INTERNAL CONTROL INFORMATION FOR THE SMALL BUSINESS OWNER

ARE YOUR BUSINESS ASSETS VULNERABLE TO THEFT?

The United States Trustee ("UST") encourages every chapter 11 small business owner to think about whether assets essential to the business are protected against theft or fraud. The potential for employee dishonestly, the most common type of business theft, increases when one or more employees have too much control over cash or other vulnerable assets concurrently with control over accounting functions. By implementing basic internal controls and maintaining strong personal oversight of the accounting functions, the small business owner can minimize the opportunities for an employee theft to occur. Consider these examples of internal controls:

SEGREGATION OF DUTIES -- Related duties should be assigned to different people whenever possible.

- Know your employees. Employee theft occurs when you provide the opportunity and an employee has a personal situation that lends itself to committing a crime. Always check work references and when feasible conduct background checks.

- When one or two employees perform most of the accounting functions, actively supervise the employees and spot check your accounting records on a frequent basis.

- If staffing levels permit, segregate these accounting functions:
  - Receiving cash and checks *versus* recording receipts in the accounting records.
  - Receiving inventory *versus* ordering or paying for inventory.

BANK RECONCILIATIONS -- Receive bank statements unopened and scrutinize for unusual activity.

- Carefully scan bank statements after opening and question any unusual transactions.
- Review canceled checks each month, including payee endorsements on the reverse side.
- Reconcile bank statements timely each month.
- Review reconciliations prepared by employees, particularly the list of reconciling items.
- Review transfers between bank accounts.

RECEIPTS & OTHER ASSETS -- Safeguard valuable assets.

- Immediately record and restrictively endorse incoming checks.
- Make daily (or more frequent) deposits of checks and cash.
- Secure blank check stock.
- Maintain accurate inventory records.
- Backup computer records regularly and store at least one recent backup off-site.
- Restrict access to sensitive customer information.
- Change computer passwords regularly, particularly after terminating someone's employment.

DISBURSEMENTS -- Review the appropriateness of payments.

- Restrict signature authority on company bank accounts, especially for employees writing checks.
- Compare payroll checks with current employee records.
- Verify the name of each vendor paid.
- Track the number of credit card bills signed each month.
- Verify the account number when signing a check made payable to a credit card company.

BANKRUPTCY RELATED -- Verify payment of *post-petition* taxes.

- Verify that tax reports are timely filed and that payments for *post-petition* taxes are timely made and *received* by the appropriate taxing agencies. (Note: Failure to pay post-petition taxes while in chapter 11 may be cause for conversion or dismissal of the case.)