The Seven Internal Control Procedures in Accounting

Internal controls are policies and procedures put in place to ensure the continued reliability of accounting systems. Accuracy and reliability are paramount in the accounting world. Without accurate accounting records, managers cannot make fully informed financial decisions, and financial reports can contain errors. Internal control procedures in accounting can be broken into seven categories, each designed to prevent fraud and identify errors before they become a problem.

1. Separation of Duties

Separation of duties involves splitting responsibility for bookkeeping, deposits, reporting and auditing. The further duties are separated, the less chance any single employee has of committing fraudulent acts. For small businesses with only a few accounting employees, sharing responsibilities between two or more people or requiring critical tasks to be reviewed by co-workers can serve the same purpose.

2. Access Controls

Controlling access to different parts of an accounting system via passwords, lockouts and electronic access logs can keep unauthorized users out of the system while providing a way to audit the usage of the system to identify the source of errors or discrepancies. Robust access tracking can also serve to deter attempts at fraudulent access in the first place.

3. Physical Audits

Physical audits include hand-counting cash and any physical assets tracked in the accounting system, such as inventory, materials and tools. Physical counting can reveal well-hidden discrepancies in account balances by bypassing electronic records altogether. Counting cash in sales outlets can be done daily or even several times per day. Larger projects, such as hand counting inventory, should be performed less frequently, perhaps on an annual, quarterly or monthly basis - depending on whether you use a manual stock control system or you use a computer-based perpetual inventory management system.

4. Documentation

Standardising documents used for financial transactions, such as invoices, internal materials requests, inventory receipts and travel expense reports, can help to maintain consistency in record keeping over time. Using standard document formats can make it easier to review past records when searching for the source of a discrepancy in the system. A lack of standardization can cause items to be overlooked or misinterpreted in such a review.

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5. Trial Balances

Using a double-entry accounting system adds reliability by ensuring that the books are always balanced. Even so, it is still possible for errors to bring a double-entry system out of balance at any given time. Calculating daily or weekly trial balances can provide regular insight into the state of the system, allowing you to discover and investigate discrepancies as early as possible.

6. Reconciliations

Monthly, weekly, or daily (best) accounting reconciliations with your bank can ensure that balances in your accounting system match up with balances in accounts held in your bank... and then also reconcile with other entities, including long-term bank loan accounts, your suppliers and your credit customers. For example, a bank reconciliation involves comparing cash balances and records of deposits and receipts between your accounting system and bank statements. Differences between these types of complementary accounts can reveal errors or discrepancies in your own accounts, or the errors may originate with your bank(s) or the other entities.

7. Approval Authority

Requiring specific managers to authorize certain types of transactions can add a layer of responsibility to accounting records by proving that transactions have been seen, analysed and approved by appropriate authorities. Requiring approval for large payments and expenses can prevent unscrupulous employees from making large fraudulent transactions with company funds, for example.

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