HIGH-LEVEL CONTROLS MODULE

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HC-A.1 Purpose

Executive Summary

HC-A.1.1 This Module presents requirements that have to be met by Islamic bank licensees with respect to:

(a) Corporate governance principles issued by the Ministry of Industry and Commerce as "The Corporate Governance Code"; and

(b) International best practice corporate governance standards set by bodies such as the Islamic Financial Services Board (IFSB) and the Basel Committee on Banking Supervision (specifically the 'Compliance and compliance function in banks' paper and the 'Principles for enhancing corporate governance' paper issued by the Basel Committee in April 2005 and October 2010 respectively) and the Islamic Financial Services Board (specifically the IFSB-3 paper of December 2006 'Guiding Principles on Corporate Governance for Institutions Offering Only Islamic Financial Services (Excluding Insurance (Takaful) Institutions and Islamic Mutual Funds'); and

(c) Related high-level controls and policies.

HC-A.1.2 [This paragraph was deleted].

HC-A.1.3 The purpose of the Module is to establish best practice corporate principles in Bahrain, and to provide protection for investors and other Islamic bank licensee's stakeholders through compliance with those principles.

HC-A.1.4 Whilst the Module follows best practice, it is nevertheless considered as the minimum standard to be applied. This Module also includes rules and guidance issued by the CBB prior to the publication of the Code, the Basel Committee document and the IFSB document and contained in the previous version of Module HC.

Structure of this Module

HC-A.1.5 This Module follows the structure of the Corporate Governance Code and each of the first 9 Chapters deals with one of the nine Principles of corporate governance. The numbered directives included in the Code are Rules for purposes of this Module. Recommendations under the Code have been included as guidance. However, where the previous version of Module HC had a similar recommendation as a Rule, the Module retains this Paragraph as a Rule.

HC-A.1.6 [This paragraph was deleted].

HC-A.1.7 All references in this Module to 'he' or 'his' should, unless the context otherwise requires, be construed as also being references to 'she' and 'her'.

HC-A.1 Purpose (continued)

The Comply or Explain Principle

HC-A.1.8 **This Module is issued as a Directive (as amended from time to time) in accordance with Article 38 of the Central Bank of Bahrain and Financial Institutions Law 2006 ('CBB Law'). In common with other Rulebook Modules, this Module contains a mixture of Rules and Guidance (See Module UG-1.2 for detailed explanation of Rules and Guidance). All Rulebook content that is categorised as a Rule must be complied with by those to whom the content is addressed. Other parts of this Module are Guidance; nonetheless every Islamic bank licensee to whom Module HC applies, is expected to comply with recommendations made as Guidance in Module HC or explain its noncompliance in the Annual Report in accordance with Subparagraph PD-1.3.10(x) and to the CBB (see Chapter HC-8).**

Monitoring and Enforcement of Module HC

HC-A.1.9 Disclosure and transparency are underlying principles of Module HC. Disclosure is crucial to allow outside monitoring to function effectively. This Module looks to a combined monitoring system relying on the Board, the Islamic bank licensee's shareholders and the CBB.

HC-A.1.10 It is the Board's responsibility to see to the accuracy and completeness of the Islamic bank licensee's corporate governance guidelines and compliance with Module HC. Failure to comply with this Module is subject to enforcement measures as outlined in Module EN (Enforcement).

Legal Basis

HC-A.1.11 **This Module contains the CBB's Directive (as amended from time to time) relating to high-level controls and is issued under the powers available to the CBB under Article 38 of the Central Bank of Bahrain and Financial Institutions Law 2006 ('CBB Law'). The Directive in this Module is applicable to Islamic bank licensees (including their approved persons).**

HC-A.1.12 For an explanation of the CBB's rule-making powers and different regulatory instruments, see Section UG-1.1.

HC-A.1 Purpose (continued)

Effective Date

HC-A.1.13 [This paragraph was deleted].

HC-A.2 Module History

HC-A.2.1 This Module was first issued in June 2004 by the BMA and updated in October 2007 to reflect the switch to the CBB. Following the issuance of the Corporate Governance Code by the Ministry of Industry and Commerce in March 2010, the Module was amended in October 2010 to be in line with the new Corporate Governance Code and to include previous requirements that were in place in the originally issued Module HC. Any material changes that have subsequently been made to this Module are annotated with the calendar quarter date in which the change was made: Chapter UG-3 provides further details on Rulebook maintenance and version control.

HC-A.2.2 A list of recent changes made to this Module is detailed in the table below:

Module Ref.	Change Date	Description of Changes
HC-1 to HC-8	10/2010	Amendments due to introduction of new MOIC Corporate Governance Code. Amendments issued in October 2010 are effective on 1st January 2011. All Islamic bank licensees to which Module HC applies must be in full compliance by the financial year end 2011.
HC-1.3	10/2010	Prohibition of proxies and requirement to attend 75% of Board meetings in a financial year.
HC-A.1.8 and HC-A.1.11	01/2011	Clarified legal basis.
HC-1.3.8	01/2011	Corrected cross reference.
HC-2.2.4, 2.2.5 and 3.2.1	01/2011	Corrected cross references.
HC-2.3.2	01/2011	Corrected cross reference; reference changed to connected persons.
Appendix C	01/2011	Corrected cross reference.
Appendix A	04/2011	Clarified membership of audit committee to be in line with Rule HC-3.2.1.
HC-6.2.1	10/2011	Clarified management structure.
HC-B.2.2	01/2012	Clarified language related to corporate governance.
HC-1.2.8 and HC-1.5.3	01/2012	Clarified that the Chairman of the Board may delegate specific duties dealt with in these Paragraphs.
HC-1.3.12	01/2012	Amended Rule on Directorships.
HC-1.9.1	01/2012	Deleted last sentence to be in line with other Volumes of the CBB Rulebook.
HC-3.2.1(a) and HC-5.6.6	01/2012	Amended to be in line with other Volumes of the CBB Rulebook.
HC-6.3.1	01/2012	Clarified Rule by following corporate governance code wording.
Appendix A	01/2012	Amended criteria for audit committee member.
HC-A.1.8	04/2012	Clarified the reporting of noncompliance with Module HC in the Annual Report.
HC-7.2.5	04/2012	Clarified Guidance on election of board members.
Appendices A, B and C	04/2012	Amended requirement for written report on performance evaluation for various Board committees.
Appendix A	04/2012	Included reference to compliance under Committee Duties and Responsibilities.
HC-2.2.6A and HC-2.2.6B	07/2012	Added Rule and guidance dealing with benefits received from approved persons from projects and investments.
Appendices A, B and C	07/2012	Clarified requirement for written report on performance evaluation for various Board committees.
HC-1.3.7A	10/2012	Added requirement on minimum number of Board meetings to take place in the Kingdom of Bahrain to be consistent with other Volumes of the CBB Rulebook.

HC-A.2 Module History (continued)

HC-A.2.2 (continued)

Module Ref.	Change Date	Description of Changes
HC-2.2.6A	10/2012	Clarified Rule dealing with benefits received from approved persons from projects and investments.
Appendix A	10/2012	Corrected minor typo.
HC-2.2.2 and HC-2.4.1	01/2013	Clarified scope of application for Rules.
HC-2.2.6A, HC-5 and Appendix C	01/2014	Amendments due to new rules on sound remuneration practices.
HC-1.2.6	04/2014	Clarified CBB's requirements for proposed changes to strategy and/or corporate plans.
HC-5.2, HC-5.4 and HC-5.5	07/2014	Updated Rules on remuneration.
HC-1.2.11	10/2014	Corrected cross reference.
HC-1.3.10	10/2014	Corrected typo.
HC-6.4.3	10/2014	Clarified self assessment of compliance function.
HC-5.4.2	01/2015	Clarified application of remuneration rules for Bahrain operations.
HC-5.4.5	01/2015	Paragraph deleted.
HC-5.5.2	04/2015	Clarified cap on board of directors' remuneration as per Article 188 of the Company Law.

HC-B.1 Scope of Application

HC-B.1.1 The contents of this Module – unless otherwise stated – apply to all Islamic bank licensees, incorporated under the Legislative Decree No. 21 of 2001, with respect to promulgating the Commercial Companies Law ('Company Law').

HC-B.1.2 Overseas Islamic bank licensees must satisfy the CBB that equivalent arrangements are in place at the parent entity level, and that these arrangements provide for effective high-level controls over activities conducted under the Bahrain license.

HC-B.2 Subsidiaries and Foreign Branches

HC-B.2.1 **Bahraini Islamic bank licensees must ensure that, as a minimum, the same or equivalent provisions of this Module apply to their foreign branches, located outside the Kingdom of Bahrain, such that these are also subject to effective high-level controls. In instances where local jurisdictional requirements are more stringent than those applicable in this Module, the local requirements are to be applied.**

HC-B.2.2 **Bahraini Islamic bank licensees must satisfy the CBB that financial services activities conducted in subsidiaries and other group members are subject to the same or equivalent arrangements for ensuring effective corporate governance over their activities.**

HC-B.2.3 Where an Islamic bank licensee is unable to satisfy the CBB that its subsidiaries and other group members are subject to the same or equivalent arrangements, the CBB will assess the potential impact of risks – both financial and reputational – to the licensee arising from inadequate high-level controls in the rest of the group of which it is a member. In such instances, the CBB may impose restrictions on dealings between the licensee and other group members. Where weaknesses in controls are assessed by the CBB to pose a major threat to the stability of the licensee, then its authorisation may be called into question.

HC-1.1 Principle

HC-1.1.1 **All Bahraini Islamic bank licensees must be headed by an effective, collegial and informed Board of Directors ('the Board').**

HC-1.2 Role and Responsibilities

HC-1.2.1

All directors must understand the Board's role and responsibilities under the Company Law and any other laws or regulations that may govern their responsibilities from time to time. In particular:

(a) The Board's role as distinct from the role of the shareholders (who elect the Board and whose interests the Board serves) and the role of officers (whom the Board appoints and oversees); and

(b) The exercising of the Board's fiduciary duties of care and loyalty to the Islamic bank licensee and the shareholders (see HC-2.1).

HC-1.2.2

The Board has ultimate responsibility for the bank's business, risk strategy and financial soundness as well as for how the bank organises and governs itself. The Board must take into account the bank's long-term financial interests, its exposure to risk and its ability to manage risk effectively. The Board's role and responsibilities include but are not limited to:

(a) The approval and monitoring of overall business performance and strategy for the Islamic bank licensee, including its risk tolerance and appetite;

(b) Causing financial statements to be prepared which accurately disclose the Islamic bank licensee's financial position;

(c) Monitoring management performance;

(d) Convening and preparing the agenda for shareholder meetings;

(e) Monitoring conflicts of interest and preventing abusive related party transactions;

(f) Assuring equitable treatment of shareholders (including minority shareholders), investment account holders, depositors and other relevant stakeholders; and

(g) Establishing the objectives of the bank.

HC-1.2.2A

In addition to the general responsibilities outlined in Paragraph HC-1.2.2, the Board must approve and oversee the implementation of the bank's:

(a) Policies for risk management (see Chapter HC-13 for more details) and compliance;

(b) Internal controls system (see Chapter HC-13 for more details);

(c) Corporate governance framework, principles, and corporate values, including a code of conduct (see Paragraph HC-1.2.2B); and

(d) Remuneration system.

HC-1.2 Role and Responsibilities (continued)

HC-1.2.2B

Islamic bank licensees must establish a comprehensive governance policy framework which will guide them in cultivating a good governance culture. In its governance policy framework, the Islamic bank licensee must be able to set out:
(a) The strategic roles and functions of each organ of governance, including the Board of Directors (BOD), its committees, the senior management, the Shari'a Supervisory Board (SSB), the internal and external auditors, etc; and
(b) The mechanisms of balancing the accountabilities of each of the organs of governance to various stakeholders.

HC-1.2.2C

To be comprehensive, the governance framework should recognize all risks faced by the bank in its day-to-day business and strategy. In this context, the framework is a descriptive term for the bodies such as the board and senior management and the associated internal controls and reporting systems described in this Module. The framework also includes board and management committees and individuals and functions named in Chapters HC-3, HC-4, HC-5, HC-6, HC-9, HC-13 and HC-14."

HC-1.2.3

The precise functions reserved for the Board, and those delegated to management and committees will vary, dependent upon the business of the institution, its size and ownership structure. However, as a minimum, the Board must establish and maintain a statement of its responsibilities for:

(a) The adoption and annual review of strategy;
(b) Its organisational rules, by-laws, or other similar documents setting out its rights, responsibilities and key activities;
(c) The adoption and review of board structure in terms of size, frequency of meetings and the use of committees, so as to promote efficiency, sufficiently deep review of matters, and robust, critical challenge and discussion of issues;
(d) The review of management structure and responsibilities;
(e) The adoption and review of the systems and controls framework; and
(f) Monitoring the implementation of strategy by management.

HC-1.2 Role and Responsibilities (continued)

HC-1.2.4 **The directors are responsible both individually and collectively for performing the responsibilities outlined in HC-1.2.1 to HC-1.2.3. Although the Board may delegate certain functions to committees or management, it may not delegate its ultimate responsibility to ensure that an adequate, effective, comprehensive and transparent corporate governance framework is in place.**

HC-1.2.5 **In its strategy review process under Subparagraphs HC-1.2.3 (a) and (f), the Board must:**
(a) Review the bank's business plans and the inherent level of risk in these plans;
(b) Assess the adequacy of capital to support the business risks of the bank;
(c) Set performance objectives; and
(d) Oversee major capital expenditures, divestitures and acquisitions.

HC-1.2.6 **Bahraini Islamic bank licensees must obtain the CBB's prior written approval for all major proposed changes to the strategy and/or corporate plan of the Bahraini Islamic bank licensee prior to implementation (see also Paragraph BR-5.2.8).**

HC-1.2.7 The Board is expected to have effective policies and processes in place for:
(a) Approving budgets and reviewing performance against those budgets and key performance indicators; and
(b) The management of the bank's compliance risk.

HC-1.2.8 When a new director is inducted, the chairman of the Board, or the Islamic bank licensee's legal counsel or compliance officer, or other individual delegated by the chairman of the board, should review the Board's role and duties with that person, particularly covering legal and regulatory requirements and Module HC (see also HC-4.5.1).

HC-1.2.9 **The Islamic bank licensee must have a written appointment agreement with each director which recites the directors' powers, duties, responsibilities and accountabilities and other matters relating to his appointment including his term, the time commitment envisaged, the committee assignment if any, his remuneration and expense reimbursement entitlement, and his access to independent professional advice when that is needed.**

HC-1.2 Role and Responsibilities (continued)

Risk Recognition and Assessment

HC-1.2.10

The Board is responsible for ensuring that the systems and controls framework, including the Board structure and organisational structure of the bank, is appropriate for the bank's business and associated risks (see HC-1.2.2A (b) and HC-1.2.3 (e)). The Board must ensure that collectively it has sufficient expertise to identify, understand and measure the significant risks to which the bank is exposed in its business activities.

The Board must regularly assess the systems and controls framework of the bank. In its assessments, the Board must demonstrate to the CBB that:

(a) The bank's operations, individually and collectively are measured, monitored and controlled by appropriate, effective and prudent risk management systems commensurate with the scope of the bank's activities;

(b) The bank's operations are supported by an appropriate control environment. The compliance, risk management and financial reporting functions must be adequately resourced, independent of business lines and must be run by individuals not involved with the day-to-day running of the various business areas. The Board must additionally ensure that management develops, implements and oversees the effectiveness of comprehensive know your customer standards, as well as on-going monitoring of accounts and transactions, in keeping with the requirements of relevant law, regulations and best practice (with particular regard to anti-money laundering measures). The control environment must maintain necessary client confidentiality and ensure that the privacy of the bank is not violated, and ensure that clients' rights and assets are properly safeguarded; and

(c) Where the Board has identified any significant issues related to the bank's adopted governance framework, appropriate and timely action is taken to address any identified adverse deviations from the requirements of this Module.

HC-1.2.11

The Board must adopt a formal Board charter or other statement specifying matters which are reserved to it, which should include but need not be limited to the specific requirements and responsibilities of directors. This charter must cover the points in HC-1.2.1 to HC-1.2.10. Wherever possible, the documents referred to in HC-1.2.3 to HC-1.2.10 or a summary of responsibilities should be disclosed publicly, for example in the annual report, which must be submitted to the CBB in line with the requirements of Module BR.

HC-1.3 Decision Making Process

HC-1.3.1

The Board must be collegial and deliberative, to gain the benefit of each individual director's judgment and experience.

HC-1.3.2

The chairman must take an active lead in promoting mutual trust, open discussion, constructive dissent and support for decisions after they have been made.

HC-1.3.3

The Board must meet frequently to enable it to discharge its responsibilities effectively but in no event less than four times a year. All directors must attend the meetings whenever possible and the directors must maintain informal communication between meetings.

HC-1.3.4

Individual Board members must attend at least 75% of all Board meetings in a given financial year to enable the Board to discharge its responsibilities effectively (see table below). Voting and attendance proxies for Board meetings are prohibited at all times.

Meetings per year	75% Attendance requirement
4	3
5	4
6	5
7	5
8	6
9	7
10	8

HC-1.3.5

The absence of Board members at Board and committee meetings must be noted in the meeting minutes. In addition, Board attendance percentage must be reported during any general assembly meeting when Board members stand for re-election (e.g. Board member XYZ attended 95% of scheduled meetings this year).

HC-1.3.6

In the event that a Board member has not attended at least 75% of Board meetings in any given financial year, the bank must immediately notify the CBB indicating which member has failed to satisfy this requirement, his level of attendance and any mitigating circumstances affecting his non-attendance. The CBB shall then consider the matter and determine whether disciplinary action, including disqualification of that Board member pursuant to Article 65 of the CBB Law, is appropriate. Unless there are exceptional circumstances, it is likely that the CBB will take disciplinary action.

HC-1.3 Decision Making Process (continued)

HC-1.3.7 To meet its obligations under Rule HC-1.3.3 above, the full Board should meet once every quarter to address the Board's responsibilities for management oversight and performance monitoring. Furthermore, Board rules should require members to step down if they are not actively participating in Board meetings. Board members are reminded that non attendance at Board meetings does not absolve them of their responsibilities as directors. It is important that each individual director should allocate adequate time and effort to discharge his responsibilities. All Directors are expected to contribute actively to the work of the Board in order to discharge their responsibilities and should make every effort to attend Board meetings where major issues are to be discussed. Banks are encouraged to amend their Articles of Association to provide for telephonic and videoconference meetings. Participation in Board meetings by means of video or telephone conferencing is regarded as attendance and may be recorded as such.

HC-1.3.7A **At least half the Board meetings of Bahraini Islamic bank licensees in any twelve-month period must be held in the Kingdom of Bahrain.**

HC-1.3.8 **All locally incorporated banks are required to submit, on an annual basis, as an attachment to the year-end quarterly PIR, a report recording the meetings during the year by their Board of Directors. For a sample report, refer to Appendix BR-6, under Part B/CBB Reporting Forms of Volume 2.**

HC-1.3.9 **The Chairman is responsible for the leadership of the Board, and for the efficient functioning of the Board. The chairman must ensure that all directors receive an agenda, minutes of prior meetings, and adequate background information in writing before each Board meeting and when necessary between meetings. Therefore it is vital that the Chairman commit sufficient time to perform his role effectively. All directors must receive the same Board information. At the same time, directors have a legal duty to inform themselves and they must ensure that they receive adequate and timely information and must study it carefully (See also HC-7 for other duties of the Chairman).**

HC-1.3.9.A **The Chairman must possess the requisite experience, competencies and personal qualities in order to fulfill his responsibilities.**

HC-1.3.9.B **The Chairman must ensure that board decisions are taken on a sound and well-informed basis. He must encourage and promote critical discussion and ensure that dissenting views can be expressed and discussed within the decision-making process.**

HC-1.3 Decision Making Process (continued)

HC-1.3.10 The Board should have no more than 15 members, and should regularly review its size and composition to ensure that it is small enough for efficient decision making yet large enough to have members who can contribute from different specialties and viewpoints. Board perspective and the ability to exercise objective judgment can be enhanced by recruiting members from a sufficiently broad population of candidates. These candidates should be independent of the views of executive directors, directors appointed by controllers and senior management. Such candidates should also be independent of inappropriate political or personal interests, to the extent possible and practicable given the bank's size, complexity and geographical scope. The Board should recommend changes in Board size to the shareholders when a needed change requires amendment of the Islamic bank licensee's Memorandum of Association.

HC-1.3.11 Potential non-executive directors should be made aware of their duties before their nomination, particularly as to the time commitment required. The Nominating Committee should regularly review the time commitment required from each non-executive director and should require each non-executive director to inform the Committee before he accepts any Board appointments to another company.

HC-1.3.12 **No Board member may have more than one Directorship of a Retail Bank or a Wholesale Bank. This means an effective cap of a maximum of two Directorships of banks inside Bahrain. Two Directorships of licensees within the same Category (e.g. 'Retail Bank') are not permitted.**

HC-1.3.12A Serving as a board member or member of senior management of a bank that competes or does business with the bank can compromise board independence of judgment and potentially create conflicts of interest, as can cross-membership of boards. Banks may approach the CBB for exemption from the limit in Paragraph HC-1.3.12 where the directorships concern banks or financial institutions within the same group.

HC-1.3.13 One person should not hold more than three directorships in public companies in Bahrain with the provision that no conflict of interest may exist, and the Board should not propose the election or reelection of any director who does.

HC-1.4 Independence of Judgment

HC-1.4.1 **Every director must bring independent judgment to bear in decision-making. No individual or group of directors must dominate the Board's decision-making and no one individual should have unfettered powers of decision.**

HC-1.4.2 **Executive directors must provide the Board with all relevant business and financial information within their cognizance, and must recognise that their role as a director is different from their role as a member of management (see HC-2.3.2).**

HC-1.4.3 **Non-executive directors must be fully independent of management and must constructively scrutinise and challenge management including the management performance of executive directors.**

HC-1.4.4 **Where there is the potential for conflict of interest, or there is a need for impartiality, the Board must assign a sufficient number of qualified independent Board members capable of exercising independent judgement. At a minimum, all locally incorporated banks must appoint one independent director.**

HC-1.4.4A For purposes of Paragraph HC-1.4.4 above, acceptable qualifications for Board members (both professional and academic) are outlined in Appendix TC-1 of Module TC (Training and Competency).

HC-1.4.5 At least half of an Islamic bank licensee's Board should be non-executive directors and at least three of those persons should be independent directors. (Note the exception for controlled companies in Paragraph HC-1.5.2.)

HC-1.4.6 The chairman of the Board should be an independent director, so that there will be an appropriate balance of power and greater capacity of the Board for independent decision making.

HC-1.4.7 **The Chairman and/or Deputy Chairman must not be the same person as the Chief Executive Officer.**

HC-1.4.8 **The Chairman must not be an Executive Director.**

HC-1.4 Independence of Judgment (continued)

HC-1.4.9 The Board should review the independence of each director at least annually in light of interests disclosed by them, and their conduct. Each independent director should provide the Board with all necessary and updated information for this purpose.

HC-1.4.10 To facilitate free and open communication among independent directors, each Board meeting should be preceded or followed with a session at which only independent directors are present, except as may otherwise be determined by the independent directors themselves.

HC-1.5 Representation of all Shareholders

HC-1.5.1 **Each director must consider himself as representing all shareholders and must act accordingly. The Board must avoid having representatives of specific groups or interests within its membership and must not allow itself to become a battleground of vested interests. If the Islamic bank licensee has controllers (as defined by Module GR-5.2) (or a group of controllers acting in concert), the latter must recognise its or their specific responsibility to the other shareholders, which is direct and is separate from that of the Board of directors.**

HC-1.5.2 **In Islamic bank licensees with a controller, at least one-third of the Board must be independent directors. Minority shareholders must generally look to independent directors' diligent regard for their interests, in preference to seeking specific representation on the Board.**

HC-1.5.3 In Islamic bank licensees with controllers, both controllers and other shareholders should be aware of controllers' specific responsibilities regarding their duty of loyalty to the Islamic bank licensee and conflicts of interest, regardless of who appoints them, (see Chapter HC-2) and also of rights that minority shareholders may have to elect specific directors under the Company Law or if the Islamic bank licensee has adopted cumulative voting for directors. The chairman of the board or other individual delegated by the chairman of the board should take the lead in explaining this with the help of the Islamic bank licensee's lawyers. In cases where there are board members appointed by a controller, the board should set out specific procedures or conduct periodic reviews to ensure the appropriate discharge of responsibilities by all board members.

HC-1.6 Directors' Access to Independent Advice

HC-1.6.1 **The Board must ensure by way of formal procedures that individual directors have access to independent legal or other professional advice at the Islamic bank licensee's expense whenever they judge this necessary to discharge their responsibilities as directors and this must be in accordance with the Islamic bank licensee's policy approved by the Board.**

HC-1.6.2 **Individual directors must also have access to the Islamic bank licensee's corporate secretary, who must have responsibility for reporting to the Board on Board procedures. Both the appointment and removal of the corporate secretary must be a matter for the Board as a whole, not for the CEO or any other officer.**

HC-1.6.3 Whenever a director has serious concerns which cannot be resolved concerning the running of the Islamic bank licensee or a proposed action, he should consider seeking independent advice and should ensure that the concerns are recorded in the Board minutes and that any dissent from a Board action is noted or delivered in writing.

HC-1.6.4 Upon resignation, a non-executive director should provide a written statement to the chairman, for circulation to the Board, if he has any concerns such as those in Paragraph HC-1.6.3.

HC-1.7 Directors' Communication with Management

HC-1.7.1 **The Board must encourage participation by management regarding matters the Board is considering, and also by management members who by reason of responsibilities or succession, the CEO believes should have exposure to the directors.**

HC-1.7.2 Non-executive directors should have free access to the Islamic bank licensee's management beyond that provided in Board meetings. Such access should be through the Chairman of the Audit Committee or CEO. The Board should make this policy known to management to alleviate any management concerns about a director's authority in this regard.

HC-1.8 Committees of the Board

HC-1.8.1 **To increase efficiency and allow deeper focus in specific areas, the Board must create specialised committees when and as such committees are needed.**

HC-1.8.1A The number and nature of committees depends on many factors, including the size of the bank and its board, the nature of the business areas of the bank, and its risk profile. In addition to the Audit, Corporate Governance, Remuneration and Nominating Committees and Shari'a Supervisory Board described elsewhere in this Module, these may include an Executive Committee to review and make recommendations to the whole Board on the bank's actions, or a Risk Committee to identify and minimize specific risks of the Islamic bank licensee's business.

HC-1.8.1.B To avoid undue concentration of power and to promote fresh perspectives, the board should consider occasional rotation of membership and chairmanships of the board committees provided that doing so does not impair the collective skills, experience, and effectiveness of these committees.

HC-1.8.2 The Board should establish a corporate governance committee of at least three independent members which should be responsible for developing and recommending changes from time to time in the Islamic bank licensee's corporate governance policy framework.

HC-1.8.3 **The Board or a committee may invite non-directors to participate in, but not vote at, a committee's meetings so that the committee may gain the benefit of their advice and expertise in financial or other areas.**

HC-1.8.4 **Committees must act only within their mandates and therefore the Board must not allow any committee to dominate or effectively replace the whole Board in its decision-making responsibility.**

HC-1.8.5 **Committees may be combined provided that no conflict of interest might arise between the duties of such committees, subject to CBB prior approval.**

HC-1.8.6 **Every committee must have a formal written charter, which sets out its mandate, scope and working procedures, similar in form to the model charters which are set forth in Appendices A, B and C of this Module for the Audit, Nominating and Remuneration Committees.**

HC-1.8 Committees of the Board (continued)

HC-1.8.7 **Where committees are set up, they must maintain appropriate records (e.g. full minutes of their activities or summary of matters reviewed and decisions taken) and meet regularly to fulfil their mandates.**

HC-1.8.8 For larger banks that deal with the general public, committees can be a more efficient mechanism to assist the main Board in its monitoring and control of the activities of the bank. The establishment of committees should not mean that the role of the Board is diminished, or that the Board becomes fragmented.

HC-1.8.9 The board should establish a risk committee or equivalent, responsible for advising the board on the bank's overall current and future risk tolerance/appetite and strategy, and for overseeing senior management's implementation of that strategy. This should include strategies for capital and liquidity management, as well as for credit, market, operational, compliance, reputational and other risks of the bank. To enhance the effectiveness of the risk committee, it should receive formal and informal communication from the bank's risk management function and should, where appropriate, have access to external expert advice.

HC-1.8.10 The board should appoint members to specialised committees such as those mentioned in Paragraph HC-1.8.1A with the goal of achieving an optimal mix of skills and experience that, in combination, allow the committees to fully understand, objectively evaluate and bring fresh thinking to the relevant issues. In order to achieve the needed objectivity, membership should be composed of non-executives and to the extent possible, a majority of independent members.

HC-1.8.11 In cases where a pool of independent candidates is not available, committee membership should strive to mix skills and experience in order to maximise objectivity.

HC-1.8.12 Notwithstanding the composition of the specialised committees, it may be beneficial for independent members to meet separately, both among themselves and with the relevant control functions, on a regular basis to ensure frank and timely dialogue. In addition, board consideration of risk-related issues may be enhanced by members serving on more than one committee (subject to constraints on member's time). For example, a member who serves on the remuneration committee while also serving on either the risk or audit committee may have a greater appreciation of risk considerations in these areas.

HC-1.9 Evaluation of the Board and Each Committee

HC-1.9.1 **At least annually the Board must conduct an evaluation of its performance and the performance of each committee and each individual director.**

HC-1.9.2 **The evaluation process must include:**

(a) Assessing how the Board operates, especially in light of Chapter HC-1;

(b) Evaluating the performance of each committee in light of its specific purposes and responsibilities, which must include review of the self-evaluations undertaken by each committee;

(c) Reviewing each director's work, his attendance at Board and committee meetings, and his constructive involvement in discussions and decision making;

(d) Reviewing the Board's current composition against its desired composition with a view toward maintaining an appropriate balance of skills and experience and a view toward planned and progressive refreshing of the Board; and

(e) Recommendations for new Directors to replace long-standing members or those members whose contribution to the bank or its committees (such as the audit committee) is not adequate.

HC-1.9.3 While the evaluation is a responsibility of the entire Board, it should be organised and assisted by an internal Board committee and, when appropriate, with the help of external experts.

HC-1.9.4 The Board should report to the shareholders, at each annual shareholder meeting, that evaluations have been done and report its findings.

HC-1.9.5 Where the board has serious reservations about the performance or integrity of a board member, the board should take appropriate actions.

HC-2.1 Principle

HC-2.1.1 **The <u>approved persons</u> must have full loyalty to the <u>Islamic bank licensee</u>.**

HC-2.2 Personal Accountability

HC-2.2.1 Banks are subject to a wide variety of laws, regulations and codes of best practice that directly affect the conduct of business. Such laws involve the Bahraini Stock Exchange Law, the Labour Law, the Company Law, occupational health and safety, even environment and pollution laws, as well as the Law, codes of conduct and regulations of the CBB. The Board sets the 'tone at the top' of a bank, and has a responsibility to oversee compliance with these various requirements. The Board should ensure that the staff conduct their affairs with a high degree of integrity, taking note of applicable laws, codes and regulations.

Corporate Ethics, Conflicts of Interest and Code of Conduct

HC-2.2.2 **Each member of the board must understand that under the Company Law he is personally accountable to the Islamic bank licensee and the shareholders if he violates his legal duty of loyalty to the Islamic bank licensee, and that he can be personally sued by the Islamic bank licensee or the shareholders for such violations.**

HC-2.2.3 **The Board must establish corporate standards for approved persons and employees. This requirement should be met by way of a documented and published code of conduct or similar document. These standards must be communicated throughout the bank, so that the approved persons and staff understand the importance of conducting business based on good corporate governance values and understand their accountabilities to the various stakeholders of the licensee. Banks' approved persons and staff must be informed of and be required to fulfil their fiduciary responsibilities to the bank's stakeholders.**

HC-2.2.4 An internal code of conduct is separate from the business strategy of a bank. A code of conduct should outline the practices that approved persons and staff should follow in performing their duties. Banks may wish to use procedures and policies to complement their codes of conduct. The suggested contents of a code of conduct are covered below:

(a) *Commitment by the Board and management to the code.* The code of conduct should be linked to the objectives of the bank, and its responsibilities and undertakings to customers, shareholders, staff and the wider community (see HC-2.2.3 and HC-2.2.4). The code should give examples or expectations of honesty, integrity, leadership and professionalism;

HC-2.2 Personal Accountability (continued)

(b) *Commitment to the law and best practice standards.* This commitment would include commitments to following accounting standards, industry best practice (such as ensuring that information to clients is clear, fair, and not misleading), transparency, and rules concerning potential conflicts of interest (see HC-2.3);
(c) *Employment practices.* This would include rules concerning health and safety of employees, training, policies on the acceptance and giving of business courtesies, prohibition on the offering and acceptance of bribes, and potential misuse of Islamic bank licensee's assets;
(d) How the Islamic bank licensee deals with *disputes and complaints* from clients and monitors compliance with the code;
(e) *Confidentiality.* Disclosure of client or bank information should be prohibited, except where disclosure is required by law (see HC-1.2.10 b);
(f) *Improper and illegal behaviour.* The Code should disallow behaviour that could result in the bank engaging in any improper or illegal activity, such as financial misreporting, money laundering, fraud, bribery or corruption; and
(g) *Excessive risk taking.* The Code should discourage the taking of excessive risks as defined by internal corporate policy.

HC-2.2.5 The CBB expects that the Board and its members individually and collectively:
(a) Act with honesty, integrity and in good faith, with due diligence and care, with a view to the best interest of the bank and its shareholders and other stakeholders (see Paragraphs HC-2.2.2 to HC-2.2.4);
(b) Act within the scope of their responsibilities (which should be clearly defined – see HC-1.2.9 and HC-1.2.11 and not participate in the day-to-day management of the bank;
(c) Have a proper understanding of, and competence to deal with the affairs and products of the bank and devote sufficient time to their responsibilities;
(d) Possess appropriate experience, competencies and personal qualities, including professionalism and integrity (see Paragraph HC-2.2.8); and
(e) Independently assess and question the policies, processes and procedures of the bank, with the intent to identify and initiate management action on issues requiring improvement. *(i.e. to act as checks and balances on management).*

HC-2.2.6 **The duty of loyalty (mentioned in Paragraph HC-2.2.2) includes a duty not to use property of the Islamic bank licensee for his personal needs as though it was his own property, not to disclose confidential information of the Islamic bank licensee or use it for his personal profit, not to take business opportunities of the Islamic bank licensee for himself, not to compete in business with the Islamic bank licensee, and to serve the Islamic bank licensee's interest in any transactions with a company in which he has a personal interest.**

HC-2.2 Personal Accountability (continued)

HC-2.2.6A **[This Paragraph was moved to Paragraph HC-5.4.39].**

HC-2.2.6B [This Paragraph was moved to Paragraph HC-5.4.40].

HC-2.2.7 **For purposes of Paragraph HC-2.2.6, an <u>approved person</u> should be considered to have a "personal interest" in a transaction with a company if:**

(a) He himself; or

(b) A member of his family (i.e. spouse, father, mother, sons, daughters, brothers or sisters); or

(c) Another company of which he is a director or controller,

is a party to the transaction or has a material financial interest in the transaction. (Transactions and interests which are de minimis in value should not be included.)

HC-2.2.8 The Board collectively should have adequate knowledge and experience relevant to each of the material financial activities that the bank intends to pursue in order to enable effective governance and oversight. Examples of areas where the Board should seek to have, or have access to, appropriate experience or expertise include finance, accounting, lending, bank operations and payment systems, strategic planning, communications, governance, risk management, internal controls, bank regulation, auditing and compliance.

HC-2.3 Avoidance of Conflicts of Interest

HC-2.3.1

Each approved person must make every practicable effort to arrange his personal and business affairs to avoid a conflict of interest with the Islamic bank licensee.

HC-2.3.2

The Board must establish and disseminate to its members and management, policies and procedures for the identification, reporting, disclosure, prevention, or strict limitation of potential conflicts of interest. It is senior management's responsibility to implement these policies. Rules concerning connected party transactions and potential conflicts of interest may be dealt with in the Code of Conduct (see HC-2.2.4). In particular, the CBB requires that any decisions to enter into transactions, under which approved persons would have conflicts of interest that are material, should be formally and unanimously approved by the full Board. Best practice would dictate that an approved person must:

(a) Not enter into competition with the bank;
(b) Not demand or accept substantial gifts from the bank for himself or connected persons;
(c) Not misuse or misappropriate the bank's assets or resources;
(d) Not use the Islamic bank licensee's privileged information or take advantage of business opportunities to which the Islamic bank licensee is entitled, for himself or his associates; and
(e) Absent themselves from any discussions or decision-making that involves a subject where they are incapable of providing objective advice, or which involves a subject or (proposed) transaction where a conflict of interest exists.

HC-2.4 Disclosure of Conflicts of Interest

HC-2.4.1 **Each approved person must inform the entire Board of (potential) conflicts of interest in their activities with, and commitments to other organisations as they arise. Board members must abstain from voting on the matter in accordance with the relevant provisions of the Company Law. This disclosure must include all material facts in the case of a contract or transaction involving the approved person. The approved persons must understand that any approval of a conflicted transaction is effective only if all material facts are known to the authorising persons and the conflicted person did not participate in the decision. In any case, all approved persons must declare in writing all of their other interests in other enterprises or activities (whether as a shareholder of above 5% of the voting capital of a company, a manager, or other form of significant participation) to the Board (or the Nominations or Audit Committees) on an annual basis.**

HC-2.4.2 The Board should establish formal procedures for:

(a) Periodic disclosure and updating of information by each approved person on his actual and potential conflicts of interest; and

(b) Advance approval by directors or shareholders who do not have an interest in the transactions in which an Islamic bank licensee's approved person has a personal interest. The Board should require such advance approval in every case.

HC-2.4.3 Conflicts of interest may arise:

(a) As a result of the various activities and roles of the bank (e.g. where the bank extends loans to a firm while its proprietary trading function buys and sells securities issued by that firm);

(b) Between the interests of the bank or its customers and those of the bank's board members or senior managers (e.g. where the bank enters into a business relationship with an entity in which one of the bank's board members has a financial interest); or

(c) When a bank is part of a broader group where reporting lines and information flows between the bank, its parent company and/or other subsidiaries can lead to the emergence of similar conflicts of interest (e.g. sharing of potential proprietary, confidential or otherwise sensitive information from different entities).

HC-2.4.4 **The board must ensure that policies to identify potential conflicts of interest are developed and implemented and, if these conflicts cannot be prevented, that these conflicts are appropriately managed (based on the permissibility of relationships or transactions under sound corporate policies consistent with relevant laws in Bahrain and CBB standards).**

HC-2.4 Disclosure of Conflicts of Interest (continued)

HC-2.4.5 For purposes of Paragraph HC-2.4.4, relevant laws in Bahrain refer to the Company Law and the Commerce Law.

HC-2.4.6 The board must have a formal written conflict of interest policy and an objective compliance process for implementing the policy. The policy must include:

(a) A member's duty to avoid to the extent possible activities that could create conflicts of interest or the appearance of conflicts of interest;

(b) A review or approval process for members to follow before they engage in certain activities (such as serving on another board) so as to ensure that such activity will not create a conflict of interest;

(c) A member's duty to disclose any matter that may result, or has already resulted, in a conflict of interest;

(d) A member's responsibility to abstain from voting on any matter where the member may have a conflict of interest or where the member's objectivity or ability to properly fulfil duties to the bank may be otherwise compromised;

(e) Adequate procedure for transactions with related parties to be made on an arm's-length basis; and

(f) The way in which the board will deal with any non-compliance with the policy.

HC-2.5 Disclosure of Conflicts of Interest to Shareholders

HC-2.5.1 **The Islamic bank licensee must disclose to its shareholders in the Annual Report (See PD-1.3.8) any abstention from voting motivated by a conflict of interest and must disclose to its shareholders any authorisation of a conflict of interest contract or transaction in accordance with the Company Law.**

HC-2.5.2 At every Islamic bank licensee's annual shareholder meeting, corporate governance should be an item on the agenda for information and any questions from shareholders regarding the Islamic bank licensee's governance. Where possible, the Islamic bank licensee should also have corporate governance guidelines in place at that time and should have a "comply or explain" report as described in Paragraph HC-A.1.8.

HC-3.1 Principle

HC-3.1.1

The Board must have rigorous controls for financial audit and reporting, internal control, and compliance with law. As part of this overall Principle, the board and senior management must effectively utilise the work conducted by internal audit, the compliance officer, other control functions and external auditors.

HC-3.1.2 The board should recognise and acknowledge that independent, competent and qualified internal and external auditors, as well as compliance function and other internal control functions, are vital to the corporate governance process in order to achieve a number of important objectives. Senior management should also recognise the importance of the effectiveness of these functions to the long-term soundness of the bank.

HC-3.2 Audit Committee

HC-3.2.1

The Board must establish an audit committee of at least three directors of which the majority must be independent including the Chairman. The committee must:

(a) Review and monitor the Islamic bank licensee's accounting and financial practices through close cooperation with the internal and external auditors;
(b) Review the integrity of the Islamic bank licensee's financial and internal controls and financial statements (particularly with reference to information passed to the Board - see HC-1.2.10). The information needs of the Board to perform its monitoring responsibilities must be defined in writing, and regularly monitored by the Audit Committee;
(c) Review the Islamic bank licensee's compliance with legal requirements and provide the Board with reports and recommendations with a particular reference to the Islamic bank licensee's compliance with relevant International Financial Reporting Standards (IFRS) and AAOIFI issued accounting, auditing and governance standards in reporting their financial and non-financial information;
(d) Recommend the appointment, compensation and oversight of the Islamic bank licensee's external auditor and review its compliance with applicable codes and standards of professional practice;
(e) Recommend the appointment of the internal auditor;
(f) Review internal and external audit reports and compliance review reports;
(g) Regularly check with those responsible for the compliance function of the Islamic bank licensee to ensure that the bank is in full compliance with regulatory requirements; and
(h) Communicate and coordinate with both the SSB and the Corporate Governance Committee to ensure that information on compliance with Islamic Shari'a rules and principles by the Islamic bank licensee is reported in a timely and adequate manner.

HC-3.2 Audit Committee (continued)

HC-3.2.2

In its review of the systems and controls framework in Paragraph HC-3.2.1, the audit committee must:

(a) Make effective use of the work of external and internal auditors. The audit committee must ensure the integrity of the bank's accounting and financial reporting systems through regular independent review (by internal and external audit). Audit findings must be used as an independent check on the information received from management about the bank's operations and performance and the effectiveness of internal controls; and

(b) Make use of self-assessments, stress/scenario tests, and/or independent judgements made by external advisors. The Board should appoint supporting committees, and engage senior management to assist the audit committee in the oversight of risk management;

(c) Ensure that senior management have put in place appropriate systems of control for the business of the bank and the information needs of the Board; in particular, there must be appropriate systems and functions for identifying as well as for monitoring risk, the financial position of the bank, and compliance with applicable laws, regulations and best practice standards. The systems must produce information on a timely basis;

(d) Ensure that senior management is taking necessary corrective actions in a timely manner to control weaknesses, non-compliance with policies, laws and regulations and other problems identified by internal or external auditors and the compliance officer; and

(e) Oversee the establishment of accounting policies and practices by the bank.

HC-3.2 Audit Committee (continued)

HC-3.2.3 **The Islamic bank licensee must set up an internal audit function, which reports directly to the Audit Committee and administratively to the CEO.**

HC-3.2.3A The board and senior management can enhance the ability of the internal audit function to identify problems with a bank's governance, risk management and internal control systems by:

(a) Encouraging internal auditors to adhere to national and international professional standards, such as those established by the Institute of Internal Auditors;
(b) Requiring that audit staff have skills that are commensurate with the business activities and risks of the bank;
(c) Promoting the independence of the internal auditor, for example by ensuring that internal audit reports are provided to the board and the internal auditor has direct access to the board or the board's audit committee;
(d) Recognising the importance of the audit and internal control processes and communicating their importance throughout the bank;
(e) Requiring the timely and effective correction of identified internal audit issues by senior management; and
(f) Engaging internal auditors to judge the effectiveness of the risk management function and the compliance function, including the quality of risk reporting to the board and senior management, as well as the effectiveness of other key control functions.

HC-3.2.4 **The CEO must not be a member of the audit committee.**

HC-3.3 Audit Committee Charter

HC-3.3.1 **The audit committee must adopt a written charter which must, at a minimum, state the duties outlined in Paragraph HC-3.2.1 and the other matters included in Appendix A to this Module.**

HC-3.3.2 **A majority of the audit committee must have the financial literacy qualifications stated in Appendix A.**

HC-3.3.3 The Board should adopt a "whistleblower" program under which employees can confidentially raise legitimate concerns about illegal, unethical or questionable practices. Under the program, concerns may be communicated directly to any audit committee member or, alternatively, to an identified officer or employee who will report directly to the Audit Committee on this point. The Board should determine how and by whom legitimate concerns shall be investigated and addressed.

HC-3.4 CEO and CFO Certification of Financial Statements

HC-3.4.1 **To encourage management accountability for the financial statements required by the directors, the Islamic bank licensee's CEO and chief financial officer must state in writing to the audit committee and the Board as a whole that the Islamic bank licensee's interim and annual financial statements present a true and fair view, in all material respects, of the Islamic bank licensee's financial condition and results of operations in accordance with applicable accounting standards.**

HC-4.1 Principle

HC-4.1.1

The Islamic bank licensee must have rigorous and transparent procedures for appointment, training and evaluation of the Board and senior management.

HC-4.2 Nominating Committee

HC-4.2.1

The Board must establish a Nominating Committee of at least three directors which must:

(a) Identify persons qualified to become members of the Board of directors or Chief Executive Officer, Chief Financial Officer, Corporate Secretary and any other officers of the Islamic bank licensee considered appropriate by the Board, with the exception of the appointment of the internal auditor which must be the responsibility of the Audit Committee in accordance with Paragraph HC-3.2.1 above;

(b) Make recommendations to the whole Board of directors including recommendations of candidates for Board membership to be included by the Board of directors on the agenda for the next annual shareholder meeting; and

(c) Oversee the bank's personnel or human resource policies.

HC-4.2.2

The committee must include only independent directors or, alternatively, only non-executive directors of whom a majority must be independent directors and the chairman must be an independent director. This is consistent with international best practice and it recognises that the Nominating Committee must exercise judgment free from personal career conflicts of interest.

HC-4.3 Nominating Committee Charter

HC-4.3.1 The Nominating Committee must adopt a formal written charter which must, at a minimum, state the duties outlined in Paragraphs HC-4.2.1, HC-1.3.11 and the other matters included in Appendix B to this Module.

HC-4.4 Board Nominations to Shareholders

HC-4.4.1 **Each proposal by the Board to the shareholders for election or reelection of a director must be accompanied by a recommendation from the Board, a summary of the advice of the Nominating Committee, and the following specific information:**

(a) The term to be served, which may not exceed three years (but there need not be a limit on reelection for further terms);
(b) Biographical details and professional qualifications;
(c) In the case of an independent director, a statement that the Board has determined that the criteria of independent director have been met;
(d) Any other directorships held;
(e) Particulars of other positions which involve significant time commitments, and
(f) Details of relationships between:
  (i) The candidate and the Islamic bank licensee, and
  (ii) The candidate and other directors of the Islamic bank licensee.

HC-4.4.2 The chairman of the Board should confirm to shareholders when proposing re-election of a director that, following a formal performance evaluation, the person's performance continues to be effective and continues to demonstrate commitment to the role. Any term beyond six years (e.g. two three-year terms) for a director should be subject to particularly rigorous review, and should take into account the need for progressive refreshing of the Board. Serving more than six years is relevant to the determination of a non-executive director's independence.

HC-4.5 Induction and Training of Directors

HC-4.5.1 **The chairman of the Board must ensure that each new director receives a formal and tailored induction to ensure his contribution to the Board from the beginning of his term. The induction must include meetings with senior management, visits to the Islamic bank licensee's facilities, presentations regarding strategic plans, significant financial, accounting and risk management issues, compliance programs, its internal and external auditors and legal counsel.**

HC-4.5.2 **All continuing directors must be invited to attend orientation meetings and all directors must continually educate themselves as to the Islamic bank licensee's business and corporate governance.**

HC-4.5.3 Management, in consultation with the chairman of the Board, should hold programs and presentations to directors respecting the Islamic bank licensee's business and industry, which may include periodic attendance at conferences and management meetings. The Nominating Committee should oversee directors' corporate governance educational activities.

HC-5.1 Principle

HC-5.1.1

The Islamic bank licensee must remunerate approved persons and material risk-takers fairly and responsibly. The board of directors must actively oversee the remuneration system's design and operation for approved persons as well as for material risk-takers. The CEO and senior management must not primarily control the remuneration system.

HC-5.2 Role of the Board of Directors and Remuneration Committee

HC-5.2.1AA **[This paragraph has been moved to HC-5.1.1]**

HC-5.2.1 **The Board must establish a remuneration committee of at least three directors which must:**

(a) Have responsibility for the overall design and operation of the remuneration system of the entire bank;

(b) Review the Islamic bank licensee's remuneration policies for the approved persons and material risk-takers, which must be approved by the shareholders and be consistent with the corporate values and strategy of the bank as well as with any legal or regulatory requirements;

(c) Approve the remuneration policy and amounts for each approved person and material risk-taker, as well as the total variable remuneration to be distributed, taking account of total remuneration including salaries, fees, expenses, bonuses and other employee benefits;

(d) Approve, monitor and review the remuneration system to ensure the system operates as intended; and

(e) Recommend Board member remuneration based on their attendance and performance and in compliance with Article 188 of the Company Law.

HC-5.2.1A In reviewing the remuneration system (see Subparagraph HC-5.2.1(d)), the remuneration committee should ensure that the system includes effective controls, including back testing and stress testing of the remuneration policy. The practical operation of the system should be regularly reviewed for compliance with regulations, internal policies and bank procedures. In addition, remuneration outcomes, risk measurements, and risk outcomes should be regularly reviewed by the Board for consistency with Board's approved risk appetite.

HC-5.2.1B Stress testing or stressed measures might be used by banks to help ex-ante risk adjustments take into account severe but plausible scenarios, based on possible expected loss on loans, as an example. Due to the uncertainty of payoffs, there will always be a need for ex-post adjustments so as to back-test actual performance against risk assumptions.

HC-5.2.1C **As part of the duties noted under Paragraph HC-5.2.1, the remuneration committee must carefully evaluate practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. It must demonstrate that its decisions are consistent with an assessment of the bank's financial condition and future prospects.**

HC-5.2.2 The committee may be merged with the nominating committee.

HC-5.3 Remuneration Committee Charter, Membership Criteria and Scope of Operation

HC-5.3.1 **The committee must adopt a written charter which must, at a minimum, state the duties in Paragraph HC-5.2.1 and other matters in Appendix C of this Module.**

HC-5.3.1A **Members of the remuneration committee must have independence of any risk taking function or committees.**

HC-5.3.2 The committee should include only independent directors with substantial knowledge about remuneration arrangements and the incentives and risks that arise from such arrangements. Members should have an understanding of the bank's risk measurement and management. The remuneration committee should work closely with the bank's risk committee to evaluate incentives arising from remuneration and ensure that an annual remuneration review is undertaken.

HC-5.3.3 The criteria mentioned in Paragraph HC-5.3.2 are consistent with international best practice and recognise that the Remuneration Committee should exercise judgment free from personal career conflicts of interest.

HC-5.4 Standard for all Remuneration

HC-5.4.1 **Remuneration of approved persons and material risk-takers must be sufficient enough to attract, retain and motivate persons of the quality needed to run the Islamic bank licensee successfully, but the Islamic bank licensee must avoid paying more than is necessary for that purpose.**

HC-5.4.2 **While this Section applies to all approved persons and material risk-takers for the Bahrain operations, the rules on the proportion of fixed and variable remuneration (Paragraph HC-5.4.30) as well as those rules related to the deferral of variable remuneration (Paragraphs HC-5.4.31 and HC-5.4.32) and the obligation to have part of the variable remuneration in shares (Paragraphs HC-5.4.33 and HC-5.4.34) apply only to:**

(a) Approved persons; or

(b) Material risk-takers

whose total annual remuneration (including all benefits) is in excess of BD100,000, unless the board of directors requires the application of these Rules to all staff.

HC-5.4.3 All policies for performance-based incentives should be approved by the shareholders, but the approval should be only of the plan itself and not of the grant to specific individuals of benefits under the plan.

HC-5.4.3A As noted in Sections AU-3.7 and BR-4A.3, the external auditor must undertake an annual review of the bank's compliance with the remuneration Rules outlined in this Chapter. The results of this review are to be submitted to the CBB within 3 months from the financial year end.

Application to Overseas Islamic Banks

HC-5.4.4 **Banks operating as overseas Islamic bank licensees in Bahrain must apply the most stringent set of remuneration rules to which they may be subject to. Such rules are:**

(a) The requirements imposed in Bahrain with respect to remuneration as outlined in Volume 1 CBB Rulebook; and

(b) The requirements imposed by their home supervisor and head office.

HC-5.4.5 **[This Paragraph was deleted in January 2015.]**

HC-5.4 Standard for all Remuneration (continued)

HC-5.4.6 [Moved to Paragraph HC-5.4.3A in January 2015.]

Approved Persons in Risk Management, Internal Audit, Operations, Financial Controls, Internal Shari'a Review/Audit, AML and Compliance Functions

HC-5.4.7 **The bank's approved persons engaged in risk management, internal audit, operations, financial controls, internal Shari'a review/audit, AML and compliance functions must be independent, have appropriate authority, and be remunerated in a manner that is independent of the business areas they oversee and commensurate with their key role in the bank. Effective independence and appropriate authority of such staff are necessary to preserve the integrity of financial risk and management's influence on incentive remuneration.**

HC-5.4.8 **The performance measures of approved persons referred to in Paragraph HC-5.4.7 must be based principally on the achievement of the objectives and targets of their functions.**

HC-5.4.9 **The mix of fixed and variable remuneration for risk management, internal audit, operations, financial controls, internal Shari'a review/audit, AML and compliance functions personnel must be weighted in favour of fixed remuneration.**

Effective Alignment of Remuneration with Prudent Risk-Taking

HC-5.4.10 **Remuneration must be adjusted for all types of risks.**

HC-5.4.11 In relation to Paragraph HC-5.4.10, two employees who generate the same short-run profit but take different amounts of risk on behalf of their bank should not be treated the same by the remuneration system.

HC-5.4.12 **Both quantitative measures and human judgement must play a role in determining risk adjustments.**

HC-5.4 Standard for all Remuneration (continued)

HC-5.4.13 Risk adjustments must account for all types of risk, including intangible and other risks such as reputation risk, liquidity risk and the cost of capital.

HC-5.4.14 Banks' remuneration policies and practices must be designed to reduce employees' incentives to take excessive and undue risk.

HC-5.4.15 Remuneration outcomes must be symmetric with risk outcomes.

HC-5.4.16 The mix of cash, equity and other forms of remuneration must be consistent with risk alignment. The mix will vary depending on the employee's position and role and the bank must be able to explain the rationale for its mix to the CBB.

HC-5.4.17 Existing contractual payments related to a termination of employment must be re-examined, and kept in place only if there is a clear basis for concluding that they are aligned with long-term value creation and prudent risk-taking. Prospectively, any such payments must be related to performance achieved over time and designed in a way that does not reward failure.

HC-5.4.18 Banks must ensure that their employees commit themselves not to use personal hedging strategies or remuneration- and liability-related insurance to undermine the risk alignment effects embedded in their remuneration arrangements. Banks must ensure that appropriate compliance mechanisms are in place to monitor their employees commitment in this regard such as signed adherence by staff to the bank's code of ethics which should include the conditions outlined in this Paragraph.

Variable Remuneration

HC-5.4.19 Remuneration systems must link the size of the bonus pool to the overall performance of the bank.

HC-5.4.20 Employees' incentive payments must be linked to the contribution of the individual and business to such performance.

HC-5.4.21 As profits and losses of different activities of a bank are realised over different periods of time, remuneration payout schedules must be sensitive to the time horizon of risks and variable remuneration must therefore be deferred accordingly. Variable remuneration must not be finalised over short periods where risks are realised over long periods.

HC-5.4 Standard for all Remuneration (continued)

HC-5.4.22 **The remuneration committee of the bank must question payouts for income that cannot be realised or whose likelihood of realisation remains uncertain at the time of payout.**

HC-5.4.23 **Banks must ensure that total variable remuneration does not limit their ability to strengthen their capital base. The extent to which capital needs to be built up must be a function of a bank's current capital position and its ICAAP.**

HC-5.4.24 **The size of the variable remuneration pool and its allocation within the bank must take into account the full range of current and potential risks, including:**

(a) The cost and quantity of capital required to support the risks taken;

(b) The cost and quantity of the liquidity risk assumed in the conduct of business; and

(c) Consistency with the timing and likelihood of potential future revenues incorporated into current earnings.

HC-5.4.25 Paragraph HC-5.4.24 focuses on the overall size of the variable remuneration, at the overall bank level, in order to ensure that the recognition and accrual of variable remuneration will not compromise the financial soundness of the bank.

HC-5.4.26 **Bonuses must diminish or be deferred in the event of poor bank, divisional or business unit performance.**

HC-5.4.27 Subdued or negative financial performance of the bank should generally lead to a considerable contraction of the bank's total variable remuneration, taking into account both current remuneration and reductions in payouts of amounts previously earned, including through malus and clawback arrangements. Recognition of staff who have achieved their targets or better, may take place by way of deferred compensation, which may be paid once the bank's performance improves.

HC-5.4.28 **If the bank and/or relevant line of business is incurring losses in any year during the vesting period, any unvested portions must be subject to <u>malus</u>.**

HC-5.4.29 Accrual and deferral of variable remuneration does not oblige the bank to pay the variable remuneration, particularly when the anticipated outcome has not materialised or the bank's financial position does not support such payments.

HC-5.4 Standard for all Remuneration (continued)

HC-5.4.30 **For approved persons and material risk-takers, other than those covered under Paragraphs HC-5.4.9 and Section HC-5.5, as their actions have a material impact on the risk exposure of the bank:**

(a) A substantial proportion of remuneration must be variable and paid on the basis of individual, business-unit and bank-wide measures that adequately measure performance; and

(b) The variable proportion of remuneration must increase significantly along with the level of seniority and/or responsibility.

HC-5.4.30A In Subparagraph HC-5.4.30(a), the word 'substantial' refers to a proportion of the total remuneration above 40%. Where employment contracts that are in place have a lower level of variable remuneration, the bank concerned should agree with the CBB on alternative arrangements.

HC-5.4.31 **For purposes of Paragraph HC-5.4.30:**

(a) At least 40% of the variable remuneration must be payable under deferral arrangements over a period of at least 3 years; and

(b) For the CEO, his deputies and the other 5 most highly paid business line employees, at least 60% of the variable remuneration must be payable under deferral arrangements over a period of at least 3 years.

HC-5.4.32 The deferral period referred to under Subparagraph HC-5.4.31(a) must be aligned with the nature of the business, its risks and the activities of the employee in question. Remuneration payable under deferral arrangements should generally vest no faster than on a pro rata basis.

HC-5.4.33 **As a minimum, 50% of variable remuneration (including both the deferred and undeferred portions of the variable remuneration) must be awarded in shares or share-linked instruments or where appropriate, other non-cash instruments.**

HC-5.4.34 **The remaining portion (other than that mentioned under Paragraph HC-5.4.33) of the deferred remuneration can be paid as cash remuneration vested over a minimum 3-year period.**

HC-5.4.34A **The only instance where deferred remuneration can be paid out before the end of the vesting period is in the case of the death of the employee where the beneficiaries would receive any unpaid deferred remuneration.**

HC-5.4 Standard for all Remuneration (continued)

HC-5.4.35 **Banks must not provide any form of guaranteed variable remuneration as part of the overall remuneration package. Exceptional minimum variable remuneration must only occur in the context of hiring new staff and limited to the first year.**

Remuneration in the Form of Shares or Share-Linked Instruments

HC-5.4.36 **Awards in shares or share-linked instruments must be subject to a minimum share retention policy of 6 months from the time the shares are awarded, unless the bank's policy requires a longer period.**

HC-5.4.37 **For Bahraini Islamic bank licensees, where fixed or variable remuneration include common shares, banks must limit the shares awarded to an annual aggregate limit of 10% of the total issued shares outstanding of the bank, at all times.**

HC-5.4.38 **For Bahraini Islamic bank licensees, all share incentive plans must be approved by the shareholders.**

Remuneration from Projects and Investments

HC-5.4.39 **In reference to Paragraph HC-2.2.6, for greater certainty, approved persons are not allowed to take any benefits from any projects or investments which are managed by the Islamic bank licensee or promoted to its customers or potential customers except for board related remuneration (declared as per Paragraph HC-2.4.1) linked to their fiduciary duties to the investors of the project/investment. This Rule applies to all approved persons including those appointed as members of the board of special purpose vehicles or other operating companies set up by the Islamic bank licensee for projects or investments.**

HC-5.4.40 The reference to benefits in Paragraph HC-5.4.39 includes commission, fees, shares, consideration in kind, or other remuneration or incentives in respect of the performance of the project or investment

HC-5.5 Board of Directors' Remuneration

HC-5.5.1 **Remuneration of non-executive directors must not include performance-related elements such as grants of shares, share options or other deferred stock-related incentive schemes, bonuses, or pension benefits.**

HC-5.5.2 **The Board of Directors' remuneration must be capped so that total remuneration is in line with Article 188 of the Company Law, in any financial year and has been approved by the shareholders.**

HC-5.5.3 **If a senior manager is also a director, his remuneration as a senior manager must take into account compensation received in his capacity as a director.**

HC-5.5.4 **In the years where the bank has not generated any profits it must comply with the approval requirements of Article 188 of the Company Law.**

HC-5.5.5 **In addition to the requirements of Article 188 of the Company Law, the articles of association regarding remuneration of the board of directors must be in line with the Rules outlined in this Chapter.**

HC-5.6 [This Section was deleted and is replaced with requirements contained under Section HC-5.4]

HC-6.1 Principle

HC-6.1.1 **The Board must establish a clear and efficient management structure.**

HC-6.2 Establishment of Management Structure

HC-6.2.1 **The Board must appoint, and when necessary, replace senior management whose authority must include management and operation of current activities of the Islamic bank licensee, reporting to and under the direction of the Board. The senior management must include at a minimum:**

(a) A CEO;
(b) A chief financial officer;
(c) A corporate secretary; and
(d) An internal auditor,

and must also include such other approved persons as the Board considers appropriate.

HC-6.2.2 The senior management consists of a core group of individuals who are responsible and should be held accountable for overseeing the day-to-day management of the bank. These individuals should have the necessary experience, competencies and integrity to manage the businesses under their supervision as well as have appropriate control over the key individuals in these areas.

HC-6.2.3 The senior management contributes substantially to a bank's sound corporate governance through personal conduct (e.g., by helping to set the "tone at the top" along with the board by providing adequate oversight of those they manage, and by ensuring that the bank's activities are consistent with the business strategy, risk tolerance/appetite and policies approved by the bank's board).

HC-6.2.4 Senior management is responsible for delegating duties to the staff and should establish a management structure that promotes accountability and transparency. Senior management should remain cognisant of its obligation to oversee the exercise of such delegated responsibility and its ultimate responsibility to the board for the performance of the bank.

HC-6.2.5 Senior management should implement, consistent with the direction given by the board, appropriate systems for managing the risks - both financial and non-financial - to which the bank is exposed. This includes a comprehensive and independent risk management function and an effective system of internal controls, as discussed in greater detail in Chapters HC-13 and HC-14.

HC-6.2 Establishment of Management Structure (continued)

HC-6.2.6 Senior management should promote strong internal controls and should avoid activities and practices that undermine their effectiveness. Examples of problematic activities or practices include failing to ensure that there is effective segregation of duties where conflicts could arise; not exercising effective control over employees in key business positions (even apparent "star" employees); and failing to question employees who generate revenues or returns out of line with reasonable expectations (eg where supposedly low-risk, low-margin trading activity generated unexpectedly high returns) for fear of losing either revenue or the employees.

HC-6.2.7 **The board must exercise proper oversight of senior management as part of the bank's checks and balances. In doing so, the board must:**

(a) Ensure that senior management's actions are consistent with the strategy and policies approved by the board, including risk tolerance/appetite;

(b) Meet regularly with senior management;

(c) Question and review critically explanations and information provided by senior management;

(d) Set formal performance standards for senior management consistent with the long-term objectives, strategy and financial soundness of the bank, and monitor senior management's performance against these standards; and

(e) Ensure that senior management's knowledge and expertise remain appropriate given the nature of the business and the bank's risk profile.

HC-6.2.8 **The board must also ensure that the bank's organisational structure facilitates effective decision making and good governance. This must include ensuring that lines of responsibility and accountability - which define clearly the key responsibilities and authorities of the board itself, as well as of senior management and those responsible for the control functions – are set and enforced throughout the organisation.**

HC-6.2.9 **The board must regularly review policies and controls with senior management and internal control functions (including internal audit, internal Shari'a review/audit, risk management and compliance) in order to determine areas needing improvement, as well as to identify and address significant risks and issues. The board must ensure that the internal control functions are properly positioned, staffed and resourced and are carrying out their responsibilities independently and effectively.**

HC-6.3 Titles, Authorities, Duties and Reporting Responsibilities

HC-6.3.1 **The Board must adopt by-laws prescribing each senior manager's title, authorities, duties, accountabilities and internal reporting responsibilities. This must be done with the advice of the Nominating Committee and in consultation with the CEO, to whom the other senior managers should normally report.**

HC-6.3.2 **These provisions must include but should not be limited to the following:**

(a) The CEO must have authority to act generally in the Islamic bank licensee's name, representing the Islamic bank licensee's interests in concluding transactions on the Islamic bank licensee's behalf and giving instructions to other senior managers and Islamic bank licensee employees;

(b) The chief financial officer must be responsible and accountable for:

(i) The complete, timely, reliable and accurate preparation of the Islamic bank licensee's financial statements, in accordance with the accounting standards and policies of the Islamic bank licensee (see also HC-3.4.1); and

(ii) Presenting the Board with a balanced and understandable assessment of the Islamic bank licensee's financial situation;

(c) The corporate secretary's duties must include arranging, recording and following up on the actions, decisions and meetings of the Board and of the shareholders (both at annual and extraordinary meetings) in books to be kept for that purpose; and

(d) The internal auditor's duties must include providing an independent and objective review of the efficiency of the Islamic bank licensee's operations. This would include a review of the accuracy and reliability of the Islamic bank licensee's accounting records and financial reports as well as a review of the adequacy and effectiveness of the Islamic bank licensee's risk management, control, and governance processes.

HC-6.3.3 The Board should also specify any limits which it wishes to set on the authority of the CEO or other senior managers, such as monetary maximums for transactions which they may authorise without separate Board approval.

HC-6.3.4 The corporate secretary should be given general responsibility for reviewing the Islamic bank licensee's procedures and advising the Board directly on such matters (see Rule HC-6.3.2(c)). Whenever practical, the corporate secretary should be a person with legal or similar professional experience and training.

HC-6.3 Titles, Authorities, Duties and Reporting Responsibilities (continued)

HC-6.3.5 At least annually the Board should review and concur in a succession plan addressing the policies and principles for selecting a successor to the CEO, both in emergencies and in the normal course of business. The succession plan should include an assessment of the experience, performance, skills and planned career paths for possible successors to the CEO.

HC-6.4 Compliance

HC-6.4.1 In order to promote best practice with respect to banks' internal systems and controls, the CBB, in this Chapter, outlines its requirements for the compliance function of banks, including Shari'a compliance. The expression 'Compliance Function' in this Chapter is used to describe staff carrying out compliance duties.

HC-6.4.2 The expression 'Compliance Risk', in this Chapter refers to the risk of legal or regulatory sanctions, material or financial loss, or loss to reputation a bank may suffer as a result of its failure to comply with laws, regulations, rules, reporting requirements, Shari'a standards and principles and codes of conduct applicable to its activities, rather than compliance with a bank's internal limits or procedures.

HC-6.4.2A Compliance laws, rules and standards also cover the following: managing conflicts of interest, treating customers fairly and ensuring suitability of customer advice, as well as the points mentioned in HC-6.4.2 above.

HC-6.4.3 [This paragraph has been deleted].

Responsibilities of the Board of Directors for Compliance

HC-6.4.4 **In the case of <u>Bahraini Islamic bank licensees</u>, the responsibilities of the board of directors for compliance are the following:**

(a) The board must approve the bank's compliance policy; and

(b) The board must oversee the implementation of the policy and ensure that compliance issues are resolved effectively and expeditiously by <u>senior management</u>.

HC-6.4.5 The board may delegate the tasks outlined in Paragraph HC-6.4.4 to an appropriate board level committee (e.g. its audit committee).

HC-6.4 Compliance (continued)

Responsibilities of Senior Management for Compliance

HC-6.4.6 The responsibilities of senior management for compliance are the following:

(a) Establishing a written compliance policy that contains basic principles to be followed by management and staff and explain the main processes by which compliance risks are to be identified and managed through all levels of the bank;

(b) Ensuring that appropriate remedial or disciplinary action is taken if breaches are identified; and

(c) Establishing a permanent and effective compliance function within the bank as part of the bank's compliance policy.

HC-6.4.7 In addition to the requirements of Paragraph HC-6.4.5, senior management, must, with the assistance of the compliance function, at least once a year, identify and assess the main compliance risk issues facing the bank and the plans to manage them.

HC-6.4.8 In the case of Bahraini Islamic bank licensees, senior management, must, with the assistance of the compliance function:

(a) At least once a year, report to the board of directors or a committee of the board on the bank's management of its compliance risk; and

(b) Report promptly to the board of directors or a committee of the board any material compliance failures.

Responsibilities and Requirements of the Compliance Function

HC-6.4.9 All Islamic bank licensees must maintain an effective compliance function. The responsibilities of the compliance function must be clearly specified, and must include at a minimum, the monitoring of compliance with laws, corporate governance rules, regulations, codes and policies to which the bank is subject and ensuring that deviations are reported to an appropriate level of senior management. In addition, for Bahraini Islamic bank licensees, in case of material deviations, a report must be made to the board or the appropriate board committee.

HC-6.4 Compliance (continued)

HC-6.4.10 **The responsibilities of the bank's compliance function must be to assist the board and senior management in managing effectively the compliance risks faced by the bank through the following:**

(a) Advising senior management on compliance laws, rules and standards, in all jurisdictions in which the bank conducts its business, and inform them on developments in the area;

(b) Providing guidance and training on compliance issues to staff members;

(c) Identifying, measuring, documenting and assessing the compliance risks associated with the bank's business activities including new developments; and

(d) Monitoring, testing and reporting on compliance risk.

HC-6.4.11 **The compliance function must report directly to the board or the appropriate board committee.**

HC-6.4.12 **For all Islamic bank licensees, the compliance function must report to senior management and must be independent (i.e. it must not be placed in a position where its other duties or responsibilities may cause a conflict of interest with its compliance risk management responsibilities). The compliance function must be separate from the internal audit function, and its activities must be subject to periodic and independent review by the internal audit. Compliance risk must be included in the assessment methodology of the internal audit function. In case of dismissal or suspension of the compliance function, Islamic bank licensees must follow the rule in Module BR (Paragraph BR-5.1.17).**

HC-6.4.13 The compliance officer or manager may perform other limited related compliance roles (e.g. the MLRO or legal advisor), subject to the CBB's prior approval.

HC-6.4.14 **The compliance officer/manager must be appropriately qualified and experienced as required by Module TC (Appendix TC-1).**

HC-6.4.15 **The compliance function must have adequate resources to carry out its functions effectively.**

HC-6.4.16 **The appointment of a compliance manager/officer requires the CBB's prior approval and the submission of the appointee's Form 3 (Application for Approved Person status) and Curriculum Vitae to the CBB. The bank must also outline how the compliance function fits into the bank's senior management reporting structure, and must give details of relevant reporting lines within the bank and, in the case of Bahraini Islamic bank licensees, to the Board and Board committees (See LR-1A.1.13).**

HC-6.4 Compliance (continued)

HC-6.4.17 **The compliance officer/manager must have the right to communicate freely with any staff member and obtain free access to any records or files to enable him to carry out his responsibilities without any need for prior approval from senior management.**

HC-7.1 Principle

HC-7.1.1 The Islamic bank licensee must communicate with shareholders, encourage their participation, and respect their rights.

HC-7.2 Conduct of Shareholders' Meetings

HC-7.2.1 **The Board must observe both the letter and the intent of the Company Law's requirements for shareholder meetings. Among other things:**

(a) Notices of meetings must be honest, accurate and not misleading. They must clearly state and, where necessary, explain the nature of the business of the meeting;

(b) Meetings must be held during normal business hours and at a place convenient for the greatest number of shareholders to attend;

(c) Notices of meetings must encourage shareholders to attend shareholder meetings and, if not possible, to participate by proxy and must refer to procedures for appointing a proxy and for directing the proxy how to vote on a particular resolution. The proxy agreement must list the agenda items and must specify the vote (such as "yes," "no" or "abstain");

(d) Notices must ensure that all material information and documentation is provided to shareholders on each agenda item for any shareholder meeting, including but not limited to any recommendations or dissents of directors;

(e) The Board must propose a separate resolution at any meeting on each substantially separate issue, so that unrelated issues are not "bundled" together;

(f) In meetings where directors are to be elected or removed the Board must ensure that each person is voted on separately, so that the shareholders can evaluate each person individually;

(g) The chairman of the meeting must encourage questions from shareholders, including questions regarding the Islamic bank licensee's corporate governance guidelines;

(h) The minutes of the meeting must be made available to shareholders upon their request as soon as possible but not later than 30 days after the meeting; and

(i) Disclosure of all material facts must be made to the shareholders by the Chairman prior to any vote by the shareholders.

HC-7.2.2 The Islamic bank licensee should require all directors to attend and be available to answer questions from shareholders at any shareholder meeting and, in particular, ensure that the chairs of the audit, remuneration and nominating committees are ready to answer appropriate questions regarding matters within their committee's responsibility (it being understood that confidential and proprietary business information may be kept confidential).

HC-7.2 Conduct of Shareholders' Meetings (continued)

HC-7.2.3 The Islamic bank licensee should require its external auditor to attend the annual shareholders' meeting and be available to answer shareholders' questions concerning the conduct and conclusions of the audit.

HC-7.2.4 An Islamic bank licensee should maintain a website. The Islamic bank licensee should dedicate a specific section of its website to describing shareholders' rights to participate and vote at each shareholders' meeting, and should post significant documents relating to meetings including the full text of notices and minutes. The Islamic bank licensee may also consider establishing an electronic means for shareholders' communications including appointment of proxies. For confidential information, the Islamic bank licensee should grant a controlled access to such information to its shareholders.

HC-7.2.5 In notices of meetings at which directors are to be elected or removed the Islamic bank licensee should ensure that:

(a) Where the number of candidates exceeds the number of available seats, the notice of the meeting should explain the voting method by which the successful candidates will be selected and the method to be used for counting of votes; and

(b) The notice of the meeting should present a factual and objective view of the candidates so that shareholders may make an informed decision on any appointment to the board.

HC-7.3 Direct Shareholder Communication

HC-7.3.1

The chairman of the Board (and other directors as appropriate) must maintain continuing personal contact with controllers to solicit their views and understand their concerns. The chairman must ensure that the views of shareholders are communicated to the Board as a whole. The chairman must discuss governance and strategy with controllers. Given the importance of market monitoring to enforce the "comply or explain" approach of this Module, the Board should encourage investors, particularly institutional investors, to help in evaluating the Islamic bank licensee's corporate governance (see also HC-1.2 and 1.3 for other duties of the Chairman).

HC-7.4 Controllers

HC-7.4.1

In Islamic bank licensees with one or more controllers, the chairman and other directors must actively encourage the controllers to make a considered use of their position and to fully respect the rights of minority shareholders (see also HC-1.2 and 1.3 for other duties of the Chairman).

HC-7A.1 Principle

HC-7A.1.1 **Effective risk management requires robust internal communication within the Islamic bank licensee about risk, both across the organisation and through reporting to the board or its committees and senior management. Therefore the bank's risk exposures and strategy must be communicated throughout the bank with sufficient frequency.**

HC-7A.1.2 Effective communication, both horizontally across the organisation and vertically up the management chain, facilitates effective decision-making that fosters safe and sound banking and helps prevent decisions that may result in amplifying risk exposures.

HC-7A.1.3 Sound corporate governance is evidenced, among other things, by a culture where senior management and staff are expected and encouraged to identify risk issues as opposed to relying on the internal audit or risk management functions to identify them. This expectation is conveyed not only through bank policies and procedures, but also through the 'tone at the top' established by the board and senior management.

HC-7A.2 Internal Communication

HC-7A.2.1 **Information must be communicated to the board and <u>senior management</u> in a timely, complete, understandable and accurate manner so that they are equipped to make informed decisions. This is particularly important if an <u>Islamic bank licensee</u> is facing financial or other difficulties and may need to make prompt, critical decisions.**

HC-7A.2.2 If the board or its committees and <u>senior management</u> have incomplete or inaccurate information, their decisions may magnify risks rather than mitigate them. Serious consideration should be given by the board to instituting periodic reviews of the amount and quality of information the board receives or should receive.

HC-7A.2.3 In ensuring that the board and <u>senior management</u> are sufficiently informed, management and those responsible for the control functions should strike a balance between communicating information that is accurate and 'unfiltered' (i.e. that does not hide potentially bad news) and not communicating so much extraneous information that the sheer volume of information becomes counterproductive.

HC-7A.3 Risk Reporting to the Board

HC-7A.3.1 **Risk reporting to the board or its committees requires careful design in order to ensure that firm-wide and individual portfolio and other risks are conveyed in a concise and meaningful manner. Reporting must accurately communicate risk exposures and results of stress tests or scenario analyses, and must provoke a robust discussion of, for example, the Islamic bank licensee's current and prospective exposures (particularly under stressed scenarios), risk/return relationships, risk tolerance/appetite, etc. In addition to internal measurement and assessment of bank risks, reporting must include information about the external environment to identify market conditions and trends that may have a bearing on the bank's current or future risk profile.**

HC-7A.3.2 Risk reporting systems should be dynamic, comprehensive and accurate, and should draw on a range of underlying assumptions. Risk monitoring and reporting should occur not only at the disaggregated level (including risk residing in subsidiaries that could be considered significant), but should also be aggregated upward to allow for a firm-wide or consolidated picture of risk exposures. Risk reporting systems should be clear about any deficiencies or limitations in risk estimates, as well as any significant embedded assumptions (e.g. regarding risk dependencies or correlations). These systems should not only aggregate information to provide a firm-wide, integrated perspective on risk (geographically and by risk type), but should also highlight emerging risks that have the potential to become significant and may merit further analysis.

HC-7A.3.3 Organisational 'silos' can impede effective sharing of information across the Islamic bank licensee and can result in decisions being made in isolation from the rest of the bank. Overcoming information-sharing obstacles posed by silo structures may require the board and senior management to review or rethink established practices in order to encourage greater communication. Some banks have found it useful to create risk management committees - distinct from the board's risk committee - that draw members from across the bank (e.g. from business lines and the risk management function) to discuss issues related to bank-wide risks.

HC-8.1 Principle

HC-8.1.1

The Islamic bank licensee must disclose its corporate governance. The governance of an Islamic bank licensee must be adequately transparent to its shareholders, investment account holders, depositors, other relevant stakeholders and market participants.

HC-8.2 Disclosure under the Company Law and CBB Requirements

HC-8.2.1 **In each Bahraini Islamic bank licensee:**

(a) The Board must adopt written corporate governance guidelines covering the matters stated in this Module and Module PD and other corporate governance matters deemed appropriate by the Board. Such guidelines must include or refer to the principles and rules of Module HC;

(b) The Bahraini Islamic bank licensee must publish the guidelines on its website, if it has a website;

(c) At each annual shareholders' meeting the Board must report on the Bahraini Islamic bank licensee's compliance with its own guidelines and Module HC, and explain the extent if any to which it determines improvements may be needed or any necessary changes made or believes that any variance or noncompliance was justified; and

(d) At each annual shareholders' meeting the Board must also report on further items listed in Module PD. Such information should be maintained on the Bahraini Islamic bank licensee's website or held at the Bahraini Islamic bank licensee's premises on behalf of the shareholders.

HC-8.2.2 [This Paragraph has been deleted].

Board's Responsibility for Disclosure

HC-8.2.3 **The Board must oversee the process of disclosure and communications with internal and external stakeholders. The Board must ensure that disclosures made by the bank are fair, transparent, comprehensive and timely and reflect the character of the bank and the nature, complexity and risks inherent in the bank's business activities. Disclosure policies must be reviewed for compliance with the Central Bank's disclosure requirements (see Chapter PD-1).**

HC-8.2.4 Transparency is essential for sound and effective corporate governance. It is difficult for shareholders, investment account holders, depositors, other relevant stakeholders and market participants to effectively monitor and properly hold accountable the board and senior management when there is insufficient transparency. The objective of transparency in the area of corporate governance is therefore to provide these parties, consistent with relevant laws in Bahrain ~~law~~ and CBB standards, with key information necessary to enable them to assess the effectiveness of the board and senior management in governing the Bahraini Islamic bank licensee.

HC-8.2 Disclosure under the Company Law and CBB Requirements (continued)

HC-8.2.5 Although disclosure requirements may be less detailed for unlisted Bahraini Islamic bank licensees, these institutions can nevertheless pose the same types of risk to the financial system as listed Bahraini Islamic bank licensees through various activities, including their participation in payments systems and acceptance of funds from investment account holders or depositors.

HC-8.2.6 Bahraini Islamic bank licensees should disclose relevant and useful information that supports the key areas of corporate governance. Such disclosure should be proportionate to the size, complexity, structure, economic significance and risk profile of the bank.

HC-8.2.7 Disclosure should include, but not be limited to, material information on the bank's objectives, organisational and governance structures and policies (in particular the content of any corporate governance code or policy and the process by which it is implemented), major share ownership and voting rights and related parties' transactions. The bank should appropriately disclose its incentive and remuneration policy following the requirements under Section PD-1.3.

HC-8.2.8 Bahraini Islamic bank licensees should also disclose key points concerning their risk tolerance/appetite (without breaching necessary confidentiality), with a description of the process for defining it and information concerning the board involvement in such process. When involved in complex or non-transparent structures, the bank should disclose adequate information regarding the purpose, strategies, structures, risks and controls around such activities.

HC-8.2.9 **Disclosure must be accurate, clear and presented in an understandable manner and in such a way that shareholders, investment account holders, depositors, other relevant stakeholders and market participants can consult it easily. Timely public disclosure on a Bahraini Islamic bank licensee's public website is a necessary part of good corporate governance and transparency. Such disclosures should be made in a bank's annual and periodic financial reports or by other appropriate forms.**

HC-8.2.10 It is good practice that an annual corporate governance-specific and comprehensive statement is in a clearly identifiable section of the annual report depending on the applicable financial reporting framework. All material developments that arise between regular reports should be disclosed without undue delay.

HC-9.1 Principle

HC-9.1.1 **Banks which refer to themselves as "Islamic" must follow the principles of Islamic Shari'a.**

HC-9.2 Governance and Disclosure per Shari'a Principles

HC-9.2.1 **Islamic bank licensees which are guided by the principles of Islamic Shari'a have additional responsibilities to their stakeholders. Islamic bank licensees which refer to themselves as "Islamic" are subject to additional governance requirements and disclosures to provide assurance to stakeholders that they are following Shari'a Principles. In ensuring compliance with Shari'a principles, each Islamic bank licensee must establish an independent Shari'a Supervisory Board consisting of at least three Shari'a scholars and complying with AAOIFI's Governance Standards for Islamic Financial Institutions No.1 and No.2.**

HC-9.2.2 The Board should set up a Corporate Governance Committee (see also Chapter HC-8). In this case, the Committee should comprise at least three members to co-ordinate and integrate the implementation of the governance policy framework.

HC-9.2.3 In addition to its duties outlined in Chapter HC-3 and Appendix A, the Audit Committee should communicate and co-ordinate with the Islamic bank licensee's Corporate Governance Committee and the Shari'a Supervisory Board ("SSB") (where applicable) to ensure that information on compliance with Islamic Shari'a rules and principles is reported in a timely manner.

HC-9.2.4 The Corporate Governance Committee established under Chapter HC-9 should comprise at a minimum of:

(a) An independent director to chair the Corporate Governance Committee. The Chairman of the Corporate Governance Committee should not only possess the relevant skills, such as the ability to read and understand financial statements, but should also be able to coordinate and link the complementary roles and functions of the Corporate Governance Committee and the Audit Committee;

(b) A Shari'a scholar who is an SSB member for the purpose of leading the Corporate Governance Committee on Shari'a-related governance issues (if any), and also to coordinate and link the complementary roles and functions of the Corporate Governance Committee and the SSB; and

(c) An independent director who can offer different skills to the committee, such as legal expertise and business proficiency, which are considered particularly relevant by the Board of directors for cultivating a good corporate governance culture, and deemed "fit and proper" by the CBB.

HC-9.2.5 The Corporate Governance Committee should be empowered to:

(a) Oversee and monitor the implementation of the governance policy framework by working together with the management, the Audit Committee and the SSB; and

(b) Provide the Board of directors with reports and recommendations based on its findings in the exercise of its functions.

HC-9.2 Governance and Disclosure per Shari'a Principles (continued)

HC-9.2.6

All Islamic Bank Licensees must comply with all AAOIFI issued accounting standards as well as applicable Shari'a pronouncements issued by the Shari'a Board of AAOIFI. The Islamic bank licensee must have a separate function of Shari'a review to verify compliance with the above. The internal Shari'a review must be carried out in accordance with AAOIFI governance standard No.3. The Shari'a review function may be located in the Internal audit function of the Islamic bank licensee.

HC-10.1 Principle

HC-10.1.1 **Islamic bank licensees must acknowledge IAHs' right to monitor the performance of their investments and the associated risks, and put into place adequate means to ensure that these rights are observed and exercised.**

HC-10.2 Mudarabah Contracts

HC-10.2.1 Conceptually, under the principle of Mudarabah, IAHs as Rabb al-Mal bears the risk of losing their capital invested by the Islamic bank licensee as Mudarib. Effectively, this means the IAH's investment risk is similar to that of the shareholders of the Islamic bank licensee who bear the risk of losing their capital as investors in the Islamic bank licensee. However, the Islamic bank licensee as Mudarib owes a fiduciary duty to the IAH under the Mudarabah contract, which is parallel with their duty to their shareholders. In this context, the Islamic bank licensee as Mudarib refers to both their management and their shareholders, not the management alone. Therefore, the fiduciary duties of Islamic bank licensee to the IAH should always be understood as the fiduciary duties of both the management and shareholders of the Islamic bank licensee as Mudarib towards the IAH as Rabb al-Mal.

HC-10.2.2 In respect of Paragraph HC-10.2.1, whether the investment mandate is restricted or unrestricted, under a Mudarabah contract, the Islamic bank licensee has a fiduciary duty to the IAHs to uphold their interests no less than those of the Islamic bank licensee's own shareholders.

HC-10.3 Information on Investment Accounts

HC-10.3.1 **Islamic bank licensees must put IAHs on an equal footing with the Islamic bank licensee's own shareholders by duly acknowledging the IAH's right to access all relevant information in relation to their investment accounts. This would assist the IAHs in making an informed decision on their selection or choice of the investment accounts in which to place their funds with the Islamic bank licensee (for example, if the Islamic bank licensee offers different types of restricted investment accounts).**

HC-10.3.2 The IAHs' right to monitor the performance of their investment should not be misconstrued as a right to intervene in the management of the investments by the Islamic bank licensee. It should be noted that shareholders of the Islamic bank licensee who are entitled to vote in general meetings, to pass resolutions on the appointment of directors and auditors, and to access the documents of the Islamic bank licensee are also not considered as intervening in the management of the Islamic bank licensee. Therefore, it is only appropriate that Islamic bank licensees disclose to the IAHs their policies and practices in respect of the investment accounts which they offer.

HC-10.3.3 **Prior to opening an investment account with an Islamic bank licensee, IAHs must be adequately advised by the Islamic bank licensee of their contractual rights and risks in regard to investment account products, including primary investment and asset allocation strategies and the method of calculating the profit/loss made from their investments.**

HC-10.3.4 **In accordance with the Mudarabah principles governing the investment account contracts, it is only appropriate that the Islamic bank licensee recognises the IAHs' right to monitor the performance of their investment and put in place means for this right to be exercised. The Corporate Governance Committee of the Islamic bank licensee must take responsibility for protecting this right of the IAHs by ensuring that relevant disclosures to IAHs are made in a timely and effective manner, as well as ensuring proper implementation of the investment contracts.**

HC-10.3 Information on Investment Accounts (continued)

HC-10.3.5 **Islamic bank licensees must have an internal guideline that sets out:**

(a) The eligibility of the Islamic bank licensee's employees who are responsible for managing investment accounts operated by the Islamic bank licensee;

(b) The adequate protection of the IAH's investments, including the case where the unrestricted IAHs' funds are commingled with shareholders' funds;

(c) The disclosure of relevant and material information to the IAHs; and

(d) A proper and disclosed basis for profit allocation and investment policies to be based on the risk expectations of the IAHs.

HC-10.3.6 **Restricted IAHs must have the right to obtain at least all the information usually available to participants of a collective investment undertaking (CIU).**

HC-10.3.7 **Islamic bank licensees must disclose their NAV to all investment account holders and depositors.**

HC-10.3.8 **Unrestricted IAH must be allowed access to all the necessary information in respect of their investment accounts – in particular, the calculation and allocation of profits and the investment policies of the Islamic bank licensee.**

HC-10.3.9 Islamic bank licensees should inform the IAHs from the outset when opening their investment accounts that, in accordance with the principle of Mudarabah, particularly in the event of liquidation of the Islamic bank licensee:

(a) The IAHs should only bear the loss in proportion to the assets funded by their investment;

(b) The Islamic bank licensee should be liable for losses arising from their negligence, misconduct or breach of their investment mandate; and

(c) The restricted IAHs should not be liable for any obligation to other parties arising from the deficiencies of the Islamic bank licensee or its liquidity unless it is specifically related to the restricted IAHs' funds. The unrestricted IAHs should only be liable for such obligations in accordance with the proportion of their share in the commingled funds.

HC-11.1 Principle

HC-11.1.1 Islamic bank licensees must adopt a sound investment strategy which is appropriately aligned to the risk and return expectations of IAHs (bearing in mind the distinction between restricted and unrestricted IAHs), and be transparent in smoothing any returns.

HC-11.2 Investment Strategy Development and Implementation

HC-11.2.1 Islamic bank licensees must use their best endeavours to implement an investment strategy which is appropriately aligned to the risk and return expectations of the IAH as mutually agreed in the investment account contracts between the IAH and the Islamic bank licensee, taking into consideration any restrictions or requirements that may be imposed by the IAH at the time of concluding the investment contract.

HC-11.2.2 The Islamic bank licensee must inform the IAH if it practises the smoothing of returns by means of building up and drawing on reserves such as a Profit Equalization Reserve (PER). The Islamic bank licensee must also inform the IAH whenever it transfers profits to such reserves, or draws on the reserves in order to enhance the profit distribution to IAH.

HC-11.2.3 In the event that an Islamic bank licensee has to be liquidated, the PER must be disposed of in accordance with what was agreed upon at the time of establishing the reserves, which commonly would be one of the following:
(a) Distribution to the existing IAH and shareholders; or
(b) Donation to charities.

HC-11.2.4 For purposes of Paragraph HC-11.2.2, Islamic bank licensees must create practices, procedures and entitlements that adequately address any undesirable ambiguity which could be ethically questionable and tantamount to gharar with regard to the PER. The Islamic bank licensee must appropriately disclose if the PER will not be distributed to the IAH in the event of liquidation.

HC-11.2.5 In developing their investment strategy on behalf of IAHs, Islamic bank licensees must carefully consider the risk and return expectations of IAH by:
(a) Having an appropriate and systematic know-your-customer mechanism which can effectively reflect the different risk–return profiles of restricted and unrestricted IAH;
(b) Employing qualified investment managers who fully understand the needs and expectations of IAH; and
(c) Keeping the Corporate Governance Committee fully informed of the investment strategy adopted by Islamic bank licensees, where appropriate.

HC-11.2 Investment Strategy Development and Implementation (continued)

HC-11.2.6 In order to ensure that the utilisation of PER is appropriate, the Corporate Governance Committee should be mandated to scrutinise such utilisation and to make appropriate recommendations to the Board.

HC-11.2.7 Islamic bank licensees should clearly distinguish the "distribution rate" – that is, the rate of profit distributed – and the "profit rate" – that is, the actual profit earned from investments made on behalf of the IAH – in disclosing the returns to IAH. Effectively, the utilisation of PER should clearly be understood as being for "smoothing the profit payout" rather than "smoothing the profits earned" for IAH.

HC-11.2.8 Smoothing of returns distributed to IAHs using the PER excludes turning a loss into a profit, for which purpose another special type of reserve, the investment risk reserve (IRR), may be used. If the Islamic bank licensee has created an (IRR) to cushion any unexpected loss on the part of the IAH, the utilisation of IRR should be placed under the scrutiny of and subject to the recommendations of the Corporate Governance Committee to the Board.

HC-12.1 General Requirements

Principle

HC-12.1.1 **In a group structure, the overall responsibility for adequate corporate governance across the group rests with the board of the parent company and may not be delegated. The board of the Bahraini licensed parent bank must ensure that there are governance policies and mechanisms appropriate to the structure, business and risks of the group and its entities.**

Board of Bahraini Licensed Parent Bank

HC-12.1.2 **In the discharge of its corporate governance responsibilities, the board of the Bahraini licensed parent bank must be aware of the material risks and issues that might affect both the Islamic bank licensee as a whole and its subsidiaries. It must therefore exercise adequate oversight over subsidiaries, while respecting the independent legal and governance responsibilities that might apply to subsidiaries' boards.**

HC-12.1.3 **In order to fulfil its corporate governance responsibilities, the board of the parent bank in Bahrain must:**

(a) Establish a governance structure which contributes to the effective oversight of subsidiaries and which takes into account the nature, scale and complexity of the different risks to which the group and its subsidiaries are exposed;

(b) Assess the governance structure periodically to ensure that it remains appropriate in light of growth, increased complexity, geographic expansion, etc;

(c) Approve a corporate governance policy at the group level for its subsidiaries, which includes the commitment to meet all applicable governance requirements;

(d) Ensure that enough resources are available for each subsidiary to meet both group standards and local governance standards;

(e) Understand the roles and relationships of subsidiaries to one another and to the Bahraini licensed parent bank; and

(f) Have appropriate means to monitor that each subsidiary complies with all applicable governance requirement.

HC-12.1.4 In general, the board of a regulated banking subsidiary should adhere to the corporate values and governance principles espoused by its parent bank. In doing so the board should take into account the nature of the business of the subsidiary and the legal requirements that are applicable.

HC-12.1 General Requirements (continued)

HC-12.1.5 **The board of a regulated banking subsidiary must retain and set its own corporate governance responsibilities, and must evaluate any group-level decisions or practices to ensure that they do not put the regulated subsidiary in breach of applicable legal or regulatory provisions or prudential rules.**

HC-12.1.6 **The board of the regulated banking subsidiary must also ensure that such decisions or practices mentioned in Paragraph HC-12.1.5 are not detrimental to:**

(a) The sound and prudent management of the subsidiary;
(b) The financial health of the subsidiary; and
(c) The legal interests of the subsidiary's stakeholders.

HC-12.2 Complex or Opaque Corporate Structures

Principle

HC-12.2.1 **The board and senior management must know and understand the Islamic bank licensee's operational structure and the risks that it poses (i.e. 'know-your-structure').**

Establishment of Structures

HC-12.2.2 Complexity of a banking group considerably increases when the Islamic bank licensee creates structures for legal, regulatory, fiscal or product-offering purposes in the form of units, branches, subsidiaries or other legal entities. The sheer number of legal entities, and in particular the interconnections and intra-group transactions among such entities, can lead to challenges in identifying, overseeing and managing the risks of the organisation as a whole, which is a risk in and of itself.

HC-12.2.3 The board and senior management should understand the structure and the organisation of the group, i.e. the aims of its different units/entities and the formal and informal links and relationships among the entities and with the parent company. This includes understanding the legal and operational risks and constraints of the various types of intra-group exposures and transactions and how they affect the group's funding, capital and risk profile under normal and adverse circumstances.

HC-12.2.4 Sound and effective measures and systems should be in place to facilitate the generation and exchange of information among and about the various entities, to manage the risks of the group as a whole, and for the effective supervision of the group. In this regard, senior management should inform the board regarding the group's organisational and operational structure and the key drivers of the group's revenues and risks.

HC-12.2.5 Another governance challenge arises when Islamic bank licensees establish business or product line management structures that do not match the bank's legal entity structure. While this is a quite common practice, it nevertheless introduces additional complexity. Apart from ensuring the appropriateness of these matrix structures, the board or senior management as appropriate should ensure that all products and their risks are captured and evaluated on an individual entity and group-wide basis.

HC-12.2 Complex or Opaque Corporate Structures (continued)

HC-12.2.6 **The board must approve policies and clear strategies for the establishment of new structures and must properly guide and understand the bank's structure, its evolution and its limitations. Moreover, senior management, under the oversight of the board, must:**

(a) Avoid setting up unnecessarily complicated structures;

(b) Have a centralised process for approving and controlling the creation of new legal entities based on established criteria, including the ability to monitor and fulfil on an ongoing basis each entity's requirements (e.g. regulatory, tax, financial reporting, governance);

(c) Understand and be able to produce information regarding the Islamic bank licensee's structure, including the type, charter, ownership structure and businesses conducted for each legal entity;

(d) Recognise the risks that the complexity of the legal entity structure itself may pose, including lack of management transparency, operational risks introduced by interconnected and complex funding structures, intra-group exposures, trapped collateral and counterparty risk; and

(e) Evaluate how the aforementioned risks of the structure and legal entity requirements affect the group's ability to manage its risk profile and deploy funding and capital under normal and adverse circumstances.

HC-12.2.7 In order to enhance the sound governance of a banking group, internal audits of individual entities should be complemented with regular assessments of the risks posed by the group's structure. Periodic reports that assess the Islamic bank licensee's overall structure and individual entities' activities, confirm compliance with the strategy previously approved by the board, and disclose any possible discrepancies could be useful for the audit and risk committees, senior management and the board of the parent company.

HC-12.2.8 **Senior management, and the board as necessary, must discuss with and seek prior approval from the CBB on any new or amendments to the group structures or the Bahrain licensed bank structure.**

HC-12.3 Special Purpose Vehicles

Principle

HC-12.3.1 **Where an Islamic bank licensee operates through special-purpose or related structures or in jurisdictions that impede transparency or do not meet international banking standards, its board and senior management must understand the purpose, structure and unique risks of these operations. They must also seek to mitigate the risks identified (i.e. 'understand-your-structure'). More details on Shari'a compliance of special-purpose vehicles are available in Chapter BR-5.**

Operating Special Purpose Vehicles

HC-12.3.2 Islamic bank licensee may have legitimate purposes for operating in particular jurisdictions (or with entities or counterparties operating in these jurisdictions) or for establishing certain structures (e.g. special purpose vehicles or corporate trusts). However, operating in jurisdictions that are not fully transparent or do not meet international banking standards (e.g. in the areas of prudential supervision, tax, anti-money laundering or anti-terrorism financing), or through complex or non-transparent structures, may:

(a) Pose financial, legal, reputational and other risks to the banking organisation;
(b) Impede the ability of the board and senior management to conduct appropriate business oversight; and
(c) Hinder effective banking supervision.

HC-12.3.3 **For purposes of Paragraph HC-12.3.2, the Islamic bank licensee must evaluate proposed activities and transactions such as those described above and carefully consider, prior to approval, how it will implement effective board and/or managerial oversight.**

HC-12.3.4 In addition to the risks discussed above, the Islamic bank licensee may also be indirectly exposed to risk when it performs certain services or establishes structures on behalf of customers. Examples include:

(a) Acting as a company or partnership formation agent;
(b) Providing a range of trustee services; and
(c) Developing complex structured finance transactions for customers.

HC-12.3 Special Purpose Vehicles (continued)

HC-12.3.5 While the activities in Paragraph HC-12.3.4 are often profitable and can serve the legitimate business purposes of customers, in some cases customers may use products and activities provided by banks to engage in illegal or inappropriate activities. This can, in turn:

(a) Pose significant legal and reputational risks to a bank that provides such services;

(b) Could cause it to deviate from its core business; and

(c) Could preclude adequate control of the risks posed by the client to the group as a whole.

HC-12.3.6 **Senior management, and the board as appropriate, must note the above challenges and take appropriate action to avoid or mitigate them by:**

(a) Maintaining and reviewing, on an ongoing basis, appropriate policies, procedures and strategies governing the approval and maintenance of those structures or activities;

(b) Periodically monitoring such structures and activities to ensure that they remain consistent with their established purpose so that they are not held without adequate justification; and

(c) Establishing adequate procedures to identify and manage all material risks arising from these activities.

HC-12.3.7 **For purposes of Paragraph HC-12.3.6, Islamic bank licensees must only approve these operations if the material financial, legal and reputational risks can be properly identified, assessed and managed.**

HC-12.3 Special Purpose Vehicles (continued)

HC-12.3.8 **Consistent with guidance from the board, senior management must ensure that the Islamic bank licensee has appropriate policies and procedures to:**

(a) Establish processes for the approval of such activities (e.g. applicable limits, measures to mitigate legal or reputational risks, and information requirements), taking into account the implications for the resulting operational structure of the organisation;

(b) Define and understand the purpose of such activities, and ensure that the actual exercise of these activities is consistent with their intended purpose;

(c) Document the process of consideration, authorisation and risk management to make this process transparent to auditors and the CBB;

(d) Regularly evaluate the continuing need to operate in certain jurisdictions or through complex structures that reduce transparency;

(e) Ensure that information regarding these activities and associated risks is readily available to the bank's head office, and is appropriately reported to the board and supervisors; and

(f) Ensure that these activities are subject to regular internal and external audit reviews.

HC-12.3.9 The board of the parent Bahraini licensed bank should require a control function (such as internal audit, risk management or compliance) to conduct a formal review of the structures, their controls and activities, as well as their consistency with board-approved strategy and report to the board and senior management on its findings.

HC-13.1 Principle

HC-13.1.1 **Islamic bank licensees must have an effective internal controls system and a risk management function (including a chief risk officer or equivalent) with sufficient authority, stature, independence, resources and access to the board.**

HC-13.2 Risk Management vs. Internal Controls

HC-13.2.1 Risk management generally encompasses the process of:

(a) Identifying key risks to the Islamic bank licensee;
(b) Assessing these risks and measuring the Islamic bank licensee's exposures to them;
(c) Monitoring the risk exposures and determining the corresponding capital needs (i.e. capital planning) on an ongoing basis;
(d) Monitoring and assessing decisions to accept particular risks, risk mitigation measures and whether risk decisions are in line with the board-approved risk tolerance/appetite and risk policy; and
(e) Reporting to senior management, and the board as appropriate, on all the items noted in this Paragraph.

HC-13.2.2 Internal controls are designed, among other things, to ensure that each key risk has a policy, process or other measure, as well as a control to ensure that such policy, process or other measure is being applied and works as intended. As such, internal controls help ensure process integrity, compliance and effectiveness.

HC-13.2.3 Internal controls help provide comfort that financial and management information is reliable, timely and complete and that the bank is in compliance with its various obligations, including applicable laws and regulations. In order to avoid actions beyond the authority of the individual or even fraud, internal controls also place reasonable checks on managerial and employee discretion.

HC-13.2.4 Even in very small Islamic bank licensees, for example, key management decisions should be made by more than one person ("four eyes principle"). Internal control reviews should also determine the extent of an institution's compliance with company policies and procedures, as well as with legal and regulatory policies.

HC-13.3 Chief Risk Officer or Equivalent

HC-13.3.1 **Bahraini Islamic bank licensees must have an independent senior executive with distinct responsibility for the risk management function and the comprehensive risk management framework across the entire organisation. This executive is commonly referred to as the chief risk officer ('CRO').**

HC-13.3.2 **The role of the CRO must be distinct from other executive functions and business line responsibilities, and there must be no 'dual hatting' (i.e. the chief operating officer, CFO, chief auditor or other senior management must not also serve as the CRO).**

HC-13.3.3 **Regardless of reporting lines across Islamic bank licensees, the independence of the CRO is paramount. While the CRO may report to the CEO or other senior management, the CRO must also report and have direct access to the board and its risk committee without impediment. The CRO must also not have any management or financial responsibility in respect of any operational business lines or revenue-generating functions. Interaction between the CRO and the board must occur regularly and be documented adequately. Non-executive board members must have the right to meet regularly - in the absence of senior management - with the CRO.**

HC-13.3.4 The CRO should have sufficient stature, authority and seniority within the organisation. This will typically be reflected in the ability of the CRO to influence decisions that affect the Islamic bank licensee's exposure to risk. Beyond periodic reporting, the CRO should thus have the ability to engage with the board and other senior management on key risk issues and to access such information as the CRO deems necessary to form his or her judgment. Such interactions should not compromise the CRO's independence.

HC-13.3.5 **If the CRO is removed from his or her position for any reason, this must be done with the prior approval of the board and must be disclosed publicly. The bank must also discuss the reasons for such removal with the CBB.**

HC-13.4 Scope of Responsibilities, Stature and Independence of the Risk Management Function

HC-13.4.1 **The risk management function is responsible for identifying, measuring, monitoring, controlling or mitigating, and reporting on risk exposures. The mandate of this function must encompass all risks to the Islamic bank licensee, on- and off-balance sheet and at a group-wide, portfolio and business-line level, and must take into account the extent to which risks overlap (eg lines between market and credit risk and between credit and operational risk are increasingly blurred). This must include a reconciliation of the aggregate level of risk in the bank to the board-established risk tolerance/appetite.**

HC-13.4.2 The risk management function both firm-wide and within subsidiaries and business lines -- under the direction of the CRO, should have sufficient stature within the Islamic bank licensee such that issues raised by risk managers receive the necessary attention from the board, senior management.

HC-13.4.3 Business decisions by the Islamic bank licensee typically are a product of many considerations. By properly positioning and supporting its risk management function, a bank helps ensure that the views of risk managers will be an important part of those considerations.

HC-13.4.4 **While it is not uncommon for risk managers to work closely with individual business units and, in some cases, to have dual reporting lines, the risk management function must be sufficiently independent of the business units whose activities and exposures it reviews. While such independence is an essential component of an effective risk management function, it is also important that risk managers are not so isolated from business lines - geographically or otherwise - that they cannot understand the business or access necessary information.**

HC-13.4.5 **The risk management function must have access to all business lines that have the potential to generate material risk to the bank. Regardless of any responsibilities that the risk management function may have to business lines and senior management, its ultimate responsibility must be to the board.**

HC-13.5 Resources

HC-13.5.1 Islamic bank licensees must ensure through planning and budgeting processes that the risk management function has adequate resources (in both number and quality) necessary to assess risk, including personnel, access to information technology systems and systems development resources, and support and access to internal information. These processes must also explicitly address and provide sufficient resources for internal audit and compliance functions. Compensation and other incentives (e.g. opportunities for promotion) of the CRO and risk management staff must be sufficient to attract and retain qualified personnel.

HC-13.6 Qualifications

HC-13.6.1 **Risk management personnel must possess sufficient experience and qualifications, including market and product knowledge as well as mastery of risk disciplines. Staff must have the ability and willingness to challenge business lines regarding all aspects of risk arising from the bank's activities (See Appendix TC-1 in Training and Competency Module (TC)).**

HC-14.1 Principle

HC-14.1.1 **Risks must be identified and monitored on an ongoing firm-wide and individual entity basis, and the sophistication of the Islamic bank licensee's risk management and internal control infrastructures must keep pace with any changes to the bank's risk profile (including its growth), and to the external risk landscape.**

HC-14.2 Risk Methodologies and Activities

HC-14.2.1 Risk analysis should include both quantitative and qualitative elements. While risk measurement is a key component of risk management, excessive focus on measuring or modelling risks at the expense of other risk management activities may result both in overreliance on risk estimates that do not accurately reflect real exposures and in insufficient action to address and mitigate risks.

HC-14.2.2 The risk management function should ensure that the Islamic bank licensee's internal risk measurements:
(a) Cover a range of scenarios;
(b) Are not based on overly optimistic assumptions regarding dependencies and correlations; and
(c) Include qualitative firm-wide views of risk relative to return and to the bank's external operating environment.

HC-14.2.3 **Senior management and, as applicable, the board must review and approve scenarios that are used in the Islamic bank licensee's risk analysis and must be made aware of assumptions and potential shortcomings embedded in the bank's risk models.**

HC-14.2.4 As Islamic bank licensees make use of certain internal and external data to identify and assess risk, make strategic or operational decisions, and determine capital adequacy, the board should give special attention to the quality, completeness and accuracy of the data it relies on to make risk decisions.

HC-14.2.5 **As part of their quantitative and qualitative analysis, Islamic bank licensees must also utilise forward-looking stress tests and scenario analysis to better understand potential risk exposures under a variety of adverse circumstances. These must be key elements of a bank's risk management process, and the results must be communicated to, and given appropriate consideration by, the relevant business lines and individuals within the bank.**

HC-14.2.6 A forward-looking approach to risk management should include ongoing monitoring of existing risks as well as identifying new or emerging risks.

HC-14.2.7 **Islamic bank licensees must also regularly review actual performance after the fact relative to risk estimates (i.e. backtesting) to assist in gauging the accuracy and effectiveness of the risk management process and making necessary adjustments.**

HC-14.2 Risk Methodologies and Activities (continued)

HC-14.2.8 **The risk management function must promote the importance of senior management and business line managers in identifying and assessing risks critically, rather than relying excessively on external risk assessments.**

HC-14.2.9 While external assessments such as external credit ratings or externally purchased risk models can be useful as an input into a more comprehensive assessment of risk, the ultimate responsibility for assessing risk lies solely with the Islamic bank licensee. For example, in the case of a purchased credit or market risk model, the bank should take the steps necessary to validate the model and calibrate it to the bank's individual circumstances to ensure accurate and comprehensive capture and analysis of risk. In any case, Islamic bank licensees should avoid over-reliance on any specific risk methodology or model.

Subsidiaries

HC-14.2.10 **In the case of subsidiary Islamic bank licensees, the board and management of a subsidiary remain responsible for effective risk management processes at the subsidiary.**

HC-14.2.11 While parent banks should conduct strategic, group-wide risk management and prescribe corporate risk policies, subsidiary management and boards should have appropriate input into their local or regional adoption and to assessments of local risks. If group risk management systems and processes are prescribed, subsidiary management, with subsidiary board oversight, is responsible for assessing and ensuring that those systems and processes are appropriate, given the nature of the operations of the subsidiary.

HC-14.2.12 **Adequate stress testing of subsidiary banks' portfolios must occur, based not only on the subsidiaries' economic and operating environments, but also based on the ramifications of potential stress on the parent bank (e.g. liquidity, credit, reputational risk, etc). In some cases, such evaluations may be accomplished through joint head office and subsidiary teams.**

HC-14.2.13 Local management and those responsible for the control functions are accountable for prudent risk management at the local level. Parent companies should ensure that adequate tools and authorities are provided to the subsidiary and that the subsidiary understands what reporting obligations it has to the head office.

HC-14.2 Risk Methodologies and Activities (continued)

HC-14.2.14 The risk management function should evaluate possible ways to manage risk exposures. In some cases, the risk management function may direct that risk be reduced or hedged to limit exposure. In other cases, the risk management function may simply report risk positions and monitor these positions to ensure that they remain within the Islamic bank licensee's framework of limits and controls. Either approach may be appropriate provided the independence of the risk management function is not compromised.

HC-14.2.15 The sophistication of the Islamic bank licensee's risk management and internal control infrastructures - including, in particular, a sufficiently robust information technology infrastructure - should keep pace with developments such as balance sheet and revenue growth, increasing complexity of the bank's business or operating structure, geographic expansion, mergers and acquisitions, or the introduction of new products or business lines. Strategic business planning, and periodic review of such plans, should take into account the extent to which such developments have occurred and the likelihood that they will continue going forward.

Approval of New Products

HC-14.2.16 **Islamic bank licensees must have approval processes for new products. These must include:**
(a) An assessment of the risks of new products;
(b) Significant changes to existing products;
(c) The introduction of new lines of business; and
(d) Entry into new markets.

HC-14.2.17 The risk management function should provide input on risks as a part of such processes mentioned in Paragraph HC-14.2.16. This should include a full and frank assessment of risks under a variety of scenarios, as well as an assessment of potential shortcomings in the ability of the bank's risk management and internal controls to effectively manage associated risks.

HC-14.2.18 An Islamic bank licensee's new product approval process should take into account the extent to which the bank's risk management, legal and regulatory compliance, information technology, business line, and internal control functions have adequate tools and the expertise necessary to manage related risks. If adequate risk management processes are not yet in place, a new product offering should be delayed until such time that systems and risk management are able to accommodate the relevant activity. There should also be a process to assess risk and performance relative to initial projections, and to adapt the risk management treatment accordingly, as the business matures.

HC-14.2 Risk Methodologies and Activities (continued)

Mergers and Acquisitions

HC-14.2.19 Mergers and acquisitions can pose special risk management challenges to the Islamic bank licensee. In particular, risks can arise from conducting insufficient due diligence that fails to identify risks that arise post-merger or activities that conflict with the bank's strategic objectives or risk tolerance/appetite. The risk management function should therefore be actively involved in assessing risks that could arise from mergers and acquisitions, and should report its findings directly to the board and/or its relevant specialised committee.

Firm-Wide Risk Management

HC-14.2.20 While the risk management function plays a vital role in identifying, measuring, monitoring and reporting on risk exposures, other units in the Islamic bank licensee also play an important role in managing risk. In addition to business lines, which should be accountable for managing risks arising from their activities, the bank's treasury and finance functions should promote effective firm-wide risk management not only through supporting financial controls but also through applying robust internal pricing of risk especially at large banks and internationally active banks. A business unit's internal cost of funds should reflect material risks to the bank arising from its activities. Failure to do so may result in greater investment in high-risk activities than would be the case if internal pricing were risk-adjusted.

HC-14.2.21 Although the risk management function has a key leadership and coordinating role on risks, the operational responsibility for making operational decisions on risks and managing risk rests with management and ultimately extends to other employees of the bank. The bank's risk management framework should be clear and transparent regarding staff and organisational responsibilities for risk.

Appendix A Audit Committee

Committee Duties

The Committee's duties must include those stated in Paragraph HC-3.2.1.

Committee Membership and Qualifications

The Committee must have at least three members. Such members must have no conflict of interest with any other duties they have for the Islamic bank licensee.

A majority of the members of the committee including the Chairman must be independent directors.

The CEO must not be a member of this committee.

The committee members must have sufficient technical expertise to enable the committee to perform its functions effectively. Technical expertise means that members must have recent and relevant financial ability and experience, which includes:

(a) An ability to read and understand corporate financial statements including an Islamic bank licensee's balance sheet, income statement and cash flow statement and changes in shareholders' equity;
(b) An understanding of the accounting principles which are applicable to the Islamic bank licensee's financial statements;
(c) Experience in evaluating financial statements that have a level of accounting complexity comparable to that which can be expected in the Islamic bank licensee's business;
(d) An understanding of internal controls and procedures for financial reporting; and
(e) An understanding of the audit committee's controls and procedures for financial reporting.

Committee Duties and Responsibilities

In serving those duties, the Committee must:

(a) Be responsible for the selection, appointment, remuneration, oversight and termination where appropriate of the external auditor, subject to ratification by the Islamic bank licensee's Board and shareholders. The external auditor must report directly to the committee;
(b) Make a determination at least once each year of the external auditor's independence, including:
    (i) Determining whether its performance of any non-audit services compromised its independence (the committee may establish a formal policy specifying the types of non-audit services which are permissible) and;

Appendix A Audit Committee (continued)

(ii) Obtaining from the external auditor a written report listing any relationships between the external auditor and the Islamic bank licensee or with any other person or entity that may compromise the auditor's independence;

(c) Review and discuss with the external auditor the scope and results of its audit, any difficulties the auditor encountered including any restrictions on its access to requested information and any disagreements or difficulties encountered with management;

(d) Review and discuss with management and the external auditor each annual and each quarterly financial statements of the Islamic bank licensee including judgments made in connection with the financial statements;

(e) Review and discuss and make recommendations regarding the selection, appointment and termination where appropriate of the head of internal audit and head of compliance and the budget allocated to the internal audit and compliance function, and monitor the responsiveness of management to the committee's recommendations and findings;

(f) Review and discuss the activities, performance and adequacy of the Islamic bank licensee's internal auditing and compliance personnel and procedures and its internal controls and compliance procedures, risk management systems, and any changes in those;

(g) Oversee the Islamic bank licensee's compliance with legal and regulatory requirements, codes and business practices, and ensure that the bank communicates with shareholders and relevant stakeholders (internal and external) openly and promptly, and with substance of compliance prevailing over form; and

(h) Review and discuss possible improprieties in financial reporting or other matters, and ensure that arrangements are in place for independent investigation and follow-up regarding such matters;

(i) The committee must monitor rotation arrangements for audit engagement partners. The audit committee must monitor the performance of the external auditor and the non-audit services provided by the external auditor; and

(j) The review and supervision of the implementation of, enforcement of and adherence to the bank's code of conduct.

Committee Structure and Operations

The committee must elect one member as its chair.

The committee must meet at least four times a year. Its meetings may be scheduled in conjunction with regularly-scheduled meetings of the entire Board.

The committee may meet without any other director or any officer of the Islamic bank licensee present. Only the committee may decide if a non-member of the committee should attend a particular meeting or a particular agenda item. Non-members who are not directors of the Islamic bank licensee may attend to provide their expertise, but must not vote. It is expected that the external auditor's lead representative will be invited to attend regularly but that this must always be subject to the committee's decision.

The committee must meet with the external auditor at least twice per year, and at least once per year in the absence of any members of executive management.

Appendix A Audit Committee (continued)

The committee must report regularly to the full Board on its activities.

Committee Resources and Authority

The committee must have the resources and authority necessary for its duties and responsibilities, including the authority to select, retain, terminate and approve the fees of outside legal, accounting or other advisors as it deems necessary or appropriate, without seeking the approval of the Board or management. The Islamic bank licensee must provide appropriate funding for the compensation of any such persons.

Committee Performance Evaluation

The committee must prepare and review with the Board an annual performance evaluation of the committee, which must compare the committee's performance with the above requirements and must recommend to the Board any improvements deemed necessary or desirable to the committee's charter. The report must be in the form of a written report provided at any regularly scheduled Board meeting.

Appendix B Nominating Committee

Committee Duties

The committee's duties must include those stated in Paragraph HC-4.2.1.

Committee Duties and Responsibilities

In serving those duties with respect to Board membership:

(a) The committee must make recommendations to the Board from time to time as to changes the committee believes to be desirable to the size of the Board or any committee of the Board;

(b) Whenever a vacancy arises (including a vacancy resulting from an increase in Board size), the committee must recommend to the Board a person to fill the vacancy either through appointment by the Board or through shareholder election;

(c) In performing the above responsibilities, the committee must consider any criteria approved by the Board and such other factors as it deems appropriate. These may include judgment, specific skills, experience with other comparable businesses, the relation of a candidate's experience with that of other Board members, and other factors;

(d) The committee must also consider all candidates for Board membership recommended by the shareholders and any candidates proposed by management;

(e) The committee must identify Board members qualified to fill vacancies on any committee of the Board and recommend to the Board that such person appoint the identified person(s) to such committee; and

(f) Assuring that plans are in place for orderly succession of senior management.

In serving those purposes with respect to officers the committee must:

(a) Make recommendations to the Board from time to time as to changes the committee believes to be desirable in the structure and job descriptions of the officers including the CEO, and prepare terms of reference for each vacancy stating the job responsibilities, qualifications needed and other relevant matters including integrity, technical and managerial competence, and experience;

(b) Overseeing succession planning and replacing key executives when necessary, and ensuring appropriate resources are available, and minimising reliance on key individuals;

(c) Design a plan for succession and replacement of officers including replacement in the event of an emergency or other unforeseeable vacancy; and

(d) If charged with responsibility with respect to Islamic bank licensee's corporate governance guidelines, the committee must develop and recommend to the Board corporate governance guidelines, and review those guidelines at least once a year.

Committee Structure and Operations

The committee must elect one member as its chair.

Appendix B Nominating Committee (continued)

The committee must meet at least twice a year. Its meetings may be scheduled in conjunction with regularly-scheduled meetings of the entire Board.

Committee Resources and Authority

The committee must have the resources and authority necessary for its duties and responsibilities, including the authority to select, retain, terminate and approve the fees of outside legal, consulting or search firms used to identify candidates, without seeking the approval of the Board or management. The Islamic bank licensee must provide appropriate funding for the compensation of any such persons.

Performance Evaluation

The committee must preview and review with the Board an annual performance evaluation of the committee, which must compare the committee's performance with the above requirements and must recommend to the Board any improvements deemed necessary or desirable to the committee's charter. The report must be in the form of a written report provided at any regularly scheduled Board meeting.

Appendix C Remuneration Committee

Committee Duties

The committee's duties must include those stated in Paragraph HC-5.2.1.

Committee Duties and Responsibilities

In serving those duties the committee must consider, and make specific recommendations to the Board on, both remuneration policy and individual remuneration packages for the approved persons and other material risk-takers as well as the total variable remuneration to be distributed. This remuneration policy must cover at least:

(a) The following components:
   (i) Salary;
   (ii) The specific terms of performance-related plans including any stock compensation, stock options, or other deferred-benefit compensation;
   (iii) Pension plans;
   (iv) Fringe benefits such as non-salary perks; and
   (v) Termination policies including any severance payment policies; and

(b) Policy guidelines to be used for determining remuneration in individual cases, including on:
   (i) The relative importance of each component noted in a) above;
   (ii) Specific criteria to be used in evaluating a senior manager's performance.

The committee must evaluate the approved persons and material risk-takers' performance in light of the bank's corporate goals, agreed strategy, objectives and business plans and may consider the Islamic bank licensee's performance and shareholder return relative to comparable Islamic bank licensees, the value of awards to CEOs at comparable Islamic bank licensees,, and awards to the CEO in past years.

The committee should also be responsible for retaining and overseeing outside consultants or firms for the purpose of determining approved persons and material risk-takers' remuneration, administering remuneration plans, or related matters.

Committee Structure and Operations

The committee must elect one member as its chair.

The committee must meet at least twice a year. Its meetings may be scheduled in conjunction with regularly-scheduled meetings of the entire Board.

Committee Resources and Authority

The committee must have the resources and authority necessary for its duties and responsibilities, including the authority to select, retain, terminate and approve the fees of outside legal, consulting or compensation firms used to evaluate the compensation of directors, the CEO or other approved persons, without seeking the approval of the Board or management. The Islamic bank licensee must provide appropriate funding for the compensation of any such persons.

Appendix C Remuneration Committee (continued)

Performance Evaluation

The committee must preview and review with the Board an annual performance evaluation of the committee, which must compare the committee's performance with the above requirements and must recommend to the Board any improvements deemed necessary or desirable to the committee's charter. The report must be in the form of a written report provided at any regularly scheduled Board meeting.