

Internal Control: It's More Than A Locked Safe

1

**NORTH AMERICAN DIVISION
TREASURERS' TRAINING
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A Warning and a Reason

2

**Although gold dust is precious,
when it gets in your eyes
it obstructs your vision.**

Hsi-Tang Chi 735-814

Purposes of Internal Control

3

The purposes of Internal Control are to:

1. Protect the assets of the organization
2. Ensure the reliability of the accounting records

Purposes of Internal Control

4

To ensure the reliability of the accounting records, internal controls seek to reduce the risk of:

1. Misstatement due to error
2. Misstatement due to fraud
 - a. Fraudulent financial reporting
 - b. Misappropriation of assets

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5

Occupational Fraud:

The use of one's occupation for personal enrichment through the deliberate misuse or misapplication of the employing organization's resources or assets.

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6

Report covered 2,110 cases in 133 countries.

Three categories of fraud defined:

Asset misappropriation - 86%; \$100,000

Corruption - 50%; \$150,000

Financial Statement Fraud - 9%; \$593,000

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7

Not-for-profit organizations: 9% of the cases;
median loss: \$60,000

Religious, Charitable, or Social Service organizations:
2.8% of the cases; median loss: \$78,000

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8

Primary I/C Weaknesses--all types of fraud:

Lack of internal controls	29%
Override of existing controls	20%
Lack of management review	16%
Poor tone at the top	10%
Lack of competent oversight personnel	8%
Other	7%

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9

Primary methods of fraud activity:

Creating fraudulent physical documents	39%
Altering physical documents	32%
Creating fraudulent electronic files	28%
Altering electronic files	25%
Destroying/withholding physical docs	23%

The Fraud Triangle

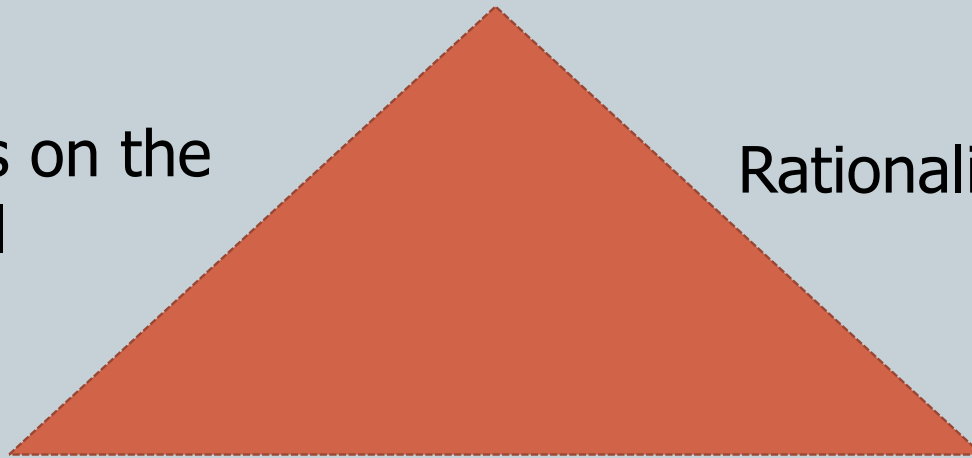
10

Control Pressure Points:

Pressures on the
individual

Rationalization

Perceived Opportunity



Purposes of Internal Control

11

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Purposes of Internal Control

12

Detective: Designed to detect errors or irregularities

Corrective: Designed to correct errors or irregularities

Preventive: Designed to keep errors or irregularities from occurring

Primary Control

13

Segregation of Duties—both preventive and detective.

Preventive: insert checks and balances into the system to make domination of the segment/process by one person more difficult.

Detective: catch unintentional errors by providing separate processing by different individuals and requiring independent reviews of work performed.

Primary Control

14

To break up duties and avoid dominance by one person:

Establish responsibility for each task to one person

Separate the custody of the recordkeeping for the asset from the person who has custody of the asset.

Special Challenges to Controls

15

Disruption of changes of personnel in the organization

Disruption of working off-site

Disruption because of remote access with the hybrid model

I/C in a Small Organization

16

I/C in a Small Organization:

1. Too few people
2. Use of Technology

Two Person Segregation of Duties

CFO	Accountant
Sign checks	Post accounts receivable
Sign employee contracts	Mail checks
Custody of securities	Write checks
Complete deposit slips	Post general ledger
Perform inter-fund transfers	Reconcile bank statements
Distribute payroll	Post credits/debits
Reconcile petty cash	Give credits and discounts
Record initial charges	Approve payroll
Approve employee time sheets	Open mail/receive cash
Prepare invoices	Disburse petty cash
Complete check log	Authorize purchase orders
	Authorize check requests
	Authorize invoices for payment

Three Person Segregation of Duties

CFO	Accountant	Bookkeeper
Sign checks	Prepare invoices	Post accounts receivable
Sign employee contracts	Records initial charges	Reconcile petty cash
Custody of securities	Open mail/receive cash	Write checks
Complete deposit slips	Mail checks	Post general ledger
Perform inter-fund trfs	Approve invoices for pymt	Reconcile bank statements
	Distribute payroll	Post credits/debits
	Authorize purchase orders	Give credits & discounts
	Authorize check requests	
	Approve time sheets	
	Approve payroll	
	Complete check log	
	Disburse petty cash	

I/C - Technology Enhancement

19

1. Use AdventistGiving.
2. Electronic approvals.
3. Electronic payment of invoices (ACH or P-Card).
4. Use of corporate credit cards or P-cards for small or repetitive expenditures.

I/C – Technology Enhancement

20

5. Direct deposit for all payroll checks.
6. Use accounting software to generate variance reports.
7. Insert other parties into the control system electronically.

Two Additional Points

21

Two additional points for Internal Control:

System Access

Delegation of Authority

System Access

22

Who has access to which parts of the system?
Is the separation of duties maintained?

Examples: Transaction entries;
Online approvals;
Review of transactions;
Changes to the master file, especially in payroll area.

System Access

23

Basic Information System Controls:

1. Use organization's equipment and systems only for authorized company business purposes.
2. Protect all organization information resources against accidental or unauthorized modification, disclosure, or destruction.

System Access

24

3. Keep passwords secret and change them frequently.
4. Never leave an active session unattended or unsecured.
5. Ensure all software installed on company devices is properly licensed.
6. Ensure approved virus detection software is installed and up-to-date.

System Access

25

7. Periodically back-up company computer data files, programs, and software.
8. Removal of any organization computer or telecommunications equipment or data files must be authorized by management.

Delegation of Authority

26

While the ultimate accountability lies with the treasurer/CFO, levels of authority should be delegated to various levels within the organization in order to streamline the approval process.

Delegation of Authority

27

Examples: Financing arrangements (contracts, etc.)
Invoice approvals
Screening & approval of suppliers
Expense report approvals
Timecard approvals
Special payments to personnel

Additional I/C Considerations

28

Business Interruption Issues

Disaster Recovery Plans

10 Basic I/C for Small Business

29

1. Review the numbers regularly.
2. Segregate duties.
3. Be stringent about documentation.
4. Verify further with regular managerial reviews.

10 Basic I/C for Small Business

30

5. Keep the communication lines open.
6. Implement secure measures for handling cash and checks.
7. Perform reconciliations of key accounts.

10 Basic I/C for Small Business

31

8. Safeguard your electronic environment.
9. Provide guidance.
10. Keep fraud top of mind—and don't dismiss the red flags.

Internal Controls

32

Questions?

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