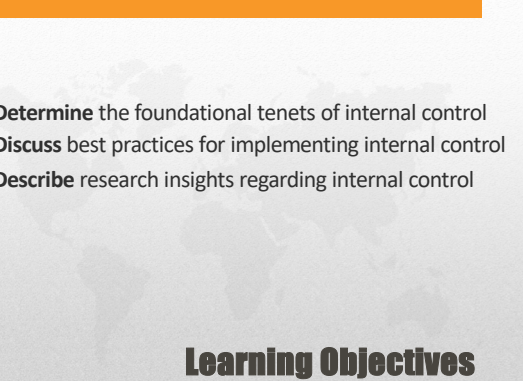





Best Practices
Internal Control


Inter American Division
3rd Annual SeLD Conference
Miami, Florida | July 15-17, 2019



- **Determine** the foundational tenets of internal control
- **Discuss** best practices for implementing internal control
- **Describe** research insights regarding internal control

Learning Objectives






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INTERNAL CONTROL 101

Designed to provide reasonable assurance that an organization has achieved the objectives of:


- **producing** reliable financial reports
- **performing** effectively and efficiently in its operations
- **complying** with applicable laws and regulations

Definition of Internal Control



A deficiency in internal control exists when the **design** or **operation** of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis

Definition of an Internal Control Deficiency




Design

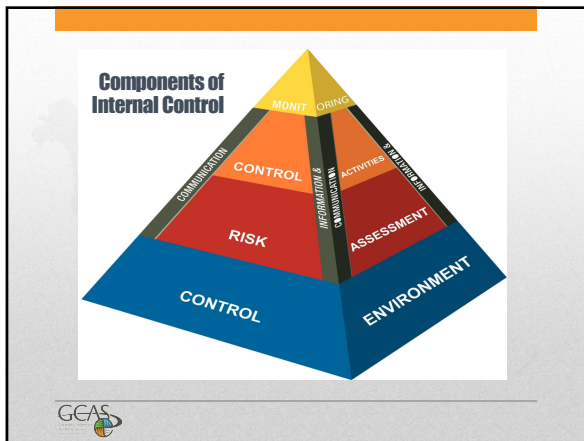
- (a) a control necessary to meet the control objective is missing
- (b) an existing control is not properly designed so that, even if the control operates as designed, the control objective would not be met

Operation

- (a) a properly designed control does not operate as designed
- (b) the person performing the control does not possess the necessary authority or competence to perform the control effectively

Types of Internal Control Deficiencies




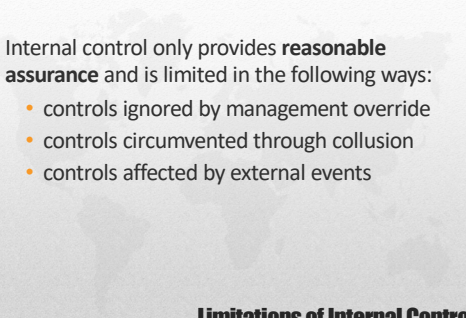


COSO's 17 principles of internal control – summarized

Control environment	Risk assessment	Control activities	Information and communication	Monitoring activities
1 Demonstrates commitment to integrity and ethical values	6 Specifies suitable objectives	10 Selects and develops control activities	13 Uses relevant information	16 Conducts ongoing and/or separate evaluations
2 Exercises oversight responsibilities	7 Identifies and analyzes risk	11 Selects and develops general controls over technology	14 Communicates internally	17 Evaluates and communicates deficiencies
3 Establishes structure, authority, and responsibility	8 Assesses fraud risk	12 Deploys through policies and procedures	15 Communicates externally	
4 Demonstrates commitment to competence	9 Identifies and analyzes significant change			
5 Enforces accountability				

Source: Audit Committee Brief, March 2014, Deloitte Development Corporation. All rights reserved.






Internal control only provides **reasonable assurance** and is limited in the following ways:


- controls ignored by management override
- controls circumvented through collusion
- controls affected by external events

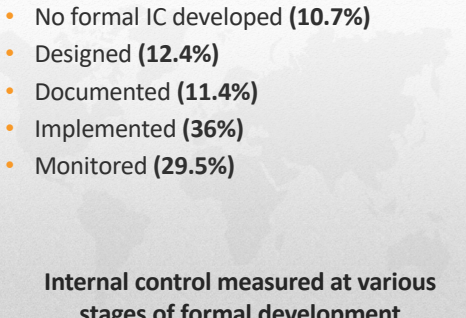
Limitations of Internal Control






RESEARCH INSIGHTS


Seventh-day
Adventist Church



- No formal IC developed **(10.7%)**
- Designed **(12.4%)**
- Documented **(11.4%)**
- Implemented **(36%)**
- Monitored **(29.5%)**

Internal control measured at various stages of formal development



- Not at all **(6.8%)**
- Slightly **(16.1%)**
- Moderately **(35.2%)**
- Very **(34.8%)**
- Extremely **(7.1%)**

Involvement of governing board in the development of the internal control



- Perform periodic risk assessments **(32.1%)**
- Use information from GCAS or external auditors' report **(49.3%)**
- Use information from internal auditor's report **(14.4%)**
- None **(4.2%)**

Mechanisms used by organizations to identify and address risks




- Prepare a written response to be shared with auditor and audit committee **(7.8%)**
- Correct deficiency before next audit engagement **(26.2%)**
- Both of the above **(65.1%)**
- Ignore reported deficiency **(.9%)**

Response to internal control deficiencies identified and reported by the auditor



- Lack of segregation of duties
- Lack of evaluation of collectability of accounts receivable
- Lack of adequate reconciliation procedures for inter-organizational accounts
- Lack of authorization of transactions
- Lack of effective oversight of budget and financial reporting
- Lack of correction of accounting errors or deficiencies

Most Frequent Internal Control Deficiencies








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**Governance takes responsibility
for internal control**

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- Determining mission and strategic direction
- Maintaining Seventh-day Adventist ethos and identity of the organization
- **Establishing/implementing key policies and strategies**
- Selecting, developing, and evaluating key leaders
- Ensuring adequate financial resources
- Enhancing the organization's reputation
- **Providing adequate risk management**
- Assessing performance against mission
- Improving board/executive committee performance


Range of Governance Responsibilities






Organization considers size and complexity in designing internal control

Best Practice






The same person should not:

- **Initiate** the transaction
- **Authorize** the transaction
- **Record** the transaction
- **Have** custody of the asset

Internal Control Design Alert





**Organization identifies
and addresses risks**


Best Practice



- What could go wrong?
- Where are we most vulnerable?
- How could someone steal from a department?
- On what do we spend our most money?
- Do we have new personnel?
- Do we have new technology?

- How could we fail?
- What assets do we need to protect?
- On what information do we most rely?
- How do we collect our revenue?
- What is our past performance?
- How can someone bypass our internal control?

Risk Questions





**Organization uses risk to link
objective and internal control**

Objective

➔

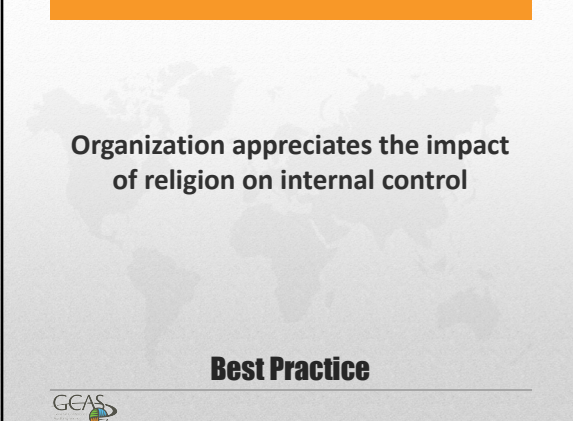
Risk

➔

Control


Best Practice





Organization appreciates the impact of religion on internal control

Best Practice




Positive

Religiosity and risk aversion does affect corporate behavior increasing the likelihood for appropriate internal control to be designed and operating effectively
(Hilary & Hui, 2009)


Negative

Religion in the workplace creates the environment for fraud to develop. At greater risk are religious organizations to experience impairing effects on the design and operation of internal controls because extending trust within the organization comes at the expense of oversight
(Koerber & Neck 2006)

Impact of Religion



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DOCUMENT



IMPLEMENT




COMMUNICATE




MONITOR

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Organization prepares a written document of internal control

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Content

- Segregation of duties
- Authorization of transactions
- Documents and records
- Physical control over assets and records
- Independent checks on performance

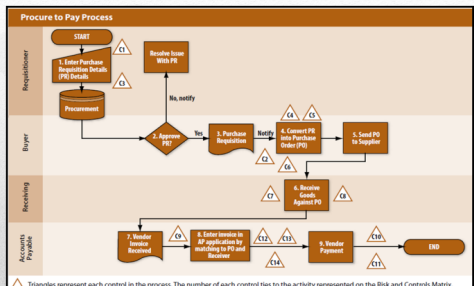
Chapters


- Written with the end-user in mind
- Illustrated with flowcharts and diagrams
- Includes templates designed to achieve desired outcomes

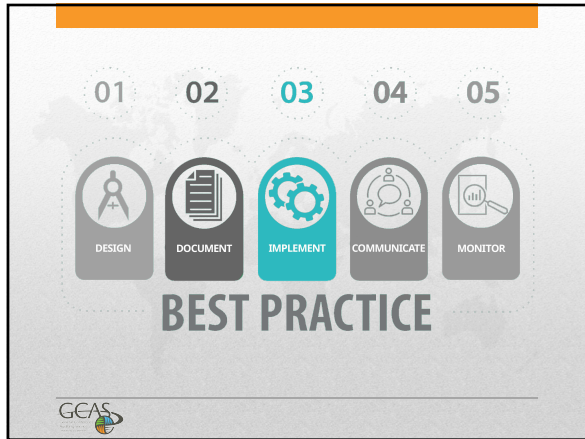
Internal Control Document



Procure to Pay Process













**Organization utilizes workflow tools
to operationalize processes**

Best Practice




WorkFlow Management System



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Organization provides job descriptions with specific areas of responsibilities and measurable expectations to the employee

Best Practice



SMART




SPECIFIC MEASURABLE ACHIEVABLE RELEVANT TIME-BASED

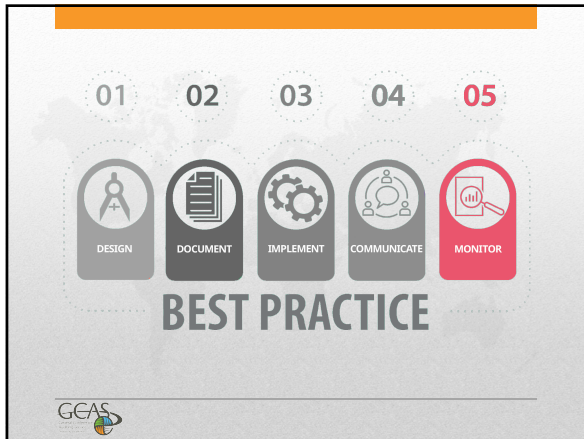


Organization promotes a working atmosphere that is transparent and holds persons accountable

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Organization performs an ongoing self-evaluation of internal control

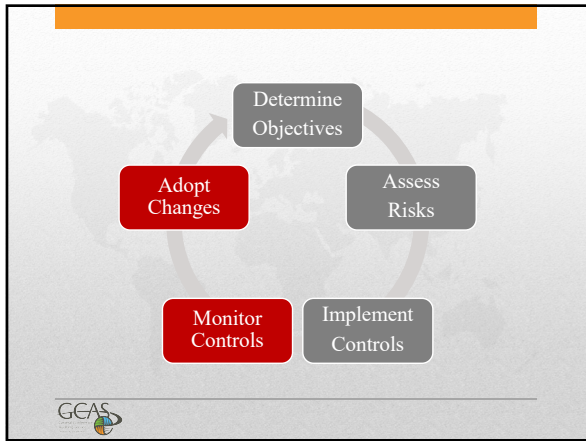
Best Practice

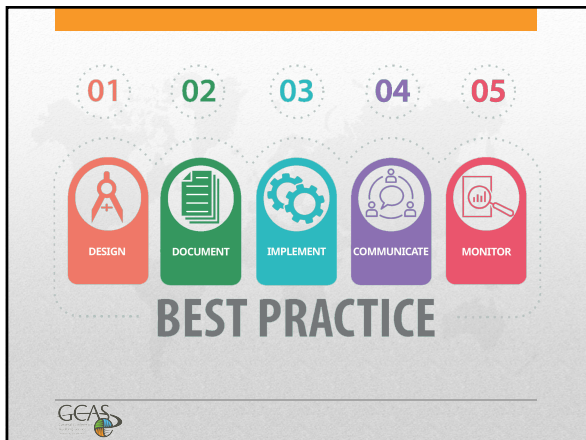
GCAS

Organization corrects deficiencies in internal control and communicates the changes made

Best Practice











RESEARCH INSIGHTS


The count of internal control deficiencies best predicts the type of an opinion an organization will receive




The count of internal control deficiencies is negatively correlated to the current ratio, cash ratio, and percentage of recommended working capital




**Internal control and fraud awareness
is positively correlated to a functioning
audit committee**



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**Leaders set the tone in an
organization by their example!**

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It is the responsibility of organizational leadership to manage financial matters with integrity. Every leader must model behavior that is guided by a commitment to ethics, transparency, and accountability. This behavior is critical for building confidence in the overall Church organization. To sustain this confidence, open communication must take place among the employees of the organization, between management and the controlling board or executive committee, between the organization and its constituents and other stakeholders, and between the organization and higher organizations. Beyond modeling behavior, it is imperative for leaders to promote and design the most appropriate systems that will safeguard the resources which are used to support the mission of the Church.



Questions



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