

INDIA HOME LOAN LIMITED



Segregation of Duties Policy

VERSION CONTROL

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1	Ravi Sharma	January 4, 2022	-		-

SEGREGATION OF DUTIES

SEGREGATION OF DUTIES DEFINED

Segregation of duties is critical to effective internal control because it reduces the risk of mistakes and inappropriate actions. Adequate segregation of duties reduces the likelihood that errors both intentional and unintentional, will remain undetected by providing for separate processing by different individuals at various stages of a transaction and for independent reviews of the work performed.

The basic idea underlying segregation of duties is that no employee or group should be in a position both to perpetrate and to conceal errors or fraud in the normal course of their duties. In general, the principal incompatible duties to be segregated are:

- Custody of assets
- Authorization or approval of related transactions affecting those assets
- Recording or reporting of related transactions
- Execution of the transaction or transaction activity

A detailed supervisory review of related activities is required as a compensating control activity if these functions cannot be separated in smaller departments.

No one person should:

- Initiate a transaction
- Approve a transaction
- Record a transaction
- Reconcile balances
- Handle assets
- Review Reports

Note: At least two sets of eyes are required for any transaction!

REQUIREMENT FOR SEGREGATION OF DUTIES (SOD) CONSIDERATIONS

Maintaining a system of effective internal control does require appropriate separation of responsibilities. If internal control is to be effective, there needs to be an adequate division of responsibilities among those who perform accounting procedures or control activities and those who handle assets. In general, the flow of transaction processing and related activities should be designed so that the work of one individual is either independent of, or serves to check on, the work of another. Such arrangements reduce the risk of undetected error and limit opportunities to misappropriate assets or conceal intentional misstatements in the financial statements. SOD serves as a deterrent to fraud and concealment of error because of the need to recruit another individual's cooperation, via collusion, to conceal it.

At the most basic level, segregation of duties means that no single individual should have control over two or more phases of a transaction or operation. Management should assign responsibilities to ensure a crosscheck of duties.

If a single person can carry out and conceal errors and/or irregularities in the course of performing their day-to-day activities, they have generally been assigned or allowed access to incompatible duties or responsibilities.

Duties or responsibilities can be broadly classified into:

- ❖ Authorization
- ❖ Custody
- ❖ Record-keeping
- ❖ Reconciliation

In an ideal system, different employees would perform each of these four major functions. In other words, no one person should have control of two or more of these responsibilities. The more negotiable the asset, the greater the need for proper segregation of duties, especially when dealing with cash, negotiable checks and inventories.

AUTHORIZATION

Authorization is the process of reviewing and approving transactions or operations.

Management authorizes employees to perform certain activities and to execute certain transactions within limited parameters. In addition, management specifies those activities or transactions that need supervisory approval before they are performed or executed by employees. A supervisor's approval (manual or electronic) implies that he or she has verified and validated that the activity or transaction conforms to established policies and procedures.

Authorization or approval is an important control activity. Authorization is the delegation of authority; it may be general or specific. Giving a department permission to expend funds from an approved budget is an example of general authorization. Specific authorization relates to individual transactions; it requires the signature or electronic approval of a transaction by a person with approval authority. Approval of a transaction means that the approver has reviewed the supporting documentation and is satisfied that the transaction is appropriate, accurate and complies with applicable laws, regulations, policies, and procedures. **Approvers should review supporting documentations, question unusual items, and make sure that necessary information is present to justify the transaction before they sign it. Signing blank forms should never be allowed.**

Approval authority may be linked to specific dollar levels. Transactions that exceed the specified dollar level would require approval at a higher level. **Under no circumstance should an approver tell someone that they could sign the approver's name on behalf of the approver. Similarly, under no circumstance should an approver with electronic approval authority share his password with another person.** To ensure **proper segregation of duties**, the person initiating a transaction should not be the person who approves the transaction. A department's approval levels should be specified in a departmental policies and procedures manual.

CUSTODY

Custody is the process of having access to, or control over, any physical asset such as cash, checks, equipment, supplies, or materials.

Liquid assets, assets with alternative uses, dangerous assets, vital documents, critical systems, and confidential information must be safeguarded against unauthorized acquisition, use, or disposition. Typically, access controls are the best way to safeguard these assets.

Separation of the custody of assets from accounting

This practice reduces temptation and fraud. For example, the bookkeeper should not handle cash, and the cashier should not have access to ledger accounts.

In a computerized system, a person with custody of assets should not have access to programming or any input records. Similarly, an individual who handles programming or input records should not have access to tempting assets.

Separation of authorization of transactions from the custody of related assets

To the extent feasible, persons who authorize transactions should not have control over the related asset. For instance, the same individual should not authorize the payment of a

supplier's invoice and also sign the check in payment of the bill. Nor should an individual who handles cash receipts have the authority to indicate which accounts receivable should be written off as uncollectible.

RECORD-KEEPING

Record-keeping is the process of creating and maintaining records of revenues, expenditures, inventories and personnel transactions. These may be manual records or records maintained in automated computer systems.

Documentation and record retention is to provide reasonable assurance that all information and transactions of value are accurately recorded and retained. Records are to be maintained and controlled in accordance with the established retention period and properly disposed of in accordance with established procedures.

RECONCILIATION

Reconciliation is verifying the processing or recording of transactions to ensure that all transactions are valid, properly authorized and properly recorded on a timely basis. This includes following-up on any differences or discrepancies identified.

Segregation of Duties Checklist

To enhance controls over the cash receipt process, the following compensating controls can be utilized:

- ✓ A lockbox system should be implemented to receive customer payments.
- ✓ Daily/ Weekly reconciliations of cash receipts to bank deposits, including lockbox receipts, should be performed.
- ✓ An employee who is independent of the cash receipts and deposit process should perform a detailed review of the accounts receivable aging or trial balance.
- ✓ **Internal audit** or an employee who is independent of the cash receipts process should periodically confirm accounts receivable balances with customers.

To enhance controls over the bank reconciliation process, the following compensating controls can be utilized:

- ✓ Perform a review of cash receipt and cash disbursement entries in the general ledger.
- ✓ Perform a regular analytical review of the cash receipts and disbursements entries.
 - ✓ Compare cash receipts and disbursement amounts to budgets.

To enhance controls over the procurement/ expenses process, the following compensating controls can be utilized:

- ✓ A system report of purchase/ expenses orders issued to vendors should be generated and reviewed by a supervisory-level employee who is not involved in initiating purchase/expenses orders with vendors.
- ✓ An employee independent of the purchasing/ expensing process checks the bills of lading to the receiving reports to inventory accounting.

To enhance controls over the cash disbursement process, the following compensating controls can be utilized:

- ✓ An employee independent of the accounts payable and disbursement process performs a review of a systems report outlining the Vendor Master File changes.
- ✓ Perform a regular analytical review of the cash disbursements.
- ✓ Require cash disbursement checks to have dual signatures.