



MCB BANK LIMITED

GLOBAL INTERNAL AUDIT POLICY

VERSION: 1.0

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TABLE OF CONTENTS

	Page
1. OVERVIEW	2
2. MISSION & OBJECTIVES	2
3. ORGANIZATION.....	3
4. SCOPE & RESPONSIBILITIES.....	5
5. AUTHORITY	7
6. ACCOUNTABILITY	7
7. LIMITATIONS	8
8. SKILLS, TRAINING & ALTERNATE ARRANGEMENTS.....	8
9. STANDARDS OF PRACTICE.....	8
10. FREQUENCY OF TESTING	8
11. REPORTING MECHANISM.....	9
12. CHECKING OF FRAUDS	9
13. MANAGEMENT RESPONSIBILITIES	10
14. CONFIDENTIALITY AND REPORTING PROCEDURES.....	10
15. REVIEW	11
16. GLOSSARY	11

1. OVERVIEW

- 1.1 The Global Internal Audit Policy Version 1.0 of MCB Bank Limited was approved by the Board of Directors of the Bank in their meeting held on February 20, 2019. This Policy governs the internal audit activities of local and overseas operations of MCB Bank Limited, Pakistan. However, there shall be separate Internal Audit Policies for Bank's domestic operations (i.e. Pakistan) and Wholesale Banking Operations UAE. These policies shall be subservient to the Global Internal Audit Policy.
- 1.2 Internal Audit function of the Bank is established in accordance with the requirements of the Listed Companies (Code of Corporate Governance) Regulations, 2017 which states that there shall be an internal audit function in every listed company. It is the policy of the Board of Directors of the Bank to maintain an independent internal audit function to primarily undertake the Internal Audit work throughout the Bank (covering its local as well as overseas operations including operations of its subsidiaries). In MCB Bank, internal audit function is performed by Audit & Risk Assets Review (Audit & RAR) Group. This Charter for Audit & RAR Group, inter alia, defines the organization, objective and responsibilities of the Group as envisaged by the Board.
- 1.3 In case of difference in the legal/regulatory requirements of Host and Home country (with respect to auditee), stringent of the two requirements will be followed. However, where there is a conflict in these requirements, matter will be referred to the concerned authority (ies) for advice.

2. MISSION & OBJECTIVES ^{[1][2]}

- 2.1 The mission of Audit & RAR Group is to provide an independent, objective assurance and consulting services designed to add value and improve operations (both domestic and global) of MCB Bank Ltd. by adopting a systematic, disciplined approach to evaluate and further improve the quality, adequacy, effectiveness of risk management, control and governance processes.
- 2.2 The prime objective of Audit & RAR Group is to examine and evaluate whether the framework for Risk Management, Control and Governance Processes of MCB Bank Ltd. is adequate and functioning in a manner to ensure that:
- a. Risks are appropriately identified and managed;
 - b. Financial, managerial and operating information is accurate, reliable and timely;
 - c. Policies, standards, procedures and applicable laws & regulations are complied with;
 - d. Compliance with those policies, plans, procedures, laws & regulations, which could have a significant impact on operations & reporting, is ensured by Bank's systems;
 - e. Assets of MCB Bank Ltd. are adequately safeguarded; and
 - f. Quality and continuous improvement are fostered into control processes.
- 2.3 The objectives of Audit & RAR Group also include advising and recommending improvements in internal controls and risk management systems to Bank's senior management.

¹ SBP's Guidelines on Compliance Risk Management issued vide circular no. BPRD Circular No. 7 of 2017 dated August 09, 2017.

² SBP's BSD Circular 03 of April 04, 2007 (Policy Framework in Banks)

3. ORGANIZATION

Independence & Line of Reporting

- 3.1 Personnel in Audit & RAR Group (including those posted at overseas jurisdictions) shall report through the chain of command to the Group Head Audit & RAR. However, the Head(s) of Internal Audit in overseas jurisdictions shall administratively report to the respective Country Head. The Group Head Audit & RAR reports functionally to the Audit Committee and administratively to the President / Chief Executive Officer (CEO) and his performance appraisal shall be done jointly by the Chairman of the Audit Committee and the President / Chief Executive Officer.

Organizational Structure

- 3.2 The core audit function including Branch Audit (both local and foreign branches), Management Audit (both local and foreign offices including Bank's subsidiaries), Investigations and Risk Assets Review shall be managed by Operational Audit Divisions, segmented geographically.
- 3.3 The IT / IS Audit Division shall undertake audit, reviews and investigations of systems, applications, infrastructure and networks etc. (both local and foreign operations).
- 3.4 The Risk Assets Review Department shall primarily review asset portfolio tagged to major lending branches of the Bank as well as Assets Rehabilitation Group and also undertake related Management Audits and other credit related assignments of Audit & RAR Group (as applicable to both local and foreign operations of the Bank). Moreover, the Basel related assignments shall also be conducted by Risk Assets Review Department.
- 3.5 Audit & RAR Group shall be further strengthened by the following Departments:

Quality Assurance & Framework Development Department

- 3.5.1 In order to ensure consistent application of audit approach and documentation of work performed, periodic quality reviews as well as ongoing monitoring for quality assurance (hereinafter referred to as 'Internal Assessments') shall be conducted. The Internal Assessments shall cover the entire audit activity including audits / reviews performed at branches, audits of management functions, IT/IS Audits, Continuous Auditing activity, activities of Monitoring and Whistleblowing Department etc. The periodic quality reviews shall be carried out for selected audit engagements as per the Quality Assurance plan approved by the Board's Audit Committee. These Periodic Reviews shall be over and above the review process to be carried out for all audit assignments.
- 3.5.2 The Quality Assurance & Framework Development Department shall also be responsible for addressing training needs of personnel in the Audit & RAR Group for ensuring continuous improvement in quality, efficiency and effectiveness of Internal Audit function.
- 3.5.3 The Quality Assurance & Framework Development Department shall further oversee the development work of Manuals, Guidelines, SOPs, Audit Master Data and regular updates thereof.

Monitoring & Whistle Blowing Department

- 3.5.4 The Monitoring & Whistleblowing Department shall comprise of following two functions:

- 3.5.4.1 **Monitoring function** shall ensure compliance follow up including validation of actions with respect to the Internal Audit findings, external auditor's observations, decisions of the Board and all sub committees of the Board. However, in line with the Bank's Policy

on Internal Controls, compliance of all the observation / issues related to regulatory bodies shall be taken care of by Compliance & Controls Group (CCG) of the Bank.

3.5.4.2 **Whistle Blowing function** shall address the concerns of Bank's staff and outside parties such as shareholders, vendors, customers etc. for reported wrongdoings, impropriety, irregularities, financial malpractices, fraud & forgeries, personnel harassment and improper conduct, as per scope approved by the Board of Directors. The Whistle Blowing function shall be governed by a separate Whistle Blowing Program. This Program shall inter alia; address the protection rights & rewards of the complainant, disciplinary actions & penalties as well as rights & responsibilities of the suspected parties.

Continuous Auditing Department

3.5.5 Continuous Auditing Department shall perform regular and timely system based audit steps for identification of breaches / gaps / weaknesses of the controls to ensure immediate follow-up and remediation by the management. These selected system based audit steps shall be recommended by the Group Head Audit & RAR and approved by the Board's Audit Committee. The Department Head Continuous Auditing shall report to Division Head IT / IS Audit.

3.6 The organizational structure of Audit & RAR shall be reviewed and recommended by the Audit Committee to the Board for its approval, as and when required.

Employment

3.7 Provisions in respect of employment of personnel within Audit & RAR Group are as follows:

3.7.1 As required by Listed Companies (Code of Corporate Governance) Regulations, 2017, the appointment (including continuation³ of service as defined in 4.7.4(d) below), remuneration and terms and conditions of employment of the Group Head Audit & RAR shall be determined with the approval of the Board of Directors, on the recommendation of Human Resource & Remuneration Committee (HR&RC).

3.7.2 The removal / non-renewal of contract / replacement of Group Head Audit & RAR shall be made with the approval of Board of Directors. Provided that the Group Head Audit & RAR Group may be removed upon the recommendation of the Audit Committee.⁴

3.7.3 Bank must promptly notify the Central Bank of the UAE in case of resignation of Group Head Audit & RAR along with the reasons thereof and shall also obtain the no-objection of the Central Bank of the UAE before his / her replacement or dismissal.⁵

3.7.4 No person shall be appointed as the Head of Audit & RAR Group unless:

a) He/she has 3 years of relevant experience in audit or finance or compliance function and is⁶ a member of the Institute of Chartered Accountants of Pakistan or Institute of Cost and Management Accountants of Pakistan or;

b) He/she has five years of relevant experience in audit or finance or compliance function and:

i. is a Certified Internal Auditor; or

³ Amendments to the Listed Companies (Code of Corporate Governance), Regulations, 2017 in light of S.R.O. 1475 (I)/2018, dated 5th December 2018.

⁴ Listed Companies (Code of Corporate Governance) Regulations, 2017.

⁵ Central Bank of the UAE Notice No. CBUAE/BSN/N/2018/3017 dated October 16, 2018 (Internal Controls, Compliance and Internal Audit Regulation).

⁶ Listed Companies (Code of Corporate Governance) Regulations, 2017.

- ii. is a Certified Fraud Examiner; or
- iii. is a Certified Internal Control Auditor; or
- iv. has a post graduate degree in business, finance from a university or equivalent, recognized and approved by the Higher Education Commission of Pakistan (HEC) and is a member of a professional body⁷ relevant to such qualification, if applicable; or

c) He/ she has at least seven years of managerial experience in field of audit or accounting or in managing financial or corporate affairs functions of a company and has a suitable degree from a university in Pakistan or abroad equivalent to graduate degree, recognized and approved by the Higher Education Commission of Pakistan (HEC). Suitability of such person for appointment as Group Head Audit & RAR shall be determined by Securities and Exchange Commission of Pakistan (SECP) based on application submitted in this respect by the Bank.

d) Provided that existing head of internal audit of bank having at least fifteen years of experience on the same position in that bank is exempt from qualification criteria above⁸.

3.7.5 Head of Audit & RAR Group must be suitably qualified, experienced and conversant with the Bank's policies and procedures. Furthermore, director of the Bank cannot be appointed, in any capacity, in the Audit & RAR Group to ensure independence of the internal audit function.

3.7.6 The Group Head Audit & RAR and all internal auditors must avoid conflicts of interest. Accordingly, internally recruited internal auditors must not engage in auditing activities for which they have had previous responsibility before at least one year "cooling off" period has elapsed.

Guest Auditor Program

3.8 Guest Auditor Program is a global concept introduced to ameliorate capacity building efforts within the internal audit function. Audit & RAR Group may also run this program to broaden understanding of internal audit's role within the Bank as well as to enhance business/process insight of the internal auditors.

4. SCOPE⁹ & RESPONSIBILITIES

4.1 Scope and responsibilities of the Audit & RAR Group are as follows:

Scope

4.2 All activities within the Bank (including outsource activities)¹⁰ are potentially within the scope of internal audit.

The scope of Audit & RAR Group is as follows:

⁷ "Body of professional accountants" means:

a) established in Pakistan, governed under a special enactment of the Federal Government as a self-regulatory organization managed by a representative National Council, and has a prescribed minimum criterion of examination and entitlement of membership of such body.

b) established outside Pakistan and established under a special enactment in the country of its origin and which is a member of the International Federation of Accountants (IFAC).

⁸ Amendments to the Listed Companies (Code of Corporate Governance), Regulations, 2017 in light of S.R.O. 1475 (I)/2018, dated 5th December 2018.

⁹ SBP's BSD Circular 03 of April 04, 2007 (Policy Framework in Banks).

¹⁰ Central Bank of the UAE Notice No. CBUAE/BSN/N/2018/3017 dated October 16, 2018 (Internal Controls, Compliance and Internal Audit Regulation)

- a. To act as a supervisory function with respect to the review of internal controls.
- b. To evaluate and validate the effectiveness of control systems, monitor control systems, and contribute to ongoing effectiveness of control systems.
- c. To report, on quarterly basis, on internal control system and significant findings to the Audit Committee of the Board.
- d. To comment on design effectiveness of controls in place / to be implemented by management.
- e. To conduct investigations e.g. fraud investigations and investigations against complaints received by Whistle Blowing Function regarding any wrongdoings, impropriety, irregularities, financial malpractices, fraud & forgeries, personnel harassment and improper conduct etc.
- f. To internally evaluate the Internal Control over Financial Reporting (ICFR) system, and make timely and practical suggestions to Board's Audit Committee for improvement.¹¹

4.3 The subsidiaries of MCB Bank Ltd. will also be subject to internal audit (if permissible by applicable laws/regulations) by MCB Bank's Audit & RAR Group as per the frequency of testing outlined in section 11.1 of this document.

Responsibilities¹²

4.4 Responsibilities of the Group Head Audit & RAR and staff of Audit & RAR Group are given below:

4.4.1 Group Head Audit & RAR has responsibility to:

- a. Develop and lead an effective and efficient Internal Audit & RAR function.
- b. Prepare annual Audit & RAR plan on a risk based methodology for review and approval of the Audit Committee. The plan is to be updated for changes in the bank's risk profile, as and when required.
- c. Implement Audit & RAR plan, including special assignments such as review of new products / systems, analysis of financial statements etc. as directed by Audit Committee or requested by the management.
- d. Ensure that function specific internal audit observations in an overseas jurisdiction are forwarded to concerned departments/functions at Head Office.¹³
- e. Maintain professional staff with sufficient knowledge, skills, experience and professional qualifications to meet the requirements of the Global Internal Audit Policy as well as cover all major heads of accounts maintained by the Bank.
- f. Conduct independent investigation of suspected / actual fraudulent activities, notify the results and give recommendations / suggestions to prevent the same, wherever required / necessary.
- g. Keep the Audit Committee abreast of developments and trends in internal auditing and give recommendations for necessary revisions in the relevant Internal Audit Policy and Internal Audit Manual.

¹¹ SBP's OSED Circular 01 of 2014 (Annexure – A).

¹² SBP's BSD Circular 03 of April 04, 2007 (Policy Framework in Banks)

¹³ SBP's BPRD Circular 06 of August 06, 2018 (Governance Framework for Banks' Overseas Operations)

- h. Liaise closely with the external auditor to share knowledge. Ensure that internal audit reports are provided for the review of external auditors if requested by them.
- i. Perform any other assignment as may be assigned by the Audit Committee of the Board.

4.4.2 The staff of Audit & RAR has responsibility to:

- a. Follow the guidelines and methodology given by the Group Head Audit & RAR.
- b. Exercise due professional care in carrying out audit & other assignments.
- c. Maintain integrity and objectivity.
- d. Remain objective, constructive and not be influenced by personal, business or other issues, which may impair impartiality.

5. AUTHORITY

5.1 The Audit & RAR Group is authorized to:

- a. Have unrestricted access to all information, functions, records, property, and personnel anywhere within the Bank (both local and overseas operations as well as Bank's subsidiaries).
- b. Allocate resources, set frequencies, select subjects, determine scope of work and apply the techniques required to accomplish audit objectives.
- c. Obtain specialized assistance, wherever required.

6. ACCOUNTABILITY¹⁴

6.1 Group Head Audit & RAR, in the discharge of his duties, shall be accountable to the Board of Directors / Audit Committee to:

- a. Submit an annual assessment on the adequacy and effectiveness of MCB Bank Ltd.'s (as well as its subsidiaries audited during the year) all processes (manual as well as technology based, including financial reporting, business operations and compliance with relevant laws & regulations) for controlling its activities and managing its risks in all the core areas of the Bank's / its subsidiary's operations.
- b. Provide periodic reports to the Audit Committee and the management summarizing the results of the audit activities, details of significant issues identified, together with recommendations for improvements.
- c. Provide half yearly/biannual report regarding sufficiency of the Audit & RAR Group resources of appropriate skills, experience and qualifications.
- d. Provide regular information on the status and results of the annual Audit & RAR Group plans.
- e. Co-ordinate with and provide oversight of other control and monitoring functions.

¹⁴ SBP's BSD Circular 03 of April 04, 2007 (Policy Framework in Banks)

- 6.2 The Board Audit Committee must assess, at least annually, the performance of the internal audit function. Further, external quality assurance review must be conducted at least once every five years by a qualified, independent assessor or assessment team from outside the Bank.¹⁵

7. LIMITATIONS

- 7.1 The internal audit function must not be involved in designing, selecting, implementing or operating specific internal control measures. Management may request advice from internal audit on matters related to risk and internal controls, nevertheless, the development and implementation of internal controls remains the responsibility of Management.¹⁶ The Audit & RAR staff is specifically prohibited from:
- a. Performing any operational duties, however Audit & RAR may comment on policies and procedures before their implementation (in line with the “Consultative” role as envisaged in the International Standards for Professional Practice of Internal Auditing published by the Institute of Internal Auditors);
 - b. Initiating or approving financial or non-financial transactions except those pertaining to Audit & RAR Group; and
 - c. Directing the activities of any member of staff not part of Audit & RAR Group, except to the extent such employee(s) have been appropriately assigned to audit team(s) or to otherwise assist the Audit & RAR Group.

8. SKILLS, TRAINING & ALTERNATE ARRANGEMENTS¹⁷

- 8.1 Audit & RAR staff will need to have sound judgment. This will require them to have appropriate experience and expertise to perform their work with proficiency and due professional care. Audit & RAR staff will engage in continuing professional development through structured training programs. However, if the knowledge, skills and competencies required to perform an engagement are not available within Audit & RAR Group, the Group Head will obtain alternative assistance from specialized professional firms or others with prior written approval of State Bank of Pakistan (SBP) /respective regulator of the host country and the Board’s Audit Committee.

9. STANDARDS OF PRACTICE

- 9.1 Audit & RAR staff must comply with Code of Ethics and the International Standards for Professional Practice of Internal Auditing published by the Institute of Internal Auditors (provided that these Standards are not in direct conflict with any regulatory instructions issued either by Host country or Home country).

10. FREQUENCY OF TESTING¹⁸

- 11.1 In general, all areas in the bank would be audited once in every two years, however, low risk non-branch entities would be audited / reviewed once in every three years subject to approval by the Audit Committee. Further, overseas operations will be covered in the audit plan at least once a

¹⁵ Central Bank of the UAE Notice No. CBUAE/BSN/N/2018/3017 dated October 16, 2018 (Internal Controls, Compliance and Internal Audit Regulation)

¹⁶ Central Bank of the UAE Notice No. CBUAE/BSN/N/2018/3017 dated October 16, 2018 (Internal Controls, Compliance and Internal Audit Regulation)

¹⁷ SBP’s BSD Circular 03 of April 04, 2007 (Policy Framework in Banks)

¹⁸ SBP’s BSD Circular 03 of April 04, 2007 (Policy Framework in Banks)

year¹⁹, however extent of the audits/reviews pertaining, to these operations, will be based on risk assessment carried out by Audit & RAR Group. Moreover, subsidiaries shall also be audited (subject to permissibility by applicable laws/regulations) at a minimum of once in every two years. Furthermore, high-risk areas would be reviewed more frequently. To determine which areas need more than minimal coverage, the following indicators will be considered:

- a. Analytical review and financial analysis that signal deterioration in a particular area.
- b. Audit findings that still require close review.
- c. Instructions/requests by Board of Directors or the Audit Committee or the management for special reviews.
- d. SBP / Regulatory Bodies / External Auditors' Inspection / Audit Report and / or exceptions in other examination reports.

11.2 Audit & RAR Group would reassess its audit / review plan and change the priorities as warranted. For example, if an unexpected crisis or demand arises, the internal audit staff should modify its schedule and possibly the scope of its reviews. In that case, it may delay the audit of an efficiently run area or restrict the scope of that audit to accommodate the demands of the more critical area.

11. REPORTING MECHANISM²⁰

11.1 Following will be the mechanism for reporting:

- a. Each audit assignment shall be followed by a report containing summary and details of findings, business impact / risk and recommendations sent to the Groups and administrative units or branches or divisions responsible.
- b. The reports shall be based on adequate working papers.
- c. The detail findings of the assignments shall be subject to a preliminary discussion with the auditee, in order to enable its responses to be included in the audit report.
- d. Depending on the criticality / degree / quantum of risk involved, findings of significance shall also be reported to the President as and when highlighted by Audit & RAR Group.
- e. Audit & RAR Group shall periodically follow-up on the implementation of its recommendations.
- f. Audit & RAR Group shall timely escalate significant audit / review findings to appropriate levels of management including the President if unresolved at levels of those responsible.
- g. Significant Audit / Review findings remaining unresolved within a reasonable time at the level of President's Office shall be reported to the Audit Committee.

12. CHECKING OF FRAUDS²¹

12.1 While it is the management's responsibility to design and implement programs and controls to prevent, deter and detect fraud, the Audit & RAR staff should have sufficient knowledge to evaluate the risk of fraud and the manner in which it is managed by the organization.

¹⁹ SBP's BPRD Circular 06 of August 06, 2018 (Governance Framework for Banks' Overseas Operations)

²⁰ SBP's BSD Circular 03 of April 04, 2007 (Policy Framework in Banks)

²¹ SBP's BSD Circular 03 of April 04, 2007 (Policy Framework in Banks)

Fraud Deterrence Programs

- 12.2 Audit & RAR Group shall assist the management in designing programs for deterrence of frauds. These programs include, but are not restricted to the following:
- a. Setting up of a Whistle Blowing Program. The Whistle Blowing Program refers to the deliberate / voluntary disclosure of individual or organizational impropriety by a person who has or had privileged access to data, events or information about an actual, suspected or anticipated wrongdoing within or by an organization that is within its ability to control.
 - b. Assisting the management in identification of internal control deficiencies and suggesting measures for removal thereof.
 - c. Commenting on the design effectiveness of the controls to be implemented by the management.
 - d. Assisting the management in ensuring strict compliance with respect to recommendations to overcome the weaknesses identified in the reports of the Internal & External Audits as well as the State Bank of Pakistan/respective regulator of the host country.

Employee Guidance Where Fraud Is Suspected

- 12.3 Employees are encouraged to report the acts involving fraudulent activities to the Whistle Blowing Function established within the Audit & RAR Group. The Whistle Blowing Program covers in detail the employees' rights, rewards and obligations with respect to making such disclosures.

13. MANAGEMENT RESPONSIBILITIES

- 13.1 The Management should ensure that all information relevant to the discharging of responsibilities by the Audit & RAR Group including those related to investigation of frauds is provided promptly. The information should be complete, correct, reliable, accurate and timely.

14. CONFIDENTIALITY AND REPORTING PROCEDURES

- 14.1 Audit & RAR Group should respect the value and ownership of information they receive. They should not disclose information without appropriate authority unless there is a legal or professional obligation to do so. They shall not use information for any personal gain or in any manner that would be contrary to the law or detrimental to the legitimate and ethical objectives of the Bank.
- 14.2 Whenever the Audit & RAR Group has determined that there is evidence that fraud may exist, that matter should be brought into the attention of an appropriate level of management. This is appropriate even if the matter might be considered inconsequential, such as a minor defalcation by an employee at a lower level within the Bank. Fraud involving senior management and fraud (whether caused by senior management or other employees) that causes a material misstatement of the financial statements should be reported directly to the Audit Committee. In addition, the Audit & RAR Group should reach an understanding with the Audit Committee regarding nature and extent of communications with the Committee about misappropriations perpetrated by lower-level employees.

15. REVIEW

- 15.1 The Audit Committee shall review and assess the adequacy of the Global Internal Audit Policy on need basis but at least once in every two years recommending changes, if necessary, to the Board of Directors for approval.

16. GLOSSARY

Audit & RAR	Audit & Risk Assets Review
CEO	Chief Executive Officer
HEC	Higher Education Commission of Pakistan
SBP	State Bank of Pakistan
SECP	Securities and Exchange Commission of Pakistan
HR&RC	Human Resource & Remuneration Committee