



## Best Practice Guide

# Implementing Financial Controls

Financial controls are the means by which an organization's financial resources are directed, monitored, and measured.

Financial controls play an important role in ensuring the accuracy of financial reporting, eliminating fraud and protecting the organization's resources, both physical and intangible. These internal control procedures reduce process variation, leading to more predictable outcomes.

# Financial Controls to Consider

Topics to consider include, but are not limited to: segregation of duties like Account Receivable (A/R) and Account Payable (A/P); segregation of duties related to check writing; managing who has access to accounting software systems, credit cards and ATM cards; and inventory management and tracking over time inventory and supplies.

Below is a comprehensive list of steps and measures a company can follow to ensure that appropriate financial controls are in place; the list has been adapted for emerging market entrepreneurs. Depending on your company size, industry, and resources, the following controls may or may not apply or be necessary.

## Management Policies/Staff

Implementing appropriate management policies and hiring qualified employees is an important first step in ensuring that financial reporting at your company is standardized and accurate.

- Hire experienced accounting and finance staff and ensure that relevant accounting standards are reviewed and implemented throughout the organization to accurately report financial data. You may want to employ an accountant that is certified by your national accounting association since, in most cases, only they can officially audit and review financial statements.
- Accounting staff should report directly to a member of senior management.
- Have comprehensive global General Ledger (G/L) frameworks and a detailed Chart of Accounts.
- Company policies should be in place for financial management procedures such as G/L and Chart of Accounts management, financial statement closing process, reconciliations, aging and charge-offs, inactive accounts, and suspended accounts.
- The management team should periodically review and evaluate company financial performance and during employee performance reviews, ensure that finance and accounting staff have appropriate knowledge and skills.
- A clear segregation of duties should exist between the following functions: sales, order placement, receiving, invoicing, accounts payable, and account reconciliation. No single employee should control a financial transaction from beginning to end. At least two people should be responsible for every transaction.

### Quick Terminology Guide

Accounts Payable A/P – Amount owed to a creditor for delivered goods or completed services.

Accounts Receivable A/R – Claim against a debtor for an uncollected amount, generally from a completed transaction of sales or services rendered.

Chart of Accounts – a list of accounts available in the accounting system in which to record entries, such as balance sheet and income statement accounts.

Chief Executive Officer (CEO) – Officer of a firm principally responsible for the activities of a company

Chief Financial Officer (CFO) – Officer who is responsible for handling funds, signing checks, keeping financial records, and financial planning for a corporation

Chief Operating Officer (COO) – The senior manager who is responsible for managing the company's day-to-day operations and reporting them to the CEO.

General Ledger (G/L) – Collection of all asset, liability, owner's' equity, revenue, and expense accounts.

## Accounts Receivable, Credit and Collections

Accounts receivable represents the money that customers owe your business for goods or services they have purchased on credit. Keeping accurate records, safeguarding your files and confirming credit worthiness of your customers can ensure that payments are collected and fraud is not committed.

- Strive to ensure that all incoming funds are received, kept under adequate security, promptly deposited, properly recorded, and reconciled.
- Require credit reporting, if applicable in your country, on all customers prior to credit issuance.
- Require periodic review of key customers to ensure ongoing credit worthiness.
- Limit system access to alter credit limits and/or terms only to appropriate personnel.
- Require manager approval for adjustments to and/or write-offs of A/R balances.
- Require monthly reconciliation of bank statements to the General Ledger.
- Access to customer files is limited to the appropriate personnel.
- Account statements are mailed and/or emailed to customers.

## Accounts Payable/Purchasing

Accounts payable represents the debts that your company owes to creditors and vendors. Keeping accurate records, safeguarding your files and establishing clear guidelines for payment procedures can help your business meet payment deadlines and prevent fraud.

- Strive to ensure that funds are disbursed only upon authorization of management, for valid business purposes, and that all disbursements are properly recorded.
- Company policies and procedures governing accounts payable and purchasing processes should be clear to accounting and finance employees.
- Access to add, modify, or delete purchase orders is restricted to appropriate personnel.
- The ability to add, modify, or delete vendor records is restricted to appropriate individuals.
- Vendor files are periodically purged of old and obsolete vendors.
- A three-way match between the invoice, purchase order (PO), and receiver must be present before payment is released to the vendor.
- Management/owner approval is required for adjustments to A/P balances and restricted to appropriate personnel.
- Checks are appropriately secured and access is restricted to appropriate personnel.
- Owner or COO signature is required on all manual check disbursements.
- Gaps in check numbers should be investigated to ensure checks have not been stolen or used for unauthorized purposes.
- Bank statements are reconciled to the general ledger monthly and reviewed by management.
- Major supplier statements are reconciled to the A/P subsidiary ledger.
- Wire transfers are executed only by the owner or senior management.
- Clear employee expense reimbursement guidelines are maintained. Accounting staff reviews expense reports in detail and reimburses only with valid receipt and approval of manager.
- Credit cards are only issued to employees with clearly defined needs (e.g. extensive travel). One general company credit card exists for non-management personnel, and access is only allowed through permission from the accountant and manager and through a formal purchase order.

### Are you a Small Company?

Consider starting out with the following practices: Establish a clear segregation of duties between

- A/R and A/P, check writing and check signing.
- Limit accounting system access to appropriate personnel.
- Reconcile bank statements, credit card statements, etc. to the General Ledger on a monthly basis.
- Designate a central point of contact for all incoming mail.
- Require credit check on customers prior to credit issuance.
- Consider hiring an outside accountant/bookkeeper to assist with and review financials at least once a year.
- Consider outsourcing payroll.

## Payroll

Keeping good payroll records is essential for accurate accounting, government reporting, and good human resources practices. Not only can the records help you calculate your company's income correctly, but also track whether you pay your employees on time, and how much you pay them. This can help you be a better manager, and maintain high morale among your employees.

- Strive to ensure that payroll disbursements are made only upon proper authorization to bona fide employees, that payroll disbursement is properly recorded and that related legal requirements (such as payroll tax deposits) are complied with.
- Policies and procedures governing payroll processes detailing timelines, responsibilities, actions, responsibilities, etc. exist.
- Access to add, modify, and delete records from the employee master file are restricted to the COO or company owner. Managerial approval is required for modification to significant data (i.e. salaries, etc.).
- Payroll files are restricted to appropriate personnel.

## Fixed Assets

Carefully managing your fixed assets, such as buildings, equipment and furniture, will ensure that the assets are secured, maintained and appropriately valued in your financial statements.

- Strive to ensure that fixed assets are acquired and disposed of only upon proper authorization, and that they are adequately safeguarded, and properly recorded.
- Company policies and procedures governing fixed asset-related processes detailing timelines, responsibilities, actions, etc. exist.
- Fixed assets should be secured appropriately.
- Book-to-physical reconciliation is conducted annually to validate condition and existence of assets.
- Access to the fixed assets register is restricted to appropriate personnel.
- Managerial approval is required for asset disposals and write-offs.
- Asset acquisitions must be approved in advance of purchase.
- Asset valuations are periodically reviewed by management for continued relevance.
- All supporting paperwork is obtained prior to entry into the fixed asset register.
- Support files are maintained in a secured area and restricted to appropriate personnel.

## Inventory

Inventory, defined as raw materials, work-in-process goods and completely finished goods, is one of the most important business assets because it is one of the primary sources of revenue generation and earnings. Management policies can help your company possess the right amount of inventory in order to maximize revenue.

- Strive to ensure that inventories are received and/or shipped only with proper authorization and documentation, and that they are properly recorded and appropriately safeguarded.
- Company policies and procedures exist that govern inventory-related processes detailing timelines, responsibilities, actions, and responsibilities.
- Inventories are appropriately secured and processing inventory adjustments is restricted to appropriate personnel.
- Book-to-physical or cycle counts are periodically conducted to validate condition and existence of inventory.
- Inventory is only received with valid support paperwork (i.e. PO).
- All inventory receipts are verified for quantity and condition against the bill of lading (shipper's receipt) the packing slip, record on pre-number receiver forms and/or a log.
- Management reviews and reconciles the receipts log to system receipts on a daily basis.
- Inventory files are maintained in a secured area and restricted to appropriate personnel.

- Management review and approval of inventory write-offs is required.
- All inventory shipments are required to be accompanied by a valid order.
- Management periodically reviews open work orders, inventory aging reports, etc.
- All shipments are recorded in a shipping log, and management reviews and reconciles to the system on a daily basis.

## Financial Closing or Reporting

Managing your financial data carefully and ensuring accurate and timely reporting is an essential component of effective financial controls. This provides management with a clear look at the financial state of the company at the end of every period, which is vital for making strategy decisions as well as for informing investors.

### International Financial Reporting Standards (IFRS)

Developed through the International Accounting Standards Board (IASB) in the UK

[These financial reporting standards](#) were developed to create transparent and comparable financial statements globally.

- Strive to ensure that financial data is recorded, consolidated, and reported accurately, timely, and in compliance with International Financial Reporting Standards (IFRS) or your country standards.
- Company policies and procedures that govern financial closing processes detailing timelines, responsibilities, actions, responsibilities, etc. exist.
- Policies regarding the segregation of duties within the account reconciliation, journal posting, and management review/approval processes exist.
- Management approval is required for all non-standard, adjusting, and/or manual journal entries.
- A budgeting and forecasting process is established. Trend analysis is used (horizontal and vertical) in order to check results and research and resolve any unusual variations.
- The ability and/or access to post journal entries should be limited to appropriate personnel.

## Accounting Software

Computer programs can be very helpful to accountants in recording and reporting your company's financial transactions. The software automates time-consuming tasks, reducing the costs of accounting and facilitating timely reporting.

- If you use accounting software, it should be password-protected and access to information and editable fields limited to appropriate personnel.

## Endnotes:

- 1 <http://www.ifrs.org/IFRS-for-SMEs/Pages/IFRS-for-SMEs.aspx>
- 2 <http://www.smetoolkit.org/smetoolkit/en/content/en/727/Preventing-Employee-Fraud>
- 3 <http://www.smetoolkit.org/smetoolkit/en/content/en/5301/Financial-Terminology>



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