

**A. Internal Controls over Financial Reporting (ICFR) Disclosure in Annual Report:**

In addition to requirements of clause 7 (a & b) of SBP's Guidelines on Internal Controls – 2004, the disclosure of ICFR in the Annual Report shall be as follows:

1. The Management shall include a separate paragraph on evaluation related to the effectiveness of ICFR, in the annual 'Statement on Internal Controls'. The management shall comment on its related future plans and timing for rectification of deficiencies, if any, in ICFR.
2. The Board of Directors, in the Directors' report, shall endorse the management's evaluation related to ICFR along with endorsement of overall Internal Controls.

**B. Governance Structure – Roles and Responsibilities of Key Stakeholders of ICFR:**

1. For effective implementation of internal controls over financial reporting (ICFR), the Board of Directors should clearly define the role of the Board's Audit Committee (BAC) and responsibilities of the management (including Chief Executive Officer, Chief Financial Officer, Chief Risk Officer and other key officials).
2. The BAC shall keep oversight and periodically review the ICFR system for effective implementation and its continuous up-gradation. If BAC is entrusted to conduct ICFR assessment, it shall submit duly approved annual assessment report on ICFR to SBP, OSED as per prescribed timelines. The report, at the minimum, shall include testing and evaluating the design and operational effectiveness of ICFR based on the assessed risk and state whether the bank/ DFI maintained, in all material respects, effective ICFR at a particular point of time. Further, the report shall highlight gaps identified, filled and still outstanding as of end of assessment period.
3. Management of the bank/ DFI is responsible for maintaining a suitable system of ICFR – depending upon the size, nature and complexity of the bank/ DFI – that provides reasonable assurance regarding the reliability of financial reporting. The management should use a top-down, risk-based approach, including the entity level and activity level controls in assessing financial reporting risks and the adequacy of controls. The system of ICFR so developed by the financial institutions should be properly documented and made available to the internal auditors, external auditors, and SBP's inspectors for their review.
4. It is primarily the responsibility of the management to build and implement ICFR infrastructure; nevertheless, if management feels necessary, they may hire services of the external consultant, with due approval of their Board of Directors. While hiring such a consultant, bank/ DFI shall ensure avoidance of any conflict of interest; particularly, the consultant hired must not be the statutory auditor of the bank/ DFI at the time of providing ICFR related consultancy services.
5. The Chief Financial Officer of the institution shall be responsible to ensure effective implementation of ICFR, its regular supervision and continuous update of related processes, risks and controls documentation. The name and particulars (phone, fax and email) of the

official shall be provided to OSED, within one month of issuance of this circular. In case of change of the official, the banks/ DFIs shall be liable to provide updated information within seven days of assumption of the charge.

6. Internal Auditors play a significant role in ensuring the existence and effectiveness of the ICFR system. As such, Internal Audit function of the bank/ DFI should monitor implementation of ICFR roadmap and internally evaluate the ICFR system, and should make timely and practical suggestions to Board's Audit Committee for improvement.
7. The banks/ DFIs:
  - a. Which have not completed ICFR roadmap; or
  - b. Which have completed ICFR roadmap but they desire, by their own, to continue with the statutory auditors' assessment; or
  - c. Which have completed ICFR roadmap but have not been allowed exemption by SBPshould engage the statutory auditors at the time of their appointment to allow them ample time for performing the assignment and timely submission of the LFR.
8. Please note that these instructions are not exhaustive. Therefore, the banks/ DFIs are strongly encouraged to develop/ adopt the measures suitable to further strengthen their ICFR systems.