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**GUIDELINES FOR EXTERNAL AUDITING OF INSTITUTIONS  
LICENSED UNDER THE BANKING ACT**



**EASTERN CARIBBEAN CENTRAL BANK  
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## **Banking Prudential Guidelines No. 1 of 2008**

The Eastern Caribbean Central Bank (ECCB), in exercise of the powers conferred on it by section 36 of the Banking Act<sup>1</sup> issues the following revised Prudential Guidelines -

### **INTRODUCTION**

#### **I. OBJECTIVES**

These Guidelines aim to:

- (a) Provide guidance to financial institutions licensed under the Banking Act in relation to the appointment of auditors and the conduct of external audits.
- (b) Establish the minimum suitability criteria for auditors of a financial institution;
- (c) Outline minimum requirements for the conduct of the external audits of financial institutions;
- (d) Direct management's attention to the obligations of the auditor as set out in Section 19<sup>2</sup> of the Banking Act, which states that, among other things, the auditor is required to report to the ECCB, transactions or conditions that impinge on the well-being of the financial institution.

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<sup>1</sup> Anguilla – Act No. 9 of 2005  
Antigua and Barbuda – Act No. 14 of 2005  
Commonwealth of Dominica – Act No. 16 of 2005  
Grenada – Act No. 19 of 2005  
Montserrat – Act No. 2 of 2005  
Saint Christopher and Nevis – Act No. 4 of 2004  
Saint Lucia – Act No. 34 of 2006  
Saint Vincent and the Grenadines – Act No. 33 of 2006

<sup>2</sup> Anguilla – s 18

## II. INTERPRETATION

**“Affiliate”** in relation to a financial institution (“F”) means

- (a) a company which is or has at any relevant time been
  - i. a holding company or subsidiary of F;
  - ii. a subsidiary of a holding company of F; or
  - iii. a holding company of a holding company or a subsidiary of a subsidiary of F;or
- (b) any company over which F has control;
- (c) any company over which F and any person associated with F has control;
- (d) any company which has common ownership with F.
- (e) any company which has the same beneficial owner and share common management and interlinked businesses with F.

**“Auditor”** means an external auditor that is -

- (a) a person who is a member of a professional body of accountants which the Minister has specified by Order published in the *Gazette*; or
- (b) any other person approved by the Minister, acting on the recommendation of the Central Bank.

**“Control”** means the ability of a person to secure, through voting rights or power in a licensed financial institution or other company or by an agreement or other powers conferred by the by-laws, articles of association or other document regulating the operations of the licensed financial institution or other company, that the business and affairs of the licensed financial institution or other company are conducted in accordance with the wishes of that person.

**“Immediate family”** refers to any person or persons who can be expected to influence an individual or be influenced by that individual. This generally includes:

- (a) A spouse, domestic partner or child; or

- (b) Any person living in a common household; or
- (c) A grandparent, parent, brother or sister; or
- (d) The spouse or domestic partner of a child, parent, brother or sister.

**“Independence”** refers to the elements of:

- (a) Independence of mind, which is the state of mind that permits the performance of an attest service without being affected by influences that compromise professional judgement, thereby allowing an individual to act with integrity and exercise objectivity and professional scepticism; and
- (b) Independence in appearance, which is the avoidance of circumstances that would cause a reasonable and informed third party, having knowledge of all relevant information, including safeguards applied, to reasonably conclude that the integrity, objectivity or professional scepticism of a firm or a member of the attest engagement team had been compromised.

**“Related Party”** in relation to an institution means -

- a) The directors and staff of the institution;
- b) An affiliate of the institution;
- c) Any director, partner, senior officer or guarantor of an affiliate of the institution or their immediate family;
- d) Any entity in which a director or senior officer of the institution assumes the role of director, partner, officer or guarantor;
- e) A significant shareholder of the institution, the significant shareholder’s senior officers, partner or immediate family member or an entity that the significant shareholder controls or is controlled by;
- f) A director or senior officer of an entity that controls or is controlled by the institution and includes their partners or immediate family members;
- g) Any person who maintains a trust on behalf of the institution or its affiliate and includes any director, partner, senior officer or guarantor of the trust or their immediate family;

- h) A person or class of persons identified under section 16(1)(a)<sup>3</sup> or section 16(1)(c)<sup>4</sup> of the Banking Act;
- i) A person or class of persons who has been designated by the ECCB as a related party because of their past or present interest in or relationship with the institution, being such that it can be reasonably expected that this related party can influence the decision of the institution regarding a transaction.

**“Significant shareholder”** means a person who either alone or with an affiliate or related or connected person, is entitled to exercise or control more than 20% of the voting rights at any general meeting of the licensed financial institution or another company of which the licensed financial institution is a subsidiary.

### **III. APPLICATION**

These guidelines apply to all financial institutions licensed under the Banking Act.

### **IV. COMMENCEMENT**

These guidelines replace the Banking Prudential Guidelines No. 5 of 2006 that took effect from 15 January 2007, and become effective from **1 July 2008**.

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<sup>3</sup> Anguilla – s 15(1)(a)

<sup>4</sup> Anguilla – s 15(1)(c)

## **GUIDELINES**

### **1.0 ASSESSING THE SUITABILITY OF THE AUDITOR**

In assessing the suitability of a candidate for auditor, the audit committee or the board of directors should, at a minimum, consider the following:

#### **1.1 INDEPENDENCE**

The auditor must have clear and comprehensive procedures for ensuring independence of all persons engaged in auditing the financial statements of the financial institution. Sections 16 (4) (d)<sup>5</sup> and 19 (14)<sup>6</sup> of the Banking Act sets out broad requirements to ensure that the independence of the auditor is maintained. It is the responsibility of the financial institution's audit committee and/or board of directors to assess the independence of candidates for auditor before the appointment is made. The auditor's independence should be assessed on a regular basis, to verify that independence is maintained.

1.1.1 The following persons should be disqualified from appointment as auditor of the financial institution:

1.1.1.1 A partner, manager or senior auditor of the audit firm who has been a liquidator (except a voluntary liquidator), trustee in bankruptcy, receiver or manager of any affiliate of the financial institution within the two years immediately preceding the appointment;

1.1.1.2 A significant shareholder of the financial institution;

1.1.1.3 A significant shareholder's senior officers, partners or immediate family members;

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<sup>5</sup> Anguilla – s 15(6)(d)  
Saint Christopher and Nevis – s 16(6)(d)

<sup>6</sup> Anguilla – s 18(14) and (15)  
Antigua and Barbuda – s 19(14) and (15)  
Saint Christopher and Nevis – s 19(14) and (15)  
Saint Vincent and the Grenadines - s 19(13)

- 1.1.1.4 Any entity that a significant shareholder controls or which controls a significant shareholder;
- 1.1.1.5 An affiliate of the financial institution; and
- 1.1.1.6 A related party as defined in these guidelines.
- 1.1.2 The lead and concurring audit partner should be rotated at least once every six years, provided however that the financial institution shall not engage the services of the same auditor for more than nine consecutive years.
- 1.1.3 The financial institution should require the auditor to disclose in writing to the financial institution's board and/or audit committee, all relationships with the institution and its related entities that could affect the auditor's objectivity and independence. The auditor should further be required to discuss these relationships with the institution's board and/or audit committee. The audit committee and the board of directors should consider whether any of the relationships or services provided by the auditor could either in fact or appearance:
- Create a conflict of interest between the institution and its auditors;
  - Place the auditor in the position of auditing their own work; or
  - Result in the auditor acting in the capacity of management or employee or acting as an advocate for the institution.

The relationships and services that may threaten independence include but are not limited to the following:

- (a) Direct or material indirect financial relationships with the institution, such as:
- Investments in the institution or the institution's investments in the audit firm,
  - Loans to or from the institution.
- (b) Employment relationships between the institution and the auditor, such as:
- The auditor being employed by the institution or serving on the institution's board or in a similar management capacity,

- A former employee of the audit firm being employed at the institution in an accounting or financial reporting oversight role.
- (c) Direct or material indirect business relationships with the institution or persons associated with the institution in decision-making capacities, such as:
- An officer, director, or significant shareholder.
- (d) Immediate family relationships within the institution.
- (e) Providing other services to the institution, such as:
- Bookkeeping or other services related to the institution's accounting records or financial statements,
  - Financial information system design and implementation,
  - Appraisal or valuation services, fairness opinions, or contribution-in-kind reports,
  - Actuarial services,
  - Internal audit services,
  - Management functions or decision-making, supervisory, or ongoing monitoring functions,
  - Human resources,
  - Broker/dealer, investment advisor, or investment banking services, or
  - Legal services and expert services not related to the audit.

[In the event that the Board and/or audit committee of the financial institution grants approval for the auditor to provide any of the non-audit services stated above, the Board and/or audit committee must ensure that the partner/manager appointed by the auditor to lead the engagement is different from the partner/manager who leads the audit engagement.]

## **1.2 EXPERTISE, RESOURCES AND CONTINUING PROFESSIONAL EDUCATION OF THE AUDITOR**

- 1.2.1 The auditor or audit firm selected should have relevant experience in auditing financial institutions, of comparable size and complexity. In addition, the staff on the audit engagement should include persons who possess sufficient specialised skills appropriate to the financial sector.
- 1.2.2 Auditors or partners of audit firms who are authorised to sign off on audit engagements should be a valid member of a recognised supervisory accounting body. Such individuals should have a minimum of five years experience in the audit of financial institutions.
- 1.2.3 All professional accounting personnel should perform relevant continuing professional education necessary to maintain their professional designation.

## **1.3 QUALITY ASSURANCE REVIEWS**

The financial institution should be satisfied that the auditor or audit firm maintains a competent quality assurance process in order to comply with internal and external standards. Such internal procedures should, include at a minimum:

- (a) Designation of an experienced professional as quality assurance reviewer;
- (b) The requirement that a senior partner sign off on larger or high-risk audits;
- (c) The conduct of internal audit reviews of selected files; and
- (d) External peer reviews.

## **1.4 PROFESSIONAL INDEMNITY INSURANCE**

The financial institution should verify that the selected auditor or audit firm has adequate professional indemnity insurance.

## **2.0 FRAMEWORK FOR THE CONDUCT OF THE EXTERNAL AUDIT**

The financial institution should ensure that the work to be performed by the auditor is carried out in accordance with International Standards on Auditing and is sufficient and appropriate for the needs of the financial institution.

## **2.1 THE ENGAGEMENT LETTER**

The financial institution's board and/or audit committee should require the auditor to submit an engagement letter prior to commencing audit work. The engagement letter is the contract between the auditor/audit firm and the financial institution's board of directors. It should include a statement of the scope and objectives of the audit and an outline of the responsibilities and obligations of both the auditor and management of the financial institution.

## **2.2 SCOPE OF THE AUDITOR'S WORK**

The financial institution's board of directors or audit committee should ensure that the scope of the auditor's work covers, at a minimum, the following as appropriate:

- (a) Examination and evaluation of the adequacy and effectiveness of the internal control systems;
- (b) Review of the application and effectiveness of risk management procedures and risk assessment methodologies;
- (c) Review of the management and financial information systems, including electronic banking services;
- (d) Review of the accuracy and reliability of accounting records and financial reports;
- (e) Review of the means of safeguarding assets;
- (f) Review of the system for assessing capital in relation to the estimated risks;
- (g) An assessment of compliance with internal policies and procedures, the Banking Act, Anti-money laundering legislation and all other relevant legislation in the territory;

- (h) Review of the systems established to ensure compliance with legal and prudential requirements, codes of conduct and the implementation of policies and procedures.

### **2.3 THE MANAGEMENT LETTER**

The management letter is issued by the auditor. It details internal control exceptions, risk assessments, recommendations for corrective action and the responses of the financial institution. At the end of an audit engagement, where the auditor has concerns relating to the internal controls of the financial institution a management letter should be issued. When there are no significant concerns, a management letter should be issued with a comment such as “nothing to report”.

### **3.0 REPORTABLE TRANSACTIONS OR CONDITIONS**

Sections 19 (1), (3) and (5)<sup>7</sup> of the Banking Act set out the reporting requirements of the auditor. Financial institutions should ensure that the auditor is aware of these obligations.

In addition to the provisions of the Banking Act, the broad categories of transactions or conditions that are reportable to the ECCB include, but are not limited to:

- (a) Transactions or conditions requiring a change in accounting basis or a disclosure note;
- (b) Transactions or conditions which contravene the assumption of management’s good faith;
- (c) Transactions or conditions requiring the auditor to issue a modified or qualified opinion or to include a disclaimer paragraph in the audit opinion;
- (d) Material adverse changes in risks inherent in the financial institution’s business, with the potential to jeopardise its ability to continue as a going concern;
- (e) Material conflict between decision-making authorities of the financial institution;

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<sup>7</sup> Anguilla – s 18(1), (3) and (5)

- (f) The auditor's intention to resign or the financial institution's planned removal of the auditor. If the auditor plans to resign or becomes aware that the financial institution intends to terminate the auditor's services, the auditor should report the matter to the ECCB; and
- (g) Any other situations which, in the opinion of the auditor, are of sufficient importance to be brought to the attention of the ECCB. The auditor shall advise the ECCB within a reasonable time of reporting to the financial institution.

The reporting requirements do not oblige the auditor to provide an assurance on the reported matters. It is however, necessary for an auditor to understand his reporting responsibility.

#### **4.0 APPLICATION FOR APPROVAL OF THE AUDITOR**

4.1 In assessing the propriety of an auditor of a financial institution pursuant to section 19 of the Banking Act, the Central Bank will consider among other things, the following:

- i) Whether the auditor is a member of the Institute of Chartered Accountants of the Eastern Caribbean (ICAEC) or any other professional body recognised by the Central Bank;
- ii) The structure and organisation of the firm, its principal place of business and branches in the ECCU;
- iii) Whether there are any direct or indirect existing relationships between the proposed auditor and audit client;
- iv) The auditor's experience in conducting audits of financial institutions of comparable size and complexity;
- v) Whether the auditor has professional indemnity insurance which is adequate for its business activities;

vi) The reputation of the auditor; and

vii) Any other information collected by the financial institution in conducting due diligence on the auditor.

4.2 Prior to appointing its auditor, the financial institution shall submit in writing to the Central Bank, a letter of application for approval of the proposed auditor, together with:

- i) Details of the auditor's background, legal and ICAEC status;
- ii) A statement of the principal place of business or head office of the auditor and other places of business or branches in the ECCU;
- iii) An organisational chart;
- iv) Details of the legal and professional status of the parent company, if any;
- v) The names, personal data and detailed resumes of all partners and senior officers;
- vi) A list of major audit assignments that have been performed by the auditor in the last three (3) years;
- vii) Details of professional indemnity insurance; and
- viii) Any other information requested by the Central Bank,

in order to facilitate an assessment of the auditor in accordance with paragraph 4.1.

4.3 Any approval of an auditor granted to a financial institution shall remain in force until withdrawn in writing by the Central Bank.

4.4 The financial institution shall promptly inform the Central Bank in writing of:

- (i) Any material changes in the information submitted in accordance with paragraph 4.2; and
- (ii) Its intention to terminate the appointment of its auditor, or not to re-appoint its auditor for a new term.

**Eastern Caribbean Central Bank**