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Library Internal Controls Best Practices and Lessons Learned

Presented by: Joey Jones, CPA



Agenda

- Lessons Learned
- Understanding Internal Controls
- Steps on Writing and Evaluating Internal Control Policies
- JJ Top 5 Controls and top 10 comments
- Best Practices



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Disclaimer

The presenter will be held harmless for any fraud you are able to commit after attending this course.



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\$64,000 Lesson Learned



- Credit card charges
- Altered bank statements
- How client addressed the issue
 - Eliminated the credit card
 - Bank reconciliations are available to board members at monthly meetings
 - Board members sign each check issued



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\$316,000 Lesson Learned

- Payroll clerk wrote additional payroll checks-\$128,000 over 2 years
- Clerk stole fine money \$188,000
- How the deficiency was addressed - Administrator reviews all checks and receives unopened bank statements and performs random checks





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\$369,848 Lesson Learned

- Internal discovery
- Patron fines and fees
- Former clerk-treasurer
- Annual receipts during theft ~\$15k
- Annual receipts after theft ~\$80k
- How Fixed-reconcile receipts to deposits, segregation of duties





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\$3,000,000 Lesson Learned

- Cashed a check and walked out of bank with a box full of cash-twice
- Vault cash short \$2.7 million-dummy account
- How client addressed the issue
 - Segregated duties
 - Limit cash on hand
 - Overage/shortage policy



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Clarified Auditing Standards AU-C 315

- Defines "internal control"
- Describes the objectives and components of internal control
- Explains how an auditor should consider internal control in planning and performing an audit



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What is "Internal Control"?

- A process
- Affected by a client's governing board, management and other personnel
- Designed to provide reasonable assurance of the achievement of certain objectives



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Objectives of Internal Control

- Reliability of financial reporting (**financial reporting**)
- Effectiveness and efficiency of operations (**operational**)
- Compliance with applicable laws and regulations (**compliance**)



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Five Interrelated Components of Internal Controls

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



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"There aren't any icons to click. It's a chalk board."

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Developing Internal Controls and Policies



- 5 step approach
- Use to develop new controls /policies
- Use to evaluate current controls/policies
- Never static



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Developing Internal Controls and Policies



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Developing Internal Controls and Policies

First determine your goals and objectives!

Then:

1. Analyze
2. Assess
3. Implement
4. Communicate
5. Monitor



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Step 1- Analyze

Analyze your control environment

- a. Attitudes
- b. Supervision
- c. Structure



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Step 2- Assess

Assess your Risk

- a. Identify Potential Problems
 - Keep in mind, a moderate loss that is likely to occur presents as much danger as a more serious loss that is less likely to occur.
- b. Identify and analyze current control cycles



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Step 3 Implement

Implement Management Control Activities

- Developing and putting your policy into action
- Decide if the defined system safeguards resources, assures accuracy of information and promotes effectiveness and efficiency



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Step 4- Communicate



Communicate Information

- a. Prepare and distribute the results of the evaluation and any related changes and new policies.
- b. When making changes, discuss the changes with the affected managers, staff and internal auditors (if you have them) to determine if the changes accomplish the control objective. Remember in evaluating alternatives, consider the costs and expected benefits of implementing the control objectives in a cost-effective manner.



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Step 5- Monitor

- a. At a minimum, evaluate your controls and cycles on an annual basis. Remember that risks can crop up rapidly and a well-developed control environment will be cognizant of changes and move to address them.
- b. Try scheduling monitoring on a regular basis, or evaluation will likely be passed up by the emergencies of day to day work.
- c. As part of monitoring, try testing the controls to see if they are still functioning as intended.



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Application Controls

- Application controls are activities directed at achieving control objectives for transaction cycles.
 - Can be done by anyone qualified and assigned to do them.
 - Can be automated (edit checks, automated computations and updates of accumulated data, etc.)
 - Are generally preventive in nature.



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Monitoring Controls

- Management and supervisory activities that determine whether management's objectives are achieved, including whether application or computer controls are working effectively.
 - Are usually done by management/ governing body) or supervisors.
 - Are *generally* detective in nature

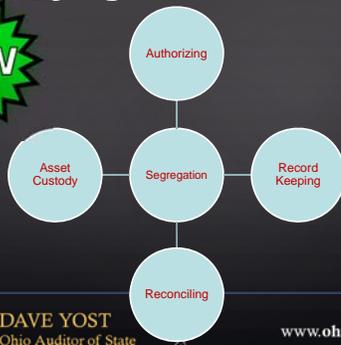


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Segregation of Duties

NEW



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How AOS will evaluate SOD

- Tool/practice aid to systematically evaluate SOD
- Spreadsheet which documents all processes in a given cycle along with the auditee staff individual responsible for completing it
- Primary cycles it will be used for include:
 - Self-assessed Taxes
 - Charges for Services
 - Over the Counter Receipts
 - Payroll Disbursements
 - Non-Payroll Disbursements
 - Capital Assets/Inventory
 - Bank/Investments



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Internal Controls

- Even if you outsource or delegate some processing, you are not absolved from your duties to have controls over that activity
- The best way to accomplish this is to ensure your service organization has a type II SOC 1 audit (SAS 70)



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Typical Service Organization

- Examples of typical SO's:
 - Payroll processing
 - Billing services
 - Self-insurance claim processing
 - Investment purchases (transaction not pre-approved)
- Examples that are not SO's:
 - Bank checking account
 - Investment purchases (entity approves each trans.)
 - Purchased insurance policy
 - Purchase of utility services for your office building



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Audit Requirements

- Auditors must evaluate internal controls and apply audit procedures to significant financial activity, even when that activity is processed by a SO.
- Failure to monitor SO's could affect your entity's audit reports.
- The financial activity processed by your SO is part of your accounting system and financial statements.



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JJ's Top 5 Controls

- Bank Reconciliation
- Financial Statement Review
- Adjustment Approval
- Budgetary Monitoring
- Policy and Procedures Manual



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Note

I have not audited these clients or can attest to the accuracy of these issues-these issues were noted from our executive summary portal based on the information input to capture the results-actual results may vary.

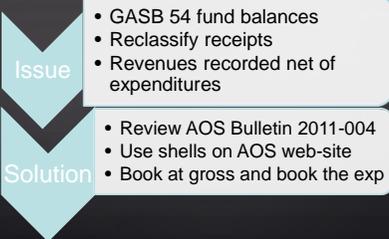


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1- Audit adjustments

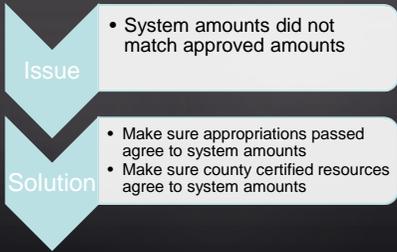


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2-Budgetary accounting system



- System amounts did not match approved amounts

- Make sure appropriations passed agree to system amounts
- Make sure county certified resources agree to system amounts

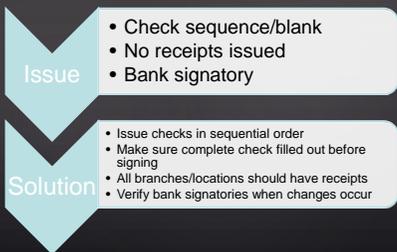


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3-Other internal control items



- Check sequence/blank
- No receipts issued
- Bank signatory

- Issue checks in sequential order
- Make sure complete check filled out before signing
- All branches/locations should have receipts
- Verify bank signatories when changes occur



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4-Cash-Bank Reconciliation



- Bank reconciliations not performed timely
- Some accounts were missing
- Old outstanding items

- Complete monthly reconciliations
- Make sure all accounts included in reconciliation
- Clear outstanding items and have board approve write-offs

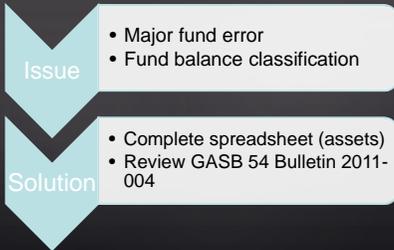


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5-Fund classification deficiency

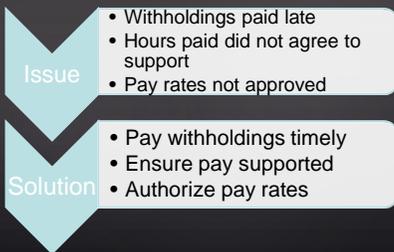


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6-Payroll deficiency

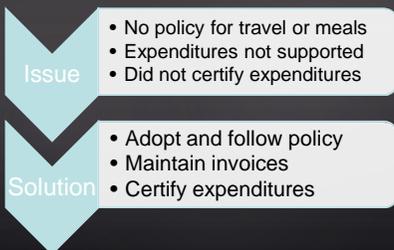


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7-Non payroll deficiency



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8-IT Disaster recovery

Issue

- No disaster recovery plan
- No system back ups
- Back ups stored on-site

Solution

- Adopt and follow policy
- Perform daily back-ups and store off-site



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9-Policy deficiency

Issue

- Credit Card
- Cash collection
- Proper public purpose

Solution

- Adopt and follow credit card policy
- Have overage/shortage policy
- Adopt policy to expend food, gift cards, prizes



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10-Financial monitoring

Issue

- Financial statement errors

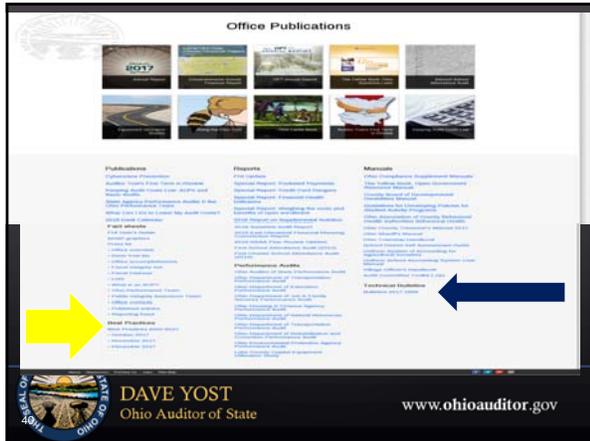
Solution

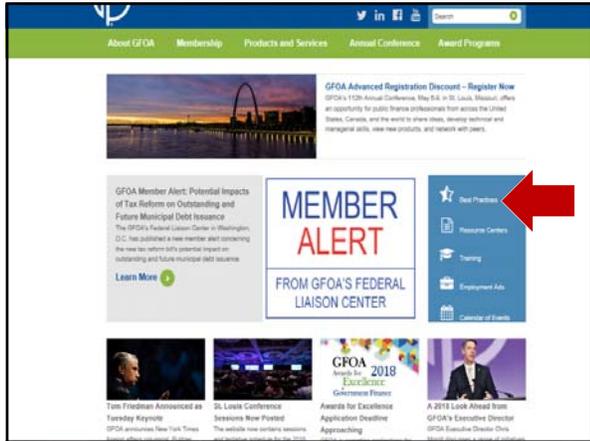
- Have a review process in place
- Monthly report and yearly f/s reviews

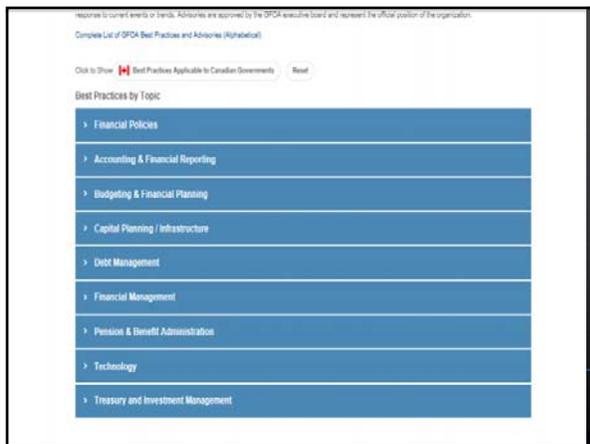


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Always Remember.....
Auditors are here to help!!



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