


Internal Controls



AIM Annual Budget Workshop
Virtual
May 2022

1



State Board of Accounts Contact Information

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2




Areas Covered in This Presentation

- ✓ **Basics of Internal Control**
- ✓ **Internal Control Objectives**
- ✓ **5 Components of Internal Control**
- ✓ **So Now What?**
- ✓ **Best Practices**



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3



Basics of Internal Control

What are Internal Controls

- Internal controls are processes executed by officials and employees that are designed to provide reasonable assurance that the objectives of the political subdivision will be achieved.
- Internal control is a basic element fundamental to the organization, rather than a list of added on tasks.
- Adaptable process that is a means to an end, not an end in itself.
- Dependent on officials & employees for effective implementation
- Achievement of objectives

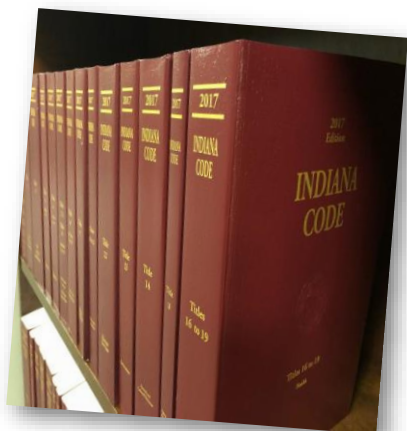


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4



Basics of Internal Control



Statutorily, internal controls . . .

- IC 5-11-1-27 – to promote government accountability & transparency
- IC 5-11-1-27(e) – SBOA defines the acceptable minimum level of standards

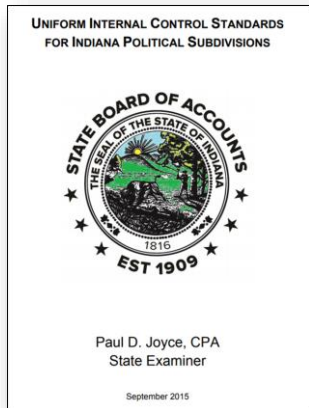


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5



Basics of Internal Control



Political Subdivisions

- General Overview
- Internal Control Standards ←
- Charter Schools
- Cities ←

www.in.gov/sboa/files/UniformInternalControlStandards.pdf



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6

Basics of Internal Control

UNIFORM INTERNAL CONTROL STANDARDS FOR INDIANA POLITICAL SUBDIVISIONS

Paul D. Joyce, CPA
State Examiner

September 2015

Internal Control Standards ▼

Standards

Indiana Code 5-11-1-27(e) provides that through the compliance guidelines authorized under *[C 5-11-1-24]* the state board of accounts shall define the acceptable minimum level of internal control standards 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.

In response, the SBOA developed the Uniform Internal Control Standards for Indiana Political Subdivisions manual, which contains the acceptable minimum level of internal control standards.

Generally Accepted Government Auditing Standards (the "Yellow Book") prohibits the SBOA from prescribing the actual internal control procedures to be used by a political subdivision. However, the manual provides examples and case studies to demonstrate implementation strategies.

Internal Control Policy and Required Certifications

After June 30, 2016 *[C 5-11-1-27(g)]* provides that the legislative body of each political subdivision must adopt the minimum internal control standards as defined by SBOA. Additionally, the legislative body must ensure that personnel receive training concerning the internal control standards and procedures adopted by the political subdivision.

At the time of submission of the Annual Financial Report (AFR) through Gateway, the fiscal officer must certify that the minimum internal control standards have been adopted and that personnel who are not otherwise on leave status have received training regarding these standards and procedures. Instructions for filing will be found as part of the AFR submission.

Apart from the required certification to be filed by the fiscal officer in Gateway during the submission of the 2016 AFR due March 1, 2017 (or August 29, 2017 for Schools), a certification for each elected official, appointee, and employee that meets the definition of personnel in *[C 5-11-1-27(g)]* should be signed as evidence for their individual training. A certification form is provided below and can also be found under the Appendix found in the Uniform Internal Control Standards for Indiana Political Subdivisions manual. These certifications are to be maintained by the political subdivision on-site.

7

Basics of Internal Control

UNIFORM INTERNAL CONTROL STANDARDS FOR INDIANA POLITICAL SUBDIVISIONS

Paul D. Joyce, CPA
State Examiner

September 2015

SECTION ONE

Minimum Level of Internal Control Standards


- Five Components
- Seventeen Principles

SECTION TWO

Approved Training Materials

- Video Presentation
- Examples
- Case Studies

8



Internal Control 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

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9



Internal Control Objectives



Objective identified Controls designed Controls in place Objective achieved

Source: GAO. | GAO-14-704G



10

Components of Internal Control



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Internal Control Components:

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



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11



1. Control Environment

Sets the “tone at the top”, influencing the control consciousness of its people.

Foundation for all other components, providing discipline & structure.



Factors:

- Integrity & ethical values
- Commitment to competence
- Management philosophy & operating style
- Organizational structure
- Assignment of authority & responsibility
- Human resource policies and procedures




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12



2. Risk Assessment

Identification & analysis of relevant risks to achievement of objectives, forming a basis for determining how the risks should be managed.



Risk Assessment




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13



2. Risk Assessment

Objectives must be established prior to the identification of risks to their achievement & to take necessary actions to manage risks



Risk Assessment

Assessment of risk includes:

- Establishing the significance of a risk
- Assessing the likelihood or frequency of the risk occurring
- Consideration of how the risk should be managed



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14



3. Control Activities

Policies & procedures that help ensure mgmt. directives are carried out.

Ensure necessary actions are taken to address risks to achievement of objectives



Control Activities



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15



3. Control Activities

Occur throughout the city/town, at all levels & in all functions.

Includes:

- Segregation of duties
- Approvals
- Authorizations
- Verifications
- Reconciliations
- Reviews of performance



Control Activities



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16



4. Information & Communication

Emphasizes the importance of quality information

City/town internally communicates information

Communicates externally



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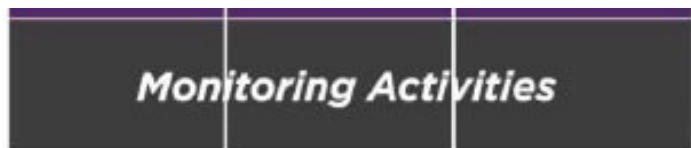
17



5. Monitoring Activities

Ongoing Evaluations – built into various levels of your unit to provide timely information

Separate Evaluations – conducted periodically




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18

Specifics	Reporting	Compliance
Control Environment		
Risk Assessment		
Control Activities		
Information & Communication		
Monitoring Activities		

Components of Internal Control

<https://allthatsaidisred.wordpress.com/2011/12/07/internal-controls-an-overview/>



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 EST. 1909

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19

Specifics	Reporting	Compliance
Control Environment		
Risk Assessment		
Control Activities		
Information & Communication		
Monitoring Activities		

So Now What???


Don't reinvent the wheel

- Identify existing controls and procedures

Where Do We Begin?

Document, document, document

- Write down who does what.
- Make lists



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 EST. 1909

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20



Control Environment
Risk Assessment
Control Activities
Information & Communication
Monitoring Activities

Organizational Structure
Competence
Integrity
Ethics
Commitment to Competence
Communication


Common Areas for Internal Controls

- Bank Reconciliations
- Receipting Process
- Disbursing Process
- Payroll
- Financial Reporting




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21

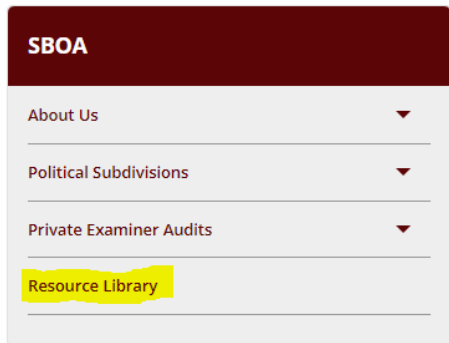


Control Environment
Risk Assessment
Control Activities
Information & Communication
Monitoring Activities

Organizational Structure
Competence
Integrity
Ethics
Commitment to Competence
Communication

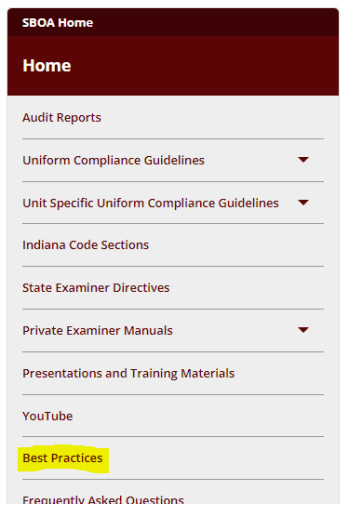
Best Practices

SBOA website has best practices in our Resource Library



SBOA


- About Us
- Political Subdivisions
- Private Examiner Audits
- Resource Library



SBOA Home


Home


- Audit Reports
- Uniform Compliance Guidelines
- Unit Specific Uniform Compliance Guidelines
- Indiana Code Sections
- State Examiner Directives
- Private Examiner Manuals
- Presentations and Training Materials
- YouTube
- Best Practices
- Frequently Asked Questions



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22





BANK ACCOUNT RECONCILEMENTS

A system of internal control may be implemented in many different ways. Because political subdivisions vary in purpose, size and complexity, no single method of internal control is universally applicable. However, the five internal control components should be present and functioning in all political subdivisions.

Questions have been accumulated for all five internal control components. This document includes questions pertaining to various noncommutative issues regarding bank account reconciliations. These questions can be used to assist in designing a proper system of internal control over bank reconciliations that will allow incorrect bank reconciliations to be prevented or detected and corrected. It is not necessary to address all questions in this document. These are only suggestions and ultimately it is up to the unit on how they implement it. The internal control system as a whole has to be designed and implemented appropriately in order to allow errors made on the bank reconciliation to be prevented or detected and corrected in a timely manner.

Control Environment
The questions in this section are divided by questions that pertain to the governing board and management.

Governing Board

	YES	NO
1) Does the governing board oversee the unit's internal control system over the preparation and review of the bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>
1a) Are there written policies documenting internal control procedures over the preparation and review of the bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>
1b) Are those written policies stating the authority and responsibility for the preparation and review of the bank reconciliation within the unit and require bank reconciliations to be performed monthly?	<input type="checkbox"/>	<input type="checkbox"/>
1c) Does the governing board have a complete listing of all bank accounts?	<input type="checkbox"/>	<input type="checkbox"/>

Management

1) What procedures did management put in place for the preparation and review of the bank reconciliation and review of cash and reconciliation balances?	<input type="checkbox"/>	<input type="checkbox"/>
a) Does management assign responsibility, and delegate authority to achieve a correct bank reconciliation and ensure it is prepared monthly?	<input type="checkbox"/>	<input type="checkbox"/>
b) Have all bank accounts been reported to management?	<input type="checkbox"/>	<input type="checkbox"/>
c) Is management willing to adjust the financial statements for misstatements that approach a material amount?	<input type="checkbox"/>	<input type="checkbox"/>

Risk Assessment


	YES	NO
1) Does management identify, analyze and respond to risks regarding the preparation and review of the bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>
a) What areas have been identified regarding the preparation and review of the bank reconciliation that may be exposed to risk?	<input type="checkbox"/>	<input type="checkbox"/>
b) How does management analyze and respond to identified risks? For example, management may accept the risk, not use risk as action, choose to eliminate certain processes to avoid the risk and/or institute proper internal controls.	<input type="checkbox"/>	<input type="checkbox"/>
c) How does management prevent fraud and errors in the accounting records, which are used to compute cash and management balances. For example, are important internal control procedures in place such as approvals, regular preparation or review of reconciliations, review of supporting schedules or reports, etc.?	<input type="checkbox"/>	<input type="checkbox"/>
d) What procedures are in place to ensure that the information reported on the bank reconciliation is correct and reflective of the accounting records and the bank reconciliation is performed monthly?	<input type="checkbox"/>	<input type="checkbox"/>

Control Activities

	YES	NO
1) Is there a system of checks and balances (segregation of duties) to ensure a correct bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>
a) Are responsibilities for reviewing the bank reconciliation segregated from those preparing the bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>
b) Are responsibilities for preparing the bank reconciliation segregated from those involved in receipting and disbursing activities?	<input type="checkbox"/>	<input type="checkbox"/>
c) Are responsibilities for preparing a reconciliation between the receipts ledger and the credits to the bank account segregated from those involved in the receipting process?	<input type="checkbox"/>	<input type="checkbox"/>
d) Are responsibilities for preparing a reconciliation between the disbursements ledger and the debits to the bank account segregated from those involved in the disbursing process?	<input type="checkbox"/>	<input type="checkbox"/>
e) Does management present the bank reconciliation to the governing board for review and approval?	<input type="checkbox"/>	<input type="checkbox"/>
2) Are bank statements received directly by the appropriate level of management or another appropriate person and reviewed prior to routing to the individual who performs the bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>


BANK ACCOUNT RECONCILEMENTS Page 1

Best Practices



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23




BANK ACCOUNT RECONCILEMENTS

Best Practices


Control Activities

	YES	NO
1) Is there a system of checks and balances (segregation of duties) to ensure a correct bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>
a. Are responsibilities for reviewing the bank reconciliation segregated from those preparing the bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>
b. Are responsibilities for preparing the bank reconciliation segregated from those involved in receipting and disbursing activities?	<input type="checkbox"/>	<input type="checkbox"/>
c. Are responsibilities for preparing a reconciliation between the receipts ledger and the credits to the bank account segregated from those involved in the receipting process?	<input type="checkbox"/>	<input type="checkbox"/>
d. Are responsibilities for preparing a reconciliation between the disbursements ledger and the debits to the bank account segregated from those involved in the disbursing process?	<input type="checkbox"/>	<input type="checkbox"/>
2) Does management present the bank reconciliation to the governing board for review and approval?	<input type="checkbox"/>	<input type="checkbox"/>
3) Are bank statements received directly by the appropriate level of management or another appropriate person and reviewed prior to routing to the individual who performs the bank reconciliation?	<input type="checkbox"/>	<input type="checkbox"/>

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24



The diagram shows the COSO Framework with five components: Control Environment, Risk Assessment, Control Activities, Information & Communication, and Monitoring Activities. It also lists the three pillars: Objectives, Reporting, and Compliance, and the three levels: Entity Level, Business Unit, and Component Level.

Best Practices

Bank Reconcilements:

Written Policies – describing controls in place, who performs which function, etc.


Regular preparation of bank reconciliations – performed monthly as required by IC

Review & Approvals – bank reconcilements reviewed by someone outside performing the actual reconciliation and acknowledging approval


Method of Review documented – evidence such as a signature, initials, email, etc. that can be retained for audit.

Communicating – are the established procedures communicated to officials and employees involved in the process

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25



The diagram shows the COSO Framework with five components: Control Environment, Risk Assessment, Control Activities, Information & Communication, and Monitoring Activities. It also lists the three pillars: Objectives, Reporting, and Compliance, and the three levels: Entity Level, Business Unit, and Component Level.

Best Practices


Schedule of Expenditures of Federal Awards (SEFA):

Written Policies – describing controls in place, who performs which function, etc.


Review & Approvals – SEFA reviewed by someone outside the preparation process acknowledging approval. Procedures should exist to ensure the amounts reported are accurate

Method of Review documented – evidence such as a signature, initials, email, etc. that can be retained for audit.


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26


 <p>Control Environment Risk Assessment Control Activities Information & Communication Monitoring Activities</p>	<h2>Common Internal Control Findings</h2>
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- ✓ Did not separate incompatible activities related to receipts, disbursements, & payroll
- ✓ Had not established a review or approval process over bank reconciliations or financial reporting
- ✓ There was no evidence or an oversight, review, or approval process




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27


 <p>Control Environment Risk Assessment Control Activities Information & Communication Monitoring Activities</p>	<h2>Depositing Collections</h2>
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Controls over Depositing

- City/Town Fees
- Utility Collections
- Various Other Fees
- State & Federal Distributions
- Donations



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28

Objectives	Reporting	Compliance
Control Environment		
Risk Assessment		
Control Activities		
Information & Communication		
Monitoring Activities		


Payroll

Controls over Payroll

- Compensation Paid
- Withholdings
- Direct Deposits / Changes to
- Payroll Service Providers



<https://www.entrepreneur.com/article/239823>



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29

Objectives	Reporting	Compliance
Control Environment		
Risk Assessment		
Control Activities		
Information & Communication		
Monitoring Activities		

Unauthorized Transactions


Controls over Unauthorized Transactions

- Utility Bill Adjustments
- Credit Card Purchases
- Electronic Funds Transfers



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30




The diagram shows the COSO Framework with five components: Control Environment, Risk Assessment, Control Activities, Information & Communication, and Monitoring Activities. The top row lists the three pillars: Objectives, Reporting, and Compliance. The right side lists the five components: Control Environment, Risk Assessment, Control Activities, Information & Communication, and Monitoring Activities.

Other Important Areas


Computer Security

- Physical security
- Log in restrictions
- Remote use
- Offsite storage of data
- Scams

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31




The diagram shows the COSO Framework with five components: Control Environment, Risk Assessment, Control Activities, Information & Communication, and Monitoring Activities. The top row lists the three pillars: Objectives, Reporting, and Compliance. The right side lists the five components: Control Environment, Risk Assessment, Control Activities, Information & Communication, and Monitoring Activities.

What You Can Do Now

- **Review you last audit report**
- **Review the Internal Control Manual**
- **Use Best Practices**
- **Evaluate procedures**
- **Address all 5 components of internal control**
- **Put controls and procedures in writing**
- **Update procedures as necessary**

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32

A presentation slide with a dark blue header and footer. The main content area is white. In the center, a cartoon man in a suit is pointing with a stick to a flip chart that says "Q&A". The "Q" is black and the "&A" is red. In the bottom right corner, there is a circular logo for the State Board of Accountants, featuring a torch and the text "STATE BOARD OF ACCOUNTANTS" and "EST. 1909".

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33

A blue banner with a white silhouette of the Indiana State Capitol dome on the left and the State Board of Accountants logo on the right. The text "Contact Info" is centered in white. Below the banner, the name and title of Todd Caldwell are listed, followed by his email and phone number.

Contact Info

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34