

AUDITOR REPORTING OF KEY AUDIT MATTERS IN THE EUROPEAN BANKING SECTOR

Analysis and good practice examples

Survey results

HIGHLIGHTS

Audit quality is vital for people to be able to rely on company information and have trust in markets. Communicating key audit matters (KAMs) in the auditor's report is a relatively recent requirement to support the quality of audits. Auditor's reporting of KAMs responds to the growing demand of investors and stakeholders for more transparency and insight in the audit process.

The banking sector is a pillar of EU economic growth and auditors are now producing more informative and insightful reports to contribute to the sector's public trust and stability.

Our survey provides insights on auditor's reporting on KAMs for more than 60 European banks. It aims to facilitate communication between banks, auditors and stakeholders on this important new requirement.

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INTRODUCTION

Starting from the financial year 2017, auditors of listed and other public interest entities (PIEs¹) including banks within the European Union (EU) are required by the EU Regulation 537/2014² (the Audit Regulation) to include in their auditor's report the following information in support of the statutory audit opinion:

- a description of the most significant assessed risks of material misstatement, including assessed risks of material misstatement due to fraud
- a summary of the auditor's response to those risks, and
- where relevant, key observations arising with respect to those risks

To address the growing needs of stakeholders for more transparency and relevance of the auditor's report, the International Auditing and Assurance Standards Board (IAASB) issued in 2015 a specific auditing standard to introduce key audit matters (KAMs) reporting requirements primarily for listed entities: ISA 701, *Communication key audit matters in the independent auditor's report* (ISA 701)³. According to the International Standards on Auditing (ISAs), KAMs are those matters that were of the most significance in performing the audit.

The standard is also applicable to PIEs, as required by law or regulation, and voluntarily for other entities. Following the issuance of the new audit standard, mandatory auditor's reporting on KAMs for listed entities and PIEs became applicable in a few jurisdictions starting for the 2016 year-end audits and in all others for 2017 year-end audits.⁴

Accountancy Europe welcomed the approach taken by the EU policymakers and the IAASB to enhance public auditor reporting and published in 2015 its briefing paper *Recent Developments in Auditor Communication*⁵. While the wording in the EU Audit Regulation is not the same as in ISA 701, the outcome could generally be expected to be the same. As concluded in our briefing paper, due to the fact that the concept of "identifying and assessing risks of material misstatements" used in the EU text comes from the ISAs⁶, both methods should result in similar matters being communicated. Therefore, the term of KAM refers to both EU and ISA auditor reporting requirements.

This new reporting requirement is a ground-breaking milestone for auditors, companies, audit committees, shareholders, regulators and other categories of users of the auditor's report and financial statements.

Accountancy Europe performed this survey on auditor's reporting of KAMs in the European banking sector to analyse the overall outcome and the impact on the value-added by the auditor's report, following the first year of KAM reporting requirement across Europe for this vital PIE segment for the EU economy.

Our survey provides insights and conclusions on auditor's reporting on KAMs for more than 60 European banks (Appendix 1), which own the vast majority of the assets in the European banking sector. The banking sector is one of the pillars for economic growth in the EU and auditors are now producing more informative and insightful reports to contribute to the public trust and stability in the sector.

¹ Public Interest Entities, as defined in Directive 2006/43/EC (Article 2 (13)) – i.e.: entities whose transferable securities are admitted to trading on a EU regulated market, credit institutions, insurance undertakings and other entities as designated by Member States in national legislation; <https://eur-lex.europa.eu/homepage.html>

² Article 10(2) of the Regulation (EU) No 537/2014 on specific requirements regarding statutory audit of public-interest entities; <https://eur-lex.europa.eu/homepage.html>

³ ISA 701 *Communication key audit matters in the independent auditor's report*; <http://www.ifac.org/publications-resources/2016-2017-handbook-international-quality-control-auditing-review-other>

⁴ As highlighted in Appendix 1, the UK and the Netherlands have adopted the ISA 701 KAM reporting requirements starting for the 2016 financial year-end, before the other EU countries

⁵ Accountancy Europe, *Recent Developments in Auditor Communication*; <https://www.accountancyeurope.eu/publications/fee-issues-a-briefing-paper-on-recent-developments-in-auditor-communication/>

⁶ ISA 315 *Identifying and assessing the risks of material misstatement through understanding the entity and its environment*; <http://www.ifac.org/publications-resources/2016-2017-handbook-international-quality-control-auditing-review-other>

Before analysing the conclusions of the survey, this paper first introduces what KAMs are and why auditors report on them. It also outlines the value and challenges in communicating KAMs and discusses how KAMs are selected.

WHAT IS A KAM?

KAMs represent the most significant audit risks with the biggest impact on the overall audit strategy and on the allocation of resources in an audit of financial statements. They are communicated by the auditor in the auditor's report.

KAMs are selected from areas of higher assessed risk of material misstatement requiring significant auditor judgment, with the highest impact on the audit. KAMs are often related to a financial statements area that involved significant management judgment. Singling-out KAMs from the risks of material misstatements identified by the auditor is in itself a matter of exercising professional judgment.

According to ISA 701, auditors of listed entities are required to set out, in a separate section of the audit report "those matters that, in the auditor's professional judgement, were of most significance in the audit of the financial statements of the current period [...] selected from matters communicated with those charged with governance".⁷

WHY ARE AUDITORS OF PIEs REQUIRED TO REPORT ON KAMs?

Including KAMs in the auditor's report is a major breakthrough for both auditors and users. Similar reporting requirements were already in place for auditors in various jurisdictions (*Appendix 2*). However, the widespread requirement to report KAMs for listed entities and other PIEs came about after the financial crisis, as stakeholders wanted to know more about the key areas that the audit covered.

In particular, investors questioned the relevance and transparency of the pass/fail auditor's report and the 'boilerplate' language auditors used in their reports. As end users of the auditor's report, they urged auditors to provide more informative and transparent audit reporting, while providing deeper insight into the company.

VALUE OF COMMUNICATING KAMs

INSIGHT AND VALUE ADDED: Auditor's reporting of KAMs opened the 'black box' of auditor's professional judgment to the public to primarily address the growing demand of the investors' community for more insight into the audit process. Ultimately, it demonstrates the value of auditors in preserving financial stability.

ENHANCED TRANSPARENCY: The requirement to report KAMs is arguably the single biggest change in auditor's reporting in the history of the profession. The auditor's report now provides extensive insight to stakeholders on the conduct of the audit, by disclosing information previously available only to audit committees.

ADDRESS PUBLIC CONCERNS: The fundamental value and relevance of audit has been increasingly scrutinised by the public. It is therefore important for the auditor to respond to calls from stakeholders, mostly from investors, for more informative audit reports with entity specific information. To this end, the progress made by auditors and improved transparency in auditor's reporting have been welcomed by stakeholders in general. In this context, auditor's reports are now easier to read and understand.

⁷ ISA 701 *Communication key audit matters in the independent auditor's report* (par. 8); <http://www.ifac.org/publications-resources/2016-2017-handbook-international-quality-control-auditing-review-other>

INCREASED ACCOUNTABILITY: Stakeholders welcomed this major upgrade of the auditor's report. While providing insight into the auditor's risk assessment process, reporting on KAMs also provides additional comfort that the material matters most relevant to them have been properly disclosed and addressed during the audit. This response was also welcomed by auditors as a necessary step to restore end users' confidence in the role and the value added of audits.

MONITOR DEVELOPMENTS: As 2017 was the first year of mandatory auditor's reporting on KAMs within the EU, this is only the first step in improving the value added and quality of audit reports. Going forward, stakeholders should expect auditors to explain in their reports what were the year on year developments in their key risk assessment, audit approach and audit findings. This will help users of financial statements to keep track, understand and assess the developments of key risk areas for companies.

BENCHMARKING: Auditor's reporting on KAMs allows benchmarking within industries, markets, geographical areas, etc., while allowing users to better understand the specific context of companies, thus enhancing the comparability of audit reports.

STAKEHOLDERS' RECOGNITION: In November 2014, the UK's Investment Association held its first Auditor Reporting Awards to recognise those audit reports which were the most informative and clear to investors. Winners were announced in two main categories – most insightful (i.e. including most entity specific information) and most innovative audit report. This event for the UK investment community was succeeded by a second Auditor Reporting Awards⁸ organised in November 2015.

CHALLENGES IN COMMUNICATING KAMs

BRING A FRESH PERSPECTIVE: A key challenge for auditors is to keep the content of the auditor's report relevant and informative, by avoiding to fall into the trap of moving to a more extensive version of boilerplate reporting.

KEEP CLARITY OF LANGUAGE: The use of ambiguous or too technical language may reduce the information content of KAMs.

DEVELOP UNDERSTANDING: Users of the auditor's report and of financial statements, such as analysts, investors or regulators will have to develop an understanding of the auditor's report, in conjunction with the related financial statements disclosures.

TAILOR AND CONTEXTUALISE⁹: This perspective was outlined by Bruce Winter, former IAASB member, in his speech on the challenges the profession is facing in regard to new auditor reporting standards: "[...] The real challenge is to make sure that those key audit matters are tailored to the company and provide useful insight to shareholders."¹⁰

WHAT TO REPORT AS KAMs?

The description of the KAMs in the auditor's report is a matter of the auditor's professional judgment and should be communicated by the auditor to those charged with governance. According to ISA 701, *Communication key audit matters in the independent auditor's report (paragraph A.46)*, the description of individual KAMs may include the following:

⁸ <http://www.theinvestmentassociation.org/media-centre/press-releases/2014/press-release-2014-11-20.html>

⁹ In the Netherlands, an assessment of Eumedion, a Dutch body representing investors, has praised good practice found in several audit reports: Evaluation of the 2016 AGM Season, page 10;

<http://www.eumedion.nl/en/public/knowledgenetwork/publications/2016-proxy-season-evaluation.pdf>

¹⁰ Bruce Winter, former IAASB Member, on the challenges the profession is facing in regard to new auditor reporting standards; <http://www.pwc.com/gx/en/services/audit-assurance/corporate-reporting/world-watch/iaasb-board-members-interview.html>

- aspects of the auditor's response or approach that were most relevant to the matter or specific to the assessed risk of material misstatement (description of the matter and an assessment of its significance)
- a brief overview of the procedures performed
- an indication of the outcome of the procedures
- key observations with respect to the matter, or some combination of these elements

While auditors previously had the obligation to communicate the significant risks of material misstatement only to those charged with governance¹¹, the inclusion of the KAMs in the auditor's report is a major improvement in public auditor's reporting.

The EU Audit Regulation has similar reporting requirements. In addition, the Regulation clearly states that, where relevant, the audit report shall include a clear reference to the relevant financial statements disclosures. Clearly cross-referencing KAMs to the related financial statements disclosures, when available, contributes to the clarity and understandability of the auditor's report.

In *Appendix 3* to this paper, we present some specific aspects and practical challenges in auditor's reporting on KAMs.

SELECTING KAMs

ISA 701, *Communication key audit matters in the independent auditor's report* (ISA 701) provides detailed guidance to assist the auditor in selecting KAMs as opposed to the Audit Regulation, which does not prescribe how to select KAMs from other significant risks of material misstatements.

From matters that the auditor communicated to those charged with governance, the auditor first determines the matters requiring significant auditor attention in performing the audit. Such matters often relate to complex areas and affect the overall audit strategy, allocation of resources and audit effort. Matters subject to statutory audit but not related to the audit of the financial statements (such as regulatory subjects) do not ordinarily qualify as KAMs.

According to ISA 701, in determining matters that require significant auditor attention, the auditor should consider:

- areas of higher assessed risk of material misstatements or significant risks (risks requiring special audit consideration)
- significant auditor judgements relating to areas of significant management judgement (e.g. complex accounting estimates)
- effects of significant events or transactions on the audit

In most cases, a KAM will relate to significant or complex matters disclosed in the financial statements, but is not limited to those. The auditor is not precluded from reporting a matter that is not disclosed in the financial statements. However, the auditor should seek to avoid providing original information about the entity that would be inappropriate for the auditor alone to report. At the same time, KAMs cannot substitute a required disclosure in the financial statements.

¹¹ ISA 260 (revised) *Communication with those charged with governance*; <http://www.ifac.org/publications-resources/2016-2017-handbook-international-quality-control-auditing-review-other>

ANALYSIS OF KAMs IN THE EUROPEAN BANKING SECTOR

OVERVIEW

We outline below the key aspects of our analysis of auditor's reporting on KAMs in the European banking sector. The sample for our analysis consisted of 62 European banks, most of them (59 banks) reporting under the International Financial Reporting Standards (IFRS), two banks reporting according to their local Generally Accepted Accounting Principles and one bank reporting under the US Generally Accepted Accounting Principles (US GAAP).

The starting point for determining our sample was the list of significant financial institutions supervised by the European Central Bank's (ECB) under the Single Supervisory Mechanism (SSM), as explained in *Appendix 1* to this paper.

AVERAGE NUMBER AND MAIN CATEGORIES OF KAMs

The starting point of the analysis was to look at the number, categorisation and recurrence of the KAMs reported, to conclude on the following aspects:

- number of KAMs reported in the European banking sector: minimum, maximum and average number
- analysis of the main categories and subcategories of topics reported as KAMs, with exemplification of reporting for the main recurring categories (good practice examples)

KAM COMPARISON

Auditor's reporting of KAMs enables users to perform comparison and benchmarking. We have made a comparison of the main KAM categories reported across jurisdictions.

CLARITY OF KAMS REPORTED

We have also analysed the clarity of the KAM reporting by verifying the cross-referencing of the auditor's reporting with the related financial statements disclosures, where applicable.

OTHER EXTENDED REPORTING ELEMENTS

Finally, we have analysed the further steps taken by auditors in the direction of extended audit reporting, by observing the additional elements disclosed in the auditor's report, such as:

- materiality disclosures
- audit scoping disclosures

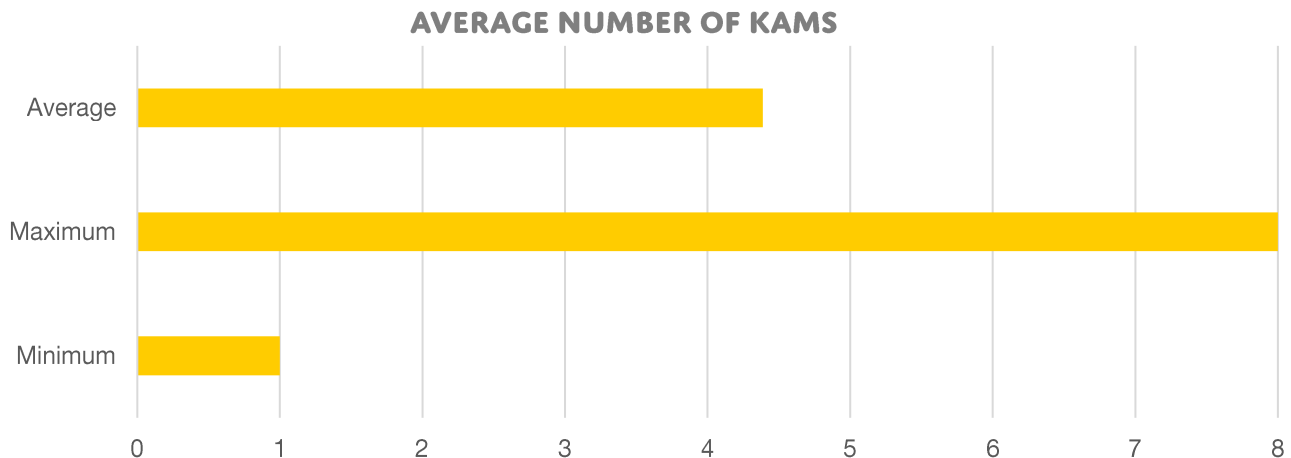
Although these additional extended reporting features are currently only required in a few European jurisdictions, as outlined in *Appendix 2*, we have observed voluntary reporting in these areas. Voluntary adoption of additional extended requirements shows a clear sign that auditors strive to improve the quality of auditor's reports, as auditors move further in the direction of providing more informative, transparent and value-adding reporting, to further enhance the relevance of audit reports.

ANALYSIS OF KAMs

AVERAGE NUMBER OF KAMs

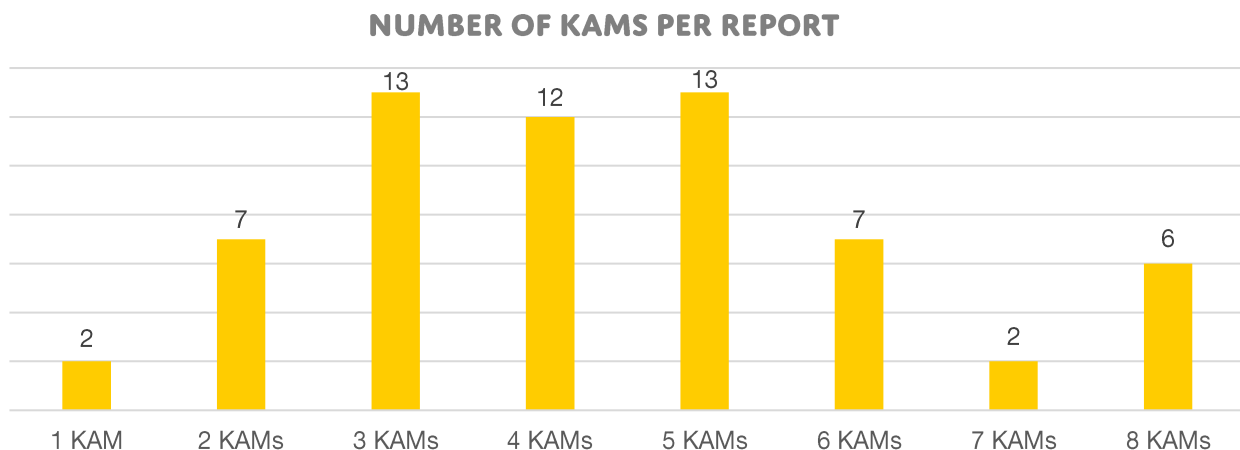
Our analysis of 62 auditor's reports within the European banking sector identified a total number of 272 matters reported as KAMs.

We have looked at the auditor's reports on the consolidated financial statements of the selected banks. On average, the number of KAMs reported in the European banking sector for 2017 was **4 KAMs per audit report**.



With an average number of 4 KAMs per report (on average, 4.4 KAMs per report), the average number of KAMs in the European banking sector is higher than the average across industries, as resulting from other studies on this subject matter. The average number of KAMs across industries in reports that we could identify (cross industries and not limited to EU), is below 4 KAMs per report.¹²

The range in the number of KAMs spreads from a **minimum of 1 KAM per report** (one bank in Germany and one in Luxembourg) to a **maximum number of 8 KAMs per report** (six banks: two from the UK, two from Portugal, and France and Spain – each with one bank). In addition, a higher average number of KAMs was reported in UK and Portugal (7 KAMs per report) and the lowest number in Luxembourg (2 KAMs per report).

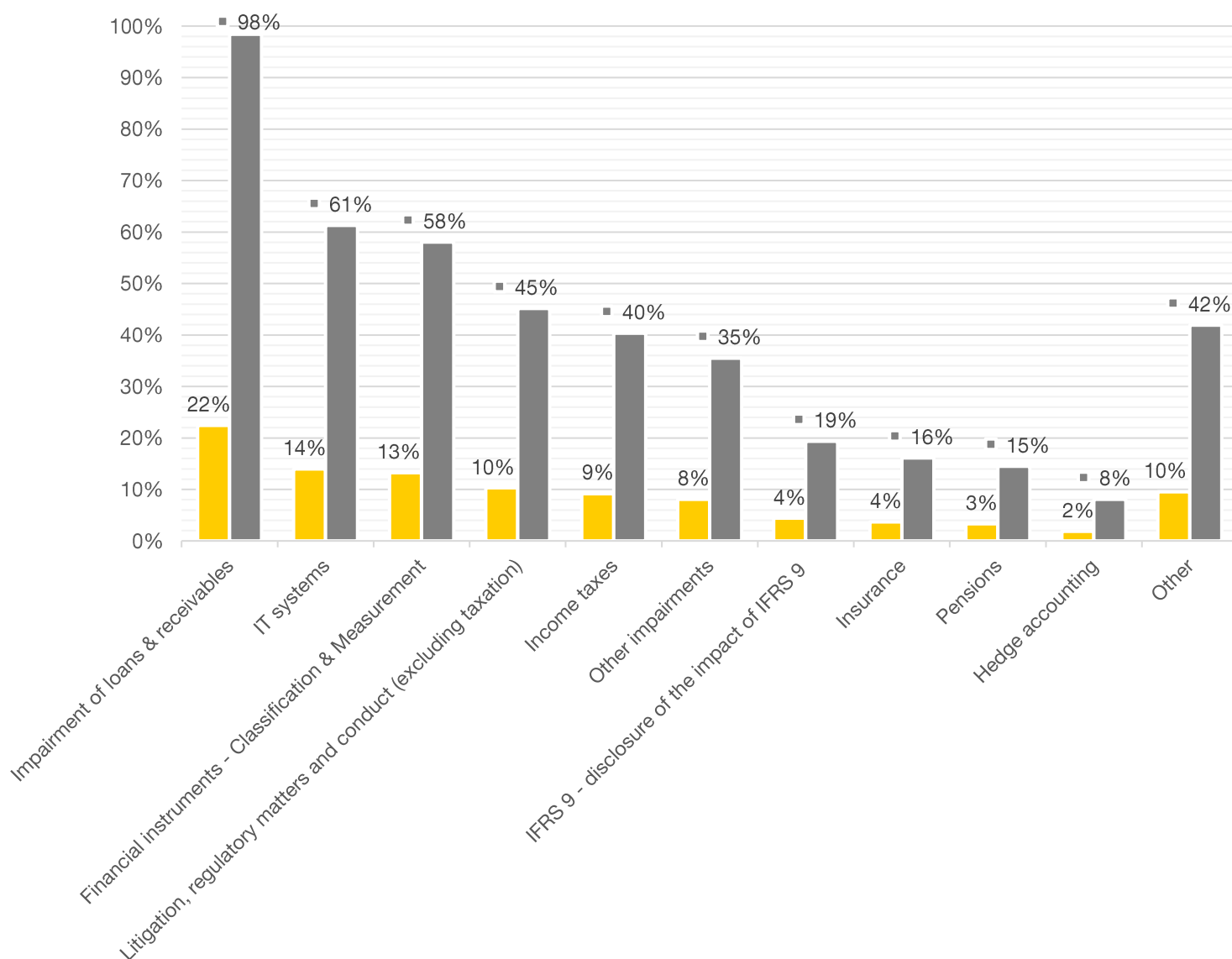


¹² ACCA, *Key Audit Matters, Unlocking the Secrets of the Audit*, 2018 (pg.19: the average number of KAMs ranged from 1.9 in the industrial sector up to 3.9 in telecom sector); <https://graduate.accaglobal.com/gb/en/technical-activities/technical-resources-search/2018/march/key-audit-matters.html>
 KPMG, *Key Audit Matters, Auditor's Report Snapshot*, 2017 (pg.7: the average number of KAMs across industries was 2.8); <https://home.kpmg.com/au/en/home/insights/2017/09/key-audit-matters-auditor-report-20-september-2017.html>
 Deloitte, *Benchmarking of the New Auditor's Report*, 2017 (pg.3: the average number of KAMs across industries was 2.8); <https://www2.deloitte.com/ch/en/pages/audit/articles/benchmarking-the-new-auditors-report.html>
 Mazars, *Les nouveaux rapports des commissaires aux comptes* (pg.8: the average number of KAMs across industries was 3.3); <https://www.mazars.fr/Accueil/News/Publications>

MAIN CATEGORIES AND RECURRENCE

We have categorised the 272 matters reported as KAMs in **ten main categories** of recurring items, as outlined in the chart below. The top ten main categories represent **90% of the KAMs** in the analysed sample. The KAMs which did not fall in one of the top ten categories were included in a separate bucket, *Other*, for the purpose of our analysis.

MAIN KAM CATEGORIES
(TOP % REPRESENTS THE % OF THE TOTAL NUMBER OF AUDIT REPORTS (62))
LOWER % REPRESENTS THE % OF THE TOTAL POPULATION OF KAMs (272))



The **top three recurring KAM categories** represent **49% of the total number of KAMs** in the analysed population. As expected, the main recurring KAMs in the banking sector are related to financial instruments (35% of the total number of KAMs):

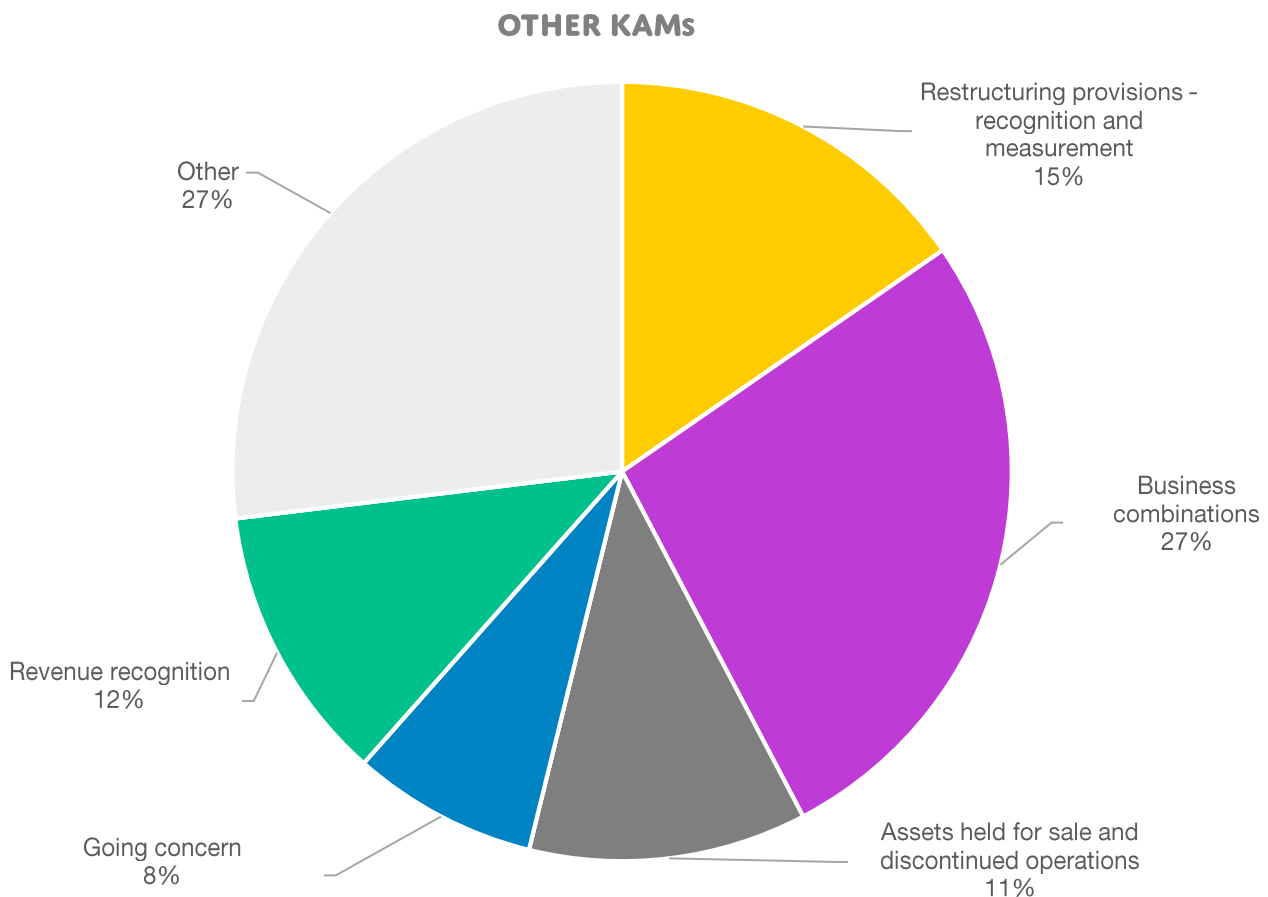
- impairment of loans and receivables: this KAM appears in 98% of the audit reports in the scope of our survey (22% of the total number of KAMs)
- classification and measurement of financial instruments: this KAM appears in 58% of the audit reports in the scope of our survey (13% of the total number of KAMs)

Interestingly, the second of the top three recurring KAM categories is related to IT systems which appears in 61% of the audit reports (14% of the total number of KAMs), highlighting the importance of IT systems and the criticality of IT risks in the banking sector.

As outlined in the chart above, **other main categories of recurring KAM topics** are listed below, while the following section presents the main subcategories of KAMs, where applicable:

- Litigation, regulatory matters and conduct, excluding taxation: 45% of the audit reports (10% of the total number of KAMs)
- Income taxes: 40% of the audit reports (9% of the total number of KAMs)
- other impairments: 35% of the audit reports (8% of the total number of KAMs)
- IFRS 9 – disclosure of IFRS 9 impact: 19% of the audit reports (4% of the total number of KAMs); we note that aspects related to IFRS 9 disclosures were included in the “impairment of loan and receivables” KAM category in some of the audit reports
- Insurance: 16% of the audit reports (4% of the total number of KAMs)
- Pensions: 15% of the audit reports (3% of the total number of KAMs)
- Hedge accounting: 8% of the audit reports (2% of the total number of KAMs)

The KAMs with lower frequency or non-recurring ones are included in the **Other category** and represent 10% of the total KAM population. We have grouped these KAMs in the categories highlighted in the chart below, with the top five categories within this bucket representing 73% of the total number of KAMs in this category:

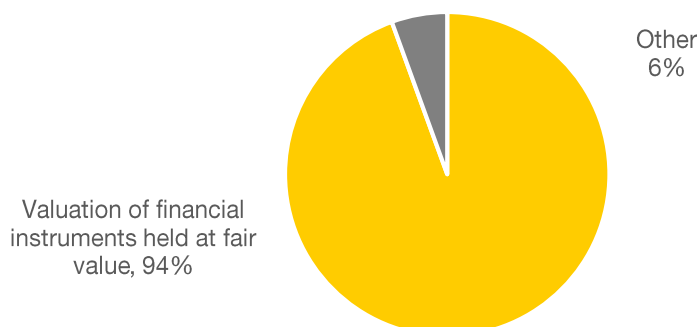


An interesting conclusion is that the *Other* sub-category within this bucket represent only 3% of the total population of KAMs in our sample; therefore the **majority of KAMs are on topics which are recurring in audit reports**. This shows that the key risks in the banking sector are relatively consistent across European banks.

MAIN SUBCATEGORIES

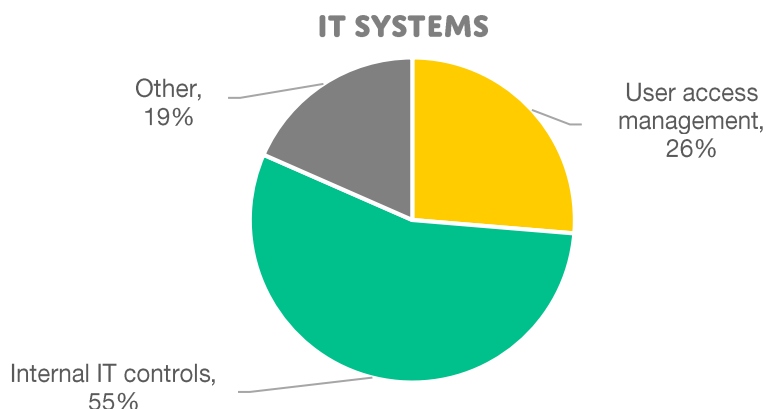
For some of the main KAM categories, we have gone further and identified the following **main recurring sub-categories of KAMs**, as presented in the charts below. However, we note that for some of the main KAM categories, we did not observe notable subcategories (e.g. for *Impairment of loans and receivables* and *Litigation, regulatory matters and conduct*).

FINANCIAL INSTRUMENTS - CLASSIFICATION & MEASUREMENT

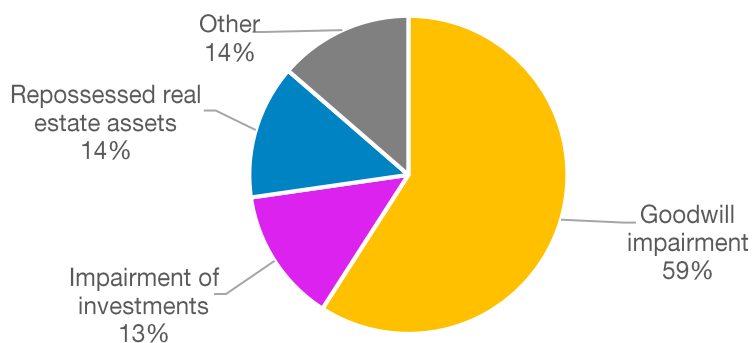


 The majority of KAMs related to *Financial instruments – classification & measurement* were related to the valuation of financial instruments held at fair value (94%).

 KAMs related to *IT systems* were mostly related to user access management (26%) and Internal IT controls (55%).



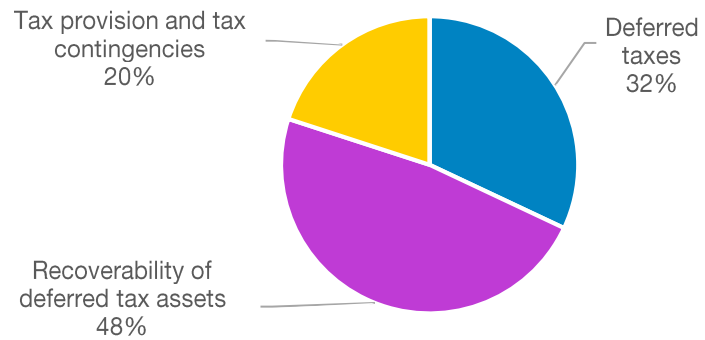
OTHER IMPAIRMENTS



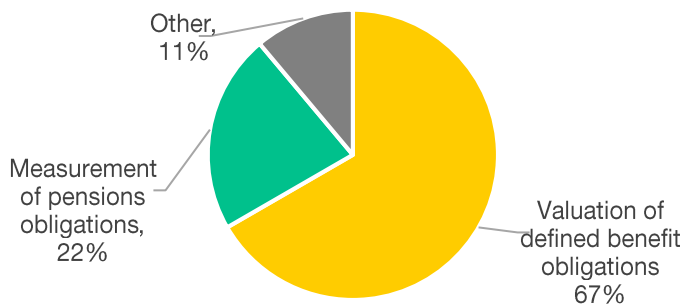
 *Goodwill impairment* is the predominant topic, representing 59% of the KAMs related to Other impairments.

A *Deferred taxes* are the most recurring topic in this category, representing 80% of the total number of KAMs in this category.

INCOME TAXES



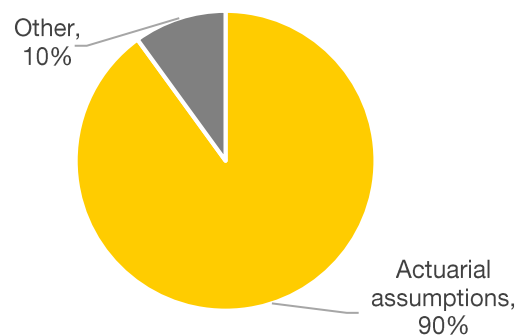
PENSIONS



A The majority of KAMs related to *Pensions* again related to the valuation component – i.e. valuation of defined benefit obligations (67%).

A KAMs related to *Insurance* were overwhelmingly related to the judgmental component – i.e. validation of actuarial assumptions (90%).

INSURANCE



EXAMPLE OF KAMS – MAIN CATEGORIES

To exemplify the ground-breaking value-added by auditor's reporting of KAMs, we have extracted below good practice examples of KAM reporting for the top seven recurring KAM main categories, which represent more than 80% of the total number of KAMs in the analysed sample:

Example 1 – 'Impairment of loans and receivables'¹³

Key audit matter	The risk	Our response
Impairment of loans and advances Charge: \$1,362 million (2016: \$2,791 million) Provision: \$5,707 million (2016: \$6,518 million) Corporate & Institutional Banking (CIB) clients, Commercial Banking (CB) clients and Private Banking clients (collectively 'larger clients') represent 72 per cent (\$264 billion) of the Group's net loan exposure, whereas Retail clients represent 28 per cent (\$103 billion). ➤ Refer to page 64 (Audit Committee Report), page 218 (note 8 Impairment losses on loans and advances and other credit risk provisions) and page 249 (note 16 Loans and advances to banks and customers) including accounting policies	Subjective estimate The carrying value of loans and advances to banks and customers held at amortised cost may be materially misstated if individual or collective impairments are not appropriately identified and estimated. The identification of impaired assets and the estimation of impairment including estimates of future cash flows and valuation of collateral involve significant management judgement. The collective impairment on CIB, CB and Retail loans and advances include overlays to the model calculated collective impairment. These overlays are calculated and assessed based on management's judgement of the performance of the book. The most significant areas are: ➔ Loan exposures in India due to high debt levels and weak balance sheets, regulatory reform and the poor performance of certain sectors such as telecoms and power ➔ Oil and gas support service related exposures following sustained depression of oil prices in prior years	Our procedures included: Control design, observation and operation: We tested the design and operation of manual and automated controls over the individual impairment provision including: ➔ the accuracy of data input into the system used for credit grading and the approval of credit facilities ➔ the ongoing monitoring and identification of loans displaying indicators of impairment and whether they are migrating, on a timely basis, to early alert or to grades 12 to 14 including generation of days past due reports. Assessing overlays: We assessed the adequacy of management overlays to the modelled collective provision for CIB, CB and Retail by recalculating the coverage provided by the collective impairment provision (including overlays) to loan book, taking into account recent loss history, performance and de-risking of the relevant portfolios. We assessed the areas identified as most significant opposite using external data and challenged whether the modelled collective impairment provision already appropriately reflected them or if an overlay was required. Assessing individual exposures: We selected a sample (based on quantitative thresholds) of larger clients where impairment indicators had been identified by management. We obtained management's assessment of the recoverability of these exposures (including individual provisions calculations) and challenged whether individual impairment provisions, or lack of, were appropriate. This included the following procedures: ➔ challenging the recoverability of the forecast cash flows by comparing them to historical performance of the customer and the expected future performance where applicable; and ➔ assessing external collateral valuer's credentials and comparing external valuations to values used in management's impairment assessments For a risk based sample of CIB and CB loans credit grades 1 to 11 not identified as displaying indicators of impairment by management, challenged this assessment by reviewing the historical performance of the customer and formed our own view whether any impairment indicators were present. Our results: We considered the credit impairment charge and provision recognised and the related disclosures to be acceptable (2016: acceptable).

¹³ Standard Chartered, UK, Auditor's report 2017 (KPMG); <https://www.sc.com/annual-report/2017>

Example 2.1.– ‘IT Systems’¹⁴

Risk	Our response to the risk
IT systems and controls Our audit procedures have a focus on IT systems and controls due to the pervasive nature and complexity of the IT environment, the large volume of transactions processed in numerous locations daily and the reliance on automated and IT dependent manual controls. Our areas of audit focus included user access management, developer access to the production environment and changes to the IT environment. These are key to ensuring IT dependent and application based controls are operating effectively.	We tested the design and operating effectiveness of the Group's IT access controls over the information systems that are critical to financial reporting. We tested IT general controls (logical access, changes management and aspects of IT operational controls). This included testing that requests for access to systems were appropriately reviewed and authorised. We tested the Group's periodic review of access rights. We inspected requests of changes to systems for appropriate approval and authorisation. We considered the control environment relating to various interfaces, configuration and other application layer controls identified as key to our audit. Where deficiencies were identified, we tested compensating controls or performed alternate procedures. In addition, we understood where relevant, changes were made to the IT landscape during the audit period and tested those changes that had a significant impact on financial reporting.
Key observations communicated to the Group Audit Committee	
We are satisfied that IT controls relevant to financial reporting operated effectively at year-end. We noticed that a number of user access related deficiencies were identified. Compensating controls were tested or alternate procedures were performed.	
Relevant references in the Annual Report and Accounts	
Report of the Group Audit Committee (page 65) Accounting policies (page 251)	

¹⁴ Royal Bank of Scotland, UK, Auditor's report 2017 (EY); <https://www.investors.rbs.com/annual-report-2017.aspx>

Example 2.2 – ‘IT Systems’¹⁵

Migration of the information systems of the former BPM Group to the Banco BPM platform

Following the completion of the business combination between Banco Popolare Group and BPM Group and in accordance with the related strategic plan, information systems of the former BPM Group- which included accounting systems- were migrated during the year to the new Group platform.

As part of our audit activities, special attention was paid to the migration of accounting systems, considering its operating complexity and possible impacts on financial statements due to the potential risk of incomplete or inaccurate migration of information from the old to the new accounting system.

In performing our audit we paid special attention to the analysis of the methodology defined and applied to the migration, as well as to the test activities planned and performed to address the related risks, including the controls performed by the internal audit function.

With the support of specialists, we analysed and verified that the key controls defined to ensure the completeness and accuracy of migrated data and any additional verification and control eventually deemed necessary in order to address anomalies and exceptions, had actually been performed also verifying, on a sample basis, the complete and accurate migration of accounting balances from the old to the new accounting system.

Furthermore, we carried out specific analyses and checks of the suspense accounts and any rejected transactions, verifying that these were appropriately and timely investigated and followed up.

¹⁵ Banco BPM S.p.A., Italy (PWC); <http://www.bancobpm.it/investor-relations/financials/?lang=en>

Example 3 – ‘Financial Instruments – Classification and Measurement’¹⁶

Financial instruments measured at fair value and classified as level 3 under IFRS 13

Description of our assessment the most significant risks of material misstatement	Summary of our response to the most significant risks of material misstatement
As described in Note 41 to the consolidated financial statements, at December 31, 2017 the Group holds financial instruments valued at fair value amounting to 11.949.365 thousand euros, of which 2.253.128 thousand euros are valued according to valuation techniques using variables not observable in the market (Level 3). The valuation of investments is subjective, given that these financial instruments (level 3) are valued based on internal models or through quotes provided by external entities that include unobservable market parameters. The consideration of this matter as significant to the audit was based on its materiality in the consolidated financial statements and the fact that the use of different valuation techniques and assumptions could give rise to different estimates of fair value.	▶ Understanding of the internal control over the process of valuation of financial instruments; ▶ Use of internal specialists to assess the reasonableness of the assumptions used on the internal valuation model; ▶ Performance of analytical review procedures on the balances of financial instruments comparing with the previous period and expectations in order to obtain an understanding of the variations that occurred with regard to changes in assumptions and methodologies; ▶ On the internal models used we performed the following procedures: (i) understanding of the approved and formal methodology, (ii) analysis, for a sample basis of financial instruments, of the underlying data used in the internal models, (iv) recalculation of the fair value of the financial instruments on a sample basis; ▶ For the recovery funds and close-ended funds, our analysis was based on the latest financial information available and/or the last net asset value disclosed by the management entities of the funds and on the reports by the Group on the value of the underlying assets of the funds; ▶ Analysis of the disclosures included in the Notes 2.8 and 41 to the consolidated financial statements, based on the requirements of International Financial Reporting Standards and on the accounting records.

¹⁶ Caixa Geral de depósitos, Portugal, Annual Report 2017 (EY); <https://www.cgd.pt/English/Investor-Relations/Financial-Information/CGD/2017/Documents/Annual-Report-CGD-2017.pdf>

Example 4 – ‘Litigation, regulatory matters and conduct (excluding taxation)’¹⁷

Key audit matters	How our audit addressed the key audit matters
Description key audit matter 4 – Identification and evaluation of the provisions for legal risk related to litigations <i>(We refer to note 3.7 Provisions in the notes of the Consolidated Financial Statements and to the litigation section in the caption “Risk Management” of the Management Report which is referred to with the note 3.7 where the Board of Directors describes the main litigations that the Group Dexia is facing)</i> In the context of its activities, the Dexia Group is involved in a certain number of legal risks and litigations. The consequences, as assessed by the Group based on the available information at closing date, of the main litigations, including those related to the ‘share leasing’ activities in the Netherlands and the investigations with a potential significant outlook on the financial situation, the results or the assets of the Group, are reflected in the Consolidated Financial Statements. The Group complies with the requirements of IAS 37 for the evaluation and recording of provisions for certain risks. The recording of a provision or contingent liability in order to cover the legal risk requires by nature the use of professional judgment due to the difficulty to estimate the outcome of litigations that may arise. Due to the nature of the current procedures against the Dexia Group and given the estimated character of the provisions, we consider the legal risk and litigations as a key audit matter.	We have assessed the adequacy of the internal control system and tested the operating effectiveness of key controls related to the process of determining the provisions for litigation. These controls mainly concern the identification of the files to be provisioned based on the motives of the dispute and the determination of the amount of the provisions estimated using the methodologies retained by the Dexia Group. Our audit work has focused on the following: • we have conducted discussion with the management and more specifically the Dexia Group’s legal department; • we have examined the motives for the current disputes and have assessed the adequacy of the existence of provisions based on the Group’s assumptions; • we have assessed the principles and assumptions used by the Group to estimate the amount of provisions for litigations; • we have inquired with the law firms with which Dexia is working to obtain and review the assessment made by these lawyers on the status of the litigations. Finally, we have examined the information in the note 3.7 of the Consolidated Financial Statements for provisions.

¹⁷ Dexia, Belgium, Auditor’s report 2017 (Deloitte and Mazars, jointly); http://www.dexia.com/EN/journalist/publications/annual_reports/Pages/default.aspx

Example 5 – ‘Income Taxes’¹⁸

Recognition and Measurement of Deferred Tax Assets

For a description of the significant accounting policies and critical accounting estimates as well as underlying assumptions for the recognition and measurement of deferred tax assets, we refer to Note 1 of the consolidated financial statements “Significant Accounting Policies and Critical Accounting Estimates” (section “Income Taxes”). For information on deferred tax assets, we refer to Note 36 of the consolidated financial statements.

The Financial Statement Risk

The consolidated financial statements contain deferred tax assets of € 6.8 billion. In the reporting period, the Group has reduced the carrying amount of deferred tax assets by € 1.4 billion due to the US tax reform.

Recognition and measurement of deferred tax assets contain judgment and besides objective factors also numerous estimates regarding future taxable profit and the usability of unused tax losses and tax credits.

Our Audit Approach

We conducted a risk assessment to gain an understanding of the applicable tax laws and regulations relevant to the Group. Based on that, we performed both tests of related internal key controls and substantive audit procedures with the assistance of KPMG-internal tax specialists. We performed the following audit procedures as part of our controls testing including, but not limited to:

- evaluation of the policies used for recognition and measurement of deferred tax assets in accordance with IAS 12 and
- test of design, implementation and operating effectiveness of internal controls with respect to recognition of deferred tax assets in the Group.

Furthermore, we performed substantive audit procedures for a risk-based sample of deferred tax assets in different countries. This included, but was not limited to:

- assessment of the appropriateness of parameters applied to the business plans, including sub-plans for relevant countries where appropriate. In doing so, we scrutinized the appropriateness of the planning parameters applied that are relevant to the Group's significant subdivisions by considering potential positive and negative indicators regarding recoverability or occurrence of planning parameters and assumptions, and
- review of the bridge from pre-tax income to the planned taxable profit for certain countries.

Our Observations

Based on the results of our key controls testing and substantive audit procedures we consider recognition and measurement of deferred tax assets in particular regarding the assumptions and parameters to develop the taxable profit and usability of tax losses and credits to be reasonable.

¹⁸ Deutsche Bank, Germany, Auditor's report 2017 (KPMG); available at:
<https://annualreport.deutsche-bank.com/2017/ar/servicepages/welcome.html>

Example 6 – ‘Other Impairments’¹⁹

Determination of goodwill and impairment tests

Risk identified and main judgements

The external growth operations carried out by the BPCE SA group lead it to define the control methods implemented over the acquired entities and to carry out an allocation test of the purchase price from which goodwill and intangible assets recorded in the consolidated balance sheet of BPCE SA group is derived.

Goodwill and intangible assets has been impairment-tested annually at least, based on the assessment of the value in use of the cash-generating units (CGU) to which it is attached or at the first signs of impairment loss. The valuation of the value in use is based on the estimated discounted cash flow of the CGU as resulting from the medium-term plans prepared in accordance with the BPCE SA group's strategic plan for the period 2018-2020 (TEC 2020).

We deemed that the treatment of business combinations and goodwill impairment tests to be a key audit matter by their very nature as they require the exercise of judgment regarding the structuring assumptions used especially for the determination of economic scenarios, financial trajectories or discount levels. Following the announcement of the TEC 2020 strategic plan, we paid particular attention to the impact of this plan on the medium-term plans used to determine value in use and more specifically those with a small difference with the book value.

At December 31, 2017, gross value of goodwill amounted to €4,247 million and accumulated impairment losses stood at €519 million.

The terms of the impairment test implemented by BPCE as well as the key assumptions used to determine the recoverable value and sensitivities of the recoverable amounts are described in note 5.14 to the consolidated financial statements.

Our response

We reviewed the structural transactions made during the year to check the consolidation method used in BPCE SA group's consolidated financial statements and the purchase price allocation work performed by BPCE SA group during the 2017 financial year.

With the help of our experts, we evaluated the procedure implemented by the group to identify signs of potential impairment loss and carried out a critical review of the method used for implementing impairment tests. In particular, our work includes:

- comparison of assumptions and parameters with external sources;
- review of the reasonableness of the medium-term plans retained for each concerned entity involving:
 - the confrontation with the strategic plan of the group approved by the governing bodies (supervisory or administrative) of the entities,
 - the assessment of the consistency and reliability of the main assumptions used to build them especially regarding the financial trajectories developed during the past financial years and actually carried out,
 - the analysis of the sensitivity to different valuation parameters (equity, discount rate...);
- check of the consistency of the information published on the results of these impairment tests.

¹⁹ BPCE, France, Auditor's report 2017 (Deloitte, Mazars and PWC, jointly); <https://www.groupebpce.fr/en/Investors/Results/Registration-documents>

Example 7 – ‘IFRS 9 disclosure of the impact of IFRS 9’²⁰

KEY AUDIT MATTER: DISCLOSURE ON ESTIMATED IMPACT OF IFRS 9 REFER TO THE SECTION ‘EXPLANATION OF THE CONSEQUENCES OF IFRS 9’ IN THE CONSOLIDATED FINANCIAL STATEMENTS

IFRS 9 ‘Financial Instruments’ becomes effective for annual reporting periods beginning on or after 1 January 2018. The possible impact of the application of IFRS 9 needs to be disclosed as required by IAS 8. As it is expected that IFRS 9 will have a significant impact on the 2018 financial statements of financial institutions, we believe that the disclosure will likely be important to stakeholders. Given the estimated impact of this new accounting standard on the opening balance sheet as at 1 January 2018 and the accounting policy choices and assumptions to be taken by management on the implementation of IFRS 9, we consider this a key audit matter in our audit.

The key judgements and estimation uncertainty specific to IFRS 9 is primarily linked to the following elements:

- On classification and measurement of financial instruments, management has performed an assessment to conclude whether the cash-flows from financial instruments fulfil the solely of payment of principal and interest criteria (‘SPPI’). In particular, for structured interest-bearing securities classified as contractually linked or non-recourse, management has to apply judgement as IFRS 9 requires an entity to ‘look through’ a financial instrument to the underlying asset pool to conclude that it comprises of financial instruments that meet SPPI or includes financial instruments that align specified cash flow mismatches or reduce cash flow variability. This makes the assessment complex and creates a high hurdle to demonstrate that an instrument meets the SPPI test. The expected impact of classification and measurement on the opening balance sheet as at 1 January 2018 based on IFRS 9 amounts to € 5 million positive.
- With respect to hedge accounting there are no implications for macro hedge accounting as IAS 39 remains in force in 2018. Micro hedge accounting has changed under IFRS 9. The key change for BNG Bank on micro hedge accounting is that cross-currency basis risk of a derivative contract can be separated and excluded from the designated hedging instrument and treated as cost of hedging. This means that fair value movements arising from the cross-currency basis spread included in the valuation of derivatives which are used in hedge accounting can be separated and accounted for as cost of hedging within OCI and accumulated in in a separate item in equity and subsequently reclassified to profit or loss in the same periods during which the hedged expected future cash flows affect profit or loss. In doing so, management has to apply judgment since there is no single method for separating the cross-currency basis spread from a derivative, separation of the cross-currency basis spread from a derivative is a technically complex area and thus requires significant valuation expertise. The cash flow hedge reserve will decrease from € 193 million positive to € 19 million positive and the new cost of hedging line item will amount to € 22 million positive in the opening balance sheet as at 1 January 2018 based on IFRS 9.
- The new impairment rules in IFRS 9 lead to an increase in complexity and in the degree of judgement required to calculate the expected credit losses. Amongst other things, this applies to the choices and judgements made in the impairment methodology, including the determination of the probability of default (‘PD’), the loss given default (‘LGD’) and the exposure at default (‘EAD’). With the introduction of IFRS 9, these calculations must also take into account forward-looking information (‘FLI’) of macro-economic factors considering multiple scenario’s. Mainly with respect to the PD and LGD used in the expected credit losses, management has applied significant judgement given the low default character of the bank’s loan portfolio. As a result there is limited internal historical data to support and back-test the PD and LGD. The estimated impact of impairments on the opening balance sheet as at 1 January 2018 based on IFRS 9 amounts to € 28 million.

²⁰ Bank Nederlandse Gemeenten N.V., Netherlands, Auditor’s report 2017 (PWC); <https://www.bngbank.com/financials/annual-report>

Example 7 – 'IFRS 9 disclosure of the impact of IFRS 9' ('continued')

HOW OUR AUDIT ADDRESSED THE MATTER

Regarding the accounting policy choices we reviewed the prospective accounting policy to determine whether this has been set up in accordance with the requirements of IFRS 9. We challenged management on their accounting policy choices judgements and they provided us with reasonable explanations and evidence supporting the judgements. We obtained an understanding of the client's implementation process for determining the possible impact of adoption, including an understanding of the entity's systems, processes and controls.

For the estimated impact of IFRS 9 in connection with impairments, our audit work including understanding and evaluating the controls in place to determine individual credit ratings and tested the design and operating effectiveness of controls to the extent possible. Based on this work performed, we concluded that, to the extent relevant to our audit, we could rely on these controls for the purposes of our audit.

Our audit work comprised of the following procedures:

- In connection with classification and measurement we paid specific attention to the SPPI test performed for structured interest-bearing securities. We reperformed a sample of SPPI tests performed by management and in addition, performed an independent SPPI test on a sample of financial instruments. Our sample was risk based and covered a range of different type of financial assets taking the complexity into consideration. As part of our testing we analysed supporting documents (mainly transaction documentation such as prospectuses and term sheets) to evaluate whether the SPPI requirements in IFRS 9 are met.
- For IFRS 9 hedge accounting, with the assistance of our valuation specialists, we tested the appropriateness of the valuation methodology applied in the separation of the cross-currency basis spread from a derivative. Furthermore, we have compared input data used in the separation of the cross-currency basis spread to independent sources and external available market data.
- We inspected hedge documentation of the hedging relationship and evaluated that the hedge accounting policies and documentation meets the hedge effectiveness requirements.
- We assessed the governance over the impairment models used, including the model documentation prepared by management and the reasonableness and frequency of overlays applied and validated that internal ratings are approved by the credit risk committee.
- For impairments, we assessed, with the assistance of our specialists, that the impairment methodology and model applied by BNG Bank are in accordance with the requirements of IFRS 9. We evaluated, amongst others, the validation procedures performed by management experts relating to the FLI model, that the impairment methodology and judgements taken by management comply with IFRS 9. We validated that multiple scenarios are taken into consideration for determining the FLI and reconciled the macro-economic factors used to external data.
- – Finally we assessed the PD and LGD applied by management in the impairment calculation. In doing so, we assessed how management analysed and applied the limited internal historical default data available supplemented with limited available external data-points such as external credit ratings.

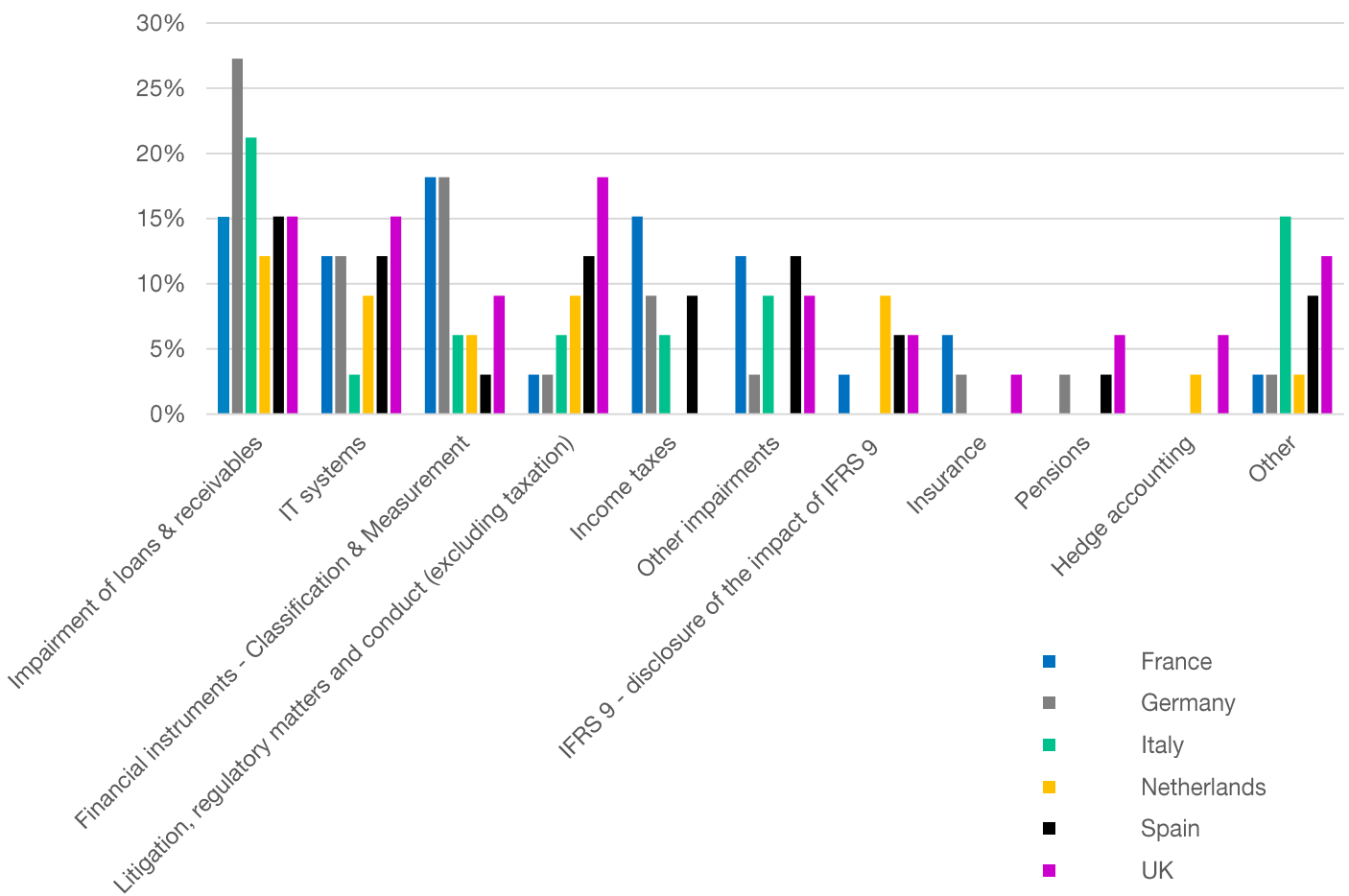
We found no material exceptions during our testing described above. We obtained the opening balance sheet of 1 January 2018 prepared under the IFRS 9 accounting policies and tested the reconciliation with the ending balance of 31 December 2017 prepared in accordance with IAS 39 and evaluated the differences. Finally, we assessed the adequacy of the IAS 8 disclosures as to the expected impact, the status of the implementation effort to date and the extent to which the entity has evaluated the possible impact. We also evaluated that the disclosures adequately reflect the significant uncertainties that exist around the application and implementation of IFRS 9.

EU COMPARISON

As outlined above, one of the benefits of the extended audit reporting is that it enables benchmarking and comparison. To demonstrate this, we have compared **main KAM categories reported for the financial institutions registered in six representative EU countries** (representing 33 banks out of the total sample of 62 banks).

While we note similarities between the main recurring KAM categories across jurisdictions, we also observed the outliers and different risk patterns, as outlined in the chart below:

COMPARISON OF MAIN KAM CATEGORIES ACROSS MAIN EU JURISDICTIONS



Note: The percentages shown in the chart above represent the distribution of each main KAM category per country. For example, the French banks which have the KAM category 'Impairment of loans & receivables' represent 15% of the total number of banks analysed in the six countries (5 banks out of 33). However, the data series presented above are influenced by the number of banks per country included in our sample.

For example, as highlighted by the chart above, the majority of KAMs reported for German banks within our sample fit in the top three recurring KAM categories, while the Italian banks have more KAMs in the *Other* category. This preliminary analysis could be continued for further insight and more relevant findings, as auditor's reporting on KAMs opens the way for more meaningful sectorial and geographical analysis.

CLEAR CROSS-REFERENCING WITH FINANCIAL STATEMENTS DISCLOSURES

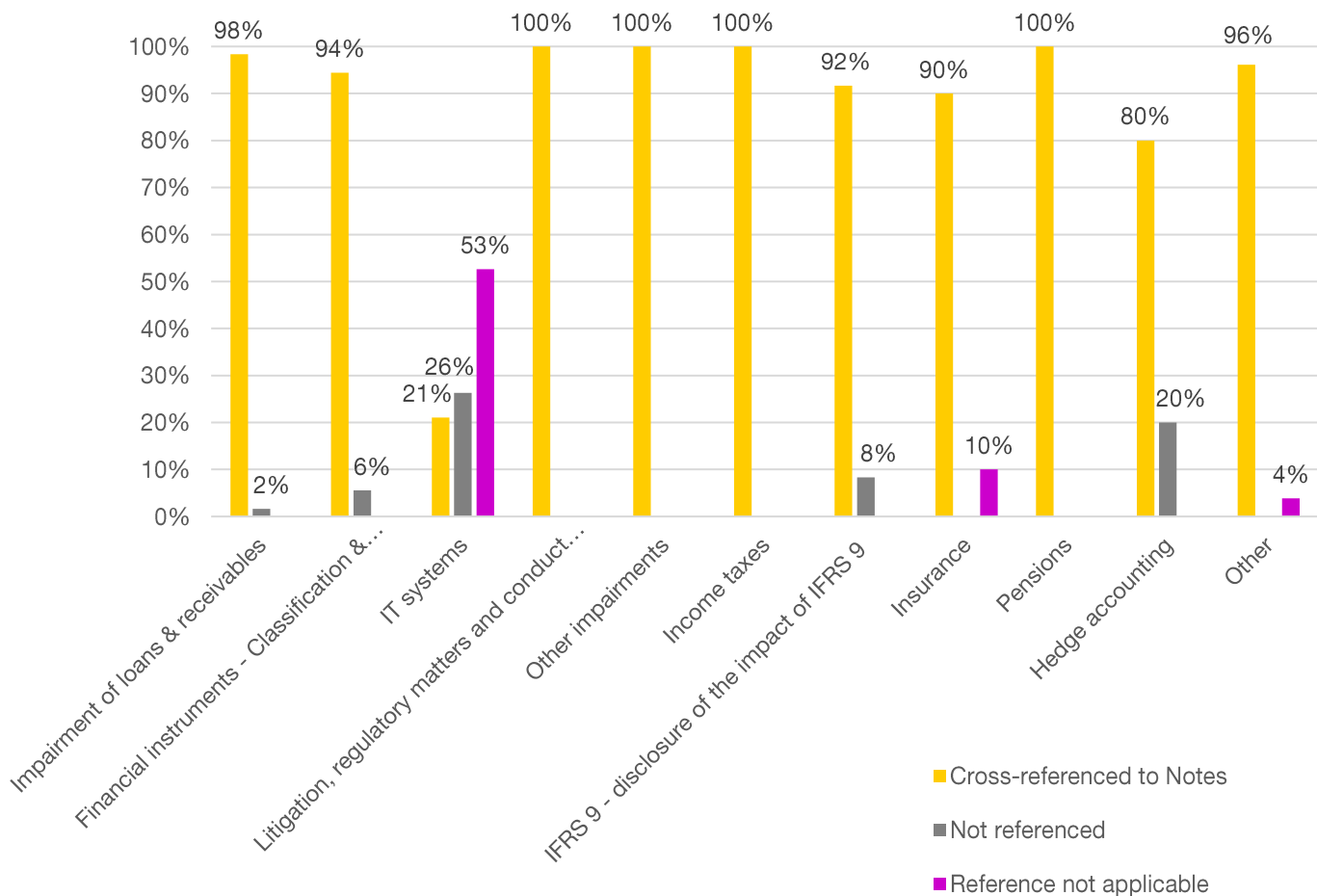
One of the benefits of the new extended audit reporting is that it enhances the understandability of the audit report. However, the auditor’s report should always be perused with reference to the related financial statements for the user to get a complete and accurate picture of issues raised by the auditor.

Auditors cannot and should not include in their auditor’s report all facts and circumstances around each KAM, as they focus on the matters of most relevance, the audit approach taken and conclusions reached. To give a complete picture of KAMs, the audit report includes cross-referencing to the related financial statements which should include more comprehensive disclosures of the matters raised, where applicable.

We have observed the cross-referencing of KAMs to the related financial statements disclosures. As highlighted in the chart below, **the majority of KAMs were clearly linked to the notes to the financial statements.**

However, we note that in some instances, due to the general and indirect financial nature of the KAM (e.g. KAMs related to IT systems), referencing is not applicable. We also note that there is a fine line between *not-applicable* and *missing cross-referencing*, as this is a subjective area.

REFERENCING OF KAMs TO FINANCIAL STATEMENTS DISCLOSURES



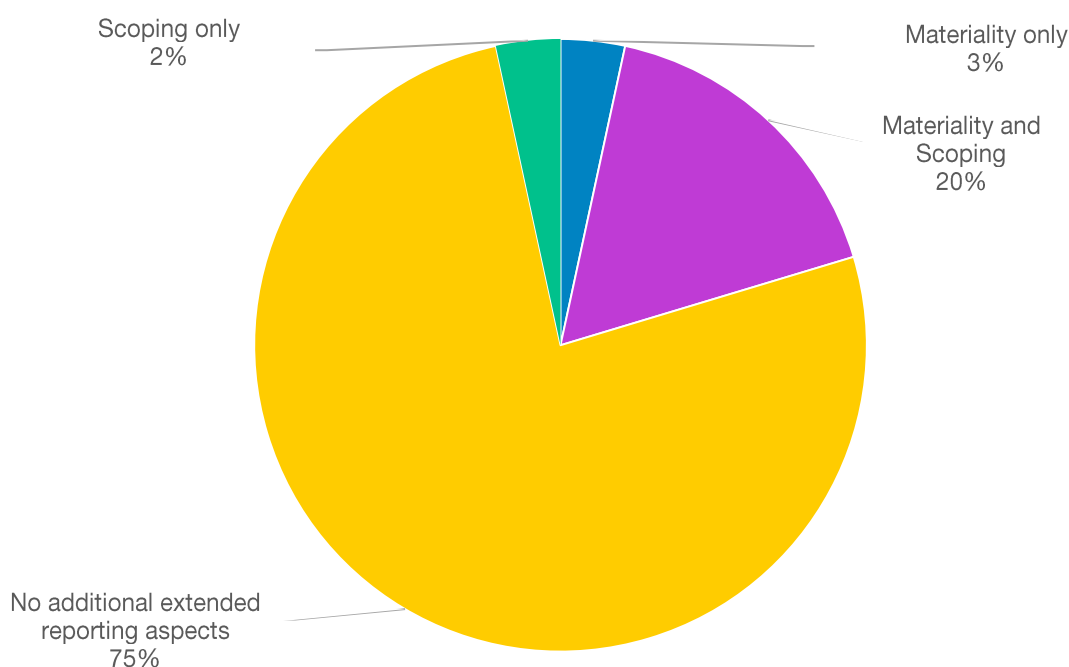
OTHER EXTENDED REPORTING ASPECTS – VOLUNTARY REPORTING

As presented in *Appendix 2* to this paper, in addition to reporting KAMs, some jurisdictions such as the UK and the Netherlands, require auditors of PIEs to include in the auditor's report the following additional extended reporting aspects:

- materiality reporting (benchmark for determining materiality, rationale and percentage used), and
- audit scoping considerations (e.g. the percentage of the operating income, net result or total assets covered by the auditor in carrying out the audit)

For the purpose of analysing other extended reporting aspects we have considered the ISA 701 auditor reporting requirements, according to which reporting on materiality and/or scoping is not required. As shown in the chart below, **a quarter of the banks in our sample had materiality and/or scoping reporting** in their auditor's report:

OTHER EXTENDED REPORTING ASPECTS



In addition to banks from the UK and the Netherlands which have mandatory auditor reporting requirements on scoping and materiality (representing 20% of the analysed sample, as presented in the chart above), we have observed extended reporting elements (materiality or scoping) for banks in Sweden, Finland and Cyprus (in total, representing 5% of our sample), opening the way for the wider adoption of these extended reporting elements.

CONCLUSIONS

AVERAGE NUMBER OF KAMs

With an **average number of 4.4 KAMs per audit report**, our survey shows a higher average number of KAMs reported for financial institutions, by reference to other cross-industries studies on this subject matter. This could be explained by the complexity of banking operations.

MAIN CATEGORIES – KAM CONCENTRATION IN THE EUROPEAN BANKING SECTOR

Our survey reveals a concentration of the KAMs in the European banking sector, as **the top three most recurring KAM topics represent 49% of the total number of KAMs** in the analysed sample, namely:

- *impairment of loan and receivables*: 22% of the total number KAMs (98% of the number of audit reports)
- *IT systems*: 14% of the total number KAMs (61% of the number of audit reports)
- *classification and measurement of financial instruments*: 13% of the total KAMs (58% of the audit reports)

As expected, the main recurring KAMs are related to financial instruments, as the two main categories of KAMs related to this topic represent 35% of the total number of KAMs. KAMs related to IT systems prove to be crucial to the banking systems, representing the second main category (14%). An important correlation that could be made here is that audit firms followed suit to keep up with the complexity of auditing requirements by investing heavily in the IFRS 9, *Financial Instruments* implementation as of 1 January 2018.

The **concentration of the KAMs in this sector** is demonstrated by the fact that non-recurring items represent only 3% of the total KAM population within the scope of our analysis.

KAM COMPARISON AND BENCHMARKING

While 2017 is only the first year of the KAM reporting requirement across the EU, this **opens the way for more in-depth analysis** in the future. Auditors will have to follow-up and explain the year-on-year developments of their key risk assessment, enabling users to perform comparison and benchmarking.

Our comparison of the main KAM categories for the banks registered within the top six EU jurisdictions (making up more than half of our analysed sample) outlines **similarities and specifics in KAM reporting patterns**, paving the way for further and more meaningful analysis.

KAM CLARITY

Generally, KAMs are presented in a clear manner and are easy to peruse and understand, as **most of the KAMs are clearly cross-referenced to the related financial statements disclosures**. Going forward, we consider there is room for improvement in this area, despite the fact that some KAMs are not directly related to financial statements disclosures.

OTHER EXTENDED REPORTING FEATURES

Auditor's reporting on KAMs can be followed by **other extended reporting features**, such as materiality and scoping reporting, which are not required by ISA 701. Overall, 25% of the reports within our sample have materiality and/or scoping reporting (20% representing banks in the UK and the Netherlands with mandatory auditor extended reporting requirements). We welcome auditors' reporting of this information voluntarily.

OTHER GENERAL FINDINGS

Auditor's reporting on KAMs **open the way for more transparent and meaningful audits**, for the benefit of users and stakeholders, at large.

Auditors demonstrated that the profession is responsive to stakeholders' calls for more informative auditor's reports, to ultimately provide **more meaningful information about the company from the auditor's perspective**, in a clear and understandable manner.

Auditor's reporting of KAMs are highly appreciated by stakeholders, especially by the investor's community, **demonstrating the value of auditors in preserving financial stability**. The new auditor's report provides more entity-specific information and makes auditors more accountable to stakeholders, while providing more relevant insights to users.

APPENDIX 1

SAMPLE FOR ANALYSIS

The sample for our analysis consisted of KAMs extracted from the 2017 auditor's reports of the biggest financial institutions across Europe.

The starting point for determining the relevant sample of financial institutions to be analysed was the European Central Bank's (ECB) list of significant supervised entities, under the Single Supervisory Mechanism (SSM), consisting of 118 financial institutions.²¹

However, in order to increase the relevance of our sample, we have adjusted the list of supervised banks under the SSM as follows:

- eliminated the subsidiaries in the ECB SSM listing from the scope of the analysis, to avoid duplication
- since a number of the scoped-out subsidiaries are subsidiaries of large non-Eurozone area financial institutions (Barclays, HSBC, DNB Norway, SEB Sweden and Swedbank Sweden), we kept these banks in the scope of our analysis to have a more relevant sample
- eliminated the smaller entities in the ECB SSM listing (banks with total assets lower than EUR 100 billion)
- in addition, we have added to the list banks from jurisdictions that were scoped-out from our revised sample based on the size criteria but that were considered relevant (Greece, Portugal and Luxembourg)
- in order to enhance the relevance of the analysis, we have added to the sample the top UK and Swiss banks to increase the relevance of the analysed sample

The resulting sample for our analysis consisted of 62 European banks, which own the vast majority of the assets in the European banking sector. We consider the sample listed below to be a highly relevant sample for our analysis:

Crt. No.	Bank Name	Country	ECB Size Criteria
1	Erste Group Bank AG	Austria	total assets EUR 150-300 bn
2	Raiffeisen Bank International AG	Austria	total assets EUR 125-150 bn
3	Belfius Banque S.A.	Belgium	total assets EUR 150-300 bn
4	Dexia SA	Belgium	total assets EUR 150-300 bn
5	KBC Group N.V.	Belgium	total assets EUR 150-300 bn
6	Bank of Cyprus Holdings Plc	Cyprus	total assets above 20 %GDP
7	Hellenic Bank Plc	Cyprus	total assets above 20 %GDP
8	RCB Bank LTD	Cyprus	total assets above 20 %GDP
9	Nordea Bank AB (publ)	Finland	total assets EUR 100-125 bn
10	OP Osuuskunta	Finland	total assets EUR 100-125 bn
11	BNP Paribas S.A.	France	total assets above EUR1,000 bn
12	BPCE S.A.	France	total assets EUR 500-1000 bn
13	Confédération Nationale du Crédit Mutuel	France	total assets EUR 500-1000 bn
14	Crédit Agricole S.A.	France	total assets above EUR1,000 bn
15	La Banque Postale	France	total assets EUR 150-300 bn
16	Société Générale S.A.	France	total assets above EUR1,000 bn
17	Bayerische Landesbank	Germany	total assets EUR 150-300 bn
18	COMMERZBANK Aktiengesellschaft	Germany	total assets EUR 300-500 bn
19	Deutsche Bank AG	Germany	total assets above EUR1,000 bn

²¹ Significant supervised entities, under the Single Supervisory Mechanism; available at: <https://www.bankingsupervision.europa.eu/banking/list/who/html/index.en.html>

Crt. No.	Bank Name	Country	ECB Size Criteria
20	DZ BANK AG Deutsche Zentral – Genossenschaftsbank	Germany	total assets EUR 300-500 bn
21	Landesbank Baden-Württemberg	Germany	total assets EUR 150-300 bn
22	Landesbank Hessen-Thüringen Girozentrale	Germany	total assets EUR 150-300 bn
23	Norddeutsche Landesbank – Girozentrale	Germany	total assets EUR 150-300 bn
24	NRW.BANK	Germany	total assets EUR 125-150 bn
25	Alpha Bank, S.A.	Greece	size (total assets EUR 50-75 bn)
26	Eurobank Ergasias, S.A.	Greece	size (total assets EUR 50-75 bn)
27	National Bank of Greece, S.A.	Greece	size (total assets EUR 75-100 bn)
28	Piraeus Bank, S.A.	Greece	size (total assets EUR 75-100 bn)
29	Bank of Ireland Group plc	Ireland	total assets EUR 100-125 bn
30	BANCA MONTE DEI PASCHI DI SIENA	Italy	total assets EUR 150-300 bn
31	Banco BPM S.p.A.	Italy	total assets EUR 125-300 bn
32	Intesa Sanpaolo S.p.A.	Italy	total assets EUR 500-1,000 bn
33	UniCredit S.p.A.	Italy	total assets EUR 500-1,000 bn
34	Unione di Banche Italiane S.p.A	Italy	total assets EUR 100-125 bn
35	Banque et Caisse d'Epargne de l'Etat	Luxembourg	size (total assets EUR 30-50 bn)
36	J.P. Morgan Bank Luxembourg S.A.	Luxembourg	total assets above 20 % of GDP
37	RBC Investor Services Bank S.A.	Luxembourg	total assets above 20 %GDP
38	Bank of Valletta plc	Malta	total assets above 20 %GDP
39	MDB Group Limited	Malta	total assets above 20 %GDP
40	ABN AMRO Group N.V.	Netherlands	total assets EUR 300-500 bn
41	Bank Nederlandse Gemeenten N.V.	Netherlands	total assets EUR 150-300 bn
42	Coöperatieve Rabobank U.A.	Netherlands	total assets EUR 500-1000 bn
43	ING Groep N.V.	Netherlands	total assets EUR 500-1,000 bn
44	Banco Comercial Português, SA	Portugal	size (total assets EUR 50-75 bn)
45	Caixa Geral de Depósitos, SA	Portugal	size (total assets EUR 75-100 bn)
46	Novo Banco, SA	Portugal	size (total assets EUR 30-50 bn)
47	Nova Ljubljanska Banka d.d. Ljubljana	Slovenia	total assets above 20 %GDP
48	Banco Bilbao Vizcaya Argentaria, S.A.	Spain	total assets EUR 500-1,000 bn
49	Banco de Sabadell, S.A.	Spain	total assets EUR 150-300 bn
50	Banco Santander, S.A.	Spain	total assets above EUR1,000 bn
51	BFA Tenedora De Acciones S.A.U.	Spain	total assets EUR 150-300 bn
52	CaixaBank, S.A.	Spain	total assets EUR 300-500 bn
53	DNB	Norway	<i>not supervised under the SSM</i>
54	Barclays	UK	<i>not supervised under the SSM</i>
55	HSBC	UK	<i>not supervised under the SSM</i>
56	Lloyds	UK	<i>not supervised under the SSM</i>
57	RBS	UK	<i>not supervised under the SSM</i>
58	Standard Chartered	UK	<i>not supervised under the SSM</i>
59	SEB	Sweden	<i>not supervised under the SSM</i>
60	Swedbank	Sweden	<i>not supervised under the SSM</i>
61	UBS	Switzerland	<i>not supervised under the SSM</i>
62	Credit Suisse	Switzerland	<i>not supervised under the SSM</i>

APPENDIX 2

COMPATIBILITY OF THE INTERNATIONAL AND EU KAMS REQUIREMENTS

Our briefing paper *Recent Developments in Auditor Communication*²², compares the revised EU legislation from 2014 with the revised international auditing standards and concludes that they are compatible. This means that an audit report prepared under EU law complies with the standards set by the IAASB. While the wording in the EU legislation is not the same as in ISA 701, the latter providing more guidance, the outcome for the audit report is expected to be the same.

The UK and the Netherlands, among others, already required reporting on KAMs before the EU Regulation and ISAs. Moreover, the requirements in the UK and Netherlands also include extended reporting requirements on materiality determinations and scoping considerations in addition to KAMs reporting, as outlined in the table below:

KAM/ extended reporting requirement	EU Regulation 537/2014	IAASB ISA 701	UK ISA UK 701 ²³	Netherlands Standard 702N ²⁴
Description/identification of the most significant assessed risks of material misstatement	✓	✓	✓	✓
Auditor's response to the identified risks	✓	✓	✓	✓
Description of key observations/outcomes with respect to the identified risks	✓ shall be included where relevant	✓ shall be included where relevant	✓ shall be included where relevant	✓ shall be included where relevant
Reference to the relevant disclosures in the financial statements	✓ shall be included where relevant	✓ shall be included where relevant	✓ shall be included where relevant	✓ shall be included where relevant
Materiality considerations	✗	✗	✓	✓
Scope of the audit considerations	✗	✗	✓	✓ for group audits

Also, we note that in France, auditors of PIEs were required to report '*Justifications of assessment*' – a similar concept to KAMs – starting in 2003.

As shown in the table comparing the differing EU reporting frameworks, auditors in the UK and the Netherlands are obliged to include materiality and the scope of the audit in the audit report (the latter relevant only for group audits). Materiality reporting shall specify the threshold used by the auditor for the audit of the financial statements as a whole and explain how the auditor has determined the threshold.

As such, auditor reporting of KAMs opens the way for the profession to provide wider, more meaningful and transparent information to interested stakeholders.

²² Accountancy Europe, *The Functioning of Audit Committees* (2015); <https://www.accountancyeurope.eu/publications/fee-issues-a-briefing-paper-on-recent-developments-in-auditor-communication/>

²³ ISA (UK) 701; [https://www.frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/ISA-\(UK\)-701.pdf](https://www.frc.org.uk/Our-Work/Publications/Audit-and-Assurance-Team/ISA-(UK)-701.pdf)

²⁴ English version of the Standard 702N Additions regarding the reporting on a complete set of general purpose financial statements at a public interest entity; https://www.nba.nl/Documents/Wet%20en%20Regelgeving/Adviescollege%20voor%20Beroepsreglementering/naar%20een%20uitgebreide%20controleverklaring/NBA_Voorlichtingsbrochure_New_auditors_report.pdf

APPENDIX 3

SOME SPECIFIC ASPECTS ON KAM REPORTING

MODIFICATIONS TO THE AUDITOR'S REPORT ARE NOT KAMs: ISA 701 clearly mentions (*paragraph 12*) that matters resulting in modifications to the auditor's report (qualifications), shall not be communicated as KAMs. These matters are highlighted separately under the section of basis for opinion.

GOING CONCERN ISSUES: Another particular topic addressed by ISA 701 (*paragraph 15*) is that a material uncertainty related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern shall not be reported as a KAM if the matter is specifically addressed under separate sections of the audit report (e.g. emphasis of matter or qualification). As such, to avoid duplication, significant risks related to the going concern of the company can be reported as KAMs if they did not materialise in a significant uncertainty. It is worth mentioning that the Audit Regulation (EU level) does not make this distinction.

SENSITIVE MATTERS: Under ISA 701 (*paragraphs 14.a and A.52*), public disclosure of a specific matter determined by the auditor to be a KAM may be precluded by law or regulations. For example, law or regulation may specifically prohibit any public communication that might prejudice an investigation by an appropriate authority.

According to the standard, it may also be necessary for the auditor to consider the professional ethics requirements of reporting on a specific KAM. The issues considered by the auditor on such decision are complex and involve significant judgment.

However, the standard highlights that instances in which a KAM will not to be communicated in the auditor's report should be extremely rare (*paragraphs 14 and A.53*).

NO KAMs TO REPORT? Under ISA 701, the auditor may state in the KAM section of the audit report that there are not such matters to report. However, this distinction is not made in the EU Audit Regulation.

VOLUNTARY REPORTING ON KAMs: Although reporting on KAMs is required for PIE audits in the EU, ISA 701 leaves room for voluntary reporting in case of non-PIE audits. National law or regulations might also extend the scope of entities for which auditor's reporting on KAMs is required.





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