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November 4, 2003 in Geneva

Association of Foreign Banks in Switzerland
Verband der Auslandsbanken in der Schweiz
Association des banques étrangères en Suisse
Associazione delle banche estere in Svizzera

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(Re-)regulated: Audit process
,old wine in expensive bottle ‘?’

Stephan Heinimann
Swiss certified public accountant

www.peqsolutions.ch



Two initial questions

■ Question 1

What are your main concerns in respect of the implementation of the new draft circulars?

■ Question 2

Do you see any added value for the banks?

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Agenda

what information will you get during the next hour?

- Overview and executive summary of the new draft circulars
- Crucial and most important aspects for banks to consider
- Benefit from the new proposed re-regulation
- Support to the auditors to assure an effective implementation

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Overview

five new draft circular letters on the audit process

- Audit
- Audit report
- Audit companies
- Supervision of big banks
- Self-regulations - minimum standards of the SFBC

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Three statements

- ‚A high quality standard of the banking supervision - and this includes the bank audit - is crucial to the international credibility of the Swiss banking supervision model and to the strength of the Swiss financial center’
- ‚The bank audit of the 21st century is based on professionalism and transparency’
- ‚The drivers of a risk focused audit should not be led by inefficient formalism and self-protection’

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What will be re-regulated?

Three key elements

- Formalizing of approach and standards already applied by the auditors
- Differentiation between the banking supervision of the big banks and the others
- Segregation of the audit into financial audit and regulatory audit

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SFBC-circular: Audit

Content

- Audit areas and concept (introduction)
- Audit scope
- Audit approach
- Audit of financial services groups and conglomerates

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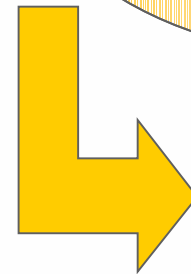
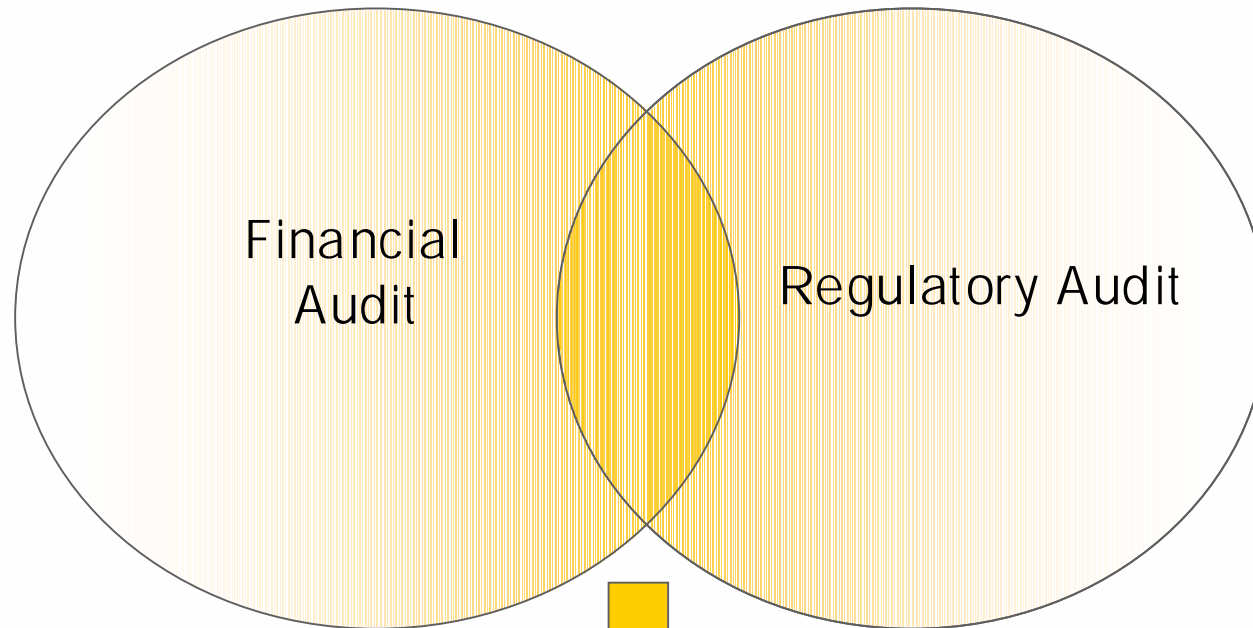
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SFBC-Circular: Audit

Audit areas



Based on generally accepted audit principles

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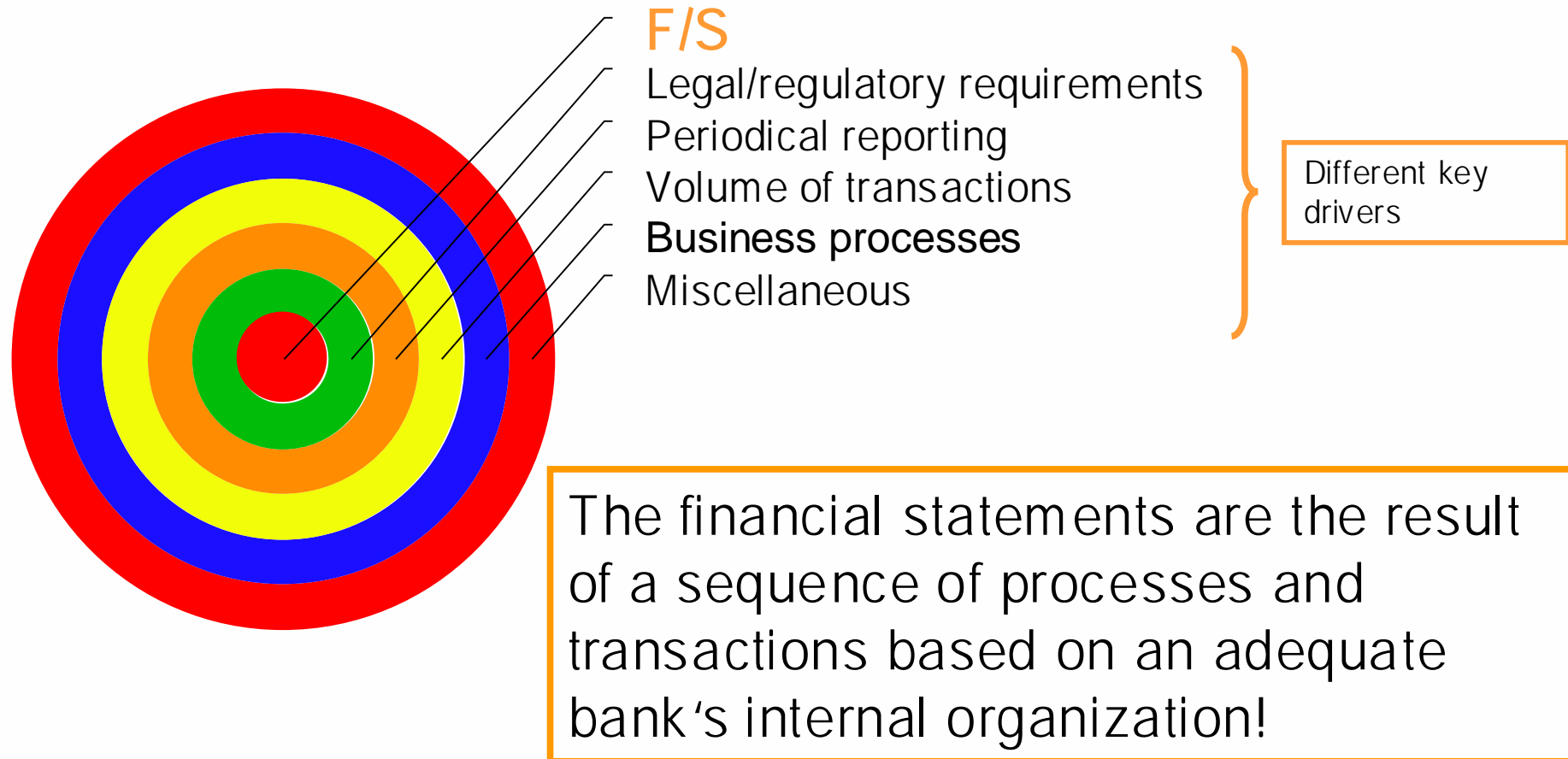
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Excuse

the bank's financial statement



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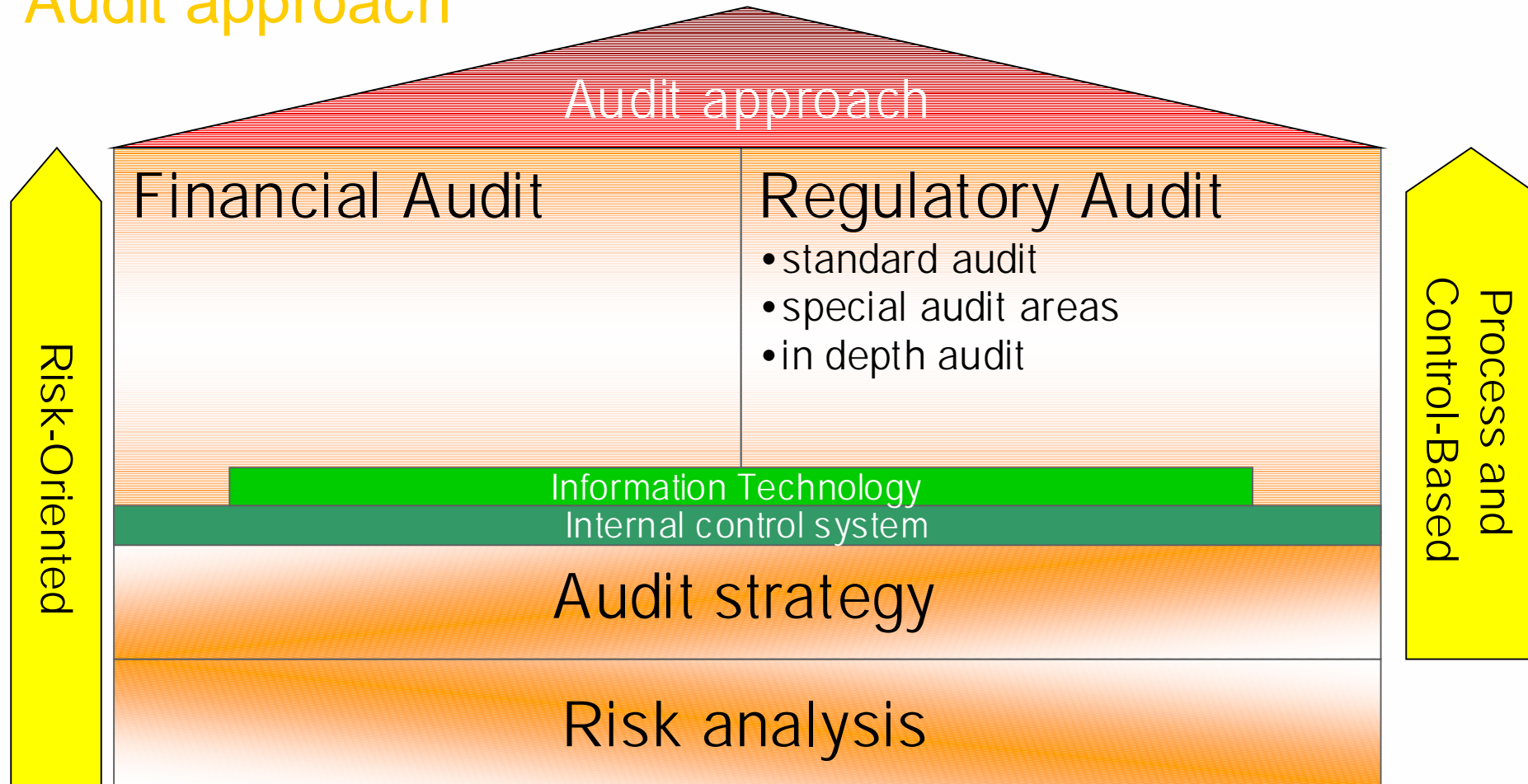
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SFBC-circular: Audit

Audit approach



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Excuse

Audit team



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SFBC-circular: Audit

Audit scope

Financial Audit

- Financial statements (and if appropriate – Group F/S) and related regulatory reporting requirements
- Adequacy and effectiveness of the bank's organization and internal controls related to the financial statements
- Valuation of the assets, off balance sheet transactions and policy and strategy of the provisions
- Adequacy of the bank's financial planning and controlling tools in place (budget and financial development)

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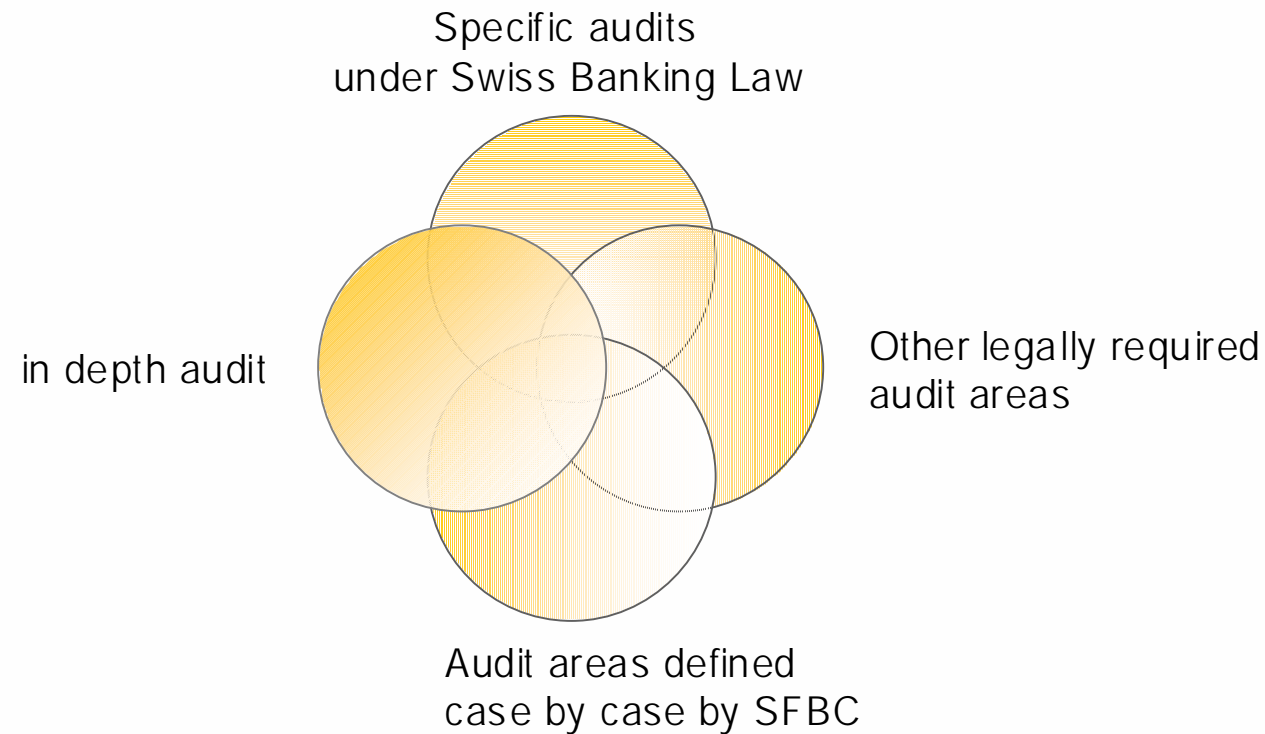
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SFBC-circular

Audit subject (2)

Regulatory audit



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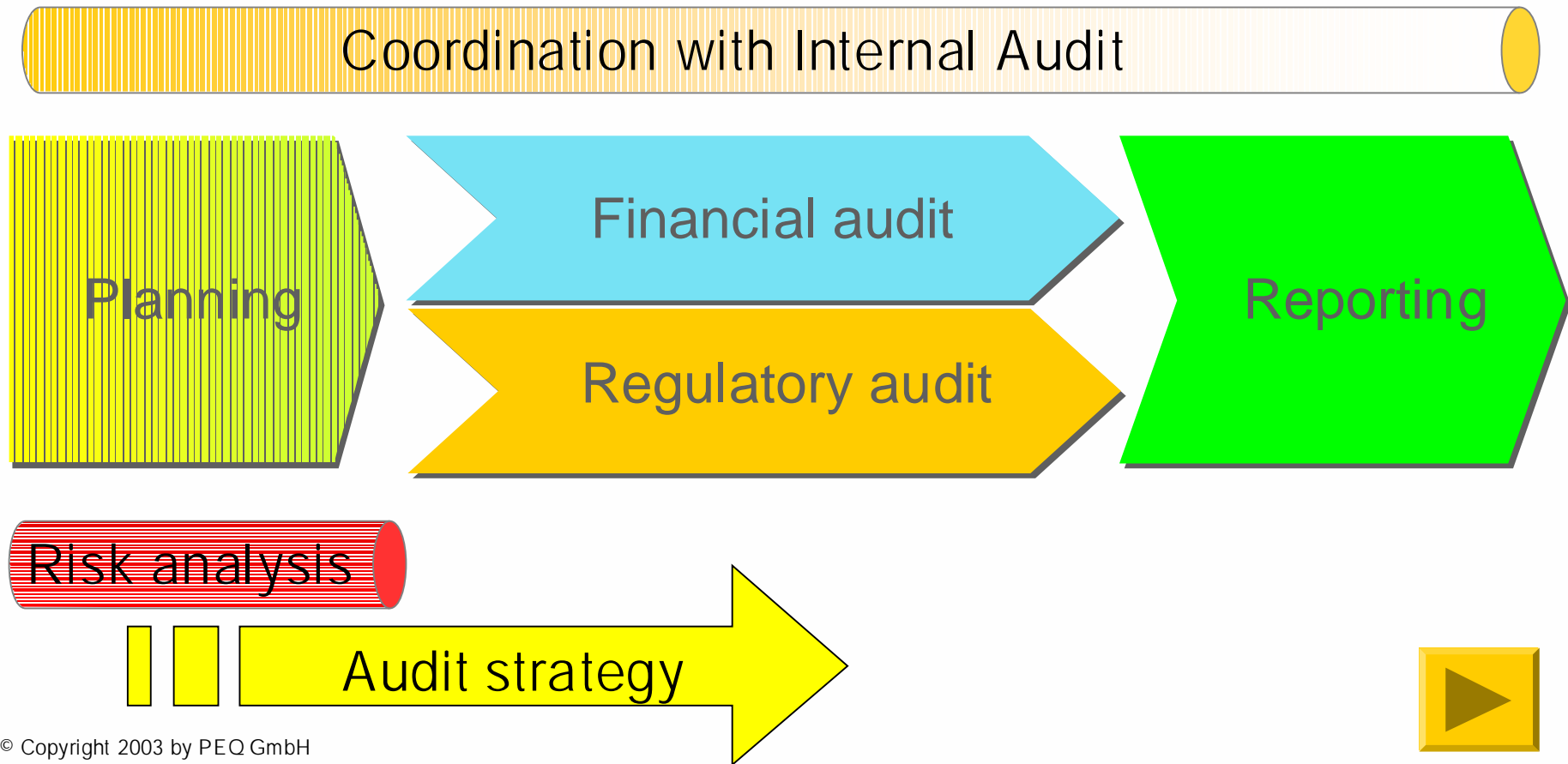
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SFBC-circular: Audit

Audit approach



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SFBC-circular: Audit report

Overview

- Reporting principles
- Audit reports

Financial audit

Regulatory audit

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SFBC-circular: Audit report

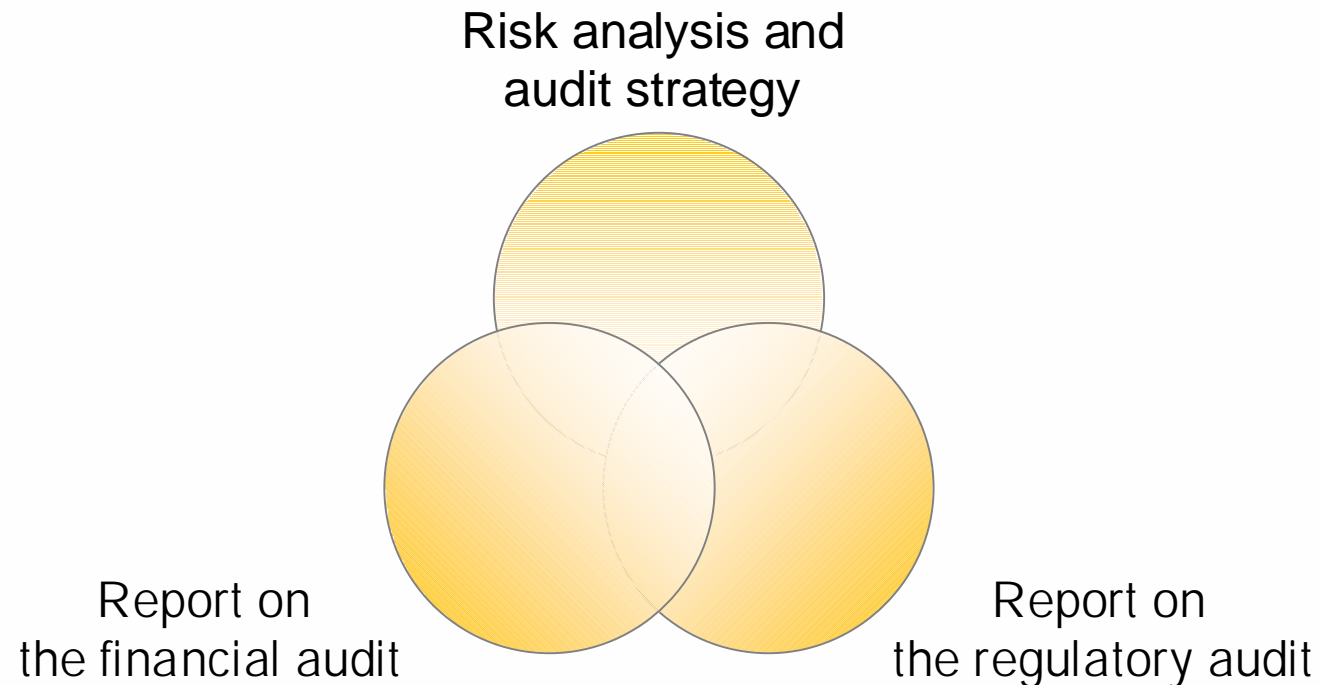
Reporting principles

- Goals and main steps 
- Treatment of the audit report
- Reporting on single-company accounts and on consolidated level
- Form, content and language
- Audit results and opinion
- Audited period and reporting deadline

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SFBC-circular: Audit report

two standard audit reports = three standard reporting



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SFBC-circular: Audit companies

Content

- Professional requirements
- Independence
- Supervision of the audit companies by the SFBC
- Engagement and change of the auditors

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SFBC-circular: Audit companies

Supervision of the auditors

- Analysis of required standard information from the audit companies

Information to be submitted to the SFBC annually

Additional information

- Quality controls (i. e. work paper reviews) 
- Supervision of the auditors during the audit work at the bank

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SFBC-circular: Self-regulations – minimum standards of the SFBC

Goal

- Applicable for all banks and securities dealer
- Applicable for fund administrator and auditors

Most significant changes

Rules FX trading

Self-regulations of Swiss Funds Association

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Added value and significant aspects

Added value

- Regulated audit framework
- Transparency
- Standard audit approach
- Increase of audit assurance

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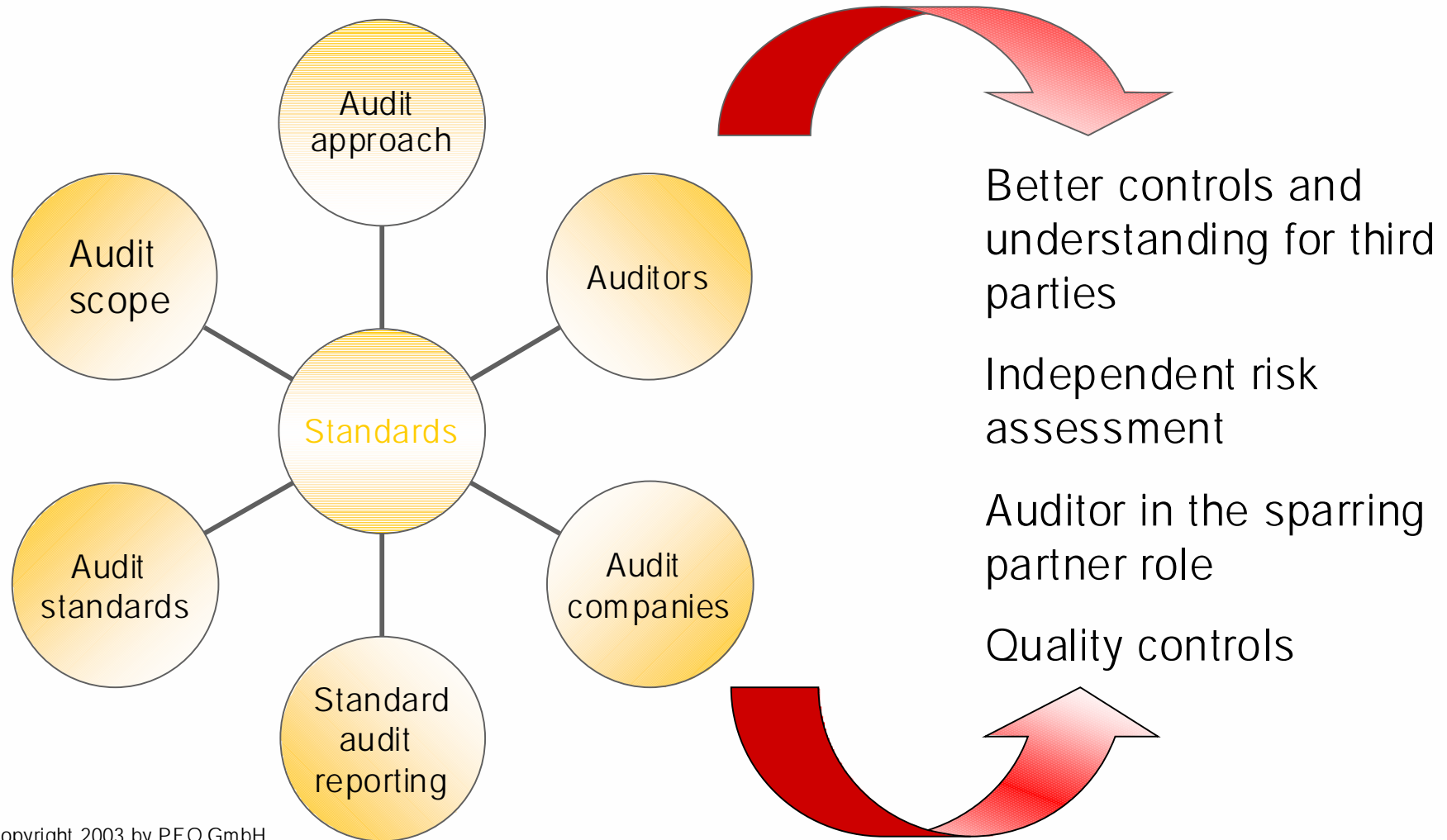
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Added Value

Key indicator



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Added value

Transparency

- Risk assessment
- Audit strategy
- Coordination of the audit work
between internal and external audit
- Standard reports
- Detailed reporting on working hours and fees

minimize

Expectation
Gap

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Added value

Generally accepted audit standards

- Audit standards of the Swiss chamber of Certified Public Accountants
- International Standards on Auditing (ISA)
- Generally Accepted Auditing Standards (US-GAAS)
- ISA 100 „Assurance Engagements“

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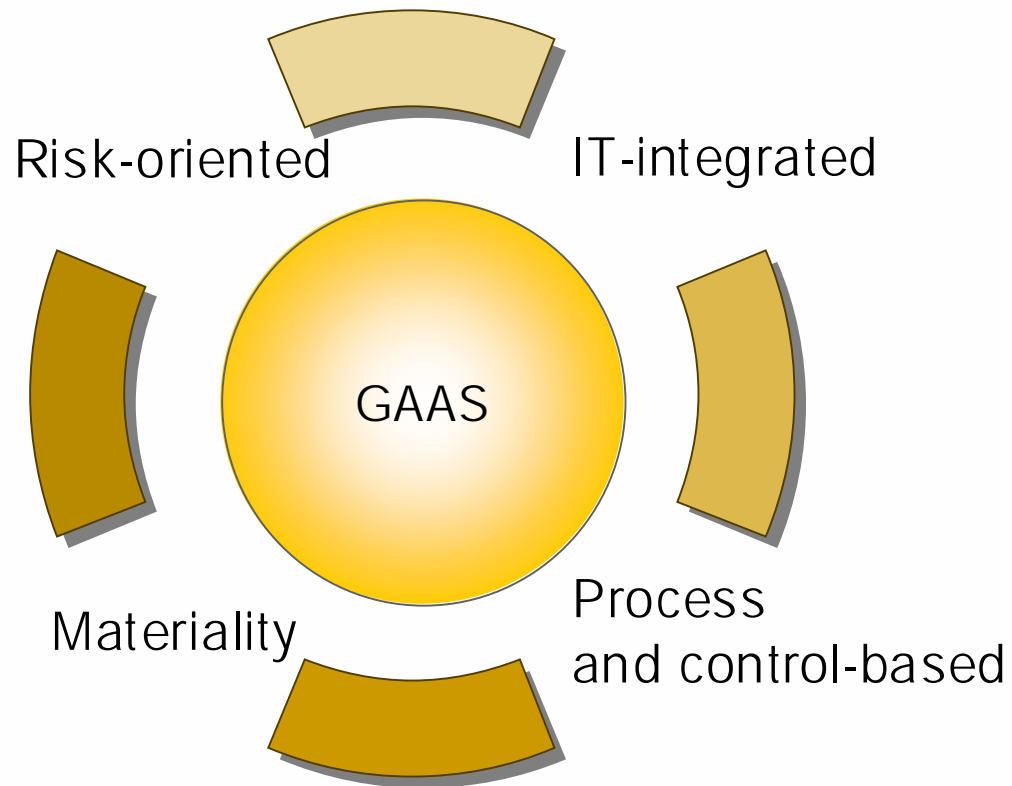
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Added value

what are the key drivers of generally accepted audit standards ?



Audit will be focused on key activities and risk areas based on the risk assessment

IT-related considerations and procedures are a major focus of an efficient and effective audit

Audit steps will be limited on material issues

Strength of the corporate governance

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Added value

Audit assurance

What are the key success factors of the increased audit assurance?

Use of generally accepted audit standards

Risk-oriented audit approach

Direct intervention of the SFBC

Higher transparency

Quality controls at the auditors performed by the SFBC

A few significant points to consider

- Risk analysis and audit strategy
- Involvement of the Internal Audit
- Audit approach
- Role of specialists
- Communication

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Significant points

Risk analysis and audit strategy

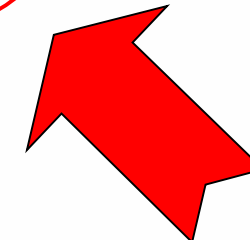
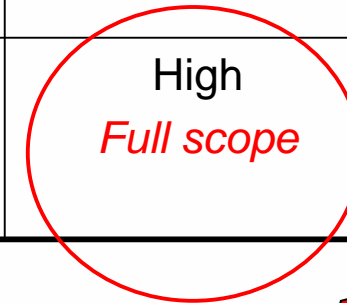
- Standard reporting ,Risk analysis and audit strategy‘ are working papers and not easy to interpret by non auditors
- The proposed risk analysis and audit strategy are already applied by the audit methodologies of the Big4
- The risk analysis and the audit strategy drive the substantive audit procedures

Be aware that the planning of the financial audit is only a minor point of the standard reporting ‘risk analysis and audit strategy‘

Significant points

Combined Risk Assessment

Inherent Risk	Control Risk		
	Minimum	Moderate	Maximum
Lower	Minimal <i>No controls</i>	Low <i>Analytical review</i>	Moderate <i>Limited review</i>
Higher	Low <i>Analytical review</i>	Moderate <i>Limited review</i>	High <i>Full scope</i>



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Significant points

Internal Audit

Based on the risk analysis and audit strategy form the audit work will be assigned and coordinated between internal and external audit

Red Flags!

- Significant increase of the audit areas
- Capacity and resource planning
- Coordination of audit strategy
- Financial audit work



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Significant points

Audit approach

Risk-oriented audit requires the auditor to understand the business and business environment of the bank

Red Flags

✎ Risk assessment

- definition of the control risk
- definition of the inherent risk

✎ Definition of materiality

✎ Development of strategy for test of controls

✎ Audit team

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Significant points

Communication

Red Flags

- Definition of your contact (single point of contact)
- Frequency of communication – regular contact
- Adequate know how
- Transparency in service delivery

Do you speak the same language as your auditor and the banking supervision authority?

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Support to your auditor

how to achieve a win-win situation?

Be actively involved in risk analysis process and provide your auditor with as much significant information as possible

- Be aware, this is a time consuming process

- Make your own risk assessment of your bank

Develop a milestone plan in cooperation with your auditor and define all relevant deadlines; declare this schedule as not changeable.

- Be aware, audit should be a goal directed project management

Conclusion

Overall

- Overall the circulars regulate the best practice of the audit business already applied by the big4 audit companies
- The circulars include a few gaps and points which should be closed or clarified by more precise definitions or additional comments

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Conclusion

Pending and critical points

- Overlaps between financial and regulatory audit and reporting
- Inconsistency between different circulars
- Reconciliation between the reporting to the SFBC and the risk analysis and audit strategy
- Transfer of the responsibility of the auditors to the bank
- Transparency

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Conclusion

Pending and critical points (2)

- Efficiency of the separation of the audit and reporting between the financial and regulatory areas?
- Quality controls of the SFBC responsibility?
Impact of the results of the quality controls for the bank?
- Responsibility of the SFBC in its role as supervisor of the bank auditors?



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Seven points to look at

Checklist

1. Did the risk environment and framework of your institute significantly change compared to the previous year?
2. Does the audit work get an appropriate attention within your organization?
Responsibility (BoD, Audit Committee)
Communication (BoD, Audit Committee, CEO, CFO, CRO, Internal Audit)
3. Do you have a transparent and open communication with your auditor?
4. Do you understand the audit strategy and the audit approach prepared by your auditor?
5. Does your auditor match your expectation in respect of
the risk assessment (key business risk)
an adequate audit approach
6. Are the members of your audit team appropriate in respect of the risk analysis and the defined audit strategy?
7. Are the necessary steps and actions planned to assure that an efficient and professional audit will be performed?

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