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2014-08

Banking and Financial Institutions (Internal Control and Internal Audit) Regulations, 2014

United Republic, Tanzania

Ministry of Finance

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SUDSIDIARY LEGISLATION

To the Gazette of the United Republic of Tanzania No. 34 Vol. 95 Dated 22nd August, 2014

Printed by the Government Printer, Dar es Salaam by order of Government

GOVERNMENT NOTICE NO. 286 published on 22/08/2014

**THE BANKING AND FINANCIAL INSTITUTIONS (INTERNAL CONTROL
AND INTERNAL AUDIT) REGULATIONS, 2014**

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THE BANKING AND FINANCIAL INSTITUTIONS ACT
(CAP 342)

REGULATIONS

Made under section 71

THE BANKING AND FINANCIAL INSTITUTIONS (INTERNAL CONTROL
AND INTERNAL AUDIT) REGULATIONS, 2014

PART I
PRELIMINARY PROVISIONS

- Citation **1.** These Regulations may be cited as the Banking and Financial Institutions (Internal Control and Internal Audit) Regulations, 2014.
- Application **2.** These regulations shall apply to all banks and financial institutions.
- Interpretation **3.** In these Regulations unless the context otherwise requires-
- “Act” means the Banking and Financial Institutions Act;
“Bank ” means Bank of Tanzania;
“bank” has the meaning ascribed to it in the Act;
“director” has the meaning ascribed to it in the Act;
“financial institution” has the meaning ascribed to it in the Act;
“independent director” means a director who-
- (a) does not hold any executive or management position in a bank or financial institution;
 - (b) does not have, directly or indirectly, a significant interest in the bank or financial institution including any parent or subsidiary in a consolidated group with the bank or financial institution;
 - (c) has not been employed by the bank or financial institution or a banking group of which he currently forms part in any executive capacity for the preceding three years;

- (d) is not a member of the family of an individual who is, or has been in any of the past three years, employed by the bank or financial institution or the banking group in an executive capacity;
 - (e) is not a professional advisor to the bank or financial institution or the banking group;
 - (f) is free from any business or other relationship which seems to interfere with the individual's capacity to act in an independent manner; and
 - (g) does not receive remuneration contingent upon the performance of the bank or financial institution;
- “internal audit” means an independent, objective assurance and consulting activity, oriented to add value and bring in a systematic and disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes;
- “internal auditor” means a person who is heading the internal audit function of a bank or financial institution;
- “internal control” means a concerted action of the Board of Directors, senior management and all levels of personnel, designed to provide reasonable assurance regarding the achievement of objectives, the effectiveness and efficiency of operations and the reliability of financial reporting and compliance with applicable laws, regulations and internal policies;
- “internal controls” means policies and procedures established and implemented individually or with other policies or procedures, to manage and control a particular risk or business activity, or combination of risks or business activities, to which the bank or financial institution is exposed or in which it is engaged; and
- “non-executive director” means a director who does not hold any executive or management position in a bank or financial institution.

Objectives

4. The objectives of these Regulations are to ensure that-
 - (a) banks and financial institutions establish effective systems of internal controls to promote the safety and soundness of their operations; and
 - (b) there exists an effective internal audit function

responsible for independent evaluation of the effectiveness of the system of internal controls.

PART II CORPORATE GOVERNANCE

Corporate
governance
framework

5.-(1) A bank or financial institution shall establish an effective corporate governance framework which defines the character of the institution and promotes an organizational culture that provide the foundation for effective internal control and internal audit.

(2) The corporate governance framework referred to in sub-regulation (1) shall, at a minimum, include the following-

- (a) duties of the Board of Directors including responsibility for business and risk strategy, organisation, financial soundness and governance;
- (b) duties of senior management including responsibility to ensure that the bank's or financial institution's activities are consistent with the business strategy, risk tolerance or appetite and policies approved by the board;
- (c) organization structure that facilitates effective decision making and good governance, with clear lines of responsibility and accountability;
- (d) effective risk management, compliance and internal audit functions, each with sufficient authority, stature, independence, resources and access to the board; and
- (e) system of internal controls consistent with the size, complexity and nature of the bank's or financial institution's operations.

Responsibilities
of Board of
Directors

6.-(1) The Board of Directors shall be responsible for ensuring that an adequate, effective and efficient system of internal controls and internal audit function are established and maintained.

(2) The Board of Directors shall, in exercising its responsibilities stipulated under sub-regulation (1)-

- (a) promote high ethical and integrity standards, and

establish a culture within the organization that emphasizes and demonstrates to all levels of personnel the importance of internal controls;

- (b) approve and review, at least annually, the overall business strategies and all significant policies of the bank or financial institution;
- (c) understand major risks facing the bank or financial institution and set acceptable levels for those risks and ensure that senior management takes the steps necessary to identify, measure, monitor and control the risks;
- (d) approve the organisational structure;
- (e) ensure that senior management monitors the effectiveness of the system of internal controls; and
- (f) review at least annually the effectiveness of the system of internal controls and internal audit function.

(3) The strategies and policies referred to under sub-regulation (2) shall be submitted to the Bank not later than thirty days after being approved by the Board, provided that where any changes are made to the strategies and policies, the bank or financial institution shall clearly indicate areas of such changes.

Establishment
and
responsibilities
of audit
committee

7.-(1) The Board of Directors shall establish an Audit Committee of the board responsible for providing oversight of the financial reporting and system of internal controls, audit process and compliance with legal and regulatory requirements.

(2) The audit committee shall, in exercising the responsibility stipulated under sub-regulation (1), carry out the duties specified in the Schedule to these Regulations.

(3) The audit committee shall be composed of at least three non-executive directors, two of whom shall be independent members having accounting, auditing or related financial management experience.

(4) The audit committee of a bank or financial institution shall report to the Board of Directors at least quarterly.

Responsibilities
of senior

8.-(1) The senior management of a bank or financial

management institution shall be responsible for implementing strategies and policies approved by the Board of Directors and for establishing an effective system of internal controls.

(2) In exercising the responsibilities stipulated under subregulation (1), senior management shall-

- (a) establish organizational and procedural controls;
- (b) develop processes that identify, measure, monitor and control risks;
- (c) maintain an organisational structure that clearly assigns responsibility, authority and reporting relationships;
- (d) ensure that delegated responsibilities are effectively carried out;
- (e) ensure that all personnel understand their roles in the internal control process and adhere to policies and procedures affecting their duties and responsibilities;
- (f) ensure that outsourced services do not jeopardize the system of internal controls; and

- (g) monitor the adequacy and effectiveness of the system of internal controls.

PART III SYSTEM OF INTERNAL CONTROLS

Establishment
of system of
internal
controls

9. A bank or financial institution shall establish an effective system of internal controls consisting of the following elements-

- (a) management oversight and the control culture;
- (b) risk identification and assessment;
- (c) control activities and segregation of duties;
- (d) information and communication; and
- (e) monitoring activities and correcting deficiencies.

Objectives of
the system of
internal
controls

10.-(1) The system of internal controls referred to under regulation 9 shall-

- (a) promote the efficiency and effectiveness of activities and measures that protect the bank or financial institution from loss;

- (b) ensure the relevance, reliability, completeness and timeliness of financial and management information;
- (c) ensure compliance with applicable laws and regulations;
- (d) reduce fraud, misappropriation and errors, and mitigate other risks faced by the institution;
- (e) identify the relative risks of each area of activity of the bank or financial institution; and
- (f) assist the bank or financial institution to allocate appropriate amounts of time and resources on the higher risk areas.

Risk
identification
and assessment

11.- (1) A bank or financial institution shall ensure that its system of internal controls is designed in a manner that it can identify and continually assess all material risks.

(2) The material risks under sub-regulation (1) shall, at a minimum, include credit, liquidity, market, operational, strategic and compliance risks.

Control
activities and
segregation of
duties

- 12.** A bank or financial institution shall-
- (a) establish an appropriate control structure, with control activities defined at every business level including-
 - (i) top level reviews;
 - (ii) appropriate activity controls for different departments or divisions;
 - (iii) physical controls;
 - (iv) assess compliance with exposure limits and follow-up on cases of non-compliance;
 - (v) a system of approvals and authorizations;
 - (vi) a system of verification and reconciliation; and
 - (b) allocate and assign its personnel with duties and responsibilities that are not conflicting and ensure that areas of potential conflict are identified, minimized, and subject to careful and independent monitoring.

Information and

13.-(1) A bank or financial institution shall-

communication

- (a) establish an effective management information system to collect, record and retain adequate and comprehensive financial and non-financial information relevant for decision making; and
- (b) establish effective channels of communication to ensure that staff fully understand and adhere to policies and procedures affecting their duties and responsibilities and other relevant information is communicated to the appropriate personnel.

- (2) The management information system referred to under sub-regulation (1) shall cover all operations of the bank or financial institution and shall be secure, monitored independently and supported by adequate contingency arrangements.

Monitoring activities and correcting deficiencies

14.-(1) A bank or financial institution shall ensure that the overall effectiveness of its internal controls is monitored on an ongoing basis through periodic evaluations and reviews carried out by its business lines and the internal auditor.

(2) Where internal control deficiencies are identified by business lines, internal audit, or other control personnel, such deficiencies shall be reported timely to senior management and the Board of Directors and shall be addressed promptly.

Annual review of system of internal controls

15. A bank or financial institution shall review its system of internal controls least once annually to assess its effectiveness and appropriately address any new or previously uncontrolled risks.

PART IV INTERNAL AUDIT

Appointment of the internal auditor

16.-(1) A bank or financial institution shall appoint an internal auditor whose function shall be to evaluate the effectiveness of the system of internal controls, risk management framework and governance processes.

(2) A bank or financial institution shall not appoint any

person to hold the post of internal auditor without obtaining prior approval of the Bank.

(3) A bank or financial institution shall, where the post of the internal auditor falls vacant, notify the Bank in writing within seven days from the date the position falls vacant.

(4) The post of internal auditor shall be deemed to be vacant due to dismissal, resignation, incapacity or any other reason.

Qualifications
of the internal
auditor

17.-(1) The internal auditor of a bank or financial institution shall be a Certified Public Accountant or its equivalent and be registered with the National Board of Accountants and Auditors.

(2) The Internal Auditor of a bank or financial institution shall be a person who has at least three years' experience in the regular audit as internal or external auditor.

Reporting by
Internal
Auditor

18.-(1) The Internal Auditor shall report to the Audit Committee or the Board of Directors.

(2) The reports of the Internal Auditor shall contain audit findings, recommendations and responses of senior management.

(3) The reports and working papers of the Internal Auditor shall be kept for at least five years.

Independence
of the Internal
Auditor

19.-(1) The Board of Directors shall ensure that the Internal Auditor is independent and competent staff and resources are available for the adequate performance of his functions and duties.

(2) The Internal Auditor shall, at least annually, confirm to the Board of Directors the status of organizational independence of the internal audit function, including adequacy of resources and any limitations of scope.

(3) The Internal Auditor shall refrain from auditing specific operations which he was previously involved.

Audit
charter

20.-(1) A bank or financial institution shall have a written audit charter stating the purpose, standing and authority of the internal audit function.

(2) Where any changes are made to the audit charter, the revised charter clearly indicating areas of change shall be submitted to the Bank not later than thirty days after its approval by the Board.

(3) The audit charter shall be approved by the Board of Directors.

(4) At a minimum, the internal audit charter shall-

(a) provide the objectives and scope of the internal audit function;

(b) state the Internal Auditor's position within the organization, his powers, responsibilities, accountability and relations with other control functions;

(c) mandate the Internal Auditor with the right of initiative and authority to have direct access to and communicate with any member of staff, to examine any activity of the institution and access any records, files or data of the institution;

(d) establish the Internal Auditor's authority to communicate directly to the Board of Directors, the audit committee, the external auditors and where appropriate to the Bank;

(e) specify the terms and conditions according to which the Internal Auditor can be called upon to provide advisory services or perform other special tasks;

(f) outline the criteria for outsourcing the internal audit function;

(g) provide for requirement to comply with sound internal auditing standards;

(h) establish procedures for the coordination of the internal audit function with the external auditor; and

(i) establish an annual independent review of the internal audit function, which may be carried out by the external auditor, the audit committee or any other independent party.

Duties of
the Internal
Auditor

to-

21.-(1) The duties of the Internal Auditor shall include

- (a) ensure that internal audit complies with sound internal auditing standards and with a relevant code of ethics;
- (b) examine and evaluate the adequacy and effectiveness of the system of internal controls;
- (c) review the application and effectiveness of risk management procedures and risk assessment methodologies;
- (d) review the adequacy of management information system;
- (e) review the accuracy and reliability of the accounting records and financial reports;
- (f) review the system of assessing capital in relation to assessment and estimation of risks;
- (g) assess the efficiency of the usage of resources;
- (h) review the system established to ensure compliance with legal and regulatory requirements, codes of conduct and the implementation of policies and procedures;
- (i) test the reliability and timeliness of the regulatory reporting; and
- (j) carry out special investigations.

Audit plan

22. -(1) The Internal Auditor shall prepare an annual plan for the assignments to be performed during the next financial year and present that plan to the audit committee for review and to the Board of Directors for approval not later than 31st December each year.

(2) A bank or financial institution shall submit its annual audit plan to the Bank not later than 15th January each year.

(3) The annual audit plan referred to under sub-regulation (1) shall include-

- (a) the timing and frequency of planned internal audit work;
- (b) an evaluation of internal controls and on a written assessment of material risks;
- (c) details of the necessary resources in terms of

- personnel and other resources; and
- (d) the time allocated for training.

(4) The Internal Auditor shall report to the Board of Directors and obtain approval for any changes in the audit plan, and submit a copy of the revised audit plan to the Bank within fourteen days after approval by the Board of Directors.

Outsourcing
internal
audit
function

23.-(1) A bank or financial institution shall not outsource its internal audit function without the prior approval of the Bank.

(2) Where a bank or financial institution outsources its internal audit function, the Board of Directors shall remain ultimately responsible for ensuring that the system of internal controls and the internal audit are adequate and operate effectively.

Duty to
inform the
Internal
Auditor

24. Senior management of a bank or financial institution shall ensure that the Internal Auditor is informed of new developments, initiatives, products and operational changes for purposes of early identification of all associated risks.

PART V GENERAL PROVISIONS

Reporting
to the Bank

25.-(1) A bank or financial institution shall submit to the Bank an audit report and minutes of the meeting of the Audit Committee or Board of Directors which discussed the audit report.

(2) The report referred to under sub-regulation (1) shall be submitted not later than forty five days after the end of the quarter.

(3) Notwithstanding the provisions of sub-regulation (1), the Internal Auditor of a bank or financial institution shall immediately report to the Bank any significant audit findings including fraud, misappropriation, errors, omission or any other significant irregularities uncovered in the course of audit.

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(4) The report submitted to the Bank shall contain a summary of significant audit findings referred to under sub-regulation (3) and remedial actions taken by senior management to rectify such findings.

(5) For the purpose of sub-regulation (3), significant audit findings are the findings which have an adverse impact on the financial performance and condition of a bank or financial institution.

Sanctions

26.-(1) Without prejudice to penalties and actions prescribed by Act, the Bank may impose on any bank or financial institution any of the following sanctions for non-compliance-

- (a) a penalty of the amount to be determined by the Bank;
- (b) suspension from office of the defaulting director, officer or employee; and
- (c) disqualification of the defaulting director, officer or employee from holding any position or office in any bank or financial institution under the supervision of the Bank.

(2) The penalty referred to in paragraph (a) of sub regulation (1) shall apply to directors, officers or employees of the bank or financial institution.

Revocation
of GN No.
79
of 2005

27. The Banking and Financial Institutions (Internal Control and Internal Audit) Regulations, 2005 are hereby revoked.

SCHEDULE

(Made under Regulation 7)

DUTIES AND RESPONSIBILITIES OF BOARD AUDIT COMMITTEE

The main areas of responsibility of the audit committee are listed below by broad categories:

Financial reporting, including disclosures

1. Monitoring the financial reporting process and its output;
2. Overseeing the establishment of accounting policies and practices by the bank or financial institution and reviewing the significant qualitative aspects of the bank's accounting practices, including accounting estimates and financial statement disclosures;
3. Monitoring the integrity of the bank's or financial institution's financial statements and any formal announcements relating to the bank's or financial institution's financial performance;
4. Reviewing significant financial reporting judgments contained in the financial statements; and
5. Reviewing arrangements by which staff of the bank or financial institution may confidentially raise concerns about possible improprieties in matters of financial reporting.

Internal control

6. Ensuring that senior management establishes and maintains an adequate and effective internal control framework. Such framework should be designed to provide assurance in areas including reporting (financial, operational, risk), monitoring compliance with laws, regulations and internal policies, efficiency and effectiveness of operations and safeguarding of assets.

Internal audit

7. Monitoring and reviewing the effectiveness of the bank's or financial institution's internal audit function;
8. Approving the internal audit plan, scope, cycle and budget;
9. Reviewing and discussing internal audit reports;
10. Ensuring that the internal audit function maintains open communication with senior management, external auditors, the supervisory authority, and the audit committee;
11. Reviewing discoveries of fraud and violations of laws and regulations as raised by the Internal Auditor;

12. Reviewing the audit charter and the code of ethics of the internal audit function;
13. Approving, or recommending to the board for its approval, the annual remuneration of the internal audit function as a whole, including the Internal Auditor; and
14. Approving, or recommending to the board for its approval, the appointment, reappointment or removal of the Internal Auditor.

External auditor

Appointment, reappointment, dismissal and remuneration

15. Approving a set of appropriate objective criteria for selecting the external audit firm of the bank or financial institution;
16. Approving, or recommending to the board or shareholders for their approval, the appointment, re-appointment and removal of the external audit firm; and
17. Approving the remuneration and terms of engagement of the external audit firm.

Compliance with relevant ethical requirements, in particular independence and objectivity

18. Reviewing and monitoring the independence of the external audit firm, and in particular the provision of additional services to the bank or financial institution, including the related safeguards that have been applied to eliminate identified threats to independence or reduce them to an acceptable level;
19. Reviewing and monitoring the external auditor's objectivity and the effectiveness of the audit process;
20. Developing and implementing a policy on the engagement of the external audit firm for the supply of non-audit services, taking into account relevant ethical guidelines on the provision of non-audit services by the external audit firm;
21. Approving the total fees charged for the audit of the financial statements and for non-audit services provided by the external audit firm and external audit network firms to the entity and its components controlled by the entity.
22. Overseeing the external audit of the annual and consolidated accounts;
23. Discussing with the external audit firm key matters arising from the external audit, and in particular any identified material weaknesses in internal controls in relation to the financial reporting process; and
24. Discussing the written representations the external audit firm is requesting from senior management and, where appropriate, those charged with governance;

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Remedial actions

25. Ensuring that senior management is taking necessary corrective actions to address the findings and recommendations of internal auditors and external auditors in a timely manner;
26. Addressing control weaknesses, non-compliance with policies, laws and regulations and other problems identified by internal auditors and external auditors, and
27. Ensuring that deficiencies identified by supervisory authorities related to the internal audit function are remedied within an appropriate time frame and reporting to the board of directors on the progress of necessary corrective actions.

Dar es Salaam,
....., 2014

BENNO J. NDULU
Governor