

## Remuneration Policy and Related Disclosures

### REMUNERATION POLICY AND RELATED DISCLOSURES

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

During the year, the Group adopted regulations concerning Sound Remuneration Practices issued by the CBB and proposed revisions to its variable remuneration framework. The revised policy framework and incentive components were submitted to its shareholders for approval. The revised policy framework and incentive components were subsequently approved by the shareholders in Annual General Meeting so that the policy became effective for the 2014 annual performance incentives and future periods.

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

#### Remuneration strategy

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

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

1. Fixed Pay;
2. Benefits;
3. Annual Performance Bonus; and
4. The Long Term Performance Incentive Plan.

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

The Group'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 Group 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 have a material impact on the Group's risk profile.

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

#### BARC role and focus

The BARC has oversight of all reward policies for the Group's employees. The BARC 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 BARC 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 Group.

The responsibilities of the BARC with regard to the Group's variable remuneration policy, as stated in its mandate, include, but are not limited to:

- Approving, monitoring and reviewing the remuneration system to ensure the system operates as intended;
- Approving 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;
- Ensuring remuneration is adjusted for all types of risks and that the remuneration system takes into consideration employees that earn the same short-run profit but take different amounts of risk on behalf of the Group;
- Ensuring that for Material Risk Takers, variable remuneration forms a substantial part of their total remuneration;
- Reviewing 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 evaluating practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain; the BARC will question payouts for income that cannot be realised or whose likelihood of realisation remains uncertain at the time of payment;
- Ensuring that for approved persons in risk management, internal audit, operations, finance and compliance functions the mix of fixed and variable remuneration is weighted in favour of fixed remuneration;
- Recommending Board members' remuneration based on their attendance and performance and in compliance with Article 188 of the Bahrain Commercial Companies Law; and
- Ensuring 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.

The aggregate remuneration paid to BARC members during the year in the form of sitting fees amounted to \$42,623 (2014: \$ 48,000). Other details concerning BARC memberships are disclosed elsewhere in this report.

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## Remuneration Policy and Related Disclosures (Continued)

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### External consultants

Consultants have been appointed to advise the Group on any relevant amendments to its variable remuneration policy required to bring it into line with the CBB's Sound Remuneration Practices and industry norms. This has included assistance in designing an appropriate Share-based Incentive Scheme for the Group.

### Scope of application of the remuneration policy

The remuneration policy has been adopted on a Groupwide basis.

### Board remuneration

The Board of Directors' remuneration is determined in line with the provisions of Article 188 of the Bahrain Commercial Companies Law, 2001. 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.

### Variable remuneration for staff

Variable remuneration is performance related and consists primarily of the annual performance bonus award. As a part of the 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 Group's strategic objectives.

The Group 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 BARC aims to balance the distribution of the Group's profits between shareholders and employees.

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

The Group uses a formalised and transparent process to adjust the bonus pool for quality of earnings. It is the Group's objective to pay bonuses out of realised and sustainable profits. If the quality of earnings is not strong, the profit base may be adjusted at the discretion of the BARC.

Funding for distribution of a bonus pool is dependent on threshold financial targets being achieved by the Group. The performance measures ensure that total variable remuneration is generally considerably contracted where subdued or negative financial performance of the Group occurs. Furthermore, the target bonus pool as determined above is subject to risk adjustments in line with the risk assessment and linkage framework.

### Remuneration of control functions

The remuneration level of staff in the control and support functions is maintained at a level which enables the Group to attract and thus employ qualified and experienced personnel in these functions. The Group ensures that the mix of fixed and variable remuneration for control and support function personnel is weighted in favour of fixed remuneration. The variable remuneration of control functions is based on function-specific objectives and is

not determined by the financial performance of the business areas they monitor.

The Group'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.

### 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 Group. 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 Group are treated differently by the remuneration system.

### Risk assessment framework

The purpose of risk linkages is to align variable remuneration to the risk profile of the Group. In its endeavour to do so, the Group 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 BARC considers whether the variable remuneration policy is in line with the Group's risk profile and ensures that, through the Group'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.

## Remuneration Policy and Related Disclosures (Continued)

Risk adjustments take into account all types of risk, including intangible and other risks such as reputation risk, liquidity risk and the cost of capital. The Group undertakes risk assessments to review financial and operational performance against business strategy and risk performance prior to distribution of the annual bonus. The Group 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 Group's current capital position and its ICAAP.

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

The size of the variable remuneration pool and its allocation within the Group 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 BARC keeps itself abreast of the Group's performance against the risk management framework. The BARC will use this information when considering remuneration to ensure that returns, risks and remuneration are aligned.

### Risk adjustments

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

In any year where the Group suffers material losses in its financial performance, the risk adjustment framework will work as follows:

- There will be considerable contraction of the Group's total variable remuneration
- At an individual level, poor performance by the Group 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 BARC, with the Board's approval, can rationalise 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

### Malus and Clawback framework

The Group's malus and clawback provisions allow the 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 Group 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 Group to reduce or cancel the awards of employees whose individual behaviour has had a materially detrimental impact on the Group during the relevant performance year.

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

The Group's malus and clawback provisions allow the Board to determine that, if

appropriate, vested/unvested elements under the deferred bonus plan can be adjusted/cancelled in certain situations. These events include the following:

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

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

## Remuneration Policy and Related Disclosures (Continued)

### Components of Variable remuneration

Variable remuneration has the following main components:

Upfront cash	The portion of the variable compensation that is awarded and paid out in cash on conclusion of the performance evaluation process for each year.
Deferred Cash	The portion of variable compensation that is awarded and paid in cash on a pro-rata basis over a period of 3 years.
Upfront share awards	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.
Deferred shares	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.

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 Group's share price as per the rules of the Group's Share Incentive Scheme. Any dividend on these shares is released to the employee along with the shares (i.e. after the retention period).

### Deferred compensation

All employees earning over BHD 100,000, or equivalent, in total compensation shall be subject to deferral of variable remuneration as follows:

Element of variable remuneration	Deferral	Deferral period	Retention	Malus	Clawback
Upfront cash	40%	immediate	-	-	Yes
Upfront shares	-	immediate	6 months	Yes	Yes
Deferred cash	0%	Over 3 years	-	Yes	Yes
Deferred share awards	60%	After 3 years	6 months	Yes	Yes

The BARC, based on its assessment of role profile and risk taken by an employee, may increase the coverage of employees that are subject to deferral arrangements.

### Details of remuneration paid

#### (a) Board of Directors

	2015	2014
• Sitting Fees	\$417,000	\$456,000
• Remuneration	\$1,500,000 *	\$1,500,000
• Other	\$229,911	\$214,655

\* To be approved in forthcoming AGM in March 2016

The category 'Other' includes the reimbursement of air fares and payment of per diem allowances for attending Board of Directors and Board Committees' meetings.

#### (b) Employee remuneration

Total fixed remuneration for Approved Persons and Material Risk Takers affected by the policy amounted to \$4,147,827 (2014: \$3,169,088) and the number of persons affected: 9 (2014: 7).

The total variable remuneration for 2015 was \$5,902,573 (2014: \$4,886,180)

#### (c) Deferred awards

Selected members of management in ABG's subsidiaries are entitled to deferred variable remuneration under a Management Incentive Programme based on pre-defined objectives and thresholds of performance. Annual amounts of such variable remuneration, in accordance with the said programme, are used

to purchase shares in ABG, which purchases are deferred over a three year period, with annual vesting. Total amounts of deferred variable remuneration amounted to \$3,541,544 (2014: \$2,931,708).

#### (d) Severance pay – Nil (2015-2014)

Al Baraka Banking Group B.S.C.

To be completed in accordance with BR -1.3.1

Details of Remuneration Paid For The Financial Year Ended 2015

(USD in '000)

Categories of Employees	No.	Fixed Remuneration			Variable Remuneration						Total
		Salaries and Wages	Other Benefits & Allowances	Total	Performance Bonuses (in Cash)	Performance Bonuses (in Shares)	Other Performance Linked Incentives	Deferred Compensation paid during the period	Others	Total	
1. Members of the Board										0	0
2. Approved persons (not included in 1,3 to 7.)										0	0
3. Approved Persons in risk management, internal audit, operations, financial controls, AML and compliance functions										0	0
4. Employees engaged in risk taking activities (business areas)	2	1,653	621	2,274	1,890	2,835				4,724	6,999
5. Employees, other than approved persons, engaged in functions under 3.	7	1,911	600	2,511	471	707				1,178	3,689
6. Other employees										0	0
7. Outsourced Employees/Service providers (engaged in risk taking activities )										0	0
<b>Total</b>	<b>9</b>	<b>3,564</b>	<b>1,221</b>	<b>4,785</b>	<b>2,361</b>	<b>3,542</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>5,903</b>	<b>10,688</b>

The aggregate remuneration paid to BARC members during the year in the form of sitting fees amounted to US\$ 42,623; other details concerning BARC memberships are disclosed elsewhere in the annual report.