Brussels, 21 January 2019

NOTICE TO THE ACCREDITED AUDITORS

NOTICE 2018-9

Dear members,

On a six-monthly basis, the Management Board of IRAIF/IREFI informs the accredited auditors of main highlights or attention points, which could impact their work.

The following overview is structured according to the relevant working groups of IRAIF/IREFI.

The FSMA and the NBB also provided their key attention points. The attention points are without prejudice to the ongoing work on the evolution of the collaboration of accredited auditors to the FSMA supervisory missions.

On 15 January 2019, a Capita Selecta training session has been held at the IBR/IRE in cooperation with the NBB explaining some of the main topics mentioned in this notice.

Due to regulatory changes, the templates for prudential reporting towards the NBB and the FSMA are currently being reviewed and will be released in January 2019.

Finally, as IREFI is committed to process personal data of its members and external partners carefully, we would like you to pay attention at and comply with the privacy statement of IREFI, published on the website of IBR-IRE: https://www.ibr-ire.be/nl/het_beroep/de_bedrijfsrevisor/berichten-irefi/Pages/Default.aspx.

Should you have any questions regarding this document, please do not hesitate to contact me, any member of the Management Board of IRAIF/IREFI or Ingrid De Poorter.

Yours sincerely,

Olivier Macq
President IRAIF/IREFI

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pour les Institutions Financières
Institut Royal
Union professionnelle reconnue

Instituut van de Revisoren Erkend
voor de Financiële Instellingen
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IRAIF IREFI

Table of Contents

I. Data Quality

The circular NBB_2017_27 on the NBB's expectations as regards to quality of reported prudential and financial data contains also the NBB's expectations to the accredited auditor with regards to data quality. More specifically, the circular states the following:

"*In addition to the measures that institutions can take internally, accredited statutory auditors will also be required to examine data quality.*

To this end, it is essential that documentation for each of the organizational elements set out above should be sufficiently detailed, clear and up-to-date in order to enable the accredited statutory auditor to verify, for the purpose of the opinion required from him on the periodic statements, whether the institution has adequately implemented all relevant and effective measures to ensure quality of reporting under the regulatory requirements and expectations laid down in this Circular. "

The purpose of this note is to further clarify the role of the accredited auditor with regards to data quality, which has also been discussed with representatives of the NBB during the past months.

Procedures to be performed on data quality in the context of the accredited auditor's reporting on the system of internal control of the institution

Circular NBB_2017_27 requires institutions to perform a self-assessment which verifies to what extent the institution already complies with the prudential expectations laid down in this circular. Although not explicitly stated, it is expected that institutions periodically update this self-assessment, and at least annually when management formally reports on its system of internal control to the board of directors in accordance with applicable circulars (i.e. circular NBB_2011_09 for credit institutions and circular NBB_2018_23 for insurance companies).

In the context of his reporting on internal control, it is expected that the accreditor auditor has obtained and evaluated the periodic self-assessment performed by the institution. The objective of this evaluation is to assess whether the self-assessment performed is complete and whether all discrepancies are identified by management with the knowledge and experience gained as part of the audit of the annual accounts and prudential reporting. In this evaluation, the auditor verifies whether the controls identified by the institution to ensure data quality are in place and effectively reduces the risk of potential errors to an acceptable level ("test of design"). The auditor also verifies whether the proposed remediation plan to address the gaps identified are deemed as sufficiently robust. The accreditor auditor also obtains an understanding of the implications of the execution of the remediation plan on the self-assessment carried out (new controls implemented by management) and new controls introduced as a result of new reporting requirements.

Factual findings and observations are part of the accredited auditor's reporting on the system of internal control to the NBB. Findings the accredited auditor is expected to include in his report are for example:

- inappropriate/incomplete reporting of gaps identified during the self-assessment by management in its annual reporting to the board of directors;
- remediation plans that will not address the gaps identified; and
- implemented controls by management not operating effectively that are observed by the accredited auditor when testing the operating effectiveness of these controls as part of the execution of the audit program on the half-year and year-end reporting.

In the context of the accredited auditor's reporting over the system of internal control, it is expected that a particular attention is to be paid whether the system of internal control with respect to data quality is in line with the principles laid down in the data quality circular. If not, the auditor should draw attention to this in his reporting over internal control (by for example referring to the report established by management with regards to their evaluation of the system of internal control in which non-compliance observations are commented more in detail), and if deemed required, exercise his signal function.

The template audit report on internal control has been adapted accordingly in order to ensure that the requirements of this circular and the auditor's findings and observations with regards to data quality are embedded within this report.

Procedures to be performed on data quality in the context of the accredited auditor's reporting on the prudential reporting

It is expected for *limited review* purposes at half-year that the auditor performs enquiries in order to assess whether the self-assessment is further completed with additional controls resulting from the implementation of the remediation plan and/or due to new reporting tables. In case of changes, it is important that the auditor verifies whether the add-ons are indeed controls that are expected to prevent/detect errors in the prudential reporting. Based on professional judgment and depending on the nature of the audit approach and where considered relevant, the auditor decides whether for selected key controls operating effectiveness is tested as part of limited review procedures.

For *year-end*, it is expected that the accredited auditor, based on professional judgment and his evaluation of the design and implementation of the controls in place with respect to data quality, tests the operating effectiveness for (selected) key controls and/or adopt a substantive audit approach on certain aspects (for efficiency reasons or in case of missing or deficient internal controls) in order to provide reasonable assurance to the NBB on the periodic financial information. It is expected that control deficiencies identified when testing the operating effectiveness of internal controls over data quality are part of the auditor's reporting over the system of internal control (cf. supra).

Note also that a draft audit program has been prepared by the working group, which summarizes the proposed approach (both for banks and insurers) to be adopted for the review and audit of the prudential reporting. This audit program has been developed as a result of preliminary discussions with the representatives of the NBB. It will be presented to the Board of the IREFI for approval and distributed to the accredited auditors.

II. Main attention points for the Credit Institutions

a) IFRS 9

For most financial institutions IFRS 9 "Financial Instruments" and IFRS 15 "Revenue from Contracts with Customers" have become applicable as from January 2018. IFRS 9 represents an important change for classification and measurement of financial assets, the additional transition disclosures required by IFRS 9 will need to be provided in the annual financial statements. The topics covered in previous communications remain valid. Please also refer to point (c) below for NPLs and section IX (d) for the attention points of NBB in respect of IFRS 9.

b) Accounting for the Irrevocable Payment Commitment (IPC) to the SRB

The Irrevocable Payment Commitments (IPC) represent an alternative to cash payments in the context of the ex-ante funding for the Single Resolution Fund (SRF). The IPC can be defined as an obligation taken by the credit institutions towards SRB to pay their contributions in the future for which a cash collateral is provided. The SRB has previously published their view on the accounting considerations with respect to the IPC, the SRB is currently discussing with certain banks on the ability to return the cash collateral upon the rendering of their banking license. Entities should consider the status of the ongoing discussions to determine whether their current policy with respect to the accounting for the IPC remains valid.

c) Credit risk: Non-Performing Loans & Credit underwriting criteria and exposure quality

Credit Risk remains an important audit and prudential priority in 2019. The current aggregate level of NPLs in European Banks remains elevated compared to international levels. Auditors will have to focus on the adequate level of provisioning of these exposures. Further in accordance with IFRS 9 and the relevant allocation of financial instruments in the stages 1 to 3, the auditor will review if there has been a significant increase in credit risk since the initial recognition and ensure the entities recognize a loss allowance at an amount equal to the lifetime ECL at each reporting date, for the exposures in stage 2 and stage 3. The NBB indicated that, as in past years, even in this relatively uncertain and difficult economic environment, the cost of risk remains relatively low in Belgium. The NBB expects that the auditors will, when considered relevant, consider the impairment on loans as a significant risk, and in particular the risk of understatement.

ECB Banking Supervision will also assess the quality of banks' underwriting criteria with a focus on new lending. The quality of banks' lending practices will be examined and lending standards will be scrutinized with a view to mitigating potential risks. This work may result in bank-specific actions. In addition, the quality of specific asset class exposures will be examined through dedicated on-site inspections related to areas such as commercial real estate, residential real estate and leverage finance.

Further developments in the past several years have shown an increased concentration of bank's assets on the Belgian residential and commercial real estate markets, which could be the source of important unexpected losses in case of large adverse shocks in these property segments.
Finally we note the EBA published on 31 October 2018 the final report on "Guidelines on management of non-performing and forborne exposures" which has to be taken into account by the auditors in their ongoing work on the NPL and provisioning processes or methodologies by banks.

d) Final outcome of the TRIM exercise – Horizontal analysis – Impact on internal models used by banks - RWA – correctness of scope / calculations

The targeted review of internal models (TRIM) will continue in 2019 with the overarching aim of reducing unwarranted variability of risk-weighted assets and confirming the adequacy of banks' approved Pillar I internal models. In the course of 2019, ECB Banking Supervision intends to continue its TRIM on-site investigations, focusing mainly on the models used to assess the credit risk for exposures to medium-sized / large corporates and institutions and specialized lending. The ECB Banking Supervision will conduct horizontal analyses on the finalized investigations and will start to

prepare a final project report. It also plans to update the existing ECB guide to internal models. The auditors will have to remain vigilant on the outcome of this exercise and assess (together with the NBB – ECB) the impact of this on the financial and prudential reporting of the banks.

e) ICAAP and ILAAP

Internal capital and liquidity adequacy assessment processes (ICAAPs and ILAAPs) are key risk management instruments for credit institutions. ECB Banking Supervision reviews the quality of institutions' ICAAPs and ILAAPs as a fundamental part of the SREP. Following on an intensive dialogue with banks, the finalized ECB guides on ICAAP/ILAAP will become available for use from 2019 onwards. Work will also continue on improving the transparency around the risk-by-risk composition of the Pillar II capital requirements.

f) Brexit

With the UK's departure from the EU scheduled in March 2019, banks' preparedness for Brexit remains a high priority for the regulators. The latter will closely monitor the implementation of banks' Brexit plans to ensure that they comply with supervisory expectations. This work is likely to be affected by the outcome of the political negotiations ongoing and the decision whether there will be a transition period. Given the persisting uncertainties, ECB banking Supervision has stressed that banks should be ready for all contingencies and should finalize their preparations.

g) Topics covered in previous communications that remain valid

We also want to draw your attention at the following points which have been communicated in the prior communications and which remain valid:

- The impact of the introduction of GDPR in May 2018;
  General Data Protection Regulation (GDPR) became applicable on 25 May 2018 regarding the protection of consumer data. Non-compliance with the law could lead to reputational damages, both from a reputational and financial perspective. The regulation also foresees penalties (potentially significant) for companies which would not comply (in addition to the reputational damages).
- The persistent low interest rate environment:
  Taking into consideration the low interest rate environment and the relating implied risks, interest rate risk relating to the mortgage book as well as the hedging strategies in place (including the assumption regarding prepayment risk) are still receiving full attention from the supervisory authorities. In this context, the accredited auditor is requested to comment on these items in his periodic report on the situation as of 31 December 2018.
  In accordance with IAS 39, the portfolio hedges are accounted for as a macro fair value hedge on a bucket of similar mortgage loans with fixed interest rates in order to reduce the P&L volatility. Given the continued stream of refinancing of mortgage loans (due to the decrease of market interest rates), the accredited auditor should take into consideration whether any impairment/derecognition/inefficiency should be recognised on the currently recognised fair value hedge adjustments of macro fair value hedge models of banks reporting under IFRS as endorsed by the EU on top of the ineffectiveness which was recognised in every period on the hedging of the change in fair value of those mortgage loans.

- The Payment Services Directive 2 (Directive 2015/2366) on payment services in the internal market transposed in Belgium into the Law of 11 March 2018 that was published and entered into force on 26 March 2018 (see also further under IV. a));
- AML / CTF and the relevant risk based approach for the duty of vigilance with respect to AML (Law of 20 July 2017 applicable as from October 2017):

  As mentioned in our Q4 2017 attention points, a new Law on Anti-Money Laundering (AML) has been introduced on September 18, 2017. Via Circular NBB_2018_02 of January 24, 2018 the NBB provides information on its expectations with respect to the general risk assessment on AML to be performed. It is expected that the accredited auditors discuss with their clients the status of the implementation of the new provisions introduced by this new legislation and circular.
- MiFID II regulation that entered into force on 3 January 2018 (its application is limited to Credit Institutions and investment firms):

  MiFID II is composed of Level 1 texts (Directive 2014/65/EU and Regulation 600/2014), Level 2 texts (Commission Delegated Regulations and Commission Delegated Directive, Regulatory Technical Standards and Implementing Technical Standards) and Level 3 texts (mainly ESMA guidelines). This regulation has entered into force on 3 January 2018 and its application is limited to the Credit Institutions and the Investment Firms (not applicable to the insurance sector).

  On 18 July 2017, the FSMA has issued a communication (FSMA 2017-11) to the Credit Institutions and to the Investment Firms to draw the attention on the necessity to have an action plan with the decisions and measures that are taken to be compliant with MiFID II.

  As the provisions of MiFID II have a significant impact on the organization and the internal control of the financial institution it is necessary that its accredited auditor discusses with the institution the measures that are taken and identify key attention points.
- IT & Cyber-security risk – ECB banking Supervision will continue to assess the IT and cyber risks facing banks and will launch a number of on-site inspections on IT risk-related topics. We remind that significant institutions will continue to report any significant cyber incidents to the ECB under the SSM cyber incident reporting process;
- Banks will also need to remain agile and adjust their business models to the challenges and opportunities offered by the digitization of many financial services.

III. Main attention points for the Insurance Sector

a) Cost allocation model for best estimate calculations

Following an analysis performed by NBB on the cost allocation model applied for the calculations of the best estimate technical liabilities of the 7 major insurance institutions, the NBB issued Communication NBB_2017_32 of December 29, 2017, which provides for all insurance institutions further instructions, guidelines and clarifications on this topic. This communication covers amongst others the following topics:

- granularity of the cost centers;
- allocation of overhead expenses;
- increase of transparency and objectivity;
- treatment of non-recurring expenses;
- application of contract boundaries on the costs;
- timing of modelling of the costs in the cash-flow projections;

- inflation of costs;
- back-testing;
- documentation of the cost allocation model.

The NBB expects that the insurance institutions prepare an action plan including the planned modifications to meet the provisions of this communication. The 7 insurance institutions subject to the analysis by the NBB as discussed above were expected to introduce their action plan at the NBB by May 31, 2018. The other institutions are expected to have their action plan available for the NBB. Awaiting for the implementation of the measures of the action plan, the NBB expects that the insurance institutions perform an impact analysis and apply the most prudent approaches.

It is expected that the accredited auditors take the results of the action plan and impact analysis into consideration in their 2018 audit plan and conclusions and report their findings to the NBB as part of their reporting on the periodic financial information.

b) Validation checks between Solvency II reporting and statutory reporting

Via an e-mail communication of May 3, 2018 the NBB provided the insurance institutions with an overview of additional validation controls which should ensure consistency of the reported figures between the QRT's and the statutory accounts. Some of the validation controls are mandatory to be respected while others can be explained if any differences would arise.

The accredited auditors are expected to discuss with their clients the results of these validation checks. If any differences would arise, they are expected to report these to the NBB as part of their reporting on the periodic financial information.

c) NBB stress tests for 2018

In 2018, the Belgian insurance sector was subject to a stress test consisting of two scenarios and a questionnaire on cyber risk. The scenarios and the questionnaire have been developed by EIOPA for their 2018 European insurance stress test and are adopted by the NBB and applied to a significant part of the Belgian insurance sector.

The first scenario (Yield Curve Down) assumes a persistent low yield environment and a significant increase in the average life expectancy across the entire population. The second scenario (Yield Curve Up) assesses the impact of a sudden and sharp increase in yields, an instantaneous increase in lapses and higher than expected claims inflation on the solvency position of an insurer.

The submission of the results to the NBB was expected by August 31, 2018.

The accredited auditors are expected to acquaint themselves with the results of the stress tests and to take these into consideration in their risk assessment, but do not have to perform additional procedures on these stress tests.

d) Interest rate risk and liquidity reporting

Circulars NBB_2018_16 and NBB_2018_17 update the prior issued circulars including the instructions for completion and reporting.

IRAIF IREFI

e) Residential mortgage loans reporting

Circular NBB_2018_27 sets up the instructions for completion and reporting over residential mortgage loans by insurance companies.

f) System of Governance

Circular NBB_2018_23 update the prior issued Circular NBB_2016_31 on the National Bank of Belgium's prudential expectations concerning the governance system in the insurance and reinsurance sector.

g) Application of IFRS 17/IFRS 9

Considering the impact of the introduction of IFRS 17 and IFRS 9 (see also infra), we recommend that the accredited auditor closely monitors the implementation of these IFRS standards to ensure that the deadlines will be met.

Note that the IASB Board of Directors members have recently voted in favor for the postponement of the implementation of the IFRS 17 standard by one additional year.

We also want to draw your attention to the fact that entities applying the deferral approach for IFRS 9 already have to prepare disclosures including the following information:

- Fair value information separately for:
  - financial assets that meet the SPPI test unless held for trading or managed on a fair value basis; and
  - all other financial assets;
- Credit risk and quality information.

We recommend the accredited auditors to verify the appropriate disclosure of the information mentioned here above and to verify the results of the SPPI test.

h) Prudential reports to the NBB

The accredited auditor's reports over the 2018 year ended prudential reporting's for insurance companies have been updated upon NBB's request in order to include an explicit comply and/or explain confirmation over the usage of the audit programs developed by the IRAIF/IREFI.

i) Topics covered in previous communications that remain valid

We also want to draw your attention at the following points which have been communicated in the prior communications and which remain valid:

— The impact of the introduction of GDPR in May 2018;
— The persistent low interest rate environment;
— The guidelines introduced by the NBB on the use of the loss absorbing capacity of deferred taxes.

IV. Main attention points for payment institutions and E-money institutions

a) Licensing under the Payment Services Directive (PSD) II

As part of the grandfathering of PSD II licenses (i.e. granting of PSD II license to institutions that already had a PSD I license based on a limited file following the implementation of the directive in the Belgian Law via the law of 11 March 2018), the NBB sent to the grandfathered institutions a letter detailing its points of attention and expected actions.
It is recommended that the accredited auditors discusses the evolution of these points with the management of the institution and documents/reports the results of this discussion in their reporting to the NBB.

In parallel, the NBB pursued the transposition of PSD II related guidelines and recently published circulars on the periodic reporting of Payment Institutions (first reporting on the situation as of 31 March 2019) and Fraud reporting (first reporting on the situation as of 30 June 2019). The circular on the prudential reporting of Electronic Money Institutions should also be published in the near future. A full overview of the applicable legal framework is available on the NBB website (https://www.nbb.be/en/financial-oversight/prudential-supervision/areas-responsibility/payment-institutions-and-electroni-4).

b) Anti-money laundering

Similar to prior periods, the NBB indicated that compliancy with the anti-money laundering regulation remained a key point of attention for the sector of Payment and Electronic Money institutions.
Particular focus is set on the activity of money remittance, which is considered as a higher risk activity by the prudential authorities.

c) Outsourcing

Article 34, §1, 1° of the Law of 11 March 2018 requests that the management of the institution report on an annual basis on the internal control framework, including specifically the measures taken to ensure that the outsourcing of activities does not negatively impact the quality of internal control (art 38, §1, 1°).
On this basis, the NBB requested the Payment and Electronic Money Institutions to evaluate their internal control over outsourced activities and to document this evaluation in a separated internal control report to be communicated to the NBB by the end of January 2019 for the first time.
The NBB also required the auditors, similarly to the overall internal control report, to comment on the report prepared by the management.
The NBB indicated that a new circular on outsourcing will be published in Q2 2019 and will clarify the expectations of NBB towards the management of an institution and the accredited auditors. It is however expected that the general principles defined in circular PPB 2004/5, with regards to sound management of outsourcing, will remain largely applicable. This new circular will be applicable to all financial institutions and therefore extend the requirements on reporting to other financial institutions categories.
For year-end 2018, in the absence of specific framework, it is expected that the accredited auditor of a payment institution or an e-money institution will include its comments relating to the internal controls regarding outsourced activities in its overall report over Management internal control evaluation.

Whereas no defined template or report structure currently exists, NBB indicated that the key focus of Management evaluation should be on the compliance with the principles defined in the circular PPB 2004/5 with a specific attention to the processes in place to follow and control the outsourced activities (as highlighted in principle 2 of the circular).

V. Main attention points regarding IFRS

a) Presentation of interest revenue for financial instruments not accounted for under the effective interest method

The IFRIC received a request about the effect of the consequential amendment that IFRS 9 made to paragraph 82(a) of IAS 1. That consequential amendment requires an entity to present separately, in the profit or loss section of the statement of comprehensive income or in the statement of profit or loss, interest revenue calculated using the effective interest method. The question was whether that requirement affects the presentation of fair value gains and losses on derivative instruments that are not part of a designated and effective hedging relationship. The Committee concluded that the requirement to present separately an interest revenue line item calculated using the effective interest method applies only to those assets that are subsequently measured at amortized cost or fair value through other comprehensive income (subject to any effect of a qualifying hedging relationship applying the hedge accounting requirements in IFRS 9 or IAS 39).

b) Brexit

The UK is due to leave the European Union on 29 March 2019. As the EC and the UK continue to negotiate the terms of the exit, businesses should be considering how this new political landscape will impact their organisations and should be considering the impact on accounting and reporting. In particular, this can include, amongst others:,

- the impact on the Disclosures of the Brexit-related risks,
- Subsequent events for events that occur between the year end and the date of signing the financial statements
- and impacts on Impairments and valuations.

c) Disclosure of IFRS 16 impact

IFRS 16, the new accounting standard for leases, becomes effective for annual reporting periods commencing on or after 1 January 2019. As with other new accounting standards, IFRS reporters are required to disclose information relevant to assessing the impact of IFRS 16 in periods prior to adoption.

VI. Main attention points regarding institutions of occupational retirement provision

As a recurring topic, the FSMA proposes that the accredited auditors devote particular attention to the prudence with which the technical provisions are calculated, and especially to the discount rate(s) used. In this context, the auditor should specifically address the comments (if any) that may have been raised by the FSMA or by the designated actuary on this matter. Also, would the accredited auditor rely on the work of the designed actuary, we recommend to explain briefly to which extent it has been done.

Furthermore, the FSMA wishes to emphasis the following:

1. The IRAIF/IREFI proposed template reports are developed by the IRAIF/IREFI with the objective to address a maximum of the comments and concerns raised by the FSMA. In consequence, the FSMA recommends using them. However, these templates should be adapted to reflect the specificities of the audited IORP and the specificities of the procedures conducted. Note that update template reports will be made available by the IRAIF/IREFI early 2019.
   The changes are mainly related to the clarification of the collaboration, if any, with the designated actuary and the follow up of the comments of the designated actuary and of the FSMA in our reports.
2. Would the accredited auditor identify inconsistencies in the "P40" reporting (on the governance and on the activities and financial structure of the IORPs) vis-à-vis the information he/ she has at disposal, he/ she should report these matters in the report towards the FSMA.
3. The valuation of the unlisted investments should be considered as a risk area.
4. The requirement of article 51 of the Law of 28 April 2003, pursuant to which accredited auditors "must bring to the FSMA's attention any fact or decision they may have become aware of in the course of their audit mission and that constitutes an infringement of the provisions" of the LPC/WAP and its implementing decrees.
5. The FSMA emphasizes that the accredited auditors should respect the deadlines for submission of their reporting. These deadlines are published in the yearly Reporting Circular. Earlier reporting is strongly recommended. If in the exceptional case a deadline cannot be respected, the FSMA wishes to be informed on the reasons of the late reporting (via a letter in E-Corporate).

VII. Other attention points

a) Materiality & signal function

Upon request of the NBB, the IRAIF/IREFI prepared a note explaining the basic principles regarding the calculation of materiality applied to credit institutions and insurance companies.

In order to manage the expectation gap, the IRAIF/ IREFI has also written a general memorandum regarding the signal function. Both notes will be distributed to the members of IRAIF/IREFI, after final review by the NBB.

b) AML

Similarly to some other supervisors, the NBB is considering to entrust the auditor of financial institutions with a specific assignment with regard to AML. The assignment could relate to follow-up of inspections or actions resulting from an offsite control, to follow up the risk analysis questionnaire as requested in Circular 2018-02 or other practical aspects. The cost of this assignment will be charged to the financial institution.

c) Others

For your information, a report on shadow banking in Belgium has been published recently:
https://www.fsma.be/nl/news/update-van-de-nbb-en-de-fsma-over-asset-management-en-shadow-banking-belgie
https://www.fsma.be/fr/news/mise-jour-de-letude-de-la-bnb-et-de-la-fsma-sur-lasset-management-et-le-shadow-banking-en.

IRAIF IREFI

VIII. Main attention points of the FSMA related to the 31 December 2018 audit[1]

a) Attention points regarding institutions of occupational retirement provision (IORP's)

Within the framework of 2018 auditwork, the FSMA wishes auditors to pay particular attention to the following points:

1. generally speaking, greater clarity in the annual reports to the FSMA as regards the auditor's examination of aspects that do not give rise to any specific comments by said auditor;
2. prudence in calculating technical provisions and, in particular, the discount rate(s) used;
3. consistency in the information contained in the 'P40' reports (on governance and on the IORP's activities and financial structure) with the information available to the auditor;
4. the valuation of the unlisted investments;
5. the codification of the IORPs' investments in securities with regard to the FSMA circular on reporting (FSMA circular on the communication of the annual accounts, statistics and related documents);
6. the IORP's follow-up to the actions taken by the FSMA (recovery plan, transversal action, inspection, specific action, etc.);
7. the IORP's reflections regarding compliance with the regulation transposing the IORP Directive (key functions including those of risk management, ORA, remuneration policy, ESG criteria and investment policy, transparency, etc.);
8. any infringements of the social legislation as regards supplementary pensions (voluntary supplementary pension, voluntary supplementary pension for the self-employed, etc.).

b) Attention points regarding regulated real estate investment company

The FSMA wishes auditors to pay particular attention to the following points:

1. the FSMA's approach to registration documents (information was sent to auditors by email);
2. the Communication of the FSMA on Disclosures IFRS 13;
3. the Regulatory Technical Standards on the European Single Electronic Format;
4. the European common enforcement priorities for 2018 annual financial report (New IFRS, Non Financial Reporting and APM's).

c) Attention points regarding collective investment schemes

1. Money Market Funds

[1] Attention points provided by the FSMA.

The MMF regulation 2017/1131 applies since 21/07/2018 to collective investment undertakings (CIU) that 1) are authorized as UCITS or AIF, 2) invest in short term assets and 3) have the objective to offer a return in line with money market rate and/or to preserve the value of the investment.

The MMF Regulation deals with product rules (investment policies requirements), risk management (portfolio rules, stress testing) and transparency (towards investors and towards the competent authority).

Regarding the reporting to the competent authority of the MMF, for each MMF that it manages, the manager shall report information (type and characteristics of the MMF, portfolio indicators, results of the stress tests, information on the assets, etc.) on at least a quarterly basis. In May 2018, the European Commission published a template (implementing technical standards) for the reporting of this information. The first reporting by the managers is expected by Q1 2020.

2. CIS reporting

Since 1 October 2017 new rules have been introduced with respect to the periodic statistical reporting of certain public CIUs to the FSMA. This new CIS reporting now consists of three tables to be reported, including the so-called AIF files, the reporting tables concerning AIFs under the reporting requirements of the AIFMD.

The FSMA has examined the content of the new CIS reports submitted to the FSMA and has found that for a substantial part of (compartments of) CIUs the reported information is not according to the guidelines of the FSMA. Firstly, a number of information items appear to be missing from the reports while they should be reported. Secondly, a number of data quality issues persist for many CIUs: reported information seems to be inconsistent with the sub-fund's portfolio, transactions, accounts or prospectus, and the calculation of some values is inconsistent with the applicable rules.

3. Liquidity tools

Since 15 October 2018 a new royal decree[2] gives the possibility to Belgian public open-ended CIS to use swing pricing, anti-dilution levy and redemption gates.

When a CIS/management company decides to use one of these liquidity tools, it has to fulfil several obligations:

- a special liquidity tools policy has to be put in place;
- the conflicts of interest policy has to be adapted. Specific attention has to be paid to the conflicts of interest that could arise out of the use of the liquidity tool;

[2] KB van 15 oktober 2018 tot wijziging van het KB van 7 maart 2006 met betrekking tot de effectenleningen door bepaalde instellingen voor collectieve belegging, het KB van 10 november 2006 op de boekhouding, de jaarrekening en de periodieke verslagen van bepaalde openbare instellingen voor collectieve belegging met een veranderlijk aantal rechten van deelneming, het KB van 12 november 2012 met betrekking tot de beheervennootschappen van instellingen voor collectieve belegging die voldoen aan de voorwaarden van richtlijn 2009/65/EG, het ICBE-KB, het AICB-KB en houdende diverse bepalingen. / AR du 15 octobre 2018 modifiant l'arrêté royal du 7 mars 2006 relatif aux prêts de titres par certains organismes de placement collectif, l'arrêté royal du 10 novembre 2006 relatif à la comptabilité, aux comptes annuels et aux rapports périodiques de certains organismes de placement collectif publics à nombre variable de parts, l'arrêté royal du 12 novembre 2012 relatif aux sociétés de gestion d'organismes de placement collectif qui répondent aux conditions de la directive 2009/65/CE, l'arrêté royal du 12 novembre 2012 relatif aux organismes de placement collectif qui répondent aux conditions de la Directive 2009/65/CE et l'arrêté royal du 25 février 2017 relatif à certains organismes de placement collectif alternatifs publics et à leurs sociétés de gestion, et portant des dispositions diverses.

- information obligations:
    - the prospectus of the CIS should contain information about the liquidity tool(s) that can be used;
    - the periodic reports of the CIS have to contain certain elements ;
    - the articles of association/fund rules
        - have to provide for the possibility to use redemption gates
        - may not contain information that inhibits the use of swing pricing
        - anti-dilution levy: the information about the description, the calculation way and rate of costs has to take into account the possibility to use anti-dilution levy ;
    - in case of the use of redemption gates, specific information obligations exist towards investors (individual information towards each investor + publication on website) + NCA;
    - the marketing materials need to inform the investors about the use of the liquidity tools.

IX. Main attention points of the NBB related to the 31 December 2018 audit[3]

a) Banks and investment firms

- Signal function: At the start of an on-site mission, on-site inspectors generally contact the accredited auditor. Based on the experience of on-site inspectors it seems that this can be very useful. However in some cases it seems the accredited auditors are aware of deficiencies that are detected during an on-site mission but that they failed to inform us on these shortcomings.
- PSD II: the introduction of PSD II has led and leads to numerous new requirements in terms of reporting, organization, operational- and security practices. Accredited auditors should be aware of these new requirements and identify areas where, based on their audit work, they identify shortcoming in meeting these new requirements.
- Review of the RWA calculator: it is expected that the accredited auditor checks whether the outputs of the IRB models (PD,LGD,EAD) are correctly translated into RWA numbers reported in the COREP tables.
- Difference between the accounting IFRS consolidation perimeter and the CRD prudential perimeter: it is expected that there is a clear understanding and verification of the difference between the accounting consolidation perimeter and the CRD perimeters.
- Update implementation of IFRS9 standards:
    - It would be interesting to know to what extent banks have integrated IFRS 9 in their business as usual practices (compared to a project approach)
    - In case the institution relies on regulatory IRB models in (parts of) its ECL calculation, has the institution documented the following:
        - Rationale that the IRB models and their underlying assumptions satisfy the IFRS9 requirements
        - The rationale for changes to IRB models in case there were changes to IRB models, before applying these models for IFRS9 purposes

[3] Attention points provided by the NBB.

- Assessment of the potential impact due to the fact that there are no floors for PD/LGD values applicable under IFRS9. Such floors (e.g. 10%/15% LGD floor for loans guaranteed by residential/commercial property; 3bp PD floor for retail exposures) are however applicable under the Basel regulatory framework.

- Digitalisation costs: How are these generally treated in accounting, as an expense or capitalized?

b) <u>Insurance companies</u>

In April 2017, the NBB issued the Circular 2017_14 introducing some new – yet broad – guidelines on the use of the loss-absorbing capacity of deferred taxes.
In February 2018, EIOPA published its second set of advice to the European Commission on specific items in the Solvency II Delegated Regulation; a chapter is dedicated to the loss-absorbing capacity of deferred taxes and consists of key principles to be considered for the projection of likely future profits. The NBB recommends the insurance undertakings to already take into account those principles that will be introduced in the delegated regulation and to further enhance the information for supervisors and public disclosure in accordance.

In this context, regarding the DTA-DTL position in the SII Balance sheet, information must be collected and available on the origin of DTA-DTL (which assets generate DTA or DTL and in the same way, which liabilities generate DTA or DTL) and the NBB expects the accredited auditors to check that sufficient granularity is applied to take into consideration the different fiscal regimes applicable to the different items of the balance sheet. In addition, the possibility to compensate DTA-DTL in the same period should be challenged. The NBB also expects the accredited auditors to check that the recoverability test developed to justify a positive amount of DTA in the SII balance sheet relies on the principle that no profit already taken into account in the Solvency II balance sheet could be used to justify the DTA. Furthermore, specific attention should be given to:

- the numbers of years over which new business sales are projected,
- the time horizon over which profits emerging from that new business are projected,
- the profits assumed for new business and its comparison with past average profit,
- the rate of return used for future investments supporting technical provisions and the rate of return of other assets,
- the tax rate applied.

Regarding the LAC DT, in addition to the principles and attention points mentioned above for the justification of DTA, auditors should focus on the sources used to justify likely utilization of LAC DT, with a justification of the effect of each source (e.g. amount justified with DTL pre-stress, amount justified with DTL post-stress, amount justified with future profits). For the amount to be justified with future profits, auditors must be aware that the assumptions applied cannot be more favorable than the assumption applied for the justification of DTA, even if some management actions could be accepted in specific conditions and that profits already used to justify DTA in the Solvency II balance sheet before shock cannot be used again for the justification of the notional DTA (avoidance of double counting).

Finally, as the consideration of the reversal of the risk margin is still a controversial topic that will be discussed in the future at NBB and at European levels, auditors are recommended to be prudent in the recognition of this element.

Sensitivity analyses, regarding the assumptions used to demonstrate likely utilization of both deferred tax assets in the pre-stress situation and LAC DT, should assess the impact of changes in the assumptions on the solvency position of the undertaking and a summary of those should be provided.

The NBB also expects the accredited auditors to review the methodologies and documentation developed by the insurance undertakings and to report any relevant issue.

c) Payment institutions and electronic money institutions

The Payment Services Directive 2 imposes the obligation for the statutory auditors to report on outsourcing. More specifically the auditors will have to check whether the institutions are still in control of the outsourced activities and if they are able to be compliant with all the rules that are applicable on the institutions under PSD2. This because of the fact that the outsourced activities fall under the responsibility of the institutions. to the NBB also draws attention to the fact that the reporting on outsourcing should be based on circular 2004/5 of the National Bank of Belgium. New guidelines on outsourcing are expected next year.

We also recommend to the auditors of payment institutions and electronic money institutions to follow-up on the points of attention that were derived from the analysis of the institutions' grandfathering file. These points of attention were included in the re-licensing under PSD2.

d) IFRS9, Financial Instruments (credit Institutions)

As already highlighted in the notice 2018-6, a proper and robust implementation of IFRS9 is a key attention point for the audit of end of year financial statements and prudential returns.

Accredited auditors are expected to report attention points regarding the application of IFRS9 that would be relevant from a prudential perspective in the context of their review as of 31 December 2018. The list of attention points mentioned in the notice 2018-6 remains relevant (with necessary adaptation to fit with the end of year reporting). As indicated in this notice, the list should not be considered exhaustive; nor should it be considered as a check list. Accredited auditors are expected to apply their professional judgement for identifying and reporting to the NBB all relevant issues emerging from their review of the credit institution's supervisory reporting.

The NBB expects all credit institutions to comply with its circular letter (NBB_2017_26) that implemented in Belgium the EBA Guidelines on credit institutions' credit risk management practices and accounting for expected credit losses. Accredited auditors are therefore expected to also consider these guidelines in their audit of IFRS9 numbers and to report to the NBB any material misapplication of these guidelines.

More recently, the following issues emerged that may warrant particular attention from the accredited auditors:

- Robustness of internal governance arrangements around model developments (post implementation fine-tuning and adaptation) and continuous validation. Processes in place and documentation for the application of overlays.
- Data quality and update of data to swiftly reflecting evolving economic conditions
- Appropriate calibration of models, assumptions and parameters so as to ensure that the staging of assets and the ECL calculations reflect early enough the collective and individual

impact on credit risk of expected deteriorations of the economic conditions (integration of forward looking information).

- Challenge of possible management bias regarding the consideration of forward looking and macro-economic information. Challenge of management overuse of thresholds and simplified solutions that may delay the recognition of lifetime ECL or lead to underestimated ECL provisions.
- Where relevant, processes in place for and documentation of the adjustments made by the banks that rely on IRB regulatory models for their IFRS9 ECL calculations.

Acronyms	
AICB	Alternative Undertakings for Collective Investments
AIFMD	Alternative Investment Fund Managers Directive
AML/CTF	Anti-Money Laundering Legislation
APM	Alternative Performance Measures
CIS	Collective Investment Schemes
CIU	Collective Investment Undertakings
COREP	Common Reporting
CRD	Capital Requirements Directive
DTA	Deferred Tax Assets
DTL	Deferred Tax Liabilities
EAD	Exposure at Default
EBA	European Banking Authority
ECB	European Central Bank
ECL	Expected Credit Loss
EIOPA	European Insurance and Occupational Pensions Authority
ESG	Economic Scenario Generator
FSMA	Financial Services and Markets Authority
GDPR	General Data Protection Regulation
ICAAP	Internal Capital Adequacy Assessment Processes
ICB	**NL**: Instelling voor Collectieve Belegging Undertakings for Collective Investment (UCI)
IFRIC	IFRS Interpretation Committee
IFRS	International Financial Reporting Standards
ILAAP	Internal Liquidity Adequacy Assessment Processes
IORP	Institutions for Occupational Retirement Provision
IPC	Irrevocable Payment Committee
IRAIF/IREFI	**FR**: Institut des Réviseurs Agréés pour les Institutions Financières **NL**: Instituut van de Revisoren Erkend voor de Financiële Instellingen
IRB	Internal Ratings Based
LAC DT	Loss Absorbing Capacity and Deferred Tax
LGD	Loss Given Default
LPC/WAP	Law of 28 April 2003 on Supplementary Pensions
MiFID	Markets in Financial Instruments Directive (2014/65/EU)
MMF	Money Market Funds
NBB	National Bank of Belgium
NPL	Non-Performing Loans
OPC	**FR**: Organisme de Placement Collectif Undertakings for Collective Investment (UCI)
ORA	Own-Risk Assesment
PD	Probability of Default
PSD	Payment Services Directive
QRT	Quantitative Reporting Templates
RWA	Risk Weighted Asset
SPPI	Solely Payment of Principal and Interest
SRB	Single Resolution Board

SREP	Supervisory Review and Evaluation Process
SRF	Single Resolution Fund
SSM	Single Supervisory Mechanism
TRIM	Targeted Review of Internal Models
UCI	Undertakings for Collective Investment
UCITS	Undertakings for Collective Investment in Transferable Securities