

# Audit Committee's Assessment

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## Of the Operations of Internal Control, Internal Audit and Risk Management Systems

The Audit Committee has convened eight times during 2020.

Within the scope of its activities throughout the year, the Audit Committee monitored the effectiveness and adequacy of internal systems, the operation of accounting and reporting systems in line with the applicable regulations, the integrity of the resulting information, and the internal audit plans.

The Committee continued to verify whether the internal audit system encompassed the Bank's current and planned operations and resulting risks.

Furthermore, the Committee also continued to fulfill its functions of overseeing the activities of the external audit company, appraisal firms and support service providers that are designated by the Board of Directors, as well as evaluating the relevant external audit results. The Audit Committee informed the Board of Directors on the activities of the Committee, its assessments about the external audit firms, appraisal firms and support services providers, and other matters.

The Internal Audit Department conducted risk-based process audits on the basis of 11 different risk types covering the Bank's head office units, domestic branches, overseas branches and subsidiaries. The Committee performed monitoring activities for quickly remedying the findings resulting from the audits and thus, mitigated the Bank's risk exposure.

The Agile Methodology began to be employed in audits conducted by the Internal Audit Department with the target of more efficient use of the workforce and generation of high added-value results. Following the introduction of this method,

the further increased effectiveness of the audit proved to be a major factor in the upgraded Corporate Governance rating of the Bank.

In order to mitigate the growing technological and cybersecurity risks and by focusing on audit processes with a data-based approach in line with the Bank's digital transformation target, the Internal Audit Department used techniques based on data modeling algorithms, image processing and machine learning in its activities.

Follow-up of suggestions resulting from the audit engagements by the Bank's senior management, the Audit Committee and the Board of Directors ensured that corrective actions were taken according to the timeline by the auditees.

Within the scope of the inspections and investigations among the activities of the Internal Audit Department, fraud and counterfeiting activities were prevented or detected, and it has been ensured that necessary managerial actions were taken promptly. Remote and on-site studies were carried out to determine internal fraud incidents. A new project was introduced within the scope of remote (centralized) studies carried out to identify transactions with the highest risk through various predetermined risk factors and early warning signals by making use of "big data" capabilities and to ensure examination on a daily basis. These methods minimized the losses resulting from internal fraud.

The Internal Control Unit continued to challenge all control activities that are performed by business and support units. In this regard, the Unit conducted second level control activities

at branches and head office departments. During on-site branch visits, the Internal Control Unit carried out examinations regarding operational risks. As part of its responsibilities, the Unit also oversaw that the internal control environments of the Bank's financial subsidiaries are adequately outfitted in terms of structure and functionality.

Reporting flows have been implemented and periodic follow-up continued for remedying the findings determined during the controls.

The Compliance Department continued to manage the Bank's potential compliance risks and kept working to identify and prevent these risks before implementation. The Department kept overseeing and coordinating the compliance of the Bank's ongoing and future activities, new transactions and products with the Banking Law, applicable legislation, internal policies and guidelines, and banking practices. With the aim of reinforcing the Bank's consolidated compliance policy, the Department supervised the compliance activities of overseas branches and consolidated subsidiaries, taking steps towards promoting compliance awareness and culture.

As part of corporate compliance activities, Garanti BBVA Conflicts of Interest Policy was created and introduced in line with the BBVA Group Conflicts of Interest Policy. Bank-wide training activities were carried out in relation to Anti-Corruption and Code of Conduct. Notifications received by Garanti BBVA Whistleblowing Channel were evaluated, upon which results were presented to the Integrity Committee. Within the scope of securities compliance function related to investment transactions, examinations were carried out within the frame of the CMB's Communiqué on Obligation of Notification Regarding Insider Trading or Manipulation Crimes regarding own-account trading and use of privileged information by the Bank employees who may have insider information or periodic information about capital market instruments or issuers. As part of Customer Compliance activities, changes in the regulatory framework were watched closely during the course of the year, ensuring the alignment of the Bank's processes therewith. In

addition, new business, products and processes were evaluated prior to implementation.

As part of anti-money laundering (AML) and countering financing of terrorism strategy (CFT) strategy, studies were carried out in order to achieve alignment with national and international regulations. Through the existing monitoring programs and other initiatives by the Compliance Officer Team, risk management, monitoring and control activities were carried out efficiently. Classroom training sessions, regional office visits and web-based AML and CFT training programs offered throughout the Bank served to secure higher awareness and consciousness of the matter among the employees.

As part of Risk Management activities, Capital and Operational Risk Department monitored the regulatory framework regarding risk management and provided the necessary internal information flow. In accordance with the regulations published by the BRSA, ICAAP (Banks' Internal Systems and Internal Capital Adequacy Assessment Process) activities, which are conducted parallel to the budget process that covers the parent bank and affiliates, were carried out so as to entail stress tests, as well. Risk appetite core metrics for solvency and profitability and operational risk limits and their thresholds were reviewed with respect to the risk appetite and submitted for approval of the Board of Directors. Necessary coordination continued for risk appetite reporting, which is done monthly to the Risk Committee of the Board, weekly to the Risk Management Committee, quarterly to the Board of Directors and on meeting dates to the Audit Committee; in this scope, core metrics and risk limits mentioned above were monitored and reported. Additionally, monitoring, analysis and internal reporting were carried out with respect to the evaluation of the capital adequacy ratio. As part of operational risk management activities, the operational risk losses at the Bank and affiliates were monitored and reported. Within the frame of operational risk appetite, synthetic indicators were established and followed up to track the changes in types of operational risks and to measure the management effectiveness of these risks. Operational Risk and Control Self-Assessment activities were

carried out; scenario and stress test analyses for operational risk were conducted within the scope of ICAAP and stress test reporting. Meetings and trainings were held and information was provided to the Bank's staff to enhance awareness of the Bank's employees regarding operational risk management. The Operational Risk Admission function that also covers the outsourcing management function coordinated the process incorporating the definition of risk exposure resulting from new initiatives (business/product/service, process/technology transformations, and outsourcing including support/appraisal services), establishment of an effective control environment necessary to mitigate those risks, and taking risk mitigation measures in accordance with internal guidelines and in a manner to incorporate the activities of Operational Risk Admission and Product Governance Committee activities.

Market and Structural Risk Department reviewed thresholds within the framework of risk appetite, in order to monitor and manage market, counterparty credit, structural interest rate, exchange rate and liquidity risks, and submitted these thresholds for the approval of the Board of Directors. Internal metrics and early warning indicators, as well as regulatory limits for risk-based limits were regularly monitored and reported to all related parties and committees. Stress tests were employed to evaluate potential and worst-case risks that may arise from economic circumstances. Limits and alert levels instituted to determine risk exposure were monitored at the Bank and affiliates, and necessary actions were taken in accordance with the applicable procedures. New regulatory framework introduced and decisions adopted within the frame of financial stability policies were watched closely. Their impact on the Bank's liquidity, structural interest rate, exchange rate, market and counterparty credit risks were analyzed thoroughly and were reflected on internal core metric measurements. Within the frame of ICAAP and stress test report, stress tests and scenario analyses were performed along with internal calculations on the basis of risk types. Intraday liquidity risk was monitored regularly using the metrics defined. Infrastructural work was carried out to increase operational efficiency. Risk management activities at subsidiaries were followed up closely.

The implications of the new regulatory framework introduced during the pandemic and of markets' performance upon the Bank's risk profile, particularly upon its liquidity, market and structural interest rate risks were analyzed in detail, the intensity of monitoring activities was increased to ensure a closer watch through Early Warning Indicators that began to be followed-up on a daily basis, daily tracking reports and detailed analyses, which resulted in proactive and effective risk management.

The Validation Function performed qualitative and quantitative validations regarding internal models. Validations performed for those models and parameters that are taken into account in ICAAP calculations were presented to the Audit Committee. The Credit Risk Control Function set limits for loan growth in view of risk-return balance and updated them as necessary with respect to COVID-19. Internal capital requirement was calculated and the internal capital threshold values set at the onset of the year were monitored. The infrastructure needed for systemic computation of risk-based profitability metrics was established, and regular reporting was carried out. Internal credit risk and credit concentration risk calculations, stress tests and scenario analyses were carried out within the framework of ICAAP and stress test report. COVID-19 scenarios were supplemented to stress tests, and regular reporting commenced. Additional studies were performed to determine how internal capital would be affected under COVID-19 circumstances, and the same were reflected in the budget. The conformity of the risk models employed at the Bank with the internal rating-based (IRB) approach was monitored and the use of the models within the Bank were assessed. The effects of the risk parameters that will be produced with the new models upon internal capital were analyzed. Regular reporting on credit risk was made to the senior management. Risk Management Control function verified that risk management activities were handled by risk units in accordance with the Bank's policy and procedures.