



SOUTH AFRICAN RESERVE BANK

Prudential Authority

**FOR PUBLIC CONSULTATION – JULY 2021**

**Prudential Standard CBA-03 – Risk management, compliance and internal controls requirements for co-operative financial institutions and co-operative banks**

***Objectives and Key Requirements of Prudential Standard CBA-03***

*This Standard sets out the requirements for risk management, compliance and internal controls for co-operative financial institutions (CFIs) and co-operative banks registered in terms of the Co-operatives Banks Act, 2007 (Act No. 40 of 2007).*

*It is the ultimate responsibility of the board of directors (board) of the CFI or co-operative bank to ensure compliance with this Standard on a continuous basis.*

*This Standard covers requirements relating to the principles for risk management which include risk management strategy, policies, procedures and tools, internal controls, risk governance, functions of the supervisory or audit committee, the risk management function and the compliance function.*

**Table of Contents**

1. Commencement .....	2
2. Legislative authority .....	2
3. Application .....	2
4. Definitions and interpretation .....	2
5. Roles and responsibilities .....	3
6. Principles .....	3
7. Risk management strategy .....	4
8. Risk management policies .....	5
9. Risk management procedures and tools .....	5
10. Internal controls .....	6
11. Risk governance – general requirements for control functions .....	7
12. Risk governance – Supervisory or Audit Committee .....	8
13. The risk management function .....	10
14. The compliance function .....	10

Attachment 1: Policies for managing financial risks .....	11
A. Strategic risk management policy (including capital management) .....	11
B. Credit risk policy .....	12
C. Interest rate risk policy.....	12
D. Liquidity Management Policy (including asset-liability management) .....	13
E. Operational Risk Policy .....	14
F. Legal and Compliance Risk Policy .....	15
G. Outsourcing policy .....	15

## 1. Commencement

This Standard commences on 1 January 2023.

Version number	Commencement date
1	1 January 2023

## 2. Legislative authority

This Standard is issued under section 46(1) of the Co-operative Banks Act, 2007 (Act No. 40 of 2007) (Act) read with sections 105 and 108 of the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) (FSR Act).

## 3. Application

- 3.1 The care, diligence, skill and prudence exhibited by the board and management of CFIs and co-operative banks with regard to risk management and internal controls have a critical influence on the CFI's and co-operative bank's viability, safety and soundness as well as its ability to meet its business objectives.
- 3.2. This Standard applies to all CFIs and co-operative banks registered under the Act.
- 3.3 This Standard applies in addition to the requirements of the Co-operatives Act, 2005 (Act No. 14 of 2005) (Co-operatives Act) and the Principles of Good Governance for Co-operatives issued under the Co-operatives Act.

## 4. Definitions and interpretation

- 4.1 The terms used in this Standard, unless indicated otherwise, are defined in the Act, the Co-operatives Act or the Financial Sector Regulation Act, 2017 (Act No. 9 of 2017) and the prudential standards made in terms of the Act and have the same meaning in this Standard.

**'auditor'** means a registered auditor as defined in the Auditing Profession Act, 2005 (Act No. 26 of 2005);

**'board'** means the board of directors of the CFI or co-operative bank as appointed by the members in accordance with the constitution of the CFI or co-operative

bank;

**‘control functions’** means risk management and compliance functions and where required the Prudential Authority may require that a CFI or co-operative bank appoints an internal audit control function and thus also under these circumstances includes the internal audit function;

**‘financial information’** refers to the audited financial statements;

**‘independent reviewer’** means a person who is qualified to be appointed as an accounting officer of a close corporation in terms of section 60(1), (2) and (4) of the Close Corporations Act, 1984 (Act No. 69 of 1984);

**‘management’** means the managing director and executive officers of the CFI or co-operative bank;

**‘material risk’** means any risk that will negatively affect the financial soundness and reputation of the CFI or co-operative bank should it materialize; and

**‘supervisory or audit committee’** means the audit committee for a co-operative bank and the supervisory or audit committee for a CFI.

- 4.2 The ‘Objectives and key requirements of Prudential Standard CBA-03’ in the preamble at the start of this Standard must not be used in the interpretation of any section of this Standard.

## **5. Roles and responsibilities**

- 5.1 The board of the CFI or the co-operative bank is ultimately responsible for ensuring that the financial institution complies with all the requirements and principles of sound risk management outlined in this Standard. This includes establishing the financial institution’s overall risk appetite and ensuring that the financial institution has implemented effective systems for risk management and internal control to address risks.
- 5.2 Auditors, independent reviewers, and/or members of the Supervisory/Audit Committee must inform the Prudential Authority in writing of any matter they become aware of in the performance of their functions that will negatively affect the maintenance of the principles and requirements of this Standard.
- 5.3 The Supervisory or Audit Committee of the CFI or co-operative bank is responsible for providing input and assurance to the members and the board about the operations, efficiency, and effectiveness of the components of the systems for risk management and internal controls in the financial institution.
- 5.4 The PA may request an independent reviewer or auditor to provide the assurance on the requirements of this Standard, if necessary.
- 5.5 CFIs and co-operative banks must ensure, at all times, adherence to the provisions of the Financial Intelligence Centre Act, 2001 (Act No. 38 of 2001) which are applicable to the CFI or co-operative bank.

## **6. Principles**

- 6.1 A financial institution is exposed to a number of risks that can adversely affect its ability to achieve its business objectives. These risks can cause a financial institution to lose earnings and capital, and may negatively affect its reputation. CFIs or co-operative banks must accordingly implement a comprehensive, robust and disciplined risk management system that is commensurate with the nature, scale and complexity of the business.
- 6.2 The objective of risk management is not to eliminate risk, but to prudently manage risk. Many risk management tools help to mitigate or transfer risk. CFIs

and co-operative banks typically try to manage some risks, such as credit risk, within defined risk or reward tolerances and other risks, such as operational risk, within expected threshold levels.

- 6.3 The details of risk management systems differ among CFIs and co-operative banks and depends on the nature, scale, complexity and risk profiles of individual financial institutions. Other factors that affect risk management system are the control environment, experience and qualifications of management and control persons as well as the delegation of authority.
- 6.4 The risk management system must correlate with the:
- (a) financial institution's business strategy and plans;
  - (b) need to generate an appropriate level of sustainable earnings;
  - (c) interrelationships among risk, reward, capital and liquidity;
  - (d) nature, size, and complexity of risks that accompany specific decisions; and
  - (e) regulatory requirements.
- 6.5 A CFI or a co-operative bank must establish, maintain and operate within a system of effective internal controls designed to ensure that the risk management system is operating effectively and incorporates appropriate checks and balances to ensure that the financial institution operates effectively and efficiently.

## **7. Risk management strategy**

- 7.1 A CFI or co-operative bank must develop and implement a board approved risk management strategy that sets out the types of risks that the financial institution is willing to retain in implementing its business plan, and the way in which it will manage those risks.
- 7.2 The risk management strategy must be proportionate to the nature, scale and complexity of the CFI or co-operative bank and holistically focus on all sources of risk emanating from the financial portfolio and business activities of the financial institution.
- 7.3 The risk management strategy must include both quantitative and qualitative risk appetite and tolerance statements for each identified risk that articulates the levels of risk that a CFI or co-operative bank is willing to assume.
- 7.4 The risk management strategy must also include a clear plan on how to prudently manage material risks.
- 7.5 At a minimum, a CFI's or co-operative bank's documented risk management strategy, must:
- (a) identify the objectives of the strategy;
  - (b) describe each material risk (including emerging risks) and the financial institution's approach to managing those risks;
  - (c) list the policies and procedures for dealing with risk management;
  - (d) summarise the roles and risk management responsibilities of the board of directors, board committees and senior management;
  - (e) include a documented process for board approval for any deviations from the risk management strategy or risk appetite;
  - (f) outline the financial institution's approach to ensuring all stakeholders of the financial institution are aware of the risk management system and for instilling an appropriate risk culture across the financial institution; and
  - (g) must be reviewed annually by the board.

## 8. Risk management policies

- 8.1 In order to give effect to the governance and risk management frameworks, the board of a CFI and co-operative bank must annually review and, if necessary amend, the risk management and operational policies, clearly reflecting the date of the board approval on such policies.
- 8.2 The following board-approved policies, as a minimum, must be developed by a CFI or co-operative bank and can exist as a stand-alone policy or can be merged under suitable common areas:
- (a) credit;
  - (b) strategic;
  - (c) capital management;
  - (d) operational risk including information technology;
  - (e) legal and compliance;
  - (f) interest rate;
  - (g) savings policy;
  - (h) loans policy;
  - (i) liquidity, including asset-liability management;
  - (j) outsourcing risk, if applicable to the CFI and co-operative bank; and
  - (k) any other policy that is determined by the Prudential Authority.
- 8.2 A CFI or co-operative bank may combine one or more of the policies for addressing risks specified in paragraph 8.1 above, provided the financial institution is satisfied that the specified risks do not justify a separate policy given the nature, scale and complexity of the financial institution's business and risks.
- 8.3 **Attachment 1 (Policies for managing risks)** outlines the minimum contents of certain risk management policies specified in paragraph 8.1 above.
- 8.4 A CFI's and co-operative bank's risk management policies must be reviewed at least annually and kept updated in light of emerging risks.
- 8.5 Material changes to the risk management policies must be approved by the board of directors, properly justified and documented. The documentation must be available for review by the Supervisory or Audit Committee, the auditor or independent review of the CFI or the co-operative bank and the Prudential Authority.
- 8.6 In terms of the loans policy, referred to in paragraph 8.2(h) above, the policy must include the requirement that the terms of loans granted to board members, management, employees, related parties of a CFI or co-operative bank may not be more favourable than loans granted to members as well as how loan write-offs will be processed.

## 9. Risk management procedures and tools

- 9.1 A CFI or co-operative bank must maintain a suite of risk management procedures and tools that enables it to assess, monitor, report and mitigate the material risks to which it is exposed.
- 9.2 The risk management procedures must include both financial and non-financial risks in its scope.
- 9.3 The suite of risk management procedures must provide the board of directors

- with an enterprise-wide view of its material risks both financial and non-financial.
- 9.4 A CFI's or a co-operative bank's suite of risk management procedures and tools must be proportionate to the nature, scale and complexity of the institution, and must, at a minimum include:
- (a) a process for identifying and assessing new and emerging risks;
  - (b) procedures and tools for quantifying and managing specified individual material risks;
  - (c) a management information system that provides reliable and informative reports on the measurement, assessment and management of all material risks; and
  - (d) a review process to ensure the risk management system remains effective in identifying, quantifying, assessing and managing material risks to which the CFI or co-operative bank is exposed.
- 9.5 Depending on the nature, scale or complexity of the CFI or co-operative bank, the PA may request:
- (a) the application of scenario analysis and stress testing programs that are commensurate with the size, business mix and complexity of the financial institution's business;
  - (b) a forward-looking approach to assessing enterprise-wide financial risk;
- 9.6 A CFI's or co-operative banks risk management procedures and tools must be reviewed regularly, but at annually, and kept updated in light of emerging risks and changes in risk management tools and techniques.
- 9.7 Material changes to the risk management procedures and tools must be approved by the board of directors, properly justified and documented. The documentation must be available for review by the Supervisory or Audit Committee, the auditor of the CFI or co-operative bank, an independent reviewer or the Prudential Authority.

## **10. Internal controls**

- 10.1 As a part of the risk management system, a CFI or co-operative bank must develop and implement a board-approved framework of effective internal controls to address the scope of risks faced by the financial institution.
- 10.2 Internal controls are a critical component of a financial institution's risk management framework and are the policies, procedures and processes established by the board and management to provide reasonable assurance on the safety, effectiveness and efficiency of the financial institutions operations, the reliability of financial and managerial reporting, and compliance with regulatory requirements.
- 10.3 An internal control system must be appropriate to the nature, scale and complexity of the CFI or the co-operative bank's business and risks.
- 10.4 At a minimum, a CFI's and co-operative bank's internal control system must provide for the following:
- (a) an appropriate constitution, tailored to the business and operational requirements of the financial institution, which must provide for all the rules on the structuring and management of the financial institution;
  - (b) rules on the administration of the financial institutions such as members, meetings, management and finances;
  - (c) an Annual General Meeting (AGM) of the members through which the

board and managers present reports to the members on the performance of the financial institution, and members elect office bearers;

- (d) appropriate segregation of duties, and controls to ensure that segregation and independence is observed;
- (e) effective controls over commitments of, and payments by, the CFI or co-operative bank;
- (f) effective controls over conflict of interests;
- (g) appropriate controls for all key business processes and policies, including for major business decisions;
- (h) controls to provide reasonable assurance over the fairness, accuracy, and completeness of the CFI's financial and non-financial information;
- (i) board-approved delegations of authority, (these should also be reviewed regularly by the board);
- (j) reliability of reported financial and non-financial information (both internally and externally);
- (k) regular monitoring of all controls to ensure they remain effective;
- (l) a centralised inventory of all key policies and procedures, and the controls in respect of each policy and procedure; and
- (m) training in respect of relevant components of the internal control system, particularly for employees in positions of trust or responsibility, or who carrying out activities that involve significant risk.

## **11. Risk governance – general requirements for control functions**

- 11.1 To provide appropriate governance over the risk management system and system of internal controls, a CFI or co-operative bank must establish and adequately resource staff to be able effectively deliver on the responsibilities regarding internal controls and control functions.
- 11.2 The board must approve the roles and responsibilities, and any changes to the roles or responsibilities control functions and must ensure that each function has the resources, authority and independence needed to meet its responsibilities.
- 11.3 The authority and responsibilities of each control function must be documented and subject to regular review.
- 11.4 A financial institution's control functions must be adequately staffed by appropriately qualified and competent persons who have sufficient authority to perform their roles effectively.
- 11.5 Control functions should operate without conflicts of interest; where a conflict arises, it must be brought to the attention of the board of directors for resolution.
- 11.6 Control functions must have the right to conduct investigations of possible breaches and to request assistance for such investigations from specialists within the financial institution, or external specialists.
- 11.7 A CFI or co-operative bank may, where appropriate, in light of the nature, scale and complexity of the business, risks, and legal and regulatory obligations of a financial institution, outsource a control function.
- 11.8 A CFI or co-operative bank may, where appropriate in light of the nature, scale and complexity of the business, risks, and legal and regulatory obligations of a CFI, and subject to approval by the Prudential Authority,

- combine the control functions with the exception that the internal audit function, if appointed, may not be combined with other control functions.
- 11.9 Each control function must conduct regular self-assessments of their respective functions and implement or monitor the implementation of any identified improvements.
- 11.10 Depending on the nature, scale and complexity of a CFI or co-operative bank or the adequacy of the risk management framework of the CFI or co-operative bank, the Prudential may require the CFI or co-operative bank to appoint an internal audit function.

## **12. Risk governance – Supervisory or Audit Committee**

- 12.1 A CFI or co-operative bank must have an effective Supervisory or Audit Committee which is enabled to provide the members and the board with independent assurance in respect of the quality and effectiveness of the financial institutions corporate governance framework, and systems for risk management and internal control.
- 12.2 Members of the Supervisory or Audit Committee must be elected by the members of the CFI or the co-operative bank at the annual general meeting and should not have operational business line responsibilities. In instances, where members of the Supervisory or Audit Committee are remunerated, their remuneration should not be linked to the financial performance of the CFI or the co-operative bank.
- 12.3 Members of the Supervisory or Audit Committee must:
- (a) be fit and proper;
  - (b) have sufficient seniority and authority within the CFI's or co-operative bank's governance structure to be effective;
  - (c) have reporting lines that support their independence;
  - (d) have unrestricted access to relevant information;
  - (e) have direct access to the board of directors or relevant Committee, without the presence of senior management if so requested, for the purpose of raising concerns about the effectiveness of the risk management system or system of internal controls; and
  - (f) have the freedom to report to the general members, board of directors or relevant Committee without fear of retaliation from the board or management.
- 12.4 The Supervisory or Audit Committee must report regularly to the general members or relevant Committee.
- 12.5 The Supervisory or Audit Committee must report in writing to the members, board of directors or relevant committee any suspected contravention of any financial sector law that applies to the CFI or co-operative bank. The suspected contravention must also be immediately reported to the Prudential Authority if, in the opinion of the Supervisory or Audit Committee, the contraventions is affecting the safety and soundness of the financial institution.
- 12.6 The Prudential Authority may require the Supervisory or Audit Committee to provide a report on the matters being considered by the Committee as well as the intended actions or actions taken.
- 12.7 The Supervisory or Audit Committee must have a signed committee charter that will govern how the committee operates as well as outlines the role, responsibilities, composition and operating guidelines of the committee.



- 12.8 The Supervisory or Audit Committee must have a three year plan, revised annually, that outlines what the committee plans to achieve.
- 12.9 The Supervisory or Audit Committee must also provide independent assurance to the board of directors, through regular audit activities, on matters such as:
- (a) the means by which the financial institution preserves its assets and those of members, and seeks to prevent fraud, misappropriation or misapplication of such assets;
  - (b) the reliability, integrity and completeness of the accounting, financial and risk reporting information, as well as the capacity and adaptability of the financial institution's information technology architecture to provide that information in a timely manner to the board and management;
  - (c) the design and operational effectiveness of the financial institution's controls in respect of the above matters;
  - (d) other matters as may be requested by the board of directors, management, the Prudential Authority or the auditor; and
  - (e) other matters which the Supervisory or Audit function determines should be reviewed to fulfil its responsibilities as set out in its charter.
- 12.10 A CFI's or co-operative bank's Supervisory or Audit Committee is responsible for selecting an independent reviewer or auditor to perform the annual audit of the financial records and books of the financial institution, coordinating with the auditors and, to the extent requested by the boards and consistent with applicable law, evaluating the quality of performance of the auditors.
- 12.11 In addition, the Supervisory or Audit Committee as mandated by the members, must:
- (a) regularly review the systems for governance, risk management and internal controls and provide an independent assurance to the members and the board of directors that the systems and processes are effective;
  - (b) must provide an independent assurance to the members and the Prudential Authority, if requested, that the CFI or co-operative bank complies with the requirements of the Act and prudential standards issued under the Act;
  - (c) must report to the members, board of directors and the Prudential Authority any matters identified during the performance of its responsibilities that are contrary to the Act or the prudential standards issued under the Act or will negatively affect the maintenance of a sound risk management framework;
  - (d) ensure that the CFI or co-operative bank has an internal process to address all the issues raised by the Supervisory or Audit Committee, an independent reviewer or auditor.
- 12.12 The Supervisory or Audit Committee must provide a detailed report to the board and the AGM on its activities and requirements set out in this Standard.
- 12.13 In its reporting, the Supervisory or Audit Committee should address at least the following areas:
- (a) the committee's annual or other periodic risk-based audit plan, detailing the proposed areas of audit focus, and any significant modifications to the audit plan;
  - (b) any factors that may adversely affect the Supervisory/Audit function's

- independence, objectivity or effectiveness;
- (c) verification of the member deposit, share, and loan accounts with the records;
- (d) receiving and investigation of any complaint or appeal by members concerning the operations of the CFI or co-operative bank;
- (e) material findings from audits or reviews conducted; and
- (f) the extent of senior management's compliance with agreed corrective or risk-mitigating measures in response to identified control deficiencies, system weaknesses, or compliance violations.

### **13 The risk management function<sup>1</sup>**

- 13.1 The CFI or co-operative bank must have an effective risk management function, capable of assisting the financial institution to identify, assess, monitor, and mitigate its material risks, and promote a sound risk culture.
- 13.2 A CFI's risk management function is responsible for assisting the board of directors and management to develop and maintain the financial institution risk management system, including promptly informing the board of any circumstance that may have an adverse material effect on the risk management system of the CFI or co-operative bank.

### **14 The compliance function**

- 14.1 A CFI or co-operative bank must have an effective compliance function capable of assisting the CFI or co-operative bank to meet its legal, regulatory and supervisory obligations and promote and sustain a sound compliance culture.
- 14.2 A CFI's or co-operative bank's compliance function is responsible for assisting the board and management to identify and meet their legal and regulatory obligations.
- 14.3 The responsibilities of a CFI's or co-operative bank's compliance function include implementing a risk-based compliance plan for monitoring compliance with the financial institution system of internal controls, as well as legal and regulatory obligations.
- 14.4 The compliance function must monitor compliance shortcomings and instances of non-compliance report such to the Prudential Authority or other relevant regulatory authorities.
- 14.5 A CFI's or co-operative bank's compliance function must ensure that regular training is conducted on compliance obligations, particularly for employees in positions of trust or responsibility, or who are involved in activities that have significant legal or regulatory risk.

---

<sup>1</sup> With respect to the risk management and compliance function, CFI's will be required to have a member of current staff that will discharge such functions.

## **Attachment 1: Policies for managing financial risks**

1. As part of prudent business management a CFI or co-operative bank must have board-approved policies that address the identification and management of the risks it faces, that are proportionate to the nature, scale or complexity of the CFI or co-operative bank.
2. This Attachment provides details on the minimum required content of the financial risk management policies set out in paragraph 8 of this Standard.
3. Unless otherwise approved by the Prudential Authority, the CFI or co-operative bank must adopt the following policies and must address at least the issues raised in this Attachment.

### **A. Strategic risk management policy (including capital management)**

A CFI's or co-operative bank's Strategic Risk Management Policy must:

1. Include strategic plans which shall be supported by appropriate organisational and functional structures, skilled and experienced personnel, an adequate budget, management information systems, as well as risk monitoring and controlling systems.
2. Be consistent with the organisational goals and shall be adjustable to changing environmental factors.
3. Provide for clear responsibility for the Strategic plan and the strategic planning process to the board of directors or a delegated committee. If the strategic planning process is not appropriate or if the assumptions are not realistic, the strategic plan will be flawed thereby exposing the institution to strategic risk.
4. Set an appropriate budget and provide for development of operational plans consistent with the overall CFI or co-operative bank's strategy by management.
5. Provide for a Capital Management Policy which must:
  - (a) Provide for an internal capital planning process.
  - (b) Set out the CFI's or co-operative bank strategy for ensuring adequate capital is maintained over time, including specific, quantifiable internal capital targets. These targets should be set in the context of the results of the CFI's or co-operative bank's reviews, the CFI's risk profile, the board of directors' risk appetite, and regulatory capital requirements. The strategy should include plans for how target levels of capital are to be met and the means available for sourcing additional capital where required. The strategy should be consistent with the CFI's or co-operative bank's overall business and risk management strategy.
  - (c) Provide for the identification and measurement of risks that may result in capital shortfalls.
  - (d) Establish procedures for monitoring the CFI's or co-operative bank's compliance with its regulatory and internal capital requirements and targets, including triggers to alert management to potential breaches of the regulatory and target capital requirements.
  - (e) Set out the actions to be taken where capital shortfalls occur or are likely to occur.
  - (f) Provide for appropriate management and regular review of capital and the capital management process (including independent review).

## **B. Credit risk policy**

A CFI's or co-operative bank's credit risk policy must:

1. Set out the CFI's or co-operative bank's approach to the identification, assessment, monitoring, management, and reporting of credit risk (including credit concentration risk). The CFI's or co-operative bank's approach to managing credit risk should be consistent with the complexity, risk profile, and scope of operations of the CFI or co-operative bank.
2. Identify the full range of credit exposures the CFI or co-operative bank is likely to encounter in its normal course of business.
3. Identify the range of credit exposures the CFI or co-operative bank is willing to take on, and the ways in which it will avoid taking on those risks that it is unwilling to retain.
4. Provide for quantification of credit risks, using a methodology that is consistent with the complexity, risk profile, and scope of operations of the CFI or co-operative bank.
5. Identify risk mitigation strategies for managing credit exposures to ensure they are kept within the credit risk limits set by the board. Where risk mitigation involves risk transfer to another party, the CFI or co-operative bank should ensure that the credit risk of the transferee is appropriately factored into the CFI's or co-operative bank's assessment of residual credit risk.

## **C. Interest rate risk policy**

CFIs and co-operative banks are not expected to have significant equity and currency risk on their balance sheets without prior approval by the Prudential Authority. Consequently, emphasis is placed on the interest rate risk component of market risk as it is the predominant factor.

A CFI's or co-operative bank interest rate risk policy must:

1. Specify clear responsibilities of the board with respect to:
  - (a) setting out the CFI's or co-operative bank's approach to the definition, identification, measurement, management and reporting of interest rate risk. The CFI's or co-operative bank approach to managing interest rate risk should be consistent with the complexity, risk profile, and scope of operations of the CFI or co-operative bank;
  - (b) reviewing the overall objectives of the CFI or co-operative bank with respect to interest rate risk and ensuring the provision of clear guidance regarding the level of interest rate risk acceptable to the CFI or co-operative bank;
  - (c) approving broad business strategies of the CFI or co-operative bank with respect to interest rate risk and ensuring that management takes the steps necessary to identify, measure, monitor, and control interest rate risk.
  - (d) approving policies that identify lines of authority and responsibility for managing interest rate risk exposures; and
  - (e) delegating responsibility for establishing interest rate risk policies to the relevant board committee.
2. Clear responsibility of management to maintain and ensure:
  - (a) appropriate limits on risk taking;
  - (b) adequate management information systems and standards for

- measuring interest rate risk;
  - (c) Standards for valuing positions and measuring performance;
  - (d) A comprehensive interest rate risk reporting and management review process; and
  - (e) Effective internal controls.
3. Provide for a mechanism to annually review the CFI's or co-operative bank's interest rate risk management policies and procedures to ensure that they remain appropriate and sound.
  4. Periodically update members and the Prudential Authority with respect to interest rate risk measurement, reporting and management procedures.

**D. *Liquidity Management Policy (including asset-liability management)***

A CFI's or co-operative bank's liquidity management policy must:

1. Set out the CFI's or co-operative bank's approach to the definition, identification, measurement, management and reporting of short-term and long-term liquidity risk, to ensure that the financial institution is able to meet its obligations as they fall due. The CFI's or co-operative bank approach to managing liquidity risk should be consistent with the complexity, risk profile, and scope of operations of the CFI or co-operative bank. The approach must include early warning indicators, triggers, action plans, and clear responsibilities for responding to liquidity stresses, should they arise.
2. Include stress testing in order to determine the impact on the CFI's or co-operative bank's liquidity position of a range of adverse scenarios. These scenarios should include major trigger events such as catastrophes, counterparty defaults, and other adverse events.
3. Take specific account of the liquidity consequences of financial difficulties or default by its counterparties, and the types of events that could lead to such difficulties.
4. Take specific account of the nature of the CFI's or co-operative bank's investments and the impact of adverse scenarios on the liquidity of these investments.
5. Clearly specify the nature, role and extent of the CFI's or co-operative bank's liquidity risk activities and their relationship with product development, pricing functions and investment management.
6. Co-ordinate the management of risks associated with liquidity risk and the complexity of those risks.
7. Recognise the interdependence between the CFI's or co-operative bank's assets and liabilities and take into account the correlation of risk between different asset classes and the correlations between different products and business lines.
8. Specify clear responsibilities of the board with respect to:
  - (a) Reviewing the overall objectives of the CFI or co-operative bank with respect to liquidity and ensuring the provision of clear guidance regarding the level of liquidity risk acceptable to the CFI or co-operative bank;
  - (b) Approving broad business strategies of the CFI or co-operative bank with respect to liquidity risk and ensuring that management takes the steps necessary to identify, measure, monitor, and control liquidity risk;
9. Delegating responsibility for establishing liquidity risk policies to the relevant board committee.
10. Clear responsibility of management to maintain and ensure:

- (a) Appropriate limits on risk taking;
- (b) Adequate management information systems and standards for measuring liquidity risk;
- 11. Effective internal controls.
- 12. Provide for a mechanism to annually review the CFI or co-operative bank's liquidity risk management policies and procedures to ensure that they remain appropriate and sound.

## **E. Operational Risk Policy**

A CFI's or co-operative bank operational risk policy must:

- 1. Set out the CFI's or co-operative bank's approach to the identification, assessment, monitoring, management and reporting of relevant operational risk exposures (including the risks associated with inadequate or failed internal processes, people or systems, or from external events).
- 2. Policies and procedures shall contain processes, among others, to identify, assess, monitor and control/mitigate operational risk such as:
  - (a) Risk and Control Self-Assessments, its methodology, the frequency with which it has to be done and the persons involved in the process;
  - (b) Key Risk Indicator identification and assessment methodology;
  - (c) The methodology for the capture and use of internal and external operational risk loss data; and
  - (d) Documented risk monitoring and reporting procedures.
- 3. Provide for the development and implementation of an information technology internal control framework that:
  - (a) addresses planning, implementation, delivery, support, monitoring and reporting;
  - (b) addresses effectiveness, efficiency, availability, integrity, confidentiality, reliability and compliance; and
  - (c) provides for independent assurance on the effectiveness of the information technology internal controls, including data management systems.
- 4. Address critical technology-related risk areas such as:
  - (a) The information technology policy must address the way in which the CFI or co-operative bank monitors, manages and responds to cyber risk (which is risk of major disruption from a cyber-attack);
  - (b) CFIs or co-operative banks must have a Cyber Attack Response Plan, with clear assignment of roles and responsibilities for responding to the attack; and
  - (c) Integration risk - the risk arising from participation in a networked banking platform/system
- 5. Provide for processes to ensure the promotion of an ethical information technology governance culture and awareness.
- 6. Provide for processes and procedures to ensure the effective management and utilisation of information technology assets.
- 7. Keeping members informed of cyber-attacks.
- 8. Provide for the development, implementation and management of systems for the management of information and data, including systems in respect of information security
- 9. Provide for contingency plans in cases of business disruptions commensurate to the nature, scale and complexity of the CFI or co-operative.

10. Provide for controls and processes relating to money-laundering and other financial crimes including processes and controls relating to Know-Your-Customer.

#### ***F. Legal and Compliance Risk Policy***

A CFI's or co-operative bank's legal and compliance risk policy must:

1. Include the nature and level of legal & compliance risk to which the CFI or co-operative bank is exposed and how its risk profile fits within the overall business strategy.
2. Clear responsibility for legal and compliance risk, including sufficient board and committee oversight;
3. Include a clear process for the review of the constitution, adherence to democratic process, including the annual general meeting.
4. Include mechanisms to review the representational responsibilities and terms of the board annually and review and develop board policies, including aspects of board succession planning.
5. In general the policies and procedures shall provide for the following among other considerations:
  - (a) a framework for dealing with legal matters of varying complexity;
  - (b) maintenance of a central inventory of key documents such as contracts, licenses, policy statements and others;
  - (c) regular review and assessment of legal risk in the CFI or co-operative bank's activities including new products;
  - (d) adequate documentation on all significant transactions including security administration;
  - (e) record maintenance in line with relevant statutory requirements; and
  - (f) maintenance of confidentiality provisions.
6. Include reporting mechanisms for deviations and non-compliance to the Prudential Authority.

#### ***G. Outsourcing policy***

A CFI's or co-operative bank's outsourcing policy must provide for the following:

1. Establish criteria and procedures for appointing and renewing outsourcing service providers;
2. Provide guidance on how to assess, monitor and managed outsourcing risk;
3. Stipulate that management and the board retains all the responsibility for all regulatory obligations, and ensuring that the outsourced activity does not increase the risk profile of the CFI or co-operative bank;
4. A risk assessment on the potential service provider to form part of the due diligence process, prior to the on-boarding of the service provider;
5. Provide for open communication channels between the CFI or co-operative bank and the outsourcing service provider; and
6. Annual review and approval by the board.