(Unofficial translation)

POLICY STATEMENT ON INTERNAL CONTROL

I- Background and Objective

The Law on Audit No CS/RKM/0300/10 dated 3rd March 2000 and the Internal Audit Sub Decree No. 40 ANK.BK dated 15th July, 2005, require all ministries and state organisations to take full responsibility for establishing internal control and internal auditing systems within their respective organisations.

This policy statement has been developed to assist all public sector institutions and enterprises and ministries to assess and improve their internal control and internal audit operations. Senior management as well as internal auditors need to pursue this policy and have a greater understanding of internal control as a key management function to improve public sector accountability and administration.

This policy paper attempts to provide guidelines of the basic features of internal control that must be maintained in each organisation. Flowing from this policy statement the Ministry of Finance and Economy intends to separately issue a more detailed accounting and internal control regulation that will cover the specific control procedures and accounting requirements that each ministry and organisation must follow. The MEF will also provide ongoing technical assistance and training to the ministries and state organisations over the coming years to ensure that the policies, procedures and regulations relating to accounting, internal control and internal audit are being properly implemented and enforced.

II- Statement of Policy

It is the policy of the Royal Government of Cambodia that management of all ministries and public sector enterprises establish and maintain systems of internal control that are designed to ensure, as far as it is practical, that the objectives of the organisation are achieved and comply with all applicable law.

III- Definition of internal control

Internal control is the composite total of all organisational and operating plans, systems, policies, procedures, and practices, as well as the attitudes and behaviour of executive management and other employees, occurring within the organisation and established by executive management, to achieve the basic objective of ensuring the disciplined and efficient conduct of the organisation's activities and operations in general, and specifically:

(a) To assure the organisation's assets are accounted for and safeguarded from losses of all kinds

(b) To assure the accuracy and reliability of accounting and financial, operational and statistical information generated within the organisation, and to assure the integrity of resulting financial reports produced for internal and external use

(c) To promote operating efficiency in all activities undertaken, and

(d) To inform and ensure adherence by all employees in the organisation to prescribed laws, regulations, policies, procedures, plans and instructions

Internal controls are therefore mechanisms that provide assurance that financial records are accurate, that resources are efficiently used and adequately protected, risks are managed, laws are complied with and that objectives are achieved.

Internal auditing is part of the internal control system. It is a control tool that functions by independently measuring and evaluating the adequacy and effectiveness of all the other controls.

IV- Types of internal control

Internal controls can be of three types:
(a) Accounting controls
(b) Administrative controls, and
(c) Operating controls

(a) Accounting controls deal with capturing, processing, accumulating, and reporting daily financial transactions. They minimise the chance for errors or fraud and ensure the accuracy of information. Examples of accounting controls are proper segregation of duties, independent verifications, and an appropriate system of authorization and/or approval.

(b) Administrative controls are a higher level of management control. They inform management personnel about the performance of activities under their responsibility. Examples of administrative controls are organisation structure, procedures, and performance reporting to management such as budgets and other comparisons of results with objectives to enable feedback, analysis and corrective action.

(c) Operating controls are those controls related to non financial activities undertaken by non managerial staff. These are controls that are built into the operating/manufacturing processes to ensure goods are produced or services delivered in an effective and efficient manner.

V- Application of Policy

As guidance to management, the following features of internal control are considered to be essential and should be implemented in the operations conducted by each ministry and state enterprise:

1. Compliance with the applicable code of conduct for employees/officers
2. Trustworthy personnel with the ability, training and experience required to perform satisfactorily
the responsibilities assigned to them
3. A plan of organisation with proper regard to the segregation of incompatible functions
4. Written delegations of authority with proper segregation of duties so that no one person is fully in
charge of all aspects of a transaction. Segregation of duties involves assigning different people the responsibilities of authorizing transactions, recording transactions, and maintaining custody
of assets with a view to reducing the opportunities to allow any person to be in a position to both perpetrate and conceal errors or fraud in the normal course of the person's duties.
5. An adequate accounting structure at each operating unit including financial, budgetary and cost

accounting techniques, a chart of accounts, and where applicable, charts depicting the flow of
transactions.

6. Procedures for controlling commitments, procurement, ordering, receiving and authorisation of
transactions.

7. Procedures for capturing, recording, classifying, verifying and reconciling transactions in the accounting system. Accounting controls should be designed to achieve five basic objectives:
(i) Validation- the examination of documentation, by someone with an understanding of the accounting system, for evidence that a recorded transaction actually took place in accordance with prescribed procedures **(ii)** Accuracy- the accuracy of amounts and account classifications is achieved by establishing control tasks to check calculations, extensions, additions, and account classifications **(iii)** Completeness- the objective of completeness controls is to ensures that all transactions are initially recorded on a control document and accepted for processing once and once only. This is achieved by either sequentially numbering all documents or by preparing control totals for comparison before and after processing **(iv)** Maintenance- the objective of the maintenance controls is to monitor accounting records after the entry of transactions to ensure that they continue to reflect accurately the operations of the business. The control system should provide systematic responses to errors when they occur, to changed conditions, and to new types of transactions **(v)** Physical security- it is important that all assets are adequately protected. Physical security of assets requires that access to assets and accounting records is limited to authorised personnel through the use of physical controls

8. Procedures for ensuring compliance with the applicable financial laws and regulations relating to revenues, expenditures, assets and liabilities. Where revenue is due, a sales invoice must be raised promptly at the time the amount is due and recorded as a debtor. Accounts receivable records should be accurate, complete, and maintained in a manner to indicate the length of time the debt has been outstanding. Procedures to follow up collection of old debtors should be in place.

9. Detailed listings of all assets and liabilities including fixed assets, cash, bank balances, investments, debtors, inventories, loans and creditors. Control should be maintained to ensure that all assets exist and are in use for operations.

10. Disposal of fixed assets should occur only after proper authorization has been given. Controls should ensure that the best possible terms are received for disposal.

11. Transactions should be recorded in reasonable detail with promptness and accuracy

12. Thorough review in the preparation of financial statements and other financial information

13. Procedures for managing and administering contracts and agreements

14. Regular monitoring by central, provincial, executive and departmental management

15. Review of the organisation's systems and controls by an extensive program of audits by the internal audit staff and external auditors

VI- Criteria for exemption

No exemptions are to be granted to ministries from establishing an internal audit function. However the Ministry of Economy and Finance will have responsibility for considering applications for exemption from establishing internal audit for certain institutions and state enterprises. In considering such applications, the following will be considered:

- The ability of the chief executive to ensure that proper internal control is maintained without the need for a separate internal audit function.
- The size of the institution or state enterprise taking into account the number of employees, the nature and value of assets managed and the agency's cash flows

- The nature of the risk profile of the institution or state enterprise, and
- Community interest

VII- Responsibility and Authority

The Secretary of State, Undersecretary of State, Secretary General, Deputy Secretary General, Director General or other equivalent executive positions and Directors of each operating department in the institutions, ministries and state enterprises have the prime responsibility for establishing and maintaining the organisation's internal control systems. In the provinces, the Governor of each province has the prime responsibility for establishing and maintaining the internal control systems. In the communes, the commune council is responsible for internal control.

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