

MUSIC MATTERS

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What Is Segregation of Duties? And, Why Does It Matter?

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Commercial crime insurance protects MUSIC members from financial losses related to school crime, including theft by employees, forgery, computer systems fraud, and social engineering fraud.

One of the most severe risks of financial loss due to theft comes from a school's employee, especially if this individual is in a position that controls access to money, property, or securities. Another area of risk is social engineering fraud, which is characterized by an outside party deceiving an unsuspecting employee into transferring funds to the perpetrator.

MUSIC's Commercial Crime policy Limits of Liability and Retentions can fluctuate based on whether the MUSIC member has internal controls surrounding financial processes designed to stop a theft attempt before it is successfully carried out.

One of these internal controls is the **Segregation of Duties**. Establishing effective segregation of duties involves understanding an employee's roles, responsibilities, and access to financial records, assets, and systems. Segregation of Duties will require members to evaluate their school's business operations. Schools should make sure different people approve bills to be paid, write checks or initiate ACH transfers, issue invoices, record cash, process payroll, and reconcile bank accounts and credit card accounts. Without the Segregation of Duties, schools are more vulnerable to fraud.

Some key questions to ask include the following:

- Does someone other than the person responsible for reconciling bank accounts make deposits? Make withdrawals? Sign checks?
- Does senior school management review and approve the bank reconciliations every month?
- Does your school require counter-signatures on all checks?
- Is a multi-authorization process required for all wire transfers?
- Does your school board track how and where the money is spent?

MUSIC members must establish internal controls so that no one employee can control the financial process from beginning to end. No single individual should be in charge of two or more parts of transactional activities. When establishing internal controls, think about segregating responsibilities into four general categories:

Authorization and Approval

Designate a point person who will authorize all financial transactions. This person will be in charge of signing checks, approving electronic cash transfers, and overseeing any money that goes out the door. Before cash leaves your school, this individual will review and approve the payment and make sure it is going to the right place.

Record-Keeping

Assign bookkeeping duties to a specific person. Make sure the person recording the school's financial transactions is not the same person who writes and signs checks.

Custody of Related Assets

The person who is the "custodian of assets" is in charge of managing your school's cash. This person collects cash or checks, makes bank deposits, and reviews bank statements. This role is separate from record-keeping or account reconciliation.

Reconciliation

Your school's accounts should be reconciled daily. The person in charge of reconciliation should not be the same person who is the custodian of assets. This person will compare the bank statements against the ledger to ensure that the transactions match. This person should not be allowed to make changes to the ledger or bank statement. All discrepancies should be noted and given to the appropriate person.

Segregation of Duties is a critical internal control for reducing the risk of fraud. By establishing protocols, MUSIC members can mitigate the risk of financial loss caused by employee theft, computer fraud, and social engineering fraud. If a MUSIC member experiences a financial loss, the school will be asked to specify how segregation of duties was implemented and followed. Failure to implement Segregation of Duties protocols will result in reduced Limits of Liability and increased Retention amounts per the Crime coverage.

These internal controls are required by the Crime carrier, as MUSIC has had a substantial number of losses due to allowing one person being in charge of all of these duties which then could lead to million dollar losses in some cases. To be able to utilize MUSIC's full crime limits, segregation of duties is a must.

MUSIC is creating training specifically for Segregation of Duties to assist you in implementing these much needed internal controls. They will be available to members in the next few weeks.

If you have questions or wish to discuss this information further, please feel free to contact Peggy Wilson.



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