

**RISK MANAGEMENT DISCLOSURE IN ISLAMIC FINANCIAL INSTITUTIONS IN MALAYSIA:  
PRE AND POST FINANCIAL CRISIS**

Prepared by:  
Rosnadzirah Ismail  
Prof Dr Rashidah Abdul Rahman  
Dr Normah Ahmad  
Siti Hilda Mokhtar

November 2012

**Contents**

1. Letter of Report Submission..... iii

2. Letter of Offer (Research Grant) ..... iv

3. Acknowledgements..... vii

4. Enhanced Research Title and Objectives.....viii

5. Report..... ix

    5.1 Proposed Executive Summary ..... ix

    5.2 Enhanced Executive Summary ..... x

    5.3 Introduction..... xi

    5.4 Brief Literature Review.....xiii

    5.5 Methodology ..... xvii

    5.6 Results and Discussion..... xx

    5.7 Conclusion and Recommendation .....xxvi

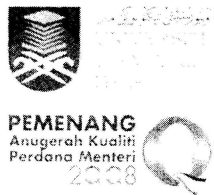
    5.8 References/Bibliography ..... xxvii

6. Research Outcomes .....xxx

7. Appendix..... xxxi

# 2. Letter of Offer (Research Grant)

Surat Kami : 100-RMI/ARI 16/6/2 (58/2010)  
Tarikh : 15 Ogos 2010



Puan Rosnadzirah Ismail  
Fakulti Perakaunan  
Universiti Teknologi MARA  
40450 SHAH ALAM

Y. Bhg. Prof./Prof. Madya/Dr./Tuan/Puan

## KELULUSAN PROJEK DI BAWAH GERAN PENYELIDIKAN ARI HICoE

Tajuk Projek : Risk Management Disclosure in Islamic Financial Institutions in Malaysia: Pre and Post Financial Crisis

Jumlah Peruntukan : RM 30,000.00

Tempoh : 1 Julai 2010 – 31 Januari 2012 (18 bulan)

Ketua Projek : Puan Rosnadzirah Ismail

Dengan hormatnya perkara di atas adalah dirujuk.

2. Sukacita dimaklumkan pihak ARI telah meluluskan cadangan penyelidikan Prof./Prof. Madya/Dr./Tuan/Puan dan membiayai projek penyelidikan di bawah dana pengurusan ARI/RMI.

3. Sehubungan dengan itu, pihak Prof./Prof. Madya/Dr./Tuan/Puan adalah diminta untuk melengkapkan kertas cadangan penyelidikan dalam format borang Dana Kecemerlangan yang boleh didapati di dalam laman web RMI. Sila pilih **Kategori A** (Institutional Research). Ini adalah perlu bagi tujuan mengemaskini sebelum penyelidik dibenarkan untuk menggunakan peruntukan penyelidikan. Sila lihat lampiran bagi tatacara tambahan untuk pengurusan projek.

4. Bagi pihak Universiti kami mengucapkan tahniah kepada Prof./Prof. Madya/Dr./Tuan/Puan kerana kejayaan ini dan seterusnya diharapkan berjaya menyiapkan projek ini dengan cemerlang.

Sekian, harap maklum.

**“SELAMAT MENJALANKAN PENYELIDIKAN DENGAN JAYANYA”**

Yang benar

  
**MUSTAFAR KAMAL HAMZAH**  
Ketua Penyelidikan (Sains & Teknologi)

Penyelidikan & Inovasi  
Kementerian Pendidikan Malaysia  
Kementerian Pendidikan Malaysia  
Kementerian Pendidikan Malaysia

Penyelidikan & Inovasi  
Kementerian Pendidikan Malaysia  
Kementerian Pendidikan Malaysia  
Kementerian Pendidikan Malaysia

Penyelidikan & Inovasi  
Kementerian Pendidikan Malaysia  
Kementerian Pendidikan Malaysia  
Kementerian Pendidikan Malaysia



Research Management Institute (RMI) Universiti Teknologi MARA, 40450 Shah Alam, Selangor, Malaysia  
<http://www.rmi.uitm.edu.my>



## **5.2 Enhanced Executive Summary**

The purpose of this study is to examine the risk management disclosure by all seventeen Islamic Financial Institutions (IFIs) in Malaysia from 2006 to 2009, covering the period before, during and after the global financial crisis. This study also aims to examine the relationship between corporate governance mechanisms on the level of risk management disclosure. A disclosure checklist consists of mandatory and voluntary items were developed to measure the level of risk disclosure. The descriptive result shows the risk management disclosure among the Islamic Financial Institutions was satisfactory. Analysis for the four-year period revealed that the risk disclosure has significantly improved before and after the financial crisis indicating that Islamic financial institutions have taken the necessary measures to improve their disclosure. Independent non-executive (BINE) and non-independent non-executive directors (BNINE) were found to have effect on the risk management disclosure indicating that external directors have significant influence on management.

**Keywords:** Risk management, Islamic Financial Institutions (IFIs)

### 5.3 Introduction

The issues on corporate disclosure are amongst the top priority of concern in today's business world. The disclosures including risk information were concerned with the risk information provided to shareholders and other stakeholders. In light of advent corporate collapses, there has been a strong demand for information on companies' exposure to risks. This was proved in the recent US sub-prime mortgage crisis which was triggered by liquidity problem faced by financial institutions as a result of overvaluation of assets. Foong (2009) suggests that poor corporate governance and lack of transparency, especially on risk management disclosure among major financial conglomerates, have intensified the financial meltdown in the US subprime mortgage crisis.

Hence, good risk management practices especially among financial institutions including Islamic financial institutions are important as they are more exposed to various types of risks due to the nature of their operations. Islamic banks and financial institutions have the similar risks as conventional banks but they are also confronted with "new and unique risks as a result of their unique asset and liability structures" (Kahf, 2006). This new type of risk is an immediate outcome of their compliance with the Shariah requirement because Islamic banking is based on interest free banking.

Several studies have focused on risk management disclosure in financial institutions (Sundrarajan, 2008; Selvarajan, 2008) and the study of Mohd Ariffin, Archer and Abdel Kareem (2008) on the perception of risk disclosure in Islamic banks. There are also several studies that theoretically focus on the disclosure among conventional banks (Hossain, 2008; Harahap, 2003; Helbok & Wegner, 2003). The only study on risk management disclosure in Islamic financial institutions was done by Sundrarajan (2008); however, it only addressed the general risk disclosure among Islamic financial institutions. There is also a study on the Malaysian scenario by Selvarajan (2008); but it only focused on issues, prospects and challenges faced by Islamic banking. Meanwhile, Mohd Ariffin et al. (2008)'s research is mainly focused on bank officers' perception towards risk disclosure.

This study attempts to look at risk management disclosure, specifically, among the Islamic financial institutions. The study will further compare the extent of disclosure by these financial institutions for four years covering the period before, after and during the global financial crisis. In addition, this study also examines the corporate governance mechanism on the amount of risk management disclosure in Islamic financial institutions. As suggested by previous literature, the corporate governance mechanism tested in this study focuses on board of directors and audit committee.