ST. MARY'S UNIVERSITY SCHOOL OF GRADUATE STUDIES

CORPORATE GOVERNANCE: THE ROLE OF BOARD OF DIRECTORS IN BANK RISK MANAGEMENT

(THE CASE OF LION INTERNATIONAL BANK S.C)

BY: MULUGETA TEKLU HAGOS

DECEMBER, 2015

ADDIS ABABA

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APPROVED BY BOARD OF EXAMINORS:

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DECLARATION

I Mulugeta Teklu Hagos, declare that this thesis titled ‘Corporate Governance: The Role of Board of Directors in Risk Management - The Case of Lion International Bank S.C.’ is done entirely by me under supervision of Dr. Wubshet Bekalu. The thesis has not been presented either wholly or partly, for any degree elsewhere before.

Mulugeta Teklu

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ACRONYMS AND DEFINITIONS OF KEY WORDS

ACRONYMS

ALCO - Asset-Liability management Committee

BCBS - Basel Committee in Banking Supervision

BIS – Bank of International Settlement

CRO - Chief Risk Officer,

CEO - Chief Executive Officer

CBE - Commercial Bank of Ethiopia

CBB - Construction and Business Bank

CGF - Corporate Governance Framework

DBE - Development Bank of Ethiopia

EBA - Ethiopian Bankers Association

FSB - Financial Stability Board

IRGC - International Risk Governance Council

IAD - Internal Audit Department

IBD - International Banking Department

LIB - Lion International Bank S.C

LLC - Limited Liability Company-

NBE - National Bank of Ethiopia

OECD - Organization for Economic Cooperation and Development

RAS - Risk Appetite Statement

RAF - Risk Appetite Framework

RCMD - Risk and Compliance Management Department

DEFINITIONS OF KEY WORDS

Corporate Governance – is the manner in which the business of the bank is governed, including setting corporate objectives and bank's risk profile, aligning corporate activities and behaviors with expectation that management will operate in a wise and sound manner, running a day-to-day operation within an established risk profile; while protecting the interest of depositors, shareholders, and other stakeholders. (Hennie, V. and Sonja, B 2003)

Risk Management - is a process of identification, assessment, management and communication of risks in a broad context. The terms assessment and measurement involves risk measurement, risk control and mentoring. Risk management includes the totality of policies, procedures, processes and mechanisms; and is concerned with how relevant risk information is collected, analyzed and communicated, and how management decisions are taken. (http://www.irgc.org, IRGC, 2005)

Risk Governance Framework - collectively refers to defining explicit structure of the board and its committees involving in risk management, the role and responsibilities of the board, the firm-wide chief risk officer, the risk management function, and the independent assessment of the risk management function. (FSB, Thematic Review on Risk Governance, peer review report, 2013)

Risk Appetite Frameworks (RAFs) - refer to risk management functions that are actionable and measurable by both the financial institutions and the supervisory organs (FSB, 2013). Risk appetite framework potentially serves as a key guiding approach for a company, including polices, processes, controls, and systems through which risk appetite is established, communicated, and monitored.

Risk Appetite Statement (RAS) refers to the articulation in written form of the aggregate level and types of risk that a financial institution is willing to accept, or to avoid, in order achieving its business objectives.

Risk Appetite - refers to the aggregate level and types of risk a financial institution is willing to assume within its risk capacity to achieve its strategic plan.

Risk Capacity - is the maximum level of risk that financial institution can assume given its current level of resources before breaching constraints determined by regulatory capital and liquidity needs, the operational environment and obligation.

Risk Limit - is a quantitative measure based on forward looking assumption that allocate the financial institution's aggregate risk appetite statement to specific risk category.

The CAMEL rating - examines the **C**apital adequacy, **A**sset quality, **M**anagement (leadership efficiency), **E**arnings, and **L**iquidity position of the Bank and rates the overall condition of the Bank leveling composite rating from '1' to '5'.

The Basel Committee on Banking Supervision - is an institution created by the central bank Governors of the Group of 10 nations(G10) (Belgium, Canada, France, Italy, Japan, the Netherlands, the United Kingdom, the United States, Germany and Sweden). The Basel Committee formulates broad supervisory standards and guidelines and recommends statements of best practice in banking supervision in the expectation those member authorities and other nations' authorities will take steps to implement them through their own national systems. The purpose of the committee is to encourage convergence toward common approaches and standards. (Risk management in banking: (Alina, D. and Ivona O. http://www.academypublish.org/papers/pdf/174.pdf)

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Abstract

Corporate governance is a system by which business corporations are directed and controlled. It involves a set of relationship between a company's management, its board, its shareholders, and other stakeholders who expect what the corporation ought to be and what structure, composition, and leadership should it have while existing in business (OECD, 1999). Risk management is a process of identification, assessment, management and communication of risks in a broad context. Thus, this study sets out to examine and describe the role of LIB's board of directors in establishing corporate governance to ensure sound risk management in the bank in a way it conforms the international and national principles and standard of risk management. In this regard, as problems are observed in LIB in relation to establishing risk governance and risk appetite frameworks to ensure risk management in the bank that hinder proper implementation of corporate governance and risk management of the bank; thus, the researcher got motivated to examine the corporate governance and risk management of the bank with objective of examining the role of LIB's board in establishing sound risk management practices and identifying the gap between the international and national standard and the LIB's practices. The researcher used descriptive type of research and employed review of documents from the LIB board secretariat office, interview with key informants, chairpersons of the Loan Review and Risk Management Committee, Audit Committee, and the HR and Business Development Committee, the President and the Director Risk and Compliance Management Department. It also employed questionnaire to employees of the bank at various levels of managerial positions and incorporated personal observation. Qualitative data gathered through interview, and questionnaires are thematically synthesized and Quantitative data are statistically analyzed. A statistical tool SPSS has been utilized in analyzing the quantitative data. The research didn't attempt to gauge the performance of operational risks based on the set limits, ratios, and matrix parameters, rather endeavors to examine and describe the role of the board in risk management in light of accepted corporate governance and risk management principles. Hence, the research has identified some gaps related to lack of provision of intensive training, awareness enhancement, and risk communication that have effect on hindering corporate governance and risk management functions of the board.

CHAPTER ONE

3. INTRODUCTION

This chapter attempts to introduce what the research is all about. It establishes the mechanisms to be utilized in carrying out the research. It also presents the application of the findings and the purpose of the research.

3.1. Background

In the aftermath of recent global financial crisis the issue of corporate governance towards focus on strong risk management and financial stability is getting serious attention by policy makers, international organizations, and banks and financial institutions. Alexandra, B (2012). The reason that financial and non-financial firms emphasized on the need for various forms of risk management is that, due to incompetent corporate governance and in adequate risk management, the rapidity with which the economic entities can get into trouble is becoming a point of concern for organizations. David, H. (1997)

Hennie, V. and Sonja, B (2003) defined bank corporate governance as *"the manner in which the business of the bank is governed, including setting corporate objectives and bank's risk profile, aligning corporate activities and behaviors with expectation that management will operate in a wise and sound manner, running a day-to-day operation within an established risk profile; while protecting the interest of depositors, shareholders, and other stakeholders."* The definition highlights corporate governance as an imperative instrument for banks in identifying their strength in risk management.

Banks feature high leverage and their maturity transformation exposes them to further liquidity risks. Alexandera, B (2012). Risk taking, therefore, is an inherent element to banking activities. Profits are rewards for successful risk taking and the reverse is true that poorly managed risks can lead to distress and failures. Thus, in response to the inherent and multifaceted banking risks, banks need to implement effective risk management practices that constitute an integral part of corporate governance that play an active role in maintaining sound financial stability. William J.

McDonough, President of the Federal Reserve Bank of New York, (2002) said, financial stability can be achieved by the interaction of sound leadership at the firm level (corporate governance), strong prudential regulation and supervision, and effective market discipline. Corporate governance includes capable board of directors, experienced management, a coherent strategy and business plan, and clear lines of responsibility and accountability.

Cognizant of the aforesaid, board of directors is a responsible body to oversee the development of overall strategy of a bank and the decisions made by senior management in pursuit of the strategic objectives. Thus, the board, in order to perform its responsibilities and prompt operational efficiency, must be supported by rigorous internal control, effective risk management and adequate and up-to-date information. Besides, an effective risk management and control structure must be accompanied by an institutional culture that ensures that written policies and procedures are translated into practice to identify, measure, monitor, and control major risks like: credit risk, liquidity risk, market risk, and operation risks. McDonough, J. (2002).

Given the above point of view, the National Bank of Ethiopia's Bank Risk Management Guideline (NBE, 2010:1) underlined that the role of the board of directors to ensure effective risk management involves:

- executing active oversight on the overall strategy of a bank and the decisions made by senior management;
- put adequate policies, procedures, and risk appetite limits in place;
- implement adequate risk monitoring and management information system; and
- Ensuring adequate internal control is in practice.

With this in mind, the intent of this research is to examine the Corporate Governance practice in Lion International Bank S.C with due focus on the Role of Board of Directors in ensuring Risk Management in light of the National Bank of Ethiopia Risk Guideline standards, and the Corporate Governance Directives, the Basel Accord (internationally renowned set of recommendations for regulations in the banking industry).

3.2. Statement of the Problem

Risk management practice of commercial banks has never been more critical and challenging than it is today. In the context of the current global financial crisis and the dynamics of global economy, banks now face risks that are more complex, interconnected and potentially overwhelming than ever before. It is evident that risk from the financial services sector has contributed to large-scale misadventures, bank failures, government intervention and rapid consolidation. And the repercussions have spread out to the broader economy that led to an increased legislative and regulatory focu6s on risk management.

It is also presupposed that the recent financial crisis, which has evolved to economic slowdown worldwide, has awaken many of the financial institutions and supervisory organs to review and asses their position towards risk management. The National Bank of Ethiopia (NBE) was one of the supervisory organs that awaken and stimulated to conduct a survey on December 2009 on 15 public and private commercial banks under its supervision to identify the status of risk management practices by the banks (NBE, http://nbe.gov.et/pdf/bankrisk/SurveyReport%20revised.pdf). Hence, the findings revealed the following facts and weaknesses of the banks in relation to the status of risk management awareness and practices that:

- Full/part of board members in 87% of banks did not sit for training on risk management; and 60% of banks' boards of directors are not provided with relevant and up-to-date economic, business and market data for informed decision-making;
- 60% of banks have not yet documented risk management strategy and 74% of banks have not yet documented risk management program;
- Risk management policies of 60% of banks do not define risk limits, & 93% of the rest either rely only on NBE limits for counterparty, or above 3/4th of them did not define limits at all for geography, product, security, sector, etc;
- Internal communication of risk appetite and findings is low in 60% of banks;
- 60% of them have not created risk register, and 87% of them do not exercise stress testing as a risk management tool;

- The survey has also identified that Credit, operational and liquidity risks were key bank risks over the last two years, and will continue to be so over the next five years.

The survey unveiled significant proportion of banks' board of directors lack: training(awareness) on risk management staff, up-to-date and relevant information for decisions making, adequate risk management budget, risk management strategies, policies and programs, timeframe to review risk management documents, risk limits, risk communication, internal and external audit review, and failed to identify risks. Though the problems discussed on the survey are generic to all banks, some problems are observed in LIB in relation to training and awareness on risk management issues. Besides, the risk communication process seems not strong. Thus, the findings along with own observation instigated researcher to raise questions about the corporate governance of banks, the vulnerability of banks to various risks and the level of involvement of the supervisory organ to curb the situation.

Hence, this research principally aims at reviewing and examining the corporate governance and risk management practices of Lion International Bank (LIB) in light of the regulatory body of the banking sector - National Bank of Ethiopia (NBE) and Basel Committee standards towards realization of the role of board of directors in ensuring risk management in the bank. In the course of the research the paper has reviewed the NBE's risk management guidelines and the Basel Committee in Banking Supervision (BCBS) principles of corporate governance and risk management. It has also reviewed various related literatures on the role of board of directors on bank risk management so as to examine the bank's risk management function and identify the gaps in that regard.

3.3. Research questions

The specific objectives of the research are spelled out in the following research questions:

1. How the board is operating to ensure/establish corporate governance in the Bank?
2. What does the board structure look like in light of risk governance principles?
3. How is the risk management being undertaken in light of risk management standards? and
4. What is the role of the board in ensuring sound risk management?

3.4. Objective of the Research

The objective of the research is to examine and describe the corporate governance and role of board of directors in ensuring effective risk management practices of Lion International Bank against the National Bank of Ethiopia's basic risk management guidelines and the Basel Accord standards. However, the specific objectives include examining and describing:

- the role of LIB's board in establishing basic sound risk governance and risk appetite frameworks to ensure risk management in the bank;
- the role of LIB's board in setting and establishing risk capacity, risk tolerance, and risk limits, and risk matrixes to ensure risk control and management in the bank;
- Identifying the gap between the international standard and supervisory organ and LIB's practices.

3.5. Significance of the Research

However, it is apparent that there are few researches conducted on Corporate Governance of financial and non-financial organization focusing on the basic principles of corporate governance and related topics, but not yet or very rare on the role of board of directors' in ensuring effective risk management on banks. Thus, this research is exclusively on the role of board of directors' in ensuring effective risk management on the case of LIB and attempts to base arguments on theoretical foundations, and international and national standards and regulatory organ requirements on risk management process. It is, therefore, believed the research can:

- ➢ indicate the gaps observed in corporate governance and risk management in LIB, and as a result of which corrective measures will hopefully be taken by the board of directors and senior management of the Bank to put in place effective/adequate risk management; and
- ➢ indicate the extent to which liquidity, market, credit and operational risks affect the activities of banks, and
- ➢ Encourage other researchers to conduct further/similar research on the LIB's or other financial institutions risk management process.

3.6. Scope of the Research

The scope of the research is assessing and describing the corporate governance and risk management practices of the board directors of Lion International Bank dealing on major issues related to board composition, overall responsibility, risk governance, risk framework risk, and board's oversight role on functions of the senior management of LIB.

3.7. Limitations of the Research

The secrecy nature of the information on risk management process of commercial banks was difficult for the researcher to find imperative data and information from the commercial Banks other than LIB. To address this constraint, the researcher has exerted efforts to convince the sources that the information they provide will be treated strictly confidential and will be used for the purpose of the research only. Therefore, the research is limited to examining the risk management practices in Lion International Bank S.C with emphasis to the role of board of directors towards ensuring risk management. However risk management highly involved in risk measurement, this research for the reason that it is concentrated on the role of board of directors in corporate governance to ensure risk management it will not deal with risk measurements. Rather, focuses on roles and responsibilities of board of directors in establishing sound risk management structures and risk governance frameworks along with the correspondent duties and responsibilities entrusted to responsible work units and individuals engaged in risk management.

3.8. Organization of the Research

Regarding organization of the research, the paper is organized into five parts. The first part provides an introduction to the research area dealing with the background of the problem, statement of the problem, research questions, objective of the research, significance of the research, scope of the research, and limitations of the research. The second part reviewed literatures related to the research in the areas of banking and risk management. Part three held research design and methodology. Data presentation and analysis has been discussed on part four; while discussion, conclusion and recommendation are followed on the next part.

CHAPTER TWO

4. LTERATURE REVIEW

This chapter is meant to review works on definition of bank, evolution of the banking system in Ethiopia, the role of the National Bank of Ethiopia in the Banking system and banking structure in Ethiopia. It mainly focuses the principles of corporate governance and risk management including the types of risk in banking.

4.1. Definition of Bank

Many literatures describe banks as any business offering deposits subject to withdrawal on demand and making loans of commercial or business nature. Peter, S. and Sylvia, C. (2008) The Basel Committee on Banking Supervision (1999) described banks as a critical components of any economy, for they provide financing for commercial enterprises, basic financial services to broad segment of the population and access to payments system.

Meanwhile, the Ethiopian proclamation to provide for banking business defined banks as "a company licensed by National Bank to undertake banking business." The proclamation further described 'banking business' as any business that consist of: receiving funds from the public, using the funds in whole or in part, for the account and at the risk of the person undertaking banking business, for loans or investments, and transfer of funds to other local and foreign persons on behalf of the banks themselves or their customers in a manner acceptable and authorized by the National Bank. (Federal Negarit Gazeta Proclamation no. 592/2008)

However, there are different kinds of financial service firms calling themselves banks: like saving banks, community banks, mortgage banks, cooperative banks, commercial banks, merchant banks, and so on (Peter, S. and Sylvia C. 2008); for the purpose of this thesis, the researcher has focused on commercial banks which serve both business and household customers. Thus, for the fact that the Ethiopian private banks are functioning activities that fit to the definition of Commercial bank, and for better clarity the researcher opts using the explicit definition of commercial banks that, a 'Commercial Bank' is a financial institution that provides services such as accepting deposits, giving business loans and mortgage lending, and basic investment products like saving accounts and certificate of deposits.

4.2. The National Bank of Ethiopia

The National Bank of Ethiopia was established in 1963 by proclamation no. 206/1963 and began operation in January 1964 (http://nbe.gov.et/history.html). Prior to this proclamation, the Bank used to carry out dual activities, i.e. commercial banking and central banking functions. By the proclamation the National Bank of Ethiopia was solely entrusted with the following responsibilities to:

- regulate the supply, availability and cost of money and credit;
- manage and administer the country's international reserves;
- license and supervise banks and hold commercial banks reserves and lend money to them;
- supervise loans of commercial banks and regulate interest rates;
- issue paper money and coins;
- act as an agent of the Government; and
- Fix and control the foreign exchange rates.

However, the responsibilities entrusted to the bank were amended by proclamation no. 99/1976 that shaped the Bank's role adoring to the socialist economic principle that the country adopted. Later in 1994 the Bank’s role was revised for a third time by a proclamation 83/1994 that reshaped it to the market-based economic policy so that it could foster monetary stability, a sound financial system and such other credit and exchange conditions as are conducive to the balanced growth of the economy of the country. Accordingly, among others, the following are some of the powers and duties vested in the Bank:

- regulate the supply and availability of money & credit and applicable interest and other changes;

- license and supervise banks, insurers and other financial institutions;
- create favorable conditions for the expansion of banking, insurance and other financial services;
- set limits on gold and foreign exchange assets which banks and other financial institutions authorized to deal in foreign exchange and hold in deposits;
- formulate and implement exchange rate policy;
- set limits on the net foreign exchange position and on the terms and amount of external indebtedness of banks and other financial institutions;
- make short and long-term refinancing facilities available to banks and other financial institutions;
- act as banker, fiscal agent and financial advisor to the Government;
- take such steps to establish, modernize, conduct, monitor, regulate and supervise payment, clearing and settlement systems;
- act in compliance with international monetary and banking agreements of Ethiopia and represent Ethiopia in the International; and
- Monetary Fund and other international financial organizations formed by central banks.

4.3. Corporate Governance Overview

The concept of corporate governance potentially covers a large number of distinct economic phenomena. Hence, since corporate governance has various definitions, models and practices in different countries it is difficult to compromise and single out one definition to the concept of corporate governance; OECD (1999) however, looking at different definitions may help to conceptualize the concept corporate governance.

The Organization for Economic Cooperation and Development (OECD, 1999) defined corporate governance as: "… the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs.

By doing this, it also provides the structure through which the company objectives are set and the means of attaining those objectives and monitoring performance" (http://e.viaminvest.com)

From the banking perspective, Uwigbe, O (2011) citing Jensen & Mecking (1976) support the above definition implying that corporate governance is a crucial issue for the management of corporations (banks) which can be viewed from two dimensions: one - the transparency in the corporate function, thus, protecting the investors' interest; while the other is concerned with having a sound risk management system in place. Meanwhile, the Basel Committee in Banking Supervision (BCBS, 2004) elaborates the transparency dimension in the corporate governance function as "protecting the depositors, meeting shareholders' obligations, and taking into account the interests of other recognized shareholders". It further elaborated the second dimension that ensuring a sound risk management system in place involves giving emphasis to key components of risk governance such as Risk culture and risk appetite and their relationship to a bank's risk capacity.

The above definitions denote that corporate governance is the system which involves a set of relationship between a company's management, its board, its shareholders, and other stakeholders who expect what the corporation ought to be and what structure, composition, and leadership should it have while existing in business. It also involves maintaining sound risk management system putting transparency into practice in the corporate function so that to maintain a balance in the interests of key role players of corporate governance in corporations.

4.4. What is Special about Bank's Corporate Governance?

Banks are critical components of any economy. BCBS (1999) the fact is that banks provide financing for commercial enterprises and basic financial services to a broad segment of the population. Moreover, banks are expected to supply credit and liquidity in difficult market conditions.

Besides, the nature of multitude stakeholders than nonfinancial firms and the opaqueness and complexity of the business distinguishes governance of banks from that of nonfinancial firms. Merhan, H et.al (2011) Banks which consists of more than 90 percent of debt (as opposed to an average of 40 percent from nonfinancial firms), have more stakeholders than nonfinancial firms. The stakeholders in bank include debt holders, the majority of which are the depositors. The deposit insurance authorities also have interest in the banks' health, as they will be called upon in the case of solvency or failure. Merhan, H et.al (2011)

Moreover, the banks' liquidity producing function i.e. the existence of banks is dependent on the liquidity they obtain from depositors, the short-term interbank marketing, and the financing markets or funding from central banks will arise a concern of the regulatory body, the central banks in the form of liquidity requirements. BIS (2008) Likewise, since banks are highly leveraged institution, there is a need of regulation in the form of minimum capital requirements. BIS (2008)

Despite of the multitude of stakeholders with varied concerns and interests, both opaqueness and complexity nature of the business distinguish banks from nonfinancial institutions. "Banks can alter the risk composition of their assets more quickly than most nonfinancial industries, and as banks can readily hide problems by extending loans to clients that cannot service previous debt obligations" Levine (2004) Besides, as compared to nonfinancial industries, banks are very much interconnected with each other and since majority part of their business is done among themselves, a problem at one bank can spread to other banks very quickly and cause significant damage on a national economy. Berka, D. (2012) Thus, due to the importance and the crucial impact banks have on the national economy, banking is a universally regulated industry; therefore, banks require strong corporate governance.

4.5. Basic Principles of Corporate Governance

Various international, financial and nonfinancial, such as the United Nations Conference on Trade and Development (UNCD), Organization foe cooperation and Development (OECD), the Basel Committee for Banking Supervision(BCBS) and others have set corporate governance guidelines and principles to ensure good governance and sound stability within their corporations. Most of the principles focus on financial and nonfinancial disclosure requirements including ensuring the rights of shareholders, roles of stakeholders, and responsibilities of boards of directors as major aspects of corporate governance. (UNCTAD. 2006, OECD. 1999, BCBS. 2014) In addition, the principles encourage corporations to utilize international best practices that suit to their respective business cultures, best tenets of policy directions and legal frameworks. For the purpose of this thesis the researcher chose dwelling on the Basel Committee for Banking Supervision (BCBS, 2014) guidelines for corporate banks issued on October 2014 for it has direct relevance with the National Bank of Ethiopia's Risk Management Guidelines (2010) and Bank Corporate Governance (2015).

The BCBS principles have been developed to ascertain sound and consistent governance and risk management practices in banks. Besides, principles reinforce the collective oversight and risk governance responsibilities of the board; emphasizes on key components of risk governance. The principles also describe the specific roles of the board and its risk committee, senior management, and the control function to strengthen banks' overall check and balance. The following are the basic principles for Corporate Governance and Risk Management of banks that developed by the Basel Committee for Banking Supervision and technically adopted by the National Bank of Ethiopia by defining and assigning the board's overall responsibilities, defining the board's composition, establishing risk governance and risk appetite frame works, and maintaining sound disclosure of information and mechanisms of control:

4.5.1. Board's Overall Responsibilities

The board has overall responsibility for the bank, including approving and overseeing the implementation of the bank's strategic objectives and governance framework. The board is also responsible for providing oversight of senior management.

Accordingly, the board should:

- establish and monitor the bank's business objectives and strategy;
- oversee implementation of the appropriate governance framework;

- develop, along with senior management and the Chief Risk Officer (CRO), the bank's risk appetite, taking into account the competitive and regulatory landscape, long-term interests, exposure to risk and the ability to manage risk effectively;
- monitor the bank's adherence to the Risk Appetite Statement (RAS), risk policy and risk limits;
- approve and oversee the implementation of the bank's capital adequacy assessment process, capital and liquidity plans, compliance policies and obligations, and the internal control system;
- approve the selection and oversee the performance of senior management; and
- Oversee the design and operation of the bank's compensation system, and monitor and review the system to ensure that it is aligned with the bank's desired risk culture and risk appetite.

4.5.2. Board qualifications and composition

Board members should be and remain qualified, individually and collectively, for their positions. They should understand their oversight and corporate governance role and be able to exercise sound, objective judgment about the affairs of the bank.

The board must be suitable to carry out its responsibilities and have a composition that facilitates effective oversight. For that purpose, the board should be comprised of individuals with a balance of skills, diversity and expertise, who collectively possess the necessary qualifications commensurate with the size, complexity and risk profile of the bank. The Board should collectively have knowledge of current national, regional, and international or global economy affairs, market forces and the legal and regulatory environment.

4.5.3. Board's own structure and practices

The board should define appropriate governance structures and practices for its own work, and put in place the means for such practices to be followed and periodically reviewed for ongoing effectiveness.

The organization and functioning of the board is essential responsibilities of the board. The board should structure itself in terms of leadership, size and the use of committees so as to effectively carry out its oversight role and other responsibilities. This includes ensuring that the board has the time and means to cover all necessary subjects in sufficient depth and have a robust discussion of issues. To increase efficiency and allow deeper focus in specific areas, a board may establish certain board committees. The committees should be created and mandated by the full board. Among which, the following committees are required to be established by the board from among the board members:

4.5.3.1. Audit committee:

The audit committee is the one advised to be established with the power to oversight both internal and external audit activities and financial positions of the bank and over see the bank's compliance to policies and laws applicable in the governance framework as well. The audit committee members should have a relevant experience in financial reporting, accounting and auditing.

4.5.3.2. Risk Management committee:

The risk Management committee is an important body of the board that shall discuss all risk strategies on both an aggregated basis and by type of risk and make recommendations to the board thereon, and on the risk appetite. It is responsible for advising the board on the bank's overall current and future risk appetite, overseeing senior management's implementation of the RAS, including the capital and liquidity management, as well as for all relevant risks of the bank, such as credit, market, operational, compliance and reputational risks, to ensure they are consistent with the stated risk appetite.

4.5.3.3. Compensation/Remuneration Committee

The compensation committee oversees the compensation system's design and operation and ensures that compensation is appropriate and consistent with the bank's long-term business and risk appetite, performance and control environment, as well as with any legal or regulatory requirements.

4.5.4. Senior Management

Under the direction and oversight of the board, senior management should carry out and manage the bank's activities in a manner consistent with the business strategy, risk appetite, incentive compensation and other policies approved by the board.

4.5.5. Risk Management

Banks should have an effective independent risk management function, under the direction of a Chief Risk Officer (CRO), with sufficient stature, independence, resources and access to the board.

The independent risk management function is a key component of the bank for overseeing risk-taking activities across the enterprise. The independent risk management function should have authority within the organization to oversee the bank's risk management activities. Key activities of the risk management function should include:

- identifying material individual, aggregate and emerging risks;
- assessing these risks and measuring the bank's exposure to them;
- supporting the board in its implementation, review and approval of the enterprise-wide risk governance framework which includes the bank's risk culture, risk appetite, RAS and risk limits;
- ongoing monitoring of the risk-taking activities and risk exposures to ensure they are in line with the board-approved risk appetite, risk limits and corresponding capital or liquidity needs (ie capital planning);

- influencing and, when necessary, challenging material risk decisions; and
- Reporting to senior management and the board or risk committee, as appropriate, on all these items, including but not limited to proposing appropriate risk-mitigating actions.

4.5.6. Risk Identification, Monitoring and Controlling

Risks should be identified, monitored and controlled on an ongoing bank-wide and individual entity basis. The sophistication of the bank's risk management and internal control infrastructure should keep pace with changes to the bank's risk profile, to the external risk landscape and in industry practice.

The bank's risk governance framework should include policies, supported by appropriate control procedures and processes, designed to ensure that the bank's risk identification, aggregation, mitigation and monitoring capabilities are commensurate with the bank's size, complexity and risk profile.

Risk identification should encompass all material risks to the bank, on- and off-balance sheet and on a group-wide, portfolio-wise and business-line level. In order to perform effective risk assessments, the board and senior management, including the CRO, should, regularly and on an ad hoc basis, evaluate the risks faced by the bank and its overall risk profile. The risk assessment process should include ongoing analysis of existing risks as well as the identification of new or emerging risks. Besides, Risks should be captured from all organizational units that originate risk. Concentrations associated with material risks shall likewise be factored into the risk assessment. As part of its quantitative and qualitative analysis, the bank should utilize stress tests and scenario analyses to better understand potential risk exposures under a variety of adverse circumstances.

4.5.7. Risk Communication

An effective risk governance framework requires robust communication within the bank about risk, both across the organization and through reporting to the board and senior management.

Ongoing communication about risk issues, including the bank's risk strategy, throughout the bank is a key tenet of a strong risk culture. A strong risk culture should promote risk awareness and encourage open communication and challenge about risk-taking across the organization as well as vertically to and from the board and senior management. Senior management should keep control functions informed of management's major plans and activities so that the control functions can properly assess the risks. Information should be communicated to the board and senior management in a timely, accurate and understandable manner so that they are equipped to take informed decisions. While ensuring that the board and senior management are sufficiently informed, management and those responsible for the risk management function should avoid voluminous information that can make it difficult to identify key issues.

4.5.8. Compliance

The bank's board of directors is responsible for overseeing the management of the bank's compliance risk. The board should approve the bank's compliance approach and policies, including the establishment of a permanent compliance function.

An independent compliance function is a key component of the bank and is responsible, among other things, for promoting and monitoring that the bank operates with integrity and in compliance with applicable, laws, regulations and internal policies. The compliance function should advise the board and senior management on compliance laws, rules and standards, including keeping them informed of developments in the area. It should also help educate staff about compliance issues, act as a contact point within the bank for compliance queries from staff members, and provide guidance to staff on the appropriate implementation of compliance laws, rules and standards in the form of policies and procedures and other documents such as compliance manuals, internal codes of conduct and practice guidelines.

4.5.9. Internal Audit

The internal audit function provides independent assurance to the board and supports board and senior management in promoting an effective governance process and the long-term soundness of the bank. The internal audit function should have a clear mandate, be accountable to the board, be independent of the audited activities and have sufficient standing, skills, resources and authority within the bank.

The board and senior management should recognize and acknowledge that an independent and qualified internal audit function is vital to an effective governance process. An effective internal audit function provides an independent assurance to the board of directors and senior management on the quality and effectiveness of a bank's internal control, risk management and governance systems and processes, thereby helping the board and senior management protect their organization and its reputation. The internal audit function should be accountable to the board.

4.5.10. Compensation

The bank's compensation structure should be effectively aligned with sound risk management and should promote long term health of the organization and appropriate risk-taking behavior.

Compensation systems form a key component of the governance and incentive structure through which the board and senior management promote good performance, convey acceptable risk-taking behavior and reinforce the bank's operating and risk culture. The board is responsible for the overall oversight of the compensation system for the entire bank. In addition, the board should regularly monitor and review outcomes to ensure that the bank-wide compensation system is operating as intended.

4.5.11. Disclosure and Transparency

The governance of the bank should be adequately transparent to its shareholders, depositors, other relevant stakeholders and market participants.

Transparency is consistent with sound and effective corporate governance. Transparency in the area of corporate governance provides shareholders, depositors, other relevant stakeholders and market participants with the information necessary to enable them to assess the effectiveness of the board and senior management in governing the bank.

4.5.12. The role of supervisors

Supervisors should provide guidance for and supervise corporate governance at banks, including through comprehensive evaluations and regular interaction with boards and senior management, should require improvement and remedial action as necessary, and should share information on corporate governance with other supervisors.

Supervisors have a keen interest in sound corporate governance as it is an essential element in the safe and sound functioning of a bank and may adversely affect the bank's risk profile if not operating effectively. Well governed banks contribute to the maintenance of an efficient and cost-effective supervisory process, as there is less need for supervisory intervention. The board and senior management are, therefore, primarily responsible for the governance of the bank, shareholders, and supervisors.

4.6. What is Risk

Risk has traditionally been defined in terms of the possibility of danger, loss, injury or other adverse consequences. In other words, it is the possibility of undesirable events occurring that might prevent or impact upon the achievement of an organization's objectives. Oxelheim and Wihlborg (1997) define risk as a measure of the timing and magnitude of unanticipated changes, which is evaluated relative to expected changes in variables. These anticipated changes are measured by the expected change, which is normally a result of forecasting. In addition, Tchankova (2002) stated that risk is an inherent part of business and public life. Dynamic market relations continuously increase the uncertainty of the environment where business and public organizations work. There are various types of risks suggested by different authors (Fatemi and Glaum 2000, Croupy, Galai and Mark 2001, and Romero 2003) summarized the underneath along with their definitions. (Source: Fund 2006 www.wikipedia.com).

- Credit Risk - refers to a risk arising from inability or unwillingness of counterparty to honor its credit obligation in accordance with agreed terms.
- Market Risk - refers to a risk that results from adverse changes in interest rates, foreign currency exchange rates, equity prices, and other relevant market rates, prices and volatilities.
- Liquidity Risk and Funding Risk - refers to a risk to a Bank or one of its business units being unable to fund assets or meet obligations at a reasonable cost or, in case of extreme market disruptions, at any price.
- Interest Rate Risk - is a risk arising from possible interest rate differentials in positions mismatch embedded in the balance sheet of the bank.
- Operational Risk - refers to the risk of direct or indirect loss to a bank resulting from inadequate or failed internal process, people and systems or external events.
- Reputational Risk - a risk that occurs when negative publicity regarding a bank's business practices leads to a loss of revenue or litigation. It results in the decline of a bank's market or service image.
- Commodity Risk - refers to a risk of changes in the price of commodities.
- Compliance Risk - refers to a risk of legal or regulatory sanctions, financial loss that a bank may suffer as a result of its failure to comply with all applicable laws, regulations, and codes of conduct and standards of good practices.
- Foreign Exchange Risk - refers to a risk that results from changes in exchange rate between domestic currency and currencies of the rest of the world.

- "IT Risk" a risk that arise from any potential adverse outcome, impairment, loss, violation, failure or disruption in the performance of business functions or processes due to the use of or reliance on technology. Exposure to this risk can result from among others, systems flaws, software defects and network vulnerabilities.
- Legal Risk - refers to a risk that arising from the potential those unenforceable contracts, lawsuits, or adverse judgments can disrupt or otherwise negatively affect bank's operations or conditions.
- Regulatory Risk - is a risk of being downgraded, fined, suspended, license revoked, etc arising from failure to comply with regulatory requirements or directives.
- Strategic Risk - refers to the potential negative impact on a bank's earnings and capital that can arise in circumstances where decisions taken by the organization or the manner in which business strategies are executed result in losses or missed opportunities for the organization to remain relevant in the marketplace as a profitable and viable business entity.
- Systemic Risk - refers to the danger that problems in a single financial institution might spread and, in extreme situations, such contagion could disrupt the normal functioning of the entire financial system.

Likewise, Risk is defined as anything that can create hindrances in the way of achievement of certain objectives. It can be because of either internal factors or external factors, depending upon the type of risk that exists within a particular situation. Exposure to that risk can make a situation more critical. A better way to deal with such a situation is to take certain proactive measures to identify any kind of risk that can result in undesirable outcomes. In simple terms, it can be said that managing a risk in advance is far better than waiting for its occurrence. Risk Management is a measure that is used for identifying, analyzing and then responding to a particular risk.

It is a process that is continuous in nature and a helpful tool in decision making process. According to the Higher Education Funding Council for England (HEFCE), Risk Management is not just used for ensuring the reduction of the probability of bad happenings but it also covers the increase in likeliness of occurring good things. A model called "Prospect Theory" states that a person is more likely to take on the risk than to suffer a sure loss. [International Journal of

Marketing, Financial Services & Management Research--ISSN 2277-3622 Vol.2, No. 2, February (2013)]

From the above discussion, however, it is clear that there are numbers of risk types require boards' and senior managements' attention, but from the contextual definition of risk that defined as reductions in firm value due to change in business environment this thesis will focus on the Interest rate risk, Credit risk, Operational risk, Liquidity risk, and Foreign currency risk as major sources of value loss which banks are particularly exposed in their operations.

4.7. Risk Management

The International Risk Governance Council describes Risk management as a process of identification, assessment, management and communication of risks in a broad context. The terms assessment and measurement involves risk measurement, risk control and mentoring. Risk management includes the totality of policies, procedures, processes and mechanisms; and is concerned with how relevant risk information is collected, analyzed and communicated, and how management decisions are taken. (http://www.irgc.org, IRGC, 2005)

Risk management is a process established to ensure that all material risks and associated risk concentrations are identified, measured, limited, controlled, mitigated and reported on a timely basis (BCBS 2014). Thus, it is a central part of any organization's strategic management. It is the process whereby organizations methodically address the risks attaching to their activities with the goal of achieving sustained benefit within each activity and across the portfolio of all activities.

The focus of good risk management is the identification and treatment of these risks. Its objective is to add maximum sustainable value to all the activities of the organization. It arrays the understanding of the potential upside and downside of all those factors which can affect the organization. It increases the probability of success, and reduces both the probability of failure and the uncertainty of achieving the organization's overall objectives. Risk management should be a continuous and developing process which runs throughout the organization's strategy and the implementation of that strategy. It should methodically address all the risks surrounding the organization's activities past, present and in particular, future.

In the process of doing business, it is inevitable for banks to face with unexpected and very often unpleasant surprises that threaten to undercut or, even worse, to destroy the business. That is the essence of risk and how a company or an individual respond to it will determine whether it will survive and succeed or not.

Risk management is often performed by an organizational unit, ideally an independent staff function reporting directly to the board of directors, making risk management a board's responsibility and task. The board has to set strategic targets and ensure, via strict controls, that the goals set are actually achieved within the centrally mandated guidelines. Running a risk - management function in a centralized manner is advantageous because it allows for an independent, integrated view of all types of risk, so that only the net positions need to be managed and specialized staff can achieve better pricing in the capital markets. Management has to develop strategic goals for the various risk areas (risk strategy) that are proportionate with the ultimate objective to maximize company value. The goal of risk management should be to ensure that any risk-management activity is consistent with value maximization. The ultimate objective should not be to minimize, or avoid all risks, but it should be to find the optimal balance between risks taken and expected returns, concentrating on the competitive advantage of the company.

The Basel Committee on Banking Supervision's guideline for corporate governance principles for banks emphasizes that Banks should have an effective independent risk management function, under the direction of a Chief Risk Officer, (in our context the Risk and Compliance Management Director) with sufficient stature, independence, resources and access to the board. (BCBS. 2014, pp22) In general risk management function involves key activities that include:

- identifying material individual, aggregate and emerging risks;
- assessing these risks and measuring the bank's exposure to them;

- supporting the board in its implementation, review and approval of the enterprise-wide risk governance framework which includes the bank's risk culture, risk appetite statement (RAS) and risk limits - (Risk Culture refers to a bank's norms, attitudes and behaviors related to risk awareness, risk taking and risk management and controls that shape decisions on risks. Risk culture influences the decisions of management and employees during the day-to-day activities and has an impact on the risks they assume);
- ongoing monitoring of the risk-taking activities and risk exposures to ensure they are in line with the board-approved risk appetite, risk limits and corresponding capital or liquidity needs (i.e. capital planning);
- establishing an early warning or trigger system for breaches of the bank's risk appetite or limits; and
- Reporting to senior management and the board or risk committee, as appropriate, on all these items, including but not limited to proposing appropriate risk-mitigating actions.

4.8. Risk Management Regulations

The Basel Committee on Banking Supervision is an institution created by the central bank Governors of the Group of 10 nations(G10) (Belgium, Canada, France, Italy, Japan, the Netherlands, the United Kingdom, the United States, Germany and Sweden). The Basel Committee formulates broad supervisory standards and guidelines and recommends statements of best practice in banking supervision (Basel II Accord, for example) in the expectation that member authorities and other nations' authorities will take steps to implement them through their own national systems. The purpose of the committee is to encourage convergence toward common approaches and standards. (Risk management in banking, Alina Mihaela Dima, Ivona Orzea).

Likewise, the National Bank of Ethiopia (NBE) has issued a Bank Risk Management Guidelines in 2010 that matched to strong risk management practices. The guidelines, consistent with international standards and best practices, are supposed to provide minimum risk management (risk identification, measurement, monitoring and control) standards for all banks operating in

Ethiopia. It covers the most common and interrelated risks facing banks in Ethiopia namely: credit, liquidity, market (foreign currency) and operational risks.

The guidelines are implemented to guide the risk-based supervision and promote safety and soundness of the banking system. Besides, the guidelines strictly oblige banks to establish comprehensive risk management program which contain:

- Active board and senior management oversight;
- Adequate policies, procedures and limits;
- Adequate risk monitoring and management information system; and
- Adequate internal control.

The NBE is, therefore, responsible to approve the bank's risk programs and review the adequacy of implementation of the risk management program of each bank through off-site analysis and on-site examinations.

4.9. Major Types of Banking Risk

4.9.1. Interest Rate Risk

Net interest income, the difference between interest income and interest expense, is the main determinant of the profitability of banks. It is determined by interest rates on assets and paid for funds, volume of funds, and as a consequence the changes in interest rate affect the net interest income. Interest rate risk is the potential negative impact on the net interest income and it refers to the vulnerability of an institution's financial condition to the movement in interest rates. Changes in interest rate affect earnings, value of assets, liability off-balance sheet items and cash flow. Therefore, the objective of interest rate risk management is to maintain earnings, improve the capability, the ability to absorb potential loss and to ensure the adequacy of the compensation received for the risk taken and affect risk return trade-off.

All financial institutions face interest rate risk. Changes in interest rates affect both bank's earning and expenses and also the economic value of its assets and liabilities. The effects resulting from these changes are reflected in the bank's capital and income. Bank regulators and supervisors place great emphasis on the evaluation of bank interest rate risk management. These have begun to grow in importance since the implementation of market-risk-based capital charges recommended by the Basel Committee. Interest rate risk management comprises various policies, actions, and techniques that banks use to reduce the risk of reduction of its net equity as a result of adverse changes in interest rates (van Greuning, Brajovic Bratanovic, 2003).

A rise in interest rates not only triggers an increase in interest earned and paid by the bank, but also a decrease in the market value of fixed-rate assets and liabilities. Usually such a change also causes a decline in demand liabilities and call loans. In effect, when market rates go up, account holders usually find it more convenient to transfer their funds to more profitable types of investment. At the same time, the bank's debtors (firms or individuals) tend to cut down on the use of credit lines due to the higher cost of these services. Nonetheless, interest rate risk pertains to all positions in the bank's assets and liabilities portfolio (namely, the banking book). To measure this risk the bank has to consider all interest-earning and interest -bearing financial instruments and contracts on both sides of the balance sheet, as well as any derivatives whose value depends on market interest rates.

4.9.2. Credit Risk

The field of credit risk gained considerable momentum due to the increased competition in the field and the challenges of the present financial crisis (Bharath and Shumway, 2008; Davydenko, 2008; Korteweg and Polson, 2008). Credit risk is one of the main risks of commercial banks that affect the banks' ability of sustainable operation.

Banks assume credit risk when they act as intermediaries of funds; and credit risk management lies at the heart of commercial banking. Studies of banking crises show that the most frequent factor in the failure of banks has been poor loan quality. The credit risk management process of a bank is believed to be a good indicator of the quality of the bank's loan portfolio.
Credit risk emerged as a significant risk management issue during the 1990s. In increasingly competitive markets, banks began taking on greater credit risk in this period.

The Bank of International Settlement report (BIS, 1996) has defined credit risk as a risk that a counterparty will not settle an obligation for full value, either when due or at any time thereafter. In exchange for value systems, the risk is generally defined to include replacement risk and principal risk.

Credit risk covers all risks related to a borrower not fulfilling his obligations on time. Even where assets are exactly matched by liabilities of same maturity, the same interest rate conditions and the same currency, the only on balance sheet risk remaining would be credit risk.

There are two main types of credit risk that a portfolio or position is exposed to, credit default risk and credit spread risk. Credit default risk is a risk that occur when an issuer of debt, obligor, is unable to meet its financial obligations. Where an obligor defaults, an investor generally incurs a loss equal to the amount owed by the obligor less any recovery amount which the investor recovers as a result of foreclosure, liquidation or restructuring of the defaulted obligor. All portfolios with credit exposure exhibit credit default risk. The magnitude of credit default risk is described by a firm's credit rating. The credit rating is announced after a formal analysis of the borrower. In the course of analysis several issues are taken into account. Among which: the balance sheet position and expected cash flows and revenues, quality of management, company's ability to meet scheduled interest and principal and an outlook of the industry as a whole the major issues being considered.

Banks can reduce credit risk by (Machiraju, 2008):

- Raising credit standards to reject risky loans;
- Obtaining collateral and guarantees;
- Ensuring compliance with loan agreement.
- Transferring credit risk by selling standardized loans;
- Transferring risk of changing interest rates by hedging in financial futures, options or by using swaps;

- Creating synthetic loans through a hedge and interest rate futures to convert a floating rate loan into a fixed rate loan; and
- Making loans to a variety of firms whose returns are not perfectly positively correlated.

4.9.3. Liquidity Risk

Liquidity of a bank may be defined as the ability to meet anticipated and contingent cash needs. Cash needs arise from withdrawal of deposits, liability maturities and loan disbursals. The requirement for cash is met by increases in deposits and borrowings, loan repayments, investment maturities and the sale of assets. Inadequate liquidity can lead to unexpected cash shortfalls that must be covered at excessive cost which reduces profitability. It can lead to liquidity insolvency of the bank without being capital insolvent (Crouhy, Galai, Mark, 2005).

Bank liquidity management policies should comprise a risk management structure, a liquidity management and funding strategy, a set of limits to liquidity risk exposures, and a set of procedures for liquidity planning under alternative scenarios, including crisis situations. Liquidity is necessary for banks to compensate for expected and unexpected balance sheet fluctuations and to provide funds for growth. A bank has adequate liquidity potential when it can obtain needed funds promptly and at a reasonable cost. The price of liquidity is a function of market conditions and the market's perception of the inherent riskiness of the borrowing in situation (Greuning,V. and Bratanovic, B. 2003).

The importance of liquidity transcends the individual institution, because a liquidity shortfall at a single institution can have system wide repercussions. It is a nature of banks to transform the term of its liabilities to different maturities on the asset side of the balance sheet.

Liquidity risks are normally managed by a bank's Asset-Liability management Committee (ALCO), which must therefore have a thorough understanding of the interrelationship between liquidity and other market and credit risk exposures on the balance sheet.

Forecasting possible future events is an essential part of liquidity planning and risk management. An evaluation of whether or not a bank is sufficiently liquid depends on the behavior of cash flows under different conditions. Liquidity risk management must therefore involve various scenarios (Greuning,V. and Bratanovic, B. 2003). The first scenario, called "going concern" is usually applied to the management of a bank's use of deposits. This scenario establishes a benchmark for balance sheet–related cash flows during the normal course of business. The second scenario is related to a bank's liquidity in a crisis situation, when a significant part of its liabilities cannot be rolled over or replaced. And the third scenario is related to general market crises. In this case the liquidity is affected in the entire banking system. Liquidity management under this scenario is predicated on credit quality, with significant differences in funding access existing among banks.

The ability to readily convert assets into cash and access to other sources of funding in the event of a liquidity shortage are very important. Diversified liabilities and funding sources usually indicate that a bank has well-developed liquidity management. The level of diversification can be judged according to instrument types, the type of fund provider, and geographical markets.

4.9.4. Operational Risk

Although operational risk is by itself not a new concept, it has by far not received the same amount of attention as credit until recent years. Operational risk will not become a major constraint since it involves taking appropriate measures to ensure the qualitative transactions without processing errors in order to deliver the best services to the customers. Fundamental changes in financial markets, increasing globalization and deregulation, as well as corporate restructuring had a large impact on the magnitude and nature of operational risks confronting banks. Following severe operational failures resulting in the restructuring of the affected financial institutions or in the sale of the entity, the emphasis on operational risk within banks has increased, leading regulators, auditors, and rating agencies to expand their focus to include operational risks as a separate entity besides market and credit risk (Helbok and Wagner, 2006).

Operational risk was for the first time treated as a self-contained regulatory issue in the "Operational Risk Management" document published by the Basel Committee on Banking Supervision in 1998. "The New Basel Capital Accord" was first formulated in a proposal in 1999 and became effective in 2007; within the framework, operational risk was integrated in the so called Pillar 1 which implies its inclusion in the calculation of a banks' overall capital charge. Along with revising the minimum capital standards already covering credit and market risk, Basel II sets a new minimum capital standard for operational risk. While requiring capital to protect against operational risk losses, the new framework is meant to encourage banks to improve their risk management techniques as to reduce operational risk exposure and mitigate losses resulting from operational failures. The new capital accord provides incentive of lower capital requirements to those banks that demonstrate strengthened risk management practices and reduced risk exposures (Haubenstock and Andrews, 2001).

Management of operational risk is not a new practice; it has always been important for banks to endeavor to prevent fraud, maintain the integrity of internal controls, reduce errors in transaction processing, and so on in order to preserve the best quality services for their customers. However, what is relatively new is the view of operational risk management as a comprehensive practice comparable to the management of credit and market risk in principle. In the past, banks were almost exclusively relying on internal control mechanisms within business lines, supplemented by the audit function, to manage operational risk. While these remain important, recently there has been an emergence of specific structures and processes aimed at managing operational risk.

When setting the policy for operational risk management, the management should consider as main objectives to:

- Define and explain exposures and incidents that result from people; processes, systems, and external events; and generate enterprise-wide understanding of the drivers of operational risk incidents;
- Provide early warning of incidents and escalation of potential risk by anticipating risks and identify problem areas through ongoing monitoring of key risk indicators;

- Clearly define the roles and responsibilities of line personnel in managing operational risk and empower business units to take necessary actions;
- Strengthen management oversight;
- Provide objective measurement tools; and
- Integrate qualitative and quantitative data and other information.

4.9.5. Foreign Exchange Rate Risk

Exposure to this risk mainly occurs during a period in which a bank has a foreign currency open position, both on- and off-balance sheet, in spot markets. It is a risk of volatility due to a mismatch, and may cause a bank to experience losses as a result of adverse exchange rate movements during a period in which it has an open on or off-balance sheet position in an individual foreign currency. Movements in exchange rates may adversely affect the value of a bank's foreign currency open positions. Currently, in the Ethiopian case banks are allowed to take open positions in foreign currencies subject to regulatory limits set by the NBE. The potential for loss arises from the process of revaluing foreign currency positions in terms of Birr. When banks have an open position in a foreign currency (where assets in a currency do not equal liabilities in that currency), the process of revaluation normally shall result in a gain or loss. The gain or loss is the difference between the aggregate change in the Birr equivalent value of assets denominated in the foreign currency and the aggregate change in the value of liabilities and capital denominated in that currency.

Whether the bank incurs a gain or a loss depends upon both the direction of the exchange rate change and whether the bank is net long or net short in the foreign currency. When the bank has a net long position in the currency, revaluation shall produce a gain if the value of the currency increases. A loss results if the value of the currency decreases. Conversely, a net short position shall produce a loss if the foreign currency's value increases. A gain results if it decreases.

Banks should have written policies governing activities in foreign currencies. The purpose of these written policies is to communicate the expectations of senior management and the board of directors to the management and staff. The policies should be reviewed and approved by the board of directors.

For management and control purposes, banks must make a clear distinction between foreign currency exposure resulting from dealing and trading operations and exposures due to a more traditional banking business involving on and off-balance-sheet exposures denominated in a foreign currency. Currency risk management involving dealing/trading operations must be an information-intensive, day-in/day-out process under close scrutiny by senior management and a risk management committee. (Risk management guideline, National Bank of Ethiopia May, 2010)

To summarize, as part of effective risk management, banks should not borne all the risks contained in their principal activities that involve in financial transactions; rather they should able to eliminate or mitigate the financial risks associated those transactions by transferring them to another party through combination of pricing and product design. Banks should accept and manage only those risks that are uniquely occurred. Thus, the essence of risk management is not avoiding or eliminating risk; but deciding which risks to accept, which risks to transfer to investors and which risks to avoid or hedge. Risk management prevents an organization from suffering unacceptable loss that can cause failure or can materially damage its competitive position. Risk management should be a continuous and developing process which runs throughout the organization's strategy and the implementation of that strategy. It should address as many of the risks surrounding the organization's activities past, present and in particular, future, as possible. It cannot be developed a one -size-fit-all risk management process for all the organizations. In the case of a bank, functions of risk management should actually be bank specific dictated by the size and quality of balance sheet, complexity of functions, technical/professional manpower and the status of Management Information System in place in that bank. Balancing risk and return is not an easy task as risk is subjective and not quantifiable, whereas return is objective and measurable. (Risk management guideline, National Bank of Ethiopia may, 2010)

Risk management must translate the strategy into tactical and operational objectives, assigning responsibility throughout the organization with each manager and employee responsible for the management of risk as part of their job description. The Basel proposals provide a good starting point that banks can use to start building processes and systems attuned to risk management practice. (AcademyPublish.org–Risk Assessment and Management)

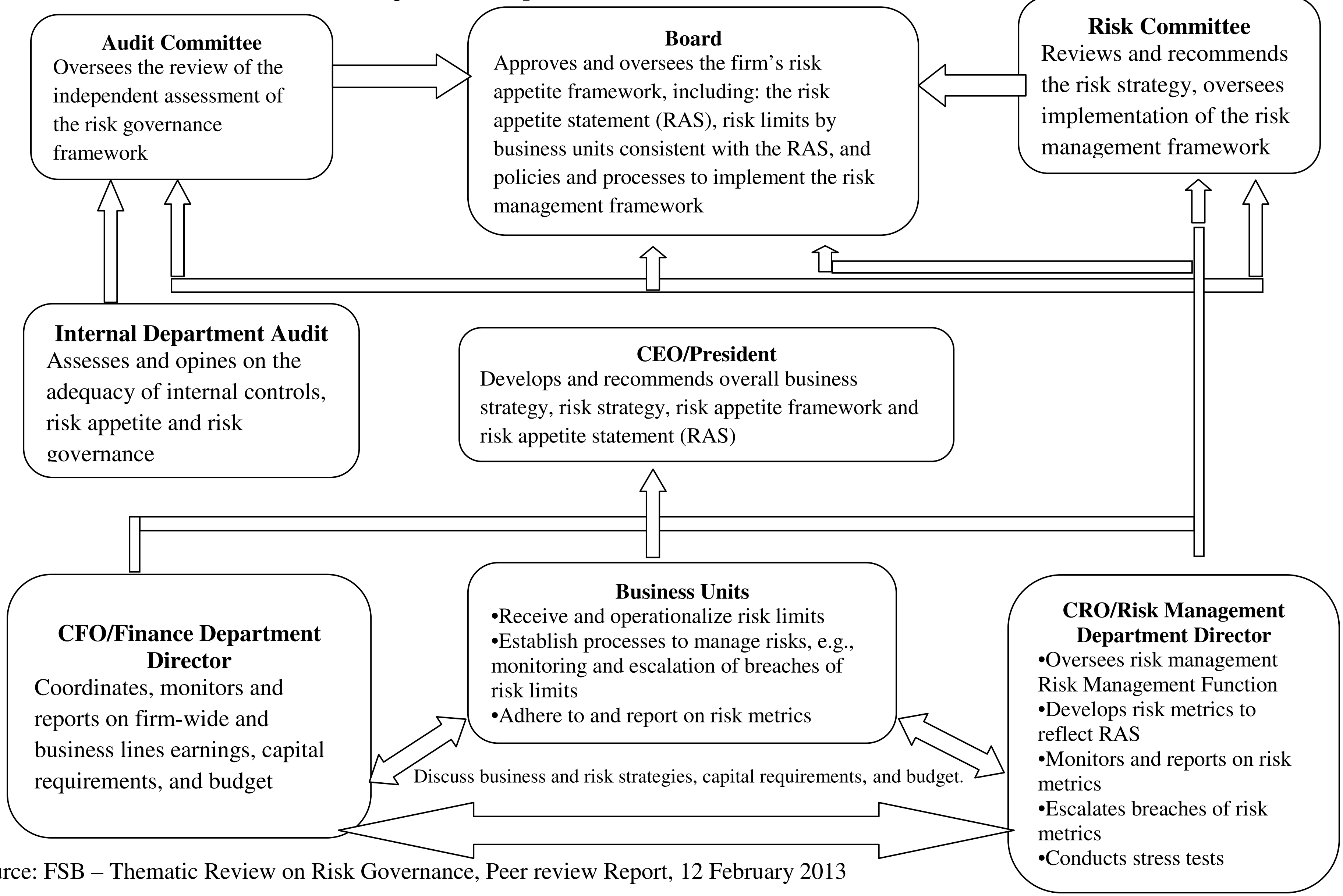
4.10. The Role of Board of Directors in Risk Management

Effective risk management involves developing sound risk governance framework and risk appetite framework. Risk management encompasses the scope of risks to be managed, the process/systems and procedures to manage risk and the roles and responsibilities of individuals involved in risk management.

4.10.1. Risk Governance Framework

Risk governance framework collectively refers to defining explicit structure of the board and its committees involving in risk management, the role and responsibilities of the board, the firm-wide chief risk officer and risk management function, and the independent assessment of the risk management function. (FSB, Thematic Review on Risk Governance, peer review report, 2013) The diagram below depicts an example of risk governance framework:

Fig. 1 **An example of a Risk Governance Framework**



Source: FSB – Thematic Review on Risk Governance, Peer review Report, 12 February 2013

4.10.2. Risk Appetite Frameworks (RAFs)

Risk appetite frameworks (RAFs) refer to risk management functions that are actionable and measurable by both the financial institutions and the supervisory organs (FSB, 2013). Risk appetite framework potentially serves as a key guiding approach for a company, including polices, processes, controls, and systems through which risk appetite is established, communicated, and monitored. It includes setting a risk appetite statement, risk limits, and an outline of the roles and responsibilities of those overseeing the implementation and monitoring of the RAF (ibd, p22)

The prime role of the board of directors in risk management is, therefore, establishing the institution wide risk governance and risk appetite frameworks and approves the risk appetite statement and the risk appetite limit which is developed in collaboration with the chief executive officer (CEO), chief risk officer (CRO), and the senior executive management.

According to the definitions given by the Financial Stability Board (FSB, 2013), risk appetite statement is the articulation in written form of the aggregate level and types of risk that a financial institution is willing to accept, or to avoid, in order to achieve its business objectives. While risk appetite refers to the aggregate level and types of risk a financial institution is willing to assume within its risk capacity to achieve its strategic plan. Risk capacity, is the maximum level of risk that financial institution can assume given its current level of resources before breaching constraints determined by regulatory capital and liquidity needs, the operational environment and obligation. While, risk limit is a quantitative measure based on forward looking assumption that allocate the financial institution's aggregate risk appetite statement to specific risk category.

The risk management function also involves considering 'the three lines of defense risk governance' when developing the risk appetite frameworks. The Deloitte Development LLC, the largest professional services network in the world engaged in audit, tax, consulting, enterprise risk and financial advisory services, on a white paper it published in 2014 on a topic "Risk appetite in the financial services industry: a requisite for risk management today" has elaborated the underlying notion of the three lines of defense risk governance framework as a ‘risk management function’ i.e. every ones job and that everyone has a specific role in the risk management.

In the first line defense, the business units are responsible for managing themselves within the statement of risk appetite; while, in the second line of defense, the risk management function is often responsible for facilitating development and drafting the risk appetite statement with input from senior management and the board and approval of the board and then monitoring the risk profile and risk utilization. The third line of defense is mainly the role of the Internal Audit. It assess whether risk management processes, including the risk appetite framework, are working effectively. Having a risk appetite framework supports all three lines of defense, by providing clear metrics for business units to manage to, allowing risk management to monitor the business units in a consistent way, and supplying Internal Audit with metrics and procedures to review and an objective framework to compare them against. Deloitte (2014) the figure below depicts the three lines of defense framework.

The three lines of defense framework and example risk appetite framework activities

Board of Directors			
	1st line of defense	**2nd line of defense**	**3rd line of defense**
	Business unit	**Risk management**	**Internal audit**
Role	**Take and manage risk**	**Set risk policy and monitor**	**Validate**
Example Responsibilities	• Conduct business in accordance with agreed strategy and related risk appetite and limits • Promote a strong risk culture and sustainable risk-return decision-making • Establish and operate business unit risk and control structure able to ensure operation within agreed policies and risk limits • Conduct rigorous self-testing against established policies, procedures, and limits • Perform thoughtful, periodic risk self-assessments • Report and escalate risk limits breaches	• Establish risk management policies and procedures, methodologies and tools, including risk appetite framework, and make available throughout enterprise • Facilitate establishment of risk appetite statement with input from senior management and the board and approval of the board and set risk limits • Monitor risk limits and communicate with the CEO and the board regarding exceptions • Provide independent risk oversight across all risk types, business units, and locations	• Perform independent testing and assess whether the risk appetite framework, risk policies, risk procedures, and related controls are functioning as intended • Perform independent testing and validation of business unit risk and control elements • Provide assurance to management and the board related to the quality and effectiveness of the risk management program, including risk appetite processes

Source: Deloitte analysis. Copyright: Deloitte Development LLC.

Fig. 2 the three lines of defense

CHAPTER THREE

4. RESEARCH DESIGN ABD METHODOLOGY

This chapter briefly presents a description of design and methodology used in the study. It gives information on how the data were gathered, what sources were used as a primary and secondary data source, and how the data were processed and analyzed. It also tells about the sampling techniques applied.

3.1 Research Design

The study is primarily designed to examine, review, and describe the practice of the corporate governance and the role of the board of LIB in ensuring risk management process and identify the observed gap between international and national standards against the Bank's actual practices. The study has incorporated review of the board structure including the organizational structure of the Bank in light of governance and risk management principles against the aforesaid standards. In carrying out the research, both primary and secondary sources of data were utilized. Concerning to the primary data, face-to-face interview were conducted with key informants, structured questionnaire, and personal observation were also employed. Besides, reviews of related literature were utilized in the process data gathering.

Concerning population, as the scope of the study is limited to Lion International Bank S.C, the population for the study is the Bank which covers total population of 925 clerical staff. Among which, the 120 staff involved in various levels of supervisory and managerial positions that have direct relevance to the risk management function of the Bank. The rule of thumb suggests that more than 80% of the Bank's activities and business are carried out in Addis Ababa and its surroundings, so does the largest share of the Bank's earnings are generated from the aforesaid areas. Thus, in order involve relevant respondents the research is designed to employ purposive sampling method. Hence, 11 (all) board members, 14 head office management staff (composed of top, middle, and line managers), and 20 branch managers and accountants been selected as respondents.

3.2 Research Method

The study employed Qualitative research method; but also quantitative data were used to support the research. Qualitative data gathered through interview from key informants have been thematically synthesized and Quantitative data gathered through questionnaire were statistically analyzed. A statistical tool SPSS has been utilized in analyzing the quantitative data. The quantitative approach places an emphasis on measurement and collection of numerical data; while the qualitative method allows developing theory from our empirical findings with a focus on meaning expressed through words and descriptions (Bryman and Bell, 2007, p402).

3.3 Data Collection

3.3.3. Primary Data

In the collection of primary data face to face interview was conduct with the Chairperson - Loan Review and Risk Management Committee, Chairman - Audit Committee, Chairman Human Resource and Business Development (Compensation) Committee, the President, and the Directors of Risk and Compliance Management Department on basic governance and risk management issues. Besides, structured questionnaire were distributed to the board members, management and staff at various levels to identify the aforementioned risk management practice gap.

Moreover, the questionnaire were maintained in ways that would focus on basic principles of governance, roles of board of directors in risk management process, the practice of risk appetite setting and communication on the appetite limits set, the risk control process and staff awareness associated with regulatory and policy framework of the Bank and respondent’s profile. With respect to identifying challenges, the respondents were provided with a five point Likert-scale showing the level of agreement/disagreement (5 being strongly agree to 1 being strongly disagree) respondents with the given statements in the mentioned above areas.

3.3.4. Secondary Data

Secondary source materials both on the theories and applications relevant to the study subject have been reviewed. Relevant books from different libraries were referred, internet resources were browsed and relevant published and unpublished documents from pertinent departments of the bank were reviewed. Moreover, data sources from the National Bank of Ethiopia (NBE), and various reports from the Basel Committee for Bank Supervision (BCBS), Financial Stability Board (FSB), and the World Bank documents were explored in line with the research objectives. Furthermore, the underneath listed secondary data were used as crucial source of information regarding the historical background of the bank, the board of directors and the risk management process of the Bank.

- Various directives of the supervisory organ NBE;
- Commercial Code of Ethiopia;
- NBE's Corporate Governance Directive(draft document);
- National Bank of Ethiopia's Risk Management Guideline for Commercial Banks.
- LIB Article and Memorandum of Association;
- LIB Board of Directors Charter;
- LIB Audit, and Risk & Compliance Management Committees Charter;
- LIB Board of Directors' meeting Minutes as deemed necessary;
- LIB Executive Management (Policy Committee)Charter;
- Risk management policy and procedure and guideline;
- Risk Management program of the Bank;
- Relevant data from the banks reports, presentations and other documents; and
- Different publications and journals regarding banking activities and policies'.

3.3.5. Sampling

According to Healey (2002), sampling is mandatory to facilitate the study maintaining large population size. As a result, officials from the top management, directors, head office managers, team leaders, branch managers, senior credit analysts, and credit follow-up managers were considered to participate as respondents representing the population of the study. However, the selection of the respondents (across all managerial levels) was made using purposive sampling. All the respondents were contacted personally by the researcher, and the responses were recorded.

The participants considered for administering the questionnaire were the board members, the top, middle and lower level management and branch managers, and accountants of the LIB. The respondents participated in the study were 55 in number, but while returning the questionnaire two board members have been failed to fill the questionnaire. Thus, the sample size of the respondents is 11board members and 44 staff of the Bank.

3.3.6. Data Collection and Analysis

Structured questionnaire were used to gather data on the risk management process of LIB; however, semi-structured interviews were carried out with senior management members of the Bank. Furthermore, all the data were exposed to appropriate statistical analysis (qualitative and quantitative) in line with the study objectives.

3.4 Research Approach.

In this research descriptive approach is chosen to carry out the study; because, the objective of the research is designed to examine and describe the process of corporate governance and risk management practices in the Lion International Bank S.C. (LIB). Using the data gained from qualitative synthesis and quantitative analysis. An attempt was made to identify basic problems in the risk management process of LIB.

CHAPTER FOUR

5. DATA PRESENTATION AND ANALYSIS

This Chapter tries to present and analyze the data gathered from documents in the Board Secretariat Office and through interviews and questionnaire concerning the Role of LIB's Board of Directors in Risk Management of the Bank's operation. The data gathered and analyzed focus on LIB's Board overall responsibilities, own structure and practices, the role of LIB's board in risk management, risk identification, monitoring and controlling process of limits, risk communication and disclosure of information, and the role of National Bank of Ethiopia (NBE) to influence banks' risk management function.

4.5. Background History of Lion International Bank S.C (LIB)

Lion International Bank is a privately owned share company established on October 2, 2006 in accordance with proclamation no. 84/94 and the Commercial Code of Ethiopia and officially inaugurated for public service on January 6, 2007. Initially, the bank was established by 3,739 shareholders with paid-up capital of Birr 108.2 million, now it has about 7,000 shareholders and paid up capital of Birr 510 million. (www.anbesabank.com/index.php/en/aboutus). Concerning financial position, the Annual Performance Report of the 2014/15 fiscal year of the Bank depicts that the Bank has total asset of birr 5.86 billion and total liability of birr 4.96 billion; while total deposits of birr 4.46 billion, and outstanding loans of birr 2.88 billion.

To date, the Bank is providing banking services with above 90 branches all over the country networking most of its branches with the DELTA Core-bank Banking Technology. It is also providing services supported by 1,875 employees; of which, the 925 are clerical staff and among the clerical staff the 120 are in supervisory and managerial positions (Top, Middle and Line level managers) which the respondent of this research are selected from this group for the reason that they have more relevance to the risk management function of the Bank.

Regarding governance, the Bank is governed by 11 members of Board of Directors elected by the General Assembly of Shareholders and led by a President accountable to the Board of Directors and two Vice Presidents (Vice President Operations and Vice President Corporate Services) reporting to the President. Pertaining organizational Structure, the Board of Directors is organized by a main board and its three sub- committees namely Loan Review, Risk & Compliance Management Committee, Audit Committee, and Human Resources & Business Development (Compensation) Committee. The committees are established by and reporting only to the board. Their primary objective is assisting the board to fulfill its oversight responsibilities and reinforcing the risk management and internal control system of the Bank.

The Management of the Bank is also structurally organized by a Senior Executive Management Team (President and Vice Presidents), Eight Departments (Finance, Credit, International Banking, Business Development & Corporate Planning, Information Technology Systems, Domestic Banking Services, Risk and Compliance Management, and Internal Audit Departments) and other Four Functional Support Service Divisions (Human Resources Management, Property & General Service, Legal Service and Engineering Divisions) that are answerable to the Vice President Corporate Services. Among the Departments the Risk and Compliance Management, and Internal Audit Departments are independent units that functionally structured to directly report to the board of directors and the supervisory organ, the National Bank of Ethiopia, and administratively responsible to the President.

Lion International Bank was established with a vision to become a 'Leading Bank in Ethiopia' by committing itself to "maximizing customers' satisfaction and shareholders' value through quality banking services delivery, technological leadership, diversified product services and motivated employees" (LIB Annual Bulletin 2014)

With the aforementioned human, technological and financial resources, the Bank has been providing both domestic and international banking services which incorporate several features of services. Besides, the Bank was successful in generating profits and offering increased dividends to shareholders in the last five years in a row.

4.6. DATA PRESENTATION AND ANALYSIS

4.2.11 Demographic Characteristics of Respondents

This part presents data and information gathered from primary (interview and questionnaire) and secondary (documents) data sources. The primary data were gathered from five key informants through interviews conducted with Chairman of the Loan Review and Risk Management Committee, Chairman of the Audit Committee, and Chairman of the Human Resources and Business Development Committee, the President, and the Director of Risk and Compliance Management Department. Besides, questionnaire' responses collected from 53 respondents have been presented and analyzed as a primary source of information. The secondary data and information has also been collected from the Bank's Board Secretariat Office and the Business Development and Corporate Planning, and the Risk and Compliance Management Departments. The Board Secretariat Office of the Bank is organized to serve as an official bureau of the Board of Directors and custodian office for the minutes, source documents, agenda items, various reports, and communication documents of the Board. The board office is led by the Board Secretary and Executive Assistant to the President. The Board Secretary is also a secretary of the board Committees and Executive Management (Policy) Committee.

To support the study with quantitative data, questionnaire (close ended and Likert scale questions) have been disseminated to 11 board members, 20 top and middle levels, and 22 lower level management members of the LIB. The questionnaire was prepared to assess opinion of the board and management members who relatively have exposure to risk management function in the Bank. Among the 55 questionnaire distributed to the respondents the 53 have been returned answering to the questions, while two board members failed to respond to the questionnaire; thus, the total questionnaire responded for analysis is 53. The researcher has exerted efforts to triangulate the data gathered from board secretary office, interview with key informants, and questionnaire responses.

4.2.12 Data and Information Gathered from Board Secretariat Office:

4.2.2.1. LIB's Board Qualifications and Composition

According to the information collected from the Board Secretariat Office, the board of directors is comprised of 11 members elected by the General Assembly of Shareholders. Based on the NBE's Bank Corporate Governance Directive no SBB/62/2015 and the Memorandum and Article of Association of the Bank 75% of the elected board member are expected to have and above educational qualification of fist degree and the remaining are supposed to have at least diploma with field of study relevant to banking and work experience of managerial position in business institutions (SBB 54/2015). The educational qualifications, composition, and work experience of board members is presented as follows:

Table: 1 LIB board qualification and composition

Qualification	Amount	Field of study	Year of Service	Area of current business engagement
PhD	2	Economics	Over 20 Years	University professors & Researchers
MBA	3	Business Administration with Management	Over 20 Years	General Managers of own private business companies
MA	2	Regional and Local Studies and International Relations	Over 20 Years	General Managers of own private business companies
MA	1	MA in Industrial Engineering	Over 20 Years	General Manager of own private business company
BA	2	BA in Accounting and prospect graduates of MBA	Over 20 Years	Department Managers in Insurance Company
BA	1	BA in Political Science and International Relation	Over 20 Years	Department Director in a public business company

Source: LIB board members profile

4.2.2.2. LIB's Board Overall Responsibilities

Board of Directors is an important part of the organization's governance system, possessing ultimate responsibility for the conduct of the organization's business. In this regard, the responsibilities of the board of directors of Lion International Bank are (Charter of the Board of Directors of LIB, 2012):

- Ensuring the preparation of strategic business objectives and set of corporate values that are to be communicated throughout the Bank;
- Ensuring that the management sets and enforces clear lines of responsibility and accountability throughout the Bank;
- Reviewing, approving and monitoring fundamental operational, financial and other internal controlling strategies and policies;
- Establishing risk governance framework, periodically reviewing risk management and internal controls system of the Bank to ensure that they remain appropriate;
- Understanding/identifying the risks that the Bank is exposed to and formulate a clear Philosophy for each risk management area; and
- Making sure that the President is monitoring the effectiveness of the internal control system of the Bank.

4.2.3. LIB's Board Own Structure and Practices

The Charter of the Board of Directors of LIB indicates that the board's governance is structured in a way it could have complete oversight role over the functions of the senior management. The main board, which is fully composed of non-executive directors elected by the general assembly of shareholders, is structured as a governing body electing among which a chairman and vice chairman. The President (CEO) and the Board Secretary, appointed by the board from among the staff, are nonvoting members. The President serves as a resource person to the board, while the secretary serves as a Minutes taker and facilitator of the board meetings.

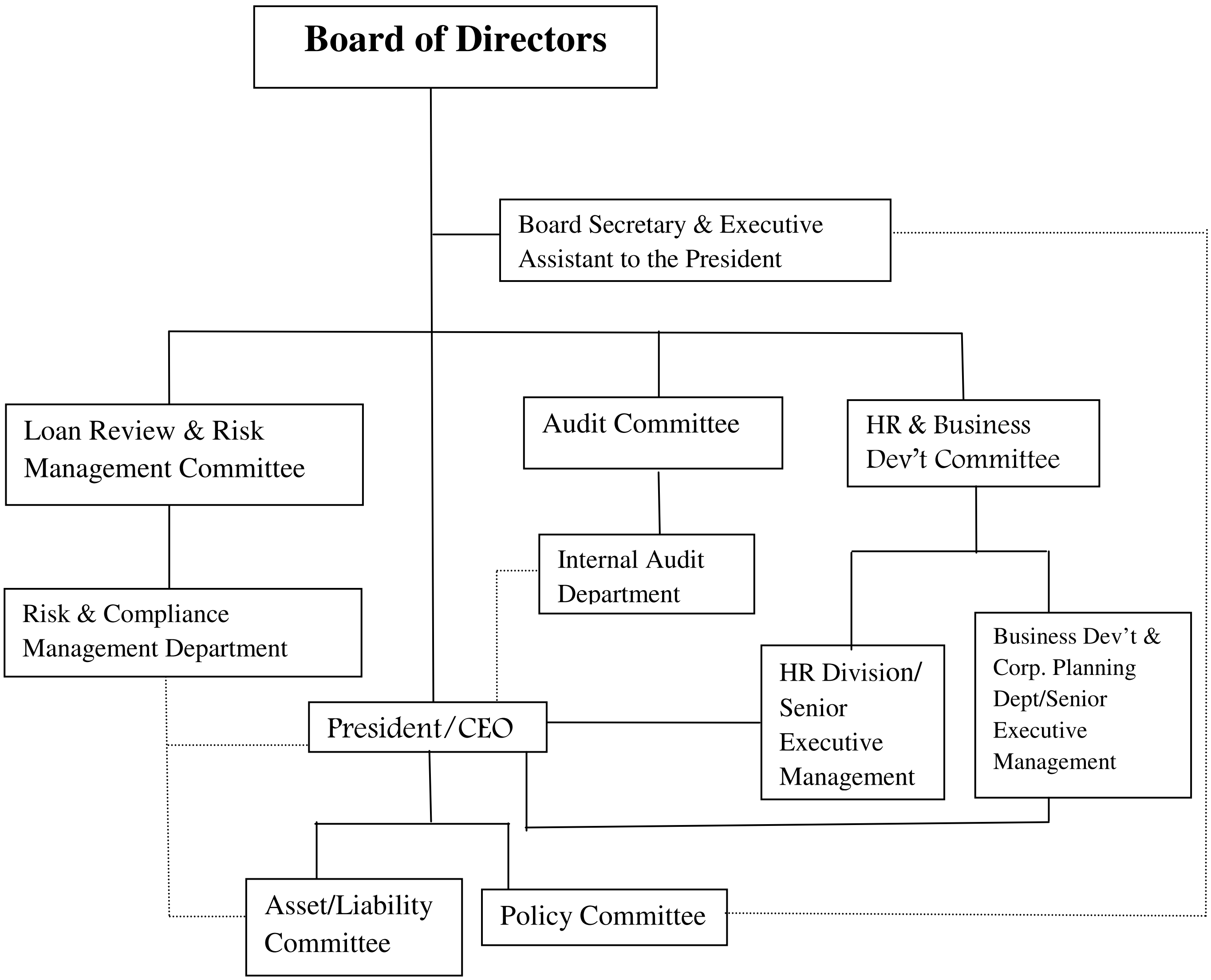
Besides, the board to carry out its oversight role and other responsibilities and ensure that it has the time and means to cover all necessary subjects in sufficient depth and increase efficiency, it structured itself into three sub committees namely:

- Loan Review, Risk and Compliance Management Committee;
- Audit Committee; and
- Human Resources and Business Development (Compensation) Committee;

The committees are established comprising of three members each. All board members are at least members of one of the committees; but the Chairman, for he is responsible to oversee the functions of every committee, is relived from membership of the committees. Members of the senior Executive Management serve the committees as resource persons. The Board Secretary is also a secretary of the committees.

LIB Board of Directors' Organizational Structure

Fig 3: LIB's Board Structure



Source: LIB Charter of board of directors (2012)

Key:

- ———— Functionally direct reporting relationship;
- ········ Functionally indirect reporting relationship.

4.2.3.1. Loan Review, Risk & Compliance Management Committee:

Based on the Board Loan Review and Risk Management Committee's Charter (2012), the committee is an important body of the board entrusted with the responsibilities of overseeing the risk management function of the Bank.

With respect to Loan Review, the Committee discharges the following oversight role in line with the supervisory organ requirement, National Bank of Ethiopia Directive No.SBB/43/2008 that:

i. Makes sure the establishment of a loan review system in the bank;
ii. Reviews and monitors the Bank's loan status, loan granting and collection performance, loan provisioning, portfolio management and the overall credit administration performance based on the quarterly, semi-annual, and annual reports; and
iii. Takes appropriate measures in response to the findings of the loan review function quarterly or more frequently as the need arise.

Besides, in relation to Risk Management, among others, the committee is possesses responsibilities of:

i. Deliberating on and approve the Bank's risk appetite and risk tolerance limits, for the various types of risks annually upon the recommendation of the Risk & Compliance Management Department;
ii. Deliberating on and approve the strategies, frameworks, policies, procedures and models for managing risks;
iii. Ensuring that risks are managed within tolerance levels of the Bank; review the Bank's actual risk profile against its risk appetite as well as any exceptions to Risk Appetite as reported by top management; and
iv. Reviewing and monitoring the implications of new and emerging risks, organizational change, regulatory requirements, major initiatives, anticipated business and economic changes and other factors to the Bank's future strategy and business performance as well as capital requirements;

The Committee in discharging its responsibilities of risk management discuses on risk strategies and risk appetite on both aggregated basis and by risk types and make recommendations to the board for its decisions and subsequent directions.

4.2.3.2. Audit Committee:

Based on the Charter of the Board - Audit Committee (2012), the audit committee possesses the responsibilities of overseeing the overall functions of management and healthiness of the operation with a view of audit-based monitoring and evaluation of the operational activities. It also oversees the risk management of the Bank with emphasis to the following specific responsibilities:

i. Oversee the financial, operational and administrative activities of the Management and the inspection activities of the Internal Audit Process by making a thorough analysis of relevant activity reports, regular and extraordinary inspection reports;
ii. regularly review the risk associated areas of the Bank to be covered within the scope of internal and external audits;
iii. regularly examine and review any accounting, auditing, and other concerns identified as a result of the external or internal audits and ensure that corrective action is taken on time; and
iv. review the Bank's quarterly, semi-annual, and annual financial statements with the Bank's Finance Department and Internal Audit Department and External Auditor to ensure that the statements, as far as possible, represent a true and reliable picture of the Bank's financial standing and that they comply with the accepted accounting principles and existing banking laws, directives, regulations and standards.

Besides, the committee facilitates communication between the board, the management and the internal and external auditors so as to establish strong internal audit and control function.

4.2.3.3. HR and Business Development (Compensation) Committee

The Human Resources and Business Development (Compensation) Committee is established to oversee the strategies and proper implementation of the strategic objectives of the Bank (HR & Business Development Committee Charter 2012). Designing the compensation system of the Bank and ensuring that the compensation is appropriate and consistent with the bank's long-term business objectives and risk appetite, performance and control environment, as well as with any legal or regulatory requirements are among the major responsibilities of the Committee. Moreover, the Committee is entrusted to periodically review the compensation of the President/ CEO and salary scale of employees that goes in line with the strategic objectives of the Bank and in consideration with the current performance (goal achievement) of employees and industry salary average so that it would enable the board to promote and balance the long term health of the organization and appropriate risk taking behavior of the CEO and employees.

Regarding human resources management, once the organizational structure and succession plan approved by the board, the Committee periodically reviews and appraises the proper implementation of the plan. Hence, in order the Bank would have competitive salary structure, the committee periodically, on annual or biannual basis, reviews and updates the compensation and bonus schemes of the CEO and employees.

4.2.4. Senior Executive Management of LIB

Under the direction and oversight of the board, senior management should carry out and manage the bank's activities in a manner consistent with the business strategy, risk appetite, compensation and other policies approved by the board (NBE Bank Risk Management Guidelines 2012).

From perspectives of risk management, the Senior Executive Management of the Lion International Bank is basically responsible for developing and implementing the Bank's strategies, policies and procedures in line with the Board of Directors direction (LIB Policy Committee charter, 2012). Thus, the Senior Executive Management in order to carry out its management function and oversight role, it has structured its self into the Policy Committee and Asset & Liability Management Committee. These committees are the highest decision making bodies of the management in the risk management function of the bank. The Committees that are established and delegated by the President have assumed the following respective responsibilities:

4.2.4.1. The Policy Committee:

The Policy Committee is the highest body of the management comprised of the President, Chairman of the committee, Vice President Operations, Vice President Corporate Services, Director Credit Department, Director Finance Department, Director Domestic Banking Services Department, and the Secretary, an Executive Assistant to the President. The following are responsibilities of the Policy Committee in connection with the management of risks:

- Develop strategic directions and policy for managing the overall risk of the Bank;
- Implement the strategic direction and policy approved by the Board of Directors;
- Ensure that appropriate policies, controls and risk monitoring systems are in place;
- Adhere to the approved limits and forward limit revision proposal, if any;
- Ensure that sufficiency, skill and knowledge of performers and major business accountability and lines of authority are clearly delineated; and
- Ensure that strong internal control system is in place.

4.2.4.2.Asset Liability Management Committee (ALCO)

In relation to management level risk management committee, the ALCO is a responsible body to oversee balance sheet risks, which mainly include liquidity and market risks. As the balance sheet risk is a critical component of the overall risk management of a bank, the committee assumes and exercises the highest risk management responsibility. Hence, the following are among the basic responsibilities entrusted to the committee:

- Regularly reviewing the effectiveness of the Asset - Liability management strategy of the Bank;
- Monitoring and deliberating on any policy and regulatory changes in relation to liquidity and market risks management; and
- Monitoring the Bank's risk exposure arising from on and off- balance sheet activities and ensuring that the Bank is liquid enough to comfortably meet obligations in normal and stressed situations.

4.2.4.3.Risk and Compliance Management Department (RCMD)

The Risk and Compliance Management function is an independent entity of the Bank that principally entrusted with responsibilities of overseeing the overall risk profile of the Bank and ensuring that the Bank is operating in compliance with the applicable national and international laws, regulations and standards (LIB Risk Management Program 2014). For the fact that the overall risk oversight role is responsibility of the board and the supervisory organ, the National Bank of Ethiopia, the Risk and Compliance Management Department is functionally accountable to board and periodically reports to the board and the National Bank of Ethiopia. Accordingly, the Department is responsible for:

- Proposing and reviewing Risk Management program of the Bank;
- Reviewing all Business units' policy and procedure of the bank from risk management perspective and forwarding to the board and executive management for incorporation;
- Developing Risk and Compliance management policies and procedures;
- Developing, proposing and reviewing risk appetite and limits for all risk types ;
- Preparing and submitting periodical risk and compliance reports to the Board/Loan Review and Risk Management Committee; and
- Proactively identifying all applicable national and international laws and regulations and ensuring the Bank's compliance accordingly.

4.2.4.4. Internal Audit Department

Similar to the Risk and Compliance Management function, the internal audit function is independent entity that oversees the overall risk management function to ensure the effectiveness of the process relating to credit and operational risk management. From perspectives of strengthening internal control and providing assurance to the board on smoothly functioning of the bank's operation, the Internal Audit Department is functionally accountable to board and periodically reports to the board and the National Bank of Ethiopia. In this regard, the Internal Audit is responsible to (LIB Internal Audit Charter 2012):

- Give assurance that credits have been granted in particular and credit process in general are in line with policy and procedure of the Bank;
- Periodically report audit findings to the Board Audit and provide same to the Risk and Compliance Management Department and the Executive Management;
- Provide independent assurance to the implementation of credit police and procedures on the ground; and
- Review the credit risk management process of the Bank.

4.2.5. Reporting and Oversight Process of the Board and its Committees in LIB

The information gathered from the key informants indicated that the Risk & Compliance Management and Internal Audit Departments as independent bodies oversee the overall operations of the bank to give assurance to the board whether management is functioning in accordance with the approved policies, procedures, and directives to manage inherent risks that could occur in the day to day activities or not. Thus, the departments independently assessing the risk management function reports to their respective board committees on quarterly basis and laterally submits the report to the Senior Executive Management for its rectification on the reported findings/irregularities pertinent to risk management. The departments equally submit the quarter reports to the National Bank of Ethiopia for its monitoring and supervision.

The Senior Executive Management after receiving the quarter report forwards the findings to pertinent organs of the Bank for their subsequent rectification and/or justifications for the reported findings. Then the organs submit their rectification reports within two weeks period of time to the Secretary of the Senior Executive Management/Policy Committee. The Secretary compiling and reviewing the rectification reports presents to the deliberation of the Policy Committee. Then the Policy Committee thoroughly deliberating on each of the findings provides suggestions and directions on the reported major findings for further rectification and simultaneously forewords the final Management's rectification report to the respective board committees within a week period of time for their review and endorsements and subsequent directions.

The Risk & Compliance Management and Audit Committees after receiving the Managements' rectification reports respectively summon the Senior Executive Management team and the Directors of the department together for a report and rectification report hearing. On this meeting the department directors separately presents their finding and observations on the irregularities against the Bank's own policies and procedures and against the NBE's directives to their respective committees. The Senior Executive Management on its part presents its rectification report and justifications on why and how the irregularities could occur and the subsequent remedial actions taken to rectify the observed irregularities. On the meetings the role of the Risk Management and Audit Committee are to maintain balance between the findings of the Departments and the rectification reports of Senior Executive Management. Then standing upon the reported major irregularities the Committee gives suggestions, directions and instructions to the Management for further correction and implementation. Meanwhile, the Committees give instructions for follow up and report for the next meeting on the proper implementation of the provided directions and instruction.

Then the Committees regularly update the Board about their activities at the earliest possible board meeting after each Committee meetings. The updates include the major irregularities observed during the quarter, the subsequent actions of the Management, and the directions and instructions given by the Committees to rectify the reported irregularities. It also incorporates any significant issues or concerns of the Committees that should be brought to the attention of the board.

Minutes of the meetings of the Policy Committee, the board committees and the Board are kept under the custody of the Board Secretary. Then, the Bank Supervision Directorate of the National Bank of Ethiopia regularly reviews the minutes and decisions of the board, the committees and the Senior Executive Management on quarterly bases. The NBE also conducts onsite and offsite examinations to oversee the overall risk management functions of the bank and rates the performance of the Management and the Board on a CAMEL rating basis. The CAMEL rating examines the Capital adequacy, Asset quality, Management (leadership efficiency), Earnings, and Liquidity position of the Bank and rates the overall condition of the Bank leveling composite rating from '1' to '5'. Composite rating '1' indicates strong performance and risk management practices that consistently provide for safe and sound operations; while composite rating '5' signifies unsatisfactory performance that is critically deficient and in need of immediate remedial attention of the supervisory organ (https://en.wikipedia.org/wiki/CAMELS_rating_system). Banks rated '5' are subject to frequent onsite examination by the supervisory organ, in our context the National Bank of Ethiopia.

4.2.6. The Role of LIB's Board of Directors In Risk Management

Risk management encompasses the scope of risk to be managed, the process/systems and procedures to manage the risk and roles and responsibilities of units/individuals involved in risk management (FSB, 2013). From this point of view the role of board of directors of LIB in risk management would basically be developing sound risk governance framework and setting appropriate risk appetite framework. Risk governance framework provides clearly defined roles, responsibilities, and reporting relationship of units involved in the risk management function throughout a bank.

The LIB's board has developed a risk governance framework supported with a Risk management Program that serves the board as a roadmap for risk management along with defined roles and responsibilities of units involved in risk management function (LIB Risk Management Program, 2014. Based on the program, the role of the Risk and Compliance Management Department in risk management is establishing processes to identify bank wide critical risks, risk capacity, risk appetite, risk tolerance, and risk limits to be approved by the board and implemented by the management and respective business units.

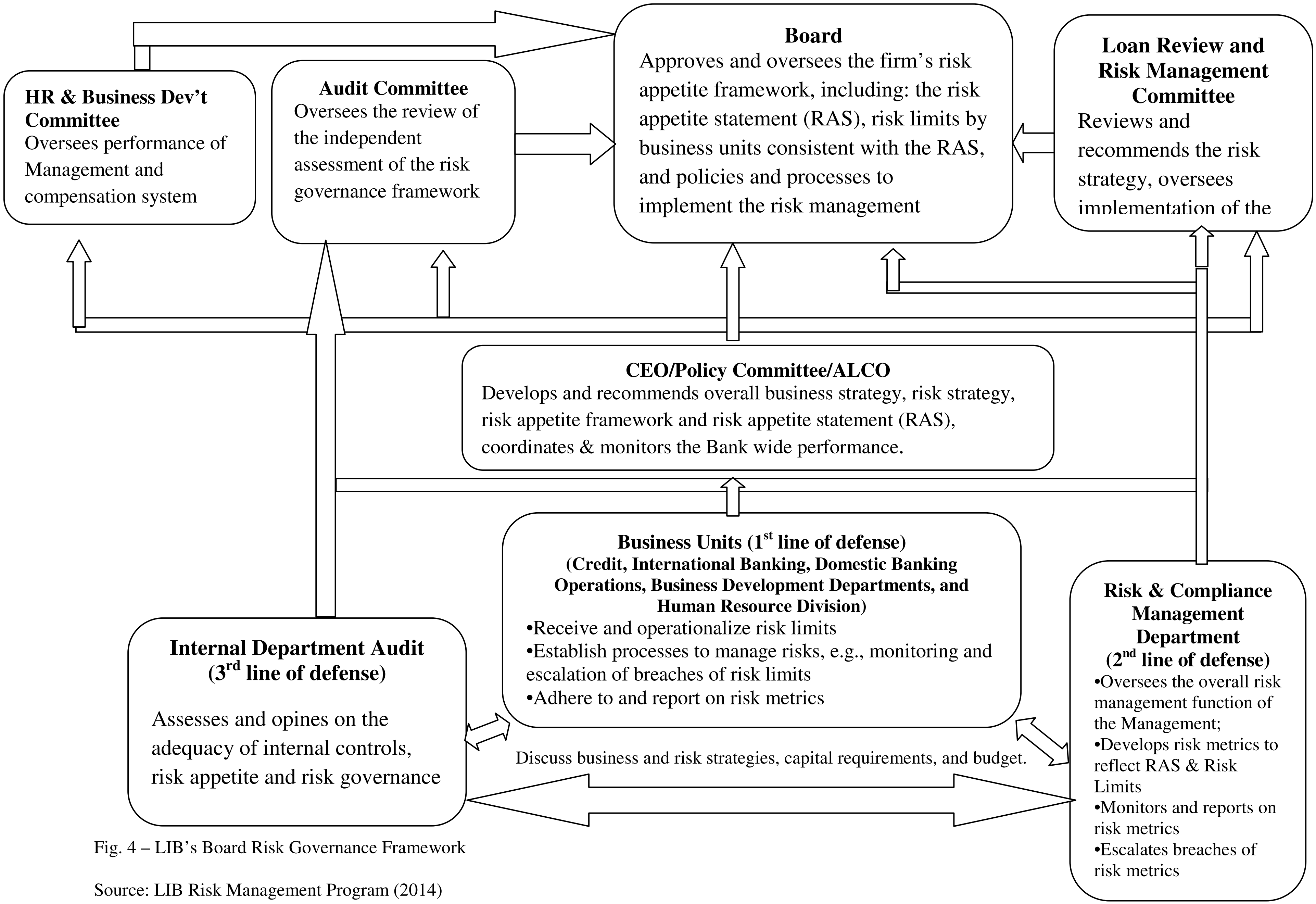


Fig. 4 – LIB's Board Risk Governance Framework

Source: LIB Risk Management Program (2014)

4.2.7. Risk Identification, Monitoring and Controlling Process of Limits in LIB

In the process of providing financial services commercial banks assume various kinds of financial risks. The risks contained in the bank's principal activities, those involving own balance sheet and basic business of lending and borrowing, are not all borne by the bank itself. In many instances banks eliminate or mitigate the financial risk associated with a transaction by proper business practices; in others words, they shift the risk to other parties through a combination of pricing and product design Santomero (1997). From risk management perspective, risks facing all financial institutions can be segmented into three separable types, these are:

(i) Risks that can be eliminated or avoided by simple business practices;

(ii) Risks that can be transferred to other participants; and

(iii) Risks that must be actively managed at the firm level.

In the first case, the practice of risk avoidance involves actions that proactively reduce the probability of occurrence of risk by standardization of process, contracts and procedures to prevent inefficient financial decisions. Risks can also be transferred to other participants through construction of portfolios that benefit from diversification across borrowers. Finally, risks can be actively managed at the firm level by implementation of incentive-compatible contracts with the institution's management to require that employees be held accountable (ibid).

The Department meticulously scrutinizing and analyzing the stated above factors and conducting stress testing upon the potential risk factors determines the risk capacity, risk tolerance and risk limits based on the capital, and expected return and previous loss exposures and approves by the board for implementation. The limit setting exercise begins with the clear understanding of the manifestation of risk taking and risk reward tradeoff or return. Thus, risks limits are set to enable the Bank to spread its exposure across individual borrowers, to enforce compliance with the bank’s diversification strategy and for board’s oversight and the supervisory organ’s control. Besides, setting and implementation of risk limits help the Bank to proactively avoid or transfer inherent risks actively manage unavoidable risks at the firm level. (See the Credit Risk limits, Liquidity risk, Liquidity risk limits and risk levels, Foreign exchange risk limits & ratios matrix, and Cash transactions limits in Appendix A)

4.2.8. Risk Monitoring and Controlling at LIB' Board

According to the respondent, once the risks are identified and risk limits are set the monitoring and controlling process follows based on the established policies, procedures, guidelines, limits, standards, and the NBE directives and requirements. Hence, the Risk & Compliance Management and Internal Audit Departments regularly oversee and assess the banking operation and risk management functions in light of the approved strategy, policy, procedures, limits, ratios and matrix, pertinent regulations and directives of the supervisory organ, and the clearly defined roles and responsibilities and foreign currency approval procedure. Then as instruments of monitoring and controlling, the Departments periodically, most often quarterly, report to the Risk Management and Audit Committees for their review, deliberation, and subsequent action and directions.

The reports mainly comprise of summary of findings and identified gaps that could show the level of risk exposure the Bank and concerns of the independent departments and issues require special attention of the board. Besides, periodic stress testing are conducted at different scenarios to assess the potential impact of a range of low probability and high impact severity circumstances on Bank's overall credit and liquidity risk profile. The stress testing is conducted:

- under different scenarios i.e. normal and stress situations;
- based on the regulatory requirements;
- under anticipated future strategy;
- in line with the approved, ratios, limits and matrices; and
- Based on sensitivity analysis.

4.2.9. Risk Communication & Disclosure of Information to LIB's Board

Ongoing communication about risk issues throughout the bank is a key principle of strong risk governance. Information should be communicated to the board and senior management in a timely, accurate and understandable manner so that they are equipped to take informed decisions; BCBS (1999). Due to the fact that, the informants said, the board and Senior Management are regularly informed by the quarterly Risk Management and Internal Audit Assessment reports that monitor the risk assumed by the bank against the pre-defined risk limits. In addition to that, the board and senior management are frequently communicated and updated on trends and current progress of the bank's operation in light of risk management. Periodic performance reports, external audit reports, and other correspondence from the regulator are also consistently communicated to the board. In this regards, the Departments all the time watch over the major inherent risks are within the acceptable limit; and when there is a situation where excessive risk exposure observed in a certain portfolio, they recommend for a board to take measures such as either to revise the limit or restrict the risk exposure of that particular portfolio based on careful examination of risk-reward trade off. Hence, information reported with regard to risk appetite will undoubtedly help the board to optimize risk-reward trade off thereby ensuring the profitability and sustainable growth of the Bank.

4.2.10. The Role of the National Bank of Ethiopia (NBE)

The National Bank of Ethiopia is a regulatory for commercial banks in Ethiopia established by a proclamation entrusted to monitor and ensure the safety, soundness, and stability of the Banking System in Ethiopia Among the authority that the NBE vested on is enacting and implementing regulations and directives, carrying out supervision, conducting off-site and on-site monitoring and examinations on banks' financial trends and other actions taken by bank management that could affect the banks' financial conditions (http://nbe.gov.et/history.html).

According to the key informants, the NBE sets various directives, circulars, and guidelines to regulate the financial condition of bank in Ethiopia. Besides, the NBE is responsible to approve the bank's risk programs and review the adequacy of implementation of the risk management program of bank's through off-site analysis and on-site examinations. The bank's risk management guidelines that the NBE put into practice enables it to guide the risk-based supervision and promote safety and soundness of the banking system.

The NBE also conducts onsite and offsite examinations to oversee the overall risk management functions of the bank and rates the performance of the Management and the Board on a CAMEL rating basis. The CAMEL rating examines the Capital adequacy, Asset quality, Management (leadership efficiency), Earnings, and Liquidity position of the Bank and rates the overall condition of the Bank leveling composite rating from ‘1’ to ‘5’.

As earlier discussed, composite rating ‘1’ indicates strong performance and risk management practices that consistently provide for safe and sound operations; while composite rating ‘5’ signifies unsatisfactory performance that is critically deficient and in need of immediate remedial attention of the supervisory organ. Banks rated ‘4’ and ‘5’ are subject to frequent onsite examination most probably on every six months basis by the supervisory organ. Under normal circumstances, in the context of the National Bank of Ethiopia, banks are examined every 12 to 18 months, where the bank’s financial condition is rated insufficient it may subject to frequent onsite examination till the conditions get improved. In this case, LIB’s financial condition is rated ‘3’ and ‘2’; thus, on the eyes of the supervisory organ the bank’s risk exposure and compliance with laws and regulations is in a safe position.

4.3. Analysis of Questionnaire

In this five scale measure - Likert’s scale approach questions categorized in seven broad issues related to risk management function were prepared for respondents. Analysis of the responses to the questionnaire in Likert’s scale has been presented as follows. The mean of the respondents’ scale and standard deviations from the mean of each question has been calculated by SPSS. To summarize the scale of each category the weighted mean and weighted standard deviation has been calculated for consideration.

1	**Composition**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
1.1	The board consists of a workable number (size) of board members to function effectively as a team.	53		2	2	44	52	4.5	0.64	**4.29**	**0.668**
1.2	The board has the right blend of skills, experience and appropriate degree of diversity of knowledge relevant to the board's tasks and the bank's operations.	53		2	2	68	28	4.3	0.56		
1.3	There is transparent and clear structure that defines roles and responsibilities, functions and relationship between board members, the President, and the senior management.	53		7		60	33	4.2	0.81		
2	**Overall responsibilities**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
2.1	The Bank has sufficient definition and documentation concerning the role and responsibilities of the board for risk governance.	53		8	17	67	8	3.8	0.71	**4.05**	**0.594**
2.2	The board approves the Bank's strategic plan (e.g. risk tolerance, risk appetite, risk limits, and business strategy).	53			17	54	29	4.1	0.68		
2.3	The board oversees senior management's implementation of the Bank's strategic plan.	53		8	19	60	13	3.8	0.78		
2.4	The board approves and oversees the implementation of the Bank's policies for risk and compliance relating to risk management.	53			8	75	17	4.1	0.49		
2.5	The board approves and oversees the implementation of the Bank's capital adequacy assessment process, capital and liquidity pans, compliance policies and obligations, and the internal controls system.	53				79	21	4.2	0.41		

2.6	The board formulates and defines the mandate and responsibilities of board-level committees dealing with risk governance.	53			8	69	23	4.2	0.54		
2.7	The board in discharging its responsibilities takes into account the legitimate interests of depositors, shareholders and other relevant stakeholders and ensures that the Bank maintains an effective relationship with its supervisory organs.	53				54	46	4.5	0.50		
2.8	The Bank's (senior executive management's) responses show that the role and responsibilities of the board are practically implemented in an appropriate and effective manner.	53		10		86	4	3.9	0.64		
3	**Board Committees Responsibilities**										
3.1	**The Board**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
3.1.1	The board has the right blend of skills, experience and appropriate degree of diversity of knowledge relevant to the board's tasks and the bank's operations.	53			17	62	21	4.0	0.63		
3.1.2	The board deliberates well on and approves the Bank's strategic plan (e.g. risk tolerance, risk appetite, risk limits, and business strategy).	53			8	69	23	4.2	0.54		
3.1.3	The board oversees senior management's implementation of the Bank's strategic plan.	53				71	29	4.3	0.46	**4.19**	**0.486**
3.1.4	The board approves and oversees the implementation of the Bank's policies for risk and compliance relating to risk management.	53				63	37	4.4	0.49		
3.1.5	The board approves and oversees the implementation of the Bank's capital adequacy assessment process, capital and	53				88	12	4.1	0.32		

	liquidity pans, compliance policies and obligations, and the internal controls system.										
3.2	**Board Risk Management Committee**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
3.2.1	The board explicitly defines and documents the role and responsibilities of the risk committee.	53			40	50	10	3.7	0.64	**3.97**	**0.540**
3.2.2	The risk committee is a self-standing committee.	53		2	8	71	19	4.1	0.59		
3.2.3	The risk committee reports and advises the board on the Bank's overall current and future risk tolerance/appetite and strategy.	53			17	67	16	4.0	0.58		
3.2.4	The risk committee ensures the strategic plans covered by the risk committee include those for capital and liquidity management, as well as for credit, market, operational, compliance, reputational and other risks of the Bank.	53			11	79	10	4.0	0.46		
3.2.5	The risk committee oversees senior management proper implementation of the strategic plan.	53			10	79	11	4.0	0.46		
3.2.6	The risk committee discusses the Banks' material risks on both an aggregated basis and along with the types of risks borne by Banks (e.g., credit risk, market, liquidity, operational risks).	53			10	67	23	4.1	0.56		
3.2.7	The management's responses show that the role and responsibilities of the risk committee are practically implemented in an appropriate and effective manner.	53			12	77	11	4.0	0.49		

3.3	Board Audit Committee	Respondents	Strongly Disagree (%)	Disagree (%)	Neutral (%)	Agree (%)	Strongly Agree (%)	Mean	Std. Dev.	Wtd. Mean	Wtd. Std. Dev
3.3.1	The board explicitly defines and documents the role and responsibilities of the audit committee.	53			15	56	29	4.1	0.66	**4.06**	**0.564**
3.3.2	The audit committee is a self-standing committee.	53			25	51	23	4.0	0.71		
3.3.3	The audit committee reports and advises the board on the Bank's overall financial reporting process and the internal control process.	53				69	31	4.3	0.47		
3.3.4	The audit committee reviews and approves the audit scope and frequency.	53			25	69	6	3.8	0.53		
3.3.5	The audit committee receives key audit reports and ensures that the senior management is taking necessary corrective actions in a timely manner to address control weaknesses, non-compliance with policies, procedures, laws and regulations, and other problems identified by auditor and other control functions.	53			10	73	17	4.1	0.52		
3.3.7	The management's responses show that the role and responsibilities of the audit committee are practically implemented in an appropriate and effective manner.	53			12	74	14	4.0	0.51		
4	**Board Process**										

4.1	Commitment	Respondents	Strongly Disagree (%)	Disagree (%)	Neutral (%)	Agree (%)	Strongly Agree (%)	Mean	Std. Dev.	Wtd. Mean	Wtd. Std. Dev
4.1.1	Board members regularly attend board meeting and make informed decisions	53				67	33	4.3	0.47	**4.03**	**0.510**
4.1.2	Board members come to meetings well prepared for the agenda items and actively participate in discussions.	53			21	66	11	3.9	0.57		

4.1.3	The board pays appropriate follow up and monitoring on proper implementation of its decisions.	53		8	19	69	4	3.7	0.67		
4.1.4	Board members make heated debates on agenda items; and conflicts of interest that occur in decision making are amicably solved by the procedure of voting.	53			8	77	15	4.1	0.48		
4.1.5	Board members critically examine proposals initiated by the management.	53				86	14	4.1	0.36		
4.2	**Strategic participation role**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
4.2.1	The board understands well the bank's business and operations environment.	53			2	62	36	4.4	0.52		
4.2.2	The board actively involves in long term strategic planning process and goals coping with changes in the external environment.	53				79	21	4.2	0.41	**4.20**	**0.461**
4.2.3	The board demonstrates awareness of emerging environmental trends affecting the bank.	53			2	85	13	4.1	0.38		
4.2.4	The board considers strategic approaches in the decision making process.	53			10	71	19	4.1	0.53		
4.3	**Advisory role**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
4.3.1	The board provides support and advise to the senior executive management whenever deemed necessary	53			8	77	15	4.1	0.48		
4.3.2	The board contributes to major market (business) and technology issues affecting the bank.	53			19	60	21	4.0	0.64	**4.07**	**0/568**
4.3.3	The board provides proper advice direction regarding achieving strategic goals.	53			12	65	23	4.1	0.58		

4.4	Control role	Respondents	Strongly Disagree (%)	Disagree (%)	Neutral (%)	Agree (%)	Strongly Agree (%)	Mean	Std. Dev.	Wtd. Mean	Wtd. Std. Dev
4.4.1	Management regularly reports on key performances and targets that flow directly from the strategy.	53				85	15	4.2	0.36	**4.16**	**o.586**
4.4.2	The board is regularly kept informed on the financial and operational positions of the bank.	53			9.6	46.2	44.2	4.4	0.65		
4.4.3	The board actively monitors and evaluates implementations of strategic decisions and key targets.	53		8	4	65	23	4.0	0.77		
4.4.4	The board critically reviews performance against strategic plan.	53			21	52	27	4.1	0.70		
4.4.5	The board monitors top management in decision making.	53			2	77	21	4.2	0.45		
5	**Oversight of senior management**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
5.1	The board provides oversight of senior management and holds members of senior management accountable for their actions.	53			10	59	30	4.2	0.61	**4.04**	**0.641**
5.2	The board monitors that senior management's actions are consistent with the strategy, policies, and procedures approved by it and the regularly requirements.	53			21	64	15	4.0	0.61		
5.3	The board critically questions and reviews explanations and information provided by senior management.	53			2	65	33	4.3	0.51		
5.4	The board ensures that senior management's knowledge and expertise remain appropriate given the nature of the business and the bank's risk profile.	53		8	27	55	10	3.7	0.76		

5.5	The board ensures that appropriate succession plans are in place for senior management positions.	53			23	48	29	4.1	0.73		
6	**Compensation**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
6.1	The board established a compensation system of the bank and regularly monitors and reviews outcomes to ensure the bank-wide compensation system is operating as intended.	53		8	35	55	2	3.5	0.67	3.42	o.800
6.2	The board approved the compensation of senior executives, including the President, and oversees management's development and operation of compensation policies, systems and related control processes.	53			58	25	17	3.6	0.77		
6.3	The board thinks the compensation structure of the bank promotes long term performance and be in line with the business and risk strategy, objectives, values and long-term interests of the bank.	53		9	50	32	9	3.4	0.77		
6.4	The board thinks the remuneration structure of the bank is sufficient enough to motivate, attract, and retain qualified management and the staff to attain better performance.	53		35	19	40	6	3.2	0.99		
7	**Internal audit**	**Respondents**	**Strongly Disagree (%)**	**Disagree (%)**	**Neutral (%)**	**Agree (%)**	**Strongly Agree (%)**	**Mean**	**Std. Dev.**	**Wtd. Mean**	**Wtd. Std. Dev**
7.1	The bank has an internal audit function that undertakes, on a regular basis, an independent assessment of the bank's risk governance framework and risk management policies and processes at the enterprise level and/or for selected revenue-generating business units.	53			19	60	21	4.0	0.64	**4.13**	**0.642**
7.2	The internal audit function reports directly to the board or a board-audit committee from an organizational perspective and with regards to findings.	53				60	40	4.4	0.50		

7.3	The bank's board audit committee and senior management review internal audit reports and prudential reports as part of the bank's risk governance framework.	53				67	33	4.3	0.47		
7.4	The bank's board and senior management monitors the timely rectification of weaknesses identified through the independent assessment of the risk governance framework and underlying functions.	53		8		63	29	4.1	0.77		
7.5	The bank has a process to evaluate the effectiveness of the independent assessment of its risk governance framework.	53		8	25	50	17	3.8	0.83		

Source: Deloitte Development LLC (2014)

Note: *the issues in the questionnaire were discussed in a working paper of the Deloitte Development LLC to indicate the responsibilities of the board and other pertinent bodies involved in bank risk management. then adopted and developed into a questionnaire format by the researcher.*

4.3.1 Composition

Regarding composition of the LIB's board 52% of the respondents strongly agree and 44% agree that the board consists of a workable number (size) to function effectively as a team while 2% remain neutral and disagree respectively. Besides, 96% of the respondents agree and strongly agree that the board has the right blend of skills, experience and appropriate degree of diversity of knowledge relevant to the board's tasks and the bank's operations, while 2% remained disagree and 2% indifferent respectively. Furthermore, 90% of the respondents agree and strongly agree that the board has transparent and clear structure that defines roles and responsibilities, functions and relationship between board members, the President (CEO), and the senior management, while 8% and 2.0% remained disagree and neutral respectively. The calculated weighted mean of the responses for the three questions in the 5 scale - Likert's scale was 4.3 and weighted standard deviation from the mean was 0.67. Since, the weighted standard deviation from the mean is close to zero that tells that the mean is reliable and the volatility is little. Thus, respondents' data indicate that the composition of the board has workable size, right blend of skills, experience and well defined structure is reliable and consistent. The data gathered from documents also support the results of the respondents.

4.3.2 Overall Responsibilities of LIB's Board

Concerning overall responsibility of the LIB's board, 8% of the respondents strongly agree and 67% agree that the Bank has sufficient definition and documentation concerning the role and responsibilities of the board for risk governance, while 8% disagree and 17% remained neutral. In relation to risk oversight, 83% of the respondents agree and strongly agree that the board approves the Bank's strategic plan, risk tolerance, risk appetite, risk limits, and business strategy, and the 17% are neutral. Besides, 73% said they agree and strongly agree that the board oversees senior management on proper implementation of the Bank's strategic plan, and the 19% are in neutral position in this regard while the 8% disagree.

Besides, 92% said that they agree and strongly agree that the board approves and oversees the implementation of the Bank's policies for risk and compliance relating to risk management, while the rest remained neutral. In the meantime, 79% agree and 21% strongly agree that the board approves and oversees the implementation of the Bank's capital adequacy assessment process, capital and liquidity pans, compliance policies and obligations, and the internal controls system.

Pertaining formulation and setting defined responsibilities, 92% of the respondents agree and strongly agree that the board formulates and defines the mandate and responsibilities of board-level committees dealing with risk governance, and the remaining 8% said they are neutral. Besides, 100% of the respondents agree and strongly agree that the board, in discharging its responsibilities, takes into account the legitimate interests of depositors, shareholders and other relevant stakeholders and ensures that the Bank maintains an effective relationship with its supervisory organs. Similarly, 90% of the respondents said they agree and strongly agree that the Bank's (senior executive management's) responses show that the role and responsibilities of the board are practically implemented in an appropriate and effective manner, and the rest of the respondents said they do not agree with this statement.

To summarize, the calculated weighted mean score to the above questions was 4.1 and the weighted standard deviation 0.59 indicating that, as the weighted standard deviation from the mean is closer to zero, the board soundly discharges its overall responsibility in the corporate governance and risk management of the Bank. Besides, the responses of respondents seem consistent with the overall responsibilities indicated in the board's charter.

4.3.3 LIB's Board Oversight Role on Its Committees

4.3.3.1 Risk Management Committee

Concerning the board's oversight role on Risk Management Committee, 60% of the respondents said they agree and strongly agree that the board explicitly defines and documents the role and responsibilities of the risk committee, while 40% said they are neutral. Besides, the 90% believe that the Risk Management Committee is a self-standing committee, while 8% remain neutral and 2% of the respondents do not believe that the committee is self standing committee. Regarding the relationship of Risk Management Committee and the board, 93% agree and strongly agree that the risk committee reports and advises the board on the Bank's overall current and future risk tolerance/appetite and strategy, and 17% of the respondent said they are neutral.

Moreover, 88% of the respondents agree and strongly agree that the risk management committee ensures the strategic plans covered by the risk committee including capital and liquidity management, as well as for credit, market, operational, compliance, reputational and other risks of the Bank, and the rest 12% remained neutral. In relation to overseeing the functions of the senior management, 90% of the respondent said they agree and strongly agree that the Committee oversees senior management proper implementation of the strategic plan, while the 10% of the respondents remained neutral. In addition, 90% of the respondent agree and strongly agree that the Committee discusses the Banks' material risks on both an aggregated basis and along with the types of risks borne by Banks (e.g., credit risk, market, liquidity, operational risks) and the 10% remained neutral. The calculated composite mean of the scale scored 4.0 and the composite standard deviation 0.54 signifies the board has strong oversight role over the Risk Management Committee's functions. But, for the fact that significant number of respondents remained neutral, this signifies that the board requires improving disclosure of information to the employees on how it is overseeing its committees to in the risk management function.

4.3.3.2 Audit Committee

Regarding board's oversight role on Audit Committee, 85% of the respondents agree and strongly agree that the board explicitly defines and documents the role and responsibilities of the audit committee, while 15% remained neutral. Besides, 75% of the respondents agree and strongly agree that the audit committee is a self-standing committee, and the 25% are neutral. In relation to reporting process, 69% of the respondents strongly agree and 31% agree that the audit committee reports and advises the board on the Bank's overall financial reporting process and the internal control process.

Concerning the board's responsibility on reviewing the audit committees' scope, 75% of the respondents agree and strongly agree that the audit committee reviews and approves the audit scope and frequency of audit assessments, and 25.0% remained neutral. Moreover, 90% of the respondents agree and strongly agree that the audit committee receives key audit reports and ensures that the senior management is taking necessary corrective actions in a timely manner to address control weaknesses, non-compliance with policies, procedures, laws and regulations, and other problems identified by auditor and other control functions, while 10% of the respondents remained neutral in responding to the question. Regarding LIB board's oversight role on the Audit Committee the calculated mean scale was 4.06 and the weighted standard deviation 0.56 that indicates good performance.

4.3.3.3 Human Resources and Business Development (Compensation) Committee

Pertaining the compensation system, 2% of the respondents strongly agree and 56% agree that the board has established a compensation system of the bank and regularly monitors and reviews outcomes to ensure the bank-wide compensation system is operating as intended, while 8% of the respondents disagree with the statement and 34% remained neutral. In relation to approval of the compensation of senior executives, including the President, and oversees management's development and operation of compensation policies, systems and related control processes, 42% of the respondents agree and strongly agree with the statement; while 58% remained in neutral. Moreover, 40% of the respondents agree and strongly agree that the board thinks the compensation structure of the bank promotes long term performance and be in line with the business and risk strategy, objectives, values and long-term interests of the bank; the majority of the respondents 51% were indifferent while 9% disagree with the statement. Concerning remuneration structure, 46% of the respondents said they agree and strongly agree that the board thinks the remuneration structure of the bank is sufficient enough to motivate, attract, and retain qualified management and the staff to attain better performance; while 35 % disagree and 19% remained neutral. Pertaining compensation, comparing to other questions above, the responses of the respondents are highly inclined to scales of neutral and disagree; the composite mean was also calculated to be 3.4 and the composite standard deviation was a little bit higher 0.80 indicating that there needs improvement in that regard.

4.3.4 LIB's Board Process:

4.3.4.1 Commitment

Concerning commitment of board members, 67.3% of the respondents agree and 33% strongly agree that the board members regularly attend board meeting and make informed decisions. In addition, 77% of the respondents agree and strongly agree while 21% remain neutral that the board members come to meetings well prepared for the agenda items and actively participate in discussions. Pertaining monitoring and follow up, 73% of the respondents agree and strongly agree that the board pays appropriate follow up and monitoring on proper implementation of its decisions, and 8% of the respondents disagree with the statement while19% remained neutral. Moreover, 92% of the respondents agree and strongly agree that board members make heated debates on agenda items; and conflicts of interest that occur in decision making are amicably solved by the procedure of voting, while 8% remained neutral. The calculated composite mean was 4.0 and composite standard deviation 0.51 indicating that there is good commitment on board members.

4.3.4.2 Strategic Participation Role

With regard Strategic participation role of the board, 98% of the respondents agree and strongly agree that the board understands well the bank's business and operations environment; and 2% respondents are neutral. Besides, 79% of the respondents agree and 21% strongly agree that the board actively involves in long term strategic planning process and goals coping with changes in the external environment. In relation to awareness, 98% of the respondents agree and strongly agree that the board demonstrates awareness of emerging environmental trends affecting the bank; and 2% of the respondents remain neutral. Moreover, 90% of the respondents agree and strongly agree that the board considers strategic approaches in the decision making process; while 10% respondents are neutral. The composite mean regarding strategic participation role of the board is 4.2 and the weighted standard deviation 0.46 indicating that there is an encouraging participation role on strategic issue.

4.3.4.3 Advisory Role

Pertaining advisory role of the board, 92% of the respondents agree and strongly agree that the board provides support and advice to the senior executive management whenever deemed necessary; while 8% respondents are neutral. What's more, 81% of the respondents said they agree and strongly agree that the board contributes to major market (business) and technology issues affecting the bank; and 19% of the respondents remain neutral. And 88% of the respondents agree and strongly agree that the board provides proper advice direction regarding achieving strategic goals; while 12% remained neutral. The calculated mean was shown as 4.1 and composite standard deviation 0.57 pointing out that the board, as a corporate leadership, is providing an advisory role to the management.

4.3.4.4 Control Role

In relation to control, 85% of the respondents agree and 15% strongly agree that Management regularly reports to the board on key performances and targets that flow directly from the strategy; and 90% of the respondents agree and strongly agree that the board is regularly kept informed on the financial and operational positions of the bank, while 10% remained neutral. Moreover, 88% of the respondents agree and strongly agree that the board actively monitors and evaluates implementations of strategic decisions and key targets; and 8% and 4% of the respondents remained disagree and neutral respectively. The composite mean for the control aspect was 4.2 and composite standard deviation 0.59 indicating that the board is exerting providing good control role over the management.

4.3.5 Oversight of Senior Management

In relation to overseeing the senior management, 90% of the respondents agree and strongly agree that the board oversees the senior management and holds members of senior management accountable for their actions; while 10% remained neutral. Further, 79% of the respondents agree and strongly agree that the board monitors that senior management’s actions are consistent with the strategy, policies, and procedures approved by it and the regularly requirements, while 21%

remained neutral. In addition, 98% of the respondents agree and strongly agree that the board critically questions and reviews explanations and information provided by senior management, whilst 2% remained neutral. Moreover, 65% of the respondents agree and strongly agree that the board ensures that senior management's knowledge and expertise remain appropriate given the nature of the business and the bank's risk profile, while 27% and 8% remained neutral and disagreed. In addition, 77% of the respondents agree and strongly agree that the board ensures that appropriate succession plans are in place for senior management positions, and 23% remained neutral. The composite mean for the board's oversight role on senior management was 4.0 and composite standard deviation 0.64 indicating that the board is properly overseeing the senior management's actions towards risk management of the bank.

4.3.6 Internal Audit

Pertaining Internal Audit as a critical function for risk management, 81% of the respondents said the bank has an internal audit function that undertakes, on a regular basis, an independent assessment of the bank's risk governance framework and risk management policies and processes at the enterprise level and/or for selected revenue-generating business units, and 19% remained neutral. Besides, 60% and 40% of the respondents agree and strongly agree respectively that the internal audit function reports directly to the board or a board-audit committee from an organizational perspective and with regards to findings. Meanwhile, 60% and 40% of the respondents agree and strongly agree respectively that the bank's board audit committee and senior management review internal audit reports and prudential reports as part of the bank's risk governance framework. Moreover, 92% of the respondent said the bank's board and senior management monitors the timely rectification of weaknesses identified through the independent assessment of the risk governance framework and underlying functions, and 8% remained neutral. Further, 67% of the respondents agree and strongly agree that the bank has a process to evaluate the effectiveness of the independent assessment of its risk governance framework, and 25% of the respondents remain neutral while 8% disagree with the statement. The calculated composite mean was shown as 4.1 and the composite standard deviation 0.64 which signifies the internal audit functions and undertakes a risk management function as an instrument to the board.

4.4. Analysis of Close Ended Questions and Interview Questions

As part of the questionnaire, close ended questions were prepared on some issues that require opinions of the respondents (nine board members and 44 management staff at various levels). In the close ended questions the respondents were asked the following questions so tat to assess their opinions regarding training, awareness, average time the board and management spend on risk management issues as agenda, and other related issues. Besides, interviews were conducted with key informants. Analysis of the data and responses to the close ended questions and interviews has been presented as follows:

- Educational qualification - among the nine respondent board members the six have MA degree and the three have BA in variety of fields of study; and among the44 employees (including Senior, Middle, and line Managers) the 32 have BA degree & 8 MA degree.

Qn. Have you ever had training on issues related to risk management and governance provide by the Bank or other institutions?

Training	No. of Resp.		Three times		Two times		At least once		Never ever	
	Board	Staff	Board	Staff	Board	Staff	Board	Staff	Board	Staff
Training on Risk Management provided by Lion International Bank	9	44	22%		22%	27 %	44%		11%	73 %
Similar trainings on the subject provided by any organization other than Lion International Bank					78%	55 %			22%	45 %

Table 2: training

Qn. Is the board/Management well aware of risk management requirements expected from the Bank?

Awareness	No. of Resp.		Board	Staff
	Board	Staff		
They personally and as a board/management team are aware of the risk management requirements expected from them and the bank.	9	44	78%	64%
They are aware for themselves, but are hesitant about few board/management members.	9	44	22%	36%

Table 3: awareness

Qn. How much time does the board/management spend on average over the last one year on risk management issues in terms of percentage?

Average Time Spend	No. of Resp.		0 to10%		11% to 20%		21% to 40%		>60%		indifferent	
	Board	Staff	Board	Staff	Board	Staff	Board	Staff	Board	Staff	Board	Staff
Average time that the board/management spend on issues related to risk management agenda in terms of percentage:	9	44	44%	18%	11%	18%	33%	36%		2%	11%	25%

Table 4: average time

Qn. How do you rate the degree (frequency) of appearance of risk management agenda on management meetings?

Rating the frequency	No. of Resp.		High		Medium		Low	
	Board	Staff	Board	Staff	Board	Staff	Board	Staff
Rating the degree (frequency) of appearance of risk management issues as agenda on board/management meetings	9	44	22%	45%	56%	45%	22%	9%

Table 5: Frequency

Qn. Is the Management provided with relevant and up-to-date economic, business and market data for decision?

Disclosure of relevant information	No. of Resp.		Board	Staff
	Board	Staff		
the board/management is provided with necessary information	9	44	78%	36%
the board/management is provided with necessary information, but not in complete way	9	44	22%	55%
the board/management is provided with necessary information, but not frequently (it is rarely)	9	44		9%

Table 6: disclosure

Regarding training, as depicted on the table 11% of the board members and 73% of the staff have never ever taken training on risk management issues provided by the bank; and 44%of the board members have taken training for only one time. On the other hand 78% of the board members have taken such training for two times from other training institutions. This indicates that though there is exposure of training and understanding on risk management issues on the board side, but there is lack of such exposure on the staff side. From the point view of risk governance framework, it is the staff that plays a first line of defense role in risk management function. In this regard the responses suggest that there is a gap in training and probably clarity of understanding on risk management on the first line defense players. The NBE's corporate Governance Directive SBB62/2015 stipulates banks to provide training to board members and pertinent staff at least for once a year.

In relation to awareness of the board/management on risk management requirements expected from the bank, 78% of the board members and 64% of the staff responded that they personally and as a board/management team are aware of the risk management requirements expected from them and the bank; while 22% of the board members and 36% of the staff responded they are aware for themselves, but hesitant about few of the board/management members. Comparing the responses with the above training gaps it seems in consistent. However, the responses suggest though there is awareness among the board members and the staff, but the bank requires further enhancing the collective awareness of the role players in risk management of the Bank.

Concerning the average time the board/management spend on risk management issues as agenda over the last one year 44% of the board members and 18% of the staff rated 0 to 10%, and 11% of the board members and 18% of the staff rated 11 to 20%, while 33% of the board members and 36% of the staff rated 21 to 40%, and 11% of the board members and 25% of the staff remained in deferent. As the responses indicate there is diversified opinion regarding the average time devoted to risk management issues as agenda. From the ratings, one could observe that though diversified ratings the maximum average time devoted to the issue is between 21% and 40% of the other agendas. This may signifies that the lack of awareness on risk management issue to devote the board/management less time on the agenda.

Regarding rating the frequency of appearance of risk management agenda on board/management meetings, 22% of the board members and 45% of the staff rated high, and 56% of the board members and 45% of the staff rated medium, while 22% of the board members and 9% of the staff rated low. The rating suggests that the highest point is rated to medium in appearance of risk management agenda on board/management meetings.

In relation to disclosure of relevant and up-to-date economic, business and market data for decision, 78% of the board members and 36% of the staff responded that the board/management is provided with necessary information, and 22% of the board members and 55% of the staff responded the board/management is provided with necessary information, but not in complete way; while 9% of the staff responded the board/management is provided with necessary information, but not frequently (it is rarely). In this regard majority of the board members agree that the board/management is provided with necessary information for decision making; while majority of the staff are uncertain that the board/management is provided with necessary information, frequent and in complete form.

Concerning the analysis of interviews conducted with key informants regarding Risk Governance Framework and Risk appetite Framework; the respondents briefly elaborated that:

> *"The board as a governing body has established risk governance framework structuring itself into subcommittees and organizing the Risk & Compliance Management and Internal Audit Departments that meticulously oversee and identify the risk factors that occur in the day to day operations of the bank and report to the board for its subsequent actions and direction. Besides, the board has approved the bank's risk appetite framework, set risk appetite statement, and risk limits in consideration to the bank's risk tolerance capacity and the appetite to entertain maximum risk. Moreover, the President, as delegated from the board and entrusted with roles and responsibilities to manage the risks involve during operation, has established Policy and Asset/Liability Committees that provide support to the board to set corporate strategy that is consistent with the risk appetite and establish appropriate controls, policies, and reporting process. It has also organized business units that receive and operationalize risk limits, set up process to identify and manage emerging risk issues and their potential impact on the compliance with the risk appetite and report on the risk merits."*

Concerning Risk Identification, Monitoring and Reporting, the informants said:

"The LIB's Risk and Compliance Management Department identifies risks inherent to the banking business that could severely affect earnings and capital base of the bank, based on the magnitude of loss exposure of each risk. Hence, the bank mainly indentified such major risks as: credit risk, liquidity risk, interest rate risk, foreign exchange risk, and operational risks. Thus, the RCMD monitors the developments of risk factors in each of the foregoing indentified risks through careful assessment on risk factors that affect the level of emergence of potential risks like change on:

- *external environment, such as macroeconomic environment, changes in regulatory and other legal requirements;*
- *Level and direction of early warning ratios such as non-performing loans (NPLs) to deposit ratio, liquidity ratio, effective interest rate, exchange rate movements;*
- *Compliance to regulatory requirements;*
- *Concentration in loan portfolio as well as funding sources; and*
- *Impact of stress testing on asset quality and funding sources of the bank.*

The responses of the key informants indicates that the board has established risk governance framework and set reporting relationship mechanisms to implement the risk identification, monitoring, controlling, and reporting system.

CHAPTER FIVE

5 DISCUSSION , CONCLUSION, AND RECOMMENDATION

This chapter discusses about the data and facts gathered through interview, questionnaire, and personal observations in view of the theories and practices discussed in chapter two. This chapter may reflect the belief and stand point of the researcher. Important points discussed here could help fill the observed gaps in the LIB's board oversight role in the corporate governance and risk management functions of the Bank.

5.1. Discussion

As discussed in chapter two, various scholastic definitions on corporate governance have highlighted it as an imperative instrument for banks in identifying their strengths in risk management. Risk taking is an inherent element to banking activities Alexandera, B (2012). Profits are rewards for successful risk taking and the reverse is true that poorly managed risks can lead to distress and failures. Thus, in response to the inherent and multifaceted banking risks, banks need implementing effective risk management practices that constitute an integral part of corporate governance that play an active role in maintaining sound financial stability. Corporate governance includes having capable board of directors with appropriate composition, experienced management, coherent and clear lines of responsibility and accountability among work units and individuals in organization.

Based on the definitions of corporate governance and risk management, the researcher has attempted to analyze the role of LIB's board of directors in ensuring corporate governance and risk management in light of the Basel Committee for Banking Supervision (BCBS) and the National Bank of Ethiopia's Bank Corporate Governance Directive and Bank Risk Management Guidelines. To begin with the board qualification and composition, the NBE's Bank Corporate Governance Directive No SBB/62/2015 article 5.1 and 5.2 dictates that a bank shall have at least nine directors and may preferably comprise of directors who as a group provide a mixture gender and core competencies such as banking, finance, legal, business administration, audit, and etc. And, the NBE directive no SBB/54/2012 article 5.1.1 suggests at least 75% of bank board members to hold a minimum of first degree or equivalent from recognized higher learning institution. Moreover, the Basel Committee for Banking Supervision (BCBS) Principles of Corporate Governance advises bank board members to be qualified, individually and collectively, for their positions. From these perspectives, the researcher found the board of Lion International Bank qualifies both the international standards and the NBE requirements for it has workable size that comprised of 11members (10 men and one woman), which is above the minimum requirement. Pertaining educational qualifications 73% of the board members hold MA degree and above with related fields of study and 27% are with BA degree. Besides, the calculated weighted mean score regarding composition of the board that gathered from respondents' on the questionnaire has shown 4.3 that indicates the board, though has slight mixture of gender, consists of a workable size, right blend of skills with appropriate degree of diversity of knowledge and experience relevant to the board's task and the bank's operation.

One thing that goes in line with composition and qualification is that the board's awareness and understanding on the concept of corporate governance and risk management so that they can properly carryout the oversight role. In this regard, the SBB/62/2015 article 10.2.2 requires banks to provide training to directors at least once in a year on priority basis in areas of financial analysis, corporate governance, applicable laws, regulations, directives, risk management, and internal control. In this respect, the data collected from board members revealed that 44 % of the board members have taken at list two trainings on risk management organized by the bank, while the remaining 44% have taken at least one and 11% none. Besides, 78% of the board members think that they, personally and as a board, are aware of the risk management requirements expected from them and the bank as well; while the 22% think that they are aware for themselves but hesitant about few board members. Similarly, only 27% of the employees have taken training on risk management; and only 64% of the employees believe that they are aware of the risk management requirements expected from them and the bank. This implies that there is a gap in awareness among the board members and within the management team and employees that require provision of intensive trainings to narrow the observed gap on awareness and understanding of risk management.

Concerning overall responsibilities, the NBE's directive SBB/62/2015 article 10.4.8 signifies that one of the major responsibilities of the banks' board is "*establishing and ensuring the effective functioning of various board committees including but not limited to, Audit Committee, Risk and Compliance Committee, and Human Resource Affairs Committee*." from this viewpoint the LIB's board, in carrying out its overall responsibilities for overseeing, approving and implementing the bank's strategic objectives, and risk governance framework has established the Loan Review & Risk Management, Audit, and Human Resources and Business Development (Compensation) Committees with clearly defined responsibilities and reporting relationship to monitor and oversee the risk management function of the senior management. On top of that, the board has enabled the senior management to establish Policy and Asset Liability (ALCO) Committees to oversee the day to day operations of the Bank. Besides, the board has put in place the Risk and Compliance Management and Internal Audit Departments that assess the proper functioning of risk management so as to give assurance to the board whether management is functioning in light of the approved policies, procedures, and directives. Moreover, the composite mean of respondents' answers to the questionnaire regarding board's overall responsibility indicated 4.05 which if very good despite some indications that suggest further emphasis on overseeing the senior management's action on implementation of the Bank's policies for risk management.

From point view of ensuring sound risk management, the board's overall responsibility is establishing sound risk governance frame work long with clearly defined responsibilities, check and balance mechanisms, and accountabilities held by the role players in the risk management function for their actions. Establishing risk appetite frame work along well defined risk capacity, risk appetite, risk limits, ratios, and matrixes for it would enhance the control in the day to day operations of management in carrying out its responsibilities. Hence, however the board has established the risk governance risk appetite frameworks it requires devoting appropriate time and pay serious attention to the overseeing of the management function. In this regard, the data gathered from close ended questions indicated that the average time the board and management spend on risk management issues as agenda on its meetings over the last one year was between 10% - 40%. Besides, the frequency of appearance of risk management agenda on board and management meetings is rated between medium and high. This may indicate that though the issue of risk management as a core part of corporate governance frequently appears in board meetings, the time allocated for the agenda and the depth of discussion on the issue requires further attention of the board.

Regarding board's own structure, standing from the data gathered from documents in the board secretariat office, the key informants, and the questionnaire, the researcher noted that the board has properly established its own structure that complies with the international principles of corporate governance and the NBE's Bank Risk Management Guidelines and Bank Corporate Governance Directive SBB/62/2015. Both the Basel Committee for Banking Supervision (BCBS) and the NBE suggests a board of a bank to define appropriate governance structures and practices for its own work, and put in place board risk management, audit and compensation committees to oversee, periodically review, and follow up the senior management's action towards risk management.

According to the NBE Bank Risk Management Guidelines, *"risk identification is critical process for banks in implementing operational risk measurement, monitoring and control. Effective risk identification considers both internal factors (such as the complexity of the bank's structure, the nature of the bank's activities, the quality of personnel, organizational changes and employee turnover) and external factors (such as fluctuating economic conditions, changes in the industry and technological advances) that could adversely impact on the bank's earnings and capital"*(2010, p34). Further, the BCBS principles of corporate governance signifies that risk management, identification, monitoring and controlling process should be carried out by an independent risk management function, under the direction of the board with sufficient independence, resources and access to the board. In this regard, though the risk management, identification, monitoring and controlling process in LIB is carried out by the independent units, the Risk and Compliance Management and Internal Audit Departments under the direction of Loan Review & Risk Management and Audit Committees with sufficient independence and defined responsibilities, the board requires pay serious attention on thoroughly reviewing the findings of the independent units and give appropriate time for discussion on the issues.

The risk identification LIB's RCMD identifies risks inherent to the banking business that could severely affect earnings and capital base of the bank, based on the magnitude of loss exposure of each risk. Hence, the bank mainly indentified such major risks as: credit risk, liquidity risk, interest rate risk, foreign exchange risk, and operational risks. Based on the identified risks the RCMD and IAD monitor the developments of risk factors in each of the foregoing indentified risks through careful assessment on risk factors that affect the level of emergence of potential risks like change on external environment, such as macroeconomic environment, changes in regulatory and other legal requirements, and internal environment like: level and direction of early warning signals on ratios such as non-performing loans (NPLs)to deposit ratio, liquidity ratio, effective interest rate, exchange rate movements, and etc. the calculated composite means to the answers responded by respondents regarding the roles of board Risk and Audit Committees indicated that 4.0 and 4.1 respectively which signifies that the committees are employing oversight role.

The senior management under the direction and oversight of the board carries out and manage the bank's activities in a manner consistent with the business strategy, risk appetite, and other policies approved by the board. Thus, the management based on the risk appetite framework established for the bank set and approved a risk appetite, risk tolerance, and risk limits, and ratios and matrixes for major risk areas like credit, liquidity, foreign exchange (marketing risk), and operations. Besides, the first lines of defense, mainly Credit, International Banking and Domestic Banking Services Departments interpret and implement the limits and ratios set, while the Risk and Compliance Management and Internal Audit Departments, second and third lines of defense, monitors the performance of management through periodically measuring the proper implementations of the limits and matrixes including through conducting stress testing under normal and worst scenarios. The board, as a supervisory body, regularly oversees the proper implementation of senior management over the approved limits, ratios and matrixes. Concerning the board's oversight role over the senior management the composite score of respondents indicated 4.04 that signifies the board oversees the senior management's actions.

Regarding disclosure of information and risk communication, the data gathered through interview and documentation indicated that the board based on the risk governance framework it established on the Bank ensures it gains reports and information on regular basis, mainly on quarter reports and President/CEO's briefings on major updates on every meetings, regarding the overall operations and new phenomena, while the senior management facilitates communication within the bank about risk, both across the organization and through reporting to the board and senior management. However, majority of the respondents respond that the board and management are provided with necessary information for decision making; for there are uncertainties on the timeliness, frequency, and completeness of the information the board requires further assessing and ensuring quality disclosure of information in the bank.

5.2. Conclusion

As stated in chapter one, this study sets out to examine whether the LIB's board of directors carrying out its role of corporate governance to ensure sound risk management in the bank in a way it conforms the international and national principles and standard of risk management. The study employed review of documents from the LIB board secretariat office, conducted interview with key informants, chairpersons of the Loan Review and Risk Management Committee, Audit Committee, and the HR and Business Development (Compensation) Committee, The President and the Director Risk and Compliance Management Department. It also employed questionnaire to employees of the bank at various levels and incorporated personal observation of the researcher. Qualitative data gathered through interview, and questionnaire is thematically synthesized and Quantitative data are statistically analyzed. The research didn't attempt to gauge the performance of operational risks based on the set limits, ratios, and matrix parameters, rather endeavors to describe the role of the board in risk management in light of accepted corporate governance and risk management principles.

The findings of the study indicate that however the board is implementing corporate governance and risk and risk management that comply with the international and national principles and standards, it requires working on strengthening the risk management function of the bank. The board seems demonstrated a workable size and composition in relation to experience, skill, and knowledge of banking operations; but lacked balancing gender composition. However it is the duty of the Shareholders' General Assembly to balance the gender composition of the board, but as principle of corporate governance the board failed in that regard.

In shouldering the overall corporate governance responsibilities entrusted to it, the board has set a clearly defined charter that guides and governs its actions. Besides, the board has structured itself in sub committees that direct and oversee the senior managements. Based on the tone set on the top, the senior management has structured its work units in departments (first lines of defense in risk management), the independent risk management and internal audit (the second and third lines of defense), and to oversee the bank's overall operations it has established the Policy and Asset & Liability Committees entrusted with defined responsibilities and accountabilities to their actions.

The board, in order to facilitate internal communication and transparency, has established a clearly defined reporting relationship system among work units, the senior management, and the board and its committees. What the researcher observed as a gap is that there is lack of awareness on risk management both on resulted from provision of adequate training. This may affect the communication process and disclosure of quality information to the board.

As means of monitoring and control the board has set sound risk appetite framework bundled with risk capacity, risk tolerance, and risk limits along with ratios and risk matrixes on major risk areas. It is obviously good to establish risk appetite framework. But, to the matter of fact that to ensure sound control on the risk involved operation, the board requires implementing a system that ensure disclosure of frequent and complete information for decision making and simultaneously should devote proper time for discussion on the information.

In general, regardless the aforementioned gaps, the research indicated the board has established risk governance and risk appetite frameworks that enable it carry out its overall responsibility to put the bank into safe and stable banking system. Undeniably, the role of the National Bank of Ethiopia, as a bank supervisory body, was immense in strengthening corporate governance and risk management of commercial banks enforcing them through the directives and regular on-site and off-site examinations, periodic monitoring and follow up, and the subsequent administrative actions it took over banks on non-compliance to the directives. The researcher believes this active role of the supervisory body has helped the LIB's board to properly carry out its role and establish sound corporate governance and stable risk management system in the Bank.

5.3. Recommendations

In light of the literature reviewed and findings of the research, the researcher would like to make the following recommendations:

- The Board of Directors of Lion International Bank is properly carrying out its overall responsibilities in the corporate governance and risk management of the Bank, but in order to strengthen its role the bank is highly required to provide intensive trainings to board members and staff at various level. The bank should at least meet the NBE's requirement that obliges banks to provide training to board members at least once a year.
- From the point view of risk governance framework, it is the staff that plays a first line of defense role in risk management function. Thus, the senior management should provide awareness enhancement works on current updates and progresses on risk management to the board and employees including the risk and compliance management and internal audit department staff as they are the role players in the three lines of defenses in the risk management.
- However it is the duty of the Shareholders General Assembly to elect women for board membership and balance the gender composition of the board, it should able to promoting the role of women in the board in the shareholders general assembly so as to elect and raise number of women in the board.
- Awareness enhances understanding and skills of risk management of employees and the board, by which increases quality of reporting and disclosure of information. And as a result of which facilitation within the bank and among work units and the senior management and the board will increase.
- Implementation of balanced and competitive compensation system in the bank motivates the President/CEO and employees to increase performance and profitability. Besides, ensures belongingness of employees and serves the board as a tool to reduce employee turnover and retain qualified staff. Thus, the board should periodically review and ensure there is a compensation structure in the bank that promotes long term performance in line with the business and risk strategy, objectives and long term interest of the bank.

- The bank has clearly defined policies and procedures that enable the board and the management ensure risk management, but having policies and procedures is not enough by itself. The board should periodically review, update, and revise the policies and procedures at least every two years so as to comply with the directives of the NBE and own charter.
- From point view of ensuring sound risk management, the board should periodically oversee the proper implementation of the risk governance and risk appetite frameworks, risk capacity, risk appetite, risk limits, ratios, and matrixes it put in place. and
- As the issue of risk management is a core of corporate governance the board should frequently discuss on its board meetings, the time allocated for the risk management issues and the depth of discussion on the issue should attain serious attention of the board.

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Appendix: A

LIB's Credit, Foreign Exchange, Liquidity, and Operations Risk Limits, Ratios, &Matrixes

The following are the limits set by the LIB's board of directors of the Bank based on the risk capacity and appetite of the Bank and directives of the National Bank of Ethiopia; excerpted from the Risk Management Program (2014) of the Bank.

I. Credit Risk Limits:

Table 7 - Credit Limits by Sector

S/No	Economic Sector Items	Limits	Risk Level		
			Low	Moderate	High
1	Agriculture	3	Below 3%	[3-6]%	Above 6%
2	Industry	2	Below 2%	[2-4]%	Above 4%
3	Export	18	Below 18%	[18-28]%	Above 28%
4	Import	32	Below 32%	[32-42]%	Above 42%
5	Hotel & Tourism	6	Below 6%	[6-12]%	Above 12%
6	Transport & Communication	8	Below 8%	[8-13]%	Above 13%
7	Building & Construction	10	Below 10%	[10-15]%	Above 15%
8	Domestic Trade	18	Below 18%	[18-28]%	Above 28%
9	Others	3	Below 3%	[3-6]%	Above 6%
	Total	100%			

Table 8 - Credit Limit by Tenure

S/No	Description of Tenure	Limits	Risk Level		
			Low	Moderate	High
1	Short Term Loans	40%	Above 40%	[30-40]%	Below 40%
2	Medium Term Loans	50%	Below 50%	[30-60]%	Above 60%
3	Long Term Loans	10%	Below 10%	[10-20]%	Above 20%
	Total	100%			

Table 9 - Credit Limit by Product Type

S/N	Type of Product	Limits	Risk Level		
			Low	Moderate	High
1	Term Loan	66	Below 66%	[66-76]%	Above 76%

2	Overdraft	15	Below 15%	[15-20]%	Above 20%
3	Merchandise	11	Below 11%	[11-16]%	Above 16%
4	Others	8	Below 8%	[8-13]%	Above 13%
	Total	100%			

Table 10 - Other Limits

S. N	Risk Indicators (Ratios)	Limits	Risk Level		
			Low	Moderate	High
1	Loan to Deposit	80%	Below 70%	[70-80]%	Above 80%
2	Off balance sheet to Total assets	55%	Below 40%	[40-65]%	Above 65%

Table 11 - Off Balance Sheet Limits

S. No.	Risk Indicators (Ratios)	Limits	Risk Level		
			Low	Moderate	High
1	L/G	250%	Below 250%	[250- 60]%	Above 260%
2	L/C	35%	Below 25%	[25-45] %	Above 45%
3	Unutilized Portion of OD	12%	Below 12%	[12-17 %	Above 17%
4	Loan Commitment	8%	Below 8%	[8-18] %	Above 18%
	Total	305	Below 305%	[295-325] %	Above 325%

Table 12 - Credit Limit on Revolving Credit Facilities

Credit exposure Limit on Portfolio share of Revolving Credit facility

Risk Indicator	Limit (Outstanding Loan)	Risk Level		
		Low	Moderate	High
Revolving Credit Facility *	10%	Below 8%	[8-10]%	Above 10%

*Includes Pre-Shipment Export loan, Merchandise Loan & Advance on Import Bills

Table 13 - Credit Limit by Geography - Credit exposure Limit based on Region

Risk Indicator	Limit (Outstanding Loan)	Tolerance
City Branches	75%	± 10%
Outlying Branches	25%	± 15%
	100%	

Single borrower limit based on Risk Grade

The proposed single borrower limit is prepared based upon the risk grade of a customer and Directive no. SBB/29/2002 on Single Borrower Limit (Set the limit at 25% of the total capital of the Bank). Accordingly, the following maximum limits are set along with the corresponding risk grade of the customer.

- Risk grade 1: 25% the bank's capital
- Risk grade 2: 20 % the bank's capital
- Risk grade 3 : 15% the bank's capital
- Risk grade 4 : 10% the bank's capital
- Risk grade 5 : 5% the bank's capital

II. Liquidity Risk

Liquidity risk is measured by a matrix of limits and ratios that serve as a vital tool for gauging and monitoring the risk level of a bank. Thus, the board has approved the following risk limits and ratio matrixes on liquidity, foreign exchange, foreign currency, and interest rate risks:

Table 14 - Liquidity risk limits and risk levels

S. N	Risk Indicators (Ratios)	Limits	Risk Level		
			Low	Moderate	High
1	Loan to Deposit	70%	Below 60%	[60-75]%	Above 75%
2	Liquid assets to Net deposit	20%	Above 30%	[20-30]%	Below 20%
3	Off balance sheet to Total assets	55%	Below 40%	[40-65]%	Above 65%
4	Net short-term Liquidity gap/Asset Liability mismatch/ to Total asset	24%	Below 10%	[10-25]%	Above 25%
5	Liquid assets to Total assets	32%	Above 35%	[20-35]%	Below 20%

III. Foreign Exchange Matrix, Limits and Ratios

Table 15 - Foreign Exchange Risk Limits & Ratios Matrix

S. N	Risk Indicators	Risk Level		
		Low	Moderate	High
1	Net open position to Total capital	Below 10%	[10-15%]	Above 15%
2	Forex assets to Forex liabilities	Above 100%	[90-100%]	Below 90%
3	Foreign currency denominated assets to Total assets	Below 10%	[10-30%]	Above 30%
4	Foreign currency denominated liabilities to Total liabilities	Below 10%	[10-30%]	Above 30%

Table 16 - Foreign Exchange Risk Limits

S. N	Applicable Ratios	Limits
1	Net open position to total capital	±15*
2	Forex Asset to Total Asset	21.05
3	Forex assets to forex liabilities	425.67

*Regulatory limit

Table 17 - Foreign Currency risk Limits

S. N	Applicable Limits	Limits
1	US Dollar	96%
2	Euro	1.6%
3	GBP	1.4%
4	Other Currencies	1%

Table 18 - Limits for transaction /Foreign Currency Approval discretion limit

Limit for documentary transaction approval

S/N	Approving body	Discretionary Limit
1	Junior Officer	Up to ETB 2,000,000
2	Officers	Up to ETB 10,000,000
3	Division Manager IBD/Branch Managers	Above ETB 10,000,000

Table 19 - Interest Rate Risk Limits, Ratios and Matrix

S. N	Risk Indicators	Risk Level		
		Low	Moderate	High
1	Interest sensitive Asset/ Interest Sensitive Liability Gap/ Interest sensitive Asset	Below ±15%	± [15-25%]	Above ±25%
2	Interest Sensitive Assets to Total Assets	Below 30%	[30-75%]	Above 75%
3	Interest sensitive Liability to Total Liability	Below 40%	[40-70%]	Above 70%

IV. Operational Risk Limits

Table 20 - Cash TransactionsLimits

S/N	Description	Font Maker	Font Maker With Front Checker (Up to Birr)	Font Maker With Senior Customer service Officer (Up to Birr)	Font Maker With Customer Service Manager
1	S/A Authorization Limit	≤ Birr 15,000	50,000	250,000	No Limit
2	C/A (SP S/A) Authorization Limit	≤ Birr 25,000	75,000	350,000	No Limit
3	Payment for Incoming Automatic Fund transfer in cash	≤ Birr 5,000	25,000	200,000	No Limit
4	Incoming local transfer in cash (Massage received from offline Branches)	≤ Birr 25,000	50,000	350,000	No Limit
5	CPO and DD refund at Issuing branch and other than issuing branch in cash	≤ Birr 25,000	50,000	350,000	No Limit

Source: LIB Risk Management Program (2014)

Appendix: B

Structured Questionnaires employed in the Study

St. Mary's University School of Graduate Studies

Department of Bank

MBA Program - General

Dear Board Member,

Thank you very much for your cooperation to take time to respond to this research questionnaire. The research is being conducted by a prospective graduate student of St. Mary's University MBA program.

The survey is asking questions on bank corporate governance and the role of board of directors in risk Bank in the particular case of Lion International Bank S.C. As experienced board member, your accurate and candid response is imperative for the successful accomplishment of the study. Please be certain that your responses will be treated strictly confidential, your identity anonymous, and the results will be used for the purpose of this research only.

Enclosed with this letter is a brief questionnaire that asks a variety of questions about the corporate governance and risk Bank practices of the Lion International Bank S.C. the survey questionnaire contains two parts: the first part is on personal profile and the second part on corporate governance and risk Bank issues. Kindly return the questionnaire appropriately filled by answering every item at your earliest convenience.

Sincerely,

Mululgeta Teklu

Prospective Graduate in Masters of Business Administration

School of Graduate Studies

St. Mary's University

Section I

This section requires your personal information and observation regarding risk governance of the bank. Please tick (✓) mark on one of the following boxes. Thank you very much for your cooperation to answer every item

Personal Information:

1. Gender:
   - Male ☐
   - Female ☐

2. Highest level of education:
   - Certificate ☐
   - Diploma ☐
   - Bachelor Degree ☐
   - Masters Degree ☐
   - Doctoral Degree ☐
   - Other (please specify)……………………………..

3. Field of study - major …………………………………………….

4. Work experience in a managerial/supervisory position in private or public enterprises:

   5 -10 years ☐

   11-15 years ☐

   16-20 years ☐

   Above 20 years ☐

5. Work experience other than serving as a board member
   - 1 -5 years ☐
   - 6 -10 years ☐
   - 11-20 years ☐
   - over 21years ☐

6. Have you ever sat for training provided by the Bank on risk Bank and governance issues?
    - At least once ☐
    - Twice ☐
    - Three and above sessions ☐
    - Never ever ☐
7. Have you ever had training on issues related to risk Bank and governance by other training institutions? Yes…………, No……………

    If yes, how often: Once ☐ Twice ☐ Three and above sessions ☐

8. Are you individually and the board, as a team, aware of risk Bank requirements expected from the Bank?
    - Yes I and the board members are aware ☐
    - Yes I and some or few of the board members are aware ☐
    - Yes I am but I am not sure about others ☐
    - No I am not but others do ☐
    - No we are not aware at all ☐
9. How much time does the board spend on average over the last one year on risk Bank issues in terms of percentage?
    - 0-10% ☐
    - 11-20% ☐
    - 21-40% ☐
    - 41-60% ☐
    - >60% ☐
10. How do you rate the degree (frequency) of appearance of risk Bank issues as agenda on board meetings?
    - High ☐
    - Medium ☐
    - Low ☐

11. Is the board provided with relevant and up-to-date economic, business and market data/information for decision?

- Yes, definitely it is provided
- Yes, but not in completed way
- I am not quite sure of that
- rarely
- Not at all

12. Does the board have continuity/disaster recovery/contingency plan in place in case unexpected risk that may occurs?

- Yes, it does have
- I am not quite sure of that
- I think Bank could have
- Not at all

13. If it does have, how often the board review and revise it?

- once in every year
- once in two years
- I don't remember we review it
- I don't think it needs review and revision
- Not at all

Section II

This section requires your observation regarding the roles, responsibilities, and structure of the board towards risk governance of the Bank. Please rate the extent to which you agree or disagree with the statement by putting a tick (✓) mark on one of the following: Strongly disagree, Disagree, Neutral (indifferent), Agree, or Strongly Agree. Thank you very much for your cooperation to answer every item.

1	**Composition**	**Strongly Disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly agree**
1.1	The board consists of a workable number (size) of board members to function effectively as a team.					
1.2	The board has the right blend of skills, experience and appropriate degree of diversity of knowledge relevant to the board's tasks and the bank's operations.					
1.3	There is transparent and clear structure that defines roles and responsibilities, functions and relationship between board members, the President, and the senior Bank.					
2	**Overall responsibilities**	**Strongly Disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly agree**
2.1	The Bank has sufficient definition and documentation concerning the role and responsibilities of the board for risk governance.					
2.2	The board approves the Bank's strategic plan (e.g. risk tolerance, risk appetite, risk limits, and business strategy).					
2.3	The board oversees senior Bank's implementation of the Bank's strategic plan.					
2.4	The board approves and oversees the implementation of the Bank's policies for risk and compliance relating to risk Bank.					
2.5	The board approves and oversees the implementation of the Bank's capital adequacy assessment process, capital and liquidity pans, compliance policies and obligations, and the internal controls system.					
2.6	The board formulates and defines the mandate and responsibilities of board-level committees dealing with risk governance.					

2.7	The board in discharging its responsibilities takes into account the legitimate interests of depositors, shareholders and other relevant stakeholders and ensures that the Bank maintains an effective relationship with its supervisory organs.					
2.8	The Bank's (senior executive Bank's) responses show that the role and responsibilities of the board are practically implemented in an appropriate and effective manner.					
3	**Board Committees Responsibilities**					
3.1	**Board Risk Bank Committee**	**Strongly Disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly agree**
3.1.1	The board explicitly defines and documents the role and responsibilities of the risk committee.					
3.1.2	The risk committee is a self-standing committee.					
3.1.3	The risk committee reports and advises the board on the Bank's overall current and future risk tolerance/appetite and strategy.					
3.1.4	The risk committee ensures the strategic plans covered by the risk committee include those for capital and liquidity Bank, as well as for credit, market, operational, compliance, reputational and other risks of the Bank.					
3.1.5	The risk committee oversees senior Bank proper implementation of the strategic plan.					
3.1.6	The risk committee discusses the Banks' material risks on both an aggregated basis and along with the types of risks borne by Banks (e.g., credit risk, market, liquidity, operational risks).					
3.1.7	The Bank's responses show that the role and responsibilities of the risk committee are practically implemented in an appropriate and effective manner.					
3.2	**Board Audit Committee**	**Strongly disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly Agree**
3.2.1	The board explicitly defines and documents the role and responsibilities of the audit committee.					
3.2.2	The audit committee is a self-standing committee.					

3.2.3	The audit committee reports and advises the board on the Bank's overall financial reporting process and the internal control process.					
3.2.4	The audit committee reviews and approves the audit scope and frequency.					
3.2.5	The audit committee receives key audit reports and ensures that the senior Bank is taking necessary corrective actions in a timely manner to address control weaknesses, non-compliance with policies, procedures, laws and regulations, and other problems identified by auditor and other control functions.					
3.2.6	The audit committee oversees establishment of accounting policies and practices by the bank.					
3.2.7	The Bank's responses show that the role and responsibilities of the audit committee are practically implemented in an appropriate and effective manner.					
4	**Board Process**					
4.1	**Commitment**	**Strongly disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly Agree**
4.1.1	Board members regularly attend board meeting and make informed decisions					
4.1.2	Board members come to meetings well prepared for the agenda items and actively participate in discussions.					
4.1.3	The board pays appropriate follow up and monitoring on proper implementation of its decisions.					
4.1.4	Board members make heated debates on agenda items; and conflicts of interest that occur in decision making are amicably solved by the procedure of voting.					
4.1.5	Board members critically examine proposals initiated by the Bank.					
4.2	**Strategic participation role**	**Strongly disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly Agree**
4.2.1	The board understands well the bank's business and operations environment.					
4.2.2	The board actively involves in long term strategic planning process and goals coping with changes in the external environment.					

4.2.3	The board demonstrates awareness of emerging environmental trends affecting the bank.					
4.2.4	The board considers strategic approaches in the decision making process.					
4.3	**Advisory role**	**Strongly disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly Agree**
4.3.1	The board provides support and advise to the senior executive Bank whenever deemed necessary					
4.3.2	The board contributes to major market (business) and technology issues affecting the bank.					
4.3.3	The board provides proper advice direction regarding achieving strategic goals.					
4.3.4	Individual board members take initiatives to give advice to the board/Bank based on their personal knowledge and experiences.					
4.4	**Control role**	**Strongly disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly Agree**
4.4.1	Bank regularly reports on key performances and targets that flow directly from the strategy.					
4.4.2	The board is regularly kept informed on the financial and operational positions of the bank.					
4.4.3	The board actively monitors and evaluates implementations of strategic decisions and key targets.					
4.4.4	The board critically reviews performance against strategic plan.					
4.4.5	The board monitors top Bank in decision making.					
5	**Oversight of senior Bank**	**Strongly disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly Agree**
5.1	The board provides oversight of senior Bank and holds members of senior Bank accountable for their actions.					
5.2	The board monitors that senior Bank's actions are consistent with the strategy, policies, and procedures approved by it and the regularly requirements.					
5.3	The board critically questions and reviews explanations and information provided by senior Bank.					
5.4	The board ensures that senior Bank's knowledge and expertise remain appropriate given the nature of the business and the bank's risk profile.					

5.5	The board ensures that appropriate succession plans are in place for senior Bank positions.					
6	**Compensation**	**Strongly disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly Agree**
6.1	The board established a compensation system of the bank and regularly monitors and reviews outcomes to ensure the bank-wide compensation system is operating as intended.					
6.2	The board approved the compensation of senior executives, including the President, and oversees Bank's development and operation of compensation policies, systems and related control processes.					
6.3	The board thinks the compensation structure of the bank promotes long term performance and be in line with the business and risk strategy, objectives, values and long-term interests of the bank.					
6.4	The board thinks the remuneration structure of the bank is sufficient enough to motivate, attract, and retain qualified Bank and the staff to attain better performance.					
7	**Internal audit**	**Strongly disagree**	**Disagree**	**Neutrals (indifferent)**	**Agree**	**Strongly Agree**
7.1	The bank has an internal audit function that undertakes, on a regular basis, an independent assessment of the bank's risk governance framework and risk Bank policies and processes at the enterprise level and/or for selected revenue-generating business units.					
7.2	The internal audit function reports directly to the board or a board-audit committee from an organizational perspective and with regards to findings.					
7.3	The bank's board audit committee and senior Bank review internal audit reports and prudential reports as part of the bank's risk governance framework.					
7.4	The bank's board and senior Bank monitors the timely rectification of weaknesses identified through the independent assessment of the risk governance framework and underlying functions.					
7.5	The bank has a process to evaluate the effectiveness of the independent assessment of its risk governance framework.					

Thank You Very Much!!

Appendix C:

Interview Questions Prepared for Committee Chairpersons and Officials of LIB

1. Does the Bank have clearly defined Risk Appetite Statement & Risk Appetite Limits? What are the basic elements of the RAS & RAL?
2. How the Bank/Board/Management/RCMD identify the critical risks, risk capacity, risk appetite, risk tolerance, and risk limits of the Bank?
3. Does the risk limits align with the banks objectives and strategy? How?
4. Do the roles and responsibilities of the first, second, and third lines of defense (the business units, the risk management and internal audit functions) have explicitly defined? How are they involving in the risk management activities?
5. How the approved risk appetite statement and risk limits be communicated to pertinent staff of the Bank? How?
6. How compliance with the risk appetite is being monitored?
7. How relevant risk appetite information is reported to the board?
8. Does management carryout revision on risk limit adjustment? How & how often?
9. How compensation is carried out in the Bank?
10. How Reporting, Monitoring and Follow up is carried out by the committees and the board?

Appendix D – SPSS Data Analysis