

PEMPAL TCoP

Treasury Internal Control

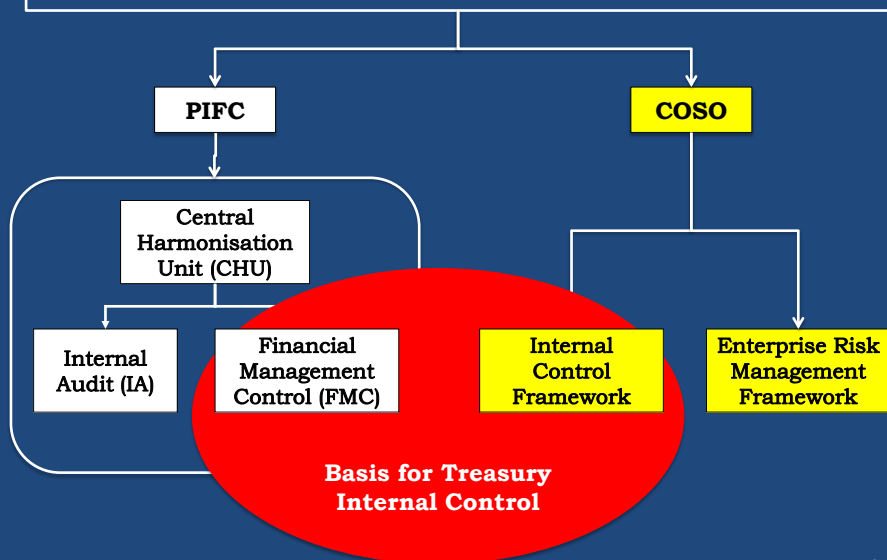
Kiev

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Approaches to Internal Control



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Public Internal Financial Control (PIFC)

- EU concept
 - Applicable to member and accession countries
 - Model of best practice for all countries
- PIFC aims
 - “to *provide a reasonable assurance that public funds are being used for the objectives selected by the budgetary authority ...[and] ... preventing corruption and fraud*”
- Financial Management (or Internal) Control a key component of PIFC
 - Based on COSO framework

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COSO

- COSO – Committee of Sponsoring Organisations
 - 5 US professional accounting and auditing bodies
- Developed internationally recognised Internal Control (IC) Framework
 - Generic for all public and private sector entities
 - Principle based
 - Suitable basis for Treasury Internal Control
- New COSO Internal Control Framework to be issued in 2013
 - This presentation based on Exposure Draft for new COSO framework

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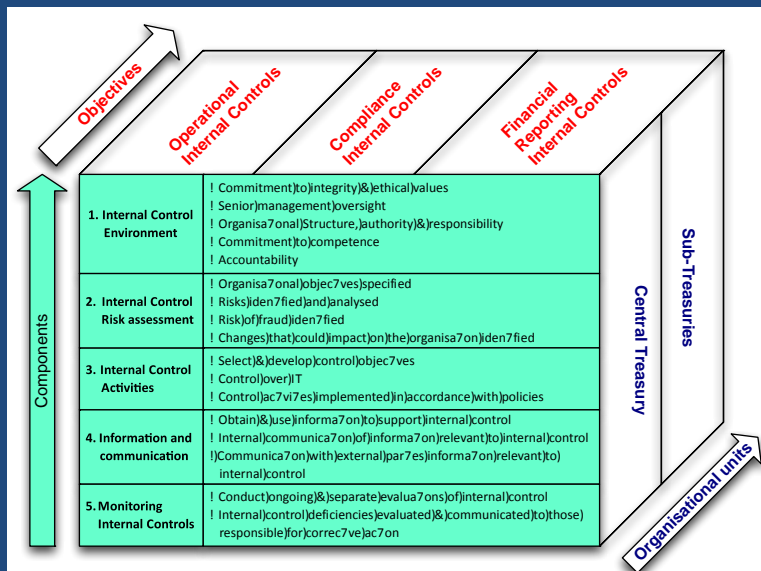
COSO definition of internal control

Internal control is a *process*, effected by an entity's board of directors, management and other personnel, designed to provide a *reasonable assurance* regarding the achievement of the objectives in the following categories:

- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations

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COSO Internal Control Framework & Principles



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Applying COSO to Treasury: The Groups of Objectives

Operational	<ul style="list-style-type: none">• Effective and efficient cash management, payments and collections• Minimizing fiduciary risks – fraud, theft, loss or misuse of money• Minimizing transaction costs• Use of money for purpose intended
Reporting	<ul style="list-style-type: none">• Reliable, timely and relevant internal and external reporting• Internal reports useful for management decisions and control• External reports including financial statements in accordance with international standards
Compliance	<ul style="list-style-type: none">• Compliant with national laws and regulations• Compliant with international standards and best practice

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APPLYING COSO TO TREASURY: FIVE COMPONENTS OF INTERNAL CONTROL

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1. Treasury Internal Control (IC) Environment

1.1 Integrity & ethical values	<ul style="list-style-type: none">• Management commitment• Ethics included within staff training• Professionalization & professional values
1.2 Management oversight	<ul style="list-style-type: none">• Oversight structure e.g. Audit Committee, Central Harmonization Unit• Actions on identified issues
1.3 Organisational structure	<ul style="list-style-type: none">• Clearly defined roles & responsibilities• Job descriptions• Segregation of duties
1.4 Commitment to competence	<ul style="list-style-type: none">• Effective HR management• Recruitment of high quality staff• Structured an ongoing training• Professionalization
1.5 Accountability	<ul style="list-style-type: none">• Identified responsibility leads to accountability• Internal and external accountability for actions• Rewards and sanctions

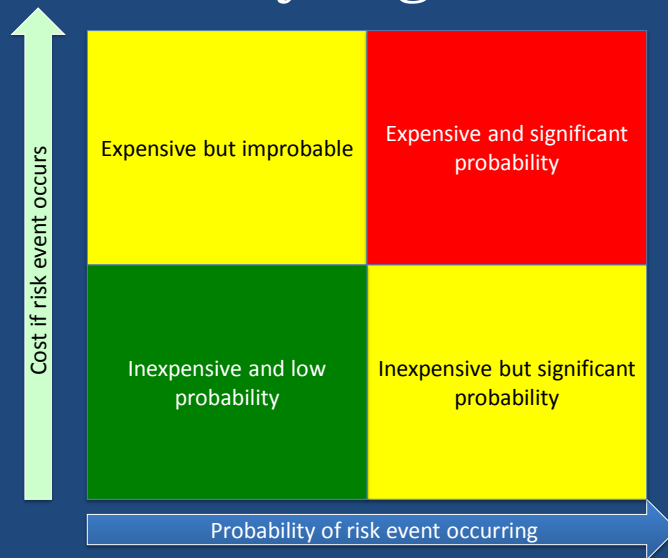
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2. Treasury Risk Assessment



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Analysing risks



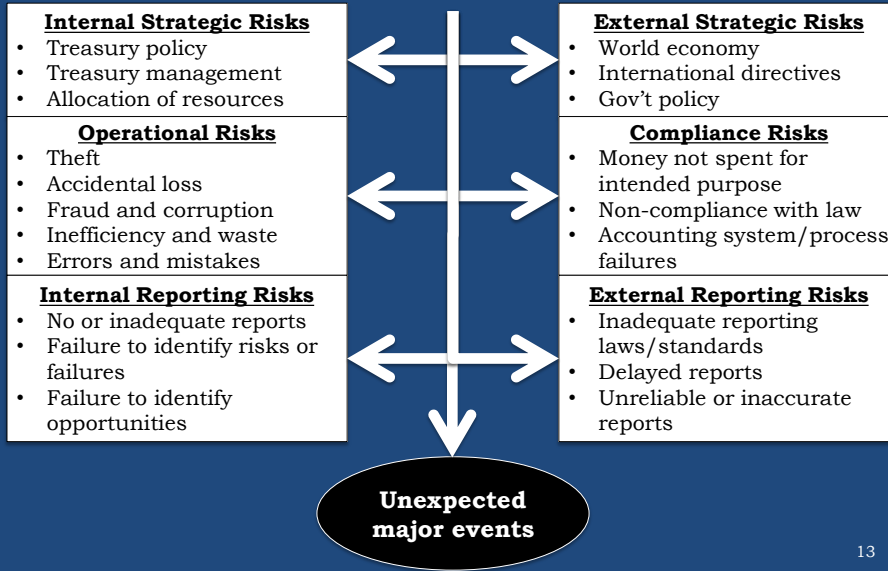
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Balance of risk and cost



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Treasury Risk Framework



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3. Treasury IC activities (1)

Process controls	<ul style="list-style-type: none"> • Documented procedures • Staff trained in procedures • Procedures operated in accordance with instructions
3.1 Organizational controls	<ul style="list-style-type: none"> • Segregation of duties • Clearly defined responsibilities & accountability • Job descriptions • Hierarchy of payment approval limits • Regular holidays and rotation of staff • Effective disciplinary procedures
3.2 Budget execution controls	<ul style="list-style-type: none"> • Procedures for releasing budget allocations (warranting) • Managing expenditure within budget/release limits (commitment management) • Early signaling of budget overspend
3.3 Cash management controls	<ul style="list-style-type: none"> • Procedures for cash management • Revenue/expenditure profiling and cash forecasts
3.4 Loan payment controls	<ul style="list-style-type: none"> • Debt management system integrated with debt payments • Loan/interest payments made on time

3. Treasury IC activities (2)

Payment procedures	<ul style="list-style-type: none"> • Payment separated from authorization • Approved list of suppliers • Payment by bank transfer • Identification & review of large or unusual payments
3.5 Payroll controls	<ul style="list-style-type: none"> • Dedicated payroll system/procedures • Integrated with personnel records • Payment through bank transfers • Physical verification of employees
3.6 Supplier payments	<ul style="list-style-type: none"> • Approved list of suppliers • Procedures for ordering, receipting goods/services linked to payment authorization • Early recording invoices/bills (accrual accounting) • Payment through bank transfers
3.7 Controls through external evidence	<ul style="list-style-type: none"> • Identified and documented government bank accounts • Regular bank reconciliations & resolution of reconciling items • Regular reconciliation with supplier records

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3. Treasury IC activities (3)

Advances and prepayments	
3.8 Advances and prepayments	<ul style="list-style-type: none"> • Authorization procedures • Accounting records (accrual) or registers (cash accounting) • Regular reconciliation and confirmation • Clearance of all balances within specified time limits
3.9 Records management	<ul style="list-style-type: none"> • Documents filed and accessible • Electronic authorization - ability to identify individuals providing authorization • Policies on document retention
3.10 Physical controls	<ul style="list-style-type: none"> • Physical security of cash and assets • Security of cash in transit
3.11 Revenue and other cash receipts	<ul style="list-style-type: none"> • Reconciliation with document identifying planned receipts, e.g. tax demands • Segregation revenue demands from receiving cash • Bank transfers and/or automatic receipting machines • Regular reconciliation anticipated and actual revenue receipts

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3. Treasury IC Activities (4) – IT

System development controls	<ul style="list-style-type: none">• Documented specification including internal control requirements• Rigorous and documented system testing• Control over opening balances• Controls over system administrator access (all access logged and no “back doors”)
3.12 Management and supervision	<ul style="list-style-type: none">• Non-IT managers trained to manage IT functions• Controls over data input• System generated logs of control issues, exceptions, etc.• Regular review and follow up of logs
3.13 Process controls	<ul style="list-style-type: none">• System controls, e.g. authorizations, parameters• Automatic generation of standard and exception reports
3.14 Security	<ul style="list-style-type: none">• Non-IT management of security and access rights to systems and data• Access controls (password or biometric)• Controls to prevent unauthorized access and viruses• Physical security of systems, networks and hardware

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The Big Man Problem



You are a junior clerk responsible for payments

One day the Minister approaches you personally and says “Make this payment NOW – on my authority”

You know this is an improper payment – but how can you say no? Your career will be at risk.

BUT you can say NO if there is a good internal control system:

“Minister I want to help – but the system will not allow me to make this payment unless proper procedures are followed.”

- The Minister is controlled by the system
- The junior clerk is protected by the system

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3. Treasury IC activities (5) – Disaster & business continuity

- 3.15 Contingency plans for physical or system disasters/failures
- 3.16 Data regularly backed up as multi generation off site records
- 3.17 Contingency provision for off site data processing
- 3.18 All business continuity procedures regularly tested

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4. Treasury IC Information & Communication

Reports to support internal control	<ul style="list-style-type: none">• Logs, exception reports, reconciliations, etc.• Specific reports on internal control issues, e.g. by internal audit• Follow up action on reports
4.1 Internal reporting	<ul style="list-style-type: none">• Management reports to support decision making and control• Reliable, understandable, timely and relevant reports• Reports utilised by management
4.2 External reporting	<ul style="list-style-type: none">• Financial statements in accordance with international standards• Published independent audit reports of financial statements adds credibility• Other external reports, e.g. monthly/quarterly financial bulletins• Statistical reports to international agencies, e.g. IMF GFS• Reliable, understandable, timely and relevant reports

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5. Treasury IC Monitoring

Monitoring process	<ul style="list-style-type: none">• Ongoing monitoring of internal control, e.g. by internal audit• Monitoring of new or emerging risks, e.g. cyber attacks• Structure to manage internal control and risk monitoring and responses
5.1 Evaluation of internal control issues	<ul style="list-style-type: none">• Identified issue, potential loss, probability and cost of actions to address issue• Referred to management• Decision on actions
5.2 Corrective actions	<ul style="list-style-type: none">• Action taken• Follow up review and evaluation

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Treasury Internal Control: Conclusions

1. Internal Control part of good governance
 - Essential for EU membership as part of PIFC
 - Good practice for all governments
2. Treasury internal control
 - Key component of public sector internal control
 - Cash receipts and payments especially vulnerable
3. No system of internal control can provide complete protection
 - Balance of cost of controls compared to amount and probability of loss

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