Internal Control Systems and Maintenance of Accounting and Other Records for Interactive Gaming & Interactive Wagering Corporations (IGIWC)

1 Introduction

1.1 Section 316 (4) of the International Business Corporations Act (IBC Act) requires the Commission to take any necessary action required to ensure the integrity of the International Business Corporation sector. The International Business Corporations (Prudential Management of Licensed Corporations) Regulations, 2004 - Statutory Instrument No. 9 of 2004- prescribe that a licensed corporation shall carry out its business in a prudent manner in accordance with the industry standards and best practices and any guidelines or directions issued by the Commission. These Regulations require an IGIWC to establish and implement policies, practices and procedures relating to internal controls including independent internal or external audit and compliance functions to test the adequacy and effectiveness of these controls as well as applicable laws and regulations.

1.2 Accordingly, these guidelines are being issued for the guidance and compliance by the corporations licensed to carry on international business under the IBC Act and the Interactive Gaming & Interactive Wagering Regulations.

2 Internal controls

2.1 Internal control consists of five interrelated elements:

1. management oversight and the control culture;
2. risk recognition and assessment;
3. control activities and segregation of duties;
4. information and communication; and
5. monitoring activities and correcting deficiencies.

2.2 The internal control systems should provide reasonable assurance that:-

- the business is planned and conducted in an orderly and prudent manner;
- transactions and commitments entered into have proper authority;
- management is able to safeguard the assets and control the liabilities of the business;
- there are measures to minimize the risk of loss from irregularities, fraud and error, and to identify and rectify them when they occur;
- the accounting and other records provide complete, accurate and timely information;
- management is able to monitor on a regular and timely basis, among other things, the adequacy of the capital, liquidity, profitability and the quality of assets;

- management is able to identify, regularly assess and, where appropriate, quantify the risk of loss in the conduct of the business so that: (i) the risks can be monitored and controlled on a regular and timely basis; and (ii) appropriate provisions can be made for bad and doubtful debts, and for any other exposures both on and off balance sheet;
- management is able to comply with regulatory reporting requirements

2.3 In establishing an internal control system management should have regard to the cost of establishing and maintaining a control procedure in relation to the benefits.
2.4 It is a responsibility of directors and management to review, monitor and test its systems of internal control on a regular basis in order to assure their effectiveness and continuing relevance to the business.

3 Management oversight and the control culture

The board's role

3.1 The board of directors should have responsibility for approving and periodically reviewing the overall business strategies and significant policies of the IGIWC; understanding the major risks run by the IGIWC, setting acceptable levels for these risks and ensuring that senior management takes the steps necessary to identify, measure, monitor and control these risks; approving the organizational structure; and ensuring that senior management is monitoring the effectiveness of the internal control system. The board is ultimately responsible for ensuring that an adequate and effective system of internal controls is established and maintained.

Senior Management's role

3.2 Senior management should have responsibility for implementing strategies and policies approved by the board; developing processes that identify, measure, monitor and control risks incurred by the IGIWC; maintaining an organizational structure that clearly assigns responsibility, authority and reporting relationships; ensuring that delegated responsibilities are effectively carried out; setting appropriate internal control policies; and monitoring the adequacy and effectiveness of the internal control system.

Control culture

3.3 The board of directors and senior management are responsible for promoting high ethical and integrity standards, and for establishing a culture within the organization that emphasizes and demonstrates to all levels of personnel the importance of internal controls. All personnel in the organization need to understand their role in the internal controls process and be fully engaged in the process.

3.4 The control culture encompasses the management style, and corporate culture and values shared by all employees. It includes:

(a) the importance which is attached to controls by management;
(b) the way in which staff are assessed and rewarded (including remuneration and bonus schemes as well as promotion policies);
(c) controls training, and the methods for reviewing control, including internal audit.
(d) a strong ethical environment, sound personnel policies and Code of Conduct.

3.5 Controls may be High-level controls which are primarily exercised at director and senior manager level, or the detailed controls, the operation of which is delegated to others. High level controls typically include: (a) the setting of strategy and plans; (b) approval of risk policies; (c) establishment and review of the organizational structure; (d) the system for delegation; (e) review of high level management information; (f) maintaining the framework for monitoring and/or periodic review of risk management and detailed control systems and for the implementation of action points following such a review.

4 Risk Recognition and assessment

4.1 The board and senior management should establish an effective internal control system in which the material risks that could adversely affect the achievement of the organization's goals are recognized and continually assessed. This assessment should cover all risks facing the organization (that is, credit risk, country and transfer risk, market risk, liquidity risk, operational risk, legal risk and reputational risk etc).

4.2 Senior management should continually evaluate the risks affecting the achievement of its goals and react to changing circumstances and conditions. Internal controls may need to be revised to appropriately address any new or previously uncontrolled risks.

5 Control objectives

5.1 At a minimum each organization should address the following control objectives:-

(a) Organizational structure: including allocation of responsibilities, identifying lines of reporting and delegation of authority and responsibility.
(b) Risk management
(c) Monitoring procedures
(d) Segregation of duties
(e) Authorization and approval of all transactions by an appropriate person.
(f) Completeness and accuracy of transactions and records
(g) Safeguarding assets: The controls should be designed to ensure that access- both direct and indirect access via documentation- to assets or information is limited to authorized personnel.
(h) Personnel: Procedures should ensure that personnel have competence and integrity and capabilities commensurate with their responsibilities.

Control Activities

5.2 The board and senior management should apart from setting up an appropriate control structure, define control activities at every business level. These should include:

<u>Top level reviews</u> – by board of directors and senior management to detect problems such as control weaknesses, errors in financial reporting or fraudulent activities.

<u>Activity controls</u> - Department or division level management should receive and review standard performance and exception reports on a daily, weekly or monthly basis. These functional reviews should occur more frequently than top-level reviews.

<u>Physical controls</u> - to restrict access to tangible assets, including cash, gaming database and securities, and may include such control activities as physical limitations, dual custody, and periodic inventories.

<u>Compliance with exposure limits</u> – to ensure that prudential limits on risk exposures set by management or in law or regulations are complied with.

<u>Approvals and authorizations</u> - for transactions over certain limits to ensure that an appropriate level of management is aware of the transaction or situation and to help establish accountability.

Verifications and reconciliations - Verifications of transaction details and activities and the output of risk management models and periodic reconciliations, such as those comparing cash flows to account records and statements, should be done to identify activities and records that need correction. The results should be reported to the appropriate levels of management whenever problems or potential are detected.

Segregation of duties

5.3 A prime means of control is the separation of those responsibilities or duties which would, if combined, enable one individual to record and process a complete transaction. Segregation of duties reduces the risk of intentional manipulation or error and increases the element of checking. Functions which should be separated include those of authorization, execution, valuation, reconciliation, custody and recording. Some examples of areas where segregation should be effected are:

(a) In the case of a computer-based accounting system, systems development and daily operations should be separated.
(b) Segregation of duties involving simultaneous front and back office control by one individual.
(c) approval of the disbursement of funds and the actual disbursement;
(d) customer and proprietary accounts;
(e) transactions in both the "gaming" and "wagering " books;
(f) informally providing information to customers about their positions while marketing to the same customers;
(g) any other areas where significant conflicts of interest emerge and are not mitigated by other factors.

5.4 Areas of potential conflict should be identified, minimized, and subject to careful monitoring by an independent third party. There should also be periodic reviews of the responsibilities and functions of key individuals to ensure that they are not in a position to conceal inappropriate actions.

5.5 For smaller organizations, segregation of duties can be difficult due to limited number of staff. In such circumstances, the Board should satisfy itself that the IGIWC is not running undue risk and that there are compensating controls in place e.g. frequent review of the area by internal audit and/or executive directors.

6 Information and Communication

6.1 Senior management should establish:

(a) systems to capture adequate and comprehensive internal financial, operational and compliance data, as well as external market information about events and conditions that are relevant to decision making. Information should be reliable, timely, accessible, and provided in a consistent format.
(b) reliable information systems that cover all significant activities of the corporation. These systems, including those that hold and use data in an electronic form, must be secure, monitored independently and supported by adequate contingency arrangements.
(c) effective channels of communication to ensure that all staff fully understand and adhere to policies and procedures affecting their duties and responsibilities and that other relevant information is reaching the appropriate personnel.

7 Monitoring Activities and Correcting Deficiencies

7.1 The Board and senior management should monitor the overall effectiveness of the internal controls on an ongoing basis. Monitoring of key risks should be part of the daily activities. In addition, periodic evaluations should be conducted by business function itself, by the financial control and by the internal audit.

7.2 There should be an effective and comprehensive internal audit of the internal control system carried out by operationally independent, appropriately trained and competent staff. The internal audit function, as part of the monitoring of the system of internal controls, should report directly to the board of directors or its audit committee, and to senior management.

7.3 Internal control deficiencies, whether identified by business line, internal audit, or other control personnel, should be reported in a timely manner to the appropriate management level and addressed promptly. Material internal control deficiencies should be reported to senior management and the board of directors, who should have a system for monitoring the action taken on the identified deficiencies.

8 Controls in an Information Technology Environment

8.1 It is the responsibility of management to understand the extent to which the organization relies upon electronic information, to assess the value of that information and to establish an appropriate system of controls. The control objectives and activities described above apply equally to operations undertaken in electronic environments, although there are additional risks associated with electronic environments.

8.2 The types of risk most often associated with the use of information technology in Corporations may be classified as follows:

(a) Fraud and theft: Access to information and systems can create opportunities for the manipulation of data in order to create or conceal significant financial loss. Additionally, information can be stolen, even without its physical removal or awareness of the fact, which may lead to loss of competitive advantage. Such unauthorized activity can be committed by persons with or without legitimate access rights.

(b) Errors: Although they most frequently occur during the manual inputting of data and the development or amendment of software, errors can be introduced at every stage in the life cycle of an information system.

(c) Interruption: The components of electronic systems are vulnerable to interruption and failure; without adequate contingency arrangements this can lead to serious operational difficulty and/or financial loss.

(d) Misinformation: Problems may emerge in systems that have been poorly specified or inaccurately developed. These might become immediately evident, but can also pass undetected for a period during which they could undermine the veracity of supposedly sound information. This is a particular risk in systems where audit trails are poor and the processing of individual transactions difficult to follow.

8.3 Management should be aware of its responsibility to promote and maintain a climate of security awareness and vigilance throughout the organization. In particular, it should give consideration to:

(a) IT security education and training, designed to make all relevant staff aware of the need for, and their role in supporting, good IT security practice and the importance of protecting company assets;

(b) IT security policy, standards, procedures and responsibilities, designed to ensure that arrangements are adequate and appropriate.

9 Accounting and other records

9.1 It is the responsibility of the directors and management to take reasonable care to establish and maintain systems and controls and adequate records (including accounting records), appropriate to the nature, scale and complexity of its business.

9.2 A corporation should maintain adequate records and systems for all aspects of its business which includes off-balance sheet business, and situations where the corporation acts as agent or arranger.

9.3 The scope and nature of the accounting and other records should be commensurate with the needs and particular circumstances and should have regard to the manner in which the business is structured, organized and managed, and to the nature, and complexity of its transactions and commitments.

9.4 The accounting and other records should be located where they will best assist management to conduct the business of the banking or trust corporation. They should:-

(a) capture and record on a timely basis and in an orderly fashion, every transaction and commitment which the corporation enters into, with sufficient information to explain (i) its nature and purpose; (ii) any asset or liability, actual or contingent, which respectively arises or may arise from it; and (iii) any income or expenditure, current or deferred, which arises from it;

(b) provide details, as appropriate, for each transaction and commitment,

(c) be maintained in such a manner that financial and business information can be extracted promptly to enable management to:-

(i) identify, measure, monitor and control the quality of the IGIWC assets and safeguard them, including those held as custodian; its exposures by related counterparties across all products; its exposures to liquidity risk, and foreign exchange and other market risks across all products;
(ii) monitor the performance of all aspects of its business on an up-to-date basis;
(iii) make timely and informed decisions;

(d) contain details of exposure limits authorised by management ;
(e) provide information which can be summarised in such a way as to enable actual exposures to be readily, accurately and regularly measured against these limits;
(f) contain details of the factors considered, the analysis undertaken and the authorisation or rejection by management of a loan, advance or other credit exposure; and
(g) provide details of every transaction entered into in the name of or on behalf of another party on an agency or fiduciary (trustee) basis where the corporation itself is not legally or contractually bound by the transaction.

10 Information for management

10.1 Every corporation should prepare information for directors and management so that they can monitor, assess and control the performance of its business, the state of its affairs and the risk to which it is exposed. This information should be prepared on an individual company and, where appropriate, on a consolidated basis.

10.2 It is the responsibility of directors and management to decide what information is required and to decide who should receive it. Appropriate management information should be provided to:-

(a) persons responsible for exercising managerial functions or for maintaining accounting and other records;

(b) executives who are responsible under the immediate authority of the directors for the conduct of the business of the corporation; and

(c) the directors of the corporation.

10.3 This information should be prepared:-

(a) to show the state of affairs of the corporation;

(b) to show the operational results of the business and to give a comparison with budgets and previous periods;

(c) to provide an analysis of assets and liabilities showing how they have been valued;

(d) to provide an analysis of off-balance sheet positions showing their valuation;

(e) to provide an analysis of income and expenditure showing how it relates to different categories of asset and liability and off-balance sheet positions; and

(f) to show the corporation's exposure to each type of risk, compared to the relevant limits set by management.

11 Money laundering and terrorist financing deterrence

11.1 The corporations should have policies and procedures in place to guard against their business being used for the purpose of money laundering or terrorist financing. These should conform to the laws and regulations in Antigua and Barbuda and any guidelines issued by appropriate authority.

12 Outsourcing

12.1 Where a corporation has outsourced an aspect of its operations to another part of the group, or to an external supplier, it should ensure that its records and controls adequately cover that business. It should put in place procedures for monitoring and controlling the outsourced operations.

13 Internal audit

13.1 The corporations should have an appropriate internal audit function. The Internal audit should provide independent assurance over the integrity and effectiveness of systems. Important considerations in assessing the effectiveness of internal audit include the scope of its terms of reference, its independence from operational management, its reporting regime and the quality of its staff.

13.2 The following control functions could be undertaken by internal audit:-

(a) review of accounting and other records and the control environment;

(b) assist management with the identification of risk;

(c) challenge the assumptions within the control systems;

(d) review of the appropriateness, scope, efficiency and effectiveness of internal control systems;

(e) detailed testing of transactions and balances and the operation of individual internal controls to ensure that specific control objectives have been met; and

(f) review of the implementation of management policies.

(g) special investigations for management where there are areas of particular concern.

13.3 The internal audit function should be appropriately structured and resourced to enable it to provide the independent appraisal of internal controls. The position of head of Internal Audit should be a key role within the IGIWC and, accordingly, should be undertaken by an experienced and senior individual. The objectivity and independence of internal audit should be supported by appropriate reporting lines. In most cases this would be dual reporting lines from the head of internal audit to the Chief Executive Officer or equivalent, and access to the Audit Committee, usually via the non-executive chairman of the Audit Committee.

13.4 Internal audit should not have authority or responsibility for the activities it audits. It should have unrestricted access to all activities, records, property and personnel of the IGIWC to the extent necessary for the effective completion of its work.

13.5 The internal audit function should be staffed with individuals who are appropriately qualified for the function either by holding professional qualifications or by having the requisite experience;

14 Audit committee

14.1 The corporations should have an audit committee chaired by a non-executive director of the corporation or be an audit committee of non-executive directors of the corporation's holding company.

14.2 The audit committee should have a minimum of three members all of whom should be non-executive and a majority of whom should be independent of the company.

14.3 The audit committee should have a formal constitution and terms of reference, explicit authority to investigate matters within its terms of reference and access to information and external advice. Its meetings should normally be attended by the head of internal audit and the finance director and there should be at least one meeting with the external auditors each year, without executive board members present.

14.4 Small corporations may find it difficult to appoint suitable non-executive directors for an audit committee. In these circumstances, the non-executive director who chairs the audit committee should be (i) independent of executive management, (ii) have no allegiance to a particular group of shareholders, (iii) have relevant gaming, financial services, auditing or accounting expertise and (iv) be capable, if necessary, of standing up to the executive management.

15 Reporting

15.1 Information about the operation of the interactive gaming and interactive wagering system is an important supervisory tool that helps in monitoring and ensuring timely action to protect the integrity of the system. A licensed corporation should establish systems and procedures to ensure that reporting requirements as prescribed in law or by supervisory directions/ guidelines are adequately and satisfactorily met. Such reporting should include, among other things, the following:

(a) Periodic returns and reports prescribed under the IBC Act and regulations framed under the IBC Act and the IGIW Regulations
(b) Suspicious Activity Report to the Supervisory Authority under the Money Laundering (Prevention) Act 1996 with a copy to the Commission, as prescribed under the Statutory Instrument 41 of 1998
(c) Incidents of fraud material to the safety, soundness or reputation of the corporation
(d) Any substantive changes in activities or any material adverse developments, including breaches of legal and prudential requirements

15.2 A corporation should furnish any relevant information relating to its related companies, irrespective of their activities, where the Commission believes that it is material to the financial situation of the corporation or to the assessment of the risks of the corporation.

15.3 It is the responsibility of the board of directors and the senior management of a corporation to ensure that the information contained in the reports made by the corporation is accurate, sufficient, reliable and relevant.