DEVELOPING AN EFFECTIVE INTERNAL CONTROL ENVIRONMENT AND SAFEGUARDING AGAINST FRAUD

Advancing into Management Program (AIM)

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Presentation Outline

- Role of the Internal Audit Department
- Departmental Audits: Objectives
- Components of Effective Internal Control
- Fraud and Financial Impropriety
The Role of Internal Audit

- Management Auditors - provide assurance to senior management about internal controls, efficiency of operations and safeguarding of assets.
Other Auditors

- External Auditors - Ernst & Young LLP
- Funded Research Auditors - NSERC, SSHRC, CIHR, MOH
- Canada Customs and Revenue Auditors (CCRA)
- Federal and Provincial Government Auditors (GST/PST/EHT/etc.)
- Provincial Auditor
Departmental Audit Objectives

To Assess and Report on:

- Adequacy and Effectiveness of Systems of Internal Control
- Compliance with University and Sponsor Policies and Procedures
- Efficiency and Effectiveness of Financial Administration
Audit Objective 1 - Adequacy and Effectiveness of Systems of Internal Control

Definition

- “Control .support(s) people in the achievement of the organization’s objectives ... Control is what makes an organization reliable in achieving its objectives”

- from Guidance on Control, The Canadian Institute of Chartered Accountants
5 Components of Internal Control:

- Risk Assessment
- Control Environment
- Control Activities
- Monitoring Systems
- Information Systems
Component 1: Risk Assessment

Risk Defined:
the probability that events or actions may jeopardize the achievement of the University’s objectives
Risk Factors

- Management’s integrity - ‘Tone at the Top’
- Effectiveness of Internal Controls
- Complexity of Operations
- External Exposure
- Liquidity of Assets
- Changes in Key Personnel
- Size of operating, research, trust and capital budgets
Effects of Risk

- failure to attain objectives and goals
- erroneous decision making
- erroneous record keeping, inappropriate accounting practices, fraud, fraudulent financial reporting, loss and exposure
Effects of Risk

- failure to safeguard assets
- ‘customer’ dissatisfaction, negative publicity, damage to reputation
- non-compliance with policy, plans, procedures, laws
- acquiring resources uneconomically or using them inefficiently or ineffectively
Component 2: Control
Environment

- Integrity
- Ethical Values
- Competence
- Organization
Control Environment - Segregation of Duties

- Asset Transactions have three components:
  - Initiating/Authorization
  - Recording & Reconciliation
  - Custody

- No one person should be responsible for all three
Lack of Segregation of Duties

Frequent Causes:
- Delegation of Authority
- Resource Limitations

Effects:
- Lack of effective control
- Increased risk of errors and improprieties
Component 3: Control Activities

- University Policies and Procedures
  - Guide to Financial Management (GFM)
  - Purchasing Policy/Purchasing Card Guidelines
  - Taxation of Payments Manual
  - Human Resources - Administrative Staff Policies
Control Activities

- **Funded Research Sponsor Requirements**
  - Federal Granting Agency Guidelines - NSERC, SSHRC, CIHR
  - Funded Research Digests (FReDs) - RIS

- **Legislative Requirements**
  - Health and Safety
  - Employment Standards Act
  - Sales tax legislation
Component 4: Monitoring - Departmental and Central

- Departmental - Review and reconciliation of Fund and Fund Center Statements of Account and Payroll Distributions and Management Reports
- Central monitoring - Financial Services Dept., Procurement Services, Internal Audit
Monitoring - Department Head and PI Review

Objectives:

- Provides assurance that transactions recorded in AMS are complete, accurate and authorized.
- Provides reliable information about the source, use and availability of funds.
- Assists with detection of errors and/or improprieties.
Component 5: Information Systems

- Central
  - FIS
  - HRIS
  - RIS
  - DIS
  - ROSI
- Departmental
Audit Objective 2 - Compliance with University and Sponsor Policies and Procedures

- University Policies and Procedures
- Sponsor requirements
- Laws and Regulations
Audit Objective 3 - Efficiency and Effectiveness of Financial Administration

Objectives:

- Streamline workflow - identify redundant activities
- Minimize costs - identify non-value added processes and controls
- Skills Assessment - Training
Fraud and Financial Impropriety

- Reporting Incidents of Suspected Financial Impropriety
Fraud and Financial Impropriety

Statistics:

- 25% of employees committed or witnessed fraud
- 34% of employees reported a fraud to employer
- 80% of employers say they were defrauded by employees
  
  – Ernst & Young- Fraud Survey 2000
Fraud and Financial Impropriety

- Estimated annual cost in North America exceeds $100 billion
- 75% of all fraud goes undetected
- Nearly 70% of all fraud involve former or current employees, suppliers or customers.
Fraud and Financial Impropriety

“Red Flags”
Fraud and Financial Impropriety

How to safeguard against it:

- Set the Right Tone
- Review and Reconciliation
- Adequate supervision
- Segregate inappropriate combinations of duties
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