



# **HIGH-LEVEL CONTROLS MODULE**

CONSULTATION



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<b>MODULE</b>	<b>HC: High-Level Controls</b>
<b>CHAPTER</b>	<b>HC-A: Introduction</b>

## **HC-A.1 Executive Summary**

### *Purpose*

- HC-A.1.1 The purpose of this Module is to:
- (a) Explicitly reinforce the collective oversight and risk governance responsibilities of the board;
  - (b) Emphasise key components of risk governance such as risk culture, risk appetite and their relationship to a licensee's risk capacity;
  - (c) Delineate the specific roles of the board, board committees, senior management, chief financial officer, internal auditor, chief risk officer and head of compliance; and
  - (d) Strengthen licensees' overall checks and balances.
- HC-A.1.2 All references in this Module to 'he' or 'his' shall, unless the context otherwise requires, be construed as also being references to 'she' and 'her'.

### *Legal Basis*

**HC-A.1.3** 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 licensees (including their approved persons).

### *Rules and Guidance*

**HC-A.1.4** 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 paragraphs which are considered best market practices and licensees are encouraged to implement the same.

### *Effective Date*

**HC-A.1.5** The new requirements in this amended Module are effective from XXX 2023 on which date the existing Module HC will become redundant, and any exemptions allowed under the existing Module will be subject to grandfathering requirements unless the relevant requirement has undergone change within this amended Module.





MODULE	HC:	High-Level Controls
CHAPTER	HC-B:	Scope of Application

## HC-B.1 Scope of Application

- HC-B.1.1** The contents in this Module apply to the following specialised license types, except where it is stated otherwise:
- (a) Money changer licensees;
  - (b) Financing company licensees;
  - (c) Microfinance institutions;
  - (d) Payment service providers (PSP); and
  - (e) Trust service providers.
- HC-B.1.2 The implementation of the rules in this Module should be commensurate with the size, complexity, structure, economic significance, risk profile and business model of the licensee and the group to which it belongs, if any. In cases of certain licensees (e.g. overseas licensees, smaller and limited scope firms where CBB assesses that certain specific rules in this Module are less relevant or too cumbersome to apply, it will be willing to consider alternative governance arrangement.
- HC-B.1.3 For overseas licensees, all references in this Module to the board of directors or a board sub-committee should be interpreted as references to the Head Office (HO), Regional Office (RO) or the relevant function(s) at HO or RO (as applicable).
- HC-B.1.4 Overseas licensees should satisfy the CBB that equivalent or similar arrangements are in place at either the overseas licensee or the parent entity level, and that such arrangements provide for effective high-level controls over activities conducted by the overseas licensee, commensurate with the size, complexity, nature and the risk profile of the overseas licensee. If the overseas licensee is unable to satisfy the CBB that the governance arrangements are equivalent, the CBB will assess the potential impact of risks and require that the licensee satisfy that compensating alternative arrangements are in place to address any risks relevant to the Bahrain operations.



MODULE	HC:	High-Level Controls
CHAPTER	HC-B:	Scope of Application

## HC-B.2 Subsidiaries and Overseas Branches of Bahraini Licensees

**HC-B.2.1** Bahraini licensees must ensure that, as a minimum, the same or equivalent provisions of this Module apply to their subsidiaries and overseas branches. 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 Where a licensee is unable to satisfy the CBB that its subsidiaries and overseas branches are subject to the same or equivalent arrangements, the CBB will assess the potential impact of risks to the licensee arising from inadequate high-level controls. In such instances, the CBB may impose certain restrictions on the licensee. Where weaknesses in controls are assessed by the CBB to pose a major threat to the financial soundness of the licensee and/or the financial stability in the Kingdom, then its license may be called into question.



MODULE	HC: High-Level Controls
CHAPTER	HC-1: Board's Overall Responsibilities

## HC-1.1 Responsibilities of the Board

### HC-1.1.1

The board of directors ("Board") of the licensee must:

- (a) Set the "tone at the top" and play a leading role in establishing the licensee's corporate culture and values, and oversee management's role in fostering and maintaining a sound corporate and risk culture;
- (b) Ensure that no individual or group of directors dominates the Board's decision-making and no individual or group has unfettered powers of decision;
- (c) Approve and oversee the development of the licensee's strategy, business plans and budget, and monitor their implementation;
- (d) Actively engage in the affairs of the licensee, keep up with material changes in the licensee's business and the external environment and act in a timely manner to protect the long-term interests of the licensee;
- (e) Convene and prepare the agenda for shareholder meetings;
- (f) Approve, and oversee the implementation of, the licensee's governance framework, risk management framework and all policies, and review the relevant parts of these as well as review key controls in case a new business activity is considered, or in case of material changes to the licensee's size, complexity, business strategy, markets or regulatory requirements, or the occurrence of a major failure of controls;
- (g) Establish, along with senior management and the chief risk officer, or its equivalent, the licensee's risk appetite, considering the licensee's strategy, competitive and regulatory landscape, the licensee's long-term interests, risk exposure and ability to manage risk effectively, and oversee the licensee's adherence to the risk appetite statement, risk policy and risk limits;
- (h) Ensure that:
  - i. Adequate systems, controls, processes and procedures are implemented by senior management in line with the Board approved policies;
  - ii. The licensee has adequate processes to ensure full compliance with the requirements of the CBB Law, other relevant laws and the pertinent rulebooks;





MODULE	HC: High-Level Controls
CHAPTER	HC-1: Board's Overall Responsibilities

## HC-1.1 Responsibilities of the Board (continued)

- iii. The licensee has a robust finance function responsible for accounting and financial data;
- iv. The risk management, compliance and internal audit functions are properly positioned, staffed and resourced and carry out their responsibilities independently, objectively and effectively; and
- v. Senior management maintains an effective and transparent relationship with the CBB;
- (i) Approve the annual financial statements and, where applicable, the interim financial statements;
- (j) At minimum, approve the selection and oversee the performance of the chief executive officer (CEO), chief financial officer and heads of the risk management, compliance and internal audit functions;
- (k) Actively oversee the remuneration system's design and operation for approved persons and monitor and review executive compensation and assess whether it is aligned with the licensee's remuneration policy, risk culture and risk appetite; and
- (l) Consider the legitimate interests of shareholders and other relevant stakeholders in their decision-making process.

HC-1.1.2 The Board may, where appropriate, delegate some of its functions, but not its responsibilities, to the Board committees.

**HC-1.1.3** The members of the Board must exercise their fiduciary and other duties of care, candor and loyalty to the licensee in accordance with local laws and regulations.

**HC-1.1.4** Each director must:

- (a) Understand the Board's role and responsibilities pursuant to the CBB Rulebook, the Commercial Companies Law and any other laws or regulations that may govern their responsibilities from time to time;
- (b) Consider themselves as representing all shareholders and must act accordingly; and
- (c) Ensure that they receive adequate and timely information before each meeting and must study it carefully.



MODULE	HC: High-Level Controls
CHAPTER	HC-1: Board's Overall Responsibilities

## HC-1.2 Corporate Culture and Values

### HC-1.2.1

In order to promote a sound corporate culture, the Board must:

- (a) Approve an appropriate code of conduct/ ethics that must outline the acceptable practices that all Board members, senior management and other staff must follow in performing their duties, and the unacceptable practices/ conduct that must be avoided;
- (b) Set and adhere to corporate values that create expectations that the business must be conducted in a legal, professional and ethical manner, and oversee the adherence to such values by Board members, senior management and other employees;
- (c) Promote risk awareness within a strong risk culture, convey the Board's expectation that it does not support risk-taking beyond the risk appetite and risk limits set by the Board, and that all employees are responsible for ensuring that the licensee operates within the established risk appetite and risk limits;
- (d) Ensure that the corporate values, professional standards and codes of conduct it sets, together with supporting policies, are adequately communicated throughout the licensee; and
- (e) Ensure that all directors, senior management and other staff are aware that appropriate disciplinary or other actions will follow unacceptable behaviour, practices and transgressions.

### HC-1.2.2

Employees must be encouraged and be able to communicate, confidentially and without the risk of reprisal, legitimate concerns about illegal, unethical or questionable practices. This must be facilitated through a well communicated and Board approved whistleblowing policy and adequate procedures and processes, consistent with applicable laws. This includes the escalation of material concerns to the CBB.

### HC-1.2.3

The Board of the licensees must:

- (a) Have oversight of the whistleblowing policy mechanism and ensure that senior management addresses legitimate issues that are raised;
- (b) Take responsibility for ensuring that staff who raise concerns are protected from detrimental treatment or reprisals, and that their rights are not undermined;



MODULE	HC: High-Level Controls
CHAPTER	HC-1: Board's Overall Responsibilities

## HC-1.2 Corporate Culture and Values (continued)

- (c) Approve and oversee how and by whom legitimate material concerns shall be investigated and addressed such as by an objective and independent internal or external body, senior management and/or the Board itself; and
- (d) Ensure that, after verifying the validity of the allegations, the person responsible for any misconduct is held accountable and is subjected to an appropriate disciplinary measure.

### HC-1.2.4

The Board must establish a conflict of interest policy on identifying and managing potential conflicts of interest related to all approved persons. The policy must include:

- (a) An approved person's duty to:
  - i. Avoid, to the extent possible, activities that could create conflicts of interest or the appearance of conflicts of interest. An approved person shall be considered to have a "personal interest" in a transaction with a company if they themselves, or a member of their family (i.e. spouse, father, mother, sons, daughters, brothers or sisters), or another company of which they are a director or controller, are a party to the transaction or have a material financial interest in the transaction or are expected to derive material personal benefit from the transaction (transactions and interests which are de minimis in value should not be included);
  - ii. Promptly disclose any matter that may result, or has already resulted, in a conflict of interest;
  - iii. Abstain from getting involved in or voting on any matter where they may have a conflict of interest or where their objectivity or ability to properly fulfil duties to the licensee may be otherwise compromised. Any decision to enter into a transaction in which an approved person appears to have a material conflict of interest must be formally and unanimously approved by the entire Board;
  - iv. Act with honesty, integrity and care for the best interest of the licensee and its shareholders and other stakeholders;
  - v. Not use properties of the licensee for their personal needs;
  - vi. Not misuse or misappropriate the licensee's assets or resources;



MODULE	HC: High-Level Controls
CHAPTER	HC-1: Board's Overall Responsibilities

## HC-1.2 Corporate Culture and Values (continued)

### HC-1.2.4

(cont'd)

- vii. Not disclose confidential information of the licensee or use it for their personal profit or interest;
  - viii. Make every practicable effort to arrange their personal and business affairs to avoid a conflict of interest with the licensee;
  - ix. Not take business opportunities of the licensee for themselves; and
  - x. Not compete in business with the licensee or serve the licensee's interest in any transaction with a company in which they have a personal interest.
- (b) Examples of where conflict of interest may arise when serving as an approved person and measures to mitigate them;
- (c) A rigorous review and approval process for approved persons 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;
- (d) Adequate requirements that transactions with related parties must be made on an arm's length basis;
- (e) Sufficient restrictions on and/or a robust and transparent process for the employment of relatives of approved persons;
- (f) Requirements for properly managing and disclosing conflict of interest that cannot be prevented;
- (g) Requirements for all approved persons to annually declare in writing all 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 a designated Board committee; and
- (h) The way in which the Board will deal with any non-compliance with the policy.

### HC-1.2.5

The CEO/General Manager of the licensee must disclose to the Board of directors on an annual basis those individuals who are occupying controlled functions and who are relatives of any other approved person within the licensee.



MODULE	HC: High-Level Controls
CHAPTER	HC-1: Board's Overall Responsibilities

### HC-1.3 Oversight of Senior Management

#### HC-1.3.1

The Board must exercise proper oversight of senior management against formal performance and remuneration standards consistent with the long-term strategic objectives and the financial soundness of the licensee. In doing so, the Board must:

- (a) Meet regularly with senior management;
- (b) Subject senior management to annual performance assessment and document such assessments;
- (c) Ensure that approved persons' collective knowledge and expertise remain appropriate given the licensee's nature of business and risk profile;
- (d) Ensure that senior management's actions are in full compliance with applicable laws and regulations and consistent with the strategy, business plan and policies approved by the Board, including risk appetite;
- (e) Question, challenge and critically review the explanations and information provided by senior management; and
- (f) Ensure that appropriate succession plans are in place for all approved persons within senior management (provided that such plans are subject to review in case of any changes to approved persons within senior management).



MODULE	HC: High-Level Controls
CHAPTER	HC-2: Board Formation

## HC-2.1 Board Composition

### HC-2.1.1

The Board must comprise of individuals with a balance of skills, diversity and expertise, who individually and collectively possess the necessary qualifications commensurate with the size, complexity and risk profile of the licensee. The Board must have a sufficient number of independent directors. Money changer licensees and trust service providers must have at least one independent director.

### HC-2.1.2

If the Bahraini licensee has a controller or a group of controllers acting in concert, such person(s) must recognise their specific responsibility to the minority shareholders as Board members have responsibilities to the licensee's overall interests, regardless of who appoints them.

### HC-2.1.3

The CBB may call the independent director at its discretion to have a general discussion on the affairs of the Bahraini licensee.



MODULE	HC: High-Level Controls
CHAPTER	HC-2: Board Formation

## HC-2.2 Board Member Selection

**HC-2.2.1** The Board must have a clear and rigorous process for identifying, assessing and selecting Board candidates. The Board, and not management, must nominate the candidates for shareholders' approval.

**HC-2.2.2** Board candidates must:

- (a) Possess the knowledge, skills, experience and, particularly in the case of non-executive directors, independence of mind necessary to discharge their responsibilities on the Board in light of the licensee's business and risk profile;
- (b) Have a record of integrity and good repute;
- (c) Have sufficient time to fully carry out their responsibilities;
- (d) Not have any conflicts of interest that may impede their ability to perform their duties independently and objectively and subject them to undue influence from:
  - i. Other approved persons, controllers or other connected parties;
  - ii. Past or present positions held; or
  - iii. Personal, professional or other economic relationships with other approved persons (or with other entities within the group); and
- (e) Not have another directorship in a competing financial institution inside Bahrain.

**HC-2.2.3** Nominated directors of a Bahraini licensee must possess the requisite experience and competencies specified in Module TC (Training and Competency), where applicable.

**HC-2.2.4** Each proposal by the Board to the shareholders for election or re-election of a director must be accompanied by a recommendation from the Board and the following specific information:

- (a) The term to be served, which may not exceed three years;
- (b) Biographical details and professional qualifications;
- (c) In the case of an independent director, a statement that the Board has determined that the applicable rules and criteria for 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 (if any) between:
  - i. the candidate and the licensee, and
  - ii. the candidate and other approved persons of the licensee.



MODULE	HC:	High-Level Controls
CHAPTER	HC-2:	Board Formation

## HC-2.2 Board Member Selection (continued)

### HC-2.2.5

Newly appointed directors must be made aware of their duties before their nomination, particularly as to the time commitment required.





MODULE	HC: High-Level Controls
CHAPTER	HC-2: Board Formation

## HC-2.3 Board Members' Appointment and Induction

### *Board Members' Appointment*

**HC-2.3.1** The chairperson of the Board must 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 they continue to demonstrate commitment to the role.

**HC-2.3.2** Where an independent director has served three consecutive terms on the Board, such director will lose his independence status and must not be classified as an independent director if reappointed.

**HC-2.3.3** Bahraini licensees must have a written appointment agreement with each director which recites the directors' powers, duties and responsibilities, accountability, term, the time commitment envisaged, the committee assignment (if any), remuneration, expense reimbursement entitlement and their access to independent legal or other professional advice at the expense of the licensee when needed to discharge their responsibilities as directors.

### *Board Members' Induction*

**HC-2.3.4** The Board must ensure that:

- (a) Sufficient time, budget and other resources are allocated annually for the Board members' induction programmes;
- (b) Each new director receives a formal and tailored induction and has access to ongoing training on relevant issues which may involve internal or external resources to ensure their effective contribution to the Board from the beginning of their term; and
- (c) The induction programmes include meetings with senior management, visits to the licensee's facilities, presentations regarding strategic plans, significant financial, accounting and risk management issues, compliance programs, and meetings with internal and external auditors and legal counsel.

**HC-2.3.5** Board members must understand their oversight and corporate governance role and be able to exercise sound, objective judgment about the affairs of the licensee.

**HC-2.3.6** All continuing directors must be invited to attend orientation meetings and all directors must continually educate themselves as to the licensee's business and corporate governance.



MODULE	HC: High-Level Controls
CHAPTER	HC-3: Board's Structure and Practices

## HC-3.1 Organisation and Assessment of the Board

### HC-3.1.1

The Board of a Bahraini licensees must:

- (a) Adopt a formal Board charter specifying matters which are reserved for it, which must include, but are not limited to, the specific requirements and responsibilities of directors stipulated in this Module and the Commercial Companies Law;
- (b) Structure itself in terms of leadership, size and the use of committees so as to effectively carry out its oversight role and other responsibilities. This includes ensuring that the Board has the time and means to cover all necessary subjects in sufficient depth and have a robust discussion of key issues;
- (c) Maintain and periodically update its governance structure, organisational rules, by-laws and other similar documents setting out its organisation, rights, responsibilities and key activities; and
- (d) Carry out annual evaluation and assessments – alone or with the assistance of external experts – of the Board, its committees and individual Board members. This must include:
  - i. Assessing how the Board operates in terms of the requirements of the CBB Rulebook and the Commercial Companies Law;
  - ii. Evaluating the performance of each committee considering its specific purposes and responsibilities, which shall include review of the self-evaluations undertaken by each committee;
  - iii. Reviewing each director's work, their attendance at Board and committee meetings, and their independence and constructive involvement in discussions and decision making;
  - iv. Reviewing the Board's current structure, size, composition as well as committees' structures and composition in order to maintain an appropriate balance of skills, diversity and experience and for the purpose of planned and progressive refreshing of the Board; and
  - v. Recommendations for new directors to replace long-standing members or those members whose contribution to the Board or its committees is not adequate.



<b>MODULE</b>	<b>HC: High-Level Controls</b>
<b>CHAPTER</b>	<b>HC-3: Board's Structure and Practices</b>

### **HC-3.1 Organisation and Assessment of the Board (continued)**

**HC-3.1.2** Where the Board has serious reservations about the performance or integrity of a Board member, or he ceases to be qualified, the Board must take appropriate action and inform the CBB accordingly.

**HC-3.1.3** The Board must report to the shareholders, at each annual shareholder meeting, that evaluations have been done and report its findings.

**HC-3.1.4** Executive directors must provide the Board with all relevant business and financial information within their knowledge and must recognise that their role as a director is different from their role as a member of management.

**HC-3.1.5** Non-executive directors must be fully independent of management and must constructively scrutinise and challenge management and executive directors.

**HC-3.1.6** The Board must maintain appropriate records of meeting minutes, including key points of discussions held, recommendations made, decisions taken and dissenting opinions (if any).

**HC-3.1.7** The Board must meet at least four times a year to enable it to discharge its responsibilities effectively, and half of all Board meetings in any financial year must be held in the Kingdom of Bahrain.

**HC-3.1.8** Individual Board members must attend at least 75% of all Board meetings in a given financial year, whether in-person or virtually (if needed) so as to enable the Board to discharge its responsibilities effectively (see table below). Voting and attendance proxies for Board meetings are prohibited.

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



MODULE	HC: High-Level Controls
CHAPTER	HC-3: Board's Structure and Practices

### HC-3.1 Organisation and Assessment of the Board (continued)

**HC-3.1.9** The absence of Board members at Board and committee meetings must be noted in the relevant 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 xx% of scheduled meetings this year).

**HC-3.1.10** If a Board member has not attended at least 75% of Board meetings in any given financial year, the licensee must notify the CBB, within one month from its financial year-end, indicating which member has failed to satisfy this requirement, their level of attendance and the reason for non-attendance. The CBB shall then consider the matter and determine whether enforcement action pursuant to Article 65 of the CBB Law is appropriate.

HC-3.1.11 Board governance framework should require members to step down if they are not actively participating in Board meetings.

HC-3.1.12 Non-executive directors should have free access to the Bahraini licensee's management beyond that provided in Board meetings. Such access should be through the chairperson of the Audit Committee or the CEO. The Board should make this policy known to management to alleviate any management concerns about a director's authority in this regard.



MODULE	HC: High-Level Controls
CHAPTER	HC-3: Board's Structure and Practices

## HC-3.2 Board Chairperson

### HC-3.2.1

The Chairperson of the Board of the Bahraini licensees must:

- (a) Not be an executive director;
- (b) Not be the same person as the CEO. This applies also to the deputy chairperson;
- (c) Commit sufficient time to perform their role effectively;
- (d) Play a critical role in promoting mutual trust, efficient functioning of the Board, open discussion, constructive dissent from decisions and constructive support for decisions after they have been made;
- (e) Ensure that all directors receive an agenda, minutes of prior meetings and adequate background information on each agenda item in writing well before each Board meeting;
- (f) Encourage and promote critical and objective discussion and ensure that dissenting views can be freely expressed, discussed and recorded in the minutes of the Board meeting; and
- (g) Ensure that Board decisions are taken on sound and well-informed basis.



MODULE	HC: High-Level Controls
CHAPTER	HC-3: Board's Structure and Practices

### HC-3.3 Board Committees

**HC-3.3.1** The Board of the Bahraini licensee (excluding money changer licensees and trust service providers) must establish at a minimum an Audit Committee. However, financing company licensees must establish Audit, Risk, Remuneration and Nomination Committees described elsewhere in this Module.

**HC-3.3.2** Committees may be combined provided that no conflict of interest arises between the duties of such committees, and subject to the CBB's prior approval.

**HC-3.3.3** Every committee must have a formal written charter or other instrument which sets out its roles and responsibilities, how the committee will report to the Board, what is expected of committee members and any tenure limits for serving on the committee.

**HC-3.3.4** Each Board committee must maintain appropriate records of their deliberations and decisions in their meeting minutes, including key points of discussions held, recommendations made, decisions taken (and update on their subsequent implementation) and dissenting opinions (if any).

**HC-3.3.5** Members of each committee must exercise judgment free from any personal conflicts of interest or bias.



MODULE	HC: High-Level Controls
CHAPTER	HC-3: Board's Structure and Practices

## HC-3.4 Audit Committee

**HC-3.4.1** The audit committee of the Bahraini financing company licensee must have at least three directors of which the majority must be independent and have no conflict of interest with any other duties they have.

**HC-3.4.2** The Chairperson of the audit committee must:

- (a) Be independent; and
- (b) Not be the chairperson of any other Board committee.

**HC-3.4.3** The CEO and other senior management of the Bahraini licensee must not be members of the audit committee.

**HC-3.4.4** The audit committee members must have sufficient experience in audit practices, financial reporting and accounting.

**HC-3.4.5** The audit committee must meet:

- (a) At least four times a year.
- (b) At least twice a year with the external auditor.
- (c) At least once a year in the absence of the CEO and any executive management, but in presence of the Head of Compliance, Internal Auditor and CRO.

**HC-3.4.6** The audit committee must, at minimum:

- (a) Ensure that the licensee has effective and adequate policies covering all its business activities, internal audit, financial reporting, compliance, risk management, prevention of frauds and cyber security breaches, etc.;
- (b) Oversee the financial reporting process;
- (c) Oversee and interact with the licensee's internal and external auditors;
- (d) Review the integrity of the licensee's financial statements;
- (e) Recommend to the Board, based on a Board approved objective criteria, the appointment, remuneration, dismissal and rotation of external auditors;
- (f) Receive internal and external audit and compliance reports and ensure that senior management is taking necessary corrective actions in a timely manner to address any control weaknesses, non-compliance with policies, laws and regulations, and other problems identified by auditors, the head of compliance and other control functions;



<b>MODULE</b>	<b>HC: High-Level Controls</b>
<b>CHAPTER</b>	<b>HC-3: Board's Structure and Practices</b>

#### **HC-3.4 Audit Committee (continued)**

- (g) Assess once a year the extent to which the licensee is managing its compliance risk effectively;
- (h) Ensure that the agenda for their meetings includes compliance and internal audit issues at least every quarter;
- (i) Recommend the appointment and dismissal of the heads of internal audit and compliance functions. The licensee must also discuss the reasons for their dismissal with the CBB.
- (j) Make a determination, at least once a year, of the external auditor's independence;
- (k) Review and supervise the implementation and enforcement of the licensee's code of conduct, unless such mandate is delegated to another committee such as the Governance Committee; and
- (l) Ensure that senior management establishes and maintains an adequate and effective internal control systems, procedures and processes for the business of the licensee.

HC-3.4.7 In case the licensee has a different board committee overseeing and monitoring compliance issues, then all of the above compliance-related requirements in Paragraph HC-3.4.6 can be handled by such committee instead.





MODULE	HC: High-Level Controls
CHAPTER	HC-3: Board's Structure and Practices

## HC-3.5 Risk Committee

**HC-3.5.1** This Section is applicable to financing company licensees only.

**HC-3.5.2** The risk committee of the Bahraini licensees must have at least three directors of which the majority must be independent. In addition, the committee members must have experience in risk management issues and practices and have no conflict of interest with any other duties they may have.

**HC-3.5.3** The chairperson of the risk committee must:

- (a) Be independent;
- (b) Not be the chairperson of the Board, unless he is considered independent; and
- (c) Not be the chairperson of any other Board committee.

**HC-3.5.4** The CEO and other senior management must not be members of the risk committee.

**HC-3.5.5** The licensee must have a strong and appropriate risk governance framework which:

- (a) Includes a strong risk culture, and a well-developed risk appetite articulated through the risk appetite statement (RAS);
- (b) Outlines actions to be taken when the stated risk limits are breached, including disciplinary actions for excessive risk-taking, escalation procedures and notification to the Board; and
- (c) Includes well-defined organisational responsibilities for risk management.

**HC-3.5.6** The Bahraini licensee's RAS must:

- (a) Include both quantitative and qualitative considerations;
- (b) Establish the individual and aggregate level and types of risks that the licensee is willing to assume;
- (c) Define the boundaries and business considerations according to which the licensee is expected to operate;
- (d) Be aligned with the licensee's strategic, capital and financial plans and compensation practices; and
- (e) Be communicated effectively throughout the licensee, linking it to daily operational decision-making and establishing the means to raise risk issues and strategic concerns across the licensee on a timely and proactive basis.



MODULE	HC: High-Level Controls
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## HC-3.5 Risk Committee (continued)

### HC-3.5.7

Licensees must avoid organisational silos that can impede effective sharing of risk information across the organisation and can result in decisions being taken in isolation from the rest of the organisation. Accordingly, the Board, senior management and control functions must re-evaluate established practices in order to encourage greater communication.

### HC-3.5.8

The risk committee must, at minimum:

- (a) Recommend the appointment or removal of the Chief Risk Officer (CRO) or equivalent. The licensee must also discuss the reasons for removal with the CBB;
- (b) Discuss all risk strategies on both an aggregated basis and by type of risk and make recommendations to the Board, and on the risk appetite;
- (c) Ensure that:
  - i. Risks are identified, measured, aggregated, controlled, mitigated, monitored and reported on an ongoing basis across all business lines, the licensee as a whole, its subsidiaries and overseas branches (if any);
  - ii. Risk identification and measurement include both quantitative and qualitative elements;
  - iii. Each key risk has a policy, process and controls;
  - iv. The licensee has sufficient and robust management information system and policies, supported by appropriate control procedures and processes, designed to ensure that the licensee's risk identification, measurement, aggregation, controlling, mitigation, monitoring and reporting capabilities are commensurate with the licensee's size, complexity and risk profile. The sophistication of the licensee's risk management information system and internal control infrastructure must keep pace with changes to the licensee's risk profile, the external risk landscape and industry practices;



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### HC-3.5 Risk Committee (continued)

- v. Senior management has in place processes to promote the licensee's adherence to the approved risk policies and risk appetite;
  - i. The licensee's policies must determine the key management decisions that must be taken by more than one person;
  - ii. The licensee has an adequate communication within the licensee about risk, both across the organisation and through reporting to the Board and senior management;
  - iii. The licensee has a strong risk culture that promotes risk awareness and encourages open communication and challenge about risk-taking across the organisation as well as vertically to and from the Board and senior management; and
  - iv. The licensee has adequate escalation procedures on risks related matters.
- (d) Advise the Board on the licensee's risk appetite, overseeing senior management's implementation of the RAS, reporting on the state of risk culture in the licensee, and interacting with and overseeing the CRO;
- (e) Oversee the strategies for capital and liquidity management as well as for all relevant risks of the licensee, such as credit, market, operational, interest rate risk and reputational risks, to ensure that they are consistent with the stated risk appetite;
- (f) Commission every five years a quality review of the effectiveness and efficiency of the risk management framework and function by a third-party consultant, other than the external auditor. The results of such independent review must be provided to the CBB by 31<sup>st</sup> May of the relevant year; and
- (g) Receive regular reporting and communication from the CRO and other relevant functions about the licensee's current risk profile, current state of the risk culture, utilisation against the established risk appetite and limits, limit breaches and mitigation plans.

#### HC-3.5.9

There must be effective communication and coordination between the audit committee and the risk committee to facilitate the exchange of information and effective coverage of all risks, including emerging risks, and any needed adjustments to the risk governance framework of the licensee.



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CHAPTER	HC-3: Board's Structure and Practices

## HC-3.6 Remuneration Committee

**HC-3.6.1** This Section is applicable to financing company licensees only.

**HC-3.6.2** The remuneration committee of the Bahraini licensee must have at least three directors.

**HC-3.6.3** Members of the remuneration committee must be independent of any risk-taking function or committee.

HC-3.6.4 The remuneration committee should include only independent directors or, alternatively, only non-executive directors of whom a majority are independent directors and the chairperson should be an independent director.

HC-3.6.5 The remuneration committee should meet at least twice a year.

**HC-3.6.6** The remuneration committee must, at minimum:

- (a) Recommend to the Board:
  - i. An appropriate remuneration policy designed to reduce employees' incentives to take excessive and undue risk, which must be approved by the shareholders; and
  - ii. A fair and internally transparent remuneration system, which includes relevant performance measures and effective controls;
- (b) Ensure on an annual basis that the remuneration policy and its implementation:
  - i. Are in full compliance with CBB requirements;
  - ii. Are consistent with the licensee's strategy, culture, long-term business objectives, risk appetite, performance and control environment; and
  - iii. Are creating the desired incentives for managing risk, capital and liquidity.
- (c) Work closely with the risk committee in evaluating the incentives created by the remuneration system. The risk committee must, without prejudice to the tasks of the remuneration committee, examine whether incentives provided by the remuneration system take into consideration risk, capital, liquidity and the likelihood and timing of earnings;



MODULE	HC: High-Level Controls
CHAPTER	HC-3: Board's Structure and Practices

### HC-3.6 Remuneration Committee (continued)

- (d) Approve the remuneration package and amounts for each approved person and material risk-taker, as well as the total variable remuneration to be distributed based on the results of the performance evaluation system and taking account of total remuneration including salaries, fees, expenses, bonuses and other employee benefits;
- (e) Regularly review remuneration outcomes, risk measurements, and risk outcomes for consistency with Board's approved risk appetite;
- (f) Question payouts for income that cannot be realised or whose likelihood of realisation remains uncertain at the time of payout;
- (g) Recommend Board member remuneration based on their attendance and in compliance with the Commercial Companies Law;
- (h) Evaluate practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain by means of both quantitative and qualitative key indicators. It must demonstrate that its decisions are consistent with the assessment of the licensee's financial condition and future prospects; and
- (i) Obtain feedback on performance evaluation of the Chief Risk Officer, Chief Internal Auditor and Head of Compliance from the designated Board committee responsible for oversight of these functions.



MODULE	HC: High-Level Controls
CHAPTER	HC-3: Board's Structure and Practices

## HC-3.7 Nomination Committee

**HC-3.7.1** This Section is applicable to financing company licensees only.

**HC-3.7.2** The nomination committee of the Bahraini licensee must have at least three independent directors, or alternatively, three non-executive directors of whom the majority must be independent directors including its chairperson.

HC-3.7.3 The committee should meet at least twice a year.

**HC-3.7.4** The nomination committee must, at minimum:

- (a) Assess and recommend to the Board from time to time the changes that the committee considers desirable to the size of the Board, any Board committee or management structure;
- (b) Regularly review the time commitment required from each non-executive director and require them to inform the committee before accepting any Board appointments to another company;
- (c) Recommend to the Board persons qualified to become members of the Board of directors or CEO and his deputies, chief financial officer, chief operating officer, chief investment officer, corporate secretary and any equivalent or other senior management positions that the Board determines are subject to its approval. The exceptions are the appointments of the chief internal auditor, chief risk officer and head of compliance who must be recommended by other committees as prescribed in this module;
- (d) Assess the role and responsibilities of a Board member, the knowledge, experience and competence which the role requires;
- (e) Assess the Board's and senior management's effectiveness;
- (f) Recommend to the Board appropriate succession plans of approved persons within senior management;
- (g) Recommend to the Board, and oversee the implementation of, appropriate personnel or human resource policies; and
- (h) Recommend to the Board the prescribed title, authority, duties, accountability and internal reporting responsibilities for each approved person within senior management.



MODULE	HC: High-Level Controls
CHAPTER	HC-4: Shareholders' Meetings

## HC-4.1 Shareholders' Meetings

### HC-4.1.1

Bahraini licensees must comply with the following with respect to any shareholders' meeting:

- (a) Provide the draft agenda to the CBB, for its review and comment, at least 5 working days prior to communicating with the shareholders or publishing in the press;
- (b) Ensure that CBB's prior approval has been obtained for any agenda items which require CBB's approval under relevant regulations, prior to the meeting taking place;
- (c) Invite a representative of the CBB to attend the meetings at least 5 working days prior to the meeting taking place; and
- (d) Submit to the CBB a copy of the minutes of the meeting within 15 calendar days of the meeting.



MODULE	HC: High-Level Controls
CHAPTER	HC-5: Remuneration of Approved Persons

## HC-5.1 Remuneration of Approved Persons

**HC-5.1.1** Bahraini licensees must have in place a Board approved remuneration policy. Licensees must ensure that all approved persons are remunerated fairly and responsibly. More specifically, the remuneration must be sufficient to attract, retain and motivate persons.

**HC-5.1.2** The performance evaluation and remuneration of senior management and staff of the licensee must be based, among other factors, on their adherence to all relevant laws, regulations and CBB rulebook requirements, including but not limited to AML/CFT requirements in the FC module.

**HC-5.1.3** 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.





<b>MODULE</b>	<b>HC: High-Level Controls</b>
<b>CHAPTER</b>	<b>HC-6: Senior Management</b>

## **HC-6.1 Senior Management**

**HC-6.1.1** The Board must establish an adequate organisational structure that promotes accountability and transparency and facilitates effective decision-making and good governance throughout the licensee. This includes clarity on the role, authority and responsibility of the various positions within senior management, including that of the CEO.

**HC-6.1.2** Senior management must:

- (a) Be selected through an appropriate promotion or recruitment process which considers the qualifications and competencies required for the position in question;
- (b) Have the necessary experience, competencies, personal qualities and integrity to manage the businesses and employees under their supervision;
- (c) Be subject to regular training to maintain and enhance their competencies and stay up to date on developments relevant to their areas of responsibility;
- (d) Assess the training needs of staff across all levels throughout the organisation taking into account the existing skills and competencies and laws and regulations and ensure that such training is provided by competent and skilled personnel (whether internal or external);
- (e) Act within the scope of their responsibilities which must be clearly defined;
- (f) Independently assess and question the policies, processes and procedures of the licensee, with the intent to identify and initiate management action on issues requiring improvement;
- (g) Not interfere in the independent duties of the risk management, compliance and internal audit functions;
- (h) Carry out and manage the licensee's activities in compliance with all laws and regulations, and in a manner consistent with the business strategy, risk appetite, business plans and remuneration and other policies approved by the Board;
- (i) Have a robust governance framework for all management committees;
- (j) Not primarily control the remuneration system in the licensee;
- (k) Actively communicate and consult with the control functions on management's major plans and activities so that the control functions can effectively discharge their responsibilities; and



MODULE	HC: High-Level Controls
CHAPTER	HC-6: Senior Management

## HC-6.1 Senior Management (continued)

- (l) Provide the Board and its committees with timely, complete, accurate and understandable information and documents so that they are equipped for upholding their responsibilities, and keep them adequately informed and updated on a timely basis about material issues including:
- Changes in the implementation of business strategy, risk strategy and risk appetite;
  - The licensee's performance and financial condition;
  - Breaches of risk limits or regulations;
  - Internal control failures, frauds and cyber-security incidents;
  - Legal or regulatory concerns;
  - Customer complaints; and
  - Issues raised as a result of the licensee's whistleblowing policy.

### HC-6.1.3

Licensee's CEO and chief financial officer must state in writing to the audit committee and the Board that the licensee's interim and annual financial statements present a true and fair view, in all material respects, of the licensee's financial condition and results of operations in accordance with applicable accounting standards.



MODULE	HC: High-Level Controls
CHAPTER	HC-7: Risk Management Function

## HC-7.1 Risk Management Function

**HC-7.1.1** This Section is applicable to financing company licensees only. For trust service providers and money changer licensees, only Paragraphs HC-7.1.2 and HC-7.1.3 (b) apply.

**HC-7.1.2** Licensees must have an effective and independent risk management function commensurate with the licensee's size, complexity and risk profile, under the direction of a chief risk officer (CRO) or equivalent, with sufficient stature, independence and skilled resources.

**HC-7.1.3** The risk management function must:

- (a) Be sufficiently independent of the business units, thus ensuring that it is not involved in revenue generation;
- (b) Be responsible for overseeing risk-taking activities across the licensee and must have authority within the organisation to do so;
- (c) Have procedures in place to identify and assess the possible increased reputational risk to the licensee if it offers products or carries out activities outside Bahrain;
- (d) Have access to all business lines that have the potential to generate risk to the licensee as well as to relevant risk-bearing subsidiaries, associated companies and overseas branches;
- (e) Challenge business units effectively regarding all aspects of risk arising from the licensee's activities; and
- (f) Have a sufficient number of employees who possess the requisite experience and qualifications, including market and product knowledge as well as command of risk disciplines, and are subject to regular training.

**HC-7.1.4** Key activities of the risk management function must include:

- (a) Implementing an enterprise-wide risk governance framework that includes appropriate policies, procedures and limits;
- (b) Identifying material individual, aggregate and emerging risks, including risks arising from potential mergers and acquisitions and hard to quantify risks, such as reputational risk;
- (c) Regularly and on an ad-hoc basis, evaluating the risks faced by the licensee and its overall risk profile. The risk assessment process must include ongoing analysis of existing risks as well as the identification of new or emerging risks. The results of such assessments must be reported to both the Risk Committee and senior management;



MODULE	HC: High-Level Controls
CHAPTER	HC-7: Risk Management Function

## HC-7.1 Risk Management Function (continued)

### HC-7.1.4

- (d) Ongoing monitoring of the risk-taking activities and risk exposures in line with the Board-approved risk policies and appetite;
- (e) Establishing an early warning or trigger system for breaches of the licensee's risk appetite or limits;
- (f) Using risk measurement and modelling techniques in addition to qualitative risk analysis and monitoring;
- (g) Evaluating possible ways to mitigate risk exposures;
- (h) Reporting regularly to the risk committee and senior management on risks, including but not limited to, material exemptions and risk-mitigating actions;
- (i) Regularly comparing actual performance against risk estimates (i.e. Backtesting) to assist in judging the accuracy and effectiveness of the risk management process and making necessary adjustments; and
- (j) Challenging decisions that give rise to material risk.

### HC-7.1.5

Licensees must have adequate risk management and approval processes for new or expanded products or services, lines of business and markets, outsourcing arrangements as well as for large and complex transactions. If such processes are not in place, a new product, service, business line or third-party relationship or major transaction must be delayed. There must 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. The risk management function must provide input on risks as part of such processes and on the outsourcer's ability to manage risks and comply with legal and regulatory obligations. Such processes must entail the following:

- (a) A full assessment of risks under a variety of scenarios as well as an assessment of potential shortcomings in the ability of the licensee's risk management and internal controls to effectively manage associated risks; and
- (b) An assessment of the extent to which the licensee's risk management, legal and regulatory compliance, information technology, internal control and business functions have adequate tools and the expertise necessary to measure and manage related risks.

### HC-7.1.6

Licensees must appoint a chief risk officer (CRO) or equivalent with an overall responsibility for the licensee's risk management function.



MODULE	HC: High-Level Controls
CHAPTER	HC-7: Risk Management Function

## HC-7.1 Risk Management Function (continued)

### HC-7.1.7

The CRO must:

- (a) Be actively engaged, together with management, in monitoring performance relative to risk-taking and risk limit adherence;
- (b) Manage and participate in key decision-making processes (e.g. Strategic planning, capital and liquidity planning, new products and services, compensation design and operation);
- (c) Be independent and have duties distinct from other executive function. This means that he must not have managerial or financial responsibility or approval authority related to any business lines or revenue-generating functions, and there must be no “dual hatting”, i.e. other approved persons within senior management must not serve as the CRO.
- (d) Have access to any information necessary to perform his duties;
- (e) Report directly to the risk committee without impediment, and administratively to the CEO;
- (f) Have the ability to interpret and articulate risk in a clear and understandable manner and to effectively engage the risk committee and senior management in a constructive dialogue on key risk issues;
- (g) Meet regularly with the non-executive directors, the board or its risk committee without executive directors and the CEO being present;
- (h) Keep the risk committee and senior management apprised of the assumptions used in and potential shortcomings of the licensee’s risk models and analyses;
- (i) Consistently remind all staff, through a regular process, under the sponsorship of the CEO, of the risk management requirements to ensure a common understanding of these requirements across the licensee; and
- (j) Ensure that:
  - i. Risk reporting to the risk committee is carefully designed to convey entity-wide, individual portfolio and other risks 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 licensee’s current and prospective exposures (particularly under stressed scenarios), risk/return relationships and risk appetite and limits. Reporting must also include information about the external environment to identify market conditions and trends that may have an impact on the licensee’s current or future risk profile;



MODULE	HC: High-Level Controls
CHAPTER	HC-7: Risk Management Function

## HC-7.1 Risk Management Function (continued)

### HC-7.1.7

- ii. Material risk-related ad-hoc information that requires immediate decisions or reactions is promptly presented to senior management and, as appropriate, the risk committee, the responsible officers and, where applicable, the heads of control functions so that suitable measures and activities can be initiated at an early stage; and
- iii. The licensee has accurate internal and external data to be able to identify, assess and mitigate risks.



MODULE	HC: High-Level Controls
CHAPTER	HC-8: Compliance

## HC-8.1 Compliance

### HC-8.1.1

The Board must:

- (a) Oversee the management of the licensee's compliance risk;
- (b) Establish an independent compliance function and approve an appropriate compliance framework for the licensee based on its size and complexity of its operations;
- (c) Set priorities for the management of its compliance risk in a way that is consistent with its risk management strategy and structures;
- (d) Not outsource the compliance function; and
- (e) Approve the licensee's compliance policy for identifying, assessing, monitoring, reporting and advising on compliance risk.

### HC-8.1.2

The compliance function and the internal audit function must be separate.

### HC-8.1.3

The Board, Audit Committee or the designated Board committee and senior management must:

- (a) Ensure that, based on an agreed remedial action plan, all compliance findings are resolved within a reasonable period of time to be set based on level and magnitude of risk;
- (b) Not restrict the compliance function from reporting any irregularities or breaches that are identified as a result of its work or investigations, and must ensure that such reporting can be done without fear of retaliation or disfavour from management, board members or other staff members;
- (c) Ensure that the head of compliance and his staff are not placed in a position where there is a possible conflict of interest between their compliance responsibilities and any other responsibilities they may have;
- (d) Not consider the compliance function as a cost center; instead it should be viewed as an activity that helps the licensee avoid enforcement action for non-compliance, enhances the licensee's reputation and promotes the right environment for better financial performance; and
- (e) Ensure the compliance function's right to:
  - i. Have unrestricted access to any records or files necessary to carry out its responsibilities, and the corresponding duty of licensee staff to co-operate in supplying this information;
  - ii. Conduct investigations of possible breaches of the applicable laws, regulations and the compliance policy; and





MODULE	HC: High-Level Controls
CHAPTER	HC-8: Compliance

## HC-8.1 Compliance (continued)

- iii. Appoint, subject to audit committee's or the board's, as applicable, approval, outside experts to perform a specific task, if appropriate.

### HC-8.1.4

Licensees must appoint a head of compliance with overall responsibility for the licensee's compliance function.

### HC-8.1.5

Subject to the CBB's approval, the role of head of compliance may be combined with the head of risk if the size and nature of the licensee justify the same.

### HC-8.1.6

The head of compliance must:

- (a) Report to the Audit Committee or the board, as applicable, or the designated Board committee and administratively to the CEO. In the case of overseas licensees, the reporting must be to the Group or Regional Head of Compliance and administratively to the CEO/GM of the branch;
- (b) Establish the operating compliance procedures and processes for identifying, assessing, monitoring, reporting and advising on compliance risk;
- (c) Establish written guidance to the licensee's staff on the appropriate implementation of laws and regulations;
- (d) Conduct, under the sponsorship of the CEO, awareness sessions for the licensee's staff on compliance policy requirements and issues; and
- (e) Report to the Audit Committee:
  - i. On a quarterly basis, the licensee's management of its compliance risk, in such a manner as to assist committee members to make an informed judgment on whether the licensee is managing its compliance risk effectively; and
  - ii. Immediately any material compliance failures as they arise (e.g. failures that may attract a significant risk of legal or regulatory sanctions, material financial loss, or loss of reputation).

### HC-8.1.7

The compliance function must:

- (a) Have a formal status with sufficient authority within the licensee;
- (b) Carry out its responsibilities under a risk-based compliance programme that sets out its planned activities, such as the implementation and review of specific policies and procedures, compliance risk assessment and compliance testing;





MODULE	HC: High-Level Controls
CHAPTER	HC-8: Compliance

## HC-8.1 Compliance (continued)

### HC-8.1.7

- (c) Assess in cooperation with the relevant functions, in case of new regulations, the appropriateness of the licensee's relevant policies as well as the compliance policy and related procedures and processes. It must promptly follow up regarding any identified deficiencies, and, where necessary, formulate proposals for amendments in cooperation with the relevant functions;
- (d) On a proactive basis, identify, measure, document and assess the compliance risks associated with the licensee's business activities including the development of new products and business practices, proposed establishment of new types of business or customer relationships, or material changes in the nature of such relationships. If the licensee has a new products and services committee, the compliance function staff must be represented on the committee;
- (e) Monitor and test compliance by performing sufficient and representative compliance testing. The results of such testing must be reported to the Audit Committee ;
- (f) Advise the audit committee and senior management on all relevant laws, regulations and standards in all jurisdictions in which the licensee conducts its business and inform them on developments on the subject;
- (g) Must provide to the CBB a compliance assessment report on every application/request for approval to the CBB confirming that all related legal and regulatory requirements pertaining to the request have been thoroughly checked, including the impact of such request on the licensee's financial position and compliance status, and a reference must be made to any previously approved arrangements by the CBB. In cases where the requests have a potential financial impact on the licensee, a report from the financial control function in consultation with external auditors must also be submitted as part of the compliance assessment report, whereas in case of any legal implication of such a request a legal opinion on the matter must be submitted;
- (h) Act as a contact point within the licensee for compliance queries from staff members; and
- (i) Have sufficient and appropriate resources to carry out its functions effectively, commensurate with the size and complexity of the licensee.



MODULE	HC: High-Level Controls
CHAPTER	HC-8: Compliance

## HC-8.1 Compliance (continued)

### HC-8.1.8

The compliance function staff must:

- (a) Have the necessary qualifications, experience and professional and personal qualities to enable them to carry out their specific duties;
- (b) Have a sound understanding of applicable laws, regulations and standards and their practical impact on the licensee's business activities and operations; and
- (c) Be subject to regular and systematic training to remain up-to-date with developments in laws, regulations and standards.

### HC-8.1.9

The CBB may at its own discretion communicate directly with the Head of Compliance to discuss issues of material concerns related to compliance risk.



MODULE	HC: High-Level Controls
CHAPTER	HC-9: Internal Audit

## HC-9.1 Internal Audit

**HC-9.1.1** Licensees must establish an effective and independent internal audit function (IAF).

**HC-9.1.2** The Audit Committee or the board, as applicable, remains ultimately responsible for the IAF regardless of whether internal audit activities are outsourced.

**HC-9.1.3** The Board, Audit Committee and senior management must:

- (a) Promote a strong and robust internal control environment within the licensee;
- (b) Provide the IAF staff full and unconditional access to all files, records, data, documents, systems, properties, subsidiaries and overseas branches of the licensee;
- (c) Require that all internal audit findings and recommendations are resolved within a reasonable period of time to be set based on level and magnitude of risk;
- (d) Allocate sufficient annual budget to support the IAF's activities and plans; and
- (e) Inform the IAF of new developments, initiatives, projects, products and operational changes.

**HC-9.1.4** All Bahraini licensees must have an internal audit charter which must be drawn up and reviewed annually by the head of internal audit and approved by the Board or Audit Committee. It must be available to all internal stakeholders, and to external stakeholders in case of a listed licensee.

**HC-9.1.5** The internal audit charter must establish, at a minimum:

- (a) The IAF's standing within the licensee, its authority, responsibilities and relations with other control functions in a manner that promotes the effectiveness of the function;
- (b) The purpose and scope of the IAF;
- (c) The obligation of the internal auditors to communicate the results of their engagements and a description of how and to whom this must be done (reporting line);
- (d) The criteria for when and how the IAF may outsource some of its engagements to external experts;
- (e) The terms and conditions according to which the IAF can be called upon to provide consulting or advisory services or to carry out other special tasks without creating a conflict with its core function;
- (f) The responsibility and accountability of the head of internal audit;
- (g) The requirement to comply with the international standard on internal audit issued by The Institute of Internal Auditor; and
- (h) Procedures for the coordination of the IAF with the external auditor.



MODULE	HC: High-Level Controls
CHAPTER	HC-9: Internal Audit

## HC-9.1 Internal Audit (continued)

### HC-9.1.6

The IAF must:

- (a) Be independent of all functions;
- (b) Have sufficient standing and authority within the licensee;
- (c) Have sufficient skilled resources to be able to judge outcomes and make an impact at the highest level of the organization;
- (d) Be able to perform its assignments on its own initiative in all areas and functions of the licensee based on the audit plan established by the head of the IAF and approved by the audit committee;
- (e) Be free to report its findings and assessments internally;
- (f) Independently review and evaluate the effectiveness and efficiency of all functions, internal controls, risk management, internal risk and finance models, governance framework, policies, procedures, systems and processes, including the licensee's outsourced activities and its subsidiaries (including SPVs) and local and overseas branches, and must ensure adequate coverage of matters of regulatory interest within the audit plan;
- (g) Develop an independent and informed view of the risks faced by the licensee based on its access to all licensee records and data, its enquiries and its professional competence;
- (h) Discuss its views, findings and conclusions directly with the audit committee and, if necessary, with the board of directors at their routine quarterly meetings; and
- (i) Not be involved in designing, selecting, implementing or operating specific internal control measures. However, the independence of the IAF must not prevent senior management from requesting input from the IAF on matters related to risk and internal controls. Nevertheless, the development and implementation of internal controls must remain the responsibility of management.

### HC-9.1.7

Licensees must appoint a head of internal audit who shall:

- (a) Report directly to the Audit Committee or the board, as applicable, and administratively to the CEO;
- (b) Demonstrate appropriate leadership and have the necessary personal characteristics and professional skills to fulfil his responsibility for maintaining the function's independence and objectivity;
- (c) Inform senior management of all significant findings so that timely corrective actions can be taken, and subsequently, he must follow up with senior management on the outcome of those corrective measures;



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## HC-9.1 Internal Audit (continued)

- (a) Report quarterly to the Audit Committee or the board, as applicable, the status of pending findings;
- (b) Arrange appropriate ongoing training for the internal audit staff to meet the growing technical complexity of the licensee's activities and the increasing diversity of tasks that need to be undertaken as a result of the introduction of new products and processes and other developments in the financial sector;
- (c) Establish an annual internal audit plan approved by the audit committee or the board, as applicable. The plan must be based on a robust risk assessment, including direct or indirect input from the board, audit committee and senior management; and
- (d) Develop and maintain appropriate tools to assess the quality of the IAF.

HC-9.1.8 The CBB may at its own discretion communicate directly with the head of the IAF to discuss issues of material concerns related to risks, compliance and internal controls.

HC-9.1.9 For purposes of Paragraph HC-9.1.7, licensees may outsource the IAF.

**HC-9.1.10** Internal audit reports must be provided to the audit committee or the board, as applicable, without management filtering.

**HC-9.1.11** All internal audit staff must:

- (a) Apply the care and skills expected of a reasonably prudent and competent professional. Due professional care does not imply infallibility. Internal auditors having limited competence and experience in a particular area must be appropriately supervised by more experienced staff;
- (b) Avoid conflicts of interest. Internal auditors appointed from within the licensee must not engage in auditing activities for which they have had previous responsibility before a one year “cooling off” period has elapsed;
- (c) Act with integrity (being straightforward, honest and truthful);
- (d) Be diligent in the protection of information acquired in the course of their duties and must not use it for personal gain or malicious action;
- (e) Adhere to the code of ethics of the licensee, the institute of internal auditors and any other relevant professional or standard setting body;
- (f) Collectively be competent to examine all areas in which the licensee operates; and
- (g) Adhere to international professional standards established by the institute of internal auditors.



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## HC-10.1 Scope of Application

- HC-10.1.1** The contents of this Section, unless otherwise stated, apply to the following licensees:
- (a) Administrators;
  - (b) Third party administrators (TPAs);
  - (c) Credit reference bureau;
  - (d) Card processing licensees;
  - (e) Crowdfunding platform operators;
  - (f) Account information service providers; and
  - (g) Payment initiation service providers.



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## HC-10.2 Board Composition and Selection

### HC-10.2.1

The Board must comprise of individuals with integrity and good repute, a balance of knowledge, skills, diversity and expertise, who individually and collectively possess the necessary qualifications commensurate with the size, complexity and risk profile of the licensee. The Board must have an adequate number of directors taking into consideration the need for independence, board committees, size and complexity of the business. Additionally, the Board must have an adequate number of independent directors, if the licensee holds client money or client assets.

### HC-10.2.2

Board candidates must have independence of mind necessary to discharge their responsibilities on the Board and not have any conflicts of interest that may impede their ability to perform their duties independently and objectively and subject them to undue influence from other approved persons, controllers or other connected parties.

### HC-10.2.3

Licensees must have a written appointment agreement with each director which recites the directors' powers, duties and responsibilities, accountability, term, the time commitment envisaged, the committee assignment (if any), remuneration, expense reimbursement entitlement and their access to independent legal or other professional advice at the expense of the licensee when needed to discharge their responsibilities as directors.





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### HC-10.3 Board Responsibilities

#### HC-10.3.1

The members of the Board must exercise their fiduciary and other duties of care, candor and loyalty to the licensee in accordance with local laws and regulations. Board members must understand their oversight and corporate governance role and be able to exercise sound, objective judgment about the affairs of the licensee.

#### HC-10.3.2

The board of directors ("Board") of the licensee must:

- (a) Approve and oversee the development of the licensee's strategy, business plans and budget, and monitor their implementation. Bahraini licensees must submit to the CBB for its review their proposed strategy and any major proposed changes to it;
- (b) Actively engage in the affairs of the licensee, keep up with material changes in the licensee's business and the external environment and act in a timely manner to protect the long-term interests of the licensee;
- (c) Ensure that:
  - vi. Adequate systems, controls, processes and procedures are implemented by senior management in line with the Board approved policies;
  - vii. The licensee has adequate processes to ensure full compliance with the requirements of the CBB Law, other relevant laws and the pertinent rulebooks;
  - viii. The licensee has a robust finance function responsible for accounting and financial data; and
- (d) Approve annual financial statements.

#### HC-10.3.3

In order to promote a sound corporate culture, the Board must approve an appropriate code of conduct/ ethics that must outline the acceptable practices that all Board members, senior management and other staff must follow in performing their duties, and the unacceptable practices/ conduct that must be avoided.

#### HC-10.3.4

The Board must establish a conflict of interest policy on identifying and managing potential conflicts of interest related to all approved persons.





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### HC-10.3 Board Responsibilities

#### HC-10.3.5

The Board must exercise proper oversight of senior management against formal performance and remuneration standards consistent with the long-term strategic objectives and the financial soundness of the licensee. In doing so, the Board must:

- (a) Meet regularly with senior management;
- (b) Subject approved persons to annual performance assessment and document such assessments; and
- (c) Ensure that appropriate succession plans are in place for all approved persons within senior management (provided that such plans are subject to review in case of any changes to approved persons within senior management).



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## HC-10.4 Board Performance

**HC-10.4.1** The Board must maintain appropriate records of meeting minutes, including key points of discussions held, recommendations made, decisions taken and dissenting opinions (if any).

**HC-10.4.2** The Board must meet at least four times a year to enable it to discharge its responsibilities effectively, and half of all Board meetings in any financial year must be held in the Kingdom of Bahrain.

**HC-10.4.3** Individual Board members must attend at least 75% of all Board meetings in a given financial year, whether in-person or virtually (if needed) so as to enable the Board to discharge its responsibilities effectively. Voting and attendance proxies for Board meetings are prohibited.



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## HC-10.5 Senior Management

### HC-10.5.1

The licensee must establish an adequate organisational structure that promotes accountability and transparency and facilitates effective decision-making and good governance throughout the licensee. This includes clarity on the role, authority and responsibility of the various positions within senior management, including that of the CEO.

### HC-10.5.2

Senior management must:

- (a) Have the necessary experience, competencies, personal qualities and integrity to manage the businesses and employees under their supervision;
- (b) Not interfere in the independent duties of compliance and internal audit;
- (c) Carry out and manage the licensee's activities in compliance with all laws and regulations, and in a manner consistent with the business strategy, business plans and remuneration and other policies approved by the Board;
- (d) Provide the Board with timely, complete, accurate and understandable information and documents and keep them adequately informed and updated on a timely basis about material issues including:
  - (i) The licensee's performance and financial condition;
  - (ii) Breaches of risk limits or regulations;
  - (iii) Internal control failures, frauds and cyber-security incidents;
  - (iv) Legal or regulatory concerns;
  - (v) Customer complaints.



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## HC-10.6 Internal Audit

### HC-10.6.1

Licensees must establish an effective independent internal audit. The Board and senior management must:

- Ensure that scope and coverage of internal audit is commensurate with the nature, size and complexity of the activities of the licensee,
- Remain accountable for the activities even if the internal audit is outsourced;
- Promote a strong and robust internal control environment within the licensee;
- Require that all internal audit findings and recommendations are resolved within a reasonable period of time to be set based on level and magnitude of risk;
- Allocate sufficient annual budget to support the internal audit activities and plans; and
- Inform the internal auditor of new developments, initiatives, projects, products and operational changes.

### HC- 10.6.2

All licensees must have an internal audit charter which must be reviewed and approved by the Board.

### HC- 10.6.3

The Internal audit must:

- Report directly to the Board;
- Be independent of all functions;
- Have sufficient skilled resources to be able to judge outcomes and make an impact at the highest level of the organization;
- Independently review and evaluate the effectiveness and efficiency of all functions, internal controls, risk management, internal risk and finance models, governance framework, policies, procedures, systems and processes, including the licensee's outsourced activities, and must ensure adequate coverage of matters of regulatory interest within the audit plan;
- Develop an independent and informed view of the risks faced by the licensee based on its access to all licensees' records and data, its enquiries and its professional competence and be free to report its findings and assessments;
- Discuss its views, findings and conclusions directly with the Board or a designated board committee; and
- Not be involved in designing, selecting, implementing or operating specific internal control measure.



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## HC-10.7 Compliance

### HC-10.7.1

The Board must:

- (a) Oversee the management of the licensee's compliance risk;
- (b) Establish an independent compliance function and approve an appropriate compliance framework for the licensee based on its size and complexity of its operations;
- (c) Set priorities for the management of its compliance risk in a way that is consistent with its risk management strategy and structures; and
- (d) Approve the licensee's compliance policy for identifying, assessing, monitoring, reporting and advising on compliance risk.

### HC-10.7.2

The licensee must:

- (a) Establish the operating compliance procedures and processes for identifying, assessing, monitoring, reporting and advising on compliance risk;
- (b) Establish written guidance to the licensee's staff on the appropriate implementation of laws and regulations;
- (c) Ensure reporting by the compliance function to the Board or a designated board committee:
  - (i) On a quarterly basis, the licensee's management of its compliance risk, in such a manner as to assist the Board or the designated board committee members to make an informed judgment on whether the licensee is managing its compliance risk effectively; and
  - (ii) Immediately any material compliance failures as they arise (e.g. failures that may attract a significant risk of legal or regulatory sanctions, material financial loss, or loss of reputation).



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## HC-10.8 Shareholders' Meetings

### HC-10.8.1

Bahraini licensees must comply with the following with respect to any shareholders' meeting:

- (a) Provide the draft agenda to the CBB, for its review and comment, at least 5 working days prior to communicating with the shareholders;
- (b) Ensure that CBB's prior approval has been obtained for any agenda items which require CBB's approval under relevant regulations, prior to the meeting taking place; and
- (c) Invite a representative of the CBB to attend the meetings at least 5 working days prior to the meeting taking place.