

Internal control is a good thing

By Tommy Wooten, John Coker and Robert Elmore

Recent high profile cases of financial mismanagement in religious organizations have brought financial control in religious organizations to the attention of the public.

Every church should be concerned about financial management and mismanagement in their organization. It must be a priority of the church leadership to protect the church, its membership and staff.

Unique problems of religious organizations

First, religious organizations rely heavily on volunteer management. Most financial programs of churches are overseen by volunteer treasurers or finance committee chairs. These individuals may lack skills in internal control design and information system development. For those larger organizations that do have a full-time accounting staff, these individuals are often more like bookkeepers with little training outside of how to do the daily accounting routine.

Second, there is an overlying sense of trust in a religious organization. In many religious organizations there is the belief that no one would purposely misuse or misappropriate the organization's money, so "we need only a few controls in place." Controls are often seen as unnecessary because "we do not have the same temptations and pressures of a traditional for-profit business." This sense of trust and "higher calling" often motivates organizations to put much less emphasis on sound internal control policy.

Third, religious organizations are more likely to receive unrestricted donations in cash. For churches, most donations are general receipts of cash with little specific follow up or specific expectations by the donor. Without specific expectations or accountability regarding this cash, volunteers may have a tendency to be less diligent about the control and use of this cash.

What is internal control?

Internal control is the structure, policies and procedures established by the organization to provide reasonable assurance that assets are safeguarded, information is reliable, operations are efficient and effective, and that

management's policies are adhered to. It is the boundary around the organization's processes to ensure things are done correctly. Internal control is a safety net for the organization and the individuals that make up the organization.

A common misconception is to think that internal control exists only for the purpose of catching and preventing fraud. This misconception often discourages religious organizations from implementing sound control policies because they don't want to appear to be untrusting.

However, internal controls are not put in place primarily to try to catch fraud. The controls are designed to help prevent putting individuals in a situation of making errors or from being tempted to engage in questionable transactions. Internal control is for the protection of the individuals as much as for the protection of the organization.

The Bible teaches that there is no one who is beyond temptation and sin, and church members are no exception. The last thing we need to do is put in place such a poor system of control that actually tempts the staff and volunteers to be dishonest. Rather, we want the system to encourage honesty and sound judgment. We want a system that protects the staff and volunteers in case there are any questions or accusations. The staff should be comfortable knowing that any questions about their individual financial dealings on behalf of the church are all blameless because everything is well documented, approved and in order, according to policy.

Controlling the environment

The foundation of any internal control system is called the control environment. It is the attitude of the organization and its leaders towards internal control. It includes the leaders' commitment to excellence, integrity and competence of the organization. An organization with a strong control environment will have a sound management philosophy, operating style and structure. It will have strong policies and procedures that help employees make good, ethical decisions.

Senior leaders of the organization must believe and

understand that strong internal controls are good for the organization. They must impress upon the staff and membership that following the adopted policies protects both the organization and individuals from actual harm (errors, fraud, bad decision making) and perceived harm (temptations, accusations, suspicions). Otherwise, reporting will not be enforced and employees will get the message that internal control is not important.

Internal control quiz

What type of control environment does your church have? Here are some characteristics of churches that believe internal control is important.

They prepare a written procedures manual. A recent survey indicated that only 24 percent of churches have a written manual covering their accounting and financial policies. Churches should formally document their financial policies and procedures. Such a manual would serve to eliminate confusion about the way things are done among church employees and especially the volunteers that the church uses for some of the accounting functions.

This is also especially helpful in the case of job turnover among the persons with accounting responsibilities. The lack of manuals and formal documentation does not imply that the financial records are incorrect; however, it raises the risk that monies will be handled inconsistently and that errors will occur. This documentation would allow for consistent application and understanding of the practices of the organization. It allows the leaders of the organization to formally agree on the process for administering and reporting the financial activities of the organization.

They adopt a clear organizational structure. A strong 80 to 90 percent of all churches report having finance committees and an annual budget adoption process. Churches with strong controls give these committees clear goals and procedures in partnering with the staff to administer the financial program of the church. These committees should not be "rubber stamp" committees, nor should they be adversarial committees always at odds with the goals and dreams of the staff and the membership.

They segregate incompatible duties. For best protection, churches should segregate the duties of authorization, recordkeeping and custody. For example, the minister that authorizes the purchase of the new Sunday school materials should have nothing to do with recording the purchase in the accounting records. The person that made the accounting entry should not be the one who signs the check for payment. Another example is that the person

involved with preparing the bank reconciliation should not have access to the cash receipts and disbursements. To ensure that these conflicting duties are segregated, require someone independent to reconcile the bank statement.

They receive an annual audit from a qualified CPA

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or CPA firm. An audit allows for external, independent oversight over the financial statements of the organization. Not only would an audit provide assurance related to the organization's financial reports and records, but the auditors would be expected to make recommendations to strengthen the church's financial accounting practices and internal control. This would have long-term benefits and would correct any deficiencies in internal control. An audit could be done through a church member, for a small fee, or even perhaps on a pro bono basis from an outside firm.

They use computerized accounting software. Each church should take advantage of computer software to track and report financial results. A number of software packages are available that do not require a great deal of accounting knowledge to operate.

Due to growth, lack of resources or lack of priority, many organizations find that the managing of the organization's finances does not get the attention needed to ensure proper control. Protecting your staff, your employees, your donors and your members must be a high priority.

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