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CONTROLS**

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Internal Controls for Small Businesses and Start-Ups

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The notion of "internal controls" can seem intimidating, but for a small business they are absolutely critical when it comes to preventing or detecting irregularities, whether due to error or fraud. Small businesses often have limited resources and limited ability to utilize the same internal controls as larger companies. But there are important measures that can and should be taken to protect those hard-won resources and ensure that the small business's profitability is not walking out the door at end of the day.

According to the Association of Certified Fraud Examiners' 2016 Report to the Nations, 30% of fraud cases occurred in small businesses, with median losses of \$150,000 and 60% of small business fraud victims not recovering any losses. A simple web search will corroborate that fraud is happening on a regular basis.

Management expert Peter Drucker wrote that "efficiency is doing things right; effectiveness is doing the right things." Below are some ideas for implementing internal controls that can help protect a company efficiently in a small business environment.

Hire the Right People

Good internal controls start with having the right people on the team. Hiring should be an organized process designed to meet the company's strategic needs, not to simply get bodies in the door. Resist hiring someone just because he or she is a friend or family. Have written job descriptions emphasizing the responsibilities of the position as well as required job skills, and consider carefully whether the individual is the best person for the job. Make job offers dependent on satisfactory background and credit checks.

Segregation of Duties

Segregation of duties is the practice of having different individuals complete different components of a task. For example, ideally, the initiation, handling, and approval steps within a cash receipt process, cash disbursement process, journal entry, or other multi-step processes should not be performed by the same person. In a small business with limited staff, segregation of duties can be challenging, but a thoughtful approach can still be effective. In a two-person office, for example, the accountant or bookkeeper could write the checks, receive cash, prepare reconciliations, etc., while the owner or manager takes care of approvals by signing the checks, completing the deposit slips, and reviewing the bank reconciliation.

Process Cash Receipts through a Lockbox

Rather than having all cash receipts come into the office, where they will need to be manually processed and then driven to the bank daily, consider utilizing your bank's lockbox services. This will accelerate the flow of cash into your account; decrease the potential for fraud, theft or error; and improve staff productivity by eliminating certain manual processes. While there is a cost, of course, for lockbox services, consider it an investment in fraud prevention with the added bonus of freeing up staff for other activities that add value to the business.

Enhance Cash Disbursements with Positive Pay

Positive pay allows the company to transmit a file to the bank each time a check is written. When a check is presented for payment, the bank compares the check to the file, confirming the payee, check number, account number, issue date, and dollar amount. If the check does not match what is on file, it will not clear. This will significantly reduce the risk of someone altering a check and is significantly easier than catching check fraud after the fact. As an added bonus, some banks can even use the positive pay service to perform the bank reconciliation for the company.

Just Because You Can Use Excel, Doesn't Mean You Should

Many business people are spreadsheet warriors who rely on Excel excessively. Spreadsheets are time-consuming to create, hard to maintain, prone to error and often unnecessary. Studies have shown that close to 90% of spreadsheets contain errors. If you have to use a spreadsheet, double check for simple mistakes such as transposition errors, bad cell references or formulas; make sure that nothing is left out and that your final results make sense. When possible, consider the use of cloud-based applications to provide "big company" functionality at entry-level pricing.

Software Updates

In 2017, the "WannaCry" ransomware hit approximately 300,000 users in more than 150 countries, demanding \$300 in Bitcoin to unlock encrypted files, with payment doubling after three days. Hackers targeted organizations that were using unsupported versions of Microsoft Windows, including Windows XP, Windows 8, and Windows Server 2003. Make sure your company is using the latest software versions. Not only do software patches and updates add new features, remove old features, and fix bugs, they can also plug significant security holes. Don't make it easier for the bad guys to exploit your data. Another possibility is to use cloud-based applications where the provider is ensuring that updates are made on a regular basis.

Regular Backups

If your information is not yet in the cloud, make sure that all accounting records and mission-critical information is securely backed up, subject to your organization's record retention policy. If something happens to your data as the result of a computer problem, an upset employee, hackers, or a natural disaster, you'll want the security of knowing that your most recent data can be recovered quickly. Make sure backups are performed regularly and are tested to ensure they actually work.

Use Checklists

Airline pilots are famous for their use of checklists to make sure that all mission-critical tasks are completed. Rather than trying to remember everything that has to be done each month, owners or managers, with the help of their accountant, should develop a checklist to make sure all important action items are accomplished and everything is up to date. The checklist can ensure that bank reconciliations have been performed and reviewed; that certain recurring journal entries have been recorded; that budget-to-actual expenditures, month to prior month, and current year to prior year, are appropriate; and that any other manual task is completed on a timely basis.

It's on your business, so it's important to set up adequate controls to prevent and detect fraud. Internal controls don't have to be big and scary, but they do need to help prevent problems from happening in the first place.

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