

# Internal Control Best Practices for Non-Profits



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# Overview

- *Internal control* is a process—effected by an entity’s board of directors, management, and other personnel—designed to provide reasonable assurance of:
- (a) reliability of financial reporting,
  - (b) effectiveness and efficiency of operations, and
  - (c) compliance with applicable laws and regulations.

# Overview

## → Internal controls:

- Are an ongoing process
  - They don't just happen once
- Are not one size fits all
  - Can be preventative or detective
  - Different sized organizations will have different controls
- Help reduce risk, they don't eliminate risk
- Do not guard against collusion
  - When two or more people are working together
- Work best with one person “doing” and another “checking”



# Trust Is NOT An Internal Control

- Controls should be blind to the individuals performing a task
- Having control procedures does not mean we don't trust people
- Controls help honest people stay honest



# Risk Assessment

- ➔ The internal control process starts with risk assessment
  - Consider your organization's operations
    - Think about the different transaction classes: cash receipts, disbursements, payroll, etc.
  - Think about where things could go wrong
    - For example, could incoming cash could be lost or stolen
  - Consider the scope/magnitude of what could go wrong
    - How much could be lost or stolen?
  - Consider what controls are in place and what controls could be added to mitigate those risks
    - Chances are you have some controls in place already, even if they are not formal
  - You may choose to accept some risk
    - Consider the cost benefit of making changes, extra processes may not be efficient

# Cash Receipts

## → Open mail with two people

- At least have two people present
- Or have two people helping to make process faster
- Or have two people in place during peak times – usually around holidays or events

## → Stamp checks for deposit only

## → Log checks and sign off on log

- This can be done on an electronic spreadsheet and printed out

## → Compare log to deposit slips or bank statement

- This is the most important step

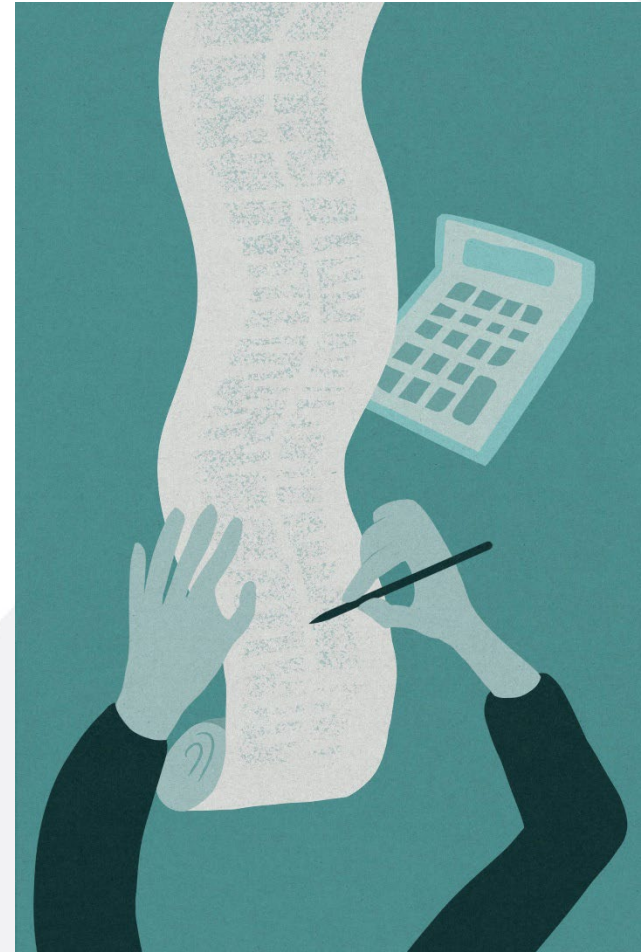
# Cash Receipts

- Reconcile the donor database - Formalize this process and do at least twice a year
  - There may be differences between how some things are recorded (like pledges), but they can be accounted for
- Keep donor restriction letters if received and/or track restrictions on a spreadsheet
  - This is important information that the accountant needs
- Have two people receiving cash at special events
  - Have a log of beginning and ending cash and sign off



# Cash Receipts

- Reconcile the player rosters to registration fees
  - Multiply the number of players by the expected registration fee and compare that figure to the associated revenue account
  - This process could detect if registration fees were stolen and not deposited to the organization's bank account



# Cash Receipts

## → Perform trend analysis

- Compare fees like registration fees or parking to other months/years
- Investigate any significant changes

# Cash Disbursements

- Authorized signor or individual reviews supporting documents **before** signing and someone marks the invoice “paid” after signing
  - This helps prevent bills from being paid twice
- Signor mails or gives checks to a person to mail who doesn't have access to accounting software
  - This prevents altering the check and hiding the change in the accounting software

# Cash Disbursements – Credit Cards

## → #1 Cause of fraud

- Personal use
  - Outside fraud
  - Theft of organization's points
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- Match receipts to statement and look for unusual transactions
  - Periodically assess who has credit cards, if they need them, and their credit limits
    - ✓ May only need cards during certain times of the year like for a fundraiser. Can change limit for when users need an increased limit
  - A board member should review the ED's credit card statement
    - ✓ In most cases, there isn't an appropriate alternative

# Cash Disbursements - Payroll

- A supervisor should review and approve timesheets for supervisees
  - It's ok if this is done online
- ED or board member should review the payroll report for changes to wage rates, fake employees, inflated hours, etc.
  - Should have a budgeted number in mind
- Someone not involved in processing payroll should be alerted when new employees are set up or rate changes
  - Maybe someone at the board level
- Keep authorized wage rates in personnel files
  - Helps prevent any confusion

# Bank Statement Review

- Perform reconciliation procedures monthly
  - The review of the reconciliation and statement should be done at least quarterly
- Look for old and odd reconciling items such as journal entries
- Review electronic payments and transfers
  - Look for unusual amounts or payees
- A person independent of the check writing process should review check images
  - Adding check images to the bank statement makes this procedure much easier!
    - Should be looking at the payee and signature

# Investments

- If investments are sizeable, have a quarterly statement sent to a board member
  - Having an extra set of eyes can be a good preventative control
- Set a policy with the brokerage to limit cash withdraws to the organization's checking account
  - To prevent the account from being wiped out by an authorized or unauthorized person
- Require two signatures/approvals for withdrawals over a certain dollar amount
  - May take quarterly disbursements for operations, set the threshold amount to just over what is normally pulled



# Physical and Logical Access



- Lock up
  - Sensitive paper files
  - Check stock
  - Signature stamps (if you have them)
- Control access to network drives
- Don't share passwords



# Journal Entries

## Journal Entries

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+ ED or board member should review a system prepared journal entry report for odd or suspicious journal entries at least quarterly

- They should review supporting documentation for any items identified as out of the ordinary

# A/R and Pledge Write Offs

- Should be approved by someone without access to accounting software that doesn't receive payments



# Governance

- One of the best controls can be to have an active engaged board
- Receive internal financial statements at least quarterly, compare them to budget, and ask questions
- Understand internal control procedures in place and periodically walk through them with staff to ensure they are functioning properly
  - Consider walking through a transaction class once or twice a year

# Falsified Documents

- Bank statements, credit card statements, receipts, and QuickBooks reports can easily be falsified with a PDF editor or in Microsoft Excel
- Consider periodically pulling source documents yourself or having copies of reports sent directly to you.

# Resources

- <https://www.councilofnonprofits.org/running-nonprofit/administration-and-financial-management/internal-controls-nonprofits>
- <https://www.wegnercpas.com/resources/>

# Questions

