Internal Control - Fiscal

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Everyday Internal Controls

• We lock our homes and vehicles.

• We keep our ATM/debit card pin number separate from the card.

• We review bills and credit card statements before paying them.

• We don’t leave blank checks or cash just lying around.

• We periodically change our computer passwords.
Why This Session Is Needed?

- Both ADWS and PARTNERS are responsible for ensuring federal funds are used properly.

- Internal Controls impact every aspect of an organization:
  - Are effective only when people and environment work together.
  - Help prevent fraud, waste and abuse.
Today’s Learning Objectives

• Discuss the definitions and requirements of internal controls as outlined in the Uniform Guidance

• Describe the components of an effective internal control framework

• Identify and describe key internal control activities

• Identify consequences of ineffective controls
Internal Controls
Internal Controls Definition

Uniform Guidance

2 CFR §200.61 Internal Controls
A process designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations
- Reliability of internal and external reporting
- Compliance with laws regulations
Internal Control over Compliance Requirements

2 CFR §200.62 Internal Control over compliance requirements for Federal Awards

A process to provide reasonable assurance that

(a) Transactions are properly recorded and accounted for, in order to:
- Permit the preparation of financial statements and reports;
- Maintain accountability over assets; and
- Demonstrate compliance with Federal statutes, regulations, and terms and conditions of Federal award;
Internal Control over Compliance Requirements

2 CFR §200.62 Internal Control over compliance requirements for Federal Awards

(b) Determine that transactions are executed in compliance with:
   ➢ Federal statutes, regulations, the terms and conditions of Federal award
   ➢ Any other Federal statutes and regulations identified in the Compliance Supplement

(c) Ensure funds, property, and other assets are safeguarded.
Internal Control Framework
Five Standards of Effective Internal Controls

1. Control Environment
2. Risk Assessment
3. Control Activities
4. Information and Communication
5. Monitoring
1. Control Environment

- Foundation for all other standards of internal control.
- Universal influence on all the decisions and activities of an organization.
- Effective organizations set a positive “tone at the top”.
- Factors include the integrity, ethical values and competence of employees, and management’s philosophy & operating style.
2. Risk Assessment

- Risks are internal & external events (economic conditions, staffing changes, new systems, regulatory changes, natural disasters, etc.) that threaten the accomplishment of objectives.

- Risk assessment is the process of identifying, evaluating, and deciding how to manage these events...
  - What is the likelihood of the event occurring?
  - What would be the impact if it were to occur?
  - What can we do to prevent or reduce the risk?
  - What is the vulnerability or likelihood of loss?
3. Control Activities

- Tools - policies, procedures, processes - designed and implemented to help ensure that management instructions are carried out.
- Help prevent or reduce the risks that can impede the accomplishment of objectives.
- Occur throughout the organization, at all levels, and in all functions.
- Includes training, approvals, authorizations, verifications, reconciliations, security of assets, reviews of operating performance, and segregation of duties.

- Types of Controls
  - Preventive
  - Detective
4. Communication and Information

• Pertinent information must be captured, identified and communicated on a timely basis.

• Effective information and communication systems enable the organization’s people to exchange the information needed to conduct, manage, and control its operations.

• Records and information systems must be sufficient to provide reliable reporting and demonstrate compliance with the federal award.
5. Monitoring

• Internal control systems must be monitored to assess their effectiveness… *Are they operating as intended?*

• Ongoing monitoring is necessary to react to changing conditions… *Have controls become outdated, redundant, or obsolete?*

• Monitoring occurs in the course of everyday operations; it includes regular management & supervisory activities and other actions personnel take in performing their duties.

• It also includes the process of monitoring subrecipients for compliance with requirements and taking appropriate actions to correct deficiencies.
Key Internal Control Activities
Key Internal Control Activities

Internal controls are usually *Preventive* or *Detective*.

- **Preventive** – let’s stop an unwanted outcome before it happens.

- **Detective** – let’s find the problem before it grows.
Preventive Controls

Preventive controls are proactive controls designed to prevent errors, omissions, loss, loopholes, or other undesirable events from occurring.

Examples of Preventive Controls

- Segregation of Duties
- Proper Authorizations
- Adequate Documentation
- Safeguarding of Assets
Detective Controls

Detective controls attempts to detect errors, loopholes, or other undesirable events that have occurred and enable prompt corrective action.

Detective controls provide evidence after-the-fact that loss or error has occurred, but do not prevent occurrence.

Examples of Detective Controls

- Supervisory Review
- Reconciliations
- Safeguarding of Assets
- Physical Inventories
- Monitoring Activities
Segregation of Duties

- **Segregation of duties** is the concept of having more than one person required to complete a task.

- Divide responsibilities between different employees so one individual does not control all aspects of a transaction.

- Reduce the opportunity for an employee to commit and conceal errors (intentional or unintentional) or perpetrate fraud.
Segregation of Duties

To help prevent FRAUD and/or error, no one person should:

- Initiate the transaction
- Approve the transaction
- Record the transaction
- Reconcile bank records
- Handle assets
- Review report
Authorization & Approval

- Management should document and communicate which activities require approval, and by whom, based on the level of risk to the organization.

- Ensure that transactions are approved and executed only by employees acting within the scope of their authority granted by management.

- Consider dual signatures on transactions over a certain threshold.
Approval Check-List

- Written policies and procedures
- Supporting documentation
- Question unusual items
- No “rubber stamps”
- No blank signed forms
Security of Assets

- Secure blank check stock and signature stamps (keep separate).
- Deposit cash and checks daily.
- Perform periodic physical inventories to verify existence, quantities, locations, condition, and utilization.
- Base the level of security on the vulnerability of items being secured, the likelihood of loss, and the potential impact should a loss occur.
Review & Reconciliation

- Examine checks and endorsements.
- Track transactions between accounts.
- Compare payroll checks with employee records.
- Examine bank statements for unusual withdrawals.

- Base level of review on materiality, risk, and overall importance to organization’s objectives.
- Ensure frequency is adequate enough to detect and act upon questionable activities in a timely manner.
Internal Control Recap
Benefits from Strong Internal Controls

- Reducing and preventing errors in a cost-effective manner
- Ensuring priority issues are identified and addressed
- Protecting employees & resources
- Providing appropriate checks and balances
- Having more efficient audits, resulting in shorter timelines, less testing, and fewer demands on staff
Why don’t Internal Controls always work?

• Inadequate knowledge of policies and procedures
• Inadequate segregation of duties
• Inappropriate access to assets
• Control override
Questions?

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