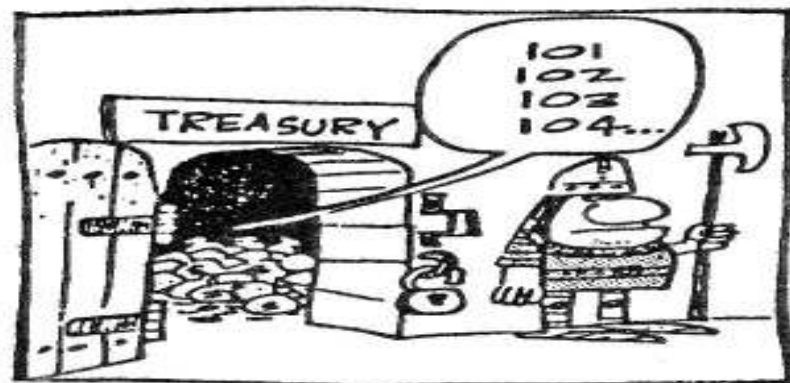


Internal Control: It's More Than A Locked Safe

1

**PRESENTATION FOR THE
NAD ORIENTATION FOR NEW TREASURERS
MARCH 30, 2016**

**Ann Gibson, PhD, CPA
Andrews University**



Purpose of Internal Control

3

The purpose of Internal Control is to:

Protect the assets of the organization

Ensure the reliability of the accounting records

Purpose of Internal Control

4

More specifically, internal control should:

Reduce the Risk of:

Misstatement due to error

Misstatement due to fraud

Fraudulent financial reporting
("cooking the books")

Misappropriation of assets (theft)

The Control Environment

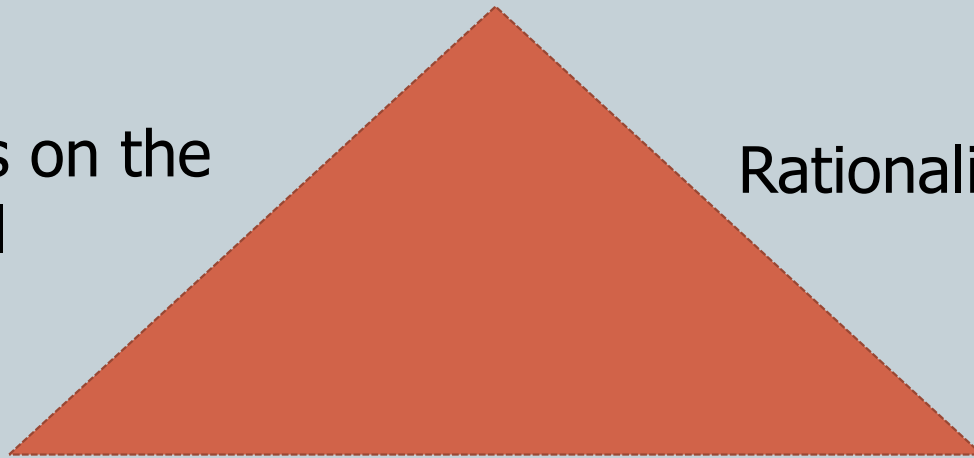
5

Control Pressure Points:

Pressures on the individual

Rationalization

Perceived Opportunity



Elements of Internal Control

6

Control Cues

Policy Communication

Record Keeping

Budgets

Reporting

Segregation of Duties

Elements of Internal Control

7

Control Cues:

The signals that management and the Board send about the importance of safeguarding the assets and the accuracy of financial reporting.

Elements of Internal Control

8

Policy Communication:

Written policies/procedure manuals

Communication via technological means

Elements of Internal Control

9

Record Keeping:

Common examples of good practices:

Pre-printed sales invoices, cash receipts,
checks

Use of an imprest petty cash system

Use of passwords for computer records

Use of a cash register for cash sales

Elements of Internal Control

10

Budgets:

Constant monitoring of the budget and investigation of any significant variations from the plan are effective forms of financial control.

Elements of Internal Control

11

Reporting:

Management should require regular monthly reports on the financial status of the organization.

Elements of Internal Control

12

Regular reports to management include:

Statement of Financial Position

Revenue and Expense Statements

Aged Accounts Receivable

Cash Flow Projections

Utilization Reports (such as payroll and related employee benefit cost reports or similar usage reports)

Elements of Internal Control

13

Segregation of Duties:

Establish responsibility for each task to one person

Separate the record keeping for the assets from the custody of the asset

Specifics for Segregation of Duties

14

Cash Receipts:

Use pre-numbered receipts

Be sure that no single person is responsible
for all aspects of the transaction

Deposit the cash in the bank as quickly as
possible—preferably daily

Specifics for Segregation of Duties

15

Cash Disbursements:

Make all disbursements by check

Use pre-numbered checks; use them in order

Store blank checks in a secure location

No checks should be made out to “Cash” or
“Bearer”

Only authorized individuals should sign the
checks

Do bank reconciliations monthly

Specifics on Segregation of Duties

16

Petty Cash:

Use as infrequently as possible

Keep the amount small

Reimburse monthly

No more than one or two custodians

Custodians should have no access to the
accounting records or cash receipts

Use imprest petty cash fund

Specifics of Segregation of Duties

17

Two-Person Segregation: Accountant and CFO

Accountant:

- Post accounts receivable
- Mail checks
- Write checks
- Post general ledger
- Reconcile bank statements
- Post credits/debits
- Give credits and discounts
- Approve payroll
- Open mail/receive cash
- Disburse petty cash
- Authorize purchase orders
- Authorize check requests
- Authorize invoices for payment

CFO:

- Sign checks
- Sign employee contracts
- Custody of securities
- Complete deposit slips
- Perform interfund transfers
- Distribute payroll
- Reconcile petty cash
- Record initial charges/pledges
- Approve employee time sheets
- Prepare invoices
- Complete check log

Specifics of Segregation of Duties

18

Three Person Segregation: CFO, Accountant, Bookkeeper

CFO

- Sign checks
- Sign employee contracts
- Custody of securities
- Complete deposit slips
- Perform interfund transfers

Accountant

- Prepares invoices
- Records initial charges/pledges
- Opens mail/receives cash
- Mails checks
- Approves invoices for payment
- Distributes payroll
- Authorizes purchase orders
- Authorizes check requests
- Approves employee time sheets

Specifics of Segregation of Duties

19

Three Person Segregation: CFO, Accountant, Bookkeeper

Bookkeeper:

Post accounts receivable

Reconcile petty cash

Write checks

Post general ledger

Reconcile bank statements

Post credits/debits

Give credits and discounts

Pressure Point Signals

20

Ineffective controls with reliance on the employees' sense of moral duty

Dominant leadership who does not wish to give authority to a control system

Overemphasis on enterprise goals which may override good business judgment

Pressure Point Signals

21

Lack of accounting orientation or education of staff, especially when volunteers are used

Failure to operate in a business-like fashion; a temptation for largely humanitarian organizations

Negative viewpoints regarding the accounting function

Pressure Point Signals

22

Over-reliance on one individual in the accounting function

Volunteer Boards; do not fail to require an audit

Lessening the Chance of Fraud

23

Provisions established by Sarbanes/Oxley (2002) that non-profits are incorporating:

CEOs and CFOs personally certify that the financial statements and disclosures are accurate and complete

Audit committees, composed of independent members and members with financial expertise, are required

Lessening the Chance of Fraud

24

Provisions of Sarbanes/Oxley Continued:

Establishment of a code of ethics for senior financial officers

Requirement that management attest to the effectiveness of the organization's internal controls

I/C for the Small Organization

25

Record all cash receipts immediately

Deposit all cash receipts intact daily

Make all payments by serially numbered checks; use an imprest petty cash fund for small disbursements

Reconcile bank accounts monthly

I/C for the Small Organization

26

Use serially numbered sales invoices and purchase orders

Issue checks to vendors after the invoices are matched with source documents and approved for payment

Balance subsidiary ledgers with control accounts monthly

I/C for Small Organizations

27

Prepare comparative financial statements monthly in sufficient detail to disclose significant variations in revenue or expense

Internal Controls

28

Questions?

References

Fleckenstein, M.P. and Bowes, J.C. (2000) “When trust is betrayed: Religious institutions and white collar crime.” *Journal of Business Ethics*, 23(1), p. 111-115

Lambert, J., Main, D., & Lambert, S. J. III. (1998). “Reduce Your Losses From Errors and Fraud.” *Nonprofit World*, 16(5), p. 46-48.

McEldowney, J.E., Thomas, L.B. & Ray, D. (1993). “Look Out for Cletus Williams.” *The CPA Journal*, 63(12), p. 44+

Tidwell, G. (1993). *Anatomy of a Fraud*. NY: Wiley