

Risk Assessment for Modest-Sized Businesses



BY NICHOLAS JENNER, CPA, MSPC CERTIFIED PUBLIC ACCOUNTANTS AND ADVISORS, P.C.

Controllers and financial managers at modest-sized businesses can appreciate the challenges posed in successfully running financial operations. Not only is there the pervasive constraint of limited resources, there are also numerous decisions critical to successfully managing risk while not hampering commerce. Financial managers play a vital role in helping discern which facets of operations are most vital to success and the order in which they must be addressed.

Business Entity

First, determine what type of legal entity (C corporation, S corporation or LLC) will afford the proper legal protection and most favorable tax consequences. When making this decision, consider the legal latitude required for structuring compensation agreements, decision-making rights granted and proposals on how to dissolve or liquidate the business should the issue arise. One must work with legal counsel who can provide services commensurate with any and all legal matters, without placing too many constraints on the small business.

Financing

Another common consideration is financing, which can take the form of term loans, credit lines and lease obligations. Depending on the cyclical nature of the business, current borrowing rates, cash-flow management or the nature of a business' commerce, these credit facilities may have a place in the business' financing scheme. Financial managers often want to know whether they should lease or buy equipment, or whether a revolving or term credit facility is optimal. They have to ask themselves if they will have the short- and long-term liquidity to satisfy the obligation and if the associated

borrowing rates or guarantees are so severe that they place excessive burden on the company, posing an unnecessary risk.

Technology

A company also needs to invest in some form of accounting software that allows for adequate financial reporting of historical information, while allowing for projecting and forecasting future operations. Although measuring goals can be summarized qualitatively, the quantitative assessments via proper financial reporting are the cornerstone to successful financial and operational management. It's the universal means by which enterprises develop expectations, compare and contrast performance, and convey the entity's goals. There are numerous off-the-shelf software packages that are relatively inexpensive and afford a modest-sized business the reporting capacity needed based on the complexity of the business.

Smaller enterprises also often require only modest technological infrastructure to effectively operate. Commonplace service providers, such as banks and payroll processing companies, can usually provide the required resources. Because these types of services are typically conducted through the Internet, care should be taken to ensure they have sufficient internal controls over the propriety of information forwarded to them, manner in which it is handled at their organization and safeguarding of data or reports back to the company.

Insurance

Companies need to ensure sufficient insurance coverage based on the nature of operations and the industry. There are currently many insurance products available. However, companies should be cautious about purchasing more

specific policies that do not provide a sufficient cost/benefit based on resource constraints. Companies can use an insurance broker to navigate them through coverage, presuming the broker's paramount concern is offering the proper product based on the company's needs and resources.

Cash Flow

All companies have a universal concern: cash-flow management. I've often heard financial managers say, "Prior to this company, no one ever told me how hard it would be to collect money." Certain collection cycle pitfalls can be avoided by developing a routine discipline of pursuing past due balances, measured by key metrics such as days sales outstanding. Additionally, receiving funds via wire transfer and providing sales discounts for timely payment can help foster a prompt collection cycle.

The people I've met who become controllers or financial managers at modest-sized companies are generally pleased with their decision and, despite the challenges faced, believe the rewards outweigh the risks. This is due, in part, to their ability to manage risk through sound operational practices while pursuing new growth opportunities. 🧩

Nicholas Jenner, CPA, is a senior manager of quality control for MSPC Certified Public Accountants and Advisors, P.C. He is a member of the New Jersey Society of CPAs Accounting & Auditing Standards Interest Group. Contact Jenner at njenner@mspc-cpa.com or 908-272-7000.