

3. INTERNAL AUDIT AND INSPECTOR GENERAL'S OPINION

The Control Department carries out the internal audit at the Bank of Albania. The main objective of the Control Department is to ensure compliance with the laws and by-laws in the activity of the Bank of Albania. The internal audit function ensures periodically and independently to the Bank's Administrators and the Supervisory Council the verification and evaluation of internal audit systems by testing certain controls and procedures but not being their substitute.

3.1. HIGHLIGHTS IN INTERNAL AUDIT OVER 2018

A. Implementation of the Internal Audit Policy

The Annual Internal Audit Plan at the Bank of Albania was reviewed and approved in accordance with the International Standards on Auditing. The annual plan for 2018 was drafted by the Control Department and the Inspector General, and was submitted for review by the Audit Committee. Once agreed by the Audit Committee, the plan was presented to the Supervisory Council, and was approved by its Decision No. 16 of 07.02.2018.

B. Drafting of the Annual Audit plan in the automated Pentana system, based on the approved risk assessment methodology

The proposed 2019 plan was based on Risk Assessment process for audit purposes through the application of the Pentana system. Risk-based planning through this system enhances the quality of planning based on the risks identified during the audit and updating of the audit universe with risks from the external environment, based on the external auditors' requirements.

Starting from 2017, the Department has drafted the complete risk-based audit plan in compliance with the International Standards in Internal Audit.

C. Relations with the Operational Risk Management Unit

Collaboration with the ORM Unit continues on regular basis. The ORM Unit makes available to audit teams (inspectors) the list of operational risks that have been identified and reported by the departments of the Bank, and monitored by the ORM. Meanwhile, the Control Department makes available to the ORM Unit, at the end of each engagement, the audit report, risk assessment of the function and findings, format of risk-check processes, and any other information that may apply to the continuous operational risk management.

In addition, the Control Department, reports regularly on the operational risks related to the internal audit itself.



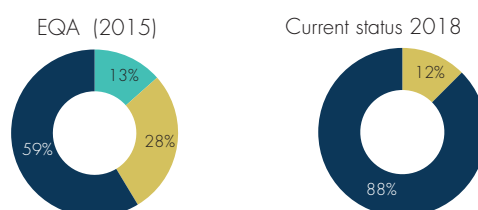
D. Implementation of Recommendations from the External Quality Assurance and Results of Internal Assessment

Following the external assessment of the Internal Audit quality (External Quality Assessment), conducted by the Central Bank of the Netherlands (DNB) in May 2015, the Control Department, at the end of 2017, accomplished the engagement of the Internal Audit quality self-assessment (Internal Quality Assessment).

The table below shows the situation at the end of 2018 regarding EQA recommendations left by the DNB and the results of the engagement of the Internal Audit Self-Assessment.

Chart 44 Internal audit assessment (EQA, 2015), self-assessment of quality (2017), actual assessment

Compliance levels according to EQA	Standards assessed during EQA by levels of compliance (2015)	Commitment status of Self-assessment of IA quality in AB në 2017	Current status after last assessment 2018
Do not comply	14	0	0
Partially complies	29	16	13
Complies	61	88	91
TOTAL	104	104	104



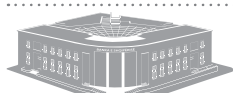
According to the chart above, only 12.5% of the standards (13 Standards) are not fully implemented (in accordance with the best practices provided by the IPPF of the International Institute of Internal Auditors).

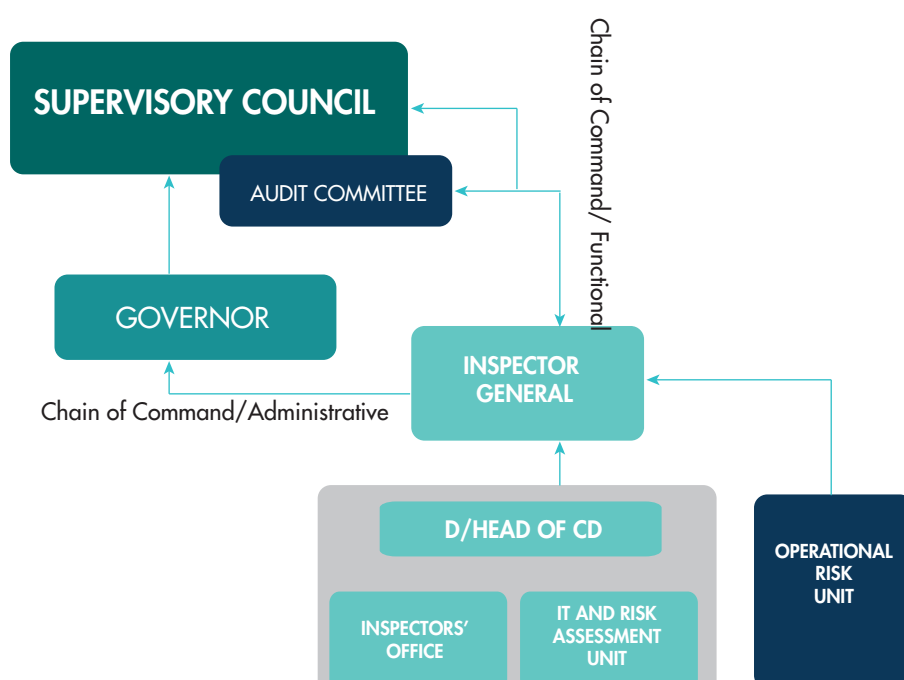
3.1.1 ABOUT THE CONTROL DEPARTMENT

In accordance with the Law "On the Bank of Albania", the statute of the Bank of Albania, the policy and regulation of the Internal Audit and the regulation of the Audit Committee, the structure of the Control Department is presented in the following chart. Its purpose is to preserve the objectivity, independence, integrity of information, the efficient use of resources and the effectiveness of internal control systems at the Bank of Albania.

A. Organizational structure of Control Department

The organizational structures under the responsibility of the Inspector General:





B. Professional capacity building and continuous training

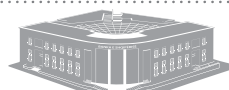
In order to meet the strategic objective regarding the capacity building of internal audit staff members, the audit inspectors have participated in training programs for internal audit and risk management provided by central banks; they have attended individual programs for their professional development; and have taken professional membership / certification exams from international institutions in the field of finance and audit. The audit inspectors continued attending the ACCA, CIA, CISA certification programs and minimum mandatory classes for upholding CIDA, ACCA, CA titles.

Table 9. The qualification status of Internal Audit staff is provided following:

Qualification and professional capacity building of staff	
Qualified inspector for CIA audit	1 inspector (1 in process)
Qualified inspector for specific audits of investments CIDA	2 inspectors
Qualified inspector for financial reporting ACCA	2 inspectors (2 in process)
Inspectors in qualification process for IT CISA audit	1 inspector

3.1.2 ENGAGEMENTS AND MAIN FINDINGS IN 2018

Audit engagements in 2018 focused on: (i) giving an opinion on the adequacy of internal audits set by the Management for the audited functions / processes, including applications supporting activities; and (ii) other unplanned audit and non-audit engagements with a special request by Administrators or other institutions.



During 2018, in total, 37 recommendations resulted from 10 audit engagements for security. The recommendations mainly addressed the need for improving the processes (49%); the review of the regulatory base (26%); and others on the implementation of the regulatory base.

The findings and recommendations for each of the audits carried out during this period were first addressed to the heads of the units and then to the Bank of Albania's Administrators.

3.2. OPERATIONAL RISK MANAGEMENT

The operational risk management is one of the newest functions at the Bank of Albania. In mid-2015, started the project for the establishment of this function, based on the Risk Management international standards and on best practices of central banks. The operational risk management function at the bank of Albania was finalised in 2016.

The main objective of the Operational Risk Management is to: manage uncertainties and possible risk to the activity of the Bank; inform at any time the Administrators; assist the decision-making process on risks that may hinder the achievement of Bank of Albania's objectives or have adverse financial and / or reputational impacts.

A. Operational risk management in 2018

In 2018, the Operational Risk Management Unit continued to monitor and review the identified risks within the Bank units, and compiled regular reports for the Administrators, the Audit Committee and the Supervisory Council, on the results and analyses of the Banks' exposure to operational risk.

In 2018, priority was given to the evidence and regular reporting of events/risks categorised as "FRAUD" for all processes of the Bank, based on the practices evidenced by Central Banks (IORËG). For all units of the bank, 34 risks classified in the "FRAUD" category are evidenced.

The operational risk management function was consolidated and matured in 2018.

In 2018, the following were realised:

- Upon the approval of tolerance level to the operational risk, by Decision No. 18, dated 29.3.2017, of the Supervisory Council, on addressing all the residual risks, which were classified as "High" and "Medium", the ORM Unit conducted the periodic re-assessment processes of Operational Risks based on the periodic reports of units, and reviewed all processes realised at Bank level. The periodic assessment helps to identify and address the occurred risks, particularly for the processes



- assessed with 'medium' and 'high' risk.
- Approval of the action plans by the Administrators. These plans were drafted by the ORM Unit in collaboration with all the involved units. In total, 27 action plans and 5 key indicators were drafted, for minimising 59 operational risks classified as "high" and "medium";
 - Periodic review and reassessment of the Operational Risk Database. The ORM Unit held meetings with all units to review the operational risk database. This stage was supported also by the data found in the latest operational risk database submitted by the International Operational Risk Working Group (IORWG). At the end, the Operational Risk Database identified 313 operational risks in total, of which 304 are specific risks and 9 comprehensive risks.
 - Review of the realised processes database. During this stage, 409 processes/sub-processes, in total, were identified for 23 functions allocated by responsibility level for the units and committees of the Bank of Albania.

B. Assessment of Operational Risk Management by international experts

The Operational Risk Management is assessed based on the methodology employed by the International Operational Risk Working Group (IORWG) for central banks, part of which is also the Bank of Albania.

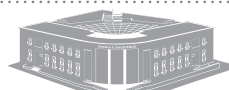
This organization, which develops and directs the Operational Risk Management for Central Banks, has been active since October 2005, and currently consists of 96 central banks and Supervision and Monetary Authorities. The Bank of Albania joined it in July 2015. Following this process, the progress of the maturity level of the Operational Risk Management has shifted from 'ad-hoc' to 'managed'. This assessment exceeds the Bank of Albania's expectations, thus overcoming the "basic" level.

The major part of Central Banks that have been consolidating the Risk Management function for more than 5 years, are currently rated in this level.

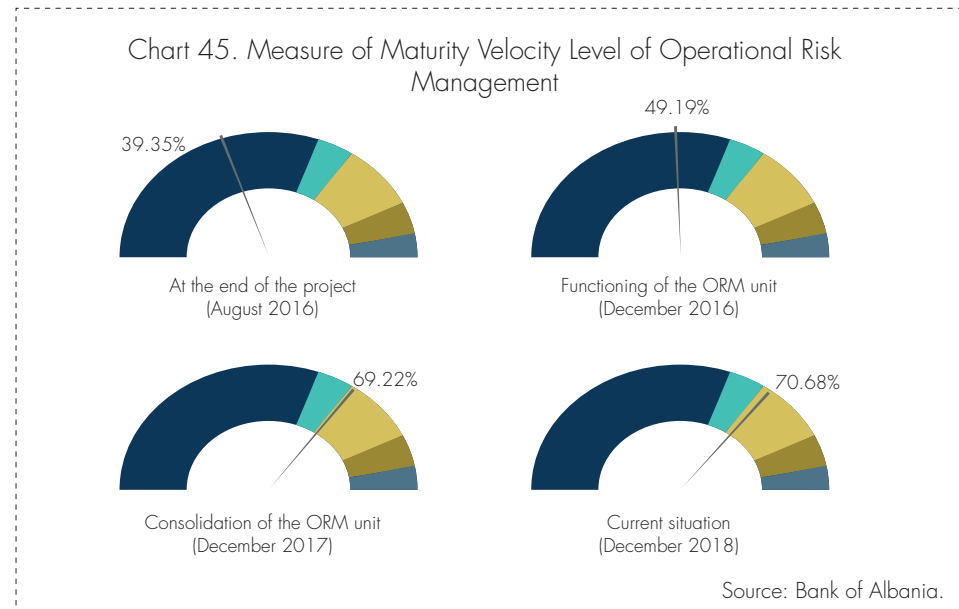
AD-HOC	BASIC	MANAGED	ADVANCED	MATURED
<61%	≥61%	≥69%	≥86%	≥94%

The maturity level, during 2017, increased considerably at 69.22% (from 49.19% at the end of 2016), upon the expression of Operational Risk Tolerance by the Supervisory Council, the drafting and approval of action plans at the Administrators, the periodic review and reassessment of operational risk database. The current maturity level assessed for 2018 is 70.68%, based on the performance of the process on the implementation of action plans and the assessment of risks periodically reported by units. This level fully complies with the medium-term objectives of ORM function at the Bank of Albania.

The assessment is conducted periodically based on IORWG matrix, which set out the designing of the processes and control systems on these processes,



organisation way and structure, reporting results after the risk management and risk culture, which is a challenge that needs continuous monitoring, coherence and awareness-raising.



C. Whistleblowing function at the Bank of Albania

The consolidation of the whistleblowing function has helped the Operational Risk Management as well. In compliance with the Law No.60/2016 “On Signalling (whistleblowing) and Protection of Whistle-blowers”, this unit aims to:

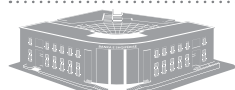
- a) prevent and suppress corruption at the Bank of Albania;
- b) promote alerts on suspected corruption actions or practices;
- c) protect whistleblowers who signal suspected corruption actions or practices at their workplace.

Upon the approval of the Regulation in December 2017 “On the Administrative Investigation of Signalling, Protection of Confidentiality and Protection from Retaliation at the Bank of Albania”, all the units at the Bank were informed on the Regulation, which is made public for all the staff members of the Bank and is accessible to each employee.

The regulatory base was completed during 2018, in addition to all the guidelines (annexes) and necessary tools to provide the staff with the possibility to signal doubtful cases.

D. Business Continuity Management (BCM) at the Bank of Albania

The Bank of Albania established a working group for the Project “Drafting and implementation of the Business Continuity Management program at the Bank of Albania”. The project is in the final stage of the engagement completion.



This process was realised based on the most updated infrastructure of the Bank and is drafted in such a way to be updated and maintained with all changes periodically.

The purpose of this project is, through the drafting of the necessary regulatory framework, in case of operational interruptions during a Crisis/Emergency, to support the Bank in its efforts to improve the response capacity, ensure the continuation of critical processes and recover the normal business of the Bank as fast as possible.

The drafted regulatory acts are based on BS 25999 Standard and best practices in the field of Business Continuity Management (BCM). BS25999 Standard is broadly accepted as the base standard for drafting and implementing and effective BCM Program and is applicable to all institutions (including industry and relevant sectors).

The standard provides a framework of the best practices with the aim for minimising the negative consequences in case of undesirable events that may drive to disruption of business. Based on this Standard, "Business Continuity Management" is a process oriented to business, which set forth a strategic and operational framework adapted to the needs, to:

- improve pro-actively the recovering capacity of the organisation against the operational disruptions, which render it unable to accomplish the main objectives;
- ensure a recovery method of the organisation's capacity to provide products and services in the agreed time and quality after the disruption of the business.
- provide a proven ability to manage the disruption of the business and to protect the reputation of the organisation.

