**Workforce 3One**

**Transcript of Webinar**

**Internal Controls: Establishing an Effective Control Environment**

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BRIAN KEATING: I want to welcome everyone to the "Internal Controls: Establishing an Effective Control Environment" webinar. And without any further ado – again just want to encourage you to introduce yourself in that welcome chat if you haven't already done so.

With that, I'm going to turn things over to our presenter today, Maggie Ewell. Maggie, take it away.

MAGGIE EWELL: Thanks, Brian. And thanks to everyone in the room and virtually joining us today. Welcome to our Youth Career Connect grantees, who are a special group with us. I hope you're enjoying your time here.

MR. KEATING: I'm sorry, Maggie. Could you just speak up a little bit just for the benefit of our audience?

MS. EWELL: Sure. So my name is Maggie Ewell. I am with our Office of Grants Management and I head the fiscal policy unit, and so I'm kind of the big gun they bring out to train our new and intermediate grantees on how to stay out of trouble.

So we're going to talk today about an internal control system, which is a really good way to safeguard your assets and ensure that you're operating safely and efficiently.

This afternoon I'm going to talk about budget controls, which is a really good way to stay on top of managing your money and also tie it to performance. And I'm also going to weave in some indirect costs and time for questions since I understand that's an area you have a lot of questions about.

MR. KEATING: All right. And sorry, Maggie. We are getting feedback that it is hard to hear. So if you could get closer to the microphone and just speak up, that'd be great. (Cross talk.)

MS. EWELL: OK. So I'm going to be a little tied down. Normally, as a speaker, I move around a lot but I'm kind of tied to the phone here.

So what we really want to talk about today is managing your federal money. And you all are schools. So I'm not sure if you in the room are the folks that have the control of the money or you're working with folks who have the money. So what's the relationship? How does the federal funds come to you? Are you guys the program manager? Do you work with your fiscal folks? OK.

So you're going to want to take a lot of what I'm talking about and you're going to bring it back to your fiscal folks. And I'm also going to let you know we are – as we speak, one of my staff people are putting some online trainings up about what I'm talking about. So I'll make sure that – (inaudible) – get that information to share with you the links when the online training is live. Maybe you'll have your accounting folks take this as well.

So why are we hitting on internal controls? There's a couple of reasons. One, it's probably the top area of findings when our regional staff come out and monitor is lack of internal controls or weak internal controls. And the second reason is that there has recently, this past December, been a big change to all of the regulations that manage, that govern federal grant awards.

Now, for your grants, it doesn't impact them because you are under the old awards. But it's kind of getting you ready if you get any future awards. And everything I talk about today is only going to help you because the same – it's one of those situations where these things were required, but they weren't in writing and now they've been much more strengthened in this new set of regulations.

Internal controls is something that effect pretty much every aspect of your organization. It may not be a word you've heard, but I think when we get into the concepts, you'll see that. They really focus on two things; the people and the environment. And these are things you can control.

And the last, why we do it. Obviously, as the government, we're very big on preventing waste, fraud, and abuse. Internal controls is the key to doing that. So we can go to the next slide.

So I'm going to talk a little bit about this new thing called the uniform guidance. We're going to talk some definitions. I'm going to go over a framework for effective internal controls and give you some references. We're going to talk about the key activities and then we're going to talk about what happens if we don't have internal controls and what we've seen.

Next slide. We're going to skip the knowledge checklist. It's for a different audience.

All right. So I mentioned that the uniform guidance was something new. And so right now, you work under the Uniform Administrative Requirements, probably for governments or – since you're not institutions of higher education, you may be a nonprofit.

Right now, we've added a new section, 303, for internal controls. This was taken from audit requirements that previously existed. So this is nothing completely new, but it's – your accounting folks should be familiar with it. Next slide.

So wanted to give you two resources here on the screen. Much of the guidance around internal controls actually comes from two sources. The first is something we call the Green Book, which actually comes from the Comptroller General of the United States and it's issued by the General Accountability Office. And the second is something – Committee of Sponsoring Organizations of the Treadway Commission or we call it COSO, and that is an internal control integrative framework. So those are good resources to check out and pass on to your accounting folks when you get back. Next slide, please. Next slide. Great.

So what are some of our basic principles for financial management? The first is that there are some state laws out there and to the extent that you are a government entity, operating within your state and local laws. The second is that above and beyond that, you need to have your own policies and procedures for how you manage funds and how you operate activities and how you control assets that are funded by our grant so that we're assured that you're in compliance with the requirements under your award. Next slide.

So we have seven standards in the administrative requirements for financial management. These are not changed in any way by this new regulation. And so the first is that our money has to be identified separately in your accounting system. We actually have some staff on the review this week that want out and the entity that they're at, they have not been able to get in the general ledger. When they say we want to see our grant, everything is all combined; all their different funding streams. You have to have a code for our funds. This is something our staff are going to look at when they come out and monitor.

Accurate, current, complete disclosure is another one. We'll talk more about that on the next few slides. Records. I always like to say that a cost that you incur can be absolutely allowable, but if you don't have any documentation for it, we're going to question it. Control over and accountability for assets. How many of you have inventory tags on computers and things that you buy? Yay. Things like that. We're going to talk about that.

Comparison of expenditures to budget. That's going to be this afternoon's session. It's really about a budget control. You had a budget that you submitted. Maybe your grant writer wrote it. It was done months in advance of when you got this award. So what are we doing now that you've started up to make sure that you're staying on track because if you deviate from that budget by more than a certain amount, you're going to need to come in and request permission to do that from the grant officer.

Talked about written procedures for payments is another form of internal control. So written policy for how you make payments, and the same for allowable costs. Let's go into a little more detail. Next slide.

So the financial system. One of the key things that we're going to want to know is who does what. What does your org chart? What role does each person play and how are they responsible for the things under them? And is there check and balance along the way?

I went out to a grantee and it was probably the worst thing I'd ever seen. I always like to tell it in the training because I don't think anyone can top it. I was looking at their grant and noticed – was interviewing folks and they had an accountant who was a contractor. And as I went through their records, I found she had prepared an invoice for her contracting services. She was a self-contractor. She submitted it. And then as the accountant, she'd approved it and paid herself. And I thought – (inaudible). So you want to have effective oversight and some internal controls.

Another one of our big areas of findings – and Rochelle (sp) and Tiffany (sp) can say this – is you have a great book with all your policies and procedures. And then we interview staff. And what we do is we say pretty much from the person who – it's the first person you see in the front door to your CEO or your president or your principal, we say tell me what happens. Tell me how this process works. And we find out that nobody knows or follows the policy and procedure that you have. And so training is very, very, very important.

And then communication and information sharing. I think there is a huge gap sometimes from the folks who put these things together, whether it be you as the project management. Maybe it's someone higher up or outside in the organization that passes on some of these policies and procedures. But if you all as a group don't make sure your staff understand and you communicate and you understand why, that's when things are going to be ignored.

So another one of our focus areas, if you can imagine, is making sure that you have reliable and current information. We never get that warm and fuzzy feeling when we go out and we can't be given an exact number for how much money you have left, what's obligated, what's expended, where you are in terms of any match requirement.

So it's really important that your accounting system is kept current, that we can come in and see that you have controls in place, whether that be two signatures on a check, an approval chain that's followed, robust records, that you have a good asset management system. You may be giving out bus transportation or other types of supportive services to students, that we're tracking those, that we're making sure that you have a policy for how you distribute those.

I think one of the biggest questions I get here is can we do this? And I always say, "Well, what's your plan?" Because just one student comes up to you and you say, "Oh. He needs that" and I give it, well, then the next one comes, how are you making those decisions? There has to be a policy and it needs to be consistent. You guys are a school, so we have art program that specialize and you have things for it, but you also likely have something that governs a lot of the student population.

So you want to make sure that just because you have our federal money, you're not treating things very differently. Now, certainly our grant is to do things different than your school does, but that doesn't mean you can change your behaviors. It doesn't mean that all of a sudden you can buy the top of the line things when the rest of the school gets midgrade.

And then we do have requirements about record retention and access to information. And so we have a seven year policy. So once your grant gets done, all the audit questions are done, you need to maintain those records and we all have access to those records. Next slide.

As I talk about internal controls, you might be feeling a little nervous. And one of the things we like to emphasize is there is no way and I'm not here saying to you that by doing these things you're going to guarantee that nothing happens to the money because things do. And if someone wants to do something bad, they're going to do it and no tracking system, no internal control is going to stop that.

But if you have a good process in place, it's going to give reasonable assurance that you are effective and efficient in your operations, that you're complying with our laws, and that you're reporting accurately and those are the things we care most about. They also provide a mechanism, I believe, that will allow you to catch errors and whether they're errors due to misunderstanding or they're errors due to malfeasance or misfeasance of someone needing extra money and taking a little from the pot. Next slide.

So what are we looking at when we talk about reasonable assurance? So we need to know that the reports you're giving us quarterly are accurate. That information just doesn't come and die here. You guys are a special select group. Many people are interested in you. We have reports that go to Congress, we have reports that go to the White House; we have reports that go to Office of Management's budget. Everybody wants to see those numbers.

And what really they don't like is one quarter we give one set and two quarters later, all of a sudden, the numbers drastically change because of errors. So we really like to be able to say to them, "Here's the numbers and they're consistently reported and they're accurate over time."

We also, then, are assured by having these things in place that you are following not only our requirements, but the general requirements regarding federal grant dollars. And those basic principles are reasonable and necessary and allocable, but they also fall under the cost principles. For example, you could not purchase alcohol, you cannot support entertainment costs. So movie tickets for people, that's an entertainment cost. Can't do it.

Food is a very difficult subject these days. Everyone's heard about the GSA donut, right? The $50 donut. We have a lot of scrutiny on us lately about food, about meetings. There's been a lot of stuff happening and that trickles to all federal awards. So the cost principle cover these things and again, things are reasonable or necessary and allocable, but you need to double check that things are unallowable, such as entertainment, or that there aren't conditions that you have to meet. Next slide.

What else do we want? We want to make sure that all of the terms of the award are matched. So how many of you have read the solicitation under which your award was given? Good. Good. So going back to look at that – because that solicitation has what are the activities you should be doing, what are the activities that are unallowable? Every solicitation has both of those. And your federal project officers use that as a guideline, too, when they come out.

Go back and read your statement of work again and compare it to that solicitation. And then make sure that you have ability to then cross-reference both of those against these government wide standards, the Uniform Administrative Requirements and the cost principles.

It mentions safeguarding a fund. This is critical. Now, computers, iPads, tablets, whatever we're using these days, I know that you guys aren't heavy equipment grants, but there's a lot of supplies you're buying and we're not talking about marking every pencil, but we're talking about keeping track. And so especially when our program, as I understand it, you have separate little parts where the students are versus the population, you have to have a system in place to control the things being bought with our funds for our students from wandering out amongst the general population.

So we're going to be looking for inventory lists; that general relates to equipment, which is $5,000 or more. But I would put as my personal caveat, laptops, computers that are less than $5,000. Those are good to keep an inventory of. Have them logged and tracked and know where they are. The same with iPads, phones, things like that.

If you are going to have any type of cash-like things – gift cards, bus or transportation subsidies, tokens, whatever we use these days, those should also be safeguarded.

So locked cabinets. People sign in and out. You have a method for tracking them.

And then the last for this is that we do – and you have students so I know you're aware of this – is we are very closely monitor personally identifiable information. So the extent that you have records that contain PII, those must be safeguarded. So locked file cabinets. Never ever, ever e-mail something with PII in it unless it's encrypted.

Simple encryption software works. If you're storing data on a laptop or flash drive, I encourage you not to have PII there, to use random identifiers. If it is PII, again, it must be password encrypted, and the password kept separately and secured. So you would never want to send a file with the password in the message you're sending. All right. Next slide.

So as you can see, this what the statute said; it's everything we talked about. The only two areas I haven't covered yet are evaluated and monitor compliance and take prompt action.

So I think another area that we see when we go out and monitor is that you start up really strong and you have all the policies and then a year goes by and staff turns over, or you change course. You're starting a new grant new program a year in, things shift, and there isn't that look back at where are we now? Are these policies and procedures still accurate? Is this the method we're going to use them? How are they working? Are people following them? Am I sampling the case files to make sure that all the documentation is there so that when Rochelle or Tiffany come out, I'm confident that what they pull is going to be a full case file?

And then if you find that there's not compliance, if you find that there, immediately act. Have a training session for staff. Go back to the procedure and make updates as needed. You know, I don't know how many of you are involved in the workforce system, but it always gets a chuckle. We have staff going out now in 2015 and finding procedures that date back to something called the Job Training Partnership Act, which was last used in 1996 – never updated. So make those updates. Keep current.

If you have a breach of PII, we have special procedures for that and it must, must, must be reported immediately. I can get you a guidance number. We have a security hotline you have to report it to. Next slide.

So let's pause for one second and does anyone have any questions on this big broad overview? Common sense.

All right. So let's go into what we call the COSO. And the COSO looks at – and we're going to modify this in our minds because you guys don't have boards of directors – but we talk about how you have the path functions of the board of directors, the head of management, the top folks, and where they fit in. And then you have the reasonable assurance component, that we are going to make sure that our operations are reporting and are compliant are going to be ensured by putting in place this framework. Let's move on.

So this is where we have. So we start with our risk assessment, we're going to move to control activities, to information and communication, monitoring, and then control environment – I guess we start with control environment.

Control environment, risk assessment, control activities, information and communication, and monitoring. We have tried very hard to come up with an acronym for this that makes sense and isn't too bad. We PRIME (ph); it didn't really work. It didn't really make sense. So we're the government; we have to come up with an acronym. So we're still working on it. Maybe next year. All right. Next slide.

So the control environment. This is laying the foundation of your house. This is ensuring that how you approach the business is pervasive. That we have an attitude that documentation is what we do. It's not OK not to document. Not OK to wait to the end of the month. It has to be pervasive. It has to start at the top and it has to be your culture.

The positive tone that we laugh about, I love talking about Dilbert, the evil boss that everyone laughs about. You have to make sure that it's not just words focused on the topic of your organization, that it's actions; that people see that the person at the top is doing exactly the same as they are and follows the same rules and have the same tones. And then it's positive. that we're all here, we all have these onerous rules that the federal government puts on our money, but look what it's getting us and we have to do this.

And then it's hard to say, but looking at the integrity, the ethical values, the competence of you employees, and your management's philosophy and operating style. We want to make sure we're not operating in an environment where we're cutting corners, that we are compliant; and that we're making sure our staff are trained. The worst thing that could happen is someone gets thrown in and we're all too busy to train that person and there they are trying to working the way they don't know. And the next thing you know we have a big problem on our hands, not due to any malice; just due to the person's incompetence and lack of oversight.

All right. So once we have our good foundation, we have a tone set from the top, we move on to the next step. Next slide, please.

Then we have to look at our risks. And you might think, risks, what are we talking about? We're going to talk so many different things that you want to think about. We give you some questions of what is the likelihood is occurring? What would the impact be? How do we prevent it? And what's our vulnerability or likelihood of loss?

So I've seen situations where there's been floods in the Midwest, buildings have been wiped out, records gone. How do we keep going? How do we come back from that? How do we meet our requirements?

I have had cases where people aren't submitting financial reports? Why aren't we sending financial reports? Well, our accountant is pregnant; she's on bed rest. And then she had the baby and there was no one else to do it. Said, you didn't have a backup plan for your accountant? What are we doing?

So it can be many different sources. And it sounds kind of crazy, but lock yourself in a room for a day retreat and come up with all these things that could happen. What would happen if? You know, we had to help our grantees recover from big hurricanes. We had Sandy. We had Katrina. You know, folks got back on their feet because they were desperately needed in those cases. How do we do that?

What do we do if all the computers go down? All these different things. How do we get back? What's our policy? Do people understand what they're supposed to do? All right. Next slide, please.

So we talked a lot about equipment. Securing equipment, ensuring that authorized folks have access. You know, the periodic inspections is a good thing to do. I will give an example from here at DOL. It was about 12 years ago. So things have changed. But I wanted a certain tech software on my computer. And they said, well, all the licenses are used. And I said OK. Well, who has the licenses? Maybe not everyone needs them. And we don't know.

And I said, OK. And then they finally came back and said, well, so and so has it. Well, so and so retired three years ago. So can I have that license? They were not keeping track of who was using the computer licenses. They had no way to know. I guarantee that has changed now. But it's little things like that where we – so now, pretty much every year we get e-mails saying, are you using this software? Do you need it? Things like that.

You also want to look at security and the vulnerability. We have some grants at CTA that they are buying $800,000 pieces of equipment. These aren't your grants. So in those settings, we really need to make sure that that equipment is protected; it's insured. Insured and allowable cost under these grants. So something with our dollars, assurance against that. Insurance against general loss is not allowable. Just like a general rainy day policy, in case you're sued, something like that, not allowable. You buy a piece of equipment and you want to get that extended warranty or that protection on it? That is allowable.

So we also talked – we want to make sure you understand that cash, credit card, laptops – I don't know how many of you, if your programs have corporate credit cards, but those are a mess. We see lots – what did we see a couple of weeks ago? Amazon Prime memberships, hair salon charges, big stuff. I don't think they were using our grant funds to necessary pay for it, but they were using the card and you just – that was against the policy and procedure.

All right. Next slide. I don't make this stuff. But you have to remember, I'm the big bad gun so I only hear about the really bad things.

OK. So what do we want to do for our control activities? We want to have policies, procedures, and processes. And this is what guides us all. And in a perfect world, everything you do should be governed by this policy and procedure. Now, I'm not saying you have to have these all out and landed on your desk and you can't be here outside the line, but there should be a step.

You know, when you're doing intake and you're meeting with a student, there should be a set of questions that you're asking consistently every time and that there should be a method that that's documented and how it's kept in the file so that it's the same for every student and you're not missing anything. Because that's going to make sure that we're reducing the risk of that activity not being allowable, that student not missing out on services that were required under the grant.

And so we want to make sure that these happen at all levels. So I'm not just talking about those front level people. The work that you do should be under this. And the work of your bosses should be under that to the extent that they're working on the grant. What is their method of checking in with you? I mean, is a certain percentage of their time donated or are they supposed to be signing off?

So it's really important for us to understand who approves what and what are the separations of duty? Because we're going to be looking for that. When we go in and we very specifically start with your financial reports and then we go to your accounting system and then we start picking charges out of there. And then we say we want to see the documentations and we're going to look and we're going to say, who approved this? Who checked that the cost was allowable?

So again, just making sure that things are being carried out, the right people are checking off, and that we have some adequate separation of duty. I know it's hard. You probably have a small staff working on this grant. So it's really important to have your org chart to note what everyone does, what the backups are. Maybe we have to pull in some folks occasionally from outside your port cluster if people are out. But having those backup plans in place is really important for us to know, especially when it comes to financial reporting. It's never an adequate excuse not to submit your report because someone's on vacation. So you either need to make sure there's someone else available or that you submit it early.

And I always like to point out there's two pieces of information; you have a password and a PIN to submit your financial report. And the password typically goes to the person who enters the data and the PIN goes to your certifying official. More often than I would like to admit, we send out communications and the grantee says, "Oh. That person hasn't been with us for two years." Well, that's funny because the PIN linked with their name and their name has been on your financial report every quarter for the past two years.

So if I was the person who had that PIN, before I left my job, I would notify the Department of Labor that I was leaving and they needed to issue a new PIN to the new person because otherwise that person's name remains on there and it's the same – you are certifying that everything is true and accurate.

So if that person is going to be on vacation, we would have to know. I mean, they would either have to very much trust the person they gave that PIN to to certify it or they would have to submit it early. I would do it early. If it were me and my name on the line, I would not give my PIN to someone else. All right. Next slide.

So this is what we're thinking about when we talk about separation of duties, that you have the custodian, the person who holds and has custody. And then you have the authorization. Who's authorizing this transaction? Then you have the person who's recording the transaction who's separate from the person who holds it, the person who authorizes it. And then you have the person who's reconciling at the end. So you have four different points and checkpoints to ensure that something funky's not happening.

Now, we have a true story from one of our regions where he said – it was interesting. They were – I guess this was in his life prior to the federal government, but he was in an organization where the guy who never took time off – ever. And everyone thought he's such a great employee. And then somehow he came across some of this work and he started looking. And the reason he never took time off was because there was no separation. He did all these things and he was covering a lot of stuff. So it's always good to keep in mind that by having four separate people, you have a reasonable assurance that that's not going to happen.

Now, those people can collude. No one can stop that. But you have a reasonable assurance. All right. Next slide.

All right. Timely capturing of information is important. One, you're required to report to us as transactions occur on our quarterly financial reports. So it's really important that there's not a lag. You want to make sure that you have a communication system in place so that information is getting out. You're in a complex situation. You don't have control necessarily over those accountants that you're working with. They don't have control over you. You're in separate places.

So you need to make sure that you're communicating back and forth. They can't submit an accurate financial report without information for you. And you need to hear from them about where you are monetarily because you might be hitting the point where you need to request a budget modification.

So it's going to be important – and when we talk about budget controls, we're going to talk about how you should be getting together regularly and what you should be comparing.

You also want to make sure that that communication system goes more broadly than just about the money. How are we doing? How's case management working these today? How's the intake? What are our trends? What are we seeing? What are blips?

And then we want to spot check records and we want to make sure that everyone understands that the records and the information systems are reliable and acceptable.

I went to a place – this is the same place with the accountants who did everything. They had a lot of problems. I went in and I kid you not, the first day, I said, OK. I need to know this. They said, oh, so and so. Well, she's out today, but she'll be back tomorrow. I said, OK. So then I went over and I sat in the program office. And then I went talked to the accountant, said, well, I need this. And they said, oh, we definitely don't have that. That's definitely so and so – Marsha (sp). I think it was Marsha. All right. Marsha's out the next day, too. Comes back. Marsha said, well, I don't do that. You got to talk to so and so. I already talked to them. You know, it was just like a game of telephone and it was crazy that no one could – and that was actually a state. It was kind of sad. All right. Next slide.

Monitoring. What do you want to look at when you monitor? It's a big word. It's a scary word. It's what we do. You want to look are things operating as I intended them to operate? You know, people, when you say monitoring, people think well, I'm going to be monitored or I need to monitor if I give my money out to someone else. But self-monitoring is just as important and I think it's a piece that people don't think about as much.

So are things operating as they intended? Has this become out-of-date? You know, because it could be we started out thinking this is the way it's going to work and then we realized it didn't work that way so we changed how we did it, but we forgot to update the policy.

Monitoring occurring in every day course of operation. It's just a regular part of what you do. Part of your management meeting. It's part of supervising. It's part of the personnel that you have as they do their duty.

(Off-mike.) Not sure? Do you guys have subrecipients? OK.

So then it's making sure that you are monitoring those that you've given money to because you are the entity that are the accountable ones. I have no relationship with your subrecipient. So if it turns out something went wrong, I'm not going to talk to them; I'm going to talk to you. You are going to owe me money. You are the one that's going to have finding. You want to make sure that you are very diligent about monitoring them for requirements, efficiencies, money, and that you're getting information from them timely and accurately for reporting. All right. Let's go to the next slide.

What are some key activities? Next slide. So I have a little example here and I think Dante (sp) came in with handouts. Are they over here? OK. All right.

And so for folks that are on the webinar, I believe Brian is putting this up as a file share. It talks a lot about policies and procedures. And so we think that there are some key areas that you want to have and I'm also passing out and available for file share is actually a very long list of recommended. It's four full pages of areas we think you should have policies and procedures on.

Now, these aren't all required, not written in writing. But you do all of these and you're probably not going to have a lot of problems with us. The big areas – budgeting, your cash management, purchasing and contracting, absolutely essential. Cost allocation; how are you allocating cost? Does it benefit my program 100 percent? Or is it part – are you splitting it? Is the money coming from somewhere else or someone sent me?

Accounting and payables, property management, personnel and payroll, financial reporting, your information systems, any participant related payments, and then finally, travel. Those are the key critical areas. And then, as I said, we got four pages of potential other areas. All right. Next slide, please.

So I know one of the thoughts going through your head is if I have to do all this, I'll never be able to get work done. Just want to keep in mind that if you have an effective control and effective procedure, it actually helps you rather than hinder you. If this is hindering you, it's not effective. So it really benefits rather than encumbers your management and that's the point of them.

And what I always say, if there's a lot of grumbling from the staff that this procedure is not working, then it really would be in everyone's interest to get together and get feedback about what would make it work. Because if it's hindering, then it's not doing what it's intended.

Internal controls are cost-effective. You should not be adding a lot of money. This is actually helping you by being more efficient. You assets are safeguarded. They are in line with your school and your school district's policies and procedures. Nothing that I'm telling you should make you go back and say guess what? I don't have to – (inaudible) – on this, unless theirs is in blatant violation of ours and I just can't imagine that happening.

And then finally, we want to make sure you're operating the most efficient way possible. And oftentimes that's why we are looking at your budgets closely and we are asking for more information because we're trying to understand why this budget change was needed. What happened that precipitated this that cost had to spiral? All right. Next slide.

So for small entities and I feel it's the small nonprofits that have four fact people. That's a little different. Your organization, because of the nature of these grants that may be smaller, too, you might have some different implementation factors. The standards all remain the same, but you have to look at how you're going to do it. You might have to get management more involved. You might be much more involved in things than a larger organization.

You're going to have a lot of direct interaction with the staff and you have to make sure that the communication lines are very easy. In a very large organization or a large government, they're having official memorandums that go out to everybody versus a staff meeting.

(off-mike question)

MS. EWELL: I'm sorry, too. Compensating controls. You want to make sure that in a small organization, you are doing some random transaction reviews, you are adding levels of reviews because there aren't as many opportunities for checks and balances. If you have three people there, you can't do what I said by having four different people handle it, right? So you have to build in some compensating controls. All right. Next slide.

So we do have some limitations. Obviously, cost versus benefit. Some of these things may cost money, especially as we relate to information systems and asset mapping systems.

Judgment. You can't teach someone judgment, right? So all you can do is try to convey your philosophy to staff and train them on the policies that your organization has, train them on the procedures, and hope that everyone exercises good judgment.

And again, just as a reminder, so the policy is that big vision statement coming down from your organization. And the procedure then is more of a step-by-step how you're going to implement.

Breakdowns. Breakdowns can occur. I know it can be a busy time. People are out. People are subbing. New staff. It's how you recover from those and you document it that's important. If you have a one-time breakdown and Tiffany comes and she picks that file and you have documented that something happened and that you course corrected, then that's not going to be as problematic as if we come and find lots of breakdowns. So how you come back from the breakdown is really important.

Management overrides. You know, this is where we talked about tone from the top. I think there's nothing more demoralizing for staff who are following everything and doing what they should and management comes in and says, no, do it differently. And then staff is in that position of well, I don't know; it's not supposed to be that way. And they feel that they can't stop management.

And this is really important in the grant world, especially with the relationship between your accounting and you because the accounting office is the one dealing with the dollars and the cents and they might be, like, well, you don't have enough money left in this line. And management says, no, we're doing it. There has to be that clear communication and that lack of reprisal that people communicate because otherwise everyone's going to get in trouble.

And I mentioned the risk of collusion. You know, we have many, many cases and unfortunately – a lot of times, people are related when they do this. They collude. Invoices are for more than the cost is. But you don't know that because the person gets the invoice and maybe someone's checking it and if people are colluding, you can't catch that. But I will say that these last two are the biggest reason that we have whistleblowers. We have a hotline that goes to our inspector general.

And most of the time when we find out – because we can go out and monitor and everything can look great. What happens? Someone will call because their manager told them to do something different. And even though as we sat down there and interviewed and they answered all our questions and it was great, they are so uncomfortable after that meeting, they called that hotline the next day.

And the same thing with collusion. People find out about it and they might be afraid because they know it's their management colluding. They call the hotline. So those are the two areas I think with internal controls that I always say in the end, I never know what people are thinking when they do bad things, but we do find out. And usually, it's because people report. Next slide.

So why do we need these things? You know, I think we've seen a lot of business interruptions over the years because of system breakdowns, we've seen hurricanes, reworking to correct for errors. So having a solid internal control framework, doing that planning of what if, what if this happens, it really benefits you in the long run because you have a much more limited interruption. You can get back off the ground really quickly. Next slide.

If you don't have the policies and procedures and think through them, it can lead to erroneous decision making; bad information. You want to make sure that everyone talks about these things up front, you've thought them through. Really good, especially for upper management, to know what the scope of the grant is.

You'd be surprised how many times I think when the upper leadership signed the application, but actually maybe haven't read it or haven't been briefed on it. And they get the money and they think I'm going to do all these great things. And you say, whoa, whoa, it's not actually for that. Trust me. Again, I've heard it all. So next slide.

And then obviously, we have fraud, embezzlement, and theft, and this is in the paper every day. Apparently right now they're making a documentary that there's a case of a woman who's apparently the biggest municipal staff over the course of 25 years or something. She was a city employee. So I'm planning to – it'll be a big night out for me to go see the documentary. I have three little kids.

But these things happen, but it also happens the other way. And we had a case – these things, they break your heart, but we went in and picked the transaction and apparently the guy who – low-level staffer went, "Oh. I wish you hadn't picked that one." And it turned out that he was in a big financial pinch that month and he had given himself some money and paid it back the next month. But still that's not legal. So it was reported to the proper authorities. He had to plea bargain. So it happens. It happens.

Loss, misuse, or destruction of assets. I think unintentional loss is huge. Potential loss. You know, I mean, people come in and steal laptops. That's a big thing. Whether they need it, whether they want to sell it. If you have iPads or something like that, they're going to want that. So lots of assets in cars is a huge risk because they're – even people who might not want to, if there's opportunity, oh, look, they're just sitting here and no one's around. No one will even notice if I just take a few.

And then it comes up to rationalization. That man I mentioned, he really needed the money and I'm just going to pay it back and he did. It can rationalize in your head when you're in a bad situation. All right. Next slide.

So what we see in monitoring reviews are a lack of understanding and staff. They don't really understand what they're supposed to be doing. We'll even see duplication of efforts. You know, staff doing the same things, even though that's not the role. And sometimes they're doing it differently. So that's not good.

Inadequate training. I always say one of the most common – we have a finding and what's our recommended action? Training, training, training. Train your staff on what you have. Develop something and train your staff.

The outdated policies, the inadequate management systems, this is what we go in and find. It's not necessarily that you did anything wrong. Your procurement might've been OK. You might've given out the gift cards fine, but you had no policy you were following.

All right. Inadequate resources. You know, I think that big one comes down to – it's not so much dollar resources. A lot of times it's people resources. You know, we're not feeling, necessarily, the large organizations. And I go back to my person, the accountant that was out on maternity leave, they only had three other people. So we have to figure out a way to ensure that we have adequate resources. All right. Next slide.

First bullet has always sounded a little patronizing to me, but it's competent, reliable and ethical staff. You know, that's obviously all of our goals. But I think the best thing you can do is have a really good mission statement when you're recruiting folks and reference checking. You just want to find someone who supports what we all do, right? We're a nonprofit world. We're here to help train people. We're not in it to make money.

Set the control environment. That's really critical. The organization has to – the foundation for a big thing. And there's compensating controls in a smaller environment. Everything's done in writing and everyone is incorporated into the process. This is critical. I know as a staff person, it was very frustrating for me when I would – and they did this with our system. And they said, OK. Here is this new system and here is how you use it. And I'm, like, what is this? And it took me forever to approve my contractor invoices. I still can't do it. And I thought, God, I wish I had been part of a focus group. I would've told you exactly what I needed. So it's really important to include everyone.

And that includes your top leadership because they have things that they want to have met. They say, I need this information and this is the way I need it. And then that lower person says, oh. Is that why I have to do it that way? OK. Keep the circle full.

All right. Anything else? I don't think my cartoon's in this one. I have a Dilbert cartoon, but because they're copyrighted, I'm always a little careful about that when we're putting it up online. All right. Next slide.

Oh. Yes. We have a little quiz for you. So if you want to take a couple of minutes and then we'll deliver the answers.

Brian, can you put the quiz up online?

MR. KEATING: Sure. I think for the quiz, it looks like it's a pdf. So maybe people can download that. Or let me see if I can replicate that. Hang on one sec.

MS. EWELL: Sure.

MR. KEATING: Yeah. I think people should probably download this and take it on their own. It looks like there's a bunch of different questions here. So folks, if you're virtual with us today, you can download that in the file stream window. (Pause.)

MS. EWELL: All right. Looks like most people are finishing up. So what about the first one? True or false. Internal controls are concerned with the reliability of financial information? True?

MR. : It's true.

MS. EWELL: True. Incompatible duties exist when an employee is in a position to perpetuate and conceal errors or fraud. True or false? True. Absolutely.

Well-designed internal controls will prevent all fraud by top management. True or false?

MR. : False.

MS. EWELL: False. It can never prevent all fraud. The relatively low number of types of transactions incurred by small entities makes the segregation of duties impossible. True or false?

MR. : False.

MS. EWELL: False. Right. You can have those compensating controls in place. All right.

And we have three multiple choice questions. Which of the following is least likely to be evidenced of effective internal controls?

MR. : C.

MS. EWELL: Actually, B. Monthly accounts payables. Because by having a monthly list, it's just less effective than if you maintained a list of vendors the organization is allowed to use for comparison to prevent ghost vendors.

Now, those who said A, supporting documents marked processed would be least effective, this control can be extremely effective in preventing duplicate payment, especially when the original documents are allowed to be processed.

All right. Then we get to six. What is not considered one of the five major components of internal controls?

MR. : B.

MS. EWELL: B. Correct. The five components, again, were control environment, risk assessment, control activities, information and communication, and monitoring. Segregation of duties falls under control activities.

And then the last one, seven. Of the following statements about internal controls, which one is not valid?

MR. : B.

MS. EWELL: It's actually D. Internal control activities reasonably ensure that collusion among employees cannot occur. We can never ensure that collusion won't occur. If people want to do it, they will do it.

All right. Are there any questions with our remaining three minutes? OK. Great.

Well, I will be back here this afternoon to talk about budget controls. We're going to have some fun little spreadsheet, play around on the computer, and then I will make sure we leave enough time at the end, probably about 15 minutes, for administrative cost and indirect costs. Thank you all.

Brian, back to you.

MR. KEATING: All right. Great.

(END)