



Audit Obligations

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AUDIT OBLIGATIONS UNDER PART V OF THE RESERVE BANK OF NEW ZEALAND ACT 1989

Introduction

1. Under the Reserve Bank of New Zealand Act 1989 (the “Act”), the Reserve Bank of New Zealand (the “Bank”) is empowered to register and supervise banks for the purposes of:
 - (a) promoting the maintenance of a sound and efficient financial system;
 - (b) avoiding significant damage to the financial system that could result from the failure of registered bank.
2. To assist in achieving these objectives, the Act permits the Bank to recommend the establishment, by way of Order in Council, of disclosure arrangements for registered banks.
3. This document identifies the obligations of auditors under the Bank’s disclosure regime, as well as the other statutory obligations of auditors under Part V of the Act, and directs auditors to appropriate sources of guidance on fulfilling these obligations.

Audit Requirements of the Disclosure Regime for Registered Banks

4. The requirements implementing the disclosure regime are contained in four Orders in Council (or “Orders”). These Orders, along with some accompanying explanatory information, are included in the Banking Supervision Handbook issued by the Bank. The Orders require certain information to be disclosed in documents called disclosure statements, and to be reported on by an external auditor. The next sections briefly describe those disclosure documents and their associated audit requirements.

Disclosure Documents

5. Registered banks are required to publish disclosure statements at quarterly intervals - a full disclosure statement for the financial year and the half year, plus a truncated or “short form” disclosure statement for the first and third quarters (or “off quarters”) of the financial year. In this pattern, the four Orders implementing the disclosure regime relate firstly to the full and half year disclosure requirements, and secondly to the off quarter disclosure requirements, for locally incorporated banks and overseas incorporated banks respectively.
6. The full disclosure statement consists of two main parts: a Key Information Summary, and a General Disclosure Statement. Additionally, a Supplemental Disclosure Statement must be published if certain information is not already contained in the General Disclosure Statement. Because the disclosure requirements applying to the first

and third quarters of the financial year are abbreviated, a disclosure statement relating to either of those periods is called a Short Form Disclosure Statement. The Short Form Disclosure Statement comprises a Key Information Summary, a General Short Form Disclosure Statement, and where necessary a Supplemental Disclosure Statement.

7. The General Disclosure Statement and the General Short Form Disclosure Statement are the substantive disclosure documents, and are aimed at those who wish to obtain comprehensive corporate, financial and risk-related information on a bank and its banking group. In contrast, the Key Information Summary contains a brief summary of key information on a registered bank's financial position and risk profile, and is principally targeted at the prudent, but non-expert, investor.
8. The kinds of information contained in the full and half year disclosure statements are described below:

(a) **The General Disclosure Statement:**

- (i) **General Disclosures:** includes details of matters such as guarantee arrangements, directorate and auditors, conditions of registration, pending proceedings and arbitration, credit ratings, historical summary of financial statements, members of the banking group, auditor's report, the directors' statement and, in the case of an overseas incorporated bank, the New Zealand chief executive officer's statement.
 - (ii) **Financial Statements:** of the registered bank and the banking group prepared in accordance with the requirements of the Financial Reporting Act 1993, as though the references in the Financial Reporting Act 1993 to a "group" were to the banking group. These statements should be prepared as though the registered bank does not qualify for any exemptions pursuant to any differential reporting framework that would otherwise be applicable. The half yearly financial statements are treated on the same basis as the full year financial statements. That is, Generally Accepted Accounting Practice applies as if the half year were an annual balance date.
 - (iii) **Supplementary Information:** includes supplementary financial disclosures, information relating to asset quality, capital adequacy of the registered bank and the banking group, concentration of credit exposures, credit exposures to connected persons (where applicable), securitisation, funds management and other fiduciary activities, risk management policies, and market risk.
- (b) **Key Information Summary:** a short summary of key information mainly drawn from the General Disclosure Statement, including: corporate information, credit ratings, profitability, size, capital adequacy, asset quality, credit exposure concentrations, credit exposures to connected persons (where applicable), and an auditor's report.

- (c) **Supplemental Disclosure Statement:** includes detailed information on guarantors and guarantee contracts. Overseas incorporated banks are also required to include financial statements for the overseas banking group and, if they conduct insurance or non-financial business in New Zealand outside the banking group, to include copies of financial statements and group financial statements for each of those businesses. Locally incorporated banks which have calculated their aggregate credit exposure to connected persons on a net basis must include a copy of the relevant bilateral netting agreement and, if the netting agreement is not an industry standard one, must also include a copy of advice from an independent third party expert validating the robustness of the agreement. Locally incorporated banks that have adopted an internal models-based approach to credit risk or operational risk (or both) under the Basel II capital adequacy framework must include a description of those approaches, and a discussion of the control mechanisms surrounding any internal credit risk rating systems. If the required disclosures are contained in the General Disclosure Statement, a Supplemental Disclosure Statement is not required.
9. The requirements applying to the off quarter Key Information Summaries and Supplemental Disclosure Statements are similar to those which apply at the full and half year periods. However, General Short Form Disclosure Statements contain abbreviated general disclosures, as well as short form financial statement disclosures, and focus mainly on banking group information, rather than both group and legal entity information as is required for full and half year General Disclosure Statements.

Conditions of Registration

10. The Orders require registered banks to disclose financial information on compliance with their conditions of registration – including in respect of capital adequacy requirements, and in respect of compliance with limits on exposures to connected persons (these conditions apply to locally incorporated banks only). The Banking Supervision Handbook contains three documents making up the capital adequacy framework (“Capital adequacy framework (Basel I approach)” (BS2), “Capital adequacy framework (standardised approach)” (BS2A), and “Capital adequacy framework (internal models based approach)” (BS2B)) which provide detailed information on capital adequacy requirements applied to locally incorporated banks as a condition of registration. Although the capital adequacy framework documents do not act as a basis for applying conditions of registration to overseas incorporated banks, the Orders do require banks incorporated overseas to disclose information on the risk-weighted exposures and market risk exposures arising from their New Zealand business, and that information must be derived in accordance with BS2 (for risk-weighted exposures) and BS2A (for market risk exposures).

Description of Audit Requirements

11. Registered banks are required to obtain a full external audit of the financial information and supplementary financial information published in the full year disclosure statement (with one exception), and a limited scope external review of the same kinds of information published in the half yearly disclosure statement. The one exception to the

full external audit requirement at the full year arises with the supplementary information on capital adequacy published by locally-incorporated banks, which is subject to a limited scope external review, as for the half year disclosure statement.

12. No specific audit requirements apply at the off quarters, and, in part for this reason, the disclosure statements relating to those periods must be published no later than two months following the off quarter balance date (in contrast to the three month publication period which applies to the full and half year quarter disclosure statements). However, an exception to the two month limit is provided for an off quarter disclosure statement, if a registered bank elects to obtain a full audit or a limited scope review of the financial information contained in the disclosure statement. Provided that the extent of the audit is not less than that which would have been required during either of the on quarters, a three month publication period applies.
13. An aspect of electing to obtain an audit or review during the off quarters relates to compliance with the Bank's capital adequacy requirements – unaudited retained earnings form part of Upper Tier Two Capital, whereas retained earnings which have been subject to audit or review are contained within Tier One Capital.
14. The audit requirements of the disclosure regime are described in more detail below. This description is intended only as a guide, and auditors should refer to the Orders for the exact requirements, and in particular, to clause 19 and Schedule 1 of the full and half year Orders; to Schedule 1 (clause 11) and Schedule 2 (clause 15) of the off-quarter Orders for New Zealand-incorporated banks; and to Schedule 1 (clause 13) and Schedule 2 (clause 20) of the off-quarter Orders for overseas-incorporated banks.
15. It should be noted that the disclosure regime does not exempt auditors from any other requirements that might be imposed on them under the Companies Act 1993 or the Financial Reporting Act 1993.

Audit of the Full Year Disclosure Statements

16. The auditor's report on the information contained in full year disclosure statements is required to contain statements on the following matters:
 - (a) **General Requirements:** For all financial and supplementary information prepared in accordance with the Orders, the general reporting requirements are similar to those which apply under section 16 of the Financial Reporting Act 1993. These requirements are set out in Schedule 1 of the full and half year Orders, and relate to the work done by the auditor, the scope and limitations of the audit, the nature of the auditor's relationship with the registered bank and the members of the banking group, whether proper accounting records have been kept, and whether the auditor has obtained all information and explanations required.
 - (b) **Financial statements:** The auditor must give an opinion as to whether the annual financial statements of the registered bank and the banking group included in the registered bank's disclosure statement:

- (i) comply with generally accepted accounting practice and, if they do not, the respects in which they fail to comply; and
 - (ii) having regard to any information or explanations that may have been added, give a true and fair view of the matters to which they relate and, if they do not, the respects in which they fail to give such a view.
- (c) **Supplementary information:** The auditor is required to give an opinion as to whether the supplementary information on the registered bank and the banking group included in the registered bank's disclosure statement:
- (i) has been prepared in accordance with guidelines issued under section 78(3) of the Reserve Bank of New Zealand Act (if any) or any conditions of registration imposed under section 74 of the Act; and
 - (ii) is in accordance with the books and records of the registered bank and banking group.

The auditor is also required to give an opinion as to whether:

- (iii) the supplementary information other than that relating to capital adequacy fairly states the matters to which it relates in accordance with the relevant requirements in the Orders, and, if it does not, the respects in which it fails to do so;

Additionally, for New Zealand incorporated banks the auditor's report is required to state:

- (iv) that the supplementary information relating to capital adequacy has been examined by the auditor; and
- (v) whether anything has come to the auditor's attention which would cause the auditor to believe that the information on capital adequacy is not in all material respects derived in accordance with the bank's conditions of registration, and in accordance with the bank's internal models for credit risk and/or operational risk if applicable, and disclosed in accordance with Schedule 5, 5A or 5B as applicable, in the Order applying to New Zealand-incorporated banks.

And for overseas incorporated banks, the auditor is required to give an opinion as to whether:

- (vi) the supplementary information relating to credit and market risk exposures and capital adequacy is in all material respects derived in accordance with Banking Supervision Handbook documents BS2 and BS2A, and is disclosed in accordance with Schedule 5 of the Order applying to overseas-incorporated banks.

17. The appropriate standards and guidance for auditors engaged to express an audit opinion in accordance with the audit requirements of the Orders are contained in the auditing standards and guidelines issued by the Institute of Chartered Accountants of New Zealand. Additionally, auditors are referred to the Market Risk Guidance Notes (BS6) contained in the Banking Supervision Handbook for guidance on the market risk disclosure requirements contained in the full and half year Orders (in Schedule 5A or 5B, as applicable, in the Order applying to New Zealand-incorporated banks, and in Schedule 5 in the Order applying to overseas-incorporated banks).

Review of Half Year Disclosure Statements

18. Registered banks are required to obtain a review by an external auditor of the financial statements and supplementary information contained in the half-year disclosure statements, unless they have obtained an audit opinion on this information. The requirements with respect to the half year review are:
- (a) **Financial statements:** The auditor is required to undertake a review of the half year financial statements included in the registered bank's disclosure statement and prepare a report stating:
 - (i) that the financial statements have been examined by the auditor; and
 - (ii) whether anything has come to the auditor's attention which would cause the auditor to believe that the financial statements do not present a true and fair view of the matters to which they relate.
 - (b) **Supplementary information not relating to capital adequacy:** The auditor's report is required to state:
 - (i) that the supplementary information has been examined by the auditor; and
 - (ii) whether anything has come to the auditor's attention which would cause the auditor to believe that the supplementary information does not fairly state the matters to which it relates in accordance with the relevant requirements in the Orders.
 - (c) **Supplementary information relating to capital adequacy:** For New Zealand incorporated banks, the auditor's report is required to state:
 - (i) that the supplementary information relating to capital adequacy has been examined by the auditor; and
 - (ii) whether anything has come to the auditor's attention which would cause the auditor to believe that the supplementary information is not in all material respects derived in accordance with the bank's conditions of registration, and in accordance with the bank's internal models for credit risk and/or operational risk if applicable, and disclosed in accordance

with Schedule 5, 5A or 5B as applicable, in the Order applying to New Zealand-incorporated banks.

For overseas incorporated banks, the auditor's report is required to state:

- (iii) that the supplementary information relating to credit and market risk exposures and capital adequacy has been examined by the auditor; and
 - (iv) whether anything has come to the auditor's attention which would cause the auditor to believe that the supplementary information is not in all material respects derived in accordance with Banking Supervision Handbook documents BS2 and BS2A, and disclosed in accordance with Schedule 5 of the Order applying to overseas-incorporated banks.
19. The audit opinion on the half year information is of a negative assurance form. The appropriate standards and guidance for auditors engaged to give a negative assurance opinion in order to fulfil the review requirements of the Orders are contained in the review engagement standards and guidelines issued by the Institute of Chartered Accountants of New Zealand. Additionally, auditors are referred to the Market Risk Guidance Notes (BS6) contained in the Banking Supervision Handbook for guidance on the market risk disclosure requirements contained in the full and half year Orders (in Schedule 5A or 5B, as applicable, in the Order applying to New Zealand-incorporated banks, and in Schedule 5 in the Order applying to overseas-incorporated banks).

Auditor's Report on Key Information Summary

20. The Key Information Summary relating to the full and half-year reporting periods is required to contain an auditor's report which states:
- (a) that the Key Information Summary has been examined by the auditor;
 - (b) whether the Key Information Summary has been completed in accordance with the relevant Order in Council and whether the information contained in it has been properly taken, where applicable, from the information contained in the registered bank's General Disclosure Statement; and
 - (c) the nature of the audit examination conducted in respect of information drawn from the General Disclosure Statement, and whether a qualified or unqualified audit opinion has been given in respect of that information.
21. The auditor's report on the Key Information Summary is required to be set out after the required disclosures and any voluntary disclosures have been made by the registered bank in the Summary.

Other obligations under Part V of the Act

22. Under section 96 of the Act, the auditor of a registered bank is required to disclose to the Bank, after informing the registered bank of an intention to do so (in accordance with section 97 of the Act), information relating to the affairs of that registered bank obtained in the course of holding office as an auditor if, in the auditor's opinion, the information indicates that the bank is in serious financial difficulties, or if the information is likely to assist the Bank in the exercise of its supervision responsibilities. Sections 96 to 98 of the Act are set out in Appendix One.
23. Auditors are protected, under section 98 of the Act, from civil, criminal or disciplinary proceedings brought against an auditor arising from the disclosure, in good faith, of any such information to the Bank.
24. Sections 93 and 94 of the Act also contain provisions which together enable the Bank to obtain audited information or data from registered banks for supervisory purposes.

APPENDIX ONE

AUDITOR OBLIGATIONS UNDER SECTIONS 96 TO 98 OF THE RESERVE BANK OF NEW ZEALAND ACT 1989

- 96. Disclosure of information to Bank by Auditors-** Every person who holds, or at any time has held, office as required by any enactment, as an auditor of a registered bank, shall disclose to the Bank information relating to the affairs of that registered bank obtained in the course of holding that office if, in the opinion of that person,-
- (a) The registered bank is insolvent or is likely to become insolvent or is in serious financial difficulties; and
 - (b) The disclosure of that information is likely to assist, or be relevant to, the exercise by the Bank of its powers under this Part of this Act.
- 97. Auditor to inform registered bank of intention to disclose -** Every auditor shall, before disclosing any information to the Bank under section 96 of this Act, take reasonable steps to inform the registered bank of the intention to disclose the information and the nature of the information.
- 98. Protection of auditors-**
- (1) No civil, criminal, or disciplinary proceedings shall lie against any auditor arising from the disclosure in good faith of information to the Bank pursuant to section 96 of this Act.
 - (2) No tribunal, body, or authority, having jurisdiction in respect of the professional conduct of any auditor shall make any order against, or do any act in relation to, that person in respect of such disclosure.
 - (3) No information received by the Bank pursuant to section 96 of this Act shall be admissible in evidence in any proceedings against the auditor concerned.
 - (4) Nothing in subsection (3) of this section shall limit the admissibility of any information obtained in any other way.