

**Ibdar Bank B.S.C. (c)**

**DISCLOSURES REQUIRED UNDER  
PD MODULE OF THE CBB RULEBOOK  
For The Year Ended 31 December 2018**

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For the year ended 31 December 2018

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## 1 INTRODUCTION

The disclosures under this section have been prepared in accordance with the CBB requirements outlined for Islamic banks in its Public Disclosure Module, of Volume 2 of the CBB rulebook (the "PD Module"). Rules concerning the disclosures under this section are applicable to Ibdar Bank B.S.C. (c) (Ibdar/the "Bank") being a locally incorporated Bank with a wholesale Islamic Investment banking license and subsidiaries (together known as "the Group"). This document should be read in conjunction with the consolidated financial statements for the year ended 31 December 2018 and the qualitative disclosures in the annual report for the year ended 31 December 2018. The disclosures in this report are in addition to the disclosures set out in the audited consolidated financial statements of the Bank for the year ended 31 December 2018. Information already included in the consolidated financial statements are not repeated.

### 1.1 Pillar I – Minimum Capital Requirements

Pillar I deals with the rules for the computation of regulatory capital requirements in respect of credit, market and operational risk. It defines the various classes of assets and the calculation of Risk Weighted Assets (RWAs) in respect of each class of assets. The capital adequacy ratio is calculated as the ratio of the Bank's regulatory capital to its total risk weighted assets. All Bahrain incorporated banks are currently required to maintain a minimum capital adequacy ratio of 12.5%.

#### 1.1.1 Credit risk

The Bank has adopted the standardized approach under which on and off-balance sheet credit exposures are assigned to exposure categories based on the type of counterparty or underlying exposure. Under the standardized approach, the risk weightings are provided by the CBB and are determined based on the counterparty's external credit rating. The external credit ratings are derived from eligible external rating agencies approved by the CBB.

#### 1.1.2 Market risk

The Bank has adopted the Standardized approach for determining the market risk capital requirement.

#### 1.1.3 Operational risk

The Bank has adopted the basic indicator approach for operational risk. It is calculated by applying a co-efficient of 15 percent to the average gross income for the preceding three financial years.

### 1.2 Pillar II – The Supervisory Review and Evaluation Process

Pillar II involves the process of supervisory review of Bank's risk management framework and capital adequacy. It requires banks to hold additional capital for risks not covered by Pillar I. Other risk types which are not covered by the minimum capital requirements in Pillar I include liquidity risk, interest rate risk in the banking book, business risk and concentration risk.

Pillar II comprises of an Internal Capital Adequacy Assessment Process (ICAAP) and supervisory review and evaluation process.

The ICAAP incorporates a review and evaluation of risk management and capital relative to the risks to which the Bank is exposed. The Bank has established an ICAAP which quantifies the capital requirements for the key risks that the Bank is exposed to including credit, investment, liquidity, strategic, reputation, operational, and concentration risks. The Bank also conducts comprehensive stress tests for various portfolios and assesses the impact on the capital and profitability. In addition, the Bank's stress testing frameworks and models allow for forward looking scenarios, which are considered for business growth strategies. The ICAAP of the Bank is driven by the Board through the Capital Adequacy Strategy and the ICAAP Policy. In case a plausible stress scenario is identified which may severely affect the capital adequacy of the Bank, the senior management decides an appropriate corrective action to be taken under such a scenario.

### 1.3 Pillar III – Market Discipline

Pillar III is related to market discipline and requires the Bank to publish detailed qualitative and quantitative information of its risk management and capital adequacy policies and processes to complement the first two pillars and the associated supervisory review process.

#### 1.3.1 Pillar II quantitative and qualitative disclosures

For the purpose of computing regulatory minimum capital requirements, the Bank follows the rules as laid out under the CBB Rulebook module CA: Capital Adequacy.

There are no restrictions on the transfer of funds or regulatory capital within the group and all investments are made fully complying with the CBB approval instructions.

### 1.4 Overall Risk and Capital Management

The consolidated financial statements of the Group has been prepared in accordance with the Financial Accounting Standards issued by the Accounting and Auditing Organization for Islamic Financial Institutions ("AAOIFI") and the Bahrain Commercial Companies Law.

In the consolidated financial statements, subsidiaries are fully consolidated from the date of acquisition, being the date on which the Bank obtains control, and continues to be consolidated to the date of loss of control.

For the purpose of computing the Capital Adequacy Ratio ("CAR") the Bank is not consolidating subsidiaries that are Commercial Entities.

The Bank does not hold interest in any insurance entities.

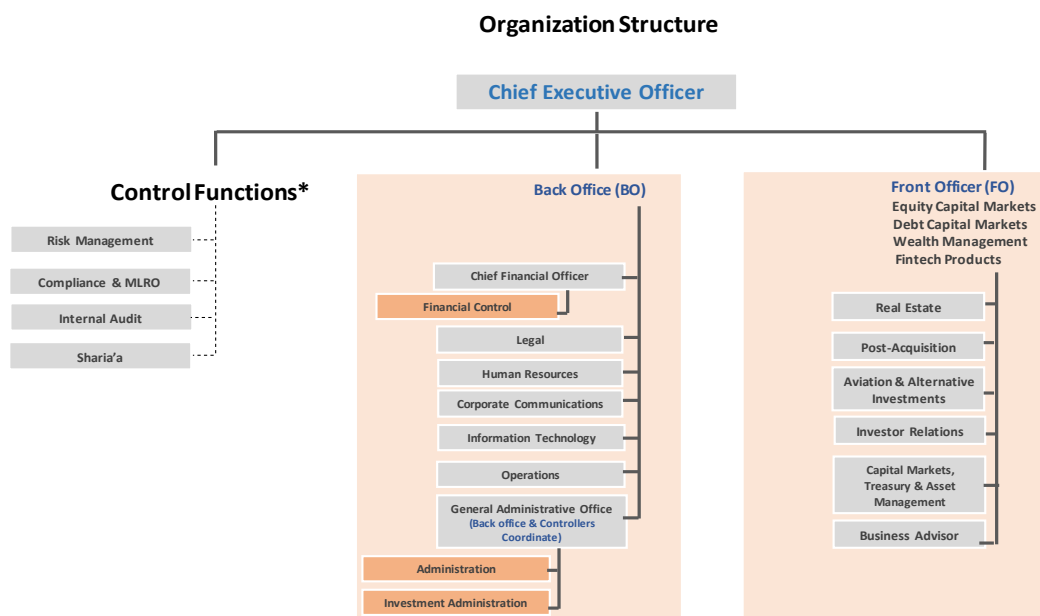
### 1.5 Compliance with High Level Control (PD-1.3.10(x))

In October 2010, CBB introduced requirements to Module (HC Module) that have to be met by all licensees with respect to, corporate governance principles to be in line with the Principles relating to the Corporate Governance Code issued by the Ministry of Industry and Commerce; International best practice corporate governance standards set by bodies such as the Basel Committee for Banking Supervision; and related high-level controls and policies. The Group made detailed self-assessments on the revised content of HC Module to ensure compliance with the new requirements with specific milestones for implementation of any shortfalls.

## 2 RISK MANAGEMENT STRUCTURE

The Board has the ultimate responsibility for understanding the nature and level of risk taken by the Bank. The Board is responsible for reviewing the strategy and objectives of the Bank with respect to various risks and ensures that there is a clear guidance regarding the level of risks acceptable to the Bank.

Figure 1 Group Organization Structure (PD-1.3.10(a))



\* Controllers are reporting to the respective BOD Committees & administratively to the CEO

### 2.1 Board of Directors (PD - 1.3.10 (n) and PD - 1.3.10 (a & o))

The Board is responsible for establishing objectives for the Bank and developing the strategies that direct the ongoing activities of the Bank to achieve those objectives. The Board is in process of reviewing and approving the Bank's strategy document which demonstrates that it is able to proactively identify and understand the risks that the Bank faces in achieving its business objectives through its business strategies and plans.

As part of its strategy review process, the Board at the minimum shall: (PD-1.3.10(n, o)):

- a. Review major strategy papers and business plans;
- b. Set performance objectives;
- c. Oversee major capital expenditures and acquisitions;
- d. Reassess annually the Bank's objectives, strategies and plans;
- e. Demonstrate its responsibility to supervisors, shareholders, employees & other stakeholders; and
- f. Monitor the control environment and risk profile of the Bank.
- g. Preparation of the financial statements of the Bank.

Detailed responsibilities of the Board are provided in the Bank's Articles of Association.

The Board has approved authority matrix which authorizes the senior management/committees to approve certain transactions. However, transactions which are beyond the authority matrix require Board or Excom approval.

The Board of Directors has delegated the management of the Bank to the Executive Management, comprising of Chief Executive Officer, Chief Investment Officer and Chief Financial Officer, who meet on a regular basis to discuss any issues and updates regarding operations and business of the Bank. The following sub-committees of the Board are involved in managing the risk and ensuring the compliance with the Bank's policies and risk management framework.

## 2 RISK MANAGEMENT STRUCTURE (continued)

### 2.2 Board Committees

#### 2.2.1 Board of Directors

##### 2.2.1.1 Objective/Function

The Board is responsible for establishing objectives for the Bank and developing the strategies that direct the ongoing activities of the Bank to achieve those objectives.

##### 2.2.1.2 Members

Tareq Sadiq	Independent	Hamad Al Sejari	Executive
Abdulkarim Bucheery	Independent	Jassem Al Yaseen	Executive
Ebrahim Al Jassmi	Independent	Jamal Abdulla Al Saleem	Non-Executive
Abdulaziz Al Afaleq	Independent	Khalid Al Maarafi	Executive
Mohamed Noorudin	Independent		
Dr. Mohamed Kameshki	Independent		

#### 2.2.2 Executive Committee

##### 2.2.2.1 Objective/Function

Consider specific matters delegated to it by the full Board and make recommendations thereon to the Board or decisions based on authorities specifically delegated by the Board.

##### 2.2.2.2 Members

Abdulkarim Bucheery	Independent
Ebrahim Al Jassmi	Independent
Hamad Al Sejari	Executive
Jassem Al Yaseen	Executive

#### 2.2.3 Audit, Risk & Compliance Committee

##### 2.2.3.1 Objective/Function

To review the Banks financial reporting process, internal controls, and process for monitoring compliance with policies, procedures, laws and regulations and the Bank's own Code of Business Conduct.

##### 2.2.3.2 Members

Dr. Mohamed Kameshki	Independent
Khalid Al Maarafi	Executive
Abdulaziz Al Afalaq	Independent

#### 2.2.4 Nomination, Remuneration & Governance Committee

##### 2.2.4.1 Objective/Function

The Nomination, Remuneration & Governance Committee reviews and approves (according to the guidelines set by the Board) policies and procedures for the remuneration of Board members, Committees members, executive and non-executive employees.

##### 2.2.4.2 Members

Tareq Sadeq	Independent
Mohamed Nooruddin	Independent
Jamal Al Saleem	Non-Executive

### 2.3 Management Committees

The following committees are the two management committees at Ibdar which are involved in managing and overseeing the Bank's activities, and in proposing new strategies, policies, and procedures to the Board. These Committees are:

#### 2.3.1 Asset and Liability Committee

##### 2.3.1.1 Objective/Function

The Asset and Liability Committee determines the appropriate levels of liquidity, and ensures that all future commitments are funded in the most appropriate and cost-efficient manner. The Committee also ensures that the Bank fully adheres to the requirements of the CBB regarding capital, liquidity, and mismatched risk. It ascertains that approved investment deposits limits are not exceeded, and Treasury management and dealing activities are within the policy guidelines set by the Board. Furthermore, it monitors and supervises the overall balance sheet structure.

##### 2.3.1.2 Members

Acting Chief Executive Officer	Chairman
Chief Financial Officer	Member
Head of Treasury and Capital Markets*	Member
Head of Risk Management	Member
Director - Treasury and Capital Markets	Member
Manager - Treasury and Capital Markets*	Secretary

\* Resigned during the year of 2018

#### 2.3.2 Investment, Credit and Risk Committee

##### 2.3.2.1 Objective/Function

The Investment, Credit and Risk Committee is a senior management committee responsible for managing and supervising all activities related to investments, credit and risk management.

##### 2.3.2.2 Members

Acting Chief Executive Officer	Chairman
Chief Executive Officer*	Chairman
Chief Financial Officer	Member
Head of Investor Relations*	Member
Head of Risk Management	Non Voting Member
Head of Legal*	Non Voting Member
Head of Treasury and Capital Market*	Non Voting Member
Head of Advisory*	Non Voting Member

\* Resigned during the year of 2018

### 3 CAPITAL ADEQUACY

The primary objective of the Group's capital management is to ensure that the Group maintains adequate risk capital, complies with the capital requirements laid down by the CBB and maintains a healthy capital ratio in order to support its business and maximize shareholder value.

The Group manages the capital base to cover risks inherent in the business. The adequacy of the Group's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision ("BIS rules/ratios") as adopted by the CBB in supervising the Bank.

Regulatory capital consists of Common Equity Tier 1 capital ("CET1"), Additional Tier 1 Capital ("AT1") and Tier 2 capital (supplementary capital). The Group's Tier 1 comprises share capital, general reserves, statutory reserves, retained earnings/accumulated losses and unrealized gains and losses arising from fair valuing equities. Tier 2 includes asset revaluation reserve - property, plant and equipment and the general financing loss provisions. From the regulatory perspective, the significant amount of the Bank's capital is in Tier 1 form.

The Group's approach to assessing capital adequacy has been in line with its risk appetite aligned with its current and future activities. To assess its capital adequacy requirements in accordance with the CBB requirements, the Group adopts the Standardized Approaches for its Credit Risk and Market Risk, and the Basic Indicator Approach for its Operational Risk.

The Group's capital adequacy policy is to maintain a strong capital base to support the development and growth of the business. Current and future capital requirements are determined on the basis of expectations for each business group, expected growth in future sources and uses of funds.

Further the Bank monitors the CAR against an Internal Trigger Ratio of 20% compared to the required capital of 12.5% under CBB rulebook. If the ICAAP CAR touches the Internal Trigger Ratio, the Bank will initiate action to reduce its risk or increase capital before the Internal Target Ratio is breached.

#### Basis of Consolidation for Accounting and Regulatory Purposes

For the purpose of preparation of consolidated financial statements, the Bank consolidates all subsidiaries which are fully owned or exercises significant control over them. These subsidiaries are consolidated from date of acquisition being the date on which the group obtains control and continues until the control ceases. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. For regulatory purposes the Bank should consolidate all banking and other financial entities which are considered to be subsidiaries of the Bank. The treatment of the Bank's investments in all entities for the purpose of regulatory reporting is risk weighting of investment exposure. The principal subsidiaries and associates are as follows:

Subsidiaries	Country of Incorporation	Total Assets	Total Equity	Description
Ibdar Corporate Services Limited*	British Virgin Islands	14,324	(7,142)	A company established to manage affiliated companies
Tamkeen Investment Company BSC	Kingdom of Bahrain	11,553	2,653	Administer Management Incentive Program ("MIP")
PKV Investment Company Limited	Cayman Islands	70,371,920	20,496,335	Investment holding vehicle for property lease
300 Riverpark Investment Company Limited	Cayman Islands	50,232,714	23,063,941	Investment holding vehicle for property lease

Associates	Country of Incorporation	Description
MENA Energy Limited	Kingdom of Saudi Arabia	Investment company holding a stake in an electrical services contracting company
Barak Ibdar Trade Finance Fund SP	South Africa	Fund established to invest in commodity-based and general trade finance transactions
Palma Ibdar Air Lease**	Kingdom of Bahrain	Managing aircraft leasing to airline companies

\* The Bank has a commitment of USD 7 thousands towards the equity shortfall.

\*\* Liquidated during 2018.

Associates which have been fully provided for, do not have any impact on regulatory reporting, and are not included in the table above.

### 3 CAPITAL ADEQUACY (continued)

#### 3.1 Composition of capital disclosure

**Table – 1. Statement of financial position under the regulatory scope of consolidation**

The table below shows the link between the statement of financial position in the published financial statements (accounting statement of financial position) and the regulatory statement of financial position.

	<i>31 December 2018</i>		<i>Reference</i>
	<i>Statement of financial position as in published financial statements (USD '000)</i>	<i>Statement of financial position as per regulatory reporting (USD '000)</i>	
<b>Assets</b>			
Cash and balances with banks	6,628	2,443	
Placements with financial institutions	34,021	34,021	
Investment in sukuk	53,413	53,413	
Financing receivables	3,204	3,204	
Receivable from ijarah investors	5,525	5,525	
Investment in equity securities	82,950	104,120	
Of which related to insignificant investments in financial entities under CET1:	-	19,246	<b>F</b>
Of which related to significant investments in financial entities under CET1	-	10,426	<b>G</b>
Of which related to other investments	-	74,448	
Investment in real estate	133,871	19,586	
Other assets	5,331	3,204	
<b>Total assets</b>	<b>324,943</b>	<b>225,516</b>	
<b>Liabilities</b>			
Financing liabilities	81,940	5,661	
Other liabilities	5,357	4,634	
Expected Credit Losses (Stages 1 & 2)	-	100	<b>H</b>
Of which related to other liabilities	-	4,534	
<b>Total liabilities</b>	<b>87,297</b>	<b>10,295</b>	
<b>Shareholders' Equity</b>			
Share capital	233,000	233,000	<b>A</b>
Statutory reserve	762	762	<b>C</b>
(Accumulated losses) / retained earnings	(20,899)	(24,106)	<b>B</b>
Investment fair value reserve	947	947	<b>J</b>
General reserve	4,618	4,618	<b>D</b>
<b>Equity attributable to shareholders of the Bank</b>	<b>218,428</b>	<b>215,221</b>	
Non-controlling interests	19,218	-	
<b>Total owners' equity</b>	<b>237,646</b>	<b>215,221</b>	
<b>Total liabilities and owners' equity</b>	<b>324,943</b>	<b>225,516</b>	

### 3 CAPITAL ADEQUACY (continued)

#### 3.1 Composition of capital disclosure (Continued)

##### Table – 2. Composition of regulatory capital

The table below provides a detailed breakdown of the bank's regulatory capital components, including all regulatory adjustments. The table also provides reference to the comparison displayed in Table 1 between accounting and regulatory statement of financial positions.

	<b>31 December 2018</b>		
	<i>Components of regulatory capital (USD '000)</i>	<i>Amounts subject to pre-2015 treatment (USD '000)</i>	<i>Reference</i>
<b>Common Equity Tier 1 capital: instruments and reserves</b>			
Directly issued qualifying common share capital plus related stock surplus	233,000	-	A
Retained earnings	(24,106)	-	B
Accumulated other comprehensive income (and other reserves)	6,327	-	C+D+J
<b>Common Equity Tier 1 capital before regulatory adjustments</b>	<b>215,221</b>	<b>-</b>	
<b>Common Equity Tier 1 capital: regulatory adjustments</b>			
Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold)	-	19,246	F
Significant investments in the common stock of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)	-	10,426	G
<b>Total regulatory adjustments to Common equity Tier 1</b>	<b>-</b>	<b>29,672</b>	
<b>Common Equity Tier 1 capital (CET1)</b>	<b>215,221</b>		
<b>Additional Tier 1 capital (AT1)</b>	<b>-</b>		
<b>Tier 1 capital (T1 = CET1 + AT1)</b>	<b>215,221</b>		
<b>Tier 2 capital: instruments and provisions</b>			
Provisions	100		H
<b>Tier 2 capital before regulatory adjustments</b>	<b>100</b>		
<b>Tier 2 capital (T2)</b>	<b>100</b>		
<b>Total capital (TC = T1 + T2)</b>	<b>215,321</b>		
<b>Risk weighted assets in respect of amounts subject to pre-2015 treatment</b>	<b>54,613</b>		
Of which: Insignificant investments in the common shares of financial entities <10% - Listed (RW at 100%)	7,472		
Of which: Insignificant investments in the common shares of financial entities <10% - Unlisted (RW at 150%)	21,076		
Of which: Significant investment in the common shares of financial entities >10% (RW at 250%)	26,065		
<b>Total risk weighted assets</b>	<b>425,376</b>		
<b>Capital ratios and buffers</b>			
Common Equity Tier 1 (as a percentage of risk weighted assets)	<b>50.60%</b>		
Tier 1 (as a percentage of risk weighted assets)	<b>50.60%</b>		
Total capital (as a percentage of risk weighted assets)	<b>50.62%</b>		
<b>National minima including CCB (where different from Basel III)</b>			
CBB Common Equity Tier 1 minimum ratio	6.50%		
CBB Tier 1 minimum ratio	8.00%		
CBB total capital minimum ratio	10.00%		



**3 CAPITAL ADEQUACY (continued)**

**3.1 Composition of capital disclosure (Continued)**

Disclosure template for main feature of regulatory capital instruments as at 31 December 2018:

1	<b>Issuer</b>	Ibdar Bank BSC (c)
2	<b>Unique identifier (e.g. CUSIP, ISIN or Bloomberg identifier for private placement)</b>	NA
3	<b>Governing law(s) of the instrument</b>	All applicable laws and regulations of the Kingdom of Bahrain
<b>Regulatory treatment</b>		
4	Transitional CBB rules	Common Equity Tier 1
5	Post-transitional CBB rules	Common Equity Tier 1
6	Eligible at solo/group/group & solo	Group & solo
7	Instrument type (types to be specified by each jurisdiction)	Equity shares
8	<b>Amount recognised in regulatory capital (Currency in mil, as of most recent reporting date)</b>	USD 233 million
9	<b>Par value of instrument</b>	USD 1.00
10	<b>Accounting classification</b>	Shareholder's equity
11	<b>Original date of issuance</b>	31 December 2012
12	<b>Perpetual or dated</b>	Perpetual
13	Original maturity date	No maturity
14	<b>Issuer call subject to prior supervisory approval</b>	NA
15	Optional call date, contingent call dates and redemption amount	NA
16	Subsequent call dates, if applicable	NA
<b>Coupons / dividends</b>		
17	Fixed or floating dividend/coupon	NA
18	Coupon rate and any related index	NA
19	Existence of a dividend stopper	NA
20	Fully discretionary, partially discretionary or mandatory	Fully discretionary
21	Existence of step up or other incentive to redeem	No
22	Non-cumulative or cumulative	NA
23	<b>Convertible or non-convertible</b>	NA
24	If convertible, conversion trigger (s)	NA
25	If convertible, fully or partially	NA
26	If convertible, conversion rate	NA
27	If convertible, mandatory or optional conversion	NA
28	If convertible, specify instrument type convertible into	NA
29	If convertible, specify issuer of instrument it converts into	NA
30	<b>Write-down feature</b>	NA
31	If write-down, write-down trigger (s)	NA
32	If write-down, full or partial	NA
33	If write-down, permanent or temporary	NA
34	If temporary write-down, description of write-up mechanism	NA
35	<b>Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)</b>	NA
36	<b>Non-compliant transitioned features</b>	NA
37	<b>If yes, specify non-compliant features</b>	NA

### 3 CAPITAL ADEQUACY (continued)

#### 3.1 Composition of capital disclosure (Continued)

**Table – 3. Capital requirement by type of Islamic financing contracts (PD - 1.3.17)**

The following table summarizes the capital requirements by type of Islamic financing contracts:

Table - 3.1 The following table summarizes the capital requirements by type of Islamic financing contracts:

Type of Islamic financing contracts	31 December 2018		
	Gross Exposure	Risk Weighted	Capital
	Amount (USD '000)	Amount (USD '000)	requirements (USD '000)
Mudaraba	34,021	6,804	851
Murabaha	3,204	3,204	401
Sukuk	39,754	28,711	3,589
	<b>76,979</b>	<b>38,719</b>	<b>4,840</b>

Table - 3.2 Capital requirement for credit risk by type of exposure:

	31 December 2018		
	On- & Off Balance		Capital
	Sheet Credit Exposures before CRM (USD '000)	Credit Risk Weighted Assets (USD '000)	requirements (USD '000)
Claims on Sovereigns	20,680	2,011	251.00
Claims on PSEs	13,833	9,597	1,200
Claim on Banks	36,500	7,421	928
Claims on Corporates including Takaful Companies & Category 3 Investment Firms	334	334	42
Investments in Equity Securities and Equity Sukuk	59,587	96,333	12,042
Holding of Real Estate	66,015	224,868	28,109
Other Assets and Specialized Financing	14,963	22,381	2,798
	<b>211,912</b>	<b>362,945</b>	<b>45,370</b>

**Table – 4. Capital requirement for Market risk (PD–1.3.18)**

The following table summarizes the amount of exposures subject to the standardized approach of market risk and related capital requirements:

	31 December 2018 (USD '000)
<b>Market Risk - Standardized Approach</b>	
Price Risk	-
Equity Position Risk	-
Sukuk Risk	831
Foreign exchange risk	1,315
<b>Total of market risk - standardized approach</b>	<b>2,146</b>
Multiplier	12.5
<b>Total Market Risk Weighted Exposures</b>	<b>26,830</b>
<b>Minimum capital requirement (12.5%)</b>	<b>3,354</b>

**Table – 5. Capital Requirements for Operational risk (PD–1.3.19 and PD–1.3.30)**

The following table summarizes the amount of exposures subject to the basic indicator approach of operational risk and related capital requirements:

	31 December 2018 (USD '000)		
<b>Indicators of operational risk</b>			
<b>Year</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Gross Income	15,915	18,135	22,911
<b>Average gross income</b>			<b>18,987</b>
Multiplier			12.5
			<b>237,338</b>
Eligible Portion for the purpose of the calculation			15%
<b>Total operational Risk Weighted Exposures</b>			<b>35,601</b>
<b>Minimum capital requirement (12.5%)</b>			<b>4,450</b>

## **4 RISK MANAGEMENT**

### **4.1 Overview**

#### **4.1.1 Bank-wide Risk Management Objectives**

The risk management objective for each area of risk is to adopt the industry best practices and adhere to Basel II and CBB requirements. The Bank identifies, captures, monitors and manages different dimensions of risk with the aim to protect asset values and income streams, and to optimize the Bank's shareholder return, while maintaining its risk exposure within defined parameters. The Bank's management believes in the proactive management of risk in the full cycle of a financial transaction including its operating circumstances from the origination stage to its final disposal from the books of the Bank.

The Bank reviews and redefines its risk appetite according to the evolving business plan of the Bank, which includes fluctuations in economic and market conditions and future forecasts.

#### **4.1.2 Strategies Processes and Internal Controls**

The Bank's risk strategy, backed by appropriate limit structures, is articulated through risk management policies and procedures. These policies and procedures are an integral part of an enterprise-wide integrated risk management framework at the Bank. These policies and procedures identify risk objectives, processes, strategies and risk governance both at the board and the management level. The capital management policy is aimed at ensuring financial stability by allocating enough capital to cover unexpected losses. Limit structures serve as a key component in articulating risk strategy in quantifiable risk appetite. In addition, the Bank intends to implement various risk systems to help quantify not just the regulatory capital but also the economic capital allocated to various portfolios.

The Bank is exposed to various types of risk, such as market, credit, profit rate, liquidity and operational, all of which require the comprehensive controls and ongoing oversight. The risk management framework encapsulates the spirit behind Basel II, which includes management oversight & control, risk culture & ownership, risk recognition & assessment, control activities, adequate information & communication channels, monitoring risk management activities and correcting deficiencies.

#### **Credit Risk**

The Bank manages its credit risk exposures by assessing the credit worthiness of all customers & counterparties. For each new product & activity, the Bank evaluates credit risk introduced by it. The Bank has established a limit structure to avoid concentration of risks for counterparty, sector and geography.

#### **Market Risk**

The Bank is not exposed to significant market risk due to the nature of its activities and its limited market risk exposure is managed through combination of limits, internal controls & processes. The Group manages its market risk exposures by evaluating each new product and activity with respect to the market risk introduced by it.

#### **Operational Risk**

The Bank has established a Risk Control and Self Assessment ("RCSA") process necessary for identifying and measuring and controlling its operational risks. This exercise covers the Bank's business lines and associated critical activities, exposing the Bank to operational risks.

#### **Equity Risk in the Banking Book**

Equity price risk is the risk that the fair values of equities decrease as the result of changes in the levels of equity indices and the value of individual stocks. The equity price risk exposure arises from the Group's investment portfolio. The Group manages and monitors its equity risk using sector, geography and investment type limits.

The strategy used has been effective throughout the year.

#### **Profit Rate Risk**

Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The Group manages its profit rate risk using various risk management tools and methodologies.

#### **Displaced Commercial Risk**

Displaced Commercial Risk ("DCR") refers to the market pressure to pay returns that exceeds the rate that has been earned on the assets financed by the liabilities, when the return on assets is under performing as compared with competitor's rates.

The Bank does not have DCR as it does not have any Restricted or Unrestricted Investment Accounts.

#### **4.1.3 Risk Measurement and Reporting System**

The Group identifies, measures, controls and monitors its material risks on a periodic basis. The Group has established relevant risk limit structures to quantify its risk appetite. Audit, Risk and Compliance Committee ("ARCC") reviews and recommends the limits, suggested by the Investment, Credit and Risk Committee ("ICRC") to the Board which is ultimately responsible for the final approval of the limit. The monitoring and controlling of risks is managed through limits approved by the Board. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept.

The Risk Management Department ("RMD") presents reports to the Board of Directors through ICRC and ARCC. These reports include risk and investment review of Group's portfolio and its impact on Group's capital adequacy.

As part of the Risk Management reporting framework, risk reports are prepared and distributed in order to ensure that all business divisions have access to necessary and up-to-date information. A periodic briefing is given to the Risk Committee on the utilization of limits, proprietary investments, and liquidity, plus any other risk developments.

#### **4 RISK MANAGEMENT (continued)**

##### **4.2 Credit risk**

###### **4.2.1 Introduction**

Credit risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract. The Group controls credit risk by monitoring credit exposures, and continually assessing the creditworthiness of counterparties.

The Group is not involved in the granting of credit facilities in the normal course of its business activities. The credit risk exposures faced by the Group are principally in respect of its placements with other financial institutions and in respect of investment related funding made to projects. The investment related funding exposures arise in the ordinary course of its investment banking activities. All such exposures are reviewed periodically for recoverability and specific provisions made where necessary having regard to the nature of the exposure and the assessment of collection. The Group uses the Standardized Approach for measuring its credit risk. The Group uses ratings from External Credit Assessment Institutions recognized by the CBB for its Group counterparty exposures, wherever available.

Counterparty limits are established by the use of a comprehensive approval process. All lines of counterparty credit limits are subject to annual reaffirmation by the Board of Directors. The limits are also reviewed frequently to ensure consistency with the Group's risk appetite and to take into account the latest market developments. Given the nature of the Group's business, the Group uses nominal balance sheet amounts including accrued interest and other receivables as its measure of exposure.

###### **4.2.2 Types of Credit Risk**

Financing receivables mainly comprise of Murabaha (International Commodity) and Musharaka.

###### **4.2.2.1 Murabaha (International Commodity)**

A commodity Murabaha is a contract between the Bank and its client for the sale of goods at a price plus an agreed profit margin for the Bank. The instrument is called an international commodity Murabaha because the profits are made on the international buying and selling of a commodity, usually metal, such as copper, aluminum or lead.

###### **4.2.2.2 Musharaka**

Musharaka financing is partnership in which the Group contributes capital. These are stated at the fair value of consideration given less impairment.

###### **4.2.3 Past Due and Impaired Islamic Financing**

The Group defines non-performing facilities as the facilities where the principal or profit is overdue for a period of 90 days or more. These exposures are placed on a non-accrual status with income being recognized to the extent that it is actually received. It is the Group's policy that when an exposure is overdue for a period of 90 days or more, the whole financing facility extended is considered as past due, not only the overdue installments and payments.

As a policy, the Group has placed on a non-accrual status any facility where there is reasonable doubt about the collectability of the receivable irrespective of whether the customer concerned is currently in arrears or not.

Financing receivables are stated at cost less impairment allowances. Specific provisions are created for impairment where losses are expected to arise on non-performing contracts. These assets are written off when they are considered to be uncollectable to reduce all impaired assets to their expected realizable values. Deferred income and provision for impairment are netted off against the related receivables. The Group assesses at each financial position date whether there is objective evidence that a financial asset is impaired.

Impairment losses on murabaha receivables and debt-type instruments at amortized cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated cash flows discounted at the assets' original effective profit rate. Losses, if any, are recognized in the consolidated statement of income and reflected in an allowance account against murabaha receivables and debt-type instruments at amortized cost. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the consolidated statement of income.

###### **4.2.4 External Credit Assessment Institutions (ECAI)**

To assess the creditworthiness of Financial Institutions ("FI") the Group relies on external ratings by ECAI like Standard & Poor's, Fitch and Moody's. In case of unrated FIs, the Group will assess the credit risk on the basis of its internally developed approach & methodology. The Bank uses ECAI's for due from financial institutions and its sukuk portfolio carried at amortised cost.

###### **4.2.5 Definition of Geographical Area**

The Group allocates exposures to a particular geographical area based on the risk domicile concept, which could be either the location of the asset or on the location of the counterparty.

#### **4 RISK MANAGEMENT (continued)**

##### **4.2 Credit risk (continued)**

###### **4.2.6 Concentration Risk**

Concentration risk is the credit risk stemming from not having a well diversified credit portfolio, i.e. being overexposed to a single customer, industry sector or geographic region. As per CBB's single obligor regulations, Banks incorporated in Bahrain are required to obtain the CBB's approval for any planned exposure to a single counterparty, or group of connected counterparties, exceeding 15% of the regulatory capital base.

In order to avoid excessive concentrations of risk, the Group's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly. In case any exposure exceeds the CBB's prescribed limits, Group obtains approval from the CBB. Currently, the Bank does not have any exposure that exceeds this threshold.

###### **4.2.7 Credit Risk Mitigation**

Credit risk mitigation is defined as the utilization of a number of techniques, such as collaterals and guarantees to mitigate the credit risks that the Group is exposed to. The Group's first priority when establishing Islamic financing is to determine the borrower's capacity to repay and not to rely principally on security or collateral. Nonetheless, the Group is in the process of developing its collateral management policy which would be in line with its business activities.

##### **4.2.8 Counterparty Credit Risk**

###### **4.2.8.1 Introduction**

A counterparty is defined as an obligor (individual, company, other legal entity), a guarantor of an obligor, or person receiving funds from the Group. It also includes the issuer of a security in case of a security held by the Group, or a party with whom a contract is made by the Group for financial transactions.

The measure of exposure reflects the maximum loss that the Group may suffer in case the counterparty fails to fulfill its commitments. Group exposure is defined as the total exposure to all counterparties closely related or connected to each other. Large exposure is any exposure whether direct, indirect or funded by restricted investment accounts to a counterparty or a group of closely related counterparties which is greater than or equal to 10% of the Group's Capital Base. The Group has adopted Standardized Approach to allocate capital for counterparty credit risk.

###### **4.2.8.2 Credit Limit Structure**

The Bank has put in place an internal counterparty limit structure which is based on internal or external ratings for different types of counterparties. The Bank has also set concentration limits as a percentage of shareholders equity. In case of a counterparty rating degrade, the Bank may require further collateral or advise the counter party to reduce its exposure on a case by case basis.

###### **Reporting**

The Bank reports large counterparty exposures to CBB and senior management on periodic basis. The Bank reports the exposures on a gross basis without any offset. However, debit balances on accounts may be offset against credit balances where both are related to the same counterparty, provided the Bank has a legally enforceable right to do so.

###### **Early warning indicators**

The Bank maintains a strong focus on identification of signs of deterioration in credit quality at an early stage in order to take remedial measures before the facility becomes substandard or doubtful.

###### **4.2.8.3 Connected counterparties**

Connected counterparties includes companies or persons connected with the bank, including, in particular, subsidiaries and associated companies (whether such association is due to control or shareholding or otherwise), Directors and their associates (whether such association is due to control or family links or otherwise), members of the Shari'a Supervisory Board, management and other staff, and shareholders holding 10% or more of the voting power of the bank.

As a strategy, exposure to connected counterparties may be undertaken only when negotiated and agreed on an arm's length basis. The Bank shall not assume any exposure to its external auditors or members of Shari'a Supervisory Board. The disclosure relating to related party transactions has been made in the consolidated financial statements. All related party transactions have been executed at arm's length basis.

###### **4.2.8.4 Highly Leverage Counterparties**

The Bank assess counterparties through financial and non-financial due diligence and uses CBB's definition of Highly Leveraged Counterparties to determine exposure to them. The Bank is not exposed to any Highly Leveraged Counterparties.

###### **4.2.8.5 Restructuring of Credit Facilities**

No facilities were restructured during the year 2018.

###### **4.2.8.6 Recourse Transactions**

The Bank does not currently have any obligations with respect to recourse transactions.

**4 RISK MANAGEMENT (continued)**

**4.2 Credit risk (continued)**

**4.2.9 Credit risk mitigation**

The credit exposure information presented in table 6 of this report represents gross exposures prior to the application of any credit risk mitigation techniques. Collateral items and guarantees which can be used for credit risk mitigation under the capital adequacy framework are referred to as eligible collateral. However, extending credit facilities is not a part of the Bank's core business activities. The Bank's credit risk mainly arises from its investment transactions.

Nonetheless, the Bank intends to develop its collateral management policy and provisioning policy which would be in line with its business activities.

**Table – 6. Credit Risk Exposure (PD–1.3.23(a))**

The following table summarizes the amount of gross funded and unfunded credit exposure and average gross funded and unfunded exposure as of:

	31 December 2018	
	Total gross credit exposure (USD '000)	*Average gross credit exposure over the year (USD '000)
<b>Funded exposure</b>		
Cash & balances with banks	6,628	6,879
Placements with financial institutions	34,021	15,951
Investment in sukuk	53,413	78,693
Financing receivables	3,204	5,873
Receivable from Ijara investors	5,525	5,662
Investment in equity securities	82,950	85,025
Equity-accounted investees	-	306
Investment in real estate	133,871	141,619
Other assets	5,331	11,377
<b>Total Funded Exposures</b>	<b>324,943</b>	<b>351,383</b>
<b>Unfunded exposure</b>		
Uncalled capital commitments in respect of investment	100	299
Operating lease commitments - within one year	-	80
<b>Total Unfunded Exposures</b>	<b>100</b>	<b>378</b>

\*Average balances are computed based on quarter-end balances.

**Table – 7. Credit Risk – Geographic Breakdown (PD–1.3.23(b))**

The following table summarizes the geographic distribution of funded and unfunded exposures, broken down into significant areas by major types of credit exposure as of:

	31 December 2018					Total (USD '000)
	Middle East (USD '000)	Europe (USD '000)	Africa (USD '000)	North America (USD '000)	Others (USD '000)	
<b>Funded exposure</b>						
Cash & balances with banks	2,280	163	-	4,185	-	6,628
Placements with financial institutions	34,021	-	-	-	-	34,021
Investment in sukuk	53,413	-	-	-	-	53,413
Financing receivables	3,204	-	-	-	-	3,204
Receivable from Ijara investors	5,525	-	-	-	-	5,525
Investment in equity securities	53,120	19,565	10,265	-	-	82,950
Investment in real estate	19,586	-	-	114,285	-	133,871
Other assets	2,617	-	427	2,287	-	5,331
<b>Total Funded Exposures</b>	<b>173,766</b>	<b>19,728</b>	<b>10,692</b>	<b>120,757</b>	<b>-</b>	<b>324,943</b>
<b>Unfunded exposure</b>						
Uncalled capital commitments in respect of investment	100	-	-	-	-	100
<b>Total Unfunded Exposures</b>	<b>100</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>100</b>

The Group allocates exposures to a particular geographical area based on the risk domicile concept, which could be either the location of the asset or on the location of the counterparty.

**4 RISK MANAGEMENT (continued)**

**4.2 Credit risk (continued)**

**4.2.9 Credit risk mitigation (continued)**

**Table – 8. Credit risk – Industry Sector Breakdown (PD–1.3.23(c))**

The following table summarizes the distribution of funded and unfunded exposure by industry type broken down by major types of credit exposure as of:

	31 December 2018					
	<i>Banks and financial institutions</i>	<i>Real Estate</i>	<i>Sovereign</i>	<i>Energy</i>	<i>Others</i>	<i>Total</i>
	(USD '000)	(USD '000)	(USD '000)	(USD '000)	(USD '000)	(USD '000)
<b>Funded exposure</b>						
Cash & balances with banks	3,098	3,530	-	-	-	6,628
Placements with financial institutions	34,021	-	-	-	-	34,021
Investment in sukuk	5,024	7,640	24,272	13,766	2,711	53,413
Financing receivables	-	3,204	-	-	-	3,204
Receivable from Ijara investors	-	-	-	-	5,525	5,525
Investment in equity securities	29,512	41,241	-	5,710	6,487	82,950
Investment in real estate	-	133,871	-	-	-	133,871
Other assets	490	3,617	249	175	800	5,331
<b>Total Funded Exposures</b>	<b>72,145</b>	<b>193,103</b>	<b>24,521</b>	<b>19,651</b>	<b>15,523</b>	<b>324,943</b>
<b>Unfunded exposure</b>						
Uncalled capital commitments in respect of investment	-	-	-	-	100	100
<b>Total Unfunded Exposures</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>100</b>	<b>100</b>

**Table – 9. Maturity breakdown of credit exposures (PD–1.3.23(g))**

The maturity breakdown for balances with banks, placements with financial institutions and financing receivables were based on residual commercial period. For the remaining exposures the residual maturities was determined based on management's expected realization period as of 31 December 2018.

	<i>Up to 3 months</i>	<i>3 months to 1 year</i>	<i>Total up to 1 year</i>	<i>1 to 5 years</i>	<i>5 to 10 years</i>	<i>No fixed maturity</i>	<i>Total</i>
	(USD '000)	(USD '000)	(USD '000)	(USD '000)	(USD '000)	(USD '000)	(USD '000)
<b>Funded exposure</b>							
Cash & balances with banks	6,628	-	6,628	-	-	-	6,628
Placements with financial institutions	34,021	-	34,021	-	-	-	34,021
Investment in sukuk	13,723	-	13,723	12,949	26,741	-	53,413
Financing receivables	-	3,204	3,204	-	-	-	3,204
Receivable from Ijara investors	-	5,525	5,525	-	-	-	5,525
Investment in equity securities	-	-	-	-	-	82,950	82,950
Investment in real estate	-	-	-	-	-	133,871	133,871
Other assets	4,073	-	-	-	-	-	4,073
<b>Total Funded Exposures</b>	<b>58,445</b>	<b>9,466</b>	<b>67,911</b>	<b>13,189</b>	<b>26,741</b>	<b>217,102</b>	<b>324,943</b>
<b>Unfunded exposure</b>							
Uncalled capital commitments in respect of investment	-	100	100	-	-	-	100
<b>Total Unfunded Exposures</b>	<b>-</b>	<b>100</b>	<b>100</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>100</b>

**4 RISK MANAGEMENT (continued)**

**4.2 Credit risk (continued)**

**Table – 10.1 Breakup of provision by industry for financing receivables exposures (PD-1.3.23(h & i)) and (PD-1.3.24(c))**

	<i>Banks and financial institutions</i> (USD '000)	<i>Real Estate</i> (USD '000)	<i>Sovereign</i> (USD '000)	<i>Energy</i> (USD '000)	<i>Others</i> (USD '000)	Total (USD '000)
Neither past due not impaired	-	-	-	-	-	-
Past due but not impaired	-	-	-	-	-	-
Individually impaired	-	5,644	-	-	-	5,644
Expected credit loss	-	(2,440)	-	-	-	(2,440)
<b>Total</b>	<b>-</b>	<b>3,204</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>3,204</b>

**Table – 10.2 Breakup of provision by geographical area for financing receivables exposures (PD-1.3.23(h & i)) and (PD-1.3.24(c))**

	<i>Middle East</i> (USD '000)	<i>Europe</i> (USD '000)	<i>Africa</i> (USD '000)	<i>North America</i> (USD '000)	<i>Others</i> (USD '000)	Total (USD '000)
<b>Expected Credit Losses:</b>						
Neither past due not impaired	-	-	-	-	-	-
Past due but not impaired	-	-	-	-	-	-
Individually impaired	5,644	-	-	-	-	5,644
Expected credit loss	(2,440)	-	-	-	-	(2,440)
<b>Total</b>	<b>3,204</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>3,204</b>

**Table – 10.3 Reconciliation of changes in provisions (PD-1.3.23(h & i)) and (PD-1.3.24(c))**

	Opening (USD '000)	Charged/ (reversed) during the period (USD '000)	Closing (USD '000)
<b>Expected Credit Losses:</b>			
Stage 1	-	-	-
Stage 2	-	-	-
Stage 3	120	2,320	2,440
<b>Total</b>	<b>120</b>	<b>2,320</b>	<b>2,440</b>

**Table – 10.4 Past due, impaired and restructured Islamic facilities**

There were no past due or restructured facilities as of 31 December 2018.



**4 RISK MANAGEMENT (continued)**

**4.2 Credit risk (continued)**

**Table – 11. Maturity Profile (PD–1.3.38)**

The maturity profile of the Group's assets and liabilities are based on contractual repayment arrangements. The contractual maturities of financial assets and liabilities have been determined on the basis of the remaining period at the financial position date to the contractual maturity date. For the remaining assets and liabilities, the maturity is determined based on expected realization/ profit settlement. The consolidated maturity profile at 31 December 2018 was as follows:

2018	<i>Up to 3 months (USD '000)</i>	<i>3 months to 1 year (USD '000)</i>	<i>Total up to 1 year (USD '000)</i>	<i>1 to 5 years (USD '000)</i>	<i>5 to 10 years (USD '000)</i>	<i>No fixed maturity (USD '000)</i>	<i>Total (USD '000)</i>
<b>Assets</b>							
Cash and balances with banks	6,628	-	6,628	-	-	-	<b>6,628</b>
Placements with financial institutions	34,021	-	34,021	-	-	-	<b>34,021</b>
Investment in sukuk	13,723	-	13,723	12,949	26,741	-	<b>53,413</b>
Financing receivables	-	3,204	3,204	-	-	-	<b>3,204</b>
Receivable from Ijarah investors	-	5,525	5,525	-	-	-	<b>5,525</b>
Investment in equity securities	-	-	-	-	-	82,950	<b>82,950</b>
Investment in real estate	-	-	-	-	-	133,871	<b>133,871</b>
Other assets	4,073	737	4,810	240	-	281	<b>5,331</b>
<b>Total assets</b>	<b>58,445</b>	<b>9,466</b>	<b>67,911</b>	<b>13,189</b>	<b>26,741</b>	<b>217,102</b>	<b>324,943</b>
<b>Liabilities</b>							
Financing liabilities	-	5,660	5,660	-	76,280	-	81,940
Other liabilities	1,801	2,565	4,366	-	-	991	5,357
<b>Total liabilities</b>	<b>1,801</b>	<b>8,225</b>	<b>10,026</b>	<b>-</b>	<b>76,280</b>	<b>991</b>	<b>87,297</b>
Commitments	-	100	100	-	-	-	100
<b>Net liquidity gap</b>	<b>56,644</b>	<b>1,141</b>	<b>57,785</b>	<b>13,189</b>	<b>(49,539)</b>	<b>216,111</b>	<b>237,546</b>
<b>Cumulative net liquidity gap</b>	<b>56,644</b>	<b>57,785</b>	<b>-</b>	<b>70,974</b>	<b>21,435</b>	<b>237,546</b>	<b>-</b>

#### 4 RISK MANAGEMENT (continued)

##### 4.3 Market risk

###### 4.3.1 Introduction

Market risk is defined as the risk of losses in on-balance sheet and off-balance-sheet positions arising from movements in market prices. The risks subject to this requirement are:

- The risks pertaining to profit rate related instruments and equities in the trading book; and
- Foreign exchange risk and commodities risk throughout the Bank.

The Group manages its market risk exposures by evaluating each new product and activity with respect to the market risk introduced by it.

###### 4.3.2 Market Risk Factor

For the Bank, market risk may arise from movements in foreign exchange rates. A single transaction or financial product may be subject to foreign exchange risk.

###### 4.3.3 Market Risk Strategy

The Board is responsible for approving and reviewing the market risk strategy. The Bank's senior management is responsible for implementing the market risk strategy approved by the Board, and continually enhancing the market policies and procedures for identifying, measuring, monitoring and controlling market risks.

In line with the Bank's Risk Management objectives and risk tolerance levels, the specific strategies for market risk management include:

- The Bank will proactively monitor and manage the market risk in its portfolio using a Board approved limit structure;
- The Bank will establish a market risk appetite which will be quantified in terms of a market risk limit structure for monitoring its market risk. This will be approved by the RC and the Board;
- The Bank will at all times hold sufficient capital in line with the Pillar I regulatory capital requirements of the CBB
- The Bank will carry out stress testing periodically to assess the effect of extreme movements in market variables which may expose the Bank to high risks;
- The Bank will clearly identify the foreign currencies in which it wishes to deal in. The Bank will manage its market risk in all foreign currencies in which it has significant exposure; and
- The Bank will manage its market risk exposure by evaluating each new product or activity with respect to the market risk introduced by it.

###### 4.3.4 Market Risk Measurement Methodology

The Group is not exposed to significant market risk due to the nature of its activities and hence uses measurements involving a combination of limits to control market risk exposures. The Board approves the overall market risk appetite and delegates responsibility for providing oversight on the Bank's market risk exposures and the sub allocation of Board limits to the ALCO. Risk Management is responsible for the market risk control framework and for monitoring compliance with the limit framework. The Group separates market risk exposures into either trading or non-trading portfolios. Trading portfolios primarily include positions arising from proprietary position-taking of Sukuks . Non-trading portfolios include positions that arise from the foreign exchange and other marked-to-market positions in financial assets designated as fair value through other comprehensive income statement. Market risk reports covering Trading Book risk exposures are report daily to the bank's senior management. The measurement techniques used to measure and control market risk include exposure and stop loss limits and stress tests.

For calculating the market risk capital charge, the Group applies the Standardized Approach.

###### 4.3.5 Market Risk Monitoring & Reporting and Limits Structure

The Bank uses a combination of limits to control its market risk exposures. Positions are monitored on a regular basis to ensure risk is maintained within established limits.

**Table – 12. Market Risk Capital Requirements**

The following table summarizes the capital requirement for each category of market risk as of:

	31 December 2018			
	Weighted risk exposures (USD '000)	Market risk capital requirement (USD '000)	Maximum value of RWE (USD '000)	Minimum value of RWE (USD '000)
Foreign exchange risk	16,443	2,055	23,088	16,443
Sukuk risk	10,387	1,299	19,077	10,387
<b>Total risk weighted exposures</b>	<b>26,830</b>	<b>3,354</b>		

As of 31 December 2018, the Group holds a portfolio of trading sukuks amounting to USD 13,723 thousand with a total gain of USD 362 thousand.

## 4 RISK MANAGEMENT (continued)

### 4.4 Operational risk

#### 4.4.1 Introduction

Operational risk is the risk of loss arising from inadequate or failed internal processes, people and systems or from external events, whether intentional, unintentional or natural. It is an inherent risk faced by all business and covers a large number of operational risk events including business interruption and systems failures, internal and external fraud, employment practices and workplace safety, customer and business practices, transaction execution and process management, and damage to physical assets.

The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

The Board has the ultimate responsibility for operational risk. Oversight rests with the RC, ICRC and RMD. Risk and Control Self Assessment ("RCSA") is an annual exercise as per Bank's policy and is a requirement by CBB based on Basel II principles related to operational risk management.

The Group has developed a Disaster Recovery and Business Continuity Plan ("DR&BCP") to enable the Group to survive a disaster and to re-establish normal business operations. The DR&BCP will enable the Group to minimize interruptions to business service operations, resume critical operations within a specified time after a disaster, minimize financial loss due to disruptions, limit the severity of the disruption, expedite the restoration of services and maintain a positive public image of the Bank.

#### 4.4.2 Sources of Operational Risk

The different sources of operational risks faced by the Bank can be classified broadly into the following categories:

**People Risk** which arise due to staffing inadequacy, unattractive remuneration structure, lack of staff training, lack in procedures for appointment, unhealthy professional working relationship and unethical environment;

**Processes Risk** which arise due to inadequate general controls, inadequate application controls, improper business and market practices and procedures, inappropriate or inadequate monitoring and reporting; and

**Systems (Technology) Risk** which arise due to the Integrity of information, hardware failures due to power surge, obsolescence, low quality and software failure due to unauthorized or incorrect modifications to software programs, computer virus, programming bug.

#### 4.4.3 Operational Risk Management Strategy

The Bank's Board is responsible for approving and reviewing (at least annually), the operational risk strategy and significant amendments to the operational risk policies. The Bank's senior management is responsible for implementing the operational risk strategy approved by the Board to identify, measure, monitor and control the risks faced by the Bank. The Bank continuously monitors the process and controls framework surrounding all business units to assess their effectiveness and efficiency.

As a strategy the Bank will identify the sources of operational risks in coordination with each business unit.

#### Management and Reporting of KRIs

The Bank plans to integrate the process of KRIs into the RCSA process and then start reporting KRIs to senior management.

#### Incident reporting

An incident is the occurrence of an operational risk event that has caused, or has the potential to cause a financial, reputation or regulatory impact on the Bank. It includes credit or market risk events, which have been caused by an operational risk event, and non-compliance with any legal or regulatory requirement, license, internal policy or procedure or code.

#### Operational Loss Database

The Operational Loss Database (OLD) is a key component to quantify past operational risk exposures. The OLD contains a subset of the information captured by the incident reporting process since all incidents involving an actual or potential financial impact (including near misses) is captured.

#### 4.4.4 Operational Risk Monitoring and Reporting

The internal monitoring and reporting process ensures a consistent approach for providing pertinent information to Senior Management and the RC for the quick detection and correction of deficiencies in the policies, processes and procedures for managing operational risk through ongoing, periodic reviews.

The objective of the reporting process is to ensure relevant information is provided to senior management and the Board to enable the proactive management of operational risk. The process ensures a consistent approach for providing information that enables appropriate decision making and action taking.

#### **4 RISK MANAGEMENT (continued)**

##### **4.4 Operational risk (continued)**

###### **4.4.5 Operational Risk Mitigation and Control**

Control activities are necessary to address the specific operational risks that the Bank has identified through the RCSA process. For the material risks identified by the Bank, the Bank decides whether to use procedures to control, mitigate, transfer, or accept the risks.

The Bank has several options for controlling and/or mitigating these risks:

- Decline to accept the risk (i.e. by avoiding certain business strategies or customers)
- Accept and retain the risk but introduce mitigating internal or external controls
- Accept the risk and transfer it in part or in whole.

###### **Key controls**

The Bank aims to control the operational risks it is exposed to by strengthening its internal controls, continuing its efforts to identify, assess, measure and monitor its risks, evolving in its risk management sophistication and promoting a strong control culture within the Bank.

Each business unit head is responsible for ensuring that the internal controls relevant to its operations are complied with on a day to day basis in spirit as well as in letter. The Bank will furthermore establish control processes and procedures and implement a system for ensuring compliance with these internal risk control processes and procedures.

###### **4.4.6 Disaster Recovery and Business Continuity Plan (“DR&BCP”)**

The Bank has developed a Disaster Recovery and Business Continuity Plan (“DR&BCP”) based on risk review of the banks activities. The Bank ensures that business recovery & contingency plans are reviewed and updated periodically.

In particular, the DR&BCP will satisfy the following:

- it will cover incidents related to IT, communication and premises;
- testing will include critical business processes; and
- testing will cover critical types of plausible scenarios to which the Bank may be vulnerable.

#### 4 RISK MANAGEMENT (continued)

##### 4.5 Equity price risk

###### 4.5.1 Equity price risk management

Equity price risk is the risk that the fair value of equity investments decreases as a result of fluctuations in the respective stock market indices. The Group has investments at fair value through income statement and fair value through equity quoted on stock exchanges. Based on the values at 31 December 2018, a change in the quoted price of plus or minus 5% would change the value of these investments by plus or minus US\$ 284 thousand (2017: US\$ 251 thousand) with a corresponding increase or decrease in equity, except in case of impairment which will result in loss being taken to consolidated statement of income.

The accounting policies, including valuation methodologies and their related key assumptions, are disclosed in the consolidated financial statements.

An assessment is made at each year-end to determine whether there is any objective evidence that equity investments may be impaired. Any impairment for significant and prolonged decline in the value of investments is reflected as a write down of investments. Any subsequent increase in their fair value is recognized directly in equity. Investments are managed within maximum concentration risk limits, approved by the Board of Directors of the Bank.

###### Table – 13. Equity Position Risk in the Banking Book (PD-1.3.31(b), (c) & (f))

The following table summarizes the total and average gross exposure of equity based financing structures by types of financing contracts and investments as of 31 December 2018:

	<b>Total gross exposure (USD '000)</b>	<b>* Average gross exposure over the period (USD '000)</b>	<b>Publicly Traded (USD '000)</b>	<b>Privately held (USD '000)</b>	<b>Capital requirement (USD '000)</b>
Fair value through income statement	18,993	27,423	-	18,993	2,374
Fair value through equity	63,957	63,947	5,682	58,275	7,995
Investment in equity-accounted investees	-	306	-	-	-
	<b>82,950</b>	<b>91,676</b>	<b>5,682</b>	<b>77,268</b>	<b>10,369</b>

\*Average balances are computed based on quarter-end balances.

###### Table – 14. Equity gains or losses in the Banking Book (PD-1.3.31(d) to (e))

The following table summarizes the cumulative realized gains / (losses) during the year ended:

	<b>31 December 2018 USD ('000)</b>
Realized gains/(losses) arising from sale of equity type sukuk (non-trading)	9

#### 4 RISK MANAGEMENT (continued)

##### 4.6 Rate of return risk

###### 4.6.1 Rate of return risk management

Profit rate risk is the potential impact of the mismatch between the rate of return on assets and the expected rate of return of the sources of finance. The table below analyses the Group's profit rate risk exposure financial assets and liabilities. The Group's assets and liabilities are included at carrying amount and categorised based on contractual repayment arrangements:

**Table – 15. Rate of Return Risk**

2018	Up to 3 Months (USD '000)	3 months to 1 year (USD '000)	1 to 5 years (USD '000)	Above 5 Years (USD '000)	Total (USD '000)
<b>Assets</b>					
Placements with financial institutions	34,021	-	-	-	<b>34,021</b>
Investment in sukuk	13,723	-	12,949	26,741	<b>53,413</b>
Financing receivable	-	3,204	-	-	<b>3,204</b>
<b>Total profit rate sensitive assets</b>	<b>47,744</b>	<b>3,204</b>	<b>12,949</b>	<b>26,741</b>	<b>90,638</b>
<b>Liabilities</b>					
Financing liabilities	-	5,660	-	76,280	<b>81,940</b>
<b>Total profit rate sensitive liabilities</b>	<b>-</b>	<b>5,660</b>	<b>-</b>	<b>76,280</b>	<b>81,940</b>
<b>Profit rate sensitivity gap</b>	<b>47,744</b>	<b>(2,456)</b>	<b>12,949</b>	<b>(49,539)</b>	<b>8,698</b>

The sensitivity of the Group's consolidated statement of income to a 200 basis points parallel increase (decrease) in market profit rates (assuming no asymmetrical movement in yield curves and a constant statement of financial position) on floating rate financial assets and liabilities, would be an increase (decrease) of profit by US\$ 174 thousand (2017:US\$ 75 thousand).

The rate of return risk is generally associated with overall balance sheet exposures where mismatches arise between assets and balances from fund providers. The Group is not exposed to any significant rate of return risk and is aware of the factors that give rise to rate of return risk. Factors that possibly will affect rate of return may include an increase in long-term fixed rates in the market. The Bank is also aware of the fact that in general, profit rates earned on assets reflect the benchmark of the previous period and do not correspond immediately to changes in increased benchmark rates.

The Bank uses a combination of mismatch gap limits to measure and control its rate of return risk. Mismatched positions are regularly monitored to ensure that mismatch is maintained within established limits.

Displaced commercial risk ("DCR") refers to the market pressure to pay returns that exceed the rate that has been earned on the assets financed by the liabilities, when the return on assets is under performing as compared with competitor's rates.

The Bank's DCR is limited as bank mainly depends on its equity to fund assets. In case DCR arises in some situation the Bank will forego its fee based on executive management decision and on case to case basis.

#### **4 RISK MANAGEMENT (continued)**

##### **4.7 Liquidity risk**

###### **4.7.1 Introduction**

Liquidity risk is the risk that the Group will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

The main action to manage the Group's liquidity is through the adherence to limits on liquidity mismatches. These include the limits of the cumulative excess of maturing liabilities over assets in the short-term and limits on dependence on short-dated funds.

Treasury department is overall responsible for ensuring that the limits enacted are adhered to, on a day-to-day basis and managing excess liquidity of the Group through short term placements and investments. Treasury maintains a constant communication with the banks. The Treasury provides a monthly report to the ALCO regarding the market conditions and the volatilities of the asset prices and as such the exogenous liquidity risk the Group is exposed to.

###### **4.7.2 Sources of Liquidity Risk**

Broadly, sources of liquidity risk can be listed as:

**Funding Risk** – Inability to replace net outflows due to unanticipated withdrawal of capital or deposits;

**Call Risk** – Crystallization of a contingent liability; and

**Event Risk** – Rating downgrades or other negative news leading to a loss of market confidence in the Bank.

Liquidity risk may also arise if certain inter-bank funding lines are withdrawn or assets do not realize cash as expected and when anticipated.

###### **4.7.3 Liquidity Risk Strategy**

The Board is overall responsible for approving and reviewing (at least annually), the liquidity risk strategy and significant amendments to the liquidity risk policies. The Bank's senior management is responsible for implementing the liquidity risk strategy to identify, measure, monitor and control the risks faced by the Bank.

The Bank monitors the liquidity positions by comparing maturing assets and liabilities in different time buckets.

To mitigate the liquidity risk, the Group works with diversified funding sources, manages its assets with liquidity in mind and closely monitors periodic cash forecasts which take into account the Group's maturity profile.

#### 4 RISK MANAGEMENT (continued)

##### 4.7 Liquidity risk (continued)

###### 4.7.4 Liquidity Risk Measurement Tools

The Bank has developed risk management policies and procedures including liquidity risk management framework. The Bank will use a combination of techniques for measurement of its liquidity risk. These would include Liquidity Gap Analysis and monitoring of liquidity ratios.

###### Table – 16. Liquidity ratios (PD-1.3.37)

The following table summarizes the liquidity ratios as of:

	<b>31 December 2018</b>
Liquid assets to total assets	<b>17.90%</b>
Short term assets to short term liabilities	<b>677.35%</b>

Formula is as follows:

Liquid Assets to total assets = (Cash and bank balances + Quoted sukuks non-trading at market value + Quoted sukuks held for trading)/total assets

Short term assets to short term liabilities = Assets with up to one year maturity/liabilities with up to one year maturity

###### Table – 17. Quantitative indicators of financial performance and position (PD–1.3.9b)

	<i>Dec</i> <b>2018</b>	<i>Dec</i> <b>2017</b>	<i>Dec</i> <b>2016</b>	<i>Dec</i> <b>2015</b>	<i>Dec</i> <b>2014</b>
Return on average total equity (ROAE)	<b>-9.36%</b>	0.41%	-17.50%	-4.62%	-4.75%
Return on average total assets (ROAA)	<b>-6.53%</b>	0.27%	-10.88%	-3.14%	-3.90%
Total operating cost to Income ratio	<b>132.48%</b>	83.20%	64.38%	60.14%	96.08%

Formula is as follows:

ROAE = Net Income (Loss) /Average Total Equity

ROAA= Net profit (Loss) / Average Total Assets

Operating cost= Total expenses excluding fair value changes and impairment allowances.

###### 4.7.5 Bank's Financial Performance (PD-1.3.9 (a))

The global economy witnessed a challenging 2018 as rising interest rates, volatile political environment, increased protectionism and an appreciating US dollar affected global markets and trade. Amidst all this, the world economy still grew by 3.9% over the year. The trade war between China and the United States threatens to disrupt the growth momentum while the ensuing political uncertainty regarding Brexit continues to cast a cloud over UK's economic outlook.

Ibdar reported total revenues of USD 11.3 million for the year, a decrease of 34% from USD 17.1 million in 2017. Loss before fair value changes and impairment allowances reached USD 3.7 million compared to a profit of USD 2.9 million in 2017. The net loss for the year was USD 22.6 million compared to a net profit of USD 1 million in 2017. Impairment and fair value changes for 2018 amounted to USD 18.9 million compared to USD 2 million in 2017. The total asset base decreased by 11% reaching USD 324.9 million by year end. The decrease in the total asset base can be explained mainly due to sale of held to maturity and held for trading sukuks.

#### 5 LEGAL CONTINGENCIES (PD-1.3.31)

The Bank has outsourced the legal function to be handled by a legal firm in Bahrain. The firm has allocated a permanent legal counsel to the bank who is consulted on all major activities conducted by the Bank. All contracts, documents, etc have to be reviewed by the legal counsel as well. The legal counsel liaises with external lawyers for legal cases filed by any party against the bank.

There are 3 claims filed against the bank by a former Board of director and an ex-employee in addition to claims raised by some investors who invested in a legacy investment pre-merger. The bank has raised claims against Investment Company in Bahrain and number of individuals'. All legal cases are handled by legal firms in Bahrain and supervised by our legal counsel.



## 6 CORPORATE GOVERNANCE AND TRANSPARENCY

The Bank is committed to adopting the best international standards and global leading practices in corporate governance. The Bank has established a strong corporate governance framework that is designed to protect the interests of all stakeholders, ensure compliance with regulatory requirements, and enhance organisational efficiency.

The Bank has established a concrete organisational structure that clearly segregates functions and responsibilities, and reflects a division of roles and responsibilities of the Board of Directors and Management. Clear mandates exist for the Board, Chairman of the Board, Board Committees, Chief Executive Officer, the Management, and Senior Management Committees.

The Bank has only one class of equity shares and the shareholders are from the following nationalities (PD-1.3.10(i)):

<b>Country</b>	<b>Percentage</b>
1- State of Kuwait	50.52%
2- Kingdom of Bahrain	23.44%
3- Kingdom of Saudi Arabia	15.06%
4- Qatar	4.71%
5- United Arab Emirates	4.00%
6- Oman	2.03%
7- Jordan	0.13%
8- Yemen	0.05%
9- Philippines	0.02%
10- Sri Lanka	0.01%
11- Canada	0.01%
12- United Kingdom	0.01%
13- India	0.01%

The distribution of ownership of shares by size of shareholder is provided below (PD-1.3.10(l)):

<b>Size</b>	<b>No. of</b>
More than 10%	1
5 - 10 %	1
1 - 5 %	18
Less than 1 %	217
	<b>237</b>

### 6.1 Board Members' Profile

The primary responsibility of the Board is to provide effective governance over the Bank's affairs and promote and achieve sustainable performance that has long-term growth potential for the benefit of its shareholders. The Board also has the duty of balancing interest of all its stakeholders, including its clientele, business partners, correspondents, employees, suppliers and local communities, all the time maintaining standards of transparency and accountability.

In all actions taken by the Board, the Directors are expected to exercise their business judgment in what they reasonably believe to be in the Bank's best interest. In discharging this obligation, they may rely on the professional integrity of the Bank's Senior Executives, as well as its external advisors and auditors. The Board of directors members are:

6 Corporate Governance and Transparency (continued)

6.1 Board Members' Profile (continued)

Table – 18. Corporate Governance and Transparency – Board Members' Profile (PD-1.3.10(b,c,q))

Ibdar's Board of Directors consists of 10 members as of December 31, 2018.

The following table summarizes the information about the profession, business title, experience in years, start date and the qualifications of the current Board members;

Name of Board Member	Profession	Business Title	Executive / Non Executive Independent / Non Independent	Experience in years	Start date & term	Qualification
Tareq Sadeq	Financial Consultant	Managing Director - Keystone Consulting Inc WLL, Board member in Bahrain International Golf Course Company BSC, Board member of Al Zayani Investments BSC and Board member of Ahli United Bank - Kuwait	Independent	Over 39	3 years from 28 April 2016	Chartered Accountant - The Institute of Chartered Accountants in England and Wales
Abdulkarim Bucheery	Banker	Board Member of Bahrain Credit Facilities Co. (BCFC) and Chairman of Bahrain Bourse	Independent	Over 42	3 years from 28 April 2016	BSc - Economic Sciences from Aleppo University in Syria
Abdulaziz Al Afaleq	Mechanical Engineer	Partner, Board Member and Group CEO - Al-Kifah Holding Company	Independent	Over 17	3 years from 28 April 2016	EMBA - King Fahad University of Petroleum and Minerals. Bachelor degree in Mechanical Engineering.
Ebrahim Al Jassmi	Banker	Board member of Bahrain Islamic Bank and Takaful International Company	Independent	Over 37	3 years from 28 April 2016	B.S degree in Economics from the University of Kuwait and an MBA from the University of Bahrain.
Hamad Al Sejari	Banker	Assistant Vice President of KFH Capital Investment Company	Executive	Over 14	3 years from 28 April 2016	Bachelors in Civil Engineering with a minor in Business Administration from Old Dominion University, USA.
Jamal Abdulla Al Saleem	Banker	Board member of Kuwait Investment Company, Executive Vice President in Privatization Holding Company - Kuwait and Vice Chairman of Kingdom Electricity Company - Jordan	Non-Executive	Over 29	3 years from 28 April 2016	Bachelors degree in Accounting from University of Kuwait, and an MSc degree in Accounting achieved with highest honors from Oklahoma City University, USA,heastern University
Jassem Al Yaseen	Banker	Executive Manager of the Treasury Sales Desk at Kuwait Finance House	Executive	Over 28	3 years from 28 April 2016	Bachelor's Degree in Industrial Engineering from the University of Miami, USA.
Khalid Al Maarafi	Banker	Executive Manager and Head of the Retail Banking Group at Kuwait Finance House-Bahrain, Chairman of Al Enma'a House for Real Estate and Board member of Family Bank and Baytik Industrial Investment Company	Executive	Over 35	3 years from 28 April 2016	Bachelor's in Accounting from the University of Bahrain, and is a Certified Public Accountant (CPA).
Mohamed Noorudin	Banker	Chairman of Newbury Investments W.L.L. - Bahrain, board member at Tadamun Capital - Bahrain and a board member at Itqan Capital - Jeddah	Independent	Over 32	3 years from 28 April 2016	Bachelors in Business Administration from University of Bahrain
Dr. Mohamed Kameshki	Business Consultant	Chairman of Mawteni Trading Company W.L.L., Vice chairman of the board of Saleh Abdulla Kameshki & Sons B.S.C. and board member of Aluminum Bahrain (ALBA).	Independent	Over 26	2 years from 11 May 2017	B.Sc. (Honours) in Engineering from Staffordshire University, M.Sc. In Management Science & Operational Research from Warwick University Business School and a Ph.D. in Business Management (New Product Development) from Loughborough University Business School.

**6 Corporate Governance and Transparency (continued)**

**6.1 Board Members' Profile (continued)**

The Board shall meet on a quarterly basis, or otherwise at least four times in every financial year. During the year ended 31 December 2018, 8 Board meetings were held. The following table summarizes the information about Board of Directors meeting dates and attendance of directors at each meeting;

**Table – 19. Corporate Governance and Transparency – Board of Directors meetings in 2018 (PD-1.3.10(w))**

Date	Names of Directors Present (Physical)	Names of Directors who participated by phone/video link	Names of Directors not Present
22-Feb-18	Tareq Sadeq (Chairman) Abdulkarim Bucheery (Vice Chairman) Abdulaziz Al Afaleq Hamad Al Sejari Mohamed Nooruddin Khalid Al Maarafi Ebrahim Al Jassmi Dr. Mohamed Kameshki Jamal Al Saleem	NA	Jassem Al Yaseen
02-Apr-18	Tareq Sadeq (Chairman) Abdulkarim Bucheery (Vice Chairman) Abdulaziz Al Afaleq Hamad Al Sejari Mohamed Nooruddin Jassem Al Yaseen Khalid Al Maarafi Dr. Mohamed Kameshki Jamal Al Saleem	Ebrahim Al Jassmi	NA
17-Apr-18	Tareq Sadeq (Chairman) Abdulkarim Bucheery (Vice Chairman) Abdulaziz Al Afaleq Hamad Al Sejari Mohamed Nooruddin Jassem Al Yaseen Khalid Al Maarafi Ebrahim Al Jassmi Dr. Mohamed Kameshki Jamal Al Saleem	NA	NA
04-Jun-18	Tareq Sadeq (Chairman) Abdulkarim Bucheery (Vice Chairman) Abdulaziz Al Afaleq Hamad Al Sejari Mohamed Nooruddin Jassem Al Yaseen Khalid Al Maarafi Ebrahim Al Jassmi Dr. Mohamed Kameshki Jamal Al Saleem	NA	NA
09-Aug-18	Tareq Sadeq (Chairman) Abdulkarim Bucheery (Vice Chairman) Hamad Al Sejari Jassem Al Yaseen Khalid Al Maarafi Dr. Mohamed Kameshki Jamal Al Saleem	Abdulaziz Al Afaleq Mohamed Nooruddin Ebrahim Al Jassmi	NA
25-Sep-18	Tareq Sadeq (Chairman) Abdulkarim Bucheery (Vice Chairman) Abdulaziz Al Afaleq Hamad Al Sejari Mohamed Nooruddin Jassem Al Yaseen Khalid Al Maarafi Ebrahim Al Jassmi Dr. Mohamed Kameshki Jamal Al Saleem	NA	NA
01-Nov-18	Tareq Sadeq (Chairman) Abdulkarim Bucheery (Vice Chairman) Abdulaziz Al Afaleq Hamad Al Sejari Mohamed Nooruddin Jassem Al Yaseen Khalid Al Maarafi Ebrahim Al Jassmi Dr. Mohamed Kameshki	NA	Jamal Al Saleem
05-Dec-18	Tareq Sadeq (Chairman) Abdulkarim Bucheery (Vice Chairman) Abdulaziz Al Afaleq Hamad Al Sejari Mohamed Nooruddin Jassem Al Yaseen Khalid Al Maarafi Ebrahim Al Jassmi Dr. Mohamed Kameshki Jamal Al Saleem	NA	NA

**6 Corporate Governance and Transparency (continued)**

**6.2 Changes in Board Structure**

The following table presents the directorships held by the directors in other boards:

**Table – 20. Information on the directorships held by the directors on other boards**

Name of Board Member	Directorship in other companies - based outside Bahrain	Directorship in other companies - based in Bahrain
Tareq Sadeq	Ahli United Bank, Egypt	Keystone Consulting Inc WLL Al Zayani Investments - Bahrain Bahrain International Golf Course Company
Abdulkarim Bucheery	-	Bahrain Credit Facilities Co. (BCFC) Bahrain Bourse
Abdulaziz Al Afaleq	Al-Kifah Holding Company Saudi Arabia	-
Ebrahim Al Jassmi	-	Bahrain Islamic Bank Takaful International company
Hamad Al Sejari	-	-
Jamal Al Saleem	Kuwait Investment Company, Kuwait Kingdom Electricity Company, Jordan Privatization Holding Company, Kuwait	-
Jasem Al Yaseen	-	-
Khalid Al Maarafi	-	Al Enma House for Real Estate Family Bank Baytik Industrial Investment Company
Mohamed Nooruddin	Itqan Capital - Saudi Arabia	Newbury Investments Tadhamon Capital
Dr. Mohamed Kameshki	-	Mawteni Trading Company W.L.L. Saleh Abdulla Kameshki & Sons B.S.C. Aluminum Bahrain (ALBA)

**6.2.1 Auditors' Appointment**

During the year, the shareholders at the AGM reappointed KPMG Fakhro as the external auditors of the bank for 2019.

**6 Corporate governance and transparency (continued)**

**6.3 Board Committees**

The following tables summarise the information about Board Committee meeting dates and attendance of directors at each meeting;

**Table – 21. Corporate Governance and Transparency – Audit, Risk & Compliance Committee meetings in 2018 (PD-1.3.10(w))**

Date	Names of Directors Present (Physical)	Names of Directors who participated by phone/video link	Names of Directors not Present
11-Feb-18	Dr. Mohamed Kameshki (Chairman) Abdulaziz Al Afaleq Khalid Al Maarafi	NA	NA
14-Feb-18	Dr. Mohamed Kameshki (Chairman) Abdulaziz Al Afaleq Khalid Al Maarafi	NA	NA
27-Mar-18	Dr. Mohamed Kameshki (Chairman) Abdulaziz Al Afaleq Khalid Al Maarafi	NA	NA
08-Apr-18	Dr. Mohamed Kameshki (Chairman) Abdulaziz Al Afaleq Khalid Al Maarafi	NA	NA
02-May-18	Dr. Mohamed Kameshki (Chairman) Abdulaziz Al Afaleq Khalid Al Maarafi	NA	NA
29-Jul-18	Dr. Mohamed Kameshki (Chairman) Abdulaziz Al Afaleq Khalid Al Maarafi	NA	NA
29-Oct-18	Dr. Mohamed Kameshki (Chairman) Abdulaziz Al Afaleq Khalid Al Maarafi	NA	NA

**Table – 22. Corporate Governance and Transparency – Executive Committee meetings in 2018 (PD-1.3.10(w))**

Date	Names of Directors Present (Physical)	Names of Directors who participated by phone/video link	Names of Directors not Present
21-Feb-18	Abdulkarim Bucheery (Chairman) Hamad Al Sejari Jassem Al Yaseen Ebrahim Al Jassmi	NA	NA
4-Jul-18	Abdulkarim Bucheery (Chairman) Hamad Al Sejari Jassem Al Yaseen Ebrahim Al Jassmi	NA	NA
24-Sep-18	Abdulkarim Bucheery (Chairman) Hamad Al Sejari Jassem Al Yaseen Ebrahim Al Jassmi	NA	NA
21-Nov-18	Abdulkarim Bucheery (Chairman) Hamad Al Sejari Jassem Al Yaseen Ebrahim Al Jassmi	NA	NA

**6 Corporate governance and transparency (continued)**

**6.3 Board Committees (continued)**

**Table – 23. Corporate Governance and Transparency – Nomination, Remuneration and Governance Committee meetings in 2018 (PD-1.3.10(w))**

Date	Names of Directors Present (Physical)	Names of Directors who participated by phone/video link	Names of Directors not Present
04-Jan-18	Tareq Sadeq (Chairman) Mohamed Nooruddin Jamal Al Saleem	NA	NA
13-Feb-18	Tareq Sadeq (Chairman) Mohamed Nooruddin Jamal Al Saleem	NA	NA
01-Mar-18	Tareq Sadeq (Chairman) Mohamed Nooruddin Jamal Al Saleem	NA	NA
07-Oct-18	Tareq Sadeq (Chairman) Mohamed Nooruddin Jamal Al Saleem	NA	NA
04-Dec-18	Tareq Sadeq (Chairman) Mohamed Nooruddin Jamal Al Saleem	NA	NA
13-Dec-18	Tareq Sadeq (Chairman) Mohamed Nooruddin Jamal Al Saleem	NA	NA

**6.4 Changes in the Corporate Governance Structures (PD-1.3.10(g))**

There has been no changes in the Corporate Governance Structure as of 31 December 2018.

**6.5 Remuneration Policy and Aggregate Remuneration Paid to Senior Management and Board (PD-1.3.10(d, ii, jj and kk))**

The Bank's remuneration policy for Senior Management is to provide competitive remuneration structure to attract and retain highly skilled personnel.

Aggregate remuneration paid to senior management during 2018 was USD 1,711 thousand (2017 USD 2,486 thousand). This includes salaries, allowances and other benefits paid for the year ended 31 December 2018. Bonuses for the year of 2018 are not included in the calculation of aggregate remuneration as the bonus allocation has not been finalized yet.

The Bank's remuneration policy for Board and Shariah Members is to appropriately compensate and remunerate board members for their active participation in board meetings. Based on this policy the Board of Directors remuneration was structured to comprise the following:

- Annual Contractual Remuneration
- Attendance fees for members attending Board and sub-committee meetings
- Daily Allowance
- First class air tickets

Remuneration of USD of 500 thousand was accrued for 2018. Payment is subject to approval of Minister of Commerce and shareholders in the AGM (Refer to note 19 in the consolidated financial statements).

**6.6 A. Ownership of Shares by government (PD-1.3.10(m))**

Name of Government Authority	Country	No. of Shares	%
Social Insurance	Kingdom of Bahrain	3,645,635	1.565%
The Public Authority for Minor Affairs	State of Kuwait	1,275,968	0.548%
Awqaf Public Foundation	State of Kuwait	1,275,968	0.548%
Directorate of Minors Affairs	Kingdom of Bahrain	201,840	0.087%

**B. Directors' and Senior Managers' trading of the bank's shares during the year (PD-6.1.1 (c)) / (PD-1.3.10 (j))**

Not applicable as the shares are not listed.

**6.7 Ownership of Shares by Directors / Senior Managers (PD-1.3.10(k)) / (PD-6.1.1 (b))**

The current Board in their individual capacity or Senior Management do not have any shares in the Bank.

## 6 Corporate governance and transparency (continued)

### 6.8 Type of Material Transactions that require Board approval (PD-1.3.10(o))

The following types of material transactions require Board approval if suggested by the approved policies:

- (a) Conclude loan agreements with certain limit;
- (b) Sell the company's assets;
- (c) Mortgage the Company's properties;
- (d) Grant guarantees to third parties;
- (e) Discharge the Company's debts; and
- (f) Engage in any other acts which may be integral to the company's objects as set out in the Memorandum of Association.
- (g) All related party transactions.

### 6.9 Induction, Education and Orientation of New Directors (PD-1.3.10(r))

All new Directors participate in an orientation exercise that is administered by the Directors and members of the Management at Ibdar. This orientation includes presentations by the Chairman and senior management to familiarize new Directors with Ibdar's strategic plans, significant financial, accounting and risk management issues, compliance programs, the Code of Conduct, its principal officers, and internal and independent auditors.

In addition, the orientation includes visits to Ibdar headquarters and, to the extent practical, Ibdar's significant investments. It is emphasized that Directors stay up-to date in relation to matters relevant to the Bank, the industry and the particular areas of expertise for which they have been invited on to the BOD in the first place. In particular the induction/orientation process will aim for a Director to have:

- (a) An appropriate level of knowledge of the industry Ibdar operates in.
- (b) A clear understanding of Ibdar's business operations.
- (c) A clear understanding of Ibdar's financial circumstances.
- (d) A clear understanding of Ibdar's strategy and direction.
- (e) A high level knowledge of the business risks that may affect its success.
- (f) Access to relevant background information on key employees and the other members of the BOD.
- (g) In addition, new Directors are provided an Induction Package

The process of director induction is critical to having the new directors effectively and efficiently contributing to the Board of Directors. As part of this process, specifically, the new director shall:

- (a) Be welcomed formally by the Chairman of the Board, who shall brief him generally on the Bank, the Board, the other directors, and the culture and operation of the Board.
- (b) Meet with the Chief Executive Officer onsite at the Bank office to discuss the Bank strategy and plan and be introduced to key management staff.
- (c) Be briefed on the history and legacy of the Bank and its key shareholders, clients, and partners by the Chief Executive Officer or other member of Senior Management.
- (d) Be briefed by the Board Secretary on the general operations of the Board.
- (e) Be provided all of the pertinent documentation, including but not limited to:
  - i. Applicable laws and regulations, including the Commercial Companies Law, the CBB Rulebook and regulations
  - ii. The Memorandum and Articles of Association
  - iii. The Corporate Governance Manual
  - iv. Organization Chart
  - v. Business Plan
  - vi. Schedule for Upcoming Board and Committee Meetings
  - vii. The Board Minutes for the last 12 months (including the audio recording of the last meeting, if available)
  - viii. The Board Packs for the last 12 months
  - ix. The Board Committee Minutes for the respective committee he will be appointed to for the last 12 months (including the audio recording of the last meeting, if available)
  - x. The Annual Reports for the last 2 years
  - xi. The Quarterly Financials for the last 12 months
- (f) Be provided any other documentation on the Bank, its products, services, market or competition, upon his request.
- (g) Be afforded the opportunity to meet with any staff, consultants, or advisors, including the external auditor, upon his request.

**6 Corporate governance and transparency (continued)**

**6.10 Executive Members' Profile**

Delegated by the Board with the authority for managing the Bank's operations, the Executive Management Team of the Bank are responsible for implementing decisions, policies, procedures, and strategies approved by the Board of Directors.

**Table – 24. Corporate Governance and Transparency – Executive Members' Profile (PD-1.3.10(b))**

The Bank does not permit the recruitment of family members of an Employee as per the family recruitment policies, however such recruitment is permissible in exceptional circumstances with approval from Chairman / CEO required based on degree of relationship with the family member. The following table summarises the information about the profession, business title, experience in years and the qualifications of each Executive member;

Name of Executive Member	Department	Business Title	Experience in year	Qualification
<b>Abdulkarim Bucheery (1)</b>	Acting Chief Executive Officer	A/CEO	Over 42	BSc - Economic Sciences from Aleppo University in Syria
<b>Ahmed Mustafa</b>	Chief Financial Officer	CFO	Over 18	Bachelors in Commerce majoring in Accounting from Helwan University in Egypt and is a Certified Public Accountant (CPA).
<b>Aysha Aljalahma</b>	Compliance & MLRO	Director	Over 14	Bachelors of Science in Accounting from the University of Bahrain and a Master of Science in International Finance from the University of Westminster, UK.
<b>Farrukh Zareef</b>	Risk Management	Director	Over 20	Associate Member of Institute of Chartered Accountant of Pakistan (ICAP)
<b>Abdulla Nima Najem</b>	Shari'ah Supervision & Advisory	Director	Over 27	Bachelor Degree in Chemical Engineering, – University of Bahrain, Advanced Diploma in Islamic Baking – BIBF, Advanced Diploma in Islamic Commercial Jurisprudence, Jordan & BIBF, High Diploma in Education – University of Bahrain, and High Diploma in Distance Teaching & Training– Arabian Gulf University, Bahrain. He is also Certified Islamic Professional Accountant (CIPA) – AAOIFI, Certified Shari'ah Advisor and Auditor (CSAA)- AAOIFI, Shari'ah Reviewer (CBB Waqf Program), and Certified Anti-Money Laundering & Compliance Officer , FINRA , ICMA & University of Reading. Prior to joining Ibdar, Abdullah served at Gulf Finance House and the University of Bahrain
<b>Bassam Sami Awdi</b>	Internal Audit	Director	Over 20	Executive Master in Business Administration and he is a Certified Public Accountant
<b>Nader AlQassab</b>	Post-Acquisition	Director	Over 18	Master of Business Administration from University of Strathclyde, Glasgow – Scotland. He is also a Chartered Fund and Asset Manager
<b>Sama Al Alawi</b>	Human Resources	Director	Over 27	Master of Science in Human Resources. Chartered Institute of Personnel and Development (level 5). Six Sigma Certificate and Six Sigma Black Belt holder
<b>Nada Kazerooni</b>	Capital Markets, Treasury & Asset Management	Director	Over 17	MBA from Strathclyde University, Scotland, and a BSc in Civil Engineering from Northeastern University, Boston-USA.



**6 Corporate governance and transparency (continued)**

**6.10 Executive Members' Profile (Continued)**

**Table – 24. Corporate Governance and Transparency – Executive Members' Profile (PD-1.3.10(b)) (Continued)**

Name of Executive Member	Department	Business Title	Experience in year	Qualification
<b>Ayman Sejiny (2)</b>	Chief Executive Officer	CEO	Over 26	BA in Finance from Eastern Michigan University, United States.
<b>Ikbal Daredia (3)</b>	Capital Markets, Treasury & Asset Management	Senior Executive Director	Over 36	Associate of the Chartered Institute of Bankers (ACIB) and holds Financial Planning Certificate from London's Chartered Insurance Institute.
<b>Hussain Jamsheer (4)</b>	Investor Relations	Executive Director	Over 23	Masters in Finance from Sheffield Halam University in the UK, a Diploma in Treasury & Capital Markets, and an ACCA Certified Diploma in Accounting & Finance.
<b>Yasser Abbady (5)</b>	Investor Relations - Advisory	Executive Director	Over 21	CFA charter holder
<b>Khalid Javaid (6)</b>	Legal & Board Secretary	Executive Director	Over 21	Diploma in UK Legal Practice, a BSc (Hons) in Quantitative Economics from the City of London University, and a Postgraduate Diploma in Law from the University of Thames Valley.
<b>Bassam Kameshki (7)</b>	Real Estate	Director	Over 15	BSc degree in Civil Engineering from University of Bahrain, Certified Development Manager from George Washington University and MBA with Merit from University of Strathclyde, Scotland.
<b>Hella Fakhro (8)</b>	Aviation & Alternative Investments	Director	Over 13	Bachelor's degree from Brown University and a Master's degree from New York University
<b>Victoria McFarlane (9)</b>	Corporate Communications	Director	Over 22	Masters Degree in Leadership and Change Management from the York St. John University, UK.

(1) Abdulkarim Bucheery has been appointed as Acting CEO effective [09 September 2018]

(2) Ayman Sejiny was terminated from the bank effective [02 September 2018]

(3) Ikbal Daredia was terminated from the bank effective [06 December 2018]

(4) Hussain Jamsheer resigned from the bank effective [31 December 2018]

(5) Yasser Abbady resigned from the bank effective [06 December 2018]

(6) Khalid Javaid was terminated from the bank effective [31 July 2018]

(7) Bassam Kameshki resigned from the bank effective [31 July 2018]

(8) Hella Fakhro resigned from the bank effective [26 August 2018]

(9) Victoria McFarlane resigned from the bank effective [02 January 2019]

## **6 Corporate governance and transparency (continued)**

### **6.11 Bank's Performance Linked Incentive Structure (PD-1.3.10(d))**

The remuneration & incentive structure of the Board Members and Shari'ah Members is discussed at the Board level. Remuneration of Board Members is approved in the Annual General Meeting ("AGM"). Bonuses are based on Bank's performance, division or department performance and individual staff performance. The board approves all performance bonus schemes for staff.

### **6.12 Related Party Transactions (PD-1.3.10(f))**

Related party transactions are governed by the Group corporate governance policy. All related party transactions were concluded at arm's length.

Where the Bank proposes to enter into a related party transaction the following procedures apply:

- 1- The relevant responsible officer involved in the transaction makes appropriate disclosure to the Compliance Officer of the bank. The Compliance Officer will review the transaction and send his/her comments to the Investment, Credit & Risk Committee about the proposed transaction. This disclosure should include the following:
  - (a) Details of the proposed transaction;
  - (b) Proposed transaction parties and how they are related;
  - (c) How arm's length may be evidenced
- 2- The committee will consider the information provided in order to determine whether and how to proceed with the proposed transaction. The committee may confer with risk management and legal department or may take external legal advice, in reaching this determination.
- 3- The Committee shall review the material facts of the transactions that require the Committee's approval and either approve or disapprove of the entry into the related party transaction.

For related party transaction and balances, please refer note 24 of the consolidated financial statements.

All related party transactions are approved by the Board of Directors and a statement is provided to the shareholders in the AGM.

### **6.13 Assessment of Board of Directors Effectiveness & Contribution (PD-1.3.10(aa))**

The Board and the management of the Bank are committed to the highest standards of corporate governance and risk management, therefore the Bank has developed a methodology which incorporates a process to self-assess the performance of the Board by the Board members on ongoing basis. This methodology and performance criteria is developed and recommended in line with the Board approved corporate governance policy and terms of reference. Self assessment shall help the board to establish clear expectations and goals to measure against these standards. The areas covered by the self assessment process are:

- Objective and strategy
- Selecting and retaining competent management
- Monitoring and assessing operations
- Efficient operations
- General assessment

The Bank is in the process of Board assessment for 2018.

### **6.14 Review of internal control processes and procedures (PD-1.3.10(y))**

Internal control processes and procedures are regularly reviewed by the Bank's Internal Auditor in line with the internal audit plan approved by the Board's Audit, Risk & Compliance Committee.

## **6 Corporate governance and transparency (continued)**

### **6.15 Governance arrangements, systems and controls employed by the bank to ensure Shari'a compliance (PD-1.3.10(ff))**

Shari'a compliance department conducts review of all business financing and investment proposals together with audit of all executed transactions of Ibdar Bank and its affiliates to confirm compliance with Shari'a rules and principles, and also with specific rulings and guidelines issued by the Shari'a Supervisory Board.

The Shari'a review and audit are conducted internally by the Shari'a Compliance Department, which includes examining all transactions without exception, with all its the relevant documentation and execution procedures adopted by Ibdar Bank.

The Shari'a review and audit are planned and performed after obtaining all the information and explanations which are considered necessary to provide sufficient evidence and give reasonable assurance that Ibdar Bank and its affiliates are in compliance with Islamic Shari'a rules and principles.

The findings are reported to the Shari'a Supervisory Board during the periodic meeting, which is held on quarterly basis or at any other time as the case may require. The Shari'a Supervisory Board reviews the review and audit reports of the Shari'a Compliance Department and provides the necessary recommendations in this regard, if needed, and issues the official opinion by means of the Shari'a Compliance Certificate after each meeting.

### **6.16 Handling of Non Shari'a compliance earnings and expenditures (PD-1.3.10(gg))**

Any amount that has been identified as being non Shari'a compliant are fully reimbursed to a charity organization or a Bahraini Non-Profit organization. Income from non islamic sources amounting to USD 14 thousand was given as charity.

### **6.17 Information on mediation, advise and complaint procedures at the bank (PD-1.3.10(dd))**

The investors may use the Bank's website for logging a query or a complaint, which is managed by the Corporate Communications Department ("CCD") through the [info@ibdarbank.com](mailto:info@ibdarbank.com) or [complaint@ibdarbank.com](mailto:complaint@ibdarbank.com) in the "Contact Us" page on the website.

After receiving a query or a complaint through the email address associated with the "Contact Us" page, CCD/Compliance channel the query or the complaint to the concerned department to follow up with a response. The investor's query is addressed accordingly by the appropriate department or person who was asked to handle the issue. An acknowledgement goes to the customer within 5 working days and a full reply within a maximum of 4 weeks.

### **6.18 Election system of directors and any termination arrangements (PD-1.3.10(s))**

As per the Memorandum and Articles of Association of the Bank, the Board shall be elected by the shareholders for a period of three years. The Board shall meet and elect its Chairman and Vice Chairman for a period equivalent to the term of the Board. The termination arrangements of the Board of Directors are as stated in the Memorandum of Articles of Association (Articles 24, 25 & 27).

Article 25-Appointment of Expert Directors: Subject to the approval of the Central Bank of Bahrain, the Ordinary General Meeting may appoint a number of persons with expertise to be members of the Board of Directors who are not founders or shareholders in the Company in such number and with powers as the Board of Directors may deem necessary in order to serve the interest of the Company and provide the necessary technical, administrative and scientific skills and practical experience for the Company and provide the necessary technical, administrative and scientific skills and practical experience for the Company and subject to satisfaction by such members of the requirements of Ministerial Order No.10 for the year 2002 with respect to qualifying conditions required to be met by members of the Board of Directors who are not founders or shareholders, and subject also to the number determined for members of the Board of Directors according to provisions of these Articles of Association.

## **6 Corporate governance and transparency (continued)**

### **6.18 Election system of directors and any termination arrangements (PD-1.3.10(s)) (continued)**

Article 26-Termination of Membership of Directors: A director's membership of the Board of Directors terminates in the following events:

1. If he was appointed or elected contrary to the provisions of Law of Articles of Association.
2. If he mis-uses his position as director in carrying on business that is competitive to that of the Company or if he causes actual damage to it.
3. If he fails to attend three consecutive meetings of the Board without lawful excuse notified in writing to the Board, and the Board shall resolve on this matter as it may deem fit.
4. If he resigns or withdraws from his office, provided the foregoing shall be done in an opportune time, otherwise he shall be liable to pay damages to the Company.
5. If he occupies any other office in the Company for which he would receive remuneration other than that which the Board of Directors may decide from time to time to remunerate its occupier because of the executive nature of his duties.

Article 27-Removal of Directors:

1. The General Meeting may terminate the membership of all or some of the members of the board Of Directors. Requisition for termination shall be presented to the Board by shareholders representing at least 10% of the capital. The Board shall forward such requisition to the General Meeting within a maximum period of one month from the date of its submission; otherwise the Ministry of Industry and Commerce may issue the notice for the Meeting. The General Meeting may not consider this requisition with respect to the said termination unless the said requisition is on the agenda. Save when serious developments are revealed during the meeting requiring such termination

2. A member of the Board of Directors may resign provided that such resignation is at a suitable time, or else, he may be liable to pay compensation to the Company.

### **6.19 Bank's Communication Strategy (PD-1.3.10(h, cc, zz))**

The CCD is responsible for preparing marketing materials in liaison with other Business Departments, which are used to communicate new product information and inform the investors of the Bank's activities. The various channels of communication may include corporate publications, website, direct mailers, electronic mail and local & regional media (through press releases). All marketing materials & corporate documents are approved by Senior Management prior to disclosing to the public.

The Bank adopted an open policy for communication where it uses all available suitable channels to communicate with its stakeholders, in line with the principle of transparency and disclosure that is integral to good corporate governance. This includes wide use of the media for the purposes of providing information on the Bank's progress.

The bank provides investment updates to its clients on a semi-annual basis.

Furthermore, the Bank provides information on all events that merit announcement, either on its website or through other communication channels. The Bank's annual report and previous years financial statements are also published on the website, as well as the Corporate Governance reports. The Bank's quarterly results are also published in both Arabic and English newspapers, and are posted on the Bank's website.

The Board attaches a high degree of importance to continuous communication with shareholders, especially direct dialogue with them at the Bank's annual general meetings. Shareholders are therefore encouraged to actively participate at such meetings.

## **6 Corporate governance and transparency (continued)**

### **6.20 Bank's Code of Ethical Business Conduct and Conflict of Interest (PD-1.3.10(v) & PD-6.1.1 (j))**

The Board establishes corporate values for itself, senior management, and employees. These values have been communicated throughout the Bank, so that the Board and senior management and staff understand their accountabilities to the various stakeholders and fulfill their fiduciary responsibilities to them.

Bank's ethics dictate that a Board Member should:

- 1 - Not enter competition with the Bank;
- 2 - Not demand or accept substantial gifts for himself or his associates;
- 3 - Not take advantage of business opportunities to which the Bank is entitled for himself or his associates;
- 4 - Report to the Board any conflict of interest in their activities with, and commitments to other organizations. In any case, all Board Members declare in writing all of their other interest in other enterprises or activities (whether as a shareholder, manager, or other form of participation) to the Board (or the Audit, risk and compliance Committee / Corporate Officer) on an annual basis;
- 5 - Absent themselves from any discussions or decision-making that involves a subject where they are incapable of providing objective advice, or which involves a subject or proposed transaction where a conflict of interest exists; and
- 6 - Ensure, collectively with the Board, that systems are in place to ensure that necessary client confidentiality is maintained and the privacy or the organization itself is not violated, and that clients' rights and assets are properly safeguarded.

Any conflict of interest that might arise from the board members is governed by the Corporate Governance Manual. Each board member is required to disclose any potential conflict of interest that might arise during the term of their membership. Any transaction that has occurred during their term as a board member must be disclosed to the board through the Board Conflict Form. Any conflict of interest arising from any board member must be ratified by the board, and the respective board member will be refrained from voting on that matter.

In the fifth board meeting held on 9th August 2018, The vice chairman abstained himself from voting in regards to resolutions passed for his appointment as an acting CEO and related remuneration thereof.

### **6.21 Monitoring Compliance to and Enforcement of Code of Conduct**

The matters covered in the Code of Conduct are of the utmost importance to the Bank, its stakeholders and its business partners and are essential to the Bank's ability to conduct its business in accordance with its stated values. The Bank clearly communicates to all of its employees that they are expected to adhere to these rules in carrying out their duties for the Bank.

The Board, through independent evaluators (i.e. Internal Auditor) and Senior Management, continuously monitor adherence to the set Code of Conduct and take appropriate action against any employee whose actions are found to violate these policies or any other policies of the Bank. Disciplinary actions may include immediate termination of employment or business relationship at the Bank's sole discretion. Employees are prohibited from participating in or concealing criminal activity or illegal behavior. Periodic reports and assessments of compliance to Code of Conduct will be presented to the board to report any incident of non compliance.

### **6.22 Auditor's Fees and Non-Audit Services (PD-6.1.1 (g & h))**

The details of the audit fees charged and non-audit services provided by the Bank's external auditors will be made available to the shareholders as and when requested. Such details will be made available to the Bank's shareholders as per their specific request, provided that these disclosures do not negatively impact the Bank's interest.

### **6.23 Social Functions and Charitable contributions of the Bank (PD-1.3.10 (ee))**

The Bank discharges its social responsibilities through donations to charitable causes and organizations.

### **6.24 Penalties or Fines by Central Bank of Bahrain (PD-1.3.44)**

In 2018, financial penalties amounting to BD 10,000 were imposed by the Central bank of Bahrain due to violations of certain CBB rules and guidelines, Bahrain commercial companies' law and AAOIFI standards noted during its regulatory inspection during the year.

### **6.25 Penalties charged to Customers for Default (PD-1.3.23(l))**

No penalties were charged to customers with regards to defaults during 2018.

### **6.26 Avoidance of conflict of interest related to approved persons**

The Bank has a policy in place that is approved by the Board on the employment of relatives of approved persons.

## **7 DISCLOSURE REQUIREMENTS PERTAINING TO REMUNERATION**

The Bank's total compensation approach, which includes the variable remuneration policy, sets out the Bank's policy on remuneration for Directors and senior management and the key factors that are taken into account in setting the policy.

The Bank adopted regulations concerning Sound Remuneration Practices issued by the Central Bank of Bahrain and has proposed revisions to its variable remuneration framework in 2014. The revised policy framework and incentive components was approved by the shareholders in the Annual General Meeting.

The key features of the proposed remuneration framework are summarised below.

### **7.1 Remuneration Strategy**

It is the Bank's basic compensation philosophy to provide a competitive level of total compensation to attract and retain qualified and competent employees. The Bank's variable remuneration policy will be driven primarily by a performance based culture that aligns employee interests with those of the shareholders of the Bank. These elements support the achievement of our objectives through balancing rewards for both short-term results and long-term sustainable performance. Our strategy is designed to share our success, and to align employees' incentives with our risk framework and risk outcomes.

The quality and long-term commitment of all of our employees is fundamental to our success. We therefore aim to attract, retain and motivate the very best people who are committed to maintaining a career with the Bank, and who will perform their role in the long-term interests of our shareholders. The Bank's reward package is comprised of the following key elements:

1. Fixed pay
2. Benefits
3. Annual performance bonus
4. Long Term Incentives

A robust and effective governance framework ensures that the Bank operates within clear parameters of its compensation strategy and policy. All compensation matters, and overall compliance with regulatory requirements, are overseen by the Board Nomination, Remuneration & Governance Committee (NRGC).

The Bank's remuneration policy in particular, considers the role of each employee and has set guidance on whether an employee is a Material Risk Taker and/ or an Approved Person in a business line, control or support function. An Approved Person is an employee whose appointment requires prior regulatory approval because of the significance of the role within the Bank and an employee is considered a Material Risk Taker if they are the Head of a significant business line or any individuals within their control who has a material impact on the Bank's risk profile.

In order to ensure alignment between what we pay our people and our business strategy, we assess individual performance against annual and long-term financial and non-financial objectives summarised in our performance management system. This assessment also takes into account adherence to the Bank's values, risks and compliance measures and above all integrity. Altogether, performance is therefore judged not only on what is achieved over the short and long-term but also importantly on how it is achieved, as the NRC believes the latter contributes to the long-term sustainability of the business.

## 7 REMUNERATION RELATED DISCLOSURES (continued)

### 7.2 NRGC Role and Focus

The NRGC has oversight of all reward policies for the Bank's employees. The NRGC is the supervisory and governing body for compensation policy, practices and plans. It is responsible for determining, reviewing and proposing variable remuneration policy for approval by the Board. It is responsible for setting the principles and governance framework for all compensation decisions. The NRGC ensures that all persons must be remunerated fairly and responsibly. The remuneration policy is reviewed on a periodic basis to reflect changes in market practices, the business plan and risk profile of the Bank.

The responsibilities of the NRGC with regards to the Bank's variable remuneration policy, as stated in its mandate, include but are not limited to, the following:

- Approve, monitor and review the remuneration system to ensure the system operates as intended.
- Approve the remuneration policy and amounts for each Approved Person and Material Risk-Taker, as well as total variable remuneration to be distributed, taking account of total remuneration including salaries, fees, expenses, bonuses and other employee benefits.
- Ensure remuneration is adjusted for all types of risks and that the remuneration system takes into consideration employees that earn same short-run profit but take different amount of risk on behalf of the bank.
- Ensure that for Material Risk Takers, variable remuneration forms a substantial part of their total remuneration.
- Review the stress testing and back testing results before approving the total variable remuneration to be distributed including salaries, fees, expenses, bonuses and other employee benefits.
- Carefully evaluate practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. The NRGC will question payouts for income that cannot be realized or whose likelihood of realization remains uncertain at the time of payment.
- Ensure that for approved persons in risk management, internal audit, operations, financial control and compliance functions the mix of fixed and variable remuneration is weighted in favor of fixed remuneration.
- Recommend Board member remuneration based on their attendance and performance and in compliance with Article 188 of the Bahrain Commercial Companies Law.
- Ensure appropriate compliance mechanisms are in place to ensure that employees commit themselves not to use personal hedging strategies or remuneration-and liability-related insurance to undermine the risk alignment effects embedded in their remuneration arrangements.

**Table – 25. NRGC Membership**

NRGC Member Name	Appointment date	Number of meetings attended
Tareq Sadeq	28-Apr-16	6
Mohamed Nooruddin	28-Apr-16	6
Jamal al Saleem	28-Apr-16	6

The aggregate remuneration paid to NRGC members during the year in the form of sitting fees amounted to USD 43,200 [2017: USD 69,600].

### 7.3 External Consultants

The Bank's variable remuneration policy is administrated by external consultants.

### 7.4 Scope of Application of the Remuneration Policy

The variable remuneration policy has been adopted on a bank-wide basis.

## **7 REMUNERATION RELATED DISCLOSURES (continued)**

### **7.5 Board Remuneration**

The Bank's Board remuneration is determined in line with the provisions of Article 188 of the Commercial Companies Law. The Board of Directors' remuneration will be capped so that total remuneration (excluding sitting fees) does not exceed 5% of the Bank's net profit after all required deductions as outlined in Article 188 of the Companies law, in any financial year. Board remuneration is subject to approval of the shareholders in the Annual General Meeting. Remuneration of non-executive Directors does not include performance-related elements such as grants of shares, share options or other deferred stock-related incentive schemes, bonuses or pension benefits.

### **7.6 Variable Remuneration for Staff**

Variable remuneration is performance related and consists primarily of the annual performance bonus award and long term incentives for future performance. As a part of our staff's variable remuneration, the annual bonus rewards delivery of operational and financial targets set each year, the individual performance of the employees in achieving those targets, and their contribution to delivering the Bank's strategic objectives.

The Bank has adopted a Board approved framework to develop a transparent link between variable remuneration and performance. The framework is designed on the basis of meeting both satisfactory financial performance and the achievement of other non-financial factors, that will, all other things being equal, deliver a target bonus pool for employees, prior to consideration of any allocation to business lines and employees individually. In the framework adopted for determining the variable remuneration pool, the NRC aims to balance the distribution of the Bank's profits between shareholders and employees.

Key performance metrics at the bank level include a combination of short term and long term measures and include profitability, solvency, liquidity and growth indicators. The performance management process ensures that all goals are appropriately cascaded down to respective business units and employees.

In determining the amount of variable remuneration, the Bank starts from setting specific targets and other qualitative performance measures that result in a target bonus pool. The bonus pool is then adjusted to take account of risk via the use of risk-adjusted measures (including forward-looking considerations).

The NRC carefully evaluates practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. NRC demonstrates that its decisions are consistent with an assessment of the Bank's financial condition and future prospects.

The Bank uses a formalized and transparent process to adjust the bonus pool for quality of earnings. It is the Bank's objective to pay out bonuses out of realized and sustainable profits. If the quality of earnings is not strong, the profit base could be adjusted based on the discretion of the NRC.

For the overall Bank to have any funding for distribution of a bonus pool; threshold financial targets have to be achieved. The performance measures ensure that total variable remuneration is generally, considerably contracted where subdued or negative financial performance of the Bank occurs. Furthermore, the target bonus pool as determined above is subject to risk adjustments in line with the risk assessment and linkage framework.

### **7.7 Remuneration of Control Functions**

The remuneration level of staff in the control and support functions allows the Bank to employ qualified and experienced personnel in these functions. The Bank ensures that the mix of fixed and variable remuneration for control and support function personnel should be weighted in favor of fixed remuneration. The variable remuneration of control functions is to be based on function-specific objectives and is not be determined by the financial performance of the business areas they monitor.

The Bank's performance management system plays a major role in deciding the performance of the support and control units on the basis of the objectives set for them. Such objectives are more focused on non-financial targets that include risk, control, compliance and ethical considerations as well as the market and regulatory environment apart from value adding tasks which are specific to each unit.



## **7 REMUNERATION RELATED DISCLOSURES (continued)**

### **7.8 Variable Compensation for Business Units**

The variable remuneration of the business units is primarily determined by key performance objectives set through the performance management system of the Bank. Such objectives contain financial and non-financial targets, including risk control, compliance and ethical considerations as well as market and regulatory requirements. The consideration of risk assessments in the performance evaluation of individuals ensures that any two employees who generate the same short-run profits but take different amounts of risk on behalf of the bank are treated differently by the remuneration system.

### **7.9 Risk Assessment Framework**

The purpose of risk linkages is to align variable remuneration to the risk profile of the Bank. In its endeavor to do so, the Bank considers both quantitative measures and qualitative measures in the risk assessment process. Both quantitative measures and human judgment play a role in determining any risk adjustments. The risk assessment process encompasses the need to ensure that the remuneration policy as designed reduces employees' incentives to take excessive and undue risks, is symmetrical with risk outcomes and delivers an appropriate mix of remuneration that is risk aligned.

The Bank's NRCG considers whether the variable remuneration policy is in line with the Bank's risk profile and ensures that through the Bank's ex-ante and ex-post risk assessment framework and processes, remuneration practices where potential future revenues whose timing and likelihood remain uncertain are carefully evaluated.

Risk adjustments take into account for all types of risk, including intangible and other risks such as reputation risk, liquidity risk and the cost of capital. The Bank undertakes risk assessments to review financial and operational performance against business strategy and risk performance prior to distribution of the annual bonus. The Bank ensures that total variable remuneration does not limit its ability to strengthen its capital base. The extent to which capital needs to be built up is a function of the bank's current capital position and its ICAAP.

The bonus pool takes into account the performance of the Bank which is considered within the context of the Bank's risk management framework. This ensures that the variable pay pool is shaped by risk considerations and Bank-wide notable events.

The size of the variable remuneration pool and its allocation within the bank takes into account the full range of current and potential risks, including:

- (a) The cost and quantity of capital required to support the risks taken;
- (b) The cost and quantity of the liquidity risk assumed in the conduct of business; and
- (c) Consistency with the timing and likelihood of potential future revenues incorporated into current earnings.

The NRCG keeps itself abreast of the Bank's performance against the risk management framework. The NRCG will use this information when considering remuneration to ensure returns, risks and remuneration are aligned.

## **7 REMUNERATION RELATED DISCLOSURES (continued)**

### **7.10 Risk Adjustments**

The Bank has an ex-post risk assessment framework which is a qualitative assessment to back-test actual performance against prior risk assumptions.

In years where the Bank suffers material losses in its financial performance, the risk adjustment framework will work as follows:

- There will be considerable contraction of the Bank's total variable remuneration.
- At an individual level, poor performance by the Bank will mean individual KPIs are not met and hence employee performance ratings will be lower
- Reduction in the value of deferred shares or awards
- Possible changes in vesting periods and additional deferral applied to unvested rewards
- Lastly, if the qualitative and quantitative impact of a loss incident is considered significant, a malus or clawback of previous variable awards may be considered.

The NRCG, with the Board's approval, can rationalize and make the following discretionary decisions:

- Increase/ reduce the ex-post adjustment
- Consider additional deferrals or increase in the quantum of non-cash awards
- Recovery through malus and clawback arrangements

### **7.11 Malus and Claw Back Framework**

The Bank's malus and clawback provisions allow the Bank's Board of Directors to determine that, if appropriate, unvested elements under the deferred bonus plan can be forfeited/ adjusted or the delivered variable remuneration recovered in certain situations. The intention is to allow the Bank to respond appropriately if the performance factors on which reward decisions were based turn out not to reflect the corresponding performance in the longer term. All deferred compensation awards contain provisions that enable the Bank to reduce or cancel the awards of employees whose individual behavior has had a materially detrimental impact on the Bank during the concerned performance year.

Any decision to take back an individual's award can only be made by the Bank's Board of Directors.

- Reasonable evidence of willful misbehavior, material error, negligence or incompetence of the employee causing the Bank/the employee's business unit to suffer material loss in its financial performance, material misstatement of the Bank's financial statements, material risk management failure or reputational loss or risk due to such employee's actions, negligence, misbehavior or incompetence during the concerned performance year.
- The employee deliberately misleads the market and/or shareholders in relation to the financial performance of the Bank during the concerned performance year.

Clawback can be used if the malus adjustment on the unvested portion is insufficient given the nature and magnitude of the issue.

**7 REMUNERATION RELATED DISCLOSURES (continued)**

**7.12 Components of Variable remuneration**

**Table - 26. Variable remuneration has following main components:**

<b>Upfront cash</b>	The portion of the variable compensation that is awarded and paid out in cash on conclusion of the performance evaluation process for each year.
<b>Deferred Cash</b>	The portion of variable compensation that is awarded and paid in cash on a pro-rata basis over a period of 3 years
<b>Upfront share awards</b>	The portion of variable compensation that is awarded and issued in the form of shares on conclusion of the performance evaluation process for each year.
<b>Deferred shares</b>	The portion of variable compensation that is awarded and paid in the form of shares on a pro-rata basis over a period of 3 years
<b>Other Non-Cash Awards</b>	Non-Cash Awards that link rewards to the risk and profitability of individual transactions or transaction portfolios including: - Profit Share in Investments - Carried Interest - Co-Investment in Assets

All deferred awards are subject to malus provisions. All share awards are released to the benefit of the employee after a six month retention period from the date of vesting. The number of equity share awards is linked to the Bank's share price as per the rules of the Bank's Share Incentive Scheme. Any dividend on these shares is released to the employee along with the shares (i.e. after the retention period).

**7.13 Deferred Compensation**

All staff earning in excess of BHD 100,000 are subject to the following rules of deferral:

The CEO and 5 most highly paid business line employees are subject to the following deferral rules:

**Table - 27. Deferral Rules - Business Line Employees**

Element of variable remuneration	Payout percentages	Vesting period	Retention	Malus	Clawback
Upfront cash	40%	immediate	-	-	Yes
Deferred cash	10%	3 years	-	Yes	Yes
Deferred Phantom Shares	10-50%	3 years	6 months	Yes	Yes
Other Non-Cash Awards	0-40%	Transaction linked	6 months	Yes	Yes

All other covered staff are subject to the following deferral rules:

**Table - 28. Deferral Rules - Other Covered Staff**

Element of variable remuneration	Payout percentages	Vesting period	Retention	Malus	Clawback
Upfront cash	50%	immediate	-	-	Yes
Upfront non-cash awards	10%	immediate	6 months	Yes	Yes
Deferred non-cash awards	40%	3 years	6 months	Yes	Yes

The NRCG, based on its assessment of role profile and risk taken by an employee could increase the coverage of employees that will be subject to deferral arrangements.

## 7 REMUNERATION RELATED DISCLOSURES (continued)

### 7.14 Details of Remuneration Paid

**Table - 29. Board of Directors**

USD	2018	2017
Sitting Fees	199,200	138,568
Remuneration	500,000	500,000
Others	69,062	44,121

Board of Directors remuneration are subject to AGM and MOIC approval.

**Table - 30. Employee Remuneration**

USD'000	Number of Staff	2018				Total
		Variable Remuneration		Fixed Remuneration		
		Cash	Others	Cash	Others	
Approved Persons:						
Business Lines	6	9	5	1,393	169	1,576
Control and Support	7	74	-	1,109	198	1,381
Other Material Risk Takers	14	23	26	1,307	250	1,606
Other staff	28	33	-	1,016	243	1,292
<b>Total</b>	<b>55</b>	<b>139</b>	<b>31</b>	<b>4,825</b>	<b>860</b>	<b>5,855</b>

The payment of variable remuneration for 2018 was approved in NRCG meeting held on 24 February 2019 subsequent to finalisation of the consolidated financial statements for the year ended 31 December 2018.

USD'000	Number of Staff	2017				Total
		Variable Remuneration		Fixed Remuneration		
		Cash	Others	Cash	Others	
Approved Persons:						
Business Lines	6	77	68	1,848	205	2,198
Control and Support	12	96	12	1,997	275	2,380
Other Material Risk Takers	12	185	-	1,703	295	2,183
Other staff	28	62	-	1,003	225	1,290
<b>Total</b>	<b>58</b>	<b>420</b>	<b>80</b>	<b>6,551</b>	<b>1,000</b>	<b>8,051</b>

**Table - 31. Severance Pay**

	2018	2017
Number of Staff	16	3
Severance Pay (USD)	886,540	196,384
Highest such award to a single person (USD)	297,761	107,323

**Table - 32. Deferred awards**

	2018			
	Cash	Shares Nos	Value	Total
Opening balance	71,858	953,146	324,552	396,410
Awarded during the period	80,436	-	-	80,436
Profit accrued during the period on deferred cash	720	-	-	720
Paid out / released during the period	(29,541)	(423,631)	(127,659)	(157,200)
Shares forfeited	(15,069)	(73,151)	(75,346)	(90,415)
Valuation adjustments	-	-	10,760	10,760
<b>Closing balance</b>	<b>108,404</b>	<b>456,364</b>	<b>132,308</b>	<b>240,712</b>

	2017			
	Cash	Shares Nos	Value	Total
Opening balance	85,904	987,061	787,279	873,183
Awarded during the period	13,276	38,301	40,216	53,492
Profit accrued during the period on deferred cash	1,496	-	-	1,496
Paid out / released during the period	(28,818)	(72,216)	(75,827)	(104,645)
Valuation adjustments	-	-	(427,116)	(427,116)
<b>Closing balance</b>	<b>71,858</b>	<b>953,146</b>	<b>324,552</b>	<b>396,410</b>