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DATE: June 14, 2017
TO: LWDB Executive Directors
FROM: Mike Beene, Director Workforce Services
CC: Workforce Services, Fiscal, CRC
RE: Establishing Internal Controls

Purpose: The purpose of this Guidance Letter is to advise Local Workforce Development Boards (LWDBs) of the need to establish adequately documented Internal Controls as sub-recipients of WIOA Title I funds.

References: 2 CFR Part 200 and 20 CFR Part 683.220

Background:

On December 26, 2013, the Office of Management and Budget (OMB) released new guidance on *Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, which has been dubbed the "Super Circular." These sweeping changes are the result of more than two years of work by both federal and nonfederal financial assistance sectors overseen by the Council on Financial Assistance Reform. The new guidance affects entities receiving and administering federal awards as well as auditors responsible for auditing federal awards programs. Final guidance is located in Title 2 of the Code of Federal Regulations.

A major goal of the circular was to provide guidance that would strengthen oversight over federal funds to reduce risks of waste, fraud and abuse

It is important to note the standard 2 CFR §200.303 establishes regarding Internal Controls.

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States and the "Internal Control Integrated Framework", issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).*

Non-Federal entities (any entity that is not Federal; such as State & Local recipients and sub-recipients) must establish internal controls that are compliant with "Standards for Internal Control in the Federal Government," (also called the Green Book) issued by the Comptroller General of the U.S., and "Internal Control Integrated Framework," issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

WIOA Regulations repeat this requirement, almost verbatim, at 20 CFR §683.220:

- (a) Recipients and subrecipients of WIOA Title I and Wagner Peyser Act funds must have an internal control structure and written policies in place . . . reasonable assurance that the entity is:
 1. Managing the award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award
 2. Complying with Federal statutes, regulations, and the terms and conditions of the Federal award. . .

(b) Internal controls should be in compliance with the guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the U.S., and “Internal Control Integrated Framework,” issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). See 2 CFR 200.303.

Guidance:

The requirement is to establish and maintain effective internal controls that provide reasonable assurance awards are being managed in compliance with Federal statutes, regulation and the terms and conditions of the Federal award. The Uniform Guidance and WIOA Regulations refer to specific documents for illustrative, rather than prescriptive, purposes. Entities and their auditors will need to exercise judgment in determining the most appropriate control in a given environment or circumstance to provide reasonable assurance for compliance with Federal program requirements.

Briefly, the ‘Green Book’ uses the same graphical representation for evaluating an organization’s internal control as was initially developed by COSO; a three dimensional cube.



One side of the cube is made up of four levels of organizational structure:

1. **Entity**
2. **Division**
3. **Operating Unit**
4. **Function**

The second side of the cube illustrates the three categories of an organization’s objectives:

1. (effective and efficient) **Operations**
2. (reliable) **Reporting**
3. (statutory/regulatory) **Compliance**

The third dimension are the five components of internal control which apply to all staff at all (4) organizational levels and to all (3) categories of objectives:

1. **Control environment:** The control environment sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure. Control environment factors include the integrity, ethical values, management's operating style,

delegation of authority systems, as well as the processes for managing and developing people in the organization.

2. **Risk assessment:** Every entity faces a variety of risks from external and internal sources that must be assessed. A precondition to risk assessment is establishment of objectives and thus risk assessment is the identification and analysis of relevant risks to the achievement of assigned objectives. Risk assessment is a prerequisite for determining how the risks should be managed.
3. **Control activities:** Control activities are the policies and procedures that help ensure management directives are carried out. They help ensure that necessary actions are taken to address the risks that may hinder the achievement of the entity's objectives. Control activities occur throughout the organization, at all levels and in all functions. They include a range of activities as diverse as approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets and segregation of duties.
4. **Information and communication:** Information systems play a key role in internal control systems as they produce reports, including operational, financial and compliance-related information that make it possible to run and control the business. In a broader sense, effective communication must ensure information flows down, across and up the organization. For example, formalized procedures exist for people to report suspected fraud. Effective communication should also be ensured with external parties, such as customers, suppliers, regulators and shareholders about related policy positions.
5. **Monitoring:** Internal control systems need to be monitored—a process that assesses the quality of the system's performance over time. This is accomplished through ongoing monitoring activities or separate evaluations. Internal control deficiencies detected through these monitoring activities should be reported upstream and corrective actions should be taken to ensure continuous improvement of the system.

This is a total of 60 intersections, or building blocks of the cube.

An internal control system compliant with this model would, among other things, include written policies and procedures for each level of an organization's (5) structural components and each of the (3) objectives. This would include activities that occur at all levels as diverse as approvals, authorizations, verifications, reconciliations, reviews, etc. This would also likely include organizational decision making and staffing charts to illustrate roles and responsibilities and accountabilities of individuals within the organization.

In addition to being a vehicle to assess the strength of internal control within an organization, a compliant model assist in achieving transparency and creating firewalls, where necessary.

In those areas where firewalls are either desirable or required, compliant entities should be able to overlay the organizational decision making and staffing charts of any two or more particular functions (e.g.; Fiscal Agent, Provider of Service, Board Staff, etc.) to reveal where overlap exists and a firewall may be appropriate.

Should a subrecipient implement an alternative internal control model of their own choosing, to be compliant that model must include the level of detail and evaluation rigor as the "Standards for Internal Control in the Federal Government," (aka Green Book) issued by the Comptroller General of the U.S., or "Internal Control Integrated Framework," issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

For questions or additional technical assistance, please contact Dennis Cooper @ (316) 771-6810, dennis.cooper@ks.gov or workforcesvcs@ks.gov