

the Quaestor Quarterly

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quaes · tor [kwes'tôr] 'one who asks questions'

"Trust" - is it an Internal Control?

Certainly, in any employee/employer relationship, the ability to trust each other is crucial. We all understand that it doesn't happen immediately upon hire...trust develops over the course of time. It takes much effort to earn trust, but trust is extraordinarily easy to lose. Because trust deals with a person's character, it is very specific to that particular person and the relationship between the two "trusting" parties. Further, trust relies on the ability of each person to be a good judge of character.

Very often during the course of our audit work when inquiring about the system of internal controls in place in the area we are auditing, the response that is received from the client goes something like this, "I have known our staff for a very long time and I completely trust them." Our response goes something like this, "That's great! Trust is a great thing! But, what is your system of **internal controls**?" And, interestingly, in the event of a fraud investigation, the phrase almost invariably uttered by a supervisor when confronted with the very real possibility that a fraud is occurring in their department is "I can't believe this...I have known this person for a very long time...I *completely* trusted them."

You see, despite what many people would like to believe, "trust" is **NOT** an internal control. Although it is extremely important to trust each other, trust - in and of itself - is not a substitute for internal controls. Trust relies purely on the character and integrity of the individual performing the function to ensure that business objectives are met; whereas, a strong system of internal controls - operating effectively - relies on a **process**, which will hold strong regardless of who is in the role by deterring or detecting errors or misuse of University assets. When we perform an audit, we are not auditing a person's integrity or character, we are auditing a process.

Implementing internal controls can be tricky in functions where "trust" was the factor previously relied upon to ensure that what was supposed to get done, did get done and in an appropriate way. Many times people think that their integrity or character is being questioned when internal controls (i.e. segregation of duties, supervisory review/approval, documented reconciliations) are implemented.

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Occupational fraud can be found in any workplace. Whether an organization is a non-profit entity such as a university or a large for-profit corporation, fraud has occurred and continues to occur.

To learn more about occupational fraud, sign up for Fraud in the Workplace Training.

Upcoming Sessions:

May 29, 2008
9:00 AM - 11:00 AM
Location: CIMS 2140

August 21, 2008
9:00 AM - 11:00 AM
Location: CIMS 2140

November 11, 2008
9:00 am - 11:00 a.m.
Location: CIMS 2140

Sign up at the CPD website
<https://finweb.rit.edu/cpd/leadership/fraud.html>

"Trust" - is it an Internal Control?

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However, what fails to be recognized is that without internal controls, the individual's integrity and character - qualities so important to the trust equation - can be irreparably damaged in a matter of a few moments with just the slightest perception of wrong-doing.

Internal controls actually serve to protect the individuals charged with responsibility for each of the aspects of a function. If strong internal controls are in place, your integrity will be able to be held above scrutiny - it will be protected. Knowing this, we should all be eager to embrace implementation of internal controls that will protect us as well as the University. Trust and internal controls must co-exist. It is imperative that "trust" exists in our relationships with each other; however, for everyone's protection, that trust should be supported by a strong process of internal controls.

If after reading this article, you are moved to improve the level of controls in your department/function (yes, the key process owner - those individuals who are actually doing the work - can and should encourage improved internal controls wherever a gap is perceived) and aren't quite sure how best to do that, please know that we are always available to provide advisory services to the University to ensure that internal controls are strong and reliable.

~ Wendy J. Roy, Senior Internal Auditor

Control of the Quarter

In the last several newsletters, we've been talking about the internal control process which is designed to provide reasonable assurance regarding the achievement of the following objectives:

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

Internal control consists of five interrelated components including:

1. Control Environment
2. Risk Assessment
3. Control Activities
4. Information and Communication
5. Monitoring

In the last issue, we reviewed "information and communication", internal control component #4. The essence of this control is that organizations must capture pertinent information relevant to managing their business and it must be delivered to those who need it in a format and timeline that allows them to carry out their control (and other) responsibilities.

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Control of the Quarter

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Furthermore, in order for employees to understand their role in the control system, as well as how their work activities relate to the work of others, effective communication must occur throughout the organization (e.g., down, across and up).

In this issue we'll discuss "monitoring," the final control component. Monitoring, which involves assessing the design and operation of controls and taking the appropriate action when required, ensures that internal controls continue to operate effectively.

To make certain that the internal control system maintains its effectiveness over time, monitoring is accomplished both through ongoing activities and separate evaluations.

Ongoing monitoring activities include:

- Monthly reconciliation of payroll distribution reports to internal department human resource and timekeeping records.
- Division of employee duties (e.g., segregation of duties) so that different individuals serve as a check on each other. For example, one employee prepares a request for reimbursement (on an Invoice Payment Form) and another individual with budget authority approves the payment prior to it being processed by accounts payable.
- Performing an annual physical inventory for all departmental fixed assets and reporting changes to the Property Control Office.

Separate evaluations of the internal control system may be conducted periodically by the people responsible for the operation of a particular business unit or function (i.e., a "self-assessment") or by internal auditors. Regardless of who performs the evaluation, the individual must understand the activities and each of the components of the internal control system being addressed. S/he determines how the system actually works by talking with employees who perform or are affected by the controls and/or by reviewing records on performance of the controls. It is not uncommon to find that procedures may have been modified to operate differently or they may no longer be performed. For example, an employee who was responsible for printing and reconciling monthly reports for several balance sheet accounts left her position. During an evaluation of monitoring activities, it was determined that the new staff person no longer performed that control function. This deficiency was reported to management, a common outcome of an evaluation, and the department manager trained the new employee to perform the control function.

Regardless of the size of an organization, it is important to determine the effectiveness of internal control by performing both monitoring activities and separate evaluations.

~ Controller's Office



Ensure that your department has established and is maintaining good internal controls.

To learn more about internal controls, sign up for Internal Controls Training.

Upcoming sessions:

April 29, 2008
9:00 AM - 11:00 AM
Location: CIMS 2140

June 24, 2008
9:00 AM - 11:00 AM
Location: CIMS 2140

August 19, 2008
9:00 AM - 11:00 AM
Location: CIMS 2140

October 14, 2008
9:00 AM - 11:00 AM
Location: CIMS 2140

December 9, 2008
9:00 am - 11:00 am
Location: CIMS 2140

Sign up at the CPD website
<https://finweb.rit.edu/cpd/leadership/cares.html>



Ask the Auditor ~

Submit a question to the IACA webpage <http://finweb.rit.edu/iaca/forms/ask/> by May 30, 2008. If your question is chosen for publication in our newsletter, you will receive a prize valued at \$15.

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R·I·T

Word on the Street

When I was informed in October 2007 that the Center for Residence Life was going to have the "opportunity" to be audited by IACA, my initial sentiments were less than positive. "Why are they targeting our organization?" "We haven't done anything improper!" "Positive fiscal management policies are in place!" "No one has complained before; why now?" Needless to say I was somewhat anxious as the process began.

Fast forward 4 months: Would I be writing and submitting this statement if my experience was less than positive? The comprehensive audit process was enlightening, professional and very reinforcing. I value the thoroughness with which IACA managed the process, whose only goal is to improve the administration of fiscal resources and the proper delivery of services to students. I would recommend any RIT department/organization or individual to collaboratively work with IACA to evaluate their processes and procedures. The IACA staff became partners and consultants to assist our organization in reviewing the proper use of our resources. The audit process has assisted Residence Life in becoming a more effective program and I would recommend this process and the IACA staff to anyone.

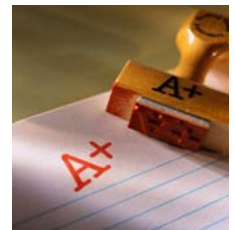
~ Charles Lamb, Director-Center for Residence Life

Pop Quiz

The first reader to correctly answer the question below will win a prize worth \$10.

Question: Which of the following is not a legal element of fraud?

- A. A material false statement.
- B. Intent.
- C. Reliance by the victim.
- D. All of the above are legal elements of fraud.



See our Quiz webpage to post your answer:

<https://finweb.rit.edu/iaca/forms/quiz/>

The winner's name and answer will be included in the next newsletter.

Congratulations to Joe Johnston, Student Affairs, for being the first reader to correctly answer the January issue Pop Quiz question.

The question and the correct answer for January:

"Executives in organizations are more honest than rank-and-file employees and are therefore less likely to commit fraud."

- B. False