Document Code No.: FIN-15-5-1-EP
Title: Internal Controls for Financial Operations, Reporting, and Compliance
Affected Agencies: Executive branch offices and agencies
Authorities: RCW 43.09.200; Washington State BARS Manual §3.1
Keywords: Internal Control; Reasonable Assurance
Sponsoring Agency: Executive Audit Committee; Finance and Business Operations

Executive signature: Dow Constantine
Date signed and effective: December 12, 2024

King County

I. Purpose

One of the foundational requirements for being the "best run government" is having strong internal controls across our enterprise. When internal controls are weak or viewed as a lower priority, it puts King County's reputation and credibility at risk with our residents, businesses, community-based organizations, and others. This policy is intended to support agencies in assessing their risks and continuously strengthening their internal controls. It provides specific guidance to King County agencies. This guidance includes how to assess, establish, and maintain internal controls necessary to promote efficiency and effectiveness in financial operations, assure reliability in financial reporting, and to ensure compliance with financial assistance laws and regulations.

Applicability and Audience This policy applies to the administrative offices and agencies supervised by the King County Executive. The Assessor and the Director of Elections have also adopted this policy. The audience may include non-Executive Branch King County departments adopting this policy. Those entities having adopted this policy are collectively referred to as the "County" in the remainder of this policy.

II. Definitions

"Internal control"- process effected by an entity's governing body, management, and other personnel designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance. The Executive Audit Committee serves as the governing body over the system of internal controls at King County.

"Internal Control Deficiency" – A shortcoming in a component or components and relevant principle(s) of internal control resulting in insufficient control to adequately reduce the likelihood that the entity can achieve its objectives. A **major deficiency** is an internal control deficiency or combination of deficiencies that severely reduces the likelihood that the entity can achieve its objectives.

"Objectives"- what the County is trying to achieve classified into the following (objectives in this policy are limited to those related to finance): a) "Operations" – efficiency and effectiveness of financial operations and safeguarding assets against loss, b) "Reporting" – pertains to accuracy and precision for both internal and external financial reporting, and may encompass reliability, timeliness, transparency or other criteria set forth by regulators, standard setters, or County policies; c) "Compliance" – adherence to all applicable financial laws and regulations, such as federal assistance regulations.

"Overcontrolling" – A misalignment between a component or components and relevant principle(s) of internal control and the risk they are trying to mitigate causing excess controls to be applied relative to the risk present in the operations, reporting, or compliance process. Overcontrolling is the opposite of an Internal Control Deficiency and can result in the Lean wastes of overprocessing and/or overproduction.

"Subunits" – The County's departments, divisions, sections, units, agencies, operating units, functions, and value streams.

III. Policies

A. Framework

Through this policy the County adopts the 2013 edition of the internal control framework drafted by the Committee of Sponsoring Organizations (COSO). This framework includes 5 integrated components and 17 principles for internal controls.

1. CONTROL ENVIRONMENT - The set of standards, processes, and structures that provide the basis for carrying out internal control across the organization.

   a. Principle 1. The organization demonstrates a commitment to integrity and ethical values.

   b. Principle 2. The Executive Audit Committee (EAC) demonstrates independence from management and exercises oversight of the development and performance of internal control.

   c. Principle 3. Management establishes, with EAC oversight, structures, reporting lines, and appropriate authorities and responsibilities in the pursuit of Objectives.

   d. Principle 4. The organization demonstrates a commitment to attract, develop, and retain competent individuals in alignment with Objectives.

   e. Principle 5. The organization holds individuals accountable for their internal control responsibilities in the pursuit of Objectives.

2. RISK ASSESSMENT – A dynamic and iterative process for identifying and analyzing risks to achieving the County's and/or departmental Objectives, forming a basis for how risks should be managed.

   a. Principle 6. The organization specifies Objectives with sufficient clarity to enable the identification and assessment of risks relating to Objectives.

   b. Principle 7. The organization identifies risks to the achievement of its Objectives across the entity and analyzes risks as a basis for determining how the risks should be managed.

   c. Principle 8. The organization considers the potential for fraud in assessing risks to the achievement of Objectives.

   d. Principle 9. The organization identifies and assesses changes that could significantly impact the system of internal control.

3. CONTROL ACTIVITIES – The actions established by policies and procedures to help ensure that management directives to mitigate risks to the achievement of Objectives are carried out.

   a. Principle 10. The organization selects and develops control activities that contribute to the mitigation of risks to the achievement of Objectives to acceptable levels.

b. Principle 11. The organization selects and develops general control activities over technology to support the achievement of Objectives.

c. Principle 12. The organization deploys control activities through policies that establish what is expected and procedures that put policies into action.

4. INFORMATION AND COMMUNICATION – Information are facts and data synthesized into knowledge which are vital for the County to carry out internal control responsibilities in support of achievement of its Objectives.

a. Principle 13. The organization obtains or generates and uses relevant, quality information to support the functioning of internal control.

b. Principle 14. The organization internally communicates information including Objectives and responsibilities for internal control, necessary to support the functioning of internal control.

c. Principle 15. The organization communicates with external parties regarding matters affecting the functioning of internal control.

5. MONITORING – Ongoing and/or ad hoc evaluations, or some combination of the two are used to ascertain whether each of the five components of internal control is present and functioning.

a. Principle 16. The organization selects, develops, and performs ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.

b. Principle 17. The organization evaluates and communicates internal control deficiencies in a timely manner to those parties responsible for taking corrective action, including senior management and the EAC, as appropriate.

B. Implementation of the Framework

Through its agencies and administrative offices, the County has implemented a comprehensive system of internal controls under the COSO Framework that covers all levels of its organization (its subunits) and is comprised of policies, procedures, and methods that will safeguard its assets, assure reliability of financial data, and comply with legal and contractual requirements.

C. Maintenance and Monitoring

1. Since organizational operations and risks (both internal and external) change over time, the comprehensive system of internal control must be monitored and adjusted. This can occur any time needed, but must be performed and documented at least once per biennial budget period.

2. Reviews evaluate whether the right level of control is being applied to current processes for the risk present. Materiality thresholds are part of this analysis. For example, what might be a tolerable error on the financial statements could result in an audit finding in the Single Audit where materiality thresholds are much lower. An Internal Control Deficiency identified shall have corrective action plans drafted and worked upon to remedy the deficiency. Major deficiencies must be corrected by management within one year from discovery.

3. Reviews shall include monitoring for changes in risks that may impact the effectiveness of internal controls.

4. On an ongoing basis, the continued functioning of vital control processes that are working, and corrective actions being undertaken to resolve major deficiencies, shall be managed through the subunit's operational performance management system used for monitoring of critical systems. This may be tier boards or other tools agencies use for operational monitoring.

5. Each subunit is expected to drive continuous improvement to their system of internal control. This includes detecting and addressing Overcontrolling situations. Sources of guidance include, but are not limited to, the Lean tools and techniques that are recommended by the County's Continuous Improvement Team in the Office of Performance, Strategy and Budget; the Government Finance Officers Association's (GFOA); and/or the Washington State Auditor's Office Center for Government Innovation.

D. Financial Reporting

1. Regardless of which Department, Office or Agency authors the report, financial statements for external purposes shall be prepared in accordance with applicable accounting standards, rules, and regulations. These financial statements for King County include:

   a. Annual Comprehensive Financial Report

   b. Financial statements, schedules, and tables in bond official statements, whether audited or unaudited

   c. Standalone enterprise financial statements

   d. State-mandated financial statements or reports (e.g. BARS reports)

   e. Popular Annual Financial Reports

   f. Condensed financial statements used in other published reports

2. In addition, financial reports that are based on the County's accounting and financial reporting data and are posted to a publicly accessible County website or reported in regulatory filings are encompassed by this policy.

E. Finance and Business Operations (FBOD)

FBOD shall provide the following support to offices and agencies to support the implementation of this policy:

1. Provide a roster of independent contractors to agencies for internal audit or internal control consulting purposes.

2. Provide training to other agencies on risk assessments and internal control evaluations.

3. Provide guidance in establishing internal control procedures or controls.

4. Include discussions of internal controls in regular meetings with departments and agencies.

5. Monitor internal controls that impact countywide financial reporting and federal assistance compliance Objectives using tools including, but not limited to, the annual five-star report over internal controls.

F. Department/Division Directors and Agency Directors

1. Ensure that internal control procedures are in place, designed to achieve reasonable assurance of financial Objectives, and are being adhered to by employees.

2. Develop corrective action plans, as needed.

3. Address and monitor deficiencies in internal controls or situations where the system of internal controls is over controlling risk.

4. Report fraud, potential fraud, and breaches of internal controls to the Chief Accountant.

5. Communicate progress of corrective actions for internal control deficiencies to the Executive Audit Committee.

G. Executive Audit Committee

1. Provide oversight and direction for the internal control environment across County government.

2. Monitor the internal control environment and address major control weaknesses and deficiencies.

3. Recommend to the Executive changes in this policy to strengthen the County's internal control environment.

IV. Implementation Plan

A. This policy becomes effective for Executive Branch agencies on the date that it is signed by the Executive. The Finance and Business Operations Division is responsible for implementation of this policy.

B. Agency and office Finance Managers are responsible for communicating this policy to the management structure within their respective agencies and other appropriate parties with support from FBOD Financial Management as needed.

C. Each department and agency director is required to develop and implement procedures to ensure that the directives in this policy are followed by the employees under their oversight.

V. Maintenance

A. This policy will be maintained by the Finance and Business Operations Division, or its successor agency.

B. This policy will automatically expire five (5) years after its effective date. A new, revised, or renewed policy will be initiated by the Finance and Business Operations Division or its successor agency prior to the expiration date.

VI. Consequences of Noncompliance

Noncompliance will result in a loss to trust between residents and King County and can result in audit findings or adverse audit opinions to the detriment of the County's bond rating, the necessity of returning grant monies, or payment of monetary fines. Noncompliance may also create opportunity for frauds or losses; see Executive Policy FIN-15-6 for more detail on fraud investigation and loss reporting.