COMPLIANCE TOPICS: THE BASICS OF INTERNAL CONTROLS

For many people working on Federal awards, this emphasis on internal controls is a new and confusing topic.

What are internal controls, and more importantly, what are they for?

It seems simple enough.

As a general rule, the *goal* of internal controls is to provide reasonable assurance that grant requirements are complied with in a timely and cost effective manner.

But meeting this goal involves many people from across the organization and includes both everyone working directly and those working indirectly on the federal grant.

In this Special Report, I'll walk you through the basics of well-developed control systems, and give you tips for making your existing controls more effective.

To your success!

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The 7 Basics of Internal Control for Grant Management

There are seven basic controls that every grant manager should look for to reduce the risk of both grant mismanagement and fraud.

Identifying *all* the necessary internal controls can be difficult as each grant may have varied specifications and requirements.

However understanding the basics will set you on the right track.

Take a minute to review the list and ask the related questions of your organization:

Control #1: Formal Written Policies and Procedures

- Has your organization formalized written policies and procedures such as who can approve grant spending, how labor is recorded and charged, and the procedures for procuring goods and services?

- Have you reviewed your grant terms and conditions for a list of policies that must be in writing, for example drug free workplace requirements, and a process to minimize the time between requesting grant funds and paying suppliers?

Control #2: Adequate Monitoring

- Does your organization check to make sure the existing policies and procedures are actually followed?

- How are you ensuring that charges to the grant are reasonable, allocable, not be limited or excluded by Federal Cost Principles regulations?

- How do you make sure that organizational policies are applied to your grants uniformly and that spending is adequately documented?

Control #3: Reconciliations

- Are your account reconciliations current and updated in a timely manner?

- Do your property records for equipment purchased with grant funds match the accounting records?

- Have you taken a physical inventory of property purchased with federal funds recently?

Control #4: Secured, Safeguarded Assets

- How is property safeguarded from loss, damage or theft?

- What is done to prevent misuse of credit cards and other assets?

- Is periodic training held for employees on grant requirements?

Control #5: Separation of Duties

- How good is your separation of duties?

- Do you have different people recording transactions, authorizing transactions, and having custody of the assets?

- Or is this handled by one or two people?

Control #6: Supervisory Review and Approval

- What is the process to have supervisors approve spending on the grant?

- What reviews are done by supervisory personnel?

- How do you demonstrate the approval and reviews were done? (Are the documents signed and dated?)

Control #7: Adequate Documentation

- Are receipts required for reimbursement of spending?

- Do the receipts have enough detail to determine if the costs are allowable to charge the grant? (i.e. itemized receipts)

- Do time cards show what grants and other activities the employee spent their time on?

The Minimalist Guide to Internal Controls

Understanding and applying internal control principles is important to both continued and new grant funding.

A lack of well-developed internal controls can lead to costs being disallowed and even suspension and debarment from future grants.

Does it seem overwhelming?

Here is the minimalist guide to internal controls: Just remember *3-5-7...*

The Simplified 3-5-7 Approach to Internal Controls:

There are *3 main objectives* for well-developed internal controls.

Each objective contains *5 key components.*

There are *7 primary benefits* of effective internal controls.

Let's break that down step-by-step:

3 Main Objectives for Internal Controls

Well-developed internal controls are a critical defense for reducing risk of fraud, waste, or abuse of grant funding.

According to the Standards for Internal Control within the Federal Government, internal controls should be designed with the goal of achieving three main objectives:

- **Objective #1:** *Effectiveness* and *efficiency* of operations

- **Objective #2:** *Reliability* of financial reporting

- **Objective #3:** *Compliance* with applicable laws and regulations

Well-developed internal controls meeting these *3 main objectives* contain *five key components:*

1. Control environment
2. Risk assessment
3. Control activities
4. Communication
5. Monitoring

5 Key Components for Internal Control Objectives:

Component #1: Control Environment

An organization's environment is established by its leadership from the top down.

Leaders of each area, activity, and department are responsible to establish and monitor their specific control environment.

Component #2: Risk Assessment

Organizations must assess both external and internal risk.

Risk assessment requires identifying and analyzing risks to achieving the goals and objectives of the funded program or project, as well as to maintaining compliance.

As conditions constantly change, periodic and systematic risk assessment and analysis is required.

Component #3: Control Activities

Control activities are the actual policies and procedures within internal control.

Examples include reviews, supervisory authorizations, separation of duties, as well as written documentation and record keeping.

Control activities are designed to reasonably ensure that actions are taken to address risk and ensure compliance throughout the organization.

These activities are implemented at all levels and within all functions of the organization.

Component #4: Effective Communication

Every employee (and even volunteers) must clearly understand their individual role and its place in the control functions.

Therefore, effective communication mechanisms must be present to collect and distribute information in all directions within the organization.

This means people not only understand their role within internal control, but how it relates to what others are doing and the organization as a whole.

Effective communication not only includes mechanisms for management to communicate with employees, but a clear channel for employees to communicate back to management as well.

Component #5: Monitoring

In order to be effective, internal controls must be consistently and regularly monitored.

Monitoring should be built into daily operations in addition to regular and periodic supervisory monitoring.

The degree, scope, and regularity of monitoring internal controls is dictated by grant specifications and requirements.

This review should include identifying relevant risks to meeting the goals and objectives of the grant.

Well-developed internal controls are consistently assessed and evaluated in order to make continuous improvements.

7 Primary Benefits of Well-developed Internal Controls

The primary benefits of well-developed internal controls include:

- **Benefit #1:** Help to ensure grant funding is properly used

- **Benefit #2:** Detect and help prevent errors

- **Benefit #3:** Reduce the risk of direct and indirect fraud

- **Benefit #4:** Contribute to accounting accuracy

- **Benefit #5:** Assist grantee in providing timely financial and management reports to grantor

- **Benefit #6:** Help ensure policies, specifications, and requirements of the grant are met

- **Benefit #7:** Foster taxpayer confidence that public funds are safeguarded and spent as intended

The **3-5-7 approach** can help you understand what a well-developed internal control system looks like and avoid the *unpleasant reality* of poor grant management.

Compare these *3 main objectives*, *5 key components* and *7 primary benefits* to grant management at your organization.

How do you stack up?

4 Elements for Operating an Effective Compliance Program

How To Keep Your Compliance Program "*Fresh?*"

Grant Management compliance programs too often are put together and then relegated to take their place *next to the potted plant* on top of the four drawer file.

However for compliance programs to be effective, they must remain "*fresh*" by being "*living documents.*"

In other words, the documents serve no purpose *unless* they are put into service.

Design vs. Operation

The best design in the world does *not* ensure an effective compliance program *unless and until* that plan is put into continuous operation.

Think of it this way:

The word compliance means to agree to *do something*.

When an organization is awarded a grant they receive funds for a *specific* purpose. By accepting the money the organization is *obligated* to maintain compliance with the grantor's expectations.

The grant funds also come with "*strings attached*" in the form of regulatory and legal requirements.

When it comes to grant management, compliance programs become the "*ways and means*" for organizations meet the expectations and requirements of the grantee.

Elements of an Effective Grant Management Compliance Program

In this section, let's expand our understanding by looking at some examples of what an effective compliance program looks like.

Effective grant management compliance programs include these *four core elements*:

1. Create
2. Train
3. Measure
4. Review

Operating effective compliance programs often require integrating complex provisions, obligations, and regulations.

Sounds overwhelming?

Let's break each of these components into some examples.

Core Element #1: Create

Creating policies and procedures serve the need for adherence to provisions and regulations dictated by the grantor and other associated agencies and legal bodies.

However, the purpose of an organization's compliance program goes beyond this limited scope.

Creating effective policies and procedures can serve as a *framework for decision-making* on issues the organization may encounter during the life of their grant.

Here are some examples of how creating strong policies and procedures can serve the organization:

- Assisting in making ethical organizational and business decisions

- Helping maintain the organization's core vision, mission, and values

- Detecting activities and practices that conflict with organizational standards and/or have a negative impact on the organization

- Providing a system to meet regulatory requirements

- Acting as a supportive resource for employees

- Supporting a culture of integrity within the organization and protecting the public reputation of an organization

How to Write the Best Policies and Procedures?

The best and most effective policies and procedures are:

- Clearly written

- Include *"real life"* examples.

- Address *both* who will be reading and following them *as well as* the job functions they are designed to address.

- Are regularly and consistently reviewed and updated.

Don't Forget: Communication is Critical

Operating effective grant management compliance programs also means creating open lines of communication.

Here are some examples:

- Surveys and other tools for obtaining feedback should be put into place in ways that can be easily accessed.

- Installing an anonymous *"Hotline"* is a pro-active way for issues and challenges will be reported. (It is equally important to enforce a non-retaliation policy for employees who report problems–*in some cases having this type of process may even be a requirement for your grant.)*

- Newsletters and internal websites can be good resources to keep employees and other constituents and stakeholders informed.

- The Board of Directors and other oversight groups should also be regularly briefed on the compliance program.

Core Element #2: Train

Training is a key element for staff to understand the expectations related to both the grant and other organizational policies and processes.

Compliance training is *most* effective when it is a job requirement and employee's understanding of training topics is tested and documented.

The first to be trained must be the trainers. This means *all* compliance staff.

Training should be carefully crafted and regularly reviewed.

Just as when writing policies and procedures, effective compliance training utilizes *"real life"* examples.

Training also needs to be geared towards continuous improvement and education.

Here are some examples of ways staff can be trained:

- Encourage staff to attend appropriate conferences and webinars
- Subscribe to related publications and email lists
- Actively network with peers.
- Enroll in classroom and online learning

Next, compliance training should be mandated for board members and other stakeholders.

Some types of training that would be relevant to them include:

- Corporate governance
- Grant compliance and oversight
- Organizational leadership

Core Element #3: Measure

Measurement is a key component of operating an effective compliance program. One of the first things to track is whether sufficient funding remains to support the program.

"**SMART**" goals should be established and measured. Goals should be **s**pecific, **m**easurable, **a**ttainable, **r**ealistic and **t**ime-sensitive.

Here are some examples of effective measurement tools for compliance programs:

- Benchmarking

- Measurable *(quantifiable)* goal-setting

- Measurement systems and reporting methods

When goals or benchmarks are *not* met, it is important to investigate the reasons why, identify problems, and implement solutions.

(This is where corrective action plans come into play.)

Core Element #4: Review

In order to be *effective* compliance programs must include appropriate **review** and monitoring to ensure enforcement of policies and procedures.

Next, goals for the grant should be evaluated to make sure the program is staying *on-track* and achieving the desired results.

Examples of review and monitoring activities include some of the following methods:

- Review compliance to purchasing policies

- Test employee understanding of grant management requirements

- Examine grant spending for proper signatory authorization

- Evaluate conflict of interest policies and compliance

Finally, review includes a *prompt response* to any and all compliance issues.

Who Should Review Grant Management Compliance?

An effective way to review and monitor activities is to delegate and empower the monitoring process to teams and employees closest to the issues, regulations, obligations, and activities that must be in compliance.

However, careful attention needs to be paid to delegating monitoring and reviews to parties who do *not* represent any conflict of interest or inadequate segregation of duties in order to receive objective reviews.

Don't Forget Consequences…

Reviews and monitoring processes and practices are ineffective *unless* policies are consistently enforced and disciplinary action is taken when required.

The best policies and procedures, the best training, the best measurement and review mean little if the organization promotes a culture of indifference, or worse acceptance of wrong-doing as *"just the way it is."*

With the increased focus on internal controls, risk assessments and performance measurements contained in the new grant regulations 2 CFR Part 200, having an accountable organizational culture takes on new and heightened importance.

Would you describe the culture at your organization as *accountable*?

"Re-fresh" to stay fresh

The secret to keeping your grant management compliance program "*fresh*" is to "*re-fresh*" these 4 key elements periodically over the life of the grant.

Are You Ready To Take Your Grant Management Even Further?

We've put together the most up-to-date and comprehensive online training on the new grant management regulations we've ever produced, we call it the **NEW Grant Management Boot Camp Bundle**.

Ready for the new regulations?

This special report you've just read has covered the very basics of building your own grant management expertise …but that's just the beginning.

We've been expanding training and resources for grant management for nearly a decade. We've been fortunate enough to enjoy a lot of success along the journey, but it took a lot of work…and we've made our share of mistakes along the path.

- What if you could benefit directly from those years of experience – and avoid making similar mistakes?

- What if you could effortlessly access the lessons of grant managers and other professionals all working towards the same goal as you?

- What if you could easily keep up with the latest grant management resources, changes and trends?

We've got something to show you. We call it Grant Management Boot Camp, and it supports a well-trained workforce with training, e-mentoring and other resources to get you ready quickly and easily.

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