



# **CORPORATE GOVERNANCE RULES AND REGULATIONS 2018**

**Royal Monetary Authority of Bhutan**

## Contents

PART 1: PRELIMINARY .....	1
PART 2: BOARD OF DIRECTORS AND SENIOR MANAGEMENT .....	2
Board's Oversight Responsibilities of Senior Management .....	4
Accountability of the Board of Directors .....	5
Composition of the Board .....	5
Independent Directors .....	6
Permanent Invitees to the Board.....	8
Appointment and Removal of Directors.....	8
Tenure of Directors.....	10
Board Orientation and Professional Development .....	10
Board Meetings .....	11
<i>Frequency and Attendance</i> .....	11
<i>Minutes of the Board Meetings</i> .....	11
Chairperson of the Board.....	12
Board Audit Committee .....	14
Performance Evaluation of the Board .....	15
Conflicts of Interest .....	15
Senior Management.....	16
PART 3: THE RISK MANAGEMENT FRAMEWORK .....	20
Risk Management Framework and Culture .....	21
The Risk Management Functions.....	22
Risks Monitoring, Controlling and Communication.....	23
Compliance Function.....	24
Internal Audit.....	25
Compliance Monitoring and Reporting.....	26
SCHEDULE I: CODE OF ETHICS OF REGULATED ENTITIES .....	29
SCHEDULE II: FIT AND PROPER QUALIFICATIONS .....	35

## **PART 1: PRELIMINARY**

1. These Rules and Regulations are issued in pursuant to Section 202 of the Financial Services Act of Bhutan 2011, and shall be read in conjunction with the additional requirements under the Financial Services Act 2011, and where applicable the Companies Act of Bhutan 2016.

### **Title, Commencement and Application**

2. These Rules and Regulations shall:
  - 2.1 be called the Corporate Governance Rules and Regulations, 2018, hereafter referred to as CGRR 2018;
  - 2.2 come into force from the 1<sup>st</sup> Day of July 2018; and
  - 2.3 be applicable to Regulated Entities as defined in CGRR 2018.

### **Purpose**

3. The purpose of the CGRR 2018 are:
  - 3.1 to promote sound corporate governance in the regulated entities under the supervision of the Authority through adoption of high standards of corporate governance principles and practices; and
  - 3.2 to have regulated entities implementing a corporate governance framework proportionate to its size, its activity, and its complexity. Regulated entities are required to self-assess their corporate governance framework to achieve compliance with the CGRR 2018. The Authority shall assess the appropriateness of the corporate governance framework implemented by the regulated entities.

### **Interpretation**

4. The power to interpret any provision of the CGRR 2018 is vested with the Authority.

### **Amendment**

5. The CGRR 2018 may be amended in part or in whole, by the Authority.

### **Supersession**

6. The CGRR 2018 shall supersede the Corporate Governance Regulations, 2011.

## **PART 2: BOARD OF DIRECTORS AND SENIOR MANAGEMENT**

7. The board of directors shall have the ultimate responsibility for the regulated entity's business strategy and financial soundness, key personnel decisions, internal organizational structure, governance, risk management and compliance obligations.
8. The board of directors shall understand that its primary responsibility is to protect the interests of the regulated entity, which shall include legitimate interests of depositors, policyholders, shareholders and other stakeholders.
9. The board of a regulated entity shall structure itself in terms of leadership, size and the use of committees to effectively carry out its oversight roles and other responsibilities. The organizational rules and procedures shall be described in the by-law set by the board, which shall be periodically reviewed and revised.
10. The board of directors may delegate the functions to its committees or the senior management, but the board shall not abrogate its responsibility for the functions delegated. The board shall establish proper mechanisms for delegating the functions and monitoring them.

## **Main Responsibilities of the Board of Directors**

11. The main responsibilities of the board of directors are to:

- 11.1 review and approve regulated entity's short term and long-term business strategies and policies;
- 11.2 review and approve the regulated entity's organizational structure and the division of responsibilities between the board and senior management;
- 11.3 define the main responsibilities of risk management, compliance, and internal audit functions;
- 11.4 establish the regulated entity's risk strategy, risk appetite, and risk tolerance;
- 11.5 oversee the regulated entity's adherence to the risk strategy, risk appetite, and risk tolerance;
- 11.6 set regulated entity's corporate culture and values that establish high ethical standards and integrity, professional conduct for the board of directors, senior management and the employees;
- 11.7 oversee the implementation of the regulated entity's governance framework and periodically review it in the light of changes to the regulated entity's size, complexity, business strategy, geographic network, and to the regulatory requirement;
- 11.8 ensure that transactions with related parties are reviewed to assess risk and are subject to appropriate restrictions (e.g. by requiring that such transactions be conducted on arm's length terms) and that corporate or business resources of the regulated entity are not misappropriated or misapplied;

- 11.9 adopt and oversee the implementation of key policies related to the regulated entity's capital adequacy assessment, capital and liquidity plan, management of the risk, compliance policies and obligations, and the internal control systems;
- 11.10 ensure that the CEO, other members of senior management and heads of the control functions are appointed with relevant qualifications, competencies, experience and integrity;
- 11.11 develop a clear and rigorous process for identifying, assessing and selecting directors. In addition, the board is required to have an appropriate succession planning of board of directors; and
- 11.12 observe and oversee the enforcement of a *Code of Ethics*, given in the *Schedule I*.

### **Board's Oversight Responsibilities of Senior Management**

12. The board of directors' oversight responsibilities of the senior management shall be to:
- 12.1 monitor that the senior management's actions are consistent with the strategies and policies approved by the board, including the risk appetite;
- 12.2 meet regularly with the senior management;
- 12.3 question and critically review explanations and information provided by senior management;
- 12.4 assess the knowledge and expertise of senior management given the nature of the business and the regulated entity's risk profile;
- 12.5 ensure that an appropriate selection process and succession plan is in place for the CEO and senior management positions; and

12.6 assess the performance of the CEO annually and submit the performance report to the Authority.

### **Accountability of the Board of Directors**

13. The board of directors is collectively accountable for the governance of the regulated entity. The directors shall be individually accountable for his or her actions as a member of the board. A director must exercise:

13.1 “*duty of care*”: he or she acts on an informed and prudent basis with respect to the regulated entity; and

13.2 “*duty of loyalty*”: he or she acts in good faith in the interest of the regulated entity, avoids acting in his or her own interest, or in the interest of another individual or group, or at the expense of the regulated entity, and its stakeholders (shareholders, depositors, policyholders, other beneficiaries).

14. In case of governance failure, the Authority shall take appropriate remedial actions ranging from changing the existing policies and practices, or requiring the replacement of the Chairperson, directors, or CEO as per Section 38 of the Act.

### **Composition of the Board**

15. The board of directors of a regulated entity shall comprise members with a balance of diverse expertise, skills, and experience to ensure effective governance and oversight of the regulated entity.

16. The board of directors shall have:

16.1 a range of knowledge and experience in relevant area, including, but not limited to business, management, corporate governance, risk management, financial analysis, financial reporting, information technology, regulation, and strategic planning;

- 16.2 varied backgrounds to promote diversity of views;
- 16.3 understanding of local, regional and global economic, legal and regulatory environment;  
and
- 16.4 an attitude that facilitates communication, collaboration and critical debate in the decision-making process.
17. The board of directors of a regulated entity shall have no more than seven directors including the Chairperson of the board and the CEO, of which at least two shall be independent directors.
18. The CEO shall become the member of the board upon appointment as the CEO.
19. In order to provide effective oversight over senior management, there shall not be an executive director on the board of regulated entity other than the CEO.
20. In order to maintain fair competition and level playing field, and to avoid conflicts of interest:
- 20.1 A director or an employee of one regulated entity shall not be permitted to serve as a director on the board of another regulated entity; and
- 20.2 Not more than one member of a family, as defined in CGRR 2018, or an associate (partner, employee, director) shall be in the board of a regulated entity.

### **Independent Directors**

21. An independent director is a non-executive member of the board who, apart from receiving director remuneration do not have any other material pecuniary relationship or transaction with the regulated entity, its promoter, its management or its subsidiary and is not under any other undue influence, internal or external, political or ownership, that would impede his or her exercise of objective judgment.

22. The regulated entity shall ensure that any transaction between the regulated entity and the independent director is made under normal commercial terms as any other customer.

23. A director shall not be considered to be independent if he or she:

23.1 owns shares exceeding 2% of the total shareholding in the regulated entity concerned;

23.2 has spouse who owns shares exceeding 2% of the total shareholding in the regulated entity concerned;

23.3 has loan exceeding 1% of the capital fund in the regulated entity concerned, however, any relationship shall be at arm's length basis and on normal terms and conditions;

23.4 is employed by a company that has shareholding in that regulated entity or vice-versa;

23.5 was employed by that regulated entity;

23.6 has family members in senior management position in that regulated entity;

23.7 is affiliated with a significant customer or supplier of the regulated entity or its related parties;

23.8 is affiliated with a non-profit organization that receives significant funding from that regulated entity; and

23.9 has previously served as an independent director on the board of that regulated entity.

24. The board of a regulated entity shall assess annually whether a director is independent and shall notify the Authority if there is any change in the independence status.

25. An independent director shall not be removed from the board without the prior approval of the Authority.

### **Permanent Invitees to the Board**

26. Permanent invitees to the board either from within the regulated entity or from outside shall not be permitted. The board may invite employees as and when required depending on the agenda of the meeting and such employees shall leave the meeting at the time the board deliberates and makes decision.
27. The board may also invite individuals from outside for professional expertise and advice as and when required depending on the agenda of the meeting.

### **Appointment and Removal of Directors**

28. The regulated entity shall have a policy and procedure for the appointment of directors on the board, which shall be approved by the board.
29. In considering or proposing nominations for the appointment of directors, the board shall review whether a director candidate:
- 29.1 possesses the knowledge, skill, experience and, particularly in the case of non-executive directors, independence of mind given his or her responsibility on the board and in the light of the regulated entity's business and risk profile;
  - 29.2 has a record of integrity and good repute;
  - 29.3 has no conflicts of interests; and
  - 29.4 has sufficient time to fully carry out the responsibilities.
30. The regulated entity shall obtain Authority's no objection letter on the fit and proper test of all candidates considered for initial appointment or reappointment in the board at least one month prior to the date of the Annual General Meeting. As described in *Schedule II* of this CGRR 2018, the Authority shall assess the candidates on: (i) honesty, integrity and reputation; (ii) competence

and capability; (iii) financial soundness; and iv) declaration of business interests. The Authority may prescribe additional fit and proper criteria as and when necessary.

31. In case of a vacancy of a director of the board occurring between two ordinary Annual General Meetings, replacement shall be decided at the time of the next Annual General Meeting or through an Extraordinary General Meeting after getting no-objection letter on fit and proper test from the Authority.

32. The regulated entity shall notify the Authority about any modification in the fit and proper situation of a director.

33. The board shall issue an appointment letter to the new director with terms of reference that includes, but are not limited to, the responsibilities and accountability as specified in CGRR 2018. The appointment letter shall also mention director's fee, which is strictly related to attendance to the board meetings, and other compensations as set in the board's by-law.

34. A director may be replaced or asked to resign if:

34.1 he or she is convicted in a court of law for a criminal offence;

34.2 his or her conduct is found to be detrimental to the regulated entity;

34.3 he or she infringes the code of conduct of the regulated entity;

34.4 he or she fails to attend two-thirds of the total board meetings held in a financial year.

Emergency board meetings shall be excluded from the total number of board meetings for the purpose of calculating the two-thirds attendance;

34.5 if it is part of the remedial actions required by the Authority; and

34.6 any other reasons as stipulated in the Act or other applicable laws, rules and regulations.

**Tenure of Directors**

35. An ordinary director of a regulated entity shall be appointed for a term not exceeding three years, which may be extended by another term. To be eligible for re-appointment as a director in the same regulated entity, he or she shall have to complete a minimum cooling period of one year after serving two consecutive terms. However, he or she shall be eligible for appointment as a director in another regulated entity after serving a minimum cooling period of six months.
36. An independent director shall be appointed for a term not exceeding three years in the same regulated entity. The independent director shall not be eligible for re-appointment in the same regulated entity as a director.
37. An ordinary director shall resign upon completion of two consecutive terms and completion of one term for an independent director. This provision shall be enforced from the date of the first Annual General Meeting after CGRR 2018 comes into force. At that date, a director whose tenure has not reached the two-term limit (one term for an independent director) may continue for the remaining of the tenure.

**Board Orientation and Professional Development**

38. A regulated entity shall ensure that new directors are provided with orientation within three months of their appointment. The programme shall cover at the minimum, about the regulated entity's nature of the business, corporate strategies, duties and responsibilities of the board, risks and risk management strategy, rules and regulations issued by the Authority and other compliance requirements of the regulated entity.
39. In order to enable the directors to perform their responsibilities effectively, a regulated entity at its expense shall periodically provide knowledge and skills development opportunities to them.

## **Board Meetings**

### ***Frequency and Attendance***

40. The board of a regulated entity shall meet as frequently as may be deemed necessary to fulfill its duties and responsibilities appropriate to the nature, size and complexity of the regulated entity.
41. The board shall meet at least every quarter per financial year.
42. The directors shall attend at least two-thirds of the total board meetings held in a financial year. Excused absences cannot be considered as attendance. The number of board meetings and attendance of every director shall be made available to the Authority and shall be disclosed in the regulated entity's annual report.
43. The board meetings shall be held within Bhutan.

### ***Quorum***

44. A quorum for a board meeting shall be at least two-thirds of the total board of directors. No business may be transacted at a board meeting, unless a required quorum is met.

### ***Information to the Board***

45. The board of directors shall be provided with adequate, accurate and timely information prior to the board meetings and on an ongoing basis to enable them to fulfill their duties and responsibilities.

### ***Minutes of the Board Meetings***

46. The board of directors shall maintain appropriate record of its activity, such as minutes of the meetings, matters reviewed, recommendations made, and decisions taken.
47. Any concern or dissenting view raised by any director, particularly by the independent directors shall be discussed and recorded in the minutes of the meeting.

48. The records of the board meetings shall be made available to the Authority, as and when required.

**Chairperson of the Board**

49. The Chairperson of the board shall be an independent or non-executive director;

50. A regulated entity shall obtain endorsement of the Authority for the appointment of the Chairperson of the board;

51. The Chairperson and the CEO shall not be the same person;

52. As the time commitment for a Chairperson may be significant, the candidate for the Chairperson of a regulated entity shall not hold more than three directorships either in the public or government companies.

53. The Chairperson of the board shall:

53.1 provide leadership to the board and is responsible for its effective overall functioning, including maintaining a relationship of trust with the directors;

53.2 possess the requisite qualification, experience, competency and personal quality to fulfill the duties and responsibilities;

53.3 ensure that all relevant issues are included in the board agenda prior to board meeting;

53.4 ensure that the board is provided with accurate, timely, and clear information to assist them in making informed decision;

53.5 ensure that board decision is taken on a sound and well-informed manner;

53.6 encourage and promote critical discussion and ensure that dissenting view on contentious issues can be freely expressed and discussed within the decision-making process;

53.7 create a climate of trust between the independent directors and the other directors allowing the independent director to contribute to the board meeting in a professional atmosphere of constructive challenge;

53.8 dedicate sufficient time to the exercise of his or her duties and responsibilities;

53.9 assess the suitability of each director periodically, considering his or her performance on the board; and

53.10 review periodically the effectiveness of its own governance practices and procedures, determine where improvements may be needed, and make any necessary change, where required.

### **Company Secretary**

54. The board shall appoint a Company Secretary to support the board in carrying out its duties and responsibilities effectively. It shall ensure that the duties and responsibilities of the company secretary are clearly defined and is accountable to the board.

55. The Company Secretary shall ensure that the board procedures and applicable rules and regulations are complied with.

56. The Company Secretary shall attend all board meetings and associated activities unless the board instructs him or her to leave the meeting. He or she shall maintain accurate and adequate minutes and resolutions of the board meetings.

57. The Company Secretary shall be responsible for circulating the relevant resolutions/decisions of the board to the senior management and employees.

### **Board Committees**

58. Every board of a regulated entity shall establish an Audit Committee.

59. The board may establish other committees depending on the size of the regulated entity and its board, the nature of the business and the risk profile of the regulated entity.
60. Each committee shall have its by-law setting out its mandate, scope and working procedures.
61. The board shall appoint a Chairperson for each board committee. The Chairperson shall be an independent director, where possible.
62. Only directors shall be the members of the committees. The Company Secretary or the relevant functional head shall be appointed as the secretary of the committee. A committee may invite other non- members and/or experts based on the agenda of the meeting. These non-members shall leave the meeting at the time when the committee deliberates and makes decision.
63. Each committee shall maintain appropriate record of committee deliberation and decisions, such as meeting minutes, summary of matter reviewed, recommendations made and decisions taken.
64. A board committee is subordinate to the board; hence the board as a whole shall be responsible and accountable for the decisions.

### **Board Audit Committee**

65. The Audit Committee shall be *distinct from other committees and must be made up entirely* of independent or non-executive directors. The chairperson of Audit Committee shall be an independent director and shall not be the Chairperson of the board, or of any other committee.
66. The main duties and responsibilities of Audit Committee are to:
- 66.1 approve, or recommend to the board or shareholder for their approval, the appointment, remuneration and dismissal of external auditor;
  - 66.2 frame policy on internal audit and financial reporting;

- 66.3 oversee the financial reporting process;
- 66.4 discuss the annual audited financial statement and quarterly financial statement with management and the external auditor and to report the board;
- 66.5 provide oversight and interact with the regulated entity's internal and external auditors;
- 66.6 review and approve the audit scope and frequency;
- 66.7 receive key audit report and ensure that senior management is taking necessary corrective action in a timely manner to address control weakness, non-compliance with policy, law, rule and regulation, and other problem identified by an auditor and other control function;
- 66.8 oversee the establishment of accounting policy and practice by the regulated entity; and
- 66.9 review the third-party opinion on the design and effectiveness of the overall risk governance framework and internal control system.

### **Performance Evaluation of the Board**

- 67. The board of directors shall put in place a procedure for regular evaluation of the board as a whole as well as performance of individual directors.
- 68. The Authority may require the regulated entity to submit the performance reports of the board and individual directors.

### **Conflicts of Interest**

- 69. The board of directors shall have a formal written conflict of interest policy and an objective compliance process for implementing the policy. The policy document *inter alia* shall include:

- 69.1 director's duties and responsibilities to avoid, to the extent possible, activities that can create conflict of interest or the appearance of conflict of interest;
- 69.2 depending on the agenda of the meeting of the board or committee, a board of director shall declare any conflict of interest before the commencement of the meeting;
- 69.3 a rigorous review and approval process for a director to follow before he or she engages in certain activity;
- 69.4 a director's duties and responsibilities to promptly disclose any matter that may result, or has already resulted, in a conflict of interest;
- 69.5 a director's duties and responsibilities to abstain from voting on any matter where the director may have a conflict of interest or where the board of director's objectivity or ability to properly fulfill duties and responsibilities to the regulated entity may be otherwise compromised; and
- 69.6 the way in which the board will deal with any non-compliance with the policy.

### **Senior Management**

70. There shall be clear separation of duties and responsibilities between the shareholders and the management so as not to impede sound corporate governance. The CEO and other members of the senior management shall operate within the mandate given by the board.
71. The senior management shall have a clear and transparent decision-making process and organizational management structure designed to promote effective management of the regulated entity, including but not limited to the role, authority and responsibility of the various positions within senior management.

72. The duties and responsibilities of the senior management shall include but not limited to the following:

72.1 contribute to the regulated entity's sound corporate governance;

72.2 provide adequate oversight of those they manage;

72.3 ensure that the regulated entity's activity is consistent with the business strategy, risk appetite and the policy approved by the board;

72.4 implement corporate plan, risk management system, risk culture, process and control for managing the risks approved by the board; and

72.5 provide the board with the information it needs to carry out its duties and responsibilities.

73. The board shall select the CEO and may select other key members of the senior management, as well as the heads of the control functions.

74. The selected CEO candidate shall obtain a no objection letter on the fit and proper test from the Authority before the appointment. The board of the regulated entity shall develop and apply fit and proper test for the appointment of other members of the senior management and heads of control functions.

75. The members of the senior management shall have the necessary qualification, experience, competency and integrity to manage the regulated entity.

**Chief Executive Officer (CEO)**

76. The CEO is the highest position holder in the organization who is entrusted with the executive duties and responsibilities for the regulated entity's operations, compliance and performance.

77. The regulated entity shall appoint the CEO following an established process set out by the policy adopted by the board.
78. The CEO of a regulated entity shall be a Bhutanese residing in Bhutan. However, the Authority may consider exceptions to a regulated entity that has FDI share holding of 51% or more.
79. A CEO of a regulated entity shall be appointed for a term not exceeding the tenure specified in Section 35 of the Act, which may be extended for another term. The CEO may be eligible for the CEO position in another regulated entity after observing a minimum cooling period of six months.
80. A candidate for the CEO position of a regulated entity shall not be more than 65 years old at the time of applying for the position. The CEO shall resign upon completion of two consecutive terms or upon reaching the age of 70 years, whichever is earlier. This provision shall be enforced from the date of the first Annual General Meeting after CGRR 2018 comes into force. At that date, the CEO whose term has not reached the maximum tenure or age may continue for the remaining of the tenure.
81. The regulated entity shall inform the Authority immediately of the vacancy of a CEO position due to resignation, completion of term/age limit or termination; and the interim measure taken for day-to-day operations of the regulated entity. The board shall ensure that a CEO is appointed within three months from the date of vacancy.
82. To ensure the CEO's attention to the operation of the regulated entity is not affected, the CEO shall hold no more than three directorships either in public or government companies.
83. A CEO of a regulated entity shall not be permitted to carry out any other business as per Section 36 of the Act.

### **Remuneration Framework for Board, Senior Management and Employees**

84. The board shall set appropriate remuneration framework of the board of directors, the senior management and approve the general framework of compensation and remuneration for staff of the regulated entity within the law and legal framework applicable in the country.

85. The general remuneration for the board related functions shall include:

85.1 sitting fee to the directors for attending board and committee meetings;

85.2 compensation and other expenses to the directors for their participation in the board and committee meetings or any other board or committee related tasks including participation in the knowledge and skills development programmes;

85.3 fifty percent of board sitting fee to the Company Secretary for attending the board meetings;

85.4 fifty percent of the board committee sitting fee to the secretary of the board committee for attending the committee meetings;

85.5 Other employees shall not receive fee for any board related work; and

85.6 With the approval of the board, the invitees other than the employees who are invited to contribute their expertise may be paid fees and other compensation.

### **Disclosure and Transparency**

86. The governance of the regulated entities shall be adequately transparent to its depositors, policy holders, shareholders, and other relevant stakeholders.

87. A regulated entity shall provide a corporate governance report as part of its annual report. At a minimum, regulated entity shall disclose the following information in the report:

- 87.1 a statement of compliance with the CGRR 2018, including a full explanation of any deviation;
- 87.2 names of directors of the board, identifying independent, non-executive and executive directors clearly, other board directorships held by any director;
- 87.3 the number of times in the year the board and each committee met and attendance details for each director and the remuneration;
- 87.4 a statement on the regulated entity's risk management and internal control systems; and
- 87.5 disclosure of material related party transactions between the regulated entity, its subsidiaries or associates or affiliates and a director or key management person.

### **Whistle-Blowing Policies**

88. The regulated entities shall develop policies that protect employees who report in good faith and on reasonable grounds wrongdoing to the board or another designated function, such as the head of internal audit or compliance. Whistle-blower policies shall set out the responsibilities for the board of directors, the audit committee, senior management and control functions, such as internal audit and compliance, to maintain policies and procedures for employees to submit, confidentially, information about accounting, internal control, compliance, audit and other matters about which the employee has concerns.

## **PART 3: THE RISK MANAGEMENT FRAMEWORK**

89. Risk management is an integral part of the internal governance involving all areas of a regulated entity and there is a strong link between good corporate governance and sound risk management. Each regulated entity shall have in place a proper risk management, covering all its functions and activities.

**Risk Management Framework and Culture**

90. A regulated entity shall implement a proper risk management framework following the “*three lines of defense*” model in which:

90.1 the business unit is the first line of defense: he takes risk and is responsible and accountable for identifying, assessing and reporting the risk within policy framework, procedure, limit and control;

90.2 the control function is the second line of defense: made of the risk management function and compliance function fully independent from the first line of defense, he monitors risk and reports to the senior management and the board; and

90.3 the third line of defense is the internal audit function. Fully independent, the internal audit review the quality of the internal control and risk governance, including the first and the second line of defense.

91. Every regulated entity shall develop an integrated and institution-wide risk culture, which is a key element of the risk management framework, through policy, example, communication, and training of staff regarding their duty and responsibility for risk.

92. The board and senior management shall be responsible for the desired risk culture through:

92.1 enabling an open and respectful atmosphere in which an employee feels motivated to speak up when observing new or excessive risk;

92.2 clarifying the range of acceptable risks using a risk appetite statement; and

92.3 aligning incentive with the objective and clarifying how breach in policy/procedure will be addressed.

**The Risk Management Functions**

93. A regulated entity shall have an effective independent risk management function, with sufficient stature, independence, resource and access to the board. The size of the risk management function shall be commensurate to the size, complexity and risk profile of the institution. The independent risk management function responsibilities are to:

93.1 oversee the risk-taking activity across the regulated entity;

93.2 identify material individual, aggregate and emerging risk;

93.3 assess the risks and measure the regulated entity's exposure to them;

93.4 develop and implement the risk governance framework approved by the board;

93.5 monitor on an ongoing basis the risk-taking activity, the risk exposures in line with the board-approved risk appetite, the risk limit, and the breach of limit;

93.6 influence and, when necessary, challenge decision that give rise to material risk; and

93.7 report to senior management and the board on all these items including, but not limited to, proposing appropriate risk-mitigating action.

94. The regulated entities shall appoint a senior risk officer preferably a Chief Risk Officer (CRO) as the head of the risk management function. CRO shall be responsible for overseeing the development and implementation of the regulated entity's risk management functions. The key duties and responsibilities of the CRO shall include:

94.1 strengthen staff skill and enhance risk management systems, policy, process, and report;

94.2 ensure that the regulated entity's risk management capability is sufficiently robust;

94.3 support the board in its oversight of the development of the regulated entity's risk appetite and risk appetite statement;

94.4 translate the risk appetite into a risk limits structure; and

94.5 monitor the risk-taking activity and the adherence to risk limit.

95. The CRO shall be independent, his or her duties and responsibilities shall be distinct from other executive functions, and shall not have management or financial responsibility related to any operational business lines or revenue-generating functions.

96. The CRO shall report to the CEO and to the board. The board shall approve the appointment, dismissal and other changes to the CRO position.

### **Risks Monitoring, Controlling and Communication**

97. The regulated entity's risk governance framework shall include policy, appropriate control procedure and process, designed to ensure that the regulated entity's risk identification, aggregation, mitigation and monitoring capabilities are commensurate with the institution's size, complexity and risk profile.

98. Risk identification and measurement shall include both quantitative and qualitative element covering all material risks to the regulated entity (including concentration or reputation), on- and off-balance sheet, and on an institution-wide, and business-line level.

99. The risk management information system (including data, IT) shall keep pace with financial position and revenue growth; consider the complexity of the regulated entity's business, its geographical expansion, the merger and acquisition, and the introduction of new product.

100. A regulated entity shall:

100.1 organize an ongoing communication about risk issues to develop a strong risk culture;

100.2 promote risk awareness and encourage open communication;

100.3 communicate information to the board and senior management in a timely, accurate and understandable manner; and

100.4 report without any delay to senior management and the board, as appropriate the information that requires immediate decisions.

101. The board shall regularly assess the relevance and the accuracy of the information it receives.

### **Compliance Function**

102. A regulated entity shall have an independent compliance function. The regulated entity's senior management shall develop a compliance policy, which shall be approved by the board.

103. The Compliance Officer shall have appropriate seniority in the management of the regulated entity.

104. The main duties and responsibilities of the compliance function are to:

104.1 monitor the effective compliance of laws, rules, regulations and directive within the regulated entity;

104.2 implement and ensure compliance all matters relating to prudential rule, regulation and directive issued by the Authority;

104.3 act as a focal point between the regulated entity and the Authority;

104.4 collect information requested by the Authority from the regulated entity;

104.5 check the correctness and promptness of the report submitted to the Authority;

104.6 deal with any query or problem concerning the Authority returns and compliance with the prudential norms;

104.7 report to the Authority on a quarterly basis the issues pertaining to non-compliance;

104.8 support corporate values through policy and process and advise the board and senior management on the regulated entity's compliance with applicable laws, rules, regulations and standards; and

104.9 educate staff about compliance issues.

105. The board shall approve the appointment, dismissal and other changes to the Compliance Officer and it shall immediately notify to the Authority.

### **Internal Audit**

106. A regulated entity shall have an internal audit that provides an independent assurance to the board of directors and senior management on the quality and effectiveness of a regulated entity's internal control, risk management and governance system.

107. A regulated entity shall have an adequate team of internal auditors, competent and professionally trained.

108. Internal audit shall:

108.1 have a clear mandate;

108.2 be accountable to the board;

108.3 be independent from the audited activity;

108.4 require timely and effective correction of audit issue by senior management;

108.5 perform a periodic assessment of the regulated entity's overall risk governance framework, including, but not limited to, an assessment of: the effectiveness of the risk management and compliance functions; the quality of risk reporting to the board and

senior management; and, the effectiveness of the regulated entity's system of internal control;

108.6 in the case of a serious breach such as fraud or embezzlement, the matter shall be reported immediately to the Authority; and

108.7 submit reports and findings to the Board Audit Committee. However, on matter of exigency, an internal auditor may present his or her finding to the shareholders. Such report shall also be communicated to the Authority.

109. The board and senior management shall contribute to the effectiveness of the internal audit function; and respect and promote the independence of the internal audit function.

### **Compliance Monitoring and Reporting**

110. The Authority shall monitor adherence to the CGRR 2018 through its regular supervision of the regulated entities.

111. The regulated entities shall be required to submit a compliance report including any non-compliance of the CGRR 2018 with such frequency that the Authority may notify to the regulated entities from time to time.

112. The report shall also explain the reasons for non-compliance if any.

### **Enforcement**

113. The Authority shall take remedial actions against the regulated entities that have not corrected the weaknesses or non-compliance issues identified by the Authority.

**Definitions**

114. In these Rules and Regulations, the following terms shall have the meanings indicated, unless the content clearly indicates otherwise.

- i. **“Act”** means the Financial Services Act of Bhutan 2011.
- ii. **“Authority”** means the Royal Monetary Authority of Bhutan established under the Royal Monetary Authority Act of Bhutan 2010.
- iii. **“Board”** or **“Board of Directors”** means the body that governs the regulated entities and supervises its management.
- iv. **“CEO”** means Chief Executive Officer as defined in Sections 34 and 35 of the Act.
- v. **“Companies Act”** means the Companies Act of Bhutan 2016.
- vi. **“Control function”** means internal audit, risk management and compliance functions.
- vii. **“Executive Director”** means a member of the board who also has management responsibilities within the regulated entity.
- viii. **“Family member”** means a natural person and includes spouse, dependent children or other dependents of a person being of the same household.
- ix. **“Independent Director”**, defined in section 371 of the Act, is further defined in this Rules and Regulations.
- x. **“Non-Executive Director”** means a member of the board who does not have management duties and responsibilities within the regulated entity.
- xi. **“Regulated Entity”** means bank, insurance company, pension and provident fund, fund management or any other entity as specified by the Authority as per the Act.

xii. **“Senior Management”** means Chief Executive Officer and senior officers appointed by the board for the day-today management of a regulated entity.

xiii. **“Significant Owner”** has the same definition as in Section 371 of the Act.

**SCHEDULE I: CODE OF ETHICS OF REGULATED ENTITIES****1. Scope and Application**

The Code of Ethics shall apply to the board of directors, officers and employees of regulated entities.

This Code is intended to serve as a guide for the promotion of proper ethical standards, and sound and prudent business practices amongst regulated entities. Such a code of ethics shall not, however, restrict or replace the mature judgment of staff in conducting his or her day-to-day business. Where there is doubt over matters relating to the code of ethics, staff shall seek guidance from his or her supervisor or from the Authority.

A regulated entity may adopt additional in-house rules, which require ethical standards not below those required by this Code.

**2. Principles of Ethical Conduct**

The following principles must guide ethical conduct by a director, officer and/or employee of regulated entities:

- a. to manage conflict of interest;
- b. to avoid misuse of position;
- c. to prevent misuse of information gained through the regulated entity's operation, either for personal gain or for any purpose other than that intended by the regulated entity;
- d. to ensure completeness and accuracy of relevant record;
- e. to ensure confidentiality of communication and transaction between the regulated entity and its supplier and customer; and
- f. to ensure fair and equitable treatment of all supplier, customer and other who engage in business with the regulate identity.

### **3. Conflict of Interest**

The directors and employees shall not engage directly or indirectly in any business activity that conflicts or competes with the regulated entity's interests. These activities include, but are not limited to:

a. **Outside Financial Interest of Directors**

The directors of regulated entities shall fully disclose to its board any commercial, financial, agricultural, industrial, or other business interest with which he or members of his immediate family may at any time directly or indirectly be interested and shall refrain from voting on any matter related thereto which becomes the subject of board action: provided that such an interest, if so disclosed, shall not disqualify the interested party for the purpose of constituting quorum.

b. **Outside Financial Interest of Employees**

Where an employee has a financial interest in a party that engages or proposes to engage in a transaction with the regulated entity, whether as a sole proprietor, partner, shareholder, creditor or debtor, such an interest must be disclosed immediately to his immediate supervisor. Thereafter, that person shall not be directly involved in the regulated entity's dealing with the counterparty so long as the interest continues to exist. This restriction does not apply in cases where persons have holding of publicly listed security, unless their immediate supervisor considers the interest to be material and likely to impair the objectivity of the person concerned.

c. **Other Business Interest**

It is a conflict of interest if an officer or employee conducts business other than the regulated entity's business during office hours. A conflict of interest also arises where the acquisition of any business interest, or participation in any business activity outside. The

regulated entity and its office hours, demands excessive time and attention from the staff, thereby depriving the regulated entity of the person's best efforts on the job.

d. Entertainment and Gift

- a director or senior officer of the regulated entity shall not accept or offer any improper payment or benefit in connection with his role at the regulated entity. He shall not obtain or seek to obtain personal advantage from any person or entity dealing with the regulated entity;
- gift and entertainment given and received with the intention of unduly influencing business decisions are a form of bribery and are prohibited. In particular, a director or senior officer must not solicit or accept any gifts or inducements where the value of such could make it appear the person giving the gift is attempting to influence the director or senior officer to gain advantage or to create a sense of obligation;
- directors and senior officers of the regulated entity shall not seek to improperly influence others or official decisions by providing gifts or favors. The regulated entity shall not support the direct giving of political donations in cash or in kind to any political party or group; and
- the board shall issue policies in relation to accepting, declaring and/or recording the receipt of gifts or benefits.

**4. Misuse of Position**

- a. a director, staff and immediate family and his or her relative, officer and employee shall not use the regulated entity's name or facility for personal advantage in investment or retail purchasing transaction, or in similar type of activity. A director and staff, and his or her relative must not use their connection with the regulated entity to borrow from or become

indebted to customers, prospective customers or suppliers. The use of position to obtain preferential treatment, such as in purchasing goods or security is prohibited; and

- b. a director, officer and employee of regulated entity must not use the institution's facility or influence for speculating in commodities, gold, silver, foreign exchange or securities, whether acting personally or on behalf of relatives. A director, officer and employee must also refrain from "back- scratching" exercises with director, officer and employee of other regulated entity to provide mutually beneficial transaction in return for similar facility, designed to circumvent this ethical rule and regulation.

#### **5. Misuse of Information**

- a. a director, officer or employee shall not use any information which he/she may obtain in the discharge of his or her duties about the regulated entity itself, or any of its customers or supplier, for his or another's personal or financial gain;
- b. a director, officer or employee shall not deal in the securities of any company listed or pending listing on a stock exchange at anytime when he or she is in possession of information obtained as a result of his/her employment by, or his or her connection with the regulated entity, which is generally not available to shareholders of that company and the public, and which, if it were so available, would likely bring about a material change in the market price of the securities of the company concerned; and
- c. a director, officer or employee who possesses on-public information concerning a company is prohibited from influencing any other person to deal in the security concerned or communicating such information to any other person, including other director, officer or employee who do not require such information in discharging their duty.

## **6. Integrity of Records and Transactions**

- a. a regulated entity must at all times maintain clearly, accurately and incomplete form accounting record and report as are necessary to reflect the true state of it affairs, to explain its transactions and its financial position;
- b. regulated entities shall not make entries or allow entries to be made for any account, record or document of the regulated entity that is false or would obscure the true nature of a transaction, or mislead the true authorization limits or approval by the relevant person of such transactions; and
- c. all records and computer files or programs of the regulated entity, including personnel files, financial statements and customer information, must be accessed and used only for the purpose approved by the management.

## **7. Confidentiality**

- a. a director, officer or employee must take precautions to protect the confidentiality of customer information and transaction. No director, officer or employee shall divulge information regarding any customer, or any correspondence, accounts or dealings of the regulated entity with its customers to any person other than administrative or judicial authorities; and
- b. business and financial information about any customer maybe used or made available to third parties only with the prior written consent of the customer, or in accordance with arrangements for the proper interchange of information between regulated entities and Credit Information Bureau about credit risk, or when law requires disclosure.

## **8. Fair and Equitable Treatment**

All business dealings on behalf of the regulated entity with current and potential customers and suppliers and with members of the staff must be conducted fairly and equitably, without granting favored terms. A director, officer and employee must not be influenced by

friendship or association, either in meeting a customer's or a supplier's requirements, or in recommending what transactions or procedures need to be conducted. Such decisions shall be strictly made on an arms-length basis. Any related party transactions must be in full compliance with applicable law, regulation and this code and must be based on normal business criteria and fully documented. All transactions with insiders or related parties must not be on preferential terms.

#### **9. Addressing Suspected or Actual Illegal or Unethical Behavior**

- a. board of directors of regulated entities shall promote ethical behavior by:
  - encouraging company employees to talk to supervisors when in doubt about the best course of action in a situation that presents an ethical issue; and
  - encouraging board of directors and employees to report violations of laws, rules, regulations or the company code of ethics to the chairman of the Audit Committee.
- b. the Chairperson of the board must keep confidential the source of information communicated to him or her concerning violation of laws, regulations or a code of ethics;
- c. a director or an employee shall not be subject to retaliation for reporting made in good faith of violations of laws, rules, regulation or a code of ethics; and
- d. the board shall ensure that credible reported violations of laws, regulations or a code of ethics will be investigated by a person designated by the board and disciplinary action will be taken inherent of any violation that is appropriate in relation to the gravity of the violation.

#### **10. Recruitment of Employees by Regulated Entities**

An employee terminated by any other regulated entity based on embezzlement of funds or fraud shall not be recruited in by any regulated entity. Before recruiting an employee, a prospective regulated entity employer must conduct due diligence of the candidate.

**SCHEDULE II: FIT AND PROPER QUALIFICATIONS****1. Criteria**

The Authority shall take into account the following criteria in determining whether a candidate for appointment as a director in the board or a CEO of a regulated entity is fit and proper:

- a. honesty, integrity and reputation;
- b. competence and capability;
- c. financial soundness; and
- d. declaration of business interests.

**2. Honesty, Integrity and Reputation**

When assessing the honesty, integrity and reputation of a candidate, the Authority shall consider whether the candidate:

- a. has been refused the right or restricted in its or his right to carry on any trade, business or profession for which a specific license registration or other authorization is required by law in any jurisdiction;
- b. has been issued a prohibition order under any Act administered by the Authority or has been prohibited from operating in any jurisdiction by any financial services regulatory authority;
- c. has been censured, disciplined, suspended or refused membership or registration by the Authority, any other regulatory authority, an operator of market or clearing facility, any professional body or government agency, whether in Bhutan or elsewhere;
- d. has been the subject of any complaint made reasonably and in good faith, in the determination of the Authority, relating to activities that are regulated by authority or under any law in any jurisdiction;

- e. has been the subject of any proceedings of a disciplinary or criminal nature or has been notified of any potential proceedings or of any investigation which might lead to those proceedings, under any law in any jurisdiction;
- f. has been convicted of any offence, or is being subject to any pending proceedings which may lead to such a conviction, under any law in any jurisdiction;
- g. has had any judgment associated with a finding of fraud, misrepresentation dishonesty entered against the relevant person in any civil proceedings or is a party to any pending proceedings which may lead to such a judgment, under any law in any jurisdiction;
- h. has accepted civil liability for fraud or misrepresentation under any law in any jurisdiction;
- i. has had any civil penalty enforcement action taken against it or him by Authority or any other regulatory authority under any law in any jurisdiction;
- j. has contravened or abetted another person in breach of any laws or regulations whether in Bhutan or elsewhere;
- k. has been the subject of any investigations or disciplinary proceedings or been issued a warning or reprimand by Authority, any other regulatory authority, an operator of a market or clearing facility, any professional body or government agency, whether in Bhutan or elsewhere;
- l. has been refused a fidelity or surety bond, whether in Bhutan or elsewhere;
- m. has demonstrated an unwillingness to comply with any legal or regulatory requirement or to uphold any professional standard, whether in Bhutan or elsewhere;
- n. has been untruthful or provided false or misleading information to Authority or been uncooperative in any dealings with the Authority or any other regulatory authority in any jurisdiction;

o. where a candidate to directorship has served, or been associated with a company or other business venture, in addition to sub-sections (a) to (n), the Authority shall consider whether the relevant person:

- is or has been a board of director, partner, significant owner or concerned in the management of a business that has been censured, disciplined prosecuted or convicted of a criminal offence, or been the subject of any disciplinary or criminal investigation or proceeding, in Bhutan or elsewhere, in relation to any matter that took place while the person was a director, partner, significant owner or concerned in the management of the business;
- is or has been a director, partner, significant owner or concerned in the management of a business that has been suspended or refused membership or registration by the Authority, any other regulatory authority, an operator of market or clearing facility, any government agency, whether in Bhutan or elsewhere;
- has been a director, partner, significant owner or concerned in the management of a business that has gone into insolvency, liquidation or administration during the period when, or within a period of one year after, the candidate was a director, partner, significant owner or concerned in the management of the business, whether in Bhutan or elsewhere;
- has been dismissed or asked to resign from: (i) office ;( ii) employment ;( iii) a position of trust; or, (iv)a fiduciary appointment or similar position, whether in Bhutan or elsewhere;
- has been disqualified from acting as a director or disqualified from acting in managerial capacity whether in Bhutan or elsewhere;

- has been an officer found liable for an offence committed by a body corporate because of the offence having proved to have been committed with the consent or connivance of, or neglect attributable to, the officer, whether in Bhutan or elsewhere; or
- has NPL for the past one year.

### **3. Competence and Capability**

When assessing the competence and capability of a candidate, the Authority shall consider whether the candidate:

- a. has educational qualification relevant to the nature of the duties they are required to perform;
- b. has experience relevant to the nature of the duties they are required to perform.
- c. has satisfactory past performance or expertise, having regards to the nature of the candidate's duties; and
- d. is an individual who is assuming concurrent responsibilities, whether such responsibilities will give rise to a conflict of interest or otherwise impair his ability to discharge his duties in relation to any activity regulated by the Authority under the relevant legislation.

### **4. Financial Soundness**

When assessing the financial soundness of a candidate, the Authority shall consider whether the candidate:

- a. is or has been unable to fulfill any of his financial obligations, whether in Bhutan or elsewhere;
- b. has entered compromise or scheme of arrangement with his or her creditors or made an assignment for the benefit of his or her creditors, being a compromise or scheme of arrangement or assignment that is still in operation, whether in Bhutan elsewhere; and
- c. is subject to a judgment for payment of debt, which is unsatisfied, in either whole or in part, whether in Bhutan or elsewhere.

**5. Declaration of Business Interests**

The Authority shall require a candidate to provide on self-declaration basis the list of all direct and indirect business interest.