



**BAHRAIN
MIDDLE EAST
BANK**

بنك البحرين والشرق الاوسط

INTERNAL AUDIT CHARTER



Internal Audit Charter

Internal Audit Department

Approval Authority
Audit Committee

Date Approved
3 May 2018

Date of previous approval
26 July 2017

DOCUMENT ORIGINATION & REVISION HISTORY

Author	Approval Authority	Date of Approval	Revision Details (Topics amended)
Internal Audit	Audit Committee	5 May 2014	Implementation of Internal Audit Charter
Internal Audit	Audit Committee	12 May 2016	Reviewed and reformatted. No other changes done.
Internal Audit	Audit Committee	26 July 2017	Amended to reflect the changes in the International Professional Practices Framework (“IPPF”) (effective 1 January 2017) Addition of Mission and Core Principles introduced as part of the amended IPPF. Replacement of references to Practice Advisories, Practice Guides and Position Papers with Implementation Guidance and Supplemental Guidance.
Internal Audit	Audit Committee	3 May 2018	In line with the new rules on Internal Audit introduced in the February 2018 update to the Rulebook a) Added section on the criteria for when and how the internal audit function may rely on other assurance service providers or may outsource some of its engagements to external expert. b) The conditions according to which the internal audit function can be called upon to provide consulting or advisory services or to carry out another special task.



Internal Audit Charter

Internal Audit Department

Approval Authority

Date Approved

Date of previous approval

Audit Committee

3 May 2018

26 July 2017

DISTRIBUTION & ACCESS

Ownership of and a hard copy of this document shall rest with the department which shall provide access to relevant staff, auditors, and other authorised persons as and when deemed necessary. External auditors and regulatory authorities can be given access to the document with the consent of the department head. No staff member or any outsider is allowed to copy or reproduce the document in any form for purposes of distributing to third parties without the approval of the department. Should there be any provisions in this policy/procedure manual that contravene Central Bank of Bahrain Regulations (CBB), CBB regulations shall prevail.



Internal Audit Charter

Internal Audit Department

Approval Authority
Audit Committee

Date Approved
3 May 2018

Date of previous approval
26 July 2017

TABLE OF CONTENTS

1. INTRODUCTION4

2. ESTABLISHMENT OF THE INTERNAL AUDIT FUNCTION4

3. ORGANIZATION4

4. PURPOSE, MISSION AND CORE PRINCIPLES4

5. PROFESSIONALISM5

6. INDEPENDENCE AND OBJECTIVITY5

7. AUTHORITY6

8. SCOPE AND RESPONSIBILITIES6

9. INTERNAL AUDIT PLAN AND RELIANCE ON OTHER SERVICE PROVIDERS7

10. REPORTING AND MONITORING8

11. RELATIONS WITH EXTERNAL PARTIES AND REGULATORY AUTHORITITES8

12. QUALITY ASSURANCE AND IMPROVEMENT PROGRAM8

13. CIRCULATION OF THE CHARTER AMONG THE BANK'S STAFF9

14. REVIEW OF THE CHARTER9

	Internal Audit Charter		
	<i>Internal Audit Department</i>		
	Approval Authority	Date Approved	Date of previous approval
	<i>Audit Committee</i>	<i>3 May 2018</i>	<i>26 July 2017</i>

1. INTRODUCTION

Internal Audit is an essential part of senior management structure of Bahrain Middle East Bank B.S.C. (the "Bank") working and reporting to and under the directions of the Audit Committee ("AC") of the Board of Directors ("Board"). An effective internal audit function is critical to Bank's control framework

Internal Audit is an independent and objective assurance and consulting activity that is guided by philosophy of adding value to improve operations of the Bank. It assists the Bank in accomplishing its objectives by bringing systematic and disciplined approach to evaluate and improve the effectiveness of Bank's Risk Management, Internal Controls and Corporate Governance systems and processes

Internal Audit also provides the Board information that is not biased in any way by the levels of management that its reports cover.

It is the policy of the Bank to maintain an effective internal audit function, which is an '*independent, objective, assurance and consulting activity*', designed to add value and improve the Bank's operations.

This Internal Audit charter defines the purpose, standing, authority and responsibility etc. of Internal Audit function and its contribution to the good corporate governance of the Bank.

2. ESTABLISHMENT OF THE INTERNAL AUDIT FUNCTION

The Internal Audit function of the Bank is established by the Board, which is the highest level of the Bank's governing body. The Board also specified the purpose, authority and responsibility etc. of Internal Audit as part of its oversight role.

3. ORGANIZATION

The Internal Audit function shall report directly to the AC and administratively to the Chief Executive Officer ("CEO") of the Bank.

The Head of Internal Audit will report functionally to the AC and administratively to CEO.

The Audit Committee will:

- Approve the internal audit charter.
- Approve the risk based internal audit plan.
- Approve the internal audit budget and resource plan.
- Receive communications from Head of the Internal Audit on the internal audit activity's performance relative to its plan and other matters.
- Approve decisions regarding the appointment and removal of the Head of Internal Audit.
- Approve the remuneration of the Head of Internal Audit.
- Make appropriate inquiries of management and the Head of Internal Audit to determine whether there is inappropriate scope or resource limitations.

The Head of Internal Audit will communicate and interact directly with the Audit Committee, including in executive sessions and between Audit Committee meetings as appropriate.

4. PURPOSE, MISSION AND CORE PRINCIPLES

The basic purpose of internal audit function is to provide independent and objective review of the efficiency of bank's operations. This would include a review of the accuracy and reliability of Bank's accounting records and financial reports as well as a review of the adequacy and effectiveness of Bank's risk management, control, and governance processes.

Internal audit provides independent and objective assurance to the Board and senior management on the quality and effectiveness of a Bank's internal control, risk management and governance systems and processes, thereby helping the Board and senior management protect the Bank and its reputation.

The mission of Internal Audit is to enhance and protect organizational value by providing risk-based and objective assurance; advice and insight ensure that the Bank's businesses are conducted according to the highest professional and ethical standards.

	Internal Audit Charter		
	<i>Internal Audit Department</i>		
	Approval Authority	Date Approved	Date of previous approval
	<i>Audit Committee</i>	<i>3 May 2018</i>	<i>26 July 2017</i>

4. PURPOSE, MISSION AND CORE PRINCIPLES (CONTINUED)

The Core Principles for the Professional Practice of Internal Auditing (Core Principles) are the key elements that describe internal audit effectiveness.

The Core Principles governing the Internal Audit function are:

- Demonstrates integrity
- Demonstrates competence and due professional care
- Is objective and free from undue influence (independent)
- Aligns with the strategies, objectives and risks of the organization
- Is appropriately positioned and adequately resourced
- Demonstrates quality and continuous improvement
- Communicates effectively
- Provides risk-based assurance
- Is insightful, proactive, and future-focused
- Promotes organizational improvement

5. PROFESSIONALISM

The internal audit activity will govern itself by adherence to Mission of Internal Audit and mandatory elements of The International Professional Practices Framework (Definition of Internal Auditing, the Core Principles, the Code of Ethics, and the International Standards for the Professional Practice of Internal Auditing (Standards)). This mandatory guidance constitutes principles of the fundamental requirements for the professional practice of internal auditing and for evaluating the effectiveness of the internal audit activity's performance.

The Institute of Internal Auditors' Implementation guidance and Supplemental guidance will also be adhered to as applicable to guide operations.

In addition, the internal audit activity will adhere to Bank's relevant policies and procedures and the internal audit activity's standard operating procedures manual.

The Head of internal audit and individual auditors shall perform their tasks with proficiency and due professional care. It is the responsibility of Head of Internal Audit to ensure that internal audit collectively possesses and maintains the skills and knowledge necessary for performing its responsibilities effectively and staff are appropriately trained.

6. INDEPENDENCE AND OBJECTIVITY

The internal audit activity will remain free from interference by any element in the Bank, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of a necessary independent and objective mental attitude.

Internal auditors will have no direct operational responsibility or authority over any of the activities audited including compliance function. Accordingly, they will not implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that may impair internal auditor's judgment or independence. The internal audit function shall not be directly responsible for operational risk management or involved with the setting of risk appetite or risk tolerance but be responsible for reviewing robustness of the process of how the limits are set and why and how they are adjusted in response to changing circumstances.

Internal auditors will exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal auditors will make a balanced assessment of all the relevant circumstances and not be unduly influenced by their own interests or by others in forming judgments.

Impairments to the independence or objectivity of the Head of Internal Audit or any individual auditor shall be reported to the AC. The Head of Internal Audit will confirm to the AC, at least annually, the organizational independence of the internal audit activity.

	Internal Audit Charter		
	<i>Internal Audit Department</i>		
	Approval Authority	Date Approved	Date of previous approval
	<i>Audit Committee</i>	<i>3 May 2018</i>	<i>26 July 2017</i>

7. AUTHORITY

The internal audit activity, with strict accountability for confidentiality and safeguarding records and information, is authorized full, free and unrestricted access to any and all of Bank's records, physical properties, functions, policy statements, procedures, and personnel as necessary for the accomplishment of its mission.

All employees are required to assist the internal audit activity in fulfilling its roles and responsibilities.

Internal audit will have free access to the AC and Board.

Internal audit will have authority to allocate resources, set frequencies, select subjects, determine scopes of work, and apply the techniques required to accomplish the audit objectives.

8. SCOPE AND RESPONSIBILITIES

Scope of Internal audit covers all activities, operations and processes (including outsourced activities) of the Bank. All the entities of the Bank, including its subsidiaries, shall fall within the overall scope of internal audit.

The scope of internal audit work includes, but not limited to, the examination and evaluation of the adequacy and effectiveness of Bank's governance, risk management, and internal controls in the context of both current and potential future risks as well as the quality of performance in carrying out assigned responsibilities to achieve Bank's stated goals and objectives. This work also involves periodic testing of transactions, best practice reviews, special audits, appraisal of regulatory requirements, investigation, and implementing measures to help prevent and detect fraud.

Internal Audit shall:

- Evaluate risk exposure relating to achievement of Bank's strategic objectives.
- Monitor and evaluate the effectiveness and efficiency of Bank's risk management processes.
- Review adequacy of systems and controls established to ensure compliance with policies, plans, procedures, laws and regulations.
- Evaluate reliability, effectiveness and integrity of management information systems including relevance, accuracy, completeness, comprehensiveness of data and the means used to identify, measure, classify, and report such information.
- Monitor and evaluate corporate governance processes.
- Evaluate the means of safeguarding assets and, as appropriate, verifying the existence of such assets.
- Evaluate effectiveness and efficiency with which resources are employed.
- Evaluate operations or programs to ascertain whether results are consistent with established objectives and goals and whether the operations or programs are being carried out as planned.
- Evaluate quality of performance of external auditors and the degree of coordination with internal audit.
- Report significant risk exposures and control issues, including fraud risks, governance issues and other matters (internal or external) needed or requested by the board or audit committee.
- Evaluate specific operations at the request of AC, Board or management as appropriate.
- Perform consultancy and advisory services related to corporate governance, risk management and controls as appropriate for the Bank and participate in working groups and committees.
- Report periodically on the internal audit activity's purpose, authority, responsibility, and performance relative to its plan.

	Internal Audit Charter		
	<i>Internal Audit Department</i>		
	Approval Authority	Date Approved	Date of previous approval
	<i>Audit Committee</i>	<i>3 May 2018</i>	<i>26 July 2017</i>

8. SCOPE AND RESPONSIBILITIES (CONTINUED)

The Internal audit function shall also have responsibilities as laid down in various rule books of Central Bank of Bahrain (CBB). The important provisions are:

- Providing independent and objective review on the adequacy and effectiveness of the holistic internal control environment within the Bank.
- Monitor internal controls framework, on an on-going basis, to provide an independent assessment of the adequacy of, and compliance with, the established policies and procedures. It should not be simply testing for compliance with approved policies and procedures but should opine on its overall appropriateness and adequacy and whether it meets Bank's needs and supervisory requirements.
- Verify Bank's daily compliance with the capital requirements for credit and market risk.
- Review at least bi-annually the Bank's rating system and its operations, including the operations of the credit function and the estimation of probability of defaults (PD), loss given defaults (LGD) and exposure at defaults (EAD). (Review to include adherence to all applicable minimum requirements and must document its findings).
- Review compliance with Bank's defined policies and procedures for determining which exposures to include in, and to exclude from, the trading book for purposes of calculating regulatory capital (Validation of various Qualitative standards at least once in 6 months as stated in CBB rule book CA-14.3).
- Periodic review/evaluation of internal systems and identify control weaknesses.
- Conduct periodic review of the Business Continuity Plan (BCP) to determine whether the plan remains realistic and relevant, and whether it adheres to the policies and standards of the Bank.
- Review the effectiveness of Bank's Customer Due Diligence/Know Your Customer (CDD/KYC) requirements, AML/CFT procedures, systems and controls at least once in a calendar year.

The internal audit function may also perform advisory and related client service activities, the nature and scope of which will be agreed with the management, provided the internal audit does not assume management responsibility. The Head of Internal audit should consider proposed consulting engagements based on the engagement's potential to improve management of risks, add value, and improve the organisations operations. Opportunities for improving the efficiency of governance, risk management, and control processes may be identified during engagements. These opportunities will be communicated to the appropriate level of management

9. INTERNAL AUDIT PLAN AND RELIANCE ON OTHER SERVICE PROVIDERS

At least annually, the Head of Internal Audit will submit to senior management and the Audit Committee an internal audit plan for review and approval. The internal audit plan will consist of a work schedule as well as budget and resource requirements for the year. The scope and frequency of the audit program should be appropriate to risk exposures of the Bank. The audit plan should be based on a robust risk assessment and should be updated periodically to enable an on-going real-time assessment of areas where significant risks lie. The Head of Internal Audit will communicate the impact of resource limitations and significant interim changes to senior management and AC.

The internal audit plan will be developed based on a prioritization of the audit universe using a risk-based methodology, including input of senior management and AC. The Head of Internal Audit will review and adjust the plan, as necessary, in response to changes in the organization's business, risks, operations, programs, systems, and controls. Any significant deviation from the approved internal audit plan will be communicated to senior management and AC through periodic activity reports.

The Head of Internal Audit may choose to rely on the work of other assurance service providers for various reasons, such as to assess specialty areas outside of the internal audit activity's expertise or to enhance risk coverage beyond the internal audit plan. However, if the internal audit activity relies on the work of another service provider, the Head of Internal Audit retains ultimate responsibility for internal audit conclusions and opinions. Thus, it is essential that the Head of Internal Audit establish a consistent process and set of criteria to determine whether the internal audit activity may rely on the work of another provider.

	Internal Audit Charter		
	<i>Internal Audit Department</i>		
	Approval Authority	Date Approved	Date of previous approval
	<i>Audit Committee</i>	<i>3 May 2018</i>	<i>26 July 2017</i>

9. INTERNAL AUDIT PLAN AND RELIANCE ON OTHER SERVICE PROVIDERS (CONTINUED)

In this process, the Head of Internal Audit may:

- Evaluate objectivity by considering whether the provider has, or may appear to have, any conflicts of interest and whether they have been disclosed.
- Consider independence by examining the provider's reporting relationships and the impact of this arrangement.
- Confirm competency by verifying whether the provider's professional experience, qualifications, certifications, and affiliations are appropriate and current.
- Assess due professional care by examining elements of the practice the provider applies to complete the work (i.e., the provider's methodology and whether the work was appropriately planned, supervised, documented, and reviewed).

10. REPORTING AND MONITORING

A written report will be prepared and issued by the Head of Internal Audit following the conclusion of each internal audit engagement and will be distributed as appropriate.

Internal audit reports should be sufficiently detailed, clear and organized to allow the senior management, AC and external auditors of the Bank to rely on them fully for their work.

The internal audit report may include management's response and corrective action taken or to be taken in regard to the specific findings and recommendations. Management's response should include a timetable for anticipated completion of action to be taken and an explanation for any corrective action that will not be implemented.

The Internal audit will be responsible for appropriate follow-up on engagement findings and recommendations. All significant findings will remain in an "open issues" file until they are rectified or resolved.

The Head of Internal Audit will periodically report to senior management and AC on the internal audit activity's purpose, authority, and responsibility, as well as performance relative to its plan and on its conformance with the Code of Ethics and the Standards. Reporting will also include significant risk and control issues, including fraud risks, governance issues, and other matters that require the attention of senior management and/or the AC.

11. RELATIONS WITH EXTERNAL PARTIES AND REGULATORY AUTHORITIES

Internal audit coordinates with and may consider relying upon the work of the external auditors appointed by the Bank in order to avoid duplication of effort and to provide maximum coverage of activities. Internal audit may also coordinate its work with regulatory authorities and other oversight bodies, where relevant.

12. QUALITY ASSURANCE AND IMPROVEMENT PROGRAM

The internal audit activity will maintain a quality assurance and improvement program that covers all aspects of the internal audit function. The program will include an evaluation of the internal audit activity's conformance with the *Standards* and an evaluation of whether internal auditors apply the Code of Ethics. The program also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement.

The Head of Internal audit will communicate to senior management and AC on the internal audit activity's quality assurance and improvement program, including results of on-going internal assessments and external assessments conducted at least every five years.

	Internal Audit Charter		
	<i>Internal Audit Department</i>		
	Approval Authority	Date Approved	Date of previous approval
	<i>Audit Committee</i>	<i>3 May 2018</i>	<i>26 July 2017</i>

12. QUALITY ASSURANCE AND IMPROVEMENT PROGRAM (CONTINUED)

Disclosure should include:

- The scope and frequency of both the internal and external assessments.
- The qualifications and independence of the assessor(s) or assessment team, including potential conflicts of interest.
- Conclusions of assessors.
- Corrective action plan

13. CIRCULATION OF THE CHARTER AMONG THE BANK'S STAFF

This charter will be circulated among the Bank's staff for their information and assistance to internal audit in fulfilling its roles and responsibilities.

14. REVIEW OF THE CHARTER

This charter will be reviewed at least annually by the AC. Any substantive changes will be formally approved by the AC upon recommendation of Head of Internal Audit and Chief Executive Officer.