UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT
MANAGE CASH FLOW

Control practices

The following control objectives provide a basis for strengthening your control environment for the process of managing cash flow. When you select an objective, you will access a list of the associated business risks and control practices. That information can serve as a checklist when you begin reviewing the strength of your current process controls.

This business risk and control information can help you assess your internal control environment and assist with the design and implementation of internal controls. Please note that this information is at the generic business process level and many companies will need to go beyond generic models to address the specific business processes that support the financial and nonfinancial disclosures being made. You can combine the insight of this business risk and control information with your industry-specific knowledge and understanding of your company's environment when conducting internal control assessments and designing and implementing recommendations.

Effectiveness and efficiency of operations

A. Cash flows are effectively and efficiently managed to increase volume, reduce uncertainty, and move cash faster and without loss of value to where it is most useful and needed.
B. Exposure of funds located in foreign countries to exchange risks and the effects of government restrictions on the movement of funds across international borders are minimized.
C. Cash funds are maximized by accelerating cash receipts and deferring cash disbursements, consistent with sound business practice.
D. Returns from investments of excess cash funds are maximized.
E. Marketable securities, investments, and other financial assets are safeguarded.
F. Cash forecasts are used to maximize short-term investment income and to avoid cash shortfalls.
G. Short-term financing sources are used to manage seasonal and temporary fluctuations in cash flow.
H. Performance audits are used as tools to evaluate cost-effectiveness of cash management systems.

UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT
MANAGE CASH FLOW

Reliability of financial reporting

A. Investment transactions are properly authorized.
B. All investment transactions are processed and recorded on a timely basis.
C. Investment transactions are accurately processed and reported.
D. Recorded investment balances are substantiated.
E. Recorded investment balances are evaluated.
F. All income from investments is accurately recorded.
G. Debt transactions are properly authorized.
H. All debt transactions are processed and recorded on a timely basis.
I. Debt transactions are accurately processed and recorded.
J. Recorded debt balances are substantiated.
K. All interest expense is accurately recorded.
L. Other financial transactions are properly authorized and recorded.

Compliance with applicable laws and regulations

A. The company complies with legal or loan restrictions.

Effectiveness and efficiency of operations

A. Cash flows are effectively and efficiently managed to increase volume, reduce uncertainty, and move cash faster and without loss of value to where it is most useful and needed.

Business risks

- Management will have inaccurate, untimely, or unavailable information regarding cash inflows and outflows necessary to maximize short-term investment income and avoid cash shortfalls.
- The company will not use resources efficiently in its operations or earn a reasonable profit.
- Management will have insufficient information on investment alternatives to optimize the return on temporary cash investments.
- The company will not meet its cash requirements.
- Managers will lack awareness of financing alternatives in the event of a cash shortfall and fail to maintain appropriate relationships with financing sources.
- Managers will be unaware of all risks in global operations and less prepared to make decisions because of lack of information about financial instruments and other global challenges, including: limited cash management options; cultural and geographical barriers, such as time zones, banking relationships, and diverse technology, that pose barriers to cross-border cash flows; worldwide information about cash flows, assets and liabilities, counter party risks that is more difficult to compile with the same speed, regularity, and efficiency as domestic business.

UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT
MANAGE CASH FLOW

Control practices

1. Implement a centralized treasury and cash management system to offer flexibility, efficiency, risk management, and control.
2. Use a treasury workstation to automate the daily cash position through an electronic, multi-bank-balance reporter, integrated with investment and debt management systems.
3. Integrate treasury systems with general ledger systems to eliminate time-consuming journal entry preparation and rekeying.
4. Prepare reports to summarize the company's liquidity status, solvency, and use of excess funds.
5. Concentrate financial assets to manage treasury risk and bank credit risk, maximize available funds, reduce borrowing costs, and maximize returns on surplus funds.
6. Create positive, strategic supplier relationships with trusted banks that are able to best meet the company's treasury needs.
7. Define and communicate cash management policies and procedures to treasury professionals. Include in these policies and procedures credit and collections policies that are responsive to existing economic situations and business plans and also specific policies and defined limits of authority and risk that provide a foundation for controlling and monitoring trading activities.
8. Require that management sets restrictions on investment type, quality, domicile, and maturity.
9. Limit trading in the following types of transactions to highly trained, skilled professionals only: security swaps, tax loss trading, repurchase agreements, reverse repurchase agreements, matched repurchase agreements, lending of government securities, interest rate futures, forward contracts, standby contracts, forward exchange contracts, currency swaps, and options transactions.
10. Configure the cash management system to flag instances of high-interest-rate borrowing or idle cash.
11. Hold treasury management responsible for evaluating liquidity management strategies in light of current interest rates and market opportunities.
12. Determine a minimum amount of cash to hold at each location.
13. Verify cash uses against supporting detailed records such as bank balances, registrar, and transfer agent.
14. Make efforts to eliminate excessive bank balances and unnecessary bank accounts.
15. Analyze each bank account as to type, balance, and bank fees per account to determine which banks are most efficient.
16. Analyze key ratio trends and variances to identify problems and areas to investigate.

B. Exposure of funds located in foreign countries to exchange risks and the effects of government restrictions on the movement of funds across international borders are minimized.

Business risks

- Volatility in exchange markets and the significant political and regulatory developments in Europe and Asia will increase uncertainty and risk.

Control practices

1. Analyze political and economic trends in each foreign country for any risks surrounding payment delays or blockage to access of funds.
2. Establish a bank account in each country where the company operates and use it to pay local expenses.
3. Use an automated netting system (computerized systems that help reduce foreign exchange conversions, intercompany transaction volume, and administrative costs) where there are diversified product lines and significant two-way flows between international subsidiaries or substantial intercompany foreign exchange volume.
4. Pool cash flows by currency rather than by country operations.

C. Cash funds are maximized by accelerating cash receipts and deferring cash disbursements, consistent with sound business practice.

Business risks

- The company will generate lower than optimal returns on cash funds.
- The company will incur higher short-term borrowing costs.

Control practices

1. Analyze the process of receiving and depositing cash, and identify unacceptable float points. (For example, mail float, processing float, and deposit collection float.)
2. Perform detailed comparisons of actual versus budgeted disbursements.
3. Evaluate root causes of unacceptable float times and take corrective steps to reduce the float.
4. Consider check-clearing time when selecting a bank.
5. Honor bank credit cards.
6. Transfer funds between banks using wire transfers (EFTs) or depository transfer checks (DTCs).
7. Bill as soon as the order is shipped.
8. Encourage customers to call an "800" number if discrepancies with orders exist.
9. Identify root causes of billing errors and take steps to eliminate them.
10. Arrange wholesale lockboxes where the collection points are closest to customers.
11. Monitor lockboxes on an ongoing basis to ensure that expected benefits are being realized.
12. Require that vendors not be paid early unless a discount rate for early payment is greater than the company's incremental borrowing or risk-free short-term investment rate.
13. Centralize the payables operation so accounts are paid at the most opportune time and disbursement float is determined.
14. Establish zero bank accounts (ZBAs) to reduce the workload required of the cash management function and enable the company to remain more fully invested.

D. Returns from investments of excess cash funds are maximized.

Business risks

- Greater uncertainty will exist in investment alternative evaluations because of cash flow forecasting challenges.

Control practices

1. Establish a policy to guide investments of excess cash funds, such as investing surplus funds in marketable securities.
2. Consider the security of the principal, such as the degree of risk involved and the company's willingness to lose part or all of the initial investment, when evaluating short-term investment decisions.
3. Consider the balance between yield and risk (For example, the greater the risk, the lower the security of the principal.) when evaluating short-term investment decisions.
4. Consider marketability and liquidity (For example, the ability to find a ready market to dispose of the investment at a fair price.) when evaluating short-term investment decisions.
5. Consider tax factors when evaluating short-term investment decisions.
6. Consider current and future income needs when evaluating short-term investment decisions.
7. Consider current and future inflation levels when evaluating short-term investment decisions.
8. Consider the company's ability to hold investments and withstand financial losses when evaluating short-term investment decisions.
9. Consider the effort that will be involved in managing each investment when evaluating short-term investment decisions.
10. Consider the extent of credit risk when evaluating short-term investment decisions.
11. Consider the extent of diversification when evaluating short-term investment decisions.

E. Marketable securities, investments, and other financial assets are safeguarded.

Business risks

- Cash or securities will be lost, stolen, destroyed, or temporarily diverted.
- Records will be misused or altered by unauthorized personnel.

Control practices

1. Limit physical access to securities to authorized personnel.
2. Physically control securities using third-party custodians.
3. Use safes, vaults, or other security devices when securities are retained onsite.
4. Require management authorization for transfers of investments to external parties. (For example, require written authorization from at least two designated officials before securities can be withdrawn from depository banks or other third parties for safekeeping, use as collateral, or consummation of a business transaction.)
5. Register securities in the company's name when possible.
6. Obtain declarations of trust for securities registered in the names of nominees.
7. Segregate investment decisions and actual investment activity from accounting activities and custodial responsibilities.
8. Segregate custody of marketable securities from the accounting for those securities.
9. Segregate disbursements of interest and dividend payments from the accounting for debt and equity securities.
10. Segregate processing from the review of monthly borrowing and investment transactions.
11. Document key investment and financial asset safekeeping activities and procedures.

F. Cash forecasts are used to maximize short-term investment income and to avoid cash shortfalls.

Business risks

- Inaccurate, untimely, or unavailable information regarding cash inflows and outflows will result in cash shortfalls.

Control practices

1. Use information systems to identify all cash sources as well as cash collection or due dates. (Such cash sources include accounts receivable collections, customer deposits, sales of assets, and loan proceeds.)
2. Use information systems to identify all cash requirements and cash payment dates. (Such requirements include accounts payable, payrolls, and loan or dividend payments.)
3. Identify all internal sources of cash-related information.
4. Compare information used to prepare cash forecasts with supporting documents and verify that the information is internally consistent.

G. Short-term financing sources are used to manage seasonal and temporary fluctuations in cash flow.

Business risks

- Forecasting cash flows and business cycles will grow more complex.

Control practices

1. Evaluate cash flows on a monthly and weekly basis. Consider economic conditions, expected cash receipts, anticipated cash payments, and seasonal requirements.
2. Consult with professional financial advisors to locate alternative sources of financing.
3. Consider various sources of short-term financing. (For example, trade credit, bank loans, lines of credit, bankers' acceptances, finance company loans, commercial paper, receivables financing, and inventory financing).
4. Consider interest rates and collateral requirements.
5. Consider costs, including interest rates and legal fees, points, and other front-end fees.
6. Consider the effect of short-term financing on financial ratios and credit rating.
7. Consider anticipated money market conditions and the availability of future financing.
8. Consider prepayment penalties, restrictions, the inflation rate, and the tax rate.

H. Performance audits are used as tools to evaluate cost-effectiveness of cash management systems.

Business risks

- Management will not know whether the cash management system is operating effectively and efficiently.
- Management will miss opportunities to improve liquidity.
- Management will not know about financial risks that are not being managed effectively.

Control practices

1. Employ cash management or treasury tactical audits to survey how well the company's systems are performing and to create awareness of the importance of managing cash and financial risks throughout the company.
2. Design cash management or treasury tactical audits to focus on all aspects of the process impacting the cash-to-cash cycle.
3. Ensure that treasury performance audits focus on identifying liquidity risks, identifying risks to day-to-day cash flows, analyzing existing processes to identify inefficiencies, and reviewing cross-border investing and borrowing activities.
4. Require that detailed questionnaires be completed by the employees responsible for the areas being audited at each location or unit. Analyze all surveys, and identify key areas for further evaluation.
5. Interview persons responsible for operations, and identify areas for improvement.
6. Document processes as they currently exist based on the information gathered.
7. Identify areas for improvement. (For example, receivables/payment float, customer/supplier pricing, and banking costs.) Provide a description showing how the improved process will work, what the specifications of the new process will be, and how improvements will be implemented.
8. Analyze costs and improvements. Assess performance against relevant benchmarks whenever possible.
9. Summarize findings of interviews and employee surveys in writing. Include specific recommendations and implementation strategies.
10. Monitor the change process on a continual basis.

UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT
MANAGE CASH FLOW

Reliability of financial reporting

A. Investment transactions are properly authorized.

Business risks

- Investments will be purchased or sold for the benefit of management, employees, or third parties, resulting in unrealized investment gains or higher than normal losses.
- Investments will be purchased or sold illegally, in violation of the company's stated policies, or in violation of loan restrictions and covenants, resulting in fines, penalties, and investment losses.
- Cash or securities will be lost, stolen, destroyed, or temporarily diverted.
- Investment transactions will not coincide with the company's objectives.

Control practices

1. Require management approval of the company's investment policy.
2. Ensure that the company's formally documented investment policy includes the following provisions: management's primary objectives, expected returns on marketable securities and investment transactions, acceptable levels and limits of risk, diversification requirements, portfolio concentration, approval requirements, and personnel responsible for managing according to the policy.
3. Designate an official to approve investment purchases and sales based on the established investment policy.
4. Compare proposed transactions with cash flow projections of the intended purchase or sale.
5. Require management approval of non-routine or unusual transactions.
6. Review investment purchases and sales periodically for compliance with authorized policies.

B. All investment transactions are processed and recorded on a timely basis.

Business risks

- Purchases and sales of investments will not be recorded.

Control practices

1. Issue pre-numbered buy and sell orders to brokers; reconcile them with the transaction log used to record each of the transactions.
2. Update schedules of investment maturities regularly.
3. Compare transactions periodically with authorizations, including board of directors' minutes.
4. Document key investment processing activities and procedures.

C. Investment transactions are accurately processed and reported.

Business risks

- Investment and related receivable account balances will be incorrect.
- Investment and related receivable account balances will be misclassified.
- Payable and income accounts will be misstated due to incorrect calculations and classifications and recognition in the wrong accounting period.
- Errors and omissions will not be detected and corrected.

Control practices

1. Approve all investment transactions and document them in the proper accounts.
2. Review broker statements closely and address any unreconciled or overdue items promptly.
3. Test the clerical accuracy of investment journals, registers, and reports periodically.

D. Recorded investment balances are substantiated.

Business risks

- Unauthorized transactions will be recorded and remain undetected.
- Errors in the processing, summarization, and recording of purchases and investments, and related investment income, will remain undetected.
- Investment sales and purchases, and related income, will not be recorded.

Control practices

1. Maintain subsidiary records for investments. Include in the records the following: specific descriptions and certificate serial numbers, names in which investments are registered, and the cost or selling prices.
2. Require that an employee not responsible for custodial responsibilities review investment subsidiary records for completeness and accuracy. Ensure that this is done by directly confirming investments held by banks and other third parties and by reviewing certificates for investments held directly by the organization.

E. Recorded investment balances are evaluated.

Business risks

- The company will miss changes in market values that could affect investments.
- The company will lose money on its investments.
- Currency translations will be inaccurate.
- The company will miss investment opportunities or situations where it should write off investments.

Control practices

1. Compare recorded investment balances against market values periodically.
2. Use outside services such as a bank's trust department to report changes in market values.
3. Adjust regularly the company's share of investee earnings, losses, and dividends for investments in which it owns 20% or more.
4. Check currency translations for foreign investments for accuracy.
5. Review periodically the alternatives for possible realization of its investments that have been fully reserved or completely written off.
6. Review periodically the process used to write off investments and to determine the carrying value of investments.
7. Require that management review investments when determining if a write-off or loss provision is necessary and in accordance with accounting principles and sound business judgment.

F. All income from investments is accurately recorded.

Business risks

- Investment income will not be reported and recorded.
- Investment income and related receivable account balances will be misstated because of incorrect calculations or classifications or recognition in the wrong accounting period.

Control practices

1. Ensure that personnel independent of the investment custodians maintain and safeguard detailed schedules regarding anticipated income.
2. Require that management reviews schedules of anticipated income and the calculations of interest and dividend income. Compare recalculated amounts with accrued amounts.
3. Base dividend accruals on reports from reliable and published sources.
4. Adhere to documented cut-off and period-end close procedures regarding investment income and losses. For example, base calculations of the accrued interest income for the period on approved policies and procedures.
5. Compare recurring entries between periods, such as entries for dividend and interest income, from one period to the next to identify any unusual fluctuations.

G. Debt transactions are properly authorized.

Business risks

- Debt transactions will not coincide with company objectives.
- Financing will be obtained at unauthorized costs and terms.
- Financing requirements will not be satisfied.
- Failure to comply with legal or loan restrictions and covenants will adversely affect lender relationships and financial statement classification of debt obligations, resulting in an inappropriate capital structure that may jeopardize the company's ability to continue in business.

Control practices

1. Document policies and procedures for acceptable cost of capital, legal restrictions, and preferred sources of funds, liquidity requirements, acceptable financing alternatives, acceptable debt covenants, and authorization and approval requirements.
2. Require board approval for significant changes in banking and borrowing relationships.
3. Require management approval for certain signing and authorization limits.
4. Require board approval for all significant debt financing arrangements and document this approval in board meeting minutes.
5. Require that legal professionals review all debt financing provisions and all financing leases prior to their execution.
6. Compare all proposed transactions with cash flow projections of the intended borrowing and loan payout.
7. Monitor all financing arrangements closely for compliance with loan covenants.

H. All debt transactions are processed and recorded on a timely basis.

Business risks

- Borrowing and retirement of debt will not be recorded.

Control practices

1. Record all new borrowings and debt retirements using specific and individual transaction numbers to properly identify and account for them.
2. Prepare and update schedules of loan payments, including principle and interest, with each payment made.
3. Track debt transactions that have been submitted for processing back to the board of directors' minutes to ensure that the board properly approved them.

UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT
MANAGE CASH FLOW

I. Debt transactions are accurately processed and recorded.

Business risks

- Debt and related asset, liability, and income or expense account balances will be misstated due to incorrect calculations and classification or recognition in the wrong accounting period.
- Errors and omissions will not be detected and corrected.

Control practices

1. Review all debt transactions for reasonableness and proper approvals.
2. Use independent registrars and transfer agents where possible.
3. Adhere to documented cut-off and period-end close procedures regarding debt transactions. (For example, calculations of the accrued interest expense for the period are based on approved policies and procedures.)
4. Track recurring entries between periods, such as entries for interest expense, from one period to the next, and identify any unusual fluctuations.

J. Recorded debt balances are substantiated.

Business risks

- Unauthorized debt transactions will remain undetected.
- Errors in processing, summarizing, and recording debt transactions will remain undetected.

Control practices

1. Maintain detailed records of outstanding loan obligations. Reconcile these records with confirmed debt balances periodically to determine that all company entries have been properly recorded.
2. Confirm debt directly with the transfer agent, registrar, and other creditors.
3. Reconcile detailed subsidiary debt records to general ledger debt accounts.

K. All interest expense is accurately recorded.

Business risks

- Interest expense will not be reported and recorded.
- Interest expense and the related payable account balances will be misstated due to incorrect calculations and classifications or recognition in the wrong accounting period.

Control practices

1. Prepare schedules of interest expense to ensure the company knows when interest will be payable and how much will be due.
2. Update interest schedules with every interest payment that is made.
3. Reconcile interest accrued with the actual amount payable on an issue-by-issue basis.
4. Require that management review interest expense calculations.

L. Other financial transactions are properly authorized and recorded.

Business risks

- Cash or securities will be lost, stolen, destroyed, or temporarily diverted.
- Cash or dividend payments will be duplicated or improperly or fraudulently disbursed.
- Transactions will not coincide with the company's objectives.

Control practices

1. Open all bank accounts in the name of the company or its legal subsidiaries only.
2. Require management approval to open a bank account.
3. Use third parties, such as banks, independent registrars, or transfer agents, where possible, to account for changes in investments and debt, changes in the capital stock accounts, and changes in ownership of the company's issued shares.
4. Require management and board approval for all capital stock transactions, such as issuance, splits, dividends, and employee stock options.
5. Maintain the confidentiality of shareholder information.
6. Account for all authorized, issued, outstanding, and treasury stock, as well as exercised and unexercised stock options, dividends, and transfers of stock.

Compliance with applicable laws and regulations

A. The company complies with legal or loan restrictions.

Business risks

- The company will incur fines, penalties, litigation, and/or a loss of reputation.
- The company will violate legal or loan restrictions and covenants.

Control practices

1. Require management and board approval for all significant debt, investment, and equity transactions.
2. Review compliance with legal or loan restrictions periodically.