White Paper

How Well Do You Manage Internal Controls?

Automated Reconciliation Is Vital to Strengthening Internal Controls and Supporting Growth for Financial Institutions

Financial institutions manage thousands of transactions every day. The sheer speed, volume and variability demand strong internal controls to keep balance sheets consistently accurate. Internal controls can also identify errors and reduce the risk of overt fraud. In fact, internal controls are so important they are mandated by the FDIC, NACU and other regulatory bodies.

So how do financial institutions meet internal control requirements while accommodating growth and customer expectations for faster payments?

Financial institutions are required by federal law to have internal controls, systems and programs appropriate for their size and the nature, scope and risk of their activities. Those with $1 billion or more in assets are subject to even higher standards. Failure to comply can result in steep monetary penalties and other punitive actions.

These regulations are in place to prevent financial misstatements, mitigate fraud and safeguard against failure. Financial institutions use regular reconciliation of accounts and certification of financial reports as a substantial part of their internal control systems.

Under FDIC rules, management reports at institutions with $1 billion or more in consolidated assets are required to assess the effectiveness of their internal control systems. This includes identifying an appropriate framework based on asset size, indicating what controls are used and whether they are effectual, and disclosing any material weaknesses.

The Sarbanes-Oxley Act of 2002 mandates that publicly traded companies establish, maintain, assess, and report on internal controls and procedures for financial reporting. The NACU has similar regulatory requirements.

The FDIC's Internal Routine and Controls manual is specific about its expectations: "Recordkeeping systems should be designed to enable the tracing of any transaction as it passes through accounts."

Tracing each transaction isn't easy. As volume climbs, reconciliation becomes more complex. The growth in payment types and methods, for instance, has led to a rise in transactions in recent years. Common reconciliation examples include:

- Ledger to sub-ledger accounts
- Federal Reserve accounts
- Cash
- Securities
- Suspense accounts
- Debit/Credit cards
- Person-to-Person (P2P) payments

Financial institutions must track and reconcile all of this – and makes balancing the books every month with Excel spreadsheets an almost impossible task. Time-consuming manual processes, with the real possibility of human error and lack of an audit trail, cannot easily support internal controls in today's digital payments environment.

Inadequacies of Manual Reconciliation and Certification

Reconciliation and certification provide an objective system of checks and balances. However, the process of manual reconciliation can be arduous. It's a time-consuming, resource-intensive process that's prone to human error, and provides limited visibility into how balance sheets are ultimately derived. This is especially true for institutions with $1 billion or more in assets.

There are a number of variables that can impact the consistency of manual reconciliation. They include a shortage of workers, scheduled leave, inexperienced employees and inherent departmental delays. Performing reconciliation at the end of the month means that fraud may not be detected in a timely manner, depending on when it occurs. Acquisition of other financial institutions – or products or lines of business – can add a large and immediate burden to the process.

> "If you've got hundreds of thousands of transactions per day, it's a lot of work to load them all onto a spreadsheet, making sure to get the right balances, making sure you get everything matched up. I've got to believe the risk is high in those areas that are manual."
>
> **Ken Valentine**
> Vice President and Senior Group Manager,
> Information Technology, Fifth Third Bank

The number of people and processes involved in the financial close increases the likelihood of high-stakes inaccuracies. And the penalty for mistakes is high. A corporate officer who submits an inaccurate certification (even if done mistakenly) can be subject to seven-figure fines and 10 years in prison.

> "With Frontier™ Reconciliation from Fiserv, we are able to maintain clear segregation of duties. This means our reconcilers aren't able to update ledger data or clear their own balances, which acts as a protection against fraud."
>
> **Daniel Cilar**
> Financial Accounting Manager
> Capital City Bank

The Value of Automated Reconciliation

An automated reconciliation and certification solution can help meet regulatory internal control requirements for financial institutions of any size. Shifting from a manual to an automated solution minimizes the risk of financial misstatement and errors at financial close and provides financial institutions with a full audit trail.

It also significantly saves time. Fully automated workflows import data from general ledger systems, bank files and statements, replacing the cumbersome process of collecting external materials from multiple sources. The need for manual intervention is nearly eliminated.

Data is automatically loaded into the system each night, minimizing opportunities for mistakes or fraud. Once imported, a multithreaded matching engine automatically syncs as many transactions as possible and flags transactions that don't match. Workflows

> "Auditors love the transparency and audit trails of Frontier Reconciliation."
>
> **Daniel Cilar**
> Financial Accounting Manager
> Capital City Bank

Internal Control Requirements for Financial Institutions

Under FDIC regulations, internal control reporting requirements must grow along with an institution.

Financial institutions with $500 million to $1 billion in assets must:

- Have an external audit program that conforms to the audit and reporting requirements of Part 363 of the FDIC rules and regulations. They must:
  - Prepare annual financial statements
  - Produce annual reports detailing management's responsibilities and assessing compliance with laws and regulations
  - Provide appropriate report signatures
- Prepare financial statements in accordance with GAAP and allow them to be audited by an independent public accountant

Those with $1 billion or more in assets must:

- Assess the effectiveness of the institution's internal control system and include statements that:
  - Identify an internal control framework
  - Indicate what controls were considered during the assessment
  - Disclose any material weaknesses in internal controls
- Obtain sign-off from the CEO, CAO or CFO

can fully automate labor-intensive processes, and automated checks ensure compliance with corporate and regulatory controls.

Having a complete reconciliation picture means that transaction-level details and exceptions are instantly visible – and facilitates your institution's compliance with internal policies, and applicable laws and regulations. Automated reconciliation helps financial institutions:

- **Assess** material misstatement risks
- **Identify** where misstatements could arise in a transaction flow
- **Evaluate** controls for the period-end financial reporting process
- **Follow** internal policies and meet their obligations under applicable laws and regulations
- **Provide** timely, accurate reporting in financial, operational and regulatory areas
- **Examine** fraud risks
- **Safeguard** assets
- **Analyze and report** on internal control effectiveness, including deficiencies or weaknesses

A comprehensive, end-to-end reconciliation and certification solution can become an integral part of an internal control framework for financial institutions. Financial institutions that are proactive about keeping pace with automation can increase efficiency, accuracy, and data transparency and position their organizations for future growth.

> "Frontier Reconciliation enables us to take a better look at our reconcilements at month-end because it locks in everything at that point in time – unlike Excel, where somebody can go in and change it."
>
> **Wade Bruendl**
> SVP and Chief Strategy Officer
> Meritrust Credit Union

Connect With Us

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