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Statement of Position

90-5

Inquiries of Representatives of Financial Institution Regulatory Agencies

August 31, 1990

Amendment to
AICPA Industry Audit Guide
Audits of Banks,
AICPA Audit and Accounting Guide
Audits of Credit Unions, and
AICPA Audit and Accounting Guide
Savings and Loan Associations

Prepared by the AICPA Committees on Banking,
Credit Unions, and Savings and Loan Associations

American Institute of
Certified Public Accountants

AICPA

NOTE

This statement of position presents the recommendations of the AICPA Committees on Banking, Credit Unions, and Savings and Loan Associations regarding the application of generally accepted auditing standards to audits of financial statements of banks, credit unions, and savings institutions. Members of the AICPA Auditing Standards Board have found the recommendations in this statement of position to be consistent with existing standards covered by rule 202 of the AICPA Code of Professional Conduct. AICPA members should be prepared to justify departures from the recommendations in this statement of position.

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Inquiries of Representatives of Financial Institution Regulatory Agencies

1. In the last few years, there have been several well-publicized incidents in which a financial institution, as a result of examinations by regulatory agencies, has been required to restate its financial statements on which an independent auditor had rendered an unqualified opinion dated during or subsequent to the period in which such examinations were being conducted.¹ These restatements have resulted from —

- a. Differences in judgment between the examiners² and the financial institution's management regarding, for instance, the adequacy of the allowance for loan losses.
- b. Information and judgments about matters, such as violations of laws or regulations, known to, or made by, the examiners but not known to management or the independent auditor.

2. The objective of this statement of position is to assure that the independent auditor considers regulatory examiners as a source of competent evidential matter in conducting an audit of a financial institution's financial statements.

3. Statement on Auditing Standards (SAS) No. 57, *Auditing Accounting Estimates* (AICPA, *Professional Standards*, vol. 1, AU sec. 342.08) states that the auditor should consider evaluating "information contained in regulatory or examination reports, supervisory correspondence, and similar materials from applicable regulatory agencies." SAS No. 54, *Illegal Acts By Clients* (AICPA, *Professional*

¹ For purposes of this statement of position, the term *financial institution* includes banks, mutual and stock savings banks, savings and loan associations, bank and savings and loan holding companies, and credit unions.

² Examiners acting on behalf of regulators of financial institutions are those individuals responsible for supervising the performance or preparation of the reports of examination or both and, when appropriate, supervisory personnel at the district and national level.

Standards, vol. 1, AU sec. 317.09) notes that “the auditor may encounter specific information that may raise a question concerning possible illegal acts, such as . . . violations of laws or regulations cited in reports of examinations by regulatory agencies that have been made available to the auditor.” Accordingly, it is appropriate that the independent auditor review reports of examination and related communications between examiners and the financial institution to obtain competent evidential matter.

4. Policies of the five federal³ and most state agencies that regulate financial institutions have traditionally allowed an institution’s independent auditor access to certain confidential reports of examinations of the institution. In addition, examiners generally have been permitted to provide pertinent information to the independent auditor with the prior approval of the financial institution. Further, examiners have permitted the independent auditor, with the permission of the financial institution, to attend, as an observer, the exit conference between examiners and the board of directors (or an appropriate board committee) or executive officers of the financial institution or both.

Conclusion

5. Chapter 2 (“Auditing Considerations”) of the AICPA Industry Audit Guide *Audits of Banks*, chapter 2 (“Auditing Considerations”) of the AICPA Audit and Accounting Guide *Audits of Credit Unions*, and chapter 2 (“Auditing—General”) of the AICPA Audit and Accounting Guide *Savings and Loan Associations* are amended to include the following:

Communications Between Independent Auditors and Examiners

The independent auditor should review reports of significant examinations and related communications between examiners and the financial institution and, when appropriate, make inquiries of the examiners. The independent auditor should—

³ The five federal agencies are the Federal Deposit Insurance Corporation, the Federal Reserve Board, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision. Under section 931 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, financial institutions are required to furnish to the independent auditor a copy of the most recent examination report, any supervisory memorandum of understanding with the financial institution, and any report of any action initiated or taken by federal or state financial institution regulatory agencies.

- Request that management provide access to all reports of examinations and related correspondence.⁴
- Review reports of significant examinations and related correspondence between examiners and the financial institution during the period under audit through the date of the independent auditor's report.
- Communicate with the examiners, with the prior approval of the financial institution, when their examination of the financial institution is in process or a report on an examination has not been received by the financial institution.

A refusal by management to allow the independent auditor to review communications from, or to communicate with, the examiner would ordinarily be a limitation on the scope of the audit sufficient to preclude an opinion (see AICPA, *Professional Standards*, vol. 1, AU secs. 508.40 through 508.44). A refusal by the examiner to communicate with the auditor may be a limitation on the scope of the audit sufficient to preclude an unqualified opinion, depending on the auditor's assessment of other relevant facts and circumstances.

In addition, the independent auditor should consider attending, as an observer, with the prior approval of the financial institution, the exit conference between the examiner and the financial institution's board of directors (or an appropriate board committee) or its executive officers or both. Also, if the examiners request permission to attend the meeting between the independent auditor and management or the financial institution's board of directors (or an appropriate board committee) or both to review the report on the audit of the financial statements, and management concurs, the independent auditor should endeavor to be responsive to that request.

Effective Date

The conclusions in this statement of position should apply to audits of financial statements for periods ending on or after September 30, 1990. Earlier application is encouraged.

⁴ Examinations of financial institutions either can be general in nature and comprehend capital adequacy, quality of loans, investments and other assets, and the financial institution's ability to manage liquidity and funding, or they can be targeted to a specific area of the financial institution's operations, such as real-estate lending or trust operations. In addition, examinations may be limited to compliance with laws and regulations applicable to the financial institution—for example, the Bank Secrecy Act, Consumer Protection, Insider Transactions, Municipal Securities Rule Making Board Requirements, or Regulatory Reporting.

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