

State Leadership Accountability Act



Ongoing Monitoring General Framework and Guidelines

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Introduction

The State Leadership Accountability Act (SLAA)¹ was enacted to reduce the waste of resources and strengthen internal controls. SLAA requires each state agency² to maintain effective systems of internal control, to evaluate the effectiveness of those controls on an ongoing basis, and to biennially review and prepare a report on the adequacy of the internal control system. SLAA also calls for state agencies to establish an ongoing internal control monitoring system to ensure a satisfactory system of internal control is maintained.

Internal controls are methods and procedures established to provide reasonable assurance an agency will achieve its objectives and mission. This includes program, operational, and administrative areas. Internal control covers all aspects of agency objectives: operations, reporting, and compliance. Ongoing internal monitoring relates to activities that monitor the effectiveness of internal controls in the ordinary course of agency operations or through separate evaluations at regular intervals. Monitoring may include regular management and supervisory activities, comparisons, reconciliations, and other routine actions. State agency heads are responsible for the establishment and maintenance of their agency's internal control system and effective, objective ongoing monitoring of the system.³ The five components of internal control are: control environment, risk assessment, control activities, information and communication, and monitoring.

Some of the concepts and principles included in the *Ongoing Monitoring General Framework and Guidelines* are adapted from other internal control and auditing publications. These publications provide detailed guidance on developing efficient and effective internal control systems and monitoring these systems. They are widely used and accepted in government and private industries. The publications are:

- *Standards for Internal Control in the Federal Government* (known as the *Green Book*)⁴
 - Issued by the Comptroller General of the United States, the *Green Book* provides government managers criteria for designing, implementing, and operating effective internal control systems. The *Green Book* may be adopted by federal, state, local, and quasi-governmental entities as a framework for internal control systems.
- *Internal Control – Integrated Framework*⁵
 - Issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), the framework enables organizations to effectively and efficiently develop internal control systems.
- *International Standards for the Professional Practice of Internal Auditing*⁶
 - Issued by the International Internal Audit Standards Board, these standards provide a framework for performing and promoting internal auditing and evaluations.

¹ Government Code sections 13400 through 13407.

² The use of "agency" throughout this document refers to any State of California agency, department, commission, board, or any other state government organization subject to the requirements of SLAA.

³ Government Code section 13402.

⁴ Visit <http://www.gao.gov/greenbook/overview> to download a free copy of the *Green Book*.

⁵ Visit <http://www.coso.org/IC.htm> for information on purchasing a copy of the *Internal Control – Integrated Framework*.

⁶ Visit <https://na.theiia.org/standards-guidance/mandatory-guidance/Pages/Standards.aspx> to download a free copy of the *International Standards for the Professional Practice of Internal Auditing*.

The *Ongoing Monitoring General Framework and Guidelines*, developed by the California Department of Finance (Finance), provides recommended practices for State of California government agencies to use when developing and monitoring internal control systems. Finance consulted with a sample of agencies through focus groups when developing the *Ongoing Monitoring General Framework and Guidelines* for input and applicability of the suggested practices. Agencies may have existing monitoring practices or systems in place. This document offers additional recommended practices and guidance to assist agencies in developing well-rounded monitoring efforts. This document also clarifies that **management** is ultimately responsible for the design, implementation, and monitoring of internal controls within their organizations. These practices are intended to be flexible, allowing agencies to adapt and implement based on available resources and business needs. The *Ongoing Monitoring General Framework and Guidelines* is structured as follows:

- I. **Monitoring General Framework:** Presents an overview of recommended practices to guide agencies in conducting active, ongoing monitoring of internal control processes.
- II. **Monitoring Organizational Structure and Responsibilities:** Describes the internal chain-of-command reporting structure for agency monitoring functions, roles and responsibilities of those tasked with monitoring, and training opportunities related to monitoring.
- III. **Documenting and Reporting Monitoring Activities:** Describes how monitoring systems should be documented, and how results should be reported to relevant parties.

A component of complying with SLAA includes agencies preparing and submitting a biennial SLAA report. To substantiate the monitoring efforts adopted, agencies are required to submit documentation of their monitoring system to Finance by December 31 of each odd numbered year with their routine SLAA report. Finance may request additional supporting documentation or information regarding monitoring practices in future SLAA cycles.

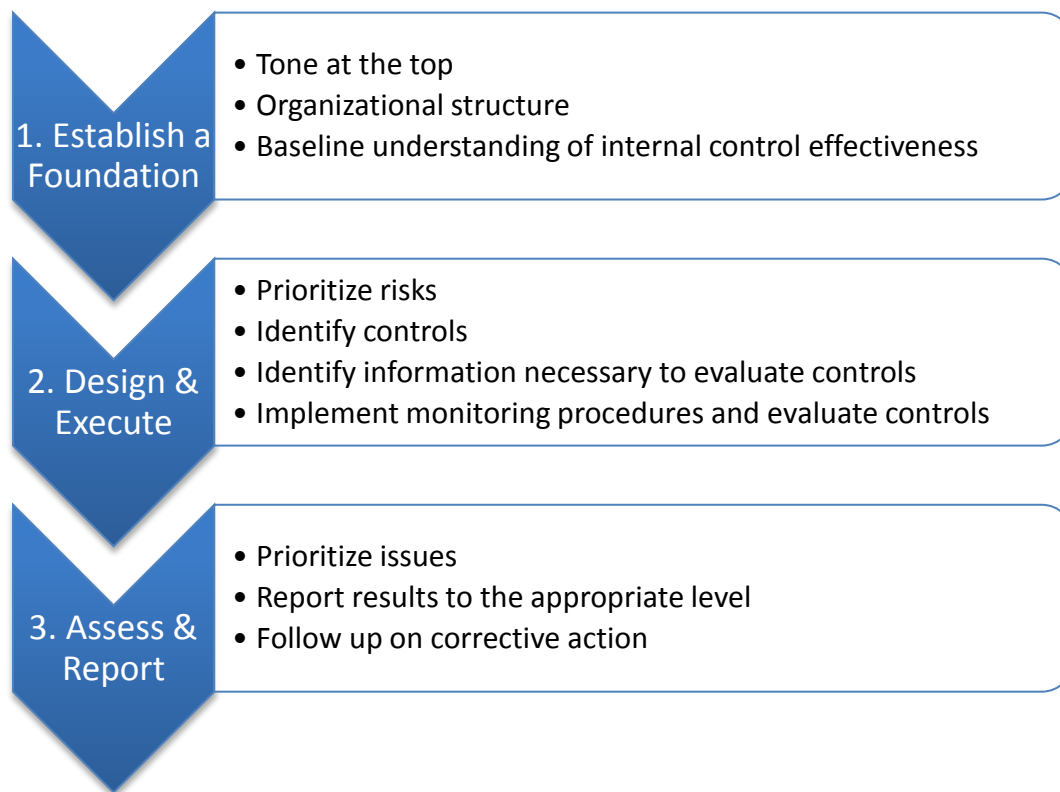
Finance updates the *Ongoing Monitoring General Framework and Guidelines* as new resources, best practices, and guidance related to internal control arise. Updated versions, as they become available, are posted to Finance's website at <http://www.dof.ca.gov/Programs/OSAE/SLAA/>.

We appreciate the assistance of the focus group agencies during the development of the *Ongoing Monitoring General Framework and Guidelines*. If you have any questions regarding this document, please email the SLAA hotline at SLAAhotline@dof.ca.gov.

I. Monitoring General Framework

Internal control is a dynamic process that should be adapted continually to the risks and changes agencies face. Monitoring the internal control system is essential in helping internal control remain aligned with changing objectives, environments, laws, resources, and risks. An effective approach to monitoring involves (1) establishing a foundation for monitoring, (2) designing and executing monitoring procedures, and (3) assessing and reporting the results. This monitoring framework is displayed in Figure 1.

Figure 1: The Monitoring General Framework⁷



A. Establish a Foundation for Monitoring

To effectively monitor internal control systems, agencies should establish a foundation for monitoring. This includes developing a tone at the top emphasizing the importance of internal controls and monitoring, establishing an organizational structure that facilitates the roles of those charged with monitoring, and using a baseline understanding of the effectiveness of existing internal controls.

⁷ Adapted from the Committee of Sponsoring Organizations of the Treadway Commission's *Internal Control – Integrated Framework (COSO)*.

Tone at the Top

Management should cultivate tone at the top reflecting their understanding of the importance of internal controls and monitoring. Management should lead by example, demonstrating the agency's values, philosophy, and operating style. Tone at the top may also be communicated in the form of an agency strategic plan.

Without a strong tone at the top, the results of monitoring may not be understood or acted upon to remediate deficiencies. In larger agencies, the various layers of management in the organizational structure may also set "tone in the middle."⁸

Organizational Structure

Agency heads and management should structure the monitoring function within their agencies to facilitate effective, objective monitoring of their internal control systems. A recommended organizational structure to facilitate monitoring internal controls is presented in Figure 3: Monitoring Organizational Structure, located in section II: Monitoring Organizational Structure and Responsibilities.

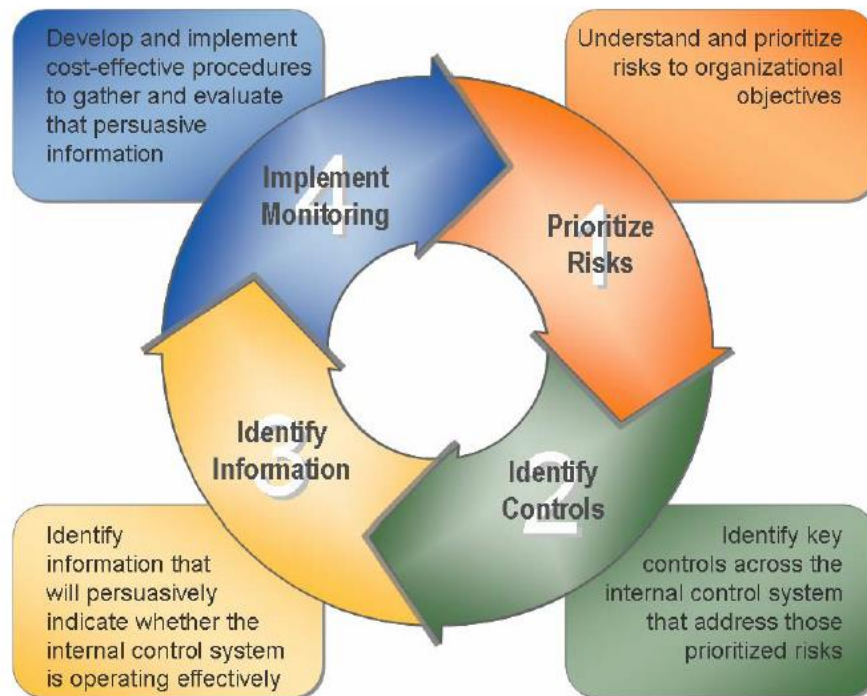
Baseline Understanding of Internal Control Effectiveness

Management should establish a baseline to monitor the internal control system. The baseline is the current state of the internal control system compared against management's design of the internal control system, i.e. the reality of internal controls compared to the planned internal controls. Once identified, the baseline understanding of internal control can be the starting point for applying monitoring procedures. For example, an agency's most recent risk assessment results could be used to identify internal control baseline understanding.

B. Design and Execute Monitoring Procedures

Monitoring is a continuous, evolving process. It should assess the quality of the internal control system's performance over time. Management monitors the internal control system through ongoing monitoring and separate evaluations. During monitoring, each of the five components of internal control should be evaluated to determine the effectiveness, efficiency, and continued applicability of the system. The five components of internal control are: control environment, risk assessment, control activities, information and communication, and monitoring. Monitoring efforts can be designed and executed by performing the tasks depicted in Figure 2 and explained as follows:

⁸ *Standards for Internal Control in the Federal Government (Green Book)*, paragraphs 1.02 through 1.05.

Figure 2: Monitoring Design and Implementation Progression⁹

1. *Prioritize Risks:* Management should understand and prioritize risks identified through its regular internal control risk assessment process to ensure relevant risks are addressed.
2. *Identify controls:* Key controls addressing the meaningful risks should be identified. Management's baseline understanding of controls can be used as a reference for an agency's internal control activities.
3. *Identify information necessary to evaluate controls:* Determine what reliable and relevant sources exist to evaluate the key controls. Develop a plan for evaluating the efficiency and effectiveness of key controls using the identified information.
4. *Implement monitoring procedures and evaluate controls:* Implement the plan and evaluate key controls. Determine if controls are operating as intended and effectively mitigate the prioritized risks.

Monitoring takes on two forms: ongoing monitoring and separate evaluations. Ongoing monitoring is built into agency operations, performed continually, and reacts to changing conditions. Ongoing monitoring is part of the normal course of operations and program implementation. Ongoing monitoring can occur through the current implementation of internal controls such as regular management and supervisory activities, comparisons, reconciliations, and other routine actions.

Separate evaluations can be used periodically and can provide formalized feedback on the effectiveness of the internal control system. Evaluations can take the form of self-assessments conducted by agency management and facilitated by executive monitoring sponsor(s).¹⁰ The

⁹ Adapted from COSO's *Internal Control – Integrated Framework*.

¹⁰ For additional description of the executive monitoring sponsor role, see section II: Monitoring Organizational Structure and Responsibilities.

scope and frequency of these evaluations will depend on agency size, complexity of operations, and needs. Management and the executive monitoring sponsor should work together to determine the scope and frequency of the evaluations necessary for their agency. Separate evaluation may also be performed by internal and external auditors, inspectors, and other external parties.

Additionally, management is responsible for monitoring the internal controls of service providers. A service provider is an organization performing certain operational processes for the agency, such as accounting and payroll processing, security services, or IT services. Monitoring efforts provide reasonable assurances regarding the effectiveness of the internal controls over the processes performed by the service provider. Monitoring activities can include management review of reports by external parties such as the service provider's external auditors.

COSO issues tools in the form of spreadsheets for assessing the effectiveness of internal control systems. The tools focus on each of the five components of internal control and different principles within each component. The document can be used to summarize and organize the results of monitoring in order to conclude if controls are present and functioning. The tools can be downloaded at www.cpa2biz.com/COSOEvalTools.

C. Assess and Report Results

Using the results of ongoing monitoring and separate evaluations, management can assess the effectiveness of the internal control system and identify issues. Management should prioritize issues so that significant internal control deficiencies are remedied on a timely basis.

The results of monitoring activities, including resulting changes in the internal control system, should be documented in a form consistent with the agency's needs. If monitoring activities are performed by individuals other than agency management, issues and results should be documented and communicated to management on a regular basis.

Corrective actions should be documented and implemented on a timely basis. Corrective actions refer to remediating issues identified during monitoring, as well as resolving outstanding audit findings.

The results of monitoring should be reported to Finance in accordance with the SLAA reporting requirements described in section III: Documenting and Reporting Monitoring Activities.

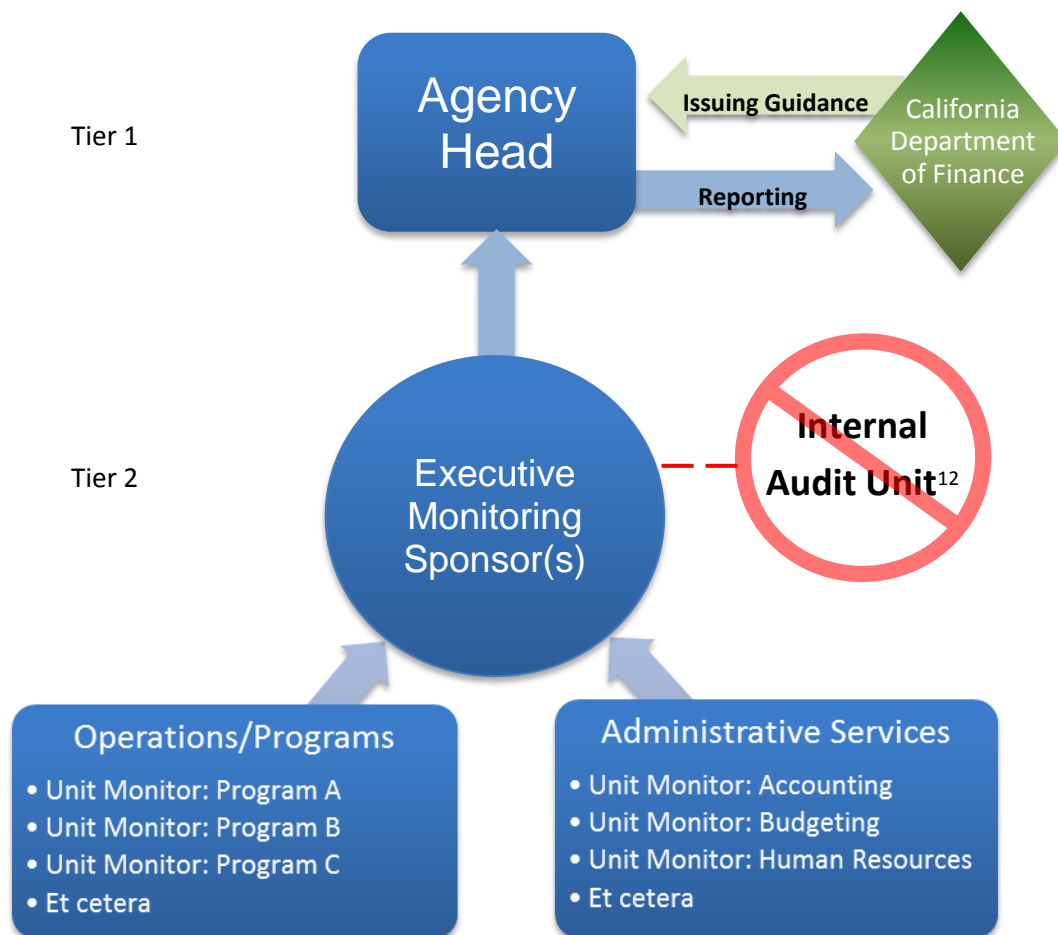
II. Monitoring Organizational Structure and Responsibilities

This section describes agency monitoring organizational structures, the roles and responsibilities of those tasked with monitoring, and professional development and training opportunities for monitors.

A. Monitoring Organizational Structure

The recommended monitoring organizational structure presented in Figure 3 is a three tiered structure emphasizing the following key concepts: (1) all levels of management must be involved in assessing and strengthening internal control systems,¹¹ (2) an executive monitoring sponsor should be assigned to facilitate the monitoring function,¹² and (3) unit monitors help ensure monitoring is thorough and implemented throughout the agency.

Figure 3: Monitoring Organizational Structure



¹¹ Government Code section 13401, subdivision (b)(3) states all levels of management of state agencies must be involved in assessing and strengthening internal control systems.

¹² The executive monitoring sponsor is a member of an agency's executive management team; it is **not** a member of the internal audit unit of an organization. Internal auditors can assist with testing of controls, but management must retain the responsibility for monitoring of internal controls.

B. Monitoring Roles and Responsibilities

Tier 1: Agency Head

Agency heads are ultimately responsible for effective and objective ongoing monitoring of their agency's internal control system and reporting such information to Finance and other control agencies.¹³ The agency head should implement a monitoring framework appropriate for the agency and establish the necessary lines of communication and reporting. The agency head should empower the executive monitoring sponsor and unit monitors to facilitate effective assessments of internal controls throughout the organization. Although responsibility for internal control ultimately resides with management, empowering dedicated roles throughout the agency enables thorough and timely monitoring to occur.

All levels of management must be involved in assessing and strengthening systems of internal control within their agencies.¹⁴ This responsibility resides with management because they are in control of establishing the tone for the agency's ethical values and integrity, internal controls, and the monitoring system.

Tier 2: Executive Monitoring Sponsor(s)

Effective systems of internal control can empower all agency employees with a duty to safeguard state assets and monitor activities as they apply to their job classifications. However, certain employees should be assigned the role of executive monitoring sponsor. The executive monitoring sponsors are responsible for facilitating and verifying the agency's internal control monitoring practices. To ensure essential practices are performed by these employees, specific job titles or duties should include their monitoring duties.

Executive monitoring sponsors should be objective and unbiased when performing their responsibilities. Objectivity is a type of judgment allowing individuals to maintain an attitude of impartiality, integrity, and a questioning state of mind. Objective individuals can assess situations or circumstances and draw comprehensive conclusions while disclosing all material facts and timely reporting the activities under review.¹⁵ To help maintain their objective attitude, executive monitoring sponsors should not be directly involved in the direct day to day decision making and operations within agency administrative or program units. If this is not feasible, executive monitoring sponsors should assign an alternative individual to reduce the need for the executive monitoring sponsor to evaluate his or her own unit.

Executive monitoring sponsors should possess integrity, strong analytical abilities, good communication skills, and flexibility. The number of executive monitoring sponsors may vary based on the needs of each agency. The executive monitoring sponsor is responsible for:

- Carrying out job functions in an objective, unbiased manner.
- Attending training to develop competence and understanding of internal control and monitoring activities.
- Distributing training materials and advising unit monitor employees on monitoring processes and activities.
- Working with agency management to implement agency-wide monitoring of internal control systems, such as the monitoring general framework.

¹³ Government Code section 13402 states agency heads are responsible for the establishment and maintenance of internal control systems and section 13405 describes the SLAA reporting requirements.

¹⁴ Government Code section 13401, subdivision (b)(3).

¹⁵ Adapted from the *International Standards for the Professional Practice of Internal Auditing*.

- Collecting information about monitoring practices from unit monitors.
- Working with agency management to document the agency's monitoring structure and practices.
- Documenting and summarizing the results of monitoring activities.
- Reporting regularly to the agency head.

Executive monitoring sponsors should be from the agency's executive management team. It is a common misconception that internal auditors are responsible for monitoring of internal control systems. SLAA distinctly states **management** is responsible for the monitoring of internal controls. Internal audit staff may be used to facilitate monitoring activities; however, responsibility for internal control monitoring should not be delegated to internal auditors and must remain with management.

The following table provides an example of candidates that may be assigned the role as executive monitoring sponsor. This list serves as an example only. It is not all-inclusive of potential positions for executive monitoring sponsors. The most prudent positions for consideration would be members of an agency's executive management team. As mentioned previously, the number of executive monitoring sponsors will depend on the size and needs of each agency. Positions not recommended include auditing positions, employees who are not members of executive management, and employees responsible for the day-to-day running of organizational operations.

Table 1: Examples of Candidates for the Executive Monitoring Sponsor Role

Recommended	Not Recommended
Executive Director ¹⁶	Chief of Internal Audits
Executive Officer	Internal Audit Manager
Director	Internal Auditor
Chief Deputy Commissioner	Auditor
Chief Financial Officer	Investigator
Chief Deputy Director	Accounting Chief
Chief Operating Officer	Fiscal Manager
Chief of Staff	Staff Services Manager
Undersecretary	Associate Governmental Program Analyst
Deputy Executive Director	Staff Services Analyst
Deputy Executive Officer	Executive Assistant
Deputy Director	Research Analyst
Deputy Commissioner	Budget Analyst
Deputy Secretary	Staff Attorney
Assistant Secretary	
Assistant Director	
Organizational Accountability Officer	
Chief Counsel	

To facilitate information sharing and oversight of internal controls and emerging risks, executive monitoring sponsors should have regular communication with key members of the agency's management team. Depending on the agency's organizational structure, monitors may communicate to executives, management sub-groups, an oversight committee, or an audit committee. Monitors may attend management meetings, and should have opportunities to meet with management on a one-on-one basis, if necessary.

¹⁶ Due to the size and number of employees in smaller organizations, individuals in an agency-head role such as Executive Director or Director may need to fill the role of executive monitoring sponsors, if no other members of the executive management team are available.

Communication between monitors and management should be relevant, reliable, and timely. Information communicated should include, but not be limited to:

- Summary of monitoring activities performed, including any limitations encountered.
- Results of monitoring activities.
- Potential risks identified by monitors or management, including fraud risks, and emerging risks or changing conditions.
- Suggested or planned actions to respond to identified weaknesses.
- Recent updates to statewide SLAA processes and best practices.

Executive monitoring sponsors should have access to previous SLAA reports and supporting documentation including risk assessments, agency policies and procedures, and other relevant documents necessary for effective and efficient monitoring. Sponsors should have the appropriate authority to communicate freely with agency employees, and perform or facilitate tasks related to monitoring within the various agency units.

Tier 3: Unit Monitors

Unit monitors are management or similar-level designated employees throughout the agency's program and administrative units. The quantity and job classifications of unit monitors will depend on an agency's size and organizational structure. Unit monitor duties may be in addition to other assigned duties related to their respective unit. Unit monitors are not objective in assessing internal control if they are involved in the day-to-day operations related to their unit.

Unit monitors are knowledgeable about their unit's routine programmatic and/or administrative operations and the implementation of the related internal controls. Unit monitors may perform evaluations and tests of controls based on identified risk areas or as directed by the executive monitoring sponsor. Monitoring results should be reported to the executive monitoring sponsor.

C. Professional Development and Training of Monitors

Finance provides training to agency heads and executive monitoring sponsors about monitoring internal control systems. Executive monitoring sponsors are responsible for disseminating information and guidance obtained from training to the unit monitors. For more information on SLAA training opportunities, visit Finance's SLAA webpage at <http://www.dof.ca.gov/Programs/OSAE/SLAA/>.

Specific training topics include:

- 1) Review of the SLAA process, highlighting updates to the SLAA reporting and monitoring process in recent years.
- 2) In-depth discussion of the monitoring general framework.
- 3) Monitoring organizational structure, roles and responsibilities, and reporting requirements.

In addition to providing training on the monitoring framework, Finance holds meetings on various SLAA topics, such as monitoring strategies. These meetings include discussions on successful strategies for implementing and monitoring effective internal control systems, knowledgeable guest speakers, and topics as they relate to emerging issues and risks. For more information on SLAA meetings, visit Finance's SLAA webpage.

Written guidance and best practices related to monitoring and internal control as well as strategies and lessons learned from successful efforts to strengthen state administration are readily available to agencies on Finance's SLAA webpage.

III. Documenting and Reporting Monitoring Activities

As depicted in Figure 3 in section II: Monitoring Organizational Structure and Responsibilities, the results of monitoring activities can be communicated vertically throughout an agency, from unit monitors to executive monitoring sponsors, and ultimately to the agency head. Status of the agency's internal controls and monitoring efforts can be communicated formally, informally, and on a frequency consistent with the agency's needs.

An agency's monitoring system should be documented and approved by agency management. Documenting the system should include, but not be limited to, the following concepts:

- The individuals responsible for performing monitoring functions.
- The frequency of monitoring activities.
- How monitoring results will be documented.¹⁷
- Where monitoring results will be documented.
- How monitoring results will be communicated within the agency.
- Procedures for addressing identified internal control deficiencies.

Reporting to the California Department of Finance

Another component of reporting on an agency's internal control system is through Finance's mandatory biennial SLAA reporting. Agencies are required to submit documentation of their monitoring practices to Finance by December 31 of each odd numbered year to substantiate the monitoring efforts adopted. Although monitoring is the responsibility of agency management, Finance will review submitted monitoring efforts documented to confirm (1) a process has been adopted, (2) management is engaged in the process, and (3) the process has been documented. Finance may request additional supporting documentation or information regarding monitoring systems in future SLAA cycles.

Information about agency ongoing monitoring is captured in the SLAA online portal report in a dedicated section titled, "Ongoing Monitoring."¹⁸ The required components included in the monitoring section of the SLAA report are shown below.

SLAA Report—Ongoing Monitoring Section

As the head of the Entity, *Agency Head Name, Title*, is responsible for the overall establishment and maintenance of the internal control and monitoring systems.

The executive monitoring sponsor responsibilities include facilitating and verifying that the Entity internal control monitoring practices are implemented and functioning as intended. The responsibilities as the executive monitoring sponsor(s) have been given to: *Selected Name, Title, and Selected Name, Title (as applicable)*.

¹⁷ Some examples include: regular management meetings (standing agenda item), meeting minutes, reports, written policies and procedures, note to file, e-mail notification, office newsletters, site visit, ride-a-long, surprise inspection, grant application criteria, all staff meeting, training plans, employee evaluations, individual development plans, risk assessment matrix, program review checklists, formal reconciliation documents, routing-signoff forms, project scoring criteria template, compliance summaries, questionnaires, budget detail worksheets, monitoring report template, strategic planning documents.

¹⁸ For additional information on SLAA reporting requirements, see the Finance SLAA webpage located at <http://www.dof.ca.gov/Programs/OSAE/SLAA>.

Monitoring Activities

Describe the process(es) used entity-wide to ensure the effectiveness of internal control systems.

Must include:

- Confirming effectiveness of internal control systems using:
 - Routine activities to identify potential problems (e.g., tracking key performance indicators, meetings, and reconciliations)
 - Periodic detailed reviews, which are best performed by:
 - Knowledgeable staff not directly involved with day to day operation of the control system under review
 - Internal or external reviewers
- Comparison of results to expectations and determination if change is needed

Addressing Vulnerabilities

Describe the process(es) used to respond to vulnerabilities as they are identified.

Must include:

- Overview of process to assign responsibility for action
- Monitoring of progress to reduce the identified vulnerability(ies)

Communication

Describe how monitoring roles, activities, and results are communicated entity-wide.

Must include:

- Monitoring roles defined, explained, and documented (e.g., Duty statements, policies and procedures, and organizational charts of responsibility)
- Channels for communicating vulnerabilities and control inefficiencies as they are identified, throughout the organization including:
 - Up and down and between staff to management
 - Across organizational lines
- Methods for communicating monitoring activities and results

Ongoing Monitoring Compliance

The report includes an overall compliance statement. The responses in the previous sections determine the overall compliance status. The portal automatically determines the entity's status. The compliance statement reads as follows:

The Entity *has implemented and documented, or is in the process of implementing and documenting, or has not begun the process of implementing and documenting* the ongoing monitoring processes as outlined in the monitoring requirements of Government Code sections 13400-13407. These processes include reviews, evaluations, and improvements to the Entity's systems controls and monitoring.

Appendix A: Examples of Applying Separate Evaluations to Risk Areas

The following table demonstrates examples of how separate evaluations could be applied to different prioritized risk areas. The prioritized risk areas serve as simplified examples only; each agency should have risk areas applicable to their operations and prioritized by management based on risk. In the examples below, the executive monitoring sponsor (Sponsor) verifies the controls are working as intended, and may identify areas where corrective action is needed.

1) Prioritized Risk Area	2) Controls Identified	3) Information Necessary to Evaluate Controls	4) Monitoring Procedures, Control Evaluation
Stakeholder Outreach	Newly eligible stakeholders are identified through monthly campus visits, and are subsequently contacted via email.	Monthly campus visit summary reports list newly identified stakeholder contact information. Email distribution lists contain stakeholder contact information and correspondence history.	The Sponsor confirms monthly campus visit occurrence, obtains a sample of summary reports, and confirms new stakeholders are added to the email distribution lists. The Sponsor identifies changes in stakeholder outreach that may have occurred or are needed.
Program Implementation	The agency hires competent, qualified individuals in program analyst and supervisor roles.	Hiring documentation and performance evaluation reports.	The Sponsor evaluates whether the knowledge and abilities of analysts and supervisors are commensurate with the requirements of their positions, and identifies trends in performance issues to recommend training programs for employees. The Sponsor identifies changes in hiring and evaluation efforts that may have occurred or are needed.
Accounts Payable	Periodic reconciliations between the general ledger and subsidiary ledger occur to identify recording errors.	Reconciliation documentation indicates comparisons were made and errors are timely corrected.	The Sponsor inspects reconciliation documentation to confirm occurrence and identifies trends in the nature and/or volume of errors. The Sponsor identifies changes in reconciliation procedures that may have occurred or are needed.