

FARO Conference

Internal Controls

- Management is responsible for establishing and maintaining effective internal control systems.
- COSO (Committee of Sponsoring Organization of the Treadway Commission) established these responsibilities

- Framework of a Control System
 - Control environment
 - Risk assessment
 - Control activities
 - Information and communication
 - Monitoring

Control Environment

- We don't work in a vacuum. IC is directly impacted by the environment management creates
- Are controls necessary evils, that those bean-counters make us comply with or are they a valuable component of the organization?
- Ask yourself these questions:
 - Is management knowledgeable of IC
 - Is management committed to the system
 - Does management communicate its support for IC

Control Environment

- Internal audit function
- Role of the audit/finance committee
 - Selecting the external auditor
 - Reviewing the financial statements
 - Developing budget and monitoring the budget
- Qualified and adequate staff in finance

Risk Assessment

A variety of risks may hamper the effectiveness of your IC system. You must identify and react to these risks

- Change in personnel
- Change in your local economy
- Change in management attitude (Board)

Risk Assessment

- Changes in information systems
- Changes in programs and services

You also have to understand the “inherent risk” associated with certain transactions

You can only manage what you can identify or anticipate, therefore risk assessment is critical.

Control Activities

This is the nuts and bolts of your IC, however, these won't work if your environment is wrong, and you have not performed your risk assessment.

- Examples

- Authorization and approval

- Security over assets

- Segregation of duties

- Periodic reconciliations

- Periodic verifications (inventory, confirms, etc.)

- Timely preparation of financial statements

Control Activities

Segregation of Duties

You cannot have a single individual in a position of being able to both commit an irregularity and then conceal it.

You accomplish this by separating access to assets from access to the books.

Think through the transaction cycle from beginning to end and make sure no one controls the whole process.

Control Activities

- Reconciliations – they are not just a good idea.
- All control activities over cash receipts and disbursements are worthless if you do not reconcile and investigate on a timely basis
- This is not just for bank accounts.

Information and Communication

- Right information – provided to the right people – at the right time – in the right format
- Must have adequate ONGOING communication within the organization and with the outside users (County's, citizens, State agencies, etc...)

Monitoring

- Biggest component missing in IC system
- Once you set your environment, assess your risks, establish policies, design your reporting system – You must monitor if your system is working.
- Bottom line – Follow up on discrepancies
- This is normally on an ongoing basis. Are people in compliance? Do we have new risks?
- Periodic reviews are also necessary.
- Reviews are the equivalent of personnel evaluations. They are designed to improve a process or discontinue it.

Examples of Public Fraud

- Kiting – detect through the “outstanding” items
- Lapping – borrowing from Peter to pay Paul
- Bid rigging
- Payroll fraud – phantoms, inflated hours, overtime
- Healthcare beneficiary fraud – not a qualified beneficiary
- False claims – billed for services not received

Examples of Public Fraud

- False claims – billed for services not received
- Double payments – billed twice for services received
- Charge off fraud
- Disposal fraud
- Travel claim fraud
- Pilfering – petty theft that becomes material
- Misuse of assets and services – technology, vehicles, etc..
- Petty cash fraud

General Statute 122C

- Establishes minimum reporting requirements that each local area management entity must provide to its partner county organizations
- Establishes requirements for local area board structure, including term limits

Budget Versus Actual

- You must design a reporting system to ensure that the cost of services provided do not exceed available resources
- Using fund balance to meet current expenses – Bad Plan
- Using fund balance for one-time expenditures – Better Idea
- Ready, Fire, Shoot – recipe for destruction. You can't find the money after you have spent it.

Budget Versus Actual

- We all know management's focus is serving those in need in your service area.
- Management CANNOT ignore its responsibility to provide services within its funding limitations.
- Prioritization of needs is a painful reality

Budget Versus Actual

- Encumbrance accounting
- Cost ceilings in contracts with service providers
 - Provides “maximum costs” which will assist with encumbrance accounting
- Enforce “prompt pay” requirement in contracts with providers. Minimizes question marks on contracts
- Stringently manage budget compliance over operating expenditures

Budget versus Actual – State Contract Requirement

You must establish “processes and procedures that ensure that funds are available to reimburse providers for legitimately authorized, provided, and billed services. This includes estimating the percentage of authorized services that will be delivered so that only those funds that will be spent are encumbered.”

There is no way out – You must develop a dynamic encumbrance accounting system.

Board Oversight

- You are not on your own, your Board has oversight responsibilities (G.S. 122C-119)
- Make sure your Board is AWARE of their responsibilities
- Management answers to the Board. They are the final decision makers. Beware of pushy management and/or “need to know” basis of information sharing.

Board Oversight

- Board's cannot perform their oversight function without accurate financial and program data from mangement.
- Timely information is useful, untimely information is a waste of paper and toner.
- Critical component of control environment is "information and communciation."

Board Oversight

- G.S. 122C-118.1(a) requires the area board to include TWO individuals with financial expertise. Are you in compliance?
- G.S. 122C-119 requires the area board to establish a finance committee that has at least TWO members with fiscal control and budgeting expertise. They must meet at least SIX TIMES per year. Are you in compliance?
- Your Board can be your finance committee, but their meetings must be their meetings must be distinctive.

Reporting Requirements (G.S. 122C-117)

You must submit the following to the LME's County Commissioners the following:

- Approved budget
- Quarterly financial reports
- LME's business plan.
- Quarterly, service delivery reports that assess the quality and availability of the public services within its service area.
- Annually, a progress report that provides an assessment of the progress in implementing local service plans, goals, and outcomes.

Reporting Requirements (G.S. 122C-117)

- Quarterly reports must be presented within 30 days of the end of the quarter.
- Two times a year (I would recommend 6 months and annually) the reports must be presented in person and read into the minutes of the County Commissioners.

Summary – The State attempted to foolproof your financial protection with all of these bogies – If you ignore them, you are doing so at your own peril.

No one wants to find out, after the fact, that you are in trouble and need their help.

