

Internal Auditors in Banking

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Introduction

Auditing is the inspection and verification of the accuracy of financial records and statements. Banks conduct internal audits of accounting records and procedures. Its task is to examine the risks that the bank faces, to review the adequacy of the controls in place to protect it from those risks, and to verify that the controls are working as intended. This report aspires to outline the purpose, roles, and standards involved in the internal auditing of banks.

The importance of internal auditing

Banks take on the role of securing and investing its customer's funds; if they gain a reputation for being untrustworthy then customers will move onto another competing bank. Also, banks are to comply with a mandatory external audit which is sent in to confirm the findings of the internal audit and to make sure everything is correct. The external auditors present an audit statement that is made public in the bank's annual report. Thus, it is better off for the bank to get their books straight the first time rather than being caught in the external audit.

The role of the internal auditor

The keys to an internal audit are independence, risk, and control. Independence from the rest of the bank is essential. This is because an auditor sometimes has to comment on unsatisfactory procedures. This may be compromised if conflict of interest situations arise. The risk is an internal auditor's starting point. It is important for auditors to focus their energy on contributing their efforts to the greatest risk in order to make an effort in remedying it. For a bank these will be areas where the loss of money or reputation is greatest. Control is an auditor's primary

objective ensuring that bank systems of internal control are adequate and are operating effectively. Proper controls can be costly, so, when assessing their sufficiency, the auditor needs to be careful not to recommend controls, the cost of which outweighs their benefit. An internal auditor must ensure that these categories are taken care of during the ongoing process of internal auditing.

The procedure for an internal audit

Internal audit is an independent function within a bank. They are conducted by the banks own audit departments to uncover bookkeeping errors, problems with controls and also to check the honesty of employees. In banking, internal auditing is an ongoing procedure. The auditors make sure that the bank has followed proper accounting procedures in its financial records and statements. They compare the current financial statements with those of the previous year to determine whether the statements are calculated consistently. If they are not, they present a distorted picture of the company's financial position. Assets and liabilities are checked to see if they have been skewed to the benefit of the bank.

The different types of auditing in banks

Financial Audits

Financial audits ensure that the risks involved in financial transactions or other procedures have adequate controls, and that the controls are working. As previously stated, controls are extremely important for an auditor to regulate properly. When examining the sufficiency of the controls, the auditor would be undertaking a *systems audit*. When testing the controls themselves, the auditor would be doing a *compliance audit*. If the auditor needed to verify the presence of physical financial assets, it would be a *custody audit*.

Computer Audits

Computer audits ensure that the bank's computers are properly controlled. An auditor must ask himself these questions: Are the physical controls over a computer site adequate? Are backups of data taken regularly? Are passwords changed frequently? When doing this work the auditor would be undertaking an *operational audit*. The computer applications themselves and the controls over them are usually the responsibility of the financial auditors since the applications form part of the business process. It is also important for auditors to become involved with any new computer system at the design stage, to ensure that proper controls are built in. This is a *development audit*.

Value-for-money Audits

These audits give management an opinion about the value for money that the bank gets from a particular process. It is not a review of the controls over risks in a system, and to this extent some internal auditors believe that efficiency audits should to be done by specialist internal or external management consultants.

Control self-assessment

Control self-assessment auditing is a form of auditing, but one which is done by the operational area on themselves, often with help from internal auditors. The aim of control self-assessment is for local management to give them a regular health check, to assess several risks in their area, finances, and controls. Control self-assessment should not be seen as a substitute for the independent audit function within a bank, but it should mean that when the auditors come to do their work, they will find a better control environment as a result of the self-assessment work done by local management.

Ethics and Accountability

The role of auditing in banking is perhaps the most important of any other entity that is to be audited. This is why ethics and accountability vital for success. Auditors are responsible for the accuracy of the financial statements and in the process must ensure that everything in the bank is following procedure. Steps are taken ensure that every little detail is taken care of and that nothing is overlooked. Audit committees in banks know that they are better off fixing any errors in financial statement before the errors become public in the external audits. Also, there are several rules and guidelines in place for internal auditors to stress the importance of accuracy in auditing. Bank create Audit Departments who not only perform the internal audit but also draw up its own set of standards to refer to when conducting their own audits. These standards are based on what they have learned from the more experienced external audits.

Conclusion

Internal audits in general are extremely important to a company's success and are vital in ensuring good consumer confidence. But when internal audits take place in banks the stakes are that much higher. Workers and businesses savings are being trusted to banks. If that line of trust were to be broken the bank would suffer great losses. This is why internal auditing in banking is so important and thus the focus of this report.

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** Thank you Lewis M.L. Cassar CA, MBA for your part in explaining key concepts related to the topic of this research assignment.

Note: Lewis is an expert in the field of accounting as well as banking with 30 years of work experience. Presently he controls the Toronto Internal Audit for States Street Bank and Trust.

