

# Internal Control FMCs

- FMC 6.1 Internal Control Standards
- FMC 6.2 Agency Risk Assessment
- FMC 6.3 Internal Audit



# FMC 6.1 Internal Control Standards

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Requires all agencies to establish effective system of internal controls.

# FMC 6.1 Internal Control Standards - Background

Effective systems of internal control provide the foundation upon which a structure of public accountability must be built. Active oversight processes, including regular and ongoing monitoring processes, for the prevention and early detection of fraud and errors in program administration are vital to public confidence and the appropriate and efficient use of public resources.



# FMC 6.1 Internal Control Standards - Function

- The FMCs **do** establish a framework for effective internal control
- The FMCs **do not** prescribe a one-size-fits-all model of specific controls
- An agency's development of specific controls is a function of management judgment based on factors unique to the agency



# FMC 6.1 Internal Control Standards - Definitions

## Definitions:

- **Control environment** means the foundation for an internal control system that provides the discipline and structure to help a State agency achieve its objectives.
- **Risk assessment** means an assessment of the risks facing the State agency as it seeks to achieve its objectives and provides the basis for developing appropriate risk responses.
- **Control activities** means the actions management establishes through policies and procedures to achieve objectives and respond to risks in the internal control system.
- **Information and communication** means the quality of vital information used and communicated to achieve the State agency's objectives.
- **Monitoring** means the activities management establishes and operates to assess the quality of performance over time and promptly resolve the findings of audits and other reviews.



# FMC 6.1 Internal Control Standards

## - Purpose

- Resources used efficiently and in compliance with laws
- Safeguard transactions
- Financial transactions recorded and reports are accurate
- Management of funds held outside the state



# FMC 6.1 Internal Control Standards – Objectives of Designing Controls

- Transactions are authorized
- Accounting records are properly designed
- Assets are secured, recorded and reconciled
- Duties are segregated
- Financial data is analyzed
- Activities are monitored
- Documents are preserved
- Cost benefit analysis of cost controls



## FMC 6.1 Internal Control Standards – Minimum Requirements

- Segregation of duties
- Limit access to assets
- Policies and procedures that provide compliance with laws
- Qualified staff
- Internal review





# FMC 6.1 Internal Control Standards – Responsibility of Management

## Agency Heads:

- Responsible for establishing, implementing and maintaining system of internal controls.
- Documenting internal controls
- Communicating requirements to staff
- Ensure staff are trained on internal controls

## Management:

- Assess and strengthen internal controls to minimize fraud, abuse and waste.



## FMC 6.1 Internal Control Standards – Evaluation and Monitoring

- Agencies must evaluate internal controls on a regular basis.
- Train new and existing staff on internal controls.



# FMC 6.1 Internal Control Standards – Deliverables

- Agency Head submits certification (form in the FMC) with budget submission that states:
  - Agency's internal controls comply with FMC 6.1
  - Personnel are trained on internal controls
  - No material weaknesses or significant deficient have been identified
- If a State agency needs to submit a corrective action plan for any SBOA or federal audit findings, the State agency must submit the corrective action plan to their budget analyst for approval by OMB and State Budget Agency (SBA) before submission to SBOA or the federal entity.





Questions

## FMC 6.2 Agency Risk Assessments

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Requires all agencies to conduct a formal risk assessment.

# FMC 6.2 Agency Risk Assessment

Effective July 1, 2022, all State agencies must conduct an annual formal risk assessment that:

- Evaluates the probability of occurrence and the likely effect of financial, managerial, compliance, and reputational risks and of risks related to the use of information technology; and
- Ranks risks according to the probability of occurrence and likely effect of the risks evaluated



# FMC 6.2 Agency Risk Assessment - Definitions

## Definitions:

**Risk** is the possibility that an event will occur and adversely affect the achievement of objectives.

**Risk assessment** is the process used to identify and assess internal and external risks to the achievement of objectives, and then establish risk tolerances. Each identified risk is evaluated in terms of its impact and likelihood of occurrence. Overall, risk assessment is the basis for determining how risk will be managed.



# FMC 6.2 Agency Risk Assessment - Required Steps

- Agency management defines objectives clearly to enable the identification of risks and defines risk tolerances.
- Agency management identifies, analyzes and responds to risk related to achieving the defined objectives.
- Agency management considers the potential for fraud when identifying, analyzing and responding to risks.
- Agency management identifies, analyzes, and responds to significant changes that could impact the internal control system.





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# FMC 6.2 Agency Risk Assessment - Agency Objectives

Operations - Effectiveness and efficiency of operations.

Reporting – Reliability of reporting for internal and external use.

Compliance – Compliance with applicable laws and regulations.



# FMC 6.2 Agency Risk Assessment

- Identify
- Analyze
- Respond



# FMC 6.2 Agency Risk Assessment

## - Consideration of Fraudulent Activities

- Agency must report misappropriation of fund to OMB, SBOA and the Inspector General or Prosecuting attorney.
- Agencies must report material variances, losses, shortages, or thefts to OMB and SBOA. Agencies should reference SBOA's Examiner Director 2015-6, or its replacement, regarding the standards for determining materiality.



# FMC 6.2 Agency Risk Assessment

## - Deliverables

The State agency shall submit annual risk assessment to the Director of OMB by September 1 of each even-numbered year.

Must include:

- 1) The top three risks identified by the agency along with proposed plans to mitigate or eliminate each risk;
- 2) Any audit or review findings from SBOA, federal agencies, or other internal or outside auditors received during the preceding state fiscal year along with proposed plans to resolve each finding;
- 3) A progress report on the resolution of audit findings and top risks previously reported to OMB under this FMC.





Questions

# FMC 6.3 Internal Audit

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Effective date: July 1, 2023

Applies to a State agency that has:

- Annual operating budget > \$10 million
- More than 100 FTEs; or
- Receives and processes more than \$10 million in cash in a FY

# FMC 6.3 Internal Audit

## - Requirements

- Audit plan
- Periodic audits of major systems and controls
- Sample testing:
  - Revenue and expenditure transactions
  - Procurement, contract and grants
  - Federal grants
- Review data processing systems





# FMC 6.3 Internal Audit

## - Standards

Must conform to:

- Standards for the Professional Practice of Internal Auditing,
- Code of Ethics contained in the Professional Practices Framework as promulgated by the Institute of Internal Auditors (IIA), and
- Generally accepted government auditing standards.



## FMC 6.3 Internal Audit

### - Requirements for Agency Internal Audit

- Head of internal audit has direct or dotted line reporting to the agency head or agency audit committee approved by OMB.
- The head of the internal audit function has free and unrestricted access to the agency's senior management and any outside auditors for the agency.
- Internal audit personnel must be free of all operational and management responsibilities that would impair the auditor's ability to review independently all aspects of the State agency's operation.



## FMC 6.3 Internal Audit

### - Requirements for Agency Internal Audit

- The internal audit function is granted authority for full, free, and unrestricted access to any and all records, physical properties, and personnel relevant to any function under review. All employees of the State agency are requested to assist internal audit in fulfilling its audit, review and consulting activities.
- To permit maintenance of an independent and objective mental attitude necessary in rendering reports, all internal audit activities will remain free of influence by any element in the organization. This freedom from influence includes matters of audit selection, scope, procedures, frequency, timing, or report content.



# FMC 6.3 Internal Audit

## - Deliverables

- Annual report due September 1
- Agencies should evaluate staffing needs and submit a change package with 2023 biennial budget submission.





Questions