

**Swiss Federal Banking Commission Circular:
Audit Reports of Banks and Securities Firms
(Audit Reports)
29 June 2005 (Latest amendment: 24 November 2005)**

Contents

| | |
|---|--------------------------|
| I. Introduction | Margin nos. 1-33 |
| A. Scope of application and definitions | Margin nos. 1-5 |
| B. Reporting principles | Margin nos. 6-33 |
| a) Objectives | Margin nos. 6-8 |
| b) Principal elements | Margin nos. 9-11 |
| c) Treatment of financial and regulatory audit reports by the institution's governing bodies | Margin nos. 12-16 |
| d) Reporting at individual and consolidated levels | Margin no. 17 |
| e) Form and content | Margin nos. 18-23 |
| f) Language | Margin no. 24 |
| g) Audit results and opinions | Margin nos. 25-28 |
| aa) <i>Notices of reservation, deadlines and notifications</i> | Margin nos. 25-27 |
| bb) <i>Important information</i> | Margin nos. 28 |
| h) Reporting period | Margin nos. 29-30 |
| i) Submission deadline | Margin nos. 31-33 |
| II. Financial audit report | Margin nos. 34-64 |
| A. Summary of audit results | Margin nos. 35-52 |
| a) Notices of reservation with their set deadlines | Margin nos. 36-39 |
| aa) <i>Notices of reservation with their set deadlines relating to the year under review</i> | Margin no. 38 |
| bb) <i>Notices of reservation with their set deadlines relating to the previous year</i> | Margin no. 39 |
| b) Confirmations relating to the annual financial statements and supervisory reporting | Margin nos. 40-46 |
| aa) <i>Confirmations relating to the annual financial statements</i> | Margin nos. 40-45 |
| bb) <i>Confirmations relating to supervisory reporting</i> | Margin no. 46 |
| c) Confirmations relating to the SFBC's recommendations and formal decisions | Margin nos. 47-48 |
| d) Summary statement regarding net assets, financial position and results of operations | Margin nos. 49-50 |
| e) Important information | Margin nos. 51-52 |
| B. Audit firm's opinions | Margin nos. 53-57 |
| a) Opinion on the organisation and internal control in the preparation of annual and interim financial statements | Margin no. 53 |
| b) Valuation of assets and off-balance-sheet exposures and policies on value adjustments and provisions | Margin no. 54 |
| c) Budgeting and planning | Margin nos. 55-56 |
| d) Response to the previous year's financial audit report by the institution's governing bodies | Margin no. 57 |

| | |
|--|---------------------------|
| C. Net assets, financial position and results of operations | Margin nos. 58-62 |
| a) Balance sheet analysis and commentary on net assets and financial position | Margin no. 60 |
| b) Analysis of income statement and commentary on income situation | Margin no. 61 |
| c) Profitability | Margin no. 62 |
| D. Additional information | Margin no. 63 |
| E. Enclosures | Margin no. 64 |
| III. Regulatory audit report | Margin nos. 65-102 |
| A. Summary of audit results | Margin nos. 66-82 |
| a) Notices of reservation with their set deadlines | Margin no. 67-69 |
| aa) <i>Notices of reservation with their set deadlines relating to the year under review</i> | Margin no. 68 |
| bb) <i>Notices of reservation with their set deadlines relating to the previous year</i> | Margin no. 69 |
| b) Confirmations relating to the adherence to licensing requirements, capital adequacy, large exposure and liquidity rules | Margin nos. 70-74 |
| aa) <i>Confirmation of adherence to licensing requirements</i> | Margin no. 70 |
| bb) <i>Confirmation of adherence to capital adequacy rules</i> | Margin no. 71 |
| cc) <i>Confirmation of adherence to large exposure rules</i> | Margin no. 72 |
| dd) <i>Confirmation of adherence to liquidity rules</i> | Margin nos. 73-74 |
| c) Confirmations relating to the SFBC's recommendations and formal decisions | Margin nos. 75-76 |
| d) Summary statement regarding the risk situation | Margin nos. 77-80 |
| e) Important information | Margin nos. 81-82 |
| B. Audit firm's opinions | Margin nos. 83-94 |
| a) Corporate governance, including personnel segregation of executive management and Board of Directors | Margin no. 84 |
| b) Adherence to generally accepted banking principles for transactions made by members of governing bodies and others with a qualified participation | Margin no. 85 |
| c) Guarantee of proper business conduct | Margin no. 86 |
| d) Internal organisation and internal control system | Margin no. 87 |
| e) Internal audit function | Margin no. 88 |
| f) Compliance function | Margin no. 89 |
| g) Adherence to anti-money laundering regulations | Margin no. 90 |
| h) Adherence to regulations on consolidated supervision | Margin no. 91 |
| i) Audit opinion regarding the additional audit areas specified by the SFBC | Margin no. 92 |
| j) Audit opinion regarding the in-depth audit | Margin no. 93 |
| k) Response to the previous year's regulatory audit report by the institution's governing bodies | Margin no. 94 |
| C. Risk situation | Margin nos. 95-100 |
| a) Risk policy | Margin no. 95 |
| b) Developments in material risk categories | Margin no. 96 |
| c) Opinion regarding the risk situation and the management of identified material risks | Margin nos. 97-100 |
| D. Additional information | Margin no. 101 |
| E. Enclosures | Margin no. 102 |
| IV. Effective date | Margin no. 103 |
| V. Transitional provision | Margin no. 104 |

Appendices:

- Appendix 1: Minimum structure of the financial audit report
- Appendix 2: Minimum structure of the regulatory audit report
- Appendix 3: Key figures system
- Appendix 4: Report on the ten largest borrowers

I. Introduction

A. Scope of application and definitions

This Circular applies to external auditors as defined in Art. 20 of the Swiss Federal Banking Act (BA) and Art. 18 of the Swiss Federal Stock Exchanges and Securities Trading Act (SESTA), hereinafter referred to as “audit firms”. 1

This Circular governs the form and content of annual reports prepared by audit firms in accordance with Art. 19 (1) BA and Art. 17 (1) SESTA on the results of their audits of banks and securities firms at individual and consolidated levels (“audit reports”). 2

The Swiss Federal Banking Commission (SFBC) may issue additional guidelines on the form and content of audit reports for large banks and special cases. 3

The term “institutions” is used in this Circular to mean all banks, securities firms and financial services groups or conglomerates that are subject to supervision by the SFBC. 4

All terms in *italics* are explained in SFBC Circular 05/1 Audit (Appendix 2: Glossary). 5

B. Reporting principles

a) Objectives

Audit reports are a key source of information for the SFBC. They are an indispensable means of acquiring the information needed for supervision and of identifying institutions for which supervisory measures are required, in particular in accordance with Art. 23^{bis}, 23^{ter}, 23^{quater} and 23^{quinquies} BA or Art. 35 and 36 SESTA. For the governing bodies of the audited institution, audit reports are an essential tool to help them exercise their duties. 6

Audit reports present the results of the financial audit and regulatory audit performed in accordance with internationally recognised auditing principles and the applicable Swiss industry standards (SFBC Circular 05/1 Audit). They are tailored to each specific case. 7

The International Standards of the International Auditing and Assurance Standards Board (IAASB) and the US Generally Accepted Auditing Standards (US-GAAS) are considered to be internationally recognised auditing principles. The applicable Swiss industry standards are the Audit Standards of the Swiss Institute of Certified Accountants and Tax Consultants. The SFBC’s rules on auditing institutions (SFBC Circular 05/1 Audit) are also applicable. 8

b) Principal elements

Audit reports consist of two separate parts: the financial audit report and the regulatory audit report (SFBC Circular 05/1 Audit). The details of the form and content of these two parts are set out in margin nos. 34-102. Duplications in reporting should be avoided. In particular, any notice of reservation or other statements and findings must only be included in one part of the report – the financial audit report or the regulatory audit report – depending on the area concerned. 9

The two parts of the report can be submitted to the recipients designated in Art. 21 BA and Art. 19 SESTA at different times. 10

The regulatory audit report and the financial audit report must be signed by the lead auditor and one other employee of the audit firm with signing authority (Art. 46 (2) of the Banking Ordinance (BO), Art. 8 (1) of the SFBC’s Stock Exchanges and Securities Trading Ordinance (SESTO-SFBC)). 11

c) Treatment of financial and regulatory audit reports by the institution’s governing bodies

The Board of Directors¹ must discuss the regulatory audit report and the financial audit report, and minutes must be taken of their discussion (Art. 48 BO). Art. 10 (2) of the Foreign Banks Ordinance applies to branches of foreign banks. 12

The lead auditor attends these meetings and explains the most important findings in the regulatory audit report and the financial audit report, as well as any action that is required. The lead auditor is available to answer questions from the Board of Directors during its in-depth discussion of the financial and regulatory audit reports. 13

The Board of Directors can delegate the in-depth discussion of financial and regulatory audit reports with the lead auditor to an audit committee. However, such delegation does not discharge the Board of Directors from its duty to acknowledge and record its acknowledgement of financial and regulatory audit reports and to discuss their material contents. The audit committee informs the Board of Directors of the material findings of its in-depth discussion on the regulatory and financial audit reports. 14

The Board of Directors and executive management are responsible for ordering any action required to rectify irregularities. 15

The Board of Directors is responsible for forwarding financial and regulatory audit reports to any other parties as appropriate. In doing so, it must ensure that banking secrecy is maintained in accordance with Art. 47 BA. The regulatory and financial audit reports may be forwarded as per Art. 4^{quinquies} BA. 16

d) Reporting at individual and consolidated levels

The results of the financial and regulatory audits at the consolidated level are usually integrated into the financial and regulatory audit reports for the individual institution. This is always the case if the parent company itself engages in banking and/or securities trading operations (parent group of companies). However, if the group is controlled by a holding company, the reporting on the group and the individual institution can be separate. This may be appropriate, for example, if the holding company controls more than one company that engages in banking and/or securities trading operations, or if the Boards of Directors of the holding company and the individual institution or institutions are not one and the same. 17

e) Form and content

In principle, the minimum structures described in margin nos. 34-102 and defined in Appendices 1 and 2 are mandatory. In specific cases, the minimum structure can be upgraded at the lead auditor's discretion, in particular with further subdivisions or additional chapters, though this must be appropriate with respect to the relevance of the facts being presented. 18

In the case of financial services groups and conglomerates, confirmations, opinions and information must be clearly attributed either to the group or to the individual institution. 19

The content of the regulatory and financial audit reports are also defined in margin nos. 34-102 of this Circular. The regulatory and financial audit reports take account of the particular characteristics of the institution being audited. Any additions to the minimum content are made at the lead auditor's discretion and must be appropriate to the relevance of the facts being presented. Any points not applicable to the institution being audited should be mentioned accordingly. 20

Any supplementary written reports (e.g. management letter) must be consistent with the financial and regulatory audit reports. The audit firm keeps an appropriate record, in particular of any *material* shortcomings and important statements, not only in the supplementary written reports, but also in the financial and/or regulatory audit reports. Reference must be made in the financial audit report and/or the regulatory audit report to the supplementary written report (see margin nos. 51 and 81). 21

The audit firm sends the regulatory audit report (including the standard report form "Risk Analysis/Audit Strategy") and the financial audit report to the SFBC both as hard copies and in electronic form. 22

¹ For the sake of simplicity, the term "Board of Directors" is used here instead of, but with the same meaning as, the "governing body responsible for supervision and control".

Strategy”) and the financial audit report to the SFBC both as hard copies and in electronic form.

On request, the SFBC may allow deviations in terms of the form and content of the regulatory and financial audit reports to take into consideration special circumstances. 23

f) Language

Reports are written in German, French or Italian. Under certain circumstances, the SFBC may, on request, allow reports to be written in English, especially when the language abilities of the members of the Board of Directors so require. The audit firm should submit such a request after consulting the institution. The SFBC is entitled to demand that the regulatory and financial audit reports be translated in full or in part into one of Switzerland’s official languages. 24

g) Audit results and opinions

aa) Notices of reservation, deadlines and notifications

If an audit firm discovers breaches of legal provisions or other irregularities, it writes a notice of reservation and sets an appropriate deadline for the irregularities to be rectified (Art. 21 (3) BA, Art. 19 (4) SESTA). In the regulatory audit report and/or the financial audit report, the audit firm explains the materiality and scope of the reservation. Any reservations under Art. 43 (2) BO must be listed in the regulatory audit report and/or the financial audit report under “Notices of reservation” (margin nos. 36-39/67-69). 25

When setting a deadline, the audit firm takes account of the materiality of the reservation. When the deadline has passed, the audit firm performs a follow-up audit. If the actions required to resolve the reservation are not taken within the deadline, a report on the results of the follow-up audit must be submitted to the SFBC without delay (SFBC Circular 05/1 Audit). 26

If the audit firm discovers serious irregularities as defined in Art. 21 (4) BA or Art. 19 (5) SESTA, it must notify the SFBC immediately, rather than wait until it submits the regulatory audit report and/or the financial audit report. It sets out the actions taken to rectify the irregularities since they were reported, as well as details of the current situation in the regulatory audit report and/or the financial audit report. 27

bb) Important information

This section includes matters that are material to the better understanding and clearer interpretation of the audit results, as well as recommendations by the audit firm. 28

h) Reporting period

The reporting period for the financial audit is the financial year (year under review) that ends on the closing date for the annual financial statements (balance sheet date). The reporting period for the regulatory audit can be different, but always covers a full year. The audit firm indicates any deviations from this rule in the regulatory audit and/or the financial audit reports under “Important information” and ensures that there are no gaps in the reporting from year to year. 29

Should the audit firm become aware of matters described in margin nos. 25-27 after the balance sheet date but before submitting its report or of matters that are particularly important to the assessment of the institution’s financial situation and/or adherence to licensing requirements, it includes these in the regulatory audit and/or the financial audit reports. 30

i) Submission deadline

The financial audit report must be submitted to the recipients listed in Art. 21 BA and Art. 19 SESTA within five months of the balance sheet date. The regulatory audit report can be submitted at the same time or at an earlier date, but it must always be submitted within five months of the completion of the regulatory audit. In the interests of timely reporting, earlier submission is particularly appropriate when the regulatory audit is completed much earlier than the financial audit. 31

Audit firms notify the SFBC of their timetable for submitting individual reports every year by the end of December at the latest. If it has good reason to do so, the SFBC can demand changes to the submission dates. 32

The timetable includes the names of the institutions to be audited and the following for every institution to be audited: 33

- the name of the lead auditor
- the date on which the lead auditor assumed responsibility for the institution
- the planned submission date for the financial audit report
- the planned submission date for the regulatory audit report
- the reporting language (margin no. 24)

II. Financial audit report

In the case of financial services groups and conglomerates, confirmations, opinions and information must clearly refer to either the group or the individual institution provided that there are relevant distinctions. If there are no such distinctions, confirmations, opinions and information for the individual institution and the group can be combined. 34

A. Summary of audit results

The summary of audit results for the individual institution and, where appropriate, for the group includes 35

- notices of reservation with their set deadlines relating to the year under review and the previous year;
- confirmations relating to the annual financial statements and supervisory reporting (SFBC Circular 05/4 Supervisory Reporting);
- confirmations relating to the SFBC's recommendations and formal decisions as per margin nos. 47-48;
- a summary statement regarding the net assets, financial position and results of its operations;
- important information.

a) *Notices of reservation with their set deadlines*

In the financial audit report, the audit firm notes any identified breaches of the *applicable provisions*, statutory and regulatory requirements and directives, as well as any material deficiencies in terms of 36

- annual and interim financial statements;
- supervisory reporting;
- SFBC's recommendations and formal decisions as per margin nos. 47-48;
- the adequacy of the organisation in drawing up the annual and interim financial statements.

Breaches and material deficiencies in other areas not covered by the financial audit are the subject of notices of reservation in the regulatory audit report. 37

aa) *Notices of reservation with their set deadlines relating to the year under review*

Under this item, the audit firm summarises its reservations with their set deadlines relating to the year under review, referring to the page numbers of the report where each reservation is discussed in detail. In the absence of reservations a statement to this effect must be made by the audit firm. 38

bb) Notices of reservation with their set deadlines relating to the previous year

Under this item, the audit firm lists its reservations with their deadlines relating to the previous year with a report on the results of the follow-up audit and its opinion on how well the deadlines have been adhered to. In the absence of any notice of reservations with its set deadline in the previous year, a statement to this effect must be made by the audit firm. 39

b) Confirmations relating to the annual financial statements and supervisory reporting

aa) Confirmations relating to the annual financial statements

The audit firm states which accounting standards the institution has used for the individual financial statements and the consolidated financial statements, as well as whether it is submitting an unqualified or modified confirmation report. In the case of institutions without consolidated financial statements, the audit firm must either confirm that no group companies are held or give the reason for not drawing up consolidated financial statements. 40

The treatment of special purpose vehicles should also be commented on here. Special purpose vehicles are autonomous legal entities controlled directly or indirectly by the institution that have no operations, staff or material infrastructure of their own and were established, for example, to gain financial, tax, accounting or other advantages or to enable the geographical allocation of one or more precisely defined transactions designated as such. 41

There is no need to reproduce the entire wording of the confirmation report. A simple reference to the institution’s annual report or an enclosure to the financial audit report will suffice. 42

The audit firm confirms whether the liabilities reported in the balance sheet are covered by the available assets and whether the reported equity is intact (Art. 43 (1) BO). 43

If the confirmation report deviates from the industry’s standard wording, the audit firm must describe the nature of the modification here and give relevant explanations. 44

If the audit firm produces a modified confirmation report, it must inform the SFBC immediately, and in any case before submitting the confirmation report. The SFBC will then instruct the institution that it can only publish its annual financial statements after the SFBC approves them. The SFBC can demand a second publication if the institution has already published its annual financial statements. 45

bb) Confirmations relating to supervisory reporting

The audit firm expresses its audit opinion on the adherence to SFBC Circular 05/4 Supervisory Reporting and on the accuracy of the data submitted by the audited institution (individual financial statements and consolidated financial statements, where appropriate). It indicates which data were subject only to a review and which to a plausibility check (SFBC Circular 05/1 Audit). 46

c) Confirmations relating to the SFBC’s recommendations and formal decisions

Indicating the *audit depth*, the audit firm expresses its audit opinion regarding adherence to the SFBC’s recommendations and legally binding formal decisions applicable in the reporting period for the areas to be covered by the financial audit. 47

If no recommendations or legally binding formal decisions were issued in the reporting period, the audit firm records this accordingly. If legally binding formal decisions were issued but did not include any provisions for which adherence had to be verified, the audit firm also states this here. 48

d) Summary statement regarding net assets, financial position and results of operations

The audit firm summarises the results of its analysis of the institution's net assets, financial position and results of its operations. It explains any structural deviations between the individual institution and the group. The relevant details are discussed in margin nos. 58-62. 49

The financial audit report must give a clear picture of the institution's general net asset situation. The audit firm also states here whether or not it believes measures by the SFBC are necessary. 50

e) Important information

The important information that has to be recorded in the financial audit report includes the following in particular: 51

- matters that occurred and came to the auditor's attention after the balance sheet date and are particularly important for assessing the institution's net assets, financial position and results of its operations
- a summary of the audit results relating to the *key audit risks* mentioned in the standard report form "Risk Analysis/Audit Strategy" (SFBC Circular 05/1 Audit, Appendix 1) insofar as these have not already been recorded under "Notices of reservation with their set deadlines relating to the year under review" (margin no. 38; if necessary, details can be explained in an appropriate section of the report)
- material statements and recommendations in the supplementary reports (e.g. management letter) insofar as these are not already listed in the regulatory audit report
- areas where the applicable accounting standards leave room for discretion and which could have a material impact on the financial statements depending on the precise interpretation used
- details of any unclear presentation in the interim and/or annual financial statements (formal or material)
- references to any difficulties during the audit (e.g. with regard to the audited institution's cooperation, availability of documentation etc.)
- material changes in the institution's governing bodies insofar as these have not already been recorded in the regulatory audit report
- important regulatory issues that were identified during the financial audit and have not already been mentioned in the regulatory audit report
- references to specific risks if these have a material influence on the financial audit
- material dependencies with implications for the annual financial statements

In the absence of any important information, a statement to this effect must be made by the audit firm. 52

B. Audit firm's opinions**a) Opinion on the organisation and internal control in the preparation of annual and interim financial statements**

Under this heading, the audit firm expresses its opinion on the adequacy of the organisation and internal control when preparing the annual and interim financial statements (account closing process), thereby indicating the *audit depth*. It also notes any material changes compared with the previous year. 53

b) Valuation of assets and off-balance-sheet exposures and policies on value adjustments and provisions

The audit firm presents the detailed valuation principles applied to material balance sheet and off-balance-sheet positions under this heading. If it refers to the disclosures in the annual financial statements, the audit firm can restrict itself to additional explanations and appraisals. The audit firm also notes any material changes compared with the previous year and explains their implications. At this point, reference is also 54

made to special risks.

c) *Budgeting and planning*

The audit firm expresses its opinion on the following, thereby indicating the *audit depth*: **55**

- the adequacy of the institution's instruments for financial planning and control;
- the key assumptions underlying the budget for the current financial year, with details of the key budgeted figures;
- material discrepancies between the actual figures for the year under review and the previous year's budgeted figures.

Furthermore, the audit firm also states here whether the institution carries out a multi-year financial plan. **56**

d) *Response to the previous year's financial audit report by the institution's governing bodies*

The audit firm expresses its opinion on adherence to Art. 48 BO at the level of the individual institution and on group level and confirms in particular whether the requirements set out in margin nos. 12-16 have been met. **57**

C. Net assets, financial position and results of operations

The audit firm analyses the balance sheet, income statement and where appropriate the cash flow statement in line with the guidelines given in margin no. 59-62 and on the basis of the key figures, as per Appendix 3. It expresses a clear and concise opinion on the institution's net assets, financial position and results of operations, focusing on the key figures that are material, atypical or unsatisfactory for the institution. It explains any structural deviations between the individual institution and the group. The audit firm comments on and appraises the trends in these key figures over a period normally covering at least three years. **58**

Where appropriate, the analysis is also carried out at business unit level. The audit firm also makes a statement about the institution's internal reporting on its net assets, financial position and results of operations, especially if the data from the internal reporting facilitate material statements that could not be derived from the key figures as per Appendix 3. **59**

a) *Balance sheet analysis and commentary on net assets and financial position*

The following points are commented on or appraised: **60**

- material changes in material balance sheet and off-balance-sheet items (comment);
- refinancing (comment);
- changes in actual equity and the capital adequacy requirement (comment);
- material changes in assets under management (comment);
- trends in the key figures pertaining to net assets and financial position as per the key figures system in Appendix 3 (appraisal).

b) *Analysis of income statement and commentary on income situation*

The following points are commented on or appraised: **61**

- material changes in material income statement items and in gross income, operating expenses, operating income, depreciation and amortisation, value adjustments and losses, as well as income before extraordinary items and taxes (interim result) (comment)
- material extraordinary items (comment)
- trends in the key figures relating to the analysis of income and results of operation as per the key figures system in Appendix 3 (appraisal)

c) Profitability

The audit firm gives an appraisal here of the development in the key profitability figures as per the key figures system in Appendix 3. **62**

D. Additional information

- Confirmation that the audit was performed in accordance with the standard report form “Risk Analysis/Audit Strategy” (SFBC Circular 05/1 Audit, Appendix 1) that was submitted to the institution in advance and on request to the SFBC; deviations from the original audit strategy must be explained and justified **63**
- Details of the periods in which the audit activities were performed
- Confirmation that the audit firm has received all the information requested from the institution (Art. 19 (2) BA, Art. 17 (2) SESTA)
- Details of any third parties’ work relied upon (i.e. work done by another external auditor, the internal auditors or an expert of any other kind)
- Information about the audit firm’s mandates at the audited institution:
 - services relating to the audit:
fees and brief description of services
 - general consulting activities (including tax consulting):
fees and brief description of activities

E. Enclosures

- List of participations, including details of the company name, registered office, business activity, capital stock, equity stake (voting rights/capital), consolidation obligation (yes/no), audit firm, supervisory authority (yes/no; if yes, details of the supervisory authority) **64**
- Calculation of key figures as per Appendix 3
- Confirmations relating to Art. 44 and 45 BO
The points listed in Art. 44 and 45 BO that also apply to securities firms under Art. 8 SESTO-SFBC must be presented in a table enclosed with the financial audit report and annotated with “yes”, “no” or “not applicable”.
- Other documents and detailed information deemed relevant by the audit firm.

III. Regulatory audit report

In the case of financial services groups and conglomerates, confirmations, opinions and information must clearly refer to either the group or the individual institution provided that there are relevant distinctions. If there are no such distinctions, confirmations, opinions and information for the individual institution and the group can be combined. **65**

A. Summary of audit results

- The summary of audit results for the individual institution, and for the group (where appropriate) includes **66**
- notices of reservation with their set deadlines relating to the year under review and the previous year;
 - confirmations relating to the adherence to licensing requirements and to capital adequacy, large exposure and liquidity rules;
 - confirmations relating to the SFBC’s recommendations and formal decisions as per margin no. 75-76;
 - a summary statement regarding the risk situation;

- important information.

a) Notices of reservation with their set deadlines

In the regulatory audit report, the audit firm notes any identified breaches of the *applicable provisions*, statutory and regulatory requirements and directives, as well as any material deficiencies in the areas to be covered by the regulatory audit. **67**

aa) Notices of reservation with their set deadlines relating to the year under review

Under this item, the audit firm summarises its reservations with their set deadlines relating to the year under review, referring to the page numbers of the report where each reservation is discussed in detail. In the absence of any reservations a statement to this effect must be made by the audit firm. **68**

bb) Notices of reservation with their set deadlines relating to the previous year

Under this item, the audit firm lists its reservations with their set deadlines relating to the previous year with a report on the results of the follow-up audit and its opinion on how well the deadlines have been adhered to. In the absence of any notice of reservations with its set deadline in the previous year a statement to this effect must be made by the audit firm. **69**

b) Confirmations relating to the adherence to licensing requirements, capital adequacy, large exposure and liquidity rules

aa) Confirmation of adherence to licensing requirements

The audit firm expresses its audit opinion on the adherence to the licensing requirements. In particular, the audit firm states to what degree the reservations with their set deadlines relating to the year under review cast doubt on the adherence to the licensing requirements. The audit firm also states whether or not it believes measures by the SFBC are necessary. **70**

bb) Confirmation of adherence to capital adequacy rules

The audit firm confirms adherence to capital adequacy rules, providing details of the key figures that are relevant to capital adequacy. **71**

cc) Confirmation of adherence to large exposure rules

Referring to the institution's latest report, the audit firm confirms adherence to large exposure rules. **72**

dd) Confirmation of adherence to liquidity rules

For banks, the audit firm confirms adherence to the liquidity rules pursuant to Art. 16-20 BO and Art. 17-18 NBA, providing details of the relevant key liquidity figures. It also comments on liquidity provisions within the group. **73**

For securities firms, the auditing firm confirms adherence to the provisions on complementary liquidity pursuant to Art. 29a SESTO, providing details of the relevant key liquidity figures. **74**

c) Confirmations relating to the SFBC's recommendations and formal decisions

Indicating the *audit depth*, the audit firm expresses its audit opinion regarding adherence to the SFBC's recommendations and legally binding formal decisions applicable in the reporting period for the areas to be covered by the regulatory audit report. **75**

If no recommendations or legally binding formal decisions were issued during the reporting period, the audit firm mentions this here. If legally binding formal decisions existed but did not include any provisions **76**

for which adherence had to be verified, the audit firm also states this here.

d) Summary statement regarding the risk situation

The audit firm summarises the results of its analysis of the risk situation here. It comments on the adequacy of the institution's identification, measurement, management and monitoring of risks. 77

If part of the institution or a subsidiary of a financial services group or conglomerate are located abroad and this appears to impact the risk situation, the audit firm needs to state this here. 78

The audit firm also states here whether or not it believes any measures by the SFBC are necessary. 79

The relevant details relating to the risk situation are given in margin nos. 95-99. 80

e) Important information

The important information that has to be included in the regulatory audit report includes the following in particular: 81

- a summary of audit results relating to the *key audit risks* mentioned in the standard report form "Risk Analysis/Audit Strategy" (SFBC Circular 05/1 Audit, Appendix 1) insofar as these have not already been included in the "Notices of reservation with their set deadlines relating to the year under review" (margin no. 68; if necessary, details can be explained in an appropriate section of the report)
- material statements and recommendations in the supplementary reports (e.g. management letter)
- references to any difficulties during the audit (e.g. with regard to the audited institution's cooperation, availability of documentation etc.)
- material changes in the composition of the institution's governing bodies
- material links to other companies (financially important contracts relating to business policy, collaborations within the group, outsourcing etc.)
- material dependencies on clients, shareholders, affiliated persons, employees etc. that have a material influence on business activities or implications for adherence to licensing requirements, as well as one-sided business areas
- material changes (e.g. mergers, reorganisations, restructuring)
- reporting period if not identical with the institution's financial year

In the absence of any such important information, a statement to this effect must be made by the audit firm. 82

B. Audit firm's opinions

For each category listed in margin nos. 84-90, the audit firm expresses its opinion whether the institution adheres to the *applicable provisions*, statutes and regulations (which must also be listed), indicating the *audit depth*. 83

The audit firm expresses its opinions as per margin nos. 84-90 for the individual institution. The corresponding opinions for the group are given in accordance with margin no. 91.

a) *Corporate governance, including personnel segregation of executive management and Board of Directors*

The audit firm expresses its opinion on the institution's corporate governance. It describes the organisation of the Board of Directors (commissions, committees, particularly the audit committee) and gives its view of whether these meet the specific needs of the audited institution. The audit firm also expresses its opinion as to whether the institution adheres to the prescribed personnel segregation of its executive management and Board of Directors (Art. 8 (2) BO). **84**

b) *Adherence to generally accepted banking principles for transactions made by members of governing bodies and others with a qualified participation*

The audit firm records any transactions by members of governing bodies that breach the generally accepted principles of the banking profession (Art. 4^{ter} BA) or show particular characteristics and forms that necessitate a special comment in the regulatory audit report. In the absence of any such transaction, a statement to this effect must be made by the audit firm. Transactions by members of governing bodies include transactions by members of the Board of Directors, the executive management or persons and companies affiliated to same. **85**

c) *Guarantee of proper business conduct*

The audit firm expresses its opinion on the guarantee of proper business conduct given by members of the governing bodies and others with a qualified participation. If the audit firm finds that such guarantee is lacking, it must provide detailed reasons for this opinion. If the audit firm finds that such a guarantee exists, the opinion is normally based on the auditor's overall opinion, wherein is a confirmation that no matters have been identified that would cast doubt on the guarantee of proper business conduct. **86**

d) *Internal organisation and internal control system*

The audit firm expresses its opinion regarding the adequacy of the internal organisation and internal control system in the material business units as well as regarding the adequacy of information technology. It also comments on the organisation of material outsourcing contracts. **87**

e) *Internal audit function*

The audit firm reports on the audits performed by the internal auditors and expresses its opinion on the material results of these audits, as well as on the measures taken by the institution as a result of these audits. It also comments on the quality of the work done by the internal auditors and on whether the organisation and resources of the internal audit function are appropriate to the specific requirements of the audited institution. In doing so, it briefly explains the organisational structure and staffing of the internal audit function and the form of cooperation with external auditors. **88**

The audit firm must receive copies of all the internal auditors' reports in due time. The audit firm records matters identified by the internal auditors in terms of margin no. 25 (breaches of legal provisions or other irregularities) in the regulatory audit report and/or the financial audit report, in the form of notices of reservation.

f) *Compliance function*

The audit firm states whether the compliance function is adequate with regard to its organisation, resources and quality of work (compliance monitoring). **89**

g) Adherence to anti-money laundering regulations

In its regulatory audit report, the audit firm expresses its opinion on adherence to the *anti-money laundering regulations* by the institution and on that of its Swiss group companies (Art. 2 (2) of the SFBC's Anti-Money Laundering Ordinance) if this is not already included under margin no. 91. **90**

If the institution to be audited has no business relationships with third parties that are relevant in terms of the *anti-money laundering regulations* (e.g. institutions whose articles of association only allow for proprietary trading on stock exchanges with clearing functions), no audit activities are necessary in this respect. In this case, the audit firm expresses its opinion as to whether the institution had any business relationships relevant to the *anti-money laundering regulations* during the reporting period.

h) Adherence to regulations on consolidated supervision

The audit firm states whether the audited institution is subject to consolidated supervision and whether the consolidated supervision is conducted by a foreign supervisory authority. The audit firm expresses its opinions for the group as per margin nos. 84-90 here. It also expresses its opinion on the following: **91**

- the adequacy of group-wide organisational measures designed to ensure adherence on a consolidated basis to capital adequacy, large exposure and liquidity rules and to manage large exposures within the group
- the adequacy of group-wide organisational measures designed to monitor adherence to Swiss and foreign supervisory regulations and codes of conduct by the companies within the financial services group or conglomerate
- any misconduct aimed at circumventing *material Swiss provisions* it identifies by group companies
- adherence to the basic principles of the SFBC's Anti-Money Laundering Ordinance (Art. 3 (1) AMLO-SFBC), global monitoring of legal and reputational risks (Art. 9 AMLO-SFBC) and adherence to the *anti-money laundering regulations* by Swiss group companies (Art. 2 (2)d AMLO-SFBC).

i) Audit opinion regarding the additional audit areas specified by the SFBC

The additional audit areas specified by the SFBC are governed by SFBC Circular 05/1 Audit. In the absence of any additional audit area specified by the SFBC, a statement to this effect must be made by the audit firm. **92**

j) Audit opinion regarding the in-depth audit

The audit firm sets out the subject matter of the in-depth audit (SFBC Circular 05/1 Audit) and the material audit results. **93**

k) Response to the previous year's regulatory audit report by the institution's governing bodies

The audit firm expresses its opinion on the adherence with Art. 48 BO at the level of both individual institution and the group and confirms in particular that the requirements set out in margin no. 12-16 have been met. **94**

C. Risk situation**a) Risk policy**

The audit firm clearly and concisely sets out the risk policy defined and applied by the institution with reference to its corporate objectives. **95**

b) Developments in material risk categories

The audit firm assesses developments in the institution's risk exposure in the risk categories identified as material as per the standard report form "Risk Analysis/Audit Strategy", section 1.1 Risk profile of the institution (SFBC Circular 05/1 Audit, Appendix 1). Trends over the last three years must be considered. **96**

c) Opinion regarding the risk situation and the management of identified material risks

The audit firm analyses qualitative and quantitative information relating to the material risk categories as per margin no. 96 and expresses a clear and concise opinion of the institution's risk situation based on this information. The audit firm also refers to the institution's own internal reporting on its risk situation. **97**

The qualitative analysis includes the following elements, where applicable, for each type of risk: **98**

- methods used to identify risks;
- methods used to measure risks;
- methods used to manage and monitor risks;
- methods used to determine appropriate value adjustments and provisions;
- the institution's own internal figures on risk and its internal risk reporting;
- rating systems and systems of limits;
- independence of the bodies in charge of risk control.

The quantitative analysis includes the following elements, where applicable, for each type of risk: **99**

- quantitative data on the risks assumed, based on market valuations;
- value at risk;
- adequacy of and compliance with limits;
- results of stress tests;
- expected losses;
- key figures on value adjustments and provisions.

The material results of this analysis must be summarised in the regulatory audit report as per margin nos. 77-80. **100**

D. Additional information

- Confirmation that the audit was performed in accordance with the standard report form "Risk Analysis/Audit Strategy" (SFBC Circular. 05/1 Audit, Appendix 1) submitted to the institution in advance and on request to the SFBC; deviations from the original audit strategy must be explained and justified **101**
- Details of the periods during which the audit activities were performed;
- Confirmation that the audit firm has received all the information requested from the institution (Art. 19 (2) BA, Art. 17 (2) SESTA);
- Details of any third parties' work relied upon (i.e. work done by another external auditor, the internal auditors or an expert of any other kind).

E. Enclosures

- Standard report form “Risk Analysis/Audit Strategy” (SFBC Circular 05/1 Audit, Appendix 1) **102**
- List of large exposures pursuant to Art. 21 (2) BO
- Report on ten largest borrowers (Appendix 4)
- Graphic representation of group structure, including breakdown of holdings
- Organisation chart(s)
- Other documents and detailed information deemed relevant by the audit firm

IV. Effective date

Effective date: 1 January 2006 **103**

This Circular replaces SFBC Circular 96/3 Audit Reports.

V. Transitional provision

This Circular may be applied on a voluntary basis to audits for the financial year ending 31 December 2005. It must be applied to all audits starting with the financial year ending 31 December 2006. For institutions whose financial year does not end on 31 December, this Circular must be applied as of the first financial year ending after 31 December 2006. **104**

Since the reporting period for the regulatory audit is no longer required to coincide with the financial year (margin no. 29), there will be a transitional phase during which the regulatory audit may cover a period of more or less than one year. Periods of more than one year are restricted to a maximum of 18 months. They are permissible only for institutions that do not have special risks or problems.

Appendices:

- Appendix 1: Minimum structure of the financial audit report
- Appendix 2: Minimum structure of the regulatory audit report
- Appendix 3: Key figures system
- Appendix 4: Report on the ten largest borrowers

Legal basis:

- BA: Art. 18-22
- BO: Art. 43-49
- SESTA: Art. 17-19
- SESTO-SFBC: Art. 8