

Pursuant to Article 39 paragraph 2 item i) of the Croatian National Bank Act (official gazette *Narodne novine*, No. 36/2001) and Article 114 paragraph 2 of the Banking Act (official gazette *Narodne novine*, No. 84/2002) the Governor of the Croatian National Bank hereby enacts the following

**DECISION
ON THE AUDIT OF FINANCIAL REPORTS AND BUSINESS FUNCTIONS OF
BANKS**

I GENERAL PROVISIONS

(1) This Decision shall govern the form, minimum scope and content of the audit of business operations and annual financial reports of a bank, a banking group and the entire group provided that the group members are, besides banks, non-financial institutions (hereinafter: financial reports).

(2) In terms of item (1) of this Decision, an audit shall comprise:

1) the audit of general financial reports prepared by a bank pursuant to the Accounting Act and International Accounting Standards, which are intended for external users including the Croatian National Bank (hereinafter: general financial reports);

2) checking of the regularity, accuracy and completeness of special financial reports prepared by banks on the basis of the Croatian National Bank's subordinate legislation (hereinafter: special financial reports); and

3) assessment of the organisation and efficiency of business functions and of the quality of a bank's by-laws and their implementation (hereinafter: other information), primarily the assessment of their compliance with the rules on risk management, internal audit functioning and the bank's information system.

II REPORTING REQUIREMENTS AND EXCHANGE OF INFORMATION

Bank

(3) A bank shall be obliged, not later than 31 July each year, to notify the Croatian National Bank in writing of the audit firm selected to carry out the audit for the current year.

(4) A bank shall be obliged to submit to the Croatian National Bank the bank's audited financial reports referred to in Chapter I, item (2) under 1), 2) and 3) of this Decision within 15 days following the date of publishing the reports, but not later than four months

following the expiry of the business year for which the reports are prepared. The reports must be signed by a certified auditor (natural person) responsible for the bank's audit.

Certified Auditor

(5) An audit firm and the persons connected with it in terms of Article 12 of the Banking Act shall be considered as one person (hereinafter: audit firm.).

(6) An audit firm entrusted with conducting an audit may not conduct an audit of a bank's financial reports and provide consulting services to that bank in the same business year. In terms of this Decision, consulting services shall include, besides the classic consulting services, carrying out of all other types of audit (merger audit, internal audit, etc.).

(7) The audit firm shall be obliged to submit to the Croatian National Bank by 30 September of the current year the audit plan for that year indicating the areas to be audited and the estimated duration of the audit for each bank which has entrusted it with conducting an audit.

(8) Where necessary, the certified auditor may request that a meeting be held with the Croatian National Bank prior to the beginning of or during the audit.

(9) In order to fulfil the obligation referred to in Article 112, paragraph 4 of the Banking Act, the audit firm shall be obliged to submit to the bank whose operations it audits the data on that firm's total income earned in the previous year and on the income earned from having conducted the audit of that bank in the previous year.

Croatian National Bank

(10) After submitting the plan for conducting the audit and/or during the audit, a meeting may be held with the audit firm or, if necessary, with the audit firm and the bank, as requested by the Croatian National Bank.

(11) While assessing whether the audit has been conducted and/or the audit report compiled in accordance with Article 114, paragraphs 1 and 2 of the Banking Act, and based on real and objective facts the Croatian National Bank may request additional explanations from the certified auditor.

(12) If the Croatian National Bank establishes that the certified auditor's opinion on or the assessment of the financial reports referred to in Chapter I, item (2) of this Decision is not based on real and objective facts, the Croatian National Bank may (by virtue of Article 114, paragraph 4 of the Banking Act) reject the reports and request the bank to select another certified auditor to conduct the audit, assess the financial reports and compile a new audit report.

(13) It shall be deemed that the financial reports are not based on real and objective facts if the Croatian National Bank establishes deviations which can lead the users of the financial reports to wrong business decisions, particularly if the deviation

- between the audited income statement and the balance established by the Croatian National Bank is five percent or more; or
- between the audited balance sheet and the balance established by the Croatian National Bank is two percent or more.

(14) Based on the actual circumstances in each individual case, the Croatian National Bank shall adopt a decision on rejecting the financial report or pass another enactment to set a time limit for the submission of new financial reports.

III GENERAL FINANCIAL REPORTS

(15) In terms of Chapter I, item (2) under 1) of this Decision, general financial reports shall comprise:

1. income statement
2. balance sheet
3. statement of changes in equity
4. cash flow statement
5. notes to the financial reports.

(16) The audit of the general financial reports referred to in item (15) of this Decision shall be carried out in accordance with the Audit Act, International Accounting Standards and the Code of Professional Ethics for Auditors.

(17) The audit of the general financial reports shall comprise the examination of the data and methods of their compilation, on the basis of which auditors give their expert opinion on fair presentation of assets, liabilities, capital, cash flow and business results shown in the bank's general financial reports.

(18) In planning and conducting the audit of the general financial reports, a certified auditor decides, independently and in accordance with the professional standards, on the scope of the inspection of individual documents and examination of individual business events as the basis for giving a reliable audit opinion on fair presentation of audited general financial reports.

(19) After completing the audit, a certified auditor compiles an audit report in accordance with the provisions of the law and standards and submits it through the bank's management board to the shareholders, i.e. the bank's general assembly.

IV SPECIAL FINANCIAL REPORTS

(20) In terms of Chapter I, item (2) under 2) of this Decision, special financial reports of a bank shall include the income statement, balance sheet and off-balance items in the

form prescribed by the decisions in force on statistical reports, as well as capital adequacy reports and the following supervisory reports:

- 1) Report on Exposure by Activity
- 2) Report on Credit Exposure by Risk Categories
- 3) Report on Large Exposure
- 4) Report on Exposure to Persons in a Special Relationship with the Bank
- 5) Report on Investments in Companies' Capital
- 6) Report on Investments in Property and Equipment
- 7) Report on Changes in Placements Value Adjustment.

(21) Consolidated special financial reports of a banking group shall comprise the income statement, balance sheet and off-balance sheet items in the form prescribed by the decisions in force on statistical reports, as well as capital adequacy reports and the following supervisory reports:

- 1) Report on Credit Exposure by Risk Categories
- 2) Report on Large Exposure
- 3) Report on Exposure to Persons in a Special Relationship with the Bank
- 4) Report on Investments in Companies' Capital
- 5) Report on Investments in Property and Equipment.

(22) For the purpose of submitting reports to the Croatian National Bank, a certified auditor shall be obliged to examine and certify the following documents as parts of the special financial reports referred to in items (20) and (21) of this Decision:

- 1) supplement comprising the information on the consolidation of a banking group in accordance with the International Accounting Standards;
- 2) specification of the elimination items (items mutually offset in consolidation) and consolidation differences.

(23) During the audit, a certified auditor shall check the regularity, accuracy and completeness of special financial reports by assessing whether these reports have been compiled in accordance with the decisions and instructions of the Croatian National Bank and the policies and rules established by the bank concerned, and whether the items in these reports have been adjusted with the comparable items in the general financial reports. The auditor's assessment shall be given in the form of a statement that the reports have been compiled in accordance with the Croatian National Bank's subordinate legislation, that they have been reconciled with the general financial reports and that they reflect the current state in a true and fair manner.

(24) Should the certified auditors not be able to make the assessment in terms of item (23) of this Decision on the basis of the carried out examination of the special financial reports, they shall be obliged to give their opinion on the irregularities or illegalities established in each particular report, which they have not assessed positively.

(25) Special financial reports shall also be signed (individually or in the form of a specification) by the bank management board.

V OTHER INFORMATION

(26) Other information referred to in Chapter I, item (2) under 3) of this Decision shall relate to the assessment of the organisation of a bank's business functions, where the certified auditor shall assess:

- 1) the method of identifying all significant risks to which a bank is exposed in the course of its business operations (e.g. credit risk, market risk, operational risk, etc.) and the efficiency in managing these risks;
- 2) the adequacy of organisation and the manner and quality of the internal audit functions.

The certified auditor shall assess whether the internal audit functions in the manner prescribed by law and the by-laws, whether internal auditors are independent and whether they perform their business operations in accordance with the professional standards.

In addition, the certified auditor shall assess whether the internal audit examines the regularity of a bank's business operations and the appropriateness and efficiency of its internal control system for the purpose of ensuring a safe and prudent bank management;

- 3) the organisation and management of the information system and the related technologies, the adequacy and reliability of the information system and its adjustment to the bank's business goals, physical protection of the system and data protection, as well as the established internal and external control system.

(27) Certified auditors shall also assess the by-laws regulating a bank's business functions referred to in item (26) of this Act, quality of a bank's by-laws, their harmonisation with the law and subordinate legislation, as well as with the accounting and other standards. They shall also examine whether the bank complies with these regulations and standards in its business operations.

(28) In the case of a superordinate bank in a banking group, the certified auditor shall assess the organisational aspect of the business functions at the banking group level.

(29) Based on the assessments referred to in items (26) and (27) of this Decision the certified auditor shall give a written opinion on the quality of the by-laws and their implementation, as well as on the adequacy of the business functions organisation of a bank or a banking group, and shall submit the opinion directly to the Croatian National Bank.

(30) Should the certified auditor not be able to give a positive opinion in terms of item (29) of this Decision on the basis of the carried out examination, or in the case of any assessment, which results in identification of serious deficiencies pointing to a behaviour contrary to the safe and sound banking operations, the certified auditors shall provide a specification of the established irregularities and illegalities and their comments thereon.

VI FINAL PROVISIONS

(31) This Decision shall enter into force on the day of its publication in the official gazette *Narodne novine* and shall be first applied to the financial reports for 2003.

(32) As of the date of application of this Decision, the Decision on the Form, Minimum Scope and Content of an Audit and the Reports on Audits of Banks (official gazette *Narodne novine*, No. 64/1999) shall cease to be valid.

Dec. No.: 19-020/01-03/ŽR

Zagreb, 21 January 2003

CROATIAN NATIONAL BANK
GOVERNOR

Željko Rohatinski, Ph.D.