

SPEAKING THE SAME LANGUAGE

by [Steve Brown](#)

You might not always think about it, but the 10 most commonly used words in the English language according to experts are: the, of, to, and, a, in, is, it, you & that. So, the thing we would say this morning is "If it is in you or us to think about that as you drink a cup of coffee and eat a muffin this morning - enjoy!" Ok, it isn't that easy to get them all into a single sentence perhaps, but you get the gist. Speaking of speech about this and that, we pick up again on the internal audit discussion of yesterday to add a few more components you might like to know. As indicated in the same report from the BIS we discussed yesterday, regulators expect internal audit teams (whether actually internal or hired to do the function) to be fully prepared before any process begins. In general, the internal audit team is expected to have "an independent and informed view of the risks faced by the bank." That is a lot to prepare for, but it points out how important this function is in the overall scheme of things. Regulators also expect banks to make sure audits are based on not only files and records; but also a deeper dive into data, a process of inquiry and a professional approach. Once audit teams have completed their review, regulators expect them to "discuss their views, findings and conclusions directly with the audit committee and the board of directors." This makes sure the integrity of the process is maintained, removes undue management influence and while it can sometimes put management and staff on edge, it is designed to serve and protect the bank. Such processes are common in banking. As audits unfold, teams will commonly seek answers to questions that surface from their discussions with staff or management. To ensure accuracy, anything of note that surfaces should be double-checked again to make sure nothing is misunderstood. This is the time when management or staff has an opportunity to respond or clarify things. All of this back and forth process is then incorporated and final results are provided to the audit committee of the board. Auditing is important and to make sure the process is thorough, fair and effective; it is also critical to make certain the function is independent of the audited activities. That sounds like common sense, but when expertise resides in one area and a community bank doesn't have extra people to throw around, it can be more complex than it seems at first blush. Community banks just don't have teams of experts lying around that are unused, so care must be taken to ensure the audit process is followed. In a community bank stretched for resources, it seems to make sense that the internal audit function should be able to design and implement processes to correct findings, but this should be avoided. There are simply too many potential conflicts that can arise, so the audit function must remain independent of operational management. Questions and discussion are common and helpful, but the audit team should not be directly involved in the development or implementation of internal controls. Finally, it is important to train your audit staff to keep them at the top of their game. Understanding where risks are coming from is important, but equally important is making sure the auditor has the understanding and training to handle the bank's situation. Here the report indicates auditors should have the "ability to collect and understand information, to examine and evaluate audit evidence and to communicate with stakeholders of the internal audit function." It makes sense to not only boost training for audit teams, but to share knowledge gained throughout the bank that is obtained as a result of the audit process. Doing so will help your bank maintain best practices, as risk management is further enhanced. No matter how you speak or what words you select, as a banker you intuitively know the internal audit function is important to the proper operation and risk management of the bank.

BANK NEWS

ATM Changes

In a theme that may spread across the country, a start up is working with New York to bring it fees on ATM machines. The program waives user fees in return for having to watch a 15 second advertisement.

Foreclosure Rentals

Large private equity players are behind Waypoint Real Estate Group LLC and Colony American Homes, both of which are actively buying up thousands of foreclosed homes and then renting them out. Waypoint already owns 2,200 homes so far (on its way to a goal of 11,000) and Colony has 3,600 homes (going to 10,000).

CFPB

The CFPB has formed a Community Bank Advisory Council that will provide the agency with feedback on policy development, research and rulemaking. The Council will hold its first public meeting on Oct. 10.

Spending Cuts

To stabilize the debt to GDP ratio at 78% in 2013, the U.S. government would have to cut spending by about \$1.8T, or about 1% of GDP. As this is unlikely to occur, look for Moody's to cut the U.S. credit rating in coming months.

Prison Time

A PA court has sentenced Joseph Braas and Michael Schlager to 15Ys and 20Ys in prison, respectively, for running a 5Y fraud as loan officers at Equipment Finance LLC. Both pled guilty to the charges.

Fraud

Russell Wasendorf, the former CEO of Peregrine Financial, plead guilty to embezzling more than \$100mm from customers of his futures brokerage over a 20Y period. He also plead guilty of lying to regulators and mail fraud.

Cornered Market

The FOMC's plans to buy \$40B of agency MBS each month and the \$25B or so it is already reinvesting monthly, means the Fed will control 55% of total monthly agency MBS supply.

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