TOP THINGS YOU NEED TO KNOW ABOUT ACCOUNTING IN YOUR PRACTICE

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Objectives

1. To get you familiar with common internal control concepts and terms
2. Understand why internal controls are important
3. Understand common control breakdowns and how to avoid them
4. Provide you with basic internal controls that you can take back to your practice

Segregation of Duties

The most important concept related to internal control is segregation of duties.

My definition:

Requiring the person that is responsible for accounting for an asset be different from the person responsible for physically protecting the asset.

Why Controls are Important

1. To prevent theft of assets
2. To protect the interest of the stakeholders
3. To ensure transactions are properly authorized
4. To ensure transactions are properly recorded
5. To ensure decisions are based on accurate information
6. To establish consistent procedures for future leaders within your organization

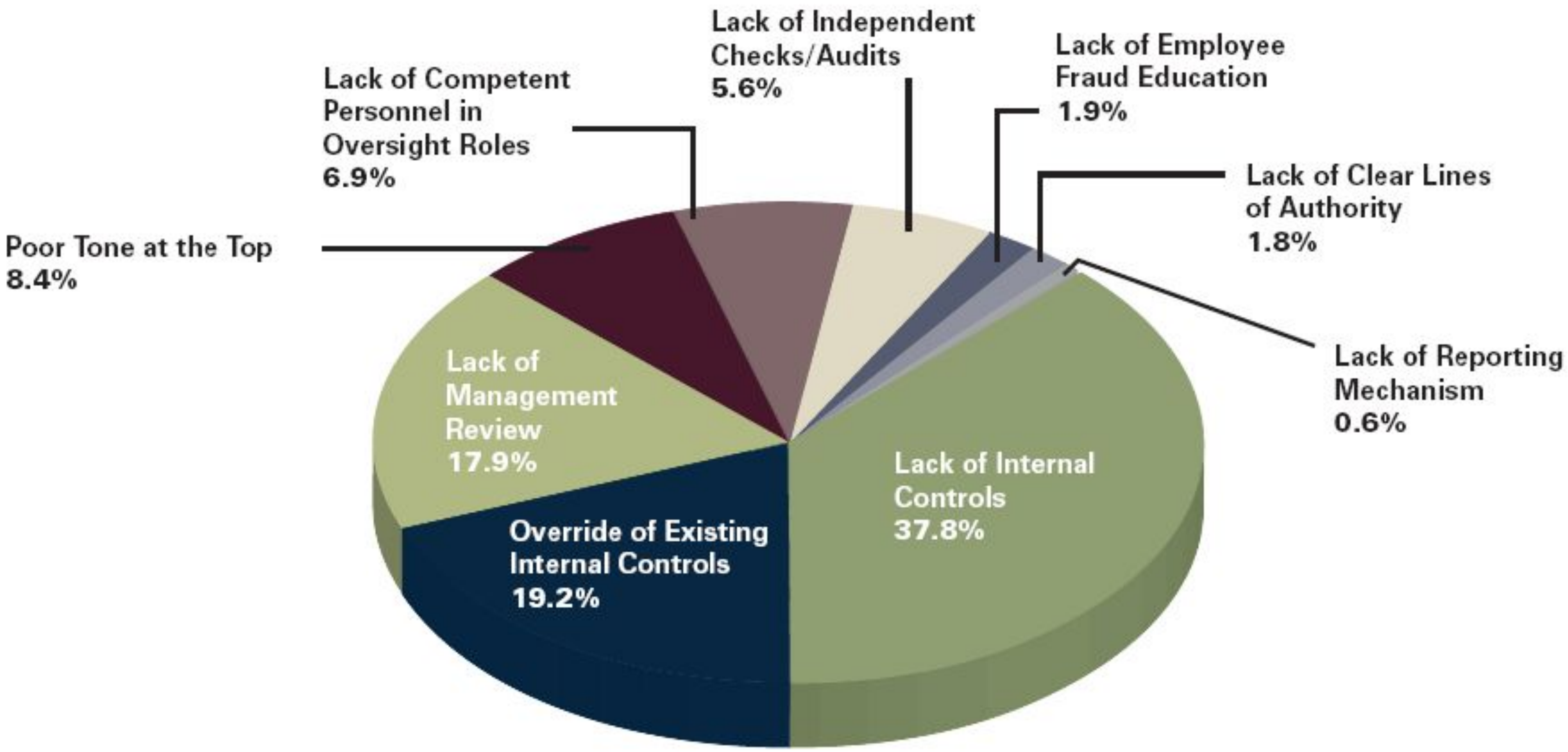
Internal Controls

- Specific procedures put in place to prevent unauthorized transactions from occurring
- To ensure transactions are properly recorded
- To determine that transactions are complete
- To protect organization assets

Common Areas in Need of Controls

1. Revenue
2. Disbursements
3. Payroll, if any
4. Expense reimbursement
5. Information Technology

Primary Internal Control Weaknesses Observed by CFEs



Most Common Frauds

Small Businesses — <100 Employees (342 Cases)		
Scheme	**Cases**	**Percent**
Billing	98	28.7%
Check Tampering	87	25.4%
Corruption	79	23.1%
Skimming	71	20.8%
Expense Reimbursement	53	15.5%
Cash on Hand	53	15.5%
Cash Larceny	52	15.2%
Non-cash	51	14.9%
Payroll	48	14.0%
Fraudulent Financial Statements	42	12.3%
Register Disbursements	12	3.5%

Most Common Frauds

Category	Description	Examples	Cases Reported	Percent of all cases[2]	Median Loss
Schemes Involving Cash Receipts					
Skimming	Any scheme in which cash is stolen from an organization *before* it is recorded on the organization's books and records.	• Employee accepts payment from a customer but does not record the sale	159	16.6%	$80,000
Cash Larceny	Any scheme in which cash receipts are stolen from an organization after they been recorded on the organization's books and records.	• Employee steals cash and checks from daily receipts before they can be deposited in the bank	99	10.3%	$75,000

Most Common Frauds

Schemes Involving Fraudulent Disbursements of Cash					
Billing	Any scheme in which a person causes his or her employer to issue a payment by submitting invoices for fictitious goods or services, inflated invoices, or invoices for personal purchases.	• Employee creates a shell company and bills employer for nonexistent services • Employee purchases personal items, submits invoice to employer for payment	229	23.9%	$100,000
Check Tampering	Any scheme in which a person steals his or her employer's funds by forging or altering a check on one of the organization's bank accounts, or steals a check the organization has legitimately issued to another payee.	• Employee steals blank company checks, makes them out to himself or an accomplice • Employee steals outgoing check to a vendor, deposits it into his own bank account	141	14.7%	$138,000
Expense Reimbursements	Any scheme in which an employee makes a claim for reimbursement of fictitious or inflated business expenses.	• Employee files fraudulent expense report, claiming personal travel, nonexistent meals, etc.	127	13.2%	$25,000

Most Common Frauds

Payroll	Any scheme in which an employee causes his or her employer to issue a payment by making false claims for compensation.	• Employee claims overtime for hours not worked • Employee adds ghost employees to the payroll	89	9.3%	$49,000
Cash Register Disbursements	Any scheme in which an employee makes false entries on a cash register to conceal the fraudulent removal of cash.	• Employee fraudulently voids a sale on his cash register and steals the cash	27	2.8%	$25,000
Cash on Hand Misappropriations	Any scheme in which the perpetrator misappropriates cash kept on hand at the victim organization's premises.	• Employee steals cash from a company vault	121	12.6%	$35,000
Non-Cash Misappropriations	Any scheme in which an employee steals or misuses non-cash assets of the victim organization.	• Employee steals inventory from a warehouse or storeroom • Employee steals or misuses confidential customer financial information	156	16.3%	$100,000

Questions To Ask Yourself

- How would we know if….
  - someone was stealing cash from us?
  - forging checks?
  - making bad wire transfers?
  - getting kickbacks at our expense?
  - Using related party vendors?
  - Paying themselves improperly?

Questions to Ask Yourself

- How do we know the controls in place are working effectively?
- How much fraud are we willing to accept?
- How do we protect information against unauthorized use/access?
- What do we know about the vendors we are paying?

Case Studies

Cash Payments

- Where I have seen controls break down
  - Lack of segregation of duties – one person responsible for setting up new vendors, approving invoices, maintaining custody of blank checks, preparing and mailing checks, recording transactions in the general ledger including adjustments, receiving the unopened bank statement and preparing the bank reconciliation
  - Lack of independent review on either end of the transaction

Cash Payments (continued)

- What are the control objectives – or – what are the risks?
  - Only authorized payments are made
  - Payments are made to legitimate vendors
  - Vendors are paid timely
  - Payments are made for the right amount
  - Transactions are recorded timely and in the right period
  - Goods and services purchased are received
  - Bank accounts reflect proper balances

Cash Payments (continued)

Questions to be answered:

- What controls should be put in place?
- What is the key control?
- What information will be maintained?
- How will the controls be monitored?

Revenues Received

- Where I have seen controls break down
  - Lack of segregation of duties – one person opens the mail, prepares the deposit slip, records the revenue in the general ledger, posts adjustments in the general ledger, and reconciles accounts receivable
  - Lack of independent review – no one reviewing the accounts receivable and associated journal entries.

Revenues Received (continued)

- What are the control objectives – or – what are the risks?
  - All revenue received is deposited
  - All deposits are made timely
  - All deposits are recorded timely
  - All deposits are recorded properly
  - Only legitimate receipts are entered in the system
  - Patients are properly billed and collections are received timely
  - Receivables are not written off without appropriate collection attempts

Cash Payments (continued)

Questions to be answered:

- What activities should be segregated to ensure cash is safeguarded?
- What controls should be put in place?
- What is the key control?
- What information will be maintained and communicated relative to this process?

Practical Solutions

- Bank statements for all accounts are received, opened and inspected by someone independent of the accounting function
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- Bank reconciliations reviewed by someone independent of the accounting function
- Other reconciliations reviewed by independent party

Practical Solutions

- Locked cabinets, file cabinets, blank checks
- Passwords and firewalls on computers
- Using security cameras (studies have shown where fake ones can deter theft)
- Background checks for all employees hired for finance/accounting functions (if not all)
- Setting a budget and reviewing actual results
- Inventory stickers on highly moveable equipment (ipads, laptops, cameras, etc)

Red Flags to Watch For

- Employees living beyond their means
- Family or personal illness
- Drug/alcohol abuse and/or excessive absences due to this.
- Insists that they have to work on weekends or at night when no one is around.

Questions?

- Contact information

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