Brussels, 28 June 2023

NOTICE TO THE ACCREDITED AUDITORS
NOTICE 2023 / 05

Dear members,

We hereby provide you with the overview of the attention points that could influence your review procedures as of 30 June 2023. These attention points have been compiled in the context of the current legal and regulatory framework of cooperation of the accredited auditors to the prudential supervision by the FSMA and the NBB.

The supervisory authorities and the different IRAIF/IREFI working groups, supported by the scientific secretariat, have contributed to this letter, by providing and drafting the enclosed attention points.

Today, a Capita Selecta session was organized in close cooperation with the FSMA and the NBB, detailing some of the topics mentioned in the attached letter. The slides of this training are available on the ICCI portal (Past events (icci.be)).

The IRAIF/IREFI working group dealing with the model reports has finalized the templates for prudential reporting as of 30 June 2023 to the NBB and the FSMA. The updated versions will be communicated shortly.

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

Yours sincerely,

Olivier Macq
President

Institut des Réviseurs Agréés
pour les Institutions Financières ASBL
Institut Royal
ASBL agréée comme union professionnelle

Instituut van de Revisoren Erkend
voor de Financiële Instellingen VZW
Koninklijk Instituut
VZW erkend als beroepsvereniging

Bld E. Jacqmainlaan 135/1 – Brussel B-1000 Bruxelles – Tel. 02/512.51.36 – Fax. 02/512.78.86

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INTRODUCTION

The attention items presented in *italics* have been provided by the supervisory authorities (National Bank of Belgium (NBB) or the FSMA) and include their expectations with regard to the auditor's specific attention points in the context of the 30 June 2023 review procedures and the reporting thereon.

The other attention points have been identified by the respective working groups of the IRAIF/IREFI and consist of items for information of the accredited auditors. Some of these items relate to topics that were already discussed in a previous attention points letter. The accredited auditors will use their professional judgment and decide, based on facts and circumstances, whether these attention points need to be explicitly addressed in the reports to the prudential authorities.

1. ATTENTION MATTERS APPLICABLE TO ALL FINANCIAL INSTITUTIONS

1.1. REPORTING DEADLINES

Accredited auditors are requested to notify the prudential authorities of any significant delay in their reporting.

This notification should be done by e-mail or telephone call and addressed to the contact person within the NBB or the FSMA responsible for the respective financial institution, mentioning (i) the delay, (ii) the reason for the delay and the proposed remediation plan and (iii) the expected date of completion and sending of the reporting.

When the delay is entirely due to the financial institution, the NBB expects that these issues are taken up in the report of the accredited auditors on the internal control measures taken by senior management and that an adequate remediation plan and timing for resolution is taken up in that report.

1.2. COMMUNICATION OF MODIFICATIONS TO THE NBB AND THE FSMA

Accredited auditors and accredited audit firms are reminded of the obligation to notify the prudential authorities of all relevant modifications with respect to their accreditation conditions and personal file without any delay.

This obligation is mentioned in the respective accreditation regulations of the NBB and the FSMA:

- NBB: articles 5 and 14 of the accreditation regulation of 21 December 2012
- FSMA: articles 4 and 11 of the accreditation regulation of 14 May 2013

The notifications relate to, among others, (i) the transfer of an accredited auditor to another audit firm, (ii) the organizational changes or the changes to the name of an audit firm, (iii) the temporary or final ceasing of the activities of the accredited auditor, (iv) the minimum number of 2 accredited auditors for the same accreditation within an audit firm, (v) *(FSMA only)* the reason for not being able to attend the permanent training, etc.

These modifications need to be notified as soon as possible, and preferably before the modification takes place, to:

- NBB: supolaudit@nbb.be
- FSMA: eca@fsma.be

It is highly recommended to also inform the contact person(s) responsible for the financial institution(s) on which the accredited auditor is working about these modifications.

1.3. CSRD, THE NON-FINANCIAL INFORMATION DISCLOSURES REQUIREMENTS

On 5 January 2023, the Corporate Sustainability Reporting Directive (CSRD) entered into force, modernizing and strengthening the rules concerning the social and environmental information that companies have to report.

The companies will have to apply the new rules:

- as from 1 January 2024 (first reports in 2025) for companies that are already within the scope of the NFRD;
- as from 1 January 2025 (first reports in 2026) for other large companies;
- as from 1 January 2026 (first reports in 2027) for listed SMEs; and
- as from 1 January 2028 (first reports in 2029) for non-EU companies with branches/subsidiaries.

No specific intervention of the accredited auditors is expected in the context of the 30 June 2023 review procedures.

However, in view of the upcoming deadlines of the CSRD and the nature of the deliverables, accredited auditors are encouraged to inquire, in the context of the year-end audit procedures, with the institution’s senior management about (i) the specific requirements and timing applicable to the institution and (ii) the concrete project management set-up, timeline and deliverables.

2. CREDIT INSTITUTIONS

2.1. THE IMPACT OF THE CHANGING METRICS ON THE CREDIT INSTITUTIONS

Given the rapid increase of interest rates by Central Banks in the past quarters and the changed macro-economic environment with high inflation and low economic growth (within the context of the aftermath of the Covid-19 pandemic and the consequences of the invasion of Ukraine by Russia), we recommend the accredited auditors to take into consideration the risks to which the financial sector is exposed, in particular related to interest rate risk, liquidity risk and credit risk. The elevated risk levels for banks were demonstrated during the first semester of 2023, by the collapse of a number of regional banks in the United States of America and the events in Switzerland related to Credit Suisse.

Specific attention should be put on the adequate identification, measurement and reporting of risks in the financial and prudential periodic reporting as of 30 June 2023. The following elements should be considered:

- Management of interest rate risk within an ALM context and the related hedge positions from an accounting and economical perspective;
- Management of liquidity risk within a competitive environment for higher interest rates on saving products, a high focus on reputational risk and more digital banking interactions;
- Management of credit risk within a context of low economical growth and volatile macro-economic indicators, such as inflation levels and energy prices. Specific focus should be put on:
    - the governance and the evolutions of the overlays recorded by the institutions to capture the ECL not picked up by the current models, including the evolution of the overlays that were previously recorded to cover the increased expected credit losses;
    - specific measures (if any) granted by the financial institutions in the context of the current challenges, and their consequences on the staging; and
    - the back-testing process implemented by the institutions and the related results, the scenarios used in the expected credit loss and any specific sector approaches that would be applied.

We furthermore refer to section 2.2 below for the attention points of the NBB and the reporting requirements in relation to these attention points.

2.2. US BANKS RECENT BANKRUPTCIES AND THE IMPACTS ON EU CREDIT INSTITUTIONS

At the beginning of March 2023, the bankruptcy of a few US banks, characterized by specific business models as well as governance and risk management issues, created contagion effect on the US banking sector and, in combination with the Credit Suisse event, on European banks' CDS and equity prices. This highlighted that even fragile market sentiment about the robustness of credit institutions can very quickly create bank runs and significant contagion effect on the stability of the financial system as a whole. In line with the Basel Committee's review and discussion of recent market developments on 23 March and 6 June 2023, the National Bank of Belgium emphasizes the importance of strengthening the effectiveness of supervision by ensuring that credit institutions' risk management practices and governance arrangements are robust and that weaknesses in banking practices are effectively identified and promptly corrected.

The accredited auditors are therefore expected to pay special attention during their review as of 30 June 2023 and to report to the Bank, if relevant, any problems and issues concerning the credit institutions' risk management practices and governance arrangements. It is particularly important to identify the challenges that credit institutions are facing in their risk management in the current economic environment characterized by increased inflation, rising interest rates and geopolitical uncertainty, especially in terms of liquidity, interest rate risks and the hedging of emerging risks.

Therefore, special attention should be granted, from an accredited auditor's perspective, to the implementation by credit institutions of matters listed below in an exemplative and not limitative list, on the basis of inquiries: adequate diversification of funding to avoid material deposit outflows, adequate amount of liquid assets that can actually be sold without significant losses in stress periods, adequate measurement and management of interest rate risk in the banking book, including conservative hypotheses regarding the deposit outflow behavior and the prepayment risk, appropriate hedging strategies with adequate instruments and sensitivities, adequate strategies in terms of AT1 capital, efficient identification of facilities exposed to problematic counterparties, including through derivatives …

Further as already indicated in previous Attention Points' Letters, the strengthening of the resilience of credit institutions to macro-financial and geopolitical shocks and more specifically the credit risk management including exposures to vulnerable sectors and related IFRS 9 implications remain high on the agenda of the Bank.

If applicable, the accredited auditor will make use of the early warning function in case of significant issues.

3. INSURANCE SECTOR

3.1. IMPLICATIONS OF RISING INTEREST RATES FOR INSURERS

The risks posed by the low interest rate environment have long been the focus of supervisory activities. Having recently risen significantly, interest rates can have a positive effect on insurer's profitability and/or solvency. However, if there were to be an additional significant interest rate increase or if the scenario of an inversion of the yield curve were to persist, this could pose high risks for insurance undertakings that are particularly exposed due to their (long-term) business and investment policy and that have not taken adequate countermeasures. These risks include among others attractiveness of product offer, lapse risk, adaptation of asset-liability management and/or hedging constructions, liquidity issues, ...

Changing interest rates also affect insurers through market valuation effects: accredited auditors are expected to pay special attention to the valuation aspects and in particular to the items on both sides of the balance sheet valued through mark-to-model or alternative valuation methods (an adequate review of the parameters, linked to the current market conditions, might be in order) in the context of the 30 June 2023 review procedures.

3.2. CIRCULAR NBB_2022_27 ON THE VALUATION OF DTA AND THE ADJUSTMENT FOR LAC DT

We would like to remind the accreditor auditors of the circular NBB_2022_27 on the valuation of deferred tax assets (DTA) and the adjustment for the loss-absorbing capacity of deferred taxes (LAC DT), that will enter into force for the first time to the SCR calculation as of 31 December 2023.

This circular does not only clarify certain concepts and principles of article 207 of the Delegated Regulation 2015/35 on the adjustment for the loss-absorbing capacity of deferred taxes, it also introduces proportionality.

Accredited auditors are recommended to discuss with management, in the context of the year-end audit procedures, the expected impact of the application of this circular on the SCR calculation of the undertaking.

3.3. IFRS 17

IFRS 17 Insurance Contracts is an International Financial Reporting Standard that was issued by the International Accounting Standards Board in May 2017. As of 1 January 2023, IFRS 17 replaced IFRS 4 on accounting for insurance contracts.

As a reminder, IFRS 4 gave insurance companies the possibility to value their insurance liabilities at book value in line with their statutory accounts, except for the accounting of some general provisions. Under IFRS 17, the valuation of the insurance liabilities is to a much greater extent based on the current value and new concepts, like the contractual service margin (CSM) and risk adjustment, were introduced. The valuation principles under IFRS 17 are however not identical to an economic valuation (or a Solvency II valuation), which insurance companies have to include in their regulatory reporting. As a result, valuation differences will remain between the statutory, IFRS and Solvency II reporting of insurance companies.

IFRS 17 is a complex reporting standard and insurance companies that are required to prepare consolidated financial statements are struggling with the implementation and timely reporting under this standard: data flows, IT systems, processes and controls had to be revised and resulted in an increased workload for staff and management of insurance companies. Also, the interpretation and analysis of net results under this new standard turned out to be more difficult than expected.

As the implementation of IFRS 17 impacts to a large extent the whole control environment of insurance companies that are preparing consolidated financial statements, accredited auditors should closely monitor this process and its consequences on their audit approach.

3.4. ROYAL DECREE OF 27 SEPTEMBER 2009 ON THE CONSOLIDATED ACCOUNTS OF INSURERS

The Royal Decree of 27 September 2009 on the consolidated accounts of insurance and reinsurance undertakings has been repealed and replaced by the new Royal Decree of 16 April 2023.

This new Royal Decree not only includes updates with respect to the amended legislative and regulatory framework. It also removes the double condition previously applicable to the exemption of sub-consolidation, namely the requirement that the parent company needed to be an insurance or reinsurance undertaking and guaranteed the liabilities of the exempted company.

The new Royal Decree entered into force directly, for accounting years starting as from 1 January 2023 onwards.

4. Regulated real estate investment companies (GVV – SIR)

4.1. The impact of the current economic climate

In view of the current economic climate and in particular the increasing interest rates, the accredited auditors are expected to give due consideration to the impact thereof on valuation of real estate, impairment testing, financing and the risks associated with financial instruments.

Acronyms	
AICB	Alternative Undertakings for Collective Investments
AIFMD	Alternative Investment Fund Managers Directive
AML/CTF	Anti-Money Laundering Legislation
APM	Alternative Performance Measures
BE GAAP	Belgian Generally Accepted Accounting Principles
CET1	Common Equity Tier 1
CIS	Collective Investment Schemes
CIU	Collective Investment Undertakings
COREP	Common Reporting
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation
CSRD	Corporate Sustainability Reporting 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
EER/EEE	**NL:** Europese Economische Ruimte **FR:** Espace Economique Européen
EIOPA	European Insurance and Occupational Pensions Authority
ESG	Environmental, social and governance
FINREP	Financial Reporting (templates requested by the ECB)
FSMA	Financial Services and Markets Authority

GDPR	General Data Protection Regulation
GVV	Gereglementeerde Vastgoed Vennootschap
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
IRRBB	Interest Rate Risk in the Banking Book
LAC DT	Loss Absorbing Capacity of Deferred Taxes
LGD	Loss Given Default
LPC/WAP	Law of 28 April 2003 on Supplementary Pensions
LSI	Less Significant Institution
LTRO	Long-Term Refinancing Operation
MiFID	Markets in Financial Instruments Directive (2014/65/EU)
MMF	Money Market Funds
NAV	Net Asset Value
NBB	National Bank of Belgium
NFRD	Non-Financial Reporting Directive
NPL	Non-Performing Loans
OPC	**FR**: Organisme de Placement Collectif (Undertakings for Collective Investment (UCI))

ORA	Own-Risk Assessment
P2G	Pillar 2 Guidance
PD	Probability of Default
PSD	Payment Services Directive
QRT	Quantitative Reporting Templates
REIT	Real Estate Investment Trust (see also GVV and SIR)
RICS	Royal Institute of Chartered Surveyors
RSR	Regulatory Supervisory Report
RWA	Risk Weighted Asset
SCR	Solvency Capital Requirement
SFCR	Solvency and Financial Condition Report
SI	Significant Institution
SICR	Significant Increase in Credit Risk
SIR	Société Immobilière Réglementée
SME	small and medium-sized enterprises
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
TCWG	Those Charged With Governance
TLTRO	Targeted Longer-Term Refinancing Operations
TRIM	Targeted Review of Internal Models
UCI	Undertakings for Collective Investment
UCITS	Undertakings for Collective Investment in Transferable Securities