





INTERNAL CONTROLS

WHAT ARE INTERNAL CONTROLS?

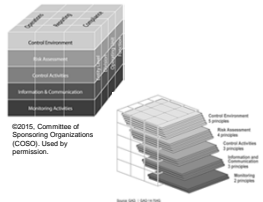
"Internal Controls means a process, implemented by a non-Federal entity, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- + Effectiveness and efficiency of **operations**;
- + Reliability of **reporting** for internal and external use; and
- + **Compliance** with applicable laws and regulations."

INTERNAL CONTROLS

ESTABLISHING INTERNAL CONTROLS

- + The Uniform Guidance states that internal controls should be in line with:
 - "Standards for Internal Control in the Federal Government" (i.e., the Green Book), issued by the Comptroller General of the United States;
 - "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations (COSO); and
 - OMB Compliance Supplement, Part 6.



INTERNAL CONTROLS

ROLE OF PART 6: APPLYING INTERNAL CONTROLS TO FEDERAL AWARDS

- + Part 6 describes characteristics of internal control relating to each of the five components of internal control (as defined by the Green Book).
- + Part 6 serves dual purposes:
 - For **institutions**, Part 6 serves as a guide to defining a control environment that facilitates compliance with Federal laws, regulations, and the terms and conditions of Federal awards.
 - For **auditors**, Part 6 serves as a guide to conducting the Single Audit to auditing the institution's compliance with Federal program requirements.

INTERNAL CONTROLS

COSO FRAMEWORK: COMPONENTS OF INTERNAL CONTROL

Control Environment

Sets the **tone of an organization** influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure.

Risk Assessment

Institution's identification and analysis of risks relevant to achievement of its objectives, forming a **basis for determining how the risks should be managed.**

Control Activities

Policies and procedures that help ensure that management directives are carried out.

Information and Communication

Identification, capture, and exchange of information in a form and time frame that enable people to carry out their responsibilities.

Monitoring Activities

Process that **assesses the quality of internal control performance** over time.

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SINGLE AUDIT APPLICATION

SINGLE AUDIT APPLICATION

COMPLIANCE REQUIREMENTS

Using Part 6, the Single Audit tests 12 Compliance Requirements:

<p>A. Activities Allowed or Unallowed</p> <p>B. Allowable Costs/Cost Principles</p> <p>C. Cash Management</p> <p>D. Reserved (Davis-Bacon Act)</p> <p>E. Eligibility</p> <p>F. Equipment and Real Property Management</p> <p>G. Matching, Level of Effort, and Earmarking</p>	<p>H. Period of Performance</p> <p>I. Procurement and Suspension and Debarment</p> <p>J. Program Income</p> <p>K. Reserved (Real Property Acquisition & Relocation Assistance)</p> <p>L. Reporting</p> <p>M. Subrecipient Monitoring</p> <p>N. Special Tests and Provisions</p>
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SINGLE AUDIT APPLICATION

CONSIDERATIONS WHEN EVALUATING INTERNAL CONTROLS

- + Internal controls will differ from institution to institution, considering:
 - Research volume (granting agencies, number of subawards).
 - Institutional history (past audits, internal investigations).
 - Enterprise structure (affiliated institutions, faculty appointments).

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SINGLE AUDIT APPLICATION




CONSIDERATIONS WHEN EVALUATING INTERNAL CONTROLS

Risk Analysis	Cost Benefit Analysis
<ul style="list-style-type: none"> ▪ Focus controls on high-risk processes: <ul style="list-style-type: none"> ○ Greatest chance for misapplication of charges to a Federal award. ○ High-dollar transactions. ○ Transaction type (equipment, foreign travel, etc.). 	<ul style="list-style-type: none"> ▪ How <i>many</i> controls impact a process? ▪ How <i>effective</i> can the control be? ▪ How <i>broadly</i> is the control applied?

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SINGLE AUDIT APPLICATION

CONSIDERATIONS WHEN EVALUATING INTERNAL CONTROLS

-  Too many controls can result in inefficient operations.
-  Strength of controls should be balanced with the relative risk.
-  The benefits of controls should outweigh the costs.

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EXAMPLE 1: COST PRINCIPLES

COST PRINCIPLES OVERVIEW

- + Cost principles must be used in determining allowable costs of work performed by the non-Federal entity under Federal awards.
- + To charge a cost to a Federal award, a cost must be:
 - Allowable;
 - Reasonable; and
 - Allocable.
- + Items of cost must be consistently treated.

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COST PRINCIPLES POTENTIAL RISK AREAS

Entity Level	Division / Operating Unit	Function
<ul style="list-style-type: none"> • Guidance around cost principles is not defined in policy. 	<ul style="list-style-type: none"> • Management lacks ability to restrict individuals who have access to make direct charges in the accounting system. • Management lacks ability to identify charges that were applied to an award in error. 	<ul style="list-style-type: none"> • Individuals without full knowledge of policy are allowed to charge awards. • Individuals who charge awards do not have sufficient guidance to determine the allocability of a direct charge.

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COST PRINCIPLES
EVALUATING AGAINST PART 6

Control Environment Management's commitment to competence ensures that staff receive adequate training to perform their duties. [Principle 4]

- + Does the research community – including departmental staff, central staff, and PIs – receive adequate training on cost principles and how they are applied?
- + Would staff be able to recognize instances of misapplication of charges?
- + Does management initiate responses to reports of noncompliance and prior compliance and control findings?

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COST PRINCIPLES
EVALUATING AGAINST PART 6

Risk Assessment Program managers and staff understand and have identified key compliance objectives and risk tolerances. [Principle 6]

- + Is there an overall approach to monitoring direct charges on grants?
- + Have major indicators of noncompliance been identified?
- + Are there processes in place for monitoring major indicators of noncompliance? For example, are there notifications/triggers indicating if:
 - Charges exceed the proposed budget?
 - Unallowable direct costs are charged?

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COST PRINCIPLES
EVALUATING AGAINST PART 6

Control Activities Adequate segregation of duties is provided between performance, review, and recordkeeping of a task. [Principle 10]

- + Are policies and procedures in place that identify responsible parties for direct charging? For example, identifying, approving, posting, and reviewing charges?

Hot Topic: Clerical and Administrative Salaries

- + The Uniform Guidance no longer requires that a project must be considered a Major Project in order to charge clerical and administrative salaries.
- + How can (and should) this revision impact the allocability analysis when determining whether to charge an administrative salary to a federal project?

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COST PRINCIPLES
EVALUATING AGAINST PART 6

Control Activities → Adequate segregation of duties is provided between performance, review, and recordkeeping of a task. [Principle 10]

- + Is there adequate segregation of duties?
- + Can direct charging policies and procedures be overridden?

Sample Segregated Process

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    graph LR
      A((Requestor (PI))) --> B((Initiator (Department Administrator)))
      B --> C((Approver (Department Business Office and/or Central Office)))
      C --> D((Recorder (System)))
  
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COST PRINCIPLES
EVALUATING AGAINST PART 6

Information and Communication → Adequate source documentation exists to support amounts and items reported. A recordkeeping system is established to ensure that records are retained for the time period required. [Principle 13]

- + Do record retention policies require maintaining supporting documentation for purchases on grants?
- + Is responsibility for maintaining source documentation clearly defined?
- + Is source documentation readily available so that detailed questions can be answered during the Single Audit?

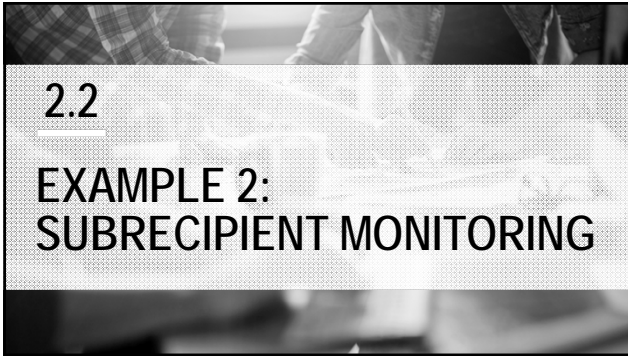
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COST PRINCIPLES
EVALUATING AGAINST PART 6

Monitoring → Periodic site visits are performed at decentralized locations and checks are performed to determine whether procedures are being followed as intended. [Principle 16]

- + Are there expectations of monitoring direct charges?
- + How is monitoring accomplished? For example:
 - Are "signed-off" reports reviewed?
 - Are charges reviewed prior to reporting?
- + How is monitoring being reported? To what bodies is it reported?

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SUBRECIPIENT MONITORING
OVERVIEW

- + Pass-through entities must monitor the activities of subrecipients as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward, and that subaward performance goals are achieved.
- + Monitoring must include:
 - Reviewing financial and performance reports required by the pass-through entity;
 - Following-up and ensuring that the subrecipient takes timely and appropriate action on all deficiencies pertaining to the Federal award; and
 - Issuing a management decision for audit findings pertaining to the Federal award.

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SUBRECIPIENT MONITORING
POTENTIAL RISK AREAS

Entity Level	Division / Operating Unit	Function
<ul style="list-style-type: none"> • Failure to take enforcement action when a subrecipient does not meet the expectations of award management. • Failure to evaluate existing and future subcontracts with a subrecipient if there are issues with the subrecipient. 	<ul style="list-style-type: none"> • Incorrectly identifying subrecipient versus contractor. • Incomplete review of a subrecipient's management practices and past audits. 	<ul style="list-style-type: none"> • Initiating a subaward with an excluded party. • Failure to communicate subaward responsibilities to a subrecipient.

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SUBRECIPIENT MONITORING
EVALUATING AGAINST PART 6

Control Environment Management initiates positive responsiveness to prior compliance and control findings. [Principle 4]

- + Has subrecipient monitoring been a previous finding on your Single Audit? Or....
- + Has internal audit found weakness in this area?
- + If so:
 - Has the process been appropriately reexamined, and have necessary revisions been made?
 - Has the revised process been evaluated?

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SUBRECIPIENT MONITORING
EVALUATING AGAINST PART 6

Risk Assessment Management considers the potential for fraud (or waste or abuse) when identifying, analyzing, and responding to risk. [Principle 8]

- + Has a proactive risk assessment process for subawards been implemented?
- + Is the risk assessment process recurring throughout the life of the subaward?
- + Are the outcomes of the assessment directly informing how the agreement is structured?

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SUBRECIPIENT MONITORING
EVALUATING AGAINST PART 6

Control Activities Personnel possess adequate knowledge and experience to discharge their responsibilities. [Principle 10]

- + Do staff conducting the risk assessment have the appropriate level of expertise to review the subrecipient's Single Audit output?
- + Do staff understand how to conduct a risk assessment for subrecipients that do not undergo a Single Audit?
- + Is there an escalation process if staff are unsure about proceeding with an area of the risk assessment?

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SUBRECIPIENT MONITORING

EVALUATING AGAINST PART 6

Information and Communication There are established channels of communication between the pass-through entity and subrecipients. [Principle 15]

- + Do PIs and the central office have regular channels and approaches to communicating with subrecipients?
- + Is current contact information a required component of subcontracts?
- + If the PI needs assistance, is the central office available, responsive, and trained to help?

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SUBRECIPIENT MONITORING

EVALUATING AGAINST PART 6

Monitoring Management follows up on irregularities and deficiencies to determine the cause. [Principle 17]

- + When issues are identified, is immediate action taken to revise the subrecipient's contract? Are other contracts with the subrecipient examined?

Subrecipient Monitoring Plan Considerations

Proposal Stage

- Determine whether the subrecipient is capable of complying with Federal law, regulation, and the terms and conditions of the Federal award.
- Risk assessment is conducted.

Project Stage

- Technical Reports and Progress Reports are reviewed to ensure services were provided as documented.
- Invoices are monitored for completeness and timeliness.

Closeout Stage

- Confirm all project deliverables were provided.
- Confirm a final invoice was received.

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ORGANIZATIONAL IMPACT

ORGANIZATIONAL IMPACT

EVALUATING YOUR INTERNAL CONTROL STRUCTURE

The Federal government emphasizes the importance of a "culture of compliance" in multiple guidance documents, including Part 6 and Draft Compliance Program Guidance for Recipients of PHS Research Awards.

- + Is compliance woven into your institution's operations?
- + Does your institution prioritize compliance, along with operational efficiency and customer service?

ORGANIZATIONAL IMPACT

EVALUATING YOUR INTERNAL CONTROL STRUCTURE: PART 6 EMPHASES



ORGANIZATIONAL IMPACT

EVALUATING YOUR INTERNAL CONTROL STRUCTURE: PART 6 EMPHASES

Culture of Compliance	<ul style="list-style-type: none"> • There is a sense of conducting operations ethically, as evidenced by a code of conduct or other verbal or written directive. [Principle 1] • Management demonstrates respect for and adherence to program compliance requirements. [Principle 5]
Managerial Oversight	<ul style="list-style-type: none"> • Key managers have adequate knowledge and experience to discharge their responsibilities. [Principle 4] • Supervision of employees is commensurate with their level of competence. [Principle 10]
Skills and Abilities of Staff	<ul style="list-style-type: none"> • Management's commitment to competence ensures that staff receive adequate training to perform their duties. [Principle 4] • Staff are knowledgeable about compliance requirements and are given responsibility to communicate all instances of noncompliance to management. [Principle 4]

ORGANIZATIONAL IMPACT

EVALUATING YOUR INTERNAL CONTROL STRUCTURE: PART 6 EMPHASES

Documentation of Authority	<ul style="list-style-type: none"> • Management prohibits intervention or overriding established controls. [Principle 11] • Key managers' responsibilities are clearly defined. [Principle 3]
Organization and Reporting Structure	<ul style="list-style-type: none"> • The organizational structure provides identification of risks of noncompliance. [Principle 7] • Key managers have been given responsibility to identify and communicate changes. • Employees who require close supervision (e.g., they are inexperienced) are identified. • Management has identified and assessed complex operations, programs, or projects.
Policies and Processes	<ul style="list-style-type: none"> • Operating policies and procedures exist and are clearly written and communicated. [Principle 11] • Procedures are in place to implement changes in statutes, regulations, and the terms and conditions affecting Federal awards. [Principle 11]

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DEVELOPING AN INTERNAL CONTROL STRUCTURE

INTERNAL CONTROL STRUCTURE

EVALUATE EXISTING CONTROLS

- + **Start Small:** Do controls exist for each area of Single Audit focus?
- + Are existing controls:
 - Appropriately **designed** to meet the control objective?
 - **Implemented** in a manner that allows the control to function as designed?
 - Consistently **deployed**?

Internal Controls should be evaluated on an ongoing basis.

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INTERNAL CONTROL STRUCTURE

EVALUATE EXISTING CONTROLS

Cost Service Efficiency Compliance

Are you striking the right balance?

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INTERNAL CONTROL RESOURCES

- + Part 6, OMB Compliance Supplement
- + COSO
- + Green Book

Though these documents are not checklists, they are there – and it is easier than starting from scratch.

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QUESTIONS?

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