STAFF AUDIT PRACTICE ALERT

September 2016

THE AUDIT IMPLICATIONS OF THE EXPECTED CREDIT LOSS MODEL FOR THE AUDITORS OF BANKS

This publication has been prepared by the IFRS 9 ECL Task Group of the Independent Regulatory Board for Auditors' (IRBA) Committee for Auditing Standards (CFAS). It does not constitute an authoritative pronouncement from the IRBA, nor does it amend or override the International Standards on Auditing, South African Standards on Auditing, South African Auditing Practice Statements or South African Guides (collectively called pronouncements).

Also, this publication is not meant to be exhaustive. Reading this publication is not a substitute for reading the abovementioned pronouncements, as they are the authoritative texts.

The IRBA has responded to the interest and concerns raised about the audit implications of the expected credit loss (ECL) model incorporated into the International Financial Reporting Standard (IFRS) 9, *Financial Instruments,* which becomes effective for annual periods beginning on or after 1 January 2018, by developing this IRBA Staff Audit Practice Alert.

This IRBA Staff Audit Practice Alert serves to provide registered auditors with (a) the background to the risks and audit implications of IFRS 9 and the ECL model in the banking environment; (b) a checklist that can be used by the engagement team when considering certain audit implications of the ECL model; and (c) related notes.

The International Standard on Auditing (ISA) 540, *Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures* (ISA 540), deals with the auditor's responsibilities relating to accounting estimates, including fair value accounting estimates, and related disclosures in an audit of financial statements. Specifically, it expands on how ISA 315 (Revised)[1], ISA 330[2] and other relevant ISAs are to be applied in relation to accounting estimates. It also includes requirements and guidance on

[1] ISA 315 (Revised), *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment*
[2] ISA 330, *The Auditor's Responses to Assessed Risks*

misstatements of individual accounting estimates as well as indicators of possible management bias.[3]

The auditor's objective is to obtain sufficient appropriate audit evidence about whether:

(a) Accounting estimates, including fair value accounting estimates, in the financial statements, whether recognised or disclosed, are reasonable; and

(b) Related disclosures in the financial statements are adequate, in the context of the applicable financial reporting framework.[4]

In South Africa, banks prepare their financial statements in accordance with IFRS, which currently include the International Accounting Standard (IAS) 39, *Financial Instruments: Recognition and Measurement* (IAS 39).

IAS 39 is soon to be replaced by IFRS 9, which was issued by the International Accounting Standards Board (IASB) in July 2014 with an effective date for annual periods beginning on or after 1 January 2018.

The IASB added to IFRS 9 the impairment requirements relating to the accounting for an entity's expected credit losses on its financial assets and commitments to extend credit.

In brief, under the impairment approach in IFRS 9 it is no longer necessary for a credit event to have occurred (incurred credit losses) before credit losses are recognised. Instead, an entity always accounts for expected credit losses and changes in those expected credit losses (lifetime expected credit losses/12-month expected credit losses).

This change in the impairment methodology has a fundamental impact on the accounting for such losses and also affects how an auditor audits such impairment losses. The accounting matters are complex and specialised and out of the scope of this IRBA Staff Audit Practice Alert. Auditors are thus encouraged to make adequate preparations for a thorough understanding of all accounting related risks and issues.

BACKGROUND

IRBA

1. One of the primary objectives of the Bank Supervision Department (BSD) of the South African Reserve Bank (SARB) is the promotion of the soundness of the banking system, thereby contributing to financial stability in South Africa. The BSD approached the IRBA early in 2015 to discuss the audit implications of IFRS 9. In March 2015, the CFAS agreed to commence a project to develop guidance on the audit implications of IFRS 9 and the ECL model, if and when the need was identified.

2. The IRBA has been monitoring developments on this front as follows:

[3] ISA 540, paragraph 1
[4] ISA 540, paragraph 6

- Engaging with audit firms and banks as part of the South African Institute of Chartered Accountants' (SAICA) IFRS 9 Implementation Working Group;
- Engaging in further discussions with the SARB; and
- Engaging in discussions on international developments with the International Auditing and Assurance Standards Board's (IAASB) ISA 540 Task Group.

3. In particular, the IRBA hosted a meeting in April 2016 to discuss the audit implications of IFRS 9 and the ECL model on the audit of banks, and also to:
   - Discuss international developments at the IAASB;
   - Hear the perspectives of the BSD and the Basel Committee on Banking Supervision (BCBS);
   - Get feedback from the audit firms (represented by Head of Audit, Banking Audit and Technical Specialists) on their progress in preparing for the audit of impairment provisions using IFRS 9 and the ECL model;
   - Discuss some preliminary views on what guidance may be necessary on the audit implications of IFRS 9 and the ECL model; and
   - Hear from the audit firms where they believe guidance may be needed on the audit implications of IFRS 9 and the ECL model.

South African Reserve Bank

4. The BSD has chosen IFRS 9 as its "flavour of the year" topic for both 2015 and 2016 as it recognises the impact it will have on banks and their accounting for impairment losses.
5. In December 2015, the BCBS issued a paper titled *Guidance on Credit Risk and Accounting for Expected Credit Losses*. The objective of that paper is to set out supervisory guidance on sound credit risk practices associated with the implementation and ongoing application of ECL accounting frameworks (e.g. IFRS 9 and the ECL model). It provides banks with supervisory guidance on how the ECL model should interact with a bank's overall credit risk practices and regulatory framework. The supervisory guidance does not contradict the applicable accounting standards established by accounting standard-setters (e.g. the IASB), but rather presents the view of the BCBS on the appropriate application of those standards (e.g. IFRS 9 and the ECL model).
6. The SARB issued Guidance Note 3/2016, *Credit risk and accounting for expected credit losses*, on 11 March 2016, the purpose of which was to bring to the attention of banks the latest supervisory guidance on sound credit risk practices associated with the implementation and ongoing application of ECL accounting frameworks, as outlined in the BCBS paper.

7. The SARB Guidance Note states that as part of its supervisory review and evaluation processes, the Office of the Registrar of Banks will review the progress made by banks to incorporate the principles and guidance set out in the BCBS paper.

8. Although the BCBS paper provides supervisory guidance to banks, the BSD has expressed the need that the auditors of banks should have sufficient and appropriate guidance (from ISA 540 and/or elsewhere) to ensure consistent interpretation and application of IFRS 9 and the ECL model in their audits. Among other things, auditors will be required to have a forward-looking view on expected credit deterioration, an approach to which auditors and their clients may currently not be fully accustomed.

9. The BSD has met with all the auditing firms that perform the audits of banks to reinforce their concerns, ascertain their readiness to audit banks and their application of IFRS 9 and the ECL model and to encourage them to develop a "firm view"[5] on the subjective inputs that a bank will use in the development of their ECL models.

IAASB

10. The IAASB also responded by establishing the Financial Institutions Working Group (FIWG) during early-2015, later named the ISA 540 Task Force.

11. The scope of the ISA 540 Task Force is to provide for a holistic revision of ISA 540 (project proposal approved by the IAASB in December 2015). A useful output of the ISA 540 Task Force is a project update (issued March 2016) providing an overview of the initial thinking on the special audit considerations relating to the ECL model provisions, including related estimation uncertainty.

12. The schedule for finalisation of the holistic revision of ISA 540 may leave too little time to provide adequate guidance for auditors of banks with regards to the audit implications of the ECL model.

13. In response, this IRBA Staff Audit Practice Alert has been developed to assist auditors in their preparation. This IRBA Staff Audit Practice Alert serves to address the IAASB's objective of consistent high audit quality work by registered auditors and taking such measures necessary to promote and protect public interest.

IAASB ISA 540 Revision Timetable

Keep up-to date on the IAASB ISA 540 Task Force web page

- IAASB Approval of Exposure Draft – December 2016 (planned)
- Comment Period – 120 Days
- IAASB Approval of ISA 540 (Revised) – December 2017 (planned)

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[5] Firm view refers to the audit firm's internally developed, independent determination of the macroeconomic and other related forward-looking factors used in the computation of expected credit losses as required by IFRS 9. It is envisaged that this be a firm-wide view, across its South African operations, to facilitate consistent application of the macroeconomic outlook across the firm's audit engagements.

14. Although this IRBA Staff Audit Practice Alert addresses the audit implications of IFRS 9 and the ECL model on the audit of banks, an auditor may find this publication, if adapted as necessary, useful when auditing other entities that have adopted IFRS 9 and the use of the ECL model.

CHECKLIST

15. This checklist can be used by the audit firm, audit engagement team and the engagement quality control (EQC) reviewers when considering the audit implications of the ECL model. It, however, is not an exhaustive list of considerations and should not take away from the requirements of the audit engagement team to exercise their professional judgement.

16. In consideration of and responding to the different content elements and questions posed in the checklist, the engagement team should be guided by the requirements and application material contained in the relevant ISAs.

17. The checklist contains questions to be responded to at the "Firm Level" and at the "Engagement Level". The "Firm Level" questions should be considered and responded to by the audit firm's leadership that has the responsibility to consider the audit implication of IFRS 9 and the ECL model at the audit firm level (or its equivalent). The "Engagement Level" questions should be considered and responded to by the audit engagement team on each banking audit engagement.

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
1. Firm level risk management process considerations, including multi-location and multi-national considerations			
- Has your firm determined, through its risk assessment procedures, which of its audit clients the ECL model (IFRS 9) affects and the possible impact?	**ISQC 1**[7]		

[7] International Standard on Quality Control 1(ISQC 1) *Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and Other Assurance and Related Services Engagements*

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
- Has your firm made any changes to its risk management processes as a result of the audit implications of IFRS 9 and the ECL model? - Has your firm developed its own "firm view"[6], including consideration of relevant guidance on IFRS 9 and the ECL model (refer **Note 1**) and the subjective inputs into the ECL model? - Is your firm consistently updating its "firm view"? - Has relevant guidance on the adaptability of the "firm view" been provided to the other network firm offices in the various jurisdictions where your "firm view" will be used? If applicable, refer to section 3 below for further considerations.			
2. Considerations for the audit of transitional disclosures made by banks in terms of IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*			
- Does your firm have the ability to audit the disclosure of known, or reasonably estimable information	**ISQC 1**	**First time adoption for year-end reporting purposes**	**ISA 315 (Revised)[8]**

[6] Firm view refers to the audit firm's internally developed, independent determination of the macroeconomic and other related forward-looking factors used in the computation of expected credit losses as required by IFRS 9. It is envisaged that this be a firm-wide view, across its South African operations, to facilitate consistent application of the macroeconomic outlook across the firm's audit engagements.
[8] ISA 315 (Revised), Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and its Environment

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
(financial and non-financial) relevant to assessing the impact of IFRS 9 in the period of initial application?		- Is your client providing the disclosures as required by International Accounting Standard (IAS) 8, *Accounting Policies, Changes in Accounting Estimates and Errors* (IAS 8) (standards issued but not effective) when it has adopted IFRS 9 (whether it has early adopted or not)? - Have you considered the requirements as outlined in IAS 8? **First time adoption for interim reporting purposes** - Have you considered the implications on interim reported results in the year of adoption of IFRS 9? **IFRS 9 impact on insurance entities** - Have you considered the impact on insurance entities within a banking group, as IFRS 9 would also need to be applied?	**ISA 330**[9] **ISA 540**[10]

[9] ISA 330, The Auditor's Responses to Assessed Risks
[10] ISA 540, Auditing Accounting Estimates, Including Fair Value Accounting Estimates, and Related Disclosures

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
3. Considerations for the development of an audit firm's independent "firm view" on the subjective inputs (including forward-looking information)			
- Has your firm established and implemented quality control procedures or processes over the development of a "firm view" that includes: • Applicable governance processes; and • Retrospective review (back-testing)? - Has your firm considered the relevant economic and market volatility (globally, regionally and locally) in the development of the "firm view"? - In developing the "firm view", has your firm identified and used a similar completed audit engagement where IFRS 9 and the ECL model has been early adopted to use as a benchmark? - Has your firm considered using the work of an auditor's expert (e.g. economists and actuaries)? - Has your firm identified all generally accepted inputs into the ECL models that would be used to develop the "firm view"?	**ISQC 1**		

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
- For each input identified, has your firm identified the source of the data, range of the data, process for regular measurement of the data and the quality control required for the ECL models used to develop the "firm view"? - Has your firm determined the weighting of each input? - Has your firm developed an approach to deal with contradictory data, including contradictory reports from experts?			
4. Consideration of the economic and market volatility that will impact the subjective inputs into ECL models			
		- Have you considered the relevant economic and market volatility (globally, regionally and locally) in your risk assessment and the development of your point estimate or range specific to your client?	**ISA 315 (Revised)** **ISA 320[11]** **ISA 330** **ISA 540**
5. Considerations for the communication with those charged with governance			

[11] ISA 320, Materiality in Planning and Performing an Audit

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		- Have you considered discussing relevant guidance on IFRS 9 and the ECL model (refer **Note 1**) with those charged with governance with a view to establishing whether they are aware of the guidance and whether they understand the impact of IFRS 9 and the ECL model on the financial statements?	**ISA 260**[12] **ISA 540**
6. Considerations for group audit engagements including groups with foreign subsidiaries and local branches of foreign banks			
- Has your firm issued relevant guidance for group and/or component auditors? - If yes, does your firm guidance cover the following: • Changes in accounting standards? • Firm methodology/approach and risk management processes? • Consideration of hosting training/workshops?	**ISQC 1**	- Have you obtained an understanding of how group management developed its ECL models? - Have you considered the need to include specific instructions to component auditors with respect to relevant details about the entity's ECL model, as well as key inputs into the model, and work done	**ISA 210**[13] **ISA 250**[14] **ISA 315 (Revised)** **ISA 320** **ISA 330** **ISA 540**

[12] ISA 260, Communication with Those Charged With Governance
[13] ISA 210, Agreeing the Terms of Audit Engagements
[14] ISA 250, Consideration of Laws and Regulations in an Audit of Financial Statements

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		centrally compared to work required to be performed at a component level? - Have you considered whether there are any legislative and/or regulatory requirements, including applicable financial reporting frameworks, of a foreign subsidiary that may affect the ECL model at the holding entity level, domiciled in a different jurisdiction? - Have you considered the financial reporting framework adopted in the countries of foreign subsidiaries and local branches of foreign banks? If the financial reporting framework adopted differs to IFRS (and IFRS 9), have you considered whether the financial information from these countries incorporated into the group financial statements is in accordance with IFRS (and IFRS 9)?	**ISA 600**[15]

[15] ISA 600, Special Considerations – Audit of Group Financial Statements (Including the Work of Component Auditors)

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		- Does your client have an ECL model that differs from country to country? Are these differences justified? - Have you obtained an understanding of the macroeconomic conditions in the different countries and considered how these will impact the different ECL models?	
7. Considerations for how and on what a registered auditor should apply professional scepticism in "challenging" their banking clients, regarding the subjective inputs applied by banks in the ongoing development and maintenance of their ECL models			
- Has your firm developed and issued guidance on how and on what a registered auditor should apply professional scepticism in "challenging" their banking clients, regarding the subjective inputs applied by banks in the ongoing development and maintenance of their ECL models?	**ISQC 1**	- Have you considered the definitions of key aspects of the ECL model? - Have you considered the variable inputs into the ECL model? - Have you considered the subjective inputs into the forward-looking information included in the ECL model?	**ISA 240**[16] **ISA 315 (Revised)** **ISA 320** **ISA 330** **ISA 500**[17] **ISA 540**

[16] ISA 240, The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements
[17] ISA 500, Audit Evidence

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		- Have you considered and distinguished between third party/external data sources and the use of management experts and the corresponding work effort required on each? - Have you considered the adjustments/overlays made outside of the ECL model? - Have you considered the possibility of management bias used in the ECL model?	**BCBS paper titled** *Guidance on Credit Risk and Accounting for Expected Credit Losses*
8. Considerations for cross-reviews and how to address material differences of opinion between joint auditors in the calculation of impairment provisions			
		- Has a process between the joint auditors been agreed to perform cross reviews regarding the ECL models, including the subjective inputs into the model, at an early stage of the audit and throughout the audit process? - Does the agreed process between the joint auditors cater for bias and disagreements between joint auditors?	**ISA 600**

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
9. Considerations for how an auditor can ~~consult with~~inform the SARB when disagreements resulting in material differences that may result in a modified audit opinion arise between impairment provisions calculated by the bank and those supported by the auditor's audit evidence			
		NOTE: The SARB has an interest in being ~~consulted~~ informed when a modified audit opinion is being considered. - Have you considered the impact of material differences that may result in a modified audit opinion on the Regulatory Reports and your reporting responsibilities under Regulation 46 of the Regulations relating to Banks?	**ISA 220**[18] **ISA 250** **ISA 315 (Revised)** **ISA 320** **ISA 330** **ISA 450**[19] **ISA 540** **ISA 705 (Revised)**[20] **Regulation 46 of the Regulations**

[18] ISA 220, Quality Control for an Audit of Financial Statements
[19] ISA 450, Evaluation of Misstatements Identified During the Audit
[20] ISA 705, Modifications to the Opinion in the Independent Auditor's Report

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other relating to Banks**
10. Considerations for the audit of the additional information disclosed in the bank's financial statements (e.g. sensitivity analysis)			
		NOTE: The nature and extent of procedures you have previously performed to test the disclosures made in the bank's financial statements in accordance with IFRS 7, *Financial Instruments: Disclosures* may not change. - Have you considered whether there are any inconsistencies between the assumptions used in the ECL model and the information disclosed in the notes to the financial statements? - Have you considered whether the disclosures in the financial statements achieve fair presentation in accordance with the applicable financial reporting framework?	**ISA 315 (Revised)** **ISA 320** **ISA 330** **ISA 450** **ISA 500** **ISA 540** **ISA 700 (Revised)[21]**
11. Considerations how to report Key Audit Matters (KAM) on the impairment provisions contained in the bank's financial statements			

[21] ISA 700 (Revised), Forming an Opinion and Reporting on Financial Statements

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		- Have you considered communicating a KAM? - Does your KAM fully address the requirements of ISA 701? - Refer to **Note 2** below.	**ISA 260** **ISA 315 (Revised)** **ISA 330** **ISA 540** **ISA 701**[22]
12. Considerations of other interventions that an audit firm and the engagement team can put in place to address the audit implications of ECL			
- Has your firm developed policies and procedures for hiring and/or partnering with appropriate skilled resources, for example, economists and actuaries? - Has your firm developed policies and procedures for training requirements on the audit implications of IFRS 9 and the ECL model? - Has your firm developed policies and procedures for sourcing data, such as appropriate available economic forecast and growth rates?	**ISQC 1**	- Does your engagement quality control reviewer have the relevant expertise and additional specialised support should it need to be provided (e.g. IFRS 9 ECL forecasting experience and support)? - Have you considered a similar completed ECL audit within your network firm offices to use as a reference?	**ISA 220** **ISA 315 (Revised)** **ISA 330** **ISA 540** **ISA 580**[23] **ISA 620**[24]

[22] ISA 701, Communicating Key Audit Matters in the Independent Auditor's Report
[23] ISA 580, Written Representations
[24] ISA 620, Using the Work of an Auditor's Expert

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		- Have you considered whether it is necessary to obtain specific written representation from management and, where appropriate, those charged with governance about whether the impairment provisions calculated using ECL models have been recognised, measured, presented and disclosed in accordance with the applicable financial reporting framework? - Have you considered the use of an auditor's expert (e.g. economists and actuaries)? - Have you considered if there is any conflict of interest and/or independence considerations (consulting engagements related to IFRS 9 and ECL models) within your firm or network firm? - Have you considered the skills set required to perform the audit of ECL?	**IRBA Code 290.154-290.163**

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<tr><th colspan="4">Question to be considered and responded to</th></tr>
<tr><td><u>FIRM LEVEL</u></td><td><u>Reference to ISA/Other</u></td><td><u>ENGAGEMENT LEVEL</u></td><td><u>Reference to ISA/Other</u></td></tr>
<tr><td></td><td></td><td>- Have you considered discussing all relevant guidance on IFRS 9 and the ECL model (refer Note 1) with management and your audit team?</td><td></td></tr>
<tr><td colspan="4">13. <u>Considerations for how current audit approaches to auditing complex accounting estimates (e.g., banking, insurance industries) can be used to assist auditors in the approach to the audit implications of ECL</u></td></tr>
<tr><td>- Has your firm considered leveraging its existing audit approach in life or health insurance companies to enhance the audit of forward-looking information?</td><td>ISQC 1</td><td>- Have you considered audit guidance that has previously been developed for other industries which may assist you in the approach to the audit implications of the ECL models? These may include:
• Access to an information store, i.e. practice notes published by the Actuarial Society.
• Leveraging from your existing audit approach in life or health insurance companies.</td><td>ISA 315 (Revised)
ISA 330
ISA 520[25]
ISA 540</td></tr>
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[25] ISA 520, Analytical Procedures

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		- Have you considered leveraging off the data analytics currently performed on financial instruments?	
14. Ethical considerations when an audit firm is engaged to consult with a bank on the development of their ECL models and the potential of self-review threat			
- Has your firm put in place client acceptance procedures that address the risk of self-review in these engagements or assignments? - Has your firm implemented appropriate safeguards? - Has your firm considered if there is sufficient capacity to perform the engagement?	**ISQC 1**	- Are you aware of services prohibited in terms of the Companies Act? - Are you aware of the prohibitions provided for in the IRBA *Code of Professional Conduct for Registered Auditors* in particular with regard to the development of financial systems? - Are there any other restrictions prescribed by other regulators? - Have you discussed with and obtained approval for non-assurance engagements from those charged with governance, if allowed?	**ISA 210** **ISA 250** **ISA 315 (Revised)** **ISA 330** **IRBA Code 290.154-290.163** **Companies Act, 2008**

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		- Have you considered the extent to which the independence provisions apply to your network firm offices?	
15. Considerations for auditor ~~rotation~~ succession and challenges to predecessor auditors			
		- If you are a successor auditor: • Have you considered the time and resource requirements needed to test the impairment provisions calculated using the ECL model? • Have you considered communicating with the predecessor auditor to review the predecessor auditor's working papers to obtain evidence regarding the opening balances?	**ISA 315 (Revised)** **ISA 330** **ISA 510**[26]
16. Considerations for internal control testing			
- Has your firm considered the availability of appropriate resources (IT auditors and others)?	**ISQC 1**	- Have you reviewed the model governance including forward looking information (e.g.	**ISA 265**[27] **ISA 315 (Revised)**

[26] ISA 510, Initial Audit Engagements – Opening Balances
[27] ISA 265, Communicating Deficiencies in Internal Control to Those Charged With Governance and Management

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		entity level controls and process level controls)? - Have you tested the design and implementation of the ECL model and related systems including IT general controls and application controls related to significant risks? - Have you considered testing the operating effectiveness of controls over: • Source data; and • Disclosure? - Have you obtained the results of the internal model validation process and reviewed the results (risk identification)? - Have you considered the findings from the work of internal auditors? - Have you considered:	**ISA 330** **ISA 540** **ISA 610 (Revised 2013)**[28]

[28] ISA 610 (Revised 2013), Using the Work of Internal Auditors

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		• The transfer of data from old to new systems? • The changes to existing systems that would have to be tested? • The inclusion of new systems for reliance? **NOTE:** Reliance on internal audit is not appropriate for significant risks. **NOTE:** Due to the nature of ECL models it is envisioned that substantive procedures alone will not be sufficient.	
17. Considerations for the audit of South African Income Tax implications			
- Has your firm employed appropriate tax skills/resources? - Refer to **Note 3** below.	**ISQC 1**	- Have you considered the use of a tax expert? - Have you considered the impact of the ECL on: • Deferred tax? • Assessed losses?	**ISA 315 (Revised)** **ISA 330** **ISA 620**

Question to be considered and responded to			
FIRM LEVEL	**Reference to ISA/Other**	**ENGAGEMENT LEVEL**	**Reference to ISA/Other**
		• Deductibility for tax purposes (as well as reversal of previous year ECL provisions? • Tax rate reconciliation disclosures?	

IRBA STAFF AUDIT PRACTICE ALERT: THE AUDIT IMPLICATIONS OF THE EXPECTED CREDIT LOSS MODEL FOR THE AUDITORS OF BANKS

NOTES

1. **Relevant Guidance on IFRS 9 and the ECL Model**

   - The IRBA website contains a list of links to relevant guidance on IFRS 9 and the ECL model, which has been developed internationally and locally, and is known to the IFRS 9 ECL Task Group at the date of the issue of this document.
   - This list of relevant guidance on IFRS 9 and the ECL model is not meant to be exhaustive.

2. **SARB KAM**

   - Banks are advised to remain alert for further guidance or communication on KAM from the SARB.

3. **South African Revenue Services (SARS) Directive**

   - A directive, dated 17 February 2012, was issued to the Banking Association of South Africa (BASA) to clarify the income tax treatment of doubtful debts as related to banks for the purpose of determining the Section 11(j) doubtful debt allowance of the Income Tax Act No.58 of 1962 (as amended).
   - This directive is applicable to all BASA members that apply IAS 39 to assess the collectability of financial assets that are measured at amortised cost and establish the appropriate impairment provision. IAS 39 will be replaced by IFRS 9 for reporting periods beginning on or after 1 January 2018.
   - SARS has initiated a process of determining the impact of IFRS 9 on a bank's impairment provisions for the purpose of determining the Section 11(j) allowance. SARS has advised that it is expected that this process will be concluded in the next 18 months, after which a new directive will be issued.
   - Registered auditors are required to use the most recent directive issued by SARS.

Commented [NB1]: Link to IRBA Website dedicated page