

BMG

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Common Internal Control Weaknesses



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Coverage

- Common Weaknesses
- Tips to address
- Fraud



Internal Controls: Process

- Different types of controls can be designed to work at varying points within **operational**, financial, **governance**, or compliance processes
- Components:
 - ✧ Control Environment
 - ✧ Risk Assessment
 - ✧ Monitoring
 - ✧ Control Activities
 - ✧ Information and Communication

Goal: Reasonable assurance



Risk Assessment

- Identification of risk factors
 - External factors (e.g., new systems, economic changes, rules and regulations)
 - Internal factors (e.g., new personnel, low morale, short staffing)
- Risk Analysis
 - Estimating the significance of the risk (e.g., dollars, reputation)
 - Estimating the likelihood of occurrence
- Assessing options for controls
 - Differing types of controls (e.g., preventive, detective)
 - Resource availability
 - Cost



What To Look For

- Top level performance monitoring
- Direct functional or activity management
- Data processing controls
- Physical controls
- Performance indicators
- Segregation of duties



Common Control Weaknesses

- Segregation of duties
- Reconciliations
 - Completeness
 - Competent and knowledgeably placed staff
- Adequate documentation supporting transactions and/or decisions
- Compliance with University policies for spending based on fund or funds purpose



Reconciliations

- Revenue completeness
 - Against source data or information
 - According to contractual expectations
 - Comparison to expectations
 - Tie to rate evaluations
- Financial statement review
 - Completeness
 - Comparison to expectations
 - Investigation of variances from expectations



Segregation

- Critical review of permissions (what *can* one do) as well as actual job responsibilities (what does one *actually* do)
- Consider operational responsibilities as well as financial process responsibilities
- Overrides are flags – defeats good segregation



Limitations of Internal Controls

- Judgment
- Breakdowns
- Management override
- Collusion
- Cost versus benefit



Most Common Fraud Areas

- Expenditure reimbursement (arranged travel, TEM)
- Equipment
- Cash (incoming, petty cash, and change funds)
- Payroll (hourly, vacation, and sick leave)
- P-Card/T-Card



Control weaknesses: Fraud

1: Collusion between supervisor and a staff

- Under-reporting time (covered for each other)
- Resale environment with poor controls over inventory and no analysis of use vs production
- No segregation in purchasing / receiving processes
- Frequent complaints, not fully investigated

2: Departmental supply distribution

- Lack of segregation in inventory receiving and control
- Poor recordkeeping for intake, uses, requests, projected needs
- Escalating consumption pattern not detected nor reviewed
- Use of a common departmental account where activity was more easily buried



Control weaknesses: Fraud

3: Unit head with unmitigated control over assets

- Personally negotiated and controlled asset trades and sponsorships
- Override of controls related to physical asset verification
- Personally designed a system where two individuals had partial asset roles, neither had complete information, and no reconciliations
- Includes existing assets and newly purchased assets

4: Internal store operations, purchasing and financial review segregation

- With authentic receipts, appropriateness of transactions not questioned by subordinate staff
- Financial / operational segregation failures and overrides: one individual responsible for purchasing, financial statement review, property accounting, financial reporting to the Head
- Red flags were observed but not acted upon, including performance issues
- Internal store operations was an easy route for asset misappropriation



What can I do?

- Critical analysis of operations, careful placement of controls
- Listen
- Understand Policy
 - OBFS policy on Internal Controls
 - All campus administrators who develop, operate, and supervise financial systems are responsible for creating and implementing control procedures
 - OBFS Section 9 (9.5 specific to reporting wrongdoing)
 - Management employees are responsible for detecting fraudulent activities or misconduct in their areas of responsibility
 - When dishonest or improper activity is detected or suspected, management should determine whether an error or misunderstanding has occurred or whether possible fraud exists
- Contact appropriate authorities
 - University Ethics
 - Office of University Audits
 - University Police
 - Human Resources
 - Legal Counsel

** We all work together **

