A Brief Presentation on Internal Control

Board of Commissioners

Working Session

April 22, 2010

Internal Control - Overview

- What is it?
- Extent of it
- Limitations of it
- Responsibility for it:
 - The governing body's responsibilities
 - Management's responsibilities

- 5 components of it (including examples from County):
 - The control environment
 - Risk assessment and monitoring
 - Control activities
 - Information and communication
 - Monitoring
- Summary

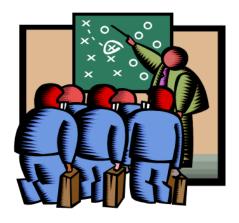
What is Internal Control?

The processes

developed by an organization

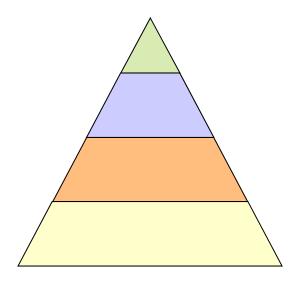
to govern itself

so that it can meet its objectives



Extent of Internal Control

- Internal control applies to:
 - the organization as a whole
 - every operating division of the organization
 - every function performed by the organization
 - every employee in the organization



Limitations of Internal Control

- <u>Reasonable</u> assurance, not <u>absolute</u> assurance
 - too much internal control = red tape and bureaucracy
- Must be balanced by the cost of the control
 - every control has a cost associated with it
- Can be circumvented by collusion of two or more people
- Can be overridden by management

Responsibility for Internal Control

□ The governing body is *ultimately* responsible

Management is <u>primarily</u> responsible

- The independent auditors only "gain an understanding" of internal controls
 - in order to determine the nature, timing and extent of their auditing procedures

Governing Body

- The governing body's responsibilities:
 - Overseeing:
 - the strategic direction of the organization
 - obligations related to the accountability of the organization
 - auditor communications, federal and state inquiries, etc.
 - management's fulfillment of its responsibilities



Management

- Management's responsibilities:
 - To operate the organization effectively and efficiently
 - To comply with applicable laws and regulations
 - 3. To have reliable financial reporting
 - 4. To identify and address the risks that the organization faces that threaten the achievement of the above
- Internal controls are the framework that management establishes to help it to meet these responsibilities
- Each County department has internal controls in place to help it satisfy the above responsibilities in the particular environment in which they operate

Management

- Management is responsible for all aspects of internal control:
 - design
 - implementation
 - monitoring
 - reporting



Components of Internal Control

1st Component – The Control Environment

The Control Environment in the Organization

- The foundation for all other components of internal control
- "The tone at the top"
- Communication and enforcement of integrity and ethical values
- Commitment to competence in employee performance



The Control Environment in the Organization

- Participation by governing body (those charged with governance)
 - their independence from management
 - their experience and stature
 - the extent of their involvement (including asking difficult questions of management)
 - their interaction with auditors
- Management's philosophy and operating style including their approach to taking and managing risks
- Human resource policies and practices recruitment, hiring, orientation, evaluation, promotion, compensation, and remedial actions

Washtenaw County Application

- Human Resources policies on employee honesty, competence in work,
 and proper conduct as well as disciplinary action for failure to comply
- Employee work plans and annual evaluation
- Bi-monthly Board of Commissioner meetings and working sessions when needed
- Chair of the Board meets with auditor at the end of the annual audit
- Auditor presentation of CAFR at BOC meeting



Components of Internal Control

2nd Component – Risk Assessment and Monitoring

Risk Assessment and Monitoring

- Identifying the risks to the organization that could hinder the accomplishment of its objectives
- Establishing and implementing a plan to address those risks
- Continually evaluating the risk environment to take into account changing internal and external conditions



Washtenaw County Application

- The County operates 35 different businesses many with potentially significant risks:
 - Jail
 - Road patrol
 - Courts / Friend of the Court
 - Public health
 - Facilities staff working on County buildings
 - Head Start working with children
 - CSTS transporting clients
 - Parks & Recreation employees working with heavy machinery
 - Fleet vehicles driven by County employees

Risk Management

- The County's Risk Management department is currently conducting an extensive assessment of risk in County departments:
 - identifying exposures to loss
 - on-site visits, risk surveys, review of contract provisions
 - analyzing the likelihood of loss
 - frequency of loss, severity of loss, potential financial impact on County
 - selecting the best techniques to handle any losses
 - insurance coverage, contract provisions, leasing

Risk Management

- implementing the techniques selected
- monitoring the losses that occur
- Parks and Recreation, Facilities, CSTS, Sheriff's Office, Courts,
 and Administration will be reviewed first



Components of Internal Control

3rd Component – Control Activities

Control Activities

- The policies and procedures that are put in place:
 - to ensure that management's directives are carried out
 - to limit the risks that have been identified
 - Supervisory approvals, separation of duties, reconciliations, building security, computer system security and password restricted access to computer programs (such as JDEdwards)



Washtenaw County Application

- County policies and procedures:
 - the County has approx. 260 policies and procedures on our website dealing with many aspects of conducting business in our organization (formerly volumes I, II and III)
 - BOC, budget, buildings, claims, emergencies, full faith and credit, human resources, IT, internet, investments, procurement, security, travel, etc.

Washtenaw County Application

- Business rules published in the Budget book:
 - one stop information source on how to conduct business with central administration departments
 - Administration, Corporation Counsel, Facilities, Budget, Accounting, Payables, Payroll, Purchasing, HR, IT, Risk Management



Specific Internal Controls

- Examples of internal controls related to County property:
 - building access and security
 - County ID tags placed on equipment
- Examples of internal controls related to County computer systems:
 - user ID and log on required to gain access
 - County firewall to protect against viruses
 - access restricted to JDEdwards to modules an employee has been trained to use and are needed for his/her work



Specific Internal Controls

- Examples of internal controls related to <u>financial</u> matters:
 - 2 signatures required on invoices prior to payment
 - fiscal staff prepare journal entries, supervisor approves and posts them to financial system
 - fiscal staff who receipt in money do not also account for it. Money often counted by two fiscal staff
 - monies received over the counter/through the mail are taken to the bank by armored car service
 - two employees involved in wire transfer transactions
 - employee prepares timesheet, supervisor approves it
 - employee pay rates entered by HR, payment made by Payroll



Components of Internal Control

4th Component – Information and Communication

Information and Communication

- Disseminating pertinent information promptly to enable employees to carry out their responsibilities
- May be operational, financial or compliance related information that is needed to run and control the organization
- Communication must flow down, across and up the organization to be effective
- All employees need to receive a clear message from top management that internal control responsibilities must be taken seriously

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- Board of Commissioner meetings
- Monthly budget projections
- Quarterly budget updates to the Board
- eCentral articles by County Administrator
- Meetings:
 - Department Head
 - □ Group of 180
 - Labor/Management
 - Town Hall
 - Payroll, Payables, Purchasing Liaisons



Components of Internal Control

5th Component - Monitoring

Monitoring

Assessing whether internal controls are being followed and recommending corrective action when necessary



Washtenaw County Application

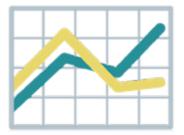
- Yearly review of several locations where cash is taken in over the counter
- Annual audit
- Periodic review of petty cash balances in departments
- Comparison of budget versus actual throughout the year
- Review of worker's compensation claims
- Review of self insurance losses due to lawsuits and settlements
- Review of County vehicle accidents

Summary



Summary

- Internal control is vital to help the County meet its objectives
- County management (Administration and each department) is responsible for designing, implementing, monitoring and reporting on internal control
 - this is an ongoing process that must be revisited continuously!
- Each County department has many internal controls in place to help it:
 - operate effectively and efficiently
 - comply with applicable federal, state and local laws and regulations
 - produce reliable financial information
 - identify and address the risks that it faces in its operations



Questions?

