

CHAPTER 13-03-25

SUPERVISORY COMMITTEE AUDITS AND VERIFICATIONS

Section

13-03-25-01	Definitions
13-03-25-02	General Responsibilities of the Supervisory Committee
13-03-25-03	Audit Responsibility of the Supervisory Committee
13-03-25-04	Requirements for Verification of Accounts
13-03-25-05	Assistance From Outside, Compensated Person
13-03-25-06	Audit Report and Working Paper Maintenance and Access
13-03-25-07	Sanctions for Failure to Comply With This Chapter
13-03-25-08	Statutory Audit Remedies for Credit Unions

13-03-25-01. Definitions.

1. "Balance sheet audit" means the examination of a credit union's assets, liabilities, and equity under generally accepted auditing standards by an independent public accountant for the purpose of opining on the fairness of the presentation on the balance sheet. Credit unions required to file call reports consistent with GAAP should ensure the audited balance sheet is likewise prepared on a GAAP basis. The opinion under this type of engagement would not address the fairness of the presentation of the credit union's income statement, statement of changes in equity (including comprehensive income), or statement of cashflows.
2. "Compensated person" means any accounting or auditing professional, excluding a credit union employee, who is compensated for performing more than one supervisory committee audit or verification of members' accounts per calendar year, or both.
3. "Financial statement audit" or "opinion audit" means an audit of the financial statements of a credit union performed in accordance with GAAS by an independent person who is licensed by the state. The objective of a financial statement audit is to express an opinion as to whether those financial statements of the credit union present fairly, in all material respects, the financial position and the results of its operations and its cashflows in conformity with GAAP, as defined herein.
4. "GAAP" means generally accepted accounting principles, which refers to the conventions, rules, and procedures which define accepted accounting practice. GAAP includes both broad general guidelines and detailed practices and procedures, provides a standard by which to measure financial statement presentations, and encompasses not only accounting principles and practices but also the methods of applying them.
5. "GAAS" means generally accepted auditing standards, which refers to the standards approved and adopted by the American institute of certified public accountants which apply when an independent, licensed certified public accountant audits financial statements. Auditing standards differ from auditing procedures in that "procedures" address acts to be performed, whereas "standards" measure the quality of the performance of those acts and the objectives to be achieved by use of the procedures undertaken. In addition, auditing standards address the auditor's professional judgment exercised in performing the audit and in preparing the report of the audit.
6. "Independent" means the impartiality necessary for the dependability of the compensated auditor's findings. Independence requires the exercise of fairness toward credit union officials, members, creditors, and others who may rely upon the report of a supervisory committee audit report.

7. "Internal control" means the process, established by the credit union's board of directors, officers, and employees designed to provide reasonable assurance of reliable financial reporting and safeguarding of assets against unauthorized acquisition, use, or disposition.
8. "Reportable conditions" means a matter coming to the attention of the independent, compensated auditor which in the auditor's judgment represents a significant deficiency in the design or operation of the internal control structure of the credit union which could adversely affect its ability to record, process, summarize, and report financial data consistent with the representations of management in the financial statements.
9. "State-licensed person" means a certified public accountant or public accountant who is licensed by the state to perform accounting or auditing services for that credit union.

History: Effective January 1, 2007.

General Authority: NDCC 6-01-04

Law Implemented: NDCC 6-06-06

13-03-25-02. General responsibilities of the supervisory committee.

1. **Basic.** The supervisory committee is responsible for ensuring that the board of directors and management of the credit union:
 - a. Meet required financial reporting objectives; and
 - b. Establish practices and procedures sufficient to safeguard members' assets.
2. **Specific.** To carry out the responsibilities set forth in subsection 1, the supervisory committee must determine whether:
 - a. Internal controls are established and effectively maintained to achieve the credit union's financial reporting objectives which must be sufficient to satisfy the requirements of the supervisory committee audit, verification of members' accounts and its additional responsibilities;
 - b. The credit union's accounting records and financial reports are promptly prepared and accurately reflect operations and results;
 - c. The relevant plans, policies, and control procedures established by the board of directors are properly administered; and
 - d. Policies and control procedures are sufficient to safeguard against error, conflict of interest, self-dealing, and fraud.
3. **Mandates.** In carrying out the responsibilities set forth in subsections 1 and 2, the supervisory committee must:
 - a. Ensure that the credit union adheres to the measurement and filing requirements for reports filed with the commissioner for the department of financial institutions under North Dakota Century Code section 6-06-08 and with the national credit union administration board under part 741.6 of national credit union administration rules and regulations;
 - b. Perform or obtain a supervisory committee audit, as prescribed in section 13-03-25-04 and under North Dakota Century Code section 6-06-15;
 - c. Verify or cause the verification of members' accounts against the record of the credit union, as prescribed in section 13-03-25-06; and

- d. Act to avoid imposition of sanctions for failure to comply with the requirements of this chapter, as prescribed in sections 13-03-25-07 and 13-03-25-08.

History: Effective January 1, 2007.

General Authority: NDCC 6-01-04

Law Implemented: NDCC 6-06-06

13-03-25-03. Audit responsibility of the supervisory committee.

1. **Annual audit requirement.** A credit union is required to obtain an annual supervisory committee audit that occurs at least once every calendar year (period of performance) and must cover the period elapsed since the last audit period (period effectively covered).
2. **Financial statement audit.** Any credit union with assets greater than twenty-five million dollars as of its previous year-end call report must obtain an annual audit of its financial statements performed in accordance with GAAS by an independent person who is licensed to do so in this state. Any credit union with assets less than twenty-five million dollars may also choose this option. Prior to obtaining a financial statement audit, the credit union will make a good-faith attempt to obtain a copy of the peer review report of the auditing firm directly from the auditing firm to ensure the firm's auditing practices and procedures are in conformance with GAAS.
3. **Supervisory committee alternative to financial statement audit.** Any credit union with assets less than twenty-five million dollars must obtain either of the following options to a financial statement audit:
 - a. **Balance sheet audit.** A balance sheet audit performed by a person who is licensed to do so by this state.
 - b. **Audit per supervisory committee guide.** An audit performed by the supervisory committee, its internal auditor, or any other qualified person (such as a certified public accountant, public accountant, league auditor, credit union auditor consultant, former financial institutions examiner, etc.) in accordance with the procedures prescribed in the national credit union administration's supervisory committee guide. Qualified persons who are not state-licensed may not provide assurance services under this subsection.

History: Effective January 1, 2007.

General Authority: NDCC 6-01-04

Law Implemented: NDCC 6-06-06

13-03-25-04. Requirements for verification of accounts.

1. **Verification obligation.** The supervisory committee, at least every two years, shall cause the accounts of members to be verified against the records of the treasurer of the credit union.
2. **Methods.** Any of the following methods may be used to verify members' passbooks and accounts, as appropriate:
 - a. **Controlled verification.** A controlled verification of one hundred percent of members' share and loan accounts.
 - b. **Statistical method.** A sampling method which provides for:
 - (1) Random selection;
 - (2) A sample which is representative of the population from which it is selected;
 - (3) An equal choice of selecting each dollar in the population;

- (4) Sufficient accounts in both number and scope on which to base conclusions concerning management's financial reporting objectives; and
 - (5) Additional procedures to be performed if evidence provided by confirmations alone is not sufficient.
- c. Nonstatistical method. When the verification is performed by an independent person licensed by the state, the auditor may choose among the sampling methods set forth in subdivisions a and b and nonstatistical sampling methods consistent with GAAS if such methods provide for:
- (1) Sufficient accounts in both number and scope on which to base conclusions concerning management's financial reporting objectives to provide assurance that the general ledger accounts are fairly stated in relation to the financial statements taken as a whole;
 - (2) Additional procedures to be performed by the auditor if evidence provided by confirmations alone is not sufficient; and
 - (3) Documentation of the sampling procedures used and of their consistency with GAAS, to be provided to the commissioner of the department of financial institutions upon request.
3. **Retention of records.** The supervisory committee must retain the records of each verification of members' passbooks and accounts until it completes the next verification of members' passbooks and accounts.

History: Effective January 1, 2007.

General Authority: NDCC 6-01-04

Law Implemented: NDCC 6-06-06

13-03-25-05. Assistance from outside, compensated person.

- 1. **Unrelated to officials.** A compensated auditor who performs a supervisory committee audit on behalf of a credit union may not be related by blood or marriage to any management employee, member of either the board of directors, the supervisory committee, or the credit committee, or loan officer of that credit union.
- 2. **Engagement letter.** The engagement of a compensated auditor to perform all or a portion of the scope of a financial statement audit or supervisory committee audit shall be evidenced by an engagement letter. In all cases, the engagement must be contracted directly with the supervisory committee. The engagement letter must be signed by the compensated auditor and acknowledged therein by the supervisory committee prior to commencement of the engagement.
- 3. **Contents of letter.** The engagement letter shall:
 - a. Specify the terms, conditions, and objections of the engagement;
 - b. Identify the basis of accounting to be used;
 - c. If a supervisory committee guide audit, include an appendix setting forth the procedures to be performed;
 - d. Specify the rate of, or total, compensation to be paid for the audit;
 - e. Provide that upon completion of the engagement letter, the auditor shall deliver to the supervisory committee a written report of the audit and notice in writing, either within the

report or communicated separately, of any internal control reportable conditions or irregularities or illegal acts, if any, which come to the auditor's attention during the normal course of the audit, i.e., no notice required if none noted;

- f. Specify a target date of delivery of the written reports, such target date not to exceed one hundred twenty days from date of calendar or fiscal yearend under audit (period covered), unless the supervisory committee obtains a waiver from the commissioner of the department of financial institutions;
 - g. Certify that department of financial institution staff or national credit union administration staff, or both, will be provided unconditional access to the complete set of original working papers, either at the offices of the credit union or at a mutually agreed-upon location, for purposes of inspections; and
 - h. Acknowledge that working papers shall be retained for a minimum of three years from the date of the written report.
4. **Complete scope.** If the engagement is to perform a supervisory committee guide audit intended to fully meet the requirements of subdivision b of subsection 3 of section 13-03-25-03, the engagement letter shall certify that the audit will address the complete scope of that engagement.
5. **Exclusions from scope.** If the engagement is to perform a supervisory committee guide audit which will exclude any item required by the applicable section, the engagement letter shall:
- a. Identify the excluded items;
 - b. State that, because of the exclusions, the resulting audit will not, by itself, fulfill the scope of the supervisory committee audit; and
 - c. Caution that the supervisory committee will remain responsible for fulfilling the scope of a supervisory committee audit with respect to the excluded items.

History: Effective January 1, 2007.

General Authority: NDCC 6-01-04

Law Implemented: NDCC 6-06-06

13-03-25-06. Audit report and working paper maintenance and access.

- 1. **Audit report.** Upon completion or receipt, or both, of the written report of a financial statement audit or a supervisory committee audit, the supervisory committee must verify that the audit was performed and reported in accordance with the terms of the engagement letter prescribed herein. The supervisory committee must submit the reports to the board of directors and provide a summary of the results of the audit to the members of the credit union orally or in writing at the next annual meeting of the credit union. If a member so requests, the supervisory committee shall provide the member access to the full audit report. If the department of financial institutions or the national credit union administration so requests, the supervisory committee shall provide either the department of financial institutions or national credit union administration a copy of each of the audit reports it receives or produces.
- 2. **Working papers.** The supervisory committee shall be responsible for preparing and maintaining, or making available, a complete set of original working papers supporting each supervisory committee audit. The supervisory committee shall, upon request, provide the department of financial institutions or national credit union administration staff unconditional access to such working papers, either at the offices of the credit union or at a mutually agreed-upon location, for purposes of inspecting such working papers.

History: Effective January 1, 2007.

General Authority: NDCC 6-01-04

Law Implemented: NDCC 6-06-06

13-03-25-07. Sanctions for failure to comply with this chapter.

Failure of a supervisory committee or its independent compensated auditor or other person, or any of them, to comply with the requirements of this section, or the terms of the engagement letter required by this section, is ground for:

1. The commissioner to reject the supervisory committee audit and provide a reasonable opportunity to correct deficiencies;
2. The commissioner to impose the remedies available in section 13-03-25-08, provided any of the conditions specified therein is present; and
3. The national credit union administration board to seek formal administrative sanctions against the supervisory committee or its independent, compensated auditor, or both, pursuant to section 206(r) of the Federal Credit Union Act [12 U.S.C. 1786(r)].

History: Effective January 1, 2007.

General Authority: NDCC 6-01-04

Law Implemented: NDCC 6-06-06

13-03-25-08. Statutory audit remedies for credit unions.

1. **Audit by alternative licensed person.** The state credit union board may compel a credit union to obtain a supervisory committee audit which meets the minimum requirements of section 13-03-25-03 and which is performed by an independent person who is licensed by the state for any fiscal year in which any of the following three conditions is present:
 - a. The supervisory committee has not obtained an annual financial statement audit or performed a supervisory committee audit;
 - b. The supervisory committee has obtained a financial statement audit or performed a supervisory committee audit which does not meet the requirements of this chapter; or
 - c. The credit union has experienced serious and persistent recordkeeping deficiencies as defined in subsection 3.
2. **Financial statement audit required.** The state credit union board may compel a credit union to obtain a financial statement audit performed in accordance with GAAS by an independent person who is licensed by the state, even if such audit is not required by section 13-03-25-03, for any fiscal year in which the credit union has experienced serious and persistent recordkeeping deficiencies as defined in subsection 3. The objective of a financial statement audit performed under this subsection is to reconstruct the records of the credit union sufficiently to allow an unqualified or, if necessary, a qualified opinion on the credit union's financial statements. An adverse opinion or disclaimer of opinion should be the exception rather than the norm.
3. **Serious and persistent recordkeeping deficiencies defined.** A recordkeeping deficiency is serious if the state credit union board reasonably believes that the board of directors and management of the credit union have not timely met financial reporting objectives and established practices and procedures sufficient to safeguard members' assets. A serious recordkeeping deficiency is persistent when it continues beyond a usual, expected, or reasonable period of time.

History: Effective January 1, 2007.
General Authority: NDCC 6-01-04
Law Implemented: NDCC 6-06-06