



EDBS/KH/C/42/2014
20th July 2014

Chief Executive Office/General Manager
All Conventional Bank Licensees
Manama
Kingdom of Bahrain

Dear Sir,

CBB Rulebook: Volume 1 – July 2014 Quarterly Update

The latest quarterly update to Volume 1 has now been incorporated in the website version of the Rulebook.¹

Changes for July 2014

The changes for July 2014 are listed in the attached table.

Implementation Date for New Reporting Requirements (Appendices BR-8 and BR-19)

The implementation date for the new reporting requirements for the large exposure report and the overseas banking subsidiaries and branches report detailed under Paragraphs BR-3.1.10 to BR-3.1.11A is for the quarter ending 31st December 2014.

The current rules in place dealing with Appendix BR-8 (Quarterly report on Overseas Branches) continue to apply for the quarter ending 30th June 2014 but will be replaced by the overseas banking subsidiaries and branches report starting with the quarter ending 31st December 2014.

Sound Remuneration Practices

As a follow up to the gap analysis provided by banks and further feedback on the implementation of the sound remuneration rules issued as part of the January 2014 update to the CBB Rulebook, further guidance to banks is being provided and changes are being incorporated as part of the July 2014 update.

Banks are requested to carefully review the changes and, where needed, adjust their remuneration policy accordingly.

¹ Volume 1 can be accessed from www.cbb.gov.bh : from the Home page, select 'CBB Rulebooks' and then 'Volume 1'

Amended Definition for Clawback

For the purposes of the CBB Rulebook, the definition of clawback is being amended as follows:

Clawback

A clawback requires that an employee (or ex-employee) return to the bank the variable remuneration that was previously paid out to him/her.

Clarification of Board of Directors' Role

Paragraph HC-5.2.1 states:

The Board must establish a remuneration committee of at least three directors which must:

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

The Board, however, may decide that such policy and remuneration packages be subject to its approval instead of only the remuneration committee.

The paragraph above states that the approval is not only for the remuneration policy but also for the individual amounts for all approved persons and material risk-takers.

Clarification of Scope of Application of Section HC-5.4

Paragraph HC-5.4.2 has been clarified as follows:

- HC-5.4.2 While this Section applies to all approved persons and material risk-takers, ~~for the remuneration of all the rules on the proportion of fixed and variable remuneration (Paragraph HC-5.4.30) as well as those rules related to the deferral of variable remuneration (Paragraphs HC-5.4.31 and HC-5.4.32) and the obligation to have part of the variable remuneration in shares (Paragraphs HC-5.4.33 and HC-5.4.34) apply only to:~~
- (a) Approved persons; or
 - (b) Material risk-takers whose total annual remuneration (including all benefits) is in excess of BD100,000, unless the board of directors requires the application of these Rules to all staff.

Application of Rules to Placement, Marketing and Sales Staff

The definition of material risk-takers includes all staff involved in direct placement, marketing or sales of the bank's products, regardless of whether they have been involved in the design of the riskiness of the products which they are selling as such staff is exposing the bank to reputational risk in the sale of such products and are therefore considered material risk takers.

Application of Rules to Subsidiaries that are Non-CBB Licensees

Where a bank has a subsidiary that is a non-CBB licensee involved in a non-financial activity (e.g. car dealership), the remuneration rules will not apply to that particular subsidiary. However, for greater certainty, the bank must obtain the CBB's prior approval to confirm the exclusion of the subsidiary from the remuneration rules.

Treatment of Deferred Pay when Leaving the Bank

The only instance where deferred pay can be paid out before the end of the vesting period is in the case of death of the employee where the beneficiaries would receive the deferred pay.

Role of the Remuneration Committee

The paragraph HC-5.4.22 has been amended as such responsibility should be part of the remuneration committee:

~~Senior management~~ The remuneration committee of the bank must question payouts for income that cannot be realised or whose likelihood of realisation remains uncertain at the time of payout.

Correction to be aligned with Basel Committee Principles and Standards

Paragraph HC-5.4.24 has been amended as follows to be aligned with Basel principles:
The size of the variable remuneration pool and its allocation within the bank must take into account the full range of current and potential risks, including:

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

Application of Malus and Clawback Provisions

As outlined in paragraphs HC-5.4.26 to HC-5.4.29, banks must take note that malus and clawback provisions must apply where the bank's performance results is subdued or results in negative financial performance.

Correction to terminology

The terminology used in paragraph HC-5.4.28 is amended as follows:

~~In the event of negative contributions of the~~ If the bank and/or relevant line of business is incurring losses in any year during the vesting period, any unvested portions must be ~~are to be clawed back~~ subject to malus, ~~subject to the realised performance of the bank and the business line.~~

Clarification of Rule for Proportion of Remuneration that is Variable Pay

- HC-5.4.30 For approved persons and material risk-takers, other than those covered under Paragraphs HC-5.4.9 and Section HC-5.5, as their actions have a material impact on the risk exposure of the bank:
- A substantial proportion of remuneration must be variable and paid on the basis of individual, business-unit and bank-wide measures that adequately measure performance; and
 - The variable proportion of remuneration must increase significantly along with the level of seniority and/or responsibility.

The above change has been made as staff covered under Paragraph HC-5.4.9 (risk management, internal audit, operations, financial controls, internal Shari'a review/audit, AML and compliance functions personnel) must have their remuneration weighed in favour of fixed remuneration. In addition, under Section HC-5.5, non-executive directors are not entitled to receive any variable remuneration.

Grandfathering of Contracts re Proportion of Fixed and Variable Pay

In instances where Paragraph HC-5.4.30 applies, and the variable pay does not represent a 'substantial' proportion of the remuneration package, the following guidance will apply:

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

Clarification of Deferral Rules for Variable Pay

The following paragraph was amended for more clarity:

- HC-5.4.31 For purposes of Paragraph HC-5.4.30:
- At least 40% of the variable remuneration must be payable under deferral arrangements over a period of at least 3 years; and
 - For the CEO, his deputies and the other 5 most highly paid business line employees, at least 60% of the variable remuneration must be ~~deferred for at least 3 years~~ payable under deferral arrangements over a period of at least 3 years.

Guaranteed Variable Remuneration

Paragraph HC-5.4.35 has been amended as follows:

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

Share Retention Period

The following amendment was made in line with international practice:

HC-5.4.36 Awards in shares or share-linked instruments must be subject to a minimum share retention policy of ~~3 years~~ 6 months from the time the shares are awarded, unless the bank's policy requires a longer period.

Other Changes in Module HC

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

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

Remuneration of Board Members

HC-5.5.2 was amended as follows:

The Board of Directors' remuneration must be ~~fixed~~ capped so that total remuneration (excluding sitting fees) must not exceed 5% of the bank's net profit, after all the required deductions outlined in Article 188 of the Company Law, in any financial year, notwithstanding the requirements of shareholders' approval.

Appendix BR-14

Appendix BR-14 has been amended to clarify that certain items do not apply for members of the Board.

New Reporting Requirements Appendix BR-14 – Details of Remuneration Paid

The due date for this reporting requirement under Paragraph BR-1.3.1 has been revised to within 3 months of the financial year end.

Disclosure Requirements Pertaining to Remuneration

A guidance Paragraph PD-1.3.8G has been added clarifying that certain disclosure requirements under Paragraph PD-1.3.8B in relation to remuneration do not apply to banks that have no approved persons or material risk-takers whose total remuneration is in excess of BD100,000.

PD-1.3.8G In instances where a bank has no approved persons or material risk-takers whose remuneration is in excess of BD100,000 as per Paragraph HC-5.4.2, the disclosure requirements under Subparagraphs PD-1.3.8B(f), (g), (l), (m), (t) and (u) are not required.

Clarification of Disclosure of Remuneration Practices

Paragraph PD-1.3.8C states that:

The disclosure of remuneration practices must cover approved persons and material risk-takers and must be broken down as follows:

- (a) Members of the board of directors;
- (b) Approved persons in business lines;
- (c) Approved persons in risk management, internal audit, operations, financial controls, internal Shari'a review/audit, AML and compliance functions; and
- (d) Material risk-takers not falling under categories (a) to (c).

Paragraph PD-1.3.8F was amended as follows to ensure consistency with Paragraph PD-1.3.8C:

PD-1.3.8F For purposes of Paragraph PD-1.3.8E, the table referred to should be completed separately for:

- (a) Members of the board of directors;

Total value of remuneration awards for the current fiscal year	Unrestricted
Fixed remuneration	
• Sitting Fees	x
• Other (please specify)	x

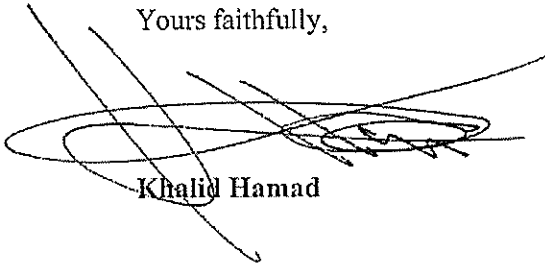
- (b) Approved persons, other than board members in business lines;
- (c) Approved persons in risk management, internal audit, operation, financial controls, internal Shari'a review/audit, AML and compliance functions; and
- (d) Material risk-takers not falling under categories (a) to (c).

Total value of remuneration awards for the current fiscal year	Unrestricted	Deferred
Fixed remuneration		
• Cash-based	x	x
• Shares and share-linked instruments	x	x
• Other	x	x
Variable remuneration		
• Cash-based	x	x
• Shares and share-linked instruments	x	x
• Other	x	x

Further information

Should you have any queries regarding these updates, you may contact the CBB Rulebook team at rulebook@cbb.gov.bh, or else please speak to your normal supervisory contact.

Yours faithfully,



Khalid Hamad

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Part A

Module Code	Summary of Changes and Printing Instructions
UG	Print off ToC.
LR	Print off ToC.
PB	Print off ToC.
HC	HC-5.2, HC-5.4 and HC-5.4: Updated Rules on remuneration. Print off ToC, Sections HC-A.2, HC-5.2, HC-5.4 and HC-5.5.
AU	AU-1.1.1A: Added guidance clarifying the information required when seeking the CBB's approval for appointment or re-appointment of the external auditor. AU-3.6: Where a conventional bank licensee has no approved persons or material risk-takers whose total annual remuneration is in excess of BD100,000, the report on compliance with remuneration rules need not be completed by the external auditor. Print off ToC, Sections AU-A.2, AU-1.1 and AU-3.6.
GR	Print off ToC.
CA	Print off ToC.
BC	Print off ToC.
CM	CM-5.10.2A: Added a guidance Paragraph to clarify the treatment of investments in entities which are otherwise not connected to the bank. Print off ToC, Sections CM-A.3 and CM-5.10.
OM	Print off ToC.
FC	Print off ToC.
PCD	Print off ToC.
TC	TC-B.1.4: Clarified scope of application. Print off ToC, Sections TC-A.2 and TC-B.1.
BR	BR-1.3.1: Changed due date for Details of remuneration paid report. BR-3.1.8A: Added quarterly reporting requirements regarding interim financial statements as per 22 January 2014 ad hoc communication letter. BR-3.1.10 to BR-3.1.11A: New quarterly reporting requirements added for details of large exposures and overseas subsidiaries and branches. BR-4A.3.1: Noted exception to requirement to submit report on the bank's compliance with the remuneration rules. Print off ToC Sections BR-A.3, BR-1.3, BR-3.1 and BR-4A.3.

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Part A

Module Code	Summary of Changes and Printing Instructions
PD	PD-1.3.8C, PD-1.3.8F and PD-1.3.8G: Amended disclosure requirements pertaining to remuneration. Print off ToC, Sections PD-A.4 and PD-1.3.
EN	Print off ToC.
CP	Print off ToC.

Part B

Module Code	Summary of Changes	
Glossary		
Amended definition for clawback.		
CBB Reporting Forms		
Appendix BR-5	Returns--PIR	Minor amendments and clarifications.
Appendix BR-8	Quarterly Report on Overseas Banking Subsidiaries and Branches	Expanded the scope of the report to include branches.
Appendix BR-14	Details of Remuneration Paid	Form clarified as certain items do not apply to Board members
Appendix BR-19	Large Exposures Report	Added new report on large exposures.
Supplementary Information		
Appendix CA-18	Bahrain Sovereign and Public Sector Entities Eligible for Zero Risk Weighting	Corrected percentage ownership for Gulf Air.