

Diocese of Covington

Policies & Procedures Manual

Section: Compliance – Accounting

Policy: Internal Control & Segregation of Duties



“Internal Control” refers to the policies and procedures established to provide reasonable assurance that parish assets are safeguarded, that accountability is achieved, and that errors in financial records will be less likely to occur and are likely to be identified. It is a means by which an organization’s resources are directed, monitored, and measured. It plays an important role in preventing and detecting fraud and protecting the organization’s resources, both physical (e.g. cash, property, equipment, etc.) and intangible (e.g. reputation).

Effective internal control typically has five components:

1. *Control Environment* – sets the tone for the organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control.
2. *Risk Assessment* – the identification and analysis of relevant risks to the achievement of objectives, forming a basis for how the risks should be managed.
3. *Information and Communication* – systems or processes that support the identification, capture, and exchange of information in a form and time frame that enable people to carry out their responsibilities.
4. *Control Activities* – the policies and procedures that help ensure management directives are carried out.
5. *Monitoring* – processes used to assess the quality of internal control performance over time.

These components are designed to provide reasonable assurance that particular objectives are achieved. The specific target used to determine whether a control is operating effectively is called the *control objective*.

Control objectives fall under several detailed categories as follows:

1. *Existence (Validity)* – Only valid or authorized transactions are processed (i.e., no invalid transactions).
2. *Occurrence (Cutoff)* – Transactions occurred during the correct period or were processed timely.
3. *Completeness* – All transactions are processed that should be (i.e., no omissions).
4. *Valuation* – Transactions are calculated using an appropriate methodology or are computationally accurate.
5. *Rights & Obligations* – Assets represent the rights of the company, and liabilities its obligations, as of a given date.
6. *Presentation & Disclosure (Classification)* – Components of financial statements (or other reporting) are properly classified (by type or account) and described.
7. *Reasonableness* – Transactions or results appear reasonable relative to other data or trends.

Based on the above parameters as described, a system of good internal control requires that, at a minimum, the following are present at a parish:

Healthy Financial Environment

The pastor and parish leadership, including the Parish Council and Finance Council, must commit to establishing and monitoring effective financial policies and procedures. All persons, either volunteers or paid employees, who accept responsibility for the raising or spending of parish funds, or custody of the material goods of the parish, must also accept the responsibility to abide by the internal financial controls established by the parish. However, it should be clearly understood that the pastor is ultimately responsible for sound fiscal management of the parish. Delegation to others of fiscal tasks or procedures does not mean the pastor’s responsibility has been removed. It does, however, make it easier for him to effectively and efficiently carry out his responsibilities.

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Organizational Structure

The proper allocation of responsibility and authorization of transactions is essential to good internal control. In general, no one person should be responsible for handling all aspects of a transaction. For example, a person who authorizes a transaction should not record the transaction nor should that person have custody or control over the asset being purchased or the services being performed. Other examples of transactions which should be segregated include:

- Handling of cash receipts and recording of cash receipts.
- Authorizing expenditures, verifying invoices and preparing checks in payment of invoices.
- Preparing checks and signing checks.
- Counting the collection and recording the deposit in the records or posting to the individual donors' accounts.

Staff size may limit a parish's ability to segregate duties in a practical manner. In some smaller parishes, the bookkeeper may perform most of the procedures on a monthly basis. In those instances, the ability of the bookkeeper to authorize and execute transactions should be limited to the greatest extent practicable. To the extent that otherwise appropriate segregation of functions is not practical, the Parish Finance Council should consider performing procedures with the objective of offsetting the resulting deficiencies in the internal control.

A sample chart showing an example of how duties can be delegated is included in **Appendix A** of this policy. It demonstrates how duties/functions can be delegated in smaller staff environments and still be in compliance with good internal control objectives. Staff sizes of two, three or four employees are included.

Parish Accounting System

Most financial information needed by the parish comes from the accounting records. To be of maximum value, the information must be reliable, complete and available as quickly as possible. All parish employees that use the accounting system should be fully trained and capable of using the accounting system appropriately.

Internal Control Self-Evaluation

Each parish should be focused on implementing good internal control processes and procedures. A good tool to use for self-evaluation is the "Internal Control Questionnaire" that is used in the Agreed Upon Procedures (AUP) audits of parishes. The document can be found on the diocesan website in the "Agreed Upon Procedures Parish Audit" section of the Parish Policies and Procedures webpage. It should be reviewed periodically by parish management – preferably no less than annually. This is also the document that external auditors will use when auditing a parish during the AUP audit.

The AUP Internal Control Questionnaire is somewhat lengthy at 11 pages and over 80 questions. As an alternative, a parish could use an abbreviated internal control self-evaluation tool. **Appendix B** contains just such an abbreviated checklist.

Policies and Procedures Manual

A good internal control system must include certain policies and procedures with respect to the financial transactions of the parish, such as how to handle cash receipts, disbursements, bank reconciliations, etc. This manual contains Diocesan policies to be implemented at each parish. If desired, the parishes may establish more stringent policies than those described herein.



**APPENDIX A
TWO PERSON STAFF**

Business Manager	Pastor/Administrator
<u>Accounts Payable</u> <ul style="list-style-type: none"> Process vendor invoices Write checks Mail checks Reconcile bank statements Disburse petty cash <u>Accounts Receivable</u> <ul style="list-style-type: none"> Receive/count cash collections Record AR/Cash entries <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Record GL entries Review and approve payroll 	<u>Accounts Payable</u> <ul style="list-style-type: none"> Authorize purchase orders, check requests and vendor invoices Sign checks Open and review bank statements Reconcile petty cash <u>Accounts Receivable</u> <ul style="list-style-type: none"> Prepare deposit slips Take deposit to bank <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Approve employee time sheets Distribute payroll checks Approve/sign teacher and principal contracts

THREE PERSON STAFF

Bookkeeper	Business Manager	Pastor/Administrator
<u>Accounts Payable</u> <ul style="list-style-type: none"> Process vendor invoices Write checks Reconcile bank statements Reconcile petty cash <u>Accounts Receivable</u> <ul style="list-style-type: none"> Prepare deposit slips Record AR/Cash entries <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Record GL entries 	<u>Accounts Payable</u> <ul style="list-style-type: none"> Authorize purchase orders Authorize check requests Authorize vendor invoices Mail checks Disburse petty cash <u>Accounts Receivable</u> <ul style="list-style-type: none"> Receive/count cash <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Approve employee time sheets Review and approve payroll Distributes payroll checks. 	<u>Accounts Payable</u> <ul style="list-style-type: none"> Sign checks Open and review bank statements <u>Accounts Receivable</u> <ul style="list-style-type: none"> Take deposit to bank <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Approve/sign teacher and principal contracts

FOUR PERSON STAFF

Clerk	Bookkeeper	Business Manager	Pastor/Administrator
<u>Accounts Payable</u> <ul style="list-style-type: none"> Authorize purchase orders and check requests Mail checks Disburse petty cash <u>Accounts Receivable</u> <ul style="list-style-type: none"> Receive/count cash <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Distribute payroll checks 	<u>Accounts Payable</u> <ul style="list-style-type: none"> Writes checks Reconcile bank statements Reconcile petty cash <u>Accounts Receivable</u> <ul style="list-style-type: none"> Record AR entries <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Record GL entries 	<u>Accounts Payable</u> <ul style="list-style-type: none"> Process vendor invoices Authorize vendor invoices <u>Accounts Receivable</u> <ul style="list-style-type: none"> Prepare deposit slips <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Approve payroll 	<u>Accounts Payable</u> <ul style="list-style-type: none"> Sign checks Open and review bank statements <u>Accounts Receivable</u> <ul style="list-style-type: none"> Take deposit to bank <u>Payroll & General Ledger</u> <ul style="list-style-type: none"> Approve/sign teacher and principal contracts Approve employee time sheets



APPENDIX A
INTERNAL CONTROL CHECKLIST

How to use this checklist

Review the concept for each internal control area and answer the questions following each section. Each 'yes' answer identifies an area that needs stronger internal controls. Such deficiencies should be corrected as soon as possible to protect parish assets and financial records.

Segregation of Duties

CONCEPTS:

- Certain accounting and bookkeeping functions are designed to cross-reference each other for accuracy. If the same person is responsible for multiple duties, the natural check and balance system is removed and/or circumvented.
- Trust is not the issue; the issue is verifying business transactions. Giving a single person unquestioned authority of your finances is not a wise business practice.

CHECKLIST (each 'yes' answer is a potential problem area):

- Is the person who handles your cash also responsible for recording cash?
- Does the person who pays or orders materials/supplies for the parish also responsible for receiving and/or approving the invoice?
- Are two or fewer people responsible for the accounting function?
- Is there only one person responsible for reviewing financial statements each month?
- Is the review of financial journal entries and transactions sporadic?

Supporting Documentation

CONCEPT:

- Enhances communications and serves as a final check point.

CHECKLIST (each 'yes' answer is a potential problem area):

- Are blank checks ever signed?
- Are checks ever signed without original supporting documentation?
- Supporting documentation is rarely verified against the actual check written?
- Are checks ever signed without canceling (i.e. initialed, approved, stamped, etc.) the supporting documentation?
- Are checks mailed by the check preparer?
- Are funds ever transferred between accounts by one person without review or verification?
- Are checks ever signed for new business vendors without knowing and/or verifying their name and association with the parish?



Bank Reconciliations

CONCEPTS:

- Bank statements can only flag discrepancies if they are reconciled on a timely basis. Reconciliations should be done once a month. Bank adjustments need to be tracked carefully from one month to the next.
- Segregating duties is very important in this area. Reconciliations should be performed by one person and reviewed by another. Also, the person who writes the checks should not have authority to sign checks.

*CHECKLIST (each **'no'** answer is a potential problem area):*

- Are canceled checks and endorsements reviewed on a monthly basis?
- Are payroll checks compared with your current employee records?
- Are funds transferred between bank accounts reviewed closely?
- Are the number of credit card statements paid tracked each month?
- Are bank reconciliations performed on a timely (and monthly) basis?
- Is someone responsible for reviewing reconciliations each month?
- Are reconciled items verified?
- Does the pastor (or someone independent of the account and bank reconciliation process) receive, open and review the bank statement prior to turning it over to the person who performs the bank reconciliation? A good review would include at least the following:
 - ✓ Looking for unusual payees
 - ✓ Verifying the check signatures
 - ✓ Reviewing amounts for reasonableness
 - ✓ Looking for signs of alterations to checks and deposit slips
 - ✓ Review all ACH/Wire transfers for unusual or unfamiliar items
- Does the pastor and/or Parish Council and/or Finance Council review all completed bank reconciliations?

Employees & Personnel

CONCEPT:

- Know your employees and be aware of changes in behavior.

*CHECKLIST (each **'yes'** answer is a potential problem area):*

- Are employees extremely possessive of their work records and reluctant to share their tasks and duties?
- Are employees apprehensive about vacation and time off while always being the first in the office and last out?
- Have you noticed a substantial change in lifestyle in any of your employees?
- Do any employees appear to be living beyond their means?
- Are employees ever hired without first checking references or doing a background check?
- Are accounting personnel permitted to work longer than a year without taking a vacation or time off?
- Are there any accounting staff or key personnel that are not secured with a fidelity bond?

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Safeguarding Assets

CONCEPT:

- List and monitor access to important assets, documents, and supplies.

CHECKLIST (each **'no'** answer identifies a potential problem area):

- Are blank check stocks safely secured?
- Are signature stamps prohibited?
- Are checks restrictively endorsed upon receipt?
- Are cash and checks deposited daily, or kept in a limited access and locked safe?
- Is a list maintained of all office furniture, equipment, company vehicles and all other assets?
- Is adequate insurance coverage in place for assets?
- Are all computers (workstations and network) backed up on a daily basis?
- Are all computer/network backups stored off-site on a regular basis?
- Are all computers and programs password protected?
- Are passwords required to be changed on a regular basis; i.e. at least every 6 months?