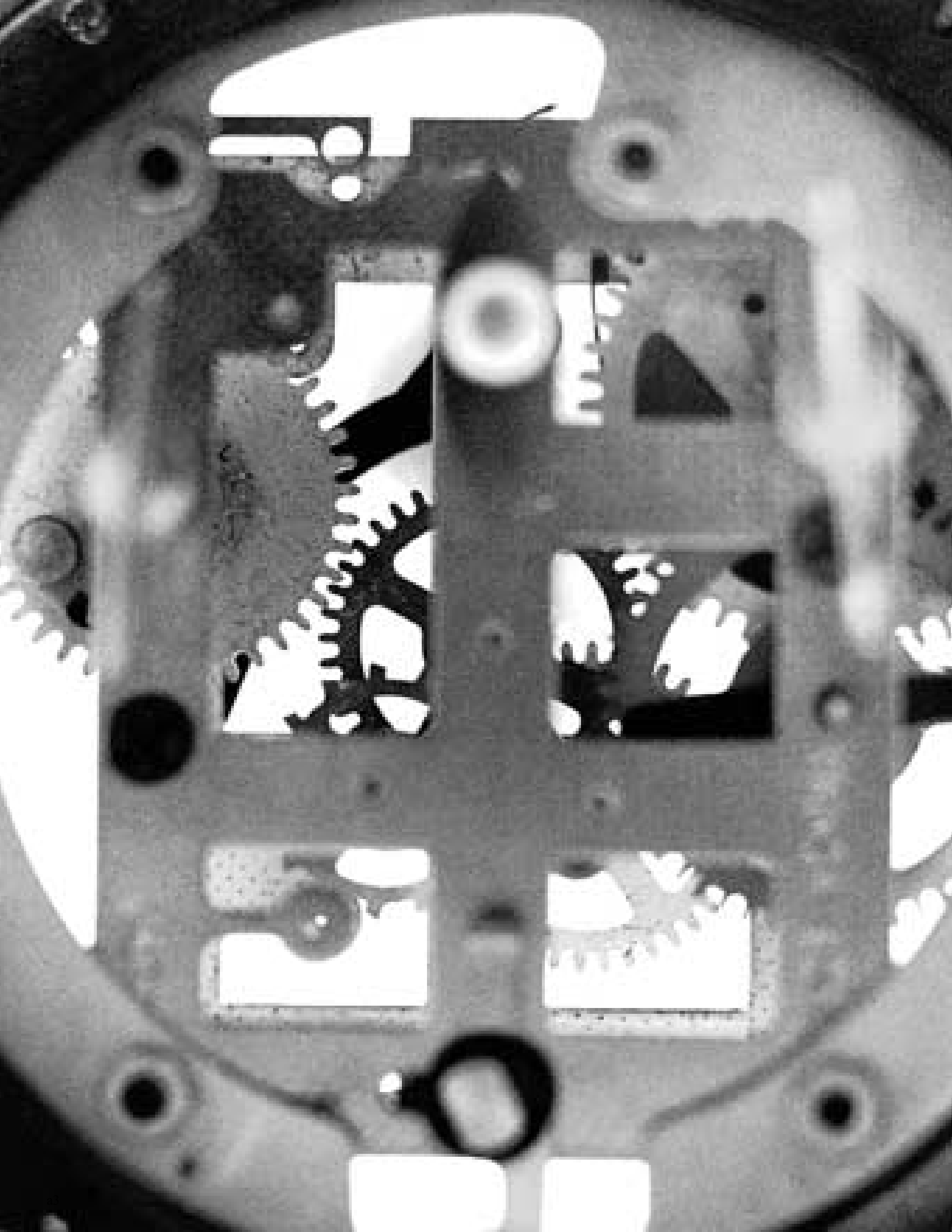


 **ERNST & YOUNG**
Quality In Everything We Do

Evaluating Internal Controls

Considerations for Evaluating Internal Control
at the Entity Level





To Our Clients and Other Friends

The Sarbanes-Oxley Act of 2002 (the Act) makes reporting on internal controls mandatory for SEC registrants and their independent auditors. Section 404 of the Act directs the SEC to adopt rules requiring annual reports of public companies to include an assessment, as of the end of the fiscal year, of the effectiveness of internal controls and procedures for financial reporting. Section 404 also requires the company's independent auditors to attest to and report on management's assessment. The SEC issued its proposed rules in late October 2002. The SEC rule proposal, if adopted, would apply to companies whose fiscal years end on or after September 15, 2003. Therefore, companies should be getting ready now for the comprehensive documentation and evaluation of internal control that will be needed to support management's assessment and the auditors' attestation report. Our publication, *Preparing for Internal Control Reporting—A Guide for Management's Assessment under Section 404 of the Sarbanes-Oxley Act* (the Guide) (Ernst & Young SCORE Retrieval File No. EE0677), provides a methodology and framework for completing the evaluation.

The methodology outlined in the Guide includes five phases:

- ▶ Understand the Definition of Internal Control
- ▶ Organize a Project Team to Conduct the Evaluation
- ▶ Evaluate Internal Control at the Entity Level
- ▶ Understand and Evaluate Internal Control at the Process, Transaction, or Application Level
- ▶ Evaluate Overall Effectiveness, Identify Matters for Improvement, and Establish Monitoring System

Additional guidance on the first two phases of the methodology is provided in the Guide. We will be providing more information about the detailed documentation and evaluation—the last two phases—in future publications. This document is a tool to assist management in performing the third phase: evaluating internal control at the entity level.

A logical place to begin any comprehensive evaluation of internal controls is at the top—entity-level controls that might have a pervasive effect on the organization. This includes a consideration of factors in each of the five components of internal control that can have a pervasive effect on the risk of errors or fraud. These five interrelated components are:

- ▶ Control Environment
- ▶ Risk Assessment
- ▶ Information and Communication
- ▶ Control Activities
- ▶ Monitoring

Documenting and evaluating internal control at the entity level does not by itself provide a complete perspective of internal control of an entity. However, it is an important

starting point because the assessment of entity-level controls—particularly when weaknesses are identified—can have a significant effect on the overall assessment of the effectiveness of internal controls and procedures for financial reporting.

To help management evaluate internal control at the entity level, we have provided in this document numerous points to consider for each of the five components of internal control. These points are not all-inclusive, and not all the points listed herein will apply to every company. Internal and external factors unique to a particular entity may result in companies developing unique control mechanisms, and these unique factors and control mechanisms may give rise to additional points to consider. While a “no” response to an individual point does not necessarily mean that the entire component of internal control at the entity level is ineffective, a “no” response (particularly when there are several “no” responses) should heighten awareness to potential weaknesses in internal control and indicate areas where management should focus attention.

Management of many companies will prepare a single evaluation of the organization’s internal control at the entity level. In other situations, such as larger companies

with multiple locations or lines of business that operate on a decentralized basis, it may be appropriate to perform a separate evaluation of the entity level controls for the individual locations or business lines and use the results in making an overall assessment at the entity level.

Ernst & Young has developed the Guide and this supplemental publication based on our extensive knowledge of and experience with evaluating internal controls over financial reporting. These publications cannot consider all possible questions related to an assessment of a company’s internal control, but they provide a useful methodology and framework to assist management in its evaluation. We would be pleased to discuss the evaluation of internal control in your company. We also have the knowledge and experience to assist you in documenting internal controls.

An electronic copy of this document is available to clients, free of charge, on Ernst & Young Online. To obtain a private password to Ernst & Young Online, or to simply request an electronic copy of this document, contact your Ernst & Young engagement team or local Ernst & Young representative.

Ernst & Young LLP

Control Environment

The control environment reflects the tone set by top management and the overall attitude, awareness and actions of the board of directors, management, owners, and others concerning the importance of internal control and the emphasis placed on control in the company's policies, procedures, methods, and organizational structure. It is the foundation for all other components of internal control, providing discipline and structure.

Points to Consider	Responses/Comments	
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Integrity, ethical values, and behavior of key executives

- | | | | |
|---|------------------------------|-----------------------------|-----------|
| ▶ Does the board of directors show concern for integrity and ethical values? Is there a code of conduct and/or ethics policy and has it been adequately communicated? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Is management's commitment to integrity and ethical behavior communicated effectively throughout the company, both in words and deeds? Does management lead by example? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Are those in top management hired from outside made familiar with the importance of high ethics and controls? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Does management act to remove or reduce incentives or temptations that might prompt personnel to engage in dishonest, illegal, or unethical acts? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Do rewards, such as bonuses and stock ownership, foster an appropriate ethical tone (i.e., not given to those who meet objectives but, in the process, circumvent established policies, procedures, or controls)? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Does management take appropriate disciplinary action in response to departures from approved policies and procedures or violations of the code of conduct? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |

Management's control consciousness and operating style

- | | | | |
|---|------------------------------|-----------------------------|-----------|
| ▶ Is the management structure appropriate (i.e., not dominated by one or a few individuals) and is there effective oversight by the board of directors or audit committee? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Does management's financial reporting philosophy, including its attitude toward the development of estimates, tend to be conservative? Are biases that may affect significant accounting estimates and other judgments minimized? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |

Points to Consider	Responses/Comments		
▶ Is there a mechanism in place to regularly educate and communicate to management and employees the importance of internal controls, and to raise their level of understanding of controls?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Does management give appropriate attention to internal control, including the effects of information systems processing?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Does management correct identified internal control deficiencies on a timely basis?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Are management incentives balanced (i.e., the portion of management compensation derived from bonuses, stock options, or other incentives does not promote an excessive level of interest in maintaining or increasing the entity's stock price or earnings trend)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Does management set realistic (i.e., not unduly aggressive) financial targets and expectations for operating personnel?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<i>Management's commitment to competence</i>			
▶ Do personnel appear to have the competence and training necessary for their assigned level of responsibility or the nature and complexity of the entity's business?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Does management possess broad functional experience (i.e., management comes from several functional areas rather than from just a few, such as production and sales)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is departmental staffing appropriate (particularly with regard to knowledge and experience of management and supervisory levels within the accounting, information systems, and financial reporting areas)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Does management show a willingness to consult with the auditors on and address significant matters relating to internal control and accounting issues?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Does management demonstrate a commitment to provide sufficient accounting and financial personnel to keep pace with the growth and/or complexity of the business?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:



Points to Consider	Responses/Comments
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Board of directors' and/or audit committee participation in governance and oversight

- ▶ Is the makeup of the board of directors, including the number of directors and their background and expertise, appropriate given the nature of the company? Has the independence of outside board members been adequately reviewed, including affiliations and relationships and transactions with the company? Yes No Comments:
- ▶ Is the board of directors and audit committee independent from management, such that necessary, and often probing, questions are raised? Yes No Comments:
- ▶ Does the board of directors and/or audit committee give adequate consideration to understanding management's processes for monitoring business risks affecting the organization? Yes No Comments:
- ▶ Does the audit committee represent an informed, vigilant, and effective overseer of the financial reporting process and the company's internal control, including information systems processing and related computer controls? Yes No Comments:
- ▶ Does the audit committee include at least one "financial expert"? Yes No Comments:
- ▶ Does the audit committee adequately maintain a direct line of communication with the entity's external and internal auditors? Yes No Comments:
- ▶ Does the audit committee have a charter outlining its duties and responsibilities? Does the audit committee have adequate resources and authority to discharge its responsibilities? Yes No Comments:

Organizational structure and assignment of authority and responsibility

- ▶ Is the organizational structure adequate for the size, operating activities, and locations of the company? Yes No Comments:
- ▶ Is the overall organizational structure appropriate (i.e., not overly complex and not involving numerous or unusual legal entities, managerial lines of authority, or contractual agreements without apparent business purpose)? Yes No Comments:

Points to Consider	Responses/Comments		
▶ Is there an appropriate structure for assigning ownership of data, including who is authorized to initiate and/or change transactions? Is ownership assigned for each application and database within the IT infrastructure?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Are there appropriate policies for such matters as accepting new business, conflicts of interest, and security practices? Are they adequately communicated throughout the organization?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Are there adequate policies and procedures for authorization and approval of transactions at the appropriate level?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is assignment of responsibilities clear, including responsibilities for information system processing and program development?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Does management review and make modifications to the organizational structure of the company in light of changed conditions?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is there adequate supervision and monitoring of decentralized operations (including accounting personnel and information systems)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is there an appropriate segregation of incompatible activities (i.e., separation of accounting for and access to assets)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<i>Human resource policies and practices</i>			
▶ Are there standards and procedures for hiring, training, motivating, evaluating, promoting, compensating, transferring, and terminating personnel that are applicable to all functional areas (e.g., accounting, marketing, information systems)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Are there screening procedures for job applicants, particularly for employees with access to assets susceptible to misappropriation?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Are policies and procedures clear and are they issued, updated, and revised on a timely basis? Are they effectively communicated to personnel at decentralized and/or foreign locations?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Are there written job descriptions, reference manuals or other forms of communication to inform personnel of their duties?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is job performance periodically evaluated and reviewed with each employee?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:



Evaluation of Control Environment:

Effective

Ineffective

Summarize the reasons supporting the evaluation, unless obvious:

Risk Assessment

Risk assessment is the entity's identification and analysis of relevant risks (both internal and external) to the achievement of its objectives, forming a basis for determining how the risks should be managed.

Points to Consider			Responses/Comments
<p><i>Entity-level objectives, including how they are supported by strategic plans and complemented on a process/application level, have been established and communicated. A risk assessment process, including estimating the significance of risks, assessing the likelihood of their occurrence, and determining needed actions, has been established.</i></p>			
<p>▶ Are business objectives established, communicated, and monitored? Are the key elements of the entity's strategic plan communicated throughout the entity so all employees have a basic understanding of the company's overall strategy? Do the entity's strategic plan and its business objectives complement each other?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Is a process in place to periodically review and update entity-wide strategic plans? Is the strategic plan reviewed and approved by the entity's board of directors?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Does the entity-wide strategic plan include IT or is there a separate IT strategic plan that addresses the technology needs of the entity to effectively and efficiently meet its strategic plan?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Is there an adequate mechanism for identifying business risks, including those resulting from:</p>			
<p>— Entering new markets or lines of business?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>— Offering new products and services?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>— Privacy and data protection compliance requirements?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>— Other changes in the business, economic, and regulatory environment?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:



Points to Consider	Responses/Comments		
<ul style="list-style-type: none"> ▶ Does internal audit (or another group within the company) perform a periodic (at least annual) risk assessment? If yes, does senior management review the risk assessment and consider actions to mitigate the significant risks identified? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<ul style="list-style-type: none"> ▶ Does management consider how much risk it is willing to accept when setting strategic direction or entering new markets, and does it strive to maintain risk within those levels? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<ul style="list-style-type: none"> ▶ Does the board of directors and/or the audit committee oversee and monitor the risk assessment process and take action to address the significant risks identified? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p><i>Mechanisms are in place to anticipate, identify, and react to changes that may have a dramatic and pervasive effect on the entity (e.g., asset/liability management committee in a financial institution, commodities trading risk management group in a manufacturing entity) or that may affect achievement of entity or process/application-level objectives.</i></p>			
<ul style="list-style-type: none"> ▶ Are acquisitions and divestitures of significant businesses and assets well controlled (e.g., finalized after the completion of due diligence procedures, reviewed by an appropriate level of management)? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<ul style="list-style-type: none"> ▶ Are there groups or individuals who are responsible for anticipating or identifying changes with possible significant effects on the entity? Are there processes in place to inform appropriate levels of management about changes with possible significant effects on the entity? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<ul style="list-style-type: none"> ▶ Are budgets/forecasts updated during the year to reflect changing conditions? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<ul style="list-style-type: none"> ▶ Are periodic reviews performed or other processes in place to, among other things, anticipate and identify routine events or activities that may affect the entity's ability to achieve its objectives and address them? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<ul style="list-style-type: none"> ▶ Does management report to the board of directors and/or the audit committee on changes that may have a significant effect on the entity? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:

Points to Consider	Responses/Comments		
<p><i>The accounting department has established processes to (1) identify significant changes in generally accepted accounting principles (GAAP) promulgated by relevant authoritative bodies, (2) notify the accounting department of changes in the entity's business practices that may affect the method or the process of recording transactions, and (3) identify significant changes in internal control or the operating environment, including changes as a result of new or changing regulations.</i></p>			
<p>▶ Does the accounting department have a process in place to identify and address changes in GAAP, as well as for approving changes in accounting made to address such changes?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Does management work with the company's independent auditors or other third party experts to determine if they are addressing complex changes in GAAP appropriately?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Does the board of directors and/or the audit committee review and approve significant changes in the entity's accounting practices?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Are there processes to ensure the accounting department is made aware of changes in the operating environment so they can review the changes and determine what, if any, effect the change may have on the entity's accounting practices?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Are there channels of communication between the accounting department and/or individual(s) in charge of monitoring regulatory rules so the accounting department is aware of regulatory changes that could affect the entity's accounting practices?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Are there processes to ensure the accounting department (and board of directors and/or audit committee) is aware of significant transactions with related parties so they can determine whether such transactions are appropriately accounted for and disclosed?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:



Evaluation of Risk Assessment:

Effective

Ineffective

Summarize the reasons supporting the evaluation, unless obvious:

Information and Communication

Information and communication systems support the identification, capture, and exchange of information in a form and time frame that enable management and other appropriate personnel people to carry out their responsibilities.

Points to Consider	Responses/Comments		
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Information

Information systems provide management with necessary reports on the entity's performance relative to established objectives, including relevant external and internal information, and information is provided to the right people in sufficient detail and on time to enable them to carry out their responsibilities efficiently and effectively.

- ▶ Is the entity able to prepare accurate and timely financial reports, including interim reports? Yes No Comments:

- ▶ Does the board of directors and management receive sufficient and timely information to allow them to fulfill their responsibilities? Yes No Comments:

- ▶ Are management's objectives in terms of budget, profit, and other financial and operating goals defined and measurable? Are actual results measured against these objectives? Yes No Comments:

- ▶ Is there a high level of user satisfaction with information systems processing, including reliability and timeliness of reports? Yes No Comments:

- ▶ Is there a sufficient level of coordination between the accounting and information systems processing functions/departments? Yes No Comments:

Information systems are developed or revised based on a strategic plan that is interrelated with the entity's overall business strategy, and is responsive to achieving the entity-level and process/application level objectives.

- ▶ Are there appropriate policies for developing and modifying accounting systems and controls (including changes to and use of computer programs and/or data files)? Yes No Comments:



Points to Consider	Responses/Comments		
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<ul style="list-style-type: none"> ▶ Are management’s efforts to develop or revise information systems (including accounting systems) responsive to its strategic plans? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Are there significant applications or transactions that are executed /processed by service organizations? If yes, has management documented the relevant controls at the service organization, the company, or both that mitigate the risk of errors? Are there policies for periodic monitoring of controls either at the service organization or the company and taking appropriate action to mitigate potential new risks? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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Management commits the appropriate human and financial resources to develop the necessary information systems, and ensures and monitors users involvement in the development (including revisions) and testing of programs.

<ul style="list-style-type: none"> ▶ Is the board of directors or audit committee involved in monitoring information systems projects and resource priorities? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Does the IT organization chart clearly reflect areas of responsibility and lines of reporting and communication? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Are there defined responsibilities for individuals responsible for implementing, documenting, testing and approving changes to computer programs that are purchased or developed by information systems personnel or users? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Are systems conversions well controlled (e.g., completed pursuant to written procedures or plans)? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Does financial management ensure and monitor user involvement in the development of programs, including the design of internal control checks and balances? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Is there a high degree of cooperation and interaction between users and the IT department (e.g., procedures to ensure ongoing monitoring by the IT department of user satisfaction with IT processing and policies for the development, modification, and use of programs and data files)? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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Management has established a business continuity/disaster recovery plan for all primary data centers.

<ul style="list-style-type: none"> ▶ Are application programs and data files backed-up regularly? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Is there a current disaster recovery plan for the significant components of the IT infrastructure? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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Points to Consider	Responses/Comments		
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|---|------------------------------|-----------------------------|-----------|
| ▶ Is there a business continuity plan that incorporates the disaster recovery plan and end-user department needs for timely recovery of critical business functions, systems, processes and data? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Are the disaster recovery and business continuity plans tested periodically (at least annually)? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Are the disaster recovery and business continuity plans updated for changing conditions? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |

Communication

Management communicates employees' duties and control responsibilities in an effective manner, and has established communication channels for people to report suspected improprieties.

- | | | | |
|---|------------------------------|-----------------------------|-----------|
| ▶ Are the lines of authority and responsibility (including lines of reporting) within the company clearly defined and communicated? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Are there written job descriptions and reference manuals that describe the duties of personnel? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Are policies and procedures established for and communicated to personnel at decentralized locations (including foreign operations)? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Is there training/orientation for new employees, or employees when starting a new position, to discuss the nature and scope of their duties and responsibilities? Does such training/orientation include a discussion of specific internal controls they are responsible for? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Is there a process for employees to communicate improprieties? Is the process well communicated throughout the entity? Does the process allow for anonymity for individuals who report possible improprieties? Is there a process for reporting improprieties, and actions taken to address them, to senior management, the board of directors, or the audit committee? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Are all reported potential improprieties reviewed, investigated, and resolved in a timely manner? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |



Points to Consider	Responses/Comments		
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There is adequate communication across the organization to enable people to discharge their responsibilities effectively, and management takes timely and appropriate follow-up action on communications received from customers, vendors, regulators, or other external parties.

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|---|------------------------------|-----------------------------|-----------|
| <ul style="list-style-type: none"> ▶ Do employees believe they have adequate information to complete their job responsibilities? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| <ul style="list-style-type: none"> ▶ Is there a process to quickly disseminate critical information throughout the entity when necessary? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| <ul style="list-style-type: none"> ▶ Is there a process for tracking communications from customers, vendors, regulators, and other external parties? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| <ul style="list-style-type: none"> ▶ Is ownership assigned to a member of management to help ensure the entity responds appropriately, timely, and accurately to communications from customers, vendors, regulators, and other external parties? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |

Evaluation of Information and Communication:

Effective Ineffective

Summarize the reasons supporting the evaluation, unless obvious:

Control Activities

Control activities are the policies and procedures that help ensure that management's directives are carried out.

Points to Consider	Responses/Comments		
<p><i>Necessary policies and procedures exist with respect to each of the entity's activities, and controls called for by policy are being applied.</i></p>			
<p>▶ Are accounting and closing practices followed consistently at interim dates (e.g., quarterly, monthly) throughout the year?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Is there appropriate involvement by management in reviewing significant accounting estimates and support for significant unusual transactions and non-standard journal entries?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Is there timely and appropriate documentation for transactions?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Does the entity review its policies and procedures periodically to determine if they continue to be appropriate for the company's activities?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Do members of management have ownership of the policies and procedures? Does the ownership include ensuring the policies and procedures are appropriate for the company's activities?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p><i>Management has clear objectives in terms of budget, profit, and other financial and operating goals, and these objectives are clearly written, communicated throughout the entity, and are actively monitored. Planning and reporting systems are in place to identify variances from planned performance and communicate such variances to the appropriate level of management. The appropriate level of management investigates variances and takes appropriate and timely corrective actions.</i></p>			
<p>▶ Is there a budgetary system?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Does management review key performance indicators (e.g., budget, profit, financial goals, operating goals) regularly (e.g., monthly, quarterly) and identify significant variances? Does management then investigate the significant variances and is appropriate corrective action taken?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:



Points to Consider	Responses/Comments		
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<ul style="list-style-type: none"> ▶ Are variances in planned performance communicated and discussed with the board of directors and/or audit committee at least quarterly? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Are financial statements submitted to operating management? Are they accompanied by analytical comments? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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Duties are logically divided or segregated (whether manually or through appropriate set up of information technology (IT) applications) among different people to reduce the risk of fraud or inappropriate actions.

<ul style="list-style-type: none"> ▶ Is there an appropriate segregation of incompatible activities (e.g., separation of accounting for and access to assets, IT operations function separate from systems and programming, database administration function separate from application programming and systems programming)? Are organizational charts reviewed to ensure proper segregation of duties exist? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Are appropriate approvals from management required prior to allowing an individual access to specific applications and databases? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Are IT personnel prohibited from having incompatible responsibilities or duties in user departments? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Are there processes to periodically (e.g., quarterly, semi-annually) review system privileges and access controls to the different applications and databases within the IT infrastructure to determine if system privileges and access controls are appropriate? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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Periodic comparisons are made of amounts recorded in the accounting system with physical assets. Adequate safeguards are in place to prevent unauthorized access to or destruction of documents, records, and assets.

<ul style="list-style-type: none"> ▶ Has management established procedures to periodically reconcile physical assets (e.g., cash, receivables, inventories, property and equipment) with related accounting records? 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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<ul style="list-style-type: none"> ▶ Are physical inventories/cycle counts taken on a periodic basis and the perpetual inventory system adjusted accordingly? Are significant or recurring adjustments 	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
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Points to Consider	Responses/Comments		
investigated to determine the reason for the adjustment and are appropriate actions taken to address the reasons for the adjustments?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Has management established procedures to prevent unauthorized access to, or destruction of, documents, records (including computer programs and data files), and assets?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is data processing access to non-data processing assets restricted (e.g., blank checks)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p><i>Policies for controlling access to programs and data files have been established. Access security software, operating system software, and/or application software is used to control access to data programs. An information security function is in place and responsible for monitoring compliance with information security policies and procedures.</i></p>			
▶ Are access security software, operating systems software, and application software used to control both centralized and decentralized access to:			
— Data	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
— Functional capabilities of programs (e.g., execute, update, modify parameters, read only)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is physical security over information technology assets (both IT department and users) reasonable given the nature of the company's business?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is critical computer data backed up daily and stored off-site?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Are controls in place over dial-up access to the company's computer resources (e.g., firewalls; centralized directories to store and manage user identities and resource privileges; automated policy-based request, approval, and fulfillment process for enterprise access)?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
▶ Is there a dedicated security officer function that monitors IT processing activities and are there periodic reports to the board of directors and/or audit committee on the current state of IT security at the company?	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:



Points to Consider	Responses/Comments
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▶ Are there systems to monitor and respond to potential business interruptions due to incidents stemming from malicious intrusions, and to update security protocols to prevent them? Are security violations and other incidents automatically logged and reviewed?

Yes No Comments:

▶ Does the company conduct periodic reviews/audits of IT security? If yes, are the results of the review/audit reported to the board of directors and/or audit committee?

Yes No Comments:

Evaluation of Control Activities:

Effective Ineffective

Summarize the reasons supporting the evaluation, unless obvious:

Monitoring

Monitoring is a process that assesses the quality of internal control performance over time.

Points to Consider	Responses/Comments		
<p><i>Periodic evaluations of internal control are made and personnel, in carrying out their regular duties, obtain evidence as to whether the system of internal control continues to function.</i></p>			
<p>▶ Do procedures require that management review control processes to ensure that the controls are being applied as expected?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Are procedures in place to monitor when controls are overridden and to determine if the override was appropriate?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Are policies/procedures in place to assure that corrective action is taken on a timely basis when control exceptions occur?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p><i>Management (1) implements internal control recommendations made by internal and independent auditors, (2) corrects known deficiencies on a timely basis, and (3) responds appropriately to reports and recommendations from regulators.</i></p>			
<p>▶ Does management take adequate and timely actions to correct deficiencies reported by the internal audit function?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Does management respond timely and appropriately to the findings and recommendations of the independent auditors regarding internal control and policies and procedures of the Company?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Does the company receive findings and recommendations from regulators? If yes, do they adequately and timely address the findings?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:
<p>▶ Are there other quasi-audit functions (e.g., credit review in a financial institution or risk management in an insurance company) that report to management and affect the overall control environment?</p>	<input type="checkbox"/> Yes	<input type="checkbox"/> No	Comments:



Points to Consider	Responses/Comments		
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There is an internal audit function that management uses to assist in their monitoring activities.

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|--|------------------------------|-----------------------------|-----------|
| ▶ Is the level of staffing, training, and specialized skills adequate given the environment (e.g., use of experienced, trained information systems auditors in complex and highly automated environments)? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Is the internal audit function independent (in terms of authority and reporting relationships) of the activities they audit? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Are internal auditors prohibited from having operating responsibilities that conflict with their monitoring role? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Do internal auditors have direct access to the board of directors or audit committee? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Does the internal audit function adhere to professional standards, such as those issued by the Institute of Internal Auditors? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Has there been a recent quality assurance review of the internal audit function by an external party such as the company's independent auditors? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Is the scope of internal audit activities (e.g., balance between financial and operational audits, coverage and rotation of decentralized operations) appropriate given the nature, size and structure of the company? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Is the scope of planned internal audit activities reviewed in advance with: | | | |
| — Senior management? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| — Board of directors or audit committee? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| — Independent auditors? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Does the internal audit department develop an annual plan that considers risk in determining the allocation of resources? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |
| ▶ Do the internal auditors have the authority to examine any aspect of the entity's operations? | <input type="checkbox"/> Yes | <input type="checkbox"/> No | Comments: |

Points to Consider	Responses/Comments	
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► Are the results of the internal audit activities reported to:

— Senior management?

Yes

No

Comments:

— Board of directors or audit committee?

Yes

No

Comments:

— Independent auditors?

Yes

No

Comments:

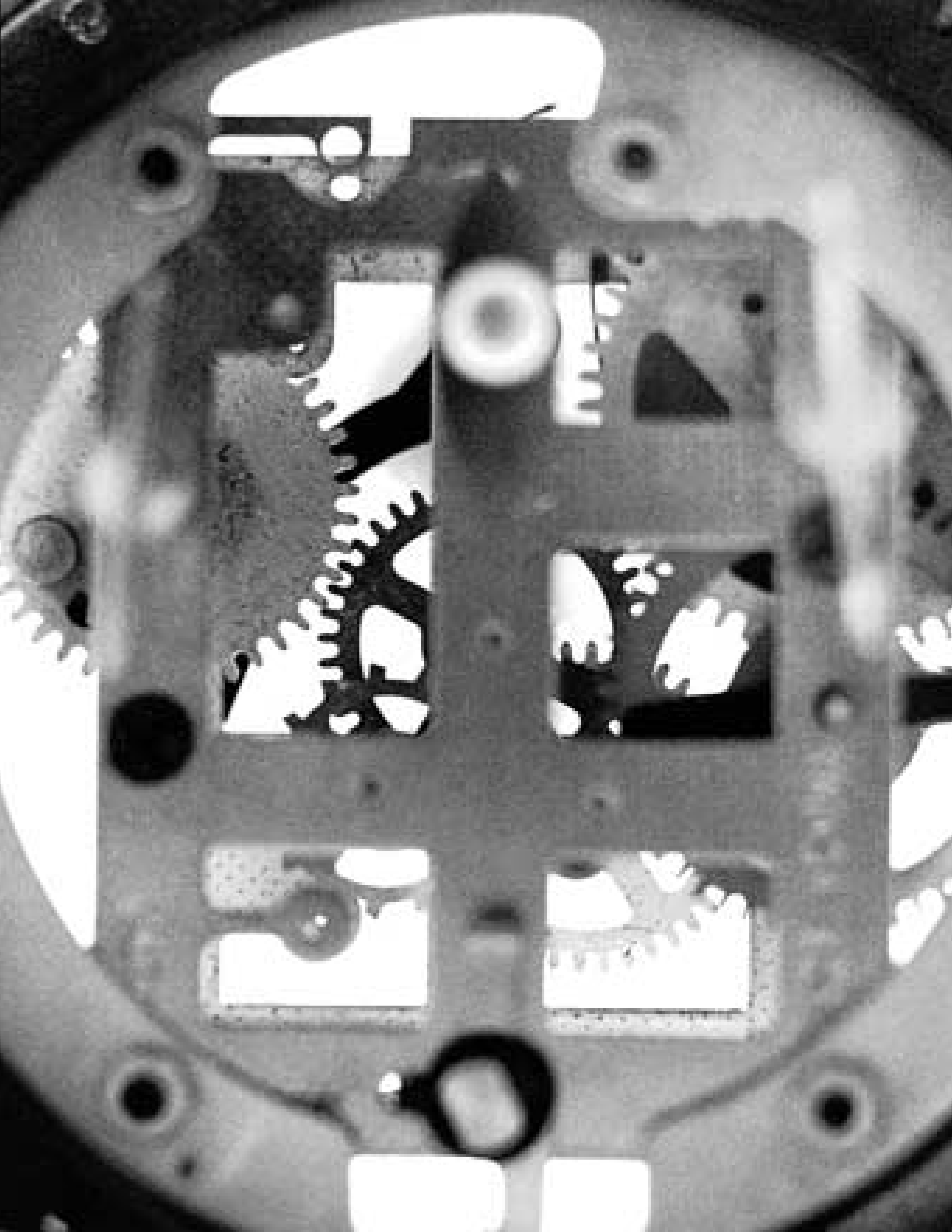
Evaluation of Monitoring:

Effective

Ineffective

Summarize the reasons supporting the evaluation, unless obvious:





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