



## TEXAS DEPARTMENT OF BANKING

Bank Name/City:

Charter #:

Exam Date:

Performed By:

### #3 - Audit

## Assignment Overview

The development and use of an effective audit program is an essential component of every bank's internal control system. It assists the bank's board of directors in ensuring adequate administrative and accounting controls are in place for the size and complexity of the bank. Ideally, a bank should have a continuous program of internal audit (to promote a controlled environment and accurate operations), coupled with a well-planned external auditing program (to test and evaluate the high-risk areas of the bank). These functions are performed by an independent auditor who may or may not be a public accountant.

Refer to the following for additional guidance: [FDIC Risk Management Manual of Examination Policies, Section 4.2 Internal Routines and Controls](#) and DOB Reference Material for this procedure which identifies related regulations, guidance, and other issuances by various regulatory authorities.

## Instructions

**IMPORTANT!** These procedures are designed to promote critical thinking. Your comments should include what you looked at, what you found, and your conclusions. It is your narrative that should tell the story for a reader who may not be familiar with this bank. The reader/reviewer should have a thorough understanding of what was performed and conclusions made.

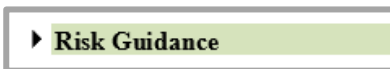
Examiners must follow the instructions below and the requirements in the Examiner Bulletin addressing Guidelines for Procedures and Work Paper Documentation for Commercial Examinations. **If there is a conflict between these Instructions and the Examiner Bulletin, the Instructions prevail.** Documentation should support weaknesses and criticisms. All examiners performing these procedures must be listed above in the "Prepared By" section.

***Examiners are responsible for exercising sound judgment and utilizing reasonable investigative and analytical skills to arrive at an accurate assessment of the risk profile of this segment of the institution's operations.***

## Evaluation Factors, Risk Guidance, and Comments

The focus of this procedure is to evaluate and address each of the Evaluation Factors. The Risk Guidance is provided to guide the examiner in developing a full and complete analysis for the Evaluation Factor. Documenting responses in the Risk Guidance section is not required. All conclusions should be documented in the Conclusion box for the Evaluation Factor. Examiners will use their discretion to determine when to comment on a risk guidance item, considering what data or findings merit emphasis and which are secondary or of little importance. The examiner is expected to write a comment in the Conclusions box that is complete and supportive of findings, recommendations, and ratings. Do not write a comment to refer to the Risk Guidance.

***The examiner may also address areas not included in the Risk Guidance section as it is not intended to be all inclusive.***



*To view the Risk Guidance, click on the arrow to the left of the “Risk Guidance” text.  
To Hide the Factors, click on the “arrow” again.*

## Documentation

Supporting documentation should include the standard required documents identified in the Reference Documents section for each Evaluation Factor.

- Embedded documents should be named such that the reviewer will know the contents.
- If a required document will not be included for any reason, DO NOT DELETE the document title, instead, check either :
  - “Not Included” and add a reason why OR
  - “N/A” if a document is not applicable”.
- Any other relevant documents may be added to fully support the examiner’s findings. These documents may be embedded in the Reference Documents section.
- If a document needs to be reference in more than one Evaluation Factor comment, include a reference in the comment indicating the Evaluation Factor where the document can be found.

Documentation is to be sufficient to allow an audit trail of the examiner’s thought process and all significant findings.

## Violations of Regulations

Violations of regulations should be addressed under the appropriate Evaluation Factor. Indicate compliance using the drop-down box next to the regulation in the Compliance section. Address non-compliance in the Comment section.

**Yes** = In compliance

**No** = Not in compliance

**Not Applicable** = Requirements in the regulation do not apply. For example, if there were no dividends paid, then the regulation related to approval of dividends would reflect “Not Applicable”.

### **Nonconformance with Policy**

Adherence with best practices identified in Department and federal financial regulatory policy/guidance should be addressed under the Comments for the appropriate Evaluation Factor. Indicate if the bank adheres to the best practices using the drop-down box next to the appropriate policy in the Adherence to Policy section. Comments regarding best practices should be summarized in the Summary Comments.

### **Summary Comments and Conclusions**

The Summary Comments and Conclusions should be a high-level summary that highlights the examiner’s material findings and conclusions. A description of what to include in the Summary Comments and Conclusions is provided. These comments are not intended to be a report ready comment and will contain comments that may not be report worthy. Summary comments must support the Summary Rating.

The EIC will determine if the use of bullet points is appropriate for completing the Summary Comments and Conclusions. *The SEIC/EIC will have discretion in determining what is included in the Report of Examination.*

### **Navigating this Procedure**

This procedure can be easily navigated by clicking on View from the Word menu bar then selecting Navigation Pane found in the Show section. All headings in this document will appear on the left side of the screen, for easy navigation through the document.

**Performing alternate or expanded procedures not listed with these guidelines may be necessary to complete this risk analysis.**

## Summary of Findings

### Audit Summary Comments and Conclusions

**Document conclusions regarding the adequacy of the bank's internal controls and internal and external audit function and overall audit program. Include recommendations for implementing best practices from policies and management responses to weaknesses. *The SEIC/EIC will determine what to include in the report of examination.***

**Summary Rating: [Click Here to Select Rating](#)**

### Violations

**Prepare a comment for any violation cited. Include management's corrective action.**

## Preliminary Review

Review the following items:

- Examination Scope Memo
- Prior examination audit comments
- Last State examination audit workpapers
- Audit risk assessment
- Audit plan and/or schedule
- Audit policy and Committee charter (if available)
- Engagement letters (internal and external audit)
- Internal audit reports
- External audit reports
- Audit workpapers
- Audit management letters (if applicable)
- Audit findings tracking matrix / mechanism for ensuring correction of findings
- Audit Committee minutes
- Actions taken by management to address audit and examination deficiencies

Provide applicable audit reports to examiners working the related areas for follow up on audit findings. Confer with examiners on status of previous audit findings.

Confer with EIC regarding following up on other prior audit findings not assigned to other examiners.

Consider the following **red flags** to assist in determining the breadth and depth of review:

1. Internal audit function lacks independence (performed by an internal employee without achieving full independence)
2. Internal audit performed by employee with limited knowledge and ability to adequately perform the function.
3. Inadequate/limited audit function
4. Internal controls are lacking
5. Evidence of lax user access security
6. Dominant authority figure is present
7. Concentration of related family members on the Board
8. No outside directors or not a reasonable number of outside directors
9. Insider abuse, Defalcation or Whistleblower tip
10. Questionable transactions with insiders or affiliates
11. Reliance on Directors Examination

*If a red flag is present, it may be necessary to dive deeper into the review of the audit function to test some of the controls in place. Consult with the EIC as necessary.*

## Audit Analysis

### EVALUATION FACTOR 1

**Review the last examination and correspondence to identify any recommendations, violations, Matters Requiring Attention, or regulatory enforcement actions. Determine Board and Management’s efforts to comply with or correct noted deficiencies or concerns.**

Reference Documents	Conclusions – Evaluation Factor 1
<p>Prior Examination Criticisms</p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p>Copy of management response/corrective action</p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p>Other Relevant Documents</p>	This area is intentionally left blank for user input

### EVALUATION FACTOR 2

**Evaluate the adequacy of the bank’s audit framework, including the Audit Policy, Risk Assessment, and the Audit Plan / Audit Schedule.**

## Risk Guidance

### 1. Assess the adequacy of the Audit policy and committee charter (if applicable).

- a. An Audit Policy should address the following:
  - i. Board approval.
  - ii. Management's reporting responsibilities to the Board or Audit Committee.
  - iii. Mechanism for justification of exceptions and Board pre-approval.
  - iv. Scope and frequency of audits.
  - v. Objective performance criteria to evaluate the internal and external audit function.

### 2. Assess the adequacy of the risk assessment. Consider the following.

- a. The audit risk assessment process is written and appropriate for the bank's size and risk profile.
- b. The audit risk assessment is updated annually or more frequently in accordance with the risk of the institution.
- c. The audit risk assessment considers all material risks of the institution.
- d. The audit frequency is commensurate with the risk.
- e. The methodology (how the risk is evaluated/quantified) is appropriate considering:
  - i. Inherent risk,
  - ii. Effectiveness of the internal control environment, and
  - iii. Residual risk.

### 3. Assess the adequacy of the audit plan/schedule. Consider the following.

- a. The audit plan/schedule is based on the risk assessment
- b. Audit plans and frequencies should be reasonable and completed as scheduled.

### 4. Determine if the internal audit plan is tailored to the bank's size and risks, and that the scope of its activities is adequate to evaluate the bank's system of internal controls. (Refer to [Appendix](#) for additional guidance.)

- a. Scope activities should look at internal controls assessment and testing.



Reference Documents	Conclusions – Evaluation Factor 2
<p data-bbox="205 289 352 318">Audit Policy</p> <p data-bbox="205 342 491 371"><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p data-bbox="205 440 411 469">Risk Assessment</p> <p data-bbox="205 493 491 522"><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p data-bbox="205 591 445 620">Audit Plan/Schedule</p> <p data-bbox="205 644 491 673"><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p data-bbox="205 742 407 800">Other Supporting Documents:</p>	

**EVALUATION FACTOR 3**  
**Determine the adequacy of the bank’s internal audit function, staff, and process.**

**Risk Guidance**

1. **Assess the competence and independence of internal audit staff, whether in-house or outsourced. Consider the following:**
  - a. Auditor and staff experience are appropriate,
  - b. Auditor and staff tenure, turnover, and vacancies are reasonable,
  - c. Conflicting duties performed by auditor or staff is not evident,
  - d. Lines of reporting, operational duties assigned to the auditor, or other restrictions or relationships is appropriate,

- e. Staff has the ability to meet audit schedule,
- f. Size of audit staff is reasonable, and
- g. Training frequency and level is appropriate, and
- h. Organizational chart shows segregation of audit department from operations and the segregation is practiced.

Refer to [Appendix](#) for additional guidance.

**2. Review a sample of internal audit reports and internal audit work papers and determine their adequacy by considering:**

- a. Appropriateness of audit coverage, given banks' risk profile and risk assessment.
- b. Adequacy and effectiveness of internal control assessments, including those for financial reporting.
- c. Appropriateness of audit reports.
- d. Appropriateness of audit workpapers in documenting work performed and supporting the audit report.
  - i. Quality of Internal Audit Workpapers should consider:
    - a) Are all audit findings identified in the audit workpapers included in the audit reports?
    - b) Do the audit workpapers adequately assess the controls and scope of the area being reviewed?
    - c) Is the sample size selected by the auditors sufficient to determine adequacy of controls?

**3. Determine if the Audit Function reviews/reconciles the Call Report.** If no, consider making a recommendation for the Audit Function to begin reviewing the Call Report.

**4. Discuss with other examiners working other procedures to determine if violations or nonconformance with policy statements are identified at this examination. If so:**

- a. Did the internal audit identify the concern in prior reports?
- b. If the internal audit did not identify the weakness, was it because it was not included in the scope or because it was not properly reviewed?
  - i. If yes, then consider a recommendation to expand the internal audit's depth of review or its scope.
- c. Did the audit find the weakness, but management has not properly corrected the finding?

- 5. Evaluate the adequacy of internal audit activities, including outsourced internal audit activities, by considering:**
- a. Content of audit plans.
  - b. Progress made toward completing annual audit plans or schedules.
  - c. Audit scope. Adjusts for significant changes in the bank’s environment, structure, activities, risk exposures, systems, or new products or services.
    - i. Refer to [Appendix](#) for scope considerations for various areas that require an independent review per joint agency or interagency policy statements (liquidity, sensitivity, ACL, and investments).
  - d. Reporting lines to the Board or audit committee.
  - e. Audit reports submitted to the Audit Committee timely.
  - f. Audit follows up on significant findings in a timely manner to assess effectiveness of management’s responses.
  - g.No indication that management has influence over the audit findings,
- 6. Review any internal audit outsourcing arrangement contracts or engagement letter to determine whether they adequately address the roles and responsibilities of the bank and the third party. Consider the policy statements on outsourcing, if applicable:**
- a. [Interagency Policy Statement on the Internal Audit Function and Its Outsourcing](#) (if applicable); and
  - b. [Supplemental Policy Statement on the Internal Audit Function and Its Outsourcing \(SR 13-01\)](#). (This guidance does not apply to community banking organizations, defined as institutions supervised by the Federal Reserve with total consolidated assets of \$10 billion or less.)
- 7. Determine what independence considerations are given when external auditors also provide internal audit services.**

<b>Adherence to Best Practices in Interagency Policy</b>	
<a href="#">Interagency Policy Statement on the Internal Audit Function and Its Outsourcing</a>	<b>Select Response</b>
<a href="#">Supplemental Policy Statement on the Internal Audit Function and Its Outsourcing (SR 13-01)</a> , if applicable	<b>Select Response</b>

Reference Documents	Conclusions - Evaluation Factor 3
<p>Organizational Chart</p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p>Internal audit engagement letters / outsourcing agreement</p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p>Internal Audit Reports</p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p>Other Supporting Documents:</p>	

**EVALUATION FACTOR 4**  
**Determine if the audit program appropriately evaluates the banks' internal controls.**

**Risk Guidance**

Based on information reviewed in the audit scope, audit reports and audit workpapers, consider the following:

1. Were any concerns or weaknesses identified with dual controls and segregation of duties?
  - a. Are user access levels appropriate and ensure that one person cannot dominate a transaction from inception to completion?

2. **Were internal controls adequately tested within the internal audit function?**
3. **Has the Board implemented an adequate vacation policy or rotation of duties?**
  - a. Policy ensures that employees in key sensitive positions are absent from their duties either through vacation or rotation of duties, and the Board accepts any necessary risk.
  - b. Refer to the FRB’s [SR 96-37 Supervisory Guidance on Required Absences from Sensitive Positions](#).
  - c. Refer to the FDIC’s [FIL-52-95 FDIC’s Position on the Role of Vacation Policy as an Important Internal Safeguard](#)
4. **Are proper controls in place for reports going to the Board for review?**
5. **Is there a process for internally reviewing employees’ checking and savings account statements?**

<b>Adherence to Best Practices in Interagency Policy</b>	
<a href="#">SR 96-37 Supervisory Guidance on Required Absences from Sensitive Positions</a>	<b>Select Response</b>
<a href="#">FIL-52-95 FDIC’s Position on the Role of Vacation Policy as an Important Internal Safeguard</a>	<b>Select Response</b>

<b>Reference Documents</b>	<b>Conclusions – Evaluation Factor 4</b>
<p><a href="#">User Access Information</a></p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p><a href="#">Other Supporting Documents</a></p>	

**EVALUATION FACTOR 5****Determine the adequacy of the bank's external audit program.**

Section 36 of the FDI Act, as implemented by [Part 363 of the FDIC Rules and Regulations](#), establishes annual independent audit and reporting requirements for insured depository institutions with total assets of \$500 million or more. The 1999 [Interagency Policy Statement on External Auditing Programs of Banks and Savings Associations](#) encourages banks and savings associations that have less than \$500 million in total assets and that are not subject to other audit requirements to adopt an external auditing program as a part of their overall risk management process.

**Provide the information below and update SAER/CENTS.**

<b>External Audit Firm (Name/City)</b>	
<b>Audit Manager</b>	
<b>Date of Last Audit</b>	
<b>Type of Audit:</b> 1 = Full Audit 2 = Director's Examination 3 = Other, please specify	

**The bank has the following type of external audit program(s) (Check appropriate box(s))**

- Financial statement audit by an independent public accountant.
- Reporting by an independent public accountant on the bank's internal control structure governing financial reporting.
- Integrated audit (a financial statement audit combined with an internal control audit) by an independent public accountant.

- Balance sheet audit performed by an independent public accountant.
- Agreed-upon procedures.
- The bank does not have an external audit program

**If a financial statement audit was performed, indicate type of opinion issued (check appropriate box):**

- Unmodified opinion
- Qualified opinion
- Adverse opinion
- Disclaimer
- Not Applicable – No Financial Statement Audit

**Risk Guidance**

**1. Determine whether the external audit program is:**

- a. Performed by an independent public accountant or other independent external party, and
- b. Appropriate given the bank’s size, nature, and extent of its activities and operations, and risk profile.

Consider the 1999 [Interagency Policy Statement on External Auditing Programs of Banks and Savings Associations](#) which encourages banks and savings associations that have less than \$500 million in total assets and that are not subject to other audit requirements to adopt an external auditing program as a part of their overall risk management process.

**2. Review the external audit engagement letter and assess its adequacy. Consider the following:**

- a. Purpose and scope of the audit

- b. Period of time to be covered by the audit
- c. Reports expected to be rendered
- d. Limitations placed on the auditor's scope or work
- e. Provides examiner access to audit workpapers

**3. Review the materiality calculation and adjusting entries received from the external auditor, if applicable.**

- a. Determine who is aware of the materiality threshold.
- b. Determine if the materiality threshold is reasonable. Consider the threshold in reference to the asset size of the institution.
- c. If management declined any of the adjusting entries suggested, was the reason documented and reasonable?
- d. Through discussion with management determine who is aware of the materiality threshold and the adjustments to the financial statements. Ensure individuals who have general ledger writing ability are not informed of the material threshold to avoid manipulation of results. If not, make a recommendation.

**4. If the bank does not have an external audit function, determine the board's rationale and mitigating factors. Consider the following:**

- a. Bank's size.
- b. Nature, scope, and complexity of bank activities.
- c. Bank's risk profile.
- d. Actions (taken or planned) to minimize or eliminate identified weaknesses.
- e. Extent of the bank's internal auditing program. Compensating internal controls in place.

**5. If applicable, determine that the external audit program conforms with [Part 363 of FDIC Rules and Regulations](#). ([12 CFR 363 Annual Independent Audits and Reporting Requirements](#))**

**Adherence to Best Practices in Interagency Policy**



<a href="#"><u>Interagency Policy Statement on External Auditing Programs of Banks and Savings Associations</u></a>	<b>Select Response</b>
<b>Compliance with Regulation</b>	
Part 363 of FDIC Rules and Regulations. ( <a href="#"><u>12 CFR 363</u></a> ) Annual Reporting Requirements ( <a href="#"><u>12 CFR 363.2</u></a> ), Independent Public Accountant ( <a href="#"><u>12 CFR 363.3</u></a> ) and Filing and Notice Requirements ( <a href="#"><u>12 CFR 363.4</u></a> )	<b>Select Response</b>

<b>Reference Documents</b>	<b>Conclusions - Evaluation Factor 5</b>
<p><a href="#"><u>External Engagement Letter</u></a></p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p><a href="#"><u>External Audit Reports</u></a></p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p><a href="#"><u>Financial Materiality Calculation</u></a></p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p><a href="#"><u>Other Supporting Documents:</u></a></p>	

**EVALUATION FACTOR 6**

**Determine the adequacy of Board and audit committee oversight of the bank's audit program, including the internal audit and external audit functions. Describe these actions.**

**Risk Guidance****1. Evaluate the effectiveness of the audit committee considering:**

- a. Composition, independence, diversity and breadth of industry experience.
  - i. Refer to [12 CFR 363.5](#)
  - ii. Institutions with \$500MM or more in total assets must establish an independent audit committee made up of outside directors who are independent of management.
- b. Adequacy of minutes maintained and supporting documentation,
- c. Approval of the internal and external audit programs, audit risk assessment, annual audit plan and schedule, and significant audit program or audit schedule changes,
- d. Frequency of meetings,
- e. Adherence to audit plan/schedule,
- f. Adequacy of audit reports submitted,
- g. Approval of internal and external audit reports,
- h. Timeliness of response to audit findings by management,
- i. Adequacy of follow-up procedures and tracking of findings to resolution,
- j. Adequacy of Audit Committee function considering the size and complexity of the institution, and
- k. Review and approval of any decision to forego any portion of the audit function, as applicable.

**2. Evaluate the bank's audit findings tracking system considering:**

- a. Inclusion of findings from all audit types and examinations,
- b. Inclusion of proposed corrective action,
- c. Assignment of responsibility for corrective action,

- d. Inclusion of completion/correction dates on the matrix,
- e. Timeliness of corrections,
- f. Ability to track deficiencies and corrections completed and include those in the reporting to the board for at least one reporting cycle,
- g. Review and discussion of the identification and resolution of audit findings by the Audit Committee or Board,
- h. Frequency of review by management, audit staff, and the Audit Committee, and
- i. Process to determine/verify closure of findings.

**3. Consider potential changes in the audit program such as:**

- a. Changes in how the Board / Audit Committee supervises audit activities.
- b. Any significant changes in business strategy or activities that could affect the audit functions (e.g., third-party relationships, products, services, delivery channels, market geographies).
- c. Any material changes in the audit program, scope, schedule, or staffing related to internal and external audit activities (e.g., external auditor, outsourcing or co-sourcing scope, and audit tools or audit systems).
- d. Any other internal or external factors that could affect the audit functions (e.g., audit projects or initiatives).

<b>Compliance with Regulation</b>	
<a href="#">Part 363 of FDIC Rules and Regulations (12 CFR 363.3)</a> Annual Independent Audits, if applicable	<b>Select Response</b>
<a href="#">Part 363 of FDIC Rules and Regulations (12 CFR 363.5)</a> Audit Committees	<b>Select Response</b>

<b>Reference Documents</b>	<b>Conclusions – Evaluation Factor 6</b>
<p><a href="#">List of Audit Committee Members</a></p> <p><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p>	

Reference Documents	Conclusions – Evaluation Factor 6
<p data-bbox="212 285 491 342">Audit Findings Tracking Matrix</p> <p data-bbox="212 370 491 394"><input type="checkbox"/> N/A   <input type="checkbox"/> Not Included</p> <p data-bbox="212 467 415 524">Other Supporting Documents:</p>	

**EVALUATION FACTOR 7**  
**Based on the review of the bank’s overall audit function, determine whether the bank complies with part 364 of the FDIC rules and regulations.**

**Risk Guidance**

Determine that the Safety and Soundness Standards, as set forth in [12 CFR 364 Appendix A](#) (FDIC) or [12 CFR 208 Regulation H, Appendix D-1](#) (FRB), for internal controls and internal audit systems are appropriate for the size of the bank and the nature, scope, and risk of its activities.

These standards for internal controls and internal audit systems include:

- a. An organization structure that establishes clear lines of authority and responsibility for monitoring adherence to prescribed policies.
- b. An effective risk assessment.
- c. Timely and accurate financial, operational, and regulatory reporting.
- d. Adequate procedures to safeguard and manage assets.
- e. Internal controls that provide for compliance with applicable laws and regulations.
- f. Monitoring of internal controls through an internal audit function or independent review.

- g. An internal audit system that provides for qualified, independent objective persons.
- h. Adequate testing and review of information systems supported by documentation of tests, findings, and corrective actions.
- i. Verification and review of management actions to address material weaknesses.
- j. Review by the audit committee or Board of the effectiveness of the internal audit system.

<b>Compliance with Regulation</b>	
<a href="#">Appendix A of Part 364 / 12 CFR 208 Appendix D-1</a>	<b>Select Response</b>

<b>Reference Documents</b>	<b>Conclusions -Evaluation Factor 7</b> <i>(Comment only if non-compliance noted)</i>

## APPENDIX

### Internal Audit Program

#### **The internal audit program should:**

- Be in written form.
- Be approved by the Board of Directors or Audit Committee, including any changes to the audit schedule.
- Identify the scope of the program, which is based on the recent control risk assessment of the bank's significant business activities.
- Use varied starting dates and time intervals between audits to avoid anticipation by those subject to audit.

#### **The Scope and Workpapers for internal audits should include:**

- Prior audit findings and correction
- Verification that policies and procedures have been developed
- That policies and activities comply with regulations
- Walk-through of activity, documentation of how they tested the policies/procedures
- Transaction testing

**Adequate work papers should be maintained that document work performance and support audit reports.**

**The program should include audits of the following. The frequency should be consistent with the nature, complexity, and risk of the institution's balance sheet and off-balance sheet activities:**

- Cash Accounts
- Due From Banks
- Investments
- Loans
- Allowance for Credit Losses
- Bank Premises and Equipment
- Other Assets
- Deposits

- Borrowed Funds
- Other Liabilities
- Capital Accounts and Dividends
- Consigned Items and Other Non-Ledger Control Accounts
- Income and Expense
- Wire Transfer and Electronic Funds Transfer Activities
- Electronic Banking Activities
- In-house IT processing
- Branches

**Audit plans and frequencies should be reasonable and completed as scheduled.**

**Personnel performing internal audit should:**

- Have adequate expertise
- Be independent and objective
- Report directly to the board or committee
- Have complete control over reports submitted
- Receive ongoing training initiatives which are enough for the size and complexity of the bank.

## Outsourcing Internal Audits

Outsourcing arrangements involve contracts between an institution and a vendor that provides internal audit services. The arrangements may involve vendors providing limited or extensive audit assistance. Regardless of the level of outsourced services, an institution's directors are responsible for establishing and maintaining effective internal controls and internal audit programs. Their responsibility *cannot* be delegated to others within the institution or to outside parties.

Management should exercise appropriate due diligence in selecting vendors and periodically review outsourcing arrangements and vendor performance thereafter.

**If outsourced, the agreement should include the items detailed in the [Interagency Policy Statement on the Internal Audit Function and Its Outsourcing](#).** This policy sets forth key characteristics of the internal audit function in Part I. Sound practices concerning the use of outsourcing vendors are discussed in Part II. Part III discusses the effect outsourcing arrangements have on the independence of an external auditor who also provides internal audit services to an institution. Part III also discusses the prohibition on internal audit outsourcing to a public company's external auditor under the Sarbanes-Oxley Act of 2002, the effect of this prohibition on insured depository institutions subject to the annual audit and reporting

requirements of Section 36 of the FDI Act (12 U.S.C. 1831m), and the agencies' views on compliance with this provision of the Sarbanes-Oxley Act by institutions not subject to Section 36 (including smaller depository institutions) that are not publicly-held. Finally, Part IV of this statement provides guidance to examiners concerning their reviews of internal audit functions and related matters.

➤ [Return to Risk Guidance for Eval Factor 5](#)