

SMART
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GRANTS
MANAGEMENT 2015

Internal Controls: Providing an Effective Control Environment



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Why This Session Is Needed

Uniform Guidance has expanded the requirements and increased the focus on internal controls

Internal controls are key to protecting and safeguarding grant assets

Internal controls help ensure compliance

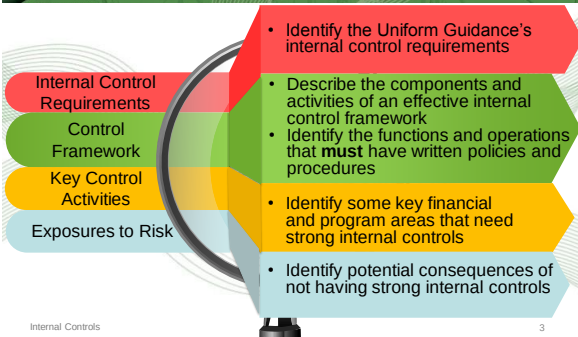
Policies and procedures reduce risk that can impede the accomplishment of objectives

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Lesson Overview & Module Objectives



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Knowledge Check

On a scale of 1 (lowest) to 5 (highest), rate your knowledge and understanding of the following by **circling** the appropriate number in the middle column of the sheet, labeled Pre-Training, for each of the statements.

- Uniform Guidance's new internal control requirements
- Five integrated components of internal controls per the COSO Framework
- Effective Internal Control practices
- Requirements for written policies and procedures
- Policies and procedures needed by an organization

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Internal Control Requirements

Learning objectives for this section

- Identify the Uniform Guidance's internal control requirements

Increased Emphasis on Internal Controls

Uniform Guidance

- 2 CFR 200.400
Policy Guide for Cost Principles
• "Sound Management Practices"
- 2 CFR 200.303
Internal Controls Requirement
- 2 CFR 200.61
Definition - Internal controls
- 2 CFR 200.62
Definition - Internal Control over Compliance Requirements

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Sound Management Practices (1 of 2)

2 CFR 200.400

Policy Guide

- Non-Federal entity is responsible for efficient and effective administration of award through use of **sound management practices**, and administering Federal funds in **compliance** with agreements, program objectives, and the terms and conditions of Federal award.



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Sound Management Practices (2 of 2)

2 CFR 200.400

- Employing sound organization and management techniques to assure proper and efficient administration of award, in recognition of non-Federal entity's **own unique combination of staff, facilities, and experience**.
- In other words, the grantee must establish an effective internal control structure.



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Seven Financial Management Standards

- | | |
|---|--|
| Identify all Federal receipts and expenditures | Comparison of expenditures to budgets |
| Accurate, current, and complete disclosure | Written procedures for payments |
| Records that identify source and application of funds | Written procedures for allowable costs |
| Effective control over and accountability for assets | |

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Effective Management Systems (1 of 2)

Effective financial management systems include:

- Clear delineation of roles and responsibilities
- Written policies and procedures
- Training
- Internal controls
- Effective oversight
- Effective communication and information sharing

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Effective Management Systems (2 of 2)

Financial systems that provide reliable and current information:

- Accounting controls
- Accurate, timely reports
- Budget controls
- Asset management
- Record retention/access controls

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Uniform Guidance Requirements for Internal Controls

2 CFR 200.303 Internal controls

- Have effective internal controls over Federal awards that provide reasonable assurance of compliance
- Comply with Federal statutes, regulations, and grant terms and conditions
- Evaluate and monitor compliance
- Take prompt action when instances of noncompliance are identified
- Safeguard protected personally identifiable information (PII) and other sensitive data.

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Internal Controls Defined

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 and regulations



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Internal Control over Compliance Requirements (1 of 2)

200.62 (a) Transactions properly recorded/accounted to:

- Permit the preparation of financial statements and reports
- Maintain accountability over assets
- Demonstrate compliance with Federal statutes, regulations, and terms and conditions of the Federal award



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Internal Control over Compliance Requirements (2 of 2)

(b) Determine that transactions executed in compliance with:

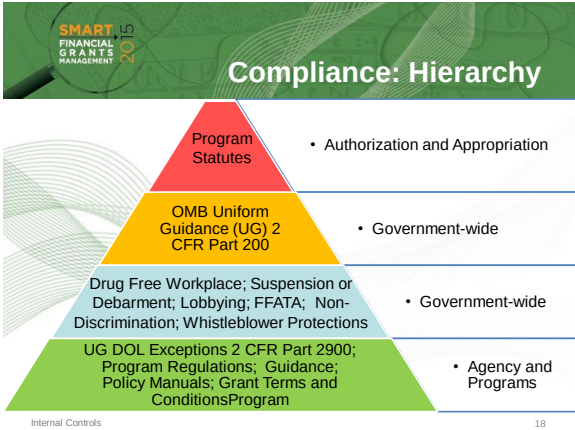
- Federal statutes, regulations, the terms and conditions of the Federal award
- Any other Federal statutes and regulations identified in the Compliance Supplement

c) Ensure funds, property, and other assets are safeguarded.



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Resources for Internal Control Guidance

“Standards for Internal Control in the Federal Government,” also known as the **“Green Book,”** issued by the Comptroller General of the United States

<http://www.gao.gov/assets/670/665712.pdf>

“Internal Control Integrated Framework” issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO)

http://www.coso.org/documents/990025P_Executive_Summary_final_may20_e.pdf

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Status Check

Are the statements true or false?

?

Internal controls provide reasonable assurance that operations achieve objectives in the following areas:

- Effectiveness and efficiency of operations
- Reliability external reporting, and
- Compliance with laws and regulations

?

Effective policies and procedures are control activities that provide reasonable assurance to reduce risks against non-compliance or loss of assets.

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Internal Control Framework

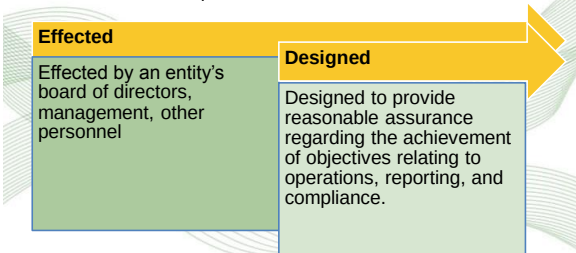
Learning objectives for this section

- Describe the components and activities of an effective internal control framework
- Identify the functions and operations for which non-Federal entities **must** have written policies and procedures

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The COSO* View of Internal Control

Internal control is a process:



* Committee of Sponsoring Organizations of the Treadway Commission

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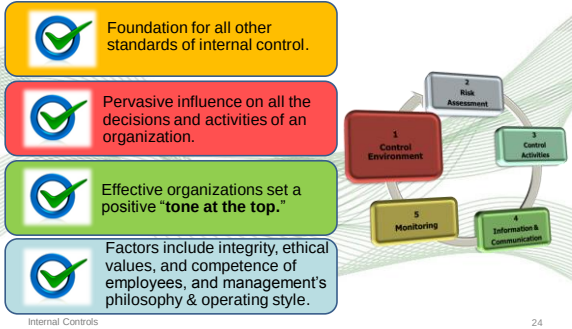
Internal Control Framework... Five Inter-Related Components



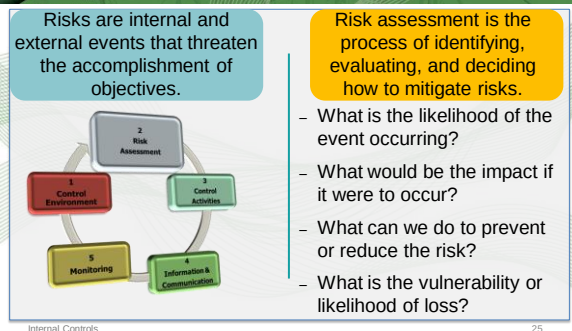
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SMART FINANCIAL GRANTS MANAGEMENT 2013 COSO Component 1: Control Environment



SMART FINANCIAL GRANTS MANAGEMENT 2013 COSO Component 2: Risk Assessment



SMART FINANCIAL GRANTS MANAGEMENT 2013 Risk Assessment for Equipment

2 CFR 200.313

Equipment

- Secure and restrict access to equipment to reduce the risk of loss or unauthorized use.
- Perform periodic physical inventories to verify existence, quantities, location, 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.

These principles apply to other assets as well: cash, credit cards, laptops, supplies, etc.



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COSO Component 3: Control Activities

Tools:
Policies, Procedures, and Processes

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Designed and implemented to help ensure that management directives 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.

Include approvals, authorizations, verifications, reconciliations, security of assets, reviews of operating performance, and adequate separation of duties.

Control Activities: Separation of Responsibilities

Custodian

- A separate person holds or has custody of the asset

Authorizing

- A separate person authorizes the transaction

Recording

- A separate person records the transaction

Reconciling

- A separate person reconciles the transaction

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What Policies and Procedures Does Your Organization Need?

Organizational Chart

- Office responsibilities
- Interactions between divisions, offices
- Interactions with external entities

Job Descriptions

Grant Structure

- Grant Administration
- Partners
- Subrecipients

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Organizational Management and Effective Internal Controls

- Effective Management Control
- Compliance with applicable laws and regulations
- Effectiveness and efficiency of operations
- Considered approach
- Transparency
- Consistency
- Clarity
 - Guidance for staff and subrecipients
 - Training tool for new staff
 - Resources



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Policy vs. Procedure

Policy – Guideline that regulates organizational activities; position statement

vs.

Procedure – Description of the normal method for handling things; protocols, steps



Authority to establish, approve

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Establishing Policies & Procedures

Some are required



Sound management practices



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Requirements for Written Policies and Procedures

Required written policies and procedures:

- ✓ Payments 200.302 (b)(6), and 305
- ✓ Procurement 200.318
- ✓ Competition 200.319
- ✓ Method for evaluation and selection 200.320
- ✓ Allowable costs 200.302 (b)(7)
- ✓ Compensation 200.430
- ✓ Fringe Benefits 200.431
- ✓ Employee relocation costs 200.464
- ✓ Travel costs 200.474

- Put these into clearly written policies and procedures
- All relevant parties should have copies



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Statutory/Regulatory Requirements for Policies and Procedures

- Policy requirements may be included in the program laws and regulations for:
 - ✓ WIA/WIOA
 - ✓ Trade Adjustment Assistance (TAA)
 - ✓ Older Americans Act (OAA)
 - ✓ Wagner Peyser Act
 - ✓ American Competitiveness and Workforce Improvement Act of 1998 (ACWIA)



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Recommended Policies and Procedures (1 of 3)

- Accounting System
- Budget Controls and Modifications
- Chart of Accounts
- Receivables
- Payables
- Approvals
- Documentation
- Audits and Resolution
- Small Purchase Process – Credit Card, Petty Cash
- Drawdowns and Cash Management



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Recommended Policies and Procedures (2 of 3)

- Bank Reconciliation
- Program Income
- Interest Income
- Human Resources – hiring and selection
- Compensation and Fringe Benefits
- Complaints/Grievances
- Cost Policies - Allowable Costs, Indirect Costs
- Staff Travel
- Participant/Program Services
- Purchasing
- Procurement



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Recommended Policies and Procedures (3 of 3)

- Monitoring
- Incident Reporting
- Property/Equipment Management
- Record Retention
- Match and Leveraged Resources
- Reporting (Financial and Performance)
- Internal Controls, Segregation of Duties
- Policies and Procedures for the Board



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Effective Policies and Procedures

Compliant

- With rules and regulations

Clear

- Precise, easy to understand, unambiguous

Complete

- Addresses the process flow; appropriate level of detail; does not leave major unanswered questions

Current

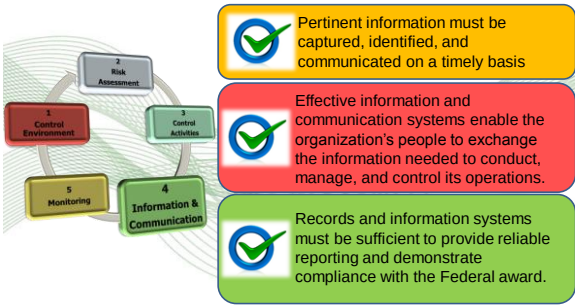
- Regular review, modify if needed

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COSO Component 4: Communication and Information



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Communicating Policies and Procedures (1 of 2)

To be effective, policies and procedures must be understood and used

- Existing policies and procedures
 - Communicated through training to new
 - Board Members
 - Staff
 - Subrecipients

Follow up to ensure implementation

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Communicating Policies and Procedures (2 of 2)

Newly developed policies and procedures

- Distributed by official issuance
- Accompanied by appropriate training

Important to create ownership

Be prepared to deal with possible attitudes

Provide appropriate forums

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COSO Component 5: Monitoring

Assess their effectiveness... *Are they operating as intended?*

React to changing conditions... *Have controls become outdated, redundant, or obsolete?*

Occurs in the course of everyday operations

Subrecipient compliance and taking appropriate actions

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Status Check

Are the statements true or false?

Written policies and procedures are required for the following:

- Payments,
- Procurement,
- Allowable Costs,
- Human Resources

The five components of the COSO internal structure are:

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

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Key Internal Control Activities

Learning objectives for this section

- Identify some key financial and program areas that need strong internal controls

Key Financial and Program Areas

Strong internal controls along with adequate separation of duties are needed in the following key financial and program areas:

Budgeting	Cash Management
Cost Allocation	Purchasing & Contracting
Accounting & Payables	Property Management
Financial Reporting	Personnel & Payroll
Information Systems	Participant Related Payments
Travel	

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Effective Internal Controls

Benefit rather than encumber management

Encourage adherence to company's policies and procedures

Are cost-effective

Promote operational efficiency

Safeguard assets

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Effective Internal Controls for Small Entities

Same standards as large entities but different implementation

Some small entities have some advantages

- Management more involved in operations
- Direct interaction with staff
- Easier lines of communication
- Use compensating controls
 - Add levels of review, random transaction reviews

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Internal Control Limitations

Cost Considerations/Cost vs. Benefit

Judgment

Breakdowns

Management Overrides

Risk of Collusion

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Exposures to Risk

Learning objectives for this section

- Identify potential consequences of not having strong internal controls

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Weak Internal Controls Increase Risk Through ... (1 of 3)



Business Interruption

System breakdowns or catastrophes, excessive re-work to correct for errors.

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Weak Internal Controls Increase Risk Through ... (2 of 3)



Erroneous Management Decisions
Based on erroneous, inadequate, or misleading information.

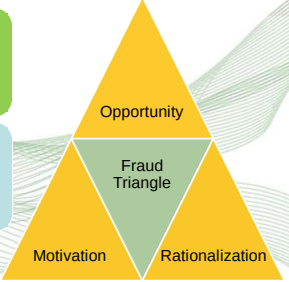
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Weak Internal Controls Increase Risk Through ... (3 of 3)

Fraud, Embezzlement and Theft
By management, employees, customers, vendors, or the public-at-large.

Loss, Misuse or Destruction of Assets
Unintentional loss of physical assets such as cash, inventory, and equipment.



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Common Contributors to Compliance Deficiencies

Inadequate resources	!
Lack of understanding of roles and responsibilities of institutional staff	!
Inadequate staff and subrecipient training and education	!
Outdated or nonexistent policies and procedures	!
Inadequate management systems	!

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Findings on Policies and Procedures

Findings

- Inconsistencies in financial operations – audit exceptions
- Lack of, or inadequate, policies
- Invalid procurements

Consequences

- Ineligible participants
- Disallowed costs
- Re-competing awards



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Common Findings and Consequences

Examples of actual findings:



No written policies and procedures for subrecipient fiscal monitoring.



No supportive services policies and procedures in place; recipient did not document participants' need for provided supportive service.



Did not maintain adequate policies and/or procedures for tracking match, preparing bank reconciliations; procurement policy covered only equipment purchases, not other procurement actions.

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Helpful Tips



✓ Hire competent, reliable, and ethical staff



✓ Set the control environment including compensating controls



✓ Formalize internal control policies and staff responsibilities in writing



✓ Entire staff, including the board, can be incorporated into the process

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CLASS QUIZ (1 of 4)

True or False

1. Internal controls are concerned with the reliability of financial information.
2. Incompatible duties exist when an employee is in a position to perpetrate and conceal errors or fraud.
3. Well-designed internal controls will prevent all fraud by top management.
4. The relatively low number of types of transactions incurred by small entities makes the segregation of duties impossible.



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CLASS QUIZ

(2 of 4)

Which of the following is LEAST likely to be evidence of effective internal controls?



A. Supporting documents stamped "Processed"



B. Monthly list of accounts payable



C. Records documenting users of automated accounting programs



D. Signatures on authorization forms

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CLASS QUIZ

(3 of 4)

Which of the following is NOT considered one of the five major components of an internal control structure?



A. Risk Assessment



B. Segregation of duties



C. Control Activities



D. Monitoring

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CLASS QUIZ

(4 of 4)

Of the following statements about internal controls, which one is not valid?

- A. No one person should be responsible for the custodial responsibility and the recording responsibility for an asset.
- B. Transactions must be properly authorized before such transactions are processed.
- C. Because of the cost/benefit relationship, certain risks may have to be accepted.
- D. Internal Control activities reasonably ensure that collusion among employees cannot occur.

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Key Concepts

Effective internal controls are required, and essential, to ensure compliance and to protect and safeguard grant assets.

Organizational culture established at the top and communicated to all employees is essential.

Policies and procedures are a critical part of an organization's control environment.

The failure to have/follow written policies and procedures can result in serious consequence, including disallowed costs.

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Knowledge Check

On a scale of 1 (lowest) to 5 (highest), rate your knowledge and understanding of the following by circling the appropriate number in the column of the sheet, labeled Pre-Training, for each of the statements.

-
- ☐

Uniform Guidance's new internal control requirements.
- ☐

Five integrated components of internal controls per the COSO Framework
- ☐

Effective internal control practices
- ☐

Requirements for written policies and procedures.
- ☐

Policies and procedures needed by an organization.

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**"If everything seems under control,
you're just not going fast enough."**

~ Mario Andretti

Thank You!

Please Complete Your Evaluations
