



**AMENDMENT**  
**NOTICE TO ISLAMIC BANKS**  
**EFFECTIVE DATE 27 NOVEMBER 2019**

**NOTICE NO. BU/N-10/2018/60 – AMENDMENT NO. 1**  
**SUPERVISORY REVIEW AND EVALUATION PROCESS (SREP)**

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**1. INTRODUCTION**

- 1.1. This Notice sets out the expectations of Autoriti Monetari Brunei Darussalam (“the Authority”) in respect of the Internal Capital Adequacy Assessment Process (ICAAP) of an Islamic bank under the Supervisory Review and Evaluation Process (SREP) (“Pillar 2 Capital Adequacy Framework”).
- 1.2. The SREP is an important and integral part of the capital adequacy framework. Its main objectives are to:
  - 1.2.1. facilitate supervisory monitoring of the capital adequacy of Islamic banks to support the risks in their business activities;
  - 1.2.2. encourage Islamic banks to enhance their risk management techniques for monitoring and controlling such risks; and
  - 1.2.3. provide the incentive for Islamic banks to adopt more active capital planning and management practices.
- 1.3. In conducting the SREP, the Authority is guided by the following key principles which should help achieve the objectives outlined above:
  - 1.3.1. Islamic banks shall have an internal process for assessing their overall capital adequacy in relation to their risk profile and a strategy for maintaining the required level of capital (“Principle 1”);
  - 1.3.2. The Authority has the responsibility of reviewing Islamic banks’ internal capital adequacy assessments and determining whether the resultant capital position is adequate (“Principle 2”);
  - 1.3.3. The Authority expects Islamic banks to operate above the minimum regulatory capital ratios<sup>1</sup> and has the power to require Islamic banks to do so (“Principle 3”); and

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<sup>1</sup> As set out in the Notice on Maintenance of Capital Adequacy Ratio as may be revised from time to time.



1.3.4. The Authority seeks to intervene at an early stage to prevent Islamic banks' capital from falling below prudent levels ("Principle 4").

The manner in which the Authority applies the four key principles is elaborated in the Guidance on SREP **[ANNEX 1]**.

- 1.4. This notice is issued pursuant to section 66 of the Islamic Banking Order, 2008 and applies to all Islamic banks under section 2 of the same.
- 1.5. This Notice shall take immediate effect.

## **2. INTERNAL CAPITAL ADEQUACY ASSESSMENT PROCESS (ICAAP)**

- 2.1. An Islamic bank, on a forward-looking basis, shall have adequate capital to support its operations and its risk profile. An Islamic bank shall maintain an appropriate level of capital above minimum Pillar 1 requirements<sup>2</sup> so that all risks of the Islamic bank are adequately covered. This will encourage Islamic banks to develop and use better risk management techniques for monitoring and controlling such risks especially those specific risks not directly or fully covered under Pillar 1. This process is known as the Internal Capital Adequacy Assessment Process (ICAAP).
- 2.2. For Islamic banks incorporated in Brunei Darussalam, its board of directors and senior management are ultimately responsible in ensuring that the Islamic bank maintains an appropriate level and quality of capital commensurate with its risk profile.
  - 2.2.1. For an Islamic bank registered in Brunei Darussalam, its group/regional or its equivalent oversight function for the operations in Brunei Darussalam and its senior management in Brunei Darussalam are ultimately responsible in ensuring that the Islamic bank maintains an appropriate level and quality of capital commensurate with its risk profile.
- 2.3. An Islamic bank shall prepare its ICAAP in accordance with **ANNEX 1** and shall be:
  - 2.3.1. comprehensive in terms of the identification and measurement of the risks associated with an Islamic bank's business and the assessment of how much capital is needed to support these risks;
  - 2.3.2. risk-based and forward-looking, with emphasis on the importance of capital planning, management and other qualitative aspects of risk management and controls, and takes into account the Islamic bank's strategic plans and how these relate to macroeconomic factors;

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<sup>2</sup> See footnote no. 1



- 2.3.3. integrated into the management process and decision-making culture of the Islamic bank;
- 2.3.4. capable of producing a reasonable outcome on the overall level of capital required and the assessment supporting such outcome.
- 2.4. The basic elements of a sound ICAAP shall include, but not limited to the following:
  - 2.4.1. policies and procedures to identify, measure, monitor, control, and report the risks inherent in an Islamic bank's activities;
  - 2.4.2. a process to relate the Islamic bank's internal capital to its risks;
  - 2.4.3. a process to state the Islamic bank's capital adequacy goals in relation to risks, taking into account its strategic focus and business plan; and
  - 2.4.4. Processes of internal controls, independent reviews and audits to ensure the integrity of the overall management process.
- 2.5. The documentation of the ICAAP shall be subject to periodic review and approval at least annually by the board (for Islamic banks incorporated in Brunei Darussalam) or by the group/regional or its equivalent oversight function for the operations in Brunei Darussalam (for Islamic banks registered in Brunei Darussalam).
- 2.6. The ICAAP and related policies, management guidelines and procedures shall be communicated and implemented firm-wide and supported by sufficient authority and resources.
- 2.7. Islamic banks shall submit its annual ICAAP documents to the Authority, no later than 30 June of each year.

[Amendment No. 1 dated 27 November 2019]

- 2.8. An Islamic bank shall notify and engage the Authority in discussions if it plans to make material changes to its ICAAP documents after it has been submitted to the Authority.

[Amendment No. 1 dated 27 November 2019]

### **3. SUPERVISORY REVIEW AND EVALUATION PROCESS (SREP)**

- 3.1. The Authority has the responsibility of reviewing Islamic banks' internal capital adequacy assessments and evaluating whether the resultant capital position is adequate relative to its risk profile. This SREP generally involves a review of the documentation of the Islamic bank's ICAAP, discussions between the Authority and the key management personnel of the Islamic bank, on-site examinations and other



methods the Authority may identify as appropriate for evaluating the robustness of the Islamic bank's ICAAP.

[Amendment No. 1 dated 27 November 2019]

3.2. In reviewing and evaluating an Islamic bank's ICAAP, the Authority will have regard to the following key factors, amongst others:

3.2.1. the soundness of the overall ICAAP given the nature and scale of the Islamic bank's business activities;

3.2.2. the degree of management involvement in the process, for example, whether the target and actual capital levels are properly monitored and reviewed by the board and senior management;

3.2.3. the extent to which the internal capital assessment is used routinely within the Islamic bank for decision-making purposes;

3.2.4. the extent to which the Islamic bank has provided for unexpected events in setting capital levels;

3.2.5. the reasonableness of the outcome of the ICAAP in terms of whether:

a) the amount of capital required as demonstrated by the ICAAP is sufficient to support the risks faced by the Islamic bank;

b) the levels and composition of capital chosen by the Islamic bank are comprehensive, relevant to the current operating environment, appropriate for the nature and scale of the Islamic bank's business activities and can withstand stressed scenarios in all the relevant stress tests (e.g. the supervisor-driven stress tests and other relevant stress tests conducted by the Islamic bank, as applicable); and

3.2.6. the appropriateness and comprehensiveness of the potential capital actions identified in the ICAAP to address any capital shortfall.

3.3. Islamic banks are expected to explain and demonstrate to the satisfaction of the Authority:

3.3.1. how their ICAAP meets supervisory requirements;

3.3.2. how their material risks are defined, categorised and measured (if their own terminology is adopted); and



- 3.3.3. how the internal capital targets are determined and how these targets are consistent with their overall risk profile and the current operating environment as well as current and planned business needs.
- 3.4. Islamic banks are also expected to explain the similarities and differences between the level of capital calculated under their ICAAP and their regulatory capital requirements<sup>3</sup>.
- 3.5. If the Authority is not satisfied with the outcomes from its review, the Authority may, among other things:
- 3.5.1. require the Islamic bank to take action to improve its risk management processes or lower the risks which it assumes;
  - 3.5.2. require the Islamic bank to maintain additional capital;
  - 3.5.3. restrict the payment of dividends by the Islamic bank;
  - 3.5.4. require the Islamic bank to implement a satisfactory capital adequacy restoration plan; and/or
  - 3.5.5. apply other supervisory measures to address the heightened risk or risk management deficiencies of the Islamic bank (e.g. intensifying supervisory monitoring of the Islamic bank or requiring the Islamic bank to strengthen risk management, apply internal limits, strengthen the level of provisions and reserves, or improve internal controls).
- 3.6. [Deleted]  
[Amendment No. 1 dated 27 November 2019]
- 3.7. An Islamic bank shall furnish to the Authority such other information relating to the capital adequacy ratios and capitalisation level of the Islamic bank, as may be requested by the Authority.

**MANAGING DIRECTOR**

**AUTORITI MONETARI BRUNEI DARUSSALAM**

Date: 30 Rabiulawal 1441H / 27 November 2019

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<sup>3</sup> See footnote no. 1