

Fraud and Insider Abuse Program

EXAMINATION OBJECTIVES

To recognize warning signs of fraud and insider abuse and to take appropriate measures to follow-up on possible instances of such activity.

To determine if the institution's internal control system is applicable to officers and directors as well as other employees.

To determine the institution's risk exposure associated with each significant instance of fraud or abuse.

To identify weaknesses in the institution's internal controls through detection and analysis of any patterns of fraud or abuse.

To properly report suspected criminal misconduct uncovered during the examination to appropriate law enforcement authorities.

To determine if the institution is reporting suspected criminal acts as § 563.180(d) requires.

To determine if the institution is properly completing SARs.

To determine if the institution has an adequate program of follow-up with law enforcement authorities regarding SARs it has filed.

EXAMINATION PROCEDURES

LEVEL I

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1. Review the adequacy of the institution's policies and procedures with respect to conflicts of interest. Determine whether the institution requires directors, officers, and employees to sign a Code of Ethics statement.

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2. Discuss the issue of fraud and insider abuse with the internal auditors and, if necessary, the external auditors to assess whether they have any concerns. Determine if they have made any reports on suspected fraud to the board or others.
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3. Review the results of the questionnaires to determine if adequate controls are in place to mitigate fraud. Assess the adequacy of controls that would prevent officers and directors from perpetrating fraud.
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4. Review the results of the various examination programs to determine if problems exist that may be symptomatic of fraud. In cases where fraud may be likely, investigate such problems to determine the cause of the problem (for example, poor staff training, errors, poor judgment).
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5. Review the institution's policies and procedures on reporting suspected criminal activity to law enforcement agencies and its board of directors for compliance with § 563.180(d).
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6. Review the institution's SARs, including those that OTS has filed, to determine if any patterns of criminality exist:

- Identify multiple SARs on individual suspects, location of violation (for example, loan center, savings branch), or type of violation.
 - Analyze any apparent pattern of fraud or abuse to determine if enhanced internal controls would deter any future abuse.
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7. Review all significant SARs, other reports, and patterns to determine if the institution has properly identified and addressed all related financial, operational, and legal risks; for example, valuation allowances established, internal controls strengthened, etc.
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8. Assess the institution's risk of fraud by reviewing the red flag warning signals and conditions in the institution. You should do this in conjunction with performing other examination programs and procedures, completing the Fraud Risk Evaluation Form (Appendix A) and, if necessary, by other appropriate means. You should notify your supervisor when you have rated any individual fraud risk score 4 or 5, and you believe that there is significant potential for insider abuse or fraud.

9. Consult with other examination crewmembers concerning the need to expand examination scope within certain areas based on an indication of a higher than acceptable risk of fraud within certain areas of the institution.

10. Notify the regional legal staff if any person attempts to obstruct the examination, in possible violation of criminal statute 18 USC 1517.

11. Obtain a list of deposit and loan accounts of directors, officers, and other affiliated persons. Test check these accounts for preferential rates and, for deposit accounts, appropriate board approval of any overdrafts.

12. Review Level II procedures and perform those necessary to test, support, and present conclusions derived from performance of Level I procedures.

LEVEL II

1. Choose a sample of SARs that the institution has filed. Review each sample SAR to determine its accuracy, completeness, timeliness, and propriety.

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2. Complete the following procedures if you have identified any instance of suspected criminal misconduct:

- Immediately notify the EIC and field manager.
- Consult with appropriate regional office staff or counsel to determine a course of action, including preparation of a SAR.
- Obtain input from regional office legal staff on Right to Financial Privacy Act issues during the preparation of every SAR.

The following elements are particularly important in preparing a successful SAR:

- A chronology of events.
- A summary of suspected violations.
- A list of key participants or affiliates.
- A list of potential helpful witnesses.
- Any supporting documentation.

3. Review the institution's independent audit reports to determine if specific procedures exist to detect fraud, as the American Institute of Certified Public Accountants (AICPA) rules require.

4. Review the institution's program of follow-up with law enforcement authorities to determine if timely and adequate follow-up is being conducted on significant SARs.

5. For institutions with composite ratings of 4 or 5, determine if, in possible violation of 12 USC § 1828(k), the institution has done either of the following:

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- Made, or has entered into an agreement to make, any golden parachute or indemnification payments.
 - Prepaid any salary, or any liability or legal expense, in anticipation of insolvency and with a view towards preventing the proper use or purpose of assets.
 - Notify the regional legal staff if the institution has done either one.
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6. Ensure that your review meets the Objectives of this Handbook Section. State your findings and conclusions, and appropriate recommendations for any necessary corrective measures, on the appropriate work papers and report pages.
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EXAMINER'S SUMMARY, RECOMMENDATIONS, AND COMMENTS

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