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Common Internal Control Weaknesses
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 **