

Agency

Risk

Management

and

Internal

Control

Standards

ARMICS

Comptroller's Directive No. 1-07

(The Commonwealth's version of the Sarbanes Oxley Act)

“...provides guidance for establishing and assessing agency internal controls in order to more effectively manage risk and maintain accountability.”

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The assessment of UMW internal control must be completed and certified to the Department of Accounts every June 30.

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Definition of Internal Control:

Ongoing process led by agency head to design and provide reasonable assurance that these types of objectives will be achieved:

- Effective and efficient operations
- Reliable financial reporting
- Compliance with applicable laws and regulations
- Safeguarding of assets

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Effective system of internal control:

- Provides accountability for meeting program objectives
- Promotes operational efficiency
- Improves the reliability of financial statements
- Strengthens compliance with laws and regulations
- Reduces the risk of financial or other asset losses due to fraud, waste or abuse

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The objective is to provide reasonable assurance of the integrity of all fiscal processes related to:

- Transactions submitted to the Commonwealth's general ledger
- Deliverables required by financial statement directives
- Compliance with laws and regulations
- Stewardship over and safeguarding the Commonwealth's assets

*In short, to **ensure fiscal accountability and safeguard the Commonwealth's assets.***

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The Commonwealth of Virginia has designed these Standards to achieve five objectives:

1. **Strategic** – to support “being recognized as the best-managed state in the nation” through internal control best practice
2. **Operational** – effective and efficient use of fiscal resources and other assets
3. **Reporting** – integrity and reliability of financial reporting
4. **Compliance** – compliance with applicable laws and regulations
5. **Stewardship** – protection and conservation of assets

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Components of Internal Control:

To meet Virginia's Standards, an agency must demonstrate that it has five internal control components established and fully functioning:

1. Control Environment
2. Risk Assessment
3. Control Activities
4. Information and Communication
5. Monitoring

1. Control Environment

Internal Control requires an adequate “Control Environment” foundation. The environment reflects top management’s expectations for how seriously agency employees should view and execute their fiduciary responsibilities.

- a. Management Philosophy
- b. Reasonable Risk
- c. Oversight by the BOV
- d. Integrity and ethical values
- e. Promoting ethics & appropriate conduct
- f. Organizational structure
- g. Assignment of authority and responsibility
- h. Work force competence
- i. Employee development

1. Control Environment

a. Management Philosophy

- Shared beliefs and attitudes characterizing how UMW handles everything it does
- Reflects UMW's values, influencing its culture and operating style
- Affects how the fiscal programs can implement, maintain and enforce control
- Appears in policy statements, oral and written communications and in decision making
- Reinforced with everyday actions

1. Control Environment

b. Reasonable Risk

- Internal control cannot be perfect and includes an element of risk
- How UMW manages risk reflects its management philosophy, affects the integrity and reliability of its reporting, compliance with laws and regulations and its protection and conservation of assets
- Management can not eliminate all risk and accepts some level of residual risk
- UMW management may only accept reasonable risk that relates to operational objectives
- Risks that jeopardize compliance with financial reporting or legal requirements can NOT be accepted and if present, MUST be eliminated as soon as possible

1. Control Environment

c. Oversight by BOV

- BOV members play a critical part in creating a control environment, assessing control adequacy and monitoring performance
- Independent from management
- Effective boards require effective internal control programs

1. Control Environment

d. Integrity and Ethical Values

- UMW's strategy, objectives and implementation stem from preferences, value judgments and management styles
- UMW's management commitment to ethics influences these preferences and judgments which translate into behavioral expectations
- Effectiveness of control activities can NOT rise above the integrity and ethical values of the people who create, lead and monitor the agency programs
- To protect UMW's reputation, standards of behavior must exceed mere compliance with law

1. Control Environment

e. Promoting Ethics & Appropriate Conduct

- Communicate these core values through a code of ethics or similar document
- Develop and reinforce a comprehensive and understandable code is a “best practice”
- Essential to internal control, linking UMW mission and vision to its operating policies and procedures

1. Control Environment

f. Organization Structure

- UMW's organization structure provides the structure to plan, execute, control and monitor activities
- Sound organizational structure defines key areas of authority and responsibility
- Organized by services, locations or enabling statutes

1. Control Environment

g. Assignment of Authority and Responsibility

- Degree to which individuals and teams are authorized and encouraged to use initiative to accomplish objectives and solve problems
- Establishing reporting relationships, fixing authorization, procedures, issuing policy that assigns appropriate personnel to each program
- Critical challenge is delegating to the extent required to achieve objectives, ensuring that decision making is based on sound practices for risk identification and assessment
- Ensuring that everyone understands UMW objectives and how their job contributes to meeting those objectives

1. Control Environment

h. Work Force Competence

- Reflects the knowledge, skills and abilities needed to meet objectives
- Management sets competencies for particular jobs and translates those into EWP and employee development programs
- Provide qualified and committed personnel to key control positions

1. Control Environment

i. Employee Development

- HR practices for hiring, orientation, training, evaluating, counseling, promoting, compensating and remediation sends messages to employees about expectations for integrity, ethical behavior and competence
- Continuous training and education should be provided
- Essential that employees be groomed to tackle new challenges as UMW becomes more complex

2. Risk Assessment

- The process of analyzing potential events and considering their likelihood and impact in order to determine those events' possible affect on the achievement of UMW's objectives
- Management considers the mix of potential events, both expected and unexpected, relevant to UMW and its activities in the context of the UMW's risk profile
- Many expected events are routine, recurring and already in UMW's programs and budgets
- Management must assess the risk of unexpected potential events
- Risk assessment is a continuous and repetitive interplay of actions occurring throughout UMW

3. Control Activities

- Policies and procedures implemented to help ensure that risk responses are effectively completed
- Occur across UMW, at all levels and in all functions
- Range of activities such as approvals, authorizations, verifications, reconciliations, security over assets and segregation of duties
- Managers set up control activities to provide reasonable assurance that their objectives are met
- Categorized by the nature of the objectives to which they relate
- Could be as simple as listing tasks assigned to staff members and then occasionally checking to verify completion on time

4. Information and Communication

- Involves identifying, capturing and communicating relevant information in a form and timeframe that enables employees to carry out their responsibilities
- Effective information and communication process will assure that all personnel receive a *clear message from top management that **internal control responsibilities must be taken seriously***
- UMW needs information to handle risks, provide services and achieve its objectives
- Quantitative and qualitative information comes from internal and external sources
- Information enables change management strategy, identifying events, analyzing risks, selecting risk responses and performing other management activities
- Information without communication has no value

5. Monitoring

- The process of assessing the presence, functioning and continuous improvement of internal control components
- Accomplished through ongoing management activities and/or separate evaluations
- Examined from three perspectives:
 - Ongoing activities
 - Separate comprehensive evaluations
 - Special ad hoc evaluations

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- Each state employee has a personal internal control responsibility
- UMW executives and managers must support UMW's internal control philosophy, promote compliance and maintain control in their area of responsibility
- The Chief Financial Officer and Fiscal Officer have the key oversight and policy enforcement roles over fiscal matters
- Other agency managers may hold lead responsibility for compliance with non-financial aspects of laws, directives, policies, procedures and code of ethics

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POLICIES AND PROCEDURES:

- must be documented to select a 3 or above on the survey
- establishes and maintains effective internal controls
- helps ensure that UMW meets its goals and objectives
- assists UMW in assessing its internal control structure
- helps manage risk more effectively
- maintains accountability within UMW
- softens the impact of turnover

1 = Strongly Disagree

Internal Control reliability level is defined as **initial** with the characteristics as indicated below:

- | | |
|---|-------------------------------|
| ■ Documentation – | Very limited |
| ■ Awareness and Understanding - | Basic awareness by management |
| ■ Perceived Value to Employees - | Unformed |
| ■ Control Procedures – | Ad hoc, unlinked |
| ■ Monitoring / Testing - | No monitoring |

2 = Somewhat Disagree

Internal Control reliability level is defined as **Informal** with the characteristics as indicated below:

- **Documentation -** Sporadic, inconsistent
- **Awareness & Understanding -** Understanding not communicated beyond management
- **Perceived Value to Employees -** Controls are separate from business operations
- **Control Procedures -** Intuitive, repeatable
- **Monitoring / Testing -** No monitoring

3 = Somewhat Agree

Internal Control reliability level is defined as **Systematic** with the characteristics as indicated below:

- **Documentation -** **Comprehensive & consistent**
- **Awareness & Understanding -** Formal communication and some training
- **Perceived Value to Employees -** Controls integral to operations
- **Control Procedures -** Formal, standardized
- **Monitoring / Testing -** No monitoring

4 = Agree

Internal Control reliability level is defined as **Integrated** with the characteristics as indicated below:

- **Documentation -** Comprehensive & consistent
- **Awareness & Understanding -** Comprehensive training on control-related matters
- **Perceived Value to Employees -** Control process considered part of strategy
- **Control Procedures -** Formal, standardized
- **Monitoring / Testing -** Periodic monitoring begins

5 = Strongly Agree

Internal Control reliability level is defined as **Optimized** with the characteristics as indicated below:

- **Documentation -** Comprehensive & consistent
- **Awareness & Understanding -** Comprehensive training on control-related matters
- **Perceived Value to Employees -** Commitment to continuous improvement
- **Control Procedures -** Formal, standardized
- **Monitoring / Testing -** Real-time monitoring

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Thank you for your cooperation on this important project for UMW. Please remember to have your completed Internal Control survey **emailed** to Laura Tabler-Allison (ltabler@umw.edu) no later March 31, 2010. Please email Laura with any questions.