**Internal Control Script**

Slide 1: In this presentation, we will discuss Internal Control and what that means for businesses. In a separate presentation, we’ll discuss ways to control that all-important asset Cash.

Slide 2: This is what is known as the Fraud Triangle, and this is a good place to begin our discussion. The three sides of the triangle are Financial Pressure, Rationalization, and Opportunity.

Slide 3: *Financial Pressure* is fairly self-explanatory – not being able to pay the bills or gambling; other pressures may come from family, society or other sources.

*Rationalization* happens when employees are able to justify the fraud. “The company’s never going to miss it” or “They don’t pay me enough” are some common examples.

*Opportunity* arises when there are weaknesses in the System of Internal Control.

Slide 4: There are three main types of fraud, as well.

*Asset misappropriation* can be forged checks, billings to companies that don’t exist, stealing, and phony expense reimbursement

*Corruption* includes bribery, embezzlement, blackmail and bribes

*Fraudulent Financials* is pretty self-explanatory and happens when revenue is overstated and/or expenses are understated or assets and overstated and/or liabilities are understated

Slide 5: The Association of Certified Fraud Examiners puts of their Report to Nations every year. For the most recent year (2016), they survey over 2,400 organizations across the globe. The total fraud involved was around $6.3 billion and it is estimated the typical company loses about 5% of their total revenues – not net income – to fraud each year.

23% of cases involved fraud over $1 million; Fraudulent Financials was the most costly at around $975,000 per occurrence.

Slide 6: This slide shows the three major fraud types we discussed in Slide 4and their median costs (median means half of the cases were less than the median and half were above the median).

Asset Misappropriation showed in 83.5% of cases with a median amount of $125,000

Corruption showed on 35.4% of cases with a $200,000 median amount

Fraudulent Financials showed in 9.6% of cases, but had the greatest median at $975,000

You might have noticed that these percentages add up to 128.5%; that is because 31.8% of cases involve more than one type of fraud.

Slide 7: These are the elements of a System of Internal Control as I have learned them over the years:

Assignment of Authority & Responsibility = somebody has to be in charge and nobody can be in control of everything – even in small operations. Who’s in charge of Accounting? Where do customers go when there are quality problems? Who deals with HR issues?

Measures of Business Performance = Are we making money? Did we do better than last year? A lot of this belongs to the Accounting/Finance Function, however, there are non-financial measures as well such defect rates, customer satisfaction surveys and community involvement.

Prevention of Errors & Fraud = This is what most people think Internal Control is all about, however it is just one part. Anything we can do to prevent errors and fraud before they happen is excellent – think of security cameras or requiring two signatures on a check. When I was president of my Homeowners Association, two officers had to sign checks – that way, I couldn’t cut a check to Eric Carstensen and have only myself authorize it.

Compliance with Laws & Regulations = being out of compliance can be costly and damaging to a business, yes, but being in compliance is the right thing to do. We need to make sure people get paid overtime, that we don’t pollute and don’t employee children, even though they work for a lot less per hour…

Regular Monitoring and Evaluation = Just because we have the first four parts of the system in place doesn’t mean we are done. We need to constantly check to ensure those things are happening and adjust for new threats and issues.

Slide 8: Other elements of a system include Protection of Assets. Companies invest in assets in order to generate revenue – loss of assets hampers that goal.

Risk assessment in part of the Regular Monitoring we just discussed.

Separation of duties means we don’t want people in charge of an asset to be in charge of recordkeeping. For instance, many retailers will bring in an outside firm to conduct inventory counts so that employees can’t “misappropriate” that costly asset.

Bonding key employees refers to having an insurance policy guarding against theft from that employee. If an employee steals, they will never be bonded again.

Technology is becoming less and less expensive and can do more things. Computerized systems help minimize errors and security cameras let employees know they are being watched.

Every employee at every level in every department is part of the system, and it starts at the top.

Slide 9: There is a Cash Control presentation that goes along with this one that covers bank reconciliations and petty cash systems.