

Indiana League of
Municipal Clerks and
Treasurers Fall Meeting

District Meeting
Fall 2015

Internal Controls

Indiana State Board of Accounts

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Internal Controls

- Why Internal Controls
- What Are Internal Controls
- Case Studies & Examples



Internal Controls

Why Internal Controls?



Indiana Code 5-11-1-27

(e) “. . . the state board of accounts shall define and the audit committee shall approve not later than November 1, 2015, the acceptable minimum level of internal control standards and internal control procedures for internal control systems of political subdivisions, including the following: (1) Control environment. (2) Risk assessment. (3) Control activities. (4) Information and communication. (5) Monitoring. The internal control standards and procedures shall be developed to promote government accountability and transparency.”

IC 5-11-1-27(f)

“Not later than November 1, 2015, the state board of accounts shall develop or designate approved personnel training materials as approved by the audit committee, to implement this section.”

Uniform Internal Control Standards for Indiana Political Subdivisions



State Board of Accounts

Paul D. Joyce, CPA

State Examiner

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Indiana Code 5-11-1-27(g)

“After June 30, 2016, the legislative body of a political subdivision shall ensure that:

- (1) the internal control standards and procedures developed under subsection (e) are adopted by the political subdivision; and
- (2) personnel receive training concerning the internal control standards and procedures adopted by the political subdivision.”

Indiana Code 5-11-1-27(c) defines “personnel”:

“As used in this section, "personnel" means an officer or employee of a political subdivision whose official duties include receiving, processing, depositing, disbursing, or otherwise having access to funds that belong to the federal government, state government, a political subdivision, or another governmental entity.”

Indiana Code 5-11-1-27(h)

(h) After June 30, 2016, the fiscal officer of a political subdivision shall certify in writing that:

- (1) the minimum internal control standards and procedures defined under subsection (e) have been adopted by the political subdivision; and
- (2) personnel, who are not otherwise on leave status, have received training as required by subsection (g)(2).

Indiana Code 5-11-1-27(h) *continued:*

“ . . . The certification shall be filed with the state board of accounts at the same time as the annual financial report required by section 4(a) of this chapter is filed. The certification shall be filed electronically in the manner prescribed under IC 5-14-3.8-7.”

Indiana Code 5-11-1-27(i)

“After June 30, 2016, if the state board of accounts finds during an audit of a political subdivision that:

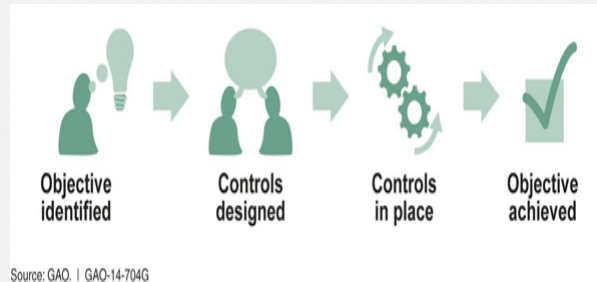
(1) the political subdivision has not adopted the internal control standards and procedures required under subsection (g)(1); or

(2) personnel of the political subdivision have not received the training required under subsection (g)(2); the state board of accounts shall issue a comment in its examination report for the political subdivision. “

Indiana Code 5-11-1-27(i) *continued...*

“... If, during a subsequent audit, the state board of accounts finds a violation described in subdivision (1) or (2) has not been corrected, the political subdivision has **sixty (60) days** after the date the state board of accounts notifies the political subdivision of its findings **to correct the violation**. If a violation is not corrected within the required period, the state board of accounts shall forward the information to the department of local government finance.”

Why are Internal Controls Important?



Benefits:

- Accountability and transparency
- Internally – quickly evaluated; inefficiencies addressed and corrected
- Encourage efficient use of government time and resources
- Conveys to citizens commitment to detect fraud, waste, abuse
- Reduces costs – timely completion of responsibilities / prevents fraud, waste, abuse
- Better internal controls can result lower audit costs

What is Internal Control?



SBOA defines internal control as follows:

- *Internal control is a process executed by officials and employees that is designed to provide reasonable assurance that the objectives of the political subdivision will be achieved.*
- *It is a basic element fundamental to the organization, rather than a list of added on tasks;*

SBOA definition of internal control (continued):

- *It is an adaptable process that is a means to an end, not an end in itself;*
- *It is focused on the achievement of objectives; and*
- *It is dependent on officials and employees for effective implementation.*

- Organizational roles are important
- All members of a city or town, including elected officials, board members, and employees full fill a role in the internal control system
- Leadership is key – the tone is set at the top
- Clear support from leadership engages a successful, effective internal control system

Procedures for Adopting Internal Control Procedures

- o Legislative body should stipulate in a policy they have adopted the internal control standards as defined by SBOA under IC 5-11-1-27(e).
- o Personnel training should be evidenced through a documentation process – *can be as simple as acknowledgement by personnel through email.*

Procedures for Adopting Internal Control Procedures

- o Fiscal officer must certify in writing the minimum internal control standards have been adopted and personnel have received training.
- o Certification filed with SBOA when completing the Annual Financial Report for 2016 (in early 2017).

Objectives:

In general, objectives originate from purposes and functions detailed in laws, regulations, ordinances, etc.

Set at both the entity level and office level by the oversight body and management

Must be viewed from a holistic, interrelationship approach

Categories of Objectives:

- **Operations** – analyze operational and performance goals along with the effectiveness and efficiencies of operation, including the safeguarding of assets
- **Reporting** – considers both financial and non-financial information, internal and external to the unit, with an expectation of reliability, accountability and transparency
- **Compliance** - assure adherence to laws and regulations

Minimum Level of Internal Controls

- COSO – *Committee of Sponsoring Organizations of the Treadway Commission*



Visit: www.coso.org

Minimum Level of Internal Controls

- U.S. Government Accountability Office publication – “*Standards for Internal Control in the Federal Government*” [otherwise referred to as the **Greenbook**]
- Visit: www.gao.gov/greenbook



Five components of internal control

The five components of internal control as described in the COSO framework are as follows:



- Monitoring
- Information and Communication
- Control Activities
- Risk Assessment
- Control Environment

CONTROL ENVIRONMENT

The control environment sets the tone of the organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure.



Control environment factors include:

- Integrity and ethical values
- Commitment to competence
- Board of Directors or Audit Committee
- Management philosophy and operating style
- Organizational structure
- Assignment of authority and responsibility
- Human resource policies and procedures

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RISK ASSESSMENT

Risk assessment is the identification and analysis of relevant risks to achievement of the objectives, forming a basis for determining how the risks should be managed.



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RISK ASSESSMENT

Objectives (i.e. assertions) must be established prior to the identification of risks to their achievement and to take necessary actions to manage the risks.

By setting objectives, both at entity and activity levels, prior to a risk assessment, a company can determine the critical success factors; then determine the risks to the critical success factors.

A risk assessment usually includes:

- a. Estimating the significance of a risk
- b. Assessing the likelihood (or frequency) of the risk occurring
- c. Consideration of how the risk should be managed

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CONTROL ACTIVITIES

Control activities are the policies and procedures that help ensure management directives are carried out. They help to ensure that necessary actions are taken to address risks to achievement of the entity's objectives. Control activities occur throughout the organization, at all levels and in all functions.



Control activities include:

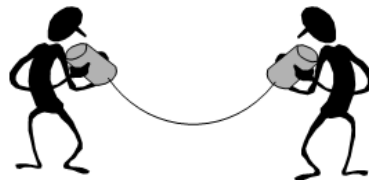
- Approvals
- Authorizations
- Verifications
- Reconciliations
- Reviews of operating performance
- Security of assets
- Segregation duties

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Information and Communication

- Emphasizes importance of quality information
- Volume and sources
- Complexity of processes
- Technology advances
- Greater interaction with 3rd party vendors



Monitoring Activities

Ongoing Evaluations

- Built into the business process at various levels
- Timely information

Separate Evaluations

- Conducted periodically
- Frequency will depend on assessment of risks and effectiveness of ongoing evaluations

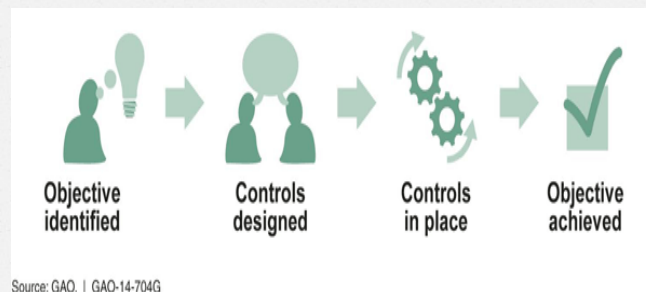


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Documentation of Internal Control System

- ❖ Management develops & maintains documentation of its internal controls.
- ❖ Management documents in policies the internal control responsibilities of the organization.
- ❖ Management evaluates & documents results of monitoring.
- ❖ Management evaluates & documents issues and appropriate actions timely.
- ❖ Management completes & documents correction actions.

U.S. GAO Greenbook, p. 71



Source: GAO. | GAO-14-704G