



KHALEEJI
COMMERCIAL
BANK | المصرف
الخليجي
التجاري

Growing with Focus

Annual Report 2014

بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ



His Royal Highness
Prince Khalifa bin Salman
Al-Khalifa
The Prime Minister of
the Kingdom of Bahrain



His Majesty King Hamad
bin Isa Al-Khalifa
The King of the
Kingdom of Bahrain



His Royal Highness Prince
Salman bin Hamad
Al-Khalifa
The Crown Prince, Deputy
Supreme Commander and
First Deputy Prime Minister
of the Kingdom of Bahrain

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Khaleeji Commercial Bank BSC
Harbour Tower East
Bahrain Financial Harbour
P.O. Box 60002
Manama, Kingdom of Bahrain
Telephone: +973 17 50 50 50
Facsimile: +973 17 10 00 17
Email: info@khcbonline.com

www.khcbonline.com

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BOARD OF DIRECTORS



Dr. Ahmed Khalil Al Mutawa
Chairman



Mr. Abdulrahman Mohammed
Jamsheer
Vice Chairman



Mr. Abdulla Abdulkarim
Showaiter
Board Member



Mr. Bashar Mohammed Al Mutawa
Board Member



Mr. Hisham Ahmed Al Rayes
Board Member



Mr. Khalid Rashid Al-Thani
Board Member



Mr. Mohammed Barrak
Al-Mutair
Board Member



Mr. Mosobah Saif Al-Mutairy
Board Member



Mr. Tariq Qasim Fakhro
Board Member

Khaleeji Commercial Bank is guided by a Shari'a Supervisory Board consisting of three distinguished scholars. This Board reviews the bank's activities to ensure that all products and investment transactions comply fully with the rules and principles of Islamic Shari'a, and consists of:

Dr. Fareed Yaqoob Al-Miftah
Chairman

Dr. Fareed Mohammed Hadi
Executive Member

Shaikh Nizam Mohammed Saleh Yaqoobi
Member

Experience:

- Member of the Supreme Council of Islamic Affairs.
- Undersecretary of the Ministry of Justice & Islamic Affairs - Bahrain.
- Former judge of the high Shari'a Court.
- Former Lecturer at the University of Bahrain.

Qualification:

- Ph.D. from the University of Edinburgh - United Kingdom.

Experience:

- Assistant Professor of Jurisprudence (Fiqh) and Hadeeth at the College of Arts, Department of Arabic and Islamic studies, University of Bahrain.
- Bachelor program Manager in Shari'a for Banking and Finance, University of Bahrain.
- Vice President of the Association of Shari'a scholars in GCC.
- Member of Shari'a Supervisory Board of a number of Islamic banks.

Qualification:

- Ph.D. in Ibn Hazm's Methodology of Jahala, University of Edinburgh - UK.
- Ph.D. in Al-Bukhari's Methodology, University of Mohammed V - Morocco.

Experience:

- Member of the Shari'a council of Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI).
- Member of the Shari'a Board of the Central Bank of Bahrain - Bahrain.
- Member of Shari'a Supervisory Board of the Dow Jones Islamic index.
- Member of Shari'a Supervisory Board of a number of Islamic banks & insurance companies.

CHAIRMAN'S REPORT



Dr. Ahmed Khalil Al Mutawa
Chairman

Dear Shareholders,

In the name of Allah, the beneficent, the merciful, prayers and peace upon the last apostle and messenger, our prophet Muhammad.

On behalf of the Board of Directors, it is my pleasure to present the annual financial statements of Khaleeji Commercial Bank for the year ended 31 December 2014. 2014 marks the Bank's tenth year of operation which has noticed significant economic events. While the regional and global economic environment has seen signs of improvement at the beginning of the year, the world economy however faced challenges and significant pressures on markets resulting from the decline in the oil prices, during the last quarter of the year. The decline in oil prices is expected to put further pressure on financial institutions' and performance.

In 2014, the Bank launched its new three years strategy and business plan. The strategy is based on the market best practices, and in line with the of the Bank's expansion and growth needs. Taking into account the available resources and capabilities of the Bank, the strategy implemented focuses on growing the retail and high net worth business operations, small to medium/commercial business (SME's) through providing innovative products and solutions to cater to each market segment. Furthermore, the strategy focused on improving customer experience by enhancing the banking channels externally to clients and improve the Bank's support operations internally through restructuring the organization and implementing the latest required technology as an enabler and base for growth. I am pleased to report that we have achieved considerable progress in accomplishing key milestones including opening new branches, launching new retail banking products and expanding our consumer finance business.

Overall Performance

Similar to many other financial institutions, the current market environment has had an adverse impact on the Bank, both directly and indirectly. However, I am pleased to report that by adopting a combination of prudent and conservative management, the Bank was able to navigate this difficult period successfully. The Bank has focused on diversifying and expanding its business while maintaining conservative liquidity and capital positions.

Positive indicators of the Bank performance show a growth in total assets from BD 542.2 million in 2013 to BD 591.9 million in 2014, i.e. 9.2% growth from last year. Total net income growth doubled from last year, i.e. BD 14.6 million in 2014 compared to BD 7.0 million reported in 2013. It is worth mentioning that although the Bank has reduced its weighted average profit distributed to depositors, results show that these deposits has actually grown by 9.9%, from BD 391.9 million in 2013 to BD 430.5 million in 2014, which confirm our customer's loyalty and their confidence in the Bank's products and services. Financing assets overall increased by 20.2% over 2013, reaching BD 347.7 million; with Consumer Finance Portfolio reaching BD 78.7 million, a 50.5% growth over 2013. Total Income from Commercial Banking comprises 88.0% of total income as a result of a significant increase in Consumer Finance activities.

As the Bank continued to execute its strategic plan, the Board and the Management conducted a review to ensure that assets, especially those acquired prior to the new business model reflect realisable and fair value. Based on this review the Board decided to take a very conservative view in dealing with the assets which were impaired or likely to be impaired in the short to medium term. Consequently, in 2014 the Bank reported a net profit of BD 3.0 million compared to a net loss of BD 19.2 million in 2013. Furthermore, this will provide considerable stability for the business in the future and will pave the way forward to achieving acceptable results. It is worth mentioning that, the Bank continues to maintain strong liquidity (with 24.9% of the Bank's assets being liquid) and adequate capital (the Bank has a regulatory capital adequacy ratio of 23.3% compared to a minimum regulatory mandated 12%), both comfortably in excess of regulatory requirements.

The Bank will continue to promote and market a full suite of Consumer Finance products which include consumer finance, mortgage finance, auto finance, Visa credit cards, and alternative credit card (Easy 36). In addition, the Bank launched new Shari'a compliant Unrestricted Mudharaba account (Call Account) all of which have attracted positive response from clients. Furthermore, the Bank commits to offer our existing and new customers innovative and attractive products and services that meet their expectations alongside growing the Bank's branch network by adding 3 more branches to better provide clients with accessibility and convenience. It is worth mentioning that the Bank opened its eighth branch in Zinj area during the year. The Bank has also introduced a new and improved Al Waffer account for the upcoming cycle to incorporate bigger prizes and greater chances for clients during the year 2015. The Bank will continue to focus on continued growth and achieving clients' satisfaction, meeting their requirements and expectations by providing competitive products and services. As the Corporate Banking team managed to sign financing deals with some of the major companies and developers during the year. The Bank's investment banking team has been actively managing the portfolio of investment products and Restricted Investment Accounts (RIA), to enhance the value of the assets held in those products and to work towards potential exits.

Organisational Development

The Board believes that to remain competitive in the long run, building organisational capacity, including human capital, is imperative. A committed and well-trained work force is a key enabler in achieving the Bank's long term objectives. In order to achieve our expansion targets the Bank hired 30 employees in 2014, mainly for the Bank's Retail Banking Business. The Bank also continued to invest in the training and development of its Human Resources through external and in-house training programmes and by enhancing the Graduate Trainees' Programme. The Board takes pride in the fact that 97% of the Bank's employees are Bahrainis. In addition, the Bank has continued to support the HRD Fund of the Kingdom of Bahrain, the Waqf Fund, and Tamkeen in addition to providing training opportunities to students from different local and international universities.

Corporate Social Responsibility

The Board believes that, as a growing institution, the Bank has a responsibility to contribute towards the communities in which it operates, and in the past, the Bank has supported several initiatives that provided benefits to the local community. In 2014, a wide range of organisations involved in humanitarian, education, health, sport and other activities received support from the Bank both in cash and in kind. The Bank also, sponsored the Bahrain International Global Reciter Competition, organized by the Ministry of Justice, Islamic Affairs and Endowments under the patronage of His Majesty King Hamad bin Isa Al Khalifa. The Board has a continued commitment to expand these through the Bank's on-going programme of Corporate Social Responsibility.

Looking Ahead

The Board believes that the recent challenges facing the banking sector will continue in 2015 and the Bank will not be immune to these challenges. However, the Board also foresees many opportunities for growing the Bank's business, not only in the primary markets of the GCC, but also in the wider MENA region. In the last five years, the Bank has taken several steps to diversify its assets, revenue streams and widen its customer base. The launch of the Bank's suite of consumer finance products and expansion of the branch network will further support this endeavour.

The key challenge in the medium term would be to build the scale necessary for the Bank to become a leading player in the local and regional market. The Bank will continue to aggressively grow its commercial and retail banking business while exploring other options; which includes viable acquisitions of other entities and asset portfolios as well as forming strategic alliances or merger with other financial institutions. The Board will also continue to expand the Bank's network of branches and distribution channels to reach wider and a larger number of customers.

The Board believes that the Bank has established a solid foundation from which to execute the new Strategic Plan and capitalise on opportunities currently available in the market.

Appreciation

On behalf of the Board, I would like to express my gratitude to His Majesty King Hamad Bin Isa Al Khalifa; His Royal Highness Prince Khalifa Bin Salman Al Khalifa, the Prime Minister; and His Royal Highness Prince Salman Bin Hamad Al Khalifa, the Crown Prince and Deputy Supreme Commander of Bahrain Defence Force and First Deputy Prime Minister for their encouragement of the growth of the private sector and the development of the banking and finance industry in Bahrain. I also extend my thanks to all government ministries and the Central Bank of Bahrain for their continued guidance and support.

Special appreciation is due to the Bank's shareholders, clients and business partners for their on-going confidence and loyalty; and to the Bank's management and staff for their hard work and dedication.

Allah the almighty is the purveyor of all success.

Dr. Ahmed Khalil Al Mutawa
Chairman

EXECUTIVE MANAGEMENT REPORT



Mr. Khalil Ismaeel Al-Meer
Chief Executive Officer

Although the world economy remained in recovery mode during 2014 with sluggish improvement, the GCC markets witnessed substantial activity despite the impact of weakening oil prices that were felt during the second half of the fiscal year. Notwithstanding instability in the global crude oil sector, the region has emerged as one of the most energetic in the global economy with robust non-oil growth and enhanced levels of Government-led project spending. As well as a firm commitment from the GCC governments to support economic activity and priority projects, the resilience of the non-oil economy is further supported by healthy financial sectors.

In Bahrain, favourable trends emerged in the Kingdom's economy. The launch of a number of important infrastructure projects, together with strengthening domestic demand drivers, supported a pronounced pick up in the economy's growth, however, the recent decline in oil prices has impacted sentiment and is a major setback for the economy's advancement. Bahrain's banking sector remains financially sound with the Islamic banking sector posting profits after substantial consolidation in 2013.

Against this challenging backdrop, the Bank maintained its long-term customer-centric strategic focus of growing the retail banking business and expanding the branch network. Building on significant strategic milestones achieved over the past years, in terms of the expansion of its distribution network and product range, the bank successfully expanded the retail banking and corporate banking asset portfolios with an increased focus on small and medium enterprises.

RETAIL BANKING

2014 was a year of growth and innovation for the Retail banking business. The Bank launched a number of pioneering products including the 'first of its kind' Call Mudharaba Account facility. The innovative account combines the flexibility and convenience of a current account with the Mudharaba investment account's concept of profit sharing. Other additions to our growing array of consumer products included the Easy 36 Card, the Bank's newest credit card. The card, which is approved on the VISA network, offers customers added flexibility and comfort with 36 equal monthly installments.

Aligned with our mission to provide customers with products that offer extra benefits, the Bank increased the prize offerings available on our popular Al-Waffer savings account, an unrestricted investment account that offers clients monthly, quarterly and annual prizes on their investment. The total Al-Waffer prize money was increased to USD 1.2 Million, while additional prizes; including luxury cars were added to the prize pool. As a result of these added benefits, the Bank's Al-Waffer accounts increased by 62% during 2014. Total cash prizes of USD \$1 million were distributed to 240 winners over the 12 months of the program in addition to 4 luxury cars. The grand draw was held in December 2014 for a total prize of US\$250,000.

The Bank also connected with its customers through a number of advertising campaigns that highlighted our enhanced product offerings as well as new and improved customer benefits. These included a consumer finance campaign promoting the Bank's offer of Gulf Air airmiles equivalent to financing amounts up to BD200,000 an offer that was very well received by customers. Further underscoring our commitment to offering our customers more, the Bank signed an agreement with the airline that entitles the Bank's credit card holders to receive exclusive discounts on their online ticket purchases. In addition to an enhanced Al-Waffer offering and Gulf Air benefits, the Bank introduced a 120-day grace period as part of its Personal Finance campaign in 2014.

The heightened promotional and marketing activities produced positive results for the Bank. The consumer finance asset portfolio, which includes Ijara, personal finance, and auto finance, more than doubled during the year - growing 50.5% to reach BD78.7 million. Customer

deposits also grew by 9.9% across all segments to BD430.5 million, with a 16.1% growth in Unrestricted Investment Accounts. This positive growth in customer deposits is attributable to the expanded branch network in addition to increasing market awareness about the Bank and its products.

Major milestones in the implementation of the Bank's expansion strategy were reached during 2014. Our Zinj branch was opened, taking the total branch network to eight, while a standalone ATM was installed in King Hamad Hospital. The branch network, including new branches in Rifaa and Hidd's Lulu Mall, are strategically located, designed and staffed to attract and serve a large number of potential customers, and provide a comprehensive range of banking services. Testament to the successful implementation of our corporate strategy, the Bank's customer base increased by 22.7% during the year.

2015 is looking bright for the Bank's retail banking business. We are optimistic that the local economy and market conditions are on a positive growth trajectory, and believe the Bank is well positioned to capitalise on emerging opportunities.

CORPORATE BANKING

2014 witnessed positive growth in the demand for credit in Bahrain, and the Bank was well placed to maximise on the opportunities that this presented. We continued to nurture existing relationships with our corporate banking clients while building new relationships and expanding the business. New business of BD98 million was booked in 2014, and the Bank achieved a net growth in assets totalling BD30.5 million. The Bank continued to actively promote Tamkeen's financing scheme, which we believe will facilitate the opening of new opportunities in the near future. The portfolio under the Tamkeen scheme reached BD13.9 million at the end of 2014.

During the year, the Bank undertook a detailed review of the financing portfolio in order to identify assets that are impaired or likely to be impaired in the short to medium term. Based on this review, the management and Board adopted a conservative view and made provisions for all identified assets, resulting in substantial increase in impairment provisions.

The Bank also signed a new corporate financing deal for the construction of Al Salam Hospital, a new specialist hospital in Bahrain. The deal will see the Bank play an integral role in raising the standard of healthcare services in Bahrain. In addition, the Bank signed an agreement with Tamkeen to increase the enterprise-financing portfolio to BD 25 million, a programme that will ensure the availability of low-cost financial solutions for the Kingdom's small and medium enterprises. Emphasising our commitment to supporting industry and economic growth in Bahrain, the Bank signed Memorandum of Understandings with a number of the Kingdom's property developers, including Dadabhai Development and Properties, The Developers Real Estate Development, and Dilmunia to provide credit facilities for their potential buyers.



Leading
Change

INVESTMENT BANKING

Although fundamental to the Bank's growth and success in the early years after the Bank's inception, the Investment Banking business was adversely impacted by the Financial Crisis, with a particularly unfavourable impact felt on the business environment and valuations of investments. As a result the Management are focused on protecting and adding value to the Bank's existing investments under management while working towards potential exits.

Aligned with this focus, the Bank sold 7 villas within the Oryx Hills Project and will endeavour to sell the remaining 25 units at favourable levels in 2015. Marketing efforts will continue for other Bahrain based assets maintained by the Bank.

Underscoring the Bank's commitment to addressing the Kingdom's demand for affordable housing solutions, the Bank is establishing joint ventures with reputable partners to develop affordable housing projects in Bahrain's high demand areas.

On the regional and global front, the Bank achieved a full exit from 2 of its real estate investments, Jawhara Green Investment in Qatar, and the Al Hareth Fund in France, and continues to pursue revised long-term joint development exits on its Indian investments.

While exit dates have been extended for many of the Bank's investment products, the Investment team continues to evaluate and explore all possible opportunities to exit from these investments. With regards to the fixed income segment, the total Sukuk portfolio increased by 23.8% to reach BD6.9 million by end of 2014.

Moving forward into 2015, and aligned with the Bank's investment strategy, we will remain focused on booking liquid investment assets in the listed equity field.

TREASURY

The Treasury division continues to be a fundamental contributor to the operation of the Bank. During 2014, the total Sukuk portfolio increased by 23.8% on the previous year. Yield on Sukuks was 3.1% by end of the year and total placements with FI's were reduced by 8.1%, from BD 82.7 million in December 2013, to BD 76 million at December 2014. Yield was 0.7% as of December 2014 while total placements from FI's were reduced by 3.4%, from BD 25.1 million in December 2013, to BD 24.2 million in December 2014. Cost was 0.59% as of December 2014. FX gain was reported at BD 435 thousand in 2014 compared to BD 293 thousand in 2013.

ORGANISATIONAL DEVELOPMENT

Throughout 2014, the Bank continued to strengthen organisational capacity in line with the growth in size and scope of the business. Attracting, developing and retaining superior talent in order to build a high performance, committed team remains a key organisational goal. In order to achieve this, we encourage a corporate culture that values learning, and nurture an environment conducive to the learning process. The Bank invests heavily in training programs that empower our staff with the relevant skills and knowledge, and ensure all employees are kept abreast of changes in the market that relate to their specialisation. As well as challenging and developing our staff to reach their full potential, the Bank plays a key role in preparing Bahrain's youth to be a value added part of the country's future workforce, and during the year the Bank provided training opportunities for university and INJAZ Bahrain students. The Bank also lent its support to the Waqf Fund.

In terms of the Bank's organisational structure, several changes were implemented, effective September 2014, in an effort to further enhance organisational efficiency and effectiveness, and support the successful implementation of the new three-year corporate strategy.

OPERATION

The Bank leverages state of the art technology in order to build the business and improve the customer experience. During 2014, the Bank's information technology Infrastructure was improved by upgrading the core banking system to the latest version, which will provide additional functionalities as well as improved performance.

Nine key processes related to trade finance, the sale and purchase of commodities, account blocking, and the issuance of various consumer finance letters were automated, while new upload features for inward salary processing and bulk payments were implemented. A number of other enhancements are also in development that will further streamline the Bank's processes and procedures.

The year saw the Operation department play a key support role in the successful completion of a number of significant projects. These included the installation of two new ATM machines, one in King Hamad University Hospital, and the second in Zinj Branch, and the launch of the Easy 36 Credit Card. Several projects are also in progress including the "Verified by Visa" (VbV), the Internet Banking upgrade project, and the Middleware upgrade "IRB upgrade Phase II" among others.

The Operations division will continue to play an invaluable role in supporting the Bank in the achievement of its goals. The division will be actively involved in the upgrade operations of Internet banking services as well as the monitoring of transactions through this channel of distribution.

CONCLUSION

Reflecting on the myriad of business challenges that 2014 presented, the Bank performed considerably well, and the Management and Board are confident that the Bank is well positioned to capitalise on opportunities available locally and regionally.

Based on our new corporate strategy, we will remain focused on diversifying the Bank's revenues, assets and customer base, and will grow the Bank's retail banking business by enhancing our product and service offerings. In the medium term, plans are in place to further expand the Bank's branch network and enhance delivery channels, while opportunities in regional markets beyond the borders of Bahrain will also be explored.

I would like to take this opportunity to thank the Board of Directors for their continued support and guidance, the Central Bank of Bahrain and the Bahrain Bourse for their guidance, and our customers for their loyalty and continued confidence. I also express my sincere gratitude to our dedicated staff; your hard work, creativity, and commitment is a key part of our success and a vital component of our success as we move forward towards an even brighter future.



Mr. Khalil Ismaeel Al-Meer
Chief Executive Officer



Mr. Silvan Varghese
*Chief Operating Officer
(Retd. 30 June 2014)*



Mr. Fuad Ali Taqi
DGM - Commercial Banking



Mr. Mahdi A. Nabi Mohammed
DGM - Support Services



Mr. Salah Khalifa Mohammed
Head of Corporate Banking

CORPORATE GOVERNANCE

Corporate Governance Structure

The Bank's corporate governance framework focuses on Board responsibility, oversight and management accountability vis-à-vis governing regulations and better practices. The framework is in line with global best practices and regulatory requirements which seek to balance entrepreneurship, control and transparency, while creating value for all stakeholders.

Corporate governance, the way the Board and Management is organized and how they operate in practice ultimately aims at leading the Bank towards successfully meeting its strategic objectives. The Board of Directors is accountable to the Bank's shareholders for the creation and delivery of strong sustainable financial performance and long-term shareholder value. To achieve this, the Board approves and monitors the Bank's strategy and financial performance, within a framework of sound corporate governance and effective risk management.

The Bank is in compliance with the Corporate Governance Code (CGC), the Public Disclosure Module and the Stock Exchange Disclosure Standards set by the CBB. The corporate governance philosophy of the Bank is to be fully ethical and transparent in all dealings. In pursuit of this goal the Board of Directors have approved a Corporate Governance Framework, Director's Conflict of Interest Policy, and the Bank Key Persons' Dealing Policy. The Bank, through its Board and Committees, endeavors to deliver the highest governing standards for the benefit of its stakeholders.

The Bank is committed to continuously reviewing and developing its corporate governance standards to ensure compliance with the requirements of the revised corporate governance framework being implemented by the Central Bank of Bahrain and other regulatory bodies, and also to keep abreast with international best practice.

Board of Directors

The Board of Directors comprises of 9 members. The chairman of the Board of Directors is charged with regular supervision and assessment of executive management and is responsible for leading the Board, ensuring its effectiveness, monitoring the performance of the CEO and maintaining a dialogue with the Bank's stakeholders. The Board has constituted certain committees with specific delegated authorities to oversee and guide the management in specific areas of the Bank's operations and decision-making. The Board, either directly or through its various committees, will oversee the management of the Bank.

Board Committees Structure

The Board of Directors has constituted three committees with specific delegated authorities.

- Board Audit and Risk Management Committee (BARMC), which is responsible for internal and external audit, compliance and anti-money laundering. Beside its responsibility in ensuring that the Bank's overall risk management framework is effective and that key risks are managed within parameters established by the Board (During the year, the Board Audit Committee (BAC) and the Board Risk Management Committee (BRMC) were merged into one committee Board Audit and Risk Management Committee (BARMC).
- Board Investment & Credit Committee (BICC), which is responsible for investment and credit approvals, setting limits and tolerances for different risks, asset liability management, monitoring asset impairment and creation of loss provisions, maintaining banking relationships, as well as for the oversight of the off-balance sheet vehicles.
- Board Nominations, Remunerations and Governance Committee (BNRGC), which is responsible for setting policies for compensation and incentives, human resources and administration. It is also responsible for the corporate governance framework of the Bank.

The Chairman, the Board of Directors and the Board Committees have direct access to the heads of Internal Audit, Risk Management, Regulatory Compliance and Shari'a Compliance.

Meetings of the Board and its committees are held as and when required but in accordance with the Regulations the Board meets at least once a quarter. The Board of Directors met seven times in 2014. The Bank held its AGM on 18 March 2014. In addition to physical meetings, several written resolutions were circulated to the Directors during 2014 for approval by mail and facsimile.

During the year, the Board Audit Committee (BAC) and the Board Risk Management Committee (BRMC) both held one meeting each before being merged into one committee - the Board Audit and Risk Management Committee (BARMC). The BARMC held 3 meetings subsequent to the merger, the Board Investment and Credit Committee (BICC) held 4 meetings, and the Board Nominations, Remunerations and Governance Committee (BNRGC) held 5 meetings.

Executive Management Committees

The Board of Directors delegates the authority for day-to-day management of the business to the Chief Executive Officer (CEO) who is responsible for implementing the Bank's strategic plan. The CEO manages the Bank through the following management committees:

BOARD OF DIRECTORS COMMITTEE



EXECUTIVE MANAGEMENT COMMITTEE



RISK MANAGEMENT

Risk Management Framework

Risk is inherent in the Bank's business and effective management of risk is seen as a core requirement to create shareholder value. It is a process by which the Bank identifies key risks, sets consistent understandable risk measures, chooses which risk to mitigate, transfer, avoid or accept and by what means and to establish procedures to monitoring the resulting risk position. Effective risk management is the cornerstone of sound operating performance and capital structure. The Board of Directors of the Bank has an overall responsibility for establishing the Bank's risk culture and ensuring that an effective risk management framework is in place. The Board approves and periodically reviews the risk management policies and risk strategies of the Bank. Risk Management is a process by which the Bank identifies key risks, sets risk measures and establishes procedures to monitor the residual risk and is driven by the objective of controlling risk to ensure that value is created for shareholders.

The Bank is exposed to risks, which include, but not limited to, credit, market, liquidity, reputational and operational risk. The bank's aim is to achieve an appropriate balance between risk and return and minimise any potential adverse impact on its financial performance.

The assumption of risks by the Bank is guided by certain fundamental principles such as protection of investor and shareholder funds by the adoption of sound credit and investment analysis, adoption of effective "risk reward" strategy to optimize stakeholders' returns, and adherence to prudent levels of exposure concentration.

The Board has established an Executive Risk Management Committee (ERMC), which is responsible for developing and implementing the Bank's risk management policies and procedures in all areas of the Bank's operations. The committee consists of Heads of Business units and other functional/support units in the Bank, meets on a monthly basis and reports regularly to the Board Audit & Risk Management Committee.

The Risk Management Department of the Bank, independent of the business units, is responsible for the day to day oversight and management of the various risks faced by the Bank. Head of Risk Management directly reports to the Board Audit & Risk Management Committee and administratively to the Chief Executive Officer. The Risk Management Department, together with the Internal Audit and Compliance Departments, provides independent assurance that all types of risk are being measured and managed in accordance with the policies and guidelines set by the Board of Directors.

Risk Management Policies

The Bank's risk management policies are established to identify and analyze the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor adherence to such limits. The Bank's risk policy as approved by the Board of Directors, analyses and sets out the risk appetite by way of limits for Credit Risk, (includes concentration risk) liquidity risk, market risk (Including profit rate risk and currency risk) and Capital Adequacy. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, as well as products and services offered. The Bank, through its training, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and responsibilities and their accountability. The Bank's risk management policies identify approval authorities, reporting requirements, and the procedures for referring risk related issues to executive management, ERMC and the Board, as appropriate. Policies are in place to address all major categories of risk including liquidity, investment and credit, market, currency, operational, legal, Reputational, and regulatory risks.

Credit and Investment Risk

The Bank has well defined policies for managing credit and investment risks. These include delegated approval authority limits, concentration limits, maximum exposure limits, etc. Credit and investment risk is defined as the potential that the Borrower or counter party will fail to meet its obligations in accordance with the agreed terms. Credit and investment limits to clients are approved after thorough assessment of counterparty's past track record and financial position as well as legal and market risks associated with it. In most cases exposures are fully or partially secured by acceptable collateral securities. The Board of Directors has delegated the responsibility for the management of Credit and Investment risk to its Executive Risk Management Committee (ERMC). A separate Risk Management Department independent of the business units are responsible for the oversight of Bank's Credit and Investment risk. The Risk Management Department reviews every credit and investment proposal and records its recommendation before the same is submitted for approval. Fair valuation of the investments are reviewed by the Investment and Financial Control departments along with Risk Management and impairment tests done for credit exposures on quarterly basis as per the Bank's approved policies. This exercise is performed by Risk Management Department and is followed by a review by the external auditors. It is the Bank's policy to ensure that adequate provisions are made for expected credit or investment losses. The Bank's policy on Impairment & Provisioning lays down guidelines for the creation of adequate allowance for impairment losses that represents the estimated future loss on its portfolio. Cross border exposures, exposures to sovereigns, banks and other financial institutions are guided by risk limits set for these entities and approved by the Board of Directors based on various risk factors. The exposures are regularly monitored by the management to ensure that they remain within the set risk appetite.

The Credit Management department ensures that credit facilities are only released upon obtaining the required approvals and documentation. Exceptions if any are duly approved by the appropriate approval authority. It also monitors excess over limits, pastdues, overdue reviews and exceptions to the policy and escalates to the relevant committee. It also follows up on all pending documentation, irregularity if any, and monitoring of non performing accounts and for the purpose of provisioning. All relationships and investments are reviewed annually and non performing accounts are reviewed more often. Problematic accounts are reviewed regularly to evaluate and 'work out' strategy adopted.



إستثمر أكثر لتربح أكثر جائزة كبيرة كل شهر BMW 520 أو \$50,000

يمكنك حساب الوافر من المصرف الخليجي التجاري هذا العام فرصة رائعة لتفوز بجائزة كبرى شهرياً، يمكنك الفوز بجائزة نقدية تبلغ \$50,000 دولار أمريكي أو سيارة BMW 520 بالإضافة إلى الجوائز النقدية الشهرية الأخرى كما يمكنك أيضاً الفوز بالجائزة النقدية الكبرى و التي تبلغ \$200,000 دولار أمريكي في نهاية العام. ليس عليك إلا فتح حساب بمبلغ 50 د.ب. و إبقاء المبلغ في الحساب لفترة لا تقل عن شهر واحد من موعد السحب. • متوافق مع احكام الشريعة الإسلامية • متاح لجميع الجنسيات

استثمر في العام الجديد و اربح الكثير!!
افتح حساب الوافر اليوم و استمتع بجوائز الوافر الكبرى!!

قدم طلبك اليوم

* تطبيق الشروط والأحكام

للمزيد من المعلومات اتصل على هاتف رقم 17 54 00 54
أو تفضل بزيارتنا على الموقع الإلكتروني www.khcbonline.com

Market Risks

Market risk is the risk that changes in market parameters, such as profit rates, equity prices, foreign exchange rates and credit spreads, (not relating to changes in the obligor's / issuer's credit standing), will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while optimizing the return on risk.

- In 2014 the bank has developed a comprehensive Sukuk Trading and Sukuk Fund Participation policy duly approved by the Board of Directors. The primary objective being Trading in Sukuks and participation in Sukuk funds and or other fixed income shari'a compliant structured products as a part of Treasury Business. The policy sets clear guidelines for Sukuk Trading and participation in Sukuk funds, limits, Target market, sectors, country, tenor, Stop loss triggers and actions and reporting. The portfolio is monitored on a mark to mark basis and reported to the ALCO.
- The Board of Directors have also approved in 2014 a comprehensive policy for Investments in listed Equity through managed 3rd party funds or discretionary portfolio with the aim of maximizing return within certain set parameters and limits. Such investments are governed by the overall risk appetite of the bank, regions, acceptable returns, target markets, sectors, stop loss limits and triggers.
- The ALCO committee reviews these investments as part of the overall monitoring of cash management and treasury and investment activities of the Bank.
- These sukuks are covered at fair value for the purpose of financial reporting and for Trading on a mark to market basis and likewise for Investments in listed equity portfolio through managed funds or discretionary portfolio.
- For the purpose of regulatory reporting, these sukuks form part of trading books and are subject to specific market risk (based on external ratings) and general market risks (based on residual maturity) for the purpose of computing capital charge for market risk.

Operational Risk

Operational risk is the risk of loss arising from inadequate or failures in systems processes, people or those related to external events. It is inherent in every business organisation and covers a wide range of issues. Failure to manage operational risk can result in to financial, reputational losses as well as legal, compliance and regulatory consequences. The Bank manages operational risk through on-going monitoring of the control environment that the Bank operates in. This includes maintenance of well-defined policies and standard operating procedures; continuous monitoring of predefined risk triggers and Immediate escalation of operational risk incidents reporting to the management. The Bank ensures operational risk is thoroughly and closely managed on daily basis. As part of the operational risk assessment, the Bank also manages its Information Security risk through the Risk Management department. The bank has a dedicated staff for Information security Management to manage the Information security posture of the bank and its process to comply with regulatory, legal and business requirements.

The Risk Management Department is responsible for the identification monitoring and management of operational risk in the Bank through the operational risk management system. A Board approved operational risk framework is also in place. The operational Risk management framework is guided by the following principles:

- Management of operational risk is the responsibility of the senior management of each segment of business;
- Appropriate and regular management reports;
- Risk assessment of critical businesses to identify risks facing each department and the risk inherent in its process and products. Periodic reviews to ensure that the circumstances under which they were identified have not changed significantly,
- Collection of operational risk loss data and reporting individual cases to senior management.
- All risks are identified and loss data reported are analysed for underlying causes and mitigants put in place.

The Risk Management Department on periodic basis conducts operational risk assessment on each department of the Bank and provides recommendation for process enhancements. The Risk Management department also provides ongoing awareness on operational risks to all staff members. Operational risks findings are periodically reported to the ERM and the Board.

Management of operational risk is the responsibility of Senior Management of each segment of business unit. While the responsibility of overseeing the process lies with Operational Risk Unit in accordance with the Operational Risk Management Framework. Internal Audit independently reviews effectiveness of the Bank's internal controls and its ability to minimize the impact of operational risks.

Business Continuity Management

Within the Bank is the implementation and management of preventative measures, planning and preparation to ensure the Bank can continue to operate following an incident, significant unplanned event or major operational disruption. The Bank ensures that its systems and procedures are resilient to ensure business continuity through potential situations of failure. The Bank has put in place Business Continuity Plans (BCP) to ensure that its business runs effectively in the event of most unforeseen disasters as required by the Central bank Business Continuity Guidelines. The Bank continuously strengthens and enhances its existing plans by implementing a robust business continuity framework to ensure that its systems and procedures are resilient and ready to meet 'emergency situations.'



Liquidity Risk

Liquidity risk is defined as the risk of failure in meeting liquidity requirement to the Bank's customers and investors when they fall due (i.e. funds not available to meet liabilities). The policy guidelines for the management of liquidity risk are laid down by the Board of Directors. The Treasury Department of the Bank is responsible for liquidity management in the Bank on a daily basis under the guidance and supervision of Asset Liability Management Committee (ALCO). The liquidity risk policy sets liquidity limits, targets, and rations to aid a strong liquidity management. and liquidity. Any breaches or deviations are reported to the Asset Liability Management committee (ALCO), which is chaired by the CEO and has senior executives of the Bank as members. The ALCO committee periodically monitors the level of liquid assets maintained by the Bank and follows a maturity laddered approach for managing liquidity risk In the short and long term of business cycle. The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity, adequate product mix and the right maturity profile to meet its liabilities under both normal and stressed conditions, without incurring unacceptable losses or causing damage to the Bank's reputation. The Bank's main source of funding is from customer deposits, and Interbank deposits and borrowings. The bank also monitors for any concentration of customer deposit base. Contingency plans are in place to withstand any specific or incidental market crisis and are reviewed by the ALCO periodically.

Profit Rate Risk

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair value of financial instruments due to changes in market profit rates. The Bank's policy on profit rate risk management aims to enable identification, measurement, monitoring, control and reporting of profit rate risks in a timely manner. Profit rate risk is managed principally through monitoring profit rate gaps and by having pre-approved limits for re-pricing bands. The management of profit rate risk against profit rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and nonstandard profit rate scenarios. Positions are monitored on a periodic basis to ensure they are maintained within the established limits.

Foreign Exchange Risk

Foreign exchange risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank's foreign exchange risk is managed on the basis of limits on net open positions set by the Board of Directors and a continuous assessment of current and expected exchange rate movements. The management of foreign exchange risk against net exposure limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various foreign exchange scenarios. The Bank does not engage in foreign exchange trading and, where possible, matches currency exposures inherent in certain assets with liabilities in the same or correlated currency. The Risk Management Department in association with the Treasury Department is responsible for all operations related to foreign exchange risk management in the Bank.

Legal and Regulatory Risk

Legal risk includes the risk of unexpected loss from transactions and/or contracts not being enforceable under applicable laws or from unsound documentation. Legal and regulatory risk may also arise from litigation initiated by clients against the Bank on certain transactions. The Bank has a full-fledged legal department which provides necessary inputs and guidance to all other departments on any legal issues that may arise. The Bank also hires external legal advisors for advice when necessary, and to handle litigations. Regulatory risk includes the risk of non-compliance with regulatory and legal requirements. The Bank has an independent compliance department which monitors the level of compliance with regulatory requirements by other departments of the Bank. It also acts as the focal point in all interaction with the Central Bank of Bahrain. The Compliance Department is also responsible for the Bank's anti-money laundering initiatives.

Capital Adequacy & the Internal Capital Adequacy Assessment Process (ICAAP)

The Bank's regulatory capital adequacy ratio is calculated in accordance with the guidelines issued by the CBB. Under this the Bank is expected to maintain a minimum prescribed ratio of total capital to total risk weighted assets. The CBB also requires the Bank to establish a process to monitor the overall capital adequacy of the Bank, taking into account all relevant risk factors. The Board of Directors has approved an Internal Capital Adequacy Assessment Process (ICAAP) to satisfy this requirement. The ICAAP is a requirement under Pillar 2 of the Basel II accord in line with the CBB requirements which seeks to ensure appropriate identification, measurement, aggregation and monitoring of all risks the Bank is exposed to and to relate the level of internal capital of the Bank to its overall risk profile and business plan. The Bank has adopted a structured approach for identifying and assessing capital required for each of the major risk categories by employing appropriate methodologies. The total of such individual risk capitals is taken as the overall capital requirement. The ICAAP also incorporates guidelines to assess the future capital needs of the Bank in line with its business plans over its strategic time horizon.

Stress Testing

Regulatory and internal capital adequacy computations are based on past data. While future projections are done, these are on the assumption that the business environment continues to be normal. It is essential for the Bank to measure sensitivity of its capital to serious adverse changes in external and internal risk environment and changes in business cycles. The Bank has developed a stress testing model for the purpose which provides an estimate of capital adequacy under a variety of stress scenarios. The first step in the process is identifying relevant stress factors that can affect the bank's revenues, liquidity, asset quality, business growth etc. Each item in the Bank's balance sheet is then re-valued on the basis of different combinations of these risk factors and at various levels of severity. The capital adequacy levels at these stress scenarios are computed on current as well as forecasted balance sheets to identify the likely worst case scenarios which will help the Bank identify preventive management actions where necessary. The Risk Management Department conducts such stress tests twice in a year and the results are reported to the Board of Directors along with suggested remedial actions if necessary.

Reputational Risk

Reputational risk arises when a business practice or an event has the potential to materially and negatively influence the public and stakeholder's trust and confidence in the whether the perception is true or no. Reputation may be intangible but it is a highly prized asset. Failure to manage this risk, can have serious impact on the Bank's business which may also lead to costly litigation that would in turn have an adverse impact on liquidity and capital adequacy of the Bank. Strong corporate reputation is an invaluable asset to any organization and if ever diminished, it's the most difficult to restore among all the other assets of the organization. Reputation has a vital impact on the long term prosperity of the organization. The senior management, through the relevant committees, examines issues that can have adverse impact on the Bank's reputation and issues guidelines to address these. The Bank also under its ICAAP provides separate capital against this risk.

Disclosures

The Bank recognizes its continuous disclosure obligations set forth by the Central Bank of Bahrain (CBB), Bahrain Stock Exchange and other relevant regulatory bodies. The Bank has approved policies related to external communications & disclosures in line with Basel II & CBB requirements which ensure disclosure of all relevant information to stakeholders in a timely manner. The Pillar 3 disclosure and Corporate Governance Code requirements prescribed by the Central Bank of Bahrain (CBB) are part of this annual report.



FOR THE FINANCIAL YEAR ENDING 31 DECEMBER 2014

In the name of Allah, the Beneficent, the Merciful

Prayers and Peace Upon the Last Apostle and Messenger, Our prophet Mohammed, His Family and companions.

The Shari'a Supervisory Board ("SSB") of Khaleeji Commercial Bank has reviewed the Bank's activities through its annual review and through the shari'a compliance department and compared them with the previously issued fatwas and rulings during the financial year ending 31st December 2014 and found them compatible with the already issued fatwas and rulings.

The Shari'a Compliance Department in collaboration with the SSB has audited the Shari'a aspects arising from the Bank's businesses for every three months so the audit happens on a quarterly basis, and submitted its report to the SSB, which in turn, reviewed the observations contained therein, and emphasized that the management must be in compliance with the rules and principles of Islamic Shari'a. The SSB has decided based on this report and the jobs done by Shari'a Compliance Department to supervised the Banks adherence to the decisions and fatwa's of the SSB under rules and principles of Islamic Sharia'a.

The SSB believes that it has expressed its opinion in respect of the activities carried on by the Bank and it is the responsibility of the management to ensure the implementation of such decisions. It is the duty of the SSB to express an independent opinion on the basis of its control and review of the Bank's operations and to prepare a report about them.

A representative of the Bank's management explained and clarified the contents of the Balance Sheet, attached notes and Income Statement for the financial year ended on 31st December 2014 to our satisfaction. The report of the SSB has been prepared based on the contents provided by the Bank.

The SSB is further satisfied that any income which is not in compliance with the Glorious Islamic Shari'a has been dispersed to charity account and that the responsibility of the payment of the Zakat lies with the shareholders in their shares.

The SSB is satisfied that the Bank's activities and services are in compliance with the Glorious Islamic Sharia'a.

Praise be to Allah, Lord of the Worlds.

Prayers on Prophet Mohammed (Peace Be Upon Him), all his Family and companions.

Dr. Fareed Yaqoob Al-Miftah
Chairman

Dr. Fareed Mohammed Hadi
Executive Member

Shaikh Nizam Mohammed Saleh Yaqoobi
Member

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Khaleeji Commercial Bank B.S.C. ("the Bank") and its subsidiaries (together the "Group"), which comprise the consolidated statement of financial position as at 31 December 2014, the consolidated statements of income, the changes in equity, cash flows, changes in restricted investment accounts and sources and uses of charity and zakah fund for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Respective responsibilities of board of directors and auditors

These consolidated financial statements and the Group's undertaking to operate in accordance with Islamic Shari'a rules and principles are the responsibility of the board of directors of the Bank. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

Basis of opinion

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by Accounting and Auditing Organisation for Islamic Financial Institutions. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2014 and of its consolidated results of operations, its consolidated cash flows, its consolidated changes in equity, its consolidated changes in restricted investment accounts and its consolidated sources and uses of charity and zakah fund for the year then ended in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and the Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank.

Report on other regulatory requirements

As required by the Bahrain Commercial Companies Law and Volume 2 of the Central Bank of Bahrain (CBB) Rule Book, we report that:

- the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith;
- the financial information contained in the chairman's report is consistent with the consolidated financial statements;
- we are not aware of any violations during the year of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 2 and applicable provisions of Volume 6 and CBB directives), the CBB Capital Markets Regulations and associated resolutions, the Bahrain Bourse rules and procedures or the terms of the Bank's memorandum and articles of association that would have had a material adverse effect on the business of the Bank or on its financial position; and
- satisfactory explanations and information have been provided to us by management in response to all our requests.



KPMG Fakhro
Partner Registration No. 137
04 February 2015



CONSOLIDATED STATEMENT OF FINANCIAL POSITION

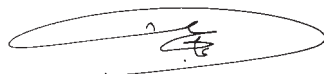
As at 31 December 2014 | BD 000's

	Notes	31 December 2014	31 December 2013
ASSETS			
Cash and bank balances	3	37,358	38,848
Placements with financial institutions	4	76,006	82,745
Financing assets	5	303,943	253,635
Investment securities	6	96,923	90,397
Assets acquired for leasing	7	42,981	32,061
Lease rentals receivable	7	798	3,569
Investment in associates	8	2,604	2,681
Investment property	9	13,715	6,583
Other assets	10	9,079	23,342
Property and equipment	11	8,517	8,381
Total assets		591,924	542,242
LIABILITIES			
Placements from financial institutions		50,208	42,940
Placements from non-financial institutions and individuals	12	43,782	80,912
Customers' current accounts		47,828	18,923
Other liabilities	13	8,115	7,407
Total liabilities		149,933	150,182
Equity of investment account holders	14	338,934	292,049
OWNER'S EQUITY			
Share capital	15	115,416	115,416
Share premium		1,535	1,535
Statutory reserve		6,730	6,425
Treasury shares		(6,351)	(6,351)
Accumulated losses		(14,273)	(17,014)
Total owner's equity (page 24)		103,057	100,011
Total liabilities, equity of investment account holders and owners' equity		591,924	542,242

The consolidated financial statements, which consist of pages 22 to 68, were approved by the Board of directors on 04 February 2015 and signed on its behalf by:



Dr. Ahmed Khalil Al Mutawa
Chairman



Abdulrahman Mohamed Jamsheer
Vice-Chairman



Khalil Ismaeel Al-Meer
Chief Executive Officer

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT

for the year ended 31 December 2014 | BD 000's

	Notes	2014	2013
Management and other fees		738	1,088
Income from placements with financial institutions		568	430
Income from financing assets and assets acquired for leasing		22,882	18,318
Income / (loss) from investment securities	16	1,417	(624)
Share of Income / (loss) from associate companies	8	27	(115)
Other income		844	599
Total income before return to investment account holders		26,476	19,696
Less: Return to investment account holders before Bank's share as Mudarib	14	(12,843)	(13,315)
Bank's share as a Mudarib	14	4,002	4,596
Return to investment account holders		(8,841)	(8,719)
Expense on placements from financial institutions, non-financial institutions and individuals		(3,060)	(3,968)
Total net income		14,575	7,009
Staff cost	17	6,183	5,692
Depreciation	11	627	1,169
Other expenses	19	4,238	4,112
Total expenses		11,048	10,973
Profit / (loss) for the year before impairment allowances		3,527	(3,964)
Impairment allowances	18	(481)	(15,245)
PROFIT / (LOSS) FOR THE YEAR		3,046	(19,209)
Earnings per share			
Basic earnings per share (fils)	24	2.71	(17.11)
Diluted earnings per share (fils)	24	2.71	(17.11)

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2014 | BD 000's

2014	Share Capital	Share premium	Statutory reserve	Treasury shares	Accumulated losses	Total
At 1 January 2014	115,416	1,535	6,425	(6,351)	(17,014)	100,011
Profit for the year	-	-	-	-	3,046	3,046
Total recognised income and expense for the year	-	-	-	-	3,046	3,046
Transfer to statutory reserve	-	-	305	-	(305)	-
At 31 December 2014	115,416	1,535	6,730	(6,351)	(14,273)	103,057

2013	Share Capital	Share premium	Statutory reserve	Treasury shares	(Accumulated losses) / Retained earnings	Total
At 1 January 2013	115,416	1,535	6,425	(6,351)	2,423	119,448
Loss for the year	-	-	-	-	(19,209)	(19,209)
Total recognised income and expense for the year	-	-	-	-	(19,209)	(19,209)
Transfer to zakah fund (2012)	-	-	-	-	(228)	(228)
At 31 December 2013	115,416	1,535	6,425	(6,351)	(17,014)	100,011

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

for the year ended 31 December 2014 | BD 000's

	Notes	2014	2013
OPERATING ACTIVITIES			
Disbursements of financing assets, net		(34,557)	(4,987)
Payment for asset acquired for leasing, net		(8,231)	(11,775)
Management fees received		2,079	850
Income from short-term placements received		568	430
Returns paid to investment account holders		(9,422)	(7,017)
Net receipts from investment account holders		46,885	75,620
Expense paid on placements		(3,060)	(3,968)
Payment for expenses		(8,699)	(10,335)
Other receipts		1,857	651
Payment for charity		(65)	(355)
Receipts in customers' current accounts		28,905	7,528
Placements from financial institutions, net		7,269	(24,792)
Placements from non-financial institutions and individuals, net		(37,130)	27,496
Net payment to CBB reserve account		(1,790)	(4,790)
Net cash (used in) / generated from operating activities		(15,391)	44,556
INVESTING ACTIVITIES			
Purchase of investment securities, net		(41,868)	(25,305)
Proceeds from sale / redemption of investment securities		46,729	15,572
Proceeds from redemption of investment in associate		104	91
Dividend / income from investment securities received		1,170	930
Purchase of equipment and capital advances made		(763)	(422)
Net cash generated from / (used in) investing activities		5,372	(9,134)
Net (decrease) / increase in cash and cash equivalents		(10,019)	35,422
Cash and cash equivalents at 1 January		106,508	71,086
Cash and cash equivalents at 31 December		96,489	106,508
Cash and cash equivalent comprise:			
Cash and bank balances (excluding CBB reserve)	3	20,483	23,763
Placements with financial institutions	4	76,006	82,745
		96,489	106,508

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN RESTRICTED INVESTMENT ACCOUNTS

for the year ended 31 December 2014 | BD 000's

2014	Balance at 1 January 2014			Movements during the year						Balance at 31 December 2014		
	No of units (000's)	Average value per share (BD)	Total (BD 000's)	Investment (with-drawals) (BD 000's)	Revalu-ation (BD 000's)	Gross income / (loss) (BD 000's)	Dividends paid (BD 000's)	Bank's fees as an agent (BD 000's)	Admin-istration expens-es (BD 000's)	No. of units (000's)	Average value per share (BD)	Total (BD 000's)
Al Hareth French Property Fund	17.05	520.12	8,868	(3,512)	(1,052)	(4,304)	-	-	-	-	-	-
Safana Investment WLL (RIA 1)	8,323	1.00	8,323	-	(10)	-	-	-	-	8,313	1.00	8,313
Janayen Holding Limited (RIA 4)	48,082	0.11	5,264	-	5	226	(746)	-	(189)	48,082	0.09	4,560
Shaden Real Estate Investment WLL (RIA 5)	8,100	1.00	8,100	-	-	-	-	-	-	8,100	1.00	8,100
Locata Corporation Pty Ltd (RIA 6)	2,948	0.34	1,001	(8)	-	-	-	-	-	2,633	0.38	993
			31,556	(3,520)	(1,057)	(4,078)	(746)	-	(189)			21,966

2013	Balance at 1 January 2013			Movements during the year						Balance at 31 December 2013		
	No of units (000's)	Average value per share (BD)	Total (BD 000's)	Investment (with-drawals) (BD 000's)	Revalu-ation (BD 000's)	Gross income / (loss) (BD 000's)	Dividends paid (BD 000's)	Bank's fees as an agent (BD 000's)	Admin-istration expens-es (BD 000's)	No. of units (000's)	Average value per share (BD)	Total (BD 000's)
Al Hareth French Property Fund	17.05	497.81	8,487	-	381 ¹	-	-	-	-	17.05	520.12	8,868
Safana Investment WLL (RIA 1)	8,323	1.00	8,323	-	-	-	-	-	-	8,323	1.00	8,323
Janayen Holding Limited (RIA 4)	48,082	0.12	5,532	-	(386)	254	-	-	(136)	48,082	0.11	5,264
Shaden Real Estate Investment WLL (RIA 5)	8,100	1.00	8,100	-	-	-	-	-	-	8,100	1.00	8,100
Locata Corporation Pty Ltd (RIA 6)	3,427	0.38	1,292	(181)	(110)	-	-	-	-	2,948	0.34	1,001
			31,734	(181)	(115)	254	-	-	(136)			31,556

¹ Includes gain or loss on revaluation of foreign currency balances as at the year end.

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF SOURCES AND USES OF CHARITY AND ZAKAH FUND

for the year ended 31 December 2014 | BD 000's

	2014	2013
Sources of charity and zakah fund		
At 1 January	835	910
Contributions by the Bank	-	228
Non-Islamic income	89	52
Total sources	924	1,190
Uses of charity and zakah fund		
Contributions to charitable organisations	65	355
Total uses	65	355
Undistributed charity and zakah fund at 31 December (note 13)	859	835

The accompanying notes 1 to 35 form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2014

1 INCORPORATION AND PRINCIPAL ACTIVITY

Khaleeji Commercial Bank BSC ("the Bank"), a public shareholding company, was incorporated on 24 November 2004 in the Kingdom of Bahrain under Commercial Registration No. 55133. The Bank operates under an Islamic retail banking license granted by the Central Bank of Bahrain ("CBB") on 20 October 2003. The Bank's shares are listed on the Bahrain Bourse.

The Bank's activities are regulated by the Central Bank of Bahrain (CBB) and supervised by a Religious Supervisory Board to ensure adherence to Shari'a rules and principles in its transactions and activities.

The principal activities of the Bank include providing banking and investment products and services to retail customers, high net worth individuals, corporate entities, and financial institutions. These include retail and corporate banking, consumer finance, wealth management, structured investment products and project financing facilities which comply with Islamic Shari'a rules and principles as determined by the Bank's Shari'a Supervisory Board.

The consolidated financial statements include the financial statements of the Bank and its subsidiaries (together "the Group"). The significant subsidiaries are as follows:

Name	Country of incorporation	% holding	Nature of business
Hawafiz Khaleeji Management Company BSC (c)	Bahrain	100%	To hold shares for the beneficial interest of the management incentive scheme. (refer note 20)
Binaa Investment 1	Cayman Islands	100%	To hold investments for the beneficial interest of the Bank.
Harbour Tower West 2 Real Estate SPC	Bahrain	100%	To hold property for the beneficial interest of the Bank.
Harbour Tower West 4 Real Estate SPC	Bahrain	100%	To hold property for the beneficial interest of the Bank.

2 SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies applied in the preparation of these consolidated financial statements are set out below. These accounting policies have been consistently applied by the Group and are consistent with those used in the previous year, except for those changes arising from revised/new AAOIFI financial accounting standards.

New standards, amendments, and interpretations effective from 1 January 2014:

There are no AAOIFI accounting standards, amendments to standards and interpretations that are effective for the first time for the financial year beginning on or after 1 January 2014 that would be expected to have a material impact on the Group.

New standards, amendments and interpretations issued but not effective

The following new standards, amendments to standards and interpretations are effective for annual periods beginning on or after 1 January 2015 and are expected to be relevant to the Group.

FAS 27 - Investments Accounts

FAS 27 Investments accounts was issued in December 2014 replacing FAS 5 - 'Disclosures of Bases for Profit Allocation between Owner's Equity and Investment Account Holders' and FAS 6 - 'Equity of Investment Account Holders and their Equivalent'. The adoption of this standard would lead to enhancing certain disclosures and is not expected to have any significant impact on the financial statements of the Group.

The Bank has no early adopted any new standards during 2014.

(a) Statement of compliance

The financial statements have been prepared in accordance with Financial Accounting Standards ('FAS') issued by the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI). In line with the requirement of AAOIFI and the CBB Rule Book, for matters that are not covered by AAOIFI standards, the Group uses guidance from the relevant International Financial Reporting Standards.

(b) Basis of preparation

The consolidated financial statements are presented in Bahraini Dinars, being the principal currency of the Bank's operations. They are prepared on the historical cost basis except for the measurement at fair value of certain investments carried at fair value.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) Basis of preparation (continued)

The Group classifies its expenses in the income statement by the nature of expense method.

The preparation of consolidated financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. Management believes that the underlying assumptions are appropriate and the Group's consolidated financial statements therefore present the financial position and results fairly. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 21.

(c) Basis of consolidation

(i) Subsidiaries

The consolidated financial statements of the Group comprise the financial statements of the Bank and its subsidiaries. Subsidiaries are those enterprises (including special purpose entities) controlled by the Bank. 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. Subsidiaries are consolidated from the date on which control is transferred to the Group and de-consolidated from the date that control ceases.

Special purpose entities (SPEs) are entities that are created to accomplish a narrow and well-defined objective such as the securitisation of particular assets, or the execution of a specific borrowing or investment transaction. An SPE is consolidated if, based on an evaluation of the substance of its relationship with the Group and the risks and rewards transferred by the SPE, the Group concludes that it controls the SPE. The assessment of whether the Group has control over an SPE is carried out at inception and normally no further reassessment of control is carried out in the absence of changes in the structure or terms of the SPE, or additional transactions between the Group and the SPE. Where the Group's voluntary actions, such as lending amounts in excess of existing liquidity facilities or extending terms beyond those established originally, change the relationship between the Group and an SPE, the Group performs a reassessment of control over the SPE. The Group in its fiduciary capacity manages and administers assets held in trust and other investment vehicles on behalf of investors.

The financial statements of these entities are not included in these consolidated financial statements except when the Group controls the entity. Information about the Group's fiduciary assets under management is set out in note 22.

(ii) Associates

Associates are those enterprises in which the Group holds, directly or indirectly, more than 20% of the voting power and exercises significant influence, but not control, over the financial and operating policies.

Investments in associates are initially recognised at cost and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investee after the date of acquisition. Distributions received from an investee reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary for changes in the investor's proportionate interest in the investee arising from changes in the investee's equity. When the Group's share of losses exceeds its interest in an associate, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued, except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate.

(iii) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Intra-group gains on transactions between the Group and its equity accounted associates are eliminated to the extent of the Group's interest in the investees. Unrealised losses are also eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment. Accounting policies of the subsidiaries and associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

(d) Foreign currency transactions

Items included in the consolidated financial statements of the Group are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Bahraini Dinars, which is the Bank's functional and presentation currency.

Foreign currency transactions are translated using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Translation differences on non-monetary items carried at their fair value, such as certain equity securities measured at fair value through equity, are included in investments fair value reserve.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(d) Foreign currency transactions (continued)

The other Group companies functional currencies are either denominated in Bahraini dinars or US dollars which is effectively pegged to the Bahraini dinar. Hence, the translation of financial statements of the group entities that have a functional currency different from the presentation currency do not result in exchange differences.

(e) Investment securities

Investment securities comprise equity investments and investments in sukuk (Islamic bonds). Investment securities exclude investments in subsidiaries and equity accounted associate companies (refer note 2(c)).

(i) Classification

The Group segregates its investment securities into debt-type instruments and equity-type instruments. Debt-type instruments are investments that have terms that provide fixed or determinable payments of profits and capital. Equity-type instruments are investments that do not exhibit features of debt-type instruments and include instruments that evidence a residual interest in the assets of an entity after deducting all its liabilities.

Debt-type Instruments:

Investments in debt-type instruments are classified in the following categories: 1) at amortised cost or 2) at fair value through income statement (FVTIS).

A debt-type investment is classified and measured at amortised cost only if the instrument is managed on a contractual yield basis or the instrument is not held for trading and has not been designated at FVTIS. Debt-type investments at amortised cost include investments in medium to long-term sukuk.

Debt-type investment classified and measured at FVTIS include investments held for trading or designated at FVTIS. At inception, a debt-type investment managed on a contractual yield basis, can only be designated at FVTIS if it eliminates an accounting mismatch that would otherwise arise on measuring the assets or liabilities or recognising the gains or losses on them on different bases. Debt-type instruments at FVTIS include investments in medium to long-term (quoted) sukuk

Equity-type investments:

Investments in equity type instruments are classified in the following categories: 1) at fair value through income statement (FVTIS) or 2) at fair value through equity (FVTE), consistent with its investment strategy.

Equity-type investments classified and measured at FVTIS include investments held for trading or designated at FVTIS.

An investment is classified as held for trading if acquired or originated principally for the purpose of generating a profit from short-term fluctuations in price or dealer's margin. Any investments that form part of a portfolio where there is an actual pattern of short-term profit taking are also classified as 'held for trading'. The Group has currently classified certain long-term listed equity sukuk and a private equity investment under this category.

Equity-type investments designated at FVTIS include investments which are managed and evaluated internally for performance on a fair value basis. This category currently includes an investment in private equity.

On initial recognition, the Bank makes an irrevocable election to designate certain equity instruments that are not designated at FVTIS to be classified as investments at fair value through equity. These include investments in certain quoted and unquoted equity securities.

ii) Recognition and de-recognition

Investment securities are recognised at the trade date i.e. the date that the Group contracts to purchase or sell the asset, at which date the Group becomes party to the contractual provisions of the instrument.

Investment securities are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risk and rewards of ownership.

(iii) Measurement

Investment securities are measured initially at fair value, which is the value of the consideration given. For FVTIS investments, transaction costs are expensed in the income statement. For other investment securities, transaction costs are included as a part of the initial recognition.

Subsequent to initial recognition, investments carried at FVTIS and FVTE are re-measured to fair value. Gains and losses arising from a change in the fair value of investments carried at FVTIS are recognised in the income statement in the period in which they arise. Gains and losses arising from a change in the fair value of investments carried at FVTE are recognised in the consolidated statement of changes in equity and presented in a separate fair value reserve within equity. The fair value gains / losses are recognised taking into consideration the split between portions related to owners' equity and equity of investment account holders. When the investments carried at FVTE are sold, impaired, collected or otherwise disposed of, the cumulative gain or loss previously recognised in the statement of changes in equity is transferred to the income statement.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Investment securities (continued)

(iii) Measurement (continued)

Investments at FVTE where the entity is unable to determine a reliable measure of fair value on a continuing basis, such as investments that do not have a quoted market price or other appropriate methods from which to derive reliable fair values, are stated at cost less impairment allowances.

Subsequent to initial recognition, debt type investments, other than those carried at FVTIS, are measured at amortised cost using the effective profit method less any impairment allowances.

(iv) Measurement principles

Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus capital repayments, plus or minus the cumulative amortisation using the effective profit method of any difference between the initial amount recognised and the maturity amount, minus any reduction (directly or through use of an allowance account) for impairment or uncollectability. The calculation of the effective profit rate includes all fees and points paid or received that are an integral part of the effective profit rate.

Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date. The Group measures the fair value of quoted investments using the market bid-prices in an active market for that instrument.

For certain unquoted investments, the Group uses proprietary models, which usually are developed from recognised valuation models for fair valuation. Some or all of the inputs into these models may not be market observable, but are estimated based on assumptions. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument.

Valuation adjustments are recorded to allow for bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state the values of these investments.

(f) Financing assets

Financing assets comprise Shari'a compliant financing contracts with fixed or determinable payments. These include financing provided through Murabaha, Musharaka, Istisna and Wakala contracts. Financing assets are recognised on the date at which they are originated and are carried at their amortised cost less impairment allowances, if any.

(g) Placements with and from financial institutions, non-financial institutions and individuals

These comprise inter-bank and over the counter customer placements made/received using Shari'a compliant contracts. Placements are usually for short-term and are stated at their amortised cost.

(h) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents comprise cash and bank balances (excluding CBB reserve account), and placement with financial institutions with maturities of three months or less when acquired which are subject to insignificant risk of changes in fair value and are used by the Group in the management of its short-term commitments.

(i) Assets acquired for leasing

Assets acquired for leasing (Ijarah Muntahia Bittamleek) are stated at cost less accumulated depreciation and any impairment in value. Under the terms of lease, the legal title of the asset passes to the lessee at the end of the lease term, provided that all lease instalments are settled. Depreciation is calculated on a straight line basis at rates that systematically reduce the cost of the leased assets over the period of the lease. The Group assesses at each reporting date whether there is objective evidence that the assets acquired for leasing are impaired. Impairment losses are measured as the difference between the carrying amount of the asset (including lease rental receivables) and the estimated recoverable amount. Impairment losses, if any, are recognised in the income statement.

(j) Investment property

Properties held for rental, or for capital appreciation purposes, or both, are classified as investment property. The Group follows cost model to measure its investment property and carries it at cost less depreciation and impairment allowances, if any. Cost includes expenditure that is directly attributable to the acquisition of the investment property. Investment property of the Group includes plots of land held for capital appreciation purposes and villas held for earning rentals.

Land is not depreciated and buildings are depreciated over 25 years. When use of a property changes such that it is reclassified as property and equipment, its fair value at the date of reclassification become its cost for subsequent accounting.

(k) Property and equipment

Property and equipment is stated at cost, net of accumulated depreciation and impairment allowances, if any. Property includes land which is not depreciated and buildings which are depreciated over 25 years. Other equipment is depreciated using the straight-line method to write-off the cost of the assets over their estimated useful lives ranging from 3 to 5 years. The assets residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Impairment of assets

The Group assesses at each reporting date whether there is objective evidence that an asset is impaired. Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a borrower, restructuring of financing facility or advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

Financial assets carried at amortised cost

These include debt-type instruments, financing assets and receivables. For financial assets carried at amortised cost impairment is measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the assets' original effective profit rate. Losses are recognised in income statement and reflected in an allowance account. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the income statement. The Group considers evidence of impairment for financial assets carried at amortised cost at both a specific asset and collective level.

All individually significant financial assets are assessed for specific impairment. All individually significant financial assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Financial assets that are not individually significant are collectively assessed for impairment by grouping together assets with similar risk characteristics.

Equity investments carried at fair value through equity (FVTE)

In the case of investments in equity securities classified as FVTE and measured at fair value, a significant or prolonged decline in the fair value of the security below its cost is an objective evidence of impairment. If any such evidence exists, the cumulative loss - measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in income statement - is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are subsequently reversed through equity.

For FVTE investments carried at cost less impairment due to the absence of reliable fair value, the Group makes an assessment of whether there is an objective evidence of impairment for each investment by assessment of financial and other operating and economic indicators. Impairment is recognised if the estimated recoverable amount is assessed to be below the cost of the investment.

Other non-financial assets

The carrying amount of the Group's assets (other than for financial assets covered above), are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. The recoverable amount of an asset is the greater of its value in use or fair value less costs to sell. An impairment loss is recognised whenever the carrying amount of an asset exceeds its estimated recoverable amount. Impairment losses are recognised in the income statement. Impairment losses are reversed only if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount.

In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash generating unit. An impairment loss is recognised whenever the carrying amount of an asset or its cash generating unit exceeds its estimated recoverable amount. Impairment losses are recognised in the income statement. Impairment losses are reversed only if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount. Separately recognised goodwill is not amortised and is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on separately recognised goodwill are not reversed.

(m) Customers' current accounts

Balances in current (non-investment) accounts are recognised when received by the Bank. The transaction are measured at the cash equivalent amount received by the Bank at the time of contracting. At the end of the accounting period, the accounts are measured at their book value.

(n) Equity of investment account holders

Equity of investment account holders are funds held by the Bank in unrestricted investment accounts, which it can invest at its own discretion. The investment account holder authorises the Bank to invest the account holders' funds in a manner which the Bank deems appropriate without laying down any restrictions as to where, how and for what purpose the funds should be invested.

The Bank charges management fee (Mudarib fees) to investment account holders. Of the total income from investment accounts, the income attributable to customers is allocated to investment accounts after setting aside provisions, reserves (Profit equalisation reserve and Investment risk reserve) and deducting the Bank's share of income as a Mudarib. The allocation of income is determined by the management of the Bank within the allowed profit sharing limits as per the terms and conditions of the investment accounts. Administrative expenses incurred in connection with the management of the funds are borne directly by the Bank and are not charged separately to investment accounts.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(n) Equity of investment account holders (continued)

Investment accounts are carried at their book values and include amounts retained towards profit equalisation and investment risk reserves, if any. Profit equalisation reserve is the amount appropriated by the Bank out of the Mudaraba income, before allocating the Mudarib share, in order to maintain a certain level of return to the deposit holders on the investments. Investment risk reserve is the amount appropriated by the Bank out of the income of investment account holders, after allocating the Mudarib share, in order to cater against future losses for investment account holders. Creation of an these reserves results in an increase in the liability towards the pool of unrestricted investment accounts.

(o) Restricted investment accounts

Restricted investment accounts represents assets acquired by funds provided by holders of restricted investment accounts and their equivalent and managed by the Bank as an investment manager based on either a Mudaraba contract or agency contract. The restricted investment accounts are exclusively restricted for investment in specified projects as directed by the investments account holders. Assets that are held in such capacity are not included as assets of the Bank in the consolidated financial statements.

(p) Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. A financial guarantee contract is recognised from the date of its issue. The liability arising from a financial guarantee contract is recognised at the present value of any expected payment, when a payment under the guarantee has become probable.

(q) Treasury shares

The amount of consideration paid including all directly attributable costs incurred in connection with the acquisition of the treasury shares are recognised in equity. Consideration received on sale of treasury shares is presented in the financial statements as a change in equity. No gain or loss is recognised on the Group's income statement on the sale of treasury shares.

(r) Statutory reserve

The Bahrain Commercial Companies Law 2001 requires that 10 per cent of the annual net profit be appropriated to a statutory reserve which is normally distributable only on dissolution. Appropriations may cease when the reserve reaches 50 per cent of the paid up share capital.

(s) Revenue recognition

Fees and commission income that are integral to the effective profit rate on a financial asset carried at amortised cost are included in the measurement of the effective profit rate of the financial asset. Other fees and commission income, including account servicing fees, sales commission, management fees, placement and arrangement fees and syndication fees, are recognised as the related services are performed.

Income from Murabaha and Wakala contracts are recognised on a time-apportioned basis over the period of the contract using the effective profit method.

Profit or losses in respect of the Bank's share in Musharaka financing transaction that commence and end during a single financial period is recognised in the income statement at the time of liquidation (closure of the contract). Where the Musharaka financing continues for more than one financial period, profit is recognised to the extent that such profits are being distributed during that period in accordance with profit sharing ratio as stipulated in the Musharaka agreement.

Istisna'a revenue and the associated profit margin is recognised using the percentage of completion method.

Income from assets acquired for leasing (Ijarah Muntahia Bittamleek) are recognised proportionately over the lease term.

Income from sukuk and income / expenses on placements is recognised at its effective profit rate over the term of the instrument.

Dividend income is recognised when the right to receive is established.

(t) Earnings prohibited by Shari'a

The Bank is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a charity account where the Bank uses these funds for charitable purposes.

(u) Zakah

Zakah is calculated on the Zakah base of the Group in accordance with FAS 9 Zakah using the net assets method. Zakah is paid by the Group based on the eligible reserve and retained earnings balances at the end of the year and the remaining Zakah is payable by individual shareholders. The Bank calculates and notifies the shareholders of their pro-rata share of the Zakah payable annually. The Group also pays Zakah on the balance of treasury shares held at the year-end based on the pro-rata share of Zakah. The calculations of Zakah is approved by the Shari'a Supervisory Board. Payment of Zakah on the unrestricted investment and other accounts is the responsibility of the investment account holders.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2014

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(v) Employee benefits

(i) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A provision is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(ii) Post-employment benefits

Pensions and other social benefits for Bahraini employees are covered by the Social Insurance Organisation scheme, which is a "defined contribution scheme" in nature, and to which employees and employers contribute monthly on a fixed-percentage-of-salaries basis. Contributions by the Bank are recognised as an expense in income statement when they are due.

Expatriate employees on fixed contracts are entitled to leaving indemnities payable under the Bahraini Labour Law, based on length of service and final remuneration. Provision for this unfunded commitment has been made by calculating the notional liability had all employees left at the reporting date.

These benefits are in the nature of "defined benefit scheme" and any increase or decrease in the benefit obligation is recognised in the income statement.

The Bank also operates a voluntary employees saving scheme under which the Bank and the employee contribute monthly on a fixed percentage of salaries basis. The scheme is managed and administered by a board of trustees who are employees of the Bank. The scheme is in the nature of a defined contribution scheme and contributions by the Bank are recognised as an expense in the income statement when they are due.

(iii) Share-based employee incentive scheme

The Bank had a share-based incentive scheme for its employees (the "Scheme") whereby eligible employees were granted the Bank's shares as compensation on achievement of certain non-market based performance conditions and additional service conditions. The Scheme was effective until December 2012. The Bank is formulating a new scheme for its employees, this would be effective from performance year 2014, subject to approval of CBB and shareholders at the annual general meeting.

(w) Dividends and board remuneration

Dividends to shareholders and board remuneration are recognised as liabilities in the period in which they are declared.

(x) Trade date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Group commits to purchase or sell the asset.

(y) Offsetting

Financial assets and liabilities are offset only when there is a legal or Sharia' based enforceable right to set off the recognised amounts and the Group intends to either settle on a net basis, or to realise the asset and settle the liability simultaneously.

(z) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

(aa) Deposit Protection Scheme

Funds held with the Bank in unrestricted investment accounts and current accounts are covered by the Deposit Protection Scheme (the Scheme) established by the Central Bank of Bahrain regulation in accordance with Resolution No (34) of 2010.

The Scheme applies to all eligible accounts held with the Bank subject to certain specific exclusions, maximum total amount entitled and other regulations concerning the establishment of a Deposit Protection Scheme and a Deposit Protection Board.

3. CASH AND BANK BALANCES

	31 December 2014	31 December 2013
Cash	2,550	2,962
Balances with banks	12,799	12,751
Balances with the Central Bank:		
- Current account	5,134	8,050
- Reserve account	16,875	15,085
	37,358	38,848

The reserve account with the Central Bank of Bahrain is not available for day-to-day operational purposes.

4. PLACEMENTS WITH FINANCIAL INSTITUTIONS

	31 December 2014	31 December 2013
Gross Murabaha and Wakala receivable	76,030	82,755
Less: Deferred profits	(24)	(10)
	76,006	82,745

The average profit rate on placement with financial institutions for 2014 was 0.70% per annum (31 December 2013: 0.66% per annum).

5. FINANCING ASSETS

	31 December 2014	31 December 2013
Murabaha	242,721	195,965
Musharaka	37,141	50,643
Wakala	36,256	22,952
Mudharaba	1,276	-
Istisna	218	400
	317,612	269,960
Less: Impairment allowances - specific	(10,192)	(12,529)
Less: Impairment allowances - collective	(3,477)	(3,796)
	303,943	253,635

Murabaha financing receivables are net of deferred profits of BD 32,490 thousand (2013: BD 32,130 thousand).

Of the total financing asset portfolio, consumer financing receivables amounted to BD 36,701 thousand (2013: BD 21,151 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2014 | BD 000's

5. FINANCING ASSETS (continued)

The movement in impairment allowances are as follows:

2014	Specific	Collective	Total
At 1 January	12,529	3,796	16,325
Net charge for the year	129	(319)	(190)
Adjusted on write-off of assets	(2,466)	-	(2,466)
At 31 December	10,192	3,477	13,669

2013	Specific	Collective	Total
At 1 January	13,645	2,740	16,385
Net charge for the year	5,401	1,056	6,457
Adjusted on write-off of assets	(6,517)	-	(6,517)
At 31 December	12,529	3,796	16,325

6. INVESTMENT SECURITIES

	31 December 2014	31 December 2013
Equity type instruments:		
<i>At fair value through income statement</i>		
- Unquoted equity securities (at fair value)	15,148	14,959
- Listed equity sukuk (at fair value)	4,961	4,765
<i>At fair value through equity</i>		
- Unquoted equity securities (carried at cost less impairment)	45,797	46,306
	65,906	66,030
Debt type instruments:		
Sukuk:		
- At amortised cost	30,619	23,351
- At fair value through income statement (quoted)	398	1,016
	31,017	24,367
	96,923	90,397

Unquoted equity securities at fair value through equity comprise investments in closed companies managed by external investment managers or represent investments in projects promoted by the Group. These investments are carried at cost less impairment in the absence of a reliable measure of fair value. The Group intends to exit these investments principally by means of private placements, strategic buy outs, sale of underlying assets or through initial public offerings.

During the year, impairment allowances of BD 432 thousand (31 December 2013: BD 7,660 thousand) was recognised on equity securities carried at cost. Impairment allowance of BD 100 thousand (31 December 2013: BD 162 thousand) was recognised on investments at amortised cost.

Unquoted equity securities carried at cost are net of specific impairment allowances of BD 16,781 thousand (2013: BD 16,349 thousand). Debt type instruments are net of specific impairment allowances of BD 300 thousand (2013: BD 200 thousand).

7. ASSETS ACQUIRED FOR LEASING

	2014	2013
Cost		
At 1 January	39,929	26,291
Additions during the year	20,218	17,824
Settlements / adjustments during the year	(9,781)	(4,186)
At 31 December	50,366	39,929
Accumulated depreciation		
At 1 January	7,868	5,353
Charge for year	9,298	6,701
Settlements during the year	(9,781)	(4,186)
At 31 December	7,385	7,868
Net book value at 31 December	42,981	32,061

At 31 December 2014, accrued lease rental receivable amounted to BD 798 thousand (2013: BD 3,569 thousand). Lease rental receivable is net of collective provision of BD 442 thousand (2013: BD 360 thousand). During the year, an impairment allowance of BD 82 thousand (2013: BD 118 thousand) was made on the lease rental receivables.

Of the total net book value of assets acquired for leasing, consumer financing amounted to BD 42,684 thousand (2013: BD 30,240 thousand).

8. INVESTMENT IN ASSOCIATES

	2014	2013
At 1 January	2,681	2,887
Redemption during the year	(104)	(91)
Share of profit / (loss) for the year	27	(115)
At 31 December	2,604	2,681

Investment in associates comprise:

Name	Country of incorporation	% holding	Nature of business
Capital Real Estate Projects Company BSC (c)	Bahrain	30.0%	Real estate holding and development
Amlak II SPV	Cayman Islands	23.1%	Purchase and sale of real estate in Bahrain

Summarised financial information of associates that have been equity accounted not adjusted for the percentage ownership held by the Group (based on their most recent unaudited management accounts):

	2014	2013
Total assets	10,643	11,748
Total liabilities	1,084	1,822
Total revenues	448	1,730
Total net profits / (losses)	101	(91)

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9. INVESTMENT PROPERTY

Investment property comprise four plots of land and thirteen villas held with the objective of future capital appreciation and to earn periodical income.

In 2010, the Bank had received two plots of land located in Bahrain Financial Harbour project in consideration for sale of an investment. Of the two plots of land received, one plot is intended for the Group's own use and has been classified under "Property and equipment" (refer note 11). The second plot of land has been classified as "Investment property".

In December 2014, the Bank recognised three plots of land and thirteen villas located in Bahrain, received as consideration for settlement/foreclosure of three non-performing financing deals (refer note 31).

10. OTHER ASSETS

	31 December 2014	31 December 2013
Receivable on sale of investment	-	11,326
Qardh Hassan receivable	5,029	5,086
Prepayments	686	638
Income from sukuk receivable	200	147
Other receivables	3,164	6,145
	9,079	23,342

Qardh Hassan receivable is net of impairment allowance of BD 955 thousand (2013: 898 thousand). Other receivables is net of impairment allowance of BD 722 thousand (2013: BD 722 thousand).

11. PROPERTY AND EQUIPMENT

	Land (note 9)	Building	Furniture and fixtures	Computers	Motor Vehicle and Other equipment	Work-in- progress	2014 Total	2013 Total
Cost								
At 1 January	6,714	483	4,149	3,040	340	248	14,974	14,348
Additions	-	10	31	119	27	576	763	626
Capitalisation	-	-	44	193	18	(255)	-	-
At 31 December	6,714	493	4,224	3,352	385	569	15,737	14,974
Accumulated depreciation								
At 1 January	-	19	3,631	2,671	272	-	6,593	5,424
Charge for year	-	20	253	317	37	-	627	1,169
At 31 December	-	39	3,884	2,988	309	-	7,220	6,593
Net book value at 31 December 2014	6,714	454	340	364	76	569	8,517	8,381
Net book value at 31 December 2013	6,714	464	518	369	68	248	8,381	

12. PLACEMENTS FROM NON-FINANCIAL INSTITUTIONS AND INDIVIDUALS

	31 December 2014	31 December 2013
Non-financial institutions	23,263	36,712
Individuals	20,519	44,200
	43,782	80,912

These represent placements in the form of Murabaha and Wakala contracts.

13. OTHER LIABILITIES

	31 December 2014	31 December 2013
Mudaraba profit accrual	3,153	3,734
Employee related accruals	775	1,008
Charity and zakah payable (page 27)	859	835
Payable for Istisna'a contracts	111	111
Other payables and accrued expenses	3,217	1,719
	8,115	7,407

14. EQUITY OF INVESTMENT ACCOUNT HOLDERS

The funds received from investment account holders have been commingled and jointly invested with the Bank in the following asset classes as at 31 December:

	31 December 2014	31 December 2013
Balances with banks	12,799	12,751
CBB reserve account	16,875	15,085
Placements with financial institutions	76,006	82,745
Debt type instruments - sukuk	31,017	24,367
Equity type instrument - sukuk	4,961	4,765
Financing assets	197,276	152,336
	338,934	292,049

The investors' share of the return on jointly invested assets and distribution to investment account holders were as follows:

	31 December 2014	31 December 2013
Returns from jointly invested assets	12,843	13,315
Banks share as Mudarib	(4,002)	(4,596)
Return / distribution to investment account holders	8,841	8,719

Approximately 2.60% (31 December 2013: 3.35%) was distributed to investors and the balance was retained by the Bank as a Mudarib fee. As at 31 December 2014, the balance of profit equalisation reserve was Nil (2013: Nil) and the balance of investment risk reserve was Nil (2013: Nil).

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15. SHARE CAPITAL

	31 December 2014	31 December 2013
Authorised:		
3,000,000,000 ordinary shares of BD 0.100 each	300,000	300,000
Issued and fully paid up:		
1,154,161,084 ordinary shares (2013: 1,154,161,084) of BD 0.100 each	115,416	115,416

The Bank has only one class of equity shares and the holders of these shares have equal voting rights. At 31 December 2014, the Bank holds 28,621,332 as treasury shares (2013: 28,621,332).

Distribution schedule of equity shares, setting out the number of holders and percentage in the following categories:

Categories *	Number of Shares	Number of Shareholders	% of total outstanding shares
Less than 1%	190,308,181	580	16.48
1% up to less than 5% **	155,757,177	8	13.50
5% up to less than 10%	103,950,000	1	9.01
10% up to less than 20%	161,700,000	1	14.01
20% and less than 50%	542,445,726	1	47.00
	1,154,161,084	591	100.00

* Expressed as a percentage of total outstanding shares of the Bank.

** Includes treasury shares and unvested employee incentive scheme shares.

Names and nationalities of the major shareholders and the number of equity shares held in which they have an interest of 5% or more of outstanding shares:

	Nationality	Number of shares	% of total outstanding shares
Gulf Finance House BSC *	Bahrain	542,445,726	47.00
Al Imtiaz Investment Company KSCC	Kuwait	161,700,000	14.01
Emirates Islamic Bank PJSC	UAE	103,950,000	9.01

*As at 31 December 2014, these shares representing 47.00% were held by KHC Asset Company on behalf of Gulf Finance House BSC.

16. INCOME / (LOSS) FROM INVESTMENT SECURITIES

	2014	2013
Income from equity-type investments:		
- Dividend and other investment income	404	1,574
- Fair value (loss) / gain on investment	195	(2,722)
	599	(1,148)
Income from debt-type investments:		
- Income from Sukuk	818	503
- Other gain on Sukuk	-	21
	1,417	(624)

17. STAFF COST

	2014	2013
Salaries and short-term benefits	5,440	4,952
Social insurance expenses	662	557
Other staff expenses	81	183
	6,183	5,692

18. IMPAIRMENT ALLOWANCES

	2014	2013
Financing assets (note 5)	(190)	6,457
Lease rental receivable (note 7)	82	118
Investments at fair value through equity (note 6)	432	7,660
Investments at amortised cost (note 6)	100	162
Other assets (note 10)	57	848
	481	15,245

19. OTHER EXPENSES

	2014	2013
Premises cost	1,008	922
Advertisement and marketing expenses	779	723
Professional fees	685	689
Information technology expenses	474	454
Board expenses	216	352
Communication expenses	239	252
Distribution channel expenses	192	145
Other administrative expenses	645	575
	4,238	4,112

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20. SHARE-BASED EMPLOYEE INCENTIVE SCHEME

During 2014, the Bank has adopted sound remuneration practices as required under Volume 2 of the CBB rule book. The management is in the process of formulating a new scheme subject to approval by CBB and shareholders in the annual general meeting.

21. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances.

Judgements

Classification of investments

In the process of applying the Group's accounting policies, management decides on acquisition of an investment whether it should be classified as debt type instruments carried at fair value through equity or amortised cost, or equity-type instruments carried at fair value through equity or fair value through income statement. The classification of each investment reflects the management's intention in relation to each investment and is subject to different accounting treatments based on such classification [refer note 2 (e)].

Special purpose entities

The Bank sponsors the formation of special purpose entities (SPE's) primarily for the purpose of allowing clients to hold investments. The Bank provides corporate administration, investment management and advisory services to these SPE's, which involve the Group making decisions on behalf of such entities. The Bank administers and manages these entities on behalf of its clients, who are by and large third parties and are the economic beneficiaries of the underlying investments.

The Bank does not consolidate SPE's that it does not have the power to control. In determining whether the Bank has the power to control an SPE, judgements are made about the objectives of the SPE's activities, its exposure to the risks and rewards, as well as about the Group's intention and ability to make operational decisions for the SPE and whether the Group derives benefits from such decisions.

Estimations

Impairment of equity investments

The Group determines that equity securities carried at fair value are impaired when there is an objective evidence of impairment and there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgment.

In case of quoted equity securities, the Group considers a decline of more than 30% in the fair value below cost to be significant and considers a decline below cost which persists for more than 6 months as prolonged. Where fair values are not readily available and the investments are carried at cost, the recoverable amount of such investment is estimated to test for impairment.

For unquoted investments carried at cost, the Group makes an assessment of whether there is an objective evidence of impairment for each investment by assessment of financial and other operating and economic indicators. Impairment is recognised if the estimated recoverable amount is assessed to be below the cost of the investment.

In making this judgment, the Bank evaluates among other factors, evidence of a deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financing cash flows. It is reasonably possible, based on existing knowledge, that the current assessment of impairment could require a material adjustment to the carrying amount of the investments within the next financial year due to significant changes in the assumptions underlying such assessments.

Fair value of unquoted equity securities

The Group determines the fair value of unquoted investments by using valuation techniques. This includes using recent arm's length transactions between knowledgeable, willing parties (if available), discounted cash flow analysis or market multiples for similar instruments. Fair value estimates are made at a specific point in time, based on market conditions and information about the investee companies/funds. These estimates involve uncertainties and matters of significant judgement and therefore, cannot be determined with precision. There is no certainty about future events (such as continued operating profits and financial strengths). It is reasonably possible, based on existing knowledge, that outcomes within the next financial year that are different from assumptions could require a material adjustment to the carrying amount of the investments.

Significant judgment is required to be made by the Group and the Board of Directors in the selection of an approach that would reflect the best measure of fair value of the investments. The choice of the models used for valuation on each reporting period may have a significant impact on the fair value of investments and the amounts reported in the consolidated financial statements. The Bank has adopted the market approach for valuation of its unquoted equity security.

21. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (continued)

Estimations (continued)

Fair value of unquoted equity securities (continued)

The potential effect of using reasonable possible alternative assumptions for valuing the investments resulting in 5% decrease / increase in the market multiple would increase / decrease the reported fair value by BD 761 thousand (31 December 2013: BD 744 thousand). The corresponding impact would be on the profit or loss reported by the Group.

Impairment of financing assets

Financing assets are evaluated for impairment on a basis described in accounting policy, refer to note 2 (I). Each counterparty exposure is evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a counterparty's financial situation and the net realisable value of any underlying assets/ collaterals. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently evaluated by the Risk Management Department.

For evaluation of the portfolio for impairment on a collective basis, management, where available, uses estimates based on historical loss experience for assets and loss experience in the industry for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio. For the purposes of a collective evaluation of impairment, financing assets are grouped on the basis of similar credit risk characteristics (that is, on the basis of the Group's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). The methodology and assumptions used for the grading process and estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. In view of the management, the current level of provisioning is adequate and no additional impairment allowances are required on a collective basis.

22. ASSETS UNDER MANAGEMENT

The Bank provides corporate administration, investment management and advisory services to its investment entities, which involve the Group making decisions on behalf of such entities. Assets that are held in such capacity are not included in these consolidated financial statements. At the reporting date, the Group had assets under management of BD 261.77 million (31 December 2013: BD 336.52 million). During the year, the Bank has charged management fees amounting to BD 738 thousand (2013: BD 1,088 thousand) for the management of these assets. During the year, the Bank sold the underlying assets of one of the RIA (Al Hareth French Property fund) and redeemed BD 3,512 thousand to the RIA account holders on full exit of the fund (refer page 26).

23. RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties include the significant shareholders and entities over which the Bank and the shareholders exercises significant influence, directors and executive management of the Bank.

A significant portion of the Bank's income from management fees arises from entities (assets under management) over which the Bank or its significant shareholders exercises influence. Although these entities are considered related parties, the Bank administers and manages these entities on behalf of its clients, who are by and large third parties and are the economic beneficiaries of the underlying investments.

Details of Directors' interests in the Bank's ordinary shares as at the end of the year were:

Categories*	Number of Shares	Number of Directors
Less than 1%	8,358,249	3
1% up to 10%	-	-

* Expressed as a percentage of total outstanding shares of the Bank.

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23. RELATED PARTY TRANSACTIONS (continued)

Compensation of key management personnel

Key management personnel of the Bank comprise of the Board of Directors and key members of management having authority and responsibility for planning, directing and controlling the activities of the Bank.

The key management personnel compensation during the year is as follows:

	2014	2013
Board member fees	81	101
Board member allowances	120	108
Salaries and other short-term benefits	868	667

Transactions with restricted investment accounts

Transactions involving transfer/sale of assets to restricted investment accounts are generally executed based on the pre-agreed values as per the terms of the contracts for each restricted investment product. During 2014, in its normal course of business, the Bank has not bought any certain investments at agreed contractual values.

The related party balances and transactions (except for compensation of key managerial personnel) included in these consolidated financial statements are as follows:

31 December 2014	Associates	Key management personnel	Significant shareholders / entities in which directors are interested	Assets under management (including special purpose entities)	Total
Assets					
Financing assets	646	-	-	7,964	8,610
Investment securities	-	-	2,284	24,929	27,213
Investment in associates	2,604	-	-	-	2,604
Other assets	100	-	-	2,285	2,385
Liabilities					
Customers' current accounts	148	-	43	1,502	1,693
Equity of investment account holders	457	349	5,671	10,398	16,875

23. RELATED PARTY TRANSACTIONS (continued)

31 December 2013	Associates	Key management personnel	Significant shareholders / entities in which directors are interested	Assets under management (including special purpose entities)	Total
Assets					
Financing assets	744	-	-	9,308	10,052
Investment securities	-	-	-	24,922	24,922
Investment in associates	2,681	-	-	-	2,681
Other assets	178	-	-	15,753	15,931
Liabilities					
Customers' current accounts	357	3	13	636	1,009
Equity of investment account holders	387	513	8,009	13,884	22,793

2014	Associates	Key management personnel	Significant shareholders / entities in which directors are interested	Assets under management (including special purpose entities)	Total
Income					
Management and other fees	-	-	-	705	705
Income from financing assets and assets acquired for leasing	102	-	-	523	625
Income from investment securities	-	-	162	(198)	(36)
Share of income from associates	27	-	-	-	27
Expenses					
Return to investment account holders	18	8	40	257	323
Staff cost	-	868	-	-	868
Other expenses	-	-	-	123	123

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23. RELATED PARTY TRANSACTIONS (continued)

2013	Associates	Key management personnel	Significant shareholders / entities in which directors are interested	Assets under management (including special purpose entities)	Total
Income					
Management and other fees	-	-	-	1,054	1,054
Income from financing assets and assets acquired for leasing	102	-	-	396	498
Income from investment securities	-	-	-	1,110	1,110
Share of losses from associates	(115)	-	-	-	(115)
Expenses					
Return to investment account holders	17	14	196	337	564
Other expenses	-	-	-	56	56
Impairment allowances	-	-	-	5,639	5,639

24. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the profit / (loss) for the year by the weighted average number of equity shares outstanding during the year. The Bank does not have any dilutive equity instruments.

Basic EPS	2014	2013
Profit / (loss) for the year (BD 000's)	3,046	(19,209)
Weighted average number of equity shares (Nos. in 000's)	1,122,668	1,122,668
Basic earnings per share (in fils)	2.71	(17.11)

25. SHARI'A SUPERVISORY BOARD

The Bank's Shari'a Supervisory Board consists of three Islamic scholars who review the Bank's compliance with general Shari'a principles and specific fatwas, rulings and guidelines issued. Their review includes examination of evidence relating to the documentation and procedures adopted by the Bank to ensure that its activities are conducted in accordance with Islamic Shari'a principles.

26. ZAKAH

Zakah is directly borne by the shareholders on distributed profits and investment account holders. The Bank currently does not collect or pay Zakah on behalf of its shareholders and investors in restricted investment accounts. Zakah payable by the shareholders is computed by the Bank on the basis of the method prescribed by the Bank's Shari'a Supervisory Board and notified to shareholders annually. During the year, the Shari'a Supervisory Board has computed Zakah payable of BD 766 thousand (2013: BD 905 thousand) of which BD Nil (2013: Nil thousand) represents the Zakah computed on the cumulative retained earnings as at 31 December 2014, payable by the Bank. The remaining Zakah balance amounting to BD 766 thousand or 0.664 fils per share (2013: BD 905 thousand or 0.784 fils per share) is due and payable by the shareholders. The Bank will pay Zakah of BD 19 thousand (2013: Nil) on the treasury shares held as of 31 December 2014 based on 0.664 fils per share (Note 32).

27. SEGMENT REPORTING

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the Group's chief operating decision maker (Board of Directors) to make decisions about resource allocation to each segment and assess its performance and for which discrete financial information is available. An operating segment is divided into business segment and geographic segments. For management purposes, the Group is organised into two major business segments:

Corporate and retail banking

Providing customer services such as accepting Mudaraba deposits, savings account and current account facilities, fund transfer facilities, bill payment facilities. It also provides financing facilities (in the form of Commodity Murabaha, Musharaka, Istisna'a and Ijarah facilities) to corporate clients and High-Networth-Individuals and consumer finance products. Provides money market and treasury services in the form of short term Commodity Murabaha and Wakala to banks, financial institutions and corporate, investments in sukuk and also used to manage funding of the Group.

27. SEGMENT REPORTING (continued)

Investment banking

Primarily relates to conceptualising of investment deals and performing roles of an arranger, lead manager, and administrator of the funds (involves structuring of deals, raising of funds through private placement and fund administration). Also offers products like Restricted Investment Accounts (RIA) and management of funds raised through the RIA structures. Also involves carrying out strategic investments in the form of equity contribution (either in the funds created and managed by the Bank or other institutions).

Segment performance is measured based on results for each department as mentioned in the internal management reports that are reviewed by the Board of directors on a quarterly basis. Segment results is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate in these industries.

The Bank reports directly attributable revenue and cost relating to transactions originating from respective segments as segment revenue and segment cost respectively. Indirect costs and corporate overheads are treated as unallocated. The internal management reports are designed to reflect revenue and cost for respective segments which are measured against the budgeted figures.

The Group primarily operates from Bahrain and does not have any overseas branches/divisions. The geographic concentration of assets and liabilities is disclosed in note 29 (b) to the consolidated financial statements.

These segments are the basis on which the Group reports its primary segment information. Transactions between segments (if any) are conducted on an arm's length basis.

31 December 2014	Investment Banking	Commercial Banking	Unallocated	Total
Cash and bank balances	-	37,358	-	37,358
Placements with financial institutions	1,428	74,578	-	76,006
Financing assets	-	303,943	-	303,943
Investment securities	60,945	35,978	-	96,923
Assets acquired for leasing (including lease rentals receivable)	-	43,779	-	43,779
Investment in associates	2,604	-	-	2,604
Investment property	13,715	-	-	13,715
Other assets	2,381	200	6,498	9,079
Property and equipment	-	-	8,517	8,517
Total segment assets	81,073	495,836	15,015	591,924
Placements from financial institutions	-	50,208	-	50,208
Placements from non - financial institutions and individuals	-	43,782	-	43,782
Customers' current accounts	1,428	46,400	-	47,828
Other liabilities	78	5,120	2,917	8,115
Total segment liabilities	1,506	145,510	2,917	149,933
Equity of investment account holders	10,855	328,079	-	338,934
Restricted investment accounts	21,966	-	-	21,966

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27. SEGMENT REPORTING (continued)

2014	Investment Banking	Commercial Banking	Unallocated	Total
Management and other fees	738	-	-	738
Income from placements with financial institutions	11	557	-	568
Income from financing assets and assets acquired for leasing	-	22,882	-	22,882
Income from investment securities	100	1,317	-	1,417
Share of income from associate companies	27	-	-	27
Other income	435	409	-	844
Total income before return to investment account holders	1,311	25,165	-	26,476
Less: Return to investment account holders before Bank's share as Mudarib	(388)	(12,455)	-	(12,843)
Bank's share as a Mudarib	121	3,881	-	4,002
Return to investment account holders	(267)	(8,574)	-	(8,841)
Less: Expense on placements from financial institutions, non-financial institutions and individuals	-	(3,060)	-	(3,060)
Total segment revenue	1,044	13,531	-	14,575
Staff cost	618	2,473	3,092	6,183
Depreciation	-	-	627	627
Other expenses	123	456	3,659	4,238
Total segment cost	741	2,929	7,378	11,048
Segment results before impairment allowances	303	10,602	(7,378)	3,527
Charge of impairment allowances	(432)	8	(57)	(481)
Segment results	(129)	10,610	(7,435)	3,046

27. SEGMENT REPORTING (continued)

31 December 2013	Investment Banking	Commercial Banking	Unallocated	Total
Cash and bank balances	-	38,848	-	38,848
Placements with financial institutions	545	82,200	-	82,745
Financing assets	-	253,635	-	253,635
Investment securities	61,265	29,132	-	90,397
Assets acquired for leasing (including lease rentals receivable)	-	35,630	-	35,630
Investment in associates	2,681	-	-	2,681
Investment property	6,583	-	-	6,583
Other assets	15,931	1,544	5,867	23,342
Property and equipment	-	-	8,381	8,381
Total segment assets	87,005	440,989	14,248	542,242
Placements from financial institutions	-	42,940	-	42,940
Placements from non - financial institutions and individuals	-	80,912	-	80,912
Customers' current accounts	545	18,378	-	18,923
Other liabilities	101	5,166	2,140	7,407
Total segment liabilities	646	147,396	2,140	150,182
Equity of investment account holders	13,917	278,132	-	292,049
Restricted investment accounts	31,556	-	-	31,556

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27. SEGMENT REPORTING (continued)

2013	Investment Banking	Commercial Banking	Unallocated	Total
Management and other fees	1,088	-	-	1,088
Income from placements with financial institutions	3	427	-	430
Income from financing assets and assets acquired for leasing	-	18,318	-	18,318
Income from investment securities	(1,165)	541	-	(624)
Share of losses from associate companies	(115)	-	-	(115)
Other income	293	306	-	599
Total income before return to investment account holders	104	19,592	-	19,696
Less: Return to investment account holders before Bank's share as Mudarib	(634)	(12,681)	-	(13,315)
Bank's share as a Mudarib	219	4,377	-	4,596
Return to investment account holders	(415)	(8,304)	-	(8,719)
Less: Expense on placements from financial institutions, non-financial institutions and individuals	-	(3,968)	-	(3,968)
Total segment revenue	(311)	7,320	-	7,009
Staff cost	569	2,277	2,846	5,692
Depreciation	-	-	1,169	1,169
Other expenses	56	401	3,655	4,112
Total segment cost	625	2,678	7,670	10,973
Segment results before impairment allowances	(936)	4,642	(7,670)	(3,964)
Charge of impairment allowances	(7,660)	(7,585)	-	(15,245)
Segment results	(8,596)	(2,943)	(7,670)	(19,209)

28. MATURITY PROFILE

The maturity profile of placements with and from financial institutions, financing assets, assets acquired for leasing, (including lease rental receivable), investment in sukuk (non-trading), and equity of investment account holders has been presented using their contractual maturity period. For other balances, maturity profile is based on expected cash flows/ settlement profile of the respective assets and liabilities.

31 December 2014	Up to 3 months	3 to 6 months	6 months - 1 year	1 to 3 years	Over 3 years	Total
Assets						
Cash and bank balances	37,358	-	-	-	-	37,358
Placements with financial institutions	76,006	-	-	-	-	76,006
Financing assets	52,664	23,199	20,336	73,844	133,900	303,943
Investment securities	35,978	-	3,770	57,175	-	96,923
Assets acquired for leasing (including lease rental receivable)	-	-	531	829	42,419	43,779
Investment in associates	-	-	-	938	1,666	2,604
Investment property	-	-	-	-	13,715	13,715
Other assets	1,633	-	42	7,404	-	9,079
Property and equipment	-	-	-	-	8,517	8,517
Total assets	203,639	23,199	24,679	140,190	200,217	591,924
Liabilities						
Placements from financial institutions	30,326	-	3,054	16,828	-	50,208
Placements from non-financial institutions and individuals	22,567	5,056	9,156	5,830	1,173	43,782
Customers' current account	37,513	3,819	3,248	3,248	-	47,828
Other liabilities	3,137	809	1,420	2,749	-	8,115
Total liabilities	93,543	9,684	16,878	28,655	1,173	149,933
Equity of investment account holders	129,488	49,705	55,610	104,131	-	338,934
Restricted Investment accounts	-	-	-	5,553	16,413	21,966
Commitments	25,961	4,736	17,772	6,300	1,231	56,000

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28. MATURITY PROFILE (continued)

31 December 2013	Up to 3 months	3 to 6 months	6 months - 1 year	1 to 3 years	Over 3 years	Total
Assets						
Cash and bank balances	38,848	-	-	-	-	38,848
Placements with financial institutions	82,745	-	-	-	-	82,745
Financing assets	41,884	15,450	17,934	77,891	100,476	253,635
Investment securities	8,335	5,825	5,786	35,696	34,755	90,397
Assets acquired for leasing (including lease rental receivable)	6	-	1,884	1,170	32,570	35,630
Investment in associates	-	-	-	2,681	-	2,681
Investment property	-	-	-	-	6,583	6,583
Other assets	1,514	13,536	-	3,206	5,086	23,342
Property and equipment	-	-	-	-	8,381	8,381
Total assets	173,332	34,811	25,604	120,644	187,851	542,242
Liabilities						
Placements from financial institutions	25,492	-	-	17,448	-	42,940
Placements from non-financial institutions and individuals	24,230	20,047	31,181	4,258	1,196	80,912
Customers' current account	18,705	218	-	-	-	18,923
Other liabilities	2,015	1,397	1,575	2,420	-	7,407
Total liabilities	70,442	21,662	32,756	24,126	1,196	150,182
Equity of investment account holders	156,922	52,336	80,078	2,713	-	292,049
Restricted Investment accounts	5,264	-	1,001	25,291	-	31,556
Commitments	8,884	21,431	12,082	1,772	-	44,169

29. CONCENTRATION OF ASSETS, LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND RESTRICTED INVESTMENT ACCOUNTS

(a) Industry sector

31 December 2014	Banks and financial institutions	Real estate	Others	Total
Assets				
Cash and bank balances	37,358	-	-	37,358
Placements with financial institutions	76,006	-	-	76,006
Financing assets	41,285	114,411	148,247	303,943
Investments securities	26,537	42,614	27,772	96,923
Assets acquired for leasing (including lease rentals receivable)	501	43,211	67	43,779
Investment in associates	-	2,604	-	2,604
Investment property	-	13,715	-	13,715
Other assets	-	1,768	7,311	9,079
Property and equipment	-	7,169	1,348	8,517
Total assets	181,687	225,492	184,745	591,924
Liabilities				
Placements from financial institutions	50,208	-	-	50,208
Placements from non-financial institutions and individuals	-	379	43,403	43,782
Customers' current accounts	2,800	7,511	37,517	47,828
Other liabilities	1,146	242	6,727	8,115
Total liabilities	54,154	8,132	87,647	149,933
Equity of investment account holders	9,014	14,864	315,056	338,934
Restricted investment accounts	-	20,973	993	21,966
Commitments	-	16,041	39,959	56,000

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29. CONCENTRATION OF ASSETS, LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND RESTRICTED INVESTMENT ACCOUNTS (continued)

(a) Industry sector (continued)

31 December 2013	Banks and financial institutions	Real estate	Others	Total
Assets				
Cash and bank balances	38,848	-	-	38,848
Placements with financial institutions	82,745	-	-	82,745
Financing assets	38,680	59,551	155,404	253,635
Investments securities	26,601	35,954	27,842	90,397
Assets acquired for leasing (including lease rentals receivable)	1,060	33,549	1,021	35,630
Investment in associates	-	2,681	-	2,681
Investment property	-	6,583	-	6,583
Other assets	434	20,973	1,935	23,342
Property and equipment	-	7,179	1,202	8,381
Total assets	188,368	166,470	187,404	542,242
Liabilities				
Placements from financial institutions	42,940	-	-	42,940
Placements from non-financial institutions and individuals	-	-	80,912	80,912
Customers' current accounts	617	2,399	15,907	18,923
Other liabilities	-	-	7,407	7,407
Total liabilities	43,557	2,399	104,226	150,182
Equity of investment account holders	11,549	3,957	276,543	292,049
Restricted investment accounts	-	30,555	1,001	31,556
Commitments	-	2,020	42,149	44,169

29. CONCENTRATION OF ASSETS, LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND RESTRICTED INVESTMENT ACCOUNTS (continued)

(b) Geographic sector

31 December 2014	GCC countries	Europe	USA	Asia	Australia	Africa	Total
Assets							
Cash and bank balances	33,833	1,256	2,251	18	-	-	37,358
Placements with financial institutions	76,006	-	-	-	-	-	76,006
Financing assets	272,720	23,158	-	8,065	-	-	303,943
Investment securities	71,181	-	-	21,824	3,918	-	96,923
Assets acquired for leasing (including lease rentals receivable)	43,598	54	-	127	-	-	43,779
Investment in associates	2,604	-	-	-	-	-	2,604
Investment property	13,715	-	-	-	-	-	13,715
Other assets	7,837	738	-	504	-	-	9,079
Property and equipment	8,517	-	-	-	-	-	8,517
Total assets	530,011	25,206	2,251	30,538	3,918	-	591,924
Liabilities							
Placements from financial institutions	50,208	-	-	-	-	-	50,208
Placements from non-financial institutions and individuals	43,782	-	-	-	-	-	43,782
Customers' current accounts	46,817	904	-	107	-	-	47,828
Other liabilities	7,994	41	-	80	-	-	8,115
Total liabilities	148,801	945	-	187	-	-	149,933
Equity of investment account holders	330,113	460	4	8,357	-	-	338,934
Restricted investment accounts	20,973	-	-	-	993	-	21,966
Commitments	55,988	12	-	-	-	-	56,000

Concentration by location for financing assets is measured based on the location of the counterparty, which has a high correlation with the location of the collateral for the exposure.

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29. CONCENTRATION OF ASSETS, LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND RESTRICTED INVESTMENT ACCOUNTS (continued)

(b) Geographic sector (continued)

31 December 2013	GCC countries	Europe	USA	Asia	Australia	Africa	Total
Assets							
Cash and bank balances	32,532	485	5,796	35	-	-	38,848
Placements with financial institutions	78,974	3,771	-	-	-	-	82,745
Financing assets	242,145	11,490	-	-	-	-	253,635
Investment securities	64,030	-	-	22,226	4,141	-	90,397
Assets acquired for leasing (including lease rentals receivable)	35,630	-	-	-	-	-	35,630
Investment in associates	2,681	-	-	-	-	-	2,681
Investment property	6,583	-	-	-	-	-	6,583
Other assets	21,937	908	-	454	43	-	23,342
Property and equipment	8,381	-	-	-	-	-	8,381
Total assets	492,893	16,654	5,796	22,715	4,184	-	542,242
Liabilities							
Placements from financial institutions	42,940	-	-	-	-	-	42,940
Placements from non-financial institutions and individuals	80,912	-	-	-	-	-	80,912
Customers' current accounts	18,073	768	-	82	-	-	18,923
Other liabilities	7,407	-	-	-	-	-	7,407
Total liabilities	149,332	768	-	82	-	-	150,182
Equity of investment account holders	280,560	420	-	11,069	-	-	292,049
Restricted investment accounts	21,687	8,868	-	-	1,001	-	31,556
Commitments	43,717	452	-	-	-	-	44,169

30. FAIR VALUE

a) Fair value of financial instruments

Fair value is an amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

The fair values of quoted Sukuk carried at amortised cost of BD 21,273 thousand (31 December 2013: BD 7,352 thousand) amounts to BD 20,889 thousand as at 31 December 2014 (31 December 2013: BD 7,081 thousand).

In case of financing assets and lease receivables, the average profit rate of the portfolio is in line with current market rates for similar facilities and hence after consideration of adjustment for prepayment risk and impairment charges it is expected that the current value would not be materially different to fair value of these assets. Other than equity investments carried at cost of BD 45,797 thousand (2013: BD 46,306 thousand), the estimated fair values of the Bank's other financial instruments are not significantly different from their carrying values due to their short-term nature.

b) Fair value hierarchy

The table below analyses the financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets and liabilities.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

31 December 2014	Level 1	Level 2	Level 3	Total
Investment securities				
Equity type instruments carried at fair value through income statement	4,961	-	15,148	20,109
Debt type instruments carried at fair value through income statement	398	-	-	398
	5,359	-	15,148	20,507

31 December 2013	Level 1	Level 2	Level 3	Total
Investment securities				
Equity type instruments carried at fair value through income statement	4,765	-	14,959	19,724
Debt type instruments carried at fair value through income statement	1,016	-	-	1,016
	5,781	-	14,959	20,740

The table below shows the reconciliation of movements in value of investments measured using Level 3 inputs:

	2014	2013
At 1 January	14,959	17,452
Total gains or losses:		
- In profit or loss	-	(2,493)
Purchases	189	-
At 31 December	15,148	14,959

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31. RISK MANAGEMENT

Introduction and overview

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risks
- operational risks

This note presents information about the Group's exposure to each of the above risks, its objectives, policies and processes for measuring and managing risk, and the Bank's management of capital.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established an Executive Risk Management Committee, which is responsible for developing and monitoring the Bank's risk management policies in the specified areas. The committee also continuously monitors consistent implementation of the Board approved policies in the Bank and reports deviations, if any, to the Board. The committee consists of heads of business and other functional units in the Bank and reports regularly to the Board Audit and Risk Management Committee.

The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Bank's Audit and Risk Management Committee is responsible for monitoring compliance with the risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Audit and Risk Management Committee is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit and Risk Management Committee.

CREDIT RISK

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's exposures to placements with financial institutions, financing assets, outstanding assets acquired for leasing, investment in sukuk and receivables classified under other assets. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual and group exposure risk, country and sector concentration risk, related party exposure, etc.). The Bank monitors the total exposure to assets acquired for leasing (including lease rentals receivable) on a cumulative basis for monitoring of market risk and credit risk.

The Board of Directors has delegated responsibility for the management of credit risk to its Executive Risk Management Committee (ERMC). A separate Risk Management and Credit Management Department (RMD), reporting to the ERMC is responsible for oversight of the Bank's credit risk, including:

- Formulating credit policies in consultation with business units, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements and submitting the same for approval to the Board of Directors.
- Establishing the authorisation structure for the approval and renewal of credit facilities. Authorisation limits are not at present allocated to business units. Smaller exposures are approved by the Executive Credit & Investment Committee. Larger facilities require approval by the Chief Executive Officer, Board Investment and Credit Committee or the full Board, as the case may be.
- Reviewing and assessing credit risk. RMD assesses all credit exposures and signs off on the relevant proposals prior to approval of the facilities by the appropriate authorities. Renewal and review of facilities are subject to the same process.
- Limiting concentrations of exposure to counterparties, countries and industries in respect of financing assets, assets acquired for leasing as well as investments.
- Developing and maintaining the Bank's risk grading's in order to categorise exposures according to the degree of probable risk of financial loss to focus management on the attendant risks. The risk grading system is also used to identify specific exposures for which impairment provisions may be required. The risk grading framework for the Bank's financing portfolio consists of ten grades reflecting varying degrees of risk of default and the availability of collateral or other credit risk mitigation. The responsibility for setting risk grades lies with the final approving executive / committee as appropriate on the recommendations of the RMD. Risk grades are subject to regular reviews by RMD.

31. RISK MANAGEMENT (continued)

CREDIT RISK (continued)

- Reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types. Regular reports are submitted to the Board on the compliance levels. RMD also provides advice, guidance and specialist skills to business units to promote best practice throughout the Bank in the management of credit risk.
- Each business unit is required to implement the Bank credit policies and procedures in respect of exposures assumed by them and are responsible for the quality and performance of its credit portfolio and for monitoring and controlling all credit risks in its portfolios, irrespective of the approving authority for the exposure. Regular audits of business units and Bank credit processes are undertaken by Internal Audit.

Exposure to credit risk

31 December 2013	Placements with financial institutions	Financing assets	Assets acquired for leasing (including lease rental receivable)	Investment securities-Sukuk	Other financial assets	Total
Impaired:						
Grade 9: Impaired	-	20,535	-	2,001	-	22,536
Unrated	-	-	-	-	7,617	7,617
Allowance for impairment	-	(10,192)	-	(300)	(1,676)	(12,168)
Carrying amount	-	10,343	-	1,701	5,941	17,985
Past due but not impaired:						
Grade 1-6 Low-Fair Risk	-	19,878	7,920	-	-	27,798
Grade 7-8 Watch list	-	7,434	553	-	-	7,987
Past due comprises:						
Up to-30 days	-	11,749	4,172	-	-	15,921
30-60 days	-	2,504	2,529	-	-	5,033
60-90 days	-	11,761	968	-	-	12,729
90-180 days	-	512	499	-	-	1,011
180 days +	-	786	305	-	-	1,091
Carrying amount	-	27,312	8,473	-	-	35,785
Neither past due nor impaired:						
Grade 1-6 Low-Fair Risk	76,006	257,391	35,748	34,277	-	403,422
Grade 7-8 Watch list	-	12,374	-	-	-	12,374
Unrated	-	-	-	-	2,452	2,452
Carrying amount	76,006	269,765	35,748	34,277	2,452	418,248
Less:						
Collective impairment provisions	-	(3,477)	(442)	-	-	(3,919)
Total	76,006	303,943	43,779	35,978	8,393	468,099

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31. RISK MANAGEMENT (continued)

CREDIT RISK (continued)

Exposure to credit risk (continued)

31 December 2013	Placements with financial institutions	Financing assets	Assets acquired for leasing (including lease rental receivable)	Investment securities- Sukuk	Other financial assets	Total
Impaired:						
Grade 9: Impaired	-	25,827	1,884	2,001	-	29,712
Unrated	-	-	-	-	7,614	7,614
Allowance for impairment	-	(12,529)	-	(200)	(1,620)	(14,349)
Carrying amount	-	13,298	1,884	1,801	5,994	22,977
Past due but not impaired:						
Grade 1-6 Low-Fair Risk	-	25,671	3,622	-	-	29,293
Grade 7-8 Watch list	-	8,372	1,339	-	-	9,711
Past due comprises:						
Up to-30 days	-	16,544	2,260	-	-	18,804
30-60 days	-	9,579	1,222	-	-	10,801
60-90 days	-	5,741	313	-	-	6,054
90-180 days	-	792	784	-	-	1,576
180 days +	-	1,387	382	-	-	1,769
Carrying amount	-	34,043	4,961	-	-	39,004
Neither past due nor impaired:						
Grade 1-6 Low-Fair Risk	82,745	196,417	29,145	27,331	-	335,638
Grade 7-8 Watch list	-	13,673	-	-	-	13,673
Unrated	-	-	-	-	16,710	16,710
Carrying amount	82,745	210,090	29,145	27,331	16,710	366,021
Less:						
Collective impairment provisions	-	(3,796)	(360)	-	-	(4,156)
Total	82,745	253,635	35,630	29,132	22,704	423,846

Impaired financial assets

Impaired financial assets are those for which the Bank determines that it is probable that it will be unable to collect all or part of the principal and profit due according to the contractual terms of the exposure. Generally these assets fall under risk grades 9 or 10, for other financial assets impairment is assessed on an individual basis for each exposure under the Bank's internal credit risk grading system.

Past due but not impaired exposures

The exposure pertains to financing assets where contractual profit or principal payments are past due but the Bank believes that impairment is not appropriate on the basis of subsequent collections, the level of security / collateral available and / or the stage of collection of amounts owed to the Bank.

31. RISK MANAGEMENT (continued)

CREDIT RISK (continued)

Renegotiated facilities

Exposures classified as neither past due nor impaired financing facilities include facilities renegotiated during the year amounting to BD 32,910 thousand (2013: BD 17,509 thousand) that would otherwise be past due as per their original repayment terms. The renegotiated terms usually require settlement of profits accrued till date on the facility and / or part payment of the principal and / or obtaining of additional collateral coverage. The renegotiated facilities are subject to revised credit assessments and independent review by the RMD. Of the total past due facilities of BD 35,811 thousand (2013: BD 39,004 thousand) only instalments of BD 4,164 thousand (2013: BD 6,370 thousand) are past due as at 31 December 2014.

Allowances for impairment

The Bank makes provisions for impairment on individual assets classified under grades 9 and 10. This is done on the basis of the present value of projected future cash flows from the assets themselves and consideration of the value of the collateral securities available. On a collective basis, the Bank has provided for impairment losses based on management's judgment of the extent of losses incurred but not identified based on the current economic and credit conditions.

Write-off policy

The Bank writes off an asset / security balance (net of any related allowances for impairment losses) when it determines that the asset / security are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the counterparty's financial position such that he can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure. During the year, the Bank has written off a financing facility amounting to BD 2,465 thousand (2013: BD 6,518 thousand) which was fully provided.

Collaterals

The Bank holds collateral against financing assets and receivables from assets acquired for leasing in the form of mortgage/ pledge over property, listed/ unlisted securities, other assets and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and updated periodically, generally at annual intervals. Collateral generally is not held against exposure to other banks and financial institutions. An estimate of the fair value of collateral and other security enhancements held against financial assets is shown below. This includes the value of financial guarantees from banks, but not corporate and personal guarantees as the values thereof are not readily quantifiable. The collateral values considered for disclosure are restricted to the extent of the outstanding exposures.

During the year, the Bank enforced collaterals of three non-performing financing facilities by transfer of ownership of three land plots and thirteen villas in the name of the Bank (refer note 9). Two of the three facilities were fully settled and one facility was rescheduled.

	As at 31 December 2014			As at 31 December 2013		
	Financing assets	Assets acquired for leasing (including lease rentals receivable)	Total	Financing assets	Assets acquired for leasing (including lease rentals receivable)	Total
Against impaired						
Property	8,753	-	8,753	11,729	1,329	13,058
Equities	-	-	-	-	-	-
Other	-	-	-	993	-	993
Against past due but not impaired						
Property	11,740	7,426	19,166	24,116	4,961	29,077
Equities	1,899	-	1,899	-	-	-
Other	5,586	-	5,586	4,561	-	4,561
Against neither past due nor impaired						
Property	84,035	37,207	121,242	77,501	28,463	105,964
Equities	6,695	-	6,695	11,362	-	11,362
Other	49,352	-	49,352	56,656	-	56,656
Total	168,060	44,633	212,693	186,918	34,753	221,671

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31. RISK MANAGEMENT (continued)

CREDIT RISK (continued)

Collaterals (continued)

The average collateral coverage ratio on secured facilities is 109.49% at 31 December 2014 (31 December 2013: 163.41%).

For analysis of concentration of total assets and liabilities refer note 29.

Further, for financing assets and assets acquired for leasing the Bank monitors concentrations of credit risk by sector and by geographic location.

An analysis of concentrations of credit risk at the reporting date is shown below:

Concentration by Sector	As at 31 December 2014			As at 31 December 2013		
	Financing assets	Assets acquired for leasing (including lease rentals receivable)	Total	Financing assets	Assets acquired for leasing (including lease rentals receivable)	Total
Banking and finance	41,283	501	41,784	38,680	1,060	39,740
Real estate:						
- Property	46,529	43,278	89,807	38,261	33,549	71,810
- Infrastructure Development	4,162	-	4,162	10,242	-	10,242
- Land	10,639	-	10,639	11,048	-	11,048
Construction	37,012	-	37,012	39,353	-	39,353
Trading	87,928	-	87,928	63,434	-	63,434
Manufacturing	16,399	-	16,399	13,116	-	13,116
Others	59,991	-	59,991	39,501	1,021	40,522
Total carrying amount	303,943	43,779	347,722	253,635	35,630	289,265

Settlement risk

The Bank's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a company to honour its obligations to deliver cash, securities or other assets as contractually agreed.

Settlement limits form part of the credit approval / limit monitoring process described earlier. Acceptance of settlement risk on free settlement trades requires transaction specific or counterparty specific approvals from RMD.

LIQUIDITY RISK

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

Management of liquidity risk

The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

Financial Control Department (FCD) collates data from treasury and other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. FCD communicates the information to the treasury who manages the Bank's portfolio of short-term liquid assets, largely made up of short-term placements with other banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole.

The daily liquidity position is monitored by FCD. The Bank has in place a Liquidity Contingency Plan, the elements of which are periodically tested. Tools for implementation of regular stress testing under various scenarios are in place. All liquidity policies and procedures are subject to review by ALCO and approval by appropriate authorities. A summary report, including any exceptions and remedial action taken, is submitted regularly to ALCO members.

31. RISK MANAGEMENT (continued)

LIQUIDITY RISK (continued)

Exposure to liquidity risk

The key measure used by the Bank for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For computation of this, net liquid assets are considered as including cash and bank balances and placements with financial Institutions and investments in sukuk less placements from financial institution, and deposits comprise current accounts, placements from non-financial institutions and individuals, and equity of investment account holders.

Details of the reported Bank ratio of net liquid assets to deposits and customers at the reporting date and during the reporting period were as follows:

	2014 %	2013 %
At 31 December	23.03	25.05
Average for the period	28.49	21.93
Maximum for the period	34.79	36.03
Minimum for the period	23.03	4.86

For maturity profile of assets and liabilities refer note 28.

MARKET RISK

Market risk is the risk that changes in market prices, such as profit rate, equity prices, foreign exchange rates and credit spreads will affect the Bank's income, future cash flows or the value of its holdings of financial instruments. Market risk comprises three types of risk: currency risk, profit rate risk and other price risk. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Management of market risks

The Bank separates its exposure to market risk between trading and non-trading portfolios. The Bank has no trading positions in equity or commodities and the main source of market risk for the Bank is its foreign exchange exposure and profit rate gap.

The Bank does not do any trading in foreign exchange. The Bank does not engage in proprietary trading of foreign exchange derivatives. However, the Bank enters into Shari'a compliant foreign exchange risk management transactions to hedge economic risks to cover significant open positions under its risk management guidelines. All foreign exchange income/ losses arising out of customer transactions and revaluation of statement of financial position assets and liabilities are booked by the treasury operations. The responsibility for monitoring and managing the related risks also rests with the Treasury department.

Overall authority for market risk management is vested with ALCO. The RMD is responsible for the development of detailed risk management policies (subject to review and approval by appropriate approval authorities) and the Financial Control Department is responsible for the day-to-day review of their implementation.

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31. RISK MANAGEMENT (continued)

MARKET RISK (continued)

Exposure to profit rate risk–non–trading portfolios

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market profit rates. Profit rate risk is managed principally through monitoring profit rate gaps and by having pre-approved limits for re-pricing bands. The ALCO is the monitoring body for compliance with these limits and is assisted by the Bank's Risk Management Department in its day-to-day monitoring activities.

A summary of the Bank's profit rate gap position at 31 December 2014 is as follows:

31 December 2014	Up to 3 months	3 - 6 months	6 months - 1 year	1 - 3 years	More than 3 years	Total
Assets						
Placements with financial institutions	76,006	-	-	-	-	76,006
Financing assets	52,664	23,199	20,336	73,844	133,900	303,943
Assets acquired for leasing (including lease rentals receivable)	-	-	531	829	42,419	43,779
Investments securities (sukuk)	35,978	-	-	-	-	35,978
Total profit rate sensitive assets	164,648	23,199	20,867	74,673	176,319	459,706
Liabilities and investment accounts						
Placements from financial institutions	30,326	-	3,054	16,828	-	50,208
Placements from non-financial institutions and individuals	22,567	5,056	9,156	5,830	1,173	43,782
Customers' current accounts	1,429	-	-	-	-	1,429
Equity of investments account holders	129,488	49,705	55,610	104,131	-	338,934
Total profit rate sensitive liabilities and investment accounts	183,810	54,761	67,820	126,789	1,173	434,353
Profit rate gap	(19,162)	(31,562)	(46,953)	(52,116)	175,146	25,353

31. RISK MANAGEMENT (continued)

MARKET RISK (continued)

31 December 2013	Up to 3 months	3 - 6 months	6 months - 1 year	1 - 3 years	More than 3 years	Total
Assets						
Placements with financial institutions	82,745	-	-	-	-	82,745
Financing assets	41,884	15,450	17,934	77,891	100,476	253,635
Assets acquired for leasing (including lease rentals receivable)	6	-	1,884	1,170	32,570	35,630
Investments securities (sukuk)	8,335	4,286	-	2,537	13,974	29,132
Total profit rate sensitive assets	132,970	19,736	19,818	81,598	147,020	401,142
Liabilities and investment accounts						
Placements from financial institutions	25,492	-	-	17,448	-	42,940
Placements from non-financial institutions and individuals	24,230	20,047	31,181	4,258	1,196	80,912
Customers' current accounts	545	-	-	-	-	545
Equity of investments account holders	156,922	52,336	80,078	2,713	-	292,049
Total profit rate sensitive liabilities and investment accounts	207,189	72,383	111,259	24,419	1,196	416,446
Profit rate gap	(74,219)	(52,647)	(91,441)	57,179	145,824	(15,304)

The management of profit rate risk against profit rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and non-standard profit rate scenarios. Standard scenarios that are considered on a monthly basis include a 100 basis point (bp) parallel fall or rise across all yield curves and a 50 bp rise or fall of all yield curves.

An analysis of the Bank's sensitivity to an increase or decrease in market profit rates (assuming no asymmetrical movement in yield curves and a constant statement of financial position position) is as follows:

	100bp parallel increase / decrease	50bp increase / decrease
At 31 December 2014	±254	±127
At 31 December 2013	±153	±77

Overall non-trading profit rate risk positions are managed by Treasury department, which uses short term investment securities, placement with banks and placement from banks to manage the overall position arising from the Bank's non-trading activities.

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31. RISK MANAGEMENT (continued)

MARKET RISK (continued)

Exposure to foreign exchange risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group had the following significant net exposures denominated in foreign currency as of 31 December.

	2014 BHD Equivalent	2013 BHD Equivalent
US Dollars*	115,278	107,636
Other GCC Currencies *	16,676	20,602
Euros	5,030	4,932
Australian Dollars	4,608	4,601
Kuwaiti Dinars	3,261	3,060
Sterling Pounds	1,493	1,455
Indian Rupee	18	35

(*) The exposure in US dollars and other GCC currencies does not create any foreign exchange risk for the Bank since Bahrain Dinars and other GCC currencies are effectively pegged to the US Dollars.

The management of foreign exchange risk against net exposure limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various foreign exchange scenarios. Standard scenarios that are considered on a monthly basis include a 5% plus / minus increase in exchange rates, for currencies other than US Dollars, other GCC currencies.

An analysis of the Bank's sensitivity to an increase or decrease in foreign exchange rates (assuming all other variables, primarily profit rates, remain constant) is as follows:

	2014 BHD Equivalent	2013 BHD Equivalent
Euros	±251	±247
Australian Dollars	±230	±230
Kuwaiti Dinars	±163	±153
Sterling Pounds	±75	±73
Indian Rupees	±1	±2

Exposure to other price risks–non–trading portfolios

Credit spread risk on debt securities is subject to regular monitoring by RMD, but is not currently significant in relation to the overall financial position of the Bank.

The Group's unquoted equity securities carried at cost are exposed to risk of changes in equity values. Refer to note 21 for significant estimates and judgments in relation to impairment assessment of unquoted equity investments carried at cost. The Group manages exposure to other price risks by actively monitoring the performance of the equity securities. The performance assessment is performed on a quarterly basis and is reported to the Board Investment and Credit Committee.

OPERATIONAL RISK

Operational risk is the risk of loss arising from systems and control failures, fraud and human errors, which can result in financial and reputation loss, and legal and regulatory consequences. The Bank manages operational risk through appropriate controls, instituting segregation of duties and internal checks and balances, including internal audit and compliance. The Risk Management Department is in charge of identifying, monitoring and managing operational risk in the bank. The Bank already has an approved policy for doing this and all required organisational and physical infrastructure are in place.

The Bank has completed conducting one cycle of Risk Control Self-Assessment (RCSA) of Operational risk for majority of the departments of the Bank to identify the important Key Risk Areas, Key Risk Indicators and Key Risk Triggers. Furthermore for the remaining departments Key Risk Areas have been identified and the next process will be the identification of Key Risk Indicators and Key Risk Triggers. The RCSA process is a continuous process and will be conducted at regular frequencies across the Bank. It will be an annual process to review all the KRIs. A software for monitoring these triggers and recording actual and near miss losses is already in place. The medium term objective of the Bank is to generate statistically reliable data to upgrade to more sophisticated modes of Operational Risk Control both to manage the risk better and to reduce capital commitment.

31. RISK MANAGEMENT (continued)

CAPITAL MANAGEMENT

The Central Bank of Bahrain (CBB), sets and monitors capital requirements for the Bank as a whole. In implementing current capital requirements CBB requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. Capital adequacy regulations of CBB is based on the principles of Basel II of the IFSB guidelines.

The Bank's regulatory capital is analysed into two tiers:

- *Tier 1 capital*, includes ordinary share capital, disclosed reserves including share premium, general reserves, legal / statutory reserve as well as retained earnings after deductions for goodwill and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.
- *Tier 2 capital*, includes interim retained profits reviewed by the auditors and an allowed portion profit equalisation reserve (PER) and investment risk reserves (IRR). As per CBB, the PER & IRR can be up to a maximum amount equal to the capital charge pertaining to 30% of the risk weighted assets financed by unrestricted investment accounts.

Certain limits are applied to elements of the capital base in line with regulatory requirements. Tier 1 capital should represent at least half of the total eligible capital, i.e., Tier 2 capital is limited to 100% of Tier 1 capital. The limit on Tier 2 capital is based on the amount of Tier 1 capital after all deductions of investments pursuant to Prudential Consolidation and Deduction Requirements (PCD) Module of the CBB. The PCD Module sets out the regulatory rules for prudential consolidation, pro-rata consolidation or deduction where the own controlling or significant minority stakes in regulated financial entities, insurance entities and have significant exposures to investment in commercial entities. It also sets out the framework for the prudential deductions from capital for various instances including exposures to counterparties exceeding the large exposure limits as set out by CBB. As on 31 December 2014, the Bank has made deduction of BD 922 thousand each (2013: BD 2,369 thousand), from its Tier 1 and Tier 2 capital respectively, in line with the requirements of the PCD Module.

Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

For computation of credit risk on assets financed by equity of investment account holders, 30% of risk weight assets are considered as against 100% for assets self-financed.

The Bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The Bank has adopted the standardised approach to credit and basic indicator approach for management of operational risk under the CBB capital adequacy framework. The Bank on a conservative basis for capital management does not claim any of the benefits for permissible credit risk mitigants against credit exposure.

The Bank's regulatory capital position at 31 December was as follows:

	31 December 2014	31 December 2013
Total risk weighted assets	450,894	439,219
Tier 1 capital	102,133	98,331
Tier 2 capital	2,997	2,476
Total regulatory capital	105,130	100,807
Total regulatory capital expressed as a percentage of total risk weighted assets	23.32	22.95

The Bank has complied with all externally imposed capital requirements throughout the year.

During the year, CBB issued the final regulations to give effect to the Basel III framework which is effective from 1 January 2015. Basel III introduces capital components like core equity tier I (CET1), and additional tier I (AT1), it also requires maintenance of certain capital buffers. Computation of CET1 is subject to certain regulatory deductions, these deductions would be effective in a phased manner through the transitional arrangements under the revised regulations over the period from 2015 to 2018. The revised regulations prescribe higher risk weight for certain type of exposures, the significant investments in financial institutions, significant investments in commercial entities and large exposures that exceed materiality thresholds. The Bank is currently assessing the full impact of the revised regulations and believes that the current capital position is sufficient to meet the new regulatory capital requirements.

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31. RISK MANAGEMENT (continued)

CAPITAL MANAGEMENT (continued)

Capital allocation

The allocation of capital between specific operations and activities is primarily driven by regulatory requirements. The Bank's capital management policy seeks to maximise return on risk adjusted while satisfying all the regulatory requirements. The Bank's policy on capital allocation is subject to regular review by the Board.

32. PROPOSED APPROPRIATIONS

The Board of Directors propose the appropriation for zakah of BD 19 thousand in 2014 (2013: Nil) which is subject to shareholders' approval in the ensuing Annual General Meeting.

33. COMMITMENTS

The commitments contracted in the normal course of business of the Bank:

	2014	2013
Undrawn commitments to extend finance	41,098	35,897
Financial guarantees	14,902	8,272
	56,000	44,169

Performance obligations

During the ordinary course of business, the Group may enter into performance obligations in respect of certain of its infrastructure development projects. It is the usual practice of the Group to pass these performance obligations, wherever possible, on to the companies that own the projects. In the opinion of the management, no liabilities are expected to materialise on the Group at 31 December 2014 due to the performance of any of its projects.

34. SOCIAL RESPONSIBILITY

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

35. COMPARITIVES

Certain prior period amounts have been regrouped to conform to current year's presentation. Such regrouping did not affect previously reported profit or equity.

These disclosures have been prepared in accordance with the Public Disclosure Module ("PD"), Section PD-1.3: Disclosures in Annual Reports, CBB Rule Book, and Volume II for Islamic Banks. To avoid any duplication, information required under PD module but already disclosed in other sections of annual report has not been reproduced. These disclosures are part of the annual report for the year ended 31 December 2014 and should be read in conjunction with the consolidated financial statements for the year ended 31 December 2014 and other sections of the annual report.

RISK MANAGEMENT DISCLOSURES

EXECUTIVE SUMMARY

The Central Bank of Bahrain's ("CBB") Basel II guidelines outlining the capital adequacy framework for banks incorporated in the Kingdom of Bahrain became effective from 1 January 2008. These disclosures have been prepared in accordance with the CBB requirements outlined in the Public Disclosure Module ("PD"), Section PD-1.3: Disclosures in Annual Reports, of the CBB Rule Book, Volume II for Islamic Banks. Section PD-1.3 reflects the requirements of Basel II - Pillar III and the Islamic Financial Services Board's ("IFSB") recommended disclosures for Islamic banks.

The disclosures in this report are in addition to or in some cases, serve to clarify the disclosures set out in the consolidated financial statements for the year ended 31 December 2014, presented in accordance with the Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"). To avoid any duplication, information required under PD module but already disclosed in other sections of the annual report has not been reproduced in these disclosures.

All figures presented in this section are reported in Bahraini Dinars (in thousand) and are as of 31 December 2014 unless otherwise stated.

Khaleeji Commercial Bank BSC ("the Bank" or "KHCBB") has adopted the Standardised Approach for Credit Risk and Market Risk and the Basic Indicator Approach for Operational Risk to determine its capital requirements, details of which are given in section 2. This section contains a description of the Bank's risk management and capital adequacy policies and practices including detailed quantitative information on risk components and capital adequacy.

The Bank's Tier I and total capital adequacy ratios comply with the minimum capital requirements under the CBB's Basel II framework.

The Bank's total risk weighted assets as at 31 December 2014 amounted to BD 450,894 thousand. Credit risk accounted for 89.1%, market risk 3.7%, and operational risk 7.2% of the total risk weighted assets. Tier I and total regulatory capital were BD 102,133 thousand and BD 105,130 thousand respectively as at 31 December 2014.

At 31 December 2014, Bank's Tier I and total adequacy ratios were 22.65% and 23.32% respectively.

1 GROUP STRUCTURE

The Bank operates under a retail banking license granted by the CBB on 20 October 2003. The Bank does not have significant operating subsidiaries. The subsidiaries set-up is primarily special purpose entities with nominal capital to execute specific investment transactions. The subsidiaries qualify as commercial entities as per the CBB guidelines and are risk weighted as investments for capital adequacy computation purposes.

2 INTRODUCTION TO BASEL II & RISK MANAGEMENT

The CBB has mandated that the Basel Committee on Banking Supervision's ("Basel Committee"). Basel II capital adequacy framework is applicable to all banks incorporated in the Kingdom of Bahrain from 1 January 2008. The Bank has accordingly taken steps to comply with these requirements. The Basel II framework is intended to strengthen risk management practices and processes within the financial institutions.

CBB's capital adequacy framework is based on three pillars, consistent with the Basel II framework adopted by the Basel Committee, as follows:

- Pillar I: calculation of the risk weighted assets ("RWA" or "RWA's") and capital requirement.
- Pillar II: the supervisory review process, including the Internal Capital Adequacy Assessment Process ("ICAAP").
- Pillar III: rules for disclosure of risk management and capital adequacy information.

Pillar I

Pillar I defines the regulatory minimum capital requirements for each bank to cover the credit risk, market risk and operational risk inherent in its business model. It also defines the methodology for measurement of these risks and the various elements of qualifying capital. The capital adequacy ratio is calculated by dividing the regulatory capital base by total RWA's. CBB has mandated that the ratio be maintained at a minimum of 12% and has set a trigger ratio of 12.5%. If the capital adequacy ratio falls below 12.5%, additional prudential reporting requirements apply, and a formal action plan to restore the ratio above the trigger level is to be formulated and submitted to the CBB.

The table below summarizes the Pillar I risks and the approach used by the Bank to calculate the RWA's in each case in accordance with the CBB's Basel II capital adequacy framework:

Risk Type	Approach used by the Bank
Credit Risk	Standardised Approach
Market Risk	Standardised Approach
Operational Risk	Basic Indicator Approach

Pillar II

Pillar II defines the process of supervisory review of an institution's risk management framework and, ultimately its capital adequacy.

Pillar II comprises two processes:

- An Internal Capital Adequacy Assessment Process ("ICAAP"), and
- A supervisory review and evaluation process.

The Bank has in place ICAAP procedures for computation of economic capital for all risks including those not covered under Pillar I. The Bank regularly monitors its internal capital adequacy ratio to ensure that there is adequate cover for all risks faced by the Bank.

RISK MANAGEMENT DISCLOSURES

2 INTRODUCTION TO BASEL II & RISK MANAGEMENT (CONTINUED)

Pillar III

Pillar III complements the other two pillars and focuses on enhanced transparency in disclosure of information by the Banks to promote better market discipline. The information to be disclosed covers all areas including business performance, capital adequacy, risk management, etc. The disclosures are designed to enable stakeholders and market participants to assess an institution's risk appetite and risk exposures and to encourage all banks, via market pressures, to move towards more advanced forms of risk management.

In April 2008, CBB published a paper covering the detailed disclosure requirements to be followed by licensed banks in Bahrain to be in compliance with Pillar III under the Basel II framework. This document is prepared in accordance with these directives.

2.1 The risk management function

The Board of Directors has overall responsibility for risk management in the Bank. The Board lays down the risk management policies of the Bank and quantifies its risk appetite through appropriate definitions of various risk limits and tolerances. The Board discharges its risk management responsibilities through the Board Audit & Risk Management Committee ("BARMC").

The Board has established an Executive Risk Management Committee ("ERMC"), which is responsible for developing and monitoring Bank risk management policies in the specified areas. The committee consists of heads of business and other functional units in the Bank and reports regularly to the BARMC. The committee meets on a monthly basis as per set agenda and its Terms of Reference covering all risk issues and policy matters.

The day to day risk management functions are performed by the Risk Management Department ("RMD") of the Bank. RMD is responsible to ensure that the policies laid down by the Board are consistently implemented across the Bank and to review the adequacy of these policies periodically. It monitors all risk taking activities and ensures that the risk limits defined by the Board are complied with. The department has specialized personnel dealing with Credit, Market, and Operational Risks. It is independent of all risk taking functions in the Bank and reports to the BARMC through the ERMC chaired by the CEO.

The Asset Liability Management Committee ("ALCO") of the Bank acting through the Treasury Department monitors the Bank's liquidity position and recommends appropriate action to the Board where necessary. There is a high level of coordination between the RMD, ERMC and ALCO.

The RMD prepares a risk overview report on a quarterly basis which covers in detail the various risks faced by the Bank and the same is discussed at the ERMC, BARMC and the Board on a quarterly basis.

The Bank considers that its overall risk management strategies have been effective throughout the reporting period.

All policies having significant impact on the overall internal control framework existing in the Bank are subject to periodic review and approval by the Board of Directors.

The RMD, together with the Internal Audit and Compliance Departments, provides independent assurance that all types of risk are being measured and managed in accordance with the policies and guidelines set by the Board of Directors.

3 CAPITAL MANAGEMENT & CAPITAL ADEQUACY RATIO

3.1 Capital management

The Bank's policy is to maintain a strong capital base to develop and retain investor, creditor and market confidence and to sustain business growth. The Bank recognises the impact of a high level of capital on shareholders' returns, while not losing sight of the security and market confidence afforded by a sound capital base. The Bank aims to maintain a minimum total capital adequacy ratio significantly in excess of that mandated by the CBB.

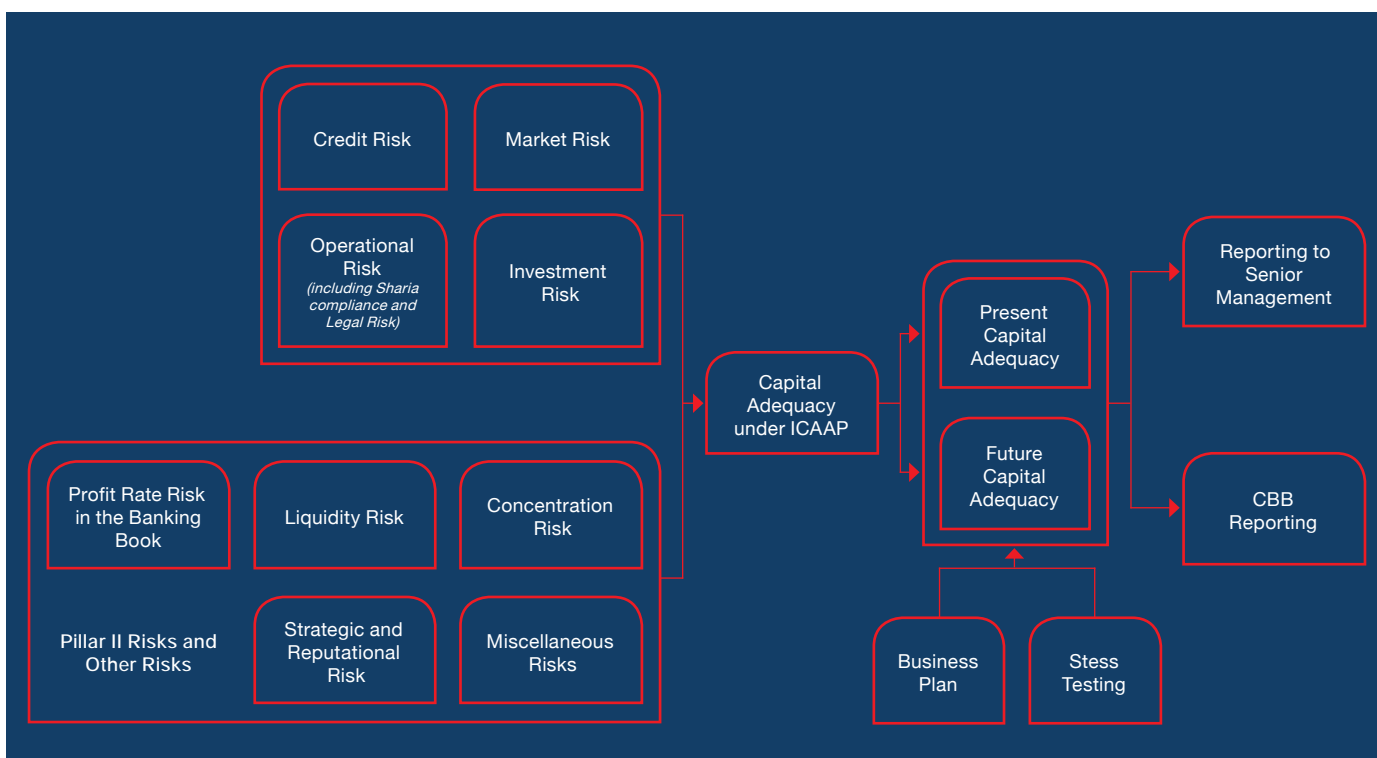
3.2 Internal Capital Adequacy Assessment Process ("ICAAP")

The Bank has an established ICAAP as per the requirements under Pillar II of Basel II. ICAAP prescribes procedures and measures designed to ensure appropriate identification, measurement, aggregation and monitoring of the Bank's risks. It also defines an appropriate level of internal capital in relation to the Bank's overall risk profile and business plan.

3 CAPITAL MANAGEMENT & CAPITAL ADEQUACY RATIO (CONTINUED)

3.2 Internal Capital Adequacy Assessment Process ("ICAAP") (continued)

ICAAP framework at the Bank



3.2.1 Risk addressed by the ICAAP

Risk Type	Metrics based on which internal capital is allocated
Credit risk Market risk Investment risk Operational risk	Regulatory capital adequacy guidelines to be used as proxy for internal capital for Pillar I risks
Liquidity risk	Maximum cumulative maturity gap, Liquidity ratio, Financing to deposit ratio
Profit rate risk (banking book)	Revaluation / sensitivity of the re-pricing gaps
Credit concentration risk	Thresholds for counterparty, country, sector exposures
Fiduciary Risk	Size of off balance sheet special purpose vehicles (RIA's) & Large Investment Products
Reputational risk	Credit quality, Operational risk, Reputation related loss
Other Risks (strategic, Shari'a / regulatory compliance, business cycle)	Additional capital based on Pillar I risk weighted exposures

RISK MANAGEMENT DISCLOSURES

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3 CAPITAL MANAGEMENT & CAPITAL ADEQUACY RATIO (CONTINUED)

3.3 Capital structure, minimum capital requirements and capital adequacy

During the year, the paid up capital of the Bank has remained the same amounting to BD 115,416 thousand. Following is the break-up of capital structure as at 31 December 2014:

	31 December 2014
Net available capital	
Issued and fully paid ordinary shares	115,416
Less: Treasury shares	(6,351)
Statutory reserve	6,728
Share premium	1,535
Accumulated losses	(14,273)
Less regulatory deduction: Excess amount over maximum permitted large exposure limit	(922)
Tier I capital	102,133
Collective impairment loss provision	3,919
Less regulatory deduction: Excess amount over maximum permitted large exposure limit	(922)
Tier II capital	2,997
Net available capital	105,130

	31 December 2014
Risk weighted assets	
Credit risk weight exposures	401,749
Market risk weight exposures	16,486
Operational risk weight exposures	32,659
Total risk weighted assets	450,894
Capital adequacy ratio (Tier I)	22.65%
Capital adequacy ratio (Total capital)	23.32%

The above capital adequacy ratios are calculated by dividing the respective regulatory capital base by the total RWA's.

Regulatory capital components

The above components of Tier I and Tier II capital are as per the relevant CBB guidelines. According to these, Tier II capital is restricted to 100% of Tier I capital after all deductions of investments pursuant to PCD module of CBB rule book. As at 31 December 2014, the Bank has deducted BD 1,844 thousand related to excess amount over maximum permitted large exposure limit in line with the PCD module.

Risk weighted assets

Credit risk

For regulatory reporting purposes, the Bank calculates the capital requirements for credit risk based on the standardised approach. Under this approach, the on and off-balance sheet credit exposures are assigned risk weights based on the type of counterparty, type of the exposure, and source of funding (equity of investment account holders ("IAH") or own funds). Further for capital adequacy computations, 100% of the RWA's is reckoned for self-financed assets while only 30% is considered for assets funded through equity of IAH. The risk weights for types of counterparties and exposures are prescribed by CBB.

3 CAPITAL MANAGEMENT & CAPITAL ADEQUACY RATIO (CONTINUED)

3.3 Capital structure, minimum capital requirements and capital adequacy (continued)

Market risk

The Bank uses the standardised approach to measure market risk. Market risk for the Bank is primarily on account of the foreign exchange exposures that are considered as specific risks. As per the CBB guidelines, capital for foreign exchange risk is computed at 8% of overall net open foreign currency positions of the Bank and this is multiplied by 12.5 to derive the market RWA's.

Operational risk

The Bank adopts the Basic Indicator Approach to evaluate operational risk charge in accordance with the CBB Capital Adequacy Module for Islamic Banks. According to this approach, the Bank's average gross income for the past three financial years is multiplied by a fixed coefficient alpha of 15% set by the CBB to arrive at the capital required and a multiple of 12.5 is used to arrive at the RWA's that are subject to capital charge.

Break-up of capital requirement in accordance with the Capital Adequacy Module of the CBB for the year ended 31 December 2014 is as follows:

Exposure classification	Exposure			Risk Weighted Assets *			Capital requirement @ 12%		
	Self-financed	IAH	Total	Self-financed	IAH	Total	Self-financed	IAH	Total
Cash and collection items	2,550	-	2,550	-	-	-	-	-	-
Sovereigns	5,349	28,151	33,500	-	-	-	-	-	-
Banks	-	84,303	84,303	-	8,094	8,094	-	971	971
Corporates	113,359	201,157	314,516	113,359	60,347	173,706	13,603	7,242	20,845
Residential mortgage	42,804	-	42,804	32,103	-	32,103	3,852	-	3,852
Past due facilities	18,852	-	18,852	24,848	-	24,848	2,982	-	2,982
Investment in equities / sukuks	26,719	19,964	46,683	40,079	8,984	49,063	4,810	1,078	5,888
Holdings of real estate	59,482	-	59,482	111,795	-	111,795	13,415	-	13,415
Other assets	2,140	-	2,140	2,140	-	2,140	257	-	257
Credit Risk	271,255	333,575	604,830	324,324	77,425	401,749	38,919	9,291	48,210
Market Risk	14,413	6,913	21,326	14,413	2,073	16,486	1,730	249	1,979
Operational Risk	32,659	-	32,659	32,659	-	32,659	3,919	-	3,919
Total	318,327	340,488	658,815	371,396	79,498	450,894	44,568	9,540	54,108

* For capital adequacy computations, 100% of the RWA's is reckoned for self-financed assets while only 30% is considered for assets funded through equity of IAH.

RISK MANAGEMENT DISCLOSURES

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4 CREDIT RISK

4.1 Credit risk management

Credit Risk is the risk that counterparty fails to meet its obligations in accordance with agreed terms and conditions. The major sources of credit risk in the Bank are under the following classes of assets:

- Placements with financial institutions,
- Financing assets,
- Assets acquired for leasing (including lease rentals receivable), and
- Investments in Sukuk.

For the purpose of capital adequacy computation (as well as certain other tables below) the following have also been considered as a part of credit risk:

- Investments in quoted and unquoted equity,
- Investment in associates,
- Investment property, and
- Other assets (including property and equipment).

The Bank has the necessary internal processes for assessing, monitoring and controlling credit risk both at the individual credit and portfolio levels. Credit limits are approved after a thorough assessment which takes into account the financial strength of the counterparty, the technical feasibility and economic viability of the business being financed, the adequacy and quality of the cash flow available for repayment, etc. in addition to availability of collateral security by way of physical assets or guarantees. The RMD reviews every credit proposal and incorporates its remarks on the proposal before the same is considered by the appropriate authority as per delegated approval levels granted by the Bank's Board of Directors.

At the portfolio level, the Board has established risk concentration limits for single counterparties and related counterparties forming a business group, geographical and economic sectors as well as exposures to counterparties related to the Bank and/or its major shareholders. The RMD regularly monitors compliance with these limits and deviations if any are reported regularly to the Senior Management, Risk Management Committees and the Board of Directors.

4.2 Levels of exposure

The table below shows gross credit exposure along with average credit exposure broken down under different exposure classes as at 31 December 2014:

Gross / Average Credit Exposures	Average Exposure ¹	Gross Exposure		
		Self-financed	IAH	Total
Cash and bank balances ²	37,272	7,684	29,674	37,358
Placement with financial institutions	85,825	-	76,006	76,006
Financing assets	280,486	106,667	197,276	303,943
Investment securities - Equity type	66,155	60,945	4,961	65,906
Investment securities - Debt type	31,292	-	31,017	31,017
Assets acquired for leasing (including lease rentals receivable)	40,974	43,779	-	43,779
Investments in associates	2,636	2,604	-	2,604
Investment property	8,366	13,715	-	13,715
Other assets, including property and equipment	20,892	17,596	-	17,596
Total funded exposures	573,898	252,990	338,934	591,924
Financial guarantees	4,245	5,465	-	5,465
Undrawn commitments to extend finance	10,411	12,801	-	12,801
Total unfunded exposures ³	14,656	18,266	-	18,266

¹ Represents quarterly average balances for the year ended 31 December 2014.

² Includes cash balance of BD 2,550 thousand.

³ Unfunded exposures are reported at cash conversion factors (CCF).

4 CREDIT RISK (CONTINUED)

4.3 Concentration of credit risk

4.3.1 Geographic distribution

The geographical exposure profile as at 31 December 2014 was as follows:

31 December 2014	GCC Countries	Europe	USA	Asia	Australia	Total
Assets						
Cash and bank balances	33,833	1,256	2,251	18	-	37,358
Placements with financial institutions	76,006	-	-	-	-	76,006
Financing assets	272,720	23,158	-	8,065	-	303,943
Investment securities	71,181	-	-	21,824	3,918	96,923
Assets acquired for leasing (including lease rentals receivable)	43,598	54	-	127	-	43,779
Investment in associates	2,604	-	-	-	-	2,604
Investment property	13,715	-	-	-	-	13,715
Other assets	7,837	738	-	504	-	9,079
Property and equipment	8,517	-	-	-	-	8,517
Total funded exposures	530,011	25,206	2,251	30,538	3,918	591,924
Financial guarantees	14,902	-	-	-	-	14,902
Undrawn commitments to extend finance	41,086	12	-	-	-	41,098
Total unfunded exposures	55,988	12	-	-	-	56,000

4.3.2 Industry / sector-wise distribution

The Board of Directors has stipulated maximum exposures to various industry sectors. The industry/ sector wise exposure as at 31 December 2014 was as follows:

31 December 2013	Banks and financial institutions	Real estate	Others	Total
Assets				
Cash and bank balances	37,358	-	-	37,358
Placements with financial institutions	76,006	-	-	76,006
Financing assets *	41,285	114,411	148,247	303,943
Investment securities	26,537	42,614	27,772	96,923
Assets acquired for leasing (including lease rentals receivable)	501	43,211	67	43,779
Investment in associates	-	2,604	-	2,604
Investment property	-	13,715	-	13,715
Other assets	-	1,768	7,311	9,079
Property and equipment	-	7,169	1,348	8,517
Total funded exposures	181,687	225,492	184,745	591,924
Financial guarantees	-	10,237	4,665	14,902
Undrawn commitments to extend finance	-	5,804	35,294	41,098
Total unfunded exposures	-	16,041	39,959	56,000

* Financing asset exposures have been classified based on the purpose of financing.

RISK MANAGEMENT DISCLOSURES

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4 CREDIT RISK (CONTINUED)

4.3 Concentration of credit risk (continued)

4.3.3 Transactions with related counterparties

Related counterparties are those entities which are related to the Bank through significant shareholding, control, or both. Wherever the Bank has entered into business transactions with such counterparties, such transactions have been done at an arm's length basis and on commercial terms that bring no disadvantage to the Bank. For the purpose of identification of related counterparties, the Bank strictly follows the guidelines issued by CBB for the purpose. Detailed break up is presented in note 23 of the consolidated financial statements for the year ended 31 December 2014.

4.3.4 Exposures in excess of 15% of capital base

Single exposures in excess of 15% of the Bank's capital base on individual counterparties require prior approval of the CBB except where exempted under CM 4.5 of the rule book. As at 31 December 2014, the Bank had two large exposures that have been communicated to CBB:

Counterparty	Exposure type	Total exposure	Exposure as a % of eligible capital	Capital deduction amount
A	Investment	17,158	16%	1,112
B	Financing	16,779	16%	732

4.3.5 Exposures in highly leveraged counterparties

The Bank has no exposure to highly leverage and other high risk counterparties as per definition provided in the CBB rule book PD 1.3.24.

4.3.6 Residual contractual maturity of the credit portfolio and investment in sukuks

The Bank's policy allows exposures up to a maximum period of 7 years for corporate customers and 25 years for retail customers with any exceptions to be approved by the Board of directors. The Bank constantly monitors the residual maturity profile of its assets to ensure that any mismatch with the maturity of its liabilities is kept within acceptable limits. The contractual residual maturity profile by type of financing contract of the Bank's credit portfolio and investment in sukuks is given in the table below:

Maturity Scale	< 1 M	1 - 3 M	3 - 6 M	6M - 1Y	1 - 3Y	3 - 5Y	5 - 10Y	10 - 20Y	Over 20Y	Total
Credit portfolio:										
Murabaha	3,975	38,940	13,855	16,833	44,951	69,012	43,929	-	-	231,495
Musharaka	-	954	661	3,503	27,762	3,949	-	-	-	36,829
Mudharaba	-	-	-	-	-	-	-	512	-	512
Wakala	3,222	5,573	8,683	-	913	16,498	-	-	-	34,889
Istisna	-	-	-	-	218	-	-	-	-	218
Ijarah	-	-	-	531	829	428	9,786	25,068	7,137	43,779
Total	7,197	45,467	23,199	20,867	74,673	89,887	53,715	25,580	7,137	347,722
Investment in Sukuk	35,978	-	-	-	-	-	-	-	-	35,978
Grand Total	43,175	45,467	23,199	20,867	74,673	89,887	53,715	25,580	7,137	383,700

The Board approved internal cap for real estate exposure at 40% of total assets. The Bank's real estate exposure as of 31 December 2014 and 2013 are within the policy limit.

4.4 Equity risk in banking book

The Bank has certain equity investments classified in the banking book and are subject to credit risk weighting under the capital adequacy framework. For regulatory capital computation purposes, the Bank's equity investments in the banking book include quoted/unquoted equity investments, and investments in associates being non-financial entities.

Please refer to notes 2 and 21 of the consolidated financial statements for policies covering the accounting of equity holdings, including the accounting policies and valuation methodologies used, key assumptions and practices affecting valuation.

4 CREDIT RISK (CONTINUED)

4.4 Equity risk in banking book (continued)

The RMD works alongside the Investment Department at all stages of the deal cycle, from pre-investment due diligence to exit, and provides an independent review of every transaction. An impairment assessment of investments takes place every quarter with inputs from the Investment department and RMD. Quarterly updates of investments are reviewed by the Board of Directors and are submitted to the CBB.

The Bank's equity investments are predominantly in its own products, which includes private equity and infrastructure development projects. The intent of such investments is a later stage exit along with the investors, by means of strategic sell outs at the project level or through initial public offerings. The Bank also has a strategic investment portfolio which is aligned with the long term investment objectives of the Bank.

Information on equity investments

Privately held	60,945
Dividend income	271
Realised gain during the year	171

The following are the categories under which equity investments are included in the capital adequacy computations as per the requirements of the CBB rules:

Equity investments in banking book	Gross exposure		Risk weighted exposure		Capital charge (@12%)	
	Self-financed	IAH	Self-financed	IAH	Self-financed	IAH
Unquoted equity investment	26,719	-	40,079	-	4,810	-
Real estate investment	34,226	-	68,452	-	8,214	-
Total	60,945	-	108,531	-	13,024	-

4.5 Risk grading of exposures

The Bank has an internal risk grading system for credit exposures based on a 10 point scale in which grades 8 through 10 are non-performing with grades 9 and 10 classified as impaired exposures. Each counterparty credit exposure is assigned a risk grade based on several quantitative and qualitative factors, including financial strength, past record and availability of collateral security. The grading is done at the time of assuming an exposure and on each renewal of the same. The grading sheets are prepared by the Business Department and reviewed by the RMD. Grades are continuously monitored by the Bank's Credit Administration Unit within RMD and exposures are downgraded as and when the quality of the exposure is found to have deteriorated, based on clear criteria laid out in the Bank's credit policy. Further, the grading for corporate customers is also subject to review at least on an annual basis. Movement of grades for credit exposures is reported quarterly to the Board.

For exposures or potential exposures on banks and financial institutions, the Bank has established internal ratings with a six point scale from A to F, in descending order of creditworthiness. These ratings are derived on the basis of the external credit ratings provided by Moody's, Standard & Poor (S&P), Capital Intelligence (CI) & Fitch. When the ratings of S&P and/or Moody's are available, those ratings will be used. In case of differences in ratings from these agencies, the more conservative rating is used for classification. The ratings of these agencies have been mapped to internal categories as follows:

External rating agencies	Internal Rating					
	A	B	C	D	E	F
S & P	>= AA-	>=A-	>=BBB-	>=B-	Below B-	Unrated
Moody's	>=aa3	>=A3	>=Baa3	>=B3	C & D	Unrated
CI	>= AA-	>=A-	>=BBB-	>=B-	C & D	Unrated
Fitch	>= AA-	>=A-	>=BBB-	>=B-	Below B-	Unrated

Please refer to note 31 of the consolidated financial statements for the year ended 31 December 2014, for details of the grading profile of credit exposures of the Bank.

RISK MANAGEMENT DISCLOSURES

BD 000's

4 CREDIT RISK (CONTINUED)

4.6 Past dues, impaired accounts, provisions

Customers may occasionally fail to meet their obligations to the Bank on due dates. Any amount not paid when due is classified as past due and the Bank initiates focused recovery efforts on such accounts. Any account which is past due for 30 days or more is classified as "Watch List"/ Grade 7 and clearly defined procedures are in place for follow-up and monitoring of such accounts.

However, if the account remains past due for a continuous period of 90 days it is considered as non-performing and classified as Grade 8. The Bank conducts a comprehensive review of all such accounts on a quarterly basis and where provisions are necessary; those exposures are classified as impaired (Grade 9/10). Provisions are created through income statement where necessary. Such provisions are made on the basis of expected shortfall in present value of projected future cash flows from the assets / securities and the estimates of such cash flows are done on a conservative basis.

On each year-end, the Bank reviews all financial assets classified at fair value through equity for any objective evidence that the financial assets are impaired. In case of any such evidence, the asset is revalued at lower of cost of acquisition and its estimated recoverable amount and a provision is created for the difference amount through the income statement.

For a detailed policy on impairment of financial assets, please refer to note 2 (l) of the consolidated financial statements for the year ended 31 December 2014.

For the quantitative disclosures relating to exposures which were past due or impaired as of 31 December 2014, please refer to note 31 of the consolidated financial statement for the year ended 31 December 2014.

During the year 2014, the Bank has undertaken a detailed assessment of its credit portfolio and has considered specific impairment allowances where necessary. In addition, the Bank has maintained a collective provision at a certain percentage of unimpaired assets based on the internal risk grades assigned to counterparties. The total collective provision thus maintained works out to approximately 1.08% of its financing assets, assets acquired for leasing, and lease rentals receivable. This practice is in line with the CBB requirements and the industry best practice in Bahrain.

For movement in provisions on financing assets and investment securities, please refer to notes 5 and 6, respectively, of the consolidated financial statement for the year ended 31 December 2014.

4.6.1 Geographical and sector-wise break-up of impairment allowances and impaired / past due accounts (financing facilities)

	GCC Countries	Europe	Asia	Total
Impaired:				
3 months to 1 year	9,177	-	-	9,177
1 year to 3 years	6,351	-	-	6,351
More than 3 years	5,007	-	-	5,007
	20,535	-	-	20,535
Less: specific impairment allowance:				
At 1 January 2014	12,529	-	-	12,529
Charge during the year	129	-	-	129
Write back during the year	-	-	-	-
Write off during the year	(2,466)	-	-	(2,466)
At 31 December 2014	10,192	-	-	10,192
Carrying amount	10,343	-	-	10,343
Past due but not impaired, including substandard:				
Up to 3 months	33,707	-	-	33,707
3 months to 1 year	1,888	-	-	1,888
More than 1 year	190	-	-	190
	35,785	-	-	35,785
Collective impairment allowance *	3,543	278	98	3,919

* Collective impairment allowance is allocated based on exposure excluding impaired exposures on which specific provision is maintained.

4 CREDIT RISK (CONTINUED)

4.6 Past dues, impaired accounts, provisions (continued)

4.6.1 Geographical and sector-wise break-up of impairment allowances and impaired / past due accounts (Continued)

	Banks and financial institutions	Real estate	Others	Total
Impaired:				
3 months to 1 year	1,278	6,212	1,687	9,177
1 year to 3 years	408	5,000	943	6,351
More than 3 years	-	1,004	4,003	5,007
	1,686	12,216	6,633	20,535
Less: specific impairment allowance:				
At 1 January 2013	1,454	6,145	4,930	12,529
Charge during the year	(279)	117	291	129
Write back during the year	-	-	-	-
Write off during the year	-	(2,466)	-	(2,466)
At 31 December 2013	1,175	3,796	5,221	10,192
Carrying amount	511	8,420	1,412	10,343
Past due but not impaired, including substandard:				
Up to 3 months	-	18,536	15,171	33,707
3 months to 1 year	-	653	1,235	1,888
More than 1 year	-	190	-	190
	-	19,379	16,406	35,785
Collective impairment allowance *	480	1,742	1,697	3,919

* Collective impairment allowance is allocated based on exposure excluding impaired exposures on which specific provision is maintained.

4.7 Renegotiated facilities

For disclosure of renegotiated loans, please refer to note 31 of the consolidated financial statements for the year ended 31 December 2014.

4.8 Legal action and write-off of exposures

The Bank has policy for initiation and prosecution of legal action when all amicable avenues for settlement of dues from a customer have been exhausted. As of 31 December 2014, the Bank was involved in eleven litigations for recovery of dues from clients amounting to BD 51 thousand. In addition, there were claims by five of the clients against the Bank amounting to BD 84 thousand in relation to restricted investment accounts and customer accounts.

The Bank has a policy that permits write-off of exposures when there is no possibility of recovery of the dues through legal and other means.

4.9 Penalties for delayed payments

In cases where customers delay the payment of dues to the Bank, the Bank has the right to collect penalties, subject to the provisions of the agreement between the customer and the Bank. The Bank recovers such penalties from customers when the amounts are significant. As per policy, such penalties are maintained in a separate account and used for charity purposes approved by the Bank's Shari'a Board.

RISK MANAGEMENT DISCLOSURES

BD 000's

4 CREDIT RISK (CONTINUED)

4.9 Penalties for delayed payments (continued)

The Bank has a policy of creating a contribution for Charity and Zakah fund for any non-Islamic income earned. During the year ended 31 December 2014, an amount of BD 89 thousand was thus transferred to Charity and Zakah fund.

For quantitative disclosures, please refer to consolidated statement of sources and uses of charity and Zakah fund in the consolidated financial statements for the year ended 31 December 2014.

4.10 Credit risk mitigation

The Bank uses a variety of tools to mitigate its credit risk, the primary one being that of securing the exposure by suitable collateral security. While existence of collateral security is not a policy precondition for financing, in practice a large part of existing exposures are at least partially supported by collateralised security. The Bank has clear policies on the type of assets that can be accepted as collateral security and the mode of valuation of these assets. In general, all assets accepted as collateral are valued at least once in a year. The legal validity and enforceability of the documents used for creating these collaterals have been established by external legal experts.

The position of collateral cover for all credit exposures categorised on the basis of the type of security as on 31 December 2014 is given in the table below:

Collateral Type	Murabaha	Musharaka	Mudharaba	Wakala	Istisna	Ijara	Value of collateral ¹	Gross Exposure ²	% of cover	% of Total
Real estate	136,168	75,123	314	6,126	2,688	81,129	301,548	170,925	176%	79%
Listed securities	542	-	-	-	-	-	542	255	213%	0%
Unlisted securities	11,136	-	-	-	-	-	11,136	9,418	118%	3%
Bank guarantee	32,542	-	-	-	-	-	32,542	23,891	136%	9%
Cash collateral	29,756	-	-	597	-	-	30,353	48,397	63%	8%
Others	-	-	-	-	-	-	-	105,165	0%	0%
Unsecured	4,589	-	-	-	-	-	4,589	3,782	121%	1%
Total	214,733	75,123	314	6,723	2,688	81,129	380,710	361,833	105%	100%

¹ Represents collateral values based on the last valuation carried out based on the Bank's valuation policy including collaterals which exceed the book value of facility.

² The amounts are gross of collective impairment allowance of BD 3,919 thousand and specific impairment allowance of BD 10,192 thousand.

Real estate properties are reckoned at values certified by qualified valuers. Other physical assets like machinery are valued at book value, invoice value or as certified by an outside expert. Listed securities are valued at market price while un-listed ones are carried at cost less impairment. The Bank has an approved panel of valuers for real estate property. Valuation exercise is supervised by RMD, independent of the business units.

Facilities are also often secured by personal/ corporate guarantees, joint ownership of vehicles, assignment of contract proceeds, assignment of insurance policies, etc. However under the Bank's credit policy these are not treated as tangible securities and the value of such guarantees/ assignments, though significant in many cases, are taken as nil for the purpose of the above analysis.

Assets financed under Ijara Muntahia Bittamleek are considered at par with physical collateral and included under Real Estate or Others in the above calculations.

The declared value of exposures in all cases is the gross exposure before any provisions. The Bank does not carry out any on or off balance sheet netting for the securities held. The Bank has not claimed any capital relief for Credit Risk Mitigation under Section CA 4.7 of the Capital Adequacy Module of CBB rule book and hence all exposures are risk weighted at their gross values for the purpose of computation of capital adequacy ratio.

The Bank has a policy of disposal of asset held as collateral not readily convertible into cash, after completion of necessary legal formalities. During the year ended 31 December 2014, the Bank repossessed and sold certain vehicles to recover an amount of BD 24 thousand. Further, in 2014, the Bank enforced collaterals of three non-performing financing facilities by transfer of ownership of three land plots and thirteen villas in the name of the Bank (refer note 9 of the financial statements).

4 CREDIT RISK (CONTINUED)

4.11 Regulatory capital requirements by type of financing contracts

Financing contract	Exposure		Credit Risk Weighted Assets		Capital Requirement @ 12%	
	Self-financed	IAH	Self-financed	IAH	Self-financed	IAH
Murabaha	69,610	160,805	73,705	48,055	8,845	5,767
Ijara assets (including lease rentals receivable)	43,779	-	33,078	-	3,969	-
Musharaka	36,545	-	38,446	-	4,614	-
Mudharaba	512	-	512	-	61	-
Wakala	-	36,256	-	10,877	-	1,305
Istisna	-	215	-	65	-	8
Total	150,446	197,276	145,741	58,997	17,489	7,080

5 MARKET RISK

5.1 Market risk management

Market risk is the risk that changes in market prices, such as foreign exchange rates, profit rates, equity prices, and commodity prices will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

CBB rules require that the Bank separates its exposure to market risk between trading and non-trading portfolios. The Bank has no trading positions in equity or commodities and the main source of market risk for the Bank is its foreign exchange exposure and sukuk exposure, although this is quite limited. There is also an extent of profit rate risk arising out of mismatches in its asset liability structure. The Bank has well-defined policies approved by the Board with clear risk limits and thresholds to effectively manage its market risk.

In 2012, the Bank had commenced trading in Sukuks on a very selective basis. To begin with trading will be restricted to listed and traded sukuks issued by sovereign/ quasi sovereign entities or by other GCC issuers with an investment grade rating from Moody's or S&P. The size of the trading book at the end of the year was BD 5,359 thousand.

The sukuk risk is monitored by marking to market of the portfolio on a daily basis. The size of the portfolio and more importantly the number of instruments is too small for any statistical model to be reliable.

The Bank has formulated a comprehensive Sukuk Trading and Sukuk Fund Participation policy duly approved by the Board of Directors. The primary objective being trading in Sukuks and participation in Sukuk funds and or other fixed income Shari'a compliant structured products as a part of Treasury Business. The policy sets clear guidelines for Sukuk Trading and participation in Sukuk funds, limits, Target market, sectors, country, tenor, Stop loss triggers and actions and reporting. The portfolio is monitored on a mark to mark basis and reported to the ALCO.

In 2014, the Board of Directors have approved a comprehensive policy for Investments in listed Equity through managed 3rd party funds or discretionary portfolio with the aim of maximizing return within certain set parameters and limits. Such investments are governed by the overall risk appetite of the bank, regions, acceptable returns, target markets, sectors, stop loss limits and triggers.

The ALCO committee reviews these investments as part of the overall monitoring of cash management and treasury and investment activities of the Bank.

These sukuks are measured at fair value for the purpose of financial reporting and for trading on a mark to market basis and likewise for investments in listed equity portfolio through managed funds or discretionary portfolio.

For the purpose of computing capital charge for market risk for regulatory reporting, these sukuks form part of trading books and are subject to specific market risk (based on external ratings) and general market risks (based on residual maturity).

Details on market risk management, net exposures and sensitivities are given as part of note 31 of the consolidated financial statements for the year ended 31 December 2014.

5.2 Regulatory capital allocation against market rate risk

The table below shows the market risk position for each category of the market risk as at 31 December 2014 along with the maximum and minimum values during the period:

RISK MANAGEMENT DISCLOSURES

BD 000's

5 MARKET RISK (CONTINUED)

5.2 Regulatory capital allocation against market rate risk (continued)

	As at 31 December	Max	Min
Equity position risk	-	-	-
Market risk on trading positions in sukuk *	166	191	166
Foreign exchange risk	1,153	1,153	1,117
Commodity risk	-	-	-
Total (A)	1,319	1,344	1,283
Risk Weighted Assets (A x 12.5)	16,488	16,800	16,038
Capital requirement @ 12%	1,979	2,016	1,925

* represents 30% of the exposure since these sukuk investments are allocated from IAH pool.

6 OPERATIONAL RISK

6.1 Operational risk management

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, systems, and/ or from external events which includes but is not limited to, legal risk and Shari'a compliance risk. Operational risk is an inherent part of normal business operations. Whilst operational risk cannot be eliminated entirely, the Bank endeavors to minimise it by ensuring that a strong control infrastructure is in place throughout the organisation. Various procedures and processes used to manage operational risk including effective staff training, appropriate controls to safeguard assets and records, regular reconciliation of accounts and transactions, close monitoring of risk limits, segregation of duties, and financial management and reporting.

Details on operational risk management are given as part of note 31 of the consolidated financial statements for the year ended 31 December 2014.

RMD monitors all operational processes to ensure that the Board directives are fully implemented and deviations are reported if any to the Senior Management and to the Board. The department has specialised personnel engaged in this process. The Bank has implemented an Operational Risk Management System which monitors Key Risk Indicators and controls across all major areas of operation and generates appropriate triggers as and when pre-defined risk events occur (through breach of triggers set) and also generates periodical update report to the Board and to the Management. In addition, the Bank's policy dictates that the operational functions of booking, recording and monitoring of transactions are carried out by staff that are independent of the individuals initiating the transactions.

The Bank's operational risk management framework includes components such as Key Risk Indicators ("KRI's"), operational loss data and Risk & Control Self-Assessment across the Bank. These are monitored periodically which helps in quickly detecting and correcting deficiencies in processes and procedures. The collected data is maintained to create a loss database which could be the starting point for a more advanced operational risk measurement approach in future.

6.2 Litigation

As of the reporting date, the Bank has no material legal contingencies including pending legal actions except as reported in Para 4.8 above. The Bank has a dedicated legal team which provides legal advice and services to all business units of the Bank.

6.3 Shari'a compliance

The Shari'a Supervisory Board ("SSB") is entrusted with the duty of directing, reviewing and supervising the activities of the Bank in order to ensure that they are in compliance with the rules and principles of Islamic Shari'a. The Bank also has a dedicated internal Shari'a reviewer, who performs an ongoing review of the compliance with the fatwas and rulings of the SSB on products and processes and also reviews compliance with the requirements of the Shari'a standards prescribed by AAOIFI. The SSB reviews and approves all products and services before launching and offering to the customers and also conducts periodic reviews of the transactions of the Bank. An annual audit report is issued by the SSB confirming the Bank's compliance with Shari'a rules and principles.

6.4 Regulatory capital allocation against operational risk

The Bank uses the Basic Indicator Approach in calculating its regulatory capital requirement for operational risk.

The risk weighted assets and capital requirement for operational risk as at 31 December 2014 is as given below:

Average gross income for 3 years (A)	17,418
Operational Risk Weighted Assets (B) = A x 15% x 12.5	32,659
Capital requirement = B x 12%	3,919

7 OTHER RISKS

7.1 Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting its financial obligations on account of a maturity mismatch between assets and liabilities. The Bank's approach to manage liquidity is to ensure that it will always have sufficient funds to meet its liabilities when due without incurring unacceptable losses or risking damage to the Bank's reputation.

The Bank has a liquidity risk policy in place, which describes the roles and responsibilities of the Asset Liability Management Committee ("ALCO"), Treasury and other concerned departments in management of liquidity. It also stipulates various liquidity ratios to be maintained by the bank, as well as gap limits under each time bucket of the maturity ladder. It is the Bank's policy to keep adequate level of high quality liquid assets such as inter-bank placements and sukuks to ensure that funds are available to meet maturing Mudharaba deposits and other liabilities, as and when they fall due. The day to day management of liquidity risk is the responsibility of the Treasury Department, which monitors the sources and maturities of assets and liabilities closely, and ensures that limits stipulated by the ALCO are complied with. RMD and Financial Control Department ("FCD") monitors the liquidity position and any violations are reported to ALCO, ERM and the Board of Directors.

For maturity profile of assets and liabilities, please refer to note 28 of the consolidated financial statements for the year ended 31 December 2014.

The following are the key liquidity ratios which reflect the liquidity position of the Bank:

	Figures in %				
	2014	2013	2012	2011	2010
Interbank assets to interbank liabilities	176.87	222.39	95.70	189.43	116.91
Liquid assets to total assets	25.23	27.80	19.81	27.06	25.00
Liquid assets to total deposits	34.69	38.46	33.33	43.65	45.94
Net liquid assets to total deposits	23.03	27.50	9.25	27.27	17.05

7.2 Profit rate risk in the banking book

The other principal risk to which the banking book is exposed, is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market profit rates. Profit rate risk is managed principally through monitoring profit rate gaps and by having pre-approved limits for re-pricing bands. The ALCO is the monitoring body for compliance with these limits and is assisted by the RMD in its day-to-day monitoring activities.

The management of profit rate risk against profit rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard and non-standard profit rate scenarios. Standard scenarios that are considered on a monthly basis include a 100 basis points (bps) parallel fall or rise across all yield curves and a 50 bps rise or fall of all yield curves. An analysis of the Bank's sensitivity to an increase or decrease in market profit rates has been disclosed in note 31 of the consolidated financial statements for the year ended 31 December 2014.

7.3 Counterparty credit risk

Counterparty credit risk is the risk that a counterparty to a contract in the profit rate, foreign exchange, equity and credit markets defaults prior to maturity of the contract. The Bank does not engage in proprietary trading of equity, foreign exchange or its derivatives. However, the Bank enters into Shari'a compliant foreign exchange risk/ profit rate risk transactions to hedge its risks arising out of mismatch in its asset liability portfolios. Clear policies for such transactions are in place. For other credit market transactions (primarily interbank placements), the Bank has established a matrix of counterparty limits based on external credit rating of such counterparties. Such limits are constantly monitored by the RMD. As at 31 December 2014, the Bank did not have any open position in foreign currency risk management instruments.

7.4 Concentration risk

Concentration risks arises when a number of obligors, counterparties or investees are engaged in similar business activities or activities in the same geographic region or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Accordingly, such concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or region. To manage this risk, the Bank has established exposure limits to various geographic regions and industry sectors. Such limits are monitored by the RMD and deviations, if any, are reported to the Board on quarterly basis. As at 31 December 2014, there has been no violation of the Board approved limits under any head. For break-up of exposure geography and industry/ sector wise, please refer to notes 4.3.1 and 4.3.2 above.

7.5 Reputational risk

Reputation risk is the risk that negative perception regarding the Bank's business practices or internal controls, whether true or not, will cause a decline in the Bank's investor base that could have an adverse impact on liquidity or capital of the Bank. This may also lead to litigation against the bank which apart from avoidable legal expenses will also damage Bank's credibility which in turn will adversely affect business growth and profitability. Being an Islamic Bank, reputation is an important asset and one of the issues that could affect the Bank's reputation is the inability to exit from investments, lower than expected returns on investments, growth of non-performing asset portfolio and poor communication to investors. The Bank has a well-developed and coherently implemented communication strategy to cover such contingencies. The Bank also allocates additional capital for such risks under its ICAAP.

RISK MANAGEMENT DISCLOSURES

7 OTHER RISKS (CONTINUED)

7.6 Displaced commercial risk

Displaced Commercial Risk refers to the market pressure to pay returns that exceeds the rate that has been earned on the assets financed by equity of investment account holders. This can be due to the return on such assets being lower than that of competitors. The Bank has adequate policies and procedures in place to identify, monitor and address all potential risks that may arise from such activities. Please refer to the section on IAH for further details.

7.7 Other risks

Other risks include strategic risk, fiduciary risks, and regulatory risks, etc. which are inherent in all business and are not easily measurable or quantifiable. The Bank's Board has overall responsibility for approving and reviewing the risk strategies and amendments to the risk policies. The Bank senior management is responsible for implementing the risk strategy approved by the Board. The management also ensures that internal systems of corporate governance and regulatory compliance for management of fiduciary and reputational risks are robust and effective. The Bank also allocates additional capital for such risks under its ICAAP.

8 PRODUCT DISCLOSURES

8.1 Product descriptions & consumer awareness

The Bank has a disclosure policy which applies to all modes of communication to the public including written, oral and electronic communications. These disclosures are made on a timely basis in a manner required by applicable local and regulatory requirements.

The Bank offers a comprehensive mix of Shari'a compliant commercial and investment banking products. This include, apart from traditional financing products, a range of innovative structured investment products like funds, repackaged investments and restricted Mudharaba's. The Investment Department of the Bank has expertise in creating innovative high-end and value added products offering a wide range of structures, expected returns, tenors and risk profiles.

Proposal for any new product is initiated by individual business lines within the Bank. The Executive Risk Management Committee ("ERMC") of the Bank reviews such proposal to ensure that the new product/ business are in line with the Bank's business and risk strategy. All new products will need the approval of the Board of Directors and the Shari'a Supervisory Board of the Bank.

Information on new products or any change in existing products will be placed on the Bank's website www.khcbonline.com and / or published in the media. Product details are also shared with customers and the general public through brochures and / or, advertisements.

8.2 Complaint handling

The Bank takes disputes and complaints from all customers very seriously. These have the potential for a breakdown in relationships and can adversely affect the Bank's reputation. Left unattended these can also lead to litigation and possible censure by the regulatory authorities. The Bank has a comprehensive policy on handling of external complaints, approved by the Board. All employees of the Bank are aware of and abide by this policy.

The Bank has a designated an officer for handling of all external complaints and his contact details are displayed on the website and also at the Branch and in all printed publicity materials. Complaints are normally investigated by persons not directly related to the subject matter of the complaint. The Bank endeavors to address all complaints within five working days. Wherever this is not possible, the customer is contacted directly and a time frame for rectification of his complaint is advised. A periodical report on status of complaints is also submitted to the Board.

8.3 Equity of investment account holders (IAH's)

The Bank accepts funds in the form of Mudharaba from small investors and high net worth individuals. Equity of investment account holders ("IAH") represents funds offered by customers to the Bank to be invested in a Shari'a compliant manner, at the Bank's discretion as Mudharib. All IAH accounts are on profit sharing basis, but the Bank does not guarantee any particular level of return. Any loss arising from the investment will be borne by the customer except in the case of the Bank's negligence. The Bank charges a Mudharib fee as its share of profit.

The Bank accepts IAH funds in Bahraini Dinar, US Dollar and other international and GCC currencies for maturity periods ranging from 1 month to 24 months. The Bank completes its full range of KYC due diligence prior to accepting any investment. The customer also signs a written agreement covering all terms and conditions of the investment including tenor, basis of profit allocation, early withdrawal, etc.

Since 2009, the Bank offers a savings account product called "Al-Waffer" which entitles the investors to certain prizes in cash and in kind, decided based on a raffle draws held on monthly, quarterly and annual basis apart from the normal share of profits declared and distributed after reducing the Mudharib fees.

IAH is a significant funding source for the Bank and the returns offered to investors are in line with the market. However, any shortfall in yield on the investments made out of these funds exposes the Bank to displaced commercial risk. The Bank regularly monitors rate of return offered by competitors to evaluate the expectations of its IAH's. Bank's policy also provides for whole or partial waiver of the Mudharib share of income from investments due to it, to provide a reasonable return to its investors.

8 PRODUCT DISCLOSURES (CONTINUED)

8.3 Equity of investment account holders (IAH's) (continued)

The Bank comingles its own funds and IAH funds and these are invested together. The Bank has identified two pools of assets where the IAH funds are invested and the income from which is allocated to such accounts. One pool is short term in nature to meet IAH short term investment requirements. The other pool is long term in nature to meet their long term investment requirements. Out of the gross income the investor's share is computed after deducting the Mudharib share. The profit allocation schedule signed by the customer prior to investment contains the scheme of allocation of the Mudharib share. Administrative expenses incurred for management of the funds are borne directly by the Bank and are not charged separately to investment accounts. Equity of IAH's are carried at their book value.

Subject to the provisions thereof, deposits held with the Bank are covered by the Deposit Protection Scheme established by the CBB regulation concerning the establishment of a Deposit Protection Scheme and a Deposit Protection Board.

The details of income distribution to IAH holders for the last five years are given below:

	2014	2013	2012	2011	2010
Allocated income to IAH	12,843	13,315	9,923	9,022	8,254
Distributed profit	8,841	8,719	6,297	6,629	5,785
Mudharib fees *	4,002	4,596	3,626	2,393	2,469
As at 31 December					
IAH ¹	336,010	260,609	193,245	183,915	192,439
Profit Equalisation Reserve (PER)	-	-	-	-	169
Investment Risk Reserve (IRR)	-	-	-	-	-
Profit Equalisation Reserve-to-IAH (%)	-	-	-	-	0.09%
Investment Risk Reserve-to-IAH (%)	-	-	-	-	-

¹ Represents average balance.

* Includes contribution towards deposit protection scheme.

Ratio of profit distributed to PSIA by type of IAH (based on tenor):

Mudaraba Tenor	Profit distribution amount in BD					Ratio of profit paid as a percentage of total				
	2014	2013	2012	2011	2010	2014	2013	2012	2011	2010
1 Month ¹	1,304	1,488	1,629	1,824	3,107	14.7	17.1	25.9	27.5	53.7
3 Months	380	680	655	1,489	1,843	4.3	7.8	10.4	22.5	31.9
6 Months	1,455	1,100	474	764	641	16.5	12.6	7.5	11.5	11.1
12 Months	4,179	3,606	2,998	2,014	1,452	47.3	41.4	47.6	30.4	25.1
18 Months	1	-	-	-	-	-	-	-	-	-
24 Months	75	228	30	-	-	0.8	2.6	0.5	-	-
VIP	1,447	1,617	511	707	729	16.4	18.5	8.1	10.7	12.6
PER and IRR expenses	-	-	-	(169)	(1,987)	-	-	-	(2.6)	(34.4)
Total	8,841	8,719	6,297	6,629	5,785	100.0	100.0	100.0	100.0	100.0

¹ Includes saving account, Al-Wafer account and Call Mudharaba accounts.

RISK MANAGEMENT DISCLOSURES

BD 000's

8 PRODUCT DISCLOSURES (CONTINUED)

8.3 Equity of investment account holders (IAH's) (continued)

Distribution of profits by type of IAH products:

Year	Avg. profit earned from IAH assets (%age of asset)	PER set aside as a %age of IAH assets	IRR set aside as a %age of IAH assets	Mudarib fees as a %age of IAH assets	Profit paid as a %age of IAH assets
2014	3.82	-	-	1.19	2.63
2013	5.11	-	-	1.76	3.35
2012	5.13	-	-	1.88	3.26
2011	4.99	-	-	1.22	3.69
2010	4.03	(0.54)	(0.49)	1.28	4.04

Following are the average profit rates declared and distributed to the investors by the Bank:

	2014	2013	2012	2011	2010
1 Month Mudaraba ¹	1.15%	1.12%	2.25%	2.51%	3.66%
3 Months Mudaraba	2.19%	2.98%	3.08%	4.25%	4.13%
6 Months Mudaraba	3.08%	3.64%	3.55%	4.52%	3.38%
12 Months Mudaraba	3.39%	4.27%	4.46%	5.01%	4.94%
18 Months Mudaraba	3.30%	-	-	-	-
24 Months Mudaraba	4.92%	5.07%	5.07%	-	-
VIP Mudaraba	3.49%	4.09%	2.79%	3.67%	4.35%

¹ Includes saving account, Al-Wafer account and Call Mudharaba accounts.

The Bank refers to the group of commercial Islamic banks incorporated in the Kingdom of Bahrain so as to benchmark the rate of return on IAH.

IAH account by type of assets:

The following table summarises the movement in type of assets in which the IAH funds are invested and allocated among various type of assets for the year ended 31 December 2014:

Particular	Allocation at 1 January 2014	Movement	Allocation at 31 December 2014	Proportion of total assets (%)
Cash and bank balances	27,836	1,838	29,674	79.4%
Placements with financial institutions	82,745	(6,739)	76,006	100.0%
Financing assets ¹	152,336	44,940	197,276	64.9%
Investment securities - Sukuk	29,132	6,846	35,978	100.0%
Total	292,049	46,885	338,934	

¹ Includes Murabaha, Wakala and Istisna contracts.

8.4 Restricted Investment Accounts (RIA's)

The Bank offers Restricted Investment Accounts ("RIA's") to both small investors and high net worth individuals in the GCC. The Bank structures its RIA products to offer its customers an opportunity to choose from a wide range of returns, maturity periods, sectors, asset classes and risk levels. No RIA product was introduced/ marketed by the Bank in 2014.

All RIA offering documents ("Offering Document") are drafted and issued with input from the Bank's Investment Banking, Shari'a, Financial Control, Legal and Risk Management Departments to ensure that the Investors have sufficient information to make an informed decision after considering all relevant risk factors.

8 PRODUCT DISCLOSURES (CONTINUED)

8.4 Restricted Investment Accounts (RIA's) (continued)

The Board of Directors is responsible for providing clear guidelines for the development, management and risk mitigation of its RIA investments and to ensure that there exist sound management and internal control systems to ensure that the interests of the IAH's are protected at all times. Wherever it is necessary for the Bank to establish Special Purpose Vehicles ("SPV's") for management of the investment, the Board ensures that the management of such SPV's is conducted in a professional and transparent manner by a duly appointed Board.

The Bank is aware of its fiduciary responsibilities in management of the RIA investments and has clear policies on discharge of these responsibilities. The Bank's Policy regarding its fiduciary responsibilities to the RIA investors and their funds, includes the following:

- Ensuring that the investment structure, Offering Documents and the investment itself are fully compliant with Islamic Shari'a principles and the CBB regulations;
- Appropriately advising investors, as part of the RIA Offering Document, of all the relevant and known risk factors and making it clear that the investment risk is to be borne by the investor before accepting the investment funds;
- Completing all necessary legal and financial due diligence on investments undertaken on behalf of the investors with the same level of rigor as the Bank requires for its own investments;
- Ensuring that the funds are invested strictly in accordance with the provisions outlined in the Offering Documents;
- Putting in place suitable resources and systems to manage and administer the investment and any necessary RIA SPV(s) and to proactively manage all risks;
- Preparing and disseminating periodical investment updates to investors on a regular basis during the tenor of the investment;
- Distributing the capital and profits to the investor in a just and equitable manner as Mudarib; and
- In all matters related to the RIA, RIA SPV(s) and the investment, act with the same level of care, good faith and diligence as the Bank would apply in managing its own investments.

Within the Bank, the above mentioned responsibilities and functions are provided, managed and monitored by qualified and experienced professionals from the Investment Banking, Shari'a, Financial Control, Legal, Investment Administration and the Risk Management Departments.

Investment update reports are prepared and disseminated by the Bank to the RIA Investors on a periodic (at least on a half yearly) basis outlining any material contracts/decisions, investment performance, distribution (if any) or exit criteria/information.

RISK MANAGEMENT DISCLOSURES

8 PRODUCT DISCLOSURES (CONTINUED)

8.4 Restricted Investment Accounts (RIA's) (continued)

RIA name	Details	Launch date	Projected returns	Return frequency	Return annualized (%)				
					2014	2013	2012	2011	2010
RIA 1 - Safana	An investment structure designed to participate in the equity interest of Safana Investment WLL. A company established for the purpose of acquiring reclaimed land to subdivide and sell. In 2011, the Bank made an offer to buy back < BD 20,000 of each investors funds in RIA 1 at par. This offer was formalized in a letter to investors dated 25 May 2011. A total of 74 of the 95 RIA 1 investors accepted the offer at a cost of BD 1,220 thousands to the Bank and resulting in a total of 39 investors being fully exited from the RIA. As a result, total investors funds have reduced to BD 8.34 million.	2007	61.78% over product tenor	Bullet payment on maturity	-	-	-	-	-
RIA 4 - Janayen	A restricted investment product designed to invest in growth and income generating real estate assets in the GCC and MENA regions. To date, RIA4 has made distributions and redemptions to depositors amounting to approximately 29.8% of the Depositors' initial capital. These distributions were in the form of yields amounting to ≈ 21.1% plus 8.74% of redeemed capital.	2007	44.33%	Quarterly	-	-	-	-	0.27

8 PRODUCT DISCLOSURES (CONTINUED)

8.4 Restricted Investment Accounts (RIA's) (continued)

RIA name	Details	Launch date	Projected returns	Return frequency	Return annualized (%)				
					2014	2013	2012	2011	2010
RIA 5 - North Gate	A restricted investment product which owns a 6.0% stake in Shaden Real Estate Investment WLL which in turn (through its subsidiaries), holds a parcel of reclaimed land measuring approximately 3.875 million Sq. Meters (located in Al-Hidd, Muharraq). The mixed-use plot will be sold to end users subsequent to the completion of infrastructure works.	2008	90.66% over product tenor	Bullet return at maturity	-	-	-	-	-
RIA 6 - Locata	A Restricted Mudaraba product which entitles the investors beneficial ownership of 25% equity share capital of Locata Corporation Pty Ltd., a company incorporated in Australia. The Company has invented a new and patented wireless radiolocation technology and shall use this funding to scale up its production capacity, sales/marketing channels and further product enhancement capabilities. During the year, 479 shares were bought back from investors.	2009	110.54% over product tenor	Bullet return at maturity	-	-	-	-	-

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES

9.1 Corporate governance structure

The Bank is governed by the Commercial Companies Law No. 21 of 2001 (the "Companies Law"), the Kingdom of Bahrain Corporate Governance Code (the "CGC"), volume 2 of the Rulebook of the CBB (and in particular the High-Level Controls ("HC Module")), and the Bahrain Stock Exchange Law of 1987 (collectively, the "Regulations").

The Bank acknowledges its responsibility to all of its stakeholders and is committed to the highest standards of corporate governance. The Bank believes good corporate governance enhances stakeholder value and provides an appropriate guidance to the Board, its committees, and the Bank's executive management to carry out their duties in the best interest of the Bank and its stakeholders. The Bank maintains the highest levels of transparency, accountability and good management through the adoption and monitoring of corporate strategies, goals and policies to comply with its regulatory and ethical responsibilities.

The Bank has adopted the CGC which was effective from January 2011. The corporate governance policies of the Bank are aligned with the requirements of HC Module of the CBB Rulebook which was introduced in October 2010 (built on the provisions of the CGC).

9.2 Board of directors

As at 31 December 2014, the Board of the Bank comprise nine members. Members of the Board were elected for a three year renewable term during the Annual General Meeting ("AGM") meeting held on March 2014. The current composition of the Board complies with the requirements of the Regulations, except for certain requirements stated in paragraph 9.15 below.

RISK MANAGEMENT DISCLOSURES

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.2 Board of directors (continued)

The Board Nominations, Remunerations and Governance Committee (“BNRGC”) reviews the skills and qualifications required of directors on periodic basis for potential nominee director. A nominee director may be elected by the shareholders upon receiving majority of votes during the election process. Positions at the Board are filled in compliance with the Bank’s Articles of Association and the Commercial Companies Law. A Director’s membership to the Board shall terminate in the event that, amongst other things, the Director is convicted of an offence of dishonor or breach of trust or is declared bankrupt.

The Chairman of the Board of Directors is charged with regular supervision and assessment of executive management and is responsible for leading the Board, ensuring its effectiveness, monitoring the performance of the CEO and maintaining a dialogue with the Bank’s stakeholders. The Board has constituted certain committees with specific delegated authorities to oversee and guide the management in specific areas of the Bank’s operations and decision-making. The Board, either directly or through its various committees, will oversee the management of the Bank.

The Board has formalized the division of work responsibilities between the Board and the Bank’s management. Working in consultation with the Bank’s management team, the Board provides oversight for the overall management of the Bank’s business. The Board reviews and approves the corporate strategy for the Bank and has overall responsibility for risk management, financial reporting and corporate governance issues. Matters that specifically require Board approval include, amongst other things, the financial statements and the acquisition and disposal of companies. The Board also ensures that the Bank upholds the Bank’s core values including the values set out in the Bank’s internal policies.

The Board Audit and Risk Management Committee (“BARMC”) in addition to the functions of control, ensures that all policies prescribed are reviewed and updated on annual basis. The Risk management department in conjunction with the Internal Audit and Control unit ensures the policies and procedures are updated and adhered to under the oversight of the related management committees. The Board is also responsible for approving any related party transaction as per the Bank’s authority matrix. Related party transactions concerning a Board member should be minimally approved by the Board Investment and Credit Committee (“BICC”). In addition, any material transaction defined by the Bank (10% of the Banks’ capital) should be approved by the Board. The preparation of the consolidated financial statements of the Bank and the Group’s undertaking to operate in accordance with Islamic Sharia rules and principles is the responsibility of the Board of Directors. The duties, functions, and responsibilities are detailed in the Bank’s Corporate Governance Framework.

Members of the Board have access to the Bank’s management at all times. The CEO together with the Bank’s senior management monitors the Bank’s performance against pre-set corporate objectives and manages the Bank’s day-to-day affairs based upon the policies, objectives, strategies and guidelines lay down and approved by the Board from time to time.

The Board of Directors of the Bank comprises of Executive and Non-Executive Directors. The Board has three independent members (out of a total of nine Directors). This is to ensure compliance with the CGC requirement that requires at least one third of the Bank’s Board to comprise independent and non-executive Directors.

Upon appointment, each Director is provided with a comprehensive, formal and tailored induction which includes, amongst other things, a review of the Board’s role and duties and the relevant Director’s roles and duties to the Bank; meetings with the bank’s senior management; visits to the Bank’s branches and other sites; presentations to explain the Bank’s strategic plans and significant financial, accounting, risk and legal issues and compliance programs; and meetings with internal and external auditors and legal counsel. In accordance with paragraph 1.9.1 of the HC module of CBB Rulebook, the Board and its committees are also individually evaluated and assessed for their performance effectiveness. The Board has conducted an evaluation of its performance and the performance of each committee and each individual director during the year 2014.

Each independent Director of the Bank is a professional in their field and possesses a background in the financial and banking field.

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.2 Board of directors (continued)

The names, title, and other positions held by the Board of Directors are set out below:

Dr. Ahmed Khalil Al-Mutawa

Chairman

Experience:

- Director since June 2012 (Non-Independent and Non-Executive).
- Over 17 years of experience in economics and financial sector.
- Nominated by Gulf Finance House BSC.
- Chairman of Gulf Finance House BSC.
- Chief Executive Officer of Khalifa Fund for Enterprise Development.
- Board Member of Dubai University College - UAE.
- Board Member of Dunia Finance - UAE.
- Board Member of Summit Bank - Pakistan.

Qualification:

- Ph.D. in Economics from Georgetown University - USA.
- Master in Economics from University of North Carolina - USA.
- Bachelor in Economics from University of Cairo - Egypt.

Abdulla Abdulkarim Showaiter

Board Member

Experience:

- Director since February 2008 (Independent and Non-Executive).
- Over 36 years of experience in the banking industry.
- Deputy CEO, Wholesale Banking, Emirates Islamic Bank - Dubai.
- Board Member of First Energy Bank - Bahrain.
- Board Member of Al-Mahraab Real Estate Company - Kuwait.

Qualification:

- Attended several courses in the field of banking and finance.

Abdulrahman Mohammed Jamsheer

Vice Chairman

Experience:

- Director since March 2011 (Independent and Non-Executive).
- Shura Council member.
- Over 43 years of experience in financial and commercial sector.
- Chairman of Delmon Poultry Company.
- Chairman of Fortuna Co. W.L.L.
- Vice Chairman of Lona Real Estate BSC Closed.
- Vice Chairman of United Cement Company.
- Board Member of Esterad Investment Company.
- Board Member of Banz Group Company.
- Board Member of Daih Real Estate Development Co. W.L.L.
- Board Member of Sanad Investment Company BSC. (CLOSED).

Qualification:

- Bachelor of Science in Engineering Agricole from the American University of Beirut - Lebanon.

Bashar Mohammed Al-Mutawa

Board Member

Experience:

- Director since March 2014 (Non-Independent and Non-Executive).
- Over 16 years of experience in Financial and Investment sector.
- Nominated by Gulf Finance House BSC.
- Board Member of Gulf Finance House BSC.
- Board Member of Al Jazeera Tourism Company.
- Board Member of Naseej BSC. (CLOSED)
- Board Member of AMA University.
- Board Member of Bahrain Film Production Company BSC. (CLOSED).
- Board Member of Sanad Investment Company BSC. (CLOSED).
- Board Member of Noon investment Co. W.L.L.
- Board Member of Vaidyaratnam Ayurvedic Health Center.

Qualification:

- B.Sc. in Finance and Economic from Babson College, Massachusetts - USA.
- International bachelorette (IB) diploma.

RISK MANAGEMENT DISCLOSURES

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.2 Board of directors (continued)

Hisham Ahmed Al-Rayes

Board Member

Experience:

- Director since June 2012 (Non-Independent and Non-Executive).
- Over 13 years of experience in the financial and banking sector.
- Nominated by Gulf Finance House BSC.
- Chief Executive Officer of Gulf Finance House BSC.
- Board Member of Cemena Holding Company (CLOSED) & Affiliated Companies - Bahrain.
- Board Member of Energy City Libya Company - Libya.
- Board Member of GFH Capital Limited.
- Board Member of Tunisia Bay S.A.R.L. - Luxembourg.
- Board Member of Al-Khaleej Fund and Investment Company (CLOSED) - Bahrain.
- Board Member of Gulf Holding Company K.S.C.C. - Kuwait.
- Board Member of BFH Real Estate SPC x9 - Bahrain.
- Board Member of Naseej Properties - Bahrain.

Qualification:

- Master in Business Administration from University of DePaul - USA.
- Bachelor of Science in Electrical / Electronic Engineering from University of Bahrain.

Mohammed Barak Al-Mutair

Board Member

Experience:

- Director since August 2010 (Non-Independent and Non-Executive).
- Over 16 years of experience in government & business sector.
- Nominated by Al-Imtiaz Investment Company KSC - Kuwait.
- Chairman of Kuwait Real Estate Holding Company - Kuwait.
- Board Member of Gulf Real Estate Development Co. - Kingdom of Saudi Arabia.

Qualification:

- Bachelor Degree in Business Administration from San Diego University - USA.

Khalid Rashid Al-Thani

Board Member

Experience:

- Director since February 2009 (Independent and Non-Executive).
- Over 23 years of experience in financial and commercial sector.
- Deputy General Secretary of Awqaf and Minors Affairs Foundation - Dubai.
- Board Member of Noor Awqaf, Dubai.
- Head of Finance Department, Dubai Land Department, from 1999 to 2004 - Dubai.
- Board Member of Dubai International Holy Quran Award 1997 to 2004 - Dubai.

Qualification:

- Bachelor in Business Accounting from University of UAE.

Mosobah Saif Al-Mutairy

Board Member

Experience:

- Director since March 2011 (Non-Independent and Non-Executive).
- Over 18 years of experience in financial and investment sector.
- Nominated by Gulf Finance House BSC.
- Board Member of Gulf Finance House BSC.
- Accounts Manager of Royal Guards of Oman.
- Acting Manager of Royal Guards of Oman Pension Fund.

Qualification:

- Master in Business Administration from University of Lincolnshire & Humberside - UK.
- Postgraduate qualification in Accounting from South Bank University, London - UK.
- Degree in Accounting from South West College, London - UK.
- National Diploma in Business and Finance from Bradford & Ilkley Community College - UK.

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.2 Board of directors (continued)

Tariq Qassim Fakhroo

Board Member

Experience:

- Director since March 2011 (Non-Independent and Non-Executive).
- Over 17 years of experience in business, commercial, telecom & IT sector.
- Nominated by Gulf Finance House BSC.
- Deputy Chief Executive, Mohammed Fakhroo & Bros. - Bahrain.
- General Manager, Fakhroo IT Services - Bahrain.
- General Manager, Fakhroo IT Services Company - Kingdom of Saudi Arabia.
- Board Member of Qasim Mohammed Fakhroo W.L.L.
- Board Member of Fakhroo International Trading Agencies - Kingdom of Saudi Arabia.

Qualification:

- Master of Science in Electrical Engineering from University of Central Florida - USA.
- Master in Business Administration from University of Bahrain.
- Bachelor of Science in Electrical Engineering from University of Bahrain.

* The qualifying criteria for 'Independent' Directors are as per the Corporate Governance guidelines of the CBB.

The Chairman, the Board of Directors, and the Board Committees have direct access to the heads of Internal Audit, Risk Management, Regulatory Compliance and Shari'a Compliance.

9.3 Board of directors' interests

The members of the Board collectively held 8,508,249 shares in the Bank as of the year ended 31 December 2014 (2013: 8,358,250 shares).

Director's name	Number of outstanding shares at 31 December 2013	Number of outstanding shares at 31 December 2014	Movement during the year	% of outstanding shares
Dr. Ahmed Khalil Al-Mutawa	Nil	Nil	-	-
Dr. Fuad Abdulla Al-Omar ¹	1	N/A	(1)	-
Abdulrahman Mohamed Jamsheer	Nil	Nil	-	-
Abdulla Abdulkarim Showaiter	1,155,000	1,155,000	-	0.10%
Bashar Mohammed Al Mutawa	Nil	Nil	-	-
Hisham Ahmed Al-Rayes	Nil	Nil	-	-
Khalid Rashid Al-Thani	100,000	100,000	-	0.01%
Mohammed Barak Al-Mutair	7,103,249	7,103,249	-	0.62%
Mosobah Saif Al-Mutairy	Nil	Nil	-	-
Tariq Qassim Fakhroo	Nil	150,000	150,000	0.013%
Total	8,358,250	8,508,249	149,999	0.74%

¹ Dr. Fuad Abdulla Al-Omar's term ended on 18 March 2014.

RISK MANAGEMENT DISCLOSURES

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.4 Distribution of ownership shares by nationality

The Bank's Register of Shareholders as at 31 December 2014 indicates a total of 591 shareholders who collectively owned 1,154,161,084 (One Billion One Hundred Fifty Four Million One Hundred Sixty One Thousand and Eighty Four) shares with a nominal value of BD 0.100 (One Hundred Fils) each. The breakdown of shareholders in the Bank by nationality is as follows:

Nationality	No. of equity shares held	No. of shareholders	% of shareholders
Bahraini	696,776,832	502	60.37
Non-Bahraini	457,384,252	89	39.63
Total	1,154,161,084	591	100.00

As at 31 December 2014, none of the Bank's shares were held by the Government of the Kingdom of Bahrain.

9.5 Board committees

The Board of Directors has constituted three Committees with specific delegated authorities.

Committee	Members	Primary responsibilities
Board Nominations, Remunerations and Governance Committee (BNRGC)	<ul style="list-style-type: none"> Abdulrahman Mohamed Jamsheer Bashar Mohammed Al Mutawa Mohammed Barrak Al-Mutair Khalid Rashid Al-Thani 	<ul style="list-style-type: none"> Human Resources Compensation and incentives Administration Corporate Governance
Board Audit and Risk Management Committee (BARMC) *	<ul style="list-style-type: none"> Khalid Rashid Al-Thani Abdulrahman Mohamed Jamsheer Tariq Qassim Fakhroo 	<ul style="list-style-type: none"> Internal Audit External Audit Compliance Anti-Money Laundering Risk management Policies related to risk management
Board Investment and Credit Committee (BICC)	<ul style="list-style-type: none"> Dr. Ahmed Khalil Al-Mutawa Abdulla Abdulkarim Showaiter Mohammed Barrak Al-Mutair Mosobah Saif Al-Mutairy Hisham Ahmed Al-Rayes Khalil Ismaeel Al Meer 	<ul style="list-style-type: none"> Investment & credit approval Setting limits Investment policies Asset Liability Management Banking relationship Oversight of Off-Balance Sheet Vehicles

* During the year, the Board Audit Committee (BAC) and the Board Risk Management Committee (BRMC) were merged into one committee Board Audit and Risk Management Committee (BARMC).

Meetings of the Board and its committees are held as and when required but in accordance with the Regulations the Board meets at least once a quarter. The Board of Directors met seven times in 2014. The Bank held its AGM on 18 March 2014. In addition to physical meetings, several written resolutions were circulated to the Directors during 2014 for approval by mail and facsimile.

During the year, the Board Audit Committee (BAC) and the Board Risk Management Committee (BRMC) both held one meeting each before being merged into one committee - the Board Audit and Risk Management Committee (BARMC). The BARMC held 3 meetings subsequent to the merger, the Board Investment and Credit Committee (BICC) held 4 meetings, and the Board Nominations, Remunerations and Governance Committee (BNRGC) held 5 meetings.

The Board of Directors and its committees receive regular reports on various aspects of the Bank's business from Senior Management as well as from Internal Audit, Risk Management, Financial Control, and Operations Departments.

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.6 Board committees meeting dates

- Board meetings: a total number of 7 meetings were held.

Director's name	BOD Meeting dates during the year 2014							Attendance %
	16 th Jan	30 th Jan	18 th Mar	24 th Apr	16 th Sep	13 th Nov	5 th Dec	
Dr. Ahmed Khalil Al-Mutawa	✓	✓	✓	✓	✓	✓	✓	100%
Dr. Fuad Abdulla Al-Omar ¹	✓	✓	N/A	N/A	N/A	N/A	N/A	100%
Abdulrahman Mohammed Jamsheer	✓	✓	✓	✓	✓	✓	✓	100%
Abdulla Abdulkarim Showaiter	✓	✓	✓	✓	✓	✓	✓	100%
Bashar Mohammed Al-Mutawa ²	N/A	N/A	✓	✓	✓	✓	✓	100%
Mohammed Barak Al-Mutair	✓	✓	✓	✓	✓	✓	✓	100%
Mosobah Saif Al-Mutairy	✓	✓	✓	✓	✓	✓	✓	100%
Tariq Qassim Fakhroo	✓	✓	✓	✓	✓	✓	-	More than 75%
Khalid Rashid Al-Thani	✓	✓	✓	✓	✓	✓	✓	100%
Hisham Ahmed Al-Rayes	✓	✓	✓	✓	✓	✓	✓	100%

¹ Dr. Fuad Abdulla Al-Omar's term ended on 18 March 2014.

² Mr. Bashar Mohammed Al-Mutawa joined the Board effective from 18 March 2014.

- BICC meetings: a total number of 4 meetings were held (minimum of 4 meetings a year).

Director's name	BICC Meetings dates during the year 2014			
	30 th Jan	24 th Apr	16 th Sep	13 th Nov
Dr. Ahmed Khalil Al-Mutawa ¹	N/A	✓	✓	✓
Dr. Fuad Abdulla Al-Omar ²	✓	N/A	N/A	N/A
Abdulla Abdulkarim Showaiter	✓	✓	✓	✓
Mohammed Barak Al-Mutair	✓	✓	✓	✓
Mosobah Saif Al-Mutairy	✓	✓	✓	✓
Hisham Ahmed Al-Rayes	✓	-	✓	✓
Khalil Ismaeel Al Meer ¹	N/A	✓	✓	✓

¹ Dr. Ahmed Al Mutawa and Mr. Khalil Al Meer joined the Committee officially in March 2014.

² Dr. Fuad Abdulla Al-Omar's term ended on 18 March 2014.

RISK MANAGEMENT DISCLOSURES

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.6 Board committees meeting dates (continued)

- BNRGC meetings: a total number of 5 meetings were held (minimum 2 meetings a year).

Director's name	BNRGC Meetings dates during the year 2014				
	30 th Jan	24 th Apr	16 th Sep	30 th Sep	10 th Dec
Abdulrahman Mohammed Jamsheer	✓	✓	✓	✓	✓
Abdulla Abdulkarim Showaiter ¹	✓	N/A	N/A	N/A	N/A
Bashar Mohammed Al-Mutawa ²	N/A	✓	✓	✓	✓
Khalid Rashid Al Thani	✓	✓	✓	✓	-
Mohammed Barak Al-Mutair	✓	✓	✓	✓	✓

¹ Mr. Abdulla Abdulkarim Showaiter resigned from the Committee effective 9 April 2014.

² Mr. Bashar Mohammed Al-Mutawa joined the Committee officially on March 2014.

- BRMC meeting: 1 meeting was held.

Director's name	BRMC Meeting date during the year 2014
	29 th Jan
Abdulrahman Mohammed Jamsheer	✓
Tariq Qassim Fakhroo	✓
Dr. Ahmed Khalil Al-Mutawa	✓

- BAC meeting: 1 meeting was held.

Director's name	BAC Meeting date during the year 2014
	29 th Jan
Khalid Rashid Al Thani	✓
Dr. Ahmed Khalil Al-Mutawa	✓
Tariq Qassim Fakhroo	✓

- BARMC meetings: a total number of 3 meetings were held (minimum of 4 meetings a year).

Director's name	BARMC Meetings dates during the year 2014 *		
	24 th Apr	16 th Sep	12 th Nov
Khalid Rashid Al Thani	✓	✓	✓
Abdulrahman Mohammed Jamsheer	✓	✓	✓
Tariq Qassim Fakhroo	✓	✓	✓

* The Board Audit Committee (BAC) and the Board Risk Management Committee (BRMC) were merged in one committee (BARMC).

9.7 Code of conduct

The Board has approved a code of conduct for all staff of the Bank and the Board members. The Code includes the process of dealing with conflict of interests. It also binds the Directors, Executive Management and staff to the highest standard of professionalism and diligence on discharging their duties. All Board members and senior management of the Bank have affirmed compliance with the Code of Conduct. A declaration is made by the Board members prior to each Board meeting confirming that they have disclosed all external appointments and notified the Chairman if there have been any changes to their external appointments since the previous meeting. Board members are excluded from dealings in matters related to an external entity where they hold an appointment at that entity.

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.8 Compliance with regulations

The Bank ensures compliance with the regulations applicable to an Islamic licensed bank at all times. It would report any non-compliance with the guidelines should there be any. The Bank's obligations to comply with the Regulations have been addressed through following a Corporate Governance Handbook in accordance with the corporate governance ("CG") and the High-Level Controls Module of the CBB Rulebook. The CG Handbook was developed to manage the Board and committees Charter, Management Committee Charters, Board and Management Code of Conduct, Conflict of Interest Policy, Whistle Blowing Policy, Corporate Governance Guidelines, Social Responsibility, Directors' Appointment Agreement, Board and Directors' Evaluation, and a Key Persons' Dealing Policy.

The Bank is committed to continuously review and develop its corporate governance policies to ensure compliance with the changing requirements of the Regulations and to ensure compliance with the international corporate governance best practice. The Bank, through its Board and Board Committees, endeavors to deliver the highest standards of governance for the benefit of its stakeholders.

9.9 Shari'a Supervisory Board

The Bank's Shari'a Supervisory Board consists of three Islamic scholars who review the Bank's compliance with general Shari'a principles and specific fatwas, rulings and guidelines issued. Their review includes examination of evidence relating to the documentation and procedures adopted by the Bank to ensure that its activities are conducted in accordance with Islamic Shari'a principles.

Dr. Fareed Yaqoob Al-Miftah

Chairman

Experience:

- Member of the Supreme Council of Islamic Affairs.
- Undersecretary of the Ministry of Justice & Islamic Affairs - Bahrain.
- Former Judge of the High Shari'a Court.
- Former Lecturer at the University of Bahrain.

Qualification:

- Ph.D. from the University of Edinburgh - UK.

Shaikh Nizam Mohammed Saleh Yaqoobi

Member

Experience:

- Member of the Shari'a council of Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI).
- Member of the Shari'a Board of the Central Bank of Bahrain - Bahrain.
- Member of Shari'a Supervisory Board of the Dow Jones Islamic index.
- Member of Shari'a Supervisory Board of a number of Islamic banks & insurance companies.

Dr. Fareed Mohammed Hadi

Executive Member

Experience:

- Assistant Professor of Jurisprudence (Fiqh) and Hadeeth at the College of Arts, Department of Arabic and Islamic studies, University of Bahrain.
- Bachelor program Manager in Shari'a for Banking and Finance, University of Bahrain.
- Vice President of the Association of Shari'a scholars in GCC.
- Member of Shari'a Supervisory Board of a number of Islamic banks.

Qualification:

- Ph.D. in Ibn Hazm's Methodology of Jahala, University of Edinburgh - UK.
- Ph.D. in Al-Bukhari's Methodology, University of Mohammed V - Morocco.

9.10 Executive management committees

The Board of Directors delegates the authority for day-to-day management of the business to the Chief Executive Officer (CEO) who is responsible for implementing the Bank's strategic plan. The CEO manage the Bank through the following management committees:

Committee	Primary responsibilities
Management Committee	Strategy, Performance review, Budget, Human Resources, Administration
Asset Liability Management Committee	Balance sheet management, Funding, Liquidity, Banking Relationships
Executive Credit & Investment Committee	Review of investments, Exit and credit proposals, Monitoring of investments
Executive Risk Management Committee	Risk Management policies, Risk review, Provisions and impairment

RISK MANAGEMENT DISCLOSURES

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.11 Executive management & other senior management

During 2014, the following changes were carried out in the executive management: the appointment of Mr. Salah Khalifa Mohammed, the Head of Corporate Banking, and Mr. Vijayan Govindarajan, the Head of Risk Management. Besides, and the resignation of Mr. Silvan Varghese, the COO, and Mr. Ozan Benlioglu, the Head of Investment Banking.

The names and title of each member of executive and other Senior Management are set out below:

Khalil Al Meer

Chief Executive Officer

Experience:

- Over 29 years of experience in corporate and retail banking that he gained from his work in the leading banks in the Kingdom of Bahrain.
- Joined the Bank in 2013.

Qualification:

- B.Sc. in Business Administration from the University of Bahrain.
- Attended the Gulf Executive Development Program at Darden Graduate School of Business in University of Virginia (USA).
- Attended the Senior International Bankers Program from the International Centre for Banking and Finance Services at Manchester Business School - UK.

Mahdi Abdulnabi Mohammed

DGM - Support Services

Experience:

- Over 34 years of banking experience.
- Joined the Bank in 2005.

Qualification:

- Certified Diploma in Accounting & Finance from The Chartered Association of Certified Accountants (ACCA).
- MBA from the University of Strathclyde - UK.

Ahmed Ali Bucheeri

Head of Internal Audit

Experience:

- Over 26 years of experience in both internal and external audit mainly in banks.
- Joined the Bank in 2007.

Qualification:

- Certified Internal Auditor (CIA) from the Institute of Internal Audit - USA.
- B.Sc. in Accounting from King Fahad University of Petroleum and Minerals - Kingdom of Saudi Arabia.

Fuad Ali Taqi

DGM - Commercial Banking

Experience:

- Over 33 years of banking experience in Islamic and conventional banks.
- Joined the Bank in 2006.

Qualification:

- Business Studies Diploma.
- MBA from the University of Glamorgan - UK.

Salah Khalifa Mohammed

Head of Corporate Banking

Experience:

- Over 20 years of experience in Islamic and conventional corporate and wholesale banking, treasury, asset management and structured finance.
- Joined the Bank in June 2014.

Qualification:

- MBA, University of Glamorgan, Wales, UK.
- Diploma in Commercial Studies, University of Bahrain
- Executive MBA from University of Bahrain.
- Diploma in Management and Information Systems, Aptech Computer Education.

Hussam Ghanem Saif

Head of Treasury & Capital Markets

Experience:

- Over 25 years of experience in treasury and Islamic banking.
- Joined the Bank in 2007.

Qualification:

- Graduate with a degree in Business Administration & Management from Western International University, London - UK.

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.11 Executive management & other senior management (continued)

Yaser Ismaeel Mudhafar
Chief Financial Officer

Experience:

- Over 17 years of extensive experience in the Islamic banking industry and audit.
- Joined the Bank in 2006.

Qualification:

- Certified Public Accountant (CPA) from the American Institute of Certified Public Accountants.
- Certified Islamic Professional Accountant (CIPA) from the Accounting and Auditing Organisation for Islamic Financial Institutions (AAOIFI).
- Executive MBA from University of Bahrain.

Mohammed Abdulla Saleh
Corporate Secretary, Head of Compliance and MLRO

Experience:

- Over 17 years of experience in management, Islamic banking, corporate governance, compliance and anti-money laundering.
- Joined the Bank in 2009.

Qualification:

- Master's in IT, Media and E-Commerce Law from the University of Essex - UK.
- B.Sc. in Law from Dubai Police Academy - UAE.
- Advanced Diploma in Islamic Finance from Bahrain Institute of Banking and Finance (BIBF).
- Diploma in Business Management from the University of Bahrain.
- ICA International Diploma in Compliance from the International Compliance Association ICA.

Vijayan Govindarajan
Head of Risk Management

Experience:

- Over 34 years of experience in the banking industry in India and Bahrain in several areas like risk and credit management.
- Joined the Bank in 2014.

Qualification:

- Bachelors of Science.
- Certified Associate, Indian Institute of Banking and Finance.

Fatooh Yusuf Al-Mannai
Head of Human Resources

Experience:

- Over 19 years of experience in human resources, training and administration.
- Joined the Bank in 2007.

Qualification:

- MBA and a BA (Hons.) in Human Resource Management.
- Fellow of the Chartered Institute of Personnel & Development (Chartered FCIPD).
- Member of Society of Human Resource Management (SHRM).
- Member of Bahrain Society for Training and Development (BSTD).

Abdul-Nasser Omar Al-Mahmood
Head of Shari'a Compliance

Experience:

- Over 24 years of experience in Shari'a Audit and Islamic banking.
- Joined the Bank in 2008.

Qualification:

- Master's in Business Administration with thesis in Shari'a Control and Review in Islamic Banks.
- B.Sc. in Shari'a and Islamic Studies.
- Associate Diploma in Shari'a Control.

RISK MANAGEMENT DISCLOSURES

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.12 Executive and senior management interests

The following table indicates the executive and senior management shareholding as 31 December 2013:

Executive and senior management	Number of outstanding shares at 31 December 2013	Number of outstanding shares at 31 December 2014
Khalil Al Meer	Nil	Nil
Silvan Varghese *	2,156,886	N/A
Fuad Ali Taqi	2,141,585	2,141,585
Mahdi Abdulnabi Mohammed	1,639,397	1,639,397
Salah Khalifa Mohammed	Nil	Nil
Ahmed Ali Bucheeri	424,850	500
Hussam Ghanem Saif	679,565	679,565
Yaser Ismail Mudhafar	526,438	526,438
Fatooh Yusuf Al-Mannai	Nil	Nil
Ozan Benlioglu *	68,994	N/A
Mohammed Abdulla Saleh	60,000	Nil
Abdul-Nasser Omar Al-Mahmood	Nil	Nil
Vijayan Govindarajan	Nil	Nil
Total	7,697,715	4,987,485

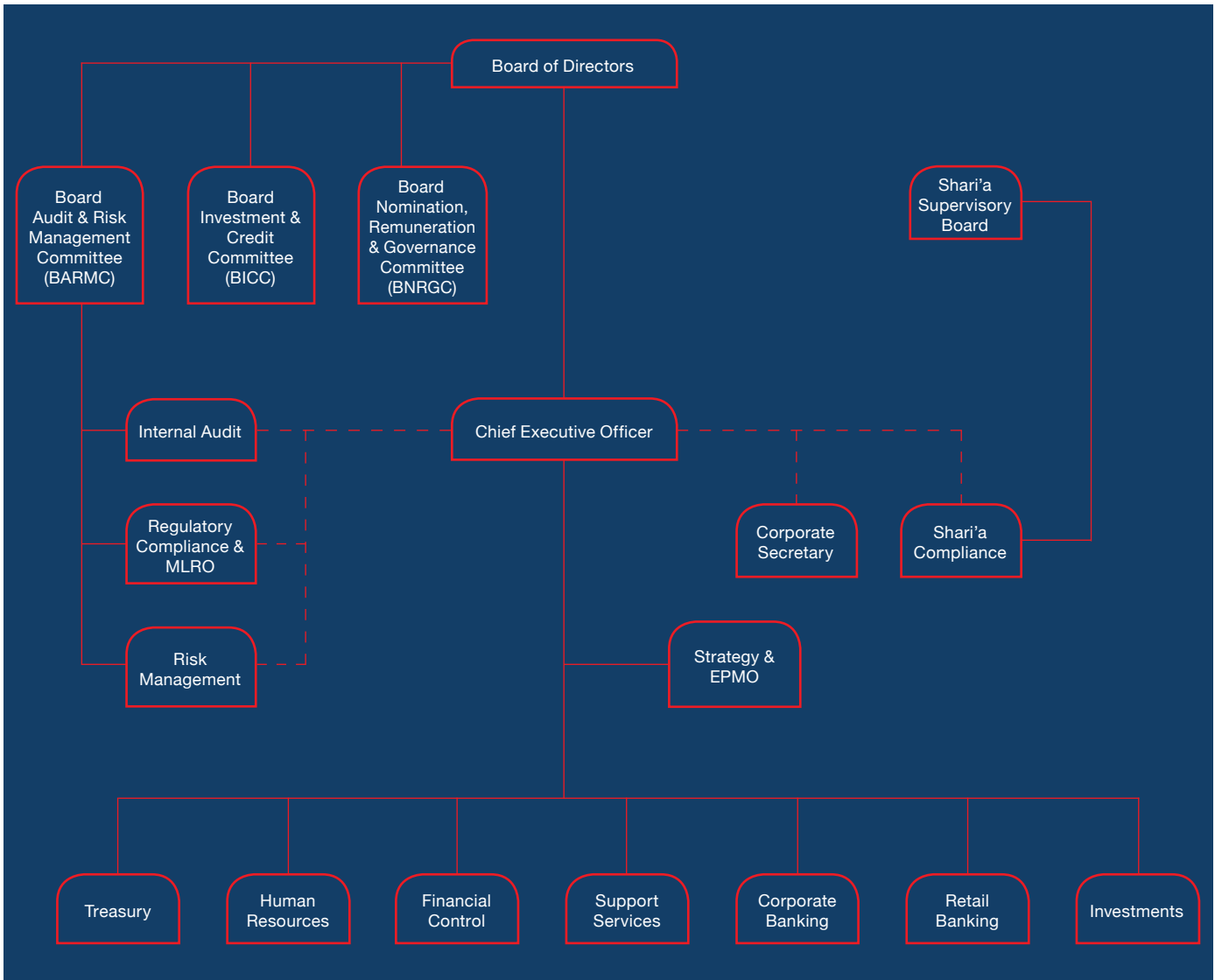
* Resigned during the year.

The change in the above number of shares is mainly due to vesting of shares under the share-based employee incentive scheme. There was no senior management's trading of the Bank's shares during the year.

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.13 Organizational chart

Set out below is the Bank's organization chart, which outlines the different committees and the lines of reporting.



9.14 Executive compensation

The Bank has both a short-term and long-term compensation structure for its executive management which has been developed based on current market surveys and industry norms. The Bank also had an incentive scheme where in eligible employees were awarded a combination of shares and cash incentives on achievement of pre-determined performance targets. For further details please refer note 23 of the consolidated financial statements for the year ended 31 December 2014. The Board of Directors is entitled to sitting fees and their annual remuneration is subject to the approval of the shareholders at the end of each year.

RISK MANAGEMENT DISCLOSURES

9 CORPORATE GOVERNANCE & OTHER DISCLOSURES (CONTINUED)

9.15 Shari'a compliance, regulatory compliance and anti-money laundering

Compliance with Shari'a laws, regulatory and statutory requirements is an ongoing process and the Bank is conscious of its responsibilities in observing all applicable provisions and best international practices in its functioning. The Bank has established the Shari'a Compliance Function and the Regulatory Compliance Function in keeping with Basel and CBB guidelines. The respective units act as a focal point for all Shari'a and regulatory compliance and for adapting other best practice compliance principles.

Anti-Money Laundering measures form an important area of the Compliance Function. The Bank has an Anti-Money Laundering and Combating Terrorist Financing Policy and Procedure approved by the Board, which contains sound Customer due diligence measures, procedure for identifying and reporting suspicious transactions, a program for periodic awareness training to staff, record-keeping, and a designated Money Laundering Reporting Officer (MLRO). The Bank's Anti-Money Laundering measures are reviewed by independent external auditors every year and their report is submitted to the CBB. The Bank is committed to combating money laundering and is in compliance with the guidelines issued by the CBB in relation to Anti-Money Laundering requirements.

The Bank is in compliance with the HC Module of the CBB Rulebook. However, due to the limited number of independent board members, the Bank has not been able to completely comply with following requirements:

- HC 1.8.2: that requires a constitution of a corporate governance committee with at least three independent members;
- HC 4.2.2: in which the Board must establish a nominating committee which would include only independent directors or only non-executive directors of whom a majority must be independent directors including the chairman;
- HC 5.3.2: in which it is requires to include only independent directors for the remuneration committee or, alternatively, only non-executive directors of whom a majority are independent directors including the chairman.
- HC 9.2.4 - in which it is requires an independent director to chair the Corporate Governance Committee.

The Bank did not comply with HC 1.4.6 - where it requires the chairman of the Board to be an independent director.

In addition, the Bank is also non-compliant to HC 9.2.4 (b) where it requires including a Shari'a scholar who is a SSB member to the Corporate Governance Committee.

9.16 Audit fees charged by the external auditor and other non-audit services provided by the external auditor and fees paid

The audit fees charged and non-audit services provided by 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 would not negatively impact the Bank's interest and its competition in the market.

9.17 Penalties paid to the Central Bank of Bahrain

During the year, there was no penalty imposed by the CBB on the Bank.

10 FINANCIAL PERFORMANCE

Following are basic quantitative indicators of the financial performance:

	2014	2013	2012	2011	2010
Return on average equity	3.00%	-16.06%	0.64%	0.44%	- 5.24%
Return on average assets	0.53%	-3.69%	0.18%	0.13%	- 1.67%
Finance income to finance expense	197.05%	147.77%	201.89%	208.06%	240.21%
Cost-to-income *	75.80%	156.56%	84.54%	72.11%	83.79%

* Cost excludes impairment allowances.

For detailed discussion on the performance for the year, kindly refer to Chairman's report on the consolidated financial statement for the year ended 31 December 2014.

11 REMUNERATION RELATED DISCLOSURES

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

During the year, the Bank has adopted the Sound Remuneration Practices issued by the Central Bank of Bahrain and has proposed revisions to its variable remuneration framework. The revised policy framework and incentive components are subject to the approval of the shareholders in the upcoming annual general meeting. Once approved, the policy will be effective for the 2014 annual performance incentives and would be fully implemented for future periods.

The key features of the proposed remuneration framework have been summarized below.

11 REMUNERATION RELATED DISCLOSURES (CONTINUED)

11.1 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 reward 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 shareholders. The Bank's reward package comprise 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 Bank operates within clear parameters of its compensation strategy and policy. All compensation matters, and overall compliance with regulatory requirements, are overseen by the Nomination, Remuneration and Governance Committee of the Board (BNRGC).

The Bank's remuneration policy in, particular, considers the role of each employee and has set guidance depending on whether an employee is a Material Risk Taker and / or an Approved Person in business line, control or support functions. An Approved Person is an employee whose appointment would require prior regulatory approval because of the significance of the role within the Bank and an employee is considered a Material Risk Taker if they head of significant business lines and any individuals within their control who have a material impact of 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 line with our performance management system. This assessment also takes into account adherence to the Bank's values, risk and compliance measures above all and acting with 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 BNRGC believes the latter contributes to the long-term sustainability of the business.

11.2 BNRGC role and focus

The BNRGC has oversight of all reward policies for the Bank's employees. The BNRGC 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 BNRGC 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 and the business plan and risk profile of the Bank.

The responsibilities of the BNRGC as regards the variable compensation policy of the Bank, 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 BNRGC 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 controls 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.

As outlined in the Corporate Governance section of the Annual Report, the Board is satisfied that all non-executive directors are independent including the BNRGC members. The BNRGC comprises of the following members:

RISK MANAGEMENT DISCLOSURES

11 REMUNERATION RELATED DISCLOSURES (CONTINUED)

11.2 BNRGC role and focus (continued)

BNRGC member name	Appointment date	Number of meetings attended
Abdulrahman Mohammed Jamsheer	May 2013	5
Abdulla Abdulkarim Showaiter ¹	March 2008	1
Bashar Mohammed Al-Mutawa ²	April 2014	4
Khalid Rashid Al-Thani	April 2011	4
Mohammed Barak Al-Mutair	April 2011	5

¹ Mr. Abdulla Abdulkarim Showaiter resigned from the Committee effective 9 April 2014.

² Mr. Bashar Mohammed Al-Mutawa joined the Committee officially on 24 April 2014.

The aggregate remuneration paid to the BNRGC members during the year in the form of sitting fees amounted to BHD 7 thousand [2013: BHD 4 Thousand].

11.3 External consultants

Consultants were appointed during the year to advise the Bank on amendments to its the variable remuneration policy to be in line with the CBB's Sound Remuneration Practices and industry norms. This included assistance in designing an appropriate Share-based Incentive Scheme for the Bank. The BNRGC also appointed consultants during the year to perform a pay benchmarking exercise to assist them in reviewing the total compensation offered by the Bank.

11.4 Scope of application of the remuneration policy

The remuneration policy has been adopted on a bank-wide basis and shall not apply to its non-banking subsidiaries and operations.

11.5 Board remuneration

The Bank's board remuneration is determined in line with the provisions of Article 188 of the Bahrain Commercial Companies Law, 2001. The board of directors' remuneration will be capped so that the total remuneration (excluding sitting fees) does not exceed 5% of the Bank's net profit, after all the required deductions outlined in Article 188 of the Companies law, in any financial year. The board remuneration is subject to approval of the shareholders in the Annual General Meeting. Remuneration of non-executive directors do not include performance-related elements such as grants of shares, share options or other deferred stock-related incentive schemes, bonuses or pension benefits.

11.6 Variable remuneration for staff

The 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 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 that the combination of meeting both satisfactory financial performance and achievement of other non-financial factors, would, all other things being equal, deliver a target bonus pool for the employees, prior to consideration of any allocation to business lines and employees individually. In the framework adopted in determining the variable remuneration pool, the BNRGC aims to balance the distribution of the Bank's profits between shareholders and employees.

The 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 would result in a target top-down 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 BNRGC carefully evaluates practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. BNRGC 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 BNRGC.

11 REMUNERATION RELATED DISCLOSURES (CONTINUED)

11.6 Variable remuneration for staff (continued)

For the overall Bank to have any funding for distribution of bonus pool; thresholds of financial targets have to be achieved. The performance measures ensure that the 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 adjustment and linkage framework.

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 based on function-specific objectives and is not determined by the individual financial performance of the business area 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.

Variable compensation for business units

The variable compensation for the business units is primarily decided by the 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 environment. The consideration of risk assessment in the performance evaluation of individuals ensures that any two employees who generate the same short-run profit but take different amounts of risk on behalf of the bank are treated differently by the remunerations system.

11.7 Risk assessment framework

The purpose of the 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 risk adjustments. The risk assessment process encompasses the need to ensure that the remuneration policy designed reduces employees' incentives to take excessive and undue risk is symmetrical with risk outcomes and has an appropriate mix of remuneration that is consistent with risk alignment.

The Bank's BNRGC 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 assessment to review financial and operational performance against the business strategy and risk performance prior 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 a 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 BNRGC keeps itself abreast with the Bank's performance against the risk management framework. The BNRGC will use this information when considering remuneration to ensure the return, risk and remuneration are aligned.

Risk adjustments

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

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

- There would be considerable contraction of the Bank's total variable remuneration.
- At the individual level, poor performance by the Bank would mean individual KPIs are not met and hence employee performance ratings would be lower

RISK MANAGEMENT DISCLOSURES

11 REMUNERATION RELATED DISCLOSURES (CONTINUED)

11.7 Risk assessment framework (continued)

Risk adjustments (continued)

- Reduction in 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 bonus awards may be considered.

The BNRGC, with 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 share awards
- Recovery through malus and clawback arrangements

Malus and Clawback framework

The Bank's malus and clawback provisions allows 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 compensation could be 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 taken by the Bank's Board of Directors.

The Bank's malus and clawback provisions allows the Bank's 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 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.

11.8 Components of Variable remuneration

Variable remuneration has 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 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).

11 REMUNERATION RELATED DISCLOSURES (CONTINUED)

11.9 Risk assessment framework

All employees above the grade of a Senior Manager shall be subject to deferral of variable remuneration as follows:

Element of variable remuneration	General Manager and above	Senior Managers and above	Deferral period	Retention	Malus	Clawback
Upfront cash	40%	50%	immediate	-	-	Yes
Upfront shares	-	10%	immediate	6 months	Yes	Yes
Deferred cash	10%	-	Over 3 years	-	Yes	Yes
Deferred share awards	50%	40%	Over 3 years	6 months	Yes	Yes

The BNRGC, based on its assessment of role profiles and risk taken by an employee could increase the coverage of employees that would subject to deferral arrangements.

11.10 Details of remuneration paid

(a) Board of directors

	2014	2013
• Sitting Fees	201	329
• Remuneration	Nil	Nil
• Others *	15	23

* This represents airfare, accommodation, transportation and food and beverages paid on behalf of the Board members.

(b) Employee remuneration

	Number of staff	Fixed remuneration		Variable remuneration					Total
		Cash	Others	Upfront		Deferred			
				Cash	Shares	Cash	Shares	Others	
Approved persons									
- Business lines	7	654	423	42	-	9	44	-	1,172
- Control & support	12	602	269	42	6	2	34	-	955
Other material risk takers	6	271	169	31	-	2	11	-	484
Other staff	178	2,234	1,120	283	-	-	-	-	3,637
TOTAL	203	3,761	1,981	398	6	13	89	-	6,248

The fixed remuneration was BD 4,716 thousand and the variable remuneration was BD 499 thousand for the year 2013.

RISK MANAGEMENT DISCLOSURES

BD 000's

11 REMUNERATION RELATED DISCLOSURES (CONTINUED)

11.10 Details of remuneration paid (continued)

(c) Deferred awards

	2014				Total (Amount)
	Cash (Amount)	Shares (Number)	(Amount)	Others (Amount)	
Opening balance	-	-	-	-	-
Awarded during the period	13	1,966,375	94	-	107
Paid out / released during the period	-	-	-	-	-
Service, performance and risk adjustments	-	-	-	-	-
Changes in value of unvested opening awards	-	-	-	-	-
Closing balance	13	1,966,375	94	-	107

(d) Severance pay

During the year Bank paid BD 652 thousand as ex-gratia to 10 employees and the highest amount paid to a single person was BD 161 thousand.