

AAA Summer 2020 Answer Plan:

MEMO (NB)

Summary based on the Indicators

Indicator 1 – Ethics:

Self Interest Threat – Check the ES Section and para

- Jeff Hayes (JH) the audit lead partner –
 - ES 5 years rotation
 - 6th year PIE
 - Safeguard = rotation
 - As GGB is a PIE no exceptions
 - Cooling off period?
- EQCR
 - 8th year
 - Rotation after 7 years
 - Cooling off period
- Manager
 - A covered person
 - Self interest and intimidation threats
 - Bank loan is an exception once
 - Safeguard – Bring to attention of JH and Ethics Partner
- Non Audit services (Payroll services and recruitment of new Head of Finance)
 - ES 5 – For PIE specifically prohibited
 - Check references

Indicator 2 –Highlight any issues noted with the controls in place so that we can report to management and those charged with governance.

- Ref ISA 265
- Structure in ISA 265
- *(note: Likely to be a bit of copying and pasting from this table to the solution. Since the exam has become a CBE I have found myself typing up the full answer for this type of question here and then copying and pasting into the memo)*

Weakness	Implications/risk	recommendation
The online portal does not have the functionality to certify the form of identification supplied. They must call into a branch to complete before any drawdown of funds	The process could begin without appropriate due diligence steps being followed	Application process should not be allowed progress until customer is identified. Functionality should be invested in to validate identification at the initial stage of the application process
Loan application forms are not allocated numbers sequentially	Could result in difficulties in following a loan through the	Application form numbers should be allocated in sequence by Sharp (The bank lending system)

	different stages of the application process	
Credit worthiness can be checked on applications where a form of ID is outstanding		As number 1 above the application process should not be allowed progress until the customer is identified Functionality should be invested in to validate identification at the initial stage of the application process
Where the application is being made by an existing customer (top-ups and renewals) the system does not reperform the credit worthiness check	Not reperforming the credit worthiness check could open the bank to significant financial loss. Increases the risk of fraudulent activity.	A credit worthiness check should be carried out on all loan applications be they new or existing customers
There are 2 senior credit team members (Dave North and Max Payne) who have the ability to manually change the in-built interest rates	Incorrect interest rates may be charged resulting in the bank over or undercharging their customers. Rates can be manipulated by Dave North and Max Payne which increases the risk of fraudulent activity.	Any changes to interest rates should be authorised by the Marie Ryan (Head of credit team). There should be a process in place before the changes can be made.
The EURIBOR rate has not been updated in over 2 years	Incorrect interest rates may be charged resulting in the bank over or undercharging their customers. Significant risk to the bank as 70% of the bank's loan portfolio is linked to EURIBOR. Increases the risk of fraudulent activity.	There should be a more detailed process in place where clear evidence is available and signed by Marie Ryan showing that this rate has not changed. This review should be conducted on a regular basis.
A Loan application can be automatically pre-approved by Sharp if it meets specific system generated limits. A Credit Team member can re-route the application back to the initial loan advisor as 'approved' with no further review necessary.	Errors made by the initial loan advisor made be overlooked if the credit application is not reviewed in further detail. Increases the risk of fraudulent activity.	As is the requirement with other loan applications, these loan applications should reviewed in detail by the Credit Team member
The bank has a relatively small credit team.	A small team increase the risks of error and fraud. In	A recruitment process should be commenced to hire additional

	<p>particular there will not be adequate segregation of duties.</p> <p>Increases the risk of fraudulent activity.</p>	<p>Credit Team members with appropriate qualifications and experience.</p>
<p>Changes to assigned level of credit authority delegated to credit team members can be changed on an ad-hoc basis by Dave Martin and Max Payne.</p>	<p>Exposes the bank to fraudulent activity and errors as the controls in place over credit authority limits can be by passed.</p>	<p>A process should be implemented which must be strictly followed before credit authority limits can be changed. For example Marie Ryan's approval should be required as part of the process.</p> <p>Remove the current authority to changes authority limits by Dave Martin and Max Payne</p>
<p>Only significant changes (defined as >€100,000) require approval by Marie Ryan and the Credit Committee</p>	<p>Exposes the bank to significant risk of fraud especially when linked to the immediately preceding weakness</p>	<p>A process should be implemented which must be strictly followed before credit authority limits can be changed. For example Marie Ryan's approval should be required as part of the process</p> <p>The Credit Committee should also be included in this approval process.</p>
<p>The level of credit authority are formally communicated to each credit team member however are not included within Sharp</p>	<p>An individual credit team member could exceed his/her credit authority either in error or as part of a fraudulent activity. This exposes the bank to additional risk</p>	<p>The level of credit authority delegated to each credit team member should be built into Sharp. As part of the process Sharp should check that individuals are not exceeding their authority limits</p>
<p>The Credit Committee last reviewed the designated level of credit authority in 2017, it is now August 2020.</p>	<p>Risk that the designated levels of credit authority are not appropriate. Some inappropriate loans may be approved increasing the risk of loan write offs by the bank.</p>	<p>A process should be put in place to ensure there is a review of the designated levels of credit authority at least annually. The Credit Committee show play a key role in this process.</p>

Indicator 3 - Review the system note documentation in the 'loan origination and approval process' as prepared by the audit junior and outline any concerns with the process, the risks arising or implications and finally if and what we should communicate with management or those charged with governance in this respect.

The relevant technical document is ISA 240 (Fraud) also ISA 200 deals with professional scepticism.

Indicators of fraud

- Significant internal control deficiencies identified earlier in the memo. Also note the point below from the audit planning meeting.
- Small team resulting in lack of segregation of duty.
- EURIBOR 3 months
 - has not been updated in over 2 years
 - Dave North giving a confirmation of this
 - Note the point below on excessive management bonuses and customer complaints
 - Deliberately being overstated?
- Level of credit authority
 - DN and MP (Dave North and Max Payne) can change their own limits
 - Limited involvement in setting limits by either Credit Committee (CC) or Marie Ryan (MR)
 - Only changes of >€100,000 require authorisation by MR or CC
- No credit worthiness tests on top-ups and renewals.

Also note: from conversation with Jeff:

- The bank has been struggling to maintain the minimum required capital adequacy levels mandated by the regulator.
- The bank has been subjected to a lot of public scrutiny recently due to
 - some news coverage on executive management bonuses and
 - Customer complaints on excessively high interest rates being charged in comparison with other lenders.

Note from the audit planning meeting:

- For such a heavily regulated bank, Green-Gate are still weak in terms of control environment

In response to the high level of risk of fraud we should consider the following, make reference to ISA 240 (relevant paragraph if available) – NB Don't requote the points in the ISA.

Investigations Of Possible Misstatements

When auditors become aware of information which indicates that fraud or error may exist, they should obtain an understanding of the nature of the event and the circumstances in which it has occurred, and sufficient other information to evaluate the possible effect on the financial statements. If the auditors believe that the indicated fraud or error could have a material effect on the financial statements, they should perform appropriate modified or additional procedures.

We need to ensure that the bank and in particular the credit team members are not aware of our suspicion.

Indicator 4: Green Gate will be publishing quarterly financial information on its website commencing 1 September 2020. The audit partner would like to know if we can provide a sign off and to outline the nature of the work to be undertaken and what type of report we could provide in this instance.

Firstly ensure there are no ES 5 issues, especially as the client is a PIE

The key step is to identify the relevant standard- this is one of the more straight forward scenarios as it should be clear that ISRE 2410 'Review of Interim Financial Information performed by the Independent Auditor of the Entity'

Sign Off: This is a reasonable assurance engagement therefore a negative opinion will be expressed