IDENTIFYING PAYMENT SYSTEM RISK
THE HOLY GRAIL OF RISK ASSESSMENTS

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AGENDA

- Definition of Risk
- Identifying Risk
- Objectives
- Barriers to Identifying Risk
- Mitigating Risks
- Internal Controls
- Emerging Risks vs. Evolving Risk
What is Risk?

The possibility that an event will occur and adversely affect the achievement of objectives

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Why does risk matter?
- Risks can keep an entity from achieving their goals
- Identifying risk allows the entity to design internal controls to mitigate the risk
- Improper identification of risk could also keep the entity from achieving their goals
What is Risk

- There are no wrong answers when evaluating risk
- Risk evaluation, management and acceptance is unique to every entity

Inherent Risk vs. Residual Risk

**Inherent Risk**
- “...the risk to the achievement of entity objectives in the absence of any actions management might take to alter either the risks’ likelihood or impact.”

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**Residual Risk**
- “...the risk to the achievement of objectives that remains after management’s responses have been developed and implemented.”

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Identifying Risk

- How do you identify risk?
  - Brainstorming
  - Experience
  - Education
  - Best practices

- What is missing from these practices?
  - Objectives (Goals)!

By definition, risks are defined as barriers to achieving an objective (goal)

- How can you identify a risk correctly if you do not have an objective?

- How do you establish objectives?
  - More importantly, what is an objective?
Objectives

What an entity strives to achieve

- Processing transactions with zero errors
- Balancing to the penny
- Having zero losses
- Migrating wires from in-person acceptance to online acceptance
- Increased deposits through enhanced service offerings

Matching Objectives to Risk

- Objective
  - Processing transactions with zero errors
- Risks
  - Checks encoding errors
  - ACH exception items
  - Wires misreading wire instructions
  - Mobile app does not identify foreign item
Objectives

- Matching Objectives to Risk
  - Objective
    • Migrating wires from in-person acceptance to online acceptance
  - Risks
    • Barriers to entry (onboarding process)
    • Client has insufficient knowledge of technology
    • Clients prefer face-to-face interactions

Objectives

- Matching Objectives to Risk
  - Objective
    • Increased deposits through enhanced service offerings
  - Risks
    • Barriers to entry (onboarding process)
    • Clients prefer face-to-face interactions
    • Solution provider is not sufficiently knowledgeable of risks

Objectives

- What happens if you objectives in one department do not match objectives in another?
  • Conflicting objectives can result in conflicting risks
  • What happens when conflicting risks collide?
Barriers to Identifying Risk

- Strategic decisions may impact objectives
  - Changes in objectives impact risk
  - May increase or decrease risk depending on objectives chosen
  - May create conflicting risks to different departments

- Using controls to identify risks
  - Creates a narrow focus and may not appropriately identify risks

- Poorly communicated objectives
  - Identifying risks is difficult without clearly defined objectives

- Unachievable Objectives
  - Processing transactions with zero errors
  - Balancing to the penny
  - Having zero losses
Mitigating Risk

- Methods for controlling/mitigating risk
  - Implement controls
  - Accept the risk
  - Avoid the risk
  - Outsource the risk

- Implement controls
  - Utilize risk assessment to identify controls
  - Design controls to mitigate risks to objectives
  - Develop objectives at sufficiently high level to minimize conflicting risks
Mitigating Risk

- Accept the risk
  • Take no action to mitigate the risk
- Avoid the risk
  • Do not offer the service/product so inherent risk is avoided
- Outsource the risk
  • Purchase insurance

INTERNAL CONTROLS

Internal Controls

“…is a process, effected by an entity’s board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance.”

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Internal Controls

- Internal control components
  - Control environment
  - Risk assessment
  - Control activities
  - Information & communication
  - Monitoring activities

Identifying risks is critical to almost every component of internal control

- Risk assessment
- Control activities
- Information & communication
- Monitoring activities

Identifying the entity’s objectives is critical to identifying risks

- Without objectives, you cannot identify risks
Internal Controls

- Without identifying risks, you cannot identify controls
- Without controls, you cannot mitigate risk
- Without mitigating risk, you cannot achieve your objectives
Payment System Risk Management

- Payment system strategies
  - Critical to include payment systems in the entity’s strategic plans
  - Lack of clear strategy can increase the change of mismatched objectives and risks
  - Allows for alignment of internal controls with risks to ensure objectives are met

Emerging vs. Evolving Risks

Emerging Risks

- New risks that have not been seen before
  - Fintech banking charter
  - Fintech start ups
Evolving Risks

- Risks that change/evolve over time
  - Corporate Account Takeover (CAT)
  - Settlement Risk for Same-Day ACH

QUESTIONS

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