

Basic Accounting Policies and Internal Controls

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People who operate with integrity are important to any church or organization (2 Kings 12:9-16); however, trust and honesty alone are never considered an internal control policy. Statistics repeatedly indicate that at any given time, 10% of any employee population are committing theft and fraud in some form, and 80% will do the same if given the opportunity. Unfortunately, my personal and professional experience confirms these statistics.

The concepts and policies summarized below reduce opportunities to commit fraud and promote operational integrity. These principles apply to any organization, large or small. Small churches should utilize the services of board members and volunteers with skills in the areas of financial and organizational management to customize cost-effective systems of internal controls. See handout, "Steps To Build Administrative Support."

Internal controls every church and organization should have in place (regardless of size).

Accountable Plans - Management must foster an ethical administrative work environment. In accounting, this is called "setting the tone at the top." The easiest way to lead and set the tone is to institute and submit to a cost reimbursement "accountable plan." Accountable plans are a set of simple policies that require all employees, leaders, volunteers, and even pastors to submit receipts along with a summary report every month to be reimbursed for operational expenses paid personally or with an organizational credit card. This simple policy, if followed, adds integrity and accuracy to any administrative department. Making everyone "accountable" for their spending will set the tone that management values financial accountability. See the attached handout "**Accountable Expense Reimbursement Plan**".

Budgeting - Management and Church leaders can also set the tone for financial accountability through proper use of budgeting. Your board should consist of persons who are skilled in this area. Budgeting is not placing limits on God. Instead, budgets are an analysis of resources provided and prayerfully using them for God's glory. Budgets are the financial framework for ministry. They are the primary oversight tool to prevent out of control spending. And most importantly, budgets force leadership to consider how to use ministry resources prayerfully. Budgeting is evidence of fiscal responsibility and good stewardship. See the attached handout "**Could your church Use and Accountability Tune-up**".

Separation of Duties - It is common for church leaders to give bookkeepers too much authority. Overworked and understaffed churches can be tempted to allow the bookkeeper to handle it all. However, do not let this happen. No one person should not have the authority to sign checks, open the mail, mail the checks, and record all the transactions within the bookkeeping system. Allowing one any person on your team to prepare the accounting records and to have the authority to sign checks, provides

the opportunity for that person to use and record church finances without oversight. The problem becomes compounded if the same person receives the mail. Under this scenario, church leadership has given someone the ability to perpetrate a theft or fraud and cover it up within the normal course of their duties. In accounting, we call this a set of “incompatible duties.” No individual should have the ability to have custody of an asset (cash or checks), sign checks or use cash, and record the transaction within the books. This is a recipe for disaster.

The best internal control policy is to separate incompatible duties. Do not allow any one person to have custody of an asset (cash, mail, equipment), the authority to purchase or dispose of an asset, and record the related transaction. For example, the bookkeeper can prepare monthly bills to pay and draft checks for signing. As a control have the bookkeeper present the checks for a signature to another person outside of accounting. That person will inspect checks and bills to pay, sign the checks, and then mail them. The second set of eyes has an opportunity to find mistakes and deter theft and fraud due to the natural separation of duties. For mail pick up, have a receptionist or similar office manager, separate from the church accounting department, open mail, date stamp, and deliver mail to all departments. This step reduces that chance that some will receive mail that they are trying to keep secret. Policies, as suggested above, promote transparency and integrity throughout the organization. See the attached handout “[Handling cash](#)”.

Reconciliation - The last “must have” internal control is reconciliation. The term “reconciliation” has an expanded meaning in accounting. Reconciliation is the process of comparing one set of records to another to verify that all transactions are recorded timely, accurately, and completely. Examples of common reconciliation are:

1. Bank statements to the check register.
2. Credit Cards statements to submitted receipts and accounting records.
3. Loan statements to the payments made and to accounting records.
4. Payroll records submitted to payroll processor to banking and accounting records.
5. Receipts to accountable plan reimbursement reports.

Reconciliations and separation of duties are the most effective and basic of all internal controls. Reconciliations are a very effective administrative and financial monitoring tool and most often used as compensating control for small office staff. I strongly recommend that reconciliations be completed within 15 to 45 days of month end. It is always best to have someone other than the bookkeeper reconcile bank statements and payroll accounts; however, this is not always practical. If the bookkeeper must perform these reconciliations, then, utilize a board member or another staff with accounting training to spot check and review the reconciliations monthly. This control creates an opportunity to double check accuracy and deter theft and fraud over key financial resources.

Consider this real-life example. A small not-for-profit hired a new bookkeeper. A board member was assigned to inspect the bank reconciliations performed by the bookkeeper each month. When it came time for the board member to inspect the bank reconciliations, the bookkeeper made excuses complaining they were sick and behind with the books. Consequently, the board member had nothing to review or reviewed bank reconciliations several months behind. Unfortunately, the board member granted concessions for many months. It turns out the bookkeeper was stealing cash and covering it up

in the books. Had the board member insisted upon completed and current bank reconciliations, the organization could have minimized its loss. Instead, my team and I discovered the fraud during an audit after this new bookkeeper had time to steal approximately \$16,000 to \$20,000 from the organization. To prevent bad publicity, the organization chose not to prosecute the culprit. No church or organization wants to be in this situation.

Enclosed is a handout describing considerations regarding receiving online donations.

Integrity starts with leadership. If leadership is committed to sound operational practices, protecting assets provided, and protecting the people God has placed into His service, then the church or organization will be *trust-worthy* to receive the gifts of the people.

Apply these concepts with the help of your board of directors, your local district, and your volunteers who have expertise in these areas. If you would like to receive training in financial or internal control matters, contact me at:

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