IREFI-IRAIF

Diegem, 18 June 2024

NOTICE TO THE ACCREDITED AUDITORS
NOTICE 2024 / 05

Dear members,

We hereby provide you with the overview of the attention points that could influence your review procedures as of 30 June 2024. These attention points have been compiled in the context of the current legal and regulatory framework of cooperation of the accredited auditors to the prudential supervision by the FSMA and the NBB.

The supervisory authorities and the chairs of the different working groups, supported by the scientific secretariat, have contributed to this letter, by providing the enclosed attention points.

On 14 June 2024, a Capita Selecta session was organized in close cooperation with the NBB, detailing some of the topics mentioned in the attached letter. The slides of this training are available on the ICCI portal (Past events (icci.be)).

The templates of the model reports for prudential reporting as of 30 June 2024 to the NBB and the FSMA are currently being reviewed. The updated versions will be communicated shortly.

Should you have any questions regarding this document, please do not hesitate to contact me, any member of the Board or Veerle Sablon.

Yours sincerely,

DocuSigned by:

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Damien Walgrave
Chairman

Institut des Réviseurs Agréés
pour les Institutions Financières ASBL
Institut Royal
ASBL agréée comme union professionnelle

Instituut van de Revisoren Erkend
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Introduction

The attention items presented in italics have been provided by the supervisory authorities (National Bank of Belgium (NBB) or the FSMA) and include their expectations with regard to the auditor's specific attention points in the context of the 30 June 2024 review procedures and the reporting thereon.

The other attention points have been identified by the members of the respective working groups and consist of items for information of the accredited auditors.

Some of the topics were already discussed in a previous attention points letter.

The accredited auditors will use their professional judgment and decide, based on facts and circumstances, whether the attention points need to be explicitly addressed in the reports to the prudential authorities.

1. Attention matters applicable to all financial institutions

1.1. CSRD, the non-financial information disclosures requirements

Early 2025, the companies that are already within the scope of the NFRD, many of which are financial institutions, will file their CSRD reports based on 2024 data. No specific intervention of the accredited auditor is expected in the context of the 30 June 2024 review procedures.

As from 2026 onwards, the other large companies will also have to apply the new rules of the Corporate Sustainability Reporting Directive. In view of the complexity of the regulation, accredited auditors are encouraged to proactively inquire with the senior management of the (smaller) financial institutions of this second wave about the specific requirements and timing.

We recommend getting acquainted with the institution's concrete project management set-up, timeline and deliverables, to discuss the scoping and double materiality exercise and to assess the level of preparedness in view of the upcoming (limited) assurance requirements for these institutions as from 2026 onwards.

2. CREDIT INSTITUTIONS

2.1. THE IMPACT OF THE CHANGING METRICS ON THE CREDIT INSTITUTIONS

Given the volatility in interest rates, the inflationary context and the low economic growth, we continue to recommend the accredited auditors to take into consideration the risks to which the financial sector is exposed, in particular related to interest rate risk, liquidity risk and credit risk.

It is suggested to put specific attention on the adequate identification, measurement and reporting of risks in the financial and prudential reporting. We recommend considering at least the following elements:

- Management of interest rate risk within an ALM context and the related hedge positions from an accounting and economical perspective (management of caps and floors on floating rate loans, valuation of hedges and sustainability of hedge effectiveness);
- Management of liquidity risk within a competitive environment for higher interest rates on saving products (including an observed shift towards short term maturing deposits), a high focus on reputational risk and more digital banking interactions (hedge relationship, and underlying duration assumptions of core current and savings accounts);
- Management of credit risk within a context of low economical growth and volatile macro-economic indicators. It is suggested to put specific focus on:
    - the sectors that are more exposed in the current economic environment;
    - the governance and the evolutions of the overlays recorded by the institutions to capture the ECL not picked up by the current models, including the evolution of the overlays that were previously recorded to cover the increased expected credit losses; and
    - the back-testing process implemented by the institutions and the related results, the scenarios used in the expected credit loss and any specific sector approaches that would be applied.

We furthermore refer to the sections 2.3 and 2.4 below for the attention points of the NBB and the reporting requirements in relation to these attention points.

2.2. NEW LEGAL PROVISIONS ON REINVESTMENT FEES

Recently, the law modification with respect to the prepayment penalties (reinvestment fees) for mortgage loans in case of refinancing entered into force. The modified legal provisions prohibit credit institutions to charge a reinvestment fee of 3 months' interest when refinancing a mortgage loan internally.

Accredited auditors are recommended to discuss this law modification and the potential impact thereof on the expected prepayments in hedge accounting relationships with senior management of the financial institution and to consider the impacts in the context of the 30 June 2024 review procedures.

2.3. PRUDENTIAL RETURNS OF CREDIT INSTITUTIONS – THE IMPORTANCE OF DATA QUALITY

Over the last two years, the NBB has identified several material errors in different regulatory prudential returns submitted by credit institutions. For example, one credit institution reported wrong figures in the FINREP for the staging of loans, S2 loans being underestimated by EUR 2 billion+ and S1 loans overestimated for the same amount. The source of the errors was to be found in the information system of the corresponding credit institution. The NBB required the credit institution to correct the errors and to resubmit the corresponding FINREP reportings. However, the credit institution was not able to resubmit the data due to deficient IT systems. For a similar incident, the Bank requested the accredited auditor to further investigate on the actions taken by the credit institution and report to the supervisory team.

The Bank reminds that it is of prime importance that credit institutions submit highly accurate and reliable data so that the NBB and the ECB, as competent authorities, can fulfil their supervisory tasks and underlines that not timely correcting and resubmitting supervisory reporting triggers referrals to the competent sanctioning authority ESA. In this regard, the NBB also refers to the EBA guidelines on resubmission of historical data under the EBA reporting framework, published on 8 April 2024 (EBA.GL/2024/04). These guidelines set out a common approach for the resubmission by the financial institutions of historical data to the competent and resolution authorities in case of errors, inaccuracies or other changes in the data reported in accordance with the supervisory and resolution reporting framework developed by the EBA (technical standards, guidelines). In case of errors or inaccuracies, credit institutions must correct data and resubmit the corresponding regulatory reporting(s) within undue delay. The guidelines also require credit institutions to have the technical capabilities to correct data and to resubmit the reportings. The period for which the resubmission is required goes back to one year in the past, except for monthly data for which a different regime is foreseen. These EBA guidelines will soon be transposed in the Belgian framework.

The circular NBB_2017_20 and article 225 of the Belgian Banking Law defines the duty of cooperation of accredited auditors with the prudential supervisory authority of the credit institutions and expects particular attention is granted to the FINREP (paragraph 4.2, page 11) and to the internal control measures implemented to ensure the reliability and accuracy of the financial and prudential reporting (paragraph 4.1.1). In this context, the NBB asks the accredited auditors to increase their focus on the data quality of the EBA reporting framework, especially on the staging and the provisions reported by credit institutions in the FINREP and to report to the NBB on a semi-annual basis on their observations. The Bank further refers to its circular NBB_2017_27 on the Bank's expectations as regards quality of reported prudential and financial data. If necessary, the accredited auditors will have to review the effective measures to ensure quality of reporting implemented by the financial institutions in accordance with the principles taken up in that circular.

In case material errors or inaccuracies are detected by the accredited auditors, indicating that the corresponding reporting(s) do not comply with the EBA guidelines on resubmission of historical data under EBA reporting framework (EBA/GL/2024/04), and in the context of their review procedures, the accredited auditors are expected to report their findings without undue delay and at the latest in their half-year report addressed to the Bank as of 30 June 2024.

2.4. COMMERCIAL REAL ESTATE EXPOSURES

2.4.1. Valuation of real estate collateral, with a focus on Commercial Real Estate

Article 208 (3b) of the CRR requires that, for loans exceeding EUR 3 million or 5% of the own funds of the credit institution, the collateralized property valuation must be reviewed (i.e., revaluation) by an independent and qualified valuer at least every three years. Additionally, 208 (3a), lays down that credit institutions have to monitor property valuations on an annual basis, in addition to revalue them every three years. In these cases, credit institutions can either monitor the value by performing a new appraisal, by reviewing the last appraisal or by using an indexed or statistical valuation method. Moreover, as required in § 200 and § 201 of the EBA Guidelines on management of non-performing and forborne exposures (EBA/GL/2018/06), these monitoring and revaluation requirements become stricter in terms of frequency when the market is subject to significant changes in conditions and when the property value decreases materially relative to general market prices (changes in the market and changes in individual asset value) which appears to be the case nowadays.

The accredited auditors are expected to provide due consideration to the adequacy of the processes applied by credit institutions to reevaluate and report their CRE collateral, considering the potential impact on their capital requirements but also on their credit provisions.

2.4.2. Definition of Default – Unlikely to Pay indicators for credit financing real estate projects

EBA guidelines on the application of the definition of default (EBA-GL-2016-07, § 58) requires institutions to specify in their internal policies and procedures other additional indications of unlikeliness to pay of an obligor, besides those specified in Article 178(3) of Regulation (EU) No 575/2013. Those additional indications should be specified per type of exposures reflecting their specificities. The occurrence of an additional indication of unlikeliness to pay should either result in an automatic reclassification to defaulted exposures or trigger a case-by-case assessment and may include indications based on internal or external information.

The accredited auditors are expected to give due consideration to the adequacy of Unlikely to Pay triggers used for credit financing Commercial Real Estate, ensuring that they consider sufficiently and appropriately the specificities of these exposures and their related risks.

If applicable, and in the context of their review procedures, the Bank expects the accredited auditors to report their findings on the above matters with respect to commercial real estate exposures in their half-year report on the prudential returns as of 30 June 2024.

3. Insurance sector

3.1. Marked-to-model and alternative valuation models

The accredited auditors are expected to give due consideration to the impact of the economic environment on the valuation aspects, impairment testing and the risks associated.

In particular in the context of the review procedures of the 30 June 2024 (Solvency II) reporting, the parameters used in marked-to-model or alternative valuation methods and the results of such valuation should be adequately reviewed for the items on both sides of the balance sheet.

On the assets side, the Bank draws in particular the attention of the accredited auditors on the valuation of the commercial real estate and of the mortgage loans.

3.1.1. Valuation of alternative assets, with a focus on Commercial Real Estate

In the context of rising interest rates and volatility in the Commercial Real Estate (CRE) sector, the Bank has established a dedicated internal task force. As part of the accredited auditors' mission, the Bank emphasizes the importance of ensuring that the valuations of assets linked to commercial real estate are conducted in accordance with Solvency II requirements.

In this context, it is crucial that valuations are properly and frequently updated to reflect the current market conditions. Meetings between the Bank and several insurance companies are scheduled in this regard in the next months, and the valuation of CRE assets in the broad sense will be a key focus.

Therefore, accredited auditors are expected to report to the Bank their findings on the valuation of Commercial Real Estate exposures as of 30 June 2024.

3.1.2. Valuation of mortgage loans

The Bank is consulting with relevant stakeholders (IREFI, Assuralia, and the IA|BE) until the end of July 2024 on recommendations and remarks regarding the valuation of mortgage loans held by insurance companies. The circular, currently under consultation, outlines various valuation methods that can be used for asset valuation. It provides insurance companies with a certain degree of freedom, subject to various safeguards. These safeguards include, but are not limited to, the determination of the chosen methodology, the valuation of a loan at issuance, prepayment models, reference rates, loan characteristics, data usage, and outsourcing.

3.2. Transitional measures on own funds

Since the entry into force of Solvency II, transitional measures ("grandfathering") have made it possible to include in Tier 1 and Tier 2 Capital certain elements of capital which do not initially comply with the requirements of these two tiers, during a transitional period of ten years and as from January 1, 2016. This transitional period will end on January 1, 2026.

The accredited auditors are expected to give due consideration to the quality and coherence of the own funds reporting as well as to the capital management policy of the insurance undertakings benefiting from those transitional measures.

4. INSTITUTIONS OF OCCUPATIONAL RETIREMENT PROVISION (IORPS)

4.1. ATTENTION POINTS TO BE PROACTIVELY DISCUSSED

Regarding the SFDR obligations, the FSMA expects that IORPs managing pension scheme(s) falling under article 8 or article 9 of the SFDR correctly comply with the applicable regulation, in particular regarding the precontractual and periodic information. The provided information must be in line with the SIP and greenwashing is not allowed.

From next year, the DORA regulation will come into force for IORPs. They should prepare for this timely. In first instance, it is important that IORPs check and if necessary amend their contracts with their service providers, start drawing up their register of information in relation to their ICT third-party service providers, revise their policy documents and introduce an incident register.

In the context of their audit procedures as per 31 December 2024, the accredited auditors are recommended to proactively discuss the above matters with the management of the institutions.

Acronyms	
ABO	Accumulated Benefit Obligation
AICB	Alternative Undertakings for Collective Investments
ALM	Asset and Liability Management
AUP	Agreed-Upon Procedures
Belgian GAAP	Belgian Generally Accepted Accounting Principles
BVK/UPC	NL: Beroepsvereniging van het Krediet FR: Union Professionnelle du Crédit
CCyB	Countercyclical Capital Buffer
CET1	Common Equity Tier 1
COREP	Common Reporting
CRD	Capital Requirements Directive
CRE	Commercial Real Estate
CRR	Capital Requirements Regulation
CSM	Contractual Service Margin
CSRBB	Credit Spread Risk in the Banking Book
CSRD	Corporate Sustainability Reporting Directive
DBI/RDT	NL: Definitief Belaste Inkomsten FR: Revenus Définitivement Taxés
DORA	Digital Operational Resilience Act
DTA	Deferred Tax Assets
DTL	Deferred Tax Liabilities
EAD	Exposure at Default
EBA	European Banking Authority
ECB	European Central Bank
ECL	Expected Credit Loss

EIOPA	European Insurance and Occupational Pensions Authority
EPC/PEB	NL: Energieprestatiecertificaat FR: Performance Energétique des Bâtiments
ESAs	European Supervisory Authorities (EBA, EIOPA, ESMA)
ESG	Environmental, Social and Governance
ESMA	European Securities and Markets Authority
EUCLID	European Centralised Infrastructure of Data
FINREP	Financial Reporting (templates requested by the ECB)
FLI	Forward-looking Information
FSMA	Financial Services and Markets Authority
GVV	Gereglementeerde Vastgoed Vennootschap
HDP	High Default Portfolio
HTC	Hold To Collect
IAS	International Accounting Standards
ICB	NL: Instelling voor Collectieve Belegging (Undertakings for Collective Investment (UCI))
IFRIC	IFRS Interpretation Committee
IFRS	International Financial Reporting Standards
IORP	Institutions for Occupational Retirement Provision
IPC	Irrevocable Payment Commitment
IRAIF/IREFI	FR : Institut des Réviseurs Agréés pour les Institutions Financières NL: Instituut van de Revisoren Erkend voor de Financiële Instellingen
IRB	Internal Ratings Based
IRRBB	Interest Rate Risk in the Banking Book
LAC DT	Loss Absorbing Capacity of Deferred Taxes
LCRE	Low Credit Risk Exemption

LGD	Loss Given Default
LSI	Less Significant Institution
MiFID	Markets in Financial Instruments Directive (2014/65/EU)
NAV	Net Asset Value
NBB	National Bank of Belgium
NFRD	Non-Financial Reporting Directive
NPL	Non-Performing Loans
OPC	FR: Organisme de Placement Collectif (Undertakings for Collective Investment (UCI))
ORA	Own-Risk Assessment
PBO	Projected Benefit Obligation
PHL	Prêts Hypothécaires-Hypothecaire Leningen (templates requested by the NBB)
PD	Probability of Default
QRT	Quantitative Reporting Templates
REIT	Real Estate Investment Trust (see also GVV and SIR)
RWA	Risk Weighted Asset
SCR	Solvency Capital Requirement
SFCR	Solvency and Financial Condition Report
SFDR	Sustainable Finance Disclosure Regulation
SI	Significant Institution
SICR	Significant Increase in Credit Risk
SIP	Statement of Investment Principles
SIR	Société Immobilière Réglementée
SME	Small and Medium-sized Enterprise
SPPI	Solely Payment of Principal and Interest

SRB	Single Resolution Board
SREP	Supervisory Review and Evaluation Process
SRF	Single Resolution Fund
SSM	Single Supervisory Mechanism
STE	Short Term Exercise (templates requested by the ECB)
UCI	Undertakings for Collective Investment
UCITS	Undertakings for Collective Investment in Transferable Securities