

Summary Table of Contents

Chapter 1:	Internal Controls and Their Basic Objectives
Chapter 2:	Designing Internal Control Systems
Chapter 3:	Monitoring Internal Controls
Chapter 4:	Internal Controls Checklists
Chapter 5:	Organizing the Internal Audit Function
Chapter 6:	Developing Audit Scope
Chapter 7:	Preparing Internal Audit Procedure Work Papers, Performing Audit Sampling, and Using Internal Audit Policy Checklists
Chapter 8:	Internal Audit Control Procedures
Chapter 9:	Internal Audit Policy Checklists

Contents

Chapter 1 Internal Controls and Their Basic Objectives

Importance of Internal Controls	1 — 1
Risk.....	1 — 1
Credit Risk	1 — 2
Interest Rate Risk	1 — 3
Liquidity Risk.....	1 — 4
Price Risk	1 — 5
Foreign Exchange Risk	1 — 6
Transaction Risk.....	1 — 6
Compliance Risk	1 — 7
Strategic Risk	1 — 8
Reputation Risk.....	1 — 8
Litigation Risk.....	1 — 9
Risk Summary	1 — 10
So What Is Internal Control?.....	1 — 10
Internal Control Defined	1 — 10
Internal Controls In Certain Regulations.....	1 — 12
Board of Director and Senior Management Responsibility.....	1 — 13
Nature and Scope of Internal Control Policy.....	1 — 14
General Goal of Internal Controls	1 — 14
Internal Control Components	1 — 15
Risk Management, Internal Controls, and Corporate Governance.....	1 — 17
Risk Management Elements	1 — 17
Exhibit 1.1: Sample Internal Control Policy Statement (for inclusion in other policies)	1 — 19
Exhibit 1.2: Sample Internal Control Policy	1 — 21
Exhibit 1.3: Sample Internal Control Procedures	1 — 29
Exhibit 1.4: Internal Control Quality Checklist	1 — 37

Chapter 2 Designing Internal Control Systems

Design Philosophies	2 — 1
The Five Components.....	2 — 1
Control Environment.....	2 — 1
Deposit and Operations Culture	2 — 2
Risk Assessment.....	2 — 3
Control Activities	2 — 3
Accounting, Information, and Communication Systems	2 — 4

Self-Assessment or Monitoring.....	2 — 5
Internal Control System Design Approach.....	2 — 5
Practice Scenario — Implementing Remote Deposit Capture	2 — 5
Control Environment.....	2 — 6
Risk Assessment.....	2 — 7
Control Activities	2 — 8
Start with the Basics.....	2 — 9
Executing New Products/Services Requires Clear Direction	2 — 10
Specific Written Operational Procedures Help Control Risk.....	2 — 12
Accounting, Information, and Communication Systems	2 — 13
Remote Deposit Capture Reporting — Different Types of Communication.....	2 — 14
Self-Assessment or Monitoring.....	2 — 14
Ongoing Monitoring for Success	2 — 14
Ensuring Efficiency and Effectiveness.....	2 — 15
Exhibit 2.1: Remote Deposit Capture Implementation	2 — 16
Exhibit 2.2: Risk Assessment Table	2 — 19
Exhibit 2.3: Risk and Existing Control Assessment Table	2 — 20

Chapter 3

Monitoring Internal Controls

Establishing a Monitoring Process	3 — 1
Initial Monitoring	3 — 1
Ongoing Monitoring.....	3 — 2
Self-Assessment.....	3 — 2
Independent Audit.....	3 — 3
How and Why to Monitor Internal Controls	3 — 3
Managing the Review Process.....	3 — 4
The Impact of Quality Controls in Daily Operations	3 — 4
Scheduling Periodic Reviews	3 — 5
Planned Reviews	3 — 5
Unplanned Reviews.....	3 — 6
Reporting the Findings of an Internal Assessment.....	3 — 6
Mandatory Follow-Up on Internal Control Exceptions.....	3 — 7
Exhibit 3.1: Sample Internal Control Advisory Memo and Monitoring Review Procedures	3 — 9
Exhibit 3.2: Sample Internal Control Analysis Worksheets	3 — 19
Exhibit 3.3: Sample Internal Control System Monitoring Schedule XYZ National Bank	3 — 24
Exhibit 3.4: Sample Internal Compliance Review Report	3 — 25
Exhibit 3.5: Sample Follow-Up on Internal Control Exceptions	3 — 26

Chapter 4 Internal Controls Checklists

Cash Accounts	4 — 1
Consigned Items and Other Customer Services	4 — 29
Bank Premises and Equipment	4 — 33
Branch Administration	4 — 63
Other Assets (and Other Liabilities)	4 — 65
Deposit Accounts	4 — 67
Payment Systems and Funds Transfer Activities (Wire Transfer Department)	4 — 79
Wire Transfer Compliance	4 — 88
Interbank Liabilities	4 — 90
Regulatory Reporting	4 — 93
EDP — Purchased Services	4 — 95
Internet Banking	4 — 101
Merchant Card Processing Policy	4 — 106
Records Retention	4 — 113
Automated Clearing House (ACH)	4 — 115
Centralized Purchasing	4 — 118
Retail Payment Systems	4 — 128
Data and Records Destruction	4 — 140
Debit Card	4 — 144
Irregularities and Illegal Acts: Investigation	4 — 151
Disaster Recovery with Regards to Power	4 — 154
Information Attacks	4 — 157
Remote Deposit Capture	4 — 166
Prepaid Cards	4 — 179

Chapter 5 Organizing the Internal Audit Function

Overview of the Internal Audit Function	5 — 1
The Role of the Internal Auditor	5 — 2
Relationship with External Audit	5 — 2
The Value of Independence	5 — 3
Reporting Relationships	5 — 3
Relationship with Regulatory Agencies	5 — 3
Developing an Internal Audit Policy	5 — 4
Establishing Job Descriptions	5 — 4
Designing the Reporting Hierarchy	5 — 5
Setting Internal Audit Staff Requirements	5 — 5
Assessing Staffing Needs for Smaller Banks	5 — 6
Rotating Assignments	5 — 6
Reporting Requirements	5 — 6
Department Management	5 — 7

Senior Management.....	5 — 7
Board of Directors.....	5 — 7

Chapter 6 Developing Audit Scope

Determining Audit Objectives.....	6 — 1
Recognizing the Environment.....	6 — 1
Internal Influences.....	6 — 1
Management Philosophy and Operating Style.....	6 — 2
Organizational Structure/Means of Delegating Authority and Responsibility.....	6 — 2
Management Control Methods.....	6 — 2
Human Resources Policies and Procedures.....	6 — 2
Audit Committee Strength and Responsibilities.....	6 — 3
FDICIA Guidelines for Audit Committee Membership.....	6 — 3
Evaluation of Internal Controls.....	6 — 5
External Influences.....	6 — 5
Monitoring and Reporting Requirements.....	6 — 5
Economic Factors.....	6 — 5
Industry Competition.....	6 — 5
Legislative Environment.....	6 — 6
FDICIA Guidelines.....	6 — 6
Provisions of FDICIA.....	6 — 6
Audit Independence.....	6 — 6
Audit Risk.....	6 — 6
Three Components of Audit Risk.....	6 — 7
Assessing Inherent Audit Risk.....	6 — 7
Assessing Audit Control Risk.....	6 — 8
Assessing Audit Detection Risk.....	6 — 8
Sample Risk Assessments.....	6 — 8
Example 1.....	6 — 8
Example 2.....	6 — 8
Risk Assessments and Internal Controls.....	6 — 8
Background.....	6 — 8
Control Environment.....	6 — 9
Control Procedures.....	6 — 9
Accounting and Internal Control Systems.....	6 — 10
Inherent Limitations of Internal Controls.....	6 — 10
Understanding the Accounting and Internal Control System.....	6 — 10
Control Procedures.....	6 — 11
Control Risk.....	6 — 11
Preliminary Assessment of Control Risk.....	6 — 11
Determining Scope of Coverage.....	6 — 11
Cost/Benefit Evaluations.....	6 — 11
Frequency and Amount of Testing.....	6 — 12
Types of Tests Performed.....	6 — 13
Tests of Controls.....	6 — 13

Substantive Tests.....	6 — 13
Information Technology (IT) Effects on Internal Controls.....	6 — 14
Risk Scoring System.....	6 — 14
Exhibit 6.1: Audit Risk Model.....	6 — 16
Exhibit 6.2: Internal Audit Review Questionnaire.....	6 — 17

Chapter 7
**Preparing Internal Audit Procedure Work Papers,
 Performing Audit Sampling, and Using Internal Audit Policy Checklists**

Internal Audit Procedure Work Papers.....	7 — 1
Work Paper Types.....	7 — 1
Classification of Work Paper Files.....	7 — 2
Permanent File.....	7 — 2
Current File.....	7 — 2
Organization of Work Papers.....	7 — 2
Work Paper Storage.....	7 — 4
Audit Sampling.....	7 — 4
Attribute Sampling.....	7 — 5
Determining Sample Size.....	7 — 6
Evaluating Sample Results.....	7 — 6
Variable Sampling.....	7 — 6
Classical Sampling.....	7 — 6
Advantages and Disadvantages of Classical Sampling.....	7 — 7
Probability Proportional Sampling.....	7 — 8
Advantages and Disadvantages of PPS.....	7 — 8
Exhibit 7.1: Wire Transfer Policy Internal Audit Procedures.....	7 — 9
Exhibit 7.2: Sample Wire Transfer Policy Internal Audit Checklist.....	7 — 10

Chapter 8
Internal Audit Procedures Checklists

Bank Security Procedures.....	8 — 1
Contingency Planning and Disaster Recovery Procedures.....	8 — 17
Bank Secrecy Act Procedures.....	8 — 26
Bank Secrecy Act: Customer Identification Program Procedures.....	8 — 65
Personal Computer Security Procedures.....	8 — 75
Information Security Procedures.....	8 — 81
Daylight Overdraft Procedures.....	8 — 117
Electronic Data Processing Procedures.....	8 — 123
Expedited Funds Availability Procedures.....	8 — 127
Record Retention and Recordkeeping Procedures.....	8 — 141
Wire Transfer Procedures.....	8 — 146

Deposit Procedures.....	8 — 150
Purchasing Procedures.....	8 — 175
Personal Banking Procedures.....	8 — 183
Servicing Arrangements Procedures.....	8 — 190
Interbank Liability Procedures.....	8 — 196
Consigned Items Procedures.....	8 — 204
Debit Card Program Procedures.....	8 — 210
Basic Financial Services Procedures.....	8 — 219
Identity Theft Risk Procedures.....	8 — 226
Contracts with Vendors Procedures.....	8 — 236
Prepaid Card Program Procedures.....	8 — 245

Chapter 9 Internal Audit Policy Checklists

Electronic Data Processing Policy.....	9 — 2
Expedited Funds Availability Policy.....	9 — 5
Wire Transfer Policy.....	9 — 17
Deposit Policy.....	9 — 20
Interbank Liability Policy.....	9 — 45
Bank Secrecy Act Policy.....	9 — 51
Information Security Policy.....	9 — 81
Daylight Overdraft Policy.....	9 — 124
Record Retention and Recordkeeping Policy.....	9 — 127
Personal Computer Security Policy.....	9 — 131
Bank Security Policy.....	9 — 135
Contingency Planning and Disaster Recovery Policy.....	9 — 150
Bank Secrecy Act: Customer Identification Program (CIP) Subpolicy.....	9 — 157
Consigned Items Policy.....	9 — 162
Purchasing Policy.....	9 — 166
Debit Card Program Policy.....	9 — 176
Basic Financial Services Policy.....	9 — 189
Identity Theft Risk Policy.....	9 — 194
Contracts with Vendors Policy.....	9 — 202
Personal Banking Policy.....	9 — 209
Prepaid Cards Program Policy.....	9 — 216