

# **Guide to Internal Controls**

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# CAMPUS PHILOSOPHY ON FISCAL RESPONSIBILITY

(Shared Responsibility for Maintaining Internal Controls)

Every individual within the University has some role in effecting internal control, including each employee, manager, and supervisor, department head, dean, director, senior executive, President and Curator. Roles vary with responsibility. Managers are ultimately responsible for the appropriate use and control of the funds entrusted to them. Management is accountable to the Board of Curators, which provides governance, guidance and oversight, and is also at times accountable to the IRS and funding agencies of federal, state and private grants and contracts. ([See Business Policy and Procedure Manual Section 2:001](#)).

## KEY CONCEPTS OF INTERNAL CONTROL

- **Internal control is a *process*.** It is a means to an end, not an end in itself. The goal is reliable financial reporting, effective and efficient operations, and compliance with laws and regulations.
- **Internal control is affected by *people*.** It's not merely policy manuals and forms, but people's actions at every level of the organization.

## COMPONENTS OF INTERNAL CONTROL

Key steps taken to achieve internal control are:

### Preventative control activities

**Preventive** controls attempt to prevent or deter undesirable acts from occurring. They are proactive controls, designed to prevent a loss, error, or omission. Examples of preventive controls are:

- **separation of duties**
- **proper authorizations**
- **adequate documentation**
- **physical security** over cash and other assets

### Detective control activities (Monitoring)

**Detective** controls attempt to detect undesirable acts that have occurred. They provide evidence after-the-fact that a loss or error has occurred, but do not prevent them from occurring.

- Regular **supervisory review** of account activity, reports, reconciliations ([See Business Policy and Procedure Manual Section 2:005](#))
- Routine **spot-checking** of transactions, records and reconciliations (do things make sense and look reasonable)
- **Variance analysis**, including budget to actual comparisons

- **Physical inventories**
- **Control self assessment** (such as this Guide and related Self-assessment Questionnaire)
- **Internal audit** review of business unit's controls

#### Information and communications

- Administrative information systems that provide necessary information to the appropriate people, at the necessary level of detail, on a timely basis
- Channels for employees to communicate suspected improprieties upstream through other than a direct supervisor

#### Risk assessment

Management is responsible for assessing risks that could undermine these objectives of financial statements:

- Establishing the existence/ownership of assets and liabilities
- Proper valuation of assets and liabilities
- Contain all transactions of the reporting period
- Proper presentation and disclosure

#### Control environment

A ***control-conscious environment*** is also necessary. It is an environment that supports ethical values and business practices. Management is responsible for "setting the tone" for their areas and encouraging the highest levels of integrity and ethical behavior, as well as exhibiting leadership behavior that promotes internal control and accountability.

The following steps are examples of this leadership behavior:

- **Communicate to employees that fraud and conflicts of interest will not be tolerated.**
- **Communicate to employees that University policies and procedures are important and will be followed.**
- **Make employees fully aware of their responsibilities, including internal controls.**
- **Monitor the internal controls system on an on-going basis.**

## **SUSPECTED THEFT OR MISUSE OF ASSETS**

See [\*Business Policy and Procedure Manual Section 8:010\*](#) for procedures that should be followed to report the loss of money, securities and property. A written report is required, and in certain cases a telephone report. Prompt reporting of losses increases the likelihood of recovering assets and limiting their misuse.

## SEGREGATION OF DUTIES

- **No single person should:**
  - **record transactions and reconcile balances.**
  - **handle cash and verify deposits.**
  - **handle assets and reconcile perpetual records to physical counts.**
  - **enter or approve a check request and have the check returned to themselves.**

Segregation of duties is essential to effective internal control. It reduces the risk of both erroneous and inappropriate actions. It is a deterrent to fraud. Key functions that must be adequately separated are described above. When it is extremely difficult to separate these functions, a detailed supervisory review of related activities or transactions is required as a compensating control activity. To ensure proper separation of duties, a person should never approve a transaction for which they are the payee.

## REVIEWS BY MANAGEMENT

- Perform budget to actual expense comparisons and investigate significant differences.
- Routinely spot-check transactions, records, and reconciliations to ensure expectations are met as to timeliness, completeness, segregation of duties, propriety of the transaction, etc.
- Follow up on unexpected results or unusual transactions. They might be indications of theft or fraud. Ask for explanations of unexpected results and ask for reasons for unusual transactions. Question the explanations and reasons if they don't seem right, ask to see the items that were purchased, etc. (See Suspected Theft or Misuse of Assets section in this Guide.)
- Document your reviews of reports and reconciliations by initialing and dating them and briefly indicating the resolution of any follow-up you performed on unexpected results or unusual transactions.

## RECONCILIATIONS

Broadly defined, *reconciliation* is a comparison of different sets of data in order to ensure the accuracy and completeness of transactions. Integral parts of the reconciliation process include identifying and investigating differences, and taking corrective action, when necessary, to resolve differences.

To ensure proper separation of duties, the person who enters or approves transactions or handles cash receipts should not be the person who performs the related reconciliations.

Reconciliations should be performed timely, documented, and approved by management.

Examples of important reconciliations that should be performed are:

- **Reconciling the dollar amount of cash and checks received per original records (not per the receipt vouchers) to the dollar amount actually deposited.**
- **Reconciling actual payroll expenses to expected payroll expenses.**

## **APPROVALS**

Approval authority should only be given to individuals with sufficient authority and knowledge to recognize and challenge unusual transactions.

- **Control authority to approve with limits on both transaction amount and number of employees granted authority**
- **Review supporting documentation**
- **Compliance with University policies and procedures**
- **Question unusual items**
- **Determine if budget exists**
- **Determine if charges to grants are allowable**
- **No "rubber stamps" or "blind" approvals**
- **No sharing of passwords**
- **No splitting of transactions to avoid higher approval levels**

To ensure proper separation of duties, a person should never approve a transaction for which they are the payee.

If the reviewer notes any transaction(s) that, after his/her investigation, is not a legitimate department expense, he/she should contact his/her supervisor.

Password security should be adjusted upon an employee's termination, transfer, or change in responsibilities.

## **ASSETS**

In addition to cash and inventory, all equipment and supplies, irregardless of original cost, are considered *assets* of the University.

- **Physically secure your area's assets.**

Cash, inventory, equipment, and supplies must be safeguarded from unauthorized access, use or theft. Examples of access controls to safeguard assets are locked doors, filing cabinets, and drawers, and safes. The number of individuals with access to the keys or lock combinations should be as few as possible. Locks should be changed when

employees who had keys to significant amounts of assets terminate.

- **Conduct periodic counts of inventories.**
- **Compare inventory counts to your department's perpetual inventory "book" records and investigate differences.**

Departments with significant inventories should maintain inventory controls over the items. Inventory items received and issued should be recorded, so that a current "book" balance is always known. Periodically, a person who is independent of the inventory purchasing and inventory custody functions should physically count the inventory items. The counts should be compared to the "book" balances. Missing items should be investigated, resolved, and analyzed for possible control deficiencies. "Book" records should be adjusted to the physically counted quantities if missing items cannot be located.

- **Update the fixed asset information distributed to you bi-annually.**
- **Record asset disposals and transfers between areas timely.**

Fixed asset listings should be periodically reviewed and compared to assets physically on-hand. Missing items should be investigated, resolved, and analyzed for possible control deficiencies. Fixed asset listings should be updated accordingly.

## **BANK ACCOUNTS**

- **Individual schools, departments, and divisions** cannot establish bank accounts without the approval of MU Administrative Services (882-7348). ([See Business Policy and Procedure Manual Section 2:035](#))

## **PETTY CASH**

There are a limited number of petty cash funds on campus. The following guidelines are for those departments with a petty cash fund.

- Keep the petty cash fund in a locked, secure place.
- Access to the petty cash fund should be restricted to the custodian and a back-up person.
- Petty cash should be disbursed only by the custodian (or a back-up person in the custodian's absence).
- Require original receipts in order to disburse petty cash. Maintain the receipts in the petty cash fund box for reconciling.
- The person to be reimbursed should indicate on the original receipt what was purchased (if not obvious on the receipt), the business purpose, and account and fund to be charged.
- The original receipts should be approved and signed by an appropriate, authorized individual, such as the supervisor of the person to be reimbursed.

- The petty cash fund should not be used for personal expenses, personal loans, or the cashing of personal checks.
- The Custodian is responsible for regularly reconciling the petty cash fund. (The sum of cash plus original receipts plus any outstanding reimbursements should equal the full, original amount of the fund.)
- Periodic, surprise counts of the petty cash fund should be performed by someone other than the custodian, such as a supervisor.
- A petty cash fund remains open on the records of the Accounting Services Department until you request that it be closed. The Accounting Services Department performs an annual written confirmation of the petty cash account balances.
- Decide if you really need a petty cash fund. If not, contact the Accounting Services Department to close the fund. Deposit the petty cash fund money, indicating on the receipt voucher that it is the closing of the petty cash fund.
- In the event of an unexplained petty cash shortage, see the section on “Suspected Theft or Misuse of Assets”
- [\*\(See Business Policy and Procedure Manual Section 2:120\)\*](#)

## **CASH, CHECK, CREDIT CARD RECEIPTS**

- Procedures should be followed for depositing cash as follows:
  - Locations that deposit directly to the bank should follow the procedures described in the [\*Cash Receipts Manual\*](#)
  - Locations that deposit with campus Cashiers should follow the procedures described in [\*Business Policy and Procedure Manual Section 2.060\*](#).
- Maintain a manual or electronic log of all cash, checks, and credit card payments received (include check numbers). This log should list the amount received, its form (cash, check, or credit card), the payor, and the purpose of the payment.
- Provide numbered receipts for all payments received, regardless of payment type (cash, check, or credit card). Two-part forms should be used, with one copy being kept and one copy provided to the payor.
- All receipts should be properly accounted for and should agree with the log used to record monies received.
- Immediately restrictively endorse checks received with a stamp as described in [\*Cash Receipts Manual\*](#).
- Keep cash, checks, and credit card forms in a locked, secure, and restricted facility, such as a drawer or safe, until they are deposited. Limit who has access and keys/combinations to the locked facility.
- Deposits must be made at least once daily unless otherwise authorized in writing by Campus Administrative Services. If minimal dollar amounts are received, deposits should be made when amounts total \$100 or at least weekly.
- Prepare on-line receipt entries (CRR’s) to the general ledger for each deposit.
- Require an employee with no cash handling responsibilities to verify that the amounts actually deposited equal the amounts from the log or receipts, not from

the receipt voucher.

## **GIFTS**

- Restrictively endorse checks upon receipt by stamping as described in [Cash Receipts Manual](#).
- Make a record of all incoming gift and endowment checks and cash.
- Deposit the endorsed checks and cash with other types of cash receipts immediately, using the Gift CRR application.
- Reconcile your record of incoming gift and endowment checks and cash to the University's gift system (ADIS) to ensure all amounts have been received and deposited.
- Notify the campus Development office upon receipt of non-cash gifts.
- Appraisals of non-cash gifts must be made by an outside appraiser and must be paid for by the donor.
- ([See Business Policy and Procedure Manual Section 2:130](#))

## **PAYROLL/PERSONNEL**

- Non-exempt employees (employees eligible for overtime pay) must complete timesheets of the number of hours they worked each day. This is a federal requirement.
- Timesheets must be approved and signed by appropriate supervisors.
- Overtime requires the advance approval of a supervisor, i.e., before it is worked.
- Track each employee's sick leave and vacation time.
- Access to payroll information should be very limited.
- Direct deposit of paychecks is required for all new employees.
- Do not release wage information externally without the written consent of the employee (or a subpoena).
- Question whether any independent contractors in your area should instead be classified as employees. The U.S. Internal Revenue Service has rules defining independent contractors versus employees. For more information contact Administrative Services, 882-7254.

## **ACCOUNTS PAYABLE**

- Do not request checks to parties outside the University to be returned to departments or employees.
- Original invoices should be sent directly to Accounts Payable by vendors.
- Don't request a rush check or an online (hand-drawn) check if the issuance of the check is not critical.
- Keep supporting documentation for auto-approved (recurring) check requests in

the departments.

- Review invoices related to blanket purchase orders for reasonableness.
- An employee should not also be paid as an independent contractor.

## **TRAVEL**

- Spouse or guest travel is unallowable as a charge to federal grants and usually unallowable as a University expense - look at meal and hotel receipts for evidence of multiple travelers.
- Alcohol is unallowable as a charge to federal grants - look at meal and hotel receipts.
- Encourage the use of the University's travel portal for information about travel at <http://www.campustravel.com/university/missouri>

## **HUMAN RESOURCES**

- Ensure terminated employees are promptly removed from the Payroll system.
- Form I-9 (employment eligibility verification) data must be collected and verified within three days of hire.
- Any court-ordered garnishments, child support orders, and tax levies should be forwarded immediately to your respective Human Resources Office.
- Employees must be paid at least minimum wage and be 16 years old.

## **PURCHASING**

- Do not permit purchases of personal items, even if employees will reimburse.
- Sales tax should not be incurred.
- When purchasing products or services from employees and/or relatives of employees, follow conflict of interest and disclosure policies.
- Competitive bids or sole source justifications must be obtained by the Purchasing Department in advance of any purchase of \$5,000 or more.
- Encourage the use of the University's preferred suppliers in order to receive special rates based on contracts the University's Purchasing Services Department has negotiated. (See [Preferred Vendor Contracts](#) for more information.)

Purchase Orders:

- Obtain purchase orders in advance of purchases.

Procurement cards:

- Procurement cards should be kept in a secure location.
- The only person authorized to use a procurement card is the cardholder whose name is on the front of the card.

- Because of the potential personal use of procurement cards, the approvals of such transactions should be serious and thorough. Any unusual items or use of unusual vendors should be questioned. Personal use of procurement cards is not permitted.
- Original receipts, not copies of receipts, should be on file in departments/schools for all procurement card transactions.

## **CONTACTS FOR ASSISTANCE**

For assistance with any questions about internal control, please contact these offices:

Cash, check, credit cards	Cashiers	Paul Toler	882-4959	<a href="mailto:TolerP@missouri.edu">TolerP@missouri.edu</a>
Payroll	Payroll	Paul Toler	882-4959	<a href="mailto:TolerP@missouri.edu">TolerP@missouri.edu</a>
Accounts payable disbursements	Accounting	Gary Burns	882-3455	<a href="mailto:burnsg@missouri.edu">burnsg@missouri.edu</a>
Human resources	HR	Jatha Sadowski	882-4859	<a href="mailto:sadowskij@missouri.edu">sadowskij@missouri.edu</a>

## **ROLE OF INTERNAL AUDIT**

The UM Internal Auditing Department is responsible for performing internal audits at the University. Internal audits assist management by providing independent and objective analyses of activities and controls. Audit scopes can range from a single process to all business activities in a division, department, or school. Internal Auditing makes recommendations as a result of those analyses. Internal Audit makes regular reports to the audit subcommittee of the Board of Curators and the President on the results of internal audits and the completion status of audit recommendations. See the [UM Internal Audit](#) website for more information about the internal audit function.

The Administrative Services office is responsible for coordinating the on-campus activities of all internal audits on the Columbia campus and serves as liaison between internal auditors and campus departments when appropriate. If your office is contacted by anyone who represents themselves as internal auditors, contact Administrative Services at 882-7348.

## **AREAS FREQUENTLY EVALUATED BY INTERNAL AUDIT**

Cash, checks, credit card receipt processing	Sponsored research processes/activities
Purchasing/accounts payable	Other regulatory requirements
Payroll	New system implementations
Procurement cards	Information technology controls
Monitoring controls, review of financial activity	