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# Industry Trends in Financial Services

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# Session CPE Requirements

- You need to attend 50 minutes to receive the full 1 CPE credit.
- 4 Knowledge Checks will be launched during this session. You must respond to a minimum of 3 to receive the full 1 CPE credit.

**\*\*Both requirements must be met to receive CPE credit\*\***



# Learning Objectives



Identify fraud



Name fraud prevention techniques



Describe internal controls



Identify efficient systems





# Fraud



# What Is Fraud?

Definition: An intentional act that results in a material misstatement in financial statements that are the subject of an audit.

Two types of misstatements are relevant to the consideration of fraud:

- Misstatements arising from fraudulent financial reporting
- Misstatements arising from misappropriation of assets (theft or defalcation)



# Characteristics of Fraud

Three conditions generally are present when fraud occurs:

- **Incentive/pressure** - Reason to commit fraud
- **Opportunity** - Absence of controls, ineffective controls, ability of management to override controls
- **Rationalize/attitude** - Individual possesses a character or set of ethical values that allows them to commit fraud



# Who Can Commit Fraud?

23% of fraud is committed by owners/executives

Fraudster's level of authority is strongly correlated with the size of the fraud

The typical fraud committed by an employee lasted 8 months before it was detected

The typical fraud committed by an owner/executive lasted 18 months

Source: 2022 Report to the Nations

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# Knowledge Check #1

Which of the following are characteristics of fraud?

- a. Opportunity
- b. Rationalization
- c. Pressure
- d. All the above
- e. None of the above



# Weak Internal Controls and Inefficient Systems

Inadequate supervision

Insufficient documentation

Detection difficulty

Quantifying losses

Lack of segregation of duties

High turnover rate

Unauthorized transactions

Management override





# Fraud Prevention



# How Difficult Is It to Identify Fraud?



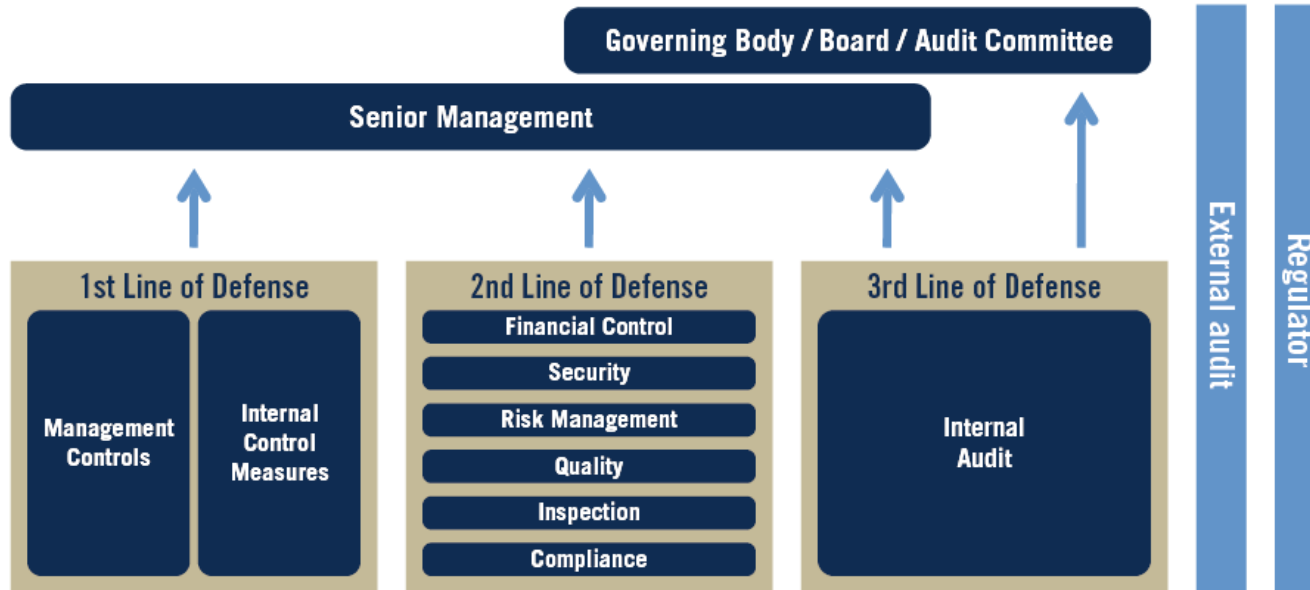
Like many, institutions are targets of insider and outsider fraud due to the easy access to money



As fraud becomes a more prevalent issue, it's important to understand when an environment is ripe for fraud and the ways that fraud is identified

# Fraud Risk Management

## The Three Lines of Defense Model



Adapted from ECIIA/FERMA *Guidance on the 8th EU Company Law Directive, article 41*

Source: IIA Position Paper: *The Three Lines of Defense in Effective Risk Management and Control*



# The Importance of Roles

Understand the varying roles of the CFO, external auditor, and forensic investigator

Why is it important for an organization to understand these varying roles?



# Efficient Systems Role in Fraud Prevention



Preventive controls



Detective controls



Corrective controls



Risk assessment



Automated monitoring



Predictive analytics



Behavioral analytics



Comprehensive ID verification



Strong authentication

# Knowledge Check #2

Which of the following is not an example of how efficient systems can help prevent fraud?

- a. Automated monitoring
- b. Risk assessment
- c. Vendor dependency
- d. Behavioral analytics







# Internal Controls



# What Is Internal Control?

Internal control is defined as a process, affected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations



# What Can Internal Controls Do?

Monitor and evaluate the effectiveness of the risk management system

Identify weaknesses in internal controls which should be corrected

Identify weaknesses which could expose the institution to loss if not corrected

Tailor the audit program so improperly controlled areas (risk areas) receive more attention

Determine the reliability and integrity of information

Determine compliance with policies, plans, procedures, laws, and regulations

Enhance the safeguarding of assets

Enhance economical and efficient use of resources



# Internal Controls Examples

Management has monitoring controls in place for all key areas at the institution

- Documentation of controls and key monitoring reports are in place
- There is validation the controls are functioning
  - Internal audit
  - Reporting as determined necessary

Management sets a zero tolerance for fraud at the institution

Institution has fraud policy

Institution has a whistleblower hotline



# Internal Controls Examples

- Institution requires rotation of duties
  - Periodic rotation
  - Mandatory vacations
- Institution has a process in place to respond to all findings from examiners, internal audit, and outside third parties
  - All third parties including:
    - Contracted internal audit including AML/CFT and ACH
    - Loan review
    - Bonding company
  - Tracking process in place with report of open items maintained
  - Identification of situations where management has accepted risk



# Knowledge Check #3

Which of the following would not be an internal control?

- a. Execute a wire transfer
- b. Test loans to determine they were approved by authorized personnel
- c. Review compliance policy for adequacy
- d. Reconcile investments safekept at the FHLB to a safekeeping statement provided by the FHLB





# Efficient Systems



# Benefits of Efficient Systems



Improve productivity



Enhance effectiveness



Enable scalability



Deliver value



Reduce costs



Support decision-making



Allocate resources



Minimize errors



Promote consistency



Reduce fraud



Regulatory compliance



Increase profitability





# Strategies to Improve Efficiency

## Assessment

Identify ways to improve operational efficiency

Structure

Process

Systems

## Optimization

Discover ways to improve process and system efficiency

Process

Systems

## Selection

Choose systems that support efficient operations

Systems



# Knowledge Check #4

How well do you believe your current systems support your operational efficiency and effectiveness efforts?

- a. Exceptionally well
- b. Adequately
- c. Inadequately, we need help now



# Actions You Can Take Today



Apply the three lines of defense (operational management, risk management and compliance, and internal audit) to help reduce the risk of fraud



Implement anti-fraud and/or ethics training to understand when conditions are favorable for fraudulent activities and the ways to identify it



Conduct fraud risk assessments and internal controls reviews to proactively reduce the risk of fraud and overall costs to the institution



Assess your existing systems to identify opportunities to enhance efficiency, minimize errors, and reduce the risk of fraud

# Thank you!

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