# AC report digitization

10 October 2024

# Agenda

- ➢ Executive summary
- ➢ Summary Statistics
- ➢ Summary of Issue findings
- ➢ Probable Risk Summary
- ➢ Issue root cause summary
- ➢ Summary of issue statistics, issue findings, root cause explanation, probable risk - Overall

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# Executive summary
## Key insights – Qualitative and Quantitative

➢ A total of 4 internal audits were performed.

➢ The reports belong to quarter 1 of 2024.

➢ The total number of issues identified were 34, with 4 being high risk, 12 being medium risk and the remaining 18 being low risk. Some issues were noted across multiple Review areas, resulting in a total of 10 unique high and medium rated risk issues: 2 high risk and 8 medium risk issues.

➢ The top 3 Review Areas with highest number of high and medium risk issues are Branch Review with 1 high and 4 medium risk issues, Wholesale LOB (Large Corporate and Mid Market segment) with 1 high and 3 medium risk issues, Wholesale LOB (Construction Finance Segent) with 1 high and 3 medium risk issues.

➢ The top Probable Risk categories with the highest overall issue counts are 'Operational' with 4 high-risk and 5 medium-risk issues, and 'Compliance' with 12 medium-risk issues. However, some issues are common across multiple review areas, resulting in a unique count of 2 high-risk and 4 medium-risk issues for 'Operational Risk,' and 4 medium-risk issues for 'Compliance Risk.'

    ➢ Operational Risk:

    High Rated Issues:

    The two high-risk operational issues identified pertain to inadequate oversight and control systems. Firstly, there's a significant gap in documentation and approvals for changes to product notes as required by the Product Working Group Charter. Secondly, there's a serious risk of data breaches due to unattended sensitive customer documents across various branches, indicating poor handling and storage of confidential information.

    Medium Rated Issues:

    The four medium-risk operational issues identified involve breaches of information security, non-compliance with established processes, non-compliance with regulatory requirements, and inadequate physical security. There have been instances of password sharing among relationship officers, compromising system integrity. Additionally, there has been a deviation from the Interest Service Reserve (ISRA) requirement for a loan, demonstrating procedural non-compliance. Furthermore, branches are failing to display notices and certificates as per RBI guidelines, indicating regulatory non-compliance. Lastly, physical security controls at branches are insufficient, compromising incident investigation capabilities.

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# Executive summary Contd…
## Key insights – Qualitative and Quantitative

- Compliance Risk:

    High Rated Issues: No high rated issues

    Medium Rated Issues:

    The four medium-risk compliance issues involve lapses in Know Your Customer (KYC) protocols, lack of policy for identifying non-cooperative borrowers, failure to verify non-profit organization customers' registration on the DARPAN Portal, and inadequate adherence to regulatory requirements. There is non-compliance with the RBI's Re-KYC mandate for co-borrowers and a lack of risk categorization for them in the Loan Management System (LMS). Additionally, the absence of a defined policy for reporting non-cooperative borrowers, as required by RBI, creates ambiguity and potential non-compliance. The organization also fails to ensure its non-profit customers are registered on the DARPAN Portal, risking regulatory penalties. Lastly, branches are not displaying various notices and certificates as per RBI guidelines, indicating potential fines or penalties.

- The top root cause categories are Lack of Documentation with 3 high and 3 medium risk issues and Process Non-adherence with 1 high and 5 medium risk issues.

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# Summary Statistics
## Basic high-level statistics based on the underlying audit reports

1. **Number of underlying internal audit reports**: 4

2. **Total Issues identified**: The total number of issues identified are 34.
   1. High-rated issues: 4
   2. Medium-rated issues: 12
   3. Low-rated issues: 18
   Some issues were noted across multiple Review areas, resulting in a total of 10 unique high and medium rated risk issues: 2 high risk and 8 medium risk issues.

3. **Review Area Level:** The Review Areas with highest number of high and medium risk issues is Branch Review with 1 high and 4 medium risk issues.

4. **Probable Risk Level**: The top Probable risks are 'Operational Risk' (2 high and 4 medium risk issues), 'Compliance Risk' (4 medium risk issues).

5. **Root Cause** : The top root cause categories are Lack of Documentation with 3 high and 3 medium risk issues and Process Non-adherence with 1 high and 5 medium risk issues.

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# Summary of Issue findings (1/3)
## Summary of issue findings for top 3 Review Areas for high and medium rated issues

- The count of high and medium risk issues under each unique review area is as follows:
  - Branch Review: 5
  - Wholesale LOB (Large Corporate and Mid Market segment): 4
  - Wholesale LOB (Construction Finance Segment): 4

- The issue findings for the identified high and medium risk issues are:

❑ Branch Review
Total High-Risk Issues: 1
Total Medium-Risk Issues: 4

High-Risk Issue:
  ‣ Inadequate Control Over Handling and Storage of Customers' Confidential Documents: Sensitive documents were found unattended in various branches, indicating a severe lapse in security protocols. This situation poses a risk of data breaches and loss of confidential information.

Medium-Risk Issues:

  ‣ Sharing of User ID and Password by Relationship Officers: Instances of password sharing among relationship officers were observed, violating information security policies. This practice increases the risk of data breaches and compromises the integrity of organizational systems.

  ‣ Inadequacies in Compliance with Regulatory Requirements: Various notices and certificates mandated by RBI guidelines were not displayed at branches, indicating a lack of adherence to statutory requirements.

  ‣ Inadequate Physical Security Controls at Branches: Deficiencies in physical security controls were noted, including missing CCTV recordings and inadequate monitoring, compromising the ability to effectively monitor and investigate incidents.

  ‣ Exceptions in compliance with information security (IS) policy: The review of Information Security (IS) policy adherence at branches revealed two instances where personal Google applications were accessible on company laptops/desktops, and 20 instances where the streaming website YouTube was functioning on user's devices. This behaviour contravenes established IS policies, exposing the organization to potential data breaches and related risks.

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# Summary of Issue findings (2/3)
## Summary of issue findings for top 3 Review Areas for high and medium rated issues contd...

❑   **Wholesale LOB (Large Corporate and Mid-Market segment)**

Total High-Risk Issues: 1
Total Medium-Risk Issues: 3

High-Risk Issue:

- ▸   Approval of Product Note: There was no evidence of approvals and formal email sign-offs for product notes as required by the Product Working Group Charter. This lack of documentation creates an absence of an audit trail, which is critical for accountability.

Medium-Risk Issues:

- ▸   Re-KYC of Co-Borrowers: Periodic Re-KYC was not conducted for co-borrowers, violating RBI regulations. The LMS system also fails to capture the risk categorization for co-borrowers, leading to potential non-compliance.

- ▸   Non-Cooperative Borrowers: There is no defined policy for identifying and reporting non-cooperative borrowers, which creates ambiguity in compliance. This lack of documentation may hinder regulatory compliance efforts.

- ▸   Registration on NITI Aayog Darpan Portal: The organization has not established a process to verify that non-profit organization customers are registered on the DARPAN Portal, as required by RBI regulations. This oversight could lead to non-compliance and regulatory penalties.

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# Summary of Issue findings (3/3)
## Summary of issue findings for top 3 Review Areas for high and medium rated issues contd…

❑ **Wholesale LOB (Construction Finance Segment)**

       Total High-Risk Issues: 1

       Total Medium-Risk Issues: 3

High-Risk Issue:

▸ Approval for Product Notes: Similar to the previous area, there was no evidence of approvals and formal email sign-offs for product notes. This indicates a significant gap in documentation and oversight, leading to a lack of audit trails.

Medium-Risk Issues:

▸ Re-KYC of Co-Borrowers: Periodic Re-KYC is not conducted for co-borrowers as mandated by RBI regulations. The LMS does not capture the risk categorization for co-borrowers, leading to potential non-compliance.

▸ Deviation for Interest Service Reserve: An instance was noted where the required Interest Service Reserve was not obtained from a borrower, and no approval was secured for this deviation, indicating a failure to adhere to established processes.

▸ Non-Cooperative Borrowers: There is currently no defined policy for identifying and reporting non-cooperative borrowers, which creates a compliance risk.

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# Probable Risk Summary
## Top probable risks identified with their summary of issues and root cause explanations

**Operational Risk**

High Rated Issues
* Observation: The audit identified significant deficiencies in the approval process for product notes. The Product Working Group Charter mandates that all members review and sign off on any variations to existing products. However, there was no evidence of approvals or formal email signoffs from the product approval committee for the current versions of the Product notes dated October/November 2023. Additionally, there was inadequate control over the handling and storage of customers' confidential documents, with sensitive materials found unsecured across various branches.
* Root Cause Explanation: The lack of a centralized repository and formal email signoff processes contributed to the absence of documentation for product approvals. Furthermore, there was a general lack of awareness and discipline regarding the handling of sensitive customer documents, leading to potential misplacement or loss.

Medium Rated Issues
* Deviations from the Construction Finance product note regarding the Interest Service Reserve (ISRA) were noted, where ISRA was not taken for one loan without requisite approval. Sharing of user IDs and passwords by relationship officers was observed, which is non-compliance with the code of conduct and information security policy. Additionally, exceptions in compliance with information security policy were noted, with unauthorized access to personal and streaming websites on company devices, and inadequate physical security controls at branches were identified.
* Root Cause Explanation: The deviations were due to operational miss-outs and process non-adherence. Staff were not sensitized to the implications of password sharing, leading to potential data breaches. There were also system deficiencies that prevented compliance with regulatory requirements, and a lack of communication regarding security issues contributed to inadequate physical security controls.

**Compliance Risk**

Medium Rated Issues
* Observation: The medium-rated issues under compliance risk include Re-KYC of co-borrowers, where periodic Re-KYC is not conducted as per RBI guidelines, leading to potential regulatory non-compliance. Additionally, the Non-Co-operative Borrowers issue highlights the absence of a defined policy for identifying and reporting non-cooperative borrowers, which may create ambiguity and hinder compliance with regulatory requirements. Other issues include Registration on NITI Aayog Darpan Portal, where the process for verifying registration of non-profit organizations was not established, and Inadequacies in compliance with respect to regulatory and statutory requirements, where branches failed to display required notices and certificates.
* Root Cause Explanation: The root causes for these issues stem from system deficiencies that prevent the execution of required Re-KYC processes, the absence of a formal policy for identifying non-cooperative borrowers, and a lack of established procedures for verifying DARPAN registration. Additionally, there is a lack of awareness and process non-adherence regarding the display of statutory requirements at branches, contributing to regulatory non-compliance.

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# Issue root cause summary
## Summary of issue root cause explanations for high and medium rated issues across review areas

**Total High & Medium Rated Issues: 10**

‣ **High-Rated Issues**: 2 unique issues identified.
‣ **Medium-Rated Issues**: 8 unique issues identified

Summary of Issue Observations Under each Root Cause

**Absence of Process**
**Medium Rated Issues:** The absence of a defined policy for identifying and reporting non-cooperative borrowers creates ambiguity in compliance with regulatory requirements. Additionally, there is no established process to verify the registration of non-profit organizations on the DARPAN portal, which may lead to non-compliance with RBI regulations.

**Lack of Documentation**
**High Rated Issues:** There was no evidence of approvals and formal email sign-offs for product notes, indicating a failure to maintain a centralized repository for documentation. This absence raises concerns about accountability and compliance, as it results in a lack of an audit trail for product note sign-offs.

**Medium Rated Issues:** Like the high-rated issues, the lack of documentation for identifying non-cooperative borrowers contributes to compliance risks and operational inefficiencies.

**Process Non-adherence**

**High Rated Issues:** Inadequate controls over handling and storage of customers' confidential documents were observed, leading to potential risks of misplacement or loss of sensitive information. This situation poses a significant threat to customer privacy and regulatory compliance.

**Medium Rated Issues:** Deviations from established processes, such as not obtaining the required Interest Service Reserve for loans, indicate a failure to adhere to operational guidelines. Additionally, instances of password sharing among staff highlight significant breaches of security protocols, increasing the risk of data breaches.

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# Issue root cause summary
## Summary of issue root cause explanations for high and medium rated issues across review areas

**System Development**
**Medium Rated Issues:** Periodic Re-KYC for co-borrowers was not conducted as required, indicating a system deficiency that could lead to non-compliance with regulatory requirements. The lack of a risk categorization field for co-borrowers further exacerbates this issue.

**System Issue**
**Medium Rated Issues:** Sharing of user IDs and passwords among relationship officers was observed, which is a violation of information security policies. This practice poses a significant risk to the integrity of organizational data and systems.

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# Summary of issue statistics, issue findings, root cause explanation, probable risk - Overall

Number of issues present are: 34
Issue Ratings: 4 high,12 medium and 18 low rated issues identified

Risk Categories:

1. Compliance Risk: 16 issues (0 high, 8 medium, 8 low)
2. Operational Risk: 24 issues (4 high. 4 medium, 16 low)
3. Financial Risk: 2 issues (2 low)
4. Reputational Risk: 1 issue (1 low)
5. Fraud Risk: 0 issue

Summary of Issue Findings:

- The observations reveal significant issues such as improper handling and storage of customers' confidential documents across various branches, and sharing of user IDs and passwords by relationship officers. There is a lack of compliance with regulatory and statutory requirements, including failure to display necessary notices and certificates. Physical security controls at branches are inadequate, with issues related to CCTV cameras and their backups. Discrepancies were found between physical assets and those listed in the Fixed Asset Register. Lastly, there were operational process exceptions, including mismatch between physical cheque quantity and the cheque inventory register.

Summary of Root Cause Explanation:

- The root causes of the issues observed include a lack of awareness or disciplined adherence to internal and regulatory requirements, particularly in handling customer documents and password sharing. There are also deficiencies in implementing IT security policies and monitoring physical security and fire safety at branches. The registers for IT and admin assets are not updated timely or properly, leading to discrepancies. Internal records are not adequately maintained or displayed. Operational processes, including FRFC management, are not adhered to due to lack of awareness. System deficiencies and operational misses have led to issues with Re-KYC of co-borrowers, unmasked Aadhaar copies, and customer detail updates. Lastly, there is a lack of adherence to regulatory guidelines regarding penal charges in facility agreements.

Root Cause Category:

- 1. Absence of Process: 5 issues (5 medium)
- 2. Lack of Documentation: 6 issues (3 medium, 3 low)
- 3. Process Non-adherence: 21 issue (1 high, 5 medium, 15 low)
- 4. System Development: 4 issues (3 medium, 1 low)
- 5. System Issue: 5 issues (1 medium, 4 low)

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