

Silver Advantage Consulting Alert

Internal Control – The Big Picture

By Janell Wilson, CPA-Partner

October 2016

To be successful, a business must have an effective internal control system in place. An internal control system is a process designed to conduct business efficiently and effectively, safeguard assets, prevent and detect errors and fraud, ensure accuracy and completeness of accounting information, produce reliable and timely financial information, and ensure adherence to company policies and compliance with laws and regulations.

The Committee of Sponsoring Organizations of the Treadway Commission (COSO) is a joint initiative that provides a framework for internal control, which includes five interrelated components that work together to create an integrated process of internal control. Below is a “big picture” summary of the components and principles that must be working together to create an effective system of internal control.

1. **Control Environment** – The control environment sets the tone of the organization. The organization must:
 - Demonstrate a commitment to integrity and ethical values.
 - Have a board of directors that demonstrates independence from management and exercises oversight of the development and performance of internal control.
 - Have management establish, with board oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of objectives.
 - Demonstrate a commitment to attract, develop, and retain competent individuals in alignment with objectives.
 - Hold individuals accountable for their internal control responsibilities in the pursuit of objectives.

2. **Risk Assessment** – Risk assessment is the organization’s process of identifying and analyzing the risks relevant to financial reporting. The organization must:
 - Specify objectives with sufficient clarity to enable the identification and assessment of risks relating to objectives.
 - Identify risks to the achievement of its objectives across the entity and analyze risks as a basis for determining how the risks should be managed.
 - Consider the potential for fraud in assessing risks to the achievement of objectives.
 - Identify and assess changes that could significantly impact the system of internal control.

3. **Control Activities** – Control activities are the steps taken to reduce risks identified during the risk assessment process. The organization must:
 - Select and develop control activities that contribute to the mitigation of risks to the achievement of objectives to acceptable levels.
 - Select and develop general control activities over technology to support the achievement of objectives.
 - Deploy control activities through policies that establish what is expected and procedures that put policies into action.

4. **Information and Communication** – Systems should be in place to identify, capture, process, and distribute information about the other components of internal control. The organization must:
 - Obtain or generate and use relevant, quality information to support the functioning of internal control.
 - Internally communicate information, including objectives and responsibilities for internal control, necessary to support the functioning of internal control.
 - Communicate with external parties regarding matters affecting the functioning of internal control.

5. **Monitoring** – The Internal control system must be monitored on an ongoing basis to ensure the system is operating as intended and is modified when appropriate. The organization must:
 - Select, develop, and perform ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.
 - Evaluate and communicate 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.

This article gives a “big picture” view of the components and principles of COSO’s Internal Control Integrated Framework. Stay tuned for future articles that delve into the specifics of each section with examples and approaches for designing, implementing, and maintaining an effective system of internal control. If your organization is ready to take a closer look at your internal control system, Michael Silver & Company CPAs is here to help. We can evaluate your existing system, make recommendations for strengthening internal controls, and assist with implementation. Contact Janell Wilson at 847-982-0333 for more information.

Janell Wilson, CPA has over 20 years of experience in public accounting with expertise in audits, reviews, and compilations of companies within the private middle market sector. She enjoys working closely with entrepreneurs and business owners to improve accounting systems and procedures and strengthen internal controls. Her industry specializations include manufacturers, automobile dealerships, professional service providers, retailers, and leasing companies. Janell works with nonprofit organizations, including religious organizations, arts and cultural organizations, trade associations, and other public charities and private foundations. Janell also has extensive experience with employee benefit plans.