

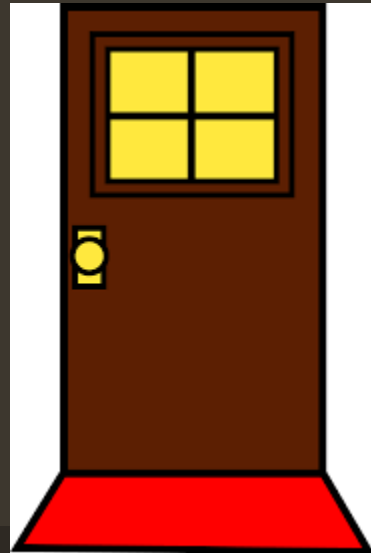
# Internal Control - Fiscal

Carl M. Danley, Jr., CFE



# 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.

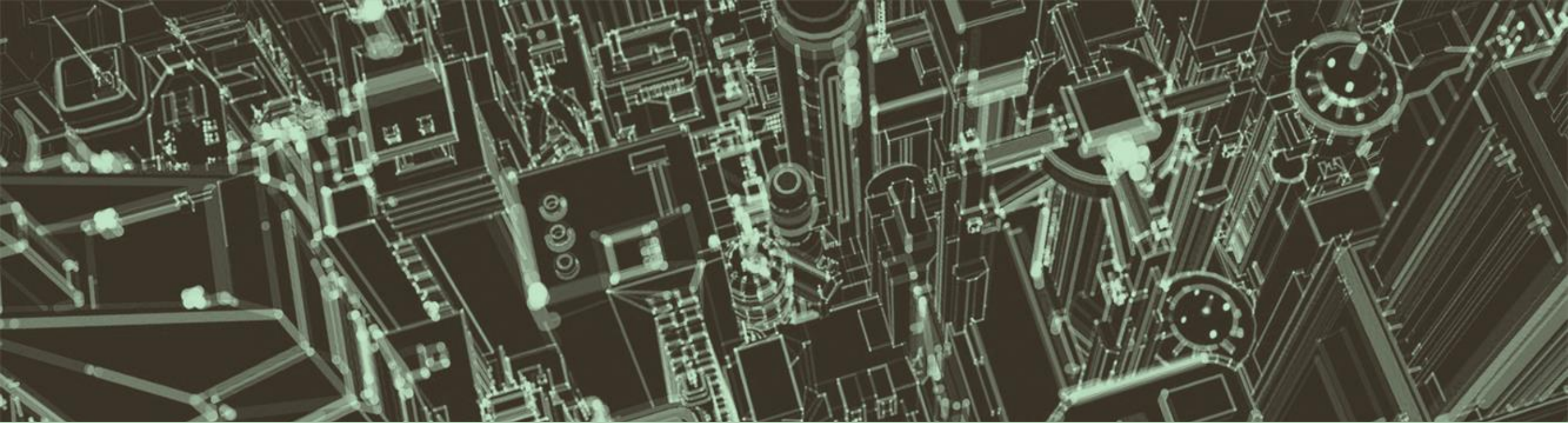


Arkansas Department  
of Workforce Services



# 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

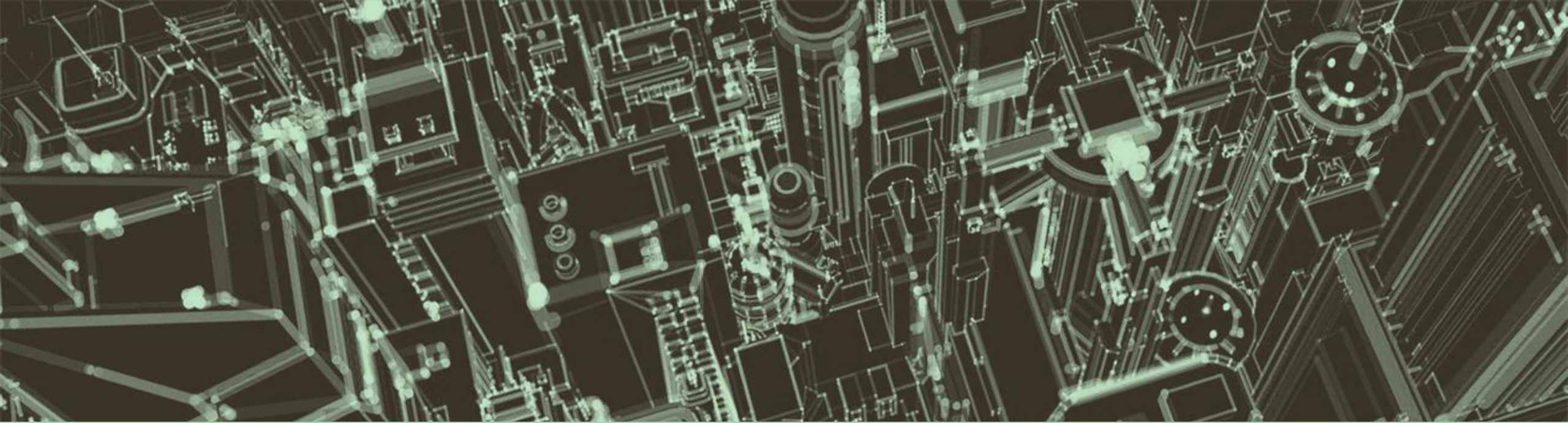
- (a) Transactions are properly recorded and accounted for, in order to:
  - Permit the preparation of financial statements and reports;
  - Maintain accountability over assets; and
  - Demonstrate compliance with Federal statutes, regulations, and terms and conditions of Federal award;

# 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

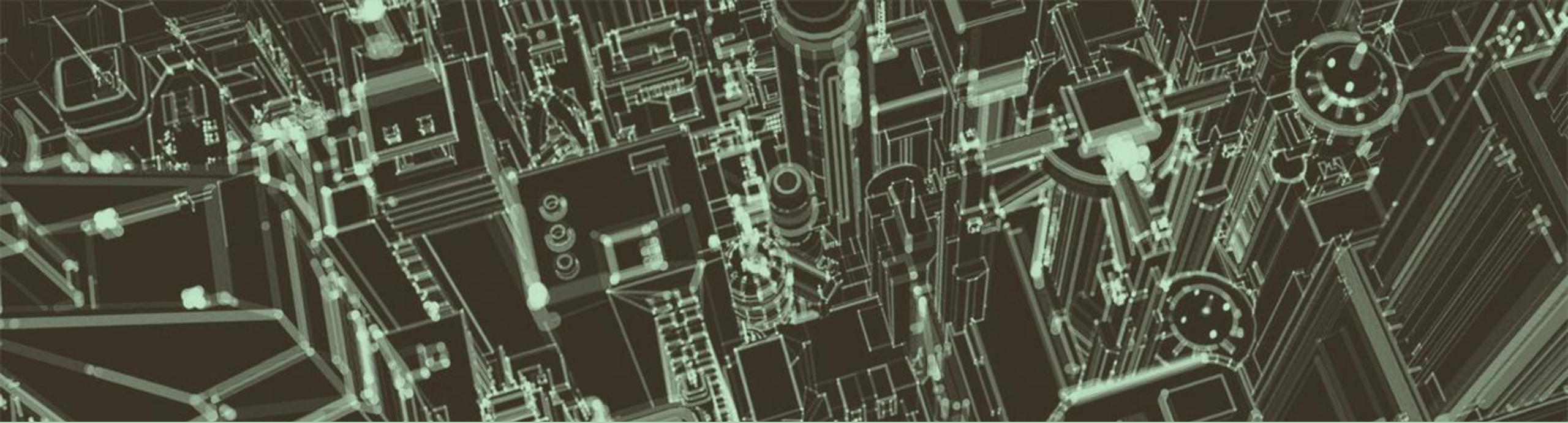
- Tools - policies, procedures, processes - designed and implemented to help ensure that management instructions are carried out.
- Help prevent or reduce the risks that can impede the accomplishment of objectives.
- Occur throughout the organization, at all levels, and in all functions.
- Includes training, 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

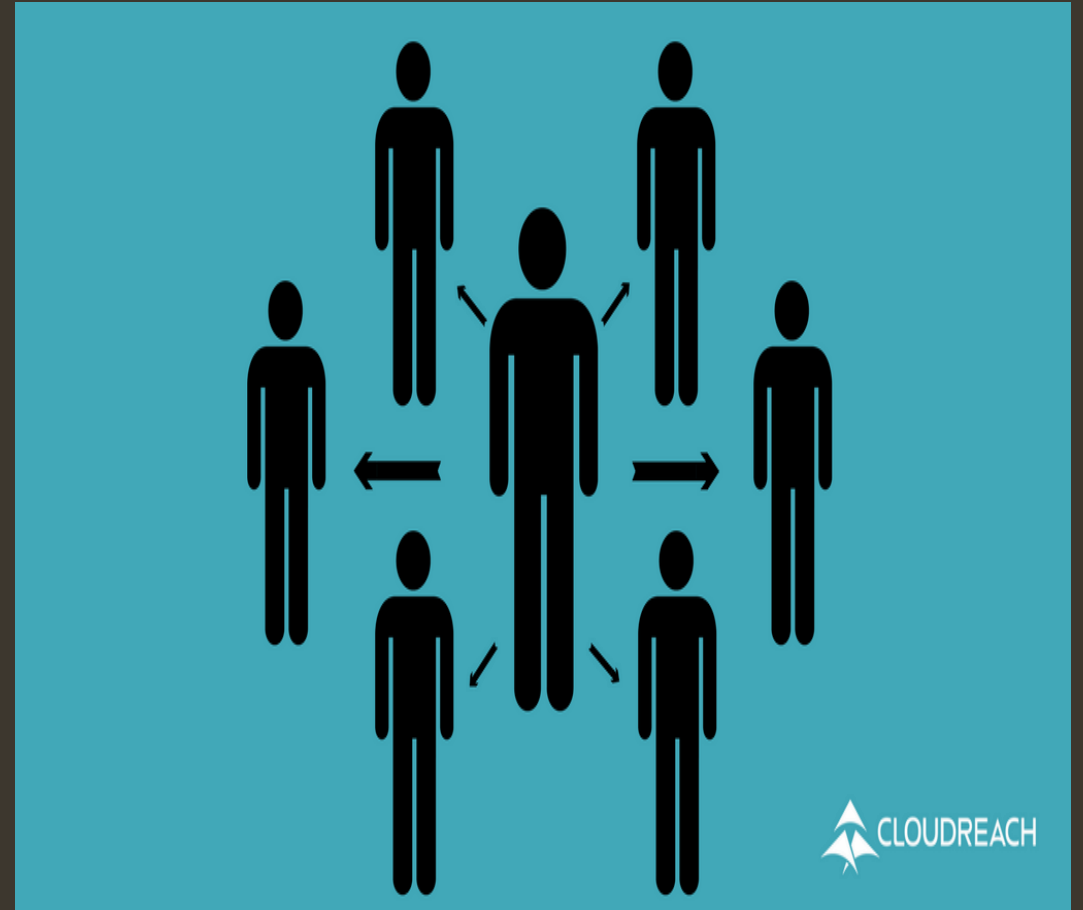
- *Detective controls* attempts to detect errors, loopholes, or other undesirable events that have occurred and enable prompt corrective action.
- Detective controls provide evidence after-the-fact that loss or error has occurred, but do not prevent occurrence.

## 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



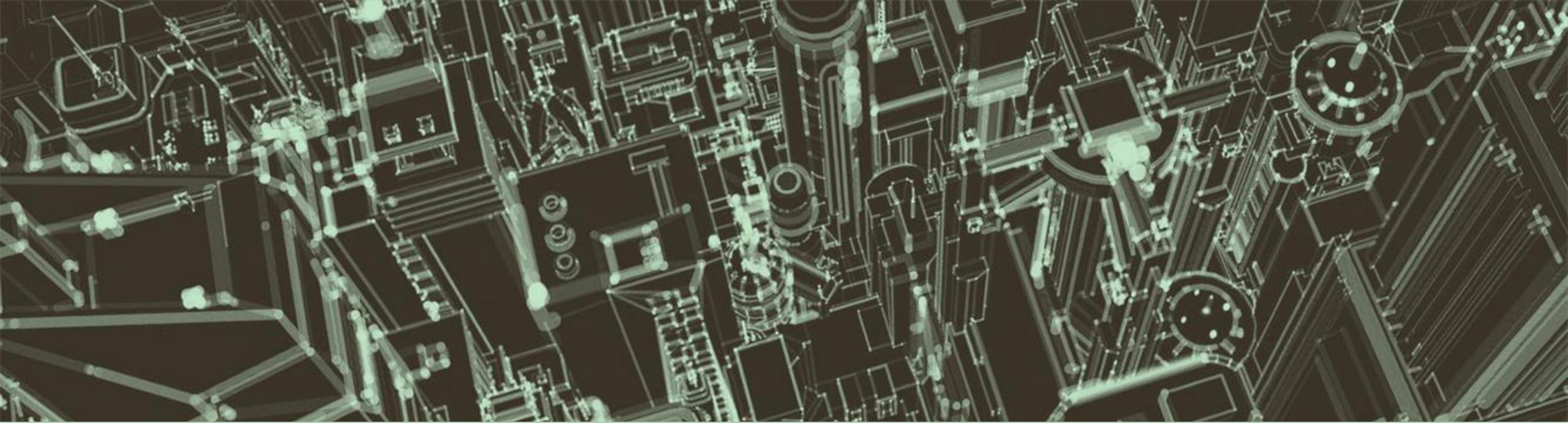
# Security of Assets

- ❖ 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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