

B-1 Central Board Decisions and Deliberations during FY12

Decisions/deliberations/approvals by the Central Board during FY12 have been categorized into matters related to Corporate Governance, Monetary Policy & Research, Banking, Financial Markets & Reserve Management, and Corporate Services.

Corporate Governance

1. Amendment in ToRs of Committees of the Central Board of SBP.
2. Nomination of a member on the Audit Committee of the Central Board of SBP.
3. Formation of Advisory Committee on Monetary Policy.
4. Governance Structure of Internal Audit.
5. Discussion on Board's effectiveness.
6. Discussion on SBP (Amendment) Act, 2012.
7. Schedule of the Central Board meetings for the year 2012.

Monetary Policy & Research

1. Monetary Policy Statement
 - July, 2011
 - February, 2012
2. Monetary Policy Decision
 - September 2011
 - November 2011
 - April 2012
 - June 2012
3. The State of Pakistan's Economy
 - First Quarterly Report (July-September, 2011)
 - Second Quarterly Report (October-December, 2011)
 - Third Quarterly Report (January-March, 2012)
4. SBP Annual Report for the year 2010-11
 - The State of Pakistan's Economy (Vol-I).
 - Performance Review (Vol-II).
5. Approval for conducting a study on "Individual Philanthropy".
6. Discussion on implementation of new Section 9C of the SBP (Amendment) Act, 2012 - Limitation on Federal Government Borrowing.

Banking

1. Financial Stability Review - November 2011.
2. Appointment of Chairman of State Bank of Pakistan's Shariah Board.
3. Appointment/Reappointment of SBP Shariah Board Members.
4. Reimbursement of bonafide losses to banks against agricultural loans extended during Jan-Jun 2005.
5. Discussion on Banking Regulation.
6. Discussion on Report on Assessment of the Banking Sector.
7. Discussion on competitive environment in Banking Industry.

Financial Markets and Reserve Management

1. Quarterly Review of Performance of Reserves – December 2011

Corporate Services

1. Finance

- Appointment of Auditors for FY12 & fixation of their remuneration.
- Ratification of 'On Account Payment' to the Federal Government.
 - September 30, 2011
 - December 31, 2011
 - March 30, 2012
- Federal Government Payment - June 30, 2011.
- Revenue Expenditure Budget and Capital Expenditure Budget of SBP and its subsidiaries for FY12.
- Profit & Loss Review of Expenditure Budget for
 - Quarter ended September 30, 2011
 - Half year ended December 31, 2011
 - Nine months ended March 31, 2012
- Consolidated Financial Statements of the Bank for the year ended June 30, 2011.
- Moratorium on penal interest on overdraft of Pakistan Railways.
- Revision of Ways and Means Limit of Gilgit-Baltistan Government.
- Overview of Government Audit Report on Accounts of SBP for FY10.

2. IT Related Matters

- Renewal of maintenance and support contract of Oracle ERP, DWH and CBA Modules

3. HR Related Matters

- Renewal of employment contract of ED-FMRM.
- Renewal of employment contract of Chief Spokesperson SBP.
- Revision of Staff Car Usage Policy for OG-6 and above officers.
- Revision of Deputation Policy.
- Revision in Policy of Mobile Phone Facility for OG-7 and OG-8 officers.
- Revision of Professional Development Incentive Program.
- Revision of Higher Studies Policy (2011).
- Allocation of Annual Merit Increase (AMI) – FY11.
- CBA's Charter of Demand (CoD) – 2011.
- Compensation/benefits survey and salary adjustment of employees.
- Employees' Compensation Policy.
- Normalization of Bell Curve and Performance Based Exit Policy.
- Application of PMS and Career Development Policy of OG-2 and above officers on OG-1s.
- Change in medical option.

4. Other Matters

- Applicability of Public Procurement Rules, 2004 on SBP and SBP-BSC.

B-2 Business Continuation Management

Business Continuity Management (BCM) is a comprehensive risk management approach which encompasses the policies, procedures and governance structure to ensure that, in the event of a disruption, the critical time sensitive functions of an organization can be performed or recovered in a timely manner. A Business Continuity Plan (BCP) is a comprehensive, written plan of action that sets out the procedures and establishes the processes and systems necessary to continue or restore operations in the event of a disaster or a major operational disruption. The BCP provides detailed guidance for implementing the recovery plan and outlines the roles and responsibilities in managing operational disruptions.

Pro-active Business Continuity Management plays a significant role in ensuring that the central bank can continue its critical and time sensitive operations even during a disaster situation. The Business Continuity Plan of the State Bank of Pakistan ensures continuity of critical functions of SBP and SBP-BSC and aims to prevent any major operational disruption in the financial system of the country in the face of a catastrophe caused, either by natural disaster, fire, civil strife, sabotage or an act of war.

In order to establish controls and minimize the chances of major operational disruption of critical time sensitive functions of SBP and SBP-BSC, the Business Continuity Plan sets out a governance structure in the form of various committees, groups and teams which ensure senior management's commitment and define management's role and responsibilities in the event of a disaster. The BCP Committee is the apex steering body for all BCP related activities, and is headed by the Deputy Governor (Operations) and comprises of members of senior management, drawn from the critical areas of the bank representing Operations, Financial Markets & Reserve Management, SBP Banking Services Corporation, Financial Resource Management and Office of the Corporate Secretary. During FY12, two meetings of the BCP Committee were convened where the Committee took various decisions to improve the effectiveness and implementation of BCP.

The State Bank of Pakistan has strengthened its level of preparedness and readiness by establishing a state of the art Disaster Recovery Site and a fully equipped Backup Site for critical time sensitive functions. To further enhance the state of readiness of the Business Continuity Program of SBP, the following initiatives were taken during the year:

BCM Workshops

The most effective approach to achieving organizational resilience, besides instilling resilient structures and processes, is to train the relevant personnel in handling crisis, as the organizations can only cope, respond and recover from a major crisis with the intervention of trained personnel. In order to embed business continuity in the organization's culture, a major initiative was launched where a series of workshops on Business Continuity Management (BCM) were organized in Karachi, Lahore, Islamabad and Multan where more than 120 officers from SBP and SBP-BSC field offices all over the country participated. The purpose of these workshops was to equip the participants with the knowledge and skills of BCP and to ensure that they are familiar with SBP's BCP plan, understand the escalation process and are able to activate the recovery procedures developed in the BCP program.

BCP Preparedness Review

The size, complexity and geographically dispersed nature of operations make the implementation of BCP even more challenging. To assess the BCP arrangements at the field offices, infrastructure,

environment and facilities available at the existing backup sites and to evaluate the suitability of backup sites identified by the respective offices as per the benchmarks approved by the BCP Committee, an exercise was initiated in which the offices of Hyderabad, Sukkur, Multan, Bahawalpur, Faisalabad, Gujranwala, Lahore, Peshawar, Sialkot and Muzaffarabad were evaluated.

Table top, Mock Exercises and Rehearsals

The purpose of testing is to achieve organizational acceptance that the business continuity solution satisfies the organization's recovery requirements. An untested plan may be worse than not having a plan in place because it gives a false sense of security to the organization. Continuous testing of the Business Continuity Plan enhances the readiness of employees to cope with a disaster. To further streamline the testing procedure at SBP and SBP BSC and to facilitate the departments/offices to conduct their tests and rehearsals smoothly, an Annual Test Plan was compiled in coordination with the critical departments and field offices where all critical departments/field offices planned to conduct quarterly table top exercise, half yearly mock exercise and annual rehearsals. Consequently, 87 table top tests, 53 mock exercises and 22 rehearsals were conducted by departments and field offices. In addition to that, evacuation and fire fighting drills were also held at field offices and the SBP main building.

Updation of BCP Manuals

Through a documented Business Continuity Plan, the organization builds an effective program that provides a planned response, recovery, and restoration mechanism to safeguard the interests of key stakeholders and its reputation. At SBP, BCP Book I is designed for the critical departments of SBP and SBP BSC while BCP Book II is designed for the field offices. To reflect the effect of restructuring at State Bank of Pakistan and based on criticality, the Payment Systems Department (PSD) and Currency Management Department (CMD) were included while the Exchange Policy Department (EPD) and Risk Management & Compliance Department (RMCD) were excluded from the list of Critical (time sensitive) Departments. Similarly, the General Services Department (GSD) was included in place of the erstwhile Business Support Services Department (BSSD) in the list of Critical (support) Departments.

Combined exercises of critical (time sensitive) departments

Testing the organizations' Business Continuity Plan assesses its viability and ensures that the relevant staff is familiar with the continuity plan, understands the activation process and is able to execute the recovery strategies documented. In order to stress test the reliability of networks, equipments, services and other allied facilities, four combined exercises were successfully conducted from the backup site by the critical (time sensitive) departments. Approximately 50 persons from critical (time sensitive) departments participated in the combined exercises on each occasion.

Apart from the routine testing of the backup site, for the first time scenario-based testing was initiated from the backup site where different scenarios were proposed, documented and conducted successfully. Further, the combined exercises helped in achieving the desired level of preparedness which enabled the critical (time sensitive) departments to conduct live operations from the backup site which is in an advance level of testing.

Dedicated Backup Site for Critical (Time Sensitive) departments

To improve the level of readiness and preparedness, the backup site was upgraded and made operational on a round-the-clock basis. Complete refurbishment of the backup site was undertaken which has resulted in increased seating capacity to cater to the demands of critical (time sensitive) departments. Further initiatives were undertaken to improve and enhance the allied facilities to

provide secure boarding and lodging to the critical staff during crisis situations. To cater to the need for maintenance, supervision of civil works and preparation for exercises at the backup site, officers from SBP BSC were deputed which has significantly improved the working condition, environment of the backup site and helped in maintaining the costly equipment and allied facilities. Further, round the clock staff including electricians and a generator operator has also been deputed to provide emergency support services at the backup site.

In order to provide connectivity for the backup site, an alternative to the costly Radio Frequency (RF) Tower was proposed. The alternative solution was successfully tested on full load during the combined exercise held in December 2011 and the alternative solution was approved by the BCP Committee for the backup site of critical (time sensitive) departments.

Automation of backup sites of field offices

Over a period of time, most of the critical functions and processes have been automated and require the availability of relevant IT applications at the backup sites of field offices. Priority was allocated to upgrade the backup sites in terms of automation, proximity, backup data and cash availability to improve the readiness and preparedness of field offices.

Improved Vigilance for the Backup Site

To implement effective internal controls at the Backup site, various measures were undertaken such as vigilance of the activities at the backup site through IP cameras and its monitoring through control room manned by staff of Internal Bank Security Department (IBSD), log controls for entry/exit, movement and asset register etc.

TORs of the BCP Committee

After the realignment of BCP function in 2011, it was decided to develop Terms of Reference of the BCP Committee which will help the committee and its members to focus and work according to its mandate. The TORs of the BCP Committee were developed after reviewing the international best practices, identifying the roles, responsibilities and composition of the BCP Committee, defining the role of BCP Coordinator etc. The TORs were approved and adopted by the BCP Committee in December 2011.

B-3 Risk Based Auditing

Internal Audit & Compliance Department (IA&CD) at State Bank of Pakistan is performing the important function of providing independent and objective, assurance and consulting services, designed to add value, improve operations of SBP and help it in accomplishment of its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes. In this regard, IA&CD conducts financial, operational, and information technology (IT) based audits of SBP operations.

Presently, four financial & operational audit teams and one IT audit team are conducting audit engagements, based on risk-based internal auditing methodology. A quality assurance (QA) Unit in IA&CD undertakes the ongoing quality assurance of audit activities and ensures that these activities conform to the Institute of Internal Auditors (IIA) Standards. A Compliance Division of IA&CD obtains status of audit recommendations on quarterly basis, in order to ensure compliance of outstanding audit recommendations previously agreed by the Auditee Departments.

The functions of IA&CD are overseen by the Honorable Governor SBP and Committee of the Central Board on Audit.

The following milestones have been achieved by IA&CD during FY12:

- Continuous updation was made in the Audit Universe (Database) of auditable business processes with the feedback of Auditee Departments. This was developed by IA&CD using its own prepared risk scoring model based on IIA Research Foundation. Annual Audit Plan of the Department is being developed, based on the updated content of Audit Universe.
- Accomplished all audit assignments of the Audit Plan FY12 successfully. IA&CD also carried out different special audit assignments on the advice of Audit Committee and higher management of SBP. In addition to the above, IA&CD reviewed Internal Audit Reports of SBP BSC and highlighted significant observations to Governor SBP.
- Constant efforts were made to strengthen the role of QA with regard to its coverage in all audit activities.
- In order to bring the concept of Self Risk Assessment by business departments, IA&CD is assisting different Departments of SBP for developing their Risk Registers. Further improvements were made in Risk Registers already developed by the Departments during audit assignments in FY12.
- Close coordinations with External and Govt. Auditors were made and Audit Reports of various Departments duly audited by IA&CD were reviewed by both of them.

B-4 Legal Services Department

In order to align the activities and core functions, together with the new areas of focus, the General Counsel's Office was restructured and renamed as Legal Services Department during FY12. Given the complexity and importance of establishing a well-coordinated architecture for the legal-oriented services that ensures professional management in the respective areas, the new department consists of the following four Divisions:

1. Corporate Service Division
2. Banking Legal Division
3. Litigation Division
4. Projects, Compliance and Support Services Division

During the period under review, this department participated in achievement of Bank's goals through opinions, advices, litigation, and appearance before the Courts of Law at Lahore, Islamabad and Karachi etc. It also provided help in drafting of regulations and contracts besides vetting replies to the notices for submission to Supreme Court and various High Courts of the country. Moreover, our legal professionals have been playing a critical and decisive role in deciding appeals, addressed to the honorable Governor by various banks against the decisions given by the Banking Ombudsman. Together with these developments, the professionals of this department also attended the court proceedings at Supreme Court and other different Courts of Law at various places during the reporting period.

Legal Services department have received more than 3100 references from various stakeholders consisting of SBP, SBP BSC and NIBAF during FY12. It may be interesting to note that 65 percent references were related to the opinions, drafting, contracts and vetting the correspondence of various nature mainly of core functions of SBP and SBP BSC, 18 percent directly related with the house building advance matters and the remaining 17 percent were related to different courts notices and judgments in the respective cases of SBP, SBP BSC and NIBAF. All these references were disposed of in line with the prevailing law and policies of the Bank where applicable.

Follow up the Cases under Litigation

This department collected and analyzed the progressive status of litigation cases on a monthly basis from all stakeholders which, in return, helped the department to review of the cases under litigation at different courts of law and also to take views for any adverse orders. During the period, 735 cases were under litigation in different courts of law. Of these, 82 percent cases under litigation were related to the core banking policies and the rest 18 percent were related to the HR services related matters.

Amendments and Drafting of Legislation

In line with the emerged banking practices at international level and also to mitigate the threat of anticipated financial risks, this department participated to compile information keeping in view the latest available research in international law for comparative studies, which helped in the proposed amendments in SBP Act 1956 which was submitted to the parliament and standing committees during the period under review. Moreover, this department also remained involved in the studying, discussing, drafting and amending the proposed various Laws and Acts:

- The State Bank of Pakistan Act 1956.

- Draft Banking Act.
- State Bank of Pakistan Amendment Bill, 2010
- Amendments to the Banking Companies Ordinance, 1962.
- Corporate Rehabilitation Act
- Deposit Protection Fund Act.
- Various other amendments in regulations