



CREDIT UNION INTERNAL CONTROL REQUIREMENTS

Under the COSO (Committee of Sponsoring Organizations of the Treadway Commission) Internal Control Framework, internal control is broadly defined as a process, affected by the entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following three categories:

- Effectiveness and efficiency of operations;
- Reliability of financial reporting; and
- Compliance with applicable laws and regulations.

COSO further defines internal controls as consisting of five interrelated components:

1. **Control Environment.** The "tone at the top" - the foundation for all other components of internal control.
2. **Risk Assessment.** Manage-

ment establishes activity-level objectives and mechanisms for identifying and analyzing risk related to their achievement.

3. **Control Activities.** Policies and procedures that ensure management's objectives are carried out and help ensure that necessary actions are taken to minimize risks to achievement of the credit union's objectives.
4. **Information and Communication.** Information must be identified, captured, and communicated in a form and time frame that enable people to carry out their responsibilities.
5. **Monitoring.** Assessing the quality of the system's performance over time. This is accomplished through ongoing monitoring activities, separate evaluations or a combination of the two. ([cont.](#))

This short newsletter introduces the concept of internal controls and focuses on the need for policies and procedures as a critical component of effective internal



CREDIT UNION POLICIES AND PROCEDURES

Policies and procedures are a necessary first step of maintaining and effective system of internal controls. **Policies** are the guiding principles that give direction to the employees of a credit union. Pursuant to its statutory obligations, a credit union's Board adopts policies governing the operation of the credit union. **Procedures** represent the

methods by which the credit union implements the policies. They guide employee actions.

Policies must be written, reviewed periodically, and effectively communicated to all staff. Key areas that require written policies include:

- Lending ([cont.](#))

Policies and procedures are good business practice.

CREDIT UNION INTERNAL CONTROL REQUIREMENTS (CONT'D FROM PAGE 1)

Under Section 113 of the Federal Credit Union Act, and in most state credit union acts, the board of directors is responsible for the general direction and control of the affairs of the credit union, including the proper and profitable conduct of credit union operations, the safety of credit union assets, and the accuracy and adequacy of financial statements. As a part of that responsibility, the board establishes internal controls, which include policies, procedures, and processes to maintain control over duties delegated to employees.

Internal controls consist of both hard controls and soft controls.

- **Hard controls** are policies, procedures, and systems designed to prevent fraud and error. Examples of hard controls include separation of duties, and an ethics policy.
- **Soft controls** refer to the competency, integrity, and commitment to honest and accuracy by employees, managers, volunteers, and consultants and business partners. Examples of soft controls include regular monitoring and an objective internal audit function.

The primary object of internal controls is to prevent employee dishonest and errors, and to protect the credit union from loss. The type and scope of internal controls is dependent upon the credit union's size, complexity, and scope of activities.



CREDIT UNION POLICIES AND PROCEDURES (CONT'D FROM PAGE 1)

- Asset Liability Management
- Personnel
- Compliance
- Retail
- Member Information Security
- Information Systems

Procedures should be in writing and provide detail to staff setting for the details of the tasks required to implement the policies.

A list of policies and procedures that should be adopted and maintained by credit unions can be found [here](#).