



## Internal Controls in an Entrepreneurial Company

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### Why Do I Need Internal Controls?

How do you feel about internal controls? Have you ever thought:

- “I’m in charge here, what other controls are needed?”
- “I hire smart people who know what they are supposed to do, and they all report to me. That’s the only control I need.”
- “This is a private company, we don’t need to have controls.”

Let’s face it, as the owner, you try to stay on top of everything that is going on. Nothing gets decided without your involvement, especially the BIG decisions. Everyone knows their limits, and they know when to get your approval.

But you have a lot of things to do and you can’t always be around. What happens then? Do you stay on top of the day-to-day “normal” stuff, or do you leave those details to “the Team?” After all, that’s why you hired smart, talented people – people you can rely on to keep the business running.

When your instincts alert you that things don’t seem quite right, can you confidently rely on your people, processes and systems? Would stronger, written internal controls add value or would they just slow things down?

### How Could Internal Controls Help Me?

Let me suggest that having internal controls is about creating efficiency and effectiveness within your operations. It’s about helping you consistently achieve the results you want.

- For internal controls to be efficient, they should be part of the process, not something tacked on at the end for no apparent reason.
- For internal controls to be effective, they must address a specific need or risk associated with process.

Think of internal controls as a way to let people know what you want them to do (or not do), even when you are not there to tell them!

### **Where Would Internal Controls Fit In My Company?**

Every industry and every company has different needs for internal controls. One size does not fit all because each company has different processes and different risks. There is no need for a control that doesn't address a recognized risk!

However, there are many common controls that apply to most companies. And whether you realize it or not, you probably have many of the basic internal controls in place already. Maybe you call them standard operating procedures, budgets, spending limits or other such things.

Following are some of the critical areas of many companies and examples of some of the controls that might exist in an effectively controlled company.

#### Sales, Order Fulfillment, Invoicing

Controls over your sales and billing processes

- Do not allow shipments without paperwork
- Ensure all shipments have been invoiced
- Confirm all invoices have been recorded

#### Cash Receipts, Accounts Receivable and Bad Debts

Controls over collecting money (including wire transfers and credit card processing) and management of your customer accounts

- Credit is extended only to customers who meet minimum requirements
- All payments received are to be deposited timely into a designated bank account
- Customer payments are to be applied timely to their account
- Bad debt write-offs and other customer credits and adjustments are to be approved by an authorized manager

#### Purchasing, Cash Disbursements, Inventory

Controls over buying and paying for goods and services, including corporate credit cards and reimbursing employees for business expenses

- Only certain people are authorized to make purchases; maximum dollar limits have been established for each person
- All payments are to have appropriate supporting documentation
- Inventory is physically counted at regular intervals and exceptions are investigated
- Corporate credit card purchases are approved and monthly statements are reconciled
- Employee travel and entertainment expense reports are approved by an authorized manager

### Payroll, Benefits and Withholding Taxes

Controls over hiring and paying employees and contractors; ensuring taxes and withholdings are paid timely

- Employees are added and deleted timely from payroll records when they are hired and terminated
- Employee timesheets are approved by their supervisor
- Payroll calculations are reviewed by a senior manager
- Payroll taxes, benefits and other amounts withheld from employees are timely remitted to tax authorities or other vendors

### Accounting and Financial Reporting

Controls over accounting functions and financial reporting

- Bank accounts are reconciled every month
- Other key accounts are reconciled regularly (e.g. accounts receivable, inventory, accounts payable, long and short term loans, etc.)
- Actual results are compared to budgets and significant differences are analyzed and explained
- Financial reports must be approved by the chief executive before they are given to the bank or other external party

### Information Technology and Data Security

Controls over computer technology and financial data

- Computer technology is kept in a secure location with limited access
- System security tools are used to protect systems from unauthorized access and computer viruses
- Financial systems utilize controls to limit user access to specific systems and functions based upon the requirements of their job
- Financial data is routinely backed up and stored off-site
- Financial records are maintained in accordance with approved record retention policies

### General Controls

Controls related to management's ethics, philosophy and operating style; the assignment of authority and responsibility, and how management organizes and develops its people

- Responsibilities should be segregated so no one person can authorize, perform and record a transaction from beginning to end (“segregation of duties”)
- Transactions exceeding a specified dollar value should be approved by a designated senior manager
- Management should review critical transactions and controls randomly to ensure they are being performed in accordance with policy (“management oversight”)

## Conclusion

I believe internal controls are important to entrepreneurial companies, whether they are in start-up mode or are mature operations. They can influence your organization in the following ways:

- They are necessary for efficient and effective business operations.
- They build credibility with your banker, your CPA and others who rely upon your financial information and business behavior.
- They are a deterrent to bad behavior.  
In their recent Global Fraud Study, the Association of Certified Fraud Examiners (ACFE) states: “Our research continues to show that small businesses are particularly vulnerable to fraud. These organizations typically have fewer resources than their larger counterparts, which often translates to fewer and less-effective anti-fraud controls.”
- They establish “Tone at the Top” guidance for business behavior, even when specific rules may not exist.

Of course internal controls will grow and adapt to fit the nature and size of your organization. They exist to help you and your employees do the “right” things more often and to help prevent making the avoidable mistakes.

So, whether you are wanting to safeguard your organization from fraudulent activities or you are simply trying to make your financial operations more efficient and effective, internal controls may be helpful to your organization.

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