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Heinfeld, Meech & Co. Newsletter for Grant Schools and Dormitories

Have You Assessed Your Risks?

by Michael A. Hoerig, CPA, Partner

Risk assessments are a common procedure performed by external auditors; however, every organization should consider performing an internal risk assessment as well. The goal of an internal risk assessment is to determine if the control structure is working as originally designed and if changes are necessary.

Small procedural changes occur every year at your organization; some are the result of staff turnover, others are due to budgetary pressures or regulatory changes. After several years of small changes with no corresponding review of the internal controls organizations can develop "gaps" in their internal control structure that leave them vulnerable to costly errors or fraud. Whether documented informally or formally through the use of memos and worksheets, a periodic review of the internal control structure can be a beneficial exercise to ensure the controls are still relevant and that fraud risks are minimized. In some instances obsolete procedures may also be identified and eliminated.

An internal risk assessment generally consists of the following steps:

1. Identify the risk areas to be assessed (e.g. cash collections, or customer billing). Keep in mind that decentralized processes (e.g. functions performed by a satellite location, or functions that each department performs) are generally considered higher risk and therefore should be considered higher priority when identifying risk areas.

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Internal Controls for Expenditure Processes

by Marvin M. Mendieta, CPA, CGFM, Audit Manager

Perhaps one of the most significant business functions at your organization is expenditure processing. It is important to have adequate controls in this area to ensure only valid payments are disbursed to the appropriate parties. Consider the following the next time you take a look at your organization's internal controls for expenditure processing.

Vendor Master File Access. Access to the vendor master file should be restricted. The employee who maintains the vendor master file should not be tasked with recording payment information in the accounting system or approving expenditures. The vendor master file should be independently reviewed for changes on a regular basis to ensure accuracy and propriety of those changes.

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2016 Grant School Conference

Heinfeld, Meech & Co. will be presenting our 10th annual conference specifically for grant schools and other BIA-funded entities in Laughlin, Nevada on Thursday and Friday, **April 14 and 15**.

Details and online registration will be sent out in Februrary. Visit www.heinfeldmeech.com/hmu for information on our other upcoming trainings.

Also in This Issue

Understanding the Types of Fraud

by Anthony St. George, CPA, Senior Associate

Fraud is a common term among any organization. However, it is sometimes used when it is too late. The key in preventing fraud is to understand the types of fraud and to implement controls within your organization to reduce the risk of fraud occurring.

Two types of fraud include fraudulent financial reporting and the misappropriation of assets. Misappropriation of assets is the intentional theft or misuse of entity owned assets for personal benefits. Misappropriation of assets is usually the more common type of fraud that occurs. Fraudulent financial reporting occurs when there is an intentional misstatement to the financial statements. This could be an overstatement of revenues or an understatement of expenses to remain within budget constraints. While it is not as common, fraudulent financial reporting can be just as, if not more devastating than the misappropriation of assets.

The most notorious cases of fraudulent financial reporting include the cases of Enron and WorldCom. However, any misstatement of financial statements can have an impact on the stakeholders in the organization whether they are monetary stakeholders or simply losing the trust of the public. The misappropriation of assets is usually theft of cash collected. The likelihood of this occurring increases with decentralized operations and less oversight.

The best way to prevent fraud is to understand that it can occur to any entity at any level and also to be vigilant in implementing internal controls. The most common control is segregation of duties which ensures that one employee does not have the ability to execute an entire transaction whether it is a cash disbursement, cash collection, or adjustments made directly to the system. While there is not a way to completely eliminate the risk of fraud occurring, understanding how and when fraud occurs can be beneficial in deterring such activity. ■

Risk Assessments

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2. Document the current process in place through interviews and observation of employees involved. Flowcharts can also help visually demonstrate how information flows from one employee or department to another.
3. Develop hypothetical errors or fraud scenarios and identify if internal controls are in place to prevent or detect the issue. If a significant weakness is detected it should be analyzed to determine the necessary changes to the internal controls.
4. Consider performing tests of the internal controls. Selecting a sample of actual, historical transactions and tracing their path through the process can help complete steps 2 and 3 above by demonstrating the controls in place and where they are lacking.
5. Summarize the results of the risk assessment and communicate the results to employees, management and the governing body.

While the risk assessment process can be time-consuming, it can help strengthen your organization's internal controls, identify outdated and inefficient processes and, most importantly, limit the susceptibility to fraudulent acts. The consequences of fraud can be costly, not only because of the dollars lost, but also due to the negative perception formed by employees, customers, citizens and benefactors. Consider taking the time now to ensure your organization's controls are up-to-date. For further information on the risk assessment process, contact CW Payne, CPA, CFE, at (928) 774-4201, ext 204. ■

Expenditure Internal Controls

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Separation of Duties. Authorization and approval of expenditures should be separate from recording of disbursements in the accounting system. The employee responsible for approving invoices and payment documents should not be the same employee who is tasked with recording those invoices in the system. Also, recording of disbursements should be separate from signing of the checks. The employee responsible for recording invoices in the system should not have the ability to sign the disbursement checks or have access to the blank check stock.

In addition, if employees are tasked with printing checks, they should not be recording disbursement transactions or preparing and reviewing the bank reconciliation.

Signature Stamp Security. If a signature stamp or facsimile plate is maintained, the authorized check signer should have custody of the signature stamp and ensure that the stamp is kept in a secure location. Disbursement checks should be compared to the check listing by an independent employee to ensure the payees and amounts agree and that the distribution of the checks is performed by someone independent of the expenditure process.

Wire Transfers. For wire transfers, it is recommended to have one authorized employee to initiate the transaction and another authorized employee to approve and release the wire transfer. These individuals should not be responsible for making changes to the vendor master file or performing bank reconciliations.

Reconciliations. Finally, accounts payable and bank reconciliations should be performed regularly and timely. They should be prepared by an employee independent of the disbursement process. In addition, the reconciliations should be reviewed and approved by someone other than the preparer of the reconciliation. Budget to actual expenditure reports should be reviewed on a regular basis to monitor the expenditures that are being charged and perform analysis on variances and other anomalies.

By implementing the appropriate controls and ensuring certain tasks are separated among employees, the risk of errors and fraud can be mitigated in the expenditure process. If you would like assistance reviewing your district's procedures or providing training to your district's staff, our team can help. Contact Karin Smith, CFE, MBA, SFO, at (602) 277-9449, ext 327.

About Our Firm

Heinfeld, Meech & Co. serves governmental and non-profit organizations throughout Arizona and New Mexico, with offices in Flagstaff, Tucson, and Phoenix. We are focused exclusively on providing accounting and auditing services to governmental and not-for-profit entities. We offer this free newsletter to Community Schools and Dormitories as part of our commitment to providing resources and training to your business personnel.

For more, visit www.heinfeldmeech.com.

HM News

Michael L. Lauzon, CPA, was promoted to Partner of our firm this summer. Michael has been a member of the firm's audit division since 2003 and has been based in our Flagstaff office since it opened in 2007. For more information on Michael, visit his page on our website.

CW Payne, CPA, Consulting Partner, recently received the Certified Fraud Examiner designation. For more about this program, visit www.acfe.com