

Pursuant to Article 17 paragraph 1 point 2) of the Law on the Central Bank of Montenegro OG RoM no. 52/00 and 47/01), and with regard to Article 76, paragraph 2 of the Law on Banks (OG MNE no. 17/08), at its meeting held on 17 and 18 September 2008, the Council of the Central Bank of Montenegro passed the following

## **DECISION on Internal Audit in Banks**

### **I. General Provision**

#### **Subject of the Decision**

##### **Article 1**

This Decision regulates the main principles of organization of internal audit in bank and defines the bank's obligations with respect to the establishment and functioning of internal audit.

### **II. Organization and Functioning of Internal Audit**

#### **Normative Regulation of Internal Audit**

##### **Article 2**

Organization of internal audit in bank, as well as the position, powers and responsibilities of persons performing internal audit shall be regulated by bank's Articles of Association and other regulations in line with the Law on Banks and this Decision.

#### **Internal Audit Act**

##### **Article 3**

Bank is obliged to pass a regulation on internal audit that shall define, as the minimum requirements:

- 1) internal audit operations;
- 2) manner of internal audit functioning, with a clear and concise description of individual internal audit procedures, in particular those with regard to:
  - unannounced audit,
  - handling records and documents selected to be audited,
  - assessment and evaluation of the implemented internal control system;
- 3) elements to be included in report on performed internal audit;

- 4) elements to be included in annual report on internal audit functioning.

### **Elements of Internal Audit Annual Plan**

#### **Article 4**

In preparing the internal audit annual plan, bank is obliged to:

- 1) determine internal audit activities that will be in the function of accomplishing bank business objectives;
- 2) define the subject of audit in a comprehensive, detailed and clear manner;
- 3) increase frequency of internal audit in areas of bank business operations involving higher risks.

### **Internal Audit Methodology**

#### **Article 5**

Internal audit methodology shall be determined by internal auditor or a person who manages the internal audit unit (hereinafter: internal auditor).

### **Audit Risks**

#### **Article 6**

Internal auditor shall plan and perform audits in a manner which enables him to extend an opinion on the audit subject, with the minimum risk of extending a wrong opinion.

When defining audit findings, the internal auditor shall consider audit risks which may affect the correctness of findings, in particular:

- 1) inherent risk - the risk that some of materially important facts shall not be revealed during the audit, regardless of the established internal control system;
- 2) control risk - the risk that some of materially important facts shall not be revealed during the audit because of weaknesses in the internal control system ;
- 3) detection risk -the risk that some of materially important facts shall not be revealed by methods and techniques implemented in a specific audit.

Internal audit report shall also contain the evaluation of level of audit risks related to the specific audit.

### **Access to Bank Documents**

#### **Article 7**

Bank shall ensure that the internal auditor has free access to business books and other documents and data necessary for performing the audit.

### **Treatment of Significant Irregularities**

#### **Article 8**

If during the audit of individual elements of bank business operations the internal auditor determines that there are illegal operations or violations of risk management

rules that threaten the bank's liquidity, solvency or safety of its operations, the internal auditor is obliged to immediately inform the Central Bank, Board of Directors and Audit Committee of such facts.

## **Audit Report**

### **Article 9**

The internal auditor shall submit the audit report to the Audit Committee for comment, in accordance with the audit plan.

The report under paragraph 1 of this Article shall include, as the minimum requirements:

- 1) description of the audit subject, findings with the explanation and the analysis of effect of identified deficiencies and irregularities;
- 2) suggestions and recommendations for the removal of identified deficiencies and irregularities;
- 3) timelines for the removal of identified irregularities and names of persons responsible for the removal of these irregularities;
- 4) suggestions for the improvement of the internal control system functioning;
- 5) other statements, evaluations and suggestions with regard to the removal of identified irregularities.

## **Acting in line with the Internal Auditor's Recommendations**

### **Article 10**

The person responsible for removal of noted operational irregularities shall timely consider internal audit recommendations and report to the Board of Directors, Audit Committee and the internal auditor on activities related to the removal of identified deficiencies and irregularities.

The internal auditor shall monitor implementation of the internal audit recommendations and prepare the report on implementation of recommendations, with clearly stated degree of fulfilment of obligations arising from the recommendations and reasons for their possible non-fulfilment.

## **Internal Auditor's Working Papers**

### **Article 11**

A copy of the internal audit report that is kept in the records of the internal audit must include, as an annex, working papers produced in the process of audit in the reporting period.

Working papers shall represent documents and material collected or prepared by the internal auditor during the audit, which:

- 1) assist the internal auditor in planning and performing the audit (for example: working papers from previous audits);
- 2) serve for audit records;

- 3) serve as the evidence that the audit is performed in line with international standards for professional practice of internal auditing;
- 4) assist in supervision, revision, and coordination of internal audit;
- 5) enable the internal auditor to create the final report on performed audit.

Working papers shall incorporate documentation, data and information which would enable other internal auditor to understand the performed audit. Working papers shall not be too extensive.

## **Annual Report**

### **Article 12**

Annual report on internal audit shall be created by the internal auditor and submitted to the Audit Committee.

The report from paragraph 1 of this Article shall include, as the minimum requirements:

- 1) a report on the achievement of the internal audit annual plan;
- 2) a summary of significant internal audit findings ;
- 3) evaluation of measures undertaken to remove the identified irregularities;
- 4) information on persons responsible for the removal of operational irregularities related to the internal auditor's recommendations;
- 5) manner of follow-up on recommended activities for the removal of identified irregularities and deficiencies in bank operations;
- 6) manner and responsibility for the preparation, use and keeping of documents on the performed internal audit.

## **Cooperation with External Auditor and the Central Bank**

### **Article 13**

The internal auditor shall cooperate with the Central Bank and external auditor with a view to considering the identified risky areas, assessment of undertaken measures for the removal of irregularities in bank operations, and to improve the quality of cooperation between internal and external auditors.

## **III. Final Provisions**

### **Article 14**

With the coming into force of this Decision, the Decision on Bank Internal Audit (OG RoM No. 72/03) shall cease to be valid.

**Article 15**

This Decision shall come into force on the eighth day of its publishing in the "Official Gazette of Montenegro".

**THE COUNCIL OF THE CENTRAL BANK OF MONTENEGRO**

**PRESIDENT OF THE COUNCIL  
Ljubiša Krgović**

Decision No. 0101-323/11-11  
Podgorica, 18 September 2008