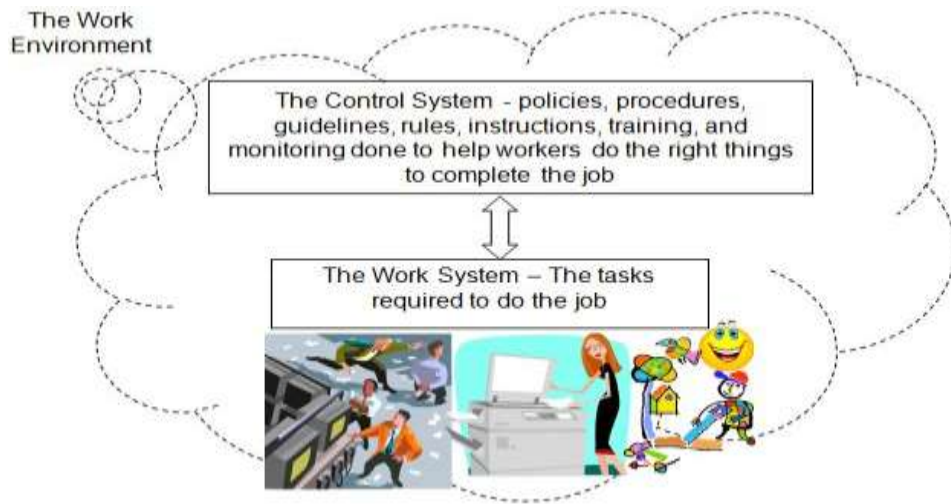


Larry's Cheat Sheet – Internal Controls

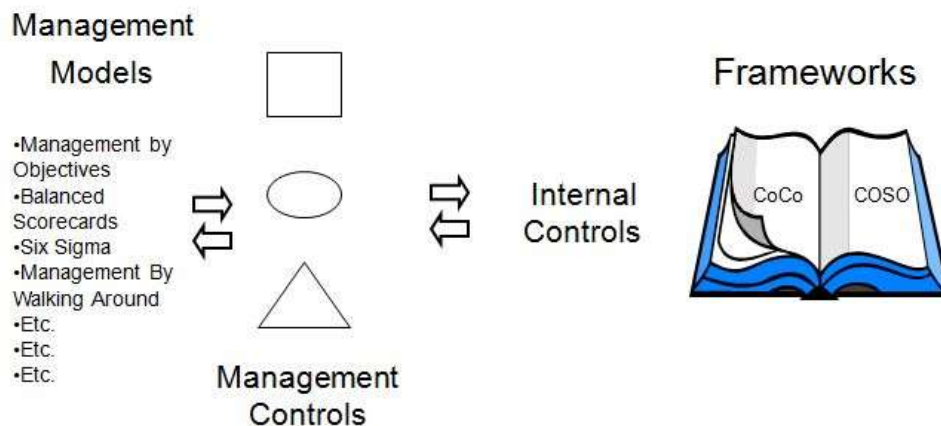


“Control” is the key to auditing – controls see that things get done, and are a key management responsibility. Controls are where auditors focus their attention, and can be simply defined as things management puts in place to be sure activities are done correctly.

Every activity has two levels:

- the work system, which are the tasks required to do a job
- the control system, which overlays the work and are the policies, procedures, guidelines, rules, instructions, training and monitoring that management establishes to help be sure the job is done correctly and objectives are achieved.

Activities also live inside a "work environment" that impacts the way people do their jobs. Managements' attitude, philosophy, and commitment to competence; the organizational structure; the clarity of roles and responsibilities; the human resource system; the risk appetite and other broad-based attributes impact the way employees interpret both their job duties and importance of the control system.



Auditors see many different operations and managers, and must evaluate them all objectively. So, auditors need common criteria against which to evaluate for reporting to the Board or Senior Management. That's where an internal control framework or model comes in. Think of “internal controls” as common criteria, and “management controls” as specific to a particular manager and management technique.

What Controls are Not

Controls are not the actual steps required to do a job, so auditors do not (or should not) critique how people do the job. Controls are above that, and help people do the job right. That's where auditors focus.



Sometimes, controls are "part of the process" because of the way the process has been designed. For instance, obtaining credit approval before shipping products to a new customer is "part of the process" in some organizations. The reason it is called a "control" is that credit checking is not part of the actual shipping of the product - it is embedded in the shipping process, but it was put there by management to ensure the shipping and collection activities work right. A company could sell to anybody and just hope to get paid, but instead they do credit checks as a control to increase the probability of getting paid. Many steps, such as reconciliations and approvals and balancing, are embedded in business processes - but they are put there by management to help "control" the process and be sure the process works as planned.

A Simple Control Identification Approach

Control identification is the MAJOR EFFORT in Audit Planning! Here is a simple approach.

Based on the audit objectives identify the major activities or jobs within the audit scope. Then for each activity or job:

1. Identify the "steps to do the job" - that is, the major steps in the actual business process or activity.
2. Identify the controls embedded directly in the process flow - the Process Flow Controls, to be sure the process works right.
3. Identify the Non-Process Flow Controls, such as training, policies and procedures, and clarity of roles and responsibilities. The Environment and Information/Communication controls.
4. Use a Risk/Control Matrix to identify objectives and any important risks that could occur, despite the controls above, and cause the process or activity to have a problem, and determine what to do about those risks (responses). Always consider the risk of fraud here.
5. Compare the above controls and risk responses to The COSO Map.

Process Flow Controls

In reviewing a process flow, that is, something you could flowchart, use this for step 2:

Identify the controls that ensure these Process Flow Objectives (CAATSS) are achieved for all the important Input, Processing, and Output:

- Complete
- Timely
- Authorized
- Safeguarded
- Accurate
- Segregation of Duties

Standard 2210.A3 Adequate criteria are needed to evaluate controls. Internal auditors must ascertain the extent to which management has established adequate criteria to determine whether objectives and goals have been accomplished. If adequate, internal auditors must use such criteria in their evaluation. If inadequate, internal auditors must work with management to develop appropriate evaluation criteria.