FDIC
FEDERAL DEPOSIT INSURANCE CORPORATION

NEWS RELEASE

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# FDIC CHAIRMAN STRESSES IMPORTANCE OF INTERNAL AUDITORS IN FRAUD DETECTION

"Internal auditors represent the front line of defense against fraud, insider abuse and unwise financial practices within the nation's corporations," FDIC Chairman L. William Seidman today told practitioners attending the 45th Annual Conference of the Institute of Internal Auditors. Mr. Seidman cited three elements the FDIC looks for in a bank's internal audit department: independence, competence and management support.

"Independence is critically important. Auditors need the power to delve into all of the bank's affairs, including those of the bank management. Without this independence the internal auditor will lack effectiveness and be of little or no real value to the bank," the FDIC Chairman told the group meeting in New York City.

Stressing the need for management support, he said: "Senior management must demonstrate, by the nature of its relationship with the internal auditors, that they are key players in the organization."

Turning to the role of outside auditors, Mr. Seidman said their most important role is confirming the strength of control systems, both internal controls and management controls. He said both internal and external auditors should watch for fraud and insider abuse when conducting bank audits, and he provided the auditors with a sampling of a new fraud and insider abuse "red flag" system now being developed by the FDIC's examination staff.

An independent bank audit "should provide assurance to the board of directors that they are well informed about the condition of the bank, that

-morethe management is complying with their policies, and that internal controls are strong," Mr. Seidman said.

"All told, fraud and insider abuse contributed to over 40 percent of bank failures between 1980 and 1983," Mr. Seidman said. He stressed that good communications between regulators and auditors can improve the performance of both groups. He noted, "I have suggested that when CPAs resign from an audit engagement because they have discovered insider abuse or fraud and the management does not take appropriate action, that it would be desirable for the CPA to inform the appropriate regulator." He emphasized that, "I have not suggested that there be any communication of this nature until the CPA is no longer engaged by the client, except with the permission of the client."

He concluded by saying that "the courts, the Congress and the people expect us as auditors, whether for the government or the private sector, to be looking for fraud and insider abuse. We should make it a high priority part of each examination. We may not always find these abuses, because clever people are good at hiding them, but we should always try to search them out."

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