David L. Buterbaugh, P.C.
CERTIFIED PUBLIC ACCOUNTANTS

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Dear Business Owner:

As our engagement letter states, we are not engaged to detect fraud or any other accounting irregularities your employees or a co-owner may perpetrate. The purpose of this letter is to make you aware of the risk and mention a few minimal steps you should take to mitigate your risk. **Because of the increasing number of employee frauds we are requiring that all business owners read and sign this document.**

The statistics about fraud (most recent study from 2016) in small businesses from the Association of Certified Fraud Examiners (ACFE) remain staggering. The following are from their most recent study (2016):

- 37.7% of all fraud originates in privately-held businesses
- The median loss in a privately-held business is $180,000
- Small businesses (fewer than 100 employees) comprise the greatest percentage of cases being victimized.
- Over three-quarters of fraud are from the employee or managerial levels combined. Most occupational fraud perpetrators are first-time offenders – only 5.2% had a criminal record for prior fraud-related offenses.
- Frauds take an average of 18 months to be discovered

You may see their entire study at:
https://s3-us-west-2.amazonaws.com/acfepublic/2016-report-to-the-nations.pdf

No system of internal control should be built on trust. Most small businesses have one “trusted” staff person handling all their accounting and financial matters. You can reduce your risk of fraud by taking these simple steps:

1. **Open the bank statement yourself**

Every small business owner should receive the unopened bank statement and review each check for authorized payee/signature, and approved electronic payments, before you provide the statement to the bookkeeper. Ask the bank to send an extra copy to your home to make sure you don’t hold up the bookkeeping process. As the business owner, you should at a minimum, open every bank statement and sign and date the statement before providing it to your bookkeeper for reconciliation. Do not sign the statement until you have thoroughly reviewed the statement including the images of every check and all other payments. Be sure all check signatures are valid and that all payments authorized. If your bank does not provide images of all cleared checks, call them and add that service immediately. Please follow the same procedure for all credit card statements.

2. **Bonding and Background Investigation**
Consider bonding employees who handle cash or perform venerable financial procedures.

3. **Required Vacation Time**
Another simple procedure is to require all employees to take their vacation time. Either you or another employee should perform their duties during their vacation. This gives you an opportunity to see if they are doing something inappropriate. If they refuse or are hesitant to take the time off, that should be a warning sign. **In prior years, ACFE reports that companies with a job rotation/mandatory vacation policy report 33% lower fraud losses**.

4. **Don't let your bill payer reconcile the bank account**
The person who pays the bills should never reconcile the bank account. That's how they cover their tracks. There should be a segregation of duties between the bill payer and the person who reconciles the bank account.

5. **Owner Approval Before Accounts Receivable Adjustments**
The business owner should have a policy that all Accounts Receivable (AR) adjustments should be approved by the owner. Either the owner or someone other than the bookkeeper should speak with a customer prior to approving an (AR) adjustment to confirm the costumer did not pay the invoice. A common fraud can involve an employee depositing customer payments into their own bank account and then writing off the receivable as a bad debt.

6. **Limit Signing Authority**
Segregate duties as much as possible so that only you, the owner, should sign checks. Avoid signature stamps. If an employee needs to sign checks for small purchases, keep a separate account with a minimal amount of cash in it. Do not grant the employee with signature authority or the right to transfer money between your various bank accounts.

7. **Attach scanned images to each transaction**
Most fraud occurs from check tampering – the bookkeeper changes the payee to themselves. Reduce the risk of fraud by scanning the bill and linking it to each transaction inside your accounting software. This makes it harder to falsify a bill.

8. **Close the prior periods**

Most software has a way to lock down the prior periods. Once you produce a financial statement that period should be "closed". This reduces the risk of hiding a fraudulent transaction in a prior year.

9. **Set up usernames and passwords for each user & restrict user access**

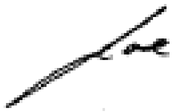
Most software, including QuickBooks, has an audit trail report which can never be turned off. However if your staff logs in as "Administrator" you have no idea who made what entry. Consider requiring monthly password changes.

10. **Backup Data**

While not really part of internal controls, regular off-site backup of your critical data cannot be overstressed. Be sure to perform a test of your system upon initiation and periodically.

These simple steps don’t cost much. But they can make the difference in being part of a growing statistic.

Sincerely,



David L. Buterbaugh, CPA

My signature below indicates that I have read this document and understand the risk of employee fraud or embezzlement. I acknowledge that David L. Buterbaugh, P.C. is not responsible to detect fraud or other irregularities. I agree to hold David L. Buterbaugh, P.C. harmless from any losses I may incur from any such loss.

____________________________________. Date:___________.

Signature

____________________________________.

Print name

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