



# SHARI'A GOVERNANCE MODULE

CONSULTATION



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<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-A: Introduction</b>

## SG-A.1 Purpose

SG-A.1.1 The purpose of the Module is to establish best practice Shari'a governance principles in Bahrain, and to provide protection for investors and other Islamic bank licensees' stakeholders through compliance with these principles.

SG-A.1.2 Shari'a Governance can be defined as a system whereby a Bahraini Islamic bank licensee attempts to comply with Shari'a in all its activities. It is the duty of all the stakeholders to strengthen Shari'a Governance framework of their respective institutions. The main objectives of a Shari'a Governance framework are:

- (a) To provide a structure and a system to govern all the business activities of the Bahraini Islamic bank licensee in order to ensure Shari'a compliance at all times and at all levels.
- (b) To enable the Bahraini Islamic bank licensee to be perceived as Shari'a compliant by the stakeholders including the general public.

SG-A.1.3 This Module provides support for certain other parts of the Rulebook, mainly:

- (a) High-level Controls;
- (b) Licensing Requirements; and
- (c) Training and Competency.

SG-A.1.4 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'.

### *Legal Basis*

**SG-A.1.5** This Module contains the CBB's Directive (as amended from time to time) relating to Shari'a Governance 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 all Bahraini Islamic bank licensees (including their approved persons).

SG-A.1.6 For an explanation of the CBB's rule-making powers and different regulatory instruments, see Section UG-1.1.

### *Effective Date*

SGA.1.7 This Module issued in Month 20xx is effective on xx xx 20xx. All Bahraini Islamic bank licensees to which Module SG applies should be in full compliance by the financial year end 20xx.



<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-B: Scope of Application</b>

## SG-B.1 Scope of Application

**SG-B.1.1** The contents of this Module – unless otherwise stated – apply to all Bahraini Islamic bank licensees incorporated in the Kingdom of Bahrain.

**SG-B.1.2** Branches of foreign banks must satisfy the CBB that equivalent arrangements are in place at the parent entity level, and that these arrangements provide for effective Shari'a governance over activities conducted under the Bahrain license.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-B: Scope of Application</b>

## SG-B.2 Subsidiaries and Foreign Branches

### SG-B.2.1

Bahraini Islamic bank licensees must ensure that, as a minimum, the same or equivalent provisions of this Module apply to their subsidiaries (operating or SPVs) and foreign branches, such that these are also subject to effective Shari'a governance. In instances where local jurisdictional requirements are more stringent than those applicable in this Module, the local requirements are to be applied.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-1: Shari'a Governance Structure</b>

## SG-1.1 Principle

**SG-1.1.1** The Shari'a Governance structure adopted by the Bahraini Islamic bank licensee must be commensurate and proportionate with the size, complexity and nature of its business.

**SG-1.1.2** The Shari'a Governance structure must consist, at a minimum, of the following:

- (a) Shari'a Supervisory Board (SSB);
- (b) Internal Shari'a Advisory Function;
- (c) Internal Shari'a Audit Function; and
- (d) Independent External Shari'a Compliance Audit

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2:</b>	<b>Shari'a Supervisory Board (SSB)</b>

## SG-2.1 Principle

### SG-2.1.1

All Bahraini Islamic bank licensees must have a Shari'a Supervisory Board (SSB), which must consist of at least three scholars specialized in fiqh al muamalat, and whose members must be approved by the shareholders in their annual general meeting upon the recommendation of the board of directors taking into consideration the CBB regulations, resolutions and directives.

### SG-2.1.2

Bahraini Islamic bank licensees must comply with the Shari'a rules and principles as expressed in the rulings of their respective SSB.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2: Shari'a Supervisory Board (SSB)</b>

## SG-2.2 SSB Charter

### SG-2.2.1

A charter must be prepared by Bahraini Islamic bank licensees and approved by their Board of directors defining the scope of work for the SSB.

### SG-2.2.2

A typical charter of the SSB must include, at a minimum, the following:

- (a) Purpose of the charter;
- (b) Authorisation of the charter;
- (c) Membership of the SSB;
- (d) Composition of the SSB;
- (e) Chairperson;
- (f) Secretary;
- (g) Possible cause/course of removal and replacement of a Member;
- (h) Authority of the SSB;
- (i) Responsibilities of the SSB;
- (j) Meetings;
- (k) Voting and decisions;
- (l) Amendments to the charter; and
- (m) Relationship with the Board of Directors, senior management and other departments.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2:</b>	<b>Shari'a Supervisory Board (SSB)</b>

### SG-2.3 Roles and Responsibilities of the SSB

SG-2.3.1

The SSB must be vested with appropriate powers and authorities as may be necessary to perform its duties and responsibilities effectively. The fatawa and rulings of the SSB are binding on the Bahraini Islamic bank licensee.

SG-2.3.2

The SSB must supervise the Bahraini Islamic bank licensee's operations and activities to ensure compliance with the Islamic Shari'a, and also monitor and review transactions to ensure full compliance with Shari'a rules and principles and SSB pronouncements.

SG-2.3.3

The SSB must ensure, with the cooperation of the independent external Shari'a compliance auditor (IESCA), the existence of an appropriate and functioning internal Shari'a control framework for the compliance with Islamic Shari'a rules and principles.

SG-2.3.4

The SSB must approve the internal Shari'a audit annual plans.

SG-2.3.5

The SSB must notify the CBB in case of any major Shari'a non-compliance issues of the Bahraini Islamic bank licensee or any failure by the Board of directors to effectively deal with any such issues.

SG-2.3.6

All relevant documentation for new products and services, including contracts, agreements, marketing and promotional materials or other legal documentation used in the Bahraini Islamic bank licensee's business transactions must be approved by the SSB.

SG-2.3.7

The SSB must review and approve the Bahraini Islamic bank licensee's annual Zakah calculations.

SG-2.3.8

The SSB must put on record, in written form, any opinion that it gives on Shari'a-related issues.

SG-2.3.9

The SSB must respond to any enquiries from the Bahraini Islamic bank licensees' shareholders during the discussion of the end of year financial results.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2:</b>	<b>Shari'a Supervisory Board (SSB)</b>

### **SG-2.3 Roles and Responsibilities of the SSB (continued)**

**SG-2.3.10**

The SSB must review the reports and observations of the internal Shari'a advisory function and internal Shari'a audit function on day to day business activities, operations and transactions and provide advice on such reports and observations.

**SG-2.3.11**

The SSB must approve the profit/loss allocation to the investment account holders.

**SG-2.3.12**

The SSB must specify the means of disposal of earnings that have been realised from sources or by means prohibited by Shari'a rules and principles.

**SG-2.3.13**

The SSB must approve the appointment and removal of the head of internal Shari'a advisory function and the head of internal Shari'a audit function and supervise their work.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2: Shari'a Supervisory Board (SSB)</b>

### SG-2.3 Roles and Responsibilities of the SSB (continued)

#### *Operating Procedures*

SG-2.3.14 The SSB must develop its own operating procedures.

#### *Relationship with the Board of Directors*

SG-2.3.15 The SSB must report administratively to the Board of directors. This reporting structure particularly reflects the SSB's independence from the management of the Bahraini Islamic bank licensee.

SG-2.3.16 The SSB must plan and arrange to meet with the Board of directors of the Bahraini Islamic bank licensee at least once a year to discuss issues of common interest. Such meeting must have a clear and specific agenda including the difficulties faced by both parties and ways to resolve them.

#### *SSB Meetings*

SG-2.3.17 The SSB must meet at least on quarterly basis to review and approve key decisions relating to Shari'a matters. Each member of SSB must attend at least three fourth (75%) of the meetings during a calendar year. Attendances through video or conference calls are accepted. Further, in addition to the mandatory quarterly meeting, the SSB chairperson may convene SSB meetings as and when he deems it necessary.

SG-2.3.18 All meetings must be chaired by the SSB chairperson and in his absence, one of the members must be elected as the acting chairperson to preside over the meeting.

SG-2.3.19 The quorum of SSB meetings must be majority of its members. The SSB decisions must be made through majority vote of SSB members.

SG-2.3.20 The agenda of the SSB meetings along with sufficient details must be sent to the SSB members well in advance, enabling them to come prepared in the meetings. The specific timelines for submission of the agenda must be set by SSB itself.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2: Shari'a Supervisory Board (SSB)</b>

### SG-2.3 Roles and Responsibilities of the SSB (continued)

**SG-2.3.21** All the SSB approvals taken through circulation must be part of the minutes of the next SSB meeting.

**SG-2.3.22** The minutes of meetings must be prepared and circulated to the SSB members. The SSB must ensure that the minutes of its meetings have necessary details of all the decisions made and / or fatawa issued along with the detailed rationale (Fiqhi or other) and difference of opinion or dissenting note, if any. Further, the minutes must be signed by all the SSB members who attend the meeting to confirm the matters addressed therein, no later than in the next meeting.

**SG-2.3.23** For purposes of Paragraph SG-2.3.22, decisions taken in SSB meetings must be reflected in policies and procedures and day to day operations of the Bahraini Islamic bank licensee as applicable.

#### *SSB Report*

**SG-2.3.24** The SSB must submit a report (See also Paragraph SG-6.1.1) to the shareholders with a copy to the Board of directors and the CBB as per AAOIFI, on the Bahraini Islamic bank licensee's Shari'a compliance, provided that the SSB report includes any non-compliance issues to the Shari'a rules and principles.

**SG-2.3.25** The SSB's report must contain, at the minimum, the following basic elements:

- (a) Title;
- (b) Addressee;
- (c) Opening or introductory paragraph;
- (d) Scope paragraph describing the nature of the work performed;
- (e) Opinion paragraph containing an expression of opinion on the compliance of the Bahraini Islamic bank licensee with Islamic Shari's Rules and Principles;
- (f) Date of report;
- (g) Signature of the members of the SSB

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2: Shari'a Supervisory Board (SSB)</b>

### SG-2.3 Roles and Responsibilities of the SSB (continued)

SG-2.3.26

The opinion paragraph of the report must at least contain the following:

- (a) Whether or not in the SSB's opinion, the contracts, transactions and dealings entered into by the Bahraini Islamic bank licensee are in compliance with the rules and principles of Shari'a;
- (b) Whether or not in the SSB's opinion, the allocation of funds, weightages, profit sharing ratios, profits and charging of losses (if any) relating to investment accounts conform to the basis given by the SSB in accordance with Shari'a rules and principles;
- (c) Whether or not in the SSB's opinion, any earnings that have been realised from sources or means prohibited by Shari'a rules and principles have been disposed to charitable causes;
- (d) Whether or not in the SSB's opinion, the calculation of Zakah is in compliance with Islamic Shari'a rules and principles; and
- (e) If the SSB has ascertained that the management of the Bahraini Islamic bank licensee has not complied with Shari'a rules and principles or the fatawa, rulings and guidelines issued by the SSB, then the SSB has to report the non-compliance issues in the opinion paragraph of its report.

SG-2.3.27

The SSB report must be read at the annual general meeting of the Bahraini Islamic bank licensee.

#### *Handling Confidential Information*

SG-2.3.28

SSB members must ensure that information obtained in the course of their duties is kept confidential as per Article (117) of the CBB Law.

SG-2.3.29

In the performance of their duties, members of the SSB may have access to files, records, draft materials and conversations that are, under the Bahraini Islamic bank licensee's internal procedures and by market practice, deemed confidential. Where a member of the SSB serves several Bahraini Islamic bank licensees simultaneously, the issue arises as to how they handle confidential or commercially sensitive information obtained in the course of performing their duties. It is a key concern of professional ethics that confidential or sensitive information obtained by a member of the SSB while serving a Bahraini Islamic bank licensee should not be used by them in ways that could be detrimental to that Bahraini Islamic bank licensee, particularly in ways that might give a competitive advantage to its competitors.

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### **SG-2.3 Roles and Responsibilities of the SSB (continued)**

#### *Handling Confidential Information (continued)*

- SG-2.3.30 The duty to observe confidentiality applies to all information with which members of the SSB are entrusted by the licensee, or which is brought to their attention during or at any time after the carrying out of their assignment. Confidentiality obligations do not end when a member of the SSB ceases to serve a Bahraini Islamic bank licensee or when a matter is completed or closed. Members of the SSB should observe the same restrictions unless they have obtained express authorisation from the Bahraini Islamic bank licensee that relieves them from such obligation.

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## SG-2.4 Terms of Appointment and Competence of the SSB

### SG-2.4.1

The appointment of the SSB must be made formally in writing, by way of a contract for service, and with the terms of reference which must contain the following information:

- (a) Who within the Bahraini Islamic bank licensee is authorised to appoint or terminate his service;
- (b) How long is the tenure of the appointment; and
- (c) Whether specific reasons are to be given and/or a certain notice period need to be served before the contract for service is terminated by either party.

### SG-2.4.2

Benefits and remuneration of SSB members must be stated from the outset.

### SG-2.4.3

Where the Bahraini Islamic bank licensee fails to appoint the SSB within 3 months of the annual general meeting, the CBB has the right to appoint a SSB for which all costs related to the appointment will be borne by the Bahraini Islamic bank licensee in addition to any liabilities related to the delay in the appointment of the SSB.

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## SG-2.4 Terms of Appointment and Competence of the SSB (continued)

### *SSB Competence/ Fit and Proper Criteria*

#### SG-2.4.4

The Board of directors of the Bahraini Islamic bank licensee must carry out a background check and consider the following criteria when assessing the fitness and propriety of individuals to serve on the SSB:

- (a) Have a clean background, a good character and conduct by being recognised for honesty, integrity and good reputation, either in their professional business or their financial dealings and not previously been convicted of any moral turpitude felony or criminal offence (See SG- 2.4.5);
- (b) Have competence, diligence, capability and soundness of judgement (See SG-2.4.9);
- (c) Have strong proficiency in Arabic, as they need to be very conversant with the primary sources of the Shari'a.
- (d) Have a reasonable understanding of English;
- (e) Have at least a bachelor degree (or its equivalent) in Islamic Shari'a;
- (f) Have a certified degree in the field of Usul al-Fiqh (rules of Islamic jurisprudence) and Fiqh al Muamalat (Islamic commercial jurisprudence);
- (g) Have adequate understanding of banking, Islamic finance and accounting; and
- (h) Have accumulated overall experience of at least seven years in Shari'a related scholarly pursuits (e.g. teaching, research, fatawa issuance, etc.).
- (i) Have a fair understanding of the legal and regulatory framework applicable to the functions of the Bahraini Islamic bank licensee.

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<b>CHAPTER</b>	<b>SG-2: Shari'a Supervisory Board (SSB)</b>

## SG-2.4 Terms of Appointment and Competence of the SSB (continued)

### *Good Character*

- SG-2.4.5 Good character – that is, honesty, integrity, fairness and reputation – are qualities that are demonstrated over time. In determining a person's good character, and to guide the hiring criteria to be applied before appointing someone to serve on the Shari'a board, the Bahraini Islamic bank licensee should, just as when considering nominations for the Board of directors, the chief executive officer or key senior management, put in place a transparent process that considers all the appropriate factors, including, but not limited to whether the person:
- (a) Has been convicted of a criminal offence, particularly an offence relating to dishonesty, fraud or financial crime;
  - (b) Has been the subject of any adverse findings or any settlement in civil proceedings, particularly in connection with banking or other financial business, misconduct, fraud, or any business in which the person is a controlling shareholder or has a controlling interest or exercises significant influence, has been investigated and disciplined or suspended by a regulatory or professional body, a court or tribunal, whether publicly or privately;
  - (c) Has been the owner, manager or director of a company, partnership or other organisation that has been refused registration, authorisation, membership or a license to conduct trade, business or profession, or has had that registration, authorisation, membership or license revoked, withdrawn or terminated, resulting in the person being refused the right to carry on a trade, business or profession requiring such a license, registration or other authorisation;
  - (d) Has been a director, partner or otherwise involved in the management of a business that has gone into receivership, insolvency or compulsory liquidation while the person was connected with that organisation or within a reasonably short period (e.g. one year) after the person's departure from the institution;
  - (e) Has been dismissed, asked to resign, or resigned from employment or from a position of trust, fiduciary appointment or similar position because of questions about honesty and integrity;
  - (f) Has ever been disqualified from acting as a director or serving in a managerial capacity because of wrongdoing;
  - (g) Has not been fair, truthful and forthcoming in dealings with customers, superiors, auditors and regulatory authorities in the past and/or has been the subject of any justified complaint relating to regulated activities; and
  - (h) Demonstrates a readiness and willingness to comply with the requirements and standards of the regulatory system and other legal, regulatory, or professional requirements and standards.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
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## SG-2.4 Terms of Appointment and Competence of the SSB (continued)

### *Competence and Capability*

SG-2.4.6 The Bahraini Islamic bank licensee should ensure that members of the SSB demonstrate the competence and ability to understand the technical requirements of the business, the inherent risks therein, and the management processes required to conduct its operations effectively, with due regard to the interests of all stakeholders. In assessing the competence and capability of a person, all relevant factors should be considered, including, but not limited to whether the person:

- (a) Has demonstrated, through qualifications and experience, the capacity to successfully undertake the responsibilities of the position;
- (b) Is physically and mentally fit to perform his duties;
- (c) Has sound knowledge of the business; and
- (d) Can allocate sufficient time and attention to the licensee taking into account his existing Shari'a board memberships with other organizations.

SG-2.4.7 The level of knowledge expected from a member serving on a Shari'a board may vary according to the level of responsibility and the type of regulated activity to be carried out by the Bahraini Islamic bank licensee. However, a member of the Shari'a board is generally expected to be able to display an understanding of the:

- (a) Shari'a rules and principles that apply to the Bahraini Islamic bank licensee's proposed activities;
- (b) General legal and regulatory framework that may apply to the functions that he performs; and
- (c) Broad impact of introducing financial products to the market and the public taking into account Maqasid al-Shari'a.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
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## SG-2.5 Independence of SSB Members

### SG-2.5.1

The SSB must play a strong and independent oversight role, with adequate capability to exercise objective judgement on Shari'a-related matters. No individual or group of individuals must be allowed to dominate the SSB's decision-making.

### SG-2.5.2

The SSB members must be truly independent and must be able to exercise independent judgement without undue influence or duress, especially from the board of directors and/or management of the Bahraini Islamic bank licensee. In this respect, a Bahraini Islamic bank licensee must formalise the independence of the SSB and its members.

### SG-2.5.3

The SSB must not include members of the executive/ management team, directors or controllers of the Bahraini Islamic bank licensee.

### SG-2.5.4

One SSB member should be a member of the corporate governance committee of the Bahraini Islamic bank licensee to provide guidance and advice on Shari'a related matters and also to coordinate and link complementary roles and functions of the corporate governance committee and the SSB (See also HC-9.2.4(b)).

### SG-2.5.5

The SSB member must not be an immediate family member (up to second degree blood relationship) with any member of the Bahraini Islamic bank licensees' approved persons including those of its subsidiaries.

### SG-2.5.6

In case of conflict of interest, the member of the SSB must declare it in writing to the SSB of the Bahraini Islamic bank licensee. He must similarly report any such conflict in regard to members of his family, business associates or companies in which he has an interest. Where there is such a conflict of interest, or a duty to another party, then he must abstain from participating in the relevant decision or action on behalf of the Bahraini Islamic bank licensee. Where a notification is made of a conflict, it must be recorded and retained by a designated officer.

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## SG-2.6 SSB Continuous Professional Development

### SG-2.6.1

Bahraini Islamic bank licensees must facilitate and sponsor appropriate induction programs and training for their continuous professional development, in order to enhance the professionalism and effectiveness of persons serving as members of the SSB.

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## SG-2.7 Assessment of the SSB

### SG-2.7.1

**Bahraini Islamic bank licensees must specify and adopt a process for assessing the effectiveness of the SSB as a whole, as well as the contribution by each individual member to its effectiveness on an annual basis. Members of the SSB must be notified of this assessment process at the time of their appointment, so that they have a precise idea as to what is expected of them.**

SG-2.7.2 For purposes of Paragraph SG-2.7.1, the assessment should be made based on an objective performance measurement that is developed in consultation with the SSB and endorsed by the board of directors.

SG-2.7.3 The performance assessment report should be submitted to the board of directors for observation and constructive comments. Where appropriate, the Bahraini Islamic bank licensee shall act on the results of the performance evaluation, such as considering nominations of new members to be appointed to the SSB or seeking the resignation of any member of the SSB who fails to meet adequately the terms and conditions of his contract.

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## SG-2.8 Management Duties to the SSB

### SG-2.8.1

Bahraini Islamic bank licensees must not dismiss any member of the SSB without the CBB's prior approval and the approval of the general assembly.

### SG-2.8.2

Bahraini Islamic bank licensees must ensure that its SSB has:

- (a) Clear terms of reference regarding its mandate and responsibility;
- (b) Well-defined operating procedures and reporting lines; and
- (c) Good understanding of, and familiarity with, professional ethics and conduct.

### SG-2.8.3

Bahraini Islamic bank licensees must equip their SSB with:

- (a) A mandate that grants it appropriate powers to carry out its role and functions;
- (b) Well-organised operating procedures with regard to meetings, the recording of meetings, the manner in which a submission or request for Shari'a pronouncements/resolutions should be made to the SSB, decision-making processes and to whom its decisions will be passed for effective implementation, including processes to review those decisions whenever necessary; and
- (c) A sound code of ethics and conduct that would enhance the integrity, professionalism and credibility of the members of the SSB.
- (d) A procedure either for each individual member or as a group, in the furtherance of their duties, to take independent professional advice, such as on legal, accounting, financial or valuation issues, if necessary, at the Bahraini Islamic bank licensee's expense.

### SG-2.8.4

The management of a Bahraini Islamic bank licensee must provide the SSB with complete, adequate and timely information prior to all meetings and on an ongoing basis.

### SG-2.8.5

The SSB must have complete and unhindered access to all records, transactions, and information from all sources including professional advisors and the Bahraini Islamic bank licensees' employees.

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## SG-2.8 Management Duties to the SSB (continued)

### SG-2.8.6

Information provided must include background or explanatory information relating to matters to be brought before the SSB, copies of disclosure documents, financial statements, legal agreements and opinions given, product and/or transaction structure, promotional materials, and risk assessment reports. As far as possible, such information must be presented in a manner that would assist the SSB to analyse not only the form of, but also the substance surrounding, the issues brought before them.

### SG-2.8.7

The Bahraini Islamic bank licensee must prepare to the SSB, on an annual basis, a management report titled "Management's Shari'a compliance and governance report" on control procedures relating to Shari'a compliance and governance structure at the Bahraini Islamic bank licensee and the management's assertion on the design and operating effectiveness of these controls. This report will form the basis on which the IESCA would issue his independent assurance report (See SG-5.2.1).

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2: Shari'a Supervisory Board (SSB)</b>

## SG-2.9 Shari'a Pronouncements/Resolutions

### SG-2.9.1

Bahraini Islamic bank licensees must have in place an appropriate mechanism for obtaining rulings from the SSB, applying fatawa and monitoring Shari'a compliance in all aspects of their products, operations and activities.

### SG-2.9.2

The mechanism for obtaining rulings from the SSB, applying fatawa and monitoring Shari'a compliance must cover:

- (a) Both ex ante and ex post aspects of all financial transactions carried out by the Bahraini Islamic bank licensee – that is, to ensure Shari'a compliance of the contracts and, later, the performance of obligations under the contracts; and
- (b) Operations of the Bahraini Islamic bank licensee, including aspects such as Shari'a compliance review, investment policies, disposal of Shari'a non-compliant income, charitable activities, etc.

### SG-2.9.3

The Bahraini Islamic bank licensee must fully understand the legal and regulatory framework for issuance of Shari'a pronouncements/resolutions in the jurisdiction where it operates. It must ensure that its SSB strictly observes the said framework.

### SG-2.9.4

The Bahraini Islamic bank licensee must ensure that the SSB adopts a specified process for changing, amending or revising any Shari'a pronouncements/resolutions issued by it. Appropriate and timely disclosure must be made to shareholders and/or the public whenever the SSB and/or its members depart from or revise any of its Shari'a pronouncements/resolutions.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-2:</b>	<b>Shari'a Supervisory Board (SSB)</b>

**SG-2.10 SSB Relationship with the CBB's Centralised SSB (CSSB)**

**SG-2.10.1** In all cases, Bahraini Islamic bank licensees must comply with the Shari'a pronouncements and opinions issued by the CSSB.

**SG-2.10.2** In case of a conflict between the opinion or interpretation of the CSSB and the SSB of the Bahraini Islamic bank licensee with respect to any Shari'a matter, the opinion of the CSSB shall prevail.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-3: Internal Shari'a Advisory</b>

## SG-3.1 Principle

**SG-3.1.1** Bahraini Islamic bank licensees must have a dedicated internal Shari'a advisory function comprised of Shari'a advisory officers and staff technically reporting to the SSB and administratively reporting to the CEO to ensure its independence. The function must be adequately staffed with proficient persons having the relevant qualification and experience (See Appendix TC-1 in Module TC (Training and Competency)).

### *Policy and Procedures*

**SG-3.1.2** The internal Shari'a advisory function must be governed by a policy and procedures manual prepared by the management, vetted by the SSB and then approved by the board of directors.

### *Head of Internal Shari'a Advisory Function*

**SG-3.1.3** The head of internal Shari'a advisory function must be a full time employee of the Bahraini Islamic bank licensee and must be responsible at the product design/development stage for assisting the SSB in the issuance of Shari'a pronouncements/resolutions, fatawa, guidelines and instructions about the products and services offered by the Bahraini Islamic bank licensee.

**SG-3.1.4** The head of internal Shari'a advisory function must be appointed by the management in consultation with the SSB and the approval of the CBB (See Chapter LR-1A).

**SG-3.1.5** The head of internal Shari'a advisory function must be appointed as the secretary to the SSB.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-3: Internal Shari'a Advisory</b>

## SG-3.2 Roles and Responsibilities of the Head of Internal Shari'a Advisory Function

### SG-3.2.1

Internal Shari'a advisory function must review and evaluate, before any product is offered to the customer, the contracts, agreements, fees, charges, policies, procedures, product manuals, product transaction structures, complete offering documentation including, promotion and marketing materials, advertisements and other communications to general public, memorandum and articles of association, and any other matter which can potentially impact the Shari'a compliance of the Bahraini Islamic bank licensee or influence the perception of its Shari'a compliance, and submit thereafter their report, along with all the relevant documentation, to the SSB for their review and decision.

### SG-3.2.2

The Internal Shari'a advisory function must be involved in the testing and implementation of any new products or services to ensure full Shari'a compliance under the relevant fatawa. The function must also assist the relevant staff in dealing with any Shari'a non-compliance issues arising from the implementation stage.

### SG-3.2.3

The head of internal Shari'a advisory function must participate in training the Bahraini Islamic bank licensee's employees by holding regular meetings, courses and seminars. He must also disseminate knowledge by publishing and distributing pamphlets, brochures, etc., explaining principles of fiqh al-muamalat in general, and in particular the fatawa, guidelines and instructions issued by the SSB about the products and services offered by the Bahraini Islamic bank licensee.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-4:</b>	<b>Internal Shari'a Audit</b>

## SG-4.1 Principle

**SG-4.1.1** Bahraini Islamic bank licensees must have an internal Shari'a audit function technically reporting to the SSB and administratively reporting to the CEO. The function must be adequately staffed with proficient staff having the relevant qualification and experience.

### *Policy and Procedures*

**SG-4.1.2** The internal Shari'a audit function must be governed by a policy and procedures manual prepared by the management, vetted by the SSB and then approved by the board of directors.

**SG-4.1.3** For purposes of Paragraph SG-4.1.2, the policy and procedures manual must include, but not limited to, the statement of purpose, authority and responsibility. The policy and procedures manual must make clear that the internal Shari'a audit staff have no executive authority or responsibility for the activities they audit.

### *Head of Internal Shari'a Audit Function*

**SG-4.1.4** The head of internal Shari'a audit function must be a full time employee of the Bahraini Islamic bank licensee and must be responsible for examining and evaluating the extent of the Islamic bank licensee's compliance with the following:

- (a) Shari'a principles;
- (b) The SSB's Fatawa, guidelines, pronouncements and instructions/ recommendations;
- (c) Shari'a related regulations, resolutions and directives issued by the CBB;
- (d) Shari'a standards issued by AAOIFI; and
- (e) Shari'a related policies and procedures of the Bahraini Islamic bank licensee.

**SG-4.1.5** The head of internal Shari'a audit function must express his opinion to the SSB on the extent of Shari'a compliance of the Bahraini Islamic bank licensee's operations through an actual audit of the business transactions.

**SG-4.1.6** The head of internal Shari'a audit function must be appointed by the management in consultation with the SSB and approved by the CBB (refer to Chapter LR-1A).

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-4:</b>	<b>Internal Shari'a Audit</b>

## SG-4.2 Roles and Responsibilities of the Head of Internal Shari'a Audit Function

**SG-4.2.1** The head of internal Shari'a audit function must review and examine the adequacy and effectiveness of the Bahraini Islamic bank licensee's Shari'a compliance system. This must cover all aspects of the Bahraini Islamic bank licensee's business operations and activities in order to assess the extent of c Shari'a compliance requirements as stated under Paragraph SG-4.1.4.

**SG-4.2.2** The head of internal Shari'a audit function must have direct and regular communications with all levels of management, SSB, Audit Committee, internal Shari'a advisors and IESCA's. No scope limitation and/or restriction of access to documents, reports, etc. must be placed on internal Shari'a audit staff.

**SG-4.2.3** Internal Shari'a audit staff must be objective and maintain independent attitude in performing their internal Shari'a audit. They must reach objective conclusions based on work performed and the results thereof.

### *Internal Shari'a Audit Report*

**SG-4.2.4** The head of internal Shari'a audit function must prepare periodic reports to the SSB, based on the audit plan, for consideration and appropriate action. A copy of such reports must also be presented to the audit committee of the board and the CEO.

**SG-4.2.5** The head of internal Shari'a audit function must follow up to ascertain that appropriate action is taken on his reported findings and recommended corrective actions. In addition, any other recommendations relating to Shari'a matters made by the SSB, the IESCA's and the CBB must be followed up.

**SG-4.2.6** Any difference of opinion between the management and the head of internal Shari'a audit function on matters relating to Shari'a interpretation must be referred to and decided by the SSB.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-4: Internal Shari'a Audit</b>

## SG-4.2 Roles and Responsibilities of the Head of Internal Shari'a Audit Function (continued)

### *Shari'a Audit Plan*

SG-4.2.7

The head of internal Shari'a audit function must have an internal Shari'a audit plan in place which must be approved by the SSB on an annual basis.

SG-4.2.8

For purposes of Paragraph SG-4.2.7, the internal Shari'a audit planning process must include, but not be limited to, the following:

- (a) Obtaining background information about the activities to be audited, such as locations, products/services, branches, divisions, etc.;
- (b) Establishing internal Shari'a audit objectives and scope of work;
- (c) Obtaining SSB Fatwas, guidelines, instructions, prior year internal and independent external Shari'a compliance audit results, relevant correspondence including with the CBB;
- (d) Determining the resources necessary to perform internal Shari'a audit;
- (e) Communicating with all the individuals at the Bahraini Islamic bank licensee who need to know about internal Shari'a audit; and
- (f) Performing, as appropriate, a survey to become familiar with activities, risks and controls to identify areas of internal Shari'a audit emphasis, and to invite comments and suggestions.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-5:</b>	<b>Independent External Shari'a Compliance Audit</b>

## SG-5.1 Principle

**SG-5.1.1** Bahraini Islamic bank licensees must appoint, on an annual basis, an independent external Shari'a compliance auditor (IESCA) approved by the CBB.

SG-5.1.2 For the purpose of Paragraph SG-5.1.1, Bahraini Islamic bank licensees may engage their external auditor or other independent audit firms as approved by the CBB.

**SG-5.1.3** The IESCA must be adequately resourced with proficient staff having the relevant qualification and experience.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-5:</b>	<b>Independent External Shari'a Compliance Audit</b>

## SG-5.2 Roles and Responsibilities of Independent External Shari'a Compliance Audit

### SG-5.2.1

The IESCA must conduct an annual independent external Shari'a compliance audit, to be completed before the issuance of the annual SSB Report, and submit his independent assurance report on the management's report (See SG-2.8.7) to the Audit Committee and thereafter to the SSB and the management of the Bahraini Islamic bank licensee (See Appendix SG-1 under Part B of the CBB Rulebook Volume 2).

### SG-5.2.2

IESCA must assess the existence of relevant controls and their effectiveness in implementation by the Bahraini Islamic bank licensee's management of the policies, procedures and decisions of the SSB to achieve Shari'a compliance.

### SG-5.2.3

The independent external Shari'a compliance audit report must be guided by International Standards on Assurance Engagements 3000, Assurance other than Audits or Reviews of Historical Financial Information in order to ensure that Bahraini Islamic bank licensee's activities are conducted in a Shari'a compliant manner in accordance with Shari'a guidelines / directives issued by its SSB and must also be in compliance with applicable AAOIFI standards and CBB regulations, resolutions and directives.

### SG-5.2.4

The IESCA should have no responsibility for assessing the competence of the members of the SSB.

### SG-5.2.5

The IESCA should satisfy himself that the Bahraini Islamic bank licensee's process for introducing new products, transaction or service or modifying existing ones includes appropriate procedures for ensuring compliance with Shari'a rules and principles including reviews by the Bahraini Islamic bank licensee's senior management, internal audit and SSB.

### SG-5.2.6

The IESCA must test on a sample basis the transaction level controls, product specific controls and other relevant controls. For detailed work requirement, see Appendix SG-1 under Part B of the CBB Rulebook Volume 2.

<b>MODULE</b>	<b>SG:</b>	<b>Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-5:</b>	<b>Independent External Shari'a Compliance Audit</b>

**SG-5.2 Roles and Responsibilities of Independent External Shari'a Compliance Audit (continued)**

**SG-5.2.7**

The IESCA must review the findings of all internal Shari'a audits carried out by the Bahraini Islamic bank licensee's internal Shari'a audit function.

**SG-5.2.8**

For the independent external Shari'a compliance audit, the audit committee in consultation with the SSB must ensure as far as possible that the IESCA is capable of conducting, and does conduct, ex post Shari'a compliance reviews.

<b>MODULE</b>	<b>SG: Shari'a Governance</b>
<b>CHAPTER</b>	<b>SG-6: Disclosure Requirements</b>

## SG-6.1 Disclosure Requirements

- SG-6.1.1** The SSB report must be published as part of the annual report and must include an opinion paragraph containing an expression of opinion on the compliance of the Bahraini Islamic bank licensee with Shari'a rules and principles, the SSB's Fatawa and guidelines, Shari'a related policies and procedures of the licensee, AAOIFI's Shari'a standards and the regulations, resolutions and directives issued by the CBB.
- SG-6.1.2** Bahraini Islamic bank licensees must make SSB's rulings of standard products and their evidence (fiqhi and other) available to the customers and the general public through appropriate publication and communication channels (e.g. making available on the website)
- SG-6.1.3** Bahraini Islamic bank licensees must disclose in their annual report the aggregate remuneration paid to SSB members during the year.
- SG-6.1.4** The Bahraini Islamic bank licensee's financial statements must disclose the amount and nature of earnings that have been realised from sources or by means which are not permitted by Shari'a. Likewise, disclosures must be made of the amount and nature of expenditures for purposes not permitted by Shari'a. The Bahraini Islamic bank licensee must also disclose how it intends to dispose of the assets generated by the prohibited earnings or acquired through prohibited expenditures.