



Review of the “Cost-effective Internal Control Guidelines – Underpinning Agency Performance”

Invitation to Comment

TOPIC PAPER 1 – PROPOSED FORMAT OF NEW GUIDELINES

Prepared by Queensland Treasury
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Introduction

Queensland Treasury is publishing this Topic Paper to contribute to the review and update of the guidance document *Cost-effective Internal Control Guidelines: Underpinning Agency Performance* (the Guidelines). With Queensland's public sector financial legislation being rewritten on a principles-based approach, there will be increased reliance on guidance material to assist agencies with applying the new legislation to their individual circumstances.

This Topic Paper focuses on the proposed format of the revised guidance material, which will be applicable to all departments and statutory bodies.

All interested stakeholders are invited to review the topic papers and provide feedback to fmbregistrations@treasury.qld.gov.au by **Monday 15 September 2008**.

All feedback will be reviewed, and incorporated where it is considered to enhance the project and subsequent Guidelines.

Comments are most helpful if they contain a clear rationale and, where applicable, provide a suggestion for alternative wording.

Enquiries about the topic papers should be addressed to either:

Ms Lee Clayton
Financial Management Branch
Queensland Treasury
Tel: (07) 322 42922
email:
lee.clayton@treasury.qld.gov.au

Ms Ruth Bergin
Financial Management Branch
Queensland Treasury
Tel: (07) 322 52783
email:
ruth.bergin@treasury.qld.gov.au

Issues

The current Guidelines are contained in a single document (available in both hard copy and electronically), covering a variety of issues with respect to financial management and internal controls. While this format ensures all the information is available in one location, there are disadvantages to having only one document, including:

1. users need to scroll through a large document to find the information being sought
2. an update to one section will require re-release of the entire document
3. a large document is more difficult to review and keep up-to-date
4. it is not as easy to update the document to include new information for emerging issues.

This Paper proposes three changes to the format of the current Guidelines.

Proposals

1. Name of Guidelines

It is proposed that the Guidelines be changed from a single document to a user manual format, called a 'Financial Management Manual'.

Treasury first published a Financial Management Manual in June 1998 which covered a wide range of issues including the Financial Management Framework, strategic planning, the State Budget process, performance evaluation and the accounting policy guidelines.

While the revised Guidelines will initially contain information about governance and the establishment and review of internal controls only, changing to a user manual format will allow for a wider scope in the future, if this is considered appropriate.

2. Information Sheets

It is proposed that the user manual will consist of a suite of brief information sheets, for example, no more than five pages per information sheet. The user manual will be accessible via the Treasury website.

The aim is for each information sheet to be a stand-alone document which is practical, user friendly and targeted to a specific aspect of financial management.

The advantages of information sheets include:

- Short, targeted information is available on specific topics
- Need to scroll through a large document to find information is diminished
- Update of one section will not require re-release of entire document
- Regular review and update of short documents is easier
- Update for emerging issues is facilitated.

Related topics can be grouped into a logical sequence under a number of 'volumes' to assist users in quickly locating all relevant and related information. Each volume can contain an overview page which outlines the purpose of the volume, as well as the list of each information sheet in the volume with its issue date. Publishing the issue date will assist users to ensure they are accessing the most recent information sheet released on the topic.

Given the proposal to keep the information sheets brief, each could contain a list of some of the external resources available on the topic, in case users are interested in more detailed information.

Refer to Topic Paper 2 for proposed list of information sheets.

3. Consideration Points

The appendices in the current Guidelines contain a number of tables identifying some of the more common key internal controls that address specific risks which would be appropriate to most agencies of reasonable size and complexity.

In their current form, the controls outlined in the tables could be perceived as mandated responses to the example risks provided. To clarify they are not intended as prescribed requirements, it is proposed that the tables be replaced with 'consideration points'.

These consideration points could be used as prompts for officers responsible for implementing and/or reviewing their agency's controls, without being too prescriptive. These consideration points could be prepared for each major system common to all agencies, e.g. revenue, expenditure and assets systems.

Attachments

Three attachments are provided to demonstrate the proposals contained within this Topic Paper:

Attachment A – contains an example format of a volume overview.

Attachment B – contains an example format of an information sheet.

Attachment C – contains an example format of the 'consideration points'.

Please note the wording in the attachments is a 'sample' only, much of which has been transferred from the current Guidelines. The attachments are to be assessed from a format view point only – not an assessment of the contents.

Invitation to Comment Questions

1. Do you support the proposed format of a user manual containing volumes and information sheets? If not, please provide reasons.
2. Do you consider the tabular format and information contained in the appendices of the existing Guidelines beneficial?
3. Do you consider that the proposal to change the current appendices into 'consideration points' will be beneficial?
4. Please provide other comments, if any, on the issues outlined in this topic paper.

Overview of Volume

Purpose

The purpose of this volume is to promote and provide guidance on internal controls appropriate to most public sector agencies of reasonable size and complexity.

Volume 5 of the Financial Management Manual identifies some of the more common key internal controls.

Content

This volume consists of the following Information Sheets:

Reference	Information Sheet Title	Date Issued
3.1	What are internal controls?	July 2008
3.2	Purpose of internal controls	July 2008
3.3	Limitations of internal controls	July 2008

Information Sheet 3.3 - Limitations of Internal Control

Introduction

It is rare for any system of internal control to provide total security over an agency's operations and inherent limitations exist in most systems that preclude absolute assurance, even through due care and diligence may have been exercised.

This is referred to as the *reasonable assurance principle*.

Factors to Consider

Factors that can impact on, or result in breakdowns in, the control structure and processes include:

- the fact that controls may not be directed at unusual transactions. An effective control culture and adequate supervision are the most effective deterrents in this area
- the potential for human error due to carelessness, distraction, faulty judgement or the misunderstanding of instructions. A strong ethical culture, an adequate professional development program and the maintenance of procedures manuals, including an agency specific Financial Management Practice Manual, can minimise this risk
- the possibility of the circumvention of controls through collusion. This risk can be minimised by a strong ethical culture and practices in the agency and adequate supervision
- the possibility that a control could be over-ridden. This risk also can be controlled by a strong ethical culture and an adequate separation of duties and supervisory functions
- the possibility that procedures have become inadequate due to changed conditions or the deterioration of procedures over time. Systems appraisals, which must be conducted at least once every three years, in conjunction with effective internal audit, will assist, maintain and enhance the efficiency and effectiveness of the control system, and
- the requirement that controls be cost-effective. In other words, there is a point at which it makes good business sense to accept a risk rather than implement a control that is disproportionate to the risk, in terms of cost.

Managers must be attentive to issues of internal controls to minimise the risk of fraud, error and loss . . .

Additional Note for Small Agencies

In relation to small regional offices and agencies, where often only a limited number of persons are employed, internal controls may not be as strong as in larger entities. For example, it may be difficult to achieve a strong separation of duties.

In these instances, it becomes important that the person in charge of the office take a proactive role in the supervision of its day to day operations and that the agency's overall system of internal control provide for some form of head office monitoring and regular internal audit.

Small agencies are often the most vulnerable to fraud because they often don't have effective internal controls . . .

For small statutory bodies where there may be a limited number of personnel and a board, committee or like structure exists, it is desirable that the chairperson or another board member with financial management skills maintain some 'hands on' supervision over the agency's operations, particularly high risk transactions.

This could occur by requiring agency cheques to be countersigned by the member, reviewing expense listings for unusual and high value items and ensuring that key accounting records and reconciliations are maintained to an up to date position.

Where practicable, an internal audit service also should be utilised. This could be provided on a part-time, shared or outsourced basis.

Related Resources

- The Financial Management Framework (FMF) forms the basis for decisions on planning, resource allocation and management, monitoring and reporting within the Queensland public sector. Visit the Resources page on the FMF website for guidance, published reports, relevant websites and other educational resources.
 - www.treasury.qld.gov.au/fmf

Further Information

If you have any questions concerning the Financial Management Manual, please contact the relevant Business Branch of Treasury for your agency.

Alternatively, email the Financial Management Helpdesk with details of your query and a response will be provided by the Financial Management Branch of Treasury:

- FMHelpdesk Email: fmhelpdesk@treasury.qld.gov.au

Payroll and HR Systems - Consideration Points

This function deals with the activities relating to the management of the agency's personnel processes, including payroll and employee data. The following is a list of aspects to be considered by an agency in establishing and maintaining their system of internal control. Some points raised may not be applicable to all agencies. The questions are designed to assist an agency in identifying adequacy of controls and to facilitate discussion of the control processes.

Legal Compliance

- ⇒ Is there adequate training of appropriate agency personnel on industrial relations, privacy and regulatory policies?
- ⇒ Is there an ongoing review and update of agency policies and procedures for compliance with applicable statutory, regulatory and other requirements?

Recruitment and retention of qualified personnel

- ⇒ Do personnel screening and recruitment practices exist that ensure appointments are only on merit, qualifications and suitability for position sought?
- ⇒ Are recruitment criteria and position descriptions sufficient to measure employee performance?
- ⇒ Is there an assessment of personnel needs as part of ongoing human resource planning process?
- ⇒ Is there adequate planning to ensure that only appropriately skilled and qualified staff undertake relieving duties?
- ⇒ Is there an assessment of employee performance in terms of individual personal performance evaluation and review processes?

Appointment and Termination Processes

- ⇒ Is there maintenance of secure records and written authorisation for all employee appointments, promotions, transfers and terminations, including in respect of casual and contracted employees?
- ⇒ Is there maintenance of secure records and written authorisation for all leave taken and reconciliation with payroll records?
- ⇒ Is there regular review of accuracy of personnel records?
- ⇒ Are the processes for termination issues, including payroll deletions, ICT access and security and return of agency resources, including keys, entry, corporate and identification cards adequate?