

Performing A Quality Assurance Review in the Banking Environment

The International Professional Practice Framework (IPPF)



Overview of The IIA Standards



Attribute Standards:

- Purpose, Authority and Responsibility _____ (1000)
- Independence and Objectivity _____ (1100)
- Proficiency and Due Professional Care _____ (1200)
- Quality Assurance and Improvement Program _____ (1300)

Performance Standards:

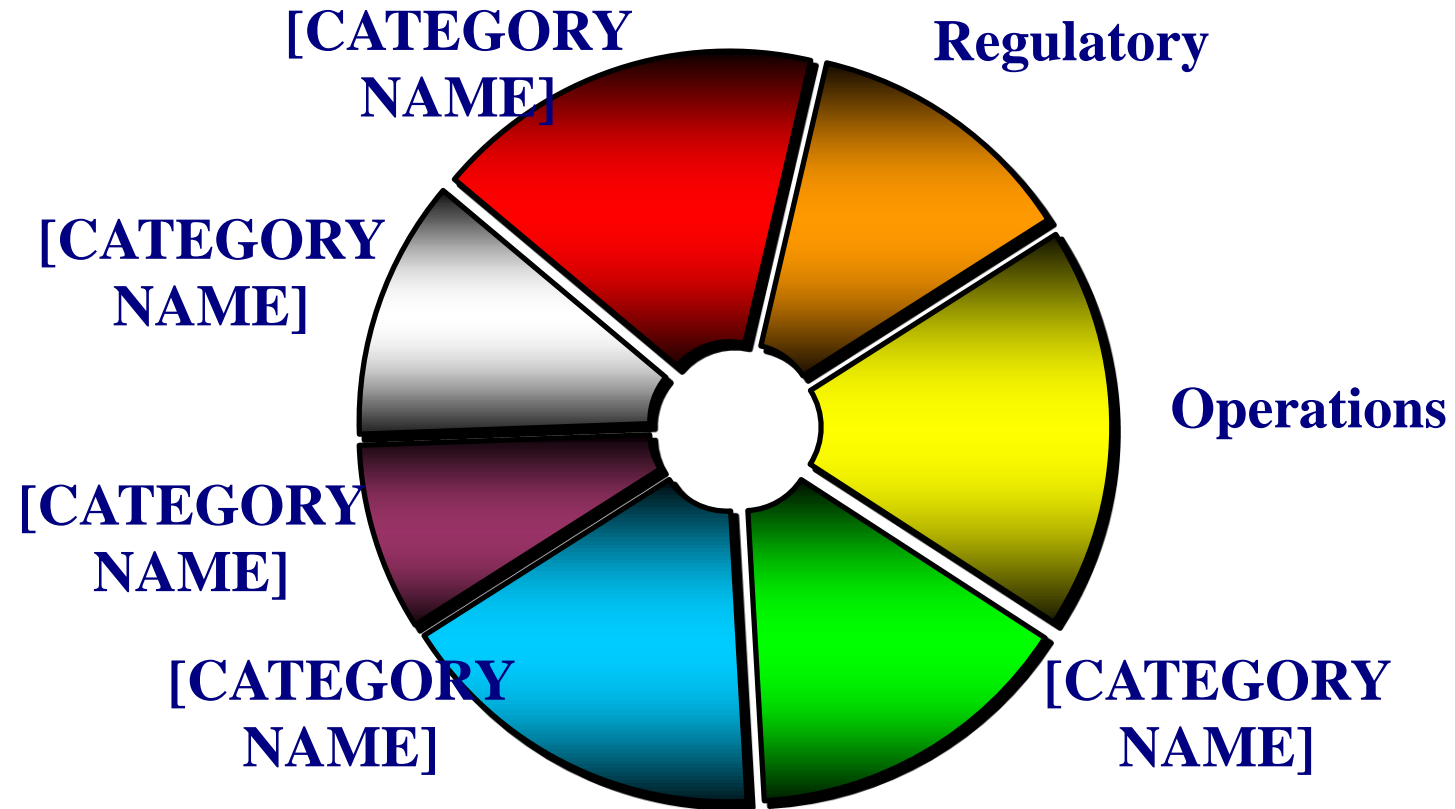
- Managing the Internal Audit Activity _____ (2000)
- Nature of Work _____ (2100)
- Engagement Planning _____ (2200)
- Performing the Engagement _____ (2300)
- Communicating Results _____ (2400)
- Monitoring Progress _____ (2500)
- Resolution of Management's Acceptance of Risks _____ (2600)

Could this Happen to Your Bank?



What is a Company?

Where is Governance, Risk & Control



Categories of Risk

- **Strategic**
- **Operational**
- **Financial**
- **Compliance**

Professional competence and due professional care

Professional competence, including the knowledge and experience of each internal auditor and of internal auditors collectively, is essential to the effectiveness of the bank's internal audit function.

Professional competence depends on the auditor's capacity to collect and understand information, to examine and evaluate audit evidence and to communicate with the stakeholders of the internal audit function. This should be combined with suitable methodologies and tools and sufficient knowledge of auditing techniques.

The head of internal audit should be responsible for acquiring human resources with sufficient qualifications and skills to effectively deliver on the mandate for professional competence and to audit to the required level. He/she should continually assess and monitor the skills necessary to do so. The skills required for senior internal auditors should include the abilities to judge outcomes and make an impact at the highest level of the organization

The Strength of a Good Decision

- In challenging times, a good financial decision begins with a strong financial company.
- A.M. Best Company: A++ (Superior; top category of 15)
Fitch Ratings: AA+ (Very Strong; second category of 21)
Moody's Investors Service: Aa2 (Excellent; third category of 21)
Standard & Poor's: AA+ (Very Strong, second category of 21)

A simple set of objectives drives Banks:

- **Quality products.** Products people are proud to own.
- **Quality service and support.** Service and support through and to our national network of local financial professionals.
- **Long-term financial stability.** Stability from balance sheet strength and business diversification.

Audit Vision

*Modern internal auditing, to be successful, must be **grounded on management support and acceptance** and on imaginative service to management The auditor must mount continuing campaign to sell his product to executive management and the products he sells must be of the quality that will **capture and keep management's interest***

Larry Sawyer 1973

What Kind of Audits Do they Perform

Claims

Third party/Outsourced Service Providers

Financial Instrument Trading (e.g., Derivatives)

Anti-Money Laundering

IT (e.g., System Development Life Cycle)

Cyber Terrorism

Internal Auditing Capabilities

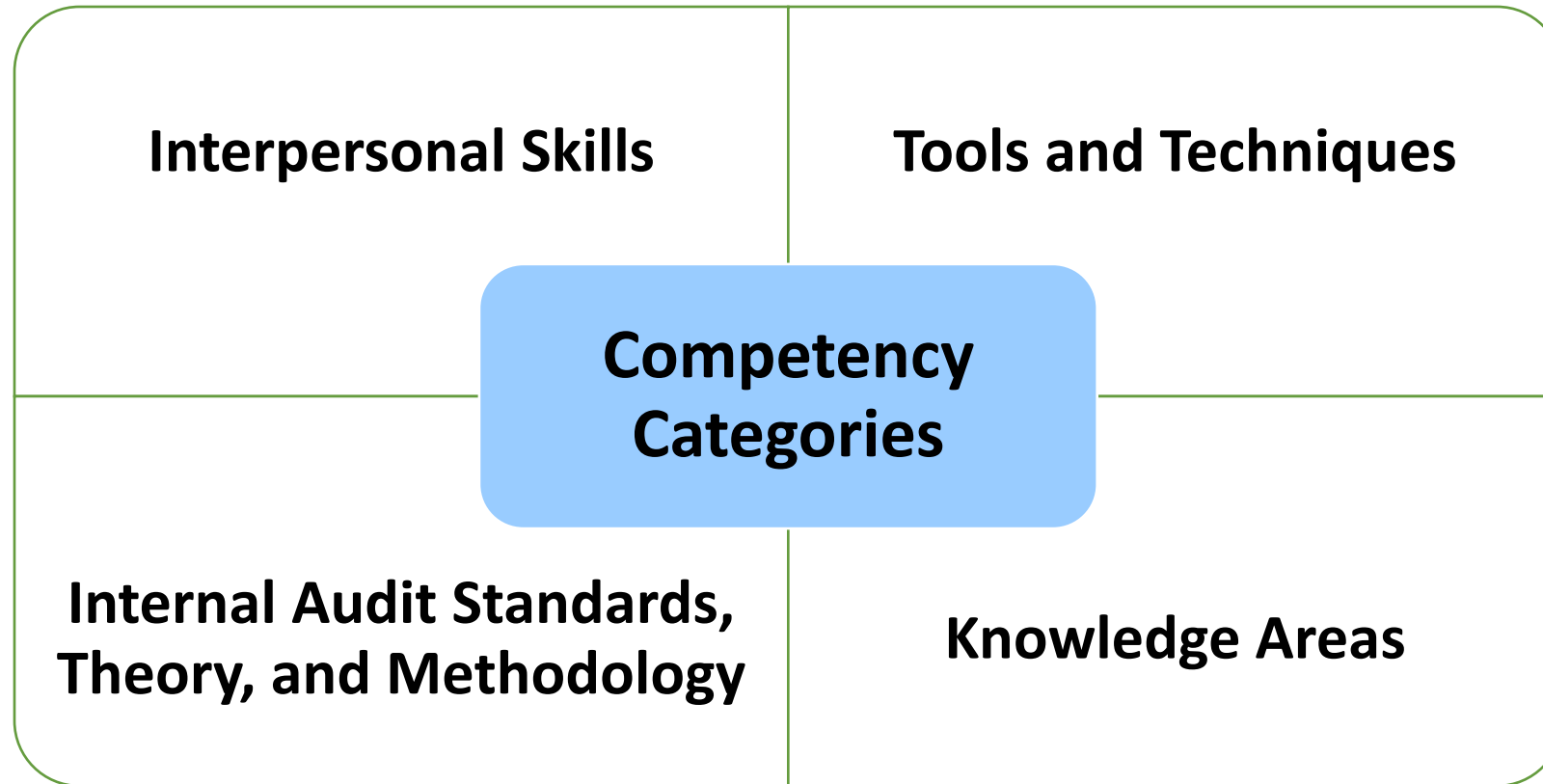
- **Independence of internal auditing and flexibility in deploying resources**
- **Business understanding**
- **More expanded role for internal auditing**
- **Expertise in IT tools for data collection and analysis**
- **Monitoring, reporting, and demonstrating value**

ISO 31000

Risk Management

- Is a value-added activity.
- Is inseparable from the organization's decision-making processes and operations.
- Addresses uncertainty in a structured, orderly, unambiguous, and timely fashion.
- Makes use of the best information available.
- Is customized to the organization's operating environment, culture, and objectives.
- Is transparent, auditable, and inclusive of all stakeholders.
- Uses an iterative cycle to generate continual improvement, organizational learning, and the ability to quickly respond to changing environments.

Internal Audit Designated Competencies



Board and Management Responsibilities and Expectations from a Q/A Review

The board of directors is responsible and accountable for establishing, overseeing, and maintaining audit functions that:

- Effectively test and monitor internal controls,
- Ensure the reliability of the bank's financial statements and reporting, and
- Satisfy statutory, regulatory, and supervisory requirements.

Effective audit programs should:

- Provide objective, independent reviews and evaluations of bank activities, internal controls, and management information systems (MIS).
- Help maintain or improve the effectiveness of bank risk management processes, controls, and corporate governance.
- Provide reasonable assurance about the accuracy and timeliness with which transactions are recorded and the accuracy and completeness of financial and regulatory reports.

Internal audit programs (including those that are outsourced or co-sourced to third-party vendors) are traditionally associated with:

- Independent and objective evaluation and testing of a bank's overall internal control system (i.e., operational and administrative controls beyond those associated with financial statement preparation),
 - Ensuring the safeguarding and proper recording of a bank's assets.

The directors must ensure that the audit programs test internal controls to identify:

- Inaccurate, incomplete, or unauthorized transactions;
- Deficiencies in the safeguarding of assets;
- Unreliable financial and regulatory reporting;
- Violations of laws or regulations; and
- Deviations from the institution's policies and procedures.

“MY BANK”: WHAT HAPPENED AND WHY

What Happened at “My Bank” ?

1. What Did Employees Do?

- “My Bank” employees applied for approximately 565,000 credit card accounts and created fake email addresses to enroll customers in online banking services without their consent.
- Without customer authorization, employees opened more than 2 million deposit accounts and transferred funds from existing accounts into them. They also issued and activated related PINs.

2. What Was the Impact on Customers?

- Customers of existing accounts were penalized for insufficient funds and/or overdrafts due to interest charges and other fees on the new fake accounts.

3. What Was the Impact for “My Bank” ?

- “My Bank” paid over \$185 million in fines to the Consumer Financial Protection Bureau, the Los Angeles City Attorney, and the Office of the Comptroller of the Currency. They also set aside more than \$5 million for customer remediation.
- The bank’s stock has dropped to its lowest level since 2014, falling 10% since the beginning of September.
- “My Bank” is clawing back compensation valued at \$41 million from its chairman and chief executive,
- The bank fired close to 5,300 employees and managers, and a class action lawsuit alleging wrongful termination is currently seeking damages of \$2.6 billion.

Why Did This Happen?

Sales targets and incentive programs coupled with pressure from leadership, including senior leaders and direct managers, fostered an environment of ethical pressure in which employees felt forced to engage in unethical business practices.

Key contributors to the overall environment of ethical pressure include:

- **Sales Targets:** “My Bank’s” pursuit of the cross-selling strategy resulted in a target of 8 different accounts per customer, while other banks similar in size average 3 accounts per customer.
- **Tone at the Top:** Employee complaints point to questionable tone at the top. For example, branch managers were pressured to reach 120% of their daily quotas and regional managers scheduled hourly check-in calls to measure employee’s progress on daily quotas.
- **Direct Manager Leadership:** Employees also allege that managers pressured new hires to meet sales quotas in their first two months, and that managers frequently suggested improper methods of conducting business as a means to increase sales.
- **Fear of Retaliation:** Former “My Bank” employees are alleging that they were terminated after reporting concerns to the company’s helpline.

A CULTURAL FAILURE

Key Attributes That Impact a Culture of Integrity

RiskClarity: A Corporate Integrity Service™

