

# National Association of Corporate Directors

## Internal Control & Compliance Issues

Fort Lauderdale, FL

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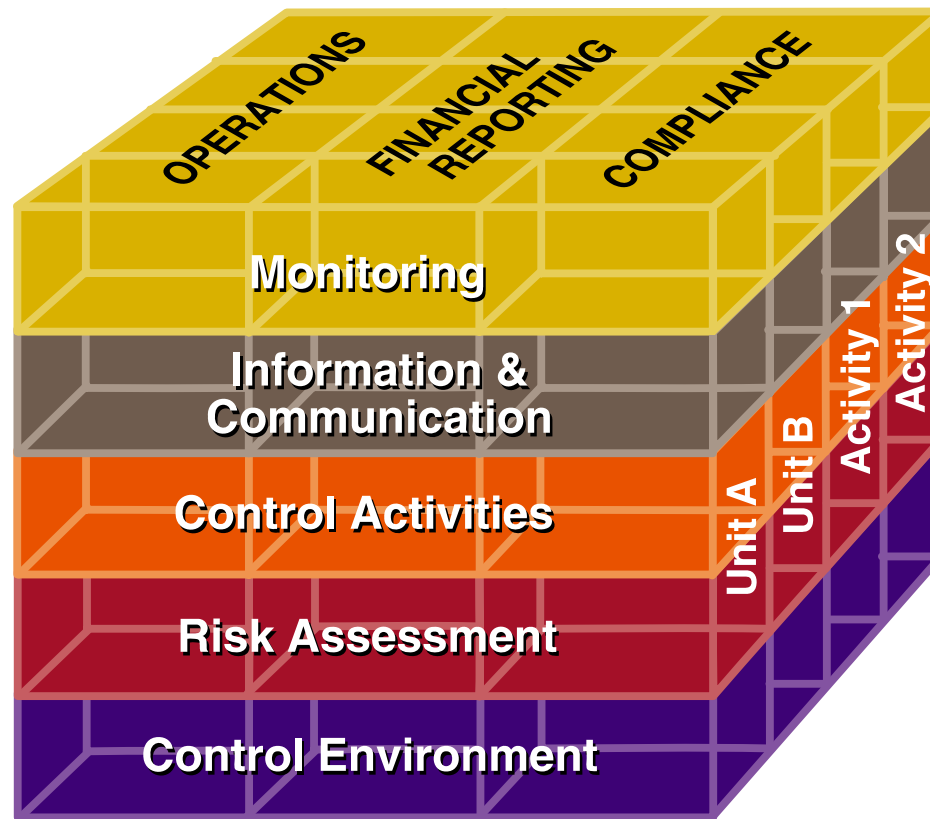
## What is Internal Control?

**Internal control** is a process, effected by an entity's board of directors, management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

- Effectiveness & efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws & regulations

(Source: COSO)

# COSO Internal Control Framework



## Control Environment

- Integrity, ethical values & competence of the organization's people
- Management's philosophy & operating style
- Assignment of authority & responsibility
- Attention & direction provided by the Board of Directors

## Risk Assessment

- Identification & analysis of relevant risks
- Determination of how risks should be managed
- Mechanisms to address change (i.e. economic, regulatory, operational)

## Control Activities

- Occur throughout the organization...at all levels within all functions
- Help to ensure that necessary actions are taken to address risks
- Include a wide range of activities: approvals, authorizations, reconciliations, segregation of duties, security of assets, etc.

## Information and Communication

- Capture & communication of relevant information required to complete daily responsibilities
- Top-down message that control responsibilities are to be taken seriously
- Individuals must understand their respective roles in the internal control system
- Effective communication must exist with external partners (e.g., customers, service providers, regulators, shareholders)

## Monitoring

- Accomplished through ongoing monitoring activities, and/or separate evaluations
- Ongoing monitoring occurs in the course of operations
- Includes regular management & supervisory activities
- Scope & frequency of separate evaluations depends upon the assessment of risks and the effectiveness of ongoing monitoring procedures

## Characteristics of Smaller Companies

- Fewer levels of management with wider spans of control
- Less complex transaction processing systems
- Leadership by management with significant ownership interest or rights
- Fewer personnel, many having a wider range of duties
- Limited ability to maintain deep resources in line and support staff (e.g., human resources, accounting, internal audit)

## Challenges in Attaining Cost-Effective Internal Controls

- Obtaining sufficient resources to achieve adequate segregation of duties
- Management's ability to dominate activities....  
opportunity for management to override a control
- Recruiting individuals with required financial reporting & other expertise to serve effectively on the Board of Directors and Audit Committee
- Maintaining appropriate control over computer information systems with limited technical resources

## Internal Control over Financial Reporting Guidance for Smaller Companies

This guidance provides a set of 20 basic principles representing fundamental concepts of internal control

Control Environment:

- Integrity & Ethical Values
- **Board of Directors**
- Management's Philosophy & Operating Style
- Organizational structure
- Financial Reporting Competencies
- Authority & Responsibility
- Human Resources

## Principle #2

### Board of Directors

#### Examples of Applying the Principle

- Reviewing & Documenting Key Activities of the Board
- Audit Committee Independence & Financial Reporting Expertise
- Reviewing Financial Statement Estimates
- Audit Committee Interacting w/External and Internal Auditors
- Audit Committee considering the potential for management override
- Audit Committee setting agendas

## Internal Audit

**Internal auditing** is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

## Regulatory 'Standards' for the Internal Audit Program

- Audit plan must be developed through a risk-based methodology (refreshed annually)
- Audit Committee approval of audit scope & timing
- Formalized tracking of audit issues
- Perform all reviews as scheduled and complete in a timely fashion
- Draw audit conclusions as they relate to risk management
- Assign risk ranking to audit issues

## Regulatory Compliance

### Examples of 2009 Hot Issues

- Troubled Assets Relief Program (TARP)
- Credit Quality – ALLL Modeling
- Identify Theft Red Flags
- Bank Secrecy Act/Anti-Money Laundering
- Gramm-Leach-Bliley Act (GLBA)
- Unfair & Deceptive Acts or Practices (UDAP)
- Risk Management Activities

## Contact Information

Bob Dynko, CIA, CISA, CBA  
Director, Financial Services  
Jefferson Wells

[robert.dynko@jeffersonwells.com](mailto:robert.dynko@jeffersonwells.com)

p. 704 972 6556