

UNIVERSITY OF TOLEDO INTERNAL AUDIT DEPARTMENT

MANAGE LEGAL AND ETHICAL ISSUES

Control practices

The following control objectives provide a basis for strengthening your control environment for the process of managing legal and ethical issues. When you select an objective, you will access a list of the associated business risks and control practices. That information can serve as a checklist when you begin reviewing the strength of your current process controls.

This business risk and control information can help you assess your internal control environment and assist with the design and implementation of internal controls. Please note that this information is at the generic business process level and many companies will need to go beyond generic models to address the specific business processes that support the financial and nonfinancial disclosures being made. You can combine the insight of this business risk and control information with your industry-specific knowledge and understanding of your company's environment when conducting internal control assessments and designing and implementing recommendations.

Effectiveness and efficiency of operations

- A. Litigation costs and settlements are properly authorized and minimized.
- B. The company properly accounts for and discloses litigation, claims, and assessments.
- C. Management recognized and evaluates significant litigation, claims, and assessments.
- D. Contracts and agreements with outsiders are clear, fair, and legally enforceable.
- E. Errors, irregularities, and illegal acts are detected and properly remedied on a timely basis.

Compliance with applicable laws and regulations

- A. The company complies with contracts, laws, and regulations.

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Effectiveness and efficiency of operations

A. Litigation costs and settlements are properly authorized and minimized.

Business risks

- The company will pay excessive settlements.
- All the facts will not be available to management in negotiating settlements.
- The company will use more attorneys than necessary.
- The company will not fully utilize insurance entity services.

Control practices

1. Require senior management approval for all settlements and legal costs over a specified amount.
2. Require management to periodically review the legal function to ensure effective and efficient operation, including assessing staffing requirements, considering need for temporary help or shared services, comparing costs of internal and outside counsel, evaluating charges from attorneys used to determine if all costs are necessary and negotiating rates with external counsel.
3. Retain the minimum number of attorneys needed in specialized areas.
4. Engage management to review insurance coverage for liabilities under litigation and to request that in covered areas the carrier provide legal counsel.

B. The company properly accounts for and discloses litigation, claims, and assessments.

Business risks

- The company will not record existing liabilities.
- The company will not adequately disclose litigation, claims and assessments.

Control practices

1. Ensure management and its advisors have the competence to make the required assessments.
2. Ensure management understands the financial reporting objectives and why the assessments are essential to fair presentation of the financial statements.
3. Establish a process to review situations that may have a financial impact on the company to determine if disclosure is required or if a liability should be recorded in the financial statements.
4. Support the process of reviewing situations that may have a financial impact on the company with relevant and reliable information.
5. Ensure the process of reviewing situations that may have a financial impact on the company functions frequently enough to result in meaningful interim financial statements.

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C. Management recognized and evaluates significant litigation, claims, and assessments.

Business risks

- The company will not take the actions necessary to prevent further litigation or claims.
- The company will not record existing liabilities.
- The company will not adequately disclose litigation, claims and assessments.

Control practices

1. Ensure the company has the services of competent internal or external legal counsel.
2. Ensure management promptly notifies legal counsel of any legal action filed against the company.
3. Require management to meet periodically with counsel and the board of directors to review legal matters that may affect the company.
4. Inform employees of applicable legal, regulatory, and contractual requirements through training and correspondence.
5. Establish formal operating procedures for employees to follow when they uncover possible litigation, claims, or assessments.
6. Engage legal counsel to review pending matters periodically and update the company's positions.

D. Contracts and agreements with outsiders are clear, fair, and legally enforceable.

Business risks

- Unclear and poorly structured contracts will increase the likelihood of claims against the company.
- The company will waste time and money resolving issues associated with unclear and poorly structured contracts.
- Unauthorized personnel will enter contracts without management approval.

Control practices

1. Require that the legal department prepares and reviews all significant contracts and agreements.
2. Use standard contracts when possible.
3. Restrict authority to execute contracts or agreements.

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E. Errors, irregularities, and illegal acts are detected and properly remedied on a timely basis.

Business risks

- Errors, irregularities and illegal acts will not be detected.
- Noncompliance with laws or regulations will continue.
- The company will incur assessments and penalties.

Control practices

1. Respond promptly to notices from regulatory agencies.
2. Review and approve all correspondence and filings with regulatory agencies.
3. Execute appropriate remedial action in response to departures from approved policies and procedures or violations of laws and regulations.
4. Ensure effective management response to violations of the code of conduct.
5. Ensure employees are informed of disciplinary actions taken in response to violations of the code of conduct.
6. Ensure employees understand the consequences of violating established behavioral standards.

Compliance with applicable laws and regulations

A. The company complies with contracts, laws, and regulations.

Business risks

- The company will incur fines or other penalties.
- Management will be unaware of regulatory or legal requirements.
- Legal counsel will not be informed of all business activities and potential risks.
- Changes in laws and regulations will not be communicated adequately, so the changes will not be addressed in the company's business processes.

Control practices

1. Consult regularly with legal counsel regarding compliance with legal and regulatory requirements, changes in laws and regulations, and other legal matters.
2. Require legal review of business plans.
3. Establish goals concerning safe working conditions and the company's public image.
4. Inform all appropriate levels of management about the exposure associated with pursuing risky lines of business or risky business strategies.
5. Establish a system to monitor exposure to risks and to provide reasonable assurance that the risks are mitigated.
6. Inform executive management and the board of directors of any risks that cannot be effectively managed within the acceptable limits defined by management and the board.
7. Establish procedures to ensure compliance with reporting requirements of government agencies.