As small businesses grow and adapt to their environment over time, they often do not realize there are dangerous holes in their internal control processes. Some of these holes in internal control result from poor segregation of duties, creating gaps in a vital area of internal control. Due to the significance of segregating certain tasks, and the minimal time it takes to identify optimal structuring of these tasks, there is no reason these job duties should be haphazardly assigned. Yet, small businesses may have never taken a step back to examine the internal control environment in place, resulting in unnecessary weak links in the company’s internal control. While large companies have more resources available to carefully segregate sensitive job tasks for optimal internal control, there are easy ways for a small business to also achieve a reasonably secure level of internal control. One of the key steps in this process is the evaluation and assignment of job duties in order to create a segregated structure for an optimal internal control environment.

Understanding segregation of duties and its effect on internal control is mandatory for any CPA due to the large role of internal control in assurance engagements, but the owner of a small business has no such requirement. Since a CPA is a trusted business adviser, advising on the proper structure and function of internal controls is another way to add value to client services. Proper segregation of duties is vital to a secure internal control environment, especially for the many small businesses who have never considered this important issue, and a CPA is best positioned to provide this valuable internal control advice.

A clarification of segregation of duties will be helpful before continuing. A definition of segregation of duties and the objective of segregating duties are both concisely stated in AICPA’s auditing standards: “Assigning different people the responsibilities of authorizing transactions, recording transactions and maintaining custody of assets [which] is intended to reduce the opportunities to allow any person to be in a position to both perpetrate and conceal errors or fraud in the normal course of his or her duties.” 1 Thus, the driving force behind segregation of duties is to “reduce opportunities … [for] errors or fraud,” and segregation of duties assists in accomplishing this goal by structuring job assignments in such a way as to reduce the chance that a single person could both make and conceal the same error or fraudulent act.

Though the above statements clarify the importance for optimally structuring job duties, it is also evident that many small businesses will not have enough employees to allow for full segregation of duties. Even with a small number of employees however, AICPA’s auditing standards note, “companies that have only a few employees … may be able to assign responsibilities to achieve appropriate segregation or, if that is not possible, to use management oversight of the incompatible activities to achieve control objectives.” 2 In other words, there is still a best solution each business, regardless of size, can find to minimize risk of errors or fraud resulting from the structure of job assignments. This best solution ought to be identified and implemented by a few minutes of planning and consideration, since anything less is exposing the business to unnecessary risk.

The table in Figure 1 is proposed as a catalyst for identifying the best structure to use when a minimal number of employees are involved in the accounting function of a business. This table is intended only as a starting point for the discussion, since each business needs to tailor segregation of duties to match its own unique requirements.

A CPA wishing to remain independent should not play a role in a client’s internal control, which includes the roles mentioned in the table on the next page. However, AICPA’s Code of Professional Conduct3 specifically allows a CPA to provide assistance to management “in assessing the client’s business risks and control processes,” and to “recommend a plan for making improvements to a client’s control processes.” Special consideration must be made before providing a service such as a bank reconciliation, which could be part of a client’s internal control if the client
performed the role in-house. For a CPA to remain independent while providing such a service, the service must be performed only under management’s direct oversight, and the CPA must be careful not to make management decisions during the course of the service. Thus, the table below should be used as a tool and catalyst for advising a client on their internal control processes, but an independent CPA should always avoid a personal role in a client’s internal control environment.

Clarification of several control activities is also needed, since incorrect handling of the control activity can render it useless. Opening the mail to receive receipts, for instance, is not an effective control activity unless the receipts received are later verified to match both what was entered into the accounting system and the amount deposited to the bank. This matching can be provided through a simple listing of the checks immediately upon opening the mail, with names and amounts listed, and spot checking later to the receipts ledger and deposit amounts. Handled in this manner, the activity can be a strong control, but is ineffective if it only consists of opening the mail and passing along the receipts without any review. Similarly, if invoice approvals are not examined before signing checks, or worse, if blank checks are signed for use when the authorized check signer is unavailable, the expense authorization and check signature controls are circumvented and ineffective. Thus, complete compliance is needed in segregation of duties or the whole concept of segregation is violated and ineffective.

Small businesses are particularly vulnerable to developing holes in their internal control during times of expansion or contraction. A short discussion could be all it takes to identify and correct shortcomings, particularly those flaws in the segregation of job duties. Consider how to optimally segregate job duties as an important first step toward obtaining a secure internal control environment. Ultimately, a few minutes of consideration now could lead to a reduction in business risk, a step towards obtaining the optimal environment for future success.

### References

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