Chapter Two

Banking Managerial Risk
Banking Managerial Risk

First: Corporate Governance

A- Corporate Governance

1- Definitions

- **QCB**: Qatar Central Bank.
- **Banks**: All national banks licensed by QCB to operate in Qatar by virtue of law.
- **Financial Services Institutions**: investment, finance companies, exchange houses or any other institution which are licensed to operate in Qatar by law or by QCB’s approval.
- **Board of Directors**: The board of directors of the bank or the financial institution.
- **Executive Management**: The general manager or the chief executive officer, his assistants, and staff of the bank or the financial services institution.
- **Corporate Governance**: A regulatory framework that assigns the responsibilities and roles of the board of directors and the executive management of the bank or financial services institution, and their relations linked with the shareholders, related parties and QCB.

2- Roles and Responsibilities of Board of Directors

The board of directors shall assume the following responsibilities:

2/1 Set and develop strategies, objectives and policies.
2/2 Organizational Structure Set-Up.
2/3 Committees Constitution and delegation of powers and authorities.
2/5 Appointment of Internal Auditing Staff and Monitoring.
2/6 External Auditor Approval.
2/7 Responsibility Towards Shareholders and Other Parties.
2/8 Board Responsibility towards QCB.
2/1 Set and Develop Strategies, Objectives and Policies

- The board of directors should provide the executive management with definite strategies, policies and plans by which the objectives of the bank or financial institution could be achieved. The board of directors should occasionally review and develop such strategies and policies consistent with the developments and changes at the local, regional, and international levels, taking into account QCB’s framework for licensing regulations and instructions.

- The board of directors shall utilize studies, reports, information and consultations prepared by the executive management in order to set strategies, plans and policies. Additionally, the board of directors may consult external experts.

- The following are some of the main policies of risk management that should be set, evaluated and developed by the bank:
  Providing and evaluating credit facilities, investment, liquidity, market risk, capital adequacy risk, concentration risk, foreign exchange risk, interest rate risk, pricing, profitability and budgets, accounting and operational risks, legal risks, combating money laundering, asset insurance, parties of common interests, compliance with supervisory instructions and laws, external and internal auditing, performance evaluation, disclosure to all concerned authorities, personnel policies regulating appointments and costs and developing systems for incentives, developing skills and promoting work ethics and attitudes, and other policies.

- The board of directors should collectively and independently practice its tasks in a neutral and objective manner and avoid influences on relations and directives related to the executive management or others.

2/2 Organizational Structure Set-Up

Forming the organizational structure of the bank or financial institution is one of the boards of director’s main responsibilities and tasks, including:

- Approve the organizational structure of the bank or the institution and determine related tasks, functions, duties, responsibilities, relationships among the different managerial levels to the members of the board of directors, chief executive officer/general manager, executive departments and
divisions, in addition to auditing units. The following controls should be taken into account:

- Functions and authorities of the board of directors should be separated from those of the executive management.
- Tasks of conducting and carrying out contracts and deals should be separated from those of transferring funds, registration, accounting, and risk management.
- Board of directors shall continuously supervise and control the transactions conducted by the individuals who are not related to those conducted by the executive departments and divisions.
- Board of directors shall establish an independent department in order to evaluate risks, including a central unit for emergencies.
- Internal auditing should be independent and directly be under supervision of the board of directors.

- Board of directors shall consult any internal or external expert in order to form the organizational structure in conformity with business volume, objective and nature. Accordingly, the board shall unanimously approve such structure.
- Board of directors shall be responsible for appointing the chief executive officer or the general manager, and the senior executive managers, assistants, experts, and consultants, in addition to determining their salaries, rewards, retirements, dismissals, and subject them to disciplinary actions. Such responsibilities shall be conducted within the framework of policies and standards unanimously defined by the board members in a neutral and objective manner. Board of directors shall also have clear plan for the succession of the executive managements.
- Board of directors should occasionally review and develop the organizational structure, status, personnel, defined duties and responsibilities in the light of results of supervision, control and evaluation of performance and activities in conformity with the current changes.

2/3 Committees Constitution and Delegation of Powers and Authorities

- Board of directors shall conduct its supervisory tasks and determine authorities in making decision by constituting committees which include its members. Additionally, the board of directors shall involve the members of the
executive management in the committees. Every committee shall be concerned with one or more of the tasks of the board of directors. The following are the most significant committees that should be constituted by the board of directors:

- Policies and Development Committee: It shall be responsible for studying, preparing and developing strategies, objectives, policies, systems, plans and budgets.

- Executive Committees: It shall have the powers delegated by the board of directors, to grant, renew and follow up credit facilities, and invest funds, the authority of the executive management could be extended, by the board

- Auditing and Risk Evaluation Committee: It shall be responsible for monitoring the internal and external auditing, and evaluating the performance and risk.

- Each committee should have well defined work program for determining the duties, responsibilities, powers, methods of decision making, and meeting dates. The meeting minutes should be recorded safely in an organized way so that they can be retrieved easily for auditing and compliance purposes.

- The proceedings of meetings conducted by committees of the board of directors should be included in the agenda of the first meeting of the board of directors that follows the meeting of the committees, whether for approval or notification, with the decisions taken by the committees according to the authority of the committee.

- Board of directors should delegate authority of decision-making, assign the powers of the signatories of the bank or the institution, and transfer funds gradually between the different managerial levels, starting from the board of directors to the board chairman, members and its committees ending with the executive management. Accordingly, board of directors should restrain individual authority and adopt the collective or joint authority.
2/4 Monitor the Implementation of Policies and Performance and Risk Assessment

Board of directors should basically supervise the implementation of policies, achievement of the bank or institution objectives, and evaluation of performance using the following main tasks and instruments:

- Evaluating the executive programs, procedures and internal control:
  The board of directors should evaluate the programs, procedures and instructions on implementing the operations set by the executive management. Board of directors should verify the executive management's ability and capability of implementing policies which they set, and check the internal control procedures. The following are the most significant programs and procedures:
  - Accounting procedures and programs and Programs on financial reports and statements.
  - Operation procedures and electronic systems programs.
  - Daily work programs and procedures in the executive managements such as: credit, treasury, customer service and others.
  - Procedures and instruments of internal control and protection.

Board of directors should request from the executive management to develop operational programs, procedures and internal control, and continuously rectify their shortcomings according to the evaluation results and the regular performance follow-up.

- Periodical Reports Review:
  Board of directors should always review various types of reports issued by its committees through the periodical meetings, during the year. Such reports shall be directly submitted to the board of directors by:
  - Executive management: provide periodical reports on results of the different activities, risk evaluation and financial statements.
  - Internal auditing: provide reports on results of the periodical auditing and compliance, with a copy of such reports to be submitted to the executive management that would furnish the feedback.
  - External auditing: provide reports on results of the periodical and specialized auditing results that may be required by board of directors, in
addition to report of the annual auditing results, with copy of such reports
to be submitted to the executive management that would furnish feedback.
In coordination with the executive management and the auditing staff,
board of directors should verify the adequacy, comprehensiveness,
credibility of the different reports submitted to the board of directors and
its committees.

- **Performance Evaluation and Rectification of Deviations:**
  In the light of studying the above mentioned periodical reports, the board of
directors shall evaluate performance of the executive management, compliance
with policies of the board of directors, and success in achieving the target
objectives and results, including revealing and evaluating the violations,
analyzing reasons and calling to account by those people who are in charge,
and issuing the necessary instructions to address such violations and avert
their occurrences.

- **Present and Future Risk Assessment:**
  In the light of studying and analyzing the above mentioned reports, the board of
directors should evaluate the current risks and issue directives to the
executive management on how to handle, mitigate and hedge risks. In the light
of such reports and other reports on the international and domestic market,
the board of directors can accordingly predict the potential risks, that may be
faced by the bank or institution, contain and hedge such risks using the current
and future plans and policies.

- **End of Year Financial Statements Approval:**
  In the light of the supervisory role, the board of directors shall be responsible
for approving the end of year financial statements, ensuring the soundness and
creditability of all financial statements’ transparency and adequacy of
disclosures in accordance with the International Accounting Standards and
disclosures according to QCB’s instructions.

**2/5 Appointment of Internal Auditing Staff and Monitoring**

The board of directors shall be responsible for appointing a highly qualified and
experienced internal auditing staff in all fields of the banks or institution. The
board of directors shall supervise such staff through the following issues:
• The internal auditing staff should be neutral and independent and should not be influenced by the executive management. They should be directly under supervision of the board of directors. Salaries, incentives and bonuses given to the internal auditing staff should be determined by the board of directors. Accordingly, they should be evaluated by the board of directors. Thus, their capabilities, qualifications, experiences and professional skills should be verified and reviewed on regular basis.

• The internal auditing should cover all departments, divisions and branches of the bank or the institution, as well as risks and activities. Auditing should be periodically and regularly conducted during the year. Furthermore, the end of year financial statements should be audited at the end of the year.

• The internal auditing should be conducted in conformity with the proper, comprehensive and professional auditing programs in pursuance with the recent international auditing guides and standards. Such programs should be evaluated and developed in order to cope with the bank/institution’s recent business developments.

• The internal auditing reports should be directly submitted to the board of directors and then transferred to the executive management for their comment and feedback. Accordingly, the board of directors shall issue directives in order to address comments in conformity within a limited time frame that shall be followed up by internal auditing.

• The reports and documents should be maintained by the Internal Auditing Department in an organized and safe manner so that board of directors, QCB's supervisors and external auditors can refer to such reports and documents.

2/6 External Auditor Approval

• Board of directors is responsible for nominating and contracting with a highly qualified and specialized independent external auditor in addition to determining his salary after the General Assembly's approval have been obtained and QCB's requirements have been fulfilled. The board of directors should set the instructions and controls and have policies and procedures to enable the external auditor to access the information, data and documents necessary for auditing, whether through the executive management or the
board of directors. Subsequently, the external auditor should be neutral and independent when concluding the auditing results.

- External auditor reports should be directly submitted to the board of directors and transferred to the executive management for their comment and feedback. Accordingly, the board of directors shall issue directives in order to address the comments on the report.

2/7 Responsibility towards Shareholders and Other Parties

The board of directors shall have the primary responsibility towards the shareholders and all customers of the bank or institution for its performance and results. In addition to the legal responsibilities that may be assumed by the board of directors due to cases of violation and negligence, the following are the most significant responsibilities of the board of directors towards the shareholders and other parties:

- Soundness and creditability of end of year financial statements of the bank's or the institution's business.

- Application of all articles of the bank/ institution's statute. One of the most important articles is conducting licensed activity, including terminating and replacing members of board of directors during their term, nominating the new members, taking into account the maximum limit for participation, requirements of increasing or decreasing the capital, distributing profits or dealing with losses and all other statutory articles in compliance with QCB's instructions framework.

- Transparency, disclosure and objectivity of all significant issues that may affect the performance, business results and achieving objectives of the bank or institution accurately, where appropriate.

- Disclosure of obligations, transactions of related parties and conflict of interests, as well as all other requirements of the local laws and international standards.

2/8 Board Responsibility towards QCB

QCB considers board of directors to be primarily responsible for the strong financial position, protection of depositor and investor rights, soundness, creditability and transparency of financial statements and data submitted to QCB.
by the bank/ institution, and compliance with all laws and instructions issued by QCB and other formal authorities of the State.

3- Roles and Responsibilities of Executive Management

The executive management shall assume the following responsibilities:

3/1 Assist in Setting up and Development of Strategies, Objectives and Policies
3/2 Assist in Forming the Organizational Structure
3/3 Conduct Transactions and Implement Policies
3/4 Submit Reports to the Board of Directors
3/5 Preparation of Financial Statements
3/6 Development of Professional Aptitude and Skills
3/7 Responsibility towards Internal and External Auditors
3/8 Responsibility towards QCB

3/1 Assist in Setting up and Development of Strategies, Objectives and Policies

The executive management should provide the board of directors with necessary information, opinions and reports on the achievements, the field and the operational expertise, current and future risk assessment, and studies on the market and external conditions. Additionally, the executive management should pursue professional transparency, objectivity and honesty.

3/2 Assist in Forming the Organizational Structure

The executive management should periodically provide the board of directors with information, reports, recommendations and expertise on needs to organize the activities and implement policies of the board of directors, operational requirements and internal control, and methods of the internal protection and overcoming obstacles in implementation. Therefore, executive management should also comply with objectivity in activating the implementation process.

3/3 Conduct transactions and implement policies

The executive management including the chief executive officer or the general manager, shall be responsible to the board of directors for conducting activities of the bank/ institution according to policies, plans, procedures and regulations set
by the board of directors. Accordingly, the executive management should perform the following:

- **Constitute executive committees and delegation of authorities:**
  The chief executive officer or the general manager shall utilize the powers and authorities delegated by the board of directors to constitute committees. The committee shall consist of chief executive officers to manage the executive operations in accordance with work requirements and to delegate some authorities to such committees, where appropriate, to facilitate daily work.

- **Set programs, procedure and issue executive instructions:**
  The executive management shall set various programs, procedures and instructions in order to control, issue, supervise and review the implementation process for an effective internal control and methods of protection. Thereafter, the executive management should submit such programs and procedures to the board of directors for approval. Additionally, it should continuously evaluate and develop such programs and procedures and address the shortcomings in the light of the requirements and results of implementation and of the directives set by the board of directors.

- **Performance evaluation and follow up:**
  It includes following up the implementation by all executive departments and divisions using the daily and periodical reports issued by the operational systems that have been prepared by executive departments' staff. Such reports should cover different activities and various risks of the bank or institution. Using such reports, the chief executive officer shall rapidly assess the compliance of the implementation, as the executive management should evaluate the risk management and performance, address and call to account for any violation and deviation, evaluate the assets, and rationalize expenditures and so on. The executive management should also verify the adequacy and soundness of information systems, the comprehensiveness and accuracy of executive reports, the safety of documentations and papers, the effectiveness of procedures of the internal control and protection in all aspects, such as; checking and auditing daily transactions in an independent manner and separating between the interrelated functions and tasks on one hand and other procedures on the other hand, such as; the recording the transactions, accounting, the financial control, error detection and correction, codes and
authorities of funds movement, adequate and valid insurance on assets of the institution, the deposited and transferred cash, and other known procedures.

3/4 Submit Reports to the Board of Directors

The executive management shall be responsible for submitting several types of periodical reports to board of directors and its committees. The following are the main three types of reports:

- Financial and qualitative periodical reports on result of different activities, evaluation of assets and risks, actual and estimated budgets in the bank/institution in accordance with requirements of the board of directors and its committees so as to meet the needs of their supervisory tasks and authority in making decisions.

- Significant additional reports that should be submitted to the board of directors or its committees by the executive management in order to be notified of any necessary information or data necessary for the bank's or institution's performance and requirements, risks, or important initiatives and information on the external market conditions and influences.

- Business development reports that include the executive management's recommendations on evaluation and development of the executive policies and procedures, the bank's or institution's future requirements including the new services and techniques in the light of the results of performance evaluation, potential risk detection and competitive market conditions. The executive management should be professionally objective, transparent and honest while submitting information, reports and recommendations to the board of directors.

3/5 Preparation of Financial Statements

The executive management shall be responsible for preparing the financial statements for banks and institutions during the year and the end of year financial statements with all required details, information and disclosures. The chief executive officer or the general manager shall be directly responsible, towards the board of directors, for the valid and sound end of year financial statements. However, the executive management shall be responsible towards the board of directors for results and developments of the activities.
3/6 Development of Professional Aptitude and Skills
The executive management should aim at:

- Developing functional skills by conducting continuous training and professional symposiums inside and outside Qatar in order to keep up with the recent developments and techniques.
- Setting convenient charter of practical behavior, taken from professional and moral culture.

3/7 Responsibility towards Internal and External Auditors
The executive management should facilitate the external and internal auditing tasks, cooperate with and provide the auditors with all information, data and documents they require for auditing purposes, taking into account the accuracy and transparency. Accordingly, it should comment and furnish feedback on auditing notes and questions, and rapidly respond to auditing results by correcting violations, addressing weakness, deficiency and shortcomings, and improving performance.

3/8 Responsibility towards QCB
The executive management shall be responsible towards QCB on the following issues:

- Compliance with all laws and instructions of QCB.
- Evaluating and hedging risks, and improving the performance, business results and work discipline.
- Preparing and submitting all periodical, correct, and accurate reports and financial statements to QCB in time.
- Facilitating QCB tasks during the on-site examination on the bank or institution, cooperating with and providing the examination team with all required information and documents.
- Transparency and creditability while dealing with QCB.
4- General Provisions

- All banks and financial services institutions should review their organizational structure, authorities, obligations and responsibilities assumed by the board of directors and executive management in conformity with the abovementioned instructions. Accordingly, they should make all the necessary amendments within six months as of the issuance date of the instructions, and should submit a written undertaking to QCB that they are complying with all instructions on corporate governance.

- In extreme cases, such as vacancy of position of the chief executive officer, the general manager or any other key administrative positions, or in any other circumstances wherein the board of directors violates any of the instructions mentioned in items no. (2) and (3), thereof, QCB's approval should be obtained and a written statement on violations, durations of violation etc, should be submitted to QCB.

- If banks or financial services institutions do not comply with the abovementioned or are repeatedly violating such instructions, QCB shall, according to its estimation, apply the article no. (127) of QCB Law.

B- 195Core Principles for Banks' Remuneration Policy/System

In accordance with the Financial Stability Board (FSB) and Basel Committee on Banking Supervision on Principles for Sound Compensation Practices in financial institutions, to enhance corporate governance responsibility to design and oversee compensation policy, and considering sound controls based on transparency, subjectivity and measurement of performance linked to achieve long term objectives through measuring current and future risks, QCB decides that banks shall comply with the following principles and controls when designing remuneration system and procedures for the bank and its group:

1- The bank's board of directors shall design and oversee policy and standards, in accordance with the principles and guidelines given below, to evaluate compensations of board members, chief executive officers, directors, and employees of the bank. The compensation system shall not be controlled by the chief executive officers or the management team. The relevant board members

and employees shall have independence and expertise in risk management and compensation.

2- The bank's board of directors shall monitor and review the compensation system to ensure the system operates as intended. The Board should regularly review the compliance with designed policies and procedures. Compensation outcomes, risks, measurements, and risk outcomes should be regularly reviewed for consistency with intentions.

3- Staff engaged in financial control, internal control, risk measurement and control, and compliance shall be independent, have appropriate authority, and be compensated in a manner that is independent of the business areas they oversee.

4- Compensation shall be adjusted for all types of risk. Two departments that generate the short-run profit but take different amounts of risk should not be treated the same by compensation system. Risk adjustments should account for all types of risk, including difficult-to-measure risks such as liquidity risk, reputation risk and cost of capital.

5- Compensation outcomes must be symmetric with the risk outcomes and the overall performance of the bank. Employees' incentive payments should be linked to the contribution of the individual and business to such performance.

6- Compensation payout schedule shall be sensitive to the time horizon of risks. Profits and losses of different activities of a bank are realized over different periods of time. Variable compensation payments should be deferred accordingly. Payments should not be finalized over short periods where risks are realized over long periods.

7- The mix of cash, equity and other forms of compensation shall be consistent with risk alignment. There should be rules to regulate such system depending on the employee's position and role.

8- Banks shall disclose clear, comprehensive and timely information about their compensation practices. Members of board of directors' compensation payments must be disclosed in accordance with Commercial Companies Law and QCB instructions in page no. (247).
Second: Bank Senior Appointments

1- Appointment of General Manager/Chief Executive Officer of the Bank

All banks operating in the State of Qatar should obtain the QCB's prior approval for appointing the general manager or the chief executive officer in the bank, provided that their resumes are sent with the approval application in conformity with the personal questionnaire in annexes no. (51) and (55), duly attached with personal documentations and certificates of qualifications, training courses and practical experiences. However, the position of the bank's general manager should not be kept vacant.

2- Bank Senior Appointments

2/1 QCB prior approval should be obtained for appointing senior staff to the vacancies indicated below:

- Deputy general manager or chief executive officer.
- Assistant general manager or chief executive officer.
- Any officer or manager who reports directly to the general manager.
- Compliance officer
- Internal auditing manager
- Shari’a auditing manager

The personal documentations and certificates of qualifications, training courses and practical experience should be attached to the personal questionnaire annexes no. (51) and (55) duly filled in and submitted to QCB.

2/2 197 With reference to QCB’s instructions on Appointment of Senior Staff, the following shall be added:

A- Banks shall consult a specialized international bureau to conduct a comprehensive survey and report on senior candidates to the bank which includes their qualifications, efficiency, ability and integrity, attested by their previous

196 Refer to circular no. (30/2007) dated 22/2/2007 (National Banks).
employers. Banks shall then provide QCB with a copy of these report along with an application for no objection for appointment to QCB.  

B- Banks shall provide QCB with names of the specialized international bureaus approved by the bank’s board of directors for this purpose.

3- Movement of Senior Staff  
If there are movements among the senior officers between different departments of the bank or its branches, QCB should be immediately notified, indicating the officer's name, movement date, and old and new titles. Upon termination of bank executives whose appointment has been approved by QCB, QCB should get written notification two weeks prior to termination date, with the executive's name, title and termination date.

4- Official Vacations and Tasks of the General Manager/Chief Executive Officer  
All banks operating in the State of Qatar should submit written notification to the Director of Supervision and Control Department when the general manager/chief executive officer is on vacation or on official mission. Notifications must include when vacation/formal mission shall start and end and name of the acting manager in charge.

5- Employment of Relatives  
QCB observed that some employees at certain banks were appointed upon recommendation of their relatives who work in the same banking institution ignoring the essential recruitment standards such as experience and work efficiency when selecting those persons.  
In compliance with Article no. (128) of QCB Law, the instructions on corporate governance for banks and financial institutions item no. (2/1) page no. (277) thereof, and for banks' own benefit, banks must not recruit any person who is of first degree kinship to existing staff members, and adopt necessary standards, and conditions regulating employment of relatives of other categories to avoid conflicts of interests. These instructions are effective from December 2007.

198 Refer to circular no. (244/2007) dated 17/12/2007.
Banking Managerial Risk

Third: Authorized Signatories

1- Statements and Correspondences

- The bank's correspondence with QCB should be signed by the bank's general manager/chief executive officer. In case of absence of the general manager, correspondence should be signed by the deputy general manager/chief executive officer. QCB shall not consider letters that are not signed by the general manager/chief executive officer or by his deputy in case of his absence.

- Statements of banks reported to QCB should be signed by the general manager/chief executive officer or the authorized signatory, and sent to Supervision and Control Department.

2- 199Names and Signature Forms of the Board of Directors and General Management Members

It has been noticed that some banks have not provided QCB, on an annual basis, with the authorized names and signature forms of the board of directors, general management and branches operating in Qatar, and QCB have not been notified of any changes on time in pursuance with paragraph no. (2) in the “Instructions to Banks - 2009”

Accordingly, banks should comply with above-mentioned instructions. Additionally, QCB should be provided with names and signature forms of the authorized signatories that have been approved for certificates of "to whom it may concern" issued by the bank to customers and for accounts’ statements to be authenticated by QCB.

Banking Managerial Risk

Fourth: Internal Auditing

1- All banks operating in the State of Qatar should establish internal auditing departments in conformity with standard practice in order to cover all activities of the bank in terms of auditing, reviewing and evaluating all banking operations, credit facilities and various administrative and financial issues. The Internal Auditing Department should also submit recommendations and express opinions with regard to the computer systems and procedures, ensuring their effectiveness, compliance with applicable policies and systems approved by the board of directors or the Superior Management of the foreign banks' branches, and authorized officers' duty respect and are committed to the delegated authority.

2- The Internal Auditing Department should be directly reporting and responsible to the board of directors. Subsequently, reports issued by the Internal Auditing Department shall be directly addressed to the chairman of board of directors or to the audit committee of board of directors for the national banks or to the Superior Management and general manager for branches of the foreign banks.

3- The head and staff of the Internal Auditing Department shall be directly appointed by the auditing committee of the board of directors for the national banks or by the head offices for branches of foreign banks. Accordingly, their salaries and allowances should be determined. The bank's management should not interfere either in the functions of the internal auditing department or in tasks of the officer.

4- The Internal Auditing Department should follow up and address the auditors' reports of the bank and the general management for the foreign banks, and submit the inspectors' reports to QCB.

5- Any other tasks as required by the board of directors.

293 Refer to item no. (7) in page no. (294).
Some banks outsource part of their subsidiary services to other service providers for the purposes of cost reduction, service improvement, or saving time for main services, such arrangement may involve risks due to factors like service provider's inefficiency, lack of supervision, possibility of access to customer secret data, in addition to legal risks. All banks must accordingly comply with the following regulations:

1- QCB's no objection must be obtained before entering into any contract of outsourcing with other entity whether such entity is inside or outside the group. The applicant must provide QCB with outsourcing (business case) details, experience of the service provider, related risks and controls, and the internal guidelines proposed to mitigate risks.

2- The board of directors and the executive management are responsible for all control systems and the relation with the service provider.

3- The outsourcing agreement must include the effective legal provisions concerning secrecy of information. Such provisions must be applicable to their partners and staff.

4- The outsourcing agreement must guarantee that internal and external auditors and QCB inspectors have full access to the data and carry out an onsite inspection in the service provider's workplace, if necessary.

5- If the service provider's headquarter is outside the country, it should confirm that there are no legal or regulatory restrictions imposed on internal or external auditors, or QCB inspectors to access data. Such service provider should notify QCB if there are such kinds of restrictions.

6- Contingency plans should be adopted for business continuity purposes if the contract has to be abruptly terminated, such as finding alternative provider or using internal service provider.

7- The internal auditing is core to banks' functions and as such may not be outsourced except in extraordinary circumstances and for short period of time to provide for urgent requirements. The services of internal auditing manager may not be extended to any external entity for any reason.
These instructions are effective from August 2006 and any other contradicting instructions or exceptions shall be null and void.
Banking Managerial Risk

Sixth: Consolidated Supervision of National Banks, Their External Branches and Subsidiaries

1- Definitions:

QCB: Qatar Central Bank

The Bank: National bank (Parent Company)

Subsidiary: Company or institution whose decisions, operations and financial business are permanently managed by the bank through at least one of the following basis:

A- The bank subscribes to the subsidiary's capital by more than 50% which grants such bank majority voting in making decisions.

B- The bank subscribes to the subsidiary’s capital by 50% or below. To achieve the overwhelming majority to make decisions, at least on of the following means should be adopted:

- The bank's voting power is more than 50% if the subsidiary's shareholders waived their voting rights to the bank according to binding agreements, laws, or rules.

- The bank has the authority to control the subsidiary's decisions and operations according to binding agreements, laws, or rules.

- The bank is authorized to appoint or dismiss the majority of the subsidiary's members of board or whoever controls its management in such away that grants the bank control over its decisions and operations.

- The bank has the power to control the voting power of the subsidiary's board of directors or whoever controls its management by any other way or in such away that it grants the bank control over its decisions and operations.

Branch Abroad: A branch of the bank operating outside the state of Qatar.

Banking Group: The bank, its branches abroad, and subsidiaries inside and outside Qatar.

Host Regulator: Authority that regulates the bank's branch or subsidiary outside Qatar.
Consolidated Financial Data: The unified data for the bank and its group (the group financial data).

Interrelated parties of common interest:
1- Members of board of the bank or the subsidiaries
2- Main owner shareholders of the bank or the subsidiaries who subscribe to the bank’s or the subsidiaries capital by minimum 5% whether in their own capacity or through their minor children or their wives or the companies in which they subscribe to the capital by a minimum 50%.
3- Key employees of the top management in the bank or the subsidiary such as; general manager, deputy general managers, executive managers, auditing manager, advisors, and others who are involved in decision making.
4- Sister companies in which the group subscribes by minimum 20%.
5- The external auditors of the bank or the subsidiary.

2- Corporate Governance

The instruction of the corporate governance stated in banking instructions shall be applied on the branches abroad and subsidiaries inside and outside Qatar in addition to the following instructions:

2/1 Roles and Responsibilities of the Bank's Board of Directors:

2/1/1 Planning objectives, implementing and developing work strategies and policies:

The board of the bank, before taking decision to establish branch abroad or subsidiary, or subscribe to the capital of companies inside or outside Qatar, should determine the objectives of such branches and companies in line with the bank’s general goals, strategies, and policies. Such objectives must be compatible with the bank's financial, technical, and administrative capabilities to expand abroad, in addition to the targeted revenue and risk levels which can be controlled provided that the supervisory requirements and instructions inside and outside Qatar are complied with.

- The board of directors of the bank should adopt clear written policies, strategies, and budgets for each branch or subsidiary abroad according to its defined goals and to the economic, market, and legal environment. Banks should take into consideration the difference between a branch
abroad and subsidiary owned or subscribed by the bank as a legal entity separated from the bank and the equities of minority shareholders as well.

- The board of directors of the bank should ensure that the managements of the branches and the subsidiaries abroad understand and implement their defined goals, policies, strategies, and budgets. The board should assess the performance of such branches and subsidiaries and the achievements of their management according to the defined goals and policies. The board should advise such entities to develop and update their policies, strategies, and work plans towards achieving the defined goals.

2/1/2 Formation of board of directors in subsidiary:

- The bank should be represented on the board of the subsidiary in such away that the bank shall have the power to control the decisions of the board of the subsidiary. Members representing the bank in the subsidiary's board shall act as a link between the board of the bank and of the subsidiary and shall act as a watchdog for the board of the bank to monitor the subsidiary's performance, and its compliance with the policy and instructions of the board of the bank.

- The board of the bank should ensure that their representatives on the subsidiary's board are well qualified and experienced, act independently and are given sufficient time to carry out their assigned duties.

2/1/3 Formation of committees, and delegation of authority:

The board of the bank should review the formation of the subsidiary's administrative and executive committees in accordance with outlined system and responsibilities. The board should supervise the formation and the performance of such committees through its representatives on the subsidiary's board.

2/1/4 Supervision of operations and assessment of performance and risks:

The bank's board must periodically assess operations and performance in the branches and the subsidiaries around the year and detect any violations in budgets, policies, and strategies and impose penalties. In this respect, banks should consider the following:

- The bank's board should decide the proper system for performance assessment that should be adopted by its committees, and its
representatives on the subsidiary's boards, the executive committees, and the internal auditors.

- The bank's board should ensure that the compliance officer is effectively carrying out his duties to detect violations in branches and subsidiaries and report regularly to the executive management and the bank's board. The bank's board should ensure that compliance officers are independent and unbiased and report regularly to them.

- The board should ensure the adequacy and efficiency of the reports and the reporting systems used by branches abroad and subsidiaries to committees and departments of the bank during the year. Such reports should at least cover the following:
  - Performance of the boards of the subsidiaries and branches abroad.
  - Information and indicators of performance assessment, banking risk analysis and assessment.
  - Effectiveness of internal control, operating systems, and risk management.
  - Exceeding overall limits and violations of policies and budgets of the board of the bank, the reasons thereof and assigning responsibility.
  - Asset quality and rating.
  - Defaulted loans and the appropriate actions and precautions.
  - Law suits, legal and taxes issues with concerned authorities.
  - Rules and regulations of host regulators.
  - Employees and managers performance, bonuses, incentives, penalties, promotions, resignation, and dismissal.
  - Any extraordinary incident which could risk or affect the company's reputation.

2/1/5 Appointing internal auditor and its control:

The board of the bank should ensure that its branches abroad and subsidiaries have highly qualified, experienced staff in internal auditing departments which apply inclusive programs and guidelines. The internal auditor should carry out the functions on unbiased and independent basis and directly report to the internal auditing committee formed by the board and the internal auditing department in the bank.
2/1/6 Appointing External Auditor:
The board of the bank should appoint external auditor to review the operations of the bank, its branches abroad, and subsidiaries according to item (1/4), page no. (351) the instructions regarding the external auditor.

2/1/7 Responsibility of the board to the shareholders and other parties:
The board of the bank is responsible for transparency and credibility to disclose any crucial issue, irregular events and risks, or statements of branches abroad and subsidiaries.

2/1/8 Responsibility of the board towards QCB:
QCB considers the board responsible for the performance of branches abroad and subsidiaries, their financial statements, and their risk management. The board is also responsible for transparency, credibility, and accuracy of the financial data of these branches and subsidiaries, the bank's financial statements and end of the year consolidated statements submitted to QCB. The board is responsible for reporting to QCB any extraordinary incident occurring in any branch abroad particularly any of the following issues:

- Any adverse view, or important remarks made by the external auditor during the year.
- Significant change to any of the financial indicator.
- Default in payment of key loans or major credit concentrations.
- Depreciation of the value of assets.
- Freezing or imposing restrictions on any of the assets or balances
- Failure or disruption in operations or IT systems.
- Any infringement of law or charges brought on the members of the subsidiary's board or the executive managers in branches abroad and subsidiaries.
- Resignation of any board member, executive director, internal auditor, or compliance officer
- Lawsuits filed against branches abroad and subsidiaries, in addition to legal risks and taxes.
- Any supervisory violations or remarks made by the host regulator or any other concerned authority in the host country.
2/2 Roles and Responsibilities of the Bank's Executive Management

The executive management of the bank carries out the following responsibilities:

- Monitoring the performance of branches abroad and subsidiaries, analyzing and measuring risks both individually and collectively, and reporting about the relevant recommendations and remarks to the board.
- Assigning manager, division, or department of the bank to follow up the performance of branches abroad and the subsidiaries and report to the board of the bank in accordance with the required regulatory rules.
- Assigning one of the managers who is responsible to follow up the performance of branches abroad and subsidiaries to act as a link between QCB and the branches abroad or the subsidiaries so as to facilitate QCB offsite and onsite supervision.
- The executive management shall be responsible for the correctness of all financial data and consolidated financial statements submitted to QCB.
- The executive management shall report to QCB about any extraordinary incidents that may occur in the branches abroad and subsidiaries as indicated in paragraph no. (2/1/8), regarding the responsibility of the board towards QCB.

3- Concentration Risks

3/1 Credit Risks for Parties of Interrelated Interests within the Banking Group

3/1/1 The following credit concentration shall be applied according to the aggregate of credit facilities obtained by a concerned party from the banking group under the same conditions mentioned in the instructions to banks:

The ratio of the maximum credit facilities to the total of banking group’s capital and reserve (Tier1) shall be as follows:

- The credit facilities granted to the borrower group of the board member of the bank (and his representative in the board, with exception of the government’ representatives) or the subsidiary or his relatives may not exceed 7% of the subsidiary's capital.

- The total credit facilities given to borrower groups for all members of board of the bank or the subsidiaries. (35%)
- The total of the credit facilities given to relatives of members of the board of the bank or the subsidiaries collectively. (20%)
- Credit facilities and investments given to borrower group of one associate company. (25%)
- Credit facility given to main shareholder of a bank or subsidiaries. (10%)
- Total credit facilities given to all parties with interrelated interest for the group. (100%)

3/1/2 The bank should comply with the ratio of the credit concentrations of parties of interrelated interest as mentioned in the instructions to banks to the bank's capital and reserve, only in case of facilities offered by the bank.

3/1/3 No employee or manager in the banking group may obtain any credit facility except loans for their personal purposes in accordance with the personnel executive regulations approved by the board of the bank or the subsidiary.

3/1/4 Credit facilities may not be granted to the external auditors of the group.

3/1/5 Granting facilities, investments, and other transactions with parties having interrelated interest should be on an equal basis as to those of other customers and in accordance with the group's main policy and general customs and norms.

3/2 Customer's Credit Concentrations

3/2/1 The following instructions and ceilings of credit concentrations of customers and their borrower groups should be implemented as mentioned in the instructions book, on an aggregate basis i.e. the customer's total facilities obtained from the banking group.

The ratio of the maximum credit facilities to the total of banking group's capital and reserve shall be as follows:

- Credit facilities granted for the borrower group of a single customer. (20%)
- Credit facilities and investments for the borrower group to a single customer. (25%)

3/2/2 The bank shall comply with customer credit concentrations ratio as indicated in the instructions to banks concerning the ratio of the bank's capital and reserve to the facilities they obtain from the bank only.
3/3 Credit Concentrations at Banks

The instructions and ceilings of credit and deposit concentrations at banks and financial institutions shall be implemented as given in the instructions to banks, in case of the group of the bank and to be calculated on an aggregate basis i.e. the ratio of total concentrations of the group of the bank at banks and financial institutions to the total capital and reserve of the group. While the bank's concentrations only at banks and financial institutions same concentration ratio shall be applied according to a ratio to the bank's capital and reserve.

3/4 Investment Risk Concentrations

3/4/1 Instructions and ceilings on concentrations for investment risks mentioned in the instructions to bank shall be applied to the whole investment of the group on an aggregate basis i.e. the ratio of the total investment of the group to its capital and reserve, such investments are:

- Investments in Equity Instruments.
- Investments in Debt Instruments and Sukuk.
- Investment in Associates.
- Investment in real state for Islamic banks only.

3/4/2 Same instructions, definitions, and exceptions mentioned in the instructions to banks shall be applied on the collective ceilings stated in paragraph (3/4/1).

3/4/3 The ratio of investment ceilings to the banks capital and reserve mentioned in paragraph (4/3/1) shall be applied only on the bank's investments, while the bank's investments in its subsidiaries are not included.

3/5 Real Estate Financing Concentrations

3/5/1 The limit of the total real estate finance for all customers of the group inside and outside Qatar shall be the same ratio as mentioned in page no. (196) on a consolidated basis (These ratios are based on the group's capital and reserves).

3/5/2 The real estate finance granted by the group to customers inside Qatar shall be subjected to the same controls that have been put on the real estate finance ratio as mentioned in page no. (198). The real estate finance granted outside Qatar shall be subject to controls mentioned in paragraph no. (2) under item (Fifth) in page no. (200).
3/5/3 The total real estate finance granted by the bank shall be subjected to the same limit mentioned page no. (196) calculated according to the ratio of the bank’s total capital and reserves.

3/6 Credit Concentrations and Transactions between the Bank and the Subsidiaries

3/6/1 The subsidiaries' funds invested in its capital, credits, deposits and other kinds of investment may not exceed the following ceilings to be calculated according to a ratio of the banks capital and reserve:

- Funds invested by a single subsidiary (25%)
- Funds invested by all subsidiaries (40%)

3/6/2 All kinds of financial and banking transactions and deals made between the bank and its subsidiaries or among each others should not have any preferential conditions, prices or special procedures and to be made in accordance with the banks policies and procedures as in normal cases. The board of the bank should adopt proper procedures and administrative rules and controls that guarantee achievement of this objective.

4- Assessment of Debts and other Assets

4/1 Banks should provide QCB with information on the assessment of debts and other assets and provisions in branches abroad and subsidiaries by November the first, each year as a deadline.

4/2 In case the provisions assessed by QCB exceeds those of the branches abroad and the subsidiaries for the debts and other assets, while such increase can not be indicated in the records for regulatory or legal purposes, the bank should record such increase in its unconsolidated financial statements and records as other provisions and include it in the group total provisions in the consolidated financial statements.

5- Capital Adequacy Ratio

The bank and its branches and the group as a whole should apply Basel II capital adequacy ratio. The whole group should all times comply with the minimum ratio stated by QCB as of the end of 2006. QCB’s instructions relating to Basel II should be adopted while calculating capital adequacy ratio.
6- Liquidity Risk

The liquidity risk management in banks and in the whole group should implement the following:

- Comply with QCB mandated liquidity ratio.
- Maturity gap management (liquidity according to maturity ladder).
- Emergency liquidity management and contingency plans.

7- Other Risks for Assets and Provisions

The bank should manage other assets and make provisions for risks such as; foreign exchange risks, market and return risks, financial derivatives, and other risks use hedging tools, both on the bank level and on the whole group.

8- Risk Management

The bank should adopt policies and procedures for risk management for the whole group in conformity with QCB’s instructions on sound practices for risk management.

9- Other Issues

9/1 The bank should obtain QCB’s approval on the following matters:

- Ownership of subsidiary inside or outside Qatar.
- Open new branches outside Qatar
- Open new branches or representative offices for the subsidiaries inside or outside Qatar.
- Conduct any new business through the subsidiaries or branches abroad other than the business licensed since the beginning of activity or owning the subsidiary.
- Increase of the banks share in the subsidiary’s capital.

9/2 QCB requirements for subsidiary's ownership or opening branches abroad

- The bank has good financial solvency indicators on the group level.
- The bank has good supervisory indicators from QCB and host regulator for the subsidiaries and branches abroad.
• The bank complies with the supervisory ratios and ceilings and has not committed any violation or have any regulatory remarks from QCB or the host regulator for the subsidiaries and branches abroad.

• The host regulator adopts the international standards and principles of consolidated supervision, and cooperates with QCB in information sharing and supervisory exchange visits.

All banks are required to be rectify their positions to implement the above-mentioned instructions and deal with any violations by the end of the year (31/12/2006). Item ")'(9) Other Issues" should be complied by as from October 2006.

10- Consolidated Statements and Reports for Bank and its Group

With reference to QCB’s instructions on consolidated supervision of national banks, their branches abroad and subsidiaries, and QCB’s desire to follow up compliance with the prudential ratios and ceilings on a consolidated basis according to these instructions, each bank shall monthly furnish QCB with the following statements and reports for each branch abroad and each subsidiary in addition to a consolidated report for the group, branches and subsidiaries within a deadline of the 15th day of every month:

• Liquidity Ratio Report
• Credit Ratio Report
• Real estate Finance Ratio Report
• Financial Investments Ceilings Report