

# The rogue trader essay



**ASSIGN  
BUSTER**

Have you ever told a lie? In most cases after telling one small lie another lie follows. After time passes and the lies began to seem like the truth, you dig yourself into a pool of lies which eventually contradicts your first lie. The same truth happens to Nick Lesson and his 8-8-8-8-8 account. It all started with 20, 000 that turned in to millions that turned in to billions that lead to the collapse of Barings Bank.

Although Nick Lesson was to blame, the direct blame goes to the board of supervisors and management of Barings. According to the Committee of Sponsoring Organizations of the Tread way Commission internal control is defined as the procedure, introduced and put into action by the executives of a company, which is designed to make available reasonable assurance of the, competence and usefulness of operations; trustworthiness and dependability of fiscal reporting; conformity to concerned rules and regulations.

The process of internal control comprises of five interconnected components. These components are Control Environment, Risk Assessment, Control Activities, Information and Communication and Monitoring. These make up for a highly competent framework for investigating and evaluating the system of internal control that is put to use in a business. In this report I will be examining Barings Banks collapse based on the movie " Rogue Trader" will comparing the banks structure to the COSO internal control framework.

### Control Environment

The first component, Control Environment, is the foundation for all the other internal control components. It is the tone setter of a company and

influences the control awareness of the employees. It is sometimes referred to as “ internal control environment.” Control Environment is expressed in many different forms such as management style, corporate culture values, philosophy and operating style, the organizational structure, and human resources policies and procedures.

Barings Bank board members and senior executives did not set a consistent example of high integrity and ethical behavior, because they themselves had an opportunity to punish Nick Lesson when he was arrested; however, they took no actions. If action would have been taken maybe Nick’s action of his unauthorized trading would have been detected. Barings also failed with its written code of conduct for employees, and reinforcing it with training; top down communication, and requiring periodic written statement of compliance from key employees. Nick was instructed to put together a team for the Singapore operation. His exact instructions from Simon Jones were “ No need to pay top dollar, get them young, get them hungry and train them up.”

Nick did just what he was told. Nick gave them an informal training then put them on the trading floor. Neither reinforced training nor code of conduct was important. One of Nick’s recruits got into a physical altercation. After he was pulled away, there was not written report of the incident. This action reveals that there was no process to resolve close ethical calls. When a Bank that was the size of Barings, have a melt-down of its magnitude, it is usually falls on the shoulders of management. Having the appropriate reaction to bad news for subordinate is important because it sends a message to the employees of the establishment where the company’s ethics truly rest.

When Barings board members took no disciplinary action on Nick for being arrested, it was because he generated millions of dollars for them; however when one of Nick's recruits losses 20, 000 he is told to fire the ill prepared worker. This shows that management reaction and ethics is based in money.

### Risk Assessment

When a company of any kind identifies organizational risk, analyze their potential in terms of cost and likelihood of occurrence, or install those controls whose projected benefits outweigh their costs, it is exercising Risk Assessment. Baring Bank board member totally dropped the ball when it came to risk assessment. During a meeting with his boss Nick stated, " I'd go up to see him in the afternoon, but we mainly talked about football... As for business, we scarlet talked about it."

This means that the business risks are not identified and are not candidly discussed with board of directors. Allowing Nick to hire who he chose was not the pre-initial problem. The pre-initial collapse was neither checking nor evaluation who he hired. This showed that Barings didn't evaluate risks with regards to new personnel. Also, since Nick was allowed to control trades on the floor and control the office on the back end; this showed the lack of checks and balances; and allowed Nick to get involved with unauthorized business activities. Through this Nick created the 8-8-8-8-8 account. When the 8-8-8-8-8 became aware to upper-level management, it was easily pushed aside.

Baring bank didn't properly evaluate all of the risk. " Nick, what's the difference between initial margin and variation margin?" This question was

asked to Nick from one of his recruits that worked in the back office with him. It is clearly true that Barings provided employees with adequate resources; however from this question Nick's personnel was sufficient but not competent and knowledgeable to manage current and new business activities. Barings did involve auditors in the risk management, but because all auditors weren't formidable like Ash Lewis most and almost all of the auditing process was lost. The auditors that took Ash Lewis place did not do a good job. Barings Bank could have saved itself if it reinforced its Risk Assessment.

### Control Activities

Control Activates are the policies and procedures that an organization develops to help protect the assists of the firm. Now this is where the meat of the problem happens. Nick Lesson was not controlled. He was allowed total access and this was where he bankrupted the company. There was no proper decision making by Simon. Nick sold contracts on the floor and because he was also working in the back office, keying in the contracts he bought or sold, he was able to cover his tracks long enough to make up for them.

When the figures of lost profits had gotten to the 7. 78billion and auditors and upper-level management started calling, Nick had already put the company on its belly. When there is not proper control activities like checks and balances there is most certain chance that there will be corruption. Ash Lewis pointed out that Nick running the trading floor and back office was unusual. Tony Railton told Ron that Nick's funding behavior was not by the

book and Ron only cared about Nick's profits that he was reporting. Nick's action wasn't total going undetected but unattended.

### Information and Communication

The part of COSO internal control framework that include the methods that management uses to record, process, and exchange information within the firm so that employees understood their roles and responsibilities pertaining to internal control is information and communication. Nick was able to manipulate numbers on the account information system to get a certain output of information. This means that Barings had very poor AIS that didn't properly identify, assemble, analyze, classify record, and report the institutions transaction in accordance with GAAP.

He continued to hide Losses in the 8-8-8-8-8 account. When it comes to understand one role, I think that everyone knew there role but didn't enforce their position. For example, Brenda Granger was in the Settlement Department in London. Nick directly made request for cash to her, and she transferred funds on a daily basis to Singapore to meet SIMEX margin payments. At one point she wanted to know about the knowledge or what he did; however she did not enforce any rules, she only took whatever explanation Nick gave her.

### Monitoring

After you have establish the control of your environment and put in place the proper risk assessments; the control activities and information and communication is what you in implement in the firm. The last thing that you

will do is process the management responsibility that assesses the quality of internal control performance overtime. This is called monitoring. This was Ash Lewis department of Baring Bank. She was the most feared auditor in the company. Just by sheer circumstances Nick go by her; but that is still no excuse.

If Barings had established a strong control environment all of the auditors would have been feared like Ash Lewis. The auditors that replaced her to audit Nick were a couple of push overs as Simon put it. This brings up the question did the audit personnel possess an appropriate level of expertise? Nick had free reign when it came to auditing. The auditor that he spoke to that asked for signatures for the transaction that covered the 7.78 billion lost was on the right track; however that particular auditor receive the document and didn't follow up on the received document.