



# Internal Controls for Small Nonprofits

Best Practices

Bill Loughery, CPA

Manager, Public Sector

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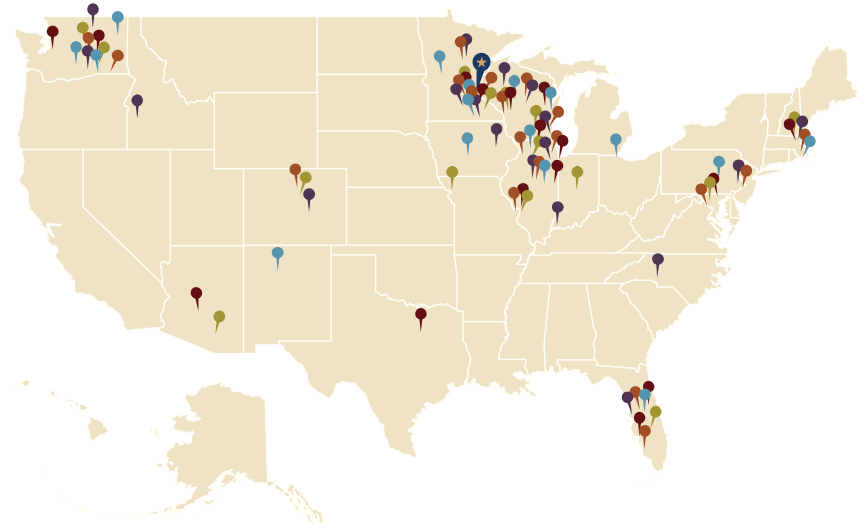
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- 3,600 employees
- Offices coast to coast
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# Learning Objectives

At the end of this session, you will be able to:

- Describe the general concepts and purpose of internal controls
- Discuss the control environment and risk assessment that create effective internal controls
- Identify risk areas that are common to nonprofit organizations
- Recognize key control activities (and personnel) specific to nonprofit organizations



# The Purpose of Internal Controls

- To safeguard assets
- To produce accurate accounting data
- To contribute to efficient operations
- To promote compliance with board policy and donor restrictions
  - **BONUS:** *An employee working under a good system of internal controls is more easily protected from suspicion should any shortages or discrepancies occur.*

Internal controls help to limit the **opportunity** to commit fraud.



# Basic Concepts

- Internal controls are a process
- People affect internal controls
- Internal controls provide reasonable, *not absolute*, assurance





# Internal Control Process Elements

- Control environment
- Risk assessment
- Control activities
- Information and communication
- Monitoring



# Control Environment

- Clear lines of authority with importance placed on internal controls
- Publicized code of conduct
- Formal budget process and regular review of variances
- Goal to attract and retain competent staff
- Effective board committees and internal audit functions

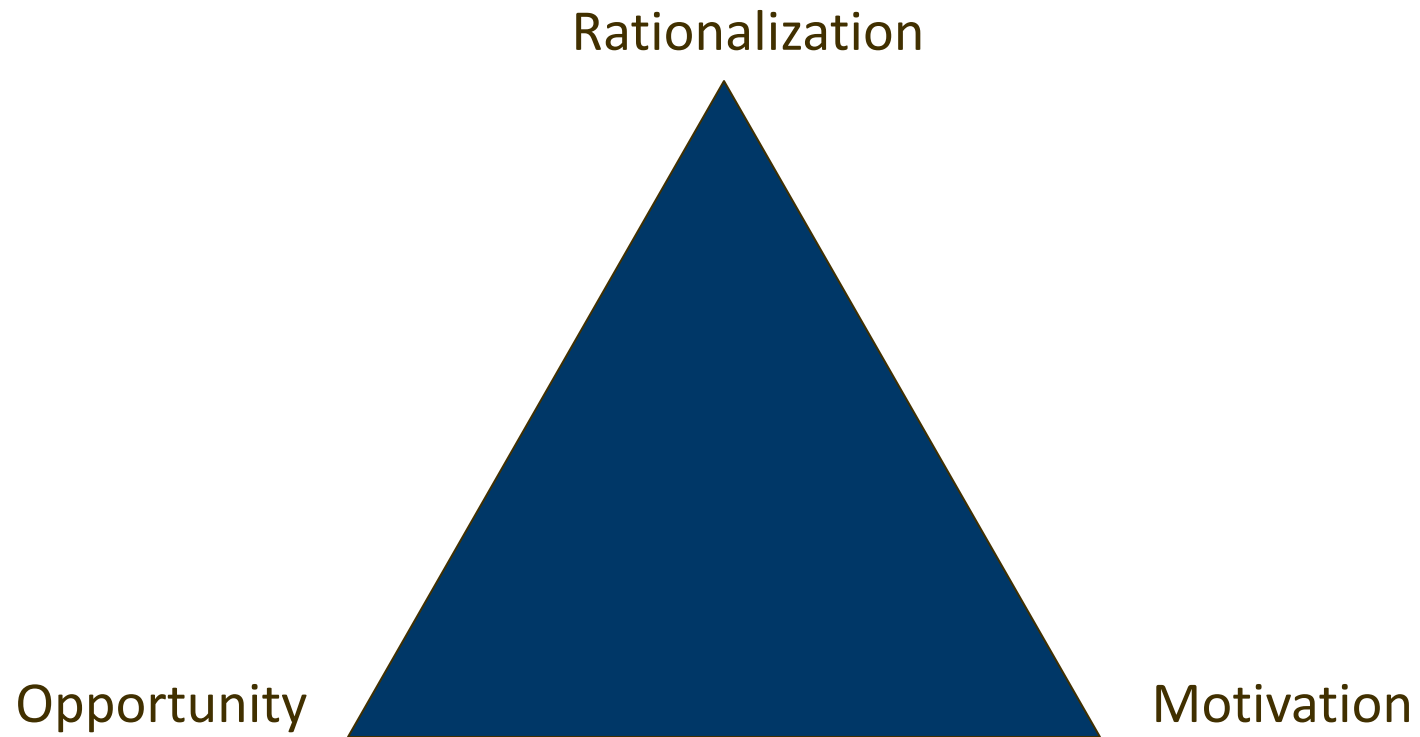


# Risk Assessment

- Clear objectives about operating, financial reporting, and legal compliance functions
- Entity-wide review to assess and evaluate risk



# Fraud Triangle



# Control Activities

- Segregation of duties
- Independent counting or confirmation of assets
- Controlled access to electronic data
- Adequate backup and data recovery procedures



# Information and Communication

- Support for developing and maintaining effective financial management information systems
- Publicized channels for employees or interested parties to report suspected fraud
- Documented procedures for handling reports of suspected fraud



# Monitoring

- Follow-up on reports of suspected fraud
- Prompt follow-up on budget versus actual variances
- Comparison of actual assets against accounting records
- Are the controls in place still being used?



# Who is Responsible?

- Finance committee
- Board
- Employees
- Volunteers





# Controls Risks Common to Nonprofits

- Limited personnel and resources
  - Accounting, HR, Payroll, Fundraising
- Executive leadership stretched too thin
- Disengaged or preoccupied board



# Specific Controls

## Financial Reporting

- Budgets
- Timely comparative financial reports
- Detailed chart of accounts
- Policy and procedures manuals
- Month end checklist & Calendar



# Specific Controls (continued)

## Bank Accounts

- Limited number of accounts
- Use of an entity name, not an individual
- Limited number of check signers
- Monthly reconciliations
- Regular review of cancelled checks and statements by independent party



# Specific Controls (continued)

## Disbursements

- Pre-numbered checks
- Use of checks for all major payments
- Verification/dual notification or authorization of electronic payments
- No pre-signed checks
- Alteration and retaining of voided checks
- Signers should not have access to the accounting records
- Require adequate support (original invoices with proper authorization) before writing checks
- Signed checks don't go back to accountant

# Specific Controls (continued)

## Cash Receipts

- Handling of cash independent of accounting:
  - ❖ Opening mail
  - ❖ Taking deposits to the bank
- List of all cash receipts should be made by someone without access to the accounting records
- Immediate endorsement of all receipts

# Specific Controls (continued)

## Fundraising

- Thank-you letters to donors
  - Who do donors call with questions?
- Regular reconciliation of donor databases to contribution revenue
- Tamper-proof collection bags
- Control access to safe
- Use of Desktop deposit



# Specific Controls (continued)

## Receivables

- Specific approval required for all write-offs
- Consider board approval above a certain dollar amount
- Allowance for doubtful accounts has special approval
- Regular review of delinquent accounts and aging reports



# Specific Controls (continued)

## Payroll

- Approval of payroll register independent of payroll processor
- Payroll register/change report goes directly to approver
- Independent review of W-2, W-3 reports
- Eliminate pay checks – use direct deposits
- Don't do your own payroll





# Specific Controls (continued)

## Internal Audits

- Procedures to review, vouch, or check the work of others
- Typical procedures:
  - ❖ Review of expense reports and credit card statements by the board/treasurer
  - ❖ Review bank statement for unusual activity
  - ❖ Review journal entries
  - ❖ Reconcile donations to deposits
  - ❖ Committee to select and vouch expenses or have all invoices on hand at committee meeting

# Month End Checklist & Accounting Calendar

- Requirements:
  - Written
  - Daily tasks
  - Weekly tasks
  - Monthly tasks
    - ◇ Journal entries required and who is responsible
    - ◇ Reconciliations required and who is responsible
    - ◇ Other
  - Annual tasks
  - Dates of meetings that need reports
  - Deadlines



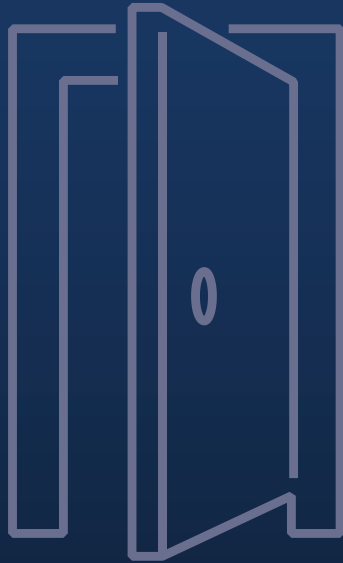
# Statistics

Position	% of Incidents	% of Losses
Executive	9	20
Electronic Data Processing Support Staff	19	22
Accounting	13	13
Treasurer	7	6
Collusion	39	32
Warehouse	13	7

(Statistics provided by the Federal Bureau of Investigation)

# Questions?





**Bill Loughery, CPA**  
**Manager**  
**[william.loughery@claconnect.com](mailto:william.loughery@claconnect.com)**  
**267-419-1156**

[CLAconnect.com](http://CLAconnect.com)