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I. PURPOSE


Examiners must be alert for indicators of fraud and take appropriate measures. Examiners must ensure adequate internal controls exist to deter and detect fraud and/or insider abuse, and that the credit union has procedures in place to take appropriate action if fraud and/or insider abuse is detected.

II. PRIMARY REFERENCES


1. Michigan Credit Union Act:
 - a. [Section 212](#): Notice of intention for removal or prohibition
 - b. [Section 214](#): Person charged with felony involving dishonesty or breach of trust
 - c. [Section 344](#): Audits
 - d. [Section 382](#): Fiscal year; accounting principles
 - e. [Section 383](#): Discharge of duties by officers; standards; indemnification
2. [Statement on Auditing Standards No. 99 \(SAS 99\)](#): Consideration of Fraud in a Financial Statement Audit

III. MINIMUM PROCEDURES

1. Review the adequacy of the policies and procedures with respect to conflicts of interest and sound internal controls.
2. Determine if the Board of Directors has developed a policy that specifically addresses fraud; this policy should address specific actions to be carried out by management and/or officials if fraud is discovered and ensure fair and consistent treatment of employees.
3. Determine if warning signals exist that may require additional examination procedures.
4. Review system-generated file maintenance reports for transactions that appear irregular; this includes changing loan due dates, changes to payment amounts or interest due, and reversal of fees or payments.
 - a. Trace items back to the source documents in the loan files, to verify they were accurate, legitimate and duly authorized.

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- b. Ensure staff is not performing file maintenance on their own accounts and/or related accounts.
 - c. Ensure internal controls are in place providing for regular and independent review of file maintenance reports.
- 5. Review the share and loan trial balance report for unusual balances, interest rates, payment amounts, due dates, account numbers, accrued interest, etc., and include several of these types of loans in the selected loan review.
- 6. Review insider transactions including both loan and share account histories. Extend review to related accounts if deemed appropriate.
- 7. Review adequacy of verification of member accounts, including internal controls over printing and mailing of statements (particularly control and review of “do not mail” accounts and returned items).
- 8. Review Cash and Bank Reconciliations
 - a. Perform a thorough review of cash controls, particularly in operations when there is limited staff and/or when overall internal controls appear weak.
 - b. Review several month’s bank and corporate reconciliations.
 - c. Trace deposits in transit to validated deposit slips and the following month’s statement.
 - d. Verify reconciling items to source documents.
 - e. Scan through checks for unusual items such as possible personal expense items, unauthorized signatures, abnormal amounts, etc.
 - f. Assess reasonableness of cash balances.
 - 1. The typical cash balance for credit unions is between 2 to 5 percent of assets. Significant deviations should be evaluated for reasonableness.
 - 2. Large fluctuations in balances, excessive deposit or withdrawal transactions, reconciling items carried forward for more than one month, and any other unusual activity should be thoroughly investigated.
- 9. Assess reasonableness of cost of funds, dividends payable, yield on assets, accrued incomes and growth rates.
- 10. Review daily and month-end overdraft reports to determine if abuse, such as repeated overdrafts and inappropriate fee reversals, is evident; special attention is warranted for insider accounts.
- 11. Review internal controls for EDP issues, when in-house systems are utilized.

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IV. PROCEDURES UPON DISCOVERY OF FRAUD OR INSIDER ABUSE

If examiners determine with reasonable certainty that fraud and/or insider abuse exists, it should be immediately discussed with the Regional Supervisor to determine the best course of action. After concurrence from the Regional Supervisor, the following should occur:

1. Ensure all evidence of fraud and/or insider abuse is well documented and maintained with the examination work papers. Examiners should maintain “clean copies” of documentation whenever practical (i.e. documentation in original form, without writing or other marks).
2. Contact the appropriate credit union officials and management to arrange a meeting to present evidence that indicates the fraud and/or insider abuse.
3. Ensure officials and/or management take appropriate actions to ensure the protection of credit union assets; this includes:
 - a. Suspension or termination of the employee(s), as appropriate.
 - b. Updating records and performing (or cause to be performed) an audit. In some cases, it may be appropriate to use a qualified independent fraud auditor.
 - c. Removing all access to credit union assets from the alleged perpetrator, such as:
 - i. Changing combinations and/or locks.
 - ii. Changing access and passwords to all electronic systems.
 - iii. Changing signatures at banks or other institutions.
 - iv. Revoking investment authority.
4. Discuss with officials and/or management the necessity of the filing of a bond claim, including contacting surety in a timely manner and complying with the bond requirements.
5. Ensure the officials and management notify FinCEN by completing and submitting a Suspicious Activity Report (SAR), and contact local law enforcement as appropriate.
6. Evaluate the necessity of further regulatory action. If deemed appropriate, examiners should submit a staff recommendation to the Director for prohibition and/or removal as outlined in [Section 212](#) of the MCUA.