Want better internal controls? Tell a story

Elaine Gregory, CPA with Gary Zeune, CPA

I am a finance manager at King County Department of Development and Environmental Services (DDES) in Seattle, WA. DDES has approximately 245 employees and recently instituted Alternative Work Schedules (AWS), which allow employees to choose from three different work plans. I have been asked to provide AWS for my finance staff. According to my director, utilizing AWS reduces unscheduled sick leave (including sick family leave for dependents), and promotes morale. That all may be true, but the problem is that my staff is small and AWS would significantly weaken internal controls by reducing segregation of duties.

When my director wanted to know why I would not consider AWS for my staff, I wasn't surprised. Of all departments, finance has the fewest staff positions eligible for the program. The Joint Labor and Management committee was "very concerned" that I wasn't considering the needs of my staff in denying AWS in finance. I'm a pretty fair boss and I try to accommodate my staff when a child is ill, an appointment to the dentist is scheduled in the middle of the day, or the washing machine springs a leak. But I always maintain proper internal controls. If I, as a CPA manager, don't listen, who will listen to me when I'm concerned about controls?

I could have written a long-winded response about the need for segregation of duties, especially in cash and accounts receivable. I could have stressed the need for strong internal controls, audit requirements and findings. Or I could have blamed our outside auditors. But instead, I chose to tell the committee a story.

I was the only "auditor" in a three-person firm and my clients consisted of small non-profit organizations and schools. Most of my clients had less than $500,000 of revenues, and used simple QuickBooks accounting software. An average audit took me about a week for field work. And in those days, auditors prepared the closing entries and the financial footnotes.

In 1995, I was assigned to audit a local Red Cross chapter, a new client. The executive director, "David", told me that there was a "problem" and that the office manager/bookkeeper, "Sheila" was no longer employed there. In fact, David was considering criminal charges for theft and destruction of property. This was not good. I learned that just a few days before, during an altercation [with David] Sheila abruptly resigned and walked out. David did not get Sheila's work keys when she left. Two days later, there was a suspicious theft of office equipment, a cash box, and several boxes of Red Cross training supplies that had just been received, but had not been stamped with the chapter name.

I asked about the files and records of the agency. David said that Sheila often "took home" the files to work in the evening. She was always such a

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conscientious employee, never taking leave, able to manage all aspects of the agency. David was not even sure what caused the argument that prompted her to leave.

I asked to see what was left and was presented with a small collection of folders with some invoices, a couple of pay stubs and an old trial balance. No checks, no bank records, no vendor payments, and most of all, the QuickBooks records that were on a disk was also missing.

The managing partner and I decided the records could not be audited and withdrew from the engagement. We suggested that the chapter contact the State Red Cross headquarters for advice, and to keep us informed if they recovered any documents.

Two months later, Sheila had advertised as a Red Cross certified first aid trainer. She had an office with various pieces of equipment, and several thousand dollars worth of training books and supplies. A package was subsequently found outside of the chapter office containing various chapter documents and files. (The chapter never found out who left the package.)

How could the Red Cross let this happen? Sheila, as David so correctly noted, never took leave, managed all aspects of the agency and had absolutely no oversight when it came to taking documents off site. There were no internal controls or segregation of duties. This was an extreme case, and although it occurred over 10 years ago, it remains with me as a guide to my business process structure. The only control was blind trust. Remember, trust is a feeling. Trust is NOT a control. Unfortunately, particularly in small organizations, no one ever thinks it's going to happen to them. But it does – far too often.

"And that is why," I said to my director, "at our agency the person who takes in the money, is not the person who prepares the deposit, is not the person who posts the payment into our billing system, and is not the person who reconciles the bank statement." Finance is the most heavily audited department regarding controls and segregations of duty – and should be. An AWS program, though beneficial for an employee, is not a benefit if it creates unacceptable risk to the agency in the form of a lack of controls.

I'm sure we will develop some compromise; I think I'm a pretty good boss.

Note to readers: Even though it appeared Shelia may have stolen $5,000 cash and maybe that much more in equipment and supplies, she was never charged.

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Gary Zeune is a nationally recognized speaker and writer on fraud, Mr. Zeune is also the founder of The Pros & The Cons, the only speakers bureau in the U.S. for white-collar criminals. Mr. Zeune teaches fraud classes for the FBI, U.S. Attorney, bar and health care associations, 30+ state and national CPA societies, and numerous banks and accounting firms.