

Protecting Profits in an Automobile Dealership by Segregating Management Duties

By Lamar Lewis-Sutton

While it may be difficult for many dealers to accept, fraud can present itself in many forms, and its damage to the bottom line can be lasting and often difficult to endure financially. While proper internal controls are vital, and most dealerships understand their importance in general, many knowledgeable owners and managers fail to understand the importance of segregating duties within the organization. The fact is, by properly defining and separating employee functions, dealerships can put the brakes on devastating financial disasters that otherwise might crash through the figurative front doors.

All too often, dealers believe that veteran employees who have demonstrated loyalty to the dealership over the course of many years are the most trustworthy, and these employees are therefore often granted unusual leeway, and given job descriptions that bridge various functions. This belief has cost dealers hundreds, thousands, and in some cases millions of dollars over the years. Veteran employees are, of course, very valuable in the sense that their work experience and understanding of dealership's operations and history is invaluable. However, without the right internal controls in place, and without complete segregation of duties, a dealership could face its greatest financial catastrophe due to a veteran employee's internal knowledge of operations.

According to fraud experts, the Fraud Triangle is critical to understanding why and how employees defraud a company. The Fraud Triangle consists of three key elements which include 1.) pressure, 2.) attitude or rationalization, and 3.) opportunity. Regardless of how trustworthy an employee is or has been in the past, if certain pressures exist (i.e. serious illness, drug dependency, divorce, economic pressures, etc.) in his or her life, and the employee begins to rationalize doing whatever it takes to cure the situation, then adequate internal controls and segregated duties may be a dealer's best defense to safeguard assets and profits.

In order to reduce the likelihood that intentional or unintentional errors and wrongdoings will go undetected, dealerships must take preventive steps. When it comes to segregation of duties, a disciplined and systematic approach is key. By having different employees conduct independent reviews of the work performed at various stages of a transaction, a dealership can ultimately reduce the opportunity for misappropriation. This procedure blocks the final piece of the Fraud Triangle, ensuring that no single employee or group of employees will have the opportunity to conceal or perpetrate errors or irregularities during the normal course of their duties.

Put your dealership to the test and ask the following questions, then determine how your dealership measures up:

Fixed Operations

1. Does the employee that authorizes credit limits for parts customers have access to perform the following duties: a. issue parts tickets; b. handle parts inventory for delivery; c. close parts tickets; d. prepare month-end customer statements e. issue customer credit memos; f. review and follow-up on customer inquires; g. access to change sale accounts and data files?
2. Does a service advisor creating a repair order have access to perform the following duties: a. approve credit limits (if applicable); b. close repair orders; c. issue customer credit memos; d. review and follow-up on customer inquires; e. access to change sale accounts and data files?

Front-End Operations

1. Does the sales manager or an employee authorized to deliver vehicles have access to perform the following duties: a. prepare sales contract; b. verify sales contract; c. post deals; d. access to change sale accounts and data files?
2. Does the employee responsible for receiving new vehicles delivered have access to perform the following duties: a. post vehicles into inventory; b. perform monthly physical inventory observation; c. reconcile physical counts to the general ledger; d. review the physical inventory reconciliation?
3. Does the F&I manager or an employee responsible for accepting customer vehicle deposits have access to perform the following duties: a. prepare bank deposits; b. take deposit to the bank; c. post deposits to the general ledger; d. reconcile the cash clearing and depository bank account; e. review the depository bank account; f. access the cash receipts function and data files?

Accounts Payable

1. Does the parts counter person or an employee assigned to issue and record purchase orders have access to perform the following duties: a. approve purchase orders; b. verify and sign-off on receiving reports; c. match receiving reports to invoices; d. post invoices into the accounts payable system; e. code and approve vendor invoices for payment f. review and follow-up on vendor inquires g. record returned items; h. prepare checks; i. sign checks; j. mail checks; k. reconcile the disbursement bank account; l. review the disbursement bank account; m. reconcile the monthly factory parts statement; n. access to accounts payable, purchasing functions, and data files?

Payroll

1. Does the employee responsible for hiring, terminating, and approving employee raises have access to perform the following duties: a. review and approve the payroll register; b. distribute payroll checks; c. handle unclaimed payroll checks; d. reconcile the payroll bank account; e. post payroll; f. sign checks; g. access payroll functions and data files?

The above-mentioned duties are not all-inclusive. However, understanding the conflict inherent in the duties listed above is a good way to start analyzing and monitoring internal control weaknesses within a dealership. Authorization, custody of assets, and recording or reporting of transactions are significant duties that must be segregated in order to prevent the opportunity for errors and misappropriation to go undetected.

Smaller dealerships tend to face more obstacles when implementing proper internal controls and segregation of duties because they lack the sheer volume of employees needed to properly separate various duties and functions. However, this obstacle can be overcome by utilizing responsible employees from different departments. Implementing internal controls and properly segregating duties within a dealership is not an easy task, but the time and energy spent to do it properly can and will prevent headaches and lost profits.

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