Public Housing Authority Financial Management Training

Module 5:
Effective Internal Controls
Module 5 Topics

• Definition of Internal Controls
• Development and Implementation of Internal Control System
• Examples of Individual Financial Policies and Procedures
• Internal Controls: Other Items to Consider
Module 5

DEFINITION OF INTERNAL CONTROLS
Internal Control Requirements

• The PHA must establish and maintain effective internal controls (OMB 2 CFR 200.303). Section 200.303 Internal Controls states:
  – The non-Federal entity must: 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)
Internal Control Requirements (Continued)

• In simple terms, this means that the PHA must have policies and procedures in place which will help ensure:
  – Effective and efficient administration of the program
  – Establishment and attainment of operational and financial performance goals
  – Assets are safeguarded against loss
  – Reliability (i.e., the information is correct), timeliness, and transparency in both internal and external reports
  – Adherence to laws and regulations to which the entity is subject
Components of Internal Control

COSO / Green Book Example

Component of Internal Controls

• Both control systems have the following components:
  – Control Environment
  – Risk Assessment
  – Control Activities
  – Information & Communication
  – Monitoring Activities
What is the Control Environment?

• Control environment can be defined as the foundation of the PHA. It represents the structure (i.e., staffing, systems, organizational structure, etc.) to carry out the internal controls across the PHA.

• The Board of Commissioners and senior management set the **tone at the top** regarding the importance of following procedures.

• Control environment principles include:
  – Demonstrating expected standards of conduct including integrity and ethical values.
  – The oversight body should oversee the PHA’s internal control system.
  – Management should establish an organization structure to achieve the PHA’s objectives within funding levels.
  – Commitment to recruit and hire competent individuals.
  – Evaluating performance of individuals and disciplining individuals that fail to adhere to established procedures and policies.
  – Management follows policies and procedures as an example to all others in the agency.
What is Risk Assessment?

• Risk assessment can be defined as a process to identify events that may occur that would adversely affect the achievement of PHA objectives. Risks could be related to objectives throughout the PHA or be specific within a department or program.

• Risk assessment principles include the following:
  – Management should establish objectives to identify risks and define risk tolerances
  – Identification, analysis, and response to noted risks (document)
  – Consider the potential for fraud in assessing risks
  – Analyze and respond to significant changes that could impact the internal control system
What are Control Activities?

• Control activities can be described as the actions through policies and procedures used to achieve objectives to identified risks in the internal control system, which may include the entity’s information system.

• Control Activities principles include the following:
  – **Management** should design control activities to achieve objectives and respond to risks.
  – **Management** should design the PHA’s information system and related control activities to achieve objectives.
  – **Management** should implement control activities through policies and procedures.

*Note:* While personnel from the finance office can aid in the development of procedures, it is ultimately the responsibility of management to determine the procedures and require that control activity principles are implemented.
What Is Information and Communication?

• The information and communication component is defined as the use of quality information to support the achievement of the objectives. Communication is a continual process of providing, sharing, and obtaining necessary information. Internal communication is the means to share information throughout the PHA, flowing up, down, or across the entity. It enables employees to receive a clear message that controls and objectives must be taken seriously.

• Principles of information and communication include:
  – Management should use quality information to achieve the entity’s objective
  – Management should internally communicate the necessary quality information to individuals to achieve the entity’s objectives
  – Management should externally communicate the necessary quality information to achieve the entity’s objectives
What Are Monitoring Activities?

• Monitoring can be defined as the evaluation of the system to ascertain that the components are present and functioning to achieve the objectives. Monitoring also includes assessing the quality of performance over time and promptly resolving the findings of audits and other reviews.

• Principles of the monitoring activities include:
  – Management should establish monitoring activities to verify the use of the internal control system and evaluate the results.
  – Management should remediate identified control deficiencies in a timely manner.
Module 5
DEVELOPMENT AND IMPLEMENTATION OF INTERNAL CONTROL SYSTEM
Development of Internal Control System

• Step 1: Identify risks related to transaction types, accounts, and compliance items
• Step 2: Identify possible resources/personnel to mitigate the risk
• Step 3: Develop control policies and procedures that target the noted risk
• Step 4: Monitor the implemented policies and procedures
Step 1 – Identify Risks

• Each PHA is unique and will have different risk factors
• Key differences between PHAs can include the following:
  – Type of programs administered by the PHA
  – The size and complexity of the programs
  – The use of in-house accounting or a fee accountant
  – The experience of employees
  – Use of third party management agents
  – The skill level and use of board members

Each PHA should develop policies based on their individual needs. Do not simply copy a policy just to have it.
Step 1 – Identify Risks (continued)

- Identification of risks should not just be related to financial controls. Risks can be identified for additional areas including the following:

<table>
<thead>
<tr>
<th>PHA Level Compliance</th>
<th>Program Level Compliance</th>
<th>Organizational Risk</th>
<th>Financial/ Budget Risk</th>
<th>Data</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Procurement procedures • Investment policy</td>
<td>• Tenant file documentation/ rent calculation</td>
<td>• Director of Finance to retire</td>
<td>• Funding concerns or excessive HAP costs</td>
<td>• Tenant SSN • Bank account information</td>
</tr>
</tbody>
</table>
Examples of Risk Factors

- The table provides examples of specific risk factors and how they can be categorized

<table>
<thead>
<tr>
<th>Noted Risk</th>
<th>General PHA</th>
<th>Low Rent Program</th>
<th>HCV Program</th>
</tr>
</thead>
<tbody>
<tr>
<td>PHA not following Open Meeting Act</td>
<td>●</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SEMAP not supported by documentation</td>
<td></td>
<td>●</td>
<td></td>
</tr>
<tr>
<td>Improper use of vehicles</td>
<td>●</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Utility allowance amounts not current</td>
<td></td>
<td>●</td>
<td>●</td>
</tr>
<tr>
<td>CFP funds not obligated in a timely manner</td>
<td></td>
<td></td>
<td>●</td>
</tr>
<tr>
<td>Cost allocation plan not supported</td>
<td>●</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Operating budgets not utilized</td>
<td>●</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Step 2 – Identify Resources / Personnel

• **Resources can include the following:**
  – Personnel at the PHA
  – Board members
  – Information/technology (software system)
  – Fee accountant
  – Neighboring PHAs
  – Use of contractors

• **A cost/benefit analysis should be conducted prior to implementing a change in control**
  – For example, a very small PHA may not have sufficient funding to hire an additional employee to prevent a segregation of duties audit finding
Step 3 – Develop Control Policies & Procedures

• Management has the task of designing and implementing controls in an effective and efficient manner to achieve an operational internal control system

• Management determines the control activities such as policies, procedures, and techniques that are used to achieve the entity’s goals and objectives
Control Activities

• Control activities consist of different types of actions. Control activities aid management in fulfilling responsibilities associated with an identified risk

• There are basically two (2) types of controls:
  – **Preventive Controls**: Controls designed to discourage errors or irregularities from occurring. These are proactive controls that help to ensure programmatic objectives are met
  – **Detective Controls**: Controls designed to find errors or irregularities after they have occurred
Control Examples

Examples of preventive and detective control activities include the following:

<table>
<thead>
<tr>
<th>Preventive Controls</th>
<th>Detective Controls</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Segregation of duties</td>
<td>• Review of performance, both financial and non-financial</td>
</tr>
<tr>
<td>• Review &amp; approvals</td>
<td>• Reconciliations</td>
</tr>
<tr>
<td>• Authorizations</td>
<td>• Annual inventory</td>
</tr>
<tr>
<td>• Verifications</td>
<td>• Audits/quality control</td>
</tr>
<tr>
<td>• Security of assets/security cameras</td>
<td>• Use of control totals</td>
</tr>
<tr>
<td>• Policies &amp; procedures</td>
<td>• Surprise reviews</td>
</tr>
<tr>
<td>• Education &amp; training</td>
<td></td>
</tr>
<tr>
<td>• Use of IT passwords</td>
<td></td>
</tr>
</tbody>
</table>
Documentation of Control Procedures

• Control procedures should be documented to provide evidence that the implemented control is achieving the objective

• For example, the Executive Director, can initial and date the monthly financial statements to indicate that the financial statements have been prepared timely and have been reviewed by senior management
Step 4 – Monitor Policies & Procedures

• Management should perform ongoing monitoring efforts to verify the effectiveness of the designed controls

• The monitoring efforts may include the review of automated tools, use of quality control reviews, external auditors, review of financials comparing actual results to budgets and the previous year’s actuals

• Monitoring efforts can also be required at the program and project level
Internal Control System Limitations

- **Management Override** - Managers may purposefully go outside established practices for illegitimate reasons
- **Breakdowns** - People with control responsibilities may not carry them out effectively or efficiently
- **Cost vs. Benefit** - Resources are limited. Managers properly accept a degree of risk when the cost of controlling the risk exceeds the benefit
- **Inadequate Segregation of Duties** - Systems in place may not adequately separate the responsibility for physical custody of an asset from the record keeping
- **Lack of Knowledge of Policies and Procedures** - Having a system of internal controls is not sufficient if all personnel are not knowledgeable of the proper policies and procedures
Module 5

EXAMPLES OF INDIVIDUAL FINANCIAL POLICIES AND PROCEDURES
Financial Policies and Procedures

• Financial policies and procedures direct how a housing authority will use and manage its money
• The documents establish financial controls within the housing authority that ensure accuracy, timeliness, and completeness of financial data
  – Helps bring order and cohesiveness to the housing authority (everyone knows what is expected)
  – Prevents or reduces fraud and theft within the housing authority
  – Provides for a system of checks and balances
  – Keeps financial and management information organized
  – Helps the housing authority reduce errors
• There is no one universal set of financial policies and procedures
  – While there is a common set of topics that need to be addressed, each housing authority needs to tailor the policy and procedures to their organization
  – Most housing authorities should have between 20 to 30 financial policies, depending on how the policies are grouped
## Financial Policies and Procedures (continued)

<table>
<thead>
<tr>
<th>Example Policies</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Bank Reconciliation</td>
</tr>
<tr>
<td>• Investment</td>
</tr>
<tr>
<td>• Credit Card</td>
</tr>
<tr>
<td>• Cost Allocation</td>
</tr>
<tr>
<td>• Disposition</td>
</tr>
<tr>
<td>• Accounts Payable</td>
</tr>
<tr>
<td>• Board Reporting</td>
</tr>
</tbody>
</table>
Policy Development

- Example policies are made available to aid PHAs in developing specific policy types.
- In most cases, more than one sample policy is provided to account for PHAs size and circumstances. *Example: Maintenance Inventory Policy*

<table>
<thead>
<tr>
<th>Sample</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sample 1</td>
<td>Small PHA with a Manual System. The sample provides an example maintenance</td>
</tr>
<tr>
<td></td>
<td>policy for a small PHA that does not track inventory using a software system.</td>
</tr>
<tr>
<td>Sample 2</td>
<td>Large PHA with a Manual System. The sample provides an example maintenance</td>
</tr>
<tr>
<td></td>
<td>inventory policy for a large PHA that does not track inventory using a software</td>
</tr>
<tr>
<td></td>
<td>system.</td>
</tr>
<tr>
<td>Sample 3</td>
<td>Large PHA with a Software System. The sample provides an example maintenance</td>
</tr>
<tr>
<td></td>
<td>policy for a large PHA with a software system that tracks maintenance</td>
</tr>
<tr>
<td></td>
<td>inventory in real time.</td>
</tr>
</tbody>
</table>
Key PHA Differences in Policy Development

• Key differences exist between PHAs that will play a significant role in the development of procedures
• Notable differences include the following:
  – PHA size
  – Use of software systems
  – Implementation of asset management
  – Use of a fee accountant
  – Cost allocation models
# Example 1. Bank Reconciliation Policy

## Key Components

| Risk Factors | Late financial reporting; missing bank transactions in financial statements; lack of review |

## Scenarios

**Sample 1** - A PHA with a fee accountant

**Sample 2** – A PHA with in-house accounting

### Key Control Procedure Issues:
- Provides PHA a timeline for preparation of bank reconciliations
- Provides a process for reviewing reconciliations
- Prescribe software system to be used
### Example 1. Bank Reconciliation Policy (continued)

<table>
<thead>
<tr>
<th>Risks</th>
<th>Preventive Control</th>
<th>Detective Control</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Bank reconciliations are late.</td>
<td>• Provide a deadline. Bank accounts will be reconciled by the 15th of the following month.</td>
<td>• Have an audit conducted on an annual basis.</td>
</tr>
<tr>
<td>• Bank accounts are not reconciled to the G/L.</td>
<td>• The bank reconciliation must be signed and dated certifying the reconciliation matches the general ledger, and is free of discrepancies.</td>
<td>• Discuss with fee accountant any issues or concerns related to bank reconciliations.</td>
</tr>
<tr>
<td>• Bank reconciliations have questionable items listed.</td>
<td>• The Executive Director will also sign and date the bank reconciliation as approved.</td>
<td>• A Board Member will review the completed bank reconciliation</td>
</tr>
<tr>
<td>• Bank accounts are comingling funds between programs.</td>
<td>• Have an audit conducted on an annual basis.</td>
<td>• Bank reconciliations will be made available to the board members or finance committee members.</td>
</tr>
</tbody>
</table>
Example 2. Budgeting Policy

### Key Components

| Risk Factors | Lack of management input; budgets not prepared correctly; actuals to budgets not reviewed; budget overruns not monitored |

### Scenarios

**Sample 1** — A small PHA

**Sample 2** — A large PHA with multiple projects/programs and a COCC

**Key Control Procedure Issues:**
- Provides PHA a timeline for preparation of operating budgets
- Provides a process for monitoring of actual to budget results
- Provides a process for determining individual roles in the preparation of the budget
## Example 2. Budgeting Policy (continued)

<table>
<thead>
<tr>
<th>Risks</th>
<th>Preventive Control</th>
<th>Detective Control</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Small PHA</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Lack of management input, the finance officer or fee accountant drives the budget process.</td>
<td>• A budgeting policy requiring the Executive Director to have significant input into the preparation of the budget including assessing the financial condition and impact of the budget for all programs.</td>
<td>• Annual auditor will verify controls are followed.</td>
</tr>
<tr>
<td>• Budgets are not used as a forecasting tool to prevent funding shortages.</td>
<td>• The Board of Commissioners has established goals as noted in the budgeting policy.</td>
<td></td>
</tr>
<tr>
<td>• Budgets are prepared late.</td>
<td>• A timeline is included in the budgeting policy.</td>
<td></td>
</tr>
<tr>
<td>• Budgets are not used throughout the fiscal year.</td>
<td>• Budget to Actual financial statements are required to be part of the monthly board package.</td>
<td>• The budgeting policy requires the Executive Director to provide an explanation as to significant budget variances noted in the financial statements to the Board of Commissioners.</td>
</tr>
</tbody>
</table>
Example 2. Budgeting Policy (continued)

<table>
<thead>
<tr>
<th>Risks</th>
<th>Preventive Control</th>
<th>Detective Control</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Large PHA</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Lack of management/staff input, the finance officer or fee accountant drives the budget process.</td>
<td>• A budgeting policy requiring the project/program managers to have significant input in the preparation of the project/program budgets.</td>
<td>• Annual auditor will verify controls are followed.</td>
</tr>
<tr>
<td>• Budgets are not used as a forecasting tool to prevent funding shortages.</td>
<td>• The Executive Director/program managers have established goals as noted in the budgeting policy.</td>
<td></td>
</tr>
<tr>
<td>• Budgets are prepared late.</td>
<td>• A timeline is included in the budgeting policy.</td>
<td></td>
</tr>
<tr>
<td>• Budgets are not used throughout the fiscal year.</td>
<td>• Budget to Actual financial statements are required to be part of the monthly board package.</td>
<td>• The budgeting policy contains provision that requires an explanation to the Board of Commissioners of significant budget variances noted in the financial statements.</td>
</tr>
</tbody>
</table>
## Example 3. Board Reporting

### Key Components

| Risk Factors | Board members are not provided key information to fulfill its oversight responsibilities; Board package and minutes are not properly archived |

### Scenarios

**Sample 1** – Board Reporting would be the same for small and large PHAs and may only differ based on the programs that are administered by the PHA

**Key Control Procedure Issues:**
- Board should meet at regular intervals consistent with state law. Best practice is monthly
- Provides a list and schedule of required reports and information to be included in the board packet
- A monthly financial statement, including budget to actuals, and monitoring reports should be part of the Board packet
### Example 3. Board Reporting (continued)

#### Risks

- Board is not fulfilling oversight role.
- Board is not provided with timely reports and information needed to properly fulfill its oversight and monitoring duties.
- Board meeting agenda is not included in the Board Package resulting in the Board to delay action or approvals.
- PHA is not maintaining accurate minutes of Board meetings and not archiving the Board package and minutes.

#### Preventive Control

- Establish a schedule of Board meetings that is compliant with state bylaws.
- Monthly financial statements, other monitoring reports and information should be prepared by the agency. The Executive Director will review the package to make sure all required reports and information are contained in the Board package.
- Executive Director will ensure that the Board package is provided to all Board members at the scheduled time.
- Executive Director will review the board meeting minutes and ensure that the Board package and minutes are archived.

#### Detective Control

- Annual auditor will review a sample of Board meeting materials and meeting minutes against the PHA policy and procedures for board reporting.
Development of Financial Management Policies

• Developing Financial Management Policies can be a lengthy process, but will provide long-term benefits to the PHA
• Steps in developing a Financial Management Policy
  1. Develop a reasonable schedule to fully develop the policy
  2. Identify risk factors related to the PHA and start with the highest risk factors
  3. Determine the policy and procedures content. Meet with key staff and board members to allow discussion
  4. Communicate policy and procedures to employees. Provide training on the policy
  5. Update and revise the procedures when needed. In many cases, certain procedures may not achieve the objective sought at first. The policy may need to be altered from time to time
  6. USE THE POLICY!!!!
Module 5

INTERNAL CONTROLS:
OTHER ITEMS TO CONSIDER
Use of a Fee Accountant

• Smaller PHAs will often use a fee accountant to provide accounting services to the PHA. Typical fee accounting services include the following:
  – Maintaining accounting records including producing financial statements, general ledgers
  – Processing and submitting the FDS
  – Reconciling bank accounts
  – Preparing operating budgets
Use of a Fee Accountant (continued)

• There are inherent limitations with using a fee accountant that may result in accounting errors or untimely financial statements
  – Fee accountants do not typically review invoices for ineligible costs. In many cases, the fee accountants do not receive copies of the invoices
  – Fee accountants are not responsible for drawing down HUD funds or filing CFP reports
  – Fee accountants are not looking for fraud
  – Fee accountants typically do not discuss financial concerns with the Board of Commissioners
Establish an Annual Management Plan

• As with many government entities, requirements for report filing, training, audit scheduling, and major compliance reviews can be daunting.

• An annual management plan provides a strategic approach for tracking major scheduled items throughout the year.

• The plan can easily be added to and separated by program or departments.
  – Through proper scheduling, many activities can be accomplished throughout the year to prevent bottlenecks of multiple tasks that must be completed.

• The plan can be provided to the Board of Commissioners for monitoring purposes.
## Abbreviated Management Plan Example

<table>
<thead>
<tr>
<th>Month</th>
<th>Finance</th>
<th>HCV Program</th>
<th>Low Rent Program</th>
<th>Executive Management</th>
<th>Maintenance</th>
</tr>
</thead>
<tbody>
<tr>
<td>January</td>
<td>• Submission of W-2 &amp; 1099 forms</td>
<td>• Verify VMS amounts for previous year</td>
<td></td>
<td></td>
<td>• Annual count of maintenance inventory</td>
</tr>
<tr>
<td>February</td>
<td>• Submission of unaudited FDS</td>
<td>• SEMAP submission</td>
<td></td>
<td></td>
<td>• Solicit lawn-care contract proposals</td>
</tr>
<tr>
<td>March</td>
<td></td>
<td></td>
<td></td>
<td>• State training session</td>
<td></td>
</tr>
<tr>
<td>April</td>
<td>• Submission of IRS 990 form for component unit</td>
<td>• Project Manager budget training</td>
<td></td>
<td>• Review of quarterly financial reports with finance committee</td>
<td></td>
</tr>
<tr>
<td>May</td>
<td></td>
<td>• Utility allowance study</td>
<td>• Utility allowance study</td>
<td></td>
<td>• Preventive maintenance, HVAC units</td>
</tr>
<tr>
<td>June</td>
<td>• Start of operating budget process</td>
<td></td>
<td></td>
<td></td>
<td>• Review of CFP program activity</td>
</tr>
</tbody>
</table>
This Ends the Training Module on Effective Internal Controls
Public Housing Authority Financial Management Training

Learning Activity 3 & 4: Effective Internal Controls
Learning Activity 3 & 4: Effective Internal Controls - Background

• Continuing your role as a new Board commissioner for the Anywhere Housing Authority, you think that internal controls are outdated or nonexistent. As such, the operations of the PHA could be compromised, especially at East Farm Road Apartments.

• You are looking to improve the PHA by helping to perform a risk assessment of East Farm Road Apartments with other Board members, and reviewing and developing some key policies.
Learning Activity 3 & 4: Effective Internal Controls – Instructions

• Question 1 of Learning Activity 3 assumes that you have completed Learning Activity 1 and 2, which introduce the Anywhere Housing Authority and East Farm Roads Apartments and provides financial statements and basic performance metrics
  – If you have not yet completed Learning Activity 1 and 2, it is suggested that you complete them prior to starting this learning activity
  – If it has been a while since you completed Learning Activity 1 and 2 or you do not have time to complete Learning Activity 1 and 2, please review the two learning activities before proceeding with this learning activity
    • Learning Activity 1 can be found in the Resources Section of the training web page
    • Learning Activity 2 can be found in the Resources Section of the training web page
  – Only question 1 of Learning Activity 3 is dependent on the prior completion / knowledge of Learning Activity 1 and 2
Learning Activity 3 & 4: Effective Internal Controls – Instructions (continued)

• When you are ready to complete the learning activities, download and print – Learning Activity 3 & 4: Effective Internal Controls

• These learning activities are designed to assist you in the process of establishing an internal control system for a PHA

• There are two learning activities presented in this module:
  – Learning Activity 3 starts on page 2 of the document
  – Learning Activity 4 starts on page 6 of the document
Learning Activity 3: Effective Internal Controls – Questions 1 and 2

• **Question 1:**
  – Risk Assessment – Based on the initial review of East Farm Road’s operations, identify high risk areas that you believe need to be addressed at East Farm Road Apartments

• **Question 2:**
  – Key Control Procedures – As part of the risk assessment noted in Question 1, three high risk items have been identified as follows:
    • Credit Card Policy
    • Maintenance Inventory Policy
    • Disposition of Equipment Policy
  – Your task is to list key control procedures that should be included in each policy
    • As an example, a key control procedure for a credit card policy would be to establish a spending limit
Learning Activity 3: Effective Internal Controls – Question 3

• **Question 3:**
  – Policy Development – The items noted in Question 2 are now finalized in the actual policy, in this case the credit card policy
  – Your task is to complete the blank fields in the credit card policy starting on page 4
Learning Activity 4: Effective Internal Controls

• Learning Activity #4
  – Policy Review and Development – The Executive Director has submitted the following two policies to the board for approval:
    • Policy 1 – Purchase and Use of PHA Vehicles
    • Policy 2 – Financial Control and Analysis Policy
  – Review the two policies and list any questions, comments, or concerns that you have for each policy

• When you are finished answering the questions, return to the video for the answers and explanations
End of Learning Activity 3 & 4

This Ends Learning Activity 3 & 4:
Effective Internal Controls
Public Housing Authority Financial Management Training

Learning Activity 3 & 4:
Solutions to Effective Internal Controls
Goal of Learning Activity 3 & 4

• The goal of these learning activities is to demonstrate the process for developing an internal control system from assessing risk items, to making a list of key components associated with a policy, to the development of a policy

• Learning Activity #3 illustrates a methodology for developing internal controls that would be in compliance with OMB requirements

• Learning activity #4 is intended to increase your skill in reviewing the existing policies of a PHA
General Solution

• The solutions provided in the next slides can also be found on pages 10 through 15 of the learning activity document

• The answers presented are not the only answers to this exercise. Different responses by other participants were common
  – There were items that some participants thought were risk items and other participants did not, and
  – There were differences in opinion on the items to include in the different policies
Solution to Learning Activity 3

Question 1

Question 1: As a Board member that has an understanding of the control environment, identify the risk items associated with East Farm Road Apartments and list them in the table below.

<table>
<thead>
<tr>
<th>#</th>
<th>Areas of Risk / Concern</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Unauthorized Maintenance Purchases and Improper Use of Maintenance Inventory</td>
</tr>
<tr>
<td>2</td>
<td>Improper Use of Credit Cards</td>
</tr>
<tr>
<td>3</td>
<td>Lack of Safeguarding of Tools and Equipment</td>
</tr>
<tr>
<td>4</td>
<td>Payment of Rent in Cash and Use of Manual Receipts</td>
</tr>
<tr>
<td>5</td>
<td>High Purchase Authorization Limits</td>
</tr>
<tr>
<td>6</td>
<td>Vacant Units Are Not Turned in an Acceptable Timeframe</td>
</tr>
<tr>
<td>7</td>
<td>Equipment and Other Material May Be Disposed of Improperly</td>
</tr>
<tr>
<td>8</td>
<td>Financial Monitoring Not Properly Conducted</td>
</tr>
<tr>
<td>9</td>
<td>Improper or Lack of a Budget Policy</td>
</tr>
<tr>
<td>10</td>
<td>Inadequate Oversight of East Farm Road Apartments</td>
</tr>
</tbody>
</table>
Question 2a: Develop key control procedures that should be addressed and included in the **Credit Card policy**.

<table>
<thead>
<tr>
<th>#</th>
<th>Items to Address</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Authorized Users of Credit Card</td>
</tr>
<tr>
<td>2</td>
<td>Permitted use of Credit Cards, including Disciplinary Action</td>
</tr>
<tr>
<td>3</td>
<td>Credit Card Limit</td>
</tr>
<tr>
<td>4</td>
<td>Limitations on Type of Credit Cards (prohibition on points / incentives / annual fees)</td>
</tr>
<tr>
<td>5</td>
<td>Documentation of Purchases / Return of Goods and Purchases</td>
</tr>
<tr>
<td>6</td>
<td>Reconciliation of Purchased Items to Purchase Orders</td>
</tr>
<tr>
<td>7</td>
<td>Notification of Lost or Stolen Credit Card</td>
</tr>
</tbody>
</table>
Solution to Learning Activity 3
Question 2b

Question 2b: Develop key control procedures that should be addressed and included in the Maintenance Inventory policy.

<table>
<thead>
<tr>
<th>#</th>
<th>Items to Address</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Level / Quantity of Inventory On-hand</td>
</tr>
<tr>
<td>2</td>
<td>Approval of Purchases</td>
</tr>
<tr>
<td>3</td>
<td>Security of Inventory</td>
</tr>
<tr>
<td>4</td>
<td>List of Materials Used in Work Orders</td>
</tr>
<tr>
<td>5</td>
<td>Monitoring and Inspection of Inventory</td>
</tr>
<tr>
<td>6</td>
<td>Annual Inventory Count</td>
</tr>
<tr>
<td>7</td>
<td>Accounting for Materials and Year-end Closing</td>
</tr>
</tbody>
</table>
Solution to Learning Activity 3

Question 2c

Question 2c: Develop key control procedures that should be addressed and included in the Disposition of Equipment policy.

<table>
<thead>
<tr>
<th>#</th>
<th>Items to Address</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Authorization / Approval to Dispose</td>
</tr>
<tr>
<td>2</td>
<td>Listing / Documentation of Items to be Disposed</td>
</tr>
<tr>
<td>3</td>
<td>Disposal Methods (formal advertising, auction style, etc.)</td>
</tr>
<tr>
<td>4</td>
<td>Disposal of Hazardous Materials</td>
</tr>
<tr>
<td>5</td>
<td>Disposition/Disposal if There Is No Buyer</td>
</tr>
<tr>
<td>6</td>
<td>Use of Disposal Income (i.e., program income)</td>
</tr>
<tr>
<td>7</td>
<td>Prohibition of Sale / Disposal to PHA staff (conflict of interest)</td>
</tr>
<tr>
<td>8</td>
<td>Documentation of Sale and Update of Accounting Records</td>
</tr>
</tbody>
</table>
Solution to Learning Activity 3

Question 3

Question 3: Create the policy / procedures for AHA for those items that are blank:

Credit Card Policy

The Authority will have use of credit cards to purchase limited materials, supplies, and services. This will modernize and streamline purchases. Credit cards will be used only for the registration and pre-approved travel expenses related to conferences and/or workshops, and prepayments required by vendors where no other form of payment is accepted. Personal use of the credit card is strictly prohibited.

The Authority will establish a corporate credit card with an overall limit of $8,000. Each card issued will have an individual limit of $1,500 for the property managers and $5,000 for the Executive Director. The employee is solely responsible for all business-related charges made to the credit card.
Credit Card Procedures

**Authorized Credit Card Holder:** The administrator of the credit cards will be the Executive Director. Qualified employees will be required to complete a Credit Card Application Form. The form provides a list of requirements accepted by the employee as well as provide an understanding of disallowed activities and costs. Credit cards will be issued to the following positions:

- Executive Director
- Property Managers

Authority credit cards may not be used for the following purchases:

- Office equipment
- Maintenance tools and equipment over $250
- Personal items of any kind
Solution to Learning Activity 4

Policy 1

Question: Concerns / Recommendations to Purchase and Use of PHA Vehicle Policy:

Answer:

Needed Changes to the Policy

1. Use of vehicle for commuting is a taxable event
2. Need for mileage log
3. Personal use of vehicle is prohibited
4. Vehicle must operated in a safe and reasonable manner
5. Authorized drivers
6. Reporting of Accidents

Additional Items to Consider

1. Security of vehicles
Solution to Learning Activity 4
Policy 2

Question: Concerns / Recommendations to Financial Control and Analysis Policy:

Answer:
Overall the policy is too vague and general

Needed Changes to the Policy
1. Frequency of review and timing of financial statements
2. Requirement for an audit and not a review to be performed

Additional Items to Consider
1. Fee accountant to attend a board meeting or communicate with Board once a year
2. Chairman of the board to attend auditor exit conference
End of Learning Activities 3 & 4 Solutions

This Ends the Solutions to Learning Activities 3 & 4:
Effective Internal Controls