

A nighttime photograph of a park featuring a calm river in the foreground. The river reflects the lights from a bridge and surrounding trees. On the right bank, there are palm trees and other vegetation illuminated with warm and green lights. In the background, city buildings are visible under a twilight sky. The text 'COSO Internal Control Training Course' is overlaid in red.

# COSO Internal Control Training Course

# Herald of Free Enterprise Disaster

- 6 March 1987
- 188 people die when a ferry capsizes crossing the English Channel
- Worst UK maritime disaster since the Titanic
- Ultimate cause: poor internal controls

# WHAT IS INTERNAL CONTROL?

# What is Internal Control?

Processes to reasonably assure achievement of objectives related to:

- **Operations**
- **Reporting**
- **Compliance**

# What is Internal Control? (cont.)

The definition emphasizes:

- **A process consisting of ongoing tasks and activities that flows through the organization**
- **Geared to the achievement of objectives in one or more overlapping categories**
- **Affected by people at every level, not just policies and forms**
- **Able to provide reasonable assurance, not absolute assurance, to an entity's management**
- **Adaptable to the entity structure, not just the operational level of the organization**

**(COSO 2013)**

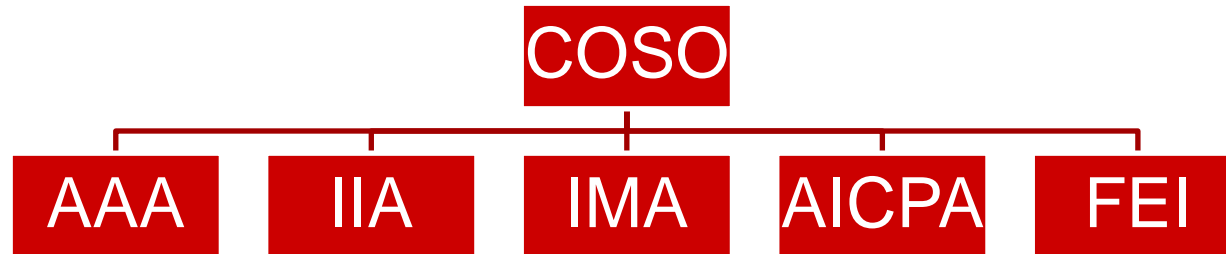
# What is Internal Control (cont.)

1. To identify the correct control, you must know what risks are present
2. To know what *risks* are present, you need to understand what *objectives* are being sought
3. Therefore:



# What is COSO?

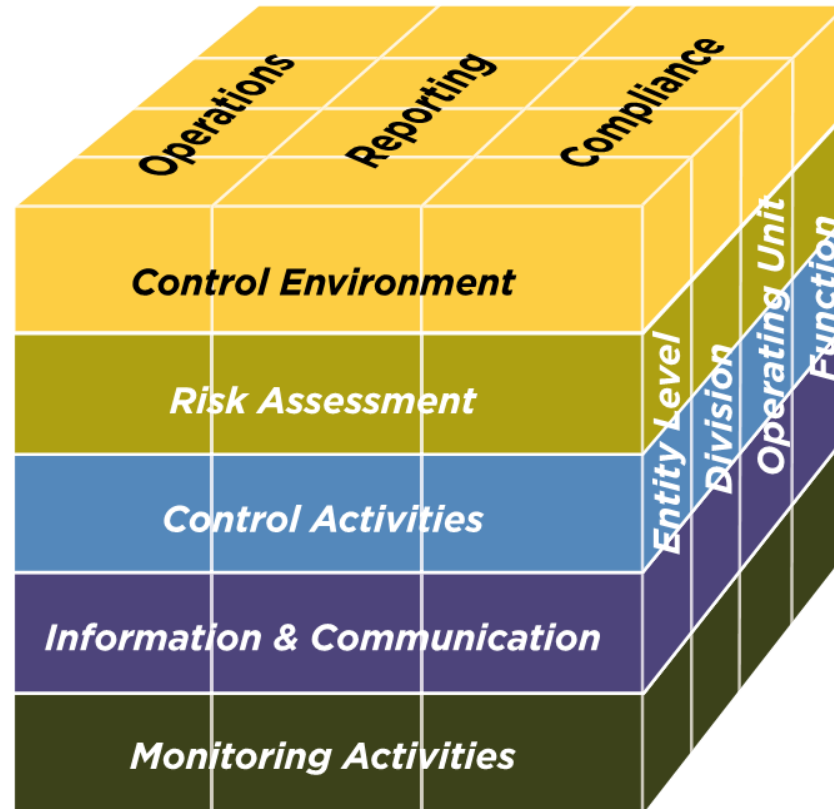
# COSO's Structure



- American Accounting Association
- Institute of Internal Auditors
- Institute of Management Accountants
- American Institute of Certified Public Accountants
- Financial Executives International



# COSO Integrated Framework



# 2013 Framework and Tools

2013 Framework	Illustrative Tools	ICEFR* Compendium
Components	Templates	Approaches
Principles	Scenarios	Examples
Points of Focus		

\* Internal Control over External Financial Reporting

# Update articulates principles of effective internal control

## Control Environment

1. Demonstrates commitment to integrity and ethical values
2. Exercises oversight responsibility
3. Establishes structure, authority and responsibility
4. Demonstrates commitment to competence
5. Enforces accountability

## Risk Assessment

6. Specifies suitable objectives
7. Identifies and analyzes risk
8. Assesses fraud risk
9. Identifies and analyzes significant change

## Control Activities

10. Selects and develops control activities
11. Selects and develops general controls over technology
12. Deploys through policies and procedures

## Information & Communication

13. Uses relevant information
14. Communicates internally
15. Communicates externally

## Monitoring Activities

16. Conducts ongoing and/or separate evaluations
17. Evaluates and communicates deficiencies

# Update articulates principles of effective internal control (cont.)

## Control Environment

1. The organization demonstrates a commitment to integrity and ethical values.
2. The board of directors demonstrates independence from management and exercises oversight of the development and performance of internal control.
3. Management establishes, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.
4. The organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with objectives.
5. The organization holds individuals accountable for their internal control responsibilities in the pursuit of objectives.

# Update articulates principles of effective internal control (cont.)

## Risk Assessment

6. The organization specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.
7. The organization identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.
8. The organization considers the potential for fraud in assessing risks to the achievement of objectives.
9. The organization identifies and assesses changes that could significantly impact the system of internal control.

# Update articulates principles of effective internal control (cont.)

## Control Activities

10. The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.
11. The organization selects and develops general control activities over technology to support the achievement of objectives.
12. The organization deploys control activities through policies that establish what is expected and procedures that put policies into place.

# Update articulates principles of effective internal control (cont.)

## Information & Communication

13. The organization obtains or generates and uses relevant, quality information to support the functioning of internal control.
14. The organization internally communicates information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.
15. The organization communicates with external parties regarding matters affecting the functioning of internal control.

# Update articulates principles of effective internal control (cont.)

## Monitoring Activities

16. The organization selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.
17. The organization evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the board of directors, as appropriate.



# Principle 1: The organization demonstrates a commitment to integrity and ethical values.

## Points of Focus

- Sets the tone at the top
- Establishes standards of conduct
- Evaluates adherence to standards of conduct
- Addresses deviations in a timely manner

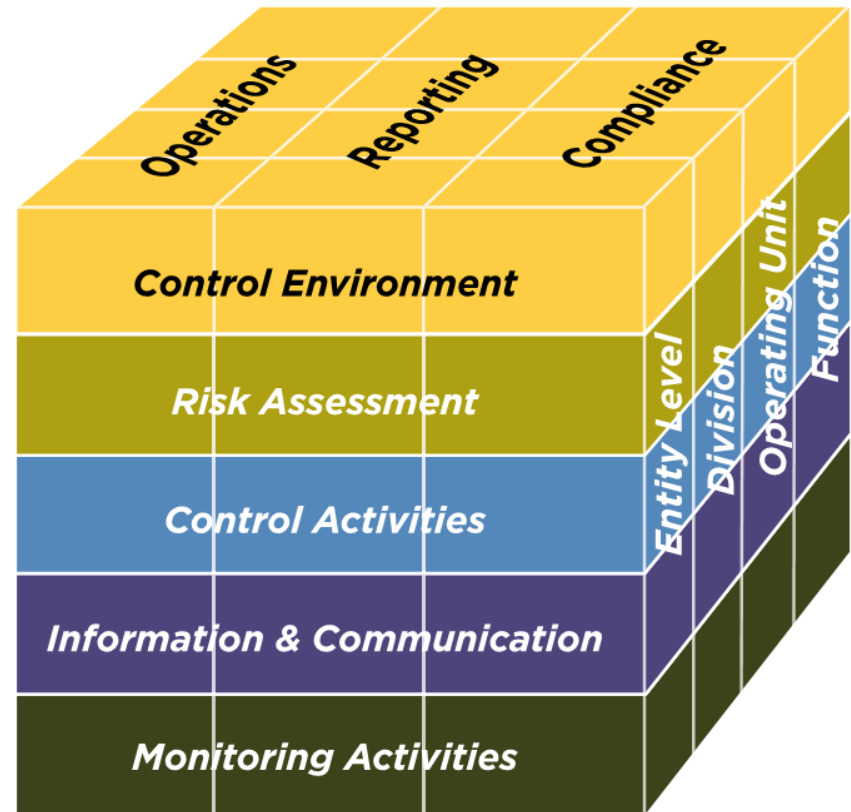
# Principle 8: The organization considers the potential for fraud in assessing risks to the achievement of objectives.

## Points of Focus

- Considers various types of fraud
- Assesses incentive and pressures
- Assesses opportunities
- Assesses attitudes and rationalizations

# Three Dimensions

- Objectives
- Entity Level
- Components of Internal Control



# Objectives

## Operations

- Achieving Mission and vision
- Improving financial performance
- Productivity
- Safeguarding of assets

## Reporting

- External Financial reporting
- External non-financial reporting
- Internal reporting

## Compliance

- Laws
- Rules
- Tax
- Environmental regulations
- Employment law

**Control Environment**

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graph TD; A[Control Environment] --> B[Risk Assessment]; B --> C[Control Activities]; C --> D[Information and Communication]; D --> E[Monitoring];
```

**Risk Assessment**

**Control Activities**

**Information and Communication**

**Monitoring**

# Control Environment

Management's attitude, actions, and awareness of the need for internal controls

- **Managements operating style**
- **Organizational structure**
- **How are authority and responsibility delegated**
- **Competence of people**

# Activity

- Identify elements of the Control Environment at ADB.

# Elements of the Control Environment

- The “tone at the top”
- Commitment to competence
- Participation by those charged with governance
- Management’s philosophy and operating style
- Organizational structure
- Assignment of authority and responsibility
- Human resource policies and practices



# Control Environment: Principles

1. The organization demonstrates a commitment to integrity and ethical values
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Control Environment

**Risk Assessment**

Control Activities

Information and Communication

Monitoring

# Risk Assessment Principles

6. The organization specifies objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.
7. The organization identifies risks to the achievement of its objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.
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Control Environment



Risk Assessment



**Control Activities**



Information and Communication



Monitoring

# Hard vs. Soft Controls

Hard controls	Soft controls
<ul style="list-style-type: none"><li>• Formal</li><li>• Objective</li><li>• Objective, measurable</li><li>• Formal rules and procedures</li></ul>	<ul style="list-style-type: none"><li>• Informal</li><li>• Subjective</li><li>• Intangible</li><li>• Values</li></ul>

# Hard vs. Soft Control Examples

Hard controls	Soft controls
<ul style="list-style-type: none"><li>• Reviews</li><li>• Reconciliations</li><li>• User IDs and Passwords</li><li>• Physical Counts</li></ul>	<ul style="list-style-type: none"><li>• People</li><li>• Honesty</li><li>• Shared values</li><li>• Communications</li></ul>

## Activity: Control Activities

A national fast food chain is experiencing a large increase in counterfeit \$20 and \$50 being received in the capital city. This problem is having an impact on the financial results of the business.

**What controls could be implemented to reduce this problem? Categorize the controls.**

# Detective Control Activity Examples

- Reconciliation
- Reviews
  - **Budget to Actual**
  - **Current to prior period comparisons**
  - **Performance measurements**



# Preventive Control Activity Examples

- Approval/Authorizations
  - **Policies and procedures**
  - **Limits to authority**
  - **Supporting documentation**
  - **Question unusual items**
- Assets Security (also Detective)
  - **Physical safeguards**
  - **Record retention / audit trail**
  - **Inventory counts**
- Segregation of Duties (also Detective)

# Control Activities: Principles

10. The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.

11. The organization selects and develops general control activities over technology to support the achievement of objectives.

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Control Environment



Risk Assessment



Control Activities



**Information and  
Communication**



Monitoring

Control Environment



Risk Assessment



Control Activities



Information and Communication



**Monitoring**

# Monitoring Activities

- Assess whether or not each of the five components is present and functioning as intended.
- Identify deficiencies in the internal control system.
- Ascertain whether each component continues to function, or if change is needed.

# Monitoring Activities (cont.)

- Ongoing evaluations are built into processes at all entity levels and provide timely information.
- Separate evaluations vary in scope and frequency depending on assessment of risks and effectiveness of ongoing evaluations.
- Findings are evaluated against criteria set by regulators, the board, or standard setting bodies.

# Putting it all together

Overall Assessment of Internal Control System



Component Evaluation



Principle Evaluation



Summary of  
Internal Control Deficiencies

# Case Study



# Any Questions

