

 <b>Office of Credit Unions</b> <b>Policies and Procedures</b>	<b>POLICY NUMBER</b>
	<b>10135</b>
<b>MANAGEMENT</b>	<b>EFFECTIVE DATE</b>
	<b>11/01/2018</b>
<b>SUBJECT</b>	<b>REVISION DATE</b>
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## I. PURPOSE

Internal controls help to minimize and monitor risk. Controls must be in place to mitigate risk within the credit union and safeguard credit union assets.

## II. PRIMARY REFERENCES / RELATED REGULATIONS

1. Michigan Credit Union Act:
  - a. [Section 342](#): Credit Union Board, general management, duties, etc.
  - b. [Section 344](#): Audits
  - c. [Section 382](#): Fiscal year; accounting principals
2. Credit Union Bylaws Article VI, Section 5: Duties of Directors
3. Credit Union Bylaws, Article IX, Section 7: Duties of Supervisory Committee

## III. CATEGORIES OF INTERNAL CONTROL

1. **Administrative Controls**
  - a. Accounting System
    - i. The accounting system should contain rigid controls with access rights granted only to the employees who require these rights to perform their duties.
    - ii. Employee access rights on the accounting systems should be tested to ensure that no employee has unwarranted access.
  - b. Directors' Approvals
    - i. The credit union's policies must be documented in the board of directors' minutes and must clearly establish responsibility and authority. There must be reporting systems which will keep the directors sufficiently informed.
  - c. Cash Controls
    - i. The Board of Directors must establish reasonable limitations for cash on hand. This should include aggregate cash balances and individual employee limitations. Each employee should have sole access to their cash. Independent surprise cash counts should be performed on a regular basis.

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- d. Dual Controls
  - i. It is recommended at least two individuals are required to obtain access to vaults, files, or other storage devices.
  - ii. Items, at a minimum, that should be kept under dual control include the following:
    1. Vault and ATM cash
    2. Negotiable collateral
    3. Investment securities
    4. Safekeeping items
    5. Reserve supply of checks
    6. Unissued traveler's checks
    7. Unissued credit cards
    8. Unissued savings bonds
    9. Unissued money orders
    10. Night depository and Mail receipt
    11. Dormant share account
    12. Safe deposit spare locks and keys
    13. Spare keys to teller's cash boxes
- e. Segregation of Duties
  - i. Participation of two employees in a transaction that causes the work of one to serve as proof of the accuracy of the other. Duties should not be arranged so that one person dominates any transaction considerably.
  - ii. The following minimal procedures should be implemented:
    1. Persons handling cash and/or purchases should not have the ability to post transactions to the general ledger.
    2. Loan approval, disbursement and collection activities should be performed by separate individuals.
    3. Persons having authority to sign and disburse checks should not be reconciling the bank accounts.
- f. Sound Personnel Policies
  - i. Background checks should be performed, and references of prospective employees should be verified prior to hiring.
  - ii. Position descriptions should be documented for each position which defines duties and responsibilities. Evaluations should be completed for each employee at least annually.

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- iii. There should be sufficient cross-training to ensure uninterrupted operations during expected and unexpected absences.
- iv. Planned and unannounced rotation of duties should occasionally occur as an additional internal control measure.
- v. Mandatory Vacations; each employee of the credit union, including senior management, should be absent from their duties for an uninterrupted period of not less than one week each year.

## 2. Accounting Controls

- a. Daily Posting: Posting records daily will maintain each day's activities separate and distinct from another day's work. At least monthly, staff must reconcile each general ledger account with its supporting subsidiary ledger, including zero balance accounts with activity during the month.
- b. Subsidiary Records: No less than monthly, accounting staff must reconcile subsidiary records such as share and loan ledgers, bank and investment statements and individual cashier records with the respective general ledger control accounts. A staff member other than the preparer of the subsidiary and reconciliations between the subsidiaries and general ledger account should perform the task.
- c. Internal Reports:
  - i. Management should design their accounting systems to facilitate the preparation of internal reports (non-amortizing loans, dormant accounts, negative share accounts, file maintenance reports, etc.) necessary to review key areas of operation.
  - ii. The reports should be reviewed by persons independent of the transaction.
- d. Pre-numbered Documents
  - i. Sequentially numbered instruments should be used for items such as checks, share certificates, traveler's checks, money orders, etc. This will assist in reconciling and controlling used and unused items. Unissued, pre-numbered items should be maintained under dual controls.
  - ii. Numbered instruments should be reconciled by a person who is independent from that particular function.

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e. Audit Trail

- i. The accounting system should be designed to allow the tracing of any given item as it passes through the credit union's records.
- ii. Recordkeeping deficiencies may include:
  1. General Ledger entries which fail to include an adequate description of the entry.
  2. Lack of sufficient documentation maintained for cash items and overdrafts.
  3. Teller's cash balancing sheets which do not contain adequate details.
  4. Investment registers which fail to list all necessary information.
  5. Reconciliation records of bank accounts which are not kept current and/or fail to reflect the description and disposition of outstanding items.
  6. Inadequate details concerning debits and credits to the cash over and short account.
  7. Failure to maintain sufficient documentation to support correcting entries.
  8. Failure to keep accounts and records posted on a current basis.
  9. Inadequate control over subsidiary records.

**3. Dormant Accounts**

- a. Dormant accounts (shares where there has been no activity for 12 months or more) must be balanced at least monthly and any changes in the accounts should be scrutinized by a managing employee.
- b. Procedures to protect dormant accounts, such as segregating the accounts by instituting controls which require a supervisory override, should be implemented.

**4. Override Reports and File Maintenance Reports**

- a. Most credit union's data processing systems produce a report which details supervisor-override transactions and file maintenance changes as standard control within the system.
- b. File maintenance reports detail changes made to data fields in the credit union's data processing system and should include 'before' and 'after' change information.
- c. Specific focus should be placed on changes made by users rather than system-generated changes (non-system file maintenance).

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- d. The review of file maintenance reports should be a routine function of the credit union's internal controls, regardless of size.
- e. File maintenance reports should be reviewed by an employee independent of the function being reviewed.
- f. Reports should be reviewed, at minimum, on a monthly basis.
- g. Examples of file maintenance reports include, but are not limited to:
  - i. Loan due date changes.
  - ii. Loan and share balance changes.
  - iii. Member address changes.
  - iv. Loan and share rate changes.
  - v. Loan payment amount changes.
  - vi. Loan or Share (as applicable) maturity date changes.
  - vii. Fee amount changes.
  - viii. Account dormancy status changes.
  - ix. Reports reviewing changes from administrative-users or users who have authority to make changes to all functions of the data processing system. These are generally created for employees who perform system testing.
- h. Override Reports detail transactions which required prior approval before making changes within the data processing system. Generally, these transactions require approval because users are unable to make changes due to system restrictions. These restrictions may be in place due to the sensitive nature of transactions or specific limits set by management among other reasons.

#### **IV. MINIMUM PROCEDURES**

- 1. At every examination contact, the examiner should review the following items:
  - a. The annual audit's evaluation of the internal control structure.
  - b. A sample of file maintenance reports for any loan due date changes, dormant share changes, etc.
  - c. The credit union's internal file maintenance review procedures.
  - d. A history of key employee and official accounts.
  - e. Controls surrounding negotiable instruments.
  - f. Account reconciliation controls.
  - g. Bank account reconciliation controls.
  - h. Dormant share accounts, including ensuring management is properly escheating unclaimed funds.
  - i. Negative shares for timeliness of expensing accounts which have been negative for an extended period of time (greater than 90 days).

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- j. The credit union's internal audit program, if applicable.
- k. Supervisory Committee procedures and oversight.
- l. Review board-assumed duties if the credit union does not have a supervisory committee.