



**FINANCIAL SUPERVISORY COMMISSION
OF THE
COOK ISLANDS**

Banking Prudential Statement

BPS05

Audit

Objectives and key requirements of this Prudential Statement

This Prudential Statement requires banks to establish appropriate external audit arrangements, in relation to the operations of the institution. The audit arrangements of banks must consider the size, complexity and risk profile of the institution.

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Authority

1. This Prudential Statement is issued by the Financial Supervisory Commission (FSC) in accordance with section 65 of the Banking Act 2011 (the Act).

Application

2. This Prudential Statement is applicable to all financial institutions licensed under the Banking Act 2011.

Definitions

3. This Prudential Statement has used the following terms, which unless otherwise indicated, have the meanings specified below:
 - 3.1. **Approved Auditor** – means the company or firm appointed and approved under section 47(1) of the Banking Act 2011. Refer also to paragraphs 9 to 11 of this Prudential Statement.
 - 3.2. **Auditor Independence** – refer to paragraphs 24 to 27 of this Prudential Statement.
 - 3.3. **Bank** – an entity licensed under the Banking Act 2011.
 - 3.4. **Prudential Requirements** – include requirements imposed by the Banking Act 2011 and prudential statements, conditions on authority and any other requirements imposed by the FSC, in relation to a bank.
 - 3.5. **Special Purpose Engagements** – refer to paragraph 23 of this Prudential Statement.

General Requirements

4. A bank must obtain an annual certified financial audit in accordance with the Act and prepared under International Financial Reporting Standards.
5. For the purposes of this Prudential Statement, a bank must appoint an approved auditor. The approved auditor must be a member of an internationally recognised professional accounting body¹ and highly reputable accounting firm.
6. A bank must set out the terms of engagement of the approved auditor in a legally binding contract between the bank and the approved auditor. The bank must ensure the terms of engagement require the approved auditor to fulfil the roles and responsibilities as specified in this Prudential Statement.

¹ For the purposes of this Prudential Statement the following would be considered internationally recognised accounting bodies: Chartered Accountants Australia and New Zealand, The Institute of Chartered Accountants in England and Wales, or any other professional body or institute approved by the FSC.

7. The costs of preparing and submitting reports, documents and other material required by this Prudential Statement, whether routinely or as part of a special purpose engagement, must be borne by the bank.
8. The FSC expects the auditor to have in place a quality assurance process that ensures that the auditor's internal, and any externally imposed standards, are being fully complied with and will, at a minimum, include: guidelines to be established and implemented requiring concurring partner review of the audit procedures and audit work, and internal quality control reviews of the audit firm's processes and methodology on a regular basis.

Auditor Approval Requirements

9. A bank must obtain prior approval from the FSC of its auditor as required under Section 47 of the Act. FSC approval is required regardless of whether the auditor has already been appointed under other legislation in the Cook Islands. The FSC will assess the proposed auditor for expertise and resources, commitment to continuing professional education, quality assurance reviews, and independence.
10. The FSC's approval of an auditor applies until further notice. The FSC reserves the right to withdraw approval if an auditor no longer meets the criteria laid out above. Where the approved auditor will be assisted in the audit, the counterpart auditor to be assigned must also be approved by the FSC.
11. The auditor must have relevant experience in auditing banks and other financial institutions of comparable size and complexity. In addition, staff must possess sufficient specialised skills appropriate to auditing a bank. In the assessment of resources, the factors to be considered include:
 - 11.1. whether the auditor is an extension of an international firm or a separate legal entity;
 - 11.2. whether the auditor will be undertaking local sign offs or 'full' audits; and
 - 11.3. other financial institutions for which the auditor has audit responsibility.

Fitness and Propriety of the Approved Auditor

12. A bank must ensure that its approved auditor (including the individuals whom are the audit partner and if different, lead auditor):
 - 12.1. is a fit and proper person in accordance with the bank's fit and proper policy as required by *Prudential Statement BPS06 – Fit and Proper*; and
 - 12.2. satisfies the auditor independence requirements set out in this Prudential Statement.

Obligations of a Bank

13. A bank must within 4 months of its annual balance date or at a further time period approved by the FSC submit copies of its financial statements and its auditor's report to the FSC².
14. A bank, if requested by the FSC, must provide the FSC with the terms of engagement, other instructions or correspondence, as well as audit reports and management letters, prepared by the approved auditor, in relation to the bank³.
15. A bank must ensure that the approved auditor has access to all data, information, reports and staff of the bank that the approved auditor reasonably believes is necessary to fulfil its role and responsibilities under this Prudential Statement.
16. A bank must ensure that its approved auditor is fully informed of all prudential requirements applicable to the bank. In addition, the bank must ensure that the approved auditor is provided with any other information the FSC has provided to the bank that may assist the approved auditor in fulfilling its role and responsibilities under this Prudential Statement.
17. A bank must ensure that the following are provided to its Board or Board Audit Committee, or Senior Overseas Officer:
 - 17.1. reports provided by the approved auditor in accordance with this Prudential Statement, and any associated assessments and other material provided by an approved auditor to the bank on request;
 - 17.2. commentary or responses provided by the FSC to the bank on reports provided by the approved auditor, and any associated assessments and other material; and
 - 17.3. any commentary or response on the reports, associated assessments and other material provided by the approved auditor that are given to the FSC by the bank.
18. A bank must notify the FSC in writing if it proposes to terminate its contract with the approved auditor.

Meetings with the Approved Auditor

19. The FSC and an approved auditor may meet, at any time, on a bilateral basis at the request of either party.
20. Where a bank is a subsidiary of a foreign bank, the FSC may meet with the head of the parent company's external auditor and internal auditor.
21. It is the responsibility of the approved auditor to supply all information and documents requested by the FSC relevant to the bank.

² Refer also to section 49(4) of the Banking Act 2011.

³ Refer also to sections 48 & 49 of the Banking Act 2011.

Responsibilities of the Approved Auditor

22. Approved auditors must within 4 months of the annual balance date of a bank, provide to the FSC a report⁴ up to the latest balance date detailing the auditor's opinions as to whether:
 - 22.1. the bank has observed all prudential requirements;
 - 22.2. the statistical and financial data provided by the bank to the FSC are reliable; and
 - 22.3. any matters which, in the auditor's opinion, may have the potential to prejudice materially the financial condition of the bank.

Special Purpose Engagements

23. The FSC may require a bank, by notice in writing, to appoint an auditor, who may be the existing approved auditor or another auditor, to provide a report on an aspect of the bank's operations, prudential reporting, risk management systems or financial position. Such a special purpose engagement report will normally be requested following consultation with the bank⁵. However, the FSC may request such a report without prior consultation with a bank.

Auditor Independence

24. The Board or Senior Overseas Officer must undertake steps to satisfy themselves that the approved auditor is independent of the bank and that there is no conflict of interest that could compromise, or be seen to compromise, the independence of the approved auditor.
25. As part of the process of ascertaining the independence of the approved auditor, a bank must obtain a declaration from the auditor to the effect that the auditor is independent, both in fact and appearance, and has no conflict of interest, and that there is nothing to the auditor's knowledge (either in relation to the individual auditor or any audit firm or audit company of which the auditor is a member or director) that could compromise that independence.
26. For the purposes of this Prudential Statement, a conflict of interest situation exists in relation to a bank if because of circumstances that exist at that time:
 - 26.1. the approved auditor is not capable of exercising objective and impartial judgement in relation to the conduct of the work that is undertaken for the bank in relation to the prudential requirements; or
 - 26.2. a reasonable person, with full knowledge of all relevant facts and circumstances, would conclude that the approved auditor is not capable of exercising objective and impartial judgement in relation to undertaking the work for the bank for the purposes of the prudential requirements.

⁴ Refer also to section 50(1) of the Banking Act 2011.

⁵ Refer also to section 51 of the Banking Act 2011.

27. As stated, unless otherwise approved by the FSC:

- 27.1. A person who was a partner of an audit firm or a director of an audit company, and who served in a professional capacity in the audit of a bank in relation to the prudential requirements, cannot be appointed to the role of director or senior manager of that bank until at least two years have passed since they served in that professional capacity.
- 27.2. A person who was an employee of an audit company and who acted as the lead auditor or review auditor in the audit of a bank in relation to the prudential requirements, cannot be appointed to the role of director or senior manager of that bank until at least two years have passed since they acted as the lead auditor or review auditor.
- 27.3. An individual whom is the audit partner, or the lead auditor in the audit of a bank in relation to the prudential requirements, for five successive years, or for more than five years out of seven successive years, cannot continue to play a significant role in the audit until at least a further two years have passed, except with an exemption from the FSC. The FSC may grant an exemption from this requirement if the individual provides specialist services that are otherwise not readily available, or there are no other individuals available to provide satisfactory auditing services for the bank.

Issuance Details

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