bank's minimum capital requirements, and decided to focus more on the banks' common equity as the most efficient type of capital to make the bank fully loss absorbing. Therefore, and under Basel III, the capital was categorized into two main tiers according to the quality and the seniority in their structure of different instruments (BIS, 2006).

1. Tier 1 'Going Concern Capital'

This tier was designed to allow the institution to remain going concern during the crisis period, without it triggering any case of default or insolvency. This tier also accounts the common equity as issued share capital[1]. This contains retained earnings, disclosed reserves, and stock surplus. If other instruments were to be added to the bank's going concern capital, they will form (Additional Tier 1), as long as they meet the requirements of this type of capital. All of those instruments provided by the bank in this stage of crisis, has to be fully discretionary, with non-cumulative coupons or dividends, and to be maturity free.

2. Tier 2 'Gone Concern Capital'

This type of capital was designed to transform the bank to be fully loss absorbing in any event of crisis or liquidation of its holdings. The instruments in such a Tier must be subordinated to depositors and general creditors of the bank. Therefore, the main focus of this tier is to transform the held capital by the bank into a cashflow in order to evade the gone concern zone in the crisis timeline.

13. More stringent capital requirements

Unlike Basel II, Basel III increased the minimum percentage of the capital, and rather than being 8%, it increased up to 13%. However, this increase was not made all at once, as it takes into account the situation and the intervention of the supervisor as well. Therefore, the total requirement in Basel III and under the normal situations should be 10.5%, and the other two percent is called the countercyclical capital buffer imposed by the supervisor (Ghandour, 2017).

[1]ACI official Material.

table (2.4): Basel III capital requirements-Source: BIS

	Common Equity	Tier 1	Total
Minimum	4.5%	6.0%	8.0%
Conservation Buffer (CB)	2.5%		
Min+CB	7.0%	8.5%5	10.5%
Countercyclical Buffer	0 – 2.5%		

14. Leverage Ratio

The leverage ratio produced by Basel III, works as a backup to stop the risk-based capital requirements, and to help contain a system-wide build-up of leverage. This ratio contains, the Tier 1 capital divided by total of on and off-balance sheet exposures (in current tests being equal to 3%). The reason of this, is to ensure the bank has a maximum permitted level of leverage of a fully-loss absorbing capital[1].

15. Counterparty Credit risk

They are a number of measures designed to increase the bank's capital requirement strength for the counterparty credit risk, which arises from over the counter derivatives and security trading[2].

16. Liquidity Coverage Ratio

Basel III idea of liquidity coverage ratio deals with the management of the institution's liquidity under specific requirements from the regulatory. Under Basel II, the second pillar suggested that that the bank should have a 30-days liquidity coverage ratio (LCR), backed-up by a long-term structural liquidity ratio called (Net Stable Funding Ratio)[3].

The practical overview to this situation should be as the following

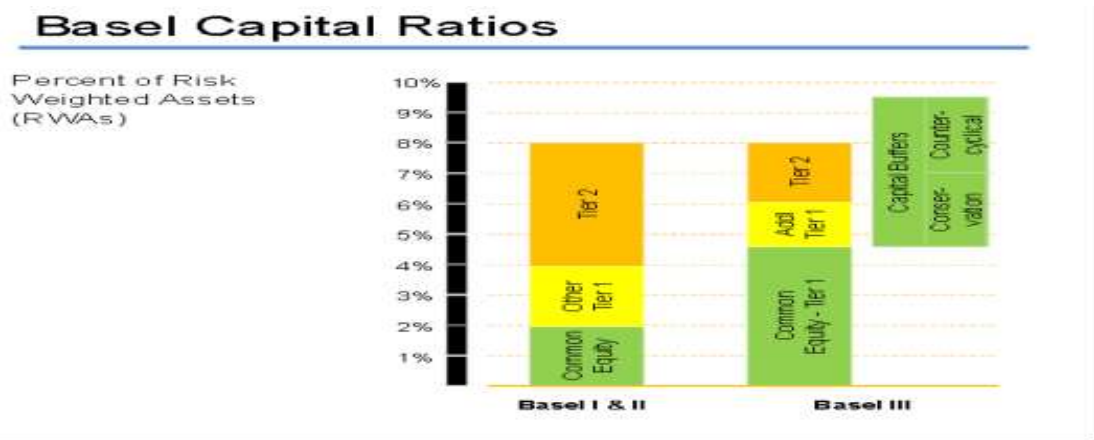
100% must be less than (or =) to (stock of HQLA)/Net Cash outflows over 30-days period

[1]Investopedia, definition of Leverage ratio
[2]Investopedia, definition of Leverage ratio
[3] Basel II Handbook, 2004

17. Summary to the Benefits of Basel III[1]

- Increase the quality and quantity of banks' capital
- Increase the risk capture
- Increase the banks' resilience by introducing capital buffers
- Reduce procyclicality in the regulatory framework
- Reduce systemic risks
- Ensure that banks have a minimum level of liquid funds
- Limit the difference in maturity between banks' assets and liabilities
- Limit banks' indebtedness and reduce dependence on their own models
- Limit banks' large exposures to individual counterparties
- Strengthen the regulations for exposures in the trading book.

To conclude the application of Basel I, II, and III[2]



figure(2.1): application of Basel I, II, and III

[1] Niemeyer, Jonas, 2016. Basel III what and why.
[2] www.BIS.org : Basel III : A global Regulatory framework for more resilient banks and banking systems 65,December 2010 (rev June 2011) .

2.3 The Implementation of Basel II by Islamic Banks: The Case of Islamic Bank of Palestine (IBP).

2.3.1 Introduction:

After any crisis, new reforms tend to be created in order to avoid the repetition in the future. Global crisis has led to the creation of what is now known as the Basel accord, which was a result of several banks entering a crisis era during the 80s and the 90s of the last century, and continued to adapt to the market crisis in 2008/09 till it reached its final form in 2010 Basel III (Louati, 2015). The interest rate failure led several institutions to go bankrupt, and the financial losses of this sequence caused a huge loss for the fund suppliers or commonly known as shareholders (Depositors).

The losses were not only financial, but also moral, as the competitiveness in the banking sector started to decrease due to these crises. Moreover, the main key behind the failure of different banks and other financial institutions were the increase in risk, as the excess risk is a major factor to enter the bankruptcy cycle(Louati, 2015). In the last years, the banking activities witnessed different changes in their policies due to the previous crisis, and that demonstrated that the existence of risk management platform is necessary for the banks survival.

Market failure, and excessive risk taking were not the only factors to demolish the banking base in the previous years. The lack of efficient management and control of the bank's financial activities is one of the reasons to blow a bank out of the competition. The information asymmetry is the main cause behind the two different issues, once combined can cause what we define as (Credit Risk). These factors are: adverse selection, which occurs before the final stage of the financial activity, and it means that the lender is entering into risk due to the lack of information provided by the borrower. The second issue is the moral hazard, which means that a party has entered a deal, without observing the action of the counter party, in other words saying, the counter party has provided misleading information about its situation (Investopedia, 2019). Therefore, we can say that moral hazard depends on the information flow between both the lender and the borrower.

Therefore, and due to all of the mentioned reasons, question like (whether to establish a risk management platform is necessary. In this research, the Islamic bank are no different than other banks, as they are also known to be risk taker in order to achieve profit.

Regardless, the Islamic banking system illustrated huge success over the recent years and established a strong based in the financial sector, but that does not mean that risk is absent. Despite this huge growth and recognition, the Islamic bank still face several obstacles in their financial formulas and their banking operation, and it is because of all of these factors, risk management was created.

2.3.2. Risk in Islamic Banking

Islamic bank, and mainly due to their policy of profit and loss sharing requires the investor's participation in the bank's equity and that by its turn help to promote a better off investment management, and proper monitoring. However, this does not eliminate the risk factor facing the Islamic banks, as the conventional banks and Islamic banks can be subject to different types of risk (Mainly credit and Market risk). When it comes to the conceptual manner, unlike conventional banks, Islamic banks has its own equity-based capital structure[1], mainly constituted by shareholders' equity and depositors' investment, and their policy of profit and loss sharing (PLS) can decrease the risk and enforce the bank's financial activities. Nevertheless, this is only if the concept of (Profit and Loss Sharing) is correctly and purely applied [2]. However, different scholars and researchers stated that Islamic banks are not purely applying the PLS formula and thus the probability of them encountering risk is not omitted. Cihak and Hesse illustrated that, due to the difficult access of liquidity in Islamic banks, they should be more selective in their capital to avoid greater risk of moral hazard (Louati, 2015).

2.3.3.Different types of Risk in Islamic Banking

The types of risk in Islamic banks are similar to those in conventional banks, as they include "credit risk, market risk, and operational risk. However, there are unique types of risks that were caused by the nature of the Islamic banking like (Musharaka, Mudhaarabh, Murabaha, Salam, Istisna, and Ijarah), which are not commonly discussed in financial international analysis

The types of risk in Islamic banks and according to Helmy are the following (Helmy, 2012):

[1]DadangMuljawan, A Capital Adequacy Framework for Islamic Banks: The Need to Reconcile Depositors' Risk Aversion with Managers' Risk Taking
[2]DadangMuljawan, A Capital Adequacy Framework for Islamic Banks: The Need to Reconcile Depositors' Risk Aversion with Managers' Risk Taking

1. Credit Risk: which is the failure of the counterparty to meet the obligations it has in any financial transaction. Usually this type of risk is involved with the default of the counterparty, or the counterparty decreasing creditworthiness.

2. Market Risk: the risk generated from the market's price movements, such like benchmarks, FX rates, and equity prices.

3. Liquidity Risk: the risk arising from the bank's inability to fulfill its obligations towards the counterparty. This can be resulted from the fall in the bank's assets, and it not being able to increase their value.

4. Operational Risk: the risk caused by failure or inadequate internal system, process, individual. It can also be caused by some other external aspects like closures, blockades, or war that lead the bank to be unable to operate.

2.3.4 Unique Risks in Islamic Banks

This section will discuss the risks that are only associated with Islamic banks, and that is according to what came Ghourbi's research (Ghourbi, 2014)

1. Risk of Murabaha: Murabaha is the action of selling where the selling price is higher than the original purchase price to generate profit. However, the risk in this context relies on the cancelation of the sale by the buyer, leading the purchased item to be stocked in the banks stores, and making the bank take all expenses like; storing expenses, changing in the price of the item or any other payments the bank has to make during this time. There is another risk factor in this context, which is the clients default and his inability to fulfill the required payments of the desired product (Ghandour, 2017).

2. Risk of Mudhaarabh: Mudhaarabh is where the bank funds a client activity, and share the profit according to a pre-arranged deal, and share loss (the bank's share is financial, meanwhile the clients share is in his efforts). The risk in this concept comes in different forms: first of all, the client does not pay the bank's share of the profit or delay the payment. The second risk is the poor effort of the client in the activity which decrease the profit generated from it thus decreasing the banks potential profit. The third risk is the decrease of the project or the activity's worth, and the fourth is the changes in price which can decrease or increase, thus affecting the banks profit.

Mudhaarabh is therefore, linked to moral hazard where moral issues can affect the income generated from this activity (Manuel Chavez, 2007).

3. Risk in Ijarah: Ijarah is where the bank purchase different tools and rent them to clients in order to be used. The bank generates profit through the lending activity, only this time it is with physical tools and not with money or derivatives. The risk of this funding source relies in two main issues; 1. The marketing risk, as the bank is required to market the tools to attract the clients' attention. 2. The risk of delaying the payments, or the inability to fulfill them by the clients.

4. Risk of Istisna: Istisna is the action where the bank fund the client in a different pre-agreed terms. The risk here is, if the client fails to deliver the products on time, or to sell them, or if the quality of the product is low, thus the bank will be unable to generate profit. Furthermore, the control of the produced product is totally within the customers, and that decreases the banks' ability to reduce the risk.

5. Risk of Salam: Salam is a common Islamic instrument in the agricultural field, and it is defined as (the pre-selling of a product before having it, with an advanced payments), i.e. the selling of a vegetables before cultivating it, but the bank still pays the price. The risk of Salam: 1. The client is does not comply with the delivery time or quantity. 2. The purchase of the products does not cover the spending. 3. The decrease of the products' prices.

Therefore, regardless of the strength demonstrated by the Islamic banking system over the past years, the risk is not completely omitted and that arises the question of "should Islamic banks adhere to the capital adequacy proposed by Basel Accord?". The answer is simply, as the banks vision states that it should maximize its profit, and thus Basel accord would provide the Islamic banking with a stable ground and a stronger presence (Musbah, 2018).

2.3.5.Capital Adequacy in Islamic Banks.

The Capital adequacy became one of the most instruments and indicators used when it comes to assessing the soundness of the banking operations[1]. Therefore, westerns established (Basel Accord) with its three different levels, that worked as regulations for banks to adhere to the capital adequacy. However, Basel was not the only step taken by the

[1]DadangMuljawan, A Capital Adequacy Framework for Islamic Banks: The Need to Reconcile Depositors' Risk Aversion with Managers' Risk Taking

Islamic banks in order to back up their activities from associated risk, as the also used the accounting and auditing organization for Islamic financial institutions commonly known as (AAOIFI). Based in Bahrain, AAOIFI started to release its statement of requirements on Islamic banks in 1999 (Jaseem, 2012), which worked as a supervisory plan, but it was not as detailed and efficient as Basel. The reason AAOIFI took in sight the regulation of Islamic banks was due to their strong and stable method of liabilities, where the Islamic banks are constituted from three different blocks:

18. Unrestricted Profit Sharing-Investment Deposits

19. Non-Investment Deposits

20. Restricted Profit-Sharing Investment Deposits.

However, this building method suggests that the Islamic banks should maintain a stable payment ability for the risk-averse depositors, and therefore distribute the highest profit for the category of investors that were willing to take the risk of investing [1].

Furthermore, the reason for which the Islamic banks should maintain and amend to the capital adequacy is divided to four different parts according to Ali Abu-Elez[2]:

1. Due to the continuous growth in the volume of deposits when it comes to Islamic banks, the unstable fluctuations in the market value of the investment, and the changes in the components of the banks' assets, have been attracted the concern of regulators, causing them to question the level of capital in reserve of the bank, in case of any further default (Niemeyer, 2016).

2. Islamic Banks tend to use their funding to finance government and public sectors, as they regard this sector to be less-risk than the private funding.

3. To absorb any type of risk, whether its common banking risk, or risk associated with the Islamic banks due to its different activity and methods of financing individuals.

4. To ensure that the bank is able to work during stress times and operates as usual to both clients and shareholders (Depositors).

[1]DadangMuljawan, A Capital Adequacy Framework for Islamic Banks: The Need to Reconcile Depositors' Risk Aversion with Managers' Risk Taking
[2] Abu Elez, Ali. Capital adequacy in Islamic banks.

However, according to Bohaidar, there are different steps that Islamic banks should take in order to minimize the taken risk in their activities, and one of the steps to be taken is to diversify the banks' activity. The diversification can come in different forms, like geographic expansion, activities with sector, and methods of funding, and the reason behind this claim is to avoid the type of depositors who are aiming to maintain profit but won't cooperate with the bare losses or risk. Regardless of how strong Islamic banks were in recent years due to their constant methods of liabilities or funding sources, the risk was never really omitted, and thus diversification shall help in this stage (Bohaidar, 2010). Nevertheless, Bohaidar also illustrated the importance for Islamic banks to apply and comply with the international regulations in regards of the risk topic. However, this comes in different forms:

* Complying with the information policies: where the information provided to the investors are clear and necessary, like the banks revenues, risk, and costs. Therefore, the bank will not go asymmetric and clients will not create the moral hazard risk (Bohaidar, 2010).

* Complying with the capital adequacy: which was stated to be the most important method to be used by any bank in order to outcome every possible risk from any banking activity (Eid, 2012).

HAs mentioned above, several organizations tried to control the risk when it came to the Islamic banks, however we cannot say that they were a success. AAOIFI in one hand, was focusing all of the regulations to strengthen the liabilities of the bank (fund sources), since they are the main method of capital for the bank. This was complicating the standards, since and after observing the balance sheet of any Islamic bank, we can see that the liabilities side there is a mixture between contracts and investment deposits, which are by nature considered as quasi-equity. These deposits are based on profit and loss sharing principles. Nevertheless, there are demand deposits whose capital is guaranteed by Islamic banks (Kabir, 2010). Moreover, the assets side is different, and more complex than this found in conventional banks, as the modes of financing are different and structured in accordance of (PLS), equity, sales, and lease-based contracts, thus generating more risk than conventional banks (Kabir, 2010).

Regardless of all the efforts, no regulation was able to with-hold the risk generating from the Islamic financial activities. In one hand, AAOIFI were to extreme and biased over

liabilities regulation, which left the assets at a greater risk, and the IFSB (Islamic Financial Service Board) considered assets to be important. None of them actually combined the importance of having a balanced structure of fund sources/uses, creating a gap between them (Bohaidar, 2010). Here, the international regulations should interfere. Basel in all of its forms was no meant to be for Islamic banks, due to the difference in both of their structure and risk, but its application can minimize those risk that are also uncommon by any conventional bank.

2.3.6. Why Basel Accord?

The information and the analysis demonstrated previously throughout this research were all leading to this section. Despite the importance of the banking activity, especially this of Islamic banks, the risk is yet to exist. Thus, it was important for all financial institutions to learn from previous mistakes and crisis, and that is why Basel was created. In the case of Islamic banks, they are trying to comply with the regulations imposed by Basel accord in order to establish the soundness and a stable ground for their financial activities. Basel is usually understood in a wrong manner, as it does not force banks and other financial institutions to apply it, but they ask them to comply in order to be safe.

The main objective of applying Basel standards is to build an efficient and prudent banking system, keeping in mind the most important thing, "regardless of the degree of caution and prudence envisaged in the bank's work, it cannot prevent the existence of risks in the banking business in the sense that any bank must take a risk in its work, a bank that does not take a risk is not a bank [1]".

2.3.7. Basel I application:

Basel I signed in 1988, was the first international accord to establish the regulations imposed on banks to omit risk or minimize it to the least possible. The tools used in this accord were the capital adequacy ratio proposed for all banks that were willing to comply with it. The capital adequacy ratio in Basel I, and as mentioned in the second chapter was (8%) (Bohaidar, 2010):

In this context, the CAR (capital adequacy ratio), is considered to be the first line of defense during period of stress. The good point in Basel is that, it did not only consider the

[1]Conference on Good Governance of the Banking Sector Shift from Basel 1 to Basel 2 (2007). Basel Risk-Based Capital Adequacy Adjusted Framework in Islamic Banks 2

CAR as a mean to risk omit, but they also established several systems to all types of banks (including Islamic banks) to decrease possible trading risk caused by credit default. These tools were classifications for countries and corporations, where they were divided into two main groups (high risk and low risk classifications). These classifications allowed Islamic banks to operate easier when it came to trading global as they served as a guide for proposed counterparties (Bohaidar, 2010).

2.3.8 Application of Basel I in Islamic Banks:

Islamic banks' application of Basel I is not different than this of commercial banks, since they both belong to the banking sector. However, several researchers discussed the CAR proposed in Basel I, and its efficiency in Islamic banking, i.e. Bohaidar. Bohaidar discussed that (8%) CAR is not sufficient for Islamic banks and that is due to various different reasons[1]:

*. Islamic banks usage of real investment makes them more likely to take higher risk.

*. Certain Islamic banks have unstable correlation with the central bank of their respective countries.

*. Islamic banks are unable to trace and observe clients, and are unable to flexibly use their safeguards.

*. The difference of financial activities' structure decreases the credibility of Islamic banks in some case when it comes to CAR calculations, due to their divided funds of on and off-balance sheet.

Therefore, we can see that most Islamic banks, and regardless of its differences, managed to comply with the capital adequacy ratio proposed by Basel I. Complying is no longer a choice, as it is a must due to the development, advancement, and expansion seen in banking systems in general, and in Islamic banking in particular.

[1]Conference on Good Governance of the Banking Sector Shift from Basel 1 to Basel 2 (2007). Basel Risk-Based Capital Adequacy Adjusted Framework in Islamic Banks

2.3.9 Basel II and Islamic Banks:

In Basel II, the capital adequacy remained one of the main tools to establish stability, even to Islamic banks. Although the types of risk in Islamic banks are more likely to be contract-centric rather than conventional product-centric, yet Basel II standards can still be applicable only with some adjustments. "Thus, applying Basel II is a matter of adoption of the standards to the needs of Islamic banks (Eid, 2012)".

Schoon argued that the transition from Basel I to Basel II, is only a matter of time to be seen. Some Islamic banks according to the argument proposed, will be complying with Basel II faster than others, as by their nature, Islamic banks usually seek to operate in countries where Basel II is not a financial priority. Schoon included Islamic banks, with smaller banks due to their problematic system of applying Basel according to her (Schoon, 2008). This is one of the core reasons for Islamic banks to apply Basel II in their banking systems.

Basel II, and as mentioned in the second chapter, kept the Capital adequacy unchanged at (8%). However, it established more regulations to cover different types of risk. The capital adequacy ratio calculation in Basel II took a new step towards Islamic bank hard capital (Bohaida, 2010).

Why scholars think that Basel II implementation in Islamic banking is important, is because of the fact that IFSB and AAOIFI regulation where never mandatory and that means that their implementation or application is not forced among banks (Eid, 2012). However, we previously stated that Basel accord itself is not forced on any banking system, but the absence of Islamic banking supervisory makes the application of an International regulation handbook more likely necessary. Islamic banking also suffers from common risks, and especially those that were never mentioned in Basel I, but taken in serious mind when the Basel amendment happen and led to the creation of the second accord.

Credit risk as mentioned above, is one of the most serious risks opposing the Islamic banking sector, with the liquidity risk. Basel II solution for liquidity risk was an applicable pattern that should analyze the bank's activity to avoid the possibility of credit risk. This was possible as it regarded, the availability of derivatives contracts with the improved provision of risk control tools has necessitated the provision of in-kind guarantees. Thus

allowing the future examination of the possible impact of these instruments or the availability of a back-up collateral (Qaron, 2013).

Basel II, was not just a regulation, but it was a clear framework that builds up a fully functional, stable, and strong financial organization. For Islamic banking, this framework could be implemented and ease the job of assessing, monitoring, and following up with all the different risks in its activity. According to Qaron, the four important elements in Basel II, are what defines the compliance and the willingness of the bank to go anti-crisis affected (Qaron, 2013).

A. All banks shall keep a capital adequacy related to the risk it faces, in addition to a strategy to allow the bank's control over this capital. In order to achieve this, Basel committee created what is called (strict censorship) that includes five different levels to ensure the bank's capital in reserve is enough for stress tests. The five levels are: 1. Board of directors' supervision, 2. Proper assessment of private funds, 3. Assessment of private capital adequacy, 4. Supervision and reporting, and 5. Analysis through internal auditing and supervision.

B. Supervisory authority has to test and examine strategies for banks calculation of its capital adequacy. In this level, the central bank, or any supervisory level institution has to field examine the mechanism of CAR calculation in banks and compare it to reports. This stage required five level of examinations that all banks should follow. Here, with the support of central banks, the Islamic banking system will be better off and would establish a better connection with the supervisory. The levels are: 1. Test the comprehensiveness of risk assessment; 2. Assessing capital adequacy; 3. Assessing the internal auditing operations; 4. Assessing the respecting of the minimum capital standards set in the first pillar; 5. Intervention of supervisory authorities (Qaron, 2013).

In this context, Islamic banks are required to assess, examine, and monitor their capital adequacy, but as all banks have operation risks, Basel II here required the intervention of the supervisory to recheck the CAR in all banks, thus avoiding any missing information that can lead to future default, risk, or loss (Louati, 2015).

C. The supervisory, if necessary can demand banks to hold more than (8%) as their capital adequacy, and that is because if any crisis or stress happens to a bank that holds only the required capital, the situation will be complicated. Thus, holding up more, will be an insurance for the bank and the depositors (In the case of Islamic banking, depositors are necessary, and asymmetric information shall be avoided, so this stage could improve the situation in Islamic banking especially since they hold up more than the requirement at usual timing).

D. Supervisor's intervention shall be rapid, so the capital adequacy requirements do not fall below the determined percentage. The consequences of such a fall can be harmful not only to the banks reputation but to its relation with the customers and shareholders. But why so, is the question usually asked. If the bank falls below the (8%) range, the supervisor has to prevent the bank from dividend sharing, and forces the bank to use a system that allow him to reach to the required amount of capital. Now in the Islamic bank's cases, the shareholders constitute a huge share of the bank's fund sources, and if they are unhappy, the bank will not sustain more stress periods. Therefore, the application of Basel II will also help the bank keep its sources in safe place (Qaron, 2013). The policy of PLS in Islamic banks is not pure, and in any case, where the bank is responsible of the loss by not adhering to the central requirements, the shareholders will not hesitate to withdraw from the bank thus using their right of false information[1].

In order to summarize the advancement of Islamic banks when it comes to following to complying with regulations over reserve capital and risk avoidance.

[1]Conference on Good Governance of the Banking Sector Shift from Basel 1 to Basel 2 (2007). Basel Risk-Based Capital Adequacy Adjusted Framework in Islamic Banks

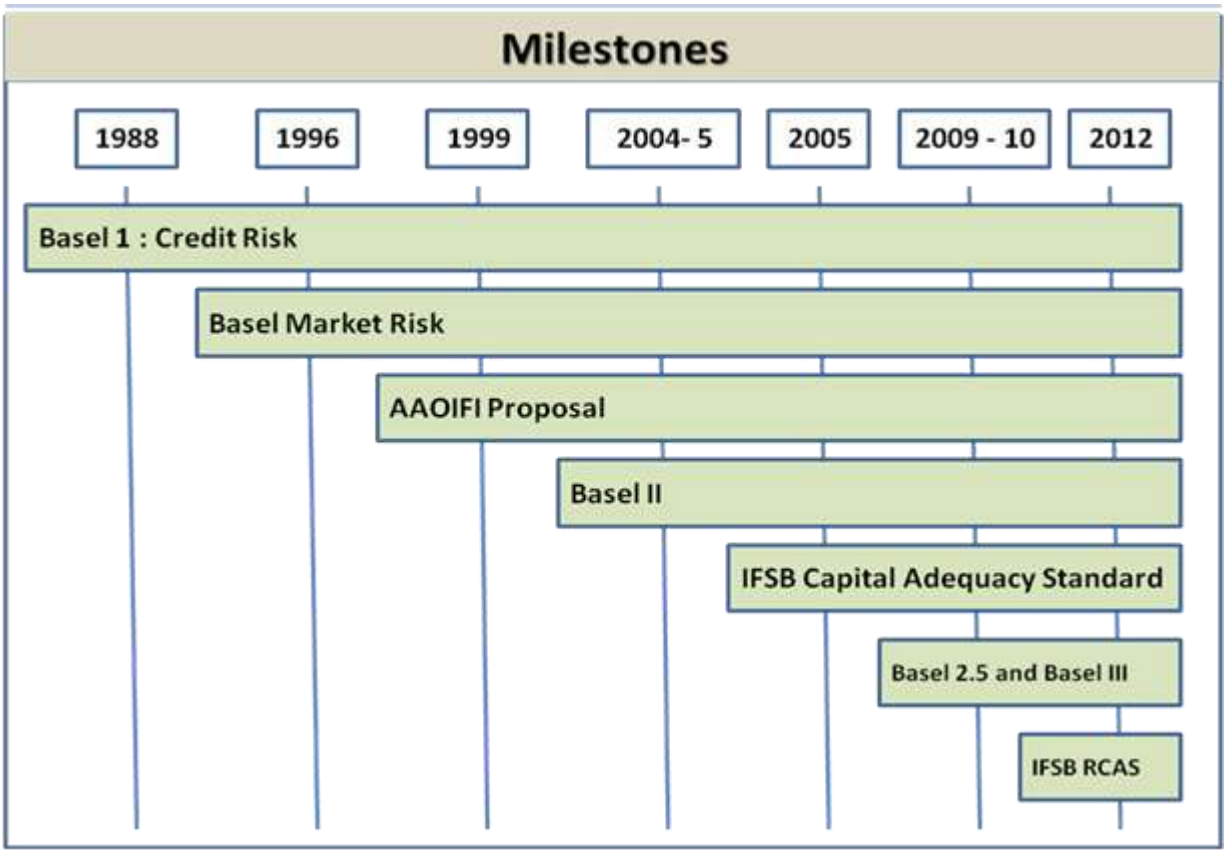


figure (2.2): summarize the advancement of Islamic banks when it comes to following to complying with regulations over reserve capital and risk avoidance (Jaseem, 2012)

*** Basel II Calculations:**

Capital adequacy ratio= Banks Total capital/Risk Weighted Assets * 100 (must be higher that/equal to) 8%.

Therefore, the formula will be generated under Basel II as following:

Capital adequacy ratio= Tier I capital + Tier Two capital/RWA (Credit Risk+ Market Risk + Operation Risk) * 100 (must be higher that/equal to) 8%[1].

Tier 1 capital are defined as: bank's core capitals that are used at times of financial emergency/crisis in order to absorb losses without causing any impact on daily operations. It includes (audited revenue reserves, ordinary share capital, intangible assets, and future tax benefits.)

[1]The development of Islamic finance in the GCC. Research Report/ Kuwait Programme on Development, Governance and Globalisation in the Gulf States, London School of Economics, May 2009.

Tier 2 capital are defined as: bank's supplemental capitals used to absorb losses at the time when assets winding up. They include (revaluation reserves, perpetual cumulative preference shares, retained earnings, subordinated debt and general provisions for bad debt.)

The lower half of the equation demonstrate the RWA of the bank, which is the sum of all the banks' assets that are weighted by risk. In this context of Basel II, (**RWA is calculated on assets on credit risk, market risk, and operational risk**). Each of these assets has its own percentage, which indicated the assets probability to decrease in value. However, there are safe assets that do not enter in the equation, such like government debt, that holds RWA of 0%[1].

2.3.10. Credit Risk Calculation in Basel II:

There are two different ways proposed by Basel II to calculate the credit risk or as referred to sometimes (expected loss)[2].

* Expected loss= Probability of default*Loss Given at default*Exposure at Default

The second method is using the internal rating of banking activities.

table (2.5): Risk on Banking Activities[3]:

Type of financial activity	Risk weighting
Government Loans	0%
Fully secured mortgage loan	35%
fully secured loan on commercial property	100%
Past due loans	150%
higher provisioning past due loans	100%
Past due housing loans	100%
Cash	0%
higher provisioning past due housing loans	50%

[1] www.BIS.org : Basel III : A global Regulatory framework for more resilient banks and banking systems 65,December 2010 (rev June 2011) .
[2] GCC Outlook - December 2010.
[3] ACI official Material

The bank allocates the assets and sort them into these buckets, then multiply them by their percentage, and add them all together. To formulate the calculation, it then becomes as (Haron & Yamirudeng, 2003):

a. RWA= Risk Weights attached to assets * Assets.

b. RWA * 0.08 (8%)= Regulatory capital for credit risk.

table (2.6): Credit ranking of sovereign and banks(ACI, 2019)

Credit Assessment	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	Below B-	Unrated
Risk Weight	0%	20%	50%	100%	150%	100%

table (2.7): Credit assessments for sovereign

Credit Assessment	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	Below B-	Unrated
Risk Weight	20%	50%	100%	100%	150%	100%

Credit assessments for Banks

2.3.11. Market Risk Calculation in Basel II:

The market risk calculation proposed by Basel accord can be calculated using the model of (Value at Risk) or what is known as VaR. in order to calculate the VaR, we have use three different parameters, which are (Holding period, Confidence level, and Reporting currency of equity.

Holding period, have two different choices, 1 day, or 10 days' period. However, most financial institutions, including Islamic banks use the 1-day interval, to the fluid

composition of their risk portfolio, but regulators require 10days holding period, since it is positively correlated with the VaR, as the longer the period, the longer the VaR will be.

The confidence level or (interval), is also divided in two groups (95% and 99%). The choice of confidence level depends mainly on the purpose for which the VaR is being used. Most banks chose to work with the 95% interval, even though the regulations of Basel II suggest that 99% interval will produce greater VaR[1].

Example: what is the correct interpretation of a EUR 5,000,000 overnight VaR figure with a 95% confidence level?

The answer is simple, since the interval used is 95%, that suggests that out of 100 days, the loss will be expected to appear on 5 days. The loss amount will be at least 5,000,000 EUR in 5 out of the upcoming 100 days.

regulators have different set of requirements in regards of this calculation as mentioned above[2];

- 99% interval must be used to be more accurate
- A 10-days (Business days) holding period is required
- VaR must be calculated daily.

Operation Risk Calculation in Basel II:

Under Basic indicator approach, the operational risk is calculated as following:

Average capital in 3 years interval * 15% of the positive annual gross income[3]

Under the standardized approach, the situation is different, as it includes more set of data. The calculation of this set is as follows[4]:

- Banks' activities are divided into 8 business lines.
- The capital charge for business lines=
- Income from each business line * Beta factor (between 12% to 18%)[1]

[1]ACI Material for Certificate exam 2019
[2] Financial Services Authority: Guidelines on Risk Assets
[3]BCBS official website.
[4] Global Insurance Center, Solvency II (2008)

- Sum of each business line over the past three years.

table (2.8): Sum of each business line over the past three years

Business Line	Beta Factor
Agency services	15%
Asset Management	12%
Commercial banking	15%
Corporate finance	18%
Payment and settlement	18%
Retail banking	12%
Retail Brokerage	12%
Trading and sales	18%

[2]

2.3.12. Palestinian Monetary Authority regulations on capital adequacy.

Banks are considered a major participant on the Palestinian financial market. As of September 2011, the Palestinian banking sector only consisted of 3 Islamic banks (Islamic Bank of Palestine, Arabic Islamic Banks, and Al-Safa Bank) and 16 conventional banks, 10 of which were foreign banks. None of them is an investment bank, and despite the weak economic situation banks total assets increased in the last 5 years by 55% to almost $9 billion (International Capital Market Association, 2013). In Palestine, the responsibility for financial regulation and supervision is shared between the Palestine Monetary Authority (PMA) and the Palestine Capital Market Authority (PCMA). When the PMA oversees and regulates banks, money changers and microfinance institutions, it is the role of the PCMA for the securities market, insurance companies and real-estate institutions(International Capital Market Association, 2013). For the record, the PCMA is

[1] Finance Train: https://financetrain.com/basel-ii-standardised-approach-for-credit-risk/
[2] http://www.bis.org/publ/bcbs107.htm Basel II: International Convergence of Capital Measurement and Capital Standards: a Revised Framework (BCBS)

in the process of applying for membership of the International Organization of Securities Commission (IOSCO).

Moreover, according to Sherin Al-Ahmad (Chief Macro-prudential supervision, Palestine Monetary Authority), the main goal of the Palestinian monetary authority is to establish the main protected base for Palestinian banking market. As she stated in a question & answer interview in 2013, "The implementation of Basel II & III by 2013 is the first item in our agenda, together with the calibration of our Central Bank law based on best international practices and the development of the Deposit Insurance scheme under the World Bank technical assistance (International Capital Market Association, 2013)". Therefore, we can see that, regardless of the Palestinian situation with pro-longed occupation, the PMA is still trying to maintain stability over its banks and act like a legit central bank.

The PMA established several regulations for all banks to be complied with, and based the formation of these regulations over the characteristics of Basel Accord. These regulations regarded highly the capital adequacy of all banks including the foreign and the local.

According to the fifth material of the Palestinian banking law published in 2002, all the Palestinian banks have to comply and adhere with the regulations proposed by Basel in the regards of capital adequacy. In particular, all banks have to create a reserve that is no less than 35 million USD, as it is considered to be the minimum capital required to practice any activities in a bank. However, the breakdown of this capital adequacy in reserve was split between local and foreign banks in the Palestinian market (PMA, 2002).

*Local Banks: the capital is 35 million USD or what is equivalent in different currencies. They also focused on maintaining a stable CAR, that is not less than 12%, although Basel 1 and 2 clearly demanded 8%, but having more capital is a safeness for stress-testing the ability of the bank to survive any financial shocks. The calculation of this CAR, is based on the PMA's requirements and is demanded quarterly. The PMA did not stop its regulations over local banks here, but they also required them to increase their paid capital (PMA, 2008), during the period of expansion.

* Foreign Banks: he capital is 35 million USD or what is equivalent in different currencies, traded in Palestine. The capital base shall remain 35 million USD in all

cases, and in any case of breach, the Head-Quarter of the bank has to close the difference immediately (PMA, 2008). These calculations are also done on quarterly basis. The main difference between the foreign banks and the local banks, is the interest paid to HQ, where foreign banks are not allowed to pay interest to HQ for branches operating in Palestine. Yet again, all foreign banks must adhere to the PMA provisions, and must place a non-withdrawable capital deposit with the PMA that is equal to/ more than 30% of the total capital paid (Keeping in mind that the PMA will not accept any CD with an amount less than 10 million USD) (PMA, 2009)

*. If foreign banks seek to take assessment loans to increase their CAR in cases of breach, the approval has to be submitted by the PMA.

Capital regulations where not the only thing regarded by the PMA, but they also took in consideration the cases of any possible breach and the penalization when this occurs. According to the laws sat by the PMA in 2002, any foreign bank failing to comply with the PMA's standard CAR has to (PMA, 2011):

* Maintain the correct amount of CAR with its account in the PMA, before placing any amount of deposits with the HQ branch.

* Banks with dividend sharing, are not allowed to share dividend if the CAR is below the requirements of the PMA (Qaron, 2013)(as mentioned above, this can be fatal for the cases of breach in the Islamic banking sector). Therefore, we can see that the PMA regulation were strict in these cases of CAR and compliance and that comes to the nature of the situation in the Palestinian economy in general.

2.3.13. Study Case of; The Islamic Palestinian Bank.

There are two main Islamic banks in Palestine, the Palestinian Islamic and the Arab Islamic as illustrated in the below table

table (2.9): main Islamic banks in Palestine

	Bank's Name	Founding	Working	Branches
1	Islamic Bank of Palestine	1995	1997	9
2	Arab Islamic	1995	1996	8

[1]

Palestine Islamic Bank History:

The Palestine Islamic Bank obtained the final approval to work in the Palestinian financial sector from the PMA on 15th of May 1997, under the name of (the Palestine Islamic Bank Company limited public shares)[2]. The bank's capital consists of 10 million U.S. dollars divided into 10 million shares, the face value of each share is one American dollar. Moreover, founders have attained over 8,035,000 share, which is equivalent to 80.35% of the common published capital(Zuabi, 2008).

The Palestine Islamic Bank is the most capital-paying among Islamic banks operating in Palestine and has a broad base of founders and shareholders inside and outside Palestine. Furthermore, the role of the Palestinian Monetary Authority in dealing with Islamic banks, and in what is related to the capital adequacy, the PMA uses the same calculations for both conventional and Islamic banks, ignoring all other recommendations produced by the AAOIFI, and kept their focus on the Basel accord regulations.

The CAR calculation proposed by PMA (Tier 1) is[3]:

* Paid Capital: which increase in 2015, to reach 50 million USD or what is equivalent in other currencies, giving all banks a timeline for three years to increase their paid capital. In addition to that, the banks shall maintain the 12% rate in all scenarios.

[1] PMA annual report (2007)
[2] Islamic Bank of Palestine Website.
[3] Palestinian Monetary instructions for the year of 2016, in regards of complying with CAR requirements under Basel II

* Legal Reserve: based on article 31 (of the Banking Law No. 9) of the provisions for the year 2010. the statutory reserve, which is formed at 10% of the net annual profits The bank's money is not paid according to the companies' law in Palestine until it becomes equal to the banks' capital

* The declared precautions: These reserves include both statutory reserve as well as undistributed earnings. However, in order to calculate the final weight of this slice, the PMA suggested to distract: Intangible assets; Profit / loss for the year; and Profits / losses under settlement(Musbah, 2018).

PMA's Tier 2 building block under Basel II:

* Subordinate Capital: that includes Precautions for revaluation; General precautions for banking operations; General precautions for non-bank operations; and Qualified support loans (remaining over 5 years old)[1].

The PMA's quarterly check-ups on compliance with Basel II, where mentioned by Musbah, as the result of his research, and according to the data provided by both the PMA and the Islamic Bank of Palestine,

table(2.10): the Islamic Bank of Palestine with ratio(Musbah, 2018).

Year	Capital	Capital to Finding Ratio	Capital ratio to weighted assets
2009	27,897,593	9.2%	35.90%
2010	42,599,007	11.92%	36.72%
2011	46,616,023	11.87%	30.09%
2012	46,365,785	10.96%	29.80%
2013	49,691,544	9.895	21.65%
2014	54,620,338	9.18%	16.37%
2015	62,225,298	13.47%	16.51%
2016	76,440,183	6.15%	12.88%

[1] Palestinian Monetary instructions for the year of 2016, in regards of complying with CAR requirements under Basel II

The table shows that the Islamic Bank of Palestine applies the ratio approved by Basel II for capital adequacy, which is 8%, and applies the percentage approved by the Palestinian Monetary Authority, which is 12%, however, once we calculate the average capital adequacy ratio consider the performance of the Islamic bank of Palestine during the years between 2009 and 2016, we find that the compliance ratio in average is equal to 24.99%.

Yet again, Zuabi in her research elaborated more on the actual compliance on the Islamic bank of Palestine taken the base year 2007, where the equation was the following(Zuabi, 2008):

Capital Adequacy Ratio= Tier 1+Tier 2/CR+MR+OR(RWA)*100

CAR= 19,345,213/ 55,813,495 + 7,147,561 + 12,186,786 * 100=25.74%

Again, we can see that during the year of 2007, the Islamic bank of Palestine complied with the 8% proposed by Basel II, and the 12% proposed by the PMA, even surpassed the requirements. Why so you might ask, since the Islamic banks are different in terms of Fund Sources/Uses, and are also experiencing different types of risks that are unique to their banking activity, it is normal that once they comply with the ratio of Basel and the PMA, they would show high compliance and strength.

Chapter Three:

3.1. Method and Procedures

This chapter deals with a detailed description that the researcher followed in carrying out the study, including defining the study method, describing the study community, identifying the study sample, preparing the study tool (the questionnaire), verifying its sincerity and consistency, and explaining the study procedures and the statistical methods used in handling the results, below is a description of these procedures.

3.2 Study Approach

In order to achieve the aims of the study, the researcher used the analytical method. It is defined as the curriculum that studies a phenomenon, event or current issue that can be obtained from which information can be answered on research questions without interference from the researcher. Through which the researcher tries to describe the phenomenon under study, and to analyze its data, and to clarify the relationship between the components and opinions that are presented around it, the processes that it includes and the effects that arise, and it is one of the forms of analysis and scientific interpretation organized to describe a phenomenon or problem, and its classification, analysis and subject to careful studies by examination and analysis.

3.3 Describe the variables of the sample members

Table (5.1) shows the distribution of respondents according to the gender variable, that 54.5% for males and 45.5% for females. The Jop title variable shows that 24.1% are head of department, 19.3% are director of department, 9% are (General director, director, deputy director, branch director), and 47.6% are employees. The variable of the educational qualification shows that 9% for diploma or less, 61.3% for Bachelor's, and 29.7% for postgraduate studies. The variable of years of experience shows that the rate of 46.2% for

less than 5 years, 30.3% for 5- less than 10 years, and 23.5% for more than 10 years. The age variable shows that the rate of 64.1% less than 30 years, 21.4% from 30-40 years, and 14.5% to more than 40 years.

Table (3.1): Distribution of study sample according to the study variables

Variables	**Levels**	**N**	**%**
Gender	Male	79	54.5
	Female	66	45.5
Job title	Head of the Department	35	24.1
	Director of the Department	28	19.3
	General director, director, deputy director, branch director	13	9.0
	employee	69	47.6
Educational qualifications	Diploma and below	13	9.0
	Bachelor's degree	89	61.3
	Postgraduate studies	43	29.7
Years of experience	Less than 5 years	67	46.2
	5 years to less than 10 years	44	30.3
	More than 10 years	34	23.5
Age	Less than 30 years	93	64.1
	30-40 years	31	21.4
	More than 40 years	21	14.5

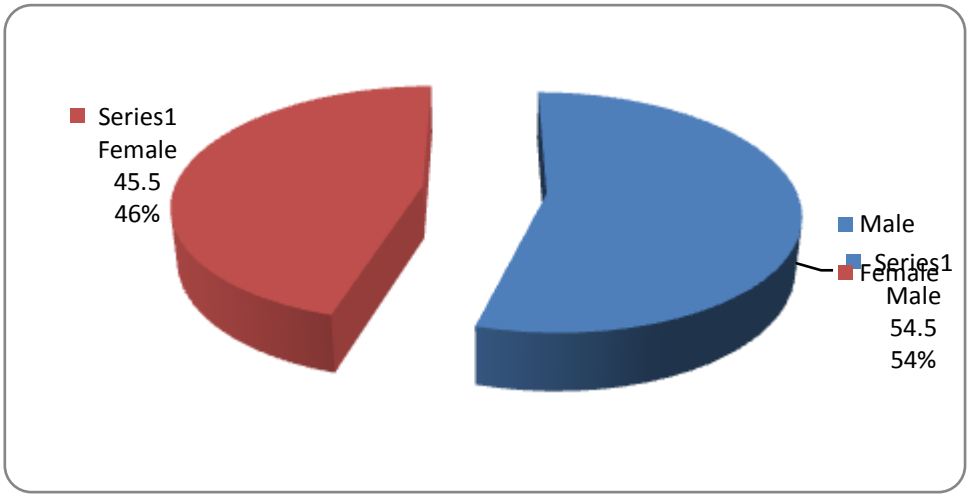


figure (3.1): Distribution of study sample according to the gender variable

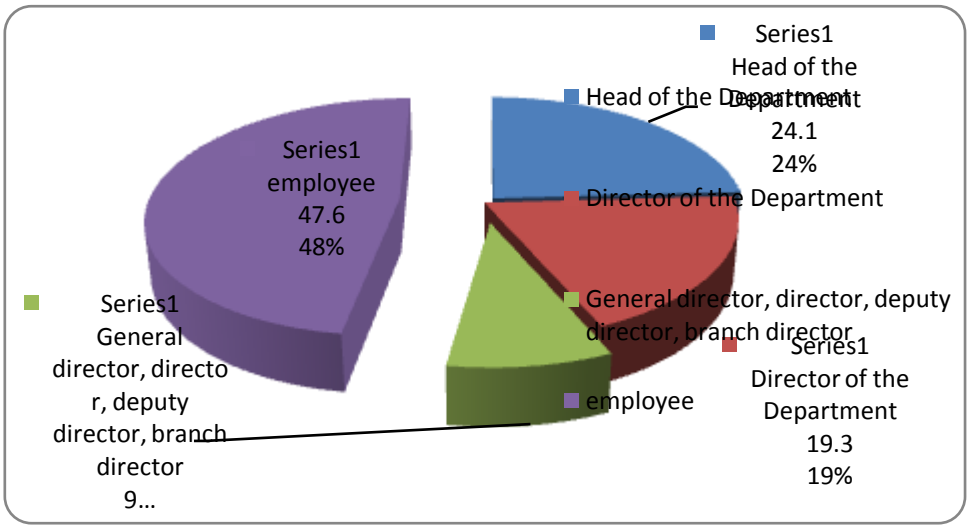


figure (3.2): Distribution of study sample according to the job title variable

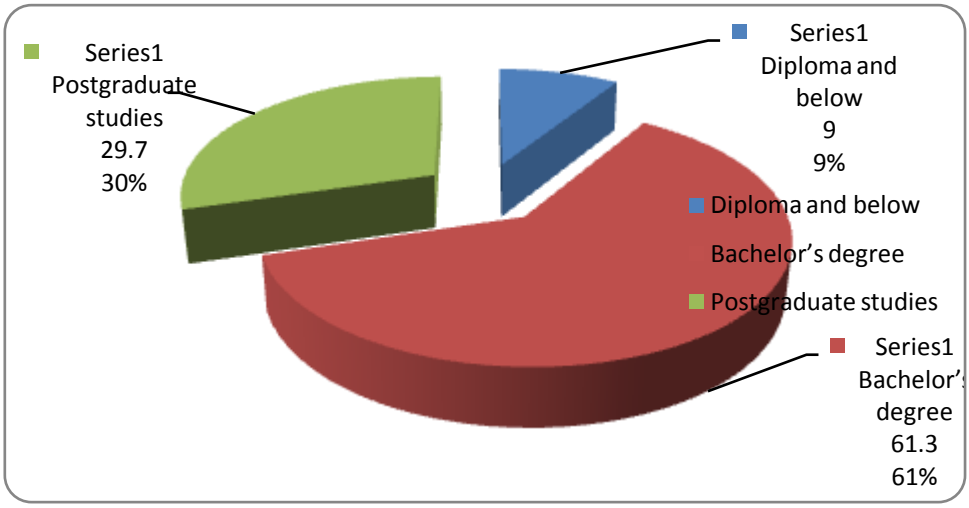


figure (3.3): Distribution of study sample according to the Educational qualifications variable

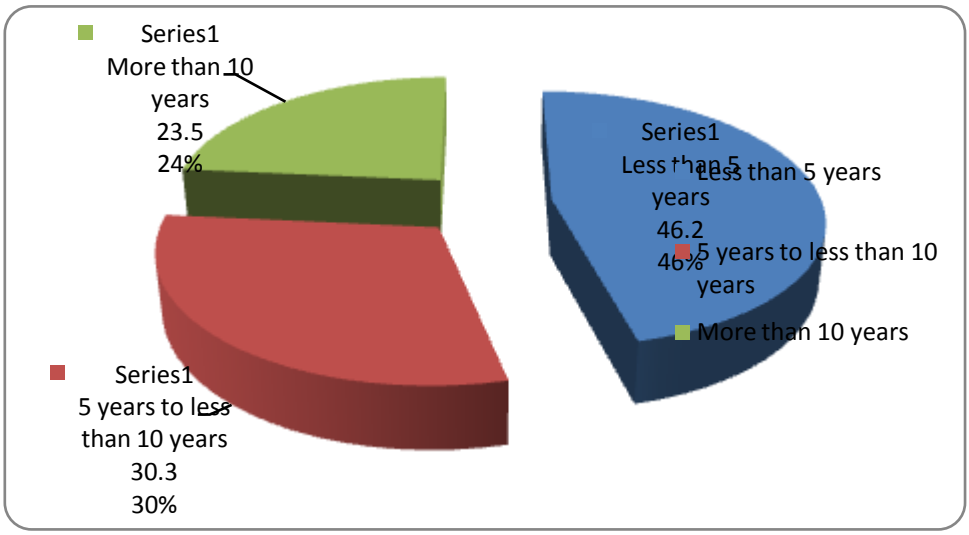


figure (3.4): Distribution of study sample according to the Years of experience variable

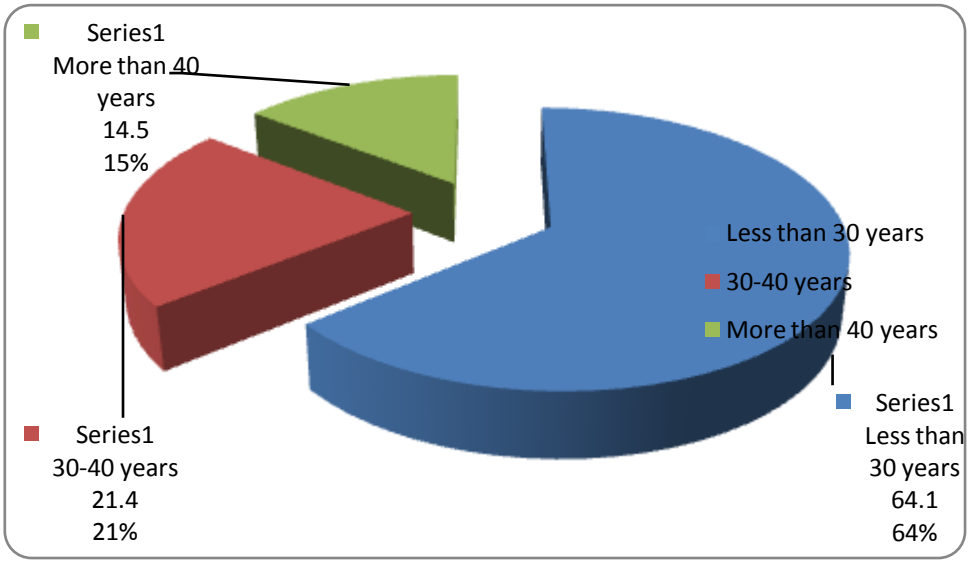


figure (3.5): Distribution of study sample according to the Age variable

3.4 Tools of study

Based on the study's objectives, the researcher used a measure to check the extent of Islamic banks 'application of the Basel Agreement by referring to a study by the Arab Committee for Banking Supervision in 2006, in addition to a master's thesis (Ghanaian, 2015), where the questionnaire consisted of personal information for the study sample in addition to 6 component areas Of the 36 complete paragraphs, they are as follows:

* personal variable:

1. Gender(Male, Female)

2. Job Title(Head of the Department, Director of the Department, General director, director, deputy director, branch director, employee)

3. Educational qualifications:(Diploma and below, Bachelor's degree, postgraduate studies)

4. Years of Experience:(Less than 5 years, form 5-less than 10 years, more than 10 years)

5. Age: (Less than 30 years, form 30- 40 years, more than 40 years)

* fields of study:

Section 1: Risk management principles in Islamic banks and It consists of (8) sentences.

Section 2: Risk management tasks in Islamic banks and It consists of (9) sentences.

Section 3: Minimum capital and risk measurement methods in accordance with Basel II and It consists of (9) sentences.

Section 4: Supervisory review according to Basel II and It consists of (3) sentences.

Section 5: Market discipline in accordance with Basel II and It consists of (3) sentences.

Section 6: Implementation Basel III and It consists of (4) sentences.

3.5 Validity

The researcher designed the questionnaire in its initial form, and then the validity of the study tool was verified by presenting it to the supervisor and a group of arbitrators with expertise and expertise (Dr. Orobah Barghouthi, Dr. Mohammad Bader, Dr. Salwa Barghouthi, Dr. Ahmad Herzallah, Dr. Omar Sleibi).

The researcher distributed the questionnaire to a number of arbitrators. Where they were asked to express their opinion on the questionnaire paragraphs in terms of: the clarity of the language of the paragraphs and their linguistic integrity, the extent to which the paragraphs cover the studied aspect, and adding any information, modifications, or paragraphs they deem appropriate, and according to these notes the questionnaire was finalized. On the other hand, the validity of the tool was also verified by calculating the Pearson correlation coefficient of the questionnaire paragraphs with the overall degree of the tool, and there was a statistical significance in all the paragraphs of the questionnaire and indicates that there is an internal consistency between the paragraphs. The following table shows this:

Table (3.2): Pearson Correlation results for The Extent of Basel Accord implementation on Islamic Banks in Palestine

N	Value (R)	Sig	N	Value (R)	Sig	N	Value (R)	Sig
1	0.707**	0.000	13	0.606**	0.000	25	0.501**	0.000
2	0.475**	0.000	14	0.462**	0.000	26	0.626**	0.000
3	0.691**	0.000	15	0.532**	0.000	27	0.882**	0.000
4	0.635**	0.000	16	0.443**	0.000	28	0.487**	0.000
5	0.396**	0.000	17	0.498**	0.000	29	0.731**	0.000
6	0.578**	0.000	18	0.845**	0.000	30	0.876**	0.000

7	0.517**	0.000	19	0.382**	0.000	31	0.500**	0.000
8	0.604**	0.000	20	0.774**	0.000	32	0.775**	0.000
9	0.797**	0.000	21	0.560**	0.000	33	0.793**	0.000
10	0.409**	0.000	22	0.493**	0.000	34	0.477**	0.000
11	0.748**	0.000	23	0.735**	0.000	35	0.749**	0.000
12	0.417**	0.000	24	0.583**	0.000	36	0.521**	0.000

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed)

3.6 Reliability

The researcher verified the stability of the tool, by calculating the stability of the total score of the stability factor, for the fields of study according to the stability equation of Cronbach Alpha, and the overall score for The Extent of Basel Accord implementation on Islamic Banks in Palestine (0.951), and this result indicates that this tool has the stability that meets the purposes of studying. The following table shows the coefficient of stability for the domains and the overall score.

Table (3.3): Reliability coefficient results for fields

Fields	N. of questions	Cronbach Alpha
Risk management principles in Islamic banks	**8**	**0.777**
Risk management tasks in Islamic banks	**9**	**0.786**
Minimum capital and risk measurement methods in accordance with Basel II	**9**	**0.857**
Supervisory review according to Basel 2	**3**	**0.794**
Market discipline in accordance with Basel 2	**3**	**0.831**
Implementation Basel 3	**4**	**0.823**
Total	**36**	**0.951**

3.7 Study Procedures

The researcher applied the tool to the members of the study sample, where the researcher distributed electronic questionnaire via Google Form, and after completing the process of collecting questionnaires from the sample members after answering them in a correct way, it became clear to the researcher that the number of valid retrieved questionnaires that were subject to statistical analysis: (145) questionnaire.

3.8. Statistical treatment

After collecting the questionnaires and verifying their validity for the analysis, they were encoded (giving them two specific numbers), in preparation for entering their data into the computer for performing the appropriate statistical treatments, and analyzing the data according to the study's questions. The study data. Statistical processing of the data was done by extracting the arithmetic averages and the standard deviations for each of the paragraphs. Resolution, t-test, one-way ANOVA, Pearson correlation coefficient, and Cronbach Alpha, using SPSS (Statistical Package For Social Sciences).

Chapter Four:

Results

4.1 Introduction

This chapter included a presentation of the results of the study, which was reached by the researcher on the subject of the study, which is "The Extent of Basel Accord implementation on Islamic Banks in Palestine" and the effect of each of the variables through the response of the sample members to the study tool, and the analysis of the statistical data obtained. In order to determine the degree of average response of the study sample, the following degrees were adopted:

Degrees	Means range
Low	2.33 and blew
Medium	Form 2.34-3.67
High	From 3.68 and above

4.2 Results of study questions

4.2.1 Results related to the first question

What is The Extent of Basel Accord implementation on Islamic Banks in Palestine?

To answer this question, the researcher calculated the arithmetic averages and the standard deviations of the responses of the study sample individuals on the questionnaire fields that express The Extent of Basel Accord implementation on Islamic Banks in Palestine.

table (4.1): Means and standard deviations for The Extent of Basel Accord implementation on Islamic Banks in Palestine

N	Fields	Mean	SD	Degree
4	**Supervisory review according to Basel 2**	**4.5195**	**0.42287**	**High**
5	**Market discipline in accordance with Basel 2**	**4.4828**	**0.47780**	**High**
2	**Risk management tasks in Islamic banks**	**4.4774**	**0.34968**	**High**
1	**Risk management principles in Islamic banks**	**4.4707**	**0.40074**	**High**
3	**Minimum capital and risk measurement methods in accordance with Basel II**	**4.3992**	**0.45915**	**High**
6	**Implementation Basel 3**	**4.3966**	**0.52423**	**High**
Average		**4.4513**	**0.37648**	**High**

It is noted from the previous table that expresses the arithmetic averages and the standard deviations of the responses of the study sample individuals on The Extent of Basel Accord implementation on Islamic Banks in Palestine that the arithmetic mean for the total score (4.45) and a standard deviation (0.376) and this indicates that The Extent of Basel Accord implementation on Islamic Banks in Palestine came High degree.

The field of Supervisory review according to Basel 2 obtained the highest mean of (4.519), and then the Market discipline in accordance with Basel 2 field with mean of (4.482), and then the Risk management tasks in Islamic banks field with mean of (4.477), and then the Risk management principles in Islamic banks with mean of (4.47), followed by the field of the Minimum capital and risk measurement methods in accordance with Basel II with mean (4.399), and then the Implementation Basel 3 with mean (4.396).

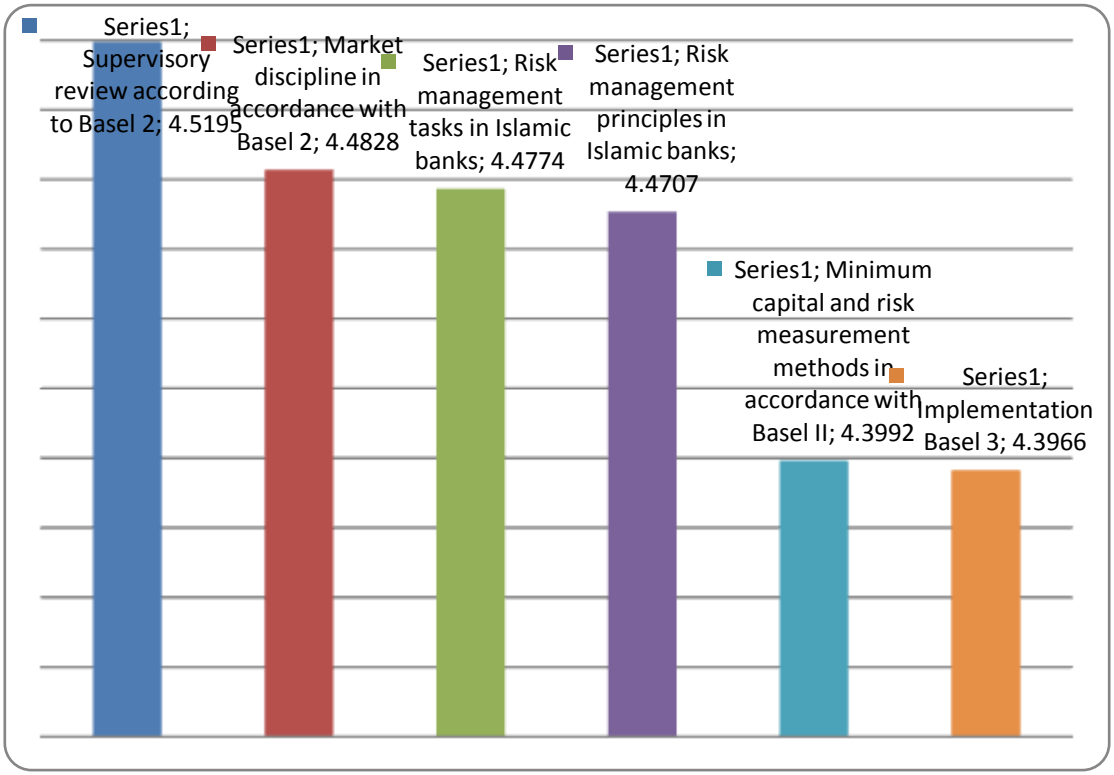


figure (4.1): Means for The fields of Reality of the Basel Accord Implementation in Islamic Banks

***What is the level of implementation of Risk principles in Islamic banks?**

The researcher calculated the arithmetic averages and the standard deviations of the responses of the study sample individuals on the questionnaire paragraphs that express the field of Risk management principles in Islamic banks.

table (4.2): Means and standard deviations for the Risk management principles in Islamic banks filed

N	Sentence	Mean	SD	Degree
1	Risk management aims to stabilize profits	4.70	0.728	High
3	Appointing an official with experience in the banking field for each type of major risk	4.64	0.674	High
6	Using modern information systems to manage risks	4.60	0.628	High
7	There is an independent unit in the bank that audits all Islamic banking business, including risk management	4.58	0.597	High

4	Establish a specific system for measuring and monitoring risks	4.56	0.676	High
5	Valuating the assets of Islamic banks, especially investment, is a fundamental principle for measuring risk and profitability	4.35	0.534	High
8	The Board of Directors is responsible for managing risks	4.32	0.733	High
2	There is an independent committee called "Risk Management Committee" that is concerned with preparing the general policy	4.01	0.527	High
Avarage		**4.4707**	**0.40074**	**High**

It is noted from the previous table that expresses the arithmetic averages and the standard deviations of the responses of the study sample individuals on the field of Risk management principles in Islamic banks that the arithmetic mean for the total score (4.47) and standard deviation (0.400) and this indicates that the field of Risk management principles in Islamic banks came with a high degree.

The results also indicate in Table No. (4.2) that all the sentences came with a high degree. The paragraph " Risk management aims to stabilize profits " at the highest arithmetic average (4.70), followed by the paragraph " Appointing an official with experience in the banking field for each type of major risk " with an average of (4.64). The paragraph “There is an independent committee called "Risk Management Committee" that is concerned with preparing the general policy” at the lowest mathematical average (4.01), followed by the paragraph “The Board of Directors is responsible for managing risks” with an average of (4.32).

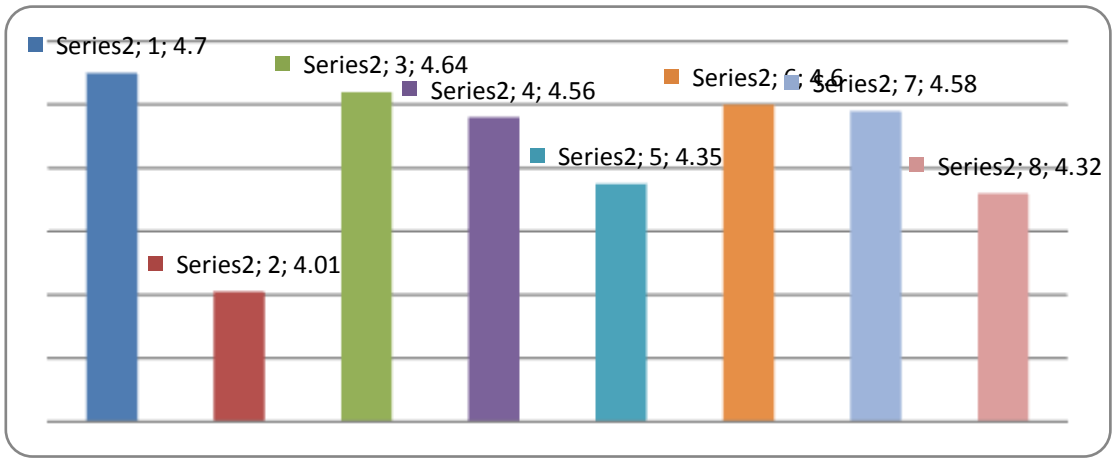


figure (4.2): Means for the Risk management principles in Islamic banks filed

*** What is the level of implementations of Risk management tasks in Islamic banks?**

The researcher calculated the arithmetic averages and the standard deviations for the responses of the study sample individuals to the questionnaire paragraphs that express the field of Risk management tasks in Islamic banks.

table (4.3): Means and standard deviations for Risk management tasks in Islamic banksfiled

N	Sentence	Mean	SD	Degree
1	An internal risk management policy	4.80	0.522	High
3	Preparing risk reports and submitting them to the board of directors and stakeholders	4.77	0.514	High
5	A method of risk management is risk control	4.48	0.698	High
7	There is effective oversight by the Board and senior management of risk management	4.48	0.625	High
8	There is a correlation between the risk management policy and the risks to which the bank is exposed	4.46	0.565	High
9	Separating jobs from the main pillars of risk management	4.44	0.588	high
4	Choosing the most appropriate way to manage the risks facing Islamic banks, according to the degree of safety and the necessary cost	4.43	0.586	High
6	A method of risk management is risk financing (by hedging or transferring)	4.40	0.606	High
2	The presence of cultural awareness within Islamic banks regarding the management of risk	4.05	0.446	High
Avarage		**4.4774**	**0.34968**	**High**

It is noted from the previous table that expresses the arithmetic averages and the standard deviations of the responses of the study sample individuals on the field of Risk management tasks in Islamic banks that the arithmetic mean for the total score (4.477) and a standard deviation (0.349) and this indicates that the reality of the field of Risk management tasks in Islamic banks came with an high degree.

The results also indicate in Table No. (4.3) that all the sentences came with a high degree. And the paragraph " An internal risk management policy " scores the highest average score (4.80), followed by a paragraph " Preparing risk reports and submitting them to the board

of directors and stakeholders "with an average score of (4.77). The paragraph "The presence of cultural awareness within Islamic banks regarding the management of risk" has the lowest arithmetic average (4.05), followed by the paragraph "A method of risk management is risk financing (by hedging or transferring)" with an average score of (4.40).

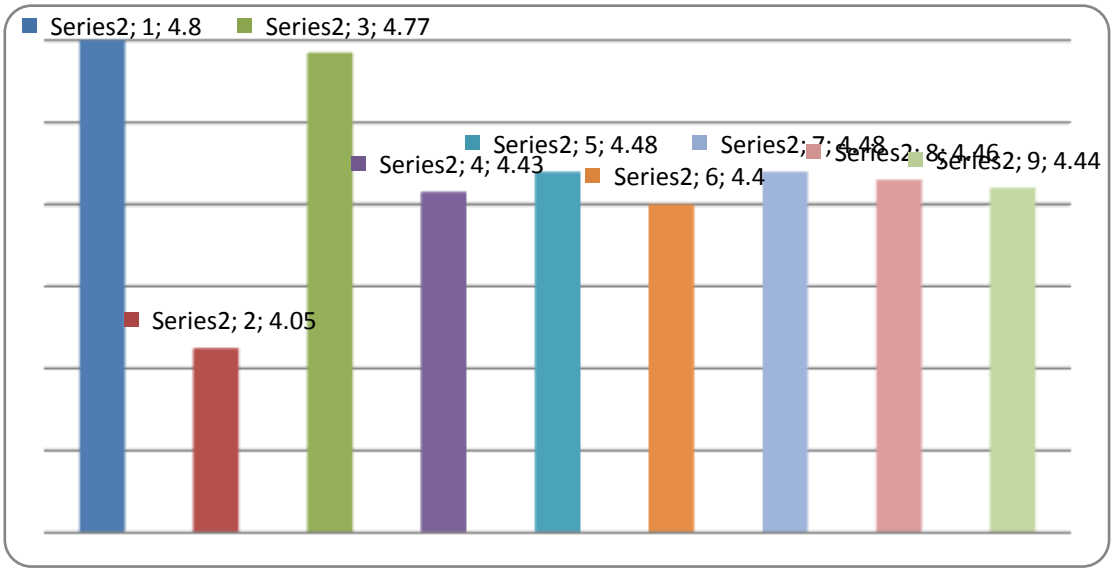


figure (4.3): Means for Risk management tasks in Islamic banksfiled

*** What is the level of Minimum capital and risk measurement methods in accordance with Basel II in Islamic banks?**

The researcher calculated the mean and standard deviations for the responses of the study sample individuals to the questionnaire paragraphs that express the field of the Minimum capital and risk measurement methods in accordance with Basel II.

table (4.4): Means and standard deviations for the Minimum capital and risk measurement methods in accordance with Basel II filed

N	Sentence	Mean	SD	Degree
1	Minimum capital adequacy ratio of 8%	4.66	0.749	high
3	To measure credit risk, the main internal rating method is used	4.63	0.735	high
9	To measure operating risks, an advanced measurement method is used	4.44	0.735	high
4	To measure credit risk, we rely on the advanced	4.43	0.653	high

	internal rating method			
6	To measure market risks, the method is used in internal models (statistical models)	4.43	0.779	high
8	To measure operating risks, the main indicator method is used	4.41	0.618	high
7	To measure operating risks, a typical method is used	4.34	0.689	high
5	To measure market risks, we rely on the standard method	4.27	0.626	high
2	To measure credit risk, the standard method is used	4.00	0.373	high
Avarage		**4.3992**	**0.45915**	**High**

It is noted from the previous table that expresses the arithmetic averages and the standard deviations of the responses of the study sample individuals on the field of the Minimum capital and risk measurement methods in accordance with Basel II that the arithmetic mean for the total score (4.399) and a standard deviation (0.459) and this indicates that the reality of the field of the Minimum capital and risk measurement methods in accordance with Basel II came with an high degree.

The results also indicate in Table No. (4.4) that all the sentences came with a high degree. The paragraph " Minimum capital adequacy ratio of 8%" at the highest arithmetic average (4.66), followed by a paragraph " To measure credit risk, the main internal rating method is used "with an average score of (4.63). And the paragraph " To measure credit risk, the standard method is used " got the lowest arithmetic average (4.00), followed by the paragraph " To measure market risks, we rely on the standard method " with an arithmetic average (4.27).

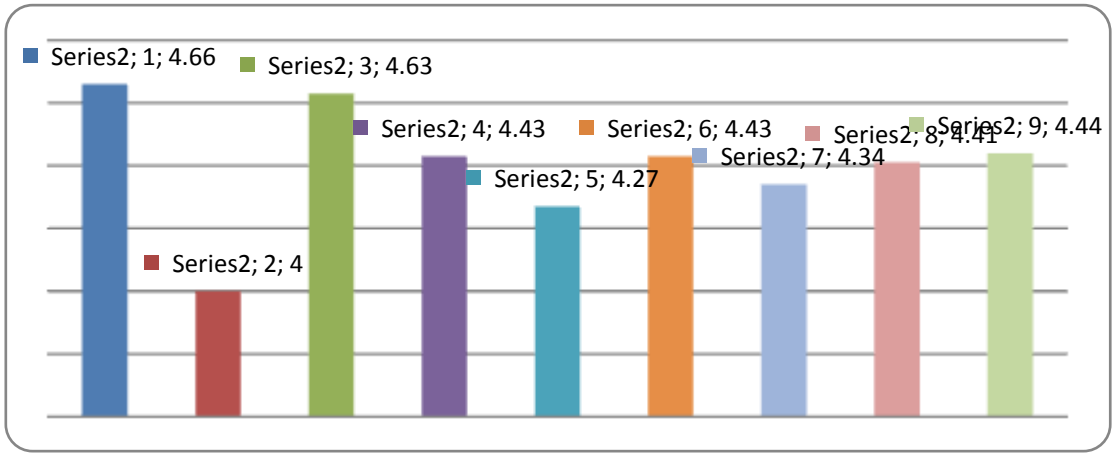


figure (4.4): Means for the Minimum capital and risk measurement methods in accordance with Basel II filed

*** What is the level of Supervisory review according to Basel II in Islamic Banks?**

The researcher calculated the arithmetic averages and the standard deviations of the responses of the study sample individuals on the questionnaire paragraphs that express the field of the Supervisory review according to Basel 2.

table (4.5): Means and standard deviations for the Supervisory review according to Basel 2 filed

N	Sentence	Mean	SD	Degree
1	The supervisory authority reviews the methods of assessing the capital adequacy used by the Islamic banks that are subject to it	4.80	0.494	High
3	The regulatory authority shall enter to prevent any decrease or decrease in the required capital	4.63	0.610	High
2	Ensuring the commitment of Islamic banks to maintain the rate of 8%	4.12	0.498	High
Avarage		**4.5195**	**0.42287**	**High**

It is noted from the previous table that expresses the arithmetic averages and the standard deviations of the responses of the study sample individuals on the field of the Supervisory review according to Basel 2 that the arithmetic mean for the total score (4.519) and a standard deviation (0.422) and this indicates that the reality of the field of the Supervisory review according to Basel 2 It came with a high degree.

The results also indicate in Table No. (4.5) that all the sentences came with a high degree. And the paragraph " The supervisory authority reviews the methods of assessing the capital adequacy used by the Islamic banks that are subject to it " at the highest arithmetic average (4.80), followed by a paragraph " The regulatory authority shall enter to prevent any decrease or decrease in the required capital" with average score (4.63), followed by the paragraph " Ensuring the commitment of Islamic banks to maintain the rate of 8%" with an arithmetic average (4.12).

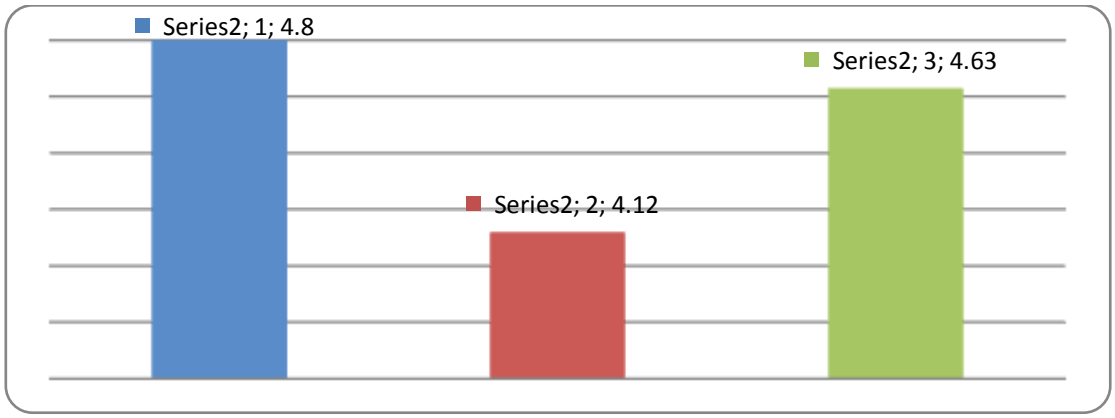


figure (4.5): Means for the Supervisory review according to Basel 2 filed

*** What is the level Market discipline in accordance with Basel II in Islamic Banks?**

The researcher calculated the arithmetic averages and the standard deviations of the responses of the study sample individuals on the questionnaire paragraphs that express the field of the Market discipline in accordance with Basel 2.

table (4.6): Means and standard deviations for the Market discipline in accordance with Basel 2 filed

N	Sentence	Mean	SD	Degree
1	Islamic banks disclose the structure and size of their private funds	4.77	0.598	High
3	Disclosure of capital adequacy according to the size of the potential risks	4.68	0.609	High
2	Disclosure of risk assessments	3.99	0.433	High
Avarage		**4.4828**	**0.47780**	**High**

It is noted from the previous table that expresses the arithmetic averages and the standard deviations of the responses of the study sample individuals on the field of the Market discipline in accordance with Basel 2 that the arithmetic mean for the total score (4.482) and a standard deviation (0.477) and this indicates that the reality of the Market discipline in accordance with Basel 2 It came with a high degree.

The results also indicate in Table No. (4.6) that all the sentences came with a high degree. And the paragraph " Islamic banks disclose the structure and size of their private funds " at the highest arithmetic average (4.77), followed by a paragraph " Disclosure of capital adequacy according to the size of the potential risks" with average score (4.68), followed by the paragraph " Disclosure of risk assessments " with an arithmetic average (3.99).

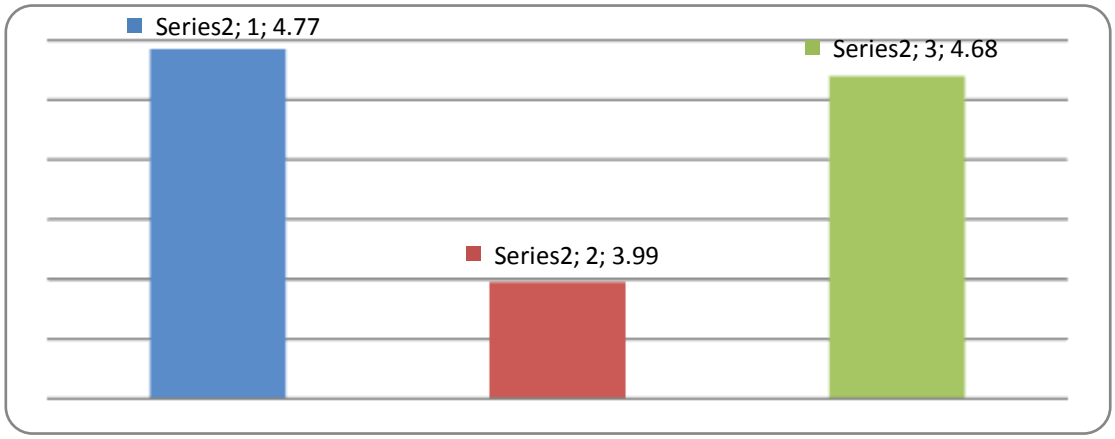


figure (4.6): Means for the Market discipline in accordance with Basel 2 filed

*** What is the level of Implementation Basel III in Islamic Banks?**

The researcher calculated the arithmetic averages and the standard deviations of the responses of the study sample individuals on the questionnaire paragraphs that express the field of the Implementation Basel 3.

table (4.7): Means and standard deviations for the Implementation Basel 3 filed

N	Sentence	Mean	SD	Degree
1	Islamic banks can raise the capital adequacy ratio to 10.5%	4.64	0.663	High
3	Islamic banks must maintain a liquidity ratio to meet short-term benefits	4.61	0.700	High
4	Islamic banks should maintain a liquidity ratio to cope with medium and long-term benefits	4.41	0.682	High
2	Islamic banks will introduce leverage of 3%	3.93	0.536	High
Avarage		**4.3966**	**0.52423**	**High**

It is noted from the previous table that expresses the arithmetic averages and the standard deviations of the responses of the study sample individuals on the field of the Implementation Basel 3 that the arithmetic mean for the total score (4.396) and a standard deviation (0.524) and this indicates that the reality of the Implementation Basel 3 It came with a high degree.

The results also indicate in Table No. (4.7) that all the sentences came with a high degree. And the paragraph " Islamic banks can raise the capital adequacy ratio to 10.5%" at the highest arithmetic average (4.64), followed by a paragraph " Islamic banks must maintain a liquidity ratio to meet short-term benefits" with average score (4.61). And the paragraph " Islamic banks will introduce leverage of 3%" at the lowest arithmetic average (3.93), followed by the paragraph " Islamic banks should maintain a liquidity ratio to cope with medium and long-term benefits " with an arithmetic average (4.41).

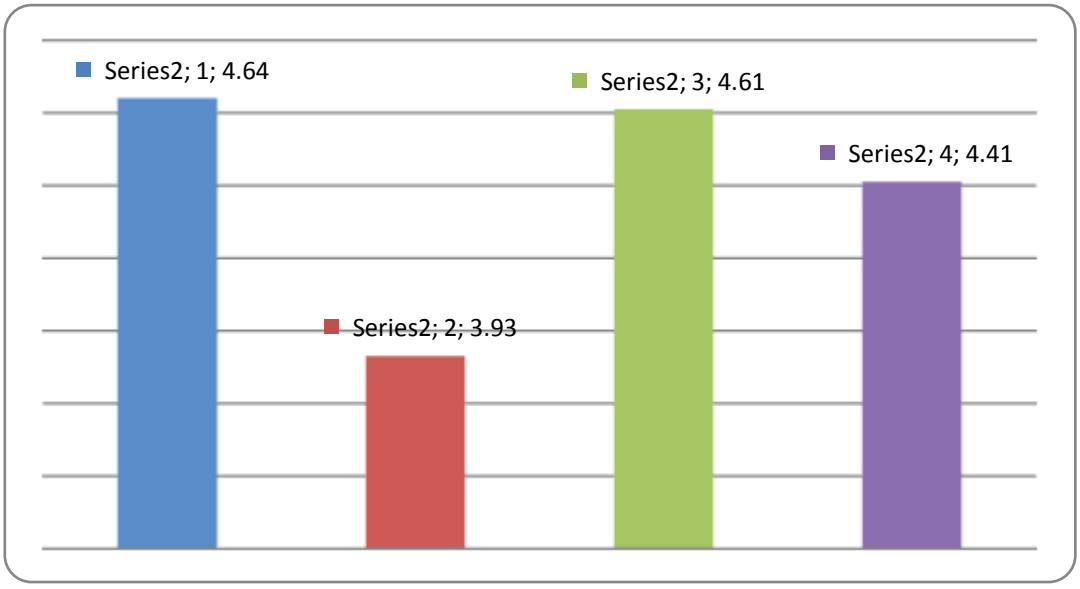


figure (4.7): Means for the Implementation Basel 3 filed

4.2.2 Results related to the second question

Is there any differences in level of The Extent of Basel Accord implementation on Islamic Banks in Palestine according to the variables(gender, Job title, educational qualification, years of experience, age)?

To answer this question, It was converted to the following hypotheses:

Results of the first hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the gender variable"

The first hypothesis was examined by calculating the results of the "T" test and the mean for the response of the study sample members in The Extent of Basel Accord implementation on Islamic Banks in Palestine according to the gender variable

table (4.8): Results of the "T" test for independent samples for The Extent of Basel Accord implementation on Islamic Banks in Palestine according to the gender variable

Fields	Gender	N	Mean	Std. Deviation	Value of "t"	Sig
Risk management principles in Islamic banks	Male	79	4.3956	0.50177	2.687	0.008
	Female	66	4.5606	0.19641		
Risk management tasks in Islamic banks	Male	79	4.4304	0.43740	1.785	0.076
	Female	66	4.5337	0.18818		
The Minimum capital and risk measurement methods in accordance with Basel II	Male	79	4.2911	0.58126	3.450	0.001
	Female	66	4.5286	0.17439		
The Supervisory review according to Basel 2	Male	79	4.4430	0.54097	2.609	0.011
	Female	66	4.6111	0.17130		
Market discipline in accordance with Basel 2	Male	79	4.3924	0.59857	2.713	0.008
	Female	66	4.5909	0.23238		
Implementation Basel 3	Male	79	4.3386	0.62022	1.525	0.130
	Female	66	4.4659	0.37181		
Avarage	Male	79	4.3755	0.47614	2.911	0.004
	Female	66	4.5421	0.16308		

It is clear from the previous table that the value of "T" for the total degree (2.911), and the level of significance (0.004), that is, there are differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the gender variable, as well as to the fields except Risk management tasks in Islamic banks and Implementation Basel 3 feilds, Where the differences in favor to female. and thus the first hypothesis was rejected.

Results of the Second hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Job title variable"

The Secondhypothesis was examined. The arithmetic averages were calculated for the response of the study sample individuals on The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Job title variable.

table (4.9): means and standard deviation for level of The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Job title variable

Feilds	Job title	N	Mean	SD
The Risk management principles in Islamic banks	Head of the Department	35	4.5643	0.15861
	Director of the Department	28	4.5000	0.34359
	General director, director, deputy director, branch director	13	4.5385	0.20656
	Employee	69	4.3986	0.51193
Risk management tasks in Islamic banks	Head of the Department	35	4.5397	0.22246
	Director of the Department	28	4.5437	0.18479
	General director, director, deputy director, branch director	13	4.5043	0.21572
	Employee	69	4.4138	0.45209
The Minimum capital and risk measurement methods in accordance with Basel II	Head of the Department	35	4.5270	0.19121
	Director of the Department	28	4.4008	0.42803
	General director, director, deputy director, branch director	13	4.4274	0.37638
	Employee	69	4.3285	0.56284
The Supervisory	Head of the Department	35	4.6286	0.21038

review according to Basel 2	Director of the Department	28	4.5476	0.30381
	General director, director, deputy director, branch director	13	4.6154	0.18490
	Employee	69	4.4348	0.54624
Market discipline in accordance with Basel 2	Head of the Department	35	4.6000	0.21082
	Director of the Department	28	4.4762	0.39988
	General director, director, deputy director, branch director	13	4.5641	0.21014
	Employee	69	4.4106	0.61343
Implementation Basel 3	Head of the Department	35	4.3643	0.44285
	Director of the Department	28	4.4732	0.32159
	General director, director, deputy director, branch director	13	4.4423	0.55108
	Employee	69	4.3732	0.62075
Avarage	Head of the Department	35	4.5349	0.16005
	Director of the Department	28	4.4851	0.22598
	General director, director, deputy director, branch director	13	4.5000	0.23102
	Employee	69	4.3861	0.49880

It is noted from Table No. (4.9) that there are apparent differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Job title variable, and to know the significance of the differences, one way ANOVA was used as shown in Table No. (4.10):

table (4.10): one way ANOVA test for The Extent of Basel Accord implementation on Islamic Banks in PalestineDepending on the Job title variable

Feilds		**Mean Square**	**df**	**Sum of Squares**	**Value of "F"**	**Sig**
The Risk management principles in Islamic banks	Between Groups	0.749	3	0.250	1.574	0.198
	Within Groups	22.376	141	0.159		
	Total	23.125	144			
Risk management tasks in Islamic banks	Between Groups	0.547	3	0.182	1.506	0.216
	Within Groups	17.061	141	0.121		

	Total	17.608	144			
The Minimum capital and risk measurement methods in accordance with Basel II	Between Groups	0.927	3	0.309	1.480	0.223
	Within Groups	29.431	141	0.209		
	Total	30.358	144			
The Supervisory review according to Basel 2	Between Groups	1.053	3	0.351	2.004	0.116
	Within Groups	24.697	141	0.175		
	Total	25.750	144			
Market discipline in accordance with Basel 2	Between Groups	0.927	3	0.309	1.364	0.256
	Within Groups	31.946	141	0.227		
	Total	32.874	144			
Implementation Basel 3	Between Groups	0.266	3	0.089	0.318	0.812
	Within Groups	39.307	141	0.279		
	Total	39.573	144			
Avarage	Between Groups	0.601	3	0.200	1.426	0.238
	Within Groups	19.809	141	0.140		
	Total	20.410	144			

It is noted that the value of P for the total score (1.426) and the level of significance (0.238) is greater than the level of significance ($\alpha \geq 0.05$), meaning that there are no statistically significant differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Job title variable, As well as for the fields. Thus the second hypothesis was accepted.

results of the third hypothesis:"There are no statistically significant differences at the level of significance (0.05 ≥ α) in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Educational qualifications variable"

The third hypothesis was examined. The arithmetic averages were calculated for the response of the study sample individuals on The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Educational qualifications variable.

table (4.11): means and standard deviation for The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Educational qualifications variable

Feilds	**Educational qualifications**	**N**	**Mean**	**SD**
The Risk management principles in Islamic banks	Diploma and below	13	4.5769	0.12010
	Bachelor's degree	89	4.4747	0.34808
	Postgraduate studies	43	4.4302	0.53612
Risk management tasks in Islamic banks	Diploma and below	13	4.5641	0.12391
	Bachelor's degree	89	4.4869	0.33564
	Postgraduate studies	43	4.4315	0.41730
The Minimum capital and risk measurement methods in accordance with Basel II	Diploma and below	13	4.5556	0.15045
	Bachelor's degree	89	4.3995	0.45156
	Postgraduate studies	43	4.3514	0.52840
The Supervisory review according to Basel 2	Diploma and below	13	4.6410	0.09245
	Bachelor's degree	89	4.5056	0.42968
	Postgraduate studies	43	4.5116	0.46774
Market discipline in accordance with Basel 2	Diploma and below	13	4.6923	0.09245
	Bachelor's degree	89	4.4719	0.42584
	Postgraduate studies	43	4.4419	0.62030
Implementation Basel 3	Diploma and below	13	4.5385	0.32026
	Bachelor's degree	89	4.3933	0.52884
	Postgraduate studies	43	4.3605	0.56511
Avarage	Diploma and below	13	4.5791	0.05876
	Bachelor's degree	89	4.4522	0.36097

	Postgraduate studies	43	4.4109	0.45302

It is noted from Table No. (4.11) that there are apparent differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Educational qualifications variable, and to know the significance of the differences, one way ANOVA was used as shown in Table No. (4.12):

table (4.12): one way ANOVA test for The Extent of Basel Accord implementation on Islamic Banks in PalestineDepending on the Educational qualifications variable

Feilds		**Mean Square**	**df**	**Sum of Squares**	**Value of "F"**	**Sig**
The Risk management principles in Islamic banks	Between Groups	0.219	2	0.109	0.677	0.510
	Within Groups	22.907	142	0.161		
	Total	23.125	144			
Risk management tasks in Islamic banks	Between Groups	0.196	2	0.098	0.800	0.451
	Within Groups	17.412	142	0.123		
	Total	17.608	144			
The Minimum capital and risk measurement methods in accordance with Basel II	Between Groups	0.416	2	0.208	0.986	0.375
	Within Groups	29.942	142	0.211		
	Total	30.358	144			
The Supervisory review according to Basel 2	Between Groups	0.212	2	0.106	0.589	0.556
	Within Groups	25.538	142	0.180		
	Total	25.750	144			
Market discipline in accordance with Basel 2	Between Groups	0.653	2	0.327	1.439	0.240
	Within Groups	32.220	142	0.227		
	Total	32.874	144			
Implementation Basel 3	Between Groups	0.319	2	0.159	0.577	0.563
	Within Groups	39.255	142	0.276		
	Total	39.573	144			
Avarage	Between Groups	0.283	2	0.141	0.997	0.372
	Within Groups	20.127	142	0.142		
	Total	20.410	144			

It is noted that the value of P for the total score (0.997) and the level of significance (0.372) is greater than the level of significance ($\alpha \geq 0.05$), meaning that there are no statistically significant differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Educational qualifications variable, as well as to the fields. Thus the third hypothesis was accepted.

results of the fourth hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Years of experience variable"

The fourth hypothesis was examined. The arithmetic averages were calculated for the response of the study sample individuals on The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Years of experience variable.

table (4.13): means and standard deviation for level of The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Years of experience variable

Feilds	Years of experience	N	Mean	SD
The Risk management principles in Islamic banks	Less than 5 years	67	4.4384	0.49542
	5 years to less than 10 years	44	4.5568	0.20075
	More than 10 years	34	4.4228	0.37816
Risk management tasks in Islamic banks	Less than 5 years	67	4.4693	0.41924
	5 years to less than 10 years	44	4.4924	0.29191
	More than 10 years	34	4.4739	0.26564
The Minimum capital and risk measurement methods in accordance with Basel II	Less than 5 years	67	4.4196	0.50021
	5 years to less than 10 years	44	4.4495	0.36100
	More than 10 years	34	4.2941	0.48384
The Supervisory review according to Basel 2	Less than 5 years	67	4.5075	0.51036
	5 years to less than 10 years	44	4.5530	0.32899
	More than 10 years	34	4.5000	0.34082
Market discipline in accordance with Basel	Less than 5 years	67	4.4527	0.57939
	5 years to less than 10 years	44	4.5000	0.40347

2	More than 10 years	34	4.5196	0.33020
Implementation Basel 3	Less than 5 years	67	4.3396	0.62870
	5 years to less than 10 years	44	4.4773	0.37671
	More than 10 years	34	4.4044	0.45650
Avarage	Less than 5 years	67	4.4374	0.46645
	5 years to less than 10 years	44	4.5000	0.27217
	More than 10 years	34	4.4158	0.28627

It is noted from Table No. (4.13) that there are apparent differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Years of experience variable, and to know the significance of the differences, one way ANOVA was used as shown in Table No. (4.14):

table (4.14): one way ANOVA test for The Extent of Basel Accord implementation on Islamic Banks in PalestineDepending on the Years of experience variable

Feilds		**Mean Square**	**df**	**Sum of Squares**	**Value of "F"**	**Sig**
The Risk management principles in Islamic banks	Between Groups	0.474	2	0.237	1.486	0.230
	Within Groups	22.651	142	0.160		
	Total	23.125	144			
Risk management tasks in Islamic banks	Between Groups	0.015	2	0.007	0.059	0.942
	Within Groups	17.593	142	0.124		
	Total	17.608	144			
The Minimum capital and risk measurement methods in accordance with Basel II	Between Groups	0.515	2	0.257	1.224	0.297
	Within Groups	29.843	142	0.210		
	Total	30.358	144			
The Supervisory review according to Basel 2	Between Groups	0.072	2	0.036	0.199	0.819
	Within Groups	25.678	142	0.181		
	Total	25.750	144			
Market discipline in accordance with	Between Groups	0.120	2	.060	0.259	0.772
	Within Groups	32.754	142	0.231		

Basel 2	Total	32.874	144			
Implementation Basel 3	Between Groups	0.506	2	0.253	0.920	0.401
	Within Groups	39.067	142	0.275		
	Total	39.573	144			
Avarage	Between Groups	0.160	2	0.080	0.561	0.572
	Within Groups	20.250	142	0.143		
	Total	20.410	144			

It is noted that the value of P for the total score (0.561) and the level of significance (0.572) is greater than the level of significance ($\alpha \geq 0.05$), meaning that there are no statistically significant differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the Years of experience variable, As well as for the fields. Thus the fourth hypothesis was accepted.

results of the fifth hypothesis:"There are no statistically significant differences at the level of significance ($0.05 \geq \alpha$) in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the age variable"

The fifth hypothesis was examined. The arithmetic averages were calculated for the response of the study sample individuals on The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the age variable.

table (4.15): means and standard deviation for level of The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the age variable

Feilds	**Age**	**N**	**Mean**	**SD**
The Risk management principles in Islamic banks	Less than 30 years	93	4.4691	0.43678
	30-40 years	31	4.5847	0.18649
	More than 40 years	21	4.3095	0.42319
Risk management tasks in Islamic banks	Less than 30 years	93	4.4827	0.37447
	30-40 years	31	4.5341	0.18239
	More than 40 years	21	4.3704	0.41026
The Minimum capital and risk measurement methods in accordance	Less than 30 years	93	4.4361	0.46256
	30-40 years	31	4.4516	0.32067

with Basel II	More than 40 years	21	4.1587	0.55508
The Supervisory review according to Basel 2	Less than 30 years	93	4.5161	0.46239
	30-40 years	31	4.6237	0.18742
	More than 40 years	21	4.3810	0.46291
Market discipline in accordance with Basel 2	Less than 30 years	93	4.4588	0.53368
	30-40 years	31	4.6022	0.24973
	More than 40 years	21	4.4127	0.45832
Implementation Basel 3	Less than 30 years	93	4.3763	0.57651
	30-40 years	31	4.5242	0.34973
	More than 40 years	21	4.2976	0.47840
Avarage	Less than 30 years	93	4.4570	0.41545
	30-40 years	31	4.5367	0.19516
	More than 40 years	21	4.3003	0.36606

It is noted from Table No. (4.15) that there are apparent differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the age variable, and to know the significance of the differences, one way ANOVA was used as shown in Table No. (4.16):

table (4.16): one way ANOVA test for The Extent of Basel Accord implementation on Islamic Banks in PalestineDepending on the agevariable

Feilds		**Mean Square**	**df**	**Sum of Squares**	**Value of "F"**	**Sig**
The Risk management principles in Islamic banks	Between Groups	0.948	2	0.474	3.037	0.051
	Within Groups	22.177	142	0.156		
	Total	23.125	144			
Risk management tasks in Islamic banks	Between Groups	0.343	2	0.171	1.409	0.248
	Within Groups	17.265	142	0.122		
	Total	17.608	144			
The Minimum capital and risk measurement methods in accordance with Basel II	Between Groups	1.426	2	0.713	3.499	0.033
	Within Groups	28.932	142	0.204		
	Total	30.358	144			

The Supervisory review according to Basel 2	Between Groups	0.740	2	0.370	2.102	0.126
	Within Groups	25.010	142	0.176		
	Total	25.750	144			
Market discipline in accordance with Basel 2	Between Groups	0.598	2	0.299	1.316	0.271
	Within Groups	32.275	142	0.227		
	Total	32.874	144			
Implementation Basel 3	Between Groups	0.749	2	0.374	1.369	0.258
	Within Groups	38.825	142	0.273		
	Total	39.573	144			
Avarage	Between Groups	0.708	2	0.354	2.553	0.081
	Within Groups	19.701	142	0.139		
	Total	20.410	144			

It is noted that the value of P for the total score (2.553) and the level of significance (0.081) is greater than the level of significance ($\alpha \geq 0.05$), meaning that there are no statistically significant differences in The Extent of Basel Accord implementation on Islamic Banks in Palestine due to the age variable, as well as to the fields except the field of the Minimum capital and risk measurement methods in accordance with Basel II, Where the differences were between (Less than 30 years) and (More than 40 years) in favor to (Less than 30 years), and between (30-40 years) and (More than 40 years) in favor to (30-40 years). Thus the fifth hypothesis was accepted.

chapterFive:

Conclusionsand Recommendations

5.1 Conclusions.

The results of analysis of the research's tool (questionnaire) demonstrated high acceptance among all levels and variables. The reason behind this high acceptance is due to the importance of Basel accord to the banking and the financial system. Basel should never be regarded as obligatory, but as a favorable framework that provides all sort of banks with a reserve plan in case of future crisis. It also allows them to classify the credibility among each other's, and amongst their clients.

Moreover, Basel was the result of high and rough crisis, failures, and shocks from the past, that could take place at any given moment whether in the near or the far future, and thus being prepared for such an issue, no matter the amount a bank places in supervisory control is never a bad thing. Basel became an introduction to bank, in all of its financial activities and trades, thus imagine a bank baring all of its risks without any backup? The situation will be tough, where in banking sectors, the most favorable type of transactions is those backed up by a collateral to ensure the deals' stability and the counterparty's ability to fulfill its obligations. Basel is similar, it's the bank collateral against default or bankruptcy.

This is the main reason behind such acceptance. In Islamic banks especially, a sort of bank that depends on PLS and distribution of dividend, if any taken risk happened to cause a loss to the bank, while not complying with Basel, the shareholders will not be willing to bare the loss this time. A loss is fine, when the risk of generating the profit is taken, but it is unforgivable when the fault is on the bank that decided not to comply with the regulatory framework. Losing the shareholders due to commercial risk, means losing around 60% of the Islamic banks' pool of fund. Regardless of the percentage required by Basel or by the PMA, Islamic banks will always be willing to comply in order to gain the trust of their clients, and to prove the height of their standards.

5.2 Results as Noted:

1. Islamic Banks are complying with the standards imposed by Basel II
2. Islamic Bank of Palestine is complying with the CAR imposed by both Basel II and the PMA.
3. Due to the different types of risk, and the complication of CAR calculating, Islamic bank of Palestine has been increasing their Reserve above the required limit.
4. The importance of Basel II existence in Islamic banks in general, and in the Islamic Bank of Palestine in particular comes from the need to satisfy and protect shareholders and customers from expected losses, and unexpected losses.
5. In Islamic banks especially, a sort of bank that depends on PLS and distribution of dividend, if any taken risk happened to cause a loss to the bank, while not complying with Basel, the shareholders will not be willing to bare the loss this time.
6. All employees demonstrated the importance of Basel II regulations on both personal and administrative levels.
7. PMA regulation on CAR for the Islamic bank of Palestine are not merely enough and need to be adjusted to include the different Islamic trades of the bank.

5.3 Recommendations:

8. All financial institutions should be willing to comply with Basel for the reasons mentioned above.
9. The Palestinian monetary authority shall be regarding the creation of a new capital adequacy ratio, that is developed for Islamic banks due to their different financial nature.
10. Directing attention to further studies dealing with: a. Assessing capital adequacy within the model proposed in Islamic banks; b. Quantification of the effects of the various banking risks facing Islamic banks in Palestine.
11. The importance of implying a clear accounting policy between Capital adequacy ratio, risk imposed on it, and their effect on its percentage.
12. The need for the Islamic oversight body and external references to follow up on the adequacy of capital to achieve solvency in the Islamic Bank so that the accounting

and auditing profession becomes an effective tool for the service of its users and society.

13. Strengthening and qualifying human resources to oversee various risks and develop their capabilities in this field.
14. Unite efforts among Islamic banks to adhere to the formulas of the Islamic Financial Services Council to reach a unified formula for their application.
15. Develop risk measurement tools and systems in accordance with internal valuation methods, to take advantage of the advantages of this method by Islamic banks.
16. Islamic banks should effectively adhere to Islamic rules to withstand traditional banks, because adherence to Islamic law is an important competitive advantage for them in the face of competition from traditional banks.

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Appendix

Appendix (1) :Questioner

Al-Quds University

Graduate Studies

Faculty of Business and economics

Dear participant in this study,

After Greetings,

The researcher is conducting a study entitled "The reality of the application of the Basel Agreement in Islamic banks: the case of the Palestine Islamic Bank" to obtain a master's degree in business administration from Al-Quds University.
We ask that you consider objectivity and credibility in completing the questionnaire, bearing in mind that confidentiality will be taken into account in the data that you will give and that this data will be used for scientific research purposes only.**Many Thanks**

Researcher :RaneenAyyad

Supervised :Dr. OrobahBarghouthi

This section: It consists of a set of questions that address the characteristics of the respondent:

1. Gender: * Male * Female

2. Job Title:.....

3. Educational qualifications:

- **Diploma and below**
- **Bachelor's degree**
- **postgraduate studies**

4. Years of Experience:

- **Less than 5 years**
- **form 5-less than 10 years**
- **more than 10 years**

5. Age:

- **Less than 30 years**
- **form 30- 40 years**
- **more than 40 years**

Section 1: Risk management principles in Islamic banks

please read each statement carefully and indicate the degree of your agreement or disagreement

	Items	Strongly agree	Agree	Neutral	Disagree	Strongly disagree
1	Risk management aims to stabilize profits					
2	There is an independent committee called "Risk Management Committee" that is concerned with preparing the general policy					
3	Appointing an official with experience in the banking field for each type of major risk					
4	Establish a specific system for measuring and monitoring risks					
5	Valuating the assets of Islamic banks, especially investment, is a fundamental principle for measuring risk and profitability					
6	Using modern information systems to manage risks					
7	There is an independent unit in the bank that audits all Islamic banking business, including risk management					
8	The Board of Directors is responsible for managing risks					

Section 2: Risk management tasks in Islamic banks

please read each statement carefully and indicate the degree of your agreement or disagreement

	Items	Strongly agree	Agree	Neutral	Disagree	Strongly disagree
1	An internal risk management policy					
2	The presence of cultural awareness within Islamic banks regarding the management of risk					
3	Preparing risk reports and submitting them to the board of directors and stakeholders					
4	Choosing the most appropriate way to manage the risks facing Islamic banks, according to the degree of safety and the necessary cost					

5	A method of risk management is risk control					
6	A method of risk management is risk financing (by hedging or transferring)					
7	There is effective oversight by the Board and senior management of risk management					
8	There is a correlation between the risk management policy and the risks to which the bank is exposed					
9	Separating jobs from the main pillars of risk management					

Section 3: Minimum capital and risk measurement methods in accordance with Basel II

please read each statement carefully and indicate the degree of your agreement or disagreement

	Items	Strongly agree	Agree	Neutral	Disagree	Strongly disagree
1	Minimum capital adequacy ratio of 8%					
2	To measure credit risk, the standard method is used					
3	To measure credit risk, the main internal rating method is used					
4	To measure credit risk, we rely on the advanced internal rating method					
5	To measure market risks, we rely on the standard method					
6	To measure market risks, the method is used in internal models (statistical models)					
7	To measure operating risks, a typical method is used					
8	To measure operating risks, the main indicator method is used					
9	To measure operating risks, an advanced measurement method is used					

Section 4: Supervisory review according to BaselII

please read each statement carefully and indicate the degree of your agreement or disagreement

	Items	Strongly agree	Agree	Neutral	Disagree	Strongly disagree
1	The supervisory authority reviews the methods of assessing the capital adequacy used by the Islamic banks that are subject to it					
2	Ensuring the commitment of Islamic banks to maintain the rate of 8%					
3	The regulatory authority shall enter to prevent any decrease or decrease in the required capital					

Section 5: Market discipline in accordance with BaselII

please read each statement carefully and indicate the degree of your agreement or disagreement

	Items	Strongly agree	Agree	Neutral	Disagree	Strongly disagree
1	Islamic banks disclose the structure and size of their private funds					
2	Disclosure of risk assessments					
3	Disclosure of capital adequacy according to the size of the potential risks					

Section 6: Implementation Basel III

please read each statement carefully and indicate the degree of your agreement or disagreement

	Items	Strongly agree	Agree	Neutral	Disagree	Strongly disagree
1	Islamic banks can raise the capital adequacy ratio to 10.5%					
2	Islamic banks will introduce leverage of 3%					
3	Islamic banks must maintain a liquidity ratio to meet short-term benefits					
4	Islamic banks should maintain a liquidity ratio to cope with medium and long-term benefits					