Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In my last article, I made mention of the Committee of Sponsoring Organization (COSO) publication on "Internal Control Integrated Framework" which is the internal control framework widely adopted worldwide. The publication, which was adopted by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and was subsequently published in 1992, has been widely adopted by organizations around the world. The framework provides a comprehensive set of guidelines and principles for the effective design and implementation of internal controls. It is designed to help organizations achieve their objectives by providing assurance regarding the effectiveness and efficiency of their internal controls. The framework also helps organizations to comply with regulatory requirements and to improve the reliability of their financial reporting.

A disposal group is a group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction and liabilities directly associated with those assets that will be transferred in the transaction. A disposal group may be a group of cash-generating units, a single cash-generating unit or part of a cash-generating unit.

1) Identify the acquirer
2) Determine the acquisition date
3) Recognise and measure the identifiable assets acquired (including inherent intangible assets not recognized in the books of acquiree nor considered as part of goodwill), the liabilities (including contingent liabilities not in the books of the acquiree) assumed and any non-controlling interests
4) Measure the consideration transferred, yet to be transferred, considerations contingent on the future happenings and determination of other compensation arrangements that constitute part of the business combination
5) Recognise and measure goodwill or gain from a bargain purchase

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COSO: An Approach to Internal Control Framework

The importance of Internal Control in the Operations and Financial Reporting of an entity cannot be over-emphasized as the existence or the absence of the process determines the quality of output produced in the Financial Statements.

The COSO Integrated Framework for Internal Control has five components which include:

1. Control Environment: The control environment sets the tone for the internal control across the organization. The board of directors and senior management establish the tone at the top regarding the importance of internal control including expected standards of conduct. Management reinforces expectations at the various levels of the organization. The control environment comprises the integrity and ethical values of the organization. The parameters enabling the board of directors to carry out its governance oversight responsibilities, the organizational structure and assignment of authority and responsibility, the processes for attracting, developing, and retaining competent individuals; and the rigor around performance measures, incentives, and rewards to drive accountability for performance. The resulting control environment has a pervasive impact on the overall system of internal control.

2. Risk Assessment: Every entity faces a variety of risks from external and internal sources. Risk is defined as the possibility that an event will occur and adversely affect the achievement of objectives. Risk assessment involves a dynamic and iterative process for identifying and assessing the risks of achievement of objectives. Risks to the achievement of these objectives from across the entity are considered relative to established risk tolerances. Thus, risk assessment forms the basis for determining how risks will be managed.

A precondition to risk assessment is the establishment of objectives linked at different levels of the entity. Management specifies objectives within categories relating to operations, reporting, and compliance with sufficient clarity to be able to identify and analyze risks to those objectives. Management also considers the suitability of the objectives for the entity. Risk assessment also requires management to consider the impact of possible changes in the external environment and within its own business model that may render internal control ineffective.

3. Control Activities: Control activities are the actions established through policies and procedures that help ensure that management’s directives to mitigate risks to the achievement of objectives are carried out. Control activities are performed at all levels of the entity, at various stages within business processes, and over the technology environment. They may be preventative or detective in nature and may encompass a range of manual and automated activities such as authorizations and approvals, verifications, reconciliations, and business performance reviews. Segregation of duties is typically built into the selection and development of control activities. Where segregation of duties is not practical, management selects and develops alternative control activities.

4. Information and Communication: Communication is the continual, iterative process of providing, acquiring, and obtaining necessary information. Internal communication is the means by which information is disseminated throughout the organization, flowing up, down, and across the entity. It enables personnel to receive a clear message from senior management that control responsibilities must be taken seriously. External communication is twofold; it enables inbound communication of relevant external information, and it provides information to external parties in response to requirements and expectations.

5. Monitoring: Monitoring involves ongoing evaluations, separate evaluations, or some combination of the two are used to ascertain whether each of the five components of internal control, including controls to effect the principles within each component, is present and functioning. Ongoing evaluations, built into business processes at different levels of the entity, provide timely information. Separate evaluations, conducted periodically, will vary in scope and frequency depending on assessment of risks, effectiveness of ongoing evaluations, and other management considerations. Findings are evaluated against criteria established by regulators, recognized standard-setting bodies or management and the board of directors, and deficiencies are communicated to management and the board of directors as appropriate.

Associated with these five principles are seventeen components which are aimed at providing clarity for designing and implementing systems of internal control and for understanding requirements for effective internal control. Every organization is expected to access the effectiveness of their Internal Control function and revise their Internal Audit function’s effectiveness.

The benefits that can be derived from the application of the COSO Internal Control Framework cannot be underestimated because the application of the COSO Internal Control Framework would provide a solid foundation for determining the degree of assurance provided by controls.

Deloitte

Obedans Uwaeacji

Obedans is the partner-in-charge of Accounting and Financial Advisory in Akinlo Williams Deloitte.

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