

Internal Controls

2023 Annual Treasurers Conference
Indiana State Board of Accounts

The logo of the Indiana State Board of Accounts is circular, featuring a central torch with rays emanating from it. The words "STATE BOARD OF ACCOUNTS" are written around the top inner edge of the circle, and "INDIANA" is written above the torch. At the bottom, it says "EST. 1909". There are stars around the inner edge of the circle.

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What are Internal Controls?

Why do we need them?

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Internal Control - Definition

Internal control is the process by which management structures an organization to provide assurance that an entity operates effectively and efficiently, has reliable financial reporting system and complies with applicable laws and regulations.

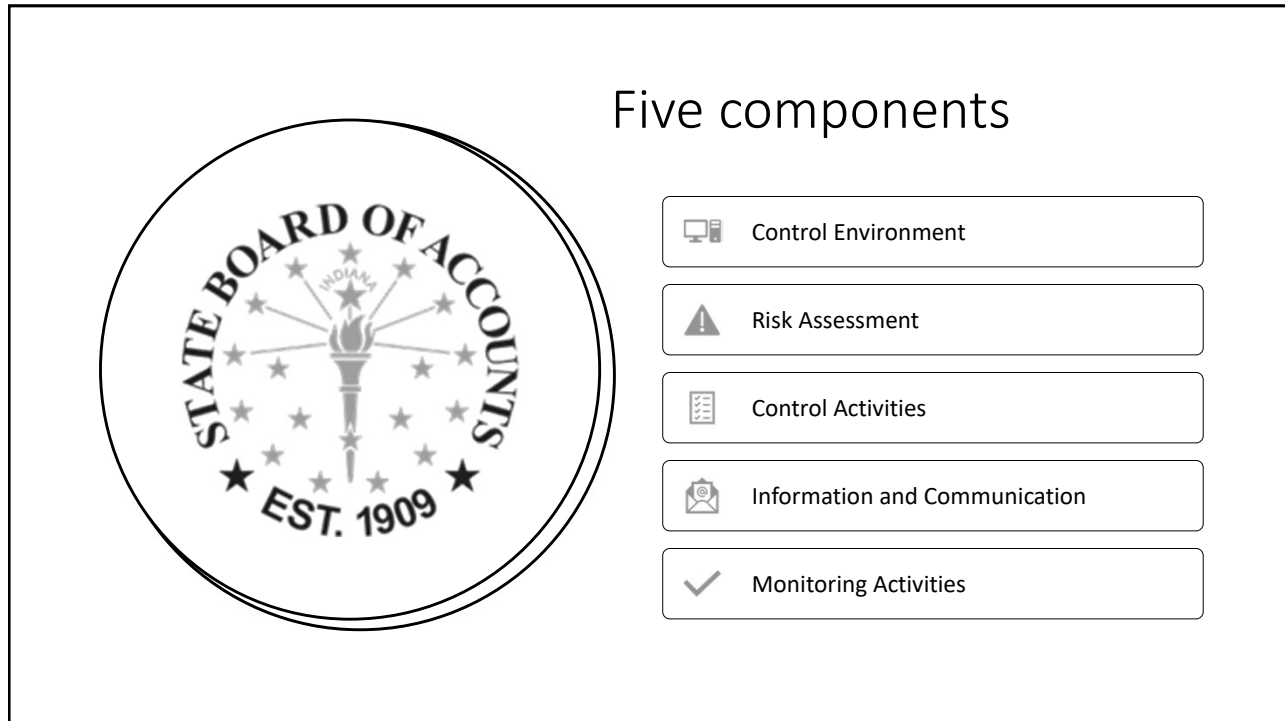
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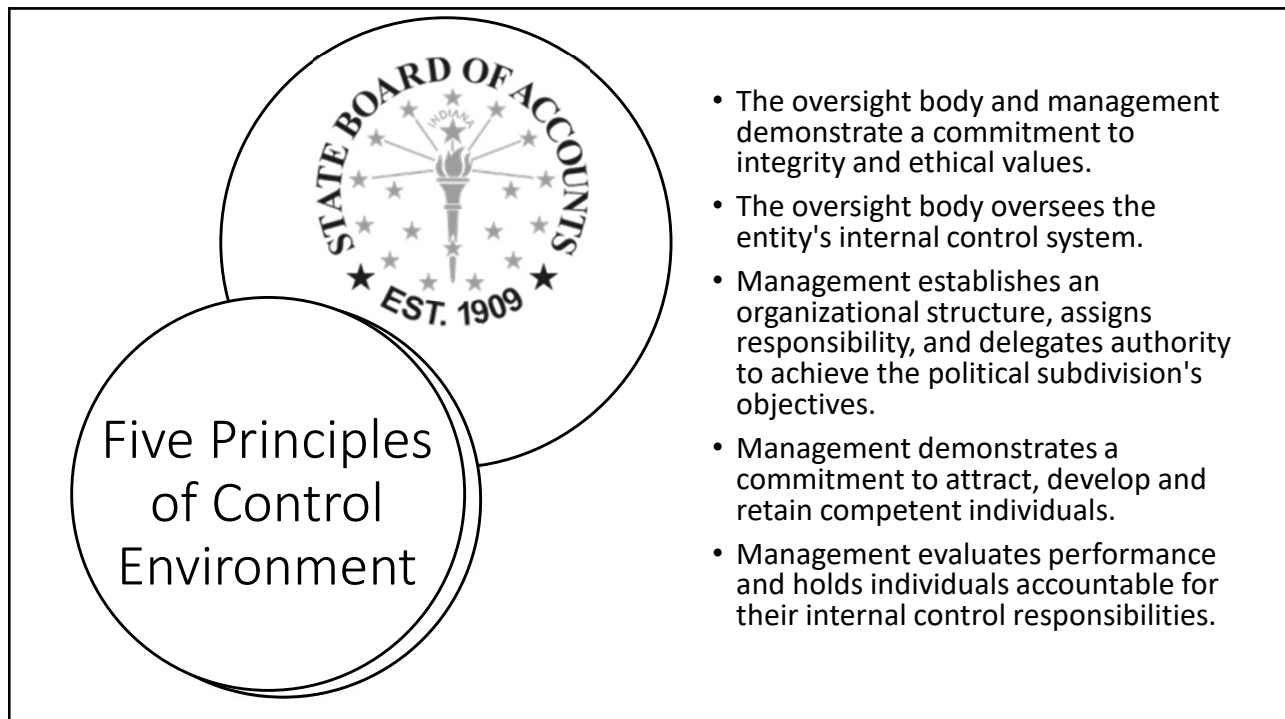
Internal Control – Purpose

To combat fraud and mistakes by preventing opportunity, detecting fraud, errors, and omissions.

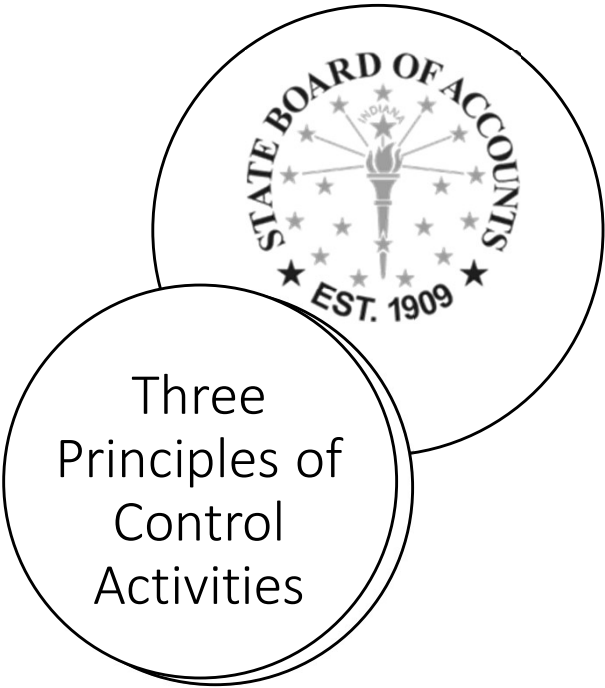
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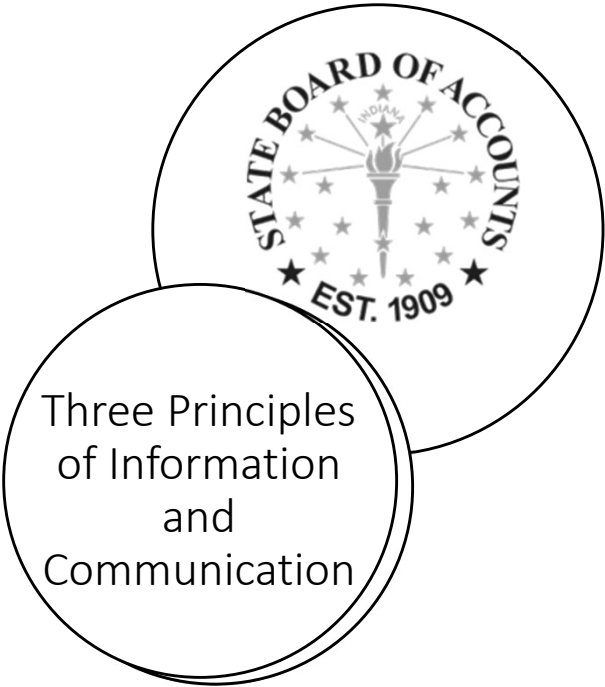
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The diagram features two overlapping circles. The upper circle contains the official seal of the State Board of Accounts, which includes a torch, the text 'STATE BOARD OF ACCOUNTS', and 'EST. 1909'. The lower circle contains the text 'Three Principles of Control Activities'.

- Management designs control activities to achieve objectives and respond to risks.
- Management designs the political subdivision's information system and related control activities to achieve objectives and respond to risks.
- Management implements control activities through policies.

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The diagram features two overlapping circles. The upper circle contains the official seal of the State Board of Accounts, which includes a torch, the text 'STATE BOARD OF ACCOUNTS', and 'EST. 1909'. The lower circle contains the text 'Three Principles of Information and Communication'.

- Management uses quality information to achieve the political subdivision's objectives.
- Management internally communicates the necessary quality information to achieve the political subdivision's objectives.
- Management externally communicates the necessary quality information to achieve the entity's objectives.

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What is risk?

What is risk assessment?




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Risk - Definition

The possibility that an event will occur and adversely affect the achievement of objectives.



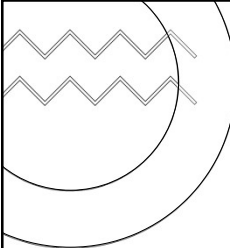
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Risk Assessment – Definition

The process used to identify and assess internal and external risks to the achievement of objectives, and then establish risk tolerances.


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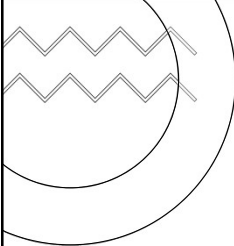
Management defines objectives clearly to enable the identification of risks and defines risk tolerances.

Objectives defined in clear terms will include information such as:

- who is to achieve the objective,
- how the objective will be achieved, and
- when the objective will be achieved.




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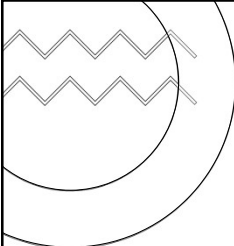
Management identifies, analyzes, and responds to risk related to achieving the defined objectives.

Management analyzes identified risk to estimate the effect of the risk on achieving the defined objectives at the entity level and transaction level. For example,

- How likely is the risk to occur?
- How will it impact the objective?
- Is the risk based on complex or unusual transactions?
- Is the risk based on fraud?




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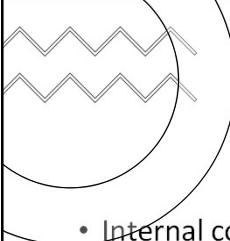


Management considers the potential for fraud when identifying, analyzing, and responding to risks.

- The types of fraud which could impact the achievement of objectives include fraudulent financial reporting, misappropriation of assets, and corruption.
- As a part of this analysis, fraud risk factors are identified: pressure, opportunity, and rationalization.




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Management identifies, analyzes, and responds to significant changes that could impact the internal control system.

- Internal control is a process, and part of that process is the responsibility for management to be **continually aware of changes**, both external and internal, that could affect the achievement of the political subdivision's objectives.
- Those changes should be analyzed for both their immediate effect and for any future impact.
- Management would then determine any modifications needed in the internal control process to adapt to these changes.



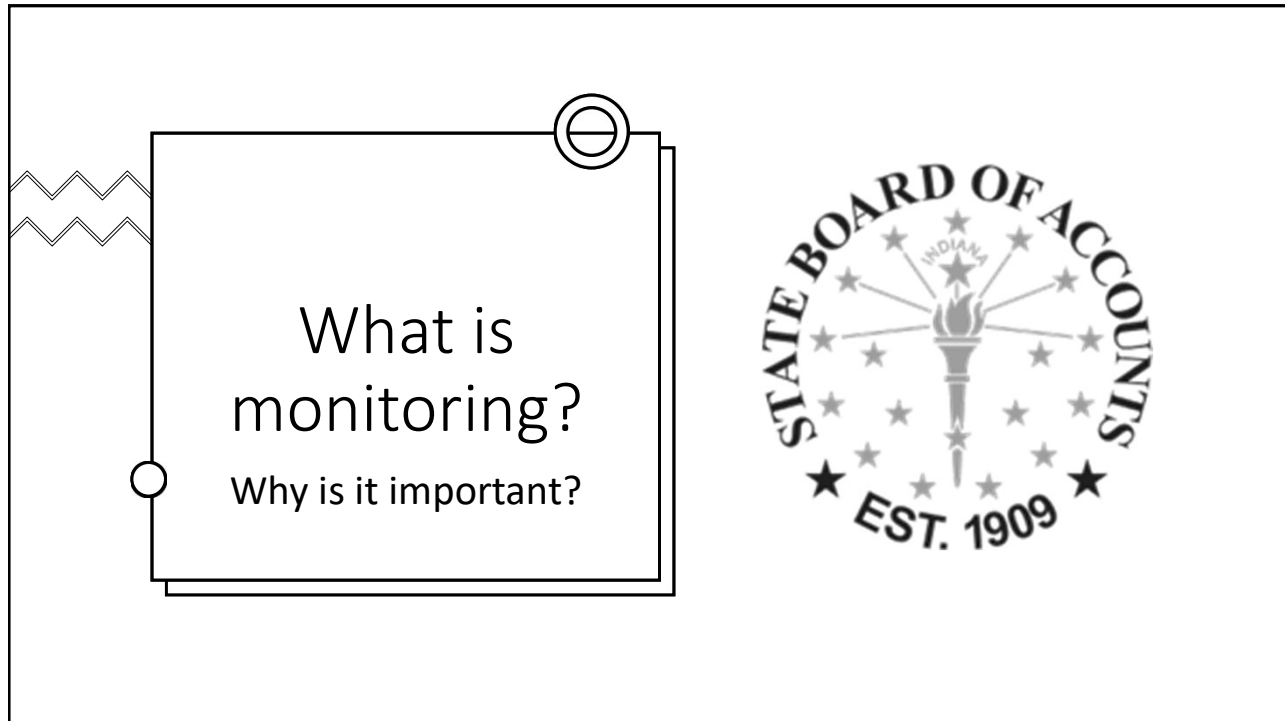
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Summary of Risk Assessment

- SET YOUR GOALS
- IDENTIFY RISKS THAT COULD PREVENT YOU FROM REACHING THE GOALS
- RISK ANALYSIS
- FORMULATE A PLAN TO ADDRESS THOSE RISKS
- DETERMINE YOUR RISK TOLERANCE

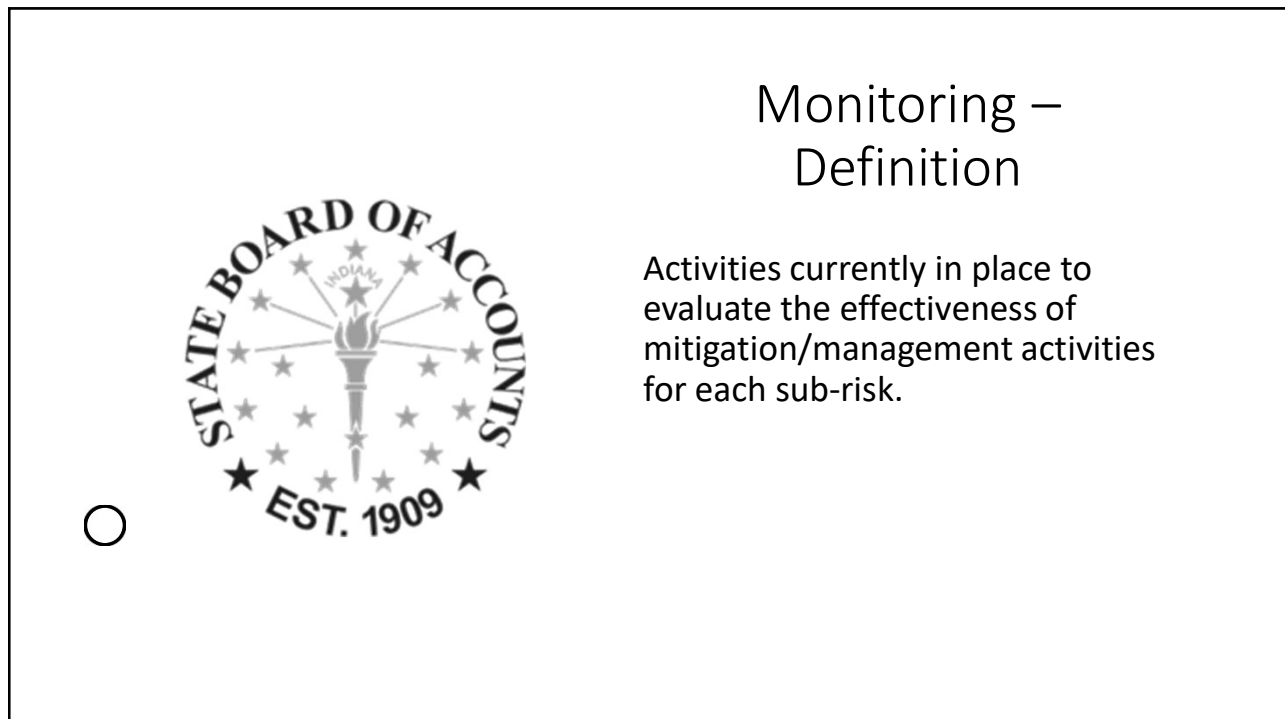
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What is monitoring?
Why is it important?

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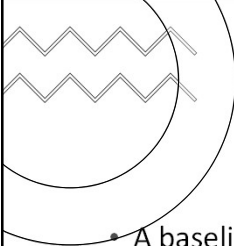


Monitoring –
Definition

Activities currently in place to evaluate the effectiveness of mitigation/management activities for each sub-risk.


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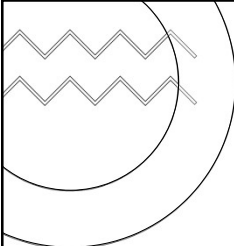


Management establishes and operates monitoring activities to monitor the internal control system and evaluate the results.

- A baseline of the current state of the internal control system is compared against the original design of the internal control system. The baseline consists of issues and deficiencies identified in the internal control system.
- The results of the monitoring process are evaluated and documented. Potential changes to the internal control system are identified.
- Control and monitoring activities may be the same, but it is the intent of the activity that distinguishes which component the activity is supporting.




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Management remediates identified internal control deficiencies on a timely basis.





- Management establishes a mechanism for personnel to report internal control issues identified while performing their responsibilities. These issues are documented and evaluated on a timely basis.
- Management remediates identified issues. Corrective actions include resolution of audit findings.




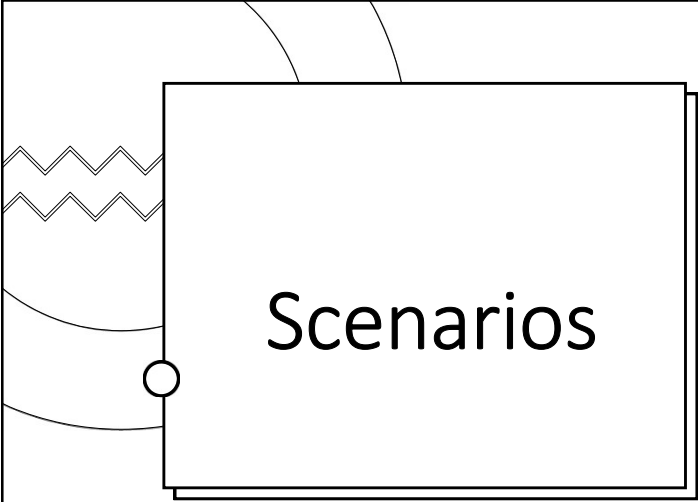
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Summary of Monitoring

-  Assess the quality of performance over time
-  Ensure that audit findings and results are promptly resolved
-  Ensure that the results of internal reviews are promptly resolved
-  Should be ongoing monitoring and separate evaluations

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Contact Us

**Government Technical
Assistance and Compliance
Directors**

Lori Rogers
Ricci Hofherr
Staci Byrns

counties@sboa.in.gov

317-232-2512