

UNOFFICIAL TRANSLATION

Governor of Bank of Mongolia's decree dated February 8, 2012, No A-18 to make amendment

In accordance with legislation article 28 law of the Central bank (Mongolbank), it enacts hereby:

1. "General guidance for conducting on-site examination in bank by Supervision Department of Bank of Mongolia" is being approved in terms of updated as in annex.
2. According to issuance of this resolution, annex 2 or "Sample guidance for conducting full scope on-site examination in bank" is withdrawn.
3. Actions to monitor enforcement of this decree shall be assigned to Supervision Department, BOM (Mr. B.Lkhagvasuren)

For the Governor L.Purevdorj /signed/

Approved by the Governor of Bank of Mongolia

General guidance for conducting on-site examination in bank by Supervision Department of Bank of Mongolia

Chapter 1. General provisions

1. On-site examination shall be conducted in accordance with this guidance.
2. The purpose of on-site examination is to assess compliance of laws, rules and regulations, make conclusion on bank's risk profile and to impose penalties if deficiencies are noted and take action to correct deficiencies.
3. Examination shall be conducted based on documents for examination cycle and "Questionnaire for guidance" which is annex of this guidance is being completed to evaluate the bank's CAMELS rating
4. Type of examination: full scope or targeted
5. Structure of examination team: team leader and members.
6. Bank is obligated to disclose in a complete and accurate manner to the Bank of Mongolia and supervisors of the Bank of Mongolia their financial statements, primary financial documents, information, data and documents regarding management of the bank that are required to be compiled as stated in the relevant legislations, and the comprehensive list which details the equipments, SWIFT, tools, software and sub-software used in their financial operations, their precise locations as well as their passwords for access to ensure independent supervision.
7. Head of work group shall organize team to get examination conducted efficiently and shall introduce to the management of BOM regarding examination process and their proposal to make amendment if it is needed.
8. Work group shall examine internal auditing controls on accounting, findings noted as a result of the control, measures taken by auditing department.
9. Work group shall examine if monthly reports submitted to BOM are completed and accurate.

Chapter 2. Scope of examination

One. Asset

- 1.1 To determine structure of adjusted assets
- 1.2 To determine if guard and storage of all supplies of currency and similar valuables are adequate
- 1.3 To examine implementation of regulations, rulings on supplies of currency and similar valuables
- 1.4 To determine if transferring cash items in BOM is compliant and if deficiencies are noted
- 1.5 To determine the structure and its change in cash and short term securities

- 1.6 To check cash and memorial slip to validate report of examination
- 1.7 To count the cash and reconcile cash count proof sheet to general ledger if it is needed
- 1.8 To examine contracts and memorial slip of outstanding amount of interbank market loans
- 1.9 To determine if total amount of securities and asset backed securities that bank can purchase is compliant with requirements of Banking law
- 1.10 To evaluate the bank lending policy, practices and authority for make decision to grant loan
- 1.11 To determine the structure of the loan portfolio /purpose of the loan, type, concentration of the credit, maturity analysis/
- 1.12 To examine a total of ... percent of loans and to determine the purpose of the risky loans
- 1.13 To examine loan granted and repaid for the period of examination cycle
- 1.14 To make conclusion on reasons for increase /decrease/ in non performing loan
- 1.15 To determine if classification of initial term restructured loans is compliant with regulation
- 1.16 To examine overlapped loans in rural areas
- 1.17 To examine asset provisioning, debit transactions to this account and provisioning policy, practices
- 1.18 To determine a total amount of loan and equivalent other assets is duly fulfilled with requirements of Banking law
- 1.19 To examine if loan and equivalent other assets to related parties is compliant with Banking law
- 1.20 To examine if loan and equivalent other assets to borrower and their connected parties is compliant with Banking law
- 1.21 To verify accuracy of information transmitted by bank to CIB through reconciling it to CIB database
- 1.22 To compare the credit concentration indicator /ratio of credit outstanding to capital system/ with average of banking system
- 1.23 To compare ratios, such as non performing loans as a percentage of total loans, its change and income assets, with average for peer group
- 1.24 To compute ratio of other real estate owned to net assets
- 1.25 To determine the risky assets is classified in compliance with regulation
- 1.26 To examine outstanding receivables by owners, establish reasonableness for booking as receivables and compare outstanding amount with previous examination period and make conclusion
- 1.27 To verify each item of other assets based on accounting documents
- 1.28 To examine if transaction on advances of done on time
- 1.29 To examine if interest is accrued on time, if accruals is written off in compliance with regulations
- 1.30 To determine if receivables provisioning made in compliance with banking regulation
- 1.31 To determine structure of the fixed and intangible assets
- 1.32 To determine total value of fixed assets fullfilled requirements of Banking regulation
- 1.33 To examine list of annual or half year inventory and determine if transferring, selling, liquidation is performed in compliance with banking regulation,
- 1.34 To determine if booking and recovering in compliance when deficiency and excess is noted
- 1.35 To determine asset risks and its risk level
- 1.36 To determine if control, evaluation of internal auditing on asset quality and corrective action is adequate when deficiency is noted
- 1.37 To determine the structure of long term investment

- 1.38 To examine account of letters of credit, guarantee is opened, booking and their quality
- 1.39 To examine the quarterly and annually reconciliation of interbank settlement

Foreign settlement

- 1.40 To examine a total of ... percent of current accounts and savings opened in foreign banks
- 1.41 To access the SWIFT network and validate information
- 1.42 To ascertain if booking of buying and selling foreign currency is compliant with banking accounting regulation
- 1.43 To determine if off-balance foreign currency trading is adequately reflected banking accounting and balance sheet
- 1.44 To determine if foreign currency position is accurate and submitted to Bank of Mongolia on time
- 1.45 To determine if internal auditing of foreign currency trading is adequate and if corrective actions is initiated if deficiency is noted
- 1.46 To evaluate risk level of foreign exchange settlement

Two. Capital adequacy

- 2.1 To determine if capital adequacy ratio, including Tier 1 ratio is adequate
- 2.2 To make comparison growth in capital and assets, influence of assets quality on earning and make conclusion
- 2.3 To examine change in structure of capital by each account
- 2.4 To determine change in capital is made in compliance with banking regulation
- 2.5 To determine risk influence on capital
- 2.6 To determine structure of fund, including revaluation fund, debit transactions to this account
- 2.7 To evaluate risk level of capital and determine risk tendency
- 2.8 To determine tier 1 and tier 2 ratio and examine if supervisory correction is made
- 2.9 To examine contract of subordinated debt and make conclusion
- 2.10 To compare capital adequacy ratios with average of peer group and make conclusion
- 2.11 To determine if banks, their subsidiaries and affiliate companies prepare financial statements in accordance with Banking law and regulation on setting and monitoring prudential ratios to banking operation

Three. Earning

- 3.1 To examine of income and expense, retained earning as end of year and examine if closing entries are done in compliant with relevant regulation
- 3.2 To determine if independent auditor is selected in compliance with Auditing law
- 3.3 To get acquainted with audit opinion and to determine if audited financial statement and information for end of year is disclosed in compliance with regulation
- 3.4 To compute income and expense as from beginning of year when calculating profit or losses for examination date
- 3.5 To determine structure of income and expense
- 3.6 To examine if revaluation of foreign currency is done is compliant and compute revaluation income and expense
- 3.7 To determine income source and determine if it reached at planned level
- 3.8 To examine income and expense, earnings based on sampling method
- 3.9 To determine if asset provisioning is adequate and make conclusion on provisioning influence on earnings

- 3.10 To examine an extraordinary income and expense
- 3.11 To examine internal auditing controls on earning, findings noted as a result of the control, measures taken by auditing department
- 3.12 To evaluate risk level of earning and its tendency
- 3.13 To compare annual average of return on assets and on equity with peer group average and make conclusion

Four. Liquidity

- 4.1 To determine the structure of the liabilities and maturity risk of liabilities
- 4.2 To determine the outstanding amount of current account of individuals and companies, their proportion in total liabilities
- 4.3 To determine if reserve requirements is met
- 4.4 To determine funding from non bank financial institution, its comparison with previous year's amount
- 4.5 To determine funding from other banks, its comparison with previous year's amount
- 4.6 To determine if computation of accrued payables of interest of liabilities is accurate
- 4.7 To examine fund of sociality development, decrease transactions to this account
- 4.8 To determine if delayed interbank settlement is noted
- 4.9 To determine if policy on improve liquidity and plan to pay up liabilities is adopted
- 4.10 To examine internal auditing controls on liquidity, findings noted as a result of the control, measures taken by auditing department
- 4.11 To evaluate risk level of earning and its tendency
- 4.12 To determine if bank has liquidity management strategy
- 4.13 To determine if bank has by-laws that regulates relations regarding strategy on liquidity management
- 4.14 To determine if bank has created database to measure, monitor and report liquidity
- 4.15 To determine if bank has liquidity contingent plan
- 4.16 To determine frequency to calculate in and out cashflow
- 4.17 To determine if accumulated depreciation is calculated on time
- 4.18 To determine if payables settlement with individual and companies paid on time
- 4.19 To examine if accrued interest is calculated complete and accurate
- 4.20 To make GAP analysis of interest rate and maturity

Five. Sensitivity to risk

- 5.1 To make conclusion if bank manage properly risk of market, interest, foreign exchange and price risk
- 5.2 To determine if bank management conduct policy to identify market risk, measure and monitor, to protect against these risks
- 5.3 To determine the structure of management information system, administration, return decision making process
- 5.4 To determine if policy on relationship of risk of market interest and price adequate
- 5.5 To determine if bank management has able to overcome and liquidate consequence of risk
- 5.6 To determine if method to evaluate risk is appropriate
- 5.7 To examine internal auditing controls on risk management
- 5.8 To determine interest rate risk
- 5.9 To determine operational risk
- 5.10 To determine if methodology to evaluate the foreign exchange risk is reliable for bank that estimate forex risk prudential ratio with VaR methodology

Six. Corporate governance

- 6.1 To examine organization chart, structure and management of the bank
- 6.2 To examine if regulation and by-laws that regulates banking activities is registered in the Bank of Mongolia in compliance with relevant law
- 6.3 To determine if business plan is developed
- 6.4 To evaluate implementation of principles of corporate governance at the bank
- 6.5 To examine if asset and liability management and activity of credit committee is compliant with regulation
- 6.6 To examine organization of chart, structure, operation of internal auditing department, measures taken by them and its result
- 6.7 To determine if Board of directors, Supervisory board and CEO met criteria stated in Banking law and determine if relevant documents are furnished to BOM
- 6.8 To determine supervision of banking activity by Board of directors, Supervisory board and its result
- 6.9 To determine if banks disclose a required information to public
- 6.10 To determine if structure and duties of owners are disclosed
- 6.11 To determine if rights and duties of external auditors are disclosed
- 6.12 To determine if rights and duties of Banking auditing committee and internal auditors are disclosed

Information technology risk management

- 6.13 To determine if bank has IT risk management and planning in all scope of IT cycles
- 6.14 To determine if information security is adequate
- 6.15 To determine if bank has adequate system processing, operation and usage
- 6.16 To determine if system input-output meet requirements of network security
- 6.17 To determine if resource management is adequate
- 6.18 To examine contract for outsourcing service
- 6.19 To determine if bank has contingent plan and documentation
- 6.20 To examine internal auditing controls on IT management and its standard of operation is compliant

Seven. Operation of bank unit

- 7.1 To examine operation of bank branch, representative office, settlement center, and settlement cash counter and determine if bank unit is licensed in compliance with regulation /Supervision department shall inform branch of BOM aimags, where bank unit operates, on conducting examination/
- 7.2 If it is considered necessary, on site examination shall be conducted in bank unit.

Eight. Miscellaneous

- 8.1 Bank, member of a financial conglomerate, their competent officials and employees are obligated to disclose in a complete and accurate manner to Bank of Mongolia and supervisors of the Bank of Mongolia their financial statements, primary financial documents and their verifying documents, information, data and documents regarding management of the bank that are required to be compiled as stated in the relevant legislations, and the comprehensive list which details the equipments, tools, software and

sub-software used in their financial operations, their precise locations as well as their passwords for access to ensure independent supervision.

8.2 Supervisors may receive letter written by Bank management to certify that financial statements, primary financial documents and their verifying documents are accurate and complete.

8.3 Cash and memorial slip can be checked to validate report of examination.

Chapter 3. Overall conclusions

1. State inspector shall use of power to impose administrative sanction take measures to correct deficiencies noted as a result of examination.

2. Work group shall evaluate the financial condition in accordance with the regulation on the full scope on-site examination and evaluation of the banks activities and its financial conditions

3. Work group shall prepare the report of examination in accordance with the Annex 1 of Decree of the Governor of Bank of Mongolia dated January 12, 2000 No 23

4. Head of work group shall introduce the report of examination to Board of directors and get adopt resolution regarding report of examination. Supervisor in charge of bank shall monitor implementation of resolution.

EXAMINATION QUESTIONNAIREOne. Asset

No	Question	(Yes/No)	Comments/ Reference
1.1	To determine if guard and storage of all supplies of currency and similar valuables are adequate		
1.2	To examine implementation of regulations, rulings on supplies of currency and similar valuables		
1.3	To determine if transferring cash items in BOM is compliant and if deficiencies are noted		
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1.10	To determine the structure of the loan portfolio /purpose of the loan, type, concentration of the credit, maturity analysis/		
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	system		
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No	Question	(Yes/No)	Comments/Reference
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6.3.	To determine if business plan is developed		
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6.5.	To examine if asset and liability management and activity of credit committee is compliant with regulation		
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6.8.	To determine supervision of banking activity by Board of directors, Supervisory board and its result		
6.9.	To determine if banks disclose a required information to public		
6.10.	To determine if structure and duties of owners are disclosed		
6.11.	To determine if rights and duties of external auditors are disclosed		
6.12.	To determine if rights and duties of Banking auditing committee and internal auditors are disclosed		

Information technology risk management

No	Question	(Yes/No)	Comments/Reference
6.12	To determine if bank has IT risk management and planning in all scope of IT cycles		
6.13	To determine if information security is adequate		
6.14	To determine if bank has adequate system processing, operation and usage		
6.15	To determine if system input-output meet requirements of network security		
6.16	To determine if resource management is adequate		
6.17	To examine contract for outsourcing service		

6.18	To determine if bank has contingent plan and documentation		
6.19	To examine internal auditing controls on IT management and its standard of operation is compliant		
6.20	To determine if bank has IT risk management and planning in all scope of IT cycles		

Seven. Operation of bank unit

No	Question	(Yes/No)	Comments/ Reference
7.1	To examine operation of bank branch, representative office, settlement center, and settlement cash counter and determine if bank unit is licensed in compliance with regulation /Supervision department shall inform branch of BOM aimags, where bank unit operates, on conducting examination/		

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