

# Enhancing Management Involvement with Internal Control

The original recommended practice was developed by the Government Finance Officers Association (GFOA). Some aspects of the practice have been revised by the Financial Management Capacity Building Committee (FMCBC) for use by Nova Scotia municipal governments. The original GFOA recommended practice is *Enhancing Management Involvement with Internal Control*, approved by the GFOA in 2004. Other sources used are footnoted in the text.

## Recommendations

Financial managers should become involved in establishing internal control measures and take responsibility for enforcing such internal controls. The GFOA recommends that the internal control procedures should be documented, which could enable employees to report instances of management override of controls that could indicate fraud. In addition, financial managers should design and implement internal control policies that achieve their intended purpose and continue to function as designed. Lastly, the GFOA recommends an evaluation of internal controls that have been implemented to ensure that they are fulfilling their intended purpose. Based on the evaluation, any weaknesses should be addressed and solutions should be adopted in a timely fashion.

## Purpose

Internal controls are an important component of a municipality's daily operations, and all municipalities should introduce internal controls that best suit their needs. Internal controls have the potential to reduce risk and error, while enhancing accountability. Internal controls provide a system of checks and balances, and have the potential to reduce fraud and theft. Furthermore, internal controls provide a system that can help identify an area for potential problems and errors.

## Background

For an effective management of public funds, there must be adequate control procedures in place to protect the public's money and services. A framework of internal controls is necessary to create a reasonable basis for finance officers to provide legitimacy and reliability for the information that they provide.

## Considerations for Policy Development

Internal controls are processes that affect municipalities' council, management, and staff. Internal controls are designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

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

Management typically has the following five objectives in designing effective internal controls (See *Appendix I* for a further description):

- Maintaining reliable systems;
- Ensuring timely preparation of reliable information;
- Safeguarding assets;
- Optimizing the use of resources; and
- Preventing and detecting error and fraud.

In addition, there are certain fundamental concepts associated with internal controls that should be addressed:

- Internal controls are a process, a means to an end, and not an end itself.
- People at every level of an organization affect internal controls.
- Internal control can be expected to provide only reasonable assurance, not absolute assurance, to a municipality's management and council.
- Internal controls are geared to the achievement of objectives in one or more separate but integrated categories (see *Appendix II* for a further description):
  1. Control Environment
  2. Risk Assessment
  3. Control Activities
  4. Information and Communication
  5. Monitoring.<sup>1</sup>

In order for internal controls to be successful in monitoring the financial transactions of a municipality, the controls must be assessed and evaluated. Employees and Councilors should understand the extent to which the municipality's objectives are being achieved.

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<sup>1</sup> Committee of Sponsoring Organizations of the Treadway Commission. Internal Control – Integrated Framework. May 1994.

## **Appendices**

Appendix I: Objectives in Designing Effective Internal Controls

Appendix II: In Depth Discussion of COSO's Internal Control Framework

Appendix III: COCO's Internal Control – Integrated Framework

Appendix IV: Control Procedures

## Appendix I: Objectives in Designing Effective Internal Controls

### *Maintaining Reliable Systems*

Management must have reliable systems so that it will have accurate information for carrying out its operations. Such reliable systems can include information technology systems, a requirement of multiple signatures on purchase orders and cheques, and a segregation of duties within the municipality.<sup>2</sup>

### *Ensuring Timely Preparation of Reliable Information*

Information must be reliable and timely if it is to be useful for management decision-making. Management should provide quarterly financial statements within thirty days of the closing period.<sup>3</sup>

### *Safeguarding Assets*

To ensure against theft and fraud, adequate controls must be in place. Examples of safeguarding assets could be the appropriate signatures on cheques or accounts receivable documents. There should be a system of checks and balances in place.<sup>4</sup>

### *Optimizing the Use of Resources*

Controls within an organization are meant to optimize efficiency. Internal controls are meant to provide reasonable reassurance that the employees of the municipality are following established procedures to prevent duplicity and unnecessary tasks. A reduction in the duplication of tasks will also result in an efficient use of time and resources, which can create financial savings for the municipality.<sup>5</sup>

### *Preventing and Detecting Error and Fraud*

Internal controls of a government play an important role in the prevention and detection of error and fraud, or other irregularities. The cost of preventing error should be assessed based on the likelihood of the error actually occurring, the frequency and/or materiality of error that could occur, and the costs associated with the error. It is important to realize that not all error can be addressed and avoided, and concentration should be placed on the most serious errors.<sup>6</sup>

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<sup>2</sup> Arens, Alvin, and W. Morely Lemon, and James Loebbecke. *Auditing: An Integrated Approach*. 5<sup>th</sup> ed. Scarborough, ON: Prentice Hall Canada Inc., 1993.

<sup>3</sup> Ibid.

<sup>4</sup> Ibid.

<sup>5</sup> Ibid.

<sup>6</sup> Ibid.

## Appendix II: In Depth Discussion of COSO's Internal Control Framework

Council of Sponsoring Organizations (COSO) of the Treadway Commission on Fraudulent Financial Reporting has developed five components to the internal control framework that are critical to improve internal control mechanisms within a government. Many governments, municipalities, and audit firms throughout Canada and the United States are readily adopting COSO's internal control framework. These internal control mechanisms have the potential to increase efficiency within a municipality, as well as reduce the risk of fraud, theft, and error.

### 1. Control Environment

There are six components within the control environment component of the internal audit framework. These components consist of commitment to competence, board of directors or audit committee, management's philosophy and operating style, organizational structure, assignment of authority and responsibility, and human resources policies and practices.

- Commitment to Competence
  - The level of skill and competence needs to be established for particular jobs to ensure that the knowledge and skills are present to complete the job appropriately.
  - This would involve a formal job description and definitions of tasks, as well as the proper analysis of the knowledge and skills needed to perform difficult and highly complex jobs.
- Audit Committee
  - An independent group of elected officials that deal with difficult questions regarding plans and performance. This component will typically deal with internal and external auditors (where applicable).
  - This component must be separate from management in order to objectively and effectively evaluate management's practices, strategies, financial positions, and operating results.
- Management's Philosophy and Operating Style
  - Essentially how an organization is managed, if risk tolerance is established, and a manager's attitude towards financial reporting.
  - This component is assessed based on the nature of business, management's attitudes towards financial reporting, safeguarding of assets, and data process and accounting functions.
- Organizational Structure
  - Involves activities for achieving objectives that are planned, executed, controlled, and monitored. Areas of authority and responsibility are also identified to establish the appropriate lines of reporting.

- The organizational structure determines an organization's ability to provide necessary information to managers, managers responsibilities, the adaptability of an organization to change, and if there are a sufficient number of employees within the organization.
- Assignment of Authority and Responsibility
  - Involves the framework for which activities for achieving objectives is planned, executed, controlled, and monitored. Also establishes areas of authority and responsibilities by identifying appropriate lines of reporting.
  - This component assesses the delegation of authority to deal with entity goals and objectives, operating functions, and regulatory requirements.
- Human Resource Policies and Practices
  - Involves hiring, orientation, training, evaluation, counseling, promoting, compensating, and remedial actions. Also involves the expected levels of integrity, ethical behaviour, and competence.
  - Human resource policies and practices involves the procedures for hiring, promotion, and compensation; the extent to which employees are aware of their responsibilities; remedial actions taken in response to disobedience of policies and practices; adherence to moral and ethical standards, and adequacy of employee retention and promotion criteria.<sup>7</sup>

## 2. Risk Assessment

Municipalities should be aware of the risks that it faces, and deal with the problems that arise. Local governments should set objectives that allow the various divisions and tasks to operate in concert. Mechanisms should also be established to identify, analyze, and manage the risks.

There are four components of risk assessment – strategic plan, operational objectives, risks, and managing change.

- Strategic Plan
  - Should include a mission, vision, and value statement; a SWOT analysis, and the objectives must identify critical success factors.
  - Essentially provide guidance of what the organization wishes to achieve – which can be described though business plans, budgets, strategic plans, and current conditions.
- Operational Objectives
  - Operational objectives are linked to various objectives, and they must be clear and easy to understand, measurable, and that the objectives are balanced with the available resources.

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<sup>7</sup> Committee of Sponsoring Organizations of the Treadway Commission. "Internal Control – Integrated Framework." May 1994.

- Helps identify which objectives are important to the achievement of entry-wide objectives. Also helps determine if the resources are available to carry out the objectives and if managers are committed to executing the objectives.
- Risks
  - Risk involves risk identification (at the strategic planning and operational objective level), risk analysis (estimate the significant, assess the likelihood, and how the risk should be managed), and the management procedures.
  - Risks are to be identified from internal and external sources, as well as for each significant activity-level objective. This also includes estimating the significance of risks, assessing the likelihood of their occurrences, and determining if action needs to be taken, and if so, what is the required action.
- Managing Change
  - The existence of mechanisms to anticipate identifies and reacts to routine events that affect the achievement of entity/activity-level objectives.<sup>8</sup>

### **3. Control Activities**

Control activities involve various tools in order to implement an internal auditing system. Some mechanisms that can be used are policies and procedures that help ensure management directives are carried out, controls divided into operations, finance, and compliance, and preventative controls, detective controls, manual controls, computer controls, and management controls. Some examples of these types of control activities are top level reviews, direct function or activity management, information processing, physical controls, performance indicators, and segregation of duties. In order for such control activities to function properly, they need to be assessed and ensured that they are being applied properly and that the appropriate policies are in place.<sup>9</sup>

### **4. Information and Communication**

- Information
  - Information that is identified, captured, and communicated should be relevant to managing the organization. Furthermore, the information should be determined if it is for the employees and elected officials of the municipality or the citizens, and if it is financial or non-financial.
  - The information should then to be relayed to the appropriate people so that they can carry out their responsibilities efficiently and effectively. Also, a strategic plan should be linked to the organization's overall strategy.

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<sup>8</sup> Committee of Sponsoring Organizations of the Treadway Commission. "Internal Control – Integrated Framework." May 1994.

<sup>9</sup> Ibid.

- Communication
  - There is communication among the employees and elected officials of the municipality (internal) and communication with the citizens (external). Internal communication involves expectations and responsibilities of individuals and groups. Internal communication also involves determining the cause behind a problem in addition to finding a solution. External communication involves opening communication channels.
  - In order to implement effective communication channels, employee's duties and responsibilities need to be communicated effectively and opportunities for employees to offer suggestions to enhance productivity.<sup>10</sup>

## 5. Monitoring

In order to effectively monitor financial activities, there must be ongoing monitoring activities, separate evaluations, and reporting deficiencies. With the reporting deficiencies, it must be ensured that internal controls continue to operate effectively and that the quality of the system's performance is assessed. Monitoring can be executed by determining if an internal control is functioning as it was initially intended, if external and internal parties are working cooperatively, and responsiveness to internal and external auditor recommendations on means to strengthen internal controls.<sup>11</sup>

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<sup>10</sup> Committee of Sponsoring Organizations of the Treadway Commission. "Internal Control – Integrated Framework." May 1994.

<sup>11</sup> Ibid.

## Appendix III: COCO's Internal Control – Integrated Framework

The Canadian Institute of Canada's Criteria of Control (COCO) report is a system of internal controls for financial reporting and internal management. COCO is an adaptation of COSO, which is the most widely adopted and accepted reference on control in the United States and internationally. COCO is especially unique because it includes objective setting as part of the control system, which enables municipalities<sup>12</sup> to examine its implicit (or explicit) assumptions and expectations about the environment. Since the assumptions underlying the objectives would be open for discussion, more unforeseen events may surface.<sup>13</sup> Since COCO is an adaptation of COSO's internal control framework, large areas of overlap exist; however, they also differ in some respects.

### COCO's Internal Control – Integrated Framework

COCO's internal control integrated framework includes four different aspects that include a purpose, commitment, capability, and monitoring and learning.

#### *Purpose*

This component of the internal control framework has separate components within itself. These components include objectives, risks and opportunities, policies, planning, and performance targets and indicators.

- Objectives
  - A mission, vision, and strategy should be established towards a municipality's overall objectives.
  - Objectives should be established, communicated, and prioritized to provide direction.
  - Objective-setting: deciding what objectives to adopt is an aspect of managing that is outside of control.
- Risks and Opportunities
  - A municipality should identify its significant internal and external risks on an ongoing basis so that it can react to changes in an appropriate and timely manner.
  - Risk assessment should be considered to estimate the likelihood of an event and the significance of its consequences so that appropriate policies and processes can be developed to manage them.
  - In addition to identifying risks, it is important to recognize where risks stem from.

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<sup>12</sup> Please note that where "municipality" is referred to, in the original COCO document, the reference is "organization".

<sup>13</sup> Zimmerman, Brenda. "Message in a Hologram: Properly Functioning Internal Control Systems can Improve the Visibility of Today's Organizations and Industries". *CA Magazine*. June/July 1995.

- Policies
  - Policies should be designed to support the achievement of a municipality's objectives and the management of its risks should be established, communicated, and practiced.
  - Policies also provide guidelines to be internal controls for municipalities.
- Planning
  - Planning translates objectives and risk assessments into strategies, action plans, and operating and financial targets.
  - It is a continuous process, and plans should not be static.
- Performance Targets and Indicators
  - Performance indicators can be used to measure performance against targets and to provide early warning if targets have been exceeded or have not been met.

### *Commitment*

This component of COCO's internal control framework also has several subheadings that include ethical values and integrity, human resource policies, authority, responsibility, and accountability, and mutual trust.

- Ethical Values and Integrity
  - Shared ethical values should be established, and these can contribute to control because it provides a guide for individual, group, or team decision-making, action, and policy.
- Human Resource Policies
  - Human resource policies and practices should be consistent with a municipality's ethical values and with the achievement of its objectives.
- Authority, Responsibility, and Accountability
  - Authority, responsibility, and accountability should be clearly defined and consistent with a municipality's objectives so that the appropriate people make decisions and take actions.
  - Clearly defined authority, responsibility, and accountability help ensure that qualified individuals make critical decisions.
- Mutual Trust
  - An atmosphere of mutual trust should be fostered to support the flow of information between people and their effective performance toward achieving the municipality's objectives.
  - Mutual trust supports the flow of information that people need in order to make decisions and take action.
  - Open communication both creates and depends on trust, and a high level of trust encourages sharing of information.

### *Capability*

The component of capability within COCO's internal control framework also has several subheadings that include knowledge, skills, and tools, communication process, information, coordination, and control activities.

- Knowledge, skills, and tools
  - People working within the municipality should have the necessary knowledge, skills, and tools to support the achievement of the municipality's objectives.
  - There should be the right match of people with the tasks to be performed along with the necessary skills and capabilities, which can be assessed through the establishment of requirements and training.
- Communication Process
  - Communication process should support the municipality's values and the achievement of its objectives.
  - For control to be effective, a municipality should have a communication process capable of supporting open communication of timely, relevant, and reliable information.
  - Two-way communication helps to ensure that communication processes are flexible and responsive, and communicating the views of those most directly affected by decisions are key to the success of implementation.
- Information
  - Sufficient and relevant information should be identified and communicated in a timely manner to enable people to perform their assigned responsibilities.
- Coordination
  - The decisions and actions of different parts of a municipality should be coordinated.
  - Since a municipality is typically complex with varying departments and divisions, decisions and actions should require coordination to achieve objectives as a whole.
  - Coordination improves integration, consistency, accountability, and limits autonomy.
- Control Activities
  - Control activities should be designed as an integral part of the municipality, taking into consideration its objectives, the risks to their achievement, and the inter-relatedness of control elements.
  - Control activities are routines established to provide assurance that processes operate as designed and meet the requirements of the municipality's policies.

### *Monitoring and Learning*

This component of the internal control framework has separate components within itself. These components include monitoring internal and external environments, monitoring performance, challenging assumptions, reassessing information needs and information systems, follow-up procedures, and assessing the effectiveness of control.

- **Monitoring Internal and External Environments**
  - External and internal environments should be monitored to obtain information that may signal a need to re-evaluate the municipality's objectives or control.
  - Monitoring the external environment can provide valuable information on the state of the internal environment, and to a large extent, managers can initiate or control changes to the internal environment.
  - Information gained through monitoring environments may signal a need to re-evaluate the municipality's objectives or other aspects of the municipality.
- **Monitoring Performance**
  - Performance should be monitored against the targets and indicators identified in the municipality's objectives and plans.
  - To monitor performance, there must be timely and reliable information made available on operating results.
- **Challenging Assumptions**
  - The assumptions behind a municipality's objectives should be periodically challenged.
  - If a municipality's assumptions are incorrect or outdated, control may be ineffective, and periodically changing a municipality's assumptions can be the key to effective control.
- **Reassessing Information Needs and Information Systems**
  - Information needs and related information systems should be reassessed as objectives change or as reporting deficiencies are identified.
- **Follow-up Procedures**
  - Follow-up procedures should be established and performed to ensure appropriate change or actions occur, enabling control to remain effective.
  - For change to be effective, information such as the results of control assessments must be communicated to those who can authorize change.
- **Assessing the Effectiveness of Control**
  - Management should periodically assess the effectiveness of control in its municipality and communicate the results to those whom it is accountable.

## **Comparison of COCO to COSO**

There are three main differences between the American COSO and Canadian COCO framework on internal controls. The differences between the two internal control frameworks can be found in the definition and the scope, the underlying concepts, the judgment of effectiveness.

### *Definition and Scope*

COSO defines internal control as a process, effected by a municipality's councilors, managers, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

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

COCO defines control as the elements of a municipality (including its resources, systems, processes, culture, structure, and tasks) that, taken together, support people in the achievement of the municipality's objectives. It defines three categories of objectives:

- Effectiveness and efficiency of operations
- Reliability of internal and external reporting
- Compliance with applicable laws and regulations and internal policies.

Consistent with its definition, COCO includes the scope of control some particular aspects of management that COSO excludes: objective setting, strategic planning and risk management, and corrective actions. COCO does exclude decision making from the scope of control.

### *Underlying Concepts*

COCO is explicit about some concepts that are not addressed in COSO. These are:

- (a) Control includes the identification and mitigation of the risk failure to maintain the municipality's capacity to identify and exploit opportunities.
- (b) Control includes the identification and mitigation of the risk of failure to maintain the municipality's resilience – its capacity to respond and adapt to unexpected risks and opportunities, and to make decisions on the basis of telltale indications in the absence of definitive information.
- (c) COCO includes two criteria not explicitly addressed in COSO. They relate to mutual trust between people and the periodic challenge of assumptions. In addition, the concept of monitoring in this COCO guidance includes monitoring of the operating performance of the municipality. COSO's discussion of monitoring could be interpreted as focused on monitoring of specific control activities.

*The Judgment of Effectiveness*

COSO addresses this as follows: “Internal control can be judged effective in each of the three categories, respectively, if the board of directors and management have reasonable assurance that:

- They understand the extent to which the municipality’s operations objectives are being achieved.
- Published financial statements are being prepared reliably.
- Compliance with applicable laws and regulations.

Determining whether a particular internal control system is effective is a subjective judgment resulting from an assessment of whether five components (control environment, risk assessment, control activities, information and communication, and monitoring) are present and functioning effectively. Their effective functioning provides the reasonable assurance regarding the achievement of one or more of the stated categories of objectives. Thus, these components are also criteria for effective internal control.

**COCO differs in three important respects:**

- (a) The judgment of effectiveness is made in relation to a specific objective, not a category of objectives.
- (b) COCO asks that an assessment of the effectiveness of control be made against twenty specific criteria. COSO asks that assessment be made for each of five components, and provides illustrative issues to consider for each component. All of COSO’s issues to consider are addressed directly or indirectly within the COCO document, except perhaps the following:
  - Receptivity of management to employee suggestions of ways to enhance productivity, quality, or other similar improvements.
  - Extent to which personnel, in carrying out their regular activities, obtain evidence as to whether the system of internal controls continues to function.
  - Extent to which outside parties have been made aware of the entity’s ethical standards.
  - Extent to which training seminars, planning sessions, and other meetings provide feedback to management on whether controls operate effectively.
  - Appropriateness of the level of documentation (of an evaluation).
- (c) COCO includes the following definition of effective control: Control is what makes a municipality reliable in achieving its objectives. Control is effective to the extent that it provides reasonable assurance that the municipality will achieve its objectives.<sup>14</sup>

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<sup>14</sup> “Guidance on Control.” Control, Risk and Governance. Toronto, ON: The Canadian Institute of Chartered Accountants, 1995.

## Appendix IV: Control Procedures

In addition to monitoring misstatements in financial reporting, there are further control procedures that can be followed in order to reduce the risk of fraud and theft in municipalities. The five control procedures include appropriate segregation of duties, proper authorization of transactions and activities, design and use of adequate documents and records, adequate safeguards over access to and use of assets and records, and computer-generated or manual verifications of performance and the accuracy of recorded amounts.

### *Appropriate Segregation of Duties*

There are four guidelines for the appropriate segregation duties to prevent both intentional and unintentional misstatements.

- Separation of the custody of assets from accounting
  - In order to protect a municipality against defalcation, the person who has temporary or permanent custody of an asset should not account for the asset. When one person performs both functions, there is an excessive risk of that person's disposing of the asset for personal gain and adjusting the records to relieve themselves of responsibility.
- Separation of the authorization of transactions from the custody of related assets
  - It is desired to prevent persons who authorize transactions from having control over the related asset. The person who authorizes the bill should not be the same person who pays the bill.
- Separation of operational responsibility from record-keeping responsibility
  - To ensure unbiased information, record keeping should be kept as a separate duty from the person who prepares the performance reports.
- Separation of duties within electronic data processing (EDP)
  - These duties should be kept separate to reduce the risk and likelihood of fraud and theft.
    - Systems Analyst – designs of the computer system.
    - Computer Programmer – should not have access to input data or computer operations because this information could be used for fraud or theft.
    - Computer Operator – has the knowledge to change computer programs, and could temporarily change the system for fraud or theft.
    - Librarian/Bookkeeper – maintains the computer programs that contain important classified information only to be released to authorized personnel.

- Data Control Group – performs internal verification, which could enable this group to use this knowledge for personal gain.

This control component emphasizes the importance of keeping duties separate to ensure that a public servant cannot have the opportunity to engage in theft or fraud. By ensuring a system of checks and balances, these functions can act as successful internal controls.<sup>15</sup>

#### *Proper Authorization of Transactions and Activities*

If internal controls are to be exercised properly, every transaction must be properly authorized. Authorization can be divided into two specific groups: general and specific. General authorization means that management establishes policies for the municipality to follow. There would be specific rules to follow to ensure accountability and that proper authorization has been granted. A general authorization may be a limitation on the amount a public servant can spend on travel expenses. Specific authorization refers to individual transactions – where management does not typically establish general policies. These situations are generally handled on a case-by-case basis. Specific authorization may be the authorization from a manager to purchase a new laptop for the office.<sup>16</sup>

#### *Design and Use of Adequate Documents and Records*

Documents and records are the physical components of transactions. Documents transmit information throughout the organization and between different organizations. The documents must be adequate to provide assurance that assets are properly controlled and transactions correctly recorded.

Documents and records should be:

- Pre-numbered consecutively to facilitate control over missing documents, and in locating documents when they are needed in the future.
- Prepared at the time a transaction takes place.
- Sufficiently simple to ensure that they are clearly understood.
- Designed for multiple use whenever possible.
- Constructed in a manner that encourages correct preparation.

An example of an effective document and record is a chart of accounts, which classifies transactions into individual balance sheet and income statement accounts. The chart of accounts is an important control because it provides the framework for determining the information presented to management and other financial statement users. It is also important because it includes information that clearly distinguishes transactions – such as capital assets, inventories, and expense items.<sup>17</sup>

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<sup>15</sup> Arens, Alvin, and W. Morely Lemon, and James Loebbecke. *Auditing: An Integrated Approach*. 5<sup>th</sup> ed. Scarborough, ON: Prentice Hall Canada Inc., 1993.

<sup>16</sup> Ibid.

<sup>17</sup> Ibid.

*Adequate Safeguards Over Access to and Use of Assets and Records*

The most important type of protective measure for safeguarding assets and records is the use of physical precautions. Access controls deal with ensuring that only authorized personnel can use equipment and have access to certain data files. Backup and recovery procedures are steps an organization can take in the event of a loss of equipment, programs, or data.<sup>18</sup> Further information on computer disaster recovery can be found in NSMFC's Technology Disaster Recovery Planning best practice.

(<http://www.gov.ns.ca/nsmfc/documents/TechnologyDisasterRecoveryPlanning.pdf>).

*Computer-Generated or Manual Verification of Performance and the Accuracy of Recorded Amounts*

This control mechanism is an example of an independent check on performance or internal verification. An essential characteristic of the persons performing internal verification procedures is that they remain independent from the individuals originally responsible for preparing the data.<sup>19</sup>

*Closing Remark:*

Realizing the challenge that a smaller municipality may face in the segregation of duties, it is important that the managers adopt strengthened internal controls. There must be segregation and independence of duties in order to reduce theft and fraud, while increasing accountability.

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<sup>18</sup> Arens, Alvin, and W. Morely Lemon, and James Loebbecke. Auditing: An Integrated Approach. 5<sup>th</sup> ed. Scarborough, ON: Prentice Hall Canada Inc., 1993.

<sup>19</sup> Ibid.

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