Internal Audit
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Executive Director, Internal Audit
Learning Objectives

- Understand Internal Audit’s mission and responsibility
- Understand the audit process
- Understand common audit areas
- Understand common audit findings
- Understand IT risks and findings
- Identify good internal controls and techniques
- Understand fraud indicators and reporting methods
Mission Statement

“To assist University units in effectively discharging their duties while ensuring proper control over University assets.”
Internal Auditor Approach

- We act as an independent objective internal assurance and consulting function designed to add value and improve the University’s operations.

- We are here to assist you and help protect our University as a whole.

- We try to view audit projects as a partnership with you and your department maintaining a relationship characterized by respect, helpfulness, and collaboration.

- We attempt to be as “transparent” as possible.
## Roles of IA & Management

<table>
<thead>
<tr>
<th>University Management</th>
<th>Internal Audit</th>
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<tbody>
<tr>
<td>Develops and enforces effective internal controls</td>
<td>Evaluates and provides reasonable assurance that <em>internal controls</em> are functioning as intended</td>
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<tr>
<td>Responsible for monitoring compliance with federal, state, or applicable laws</td>
<td>Evaluates compliance with federal, state, or other applicable laws</td>
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<tr>
<td>Responsible for setting policies and procedures</td>
<td>Evaluates compliance with MSU internal policies</td>
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<tr>
<td>RESPONSIBLE FOR MAKING MANAGEMENT DECISIONS</td>
<td>CANNOT MAKE MANAGEMENT DECISIONS</td>
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Audit Plan Development/Approval

“C’mon, why us???”

University-wide risk assessment
- Annual risk discussions - existing/emerging issues
- Special Project Time - investigations/special requests
- Cyclical Audits - inherent risks of your business
  - Likelihood (probability of occurrence)
  - Impact (effect on MSU/your unit)

Approval
- President
- Audit Committee
Audit Process

Typical Stages of an Internal Audit Review:

- **Planning**
  - Auditee Engagement
  - Inquires of Management & Staff
  - Risk Assessment
  - Audit Scope Determination

- **Fieldwork & Documentation**
  - Observations of Processes & Procedures
  - Sampling & Testing
  - Verification of Statement Made

- **Issue Discovery & Validation**
  - Risk Exposure Discovery & Evaluation
  - Risk Exposure Presentation to Management
  - Management Solution Development

- **Reporting**
  - Draft Report Development & Distribution
  - Management Response Opportunity
  - Final Report Distribution

- **Issue Tracking**
  - Post Audit Review & Follow Up
  - Periodic Status Updates

Internal Audit
Stage 1 - Planning

Audit engagement
- Engagement letter
- Preliminary information request

Opening meeting
- Project overview given to the management group
- Designate a primary contact person
- Official project start date

Inquiry of management & staff
- Interviews & Internal Control Questionnaires (ICQ)
- Tours

Scope definition
- Risk assessment
- Twelve-month “snap-shot”
Stage 2 - Fieldwork & Documentation

- Observations of processes & procedures
  - Observing critical processes or activities

- Sampling & testing
  - Select specific transactions, events or activities for testing
  - Collaboration with unit staff

- Verification of statements made
  - Sample the verbal statements made during the planning process to verify accuracy
Stage 3 - Issue Discovery & Validation

- Risk exposure discovery & evaluation
  - Risk identification process based on ICQs & fieldwork
  - Risk validation & mitigating controls discussion with personnel

- Risk exposure presentation to management
  - Discussion with management regarding identified risk & potential mitigating controls

- Management solution development
  - Risk mitigation vs. risk acceptance
  - Risk considerations in strategic planning
Stage 4 - Reporting

Draft report development & distribution
- Based on levels of identified risk
- Grade assignment is discussed
- Closing meeting discussion
- Limited draft distribution

Management response opportunity
- Due 30 days from issuance of draft report
- Short description of management’s action plan and timeline to address identified risk

Final report distribution
- Standard executive distribution list with additional unit requests
- Management responses included
Stage 5 - Issue Tracking

- Post audit review & follow up
  - Three (3) to six (6) months after final report is issued
  - Review status of management response
  - Written status report issued to final audit report distribution list

- Periodic status updates
  - Potential second post audit review
  - Otherwise, we may request periodic progress updates
Common Audit Areas & Findings
Common Audit Areas

- Understanding internal controls
  - Segregation of duties; reviews; reconciliations

- Testing significant activity including
  - Cash receipts/Accounts receivable
  - Expenditures (including payroll, travel, endowments/scholarships)
  - Procurement cards
  - Grant activity including effort reporting
  - Equipment inventory
  - Resale inventory

- Significant contracts

- Sensitive data

- Conflict of Interest/Outside work for pay
Common Findings

- Non-compliance with:
  - MSU Manual of Business Procedures (MBP)
  - Federal/State regulations

- Lack of segregation of duties – payroll, expenditures, receipting – fiscal officer role/HR roles

- Procurement cards not used or reconciled according to the Purchasing Card (Pcard) Users Manual

- Travel not authorized appropriately

- Travel voucher not completed according to Section 70 of the MBP
Contracts signed by someone without signature authority

Record retention - sensitive data stored in department

Conflict of Interest not disclosed

Outside work for pay policy not followed

Timeliness of cash deposits
Information Technology (IT) Auditing:

Defined as any audit that encompasses the review and evaluation of all aspects (or any portion) of automated information processing systems, including related non-automated processes, and the interfaces between them.
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Basically, a review of the flow of data through an IT infrastructure and the evaluation of the controls that help protect it...
“C.I.A.” Core Control Concept

Confidentiality
- Keeping sensitive data a secret from those without a need-to-know.
- Opposing Force: Disclosure (Fines, Legal Action, Loss of Public Trust)

Integrity
- Protecting data against unauthorized modifications.
- Opposing Force: Alteration (Inaccurate Info, Financial Loss, Waste of Resources)

Availability
- Ensuring data is readily accessible by authorized users.
- Opposing Force: Destruction (Waste of Resources, Financial Loss)
IT Risks

IT Infrastructure Risks:

• Sensitive information

• Electronic monetary transaction processes (PCI, ACH, etc.)

• System access restrictions and enforcement

• Weak password policies

• Overall network security controls
Typical IT Audit Findings

- Data Backup Procedures
- Business Continuity Plan
- Disaster Recovery Plan
- Access Controls
- Security Practices
IT Audit Sensitive Data Focus

Identified as a key risk to the University.

- *Examples:* SSN, Payment Card Data, Student Info., Medical Records, etc.
- *Liabilities of Disclosure:* Financial Loss, Legal Action, Loss of Public Trust, etc.

MSU Institutional Data Policy (IDP)

- Took effect on January 1\(^{st}\), 2011.
- Defines minimum requirements for securing University institutional data.
- Applies to all University business and academic units and all MSU employees.
- Visit the *MSU Information Security* webpage for more information.
  - [https://secureit.msu.edu/](https://secureit.msu.edu/)
How to Reduce Risk
Characteristics of a Good Internal Control Environment

❖ Tone at the Top
  • Management’s clear commitment to a culture of ethics, integrity and compliance

❖ Adequate management oversight

❖ Proper authorization of transactions and activities

❖ Adequate documents and records – original receipts scanned

❖ Physical safeguards – restricted access

❖ Segregation of duties

❖ Account activity is reviewed monthly and support for transactions is maintained
Fraud Indicators

- Pressure
- Opportunity
- Rationalization

The Fraud Triangle
Pressures

- High personal debt
- Poor credit
- Unexpected financial needs
- Addictions (gambling, drugs)
- Other Pressures
Opportunity

- Lack or circumvention of internal controls
- Past failure to discipline embezzlers
- Management apathy
- Ignorance or incapacity to detect fraud
- Lack of an audit trail
Rationalization

- The organization owes it to me
- I am only borrowing the money
- They can afford it
- I deserve more
- It’s for a good purpose
Methods of Reporting Misconduct

❖ MSU Misconduct Hotline
  • Phone or On-line reporting
  • Concerns reported include:
    • Conflict of Interest
    • Fiscal
    • Medical/HIPAA
    • Privacy
    • Research
    • Safety
    • Any Other Compliance Issue

❖ Direct contact with Internal Audit, MSU Police, HR, etc.

❖ Key links:
  • IA website: www.msu.edu/~intaudit
  • Misconduct Hotline website: http://misconduct.msu.edu
IT'S YOUR CALL

If you have a concern about misconduct, don't keep it to yourself. Discuss it with a supervisor, or contact the misconduct hotline online or by phone. Anonymous reports can be made 24 hours a day, seven days a week.

Report misconduct related to:
• Athletics
• Conflicts of interest
• Discrimination/harassment
• Employment
• Fiscal
Or any other compliance issues that do not fit into these categories

The Misconduct Hotline is not for reporting emergencies. If you need immediate assistance, please dial 9-1-1.

Misconduct Hotline
1-800-763-0764
misconduct.msu.edu

*Descriptions of misconduct types are provided at misconduct.msu.edu
*The MSU Misconduct Hotline is a tool for the MSU community and others to raise concerns regarding misconduct. The university contracts with a private company, The Network, Inc., to provide this reporting service.
Summary of Topics

- Internal audit overview
- Audit process
- Common audit areas and findings
- IT risks and findings
- Internal controls
- Fraud detection and prevention
Key Points for New Administrator

- Supervision – support fiscal officer – be involved
- Assignment of roles – review annually
- Conflict of interest – employment/vendor/time commitment
- Good internal controls – common sense
  - segregation of duties
  - approvals
  - reconciliations – pcards/general ledger/review transactions monthly
  - travel requirements/authorizations (section 70 Manual of Business Procedures)
    - [https://ctlr.msu.edu/combp/mbp70EBS.aspx](https://ctlr.msu.edu/combp/mbp70EBS.aspx)
- Professional service contracts
  - [https://usd.msu.edu/purchasing/purchase-orders/professional-services-contract/index.html](https://usd.msu.edu/purchasing/purchase-orders/professional-services-contract/index.html)
- Ethical decisions
- Maintain adequate documentation – scanned copies
- Compensation time – policy/documentation
- Address performance issues timely
Questions