

January
2018

Compliance & Enforcement Annual Report 2017

For the period ended December, 2017

Capital Market Supervision Directorate
Investigation & Enforcement Department



مصرف البحرين المركزي
Central Bank of Bahrain

Table of Contents

1. Introduction.....	2
2. Compliance Status 2017	3
2.1. Listed Companies	3
Figure 1	3
Table 1	5
Table 2	6
2.2. Self-Regulatory Organizations (SROs).....	7
Figure 2.....	7
2.3. Members of SROs (Licensed Brokers)	7
3. Imposition of Financial Penalties	9
4. Conclusion	10

1. Introduction



The Capital Market Supervision Directorate’s (the “CMSD”) regulatory mandate is to set and enforce high quality capital market industry standards, protect investors and strengthen market integrity while supporting a stimulating capital markets’ ecosystem. The Investigation and Enforcement (“IE”) team within the CMSD assumes responsibility to ensure effective enforcement of the Central Bank of Bahrain’s (the “CBB”) regulatory requirements, in order to achieve fairness, transparency, investor protection and safeguard public interests in the Kingdom of Bahrain.

In pursuing these mandates, IE aims to institute a fully-fledged proactive enforcement regimen that ensures the fulfilment of CMSD’s requirements by listed companies, self-regulatory organizations (“SROs”) and the related licensees. Accordingly, given each department’s invaluable role, the CMSD as a whole, strives to continue to instil and integrate the compliance and enforcement function, directorate-wide. CMSD believes that this inclusive view of enforcement strengthens and enhances the efforts expended to protect the integrity of the capital markets.

This annual report provides a comparative overview of CMSD’s efforts in 2015-2017 to identify and address non-compliances, negligence or misconduct, by accounting for all market participants in order to enact the word of the law, safeguard the interests of all stakeholders and ensure a stimulating environment within which the needs of members, investors and the regulator are met.

2. Compliance Status 2017

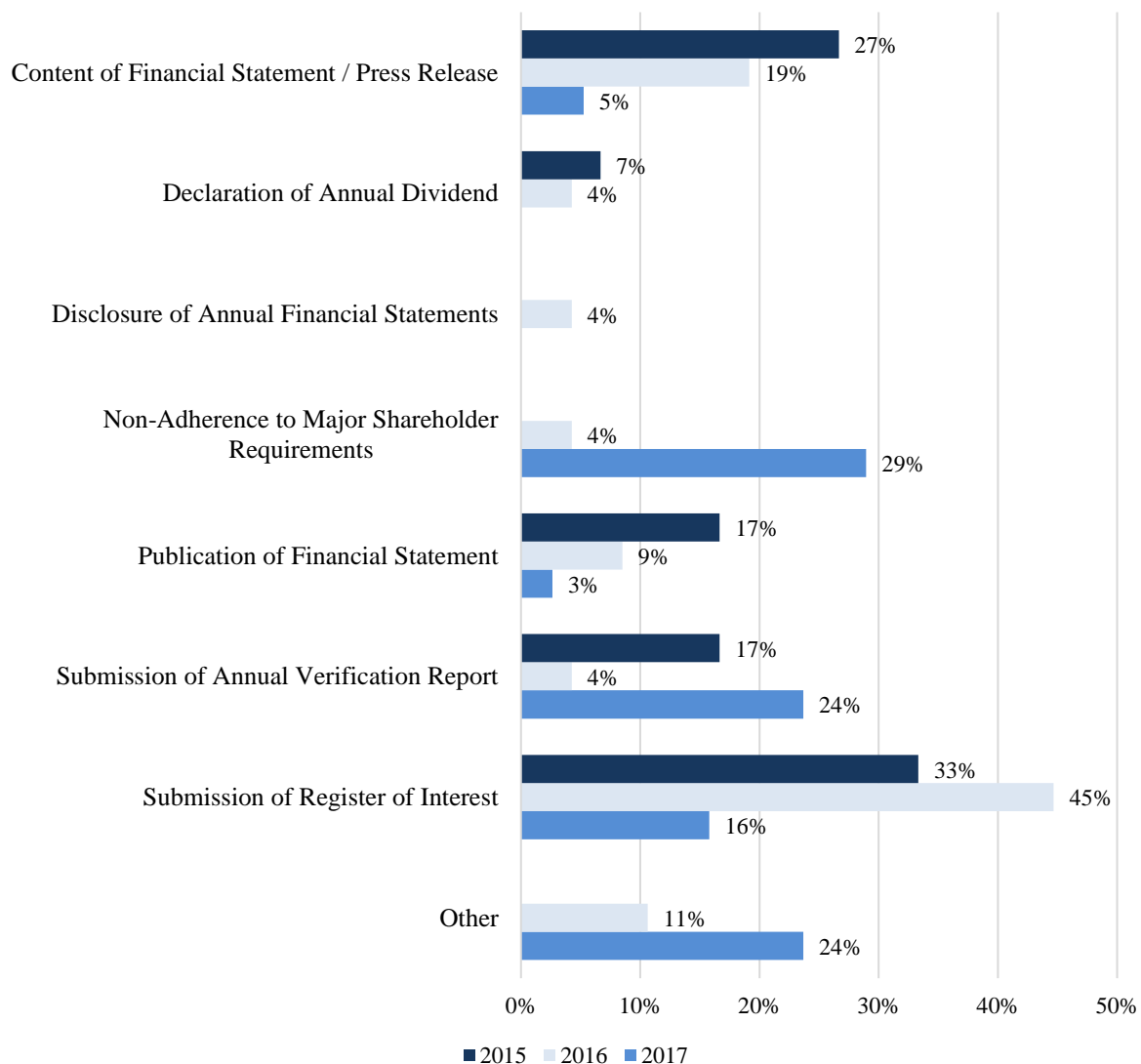
With reference to MIE-3.1.8 of the Market Surveillance, Investigation and Enforcement Module of Volume 6 of the CBB Rulebook, in deciding on any given regulatory and enforcement response, the CBB is dependent on examining the circumstance of each individual contravention against the CBB Law and the MIE Module. The CBB’s approach is three-way, in that the gravity of each respective contravention is assessed, the concerned person’s/entity’s compliance track record is examined and finally remedial measures to prevent future contraventions are evaluated and consequently instituted. Accordingly, this section will examine the most recent cases of contraventions of CBB Law and CBB rulebook requirements.

2.1. Listed Companies

Figure 1 below illustrates the overall trend of CMSD-identified contraventions (including those to which it issued Non-Compliance Letters (“NCLs”), Reminders, Notices or suspension of trading) in the years 2015-2017 across listed companies:

Figure 1

Most Recurring Contraventions by Type, (2015-2017)



With a focus on the years 2016 and 2017, as illustrated above, the three most common non-compliances across listed companies for 2016 related to Submission of Register of Interest, Content of Financial Statement/Press Release and Publication of Financial Statement. Seeing as these three categories are related to periodic submissions required by listed companies, their recurrence is usually expected from a regulatory perspective due to their high frequency.

In 2017 however, the top three contraventions were concentrated also on the Submission of Register of Interest (albeit at a lower rate of 16% of contraventions as opposed to 45% of contraventions in 2016) along with another periodic return, Submission of Annual Verification Report, but most prevalently, making up approximately a third of all contraventions of 2017, was the Non-Adherence to Major Shareholder Requirements.



To better contextualize the most prevalent contravention in 2017, Non-Adherence to Major Shareholder Requirements, the following encompasses the leading factors to such violations:

- ✓ In line with AML-7.1.1 of the Anti-Money Laundering and Combating of Financial Crime Module in Volume 6 of the CBB Rulebook, *“Any Person whose ownership alone or his ownership together with that of his minor children, or any other accounts under his disposal, or the ownership of any of his associate or affiliate companies amounts to 5% or more of any listed Security of a joint stock company, must notify the licensed exchange forthwith, which must in turn notify the CBB of this fact and the CBB may declare the name of the Person who owns such stake”*. This is also highlighted in Article 32.12.1 of CBB’s Disclosure Standards.
- ✓ With reference to AML-7.1.2 of the Anti-Money Laundering and Combating of Financial Crime Module in Volume 6 of the CBB Rulebook, *“All persons whose ownership alone or whose ownership together with that of their minor children, or the accounts standing under their disposal amounts to 5% or more of any listed security must conclude all transactions on such security on a licensed exchange in Bahrain.”*
- ✓ In accordance with AML-7.1.3 of the Anti-Money Laundering and Combating of Financial Crime Module in Volume 6 of the CBB Rulebook, *“All persons must obtain CBB prior written approval to execute any order that will bring their ownership alone or their ownership together with their minor children, or the accounts standing under their disposal to 10% or more in any listed security. Any further increase of 1% or more shall also be subject to CBB prior written approval.”*

Moreover, the two other prominent non-compliance areas in 2017 conveyed companies' non-adherence to CBB's date-sensitive requirements, namely the Submission of Register of Interest on a monthly basis (not later than 5 working days after the end of each month in accordance with CMSD's Letter CMS/L018/2007 dated 22nd January 2007) and the Submission of the Verification of Insider Register on an annual basis (as per MAM-2.15.6 of the Prohibition of Market Abuse and Manipulation Module of Volume 6 of the CBB Rulebook requiring listed companies to submit their report not later than 10 days after the Annual General Meeting date).

Table 1 below outlines these cases further:

Table 1

Listed Company Contraventions by Type (2015-2017)			
Contraventions by Type	2017	2016	2015
Content of Financial Statement / Press Release	2	9	8
Declaration of Annual Dividend		2	2
Disclosure of Annual Financial Statements		2	
Non-Adherence to Major Shareholder Requirements	11	2	
Publication of Financial Statement	1	4	5
Submission of Annual Verification Report	9	2	5
<i>Submission of Register of Interest</i>	<i>6</i>	<i>7</i>	<i>10</i>
<i>Submission of Register of Interest - through ESRAD</i>		<i>14</i>	
Submission of Register of Interest Total	6	21	10
<i>AGM Agenda Approval</i>		<i>1</i>	
<i>Corporate Governance</i>	<i>1</i>		
<i>Content of Register of Interest</i>		<i>1</i>	
<i>Disclosure of Material Corporate Information</i>	<i>3</i>	<i>1</i>	
<i>Non-compliance with CMSD Instructions</i>	<i>1</i>	<i>1</i>	
<i>Publication of Financial Statement Prior to BOD Approval</i>	<i>1</i>	<i>1</i>	
<i>Publication of OGM Agenda</i>	<i>2</i>		
<i>Treasury Share Transactions</i>	<i>1</i>		
Other Total	9	5	
Grand Total	38	47	30

As outlined in Table 1 above, total non-compliances by listed companies in 2017 (38 contraventions) has decreased from 2016's (47 contraventions) by 9 cases, the majority of which is attributed to the Submission of Register of Interest – through ESRAD (CBB's electronic submission portal) requirement which was only introduced in 2015 as per CMSD letters dated 26th January 2015 (Ref: CMS/L010/15) and 2nd February 2015 (Ref: CMS/L017/15) and subsequently enforced following CMSD's e-mail to listed companies dated 18th July 2016.

In addition to viewing the contravention cases by type and listed company in question, the CBB's enforcement mechanism must also be examined. As per Article 87 of Decree No. (64) of 2006 with respect to promulgating the Central Bank of Bahrain and Financial Institutions Law, the CBB is empowered to suspend trading of any listed securities facing exceptional circumstances which it considers as sufficient grounds for suspension. The CBB, supported by regulations specifying cases in which it will suspend the trading of securities, may decide to suspend and subsequently resume securities' trading once the requirement is met. Table 2 below denotes the notable suspension cases of 2015-2017:

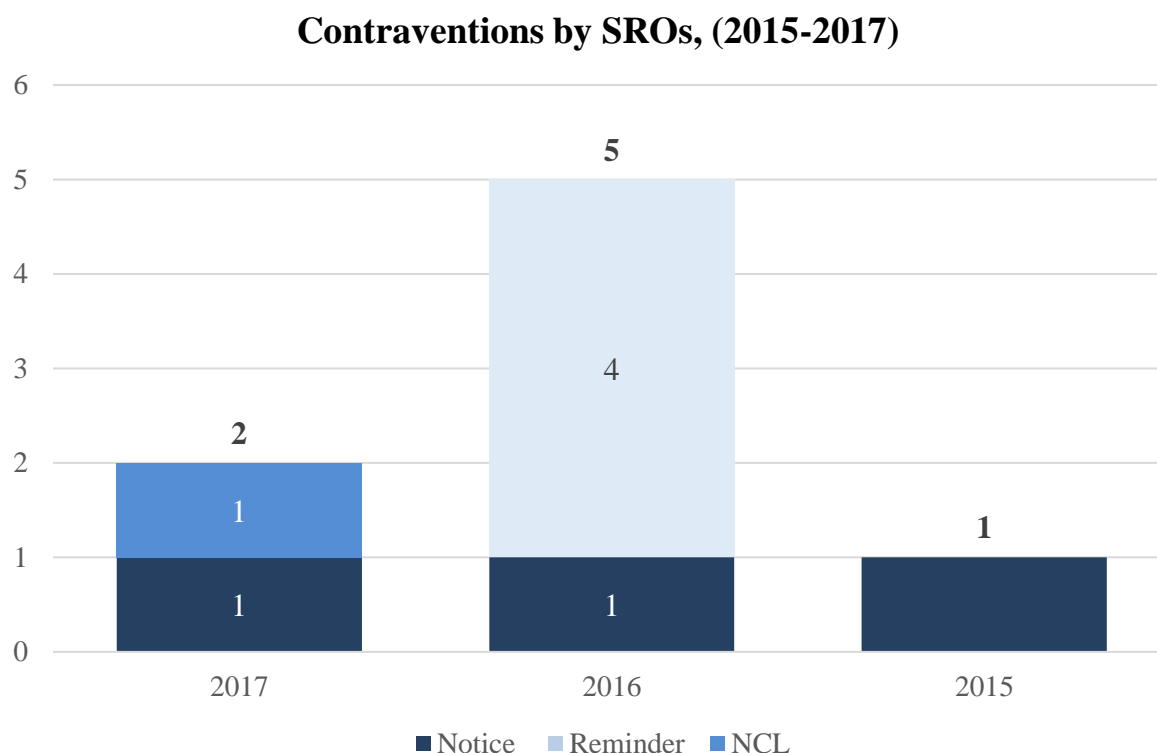
Table 2

Suspension Cases (2015-2017)					
Nature of Suspension	Listed Company	Legal Reference	2017	2016	2015
Content of Financial Statement / Press Release	INOVEST	CBB's Disclosure Standards particularly Article 65 "Content and Preparation of a Public Announcement".		1	
	GFH	CBB's Disclosure Standards particularly Article 65 "Content and Preparation of a Public Announcement" and Article 42.5.12 requiring prompt announcements relating to declaration or omission of dividends or determination of earnings.	1		
		Resolution No. (54) of 2015 in respect of The Disclosure of Listed Companies' Financial Statements & Board of Directors' Meetings.		1	
		CBB's Disclosure Standards; CBB Law 2006; Bahrain Bourse Rules & Regulations.			1
Disclosure of Annual Financial Statements	BTC	Resolution No. (54) of 2015 in respect of The Disclosure of Listed Companies' Financial Statements & Board of Directors' Meetings.		1	
Publication of Financial Statement	ITHMR	Resolution No. (49) of 2007, particularly Article (3) in respect of The Disclosure of Listed Companies' Financial Statements & Board of Directors' Meetings.			1
Unusual Trading Activity	INOVEST	Article (87) of the CBB Law 2006.	1		
Other - Disclosure of Material Corporate Information	AHLIA	CMSD letter dated 3 rd December 2003 (ref: ODG/407/03) regarding Disclosure Standards; TMA-2.3.11 of the Takeovers, Mergers & Acquisitions Module of Volume 6 of the CBB Rulebook.		1	
	AUB	CBB's Circular Ref. OG/352/2005 dated 20 th November 2005 in respect of Disclosure Standard Press Announcements, and Article (54) and (55) of CBB's Disclosure Standards; TMA-2.3.11 of the Takeovers, Mergers & Acquisitions Module of Volume 6 of the CBB Rulebook.	1		
Other - Publication of Financial Statement Prior to BOD Approval	SALAM	Resolution No. (54) of 2015 in respect of The Disclosure of Listed Companies' Financial Statements & Board of Directors' Meetings; CBB's Disclosure Standards; High-Level Controls Module of Volume 6 of the CBB Rulebook.	1		
Grand Total			4	4	2

2.2. Self-Regulatory Organizations (SROs)

With reference to MIE-A.4.2 of the Market Surveillance, Investigation and Enforcement Module of Volume 6 of the CBB Rulebook, the CBB's role includes regulatory supervision which includes licensing, supervision, inspection, investigation and enforcement and regulatory oversight on the licensed exchanges, licensed market operators, licensed clearing houses and depositories and other SROs. In line with this, during the period from 2015 to 2017 and from a supervisory standpoint, the CBB addressed the following:

Figure 2



2.3. Members of SROs (Licensed Brokers)

With reference to MIR-A.4.2 of the Market Intermediaries and Representatives Module of Volume 6 of the CBB Rulebook, the CBB's role includes regulatory supervision which includes licensing, supervision, inspection, investigation and enforcement and regulatory oversight on members of SROs. In line with this, during 2017 and from a supervisory standpoint, the CBB addressed the following:

1. Following an investigation into a suspicious transaction and its subsequent preparation of a preliminary investigation report, the CMSD issued a Reminder Letter, dated 5th April 2017, to one of its licensed brokers due to its non-adherence to MIE-A.4.9 and MIE-A.4.10 of the Market Surveillance, Investigation and Enforcement Module of Volume 6 of the CBB Rulebook and the related Article 4.1.1 of the BHB's Market Rules with regards to maintaining records of telephone conversations and electronic communications by failing to provide an actual copy of the form of communication between itself and its client. The Reminder Letter further advised the broker of its obligation to abide by MIR-A.4.4 (a) of the Market Intermediaries and Representatives

Module of Volume 6 of the CBB Rulebook, which entails the adherence to BHB's and the CBB's rules and regulations in executing client orders.

2. Following an investigation into a suspicious transaction and its preparation of a preliminary investigation report which was subsequently forwarded to the Enforcement Decisions Review Committee ("EDRC"), the CMSD issued a Formal Warning, dated 3rd July 2017, to another licensed broker due to its contravention of MAM-3.10.19 of the Prohibition of Market Abuse and Manipulation Module of Volume 6 of the CBB Rulebook as well as MIR-A.4.4 (a) and MIR-4.1.1 (k) of the Market Intermediaries and Representatives Module of Volume 6 of the CBB Rulebook, wherein a member is expected to ensure that there are sufficient records, books and systems in place to record all transactions executed, cleared and settled through its system and accordingly maintain an audit trail in accordance with the CBB's and BHB's rules and regulations.



3. The CMSD issued a Reminder Letter, dated 2nd August 2017, to a licensed broker in relation to executing a major shareholder transaction without seeking the CMSD's approval which is in contravention of AML-7.1.3 of the Anti-Money Laundering and Combating of Financial Crime Module in Volume 6 of the CBB Rulebook which stipulates that all persons must obtain the CBB's prior written approval to execute any order that will bring their ownership alone or their ownership together with their minor children, or the accounts standing under their disposal to 10% or more in any listed security or any further increase of 1% or more. Additionally, it is worth emphasizing that within its capacity as the broker, and as per MIR-A.4.4 (a) of the Market Intermediaries and Representatives Module of Volume 6 of the CBB Rulebook, the broker was obligated to be well-aware of the BHB's and the CBB's rules and regulations and as such, was expected to proactively advise the client of the potential market misconduct (i.e. major shareholder trading without CBB approval).

3. Imposition of Financial Penalties

➤ Imposition of Financial Penalty for Non-Adherence to Treasury Share Repurchase Requirements

Following the CMSD's issuance of a Non-Compliance Letter dated 3rd July 2017 to a listed company, based on EDRC's subsequent recommendation, a Notice, dated 12th September 2017, was issued to the company stipulating the imposition of a financial penalty due to its failure to comply with treasury share repurchase requirements. The Notice underscored the company's violations in relation to its treasury share repurchase program, which are detailed as follows:

- Failure to comply with the CBB requirements pertaining to treasury shares repurchase transactions in terms of the CBB's 90-day approval validity period stipulated in TMA-1.16 of the Takeovers, Mergers and Acquisitions of Volume 6 of the CBB's Rulebook, wherein the company executed a transaction to purchase treasury shares on 2nd July, 2017, well beyond the validity period ending on 23rd June, 2017.
- Failure to comply with the terms set out in the CMSD's 'No Objection Letter' and particularly the item pertaining to the restriction of trading in treasury shares solely on the Bahrain Bourse, subsequent to the CMSD's approval. On the contrary, the company has endeavored to purchase treasury shares on a secondary exchange in one of the Gulf Cooperation Council States (where the company is cross-listed), hence contravening this requirement.

In light of the above, the CMSD believes that the company should have exerted the necessary care and diligence in abiding by the stipulated requirements and seeking the CBB's formal approval prior to engaging in any further share repurchase activities beyond the remit of CMSD's initial approval and as such and in accordance with Article (129) of the CBB Law, the CBB formally imposed a financial penalty on the company. In response, the company duly submitted its appeal on 10th October 2017 which was forwarded to and subsequently rejected by the Appeal Committee hence re-enforcing the listed company's duty to pay the stipulated financial penalty.

4. Conclusion

In conclusion, the CMSD carefully considers the appropriate regulatory response to potential breaches of rules or market misconduct. Seeing as each non-compliance or suspected case is unique and involves a variety of different circumstantial elements, the CMSD strives to be as consistent and transparent as possible in the related decision-making. The CMSD's most prevalent role revolves around ensuring effective implementation and enforcement of CBB's regulatory requirements for the capital markets, as such, it continuously seeks to develop and improve its regulatory framework (including the clear articulation of regulatory requirements to all stakeholders, imposition of sanctions and enforcement of disciplinary actions) in line with regional and international counterparts and benchmarks. Ultimately, and in line with findings of this annual report, the CMSD, alongside key stakeholders, will work to improve standards of compliance in the market, reduce recurrences and overall boost market awareness of its regulatory framework – with the core objective of solidifying the efficiency of one of Bahrain's aspired key financial drivers, the capital markets.