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Internal Control and Compliance of Banks

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Internal Control and Compliance of Banks

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Foreword

In an increasingly complex and evolving financial landscape, ensuring the integrity, transparency, and resilience of banking institutions has become more critical than ever. Robust internal control and compliance (ICC) frameworks are not just regulatory imperatives—they are strategic assets that safeguard public trust and institutional sustainability.

The Bangladesh Institute of Bank Management (BIBM) has been at the forefront of fostering a sound banking ecosystem in Bangladesh by undertaking critical research, providing policy-oriented insights, and guiding capacity development. In continuation of this tradition, the current review paper titled "Internal Control and Compliance of Banks" for the reporting year 2024 offers a comprehensive assessment of the evolving practices, regulatory reforms, and institutional challenges in the ICC domain.

This year's study incorporates a methodologically rigorous combination of structured surveys, Focus Group Discussions (FGDs), and Key Informant Interviews (KIIs), ensuring that both quantitative indicators and qualitative perceptions are well captured. The research sheds light on trends in governance, the effectiveness of internal audit systems, technological integration in control mechanisms, and the overall maturity of compliance cultures across the banking sector. Importantly, the study also reflects recent regulatory developments, including risk-based supervision frameworks and enhanced expectations around internal audit independence, concurrent audits, and monitoring capabilities.

I extend my sincere appreciation to all the stakeholders who have played a crucial role in the successful completion of this research. Furthermore, I extend my appreciation to the research team for their dedication, analytical rigor, and collaborative spirit. Their efforts have yielded an insightful document that will serve not only banking professionals and policymakers, but also academics and researchers in the broader field of financial governance.

I hope the findings and recommendations outlined in this paper will support the banking industry in further strengthening its internal control architecture, enhancing compliance culture, and thereby contributing to greater financial system stability in Bangladesh.

Md. Akhtaruzzaman, Ph.D.
Director General, BIBM

Acknowledgment

The successful completion of this research study titled "Internal Control and Compliance of Banks" has been made possible through the collective contributions, cooperation, and encouragement of many individuals and institutions. We express our sincere gratitude to Dr. Md. Akhtaruzzaman, Director General of BIBM, for his continuous guidance and strong support throughout the study.

We are especially thankful to the wider banking community of Bangladesh for their enthusiastic participation and collaboration. The senior officials—including Managing Directors/CEOs and Heads of Internal Control and Compliance Departments—have generously shared data, insights, and experiences, significantly enriching the analysis and findings of this paper.

We would also like to acknowledge the support received from our fellow colleagues at BIBM, especially the teams from the Training, Administration, Accounts, and Publication Wings, whose cooperation ensured smooth execution of various aspects of the study.

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Lastly, we are grateful to all those who, directly or indirectly, contributed to this endeavor. The open dialogue and continuous engagement with stakeholders have provided us with diverse perspectives and helped make this paper a comprehensive reflection of the evolving practices in internal control and compliance in the banking sector of Bangladesh.

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Executive Summary

This report provides a comprehensive review of the internal control and compliance (ICC) systems in Bangladesh's banking sector for the year 2024. It builds upon prior studies and incorporates findings from structured questionnaires, Focus Group Discussions (FGDs), and Key Informant Interviews (KIIs) with senior banking professionals and regulatory stakeholders. The objective of the study is to evaluate the existing governance framework, highlight prevailing challenges, and recommend actionable reforms for enhancing the effectiveness of ICC mechanisms in banks.

Over the years, Bangladesh's banking industry witnessed heightened scrutiny on its internal control systems, triggered by governance lapses, rising non-performing loans, and fraud incidents. In response, the Bangladesh Bank introduced several regulatory reforms, including core risk management guidelines, the Bank Company External Auditor Rules 2024, the Guidelines for Merger/Amalgamation of Banks, and the enactment of the Bank Resolution Ordinance 2025. These frameworks aim to promote strong corporate governance, ensure audit independence, and implement early intervention strategies under the Prompt Corrective Action (PCA) regime.

The findings from the field reveal that while some changes have been made in governance awareness and institutional compliance structures, significant gaps remain. Notably, the independence of Internal Control and Compliance Department (ICCD) is still under pressure due to hierarchical imbalances, limited authority, and lack of support from senior management. Many banks continue to assign ICCD staff with business targets, directly conflicting with international best practices.

Assessment of key internal control tools such as the Health Report, Branch Risk Rating System, and risk-based internal audits reveals mixed results. Although banks comply with formal reporting requirements, delays, inconsistencies in quality, and limited management engagement hinder their utility in proactive decision-making. The study also found inadequate automation in audit and monitoring functions, with most banks relying heavily on manual processes despite acknowledging the value of digitization.

A noteworthy insight is the mismatch in perception between ICCD professionals and top management. While most banks claim high independence of ICCD functions, FGDs indicate that many recommendations are either ignored or

leadership at the top, and a more integrated ICCD model that merges audit, compliance, and monitoring units under a unified governance structure.

The report concludes with a set of practical recommendations, including the need for Bangladesh Bank to revise the ICC Guidelines 2016, formalize minimum qualifications for ICCD heads, incentivize automation, and enforce appointment of higher-ranked officers to ICCD leadership roles. It also advocates for industry-wide knowledge-sharing platforms, enhanced training, and recognition mechanisms to uplift the status and performance of internal control functions.

Overall, this year’s review highlights the critical importance of embedding integrity, transparency, and accountability across the governance fabric of banks. Strengthening internal control is not merely a compliance requirement—it is a strategic imperative for ensuring financial stability, public trust, and long-term sustainability in the banking sector of Bangladesh.

List of Abbreviation

AAOIFI	: Accounting and Auditing Organization for Islamic Financial Institutions
ACB	: Audit Committee of Board
AML	: Anti-Money Laundering
BAC	: Board Audit Committee
BB	: Bangladesh Bank
BCBL	: Basel Committee on Banking Supervision
BIBM	: Bangladesh Institute of Bank Management
BIS	: Bank for International Settlements
BoD	: Board of Directors
BRPD	: Banking Regulation and Policy Department
BSEC	: Bangladesh Securities and Exchange Commission
CAMELS	: Capital Adequacy, Asset Quality, Management Competence, Earnings, Liquidity, and Sensitivity to Market Risk
CEO	: Chief Executive Officer
CIPA	: Certified Islamic Professional Accountant
COSO	: Committee of Sponsoring Organizations of the Treadway Commission
CSAA	: Certified Shari'ah Advisor and Auditor
DCFCL	: Departmental Control Function Checklist
DOBB	: Directives of Bangladesh Bank
ECB	: Executive Committee of Board
ERM	: Enterprise Risk Management
ESG	: Environmental, Social, and Governance
FCA	: Fellow Chartered Accountant
FGD	: Focus Group Discussions
FOREX	: Foreign Exchange
HR	: Human Resource
IA	: Internal Audit
IAASB	: International Auditing & Assurance Standards Board
IASFD	: Internal Audit Surveillance and Follow-up Department
ICC	: Internal Control and Compliance
ICCD	: Internal Control and Compliance Divisions
ICS	: Internal Control System
ICT	: Information and Communication Technology
IESBA	: International Ethics Standards Board for Accountants
IFAC	: International Federation of Accountants
IFI	: Islamic Financial Institution

IFRS : International Financial Reporting Standard
IFSB : Islamic Financial Services Board
IIA : Institute of Internal Auditors
IPPF : International Professional Practices Framework
IS : Information Systems
ISA : International Standards on Auditing
IT : Information Technology
KII : Key Informant Interview
KPI : Key Performance Indicator
KYC : Know Your Customer
LDC : Loan Documentation Checklist
MANCOM : Management Committee
MBM : Masters in Bank Management
MD : Managing Director
MIS : Management Information System
N/A : Not Available/Applicable
NPI : Non-Performing Investment
NPL : Non-Performing Loan
OECD : Organization for Economic Co-operation and Development
PCA : Prompt Corrective Action
PLC : Public Limited Company
PPG : Program Policy Guidelines
QOR : Quarterly Operation Report
RBA : Risk-Based Audit
RJSC : Registrar of Joint Stock Companies
RMC : Risk Management Committee
RMD : Risk Management Division
ROA : Return on Assets
ROE : Return on Equity
S/N : Serial Number
SMT : Senior Management Team
SOP : Standard Operating Procedures
SSC : Shariah Supervisory Committee
TOR : Terms of Reference

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Internal Control and Compliance of Banks

1. Introduction

A sound and resilient internal control system (ICS) serves as the cornerstone of prudent banking operations worldwide. Given the high leverage, maturity mismatch between assets & liabilities, and systemic interlinkages characteristic of modern banks, even a single institution's failure can undermine public confidence, triggering contagion effects throughout the financial system (Ehiedu & Ogbeta, 2014). Therefore, the operational architecture of banks must be reinforced by multiple layers of oversight – central bank supervision, independent external audit, and, most critically, self-regulation through robust internal control mechanisms (COSO, 2013; Bangladesh Bank, 2016).

Globally, the Basel Committee on Banking Supervision (BCBS) has underscored the importance of internal control in fostering ethical norms, compliance culture, and operational integrity at all levels of an organization (Sokol, 2011). Internal control ensures not only adherence to laws, policies, and regulations but also enhances transparency, protects stakeholders' interests, and supports risk management (IFAC, 2012). Following the 2007–08 financial crisis, international regulators intensified their focus on governance and internal control to mitigate imprudent risk-taking and preserve financial stability (Jin et al., 2013).

Internal control is particularly pivotal in ensuring a bank's operational efficiency, asset quality, and financial sustainability. It mitigates fraud, reduces agency costs, promotes ethical conduct, and facilitates accurate financial reporting (Rittenberg & Schwieger, 2001; Maijoor, 2000). A weak internal control environment can result in asset deterioration, mismanagement, and accounting anomalies, potentially culminating in systemic failures, as was evident in the collapses of Enron, WorldCom, and Tyco (Moosa, 2007).

In Bangladesh, innovative irregularities have been witnessed in last few years, which is considered a gross failure of internal control system. Country like Bangladesh, where the financial sector remains predominantly bank-based due to an underdeveloped capital market, internal control has emerged as a strategic necessity rather than a compliance formality. The sector's remarkable growth in deposit mobilization, branch expansion, financial innovation, and service diversification has intensified its exposure to credit, market, operational, and strategic risks (Akwaa-Sekyi & Gene, 2016; Siddique et al., 2016). The Bangladesh Bank (BB), recognizing this evolving landscape, issued a comprehensive guideline on Internal Control and Compliance (ICC) in 2003, which underwent a major revision in 2016 to reflect global standards and local market dynamics (Bangladesh Bank, 2016).

Empirical research in both developed and emerging markets has repeatedly demonstrated that effective ICS positively correlates with financial performance metrics such as return on assets (ROA) and return on equity (ROE), while inadequacies in internal control are often linked to lower profitability and higher incidence of fraud (Doyle et al., 2007). These findings validate that internal control is not a cost center but a strategic enabler that allows firms to engage safely in high-value, risk-adjusted operations (Siddique at al., 2023).

In the domestic context, numerous studies and institutional evaluations have reinforced the criticality of ICC in safeguarding banking assets and enhancing operational resilience (Siddique et al., 2013; Hayali et al., 2012). Several major banking frauds in Bangladesh over the past decade – including fund embezzlements and irregular credit exposures – highlighted weaknesses in internal oversight mechanisms and prompted both regulatory and institutional reforms in the last few months in the banking sector.

Notably, the internal control framework in Bangladesh operates under a dual responsibility: banks must not only conform to regulatory guidelines but also cultivate a control culture driven by self-governance, ethics, and operational excellence (Akwaa-Sekyi et al., 2016). To that end, banks have increasingly adopted technology-based control systems, established Internal Control and Compliance Divisions (ICCD), and initiated risk-based internal audits. However, gaps still exist in the standardization of control practices, resource allocation, capacity building, and audit independence.

The Bangladesh Bank continues to play a catalytic role in nurturing a dynamic ICC culture. Its evolving guidelines, periodic risk-based audits, and compliance rating frameworks will prompt banks to improve governance practices. Besides, central bank is going to launch a risk-based supervision of the industry. Additionally, the central bank has encouraged banks to integrate ICC into Enterprise Risk Management (ERM) systems, thereby linking compliance efforts with strategic decision-making.

In the post July 2024 era, the need for resilient ICS has become even more pronounced. The pandemic of irregularities disrupted operational continuity, even exposed a high-level threat for survival of some banks. This calls for a renewed focus on digital transformation of ICC, business continuity planning, and real-time risk surveillance.

Against this backdrop, the present review paper provides a comprehensive analysis of the ICC practices of banks in Bangladesh for the reporting year. The study aims to: identify emerging trends and best practices in internal control, compare the current ICC environment with that of the previous year, highlight systemic challenges and institutional gaps, and suggest policy-level recommendations for improving governance and risk resilience.

1.1 Methodology of the Study

This study adopts a descriptive research design to examine the internal control and compliance practices in the banking sector of Bangladesh, focusing on the implementation status and operational challenges in 2024. The methodology is grounded in both primary and secondary data sources, enabling a comprehensive understanding of the subject matter.

Primary data was obtained through a structured questionnaire administered to the member banks under the purview of the Bangladesh Institute of Bank Management (BIBM). Additionally, two Focus Group Discussion (FGD) was conducted with 51 officials actively engaged in the Internal Control and Compliance Departments (ICCD) of various banks, including several Heads of ICCD and Heads of Internal Audit. The study was further enriched by Key Informant Interview (KII) with 10 industry leaders, including senior bank officials, regulatory authority representatives, and subject matter experts from the banking industry. Besides, the draft paper was presented in a review workshop participated by 85 professional bankers and industry leaders.

To complement the primary findings, secondary data was extracted from a wide range of sources, including relevant laws, regulatory frameworks, institutional policies, and earlier BIBM review reports. As part of the methodology, a comparative analysis was conducted, juxtaposing the current data with findings from previous years to identify performance trends, regulatory compliance patterns, and emerging gaps.

A core component of this study involved content analysis of both local and international regulatory frameworks related to internal control and internal audit. Locally, this encompassed guideline issued by Bangladesh Bank, such as the Internal Control and Compliance Guidelines (2016) and relevant circulars. Globally recognized standards issued by organizations such as the Committee of Sponsoring Organizations of the Treadway Commission (COSO), the Institute of Internal Auditors (IIA), the Basel Committee on Banking Supervision (BCBS) and were examined. This regulatory content analysis allowed for benchmarking domestic practices against global standards and identifying alignment or deviations in policy and execution.

The data and insights obtained have been presented using tabular formats and graphical representations, where appropriate, to facilitate clarity and visual comprehension. The report has been finalized following the incorporation of suggestions and observations raised during the review workshop.

1.2 Structure of the Report

The report is structured into five sections which are as follows: Section I covers background and objectives and methodology of the study; Section II outlines the conceptual framework of ICS; Section III reviews the domestic and international regulatory landscape; Section IV provides a detailed analysis of the operational practices and compliance levels of banks' ICCDs; and Section V concludes with key observations, issues raised in the research workshop, and forward-looking recommendations for industry stakeholders. Ultimately, the study affirms that institutionalizing a robust and adaptable ICC framework is fundamental to ensuring the sustainability, credibility, and competitiveness of the banking industry in Bangladesh.

2. Internal Control and Compliance: Conceptual Framework

In the financial sector, particularly in banking, internal control and compliance mechanisms are essential tools for sustaining operational integrity, reducing risk, and promoting accountability. This chapter provides a theoretical foundation by clarifying the concepts of internal control and compliance, analyzing relevant regulatory frameworks, and explaining their role in improving governance and risk mitigation. Understanding these fundamentals is vital to assess how these mechanisms shape bank performance and ensure sound financial practices.

2.1 Concept of Internal Control

Internal control is defined Internal control refers to a process affected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives (COSO, 2013). According to COSO, internal control focuses on three key objectives: *Operations* – ensuring efficiency and effectiveness in business functions, achieving financial and operational targets, and safeguarding assets from unauthorized use or loss; *Reporting* – promoting the accuracy, reliability, and timely delivery of both internal and external financial and non-financial reports; and *Compliance* – maintaining adherence to applicable laws, regulations, and internal policies.

This framework is built on five interdependent elements: *Control Environment*, which shapes organizational culture and sets the foundation for internal control; *Risk Assessment*, involving the identification and evaluation of potential risks that may obstruct objectives; *Control Activities*, consisting of the measures and actions taken to implement management decisions; *Information and Communication*, which facilitate the collection and dissemination of critical data across all levels; and *Monitoring*, involving continuous review to ensure the system's effectiveness and responsiveness.

In banking, a strong internal control system is essential to prevent and detect irregularities, maintain reliable financial reporting, and uphold stakeholder confidence. Deficiencies in internal control can expose banks to financial loss, regulatory sanctions, damage to reputation and even liquidation. The COSO Internal Control – Integrated Framework is provided in Appendix 1, and Appendix 2 illustrates the Enterprise Risk Management (ERM) Helix Framework.

2.2 Concept of Compliance

Compliance refers to a bank's ability to conform to internal policies and external regulatory requirements. It includes adhering to laws, rules, codes of conduct, and standards set by supervisory authorities such as Bangladesh Bank. An effective compliance function ensures that banks operate within legal boundaries, thereby minimizing regulatory risks and legal liabilities. Compliance is not merely about regulatory conformity—it also promotes ethical behavior, risk awareness, and a culture of integrity. A strong compliance framework allows for early detection of misconduct and helps maintain the institution's credibility in the market. It is expected that each bank will establish a robust self-regulatory system to ensure effective compliance. Reliance on external enforcement alone is often insufficient;

instead, internal commitment and a culture of accountability are far more effective in sustaining long-term compliance.

2.3 Interrelationship Between Internal Control and Compliance

Internal control and compliance are interdependent functions that collectively support sound governance and effective risk management. While internal control focuses on operational efficiency and safeguarding assets, compliance ensures that these operations adhere to legal and ethical standards. In practice, compliance functions often serve as part of the internal control system, especially concerning regulatory and legal obligations.

For instance, an effective internal control mechanism will contain controls related to anti-money laundering (AML), Know Your Customer (KYC), and transaction monitoring—areas where compliance oversight is critical. The synergy between these functions ensures comprehensive coverage of both operational and regulatory risks.

2.4 Three Lines of Defense in Internal Control System

The effectiveness of internal control and risk management framework of an organization is fundamentally shaped by the Three Lines of Defense model, a widely accepted structure in corporate governance. This model provides a clear delineation of roles and responsibilities across an organization to ensure that risks are properly identified, managed, and independently reviewed.

The first line of defense consists of operational management, which bears direct responsibility for maintaining effective internal controls within their specific business units. This tier owns and manages risk, implementing control activities such as approvals, reconciliations, and routine supervisory practices. Their role includes not only adhering to policies and procedures but also detecting and correcting control failures at the source. Any lapse in their compliance can result in significant operational and reputational consequences for the institution.

The second line of defense encompasses functions responsible for risk oversight, including compliance, risk management, legal, and financial control units. These functions are separate from operational management but remain part of the organization’s overall management structure. Their role is to design and monitor risk-related policies, provide guidance, and ensure that the controls implemented by the first line are adequate and effective. They support the first line by facilitating risk assessment methodologies, compliance frameworks, and policy updates while ensuring the organization does not assume undue risk beyond its appetite.

The third line of defense is formed by the internal audit function, which operates with full independence from the management structure. Internal audit provides objective assurance on the effectiveness of governance, risk management, and internal controls. From an internal control perspective, internal auditors play a critical role in evaluating whether existing control activities are sufficient to mitigate key risks and whether compliance obligations are being fulfilled across all levels of the organization.

Internal audit's scope is comprehensive. It includes evaluating the design and operational effectiveness of controls embedded within the business processes, verifying adherence to both internal policies and external regulatory requirements, and assessing the adequacy of risk management practices. Crucially, internal audit does not implement controls or manage risks directly but rather assesses how well both the first and second lines are performing their duties. Their findings, reported directly to senior management and the audit committee of the board, provide a crucial feedback loop for continuous improvement.

The efficacy of the third line of defense lies not only in its ability to detect weaknesses but also in the responsiveness of the organization to its recommendations. If audit findings are ignored or implementation is delayed, the institution becomes vulnerable to control failures, regulatory penalties, or fraud. Therefore, the value of internal audit is maximized when its insights lead to timely corrective actions, reinforcement of accountability, and enhancement of the internal control system.

Moreover, as banks increasingly adopt technology-driven models, the internal audit function must evolve. It should integrate data analytics, automate risk assessment, and enhance audit methodologies to remain effective in identifying sophisticated control breaches. In addition, strong coordination between the three lines of defense—without compromising their independence—is essential. Each line should maintain its integrity while working collaboratively to ensure a resilient control environment.

In conclusion, the internal audit, as the third line of defense, serves as the cornerstone of assurance in the Three Lines of Defense model. Its independent oversight strengthens the internal control framework by bridging gaps, enhancing transparency, and promoting accountability across all levels of the bank. A robust and well-integrated Three Lines of Defense model enables banks to proactively manage risk, comply with regulatory requirements, and build institutional resilience in an increasingly complex financial environment.

2.5 Internal Control and Compliance Department

According to regulatory requirements set by Bangladesh Bank, all banking institutions are required to establish an Internal Control and Compliance Department (ICCD) at the head office level. This department comprises three interlinked units: (a) Internal Audit Unit, (b) Monitoring Unit, and (c) Compliance Unit. These units function in coordination, with each depending on the activities of the others to maintain a cohesive control environment. Rather than functioning in isolation, the Internal Control System (ICS) is embedded throughout all levels of the bank's operations, involving personnel from the Board of Directors to entry-level employees. ICCD plays a pivotal role in ensuring compliance with all regulatory instructions, internal policies, and board-approved procedures. It is also charged with detecting potential gaps in internal controls and policy adherence across various operations.

The efficiency of the bank's overall internal control framework depends not only on ICCD's execution but also on the contributions of all branches and departments. As per Bangladesh Bank guidelines (BB, 2016), the ICCD Head is responsible for both monitoring and compliance activities and reports these to the bank's senior executives. Meanwhile, the Internal Audit Unit Head, part of ICCD, reports directly to the Board's Audit Committee, with their performance being evaluated by the committee chairperson.

2.5.1 Role and Functions of the Internal Audit Unit (On-site Audit)

The Institute of Internal Auditors (IIA) highlights internal audit as a crucial function that supports an organization's objectives through an impartial and methodical approach. It enhances the effectiveness of risk control, governance, and internal processes. Internal audit is defined as an independent, objective assurance and consulting activity designed to add value and improve an organization's operations and it helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes (www.theiia.org).

As the highest form of internal control, internal audit ensures that other control systems are functioning effectively. It does not execute the controls but instead assesses the adequacy and reliability of existing control mechanisms, policies, and procedures to ensure alignment with the organization's goals. A strict independence from day-to-day management and operations is maintained. Typically, the audit function is divided into specialized units such as regular audit, surprise audit, concurrent audit, Forex audit, IT audit.

2.5.2 Role of the Monitoring Unit (Off-site Surveillance)

The Monitoring Unit within ICCD primarily oversees off-site surveillance, ensuring continuous review of the bank's daily activities across all branches and departments. This is achieved through technology-driven systems and regular documentation assessments. The unit's primary function is to verify consistent application of approved processes and detect anomalies in day-to-day operations. It evaluates critical reports like the Departmental Control Function Checklist (DCFCL), Loan Documentation Checklist (LDC), and the Quarterly Operation Report (QOR). Upon identifying irregularities, it promptly communicates with the concerned branch or unit to initiate corrective measures. For significant discrepancies, it may recommend further inspection by the Internal Audit Unit.

One of its core responsibilities is preparing the "Self-Assessment Report on Anti-Fraud Internal Controls," which consolidates compliance data and relevant documentation from different departments. This report is submitted to Bangladesh Bank quarterly. The unit also contributes to drafting the Annual Health Report for submission to Bangladesh Bank. Through specialized software, the unit monitors sensitive areas such as staff accounts, mandatory leaves and transfers, deposits, loan accounts, and ledger transactions. Any suspicious findings are escalated to the Senior Management Team and Board through the ICCD Head.

2.5.3 Responsibilities of the Compliance Unit (Follow-up and Reporting)

As the follow-up and reporting arm of ICCD, the Compliance Unit ensures implementation of recommendations issued by internal auditors, external reviewers, and Bangladesh Bank examiners. It prepares compliance status reports that are forwarded to senior management and the Audit Committee.

The Compliance Unit actively contributes to policy formulation, awareness building, and dissemination of internal circulars. It also collaborates with training institutes to develop programs on regulatory compliance and engages with regulatory authorities to clarify complex compliance issues. The unit may hold coordination meetings and maintains a comprehensive record of audit findings. Its proactive approach includes ensuring timely resolution of identified weaknesses and assisting departments in meeting regulatory expectations. A schematic representation of the ICCD structure and its core units is presented in Appendix 3.

2.6 Internal Audit as Third Eye of Different Stakeholders

The Internal Audit (IA) function serves as a critical, independent assurance mechanism that operates like a "third eye" for various stakeholders within the banking sector. This metaphor emphasizes IA's role in providing oversight and insight into areas where other stakeholders face limitations in access, visibility, or capacity. For shareholders and the Board of Directors, who are responsible for overall governance but are not involved in daily operational activities, internal audit provides a reliable and unbiased assessment of the bank's control environment, compliance status, and risk exposure. This allows the Board to exercise effective oversight and uphold their fiduciary responsibilities with greater confidence. In line with this, the IA communicates to the Board (or its ACB) without any intervention of the management.

Regulatory and supervisory authorities, such as Bangladesh Bank, face the immense challenge of overseeing billions of daily transactions across the banking industry, making continuous, in-depth monitoring practically impossible. In this context, internal audit serves as a frontline monitoring tool by regularly assessing internal controls, policy compliance, and risk mitigation measures. Audit findings from IA serve as a valuable source of information for regulators, helping them evaluate a bank's adherence to laws and prudential standards without the need for constant on-site supervision. Therefore, IA should have a direct communication channel to a contact point of the central bank. A standard communication channel of IA is depicted in Appendix 4, as suggested by BCBS.

Similarly, external auditors conduct reviews on a limited, sample basis and typically at the end of the period. Their capacity to examine every operational area in detail is constrained. Internal audit, by contrast, operates throughout the year and provides real-time or near-real-time insights into the bank's financial and operational systems. This continuous coverage ensures that external auditors receive a broader and deeper understanding of the bank's control framework and risk landscape, thereby enhancing the quality and reliability of external audits.

For senior management and the risk management unit, internal audit acts as a support system by identifying risks, inefficiencies, and control lapses that may not be visible through reports or dashboards alone. Since management lacks the resources for extensive on-site reviews, IA provides a direct channel for discovering operational weaknesses and policy deviations through field inspections and system audits. This helps management make informed, risk-aware decisions and strengthens the overall governance framework.

Operational staff and frontline employees are often constrained by limited resources, familiarity biases, or unawareness of internal lapses. They may overlook errors or procedural breaches, whether inadvertently or due to pressure. Internal audit mitigates these risks by offering an independent perspective, identifying issues at the execution level, and helping staff understand and comply with regulatory and institutional requirements. It fosters a culture of accountability, encourages procedural adherence, and supports performance improvement at the operational level.

In summary, Internal Audit functions as an indispensable oversight instrument—an objective and independent "third eye" for the Board, regulators, auditors, management, and operational staff. It fills critical gaps in monitoring, control, and risk evaluation, ensuring that the bank operates in a secure, compliant, and efficient manner across all levels. Appendix 5 presents a summary of the concept of IA as the third eye of different stakeholders.

3. Internal Control and Compliance: Regulatory Framework

3.1 Global Context for Internal Control System Structure

Internationally recognized organizations like the Organization for Economic Co-operation and Development (OECD), the Basel Committee on Banking Supervision (BCBS), the International Ethics Standards Board for Accountants (IESBA) of the International Federation of Accountants (IFAC), the Institute of Internal Auditors (IIA), Islamic Financial Services Board (IFSB), Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI), International Auditing & Assurance Standards Board (IAASB) and Committee of Sponsoring Organizations of the Treadway Commission (COSO) issue standards, guidelines, code of ethics & principles so that Banks may regulate & promote their banking practices following global standards. Bangladesh's banking sector may continue to take suggestions from a number of international standards, guidelines, and principles set by those reputable organizations.

The updated "G20/OECD Principles of Corporate Governance" (2023 Edition) continue a universal standard of excellence in corporate governance. The policymakers can appraise and improve the legal, supervisory, as well as official frameworks, which very much needed to promote economic efficiency, stable growth, and financial stability, and are as relevant in 2025 with gradually multifaceted regulations.

The Basel Committee has continued its performance with a fundamental role by reviewing its Corporate Governance Principles for Banks and reaffirming its Core Principles for Effective Banking Supervision (most recently updated in 2025), which continue to assist as a foundation for sensible regulation as well as all-encompassing banking supervision globally.

The International Federation of Accountants (IFAC) remains to apply its guidance through its International Code of Ethics for Professional Accountants (Including International Independence Standards) (2021 Edition), uttering ethical practice Ehiedu & Ogbeta, 2014and integrity in accounting and auditing professions. Likewise, the IIA with a view to promote higher internal auditing standards in the world revised its International Professional Practices Framework (IPPF) in 2024. The Standards direct the worldwide professional practice of internal auditing and assist as a basis for appraising and elevating the quality of the internal audit function.

The role of International Auditing & Assurance Standards Board (IAASB) vital to confirming that audit quality and audit practices throughout the world is enhanced. The IAASB issues and develops International Standards on Auditing (ISAs) as well as other standards of assurance and associated services to ensure the improvement of transparency, accountability, and confidence in financial reporting.
Both IFSB and AAOIFI continue in releasing governance standards for the betterment of Islamic finance, which impose robust internal control systems as well as compliance systems exclusive to Islamic financial institutions. In December 2023 IFSB 30- Revised Guiding Principles on Corporate Governance for Islamic Financial Services (IFIs) have been adopted with a view to strengthen the integrity and resilience of IFIs by enhancing the effectiveness and efficiency of the corporate governance framework

COSO continues to be very applicable. The latter's three frameworks — Internal Control - Integrated Framework (2013), Enterprise Risk Management: Integrating with Strategy and Performance (2017), and Fraud Risk Management Guide (updated in 2023) — give detailed instruction on executing governance processes, how to manage risk, and how to prevent fraud to the organizations.

Internal control, as a process, effected by an entity's board of directors, management, and other employees, designed to give reasonable assurance about the achievement of objectives with respect to operations, reporting, or compliance, is a definition provided by COSO. The five key components—risk assessment, control activities, information and communication, control environment, and monitoring activities—remain to support internal control frameworks worldwide.

Compliance functions in banking organizations continue to be a central element of a bank's second line of defense in risk management which ensures not only compliance with regulations but also respond in advance to new concerns like digital fraud, cybersecurity-related threats, as well as ESG (Environmental, Social, and Governance) compliance obligations, solidifying the integrity and resilience of a bank.

3.2 Local Context for the Internal Control System Framework

In Bangladesh, the internal control landscape within the banking sector is designed by a balance of regulatory directives, developing industry standards, and the rising complexity of financial operations. Banks strictly operate its operation under close supervision, start with their registration through the Registrar of Joint Stock Companies and Firms (RJSC). After registration, Banks operating activities are regulated by Bangladesh Bank (BB), which administers licensing, supervision, and ongoing compliance. Additionally, when banks intend to raise any kinds of funds like issuing shares or debt instruments from markets, the Bangladesh Securities and Exchange Commission (BSEC) steps in to ensure regulatory conformity, while the Financial Reporting Council (FRC) plays a vibrant role in upholding standards in financial reporting, accounting, and auditing.

The Bangladesh Bank (BB), recognizing this evolving landscape of banking sector, issued a comprehensive guideline on Internal Control and Compliance (ICC) in 2003, which underwent a major revision in 2016. ICC Guidelines 2016 is one of the basic regulations for establishing ICS in the banking industry of Bangladesh, which have accommodated principles issued by COSO. Besides, Bangladesh Bank issued Prudential Regulations for Banks 2024.

Bangladesh Bank's 3rd Strategic Plan 2020-2024 Fostering Stable Financial System: among different goals it emphasizes the importance of Strengthen regulatory and supervisory framework and activities to enhance overall financial sector stability and increase stakeholders' confidence with a view to introduce the anticipatory supervisory system in line with international standards which would consequently develop effective governance in risk management and control processes and strengthen the transparency and disclosures. In its plan BB also emphasized to develop a risk focused supervision framework for conducting risk-focused bank supervision with a view to capture and mitigate overall risk exposure of banks. It also prioritizes to Enhance financial system stability by identifying and measuring the vulnerabilities and resilience of financial institutions and system as a whole.

Bangladesh Bank issued "Bank Company External Auditor Rules 2024" (BRPD Circular Letter No. 31, Dated: July 09, 2024) wherein it is advised to Statutory Auditors to report a statement regarding the adequacy and effectiveness of internal control systems (ICS) of the Bank focusing the area of financial reporting, risk management and operational efficiency (BB, 2024). They will also verify the independency of ICCD from the management and if found any irregularities must be reported. Statutory auditors will look into the controls over governance and Board oversight, IT & operational activities, control structure of regulatory compliance, fraud prevention systems, authorization & documentation procedures, functioning of internal audit & reporting system.

To address broadly 02 (two) objectives namely Solving Existing Problems of the weak Banks & Strengthening the Financial Sector by improving activities of comparatively strong Banks, Bangladesh Bank issued Guidelines for Merger/Amalgamation of Banks/Financial Institutions in 2024. According to the Guidelines, any Banking company, with approval or mediation of Bangladesh Bank may merge/ amalgamate with any other Banking company with mutual agreement. If any Bank goes under Prompt Corrective Action (PCA) Framework which was issued in 2023 due to deficiency in the Capital, liquidity shortage, high level of NPL/ NPI, lack of Good Governance and activities those are harmful to the depositors, Directives of Bangladesh Bank (DOBB) must be followed as indicated in the framework for recovery of the Bank.

Finally, Bank Resolution Ordinance, 2025 has been issued wherein it indicates that resolution planning will be implemented to those systematically important banks fallen under PCA framework. The Act familiarizes a structured PCA mechanism that dictates prompt detection of financial or operational deterioration, Immediate actions such as business restrictions, asset quality review, and capital restoration plans. This reveals robust internal control implementation at regulatory and bank levels.

The Bank Companies Act, 1991 necessitates every bank to form an independent internal audit and control function. In line with Section 15C, internal auditors must report directly to the Board Audit Committee (BAC), certifying transparency and accountability within the governance structure.

Furthermore, Corporate Governance Code 2018, imposed by BSEC, compel listed companies to uphold effective internal controls. BSEC also preserves authority to initiate special audits concentrated specifically on control systems, highlighting corporate accountability.

Finally, the FRC continues to advance financial integrity across the banking sector by mandating adherence to IFRS. This alignment encourages consistency, comparability, and trust in the financial statements issued by Bangladeshi banks, thereby strengthening the sector's overall credibility.

4. Results and Discussion of ICCD Activities

4.1 Summary Outcome of FGD and Key Informant Interview (KII)

This section presents the key insights gathered from the Focus Group Discussion (FGD) and Key Informant Interview (KII) involving Heads of Internal Control and Compliance Departments (ICCD), Internal Audit professionals, and senior banking officials. The themes reflect both critical issues and progressive ideas concerning the current state and future direction of Internal Control and Compliance (ICC) in the banking sector.

Overall Governance Environment

Participants widely acknowledged that governance structures in many banks are severely deteriorated, with minimal visible improvement in recent times. Although certain reform initiatives are underway, tangible outcomes remain limited. Respondents emphasized that sustainability in governance cannot be achieved without embedding ethics and honesty across all tiers of the banking hierarchy.

They underscored the necessity of establishing a balanced distribution of "POWER" to prevent undue influence, both at institutional and state levels. A cultural shift towards integrity and accountability is deemed indispensable.

Effectiveness of Internal Audit (IA)

The effectiveness of internal audit is hampered by structural and resource limitations. In several banks, the Internal Control and Compliance Department does not receive adequate support from the Board of Directors (BoD) or Senior Management Team (SMT). Furthermore, a shortage of professionally qualified staff relative to the size and complexity of bank operations compromises audit quality. It was strongly recommended that IA personnel should possess relevant professional certifications and practical banking experience. Establishing a congenial relationship between auditors and auditees is necessary for ensuring cooperation and effectiveness. Additionally, the overall tone set by top leadership must prioritize audit independence and transparency for ICCD to function meaningfully. It is very unfortunate that some of the banks assigned business target to the employees of ICCD, which is conflicting with the international best practices and BB guidelines.

Review of ICC Guidelines 2016 and Branch Risk Rating System

There is a growing consensus that the ICC Guidelines 2016 issued by Bangladesh Bank need revision to align with the evolving risk landscape and operational dynamics of the banking sector. To prevent innovative irregularities in future, operational risk management system should be strengthening and a strong internal control system can be effective in this regard. In line with this, ICC Guidelines 2016 may require revision. In particular, the Branch Risk Rating System requires further clarification and standardization to ensure objective, consistent, and transparent application across institutions.

Assessment and Appraisal of ICS and ICCD

Participants advocated for a unified assessment framework under which all three core components of ICCD—on-site audit, off-site surveillance, and follow-up & reporting—would operate as an integrated function. The Head of ICCD should be authorized to oversee and appraise the collective performance of these units and submit consolidated evaluations to the Audit Committee of the Board (ACB). While ACB remains the ultimate supervisory body for ICCD activities, it may not be feasible for them to individually evaluate every ICCD staff member's performance. Besides, the Key Performance Indicators (KPIs) for the executives of

ICCD should be designed based on the job responsibility of the department, which is absent in some banks.

Implementation of Specialized Internal Audit Software

There is unanimous agreement that automation through specialized audit software is essential for enhancing efficiency and data integrity. However, banks remain reluctant to invest for this purpose. Besides, the concerns over the long-term viability of local software providers have been raised however, some other believe that it would not create a problem at all. Because, if a company is a legal corporate entity, it would be considered as a going concern. Finally, participants concluded that such technology adoption is inevitable and must be prioritized.

Concurrent Audit System

Concurrent audit is a real-time examination of banking transactions, conducted simultaneously with their execution to ensure immediate oversight, early detection of irregularities, and prompt corrective action. Despite its inclusion in the Internal Control and Compliance Guidelines (2016) issued by Bangladesh Bank, the adoption of concurrent audit systems across banks remains inconsistent and often informal. Many institutions demonstrate limited commitment to institutionalizing this practice, largely due to inadequate policy direction and perceived operational constraints. Feedback from the Focus Group Discussion (FGD) emphasized the urgent need for Bangladesh Bank to develop a dedicated Concurrent Audit TOR (terms of reference), clearly outlining the scope, objectives, operational structure, and reporting mechanism of such audits. Standardizing this practice across the industry is essential to enhance real-time surveillance, reduce vulnerabilities, and ensure a proactive internal audit culture within banks.

Preparation, Use and Publication of Health Report

Banks generally prepare the Health Report in compliance with the ICC Guidelines 2016. Traditionally, monitoring unit of the ICCD takes the pain for compiling the data from different sources for preparing the health report. However, there is limited evidence that this report is actively utilized by management for decision-making purposes. One contributing factor is the availability of data from multiple sources which diminish the report's practical value to the internal users. Additionally, there is significant variation in the timeline for its preparation—some banks take up to 12 months after the end of the accounting period, while others complete it by March of the following year. Due to the absence of a fixed submission deadline, Bangladesh Bank has neither penalized banks for delayed submission nor recognized those that comply early. This lack of enforcement and incentive weakens the report's relevance as a timely risk-monitoring and governance tool. It is opined that the health report may be a useful source of data for the external users and therefore, the concerned authority may think to make it available for the public.

Coordination between IA and Risk Management Division (RMD)

Internal Audit (IA) and the Risk Management Division (RMD) share common goals—identifying, assessing, and mitigating risks to ensure regulatory compliance and safeguard institutional integrity. While RMD designs and monitors risk frameworks as the second line of defense, IA provides independent assurance on their effectiveness, as the third line of defense. Despite operating independently, both units aim to enhance governance and prevent control failures. A formal communication structure between IA and RMD may be established to minimize risk coverage gaps, and ensure aligned priorities. FGD participants emphasized that structured collaboration—through shared reporting, joint reviews, or regular meetings—can significantly strengthen the bank's overall risk oversight.

Envisioning the Ideal ICCD

Participants shared their vision of an ideal ICCD structure. They stressed the need for a positive perception from BoD and SMT towards ICCD's role. ICCD should be staffed with experienced banking professionals, treated as strategic partners rather than compliance enforcers. A conducive and collaborative environment must be nurtured where no party is perceived as adversarial. Compliance with laws and regulations should be internalized as a value rather than a regulatory imposition.

To enhance industry-wide capabilities, it was proposed that a Knowledge Sharing Platform be established among ICCD and IA heads. Internally, banks could create dedicated knowledge sharing corners to disseminate good practices and case-based learning. Additionally, fair recruitment, zero-tolerance for unethical behavior, and a balanced reward-punishment system should be institutionalized to attract and retain qualified ICCD personnel. There were concerns that while non-compliance is punished, positive contributions are rarely acknowledged. Moreover, training and professional development must be regular and robust.

Finally, respondents highlighted the evolving role of IA as a watchdog—not just detecting irregularities but preventing malpractices. ICCD's focus should expand from corrective to preventive controls, and Program Policy Guidelines (PPGs) and

Standard Operating Procedures (SOPs) must incorporate forward-looking risk control measures. As per their opinion of the heads of ICCD and IA, placing the right people in the right place in the banking sector need to be ensured.

4.2 Summary of Findings of Questionnaire Survey

This section summarizes data collected through questionnaire and discussion with key stakeholders covering different dimension of ICS, especially ICCD, of the banking industry of Bangladesh.

Table 4.1: CAMELS and ICC Rating of Banks

Rating		No. of Banks in 2020		No. of Banks in 2022	
		CAMELS (Dec.)	**ICC (Dec.)**	**CAMELS (June)**	**ICC (June)**
1	Strong	0	0	-	-
2	Satisfactory	38	29	28	29
3	Fair	7	23	17	23
4	Marginal	11	5	8	6
5	Unsatisfactory	1	0	5	-
Total		**57**	**57**	**58**	**58**

Source: *Bangladesh Bank*

The CAMELS and ICC ratings are supervisory assessment tools used by Bangladesh Bank to evaluate banks. While the CAMELS rating, based on a five-point scale, reflects a bank's overall financial health, the ICC rating specifically assesses the quality and robustness of its internal control systems. Table 4.1 illustrates the CAMELS and ICC ratings for all banks. According to the data, no bank attained a "strong" rating in either assessment category. Besides, there are some banks at ‘Marginal’ and ‘Unsatisfactory’ category.

Table 4.2: The Head of ICCD and Portfolio (% of banks)

Aspects		2024	2022
Does the head of ICCD perform any operational duties for the banks or its affiliates?		25	12
Is there any requirement in bank’s policy for the ICCD head?	Academic/Professional Degree	10	03
	Years of banking experience	10	03
	Areas of working experience	10	03
Is there any tenure in the bank’s policy for the ICCD head?		0	04
Is there any instance of transferring ICCD head before the completion of 3 years tenure in last 5 years?		20	19

Source: *Survey data*

As of 2024, all banks have established an Internal Control and Compliance Department (ICCD) and appointed a designated head, as required by Bangladesh Bank guidelines. However, only 10 percent of banks have a policy outlining the required academic or professional qualifications and relevant experience for this role—a figure that, while improved from 3 percent in 2022, remains critically low. Notably, 25 percent of banks reported that the Head of ICCD is also involved in operational duties, more than double the 12 percent recorded in 2022, which raises serious concerns regarding role independence and conflict of interest. Furthermore, no banks in 2024 have a formal tenure policy for the ICCD head, and 20 percent reported premature transfers of the ICCD head within the past five years, slightly above the 19 percent noted in 2022 (Table 4.2). These 2024 findings underscore persistent structural and policy gaps that could undermine the stability and effectiveness of internal control leadership across the banking sector.

Table 4.3: Rank of the Head of the Committee/Department/Unit

S/N	Aspect	Position of the Head	% of Bank (2024)	% of Bank (2022)
1.	Rank of the Head of ICCD	1/2 steps immediate below CEO	50	46
		3 steps immediate below CEO	19	30
		4 steps immediate below CEO	25	15
		5 steps immediate below CEO	6	5
		More than 5 steps below CEO	0	4
2.	Rank of the Head of Internal Audit	Up to 3 steps immediate below CEO	47	12
		4 steps immediate below CEO	7	20
		5 steps immediate below CEO	20	28
		More than 5 steps below CEO	26	40
3.	Rank of the Head of Monitoring Unit	Up to 3 steps immediate below CEO	7	8
		4 steps immediate below CEO	13	13
		5 steps immediate below CEO	7	12
		6 steps immediate below CEO	40	35
		More than 6 steps below CEO	33	32
4.	Rank of the Head of Compliance Unit	Up to 3 steps immediate below CEO	6	28
		4 steps immediate below CEO	13	6
		5 steps immediate below CEO	25	12
		6 steps immediate below CEO	13	32
		More than 6 steps below CEO	43	22

Source: *Survey data*

As of 2024, only 50 percent of banks have appointed the Head of ICCD within two steps of the CEO, as recommended by Bangladesh Bank—slightly up from 46 percent in 2022, but still leaving 50 percent non-compliant. Similar concerns exist for internal audit, monitoring, and compliance units, where most heads are positioned well below senior management, undermining their authority and independence (Table 4.3). Notably, the compliance unit saw a sharp decline in rank, with 43 percent now placed more than six steps below the CEO.

Table 4.4: ICS and Preparation & Submission of Summary Audit Findings (%)

S/N	Aspect		2024	2022
1.	Total number of members of ACB		2-5	N/A
2.	Banks where Member(s) of ACB who is/are member of ECB (%)		0	
3.	Banks where Member(s) of ACB who is/are member of RMC (%)		75	
4.	Average number of times BoD meet with internal auditors in a year (NO.)		0-4	
5.	Average number of BoD meetings were held in the year for reviewing effectiveness of internal control process (No.)		0-1	
6.	Banks where ACB conduct review of the audit process (%)		94	
7.	Banks having approved system/policy for direct reporting by internal audit to the BOD/ACB (%)		88	
8.	Banks where BOD/ACB have mechanism for ensuring timely and effective correction by management as per audit report (%)		81	
9.	Banks where ACB has taken initiative for ensuring accuracy of financial reporting (%)		100	
10.	Banks having system of meticulously examining minutes and memos of BoD/ECB by ICCD/IA (%)		63	
11.	Banks where ACB has discussed with external auditors regarding accuracy of financial statement (%)		88	
12.	Banks where ACB has evaluated the performance of external auditors/ audit report and implementation thereto (%)		100	
13.	Banks where ACB has prepared compliance report on regularization of the omission, fraud & forgeries and other irregularities detected by external/internal auditors (%)		75	
14.	Average number of meetings of ACB held during the year (No.)		7	
15.	Banks think that ACB could ensure adequate number of skilled manpower and proper IT support for effective audit (%)		94	
16.	Banks with unresolved issue between senior management and IA which was referred to ACB (%)		6	
17.	Banks having SMT and MANCOM	Only MANCOM	12	12
		Only SMT	43	23
		Both MANCOM and SMT	44	65

Source: *Survey data*

The activities of ICS of a bank should be assessed regularly. As per Table 4.4, some bank's BoD has meet with IA some did not. ACB of some banks actively review the activities of the IA. It is found that a large number of banks have formed both MANCoM and SMT.

Table 4.5: Manpower composition of ICCD –categorized by banking experience (%)

S/N	Aspect	2024	2022
1	Employees of ICCD having more than 20 years of experience	23	26
2	Employees of ICCD having 15 to 20 years of experience	22	12
3	Employees of ICCD having 5 to less than 15 years of experience	36	48
4	Employees of ICCD having 1 to less than 5 years of experience	10	14
5	Employees of ICCD having less than 1 year of banking experience	6	0
		100	100

Source: *Survey data*

Table 4.6: Manpower composition of ICCD –Professional Qualification (%)

<table>
<tr><th>S/N</th><th>Aspect</th><th>2024</th><th>2022</th></tr>
<tr><td>1</td><td>No. of employees of ICCD having professional degree in Accounting</td><td>25</td><td rowspan="4">N/A</td></tr>
<tr><td>2</td><td>No. of employees of ICCD having business education degree (other than A)</td><td>54</td></tr>
<tr><td>3</td><td>Others (other than A and B)</td><td>22</td></tr>
<tr><td></td><td></td><td>100</td></tr>
</table>

Source: *Survey data*

Table 4.7: Executives of ICCD receiving training (%)

S/N	Aspect	2024	2022
1.	Executives not receiving any training	40	20
2.	Executives getting training once in a year	27	37
3.	Executives getting training twice in a year	13	19
4.	Executives getting training more than twice in a year	19	24
5.	ICCD having authority in arranging training program for its own employees (as % of total banks)	93	77

Source: *Survey data*

Table 4.5 and 4.6 present a summary of the manpower composition of ICCD. On and average, more than 20 percent of the employees of the unit have more than 20 years of banking experiences. It is also a good sign that about 25 percent of the employees have accounting or professional degree. Table 4.7 shows that more than 90 percent of the banks' ICCD heads are empowered to arrange training for their employees, which has been increased from 77 percent of the last review.

Table 4.8: Provision for mandatory leave in banks (% of banks)

S/N	Aspect	Option	2024	2022
1.	Banks having mandatory leave policy for the employees other than ICCD of the bank	No provision	6	8
		Once a year	94	92
		Once in two years	0	0
		Once in three years	0	0
2.	Banks having similar mandatory leave provision for the employees working in ICCD of bank		88	88
3.	Banks having separate provision for recreation leave		12	19
4.	Duration of the mandatory leave (in days)		10-15	10-15
5.	Financial benefit for mandatory leave	No benefit (% of banks)	75	50
		Benefit (basic salary)	1	1
6.	Banks opining mandatory leave provisions as equally important for executives working in any unit of the bank		100	88
7.	Employees enjoying mandatory/recreation leave fully who were eligible in the year (as perceived by ICCD)	More than 90%	40	23
		81%-90%	0	7
		71%-80%	0	3
		Below 71%	60	57

Source: *Survey data*

Table 4.9: Provision for job rotation in banks (% of banks)

S/N	Aspect		2024	2022
1.	Bank having job rotation policy for the employees other than ICCD of the bank		100	92
2.	Banks being similar job rotation policy for the employees working in ICCD of the bank		88	84
3.	Banks thinking job rotation provisions as equally important for executives working in any unit of the bank		94	85
4.	Banks able to implement the job rotation provision (as perceived by ICCD/IA)	More than 90%	100	11
		81%-90%	0	19
		71%-80%	0	24
		Below 71%	0	46

Source: *Survey data*

As per Bangladesh Bank regulations, all employees working in branches and head offices are required to take 10 to 15 consecutive days of mandatory leave annually. However, Table 4.8 reveals a notable deviation. In 2024, only around 40 percent of eligible employees were granted mandatory leave—though an improvement from 23 percent in 2022, it still indicates substantial non-compliance across the sector. Additionally, the regulation mandates that, except for the CEO, Deputy Managing Director, and employees recruited for special assignments, all bank staff should be transferred every three years. The data suggest that most banks have incorporated this policy and are implementing it accordingly, reflecting improved adherence to staff rotation requirements (Table 4.9). However, consistent and transparent enforcement remains essential to prevent internal control fatigue and reduce risks of collusion or complacency.

Table 4.10: Status of reviewing banking manual/guidelines (% of banks)

S/N	Name of Manual	Within the Last Three Years of 2024	Within the Last Three Years of 2022
1.	Credit Policy Manual	62	79
2.	Operational Manual	31	39
3.	Finance and Accounting Manual	13	46
4.	Treasury Manual	56	57
5.	HR Policy Manual	69	54
6.	ICC Manual	50	75
7.	ICT Security Policy	75	68
8.	FOREX Manual	38	54

Source: *Survey data*

Bangladesh Bank requires all banks to prepare comprehensive banking manuals or guidelines and review them at least once annually to ensure relevance and regulatory alignment. As shown in Table 4.10, the highest number of banks updated their ICT Security Policy manuals in the past three years, followed by the HR Policy manual. Only 50 percent banks have reviewed ICC manuals within last 3 years. A number of banks still fail to review or update these documents in a timely manner, indicating lapses in governance and procedural discipline. Regular and systematic updates are essential to align policies with evolving risks, regulatory changes, and operational realities.

Table 4.11: Perception of ICCD regarding its target (%)

S/N	Aspect	2024	2022
1.	Does ICCD have any target other than completing audit plan?	44	50
2.	Does ICCD think that minimizing irregularities/mistake should be a target of it?	80	85
3.	Satisfaction level of ICCD to keep the extent of irregularities within tolerance level in the bank	81	84
4.	Does ICCD think that minimizing fraud should be a target of it?	80	84
5.	Satisfaction level of ICCD to keep the extent of fraud committed within tolerance level in the bank	81	86
6.	Does ICCD think that minimizing lapses in documentation should be a target of it?	75	80
7.	Satisfaction level of ICCD to keep the extent of documentation lapses within tolerance level in the bank	51	83
8.	Does ICCD think that ensuring proper credit appraisal should be a target of it?	80	76
9.	Satisfaction level of ICCD with the credit appraisal process followed by the bank	81	88

S/N	Aspect	2024	2022
10.	Does ICCD think that ensuring proper credit approval should be a target of it?	69	76
11.	Satisfaction level of ICCD with the credit approval process followed by the bank	82	91
12.	Does ICCD have any role in minimizing NPL?	50	76
13.	Satisfaction level of ICCD with the NPL position of the bank	60	79
14.	Does ICCD think that ensuring proper posting of executives should be a target of it?	56	60
15.	Satisfaction level of ICCD with the placement approach followed by the bank	70	83
16.	Does ICCD think that minimizing customer complaints should be a target of it?	56	62
17.	Satisfaction level of ICCD with the magnitude of complaints raised by customers against the bank	70	92

Source: *Survey data*

While implementing the audit plan remains the primary objective of the Internal Control and Compliance Department (ICCD), its role should extend beyond mere execution. Other key performance targets—such as reducing the number of irregularities, improving branch risk ratings, minimizing fraud incidents, and regularizing documentation lapses—are critical indicators of an effective internal control system. Table 4.11 presents the perceptions of banks regarding these broader dimensions, highlighting the growing recognition that ICCD must contribute proactively to strengthening overall control and governance beyond routine audits

Table 4.12: Perception of ICCD regarding its independence (% of banks)

<table>
<tr><th>S/N</th><th colspan="2">Components</th><th>2024</th><th>2022</th></tr>
<tr><td>1.</td><td colspan="2">Do you think that ICCD should be independent from management?</td><td>88</td><td>96</td></tr>
<tr><td>2.</td><td colspan="2">Is ICCD fully independent for discharging its duties/responsibilities?</td><td>95</td><td>97</td></tr>
<tr><td>3.</td><td colspan="2">Do you think that activities of ICCD should be controlled and evaluated by CEO?</td><td>20</td><td>42</td></tr>
<tr><td>4.</td><td colspan="2">Is ICCD satisfied with support provided by the BoD?</td><td>60</td><td>98</td></tr>
<tr><td>5.</td><td colspan="2">Is ICCD satisfied with support provided by the ACB?</td><td>60</td><td>98</td></tr>
<tr><td>6.</td><td colspan="2">Is ICCD satisfied with support provided by the CEO/SMT?</td><td>60</td><td>97</td></tr>
<tr><td>7.</td><td colspan="2">Is ICCD satisfied with support provided by the BB?</td><td>93</td><td>97</td></tr>
<tr><td>8.</td><td colspan="2">Are all recommendations made by ICCD time bound for implementation?</td><td>73</td><td>96</td></tr>
<tr><td rowspan="3">9.</td><td rowspan="3">In how many cases ICCD can enforce the compliance with the recommendations made by ICCD?</td><td>(91-100)%</td><td>36</td><td>58</td></tr>
<tr><td>(81-90)%</td><td>43</td><td>34</td></tr>
<tr><td>(71-80)%</td><td>21</td><td>8</td></tr>
<tr><td>10.</td><td colspan="2">Is there any instance in your bank that any decision of ACB was not implemented by the bank management?</td><td>12</td><td>4</td></tr>
</table>

Source: *Survey data*

According to Table 4.12, 93 percent of banks indicated through the questionnaire survey that their ICCDs operate with full independence in discharging their duties. Additionally, a majority expressed satisfaction with the level of support received from the Board of Directors (BoD), Audit Committee of the Board (ACB), Chief Executive Officer (CEO), and Bangladesh Bank. However, insights from the Focus Group Discussion (FGD) painted a more critical picture. Most participants expressed concern that, in practice, ICCDs are not exercising their independence effectively, often facing limitations in enforcing recommended actions. In some cases, ratifications proposed by ICCD were not implemented, indicating a disconnect between perceived autonomy and operational reality. This gap highlights the need for stronger institutional backing and accountability to ensure ICCD functions as an independent and empowered governance unit.

Table 4.13: Achievement of objectives of internal control system

Achievement of objectives of internal control system of bank (% of banks)

% of Achievement	Operations Objective		Reporting Objective		Complian
	2024	2022	2024	2022	2024
Above 90%	56	60	69	80	56
81% - 90%	31	36	25	20	31
71% - 80%	13	0	6	0	6
Below 71%	0	4	0	0	6

Achievement of objectives of different units of ICCD (% of banks)

% of Achievement	Audit Unit		Monitoring Unit		Complia
	2024	2022	2024	2022	2024
Above 90%	69	80	63	60	69
81% - 90%	19	16	25	36	13
71% - 80%	13	1	13	4	13
Below 71%	0	0	0	0	6

Source: *Survey data*

The core objectives of an effective Internal Control System (ICS) include ensuring operational efficiency, accurate reporting, and regulatory compliance. As shown in Table 4.13, about 69 percent of banks reported that they have achieved their reporting objectives of above 90 percent. However, a significant number of banks continue to fall short in meeting the operations and compliance objectives, both in the current and previous years. Notably, the performance of the monitoring unit remains the weakest among the three ICCD units, lagging behind both audit and compliance functions. This calls for a critical reassessment of the monitoring unit’s structure, resources, and strategic focus to enhance its effectiveness in supporting overall ICS performance.

Table 4.14: Perception of the Head of ICCD Regarding Compliance with the Principles of Internal Control as Mentioned ICC Guideline 2016

[1=Fully Compliant; 2=Reasonably Compliant; 3=Partially Compliant; 4=Not Compliant; and 5=No Comment]

S/N	Components and Principles of Internal Control	Compliance Status				
		1	**2**	**3**	**4**	**5**
A	**Control Environment**					
1.	The bank demonstrates a commitment to integrity and ethical values.	63	25	6	0	6
2.	The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control.	56	31	6	0	6
3.	Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in pursuit of objectives.	69	19	6	0	6
4.	The bank demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.	31	56	6	0	6
5.	The bank holds individuals accountable for their internal control responsibilities in pursuit of objectives.	38	50	6	0	6
B	**Risk Assessment**					
6.	The bank specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.	44	38	6	6	6
7.	The bank identifies risks to the achievement of its objectives across the bank and analyzes risks as a basis for determining how the risks should be managed.	44	38	6	6	6
8.	The bank considers the potential for fraud in assessing risks to the achievement of objectives.	44	44	0	6	6
9.	The bank identifies and assesses changes that could significantly impact the system of internal control.	56	31	0	6	6
C	**Control Activities**					
10.	The bank selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.	25	63	6	0	6
11.	The bank selects and develops general control activities over technology to support the achievement of objectives.	25	63	6	0	6
12.	The bank deploys control activities through policies that establish what is expected and procedures that put policies into action.	44	44	6	0	6
D	**Information and Communication**					
13.	The bank obtains or generates and uses relevant, quality information to support the functioning of internal control.	31	56	6	0	6
14.	The bank internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.	38	44	13	0	6

S/N	Components and Principles of Internal Control	Compliance Status				
		1	2	3	4	5
15.	The bank communicates with external parties regarding matters affecting the functioning of internal control.	31	50	13	0	6
E	**Monitoring Activities**					
16.	The bank selects, develops, and performs on going and/or separate evaluations to ascertain whether the components of internal control are present and functioning.	25	56	13	0	6
17.	The bank evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the Board of Directors, as appropriate.	25	63	6	0	6

Source: *Survey data*

Bangladesh Bank, in its ICC Guidelines 2016, incorporated the 17 principles of internal control outlined by the COSO framework to promote sound governance and effective risk management. However, as reflected in Table 4.14, a significant number of banks remain partially or non-compliant with many of these core principles. This gap poses challenges to the integrity and reliability of internal control systems across the sector. The issue warrants immediate attention from both bank management and regulators to ensure full adherence to COSO principles, which are essential for achieving operational efficiency, accountability, and long-term financial stability.

Table 4.15: General information regarding audit unit of ICCD (% of banks)

Aspect	Option	2024	2022
1. Do you have separate Audit and Inspection unit?	Yes	100	100
2. Did you assign separate executive as head of the unit?	Yes	94	100
3. Satisfaction level about adequate number of manpower in this unit	(91-100)%	6	15
	(81-90)%	56	43
	(71-80)%	31	35
	Below 70%	6	7
4. Satisfaction level about the quality of manpower in this unit	(91-100)%	19	23
	(81-90)%	56	54
	(71-80)%	19	15
	Below 70%	6	8
5. As per your opinion, who should apprise the head of this unit?	Chairman of ACB	69	70
	CEO/MD	0	0
	Head of ICCD	31	30
6. Does audit unit feel comfort to report ACB directly without involvement of the Head of ICCD?	Yes	63	69
7. Average number of branches per audit team		21	N/A
8. Average number of manpower in each team		3	3
9. Is there any incentive for audit team members?	Yes	94	16
10. Range of daily allowance for the audit team member	Max. Tk.:	5500	8000
	Min. Tk.:	600	490

Aspect	Option	2024	2022
11. Satisfaction level about delegated authority to perform duties	(91-100)%	31	48
	(81-90)%	50	52
	(71-80)%	6	0
	Below 70%	13	0
12. Does audit team conduct surprise inspection based on findings of monitoring unit?	Yes	88	100
13. Does the audit team evaluate the service quality of the branch?	Yes	100	96
14. How many cases audit team has conducted an independent testing on the anti-money laundering and prevention of terrorist financing preparation of the branch?		94	100
15. How many cases audit team has received the self-assessment report on anti-money laundering and prevention of terrorist financing in due time from the branch? (within next 15 days after six-month period)		87	88
16. To what extent was it possible for audit unit to evaluate the self-assessment report thoroughly?		85	89
17. As per evaluation of audit unit, to what extent the self-assessment report		82	79
18. How many cases, audit team has conducted surprise/immediate audit/inspection if any ML/TF risk of a branch is identified through		62	26
19. Did audit team report the status of due and availed mandatory leave by the auditee?		63	87
20. Did audit team report the status of job rotation/transfer/posting of the branch employee?		68	91
21. How many cases, audit unit has conducted audit/inspection after the branch manager is transferred in the year?		40	72
22. Have lapses been categorized as given in BB guidelines on ICC in the year?	Yes, as per BB guidelines	62	67
	Own customized policy	38	33
	No categorization	0	0

Source: *Survey data*

Internal Audit (IA) serves as a critical component of the ICCD, responsible for conducting on-site supervision and ensuring operational integrity. As shown in Table 4.15, all banks have established dedicated audit and inspection units, each led by a designated head. However, a common concern across institutions is the need for more skilled and efficient manpower to enhance audit effectiveness. Most banks reported having an average of three members per audit team.

Table 4.16: Internal Audit Plan of Banks (% of banks)

S/N	Aspect of Audit Plan	Option	2024	2022
1.	Time of preparation of audit plan	In previous year	79	73
		In current year	21	27
2.	Risk-based audit plan	Yes	100	100
		No	0	0
3.	Format of branch audit rating	As given by BB	21	38
		Customized	79	62
4.	Implementation status of audit plan	(91-100)%	79	88
		(81-90)%	24	8
		(71-80)%	7	0
		Below 70%	0	4

Source: *Survey data*

Table 4.17: Format of the audit report (% of banks)

Aspect	2024	2022
1. Did you devise any prescribed format of audit report?	100	92
2. Is the format of audit report similar to the format given in BB Guidelines on ICC 2016?	56	57
3. Average time to prepare audit report after audit of a unit (days)	10	11

Source: *Survey data*

In line with Bangladesh Bank guidelines, all banks have adopted a Risk-Based Audit (RBA) approach for internal audit planning and execution. The overall implementation status of the audit plan was encouraging, although a few banks failed to complete their annual audit plans in both the current and previous years, as shown in Table 4.16. Regarding reporting practices, Table 4.17 indicates that all banks use a prescribed format for audit reports, ensuring consistency and regulatory compliance. Notably, more than 50 percent of banks have customized the BB-prescribed audit report format to align it with their institutional needs and operational contexts, reflecting an effort to enhance relevance and usability.

Table 4.18: Divisions/Departments of head office audited by IA (% of banks)

S/N	Name of Division	2024	2022
1.	Board Division	36	42
2.	Treasury	100	100
3.	Human Resource Division	71	73
4.	Risk Management Unit	64	73
5.	Credit Risk Management Division	93	84
6.	Finance and Accounting Division	93	76
7.	International Division	93	92
8.	ICT Division	93	92

Source: *Survey data*

Table 4.19: Identifying core risk management status of the audited branch (% of banks)

S/N	Core Risk Area	2024	2022
1.	Credit Risk Management	71	62
2.	Asset-Liability Risk Management	71	50
3.	Foreign Exchange Risk Management	64	62
4.	Internal Control and Compliance Risk	64	62
5.	Money Laundering Risk	71	69
6.	Information and Communication Risk	64	65

Source: *Survey data*

As shown in Table 4.18, the majority of banks conduct internal audits across most divisions of the head office, ensuring broader oversight of key operational areas. The Treasury Division remains the most consistently audited, with 100 percent of banks auditing this function in both 2024 and 2022, reflecting its high-risk and high-impact nature. In contrast, the Board Division continues to receive the least audit coverage, with only 36 percent of banks auditing it in 2024—down from 42 percent in 2022. This limited oversight may signal a need for greater focus on governance-related audits to ensure accountability at the highest level. Table 4.19 depicts that a significant number of banks' audits appraised the position of the core risks during an audit.

Table 4.20: Impact of internal audit (IA) on the performance of banks (%)

<table>
<tr><th>S/N</th><th colspan="2">Components</th><th>2024</th><th>2022</th></tr>
<tr><td>1.</td><td colspan="2">Do you think that there is a relationship between quality of IA and bank performance?</td><td>100</td><td>100</td></tr>
<tr><td>2.</td><td colspan="2">Do you think that a strong IA system may have some negative impact on bank performance?</td><td>13</td><td>19</td></tr>
<tr><td>3.</td><td colspan="2">Do you think that a strong IA system may have some positive impact on bank performance?</td><td>100</td><td>100</td></tr>
<tr><td>4.</td><td colspan="2">Do you think that it is possible to measure the impact of IA on the performance of bank</td><td>88</td><td>85</td></tr>
<tr><td rowspan="4">5.</td><td rowspan="4">Do you measure the impact of IA on bank-performance for a period separately?</td><td>(a) Not possible to measure record</td><td>0</td><td>15</td></tr>
<tr><td>(b) Possible but never measured</td><td>87</td><td>73</td></tr>
<tr><td>(c) Rarely measured</td><td>13</td><td>4</td></tr>
<tr><td>(d) Regularly</td><td>0</td><td>8</td></tr>
<tr><td>6.</td><td colspan="2">Do you think that it is possible to measure total cost required for conducting internal audit activities separately?</td><td>94</td><td>96</td></tr>
<tr><td rowspan="2">7.</td><td rowspan="2">Do you measure total cost incurred for conducting IA/overall ICCD activities for a period separately?</td><td>(a) Not possible to measure cost</td><td>0</td><td>0</td></tr>
<tr><td>(b) Possible but never measured</td><td>87</td><td>80</td></tr>
</table>

S/N	Components		2024	2022
		(c) Rarely measured	7	8
		(d) Regularly/Always	7	12
8.	Do you think that sanctioning credit/investment may be reduced if there is a very strong IA system in a bank?		53	35
9.	Do you think that it is possible to retain record of rejected credit/investment proposals?		94	92
10.	Do you retain the record of rejected credit/ investment proposal due to audit objection?	(a) Not possible to maintain record	8	12
		(b) Possible but never retained record	54	54
		(c) Rarely retained record	23	17
		(d) Regularly	15	17
11.	Do you think that customers may switch over from a bank having a strong IA to a bank with lenient IA?	(a) It may happen generally	13	4
		(b) It may happen for customers with bad intention only	75	77
		(c) It may be for insignificant no. of customers	0	11
		(d) It may not happen	12	8
12.	Do you think that a strong IA system may be an obstacle for providing prompt and better customer services to the valued client?		6	8

Source: *Survey data*

Although a direct causal relationship between Internal Audit (IA) and a bank's financial performance may be difficult to establish, IA is widely recognized as a key enabler of sustainable growth and risk-resilient operations. As shown in Table 4.20, all banks unanimously agree that a well-functioning internal audit system positively contributes to overall performance. Through its role in identifying control weaknesses, ensuring policy compliance, and promoting operational discipline, IA supports improved decision-making, enhances governance, and ultimately strengthens institutional stability and long-term performance.

Table 4.21: Concurrent audit (%)

S/N	Aspect		2024	2022
1.	Banks having concurrent audit system		23	32
2.	Nature of concurrent audit	Physical	75	75
		ICT	2	25
3.	If yes, how many branches have been covered under concurrent audit system in 2024?		5	N/A
4.	If yes, how many auditors were posted as concurrent auditors in a branch in 2024?		2	
5.	If yes, how many total auditors were posted as concurrent auditors in branches in 2024?		10	

S/N	Aspect		2024	2022
6.	If yes, was there any time-bound for assigning the concurrent auditors for a branch?		94	
7.	Nature of concurrent auditor	ICCD Employees	100	85
		Outsourced from other departments	0	15
		Outsourced from outside bank	0	0
8.	Reporting line of concurrent auditor	Head of ICCD	50	46
		Head of IA	50	50
		Others	0	4

Source: *Survey data*

Although the concept of concurrent audit is included in the Bangladesh Bank's ICC Guidelines 2016, its implementation across banks remains limited. As shown in Table 4.21, only 23 percent of banks established a concurrent audit system in 2024, a decline from 32 percent in 2022. Concurrent audit can be conducted through two approaches: physical presence at the audit site and ICT-based real-time monitoring. Till today, no bank has yet outsourced concurrent audit functions to external professionals. Broader adoption and formalization are needed to unlock its full benefits.

Table 4.22: Information System Audit

S/N	Aspect		2024	2022
1.	Banks having separate Information System audit under ICCD (% of banks)		94	96
2.	Nature of Information System auditor	ICCD Employees	100	92
		Outsourced from another department	0	4
		Outsourced from outside bank	0	0
		Conducted by another unit of bank	0	4
3.	Reporting line of Information System audit	Head of ICCD	50	54
		Head of IA (Audit)	50	46
4.	Average number of information system auditors in a bank		6	3

Source: *Survey data*

Table 4.23: ICT facilities for internal auditor

S/N	Aspect	Positive Response (%)	
		2024	2022
1.	Did you provide laptop for each audit team in 2024?	56	N/A
2.	Did you provide laptop for each member of audit team in 2024?	50	
3.	Did you provide internet facility for audit team in 2024?	94	

Source: *Survey data*

Table 4.24: IA Automation

S/N	Aspect	Positive Response (%)	
		2024	2022
1.	Did IA use any specialized separate software? (e.g., TeamMate+, ACL, IDEA, Tahqiq, etc.)	8	30
2.	Integration of the software with core banking software (those are using specialized software)	50	50
3.	Do you believe that audit automation will bring benefits for banks?	100	94
4.	Do you believe that audit automation will be feasible for the banking industry?	94	65

Source: *Survey data*

In the modern banking environment, operations are increasingly reliant on information systems (IS), which, while enhancing efficiency, also introduce potential vulnerabilities. Recognizing these risks, IS audits have gained importance among both regulatory bodies and bank management. As shown in Table 4.22, most banks conduct IS audits through ICCD personnel, alongside oversight by their ICT divisions. To support this function, a growing number of banks are equipping auditors with laptops for greater mobility and real-time access, as reflected in Table 4.23.

However, the adoption of specialized audit software remains limited, despite widespread acknowledgment of its value. Table 4.24 indicates that a significant number of banks believe automation would enhance audit quality and efficiency, underscoring the need for greater investment in technology-driven audit tools to strengthen internal control systems and reduce manual dependency.

Table 4.25: General information regarding monitoring unit of ICCD (% of banks)

S/N	Aspect		2024	2022
1.	Banks having separate Monitoring unit for off-site surveillance		100	100
2.	Banks having separate executive assigned as the head of the unit		94	92
3.	Satisfaction level about adequate number of manpower in the unit	a. (91-100)%	13	15
		b. (81-90)%	44	35
		c. (71-80)%	25	30
		d. Below 70%	19	20
4.	Satisfaction level about quality of manpower for effective off-site surveillance	a. (91-100)%	38	42
		b. (81-90)%	31	35
		c. (71-80)%	19	15
		d. Below 70%	13	8
5.	The head of Monitoring unit should be appraised by	a. Chairman of	6	8
		b. CEO/MD	0	12
		c. Head of ICCD	94	80

Source: *Survey data*

The Monitoring Unit functions as the watchtower of a bank's internal control system, providing continuous off-site oversight of operations. As per Table 4.25, all banks have established separate monitoring units under the ICCD, with over 90 percent assigning dedicated executives to lead the unit. This structural commitment reflects growing recognition of the unit's importance in identifying control lapses and ensuring compliance. Furthermore, majority of banks believe that the Head of the Monitoring Unit should be appraised by the Head of ICCD, reinforcing the need for integrated oversight and alignment within the internal control framework.

Table 4.26: Quarterly Operations Report (QOR) of the branch (% of banks)

S/N	Aspect	2024	2022
1.	How many cases banks have received a copy of Quarterly Operations Report (QOR) on time (10th day of next month) from each Branch/Centre?	80	91
2.	To what extent, it was possible for banks to evaluate the Quarterly Operations Report thoroughly?	84	92
3.	As per your evaluation, to what extent the Quarterly Operations Report show true picture?	80	84
4.	Did you prepare the Exception Report, if necessary	67	61

Source: *Survey data*

The Quarterly Operations Report (QOR) is a key tool within the Internal Control System (ICS), used to evaluate branch performance and detect control weaknesses. As shown in Table 4.26, while most banks receive QORs on time from their branches, a few continue to face delays in submission. The ICCD reviews these reports to assess the operational soundness of branches and identify areas requiring improvement. Notably, in approximately 80 percent of cases, banks consider the QORs to be accurate and reliable, reinforcing their value as an effective monitoring instrument though the different opinions were given during the FGD.

Table 4.27: Determinants of the Effectiveness of Monitoring Unit (%)

S/N	Aspect	2024	2022
1.	Is it possible to develop a Customized Dashboard for close and timely monitoring by the different layers of bank management?	100	96
2.	Do you have any online surveillance system covering all branches under monitoring unit?	50	38
3.	Do you think that an audit system should be supported by a strong monitoring unit?	100	100
4.	Do you think that an online surveillance system covering all branches is less costly and more effective than frequently physical audit of the branches?	88	65
5.	Do you have a software-based evaluation system for reviewing QOR, LDCL, and DCFCL?	25	4
6.	Do you think that an online surveillance system covering all branches under the monitoring unit may be complementary to the concurrent audit?	100	92

Source: *Survey data*

To strengthen the role of the monitoring unit as a true watchdog of internal control, most banks believe in the potential of developing a customized dashboard, as reflected in Table 4.27. There has been significant progress in implementing online surveillance systems, enabling real-time monitoring across all branches. Additionally, some banks are planning to introduce software-based evaluation tools for key internal control instruments such as QOR, LDCL, and DCFCL. A robust online surveillance framework is seen as a valuable complement to traditional audits, potentially reducing the frequency and time required for on-site inspections while improving the overall efficiency of internal control oversight.

Table 4.28: General information regarding compliance unit of ICCD (% of banks)

S/N	Aspect		2024	2022
1.	Banks having separate Compliance unit		100	100
2.	Banks having separate executives assigned as the head of the unit		100	96
3.	Satisfaction level about the adequate number of manpower in this unit	(91-100)%	19	27
		(81-90)%	44	43
		(71-80)%	25	15
		Below 70%	13	15
4.	Satisfaction level about quality of manpower for effective follow-up of compliance	(91-100)%	44	46
		(81-90)%	31	38
		(71-80)%	13	8
		Below 70%	13	8
5.	ICCD of bank reports the compliance status of new internal/external regulatory issue/circular		88	88
6.	Banks having online system for checking compliance with audit recommendations by concerned unit		38	65
7.	The head of Compliance unit should be appraised by	a. Chairman of ACB	19	8
		b. CEO/MD	0	11
		c. Head of ICCD	81	73

Source: *Survey data*

Table 4.29: Compilation and dissemination of directives and regulations (% of banks)

S/N	Aspect	2024	2022
1.	Banks maintaining all regulations and circulars in ICCD	75	73
2.	Banks distributing all regulations and circulars to related units by ICCD	63	84

Source: *Survey data*

The Compliance Unit within the ICCD plays a vital role in ensuring that audit observations—both internal and external—are properly followed up and resolved. After receiving audit findings, the unit communicates with the concerned auditees and compiles the status of compliance for reporting purposes. As shown in Table 4.28, all banks have established a separate compliance unit under the ICCD. However, many Heads of ICCD have expressed the need for more skilled manpower to strengthen the unit's effectiveness. Most banks also agree that the performance of the compliance unit should be evaluated by the Head of ICCD, ensuring accountability and alignment with overall control objectives.

In addition, Table 4.29 reveals that a good number of banks maintain organized repositories of all relevant regulations and circulars within the ICCD. The department is also responsible for disseminating these regulatory updates to the respective departments and branches, further reinforcing the compliance culture across the institution.

5. Issues and Recommendations

5.1 Supervisory Rating and Internal Control Quality

Despite increased regulatory focus, no bank attained a "strong" status under either CAMELS or ICC ratings. Several institutions remain in marginal or unsatisfactory categories, highlighting persistent systemic weaknesses in financial health and internal control mechanisms. This stagnation suggests a gap between regulatory expectations and institutional commitment to control culture and performance improvement.

A root-cause analysis should be conducted for banks in lower-rated categories to identify recurring governance failures and compliance gaps. Bangladesh Bank (BB) should consider introducing a targeted remediation plan with enforceable milestones and periodic evaluations.

5.2 Policy Framework for ICCD Leadership

In 2024, only 10 percent of banks reported policy requirements for academic or professional qualifications for ICCD heads—though an improvement from 3 percent in 2022, it remains critically insufficient. Moreover, 25 percent of ICCD heads were involved in operational duties, risking independence, and conflict of interest.

BB should mandate a unified policy for appointing ICCD heads, stipulating qualifications, relevant banking experience, and role separation. The guideline should also restrict premature transfers without Board Audit Committee approval.

5.3 ICC Guidelines 2016 and Risk Rating Model

Stakeholders observed that the 2016 ICC Guidelines are outdated given the evolving banking risks, especially related to operational innovations and technology. The current Branch Risk Rating System lacks clarity and objectivity.
Bangladesh Bank may take initiatives to revise the ICC Guidelines with inputs from practitioners. The Branch Risk Rating model must be standardized, automated where possible, and subjected to regular review to ensure transparency and consistency.

5.4 Automation in Internal Audit

Most banks continue to rely on manual internal audit processes. A very few banks are now using specialized IA software. However, most of the banks accept that automation in IA will bring some benefits in the ICS. Besides, no institution reported using software-based evaluations for key ICS tools (DCFCL, QOR, LDCL), limiting effectiveness and real-time risk detection.

Banks should be required to adopt IA-specific software platforms. BB can offer incentives, pilot programs, or partnerships with local IT firms to ensure affordability and long-term support.

5.5 Good Governance and Ethical Culture

The overall governance environment was widely described as deteriorated. There is a deficiency in ethical commitment at both state and institutional levels, with excessive influence by powerful individuals and weak accountability mechanisms. A "Tone at the Top" campaign must be launched industry-wide. Governance codes should enforce disclosure of conflicts of interest, ensure whistleblower protections, and promote ethical decision-making from BoD to frontline operations.

5.6 Fragmented Oversight Structure of ICCD Units

Current structure often separates monitoring, internal audit, and compliance, weakening synergy. In this regard, BIBM has proposed a structure combining on-site audit, off-site surveillance, and follow-up and reporting units under a single umbrella. As a number of responsibilities are assigned to the ACB, Bangladesh Bank may allow to have a separate secretary for the committee to assist on regular basis. In the current structure, it is quite difficult for the Chairman of ACB to properly assess the performance of the IA.

Banks should adopt an integrated ICCD model where all three core units operate under a unified head who reports directly to ACB. Concerned authority may consider the BIBM proposal in this context. A consolidated performance dashboard should be designed for effective monitoring and ensuring transparency.

5.7 Concurrent Audit System in Banks

While concurrent audit is outlined in existing guidelines, its application is inconsistent. Many banks are reluctant to invest in setting up this critical real-time oversight mechanism.

BB must include a Concurrent Audit Charter in its revised guidelines and make its implementation compulsory for high-risk branches and activities. Performance of concurrent audit should be part of the supervisory rating.

5.8 Coordination Between IA and RMD

IA and Risk Management Division (RMD) function independently despite shared goals. Absence of a formal communication framework often leads to inefficiencies and risk blind spots.

Banks should institutionalize structured collaboration—via regular joint meetings, shared dashboards, and integrated risk reviews—to enhance overall oversight effectiveness.

5.9 Role of ICCD in Strategy and Prevention

ICCD is often seen merely as a compliance unit. Most banks still follow a reactive approach, focusing on correcting violations instead of preventing them. Additionally, ICCD contributions remain underappreciated.

ICCD should shift toward a preventive model by embedding risk awareness into policy and process design. A formal reward-recognition mechanism must be introduced for ICCD staff based on quality and impact of work.

5.10 Capacity Constraints in ICCD and Internal Audit

The shortage of professionally qualified staff and inadequate training are recurring issues. With expanding operations and regulatory complexity, most ICCDs remain under-resourced.

Banks should develop a structured HR policy for ICCD recruitment, linked to risk profile and branch network. BB may collaborate with BIBM to deliver certification-based training programs tailored to ICCD needs.

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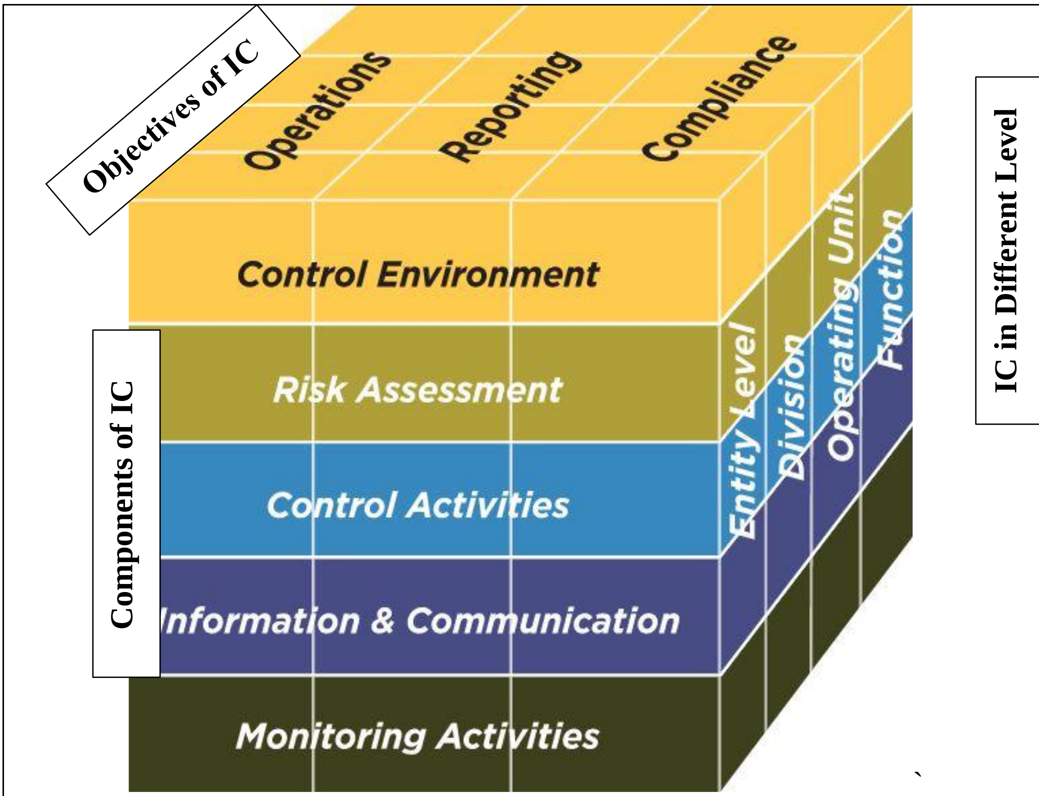
Appendix 1: Relationship of Objectives and Components of IC

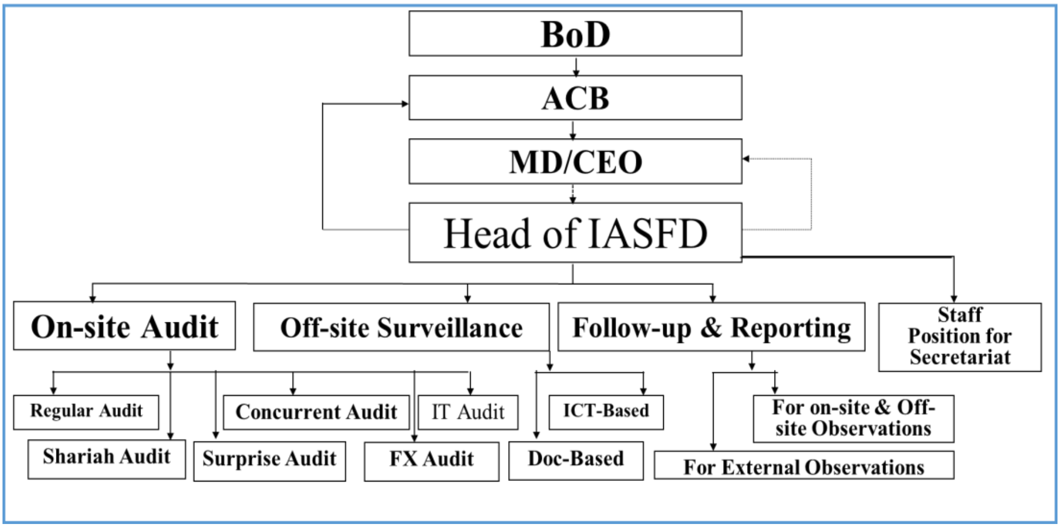


Source: *COSO (2013)*

Appendix 2: Enterprise Risk Management—Helix Framework

Source: *COSO (2017)*

Appendix 3: Suggested Organizational Chart for ICCD/IASFD



Source: *Siddique et al. (2018)*

Notes:

i) Board of Directors (BoD): The BoD holds the highest authority in crafting standard operating procedures (SOPs) and overseeing the comprehensive operations of the banks.

ii) Audit Committee of the Board (ACB): As a board committee, the ACB plays a pivotal role in the evaluation of the banks' overall Internal Control System (ICS) and the activities of the Internal Audit Surveillance and Follow-up Department (IASFD).

iii) Chief Executive Officer (CEO): The CEO assumes responsibility for executing all observations and recommendations put forth by the IASFD via the ACB. While the CEO may offer suggestions to the IASFD to conduct audits (dotted line reporting), they must not compromise its independence.

iv) Head of Internal Audit Surveillance and Follow-up Department (IASFD): The head of IASFD holds a supervisory role over all the department's activities and communicates relevant information to both the ACB and CEO in a parallel structure (dotted line reporting).

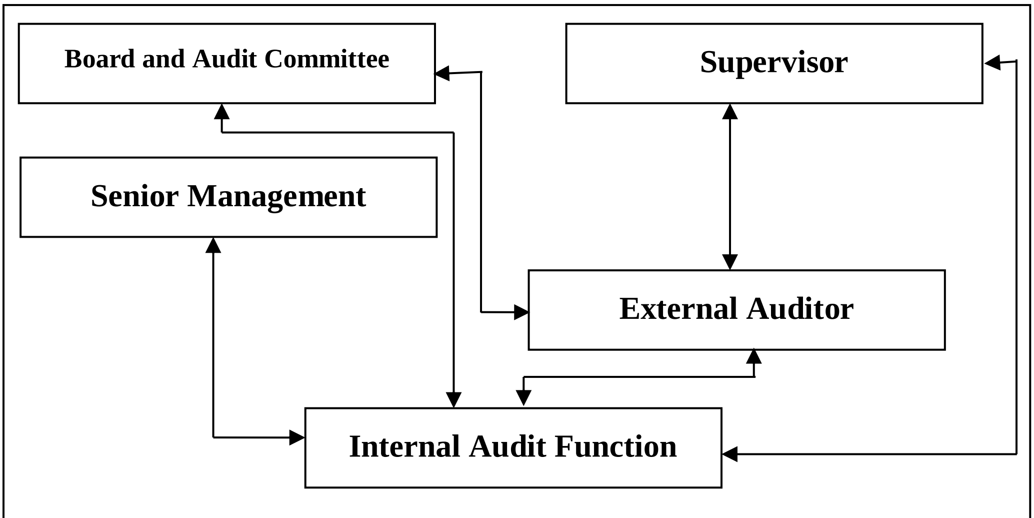
v) On-Site Audit Unit: The on-site audit unit carries out routine audits according to the established audit plan. Moreover, it conducts surprise audits, IT audits, FX audits, and Shariah audits. A team of concurrent auditors, under the on-site audit unit, is responsible for auditing high-value branches, including the top 20 branches.

vi) Off-Site Surveillance Unit: The off-site surveillance unit consists of two sub-sections. One focuses on surveillance using ICT infrastructure, while the other examines collected documents and reports for monitoring purposes.

vii) Follow-up and Reporting Unit: Within the IASFD, this unit serves as the central point for tracking the status of rectifying internal and external audit observations. It consolidates all observations and recommendations from on-site audit, off-site surveillance, external audits, regulators, and monitors the progress of their implementation. At specific intervals, this unit communicates compliance status to the ACB, Senior Management Team (SMT), and regulatory bodies.

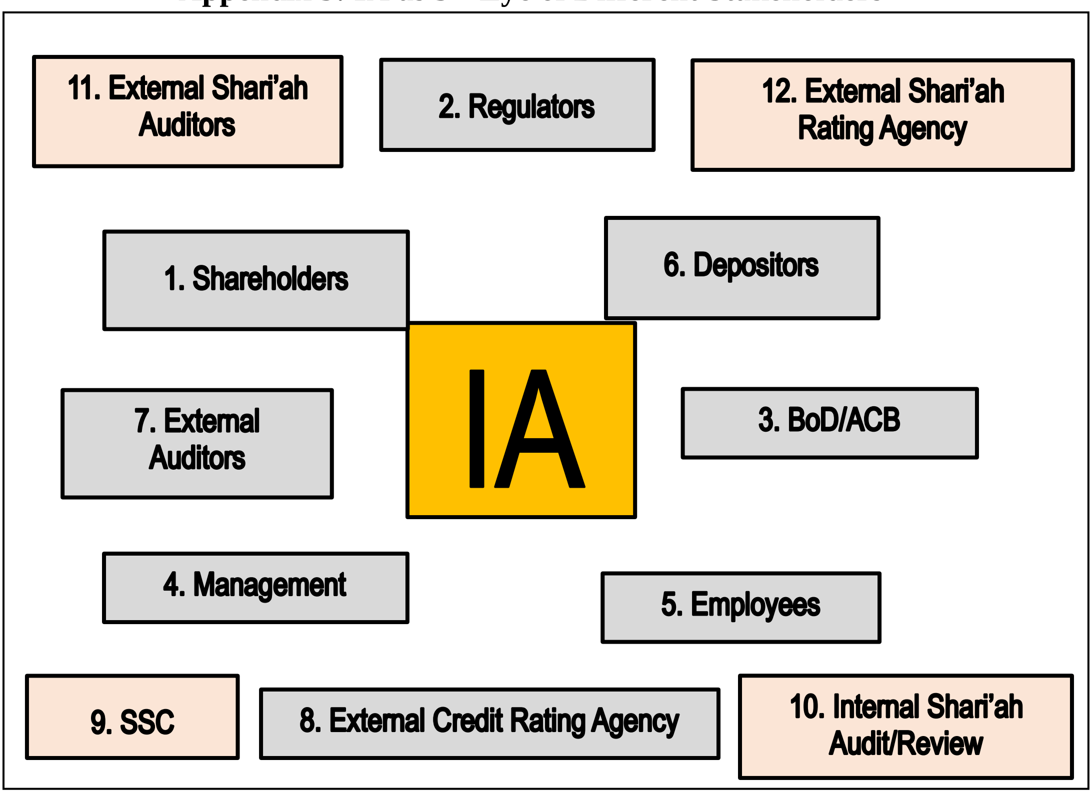
viii) SMT, Off-Site Surveillance Unit, and Follow-up & Reporting Unit: These entities have the authority to recommend to the on-site audit unit, through the head of IASFD, the necessity of conducting special audits as circumstances warrant.

Appendix 4: Internal Audit Function's Communication



Source: *BIS (2012)*

Appendix 5: IA as 3rd Eye of Different Stakeholders



Source: *Authors' Compilation*

Appendix 6: Observations and Issues Raised in Previous ICC Review Papers of BIBM

S/n	Recommendations
1.	Banks should automate internal audit functions using specialized audit software to improve efficiency and oversight.
2.	Off-site surveillance should be strengthened through ICT tools, including customized monitoring dashboards.
3.	A formal performance appraisal system should be established for ICCD activities to ensure accountability and improvement.
4.	Banks must adopt detailed manpower planning for ICCD to address skill gaps and operational needs.
5.	The ICC Health Report should be actively used by management for informed decision-making.
6.	The Board and Senior Management must demonstrate ethical leadership to ensure an effective internal control environment.
7.	Supervisory ratings under CAMELS and ICC should be improved through focused institutional reforms.
8.	Higher-ranked executives (not more than two steps below the CEO) should be appointed as Head of ICCD in line with regulations.
9.	Banks should maintain a database to track the cost and impact of internal audit and ICCD functions.
10.	Customization of internal policies should be encouraged, provided it aligns with the spirit of BB regulations.
11.	Observations from external auditors should be taken seriously to strengthen internal control and audit systems.
12.	Audit, monitoring, and compliance units under ICCD should be integrated for coordinated functioning.
13.	Bangladesh Bank should revise and clarify the ICC Guidelines to enhance regulatory clarity and relevance.
14.	The tone at the top must reflect integrity and independence to establish a strong corporate governance culture.
15.	Punitive actions should be ensured against wrongdoers, and credit discipline must apply equally across all loan types.
16.	ICS tools such as DCFCL, QOR, and LDC should be used effectively and automated where possible.
17.	Regulatory consistency should be maintained, as frequent changes may undermine the credibility of regulations.
18.	Ensuring good corporate governance is not an option rather should be mandatory for the sustainability of the banking industry.

It is noteworthy that most banks have expressed agreement with the proposed recommendations aimed at strengthening the Internal Control System (ICS) within the banking industry of Bangladesh. This collective endorsement reflects a growing recognition of the need for structural reforms, capacity enhancement, and technology-driven oversight to ensure effective governance and long-term stability.

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