

**Guidelines on communication between competent authorities supervising credit institutions and the statutory auditor(s) and the audit firm(s) carrying out the statutory audit of credit institutions**

**(EBA/GL/2016/05)**

These guidelines specify, in accordance with Article 12(2) of Regulation (EU) No 537/2014, the requirements for the establishment of effective dialogue between competent authorities supervising credit institutions, on the one hand, and statutory auditor(s) and audit firm(s) carrying out the statutory audit of those institutions, on the other hand.

These guidelines enter into force on March 31<sup>st</sup> 2017.

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## Guidelines

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# 1. Compliance and reporting obligations

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## Status of these guidelines

1. This document contains guidelines issued pursuant to Article 16 of Regulation (EU) No 1093/2010<sup>1</sup>. In accordance with Article 16(3) of Regulation (EU) No 1093/2010, competent authorities must make every effort to comply with the guidelines.
2. Guidelines set the EBA view of appropriate supervisory practices within the European System of Financial Supervision or of how Union law should be applied in a particular area. Competent authorities as defined in Article 4(2) of Regulation (EU) No 1093/2010 to whom guidelines apply should comply by incorporating them into their practices as appropriate (e.g. by amending their legal framework or their supervisory processes), including where guidelines are directed primarily at institutions.

## Reporting requirements

3. According to Article 16(3) of Regulation (EU) No 1093/2010, competent authorities must notify the EBA as to whether they comply or intend to comply with these guidelines, or otherwise with reasons for non-compliance, by 09.01.2017. In the absence of any notification by this deadline, competent authorities will be considered by the EBA to be non-compliant. Notifications should be sent by submitting the form available on the EBA website to [compliance@eba.europa.eu](mailto:compliance@eba.europa.eu) with the reference 'EBA/GL/2016/05'. Notifications should be submitted by persons with appropriate authority to report compliance on behalf of their competent authorities. Any change in the status of compliance must also be reported to EBA.
4. Notifications will be published on the EBA website, in line with Article 16(3).

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<sup>1</sup> Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, (OJ L 331, 15.12.2010, p. 12).

## 2. Subject matter, scope of application, addressees and definitions

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### 2.1 Subject matter

5. These guidelines specify, in accordance with Article 12(2) of Regulation (EU) No 537/2014<sup>2</sup>, the requirements for the establishment of effective dialogue between competent authorities supervising credit institutions (hereafter ‘competent authorities’ and ‘credit institutions’, respectively), on the one hand, and statutory auditor(s) and audit firm(s) carrying out the statutory audit of those institutions, on the other hand (hereafter ‘auditors’).
6. The objective of these guidelines is the facilitation of the task of supervision of credit institutions through promotion of effective communication between competent authorities and auditors.

### 2.2 Scope of application

7. These guidelines apply in relation to the communication between competent authorities and auditors in their role of supervising and carrying out, respectively, the statutory audit of those credit institutions.
8. These guidelines refer in particular to the communication between the competent authority and the auditor or group auditor of a credit institution (institution-specific communication, as described in section 5), and to the communication between competent authorities and auditors collectively (collective communication, as described in section 6).
9. These guidelines are without prejudice to the auditor’s ‘duty to report’, set out in Article 63(1) of Directive 2013/36/EU<sup>3</sup> and Article 12(1) of Regulation (EU) No 537/2014.

### 2.3 Addressees

10. These guidelines are addressed to competent authorities as defined in point (i) of Article 4(2) of Regulation (EU) No 1093/2010.

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<sup>2</sup> Regulation (EU) 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC (OJ L 158, 27.5.2014, p. 77).

<sup>3</sup> Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

## 2.4 Definitions

11. Unless otherwise specified, the terms used and defined in Directive 2006/43/EC<sup>4</sup>, Regulation (EU) No 537/2014 and Directive 2013/36/EU have the same meaning in these guidelines. For the purposes of these guidelines, the following definitions apply:

In-depth communication	Communication held in the cases referred to in paragraphs 22 and 23, on a more frequent, formalised and/or documented basis, in order to obtain further insights about a credit institution when a greater supervisory effort is applied or needed.
Material information	Information obtained during the supervision or the statutory audit of a credit institution which could change or influence the assessment or decision of a competent authority or an auditor relying on that information for the purpose of exercising their respective tasks.
Institution-specific information	Information concerning an individual credit institution.
Industry-specific information	Information concerning the credit institution's industry as a whole or a part of that industry.
Knowledgeable individual	A person working for the competent authority or the auditor who has the necessary technical knowledge, skills and experience related to a particular issue under discussion.
Informed individual	A person working for the competent authority or the auditor who has sufficient and up-to-date information on the risk profile, size and complexity of a credit institution's operations and related to a particular issue under discussion.
Empowered individual	A person working for the competent authority or the auditor who has the legal authority to act on behalf of their organisation so as to be able to share information and, where necessary, take appropriate decisions regarding a particular issue under discussion.

<sup>4</sup> Directive 2006/43/EC of the European Parliament and of the Council of 17 May 2006 on statutory audits of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC and repealing Council Directive 84/253/EEC (OJ L 157, 9.6.2006, p. 87).

Supervisory team leader

Staff member of the competent authority responsible for the organisation and coordination of the work within the supervisory team involved in the supervision of a credit institution.

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Bilateral meeting

Meeting between the competent authority and the auditor of a credit institution.

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Trilateral meeting

Meeting between the competent authority, the auditor and the credit institution.

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## 3. Implementation

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### Date of application

12. These guidelines apply from 31 March 2017.

## 4. General framework of the communication between competent authorities and auditors

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13. Competent authorities and auditors are both responsible for establishing effective communication between them in accordance with the first subparagraph of Article 12(2) of Regulation (EU) No 537/2014.
14. The communication to be established between competent authorities and auditors should be open and constructive, as well as adaptable to unexpected future developments.
15. Competent authorities and auditors should establish adequate processes and be aware of them in order to build and ensure effective communication.
16. Competent authorities and auditors should contribute to developing a mutual understanding of their respective roles and responsibilities.
17. The parties should discharge their respective responsibilities and one party should not use the work of the other as a substitute for its own work. The supervised credit institution should remain the main source of information for the parties' work.
18. Effective communication between competent authorities and auditors should facilitate the sharing of information about the credit institution which is relevant to the competent authorities' and the auditors' respective functions. Sharing of information should take into account the different responsibilities of competent authorities and auditors, which derive from the different scope and purpose of their functions.
19. Any information shared during the communication between competent authorities and auditors is subject to the confidentiality requirements laid down in Section II of Chapter 1 in Title VII of Directive 2013/36/EU and the disclosure in good faith to the competent authorities by auditors of any information emerging during this communication does not constitute a breach of any contractual or legal restriction on disclosure of information in accordance with Article 12(3) of Regulation (EU) No 537/2014.
20. Competent authorities should apply a proportionate approach in their communication with auditors and use their resources efficiently to establish effective communication.
21. A proportionate approach to the application of these guidelines aims to align the elements of the communication between competent authorities and auditors as referred to in Sections 5 and 6 of these guidelines (scope of information shared, form of communication, participants



in the communication, frequency and timing of communication, communication with auditors collectively) with the credit institution's size, internal organisation and nature, scope and complexity of its activities, so that the objective of these guidelines is achieved efficiently.

22. In particular, in-depth communication should be held with auditors of credit institutions referred to in Article 131 of Directive 2013/36/EU (global systemically important institutions (G-SIIs)<sup>5</sup> and other systemically important institutions (O-SIIs)<sup>6</sup>) and other institutions determined by competent authorities based on an assessment of the credit institution's size and internal organisation and the nature, scope and complexity of its activities.

23. In addition, competent authorities should assess on an on-going basis whether it is necessary to apply in-depth communication with the auditor of any credit institution due to ad hoc or emerging issues, such as:

- recent significant findings from the supervisory assessment or statutory audit
- recent developments that may change the risk assessment or the level of supervisory effort applied to a credit institution
- a change in the auditor being appointed to perform the statutory audit of a credit institution (including cases when a new auditor enters the market for statutory audits of credit institutions)
- the dismissal or resignation of the auditor during the audit engagement.

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<sup>5</sup> Commission Delegated Regulation (EU) No 1222/2014 of 8 October 2014 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards for the specification of the methodology for the identification of global systemically important institutions and for the definition of subcategories of global systemically important institutions (OJ L 330, 15.11.14, p. 27).

<sup>6</sup>EBA Guidelines on the criteria to determine the conditions of application of Article 131(3) of Directive 2013/36/EU in relation to the assessment of other systemically important institutions (O-SIIs) (EBA/GL/2014/10).

## 5. Communication between competent authorities and auditors of a credit institution

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### Scope of the information shared

**Principle 1:** The information shared should be relevant to the tasks of both parties considering the materiality of the information.

24. Competent authorities should identify in collaboration with auditors the areas of common interest to competent authorities and auditors, where sharing of relevant information may facilitate the task of supervision and potentially have an impact on the statutory audit.
25. When considering what information to share, due consideration should be given to the materiality of the information, including the likely magnitude and possible impact on the supervision and the statutory audit of the credit institution.
26. The type of information to be shared may be:
  - a. institution-specific
  - b. industry-specific
  - c. current issues
  - d. emerging issues.
27. The Annex to these guidelines provides a non-exhaustive list of areas and issues on which information could be shared between competent authorities and auditors.
28. To assist effective communication and sharing of information, and when practicable, competent authorities should prepare a list of issues for discussion. Competent authorities should consult auditors on the appropriateness of this list before the communication takes place and encourage them to contribute to it.

**Principle 2:** Competent authorities should request auditors to share information on any issues which are relevant to the supervision of the credit institution.

29. The information requested may include information related to the audit procedures performed, relevant audit evidence obtained and auditors' conclusions, whenever, in the

competent authority's judgement, such information may facilitate the exercise of supervisory tasks.

30. Relevant information is information and knowledge obtained in the statutory audit and related, but not limited, to the following areas, which are described in further detail in the Annex to these guidelines with a non-exhaustive list of issues under each of them:

- a. External environment and risk profile of the credit institution
- b. Corporate governance and internal controls
- c. Ability of the credit institution to continue as a going concern
- d. Audit approach
- e. Financial statements, valuation of assets and liabilities and disclosures
- f. Audit report and auditors' communication with the credit institution's management body, senior management or audit committee, or a body performing equivalent functions within the credit institution, on significant matters related to financial reporting and control functions
- g. The main findings of the audit procedures carried out and conclusions.

31. Where in-depth communication is applied, competent authorities should discuss with auditors, at least, the audit approach, the audit report and the auditors' communication with the credit institution's management body, senior management or audit committee, or a body performing equivalent functions within the credit institution, on significant matters related to financial reporting and control functions, including the audit report and the additional report to the audit committee referred to, respectively, in Articles 10 and 11 of Regulation (EU) No 537/2014 and as described in more detail in the Annex to these guidelines. In particular, for the discussion of the audit approach, competent authorities may take into consideration any findings or conclusions from the supervision of the credit institution.

**Principle 3:** Competent authorities should share information with auditors on issues which are relevant to the statutory audit of the credit institution.

32. Relevant information which should be shared between competent authorities and auditors includes issues that emerge during the process of supervision and which in the competent authority's judgement could be of relevance to the statutory audit of the credit institution.

33. Relevant information is information and knowledge emerging during the process of supervision and related, but not limited, to the following areas, which are described in further detail in the Annex to these guidelines with a non-exhaustive list of issues under each of them:

- a. External environment and risk profile of the credit institution
  - b. Corporate governance and internal controls
  - c. Ability of the credit institution to continue as a going concern
  - d. Financial statements, valuation of assets and liabilities and disclosures
  - e. Supervisory assessments and actions.
34. In addition, competent authorities may communicate to auditors any current or emerging issues affecting the credit institution's industry, such as changes in regulation or macroeconomic developments and results of thematic and peer-group reviews performed across the credit institution's industry.

#### **Form of communication**

**Principle 4:** Effective communication between competent authorities and auditors should be established through appropriate communication channels.

35. The form of communication can be broadly categorised as:
- written (for example email or fax) and oral (for example physical meetings or remote communication, such as phone calls)
  - regular (for example audit reports) and ad hoc (for example the text of new regulations).
36. Written communication should be used in cases when there is a need to ensure clarity or for retaining a record of the communication. Competent authorities should consider the use of written communication when communication relates to the following:
- Audit report and auditors' communication with the credit institution's management body, senior management or audit committee, or a body performing equivalent functions within the credit institution, on significant matters related to financial reporting and control functions
  - Findings and conclusions from audit procedures performed and supervisory processes
  - Complex technical matters
  - Emerging issues
  - Changes in regulation.

37. Physical meetings between competent authorities and auditors should be held to facilitate open and effective communication, particularly when in-depth communication is applied.

### Participants in the communication

**Principle 5:** The participants in the communication should include knowledgeable, informed and empowered individuals from both parties.

38. The supervisory team leader and the key audit partner should be the primary participants in the communication.
39. In cases when the communication occurs between individuals other than the supervisory team leader and the key audit partner, both the supervisory team leader and the key audit partner should be informed by their respective parties about the issues discussed and the outcome of such communication without undue delay.
40. Competent authorities should assess the usefulness of organising trilateral meetings, in particular where in-depth communication is applied. In making this assessment, competent authorities should consider whether:
- a. clarifications from the credit institution's management body, senior management or audit committee, or a body performing equivalent functions within the credit institution, are deemed necessary for a particular issue to be discussed between competent authorities and auditors
  - b. coordination of actions across the competent authority, auditor and credit institution are necessary.
41. When trilateral meetings are organised, they should be in addition to any bilateral meetings. Trilateral meetings may include members of the credit institution's audit committee, internal auditors, experts on relevant key control functions, or members of the credit institution's management body and senior management as necessary.
42. If in the competent authority's judgement it would facilitate the exercise of supervisory tasks, and subject to professional secrecy conditions required by Union or national law, competent authorities may invite other relevant public authorities (such as those responsible for the supervision of financial markets, the public oversight of auditors or the resolution of credit institutions) to the meetings with the auditors or inform these authorities of the outcome of the discussions with the auditors.
43. Effective communication between competent authorities and auditors should include adequate safeguards for the continuity of the communication regardless of the turnover of staff involved. Competent authorities should keep their own internal records of the communication to ensure that successors of the staff previously participating in the

communication are able to obtain sufficient information about the communication performed in the past. This information may include:

- a. minutes of communications or a summary of minutes
- b. key issues discussed
- c. conclusions of discussions
- d. future actions.

### Frequency and timing of communication

**Principle 6:** Communication between competent authorities and auditors should be as frequent as necessary to ensure timely sharing of relevant information.

44. Competent authorities should establish an appropriate frequency and timing of communication with auditors which enables timely sharing of information about relevant issues identified during the performance of their respective tasks.
45. Competent authorities should consult auditors on the appropriateness of the frequency and timing of communication.
46. Communication could take place during any phase of the supervisory processes or the audit processes, including one or more of the following:
  - a. during the preparation and planning of supervisory inspections (on-site or off-site)
  - b. during the performance of supervisory inspections (on-site or off-site)
  - c. after completion of supervisory inspections (on-site or off-site)
  - d. during the preparation and planning of the statutory audit
  - e. before signing of the audit report
  - f. after signing of the audit report.
47. Competent authorities should assess on an on-going basis whether there are any emerging issues that require the frequency and timing of communication to be changed or the initiation of communication on an ad hoc basis. These may include issues affecting the credit institution's entire industry or part of it (such as macroeconomic conditions) or issues affecting a particular credit institution (such as findings during the performance of supervisory processes or audit procedures, or cases when further clarifications on a specific issue are necessary).

48. When in-depth communication is applied, a bilateral meeting should be held at least on an annual basis.

## 6. Communication between competent authorities and auditors collectively

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**Principle 7:** Communication between competent authorities and auditors collectively should be as frequent as necessary to ensure timely sharing of information on issues which are relevant to the supervisory tasks and the statutory audit of credit institutions.

49. Competent authorities and auditors collectively (such as a group of auditors or a professional body representing auditors) should aim to develop a common understanding of current and emerging developments of relevance to the supervisory tasks and the statutory audit of credit institutions.
50. Competent authorities should meet with auditors collectively at least annually and irrespective of the meetings organised on an individual basis between the competent authority and the auditor of one or more credit institutions.
51. Communication could take place during any phase of the supervisory processes or the audit processes, and competent authorities should consult auditors on the appropriateness of the frequency and timing of communication.
52. The Annex to these guidelines provides a non-exhaustive list of areas and issues on which information could be shared between competent authorities and auditors collectively, as appropriate.
53. If in the competent authority's judgement it could facilitate the exercise of supervisory tasks, competent authorities may invite other competent authorities responsible for the prudential supervision of credit institutions or relevant public authorities (such as those responsible for the supervision of financial markets or for the public oversight of auditors) and associations (such as associations representing the banking, accounting or auditing industry) to these collective meetings or inform these authorities and associations of the outcome of the discussions with the auditors.



# Annex – Areas and issues for the communication between competent authorities and auditors

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54. This Annex provides a non-exhaustive list of areas and issues on which information could be shared between the competent authorities and auditors of a credit institution or auditors collectively, as appropriate, when applying these guidelines. The issues listed below are grouped by subject matter, irrespective of the provider of information.

## External environment and risk profile of the credit institution

- a. Risk assessment and scope: the competent authority's and the auditors' assessments in light of the external environment and the credit institution's performance, business model, corporate structure, risk concentration and risk appetite (including any changes of thereto).
- b. Changes in regulation.
- c. Changes in accounting and auditing standards.
- d. Macroeconomic developments affecting the credit institution's industry.

## Corporate governance and internal controls

- a. Culture, philosophy and operating style of the governing body of the credit institution (including quality of corporate governance and concentration/sharing of power amongst the members of the governing body).
- b. Suitability of the credit institution's members of the management body, the senior management or the members of the audit committee, or a body performing equivalent functions within the credit institution on significant matters related to financial reporting and control functions (including the implementation of structural internal changes of management and organisational restructuring processes).
- c. Role of the audit committee, or a body performing equivalent functions within the credit institution, in the supervision of the financial reporting process.
- d. Quality of the relationship of the audit committee, or a body performing equivalent functions within the credit institution, with the auditors.
- e. Observations on internal controls (for example the auditors' opinion on the description, included in the corporate governance statement in accordance with Article 20 of

Directive 2013/34/EU<sup>7</sup>, of the main features of the credit institution's internal control and risk management systems in relation to the financial reporting process, governance effectiveness, the control environment, the application and monitoring of controls, the quality of key control functions, and IT systems), the results of the internal control tests performed by the auditor and their consequences for the audit approach (for example their impact on the extent of performance of direct verification and the use of experts in the statutory audit).

- f. Significant deficiencies in internal control processes (for example material control weaknesses identified in the credit institution's financial reporting processes) and the auditors' observations on matters that are significant for the responsibilities of the members of the credit institution's management body, senior management or audit committee, or the members of a body performing equivalent functions within the credit institution, in overseeing the strategic direction of the credit institution or the credit institution's obligations related to its accountability. This may include, where relevant, the auditor's observations on the effectiveness of the internal audit function, risk management function and compliance function (including the assessment of fraud risks, especially due to weaknesses in internal controls).

#### Ability of the credit institution to continue as a going concern

- a. Assessment of the risks related to the continuous functioning of a credit institution, including capital adequacy risks (such as credit, market and operational risk and minimum requirement for own funds and eligible liabilities, or MREL), large exposures, leverage, liquidity and funding risks.
- b. Observations on any areas of potential reputation risk and risk from non-compliance of the credit institution with relevant legal requirements (including material actual or potential litigation and legal disputes).

#### Audit approach

- a. Materiality in planning and performing the statutory audit.
- b. Use of external experts in the statutory audit.
- c. Use of internal auditors' work in the statutory audit.
- d. Application of accounting policies and changes to them.
- e. Sources of potential management bias.

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<sup>7</sup> Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ L 182, 29.6.2013, p. 19).

- f. Areas of significant risk identified.
- g. Specific work undertaken by the auditor on particular transactions (which may have also required the use of experts).
- h. Significant difficulties encountered during the statutory audit (including disagreements between auditors and members of the credit institution's management body, senior management or audit committee, or members of a body performing equivalent functions within the credit institution).
- i. Circumstances that have led to a significant change in the audit planning.

#### Financial statements, valuation of assets and liabilities and disclosures

- a. Views and judgements on key risk areas and assumptions, including significant transactions and valuations (for example in the areas of estimation of loan loss provisions and valuation of financial instruments).
- b. Accounting practices and areas encompassing a significant degree of estimation uncertainty (for example the areas of estimation of loan loss provisions and valuation of financial instruments).
- c. Critical accounting estimates and indications of management bias:
  - i. where a credit institution consistently uses valuations that exhibit a pattern of optimism or pessimism within a range of acceptable valuations or other indications of possible management bias, or
  - ii. where a credit institution undertakes transactions to achieve a particular accounting or regulatory outcome, such that the accounting or regulatory treatment is technically acceptable, but it obscures the substance of the transaction.
- d. Misstatements in the financial statements (corrected and uncorrected) identified during the statutory audit and the auditors' evaluation of them.
- e. Adequacy and reliability of disclosures in financial statements in light of statutory reporting requirements and risks, transactions, judgements and assumptions discussed in current and previous meetings.

### Audit report and auditors' communication with the credit institution's management body, senior management or audit committee, or a body performing equivalent functions within the credit institution, on significant matters related to financial reporting and control functions

- a. Audit report referred to in Article 10 of Regulation (EU) No 537/2014.
- b. Additional report to the audit committee referred to in Article 11 of Regulation (EU) No 537/2014.

### The main findings of the audit procedures carried out and conclusions

- a. Issues identified during the statutory audit and communicated to the credit institution's management body, senior management or audit committee, or a body performing equivalent functions within the credit institution, such as deficiencies in internal control that in the auditors' professional judgement merit management's attention.
- b. Significant issues which have been intensely discussed with the credit institution's management body, senior management or audit committee, or a body performing equivalent functions within the credit institution.

### Supervisory assessments and actions

- a. Supervisory measures imposed on a credit institution.
- b. Issues arising from recent institution-specific supervisory risk assessments and reviews (such as during the supervisory review and evaluation process, or SREP<sup>8</sup>).
- c. Results of thematic reviews and peer-group reviews performed by the competent authority across the credit institution's industry.
- d. Observations arising from a credit institution's regulatory reporting, including regulatory capital.
- e. Compliance with relevant legal and prudential requirements.

### Others

- a. Issues discussed in previous years and meetings, if deemed to be still relevant.
- b. Issues related to the appointment, change, dismissal or resignation of the auditor appointed to perform the statutory audit.

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<sup>8</sup> EBA guidelines (EBA/GL/2014/13) issued in accordance with Article 107(3) of Directive 2013/36/EU.

- c. Additional matters arising from the statutory audit, such as matters arising from existing or new requirements provided for in Union or national law.
- d. Feedback on the quality of the communication between competent authorities and auditors and ways to improve communication.