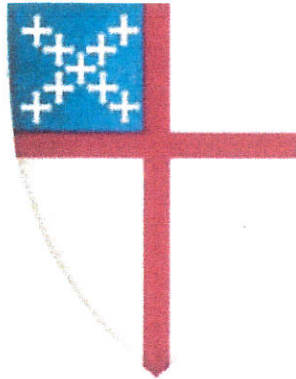


Audit Program for Internal Auditors of All Saints Church



All Saints Church

3 Chevy Chase Circle

Chevy Chase, Maryland 20815

Dear Congregation and Fellow Auditors:

The task of auditing a Church is not a simple task. However, it is an act of stewardship that should be commended by all of those involved in the Church. Likewise, the task of compiling this manual was not an easy task. As such, we are thankful to the authors of the audit manuals that came before this one, particularly the ones listed in the sources section of this guide. These sources include *The Manual of Business Methods in Church Affairs*, which is published by the Episcopal Church (In accordance with Title I, Canon 7, "Of Business Methods in Church Affairs", and Resolution D-147 (1979 GC): "Accounting Principles and Practices for Dioceses, Parishes, and Other Congregations": COPYRIGHT 2007, 2009, 2012 The Domestic and Foreign Missionary Society of the Protestant Episcopal Church in the USA). {Of Note: The opening letter of the subject Manual states, "The Canons of the Episcopal Church set forth the general responsibility and accountability for the stewardship of the Church's money and property. Title I, Canon 7 (pages i2 – i3 in this Manual) specifically addresses the business methods prescribed for every diocese, parish, mission, and institution subject to the authority of the Episcopal Church. This Manual identifies requirements and seeks to provide helpful advice on sound, practical internal controls, accounting guidelines and business practices. We believe that it can be a tool that will support your efforts to perform the duties and responsibilities of your office."}

This program has been designed to help you in conducting the internal audit of our Church.

Audit Committee of All Saints Church

Acknowledgements

Primary Sources

"The Manual of Business Methods in Church Affairs", which is published by the Episcopal Church (In accordance with Title I, Canon 7, "Of Business Methods in Church Affairs", and Resolution D-147 (1979 GC): "Accounting Principles and Practices for Dioceses, Parishes, and Other Congregations": COPYRIGHT 2007, 2009, 2012 The Domestic and Foreign Missionary Society of the Protestant Episcopal Church in the USA.

"Internal Control Standards for the Public Sector", Standard INTOSAI GOV #9100, annex 2

"The Audit Committee Toolkit", AICPA, New York; 2004.

"CPA Journal AC Responsibilities". Nysscpa.org. Retrieved 2012-09-22.

"Audit Committee Effectiveness: What Works Best-2nd Edition." Institute of Internal Auditors and Price Waterhouse. Altamonte Springs, FLA; 2000.

Purpose of this guide:

This program is intended to be used by an internal auditor and/or members of an internal audit committee within All Saints Episcopal Church, Chevy Chase, MD. This internal audit program is not intended to be and should not be used as a substitute for an external audit conducted by a certified public accountant. This program is intended to supplement an external audit. It should be used by the internal auditor(s) to help them prepare for an audit conducted by a certified public accountant. By following the instructions contained in this guide, you may be able to reduce the cost, better plan for, know what to expect from, and improve the effectiveness of your external audit.

This audit program has been compiled by the audit committee of All Saints Church. Also, it should be noted that All Saints Church, its Rectors, clergy, staff, agents and congregation is not providing legal or financial advice through this publication, nor can it be responsible for the conduct of external audits. It must be emphasized that this guide is not a substitute for regular audit programs developed by a certified public accountant and should not be used as such. Internal auditors should always seek assistance and advice on specific issues from professional accountants and auditors.

Reasons for an audit

The Church recommends that an external audit be conducted at a minimum on an annual basis. This is because an audit is the best way for the church to protect the clergy, those persons it elects to offices of financial responsibility and members of the congregation from unwarranted charges of carelessness, accident or improper handling of funds. **It is not a symbol of distrust.** In addition, since church committees, treasurers, finance committees, clergy/chaplains, and other persons in positions of responsibility "are liable for any losses which would have been discovered by an ordinary audit but were not discovered because they failed to have the audit conducted" (Manual of Business Methods in Church Affairs, Episcopal Church, p. 8), the costs of dishonesty or mismanagement, intentional or accidental, on the part of those entrusted with church funds are likely to be far higher without an internal audit [than the cost of having an external audit performed]. To the point, just as we allocate money in our church budgets to pay the costs of insurance, it makes sense to allocate money for periodic audits (Manual of Business Methods in Church Affairs, Episcopal Church p. 4).

There are two basic forms of audit:

(1) Internal Audit (described in more detail below and the true subject of this manual) involves the consistent ongoing monitoring of sound, practical internal controls, accounting guidelines and business practices. We believe that it can be a tool that will support the efforts of clergy and congregation alike to perform the duties and responsibilities of benefit to the Church and the world outside of our Church walls. A well designed Internal Audit and reporting system should assist you in fulfilling the responsibilities for the financial oversight of All Saints Church. Practical internal controls are the cornerstone of the best financial management. Management of financial resources is an important element of stewardship. The Church has entrusted us with

the funds placed in its hands for mission and ministry. We honor this trust by caring for detail and acting accountably. Treasurers at all levels in the Church are custodians of this trust.

(2) External audits are those audits conducted by a certified public accountant according to GAAP (Generally Accepted Accounting Principles) and/or formal or uniform accounting principles for any type of not-for-profit organization (NFPO), including churches, as issued by the Financial Accounting Standards Board (FASB). Annual audits are required by the Canons of the Episcopal Church for all parishes, missions, and other institutions. "The primary purpose of an audit is to assure that financial statements are fairly stated. Any person handling the monies or investments of the church needs an audit to protect the church assets and him/her against suspicion of mishandling those assets. Similarly, rectors, vestries, vicars, bishop's committees, treasurers and other persons in positions of responsibility may be liable for any losses which would have been discovered by an ordinary audit but were not discovered because they failed to have an audit conducted." (Manual of Business Methods in Church Affairs, Episcopal Church, p. 5)

Annual external audits are required by the Canons of the Episcopal Church for all parishes, missions, and other institutions. The content and extent of annual external audits is outlined in *The Manual of Business Methods in Church Affairs*, which was published by the Episcopal Church (In accordance with Title I, Canon 7, "Of Business Methods in Church Affairs", and Resolution D-147 (1979 GC): "Accounting Principles and Practices for Dioceses, Parishes, and Other Congregations": COPYRIGHT 2007, 2009, 2012 The Domestic and Foreign Missionary Society of the Protestant Episcopal Church in the USA – updated online monthly or as necessary.

The primary purpose of an audit is to assure that financial statements are fairly stated. Any person handling the monies or investments of the church needs an audit to protect the church assets and him/her against suspicion of mishandling those assets. Similarly, rectors, vestries, vicars, bishop's committees, treasurers and other persons in positions of responsibility may be liable for any losses which would have been discovered by an ordinary audit but were not discovered because they failed to have an audit conducted. Although most church officers recognize the benefits of having an audit conducted, many still are reluctant to engage professional auditors because of the expense involved. However, given the present volume and complexity of the laws and accounting standards, it should be noted that a professional would most likely save the Church money in the long run. In addition, according to the *Manual of Business Methods in Church Affairs*, published by the Episcopal Church, "an announcement to the congregation that an audit has been completed and that all monies and investments are properly accounted for will have a positive impact on stewardship" (p. 8).

Accordingly, an external audit consists of a series of procedures done to independently verify the financial statements of the Church. It includes examining, on a test basis, specific information, which supports the amounts and disclosures in the treasurer's financial statements. An audit also includes assessing the accounting principles used by the management of the Church. The purpose of an audit is generally to express an opinion about the treasurer's financial reports.

An external audit includes examination of all of the funds of the Church, not only the operating accounts. Thus, all operating accounts, capital and other special funds, endowment and trust funds, assets of Church organizations, investment funds, discretionary funds, and any other assets, liabilities, revenues, and expenses of the Church must be audited. No account should be exempted from examination.

An external audit is conducted in three parts –pre-audit planning, tests of internal controls, and substantive tests of transactions and account balances. The culmination of these tests is the formulation of an opinion on the financial statements (which should consist of at least a statement of the assets and liabilities of the church and a statement of the revenues, expenses, and net asset or fund balances of the church). The opinion is expressed in a report, which is issued to the congregation.

Internal Audit System

An internal audit system should assist both clergy and congregation in fulfilling the responsibilities for the financial oversight of our Church and congregation.

Introduction and Internal Controls Necessity

What type of bookkeeping system should we use? How many bank accounts do we need? Who should be able to sign checks? Who should deposit the weekly receipts in the bank, and how? These are just some of the questions to be answered when considering internal controls for a congregation. Of note, such questions should be periodically reviewed.

Many of these decisions require deliberate consideration. Altogether, the decisions that we make are referred to as “internal controls” and become the policies and procedures of the accounting system of All Saints Church. Good internal controls will ease the treasurer’s job by providing greater assurance that transactions are recorded properly and result in more reliable records and protection of church assets, as well as compliance with civil laws, church canons, and organizational policies. A system of internal controls consists of all measures used by an organization to safeguard its resources and ensure accuracy, efficiency and reliability in accounting and operating information. Equally as important, in order to properly plan and perform the external audit, the auditor must first obtain an understanding of the internal control environment and assess its overall effectiveness. The internal control structure consists of the church’s policies, procedures, and commitment to reasonably prevent material errors and irregularities from occurring or going undetected. Internal control can be described as the overall plan of the church and the methods employed by the church to safeguard assets, ensure the reliability of the accounting data, encourage compliance with established procedures, and promote efficient operations. Good internal controls provide greater assurance that transactions are recorded properly. The review of the control system must be done by the auditor in order to assess the risk that the financial statements are materially misstated.

It is essential to emphasize that internal controls are designed to prevent or identify inadvertent errors as much as they are intended to prevent the deliberate theft or misuse of funds. Without an appropriate system it is not possible to assure the reliability and integrity of the records or reports generated by an organization.

An effective control system ensures that procedures are in place that meets the following objectives:

1. Adequately safeguard the cash, property and other assets of the Church.
2. Review cash and material expenditures of vestry, committees and clergy to ensure compliance with purpose and amounts dictated by policies and formal votes.
3. Ensure that all financial transactions are appropriately documented and approved by authorized staff.
4. Funds are expended in accordance with donor requirements and limits.
5. Ensure that financial reporting is accurate, timely and conforms to policies.

The overriding objective of all controls is to cost-effectively reduce the risk of loss or misuse of funds or property to a tolerable level. Obviously, not all of the controls will be applicable to or cost-effective for all types of operations. We encourage the appropriate consultation whenever there is a feeling that certain controls may not be cost-effective for their particular operations.

Please note that internal controls and the internal audit of those internal controls are only as good as those overseeing the controls and internal audit. It is for this reason All Saints Church has established an Audit Committee.

Audit Committee of All Saints Church

A definition has been developed by the government auditors in the INTOSAI's Internal Control Standards for an Audit Committee:

"A committee of the (Vestry and congregation) whose role typically focuses on aspects of financial reporting and on the entity's processes to manage business and financial risk, and for compliance with significant applicable legal, ethical, and regulatory requirements. The Audit Committee typically assists the (Vestry) with the oversight of (a) the integrity of the entity's financial statements, (b) the entity's compliance with legal and regulatory requirements, (c) the independent auditors' qualifications and independence, (d) the performance of the entity's internal audit function and that of the independent auditors and (e) compensation of company executives (in absence of a remuneration committee)." (Standard INTOSAI GOV #9100, "Internal Control Standards for the Public Sector", annex 2)

The Institute of Internal Auditors denotes best practice for an Audit Committee as: *"The audit committee will consist of at least three and no more than six members of the (congregation and Vestry)... Each committee member will be both independent and financially literate. At least one member shall be designated as the "financial expert," as defined by applicable legislation and regulation"*.

To ensure independence of the Audit Committee and mitigate even the appearance of undue influence or favoritism, it is recommended that the Audit Committee be appointed by and report directly to the Vestry (rather than have any reporting obligations to the Rector, any other clergy, any financial or non-financial employee of the Church or to any committee or organization within the Church).

Responsibilities

The Vestry and Rector and their committees rely on clergy and committee chairs, along with Church employees, to run the normal operations of the Church. The Vestry's main role is better described as oversight or monitoring, rather than execution.

Responsibilities of the audit committee typically include:

- Overseeing the financial reporting and disclosure process.
- Monitoring choice of accounting policies and principles.
- Overseeing hiring, performance and independence of the external auditors.
- Oversight of regulatory compliance, ethics, and whistleblower hotlines.
- Monitoring the internal control process.
- Overseeing the performance of the internal audit function.

- Discussing risk management policies and practices with management.
- The duties of an audit committee are typically described in a committee charter.

Role in oversight of financial reporting and accounting

Audit committees typically review financial reports quarterly and annually. In addition, members will often discuss and ask for assistance and clarification from external auditors on complex accounting estimates and judgments made by management and the implementation of new accounting principles or regulations. Audit committees interact regularly with senior financial management such as the CFO and/or Treasurer of the Church and are in a position to comment on the capabilities of these managers as necessary. Should significant problems with accounting practices or personnel be identified or alleged, a special investigation may be directed by the audit committee, using outside consulting resources as deemed necessary.

Role in oversight of the external auditor

External auditors are also required to report to the committee on a variety of matters, such as their views on management's selection of accounting principles, accounting adjustments arising from their audits, any disagreement or difficulties encountered in working with management, and any identified fraud or illegal acts. Audit committees typically approve selection of the external auditor. The external auditor (also called a public accounting firm) reviews the entity's financial statements quarterly and issues an opinion on the accuracy of the entity's annual financial statements. Changing an external auditor typically also requires audit committee approval. Audit committees also help ensure the external auditor is independent, meaning no conflicts of interest exist that might interfere with the auditor's ability to issue its opinion on the financial statements.

Role in oversight of regulatory compliance

Audit committees discuss litigation or regulatory compliance risks with management, generally via briefings or reports from the General Counsel, the top lawyer in the entity. Larger corporations may also have a Chief Compliance Officer or Ethics Officer that report incidents or risks related to the entity's code of conduct.

Role in monitoring the effectiveness of the internal control process and of the internal audit

Internal control includes the policies and practices used to control the operations, accounting, and regulatory compliance of the entity. Management and both the internal auditing function and external auditors provide reporting to the audit committee regarding the effectiveness and efficiency of internal control.

Role in oversight of risk management

Organizations have a variety of functions that perform activities to understand and address risks that threaten the achievement of the organization's objectives. The policies and practices used by the entity to identify, prioritize, and respond to the risks (or opportunities) are typically discussed with the audit committee.

Particular Note

Please note that a detailed informational guideline for Episcopal Church internal and external audit is provided and (generally) updated monthly by *"The Manual of Business Methods in Church Affairs"*, which is published by the Episcopal Church (In accordance with Title I, Canon 7, "Of Business Methods in Church Affairs", and Resolution D-147 (1979 GC): "Accounting Principles and Practices for Dioceses, Parishes, and Other Congregations": COPYRIGHT 2007, 2009, 2012 The Domestic and Foreign Missionary Society of the Protestant Episcopal Church in the USA. Reference to this manual and its updates can be accessed at:

http://www.episcopalchurch.org/sites/default/files/downloads/full_manual_spring_2012.pdf

It is suggested that the Audit Committee of All Saints Episcopal Church, the Vestry, and all finance employees of All Saints Church refer to this manual frequently – and especially when amending the accounting system and when preparing for the annual external audit.

The Audit Committee should produce an "Audit Committee Certificate." The Audit Committee Certificate states that steps have been taken to ensure that the financial statements are presented fairly in all material respects. The Audit Committee Certificate should identify exceptions when the audit committee questions any aspect of the financial statement. When this occurs, the audit committee should carefully describe the condition raising the question. Such a statement does not nullify the accuracy or the importance of the audit, but it does alert the reader that the financial statements may be affected in some way because of the noted variance. (A suggested sample copy of the Audit Committee Certificate is included in the Appendices of this manual.)

The Audit Committee should comment in a separate letter to the Vestry regarding the internal control procedures in effect at the congregation. This letter should be made a part of the minutes and be titled, "Audit Committee Findings on Policies and Procedures." (A suggested copy of the Audit Committee letter of Findings and Procedures is included in the Appendices of this manual.)

Suggested worksheets and forms for the All Saints Church Audit Committee (primary credit to the Episcopal Church, *The Manual of Business Methods in Church Affairs*):

Internal Control Questionnaire

The following Internal Control Questionnaire is intended to provide guidance for setting up an accounting system and a checklist for periodic review and evaluation of an existing system. The questionnaire is designed also to assist a congregation's internal audit committee. The format is a series of questions, most of which refer to some recommended internal control. The normative answer to a question will be positive. A negative response suggests an area of the system that could be strengthened.

Developing a narrative description is suggested, to provide documentation of the current review. This narrative should be retained for reference in future evaluations.

General: The following items are intended to provide general information to aid understanding of the overall accounting and internal control system.

1. Are prior internal control questionnaires and auditors' recommendations available?

Yes No

2. Have recommendations of prior reports on internal controls been implemented?

Yes No

3. Is a complete and current chart of accounts, listing all accounts and their respective account numbers, available?

Yes No

4. Is there an accounting policy and procedure manual? Is it up to date?

Yes No

5. Is a current edition of this manual available?

Yes No

6. Is the accounting system using a double-entry bookkeeping method?

Yes No

7. Have the findings of external auditors been reported to the Vestry?

Yes No

Budget: The development and use of a budget is a critical management tool that will aid in the stewardship and administration of church resources and program.

1. Is the budget approved by the Vestry?

Yes No

2. Are all changes to the budget authorized by the Vestry and recorded in the minutes of the meetings?

Yes No

3. Is there a periodic review of the budget by the Vestry?

Yes No

Reporting: The best accounting system is of little value, unless it communicates the information it contains to those responsible. Although there may be variations, certain minimum standards exist to assure adequate communication of the financial information.

1. Is a Treasurer's report submitted to the Vestry or accounting committee each month?

Yes No

2. Is the Treasurer's report presented in sufficient detail to inform the reader about the nature of the various income and disbursement items?

Yes No

3. Does the report present the current actual financial data compared with the approved budget?

Yes No

4. Is there periodic reporting, at least quarterly, of all other funds and activities, including designated or restricted funds?

Yes No

Cash Receipts: Clearly stated policies and procedures regarding the handling of cash and other receipts help not only to protect from loss, but assure that all receipts are properly recorded in the records.

1. Are there safeguards to protect the collections from theft or misplacement from the time of receipt until the time the funds are counted and deposited?

Yes No

2. Are the collection receipts counted and deposited so that the deposit equals the entire amount of receipts on a timely basis (e.g., at least weekly)?

Yes No

3. Are there at least two unrelated persons responsible for counting and depositing the collections?

Yes No

4. Are the persons responsible for counting receipts rotated on a periodic basis?

Yes No

5. Do the counters have a standardized form for recording the deposit information?

Yes No

6. Are the counters' sheets retained and reconciled with actual deposits, and are all discrepancies investigated?

Yes No

7. Is there a control prohibiting the cashing of checks from the currency received?

Yes No

8. Are all of the pledge envelopes or other memoranda retained and reconciled to the recorded amounts?

Yes No

9. Are all other cash receipts recorded and deposited on a timely basis?

Yes No

10. Are all checks received restrictively endorsed—for deposit only “immediately upon receipt?”

Yes No

11. Are all cash receipts deposited into the general operating checking account?

Yes No

12. Are there procedures that will highlight, or bring to someone's attention, the fact that all receipts or income have not been received or recorded?

Yes No

13. Are periodic statements provided to donors of record (i.e. at least quarterly)?

Yes No

14. Do acknowledgments of contributions in excess of \$250 include a receipt from the recipient organization which states that it is “the contemporaneous acknowledgment required by the Internal Revenue Code, and states that, in accordance with Section 170(F)(8)(B), any goods or services provided consist solely of intangible religious benefits”?

Yes No

15. Are all discrepancies investigated?

Yes No

Cash Disbursements: The following procedures will assist in assuring that all payments are properly approved, recorded, and supported by appropriate documentation.

1. Are all disbursements made by check, except for small expenditures made from petty cash?

Yes No

2. Are all checks pre-numbered and used in sequence?

Yes No

3. Is there a clearly defined approval process for all disbursements?

Yes No

4. Are all voided checks properly cancelled and retained?

Yes No

5. Are all checks made payable to specified payees and not to cash or to bearer?

Yes No

6. Are all disbursements supported by original documentation?

Yes No

7. Is the original vendor's invoice or other documentation cancelled at the time of signature to prevent duplicate payment?

Yes No

8. Check signing:

a. Is signing blank checks prohibited?

Yes No

b. Is using a signature stamp or pre-printed signatures prohibited?

Yes No

c. Does all supporting documentation accompany checks presented for signature?

Yes No

d. Are all account signers authorized by the Vestry?

Yes No

e. Is more than one signature required for any check?

Yes No

f. If not, do checks for more than \$500 require more than one signature?

Yes No

g. If signature imprint machines are used, are the keys kept under lock and key except when in use?

Yes No

9. Are all disbursements requiring special approval of funding sources or the Vestry properly documented in the Vestry or Finance Committee minutes?

Yes No

10. Are there adequate controls and segregation of duties regarding electronic funds transfers?

Yes No

Journal Entries: Journal entries offer a special opportunity to make adjustments to accounting records. The general journal is an equally important book of original entry as the cash receipts and cash disbursements journals.

1. Is there an appropriate explanation accompanying each journal entry?

Yes No

2. Are all journal entries approved by a knowledgeable authority other than the person initiating the entry?

Yes No

3. Is adequate documentation maintained to support each journal entry?

Yes No

Bank Account Reconciliation: The monthly reconciliation of all bank accounts is a primary tool for assuring the proper recording and accounting for all cash account activity.

1. Are all bank accounts reconciled within 10 days of receipt of bank statement?

Yes No

2. Do two different people perform the tasks of opening and reconciling the bank statement?

Yes No

3. Does someone complete the bank account reconciliations other than the person who participates in the receipt or disbursement of cash?

Yes No

4. Do the reconciliation procedures provide for:

a. Comparison between the bank statement and the cash receipts journal of dates and amounts of deposits?

Yes No

b. Investigation of bank transfers to determine that both sides of the transactions have been recorded?

Yes No

c. Investigation of all bank debit and credit memos?

Yes No

d. Review of all checks outstanding more than 90 days?

Yes No

e. Are checks more than 180 days outstanding voided during the year-end reconciliation?

Yes No

f. Is the bank immediately notified of all changes of authorized check-signers?

Yes No

5. Are all journal entries for bank charges and bank account interest recorded routinely?

Yes No

6. Are all bank accounts included on financial reports to the Vestry?

Yes No

Petty Cash: The following controls are intended to provide a timely recording of cash expenditures in the accounting system.

1. Is the responsibility for the petty cash fund assigned to one person?

Yes No

2. Are all petty cash funds maintained on an imprest basis, i.e., the total amount of vouchers paid or disbursed, plus cash, always equal the amount of the fund?

Yes No

3. Is adequate review made of documentation before the fund is reimbursed?

Yes No

4. Is the petty cash fund reimbursed at least monthly?

Yes No

5. Are check cashing and making loans to employees prohibited?

Yes No

6. Is the actual petty cash protected from theft or misplacement?

Yes No

Investments: Procedures for proper recording and control of all investment instruments will help to assure that all assets and related income are accounted for and properly reported.

1. Are all investment instruments held in the name of the church only?

Yes No

2. Is authorization for the sale and/or purchase of investments provided for by the Vestry or authorized investment committee?

Yes No

3. Are all investment instruments adequately protected from fire, theft, or misplacement?

Yes No

4. Is the income/dividends/interest recorded?

Yes No

5. Are all investment accounts included in financial reports to the Vestry?

Yes No

Property and Equipment: Certain procedures involving the physical assets of the church will aid in detecting, Identifying, and preventing losses.

1. Is formal approval of the Vestry required for all property and equipment additions and dispositions?

Yes No

2. Is a detailed inventory of all property, furniture, fixtures, and equipment maintained showing:

a. Date acquired?

Yes No

b. Detailed description?

Yes No

c. Cost or fair market value at time of donation?

Yes No

d. Any funding source restrictions? Yes No

3. Is a periodic review conducted to compare the actual property, furniture and fixtures, and equipment with the recorded inventory listing?

Yes No

3. Is there a safe deposit box?

Yes No

a. Who is authorized to enter it?

b. Is there an inventory of its contents?

Yes No

4. Are permanent records such as articles of incorporation, if applicable, bylaws and real estate deeds kept in a safe place?

Yes No

5. Are they up to date?

Yes No

Insurance: Insurance should be maintained that is adequate to protect against all reasonable risks of loss.

1. Is a periodic review conducted to ensure the adequacy of the insurance coverage for:

a. Property?

Yes No

b. Liability?

Yes No

c. Fidelity bond?

Yes No

d. Sexual misconduct?

Yes No

e. Directors and officers liability?

Yes No

f. Workers' compensation?

Yes No

2. Is there a policy related to sexual misconduct?

Yes No

3. Is a periodic review conducted to ensure that adequate controls are in place to prevent loss?

Yes No

Liabilities and Other Debt: All liabilities and other debt must be clearly reported, and all provisions or restrictions complied with.

1. Is all borrowing or indebtedness authorized by the Vestry and the appropriate diocesan board or committee?

Yes No

2. Are all loan agreements and/or lease agreements in writing and properly safeguarded?

Yes No

3. Are there periodic reviews conducted to determine compliance with any debt/lease provisions?

Yes No

4. Are all liabilities noted on Financial Reports to Vestry?

Yes No

Restricted Gifts and Income: Gifts restricted by donors are not handled in the same manner as other contributions. Procedures are necessary to assure that these gifts are recorded properly and all restrictions are observed.

1. Are records maintained of all bequests, memorials, endowments, or any other restricted gifts to include:

a. Date, amount and donor of gift?

Yes No

b. Any restrictions or limitations?

Yes No

2. Does the Vestry or other authoritative body approve all restricted gifts and grants?

Yes No

3. Are the income and other transactions periodically reported to the Vestry?

Yes No

4. Are written acknowledgments issued for whom they are required?

Yes No

Payroll: The application of policies and procedures involving the employment of individuals assures compliance with payroll tax reporting to the various governmental entities.

1. Are personnel files maintained to include:

a. Employment application and/or letter of employment

Yes No

b. Authorizations of pay rates and effective dates?

Yes No

c. Internal Revenue Service Form W-4?

Yes No

d. Department of Justice Form I-9?

Yes No

e. State Withholding Forms?

Yes No

f. New hire reporting?

Yes No

2. Is there a written record of hours worked, approved by a supervisor when applicable?

Yes No

3. Are there adequate records to:

a. Show computation of gross pay?

Yes No

b. Account for all deductions from gross pay?

Yes No

c. Support payroll tax returns and Forms W-2?

Yes No

4. Are payroll tax returns filed on a timely basis?

Yes No

5. Are payroll tax deposits made on a timely basis?

Yes No

6. Are all employees, clergy and lay, receiving a Form W-2?

Yes No

7. Are Forms 1099 being provided for all individuals who are not employees, and for all unincorporated entities paid \$600 or more annually?

Yes No

8. Are Form W-2 wages reconciled to the general ledger accounts, and all four quarterly payroll tax returns?

Yes No

9. Are clergy housing allowances recorded in the minutes of the Vestry no later than the first meeting of the year?

Yes No

Computer Systems: The use of computers creates the need for additional procedures to safeguard the system and data.

1. Are current or duplicate copies of the operating system and programs maintained off premises?

Yes No

2. Are the files backed up daily and the backups maintained off premises?

Yes No

3. Is access to the computer and computer programs limited to authorized persons?

Yes No

4. Is there adequate documentation, including user manuals, available on-site for all computer programs?

Yes No

5. Is a printed copy retained of all journals, general ledger, financial statements and any other computerized records?

Yes No

6. Is there a plan for recovery of data and continuation of operations in the event of a disaster

Yes No

Audit Committee Certificate

The Audit Committee Certificate states that steps have been taken to ensure that the financial statements are presented fairly in all material respects. The Audit Committee Certificate should identify exceptions when the audit committee questions any aspect of the financial statement. When this occurs, the audit committee should carefully describe the condition raising the question. Such a statement does not nullify the accuracy or the importance of the audit, but it does alert the reader that the financial statements may be affected in some way because of the noted variance.

Sample Audit Committee Certificate

Date _____

To the Rector, Wardens and Vestry of All Saints Church, 3 Chevy Chase Circle, Chevy Chase, MD 20815

Subject: (Audit Year) Audit of All Saints Church

We have inspected the statement of financial position of All Saints Church as of December 31, (Audit Year), and the related statement of activities and cash flows for the year then ended.

Our inspection was made in general accordance with the audit guidelines of the Manual of Business Methods in Church Affairs, and the financial statements are prepared on a (cash, modified accrual, or accrual – accrual being the preferred method) basis in accordance with principles adopted by the Episcopal Church and approved by its General Convention except as noted. (Note exceptions here, if any: Was depreciation recognized? Were donated services recorded?)

We have taken steps to see that the accompanying financial statements present fairly, in all material respects, except as noted above, the financial position of the Congregation at December 31, (Audit Year); and that the changes in its net assets and its cash flows for the year then ended are in accordance with the principles authorized by General Convention of the Episcopal Church on a basis consistent with that of the preceding year.

Our inspection and certificate are not meant to be construed as an audit and opinion rendered by a Certified Public Accountant.

Sincerely, Members of the Audit Committee (List names and phone numbers of Audit

Committee Members and have each member sign the Audit Committee Certificate)

Audit Committee Findings on Policies and Procedures

The Audit Committee should comment in a separate letter to the Vestry regarding the internal control procedures in effect at the congregation. This letter should be made a part of the minutes.

Exceptions to adequate procedures should also be noted in these comments. Repeat items from previous years should be noted. Good business practices and policies, as well as safeguards, should be recommended. A copy of this letter should accompany the audit report. The Audit Committee should look for opportunities to educate the Treasurer, Vestry and bookkeeper by teaching the accrual method of accounting.

Sample: Audit Committee Findings on Policies and Procedures

Date _____

To the Rector, Wardens and Vestry of (Church Name)

Subject: (Audit Year) Audit of (Church Name)

During the course of the above inspection, the following items pertaining to internal control and other operation matters were noted. The first group includes areas of management control where prior year auditor recommendations have been implemented; the second group includes comments and recommendations of current year auditors.

Areas where prior year auditors' recommendations have been implemented:

Comments and recommendations of current year auditors:

Sincerely, Members of the Audit Committee (List names and phone numbers of Audit Committee Members and have each member sign the Audit Committee Findings on Policies and Procedures Letter.)

Instructions for the Audit Program

The following suggested procedures are merely acts that can be used to determine the appropriateness of the financial statements presented. An audit is a series of procedures to test, on a predetermined selective basis, the various transactions occurring in the year under examination. It is unrealistic to examine every transaction for the year. Therefore, certain tests are necessary to verify the reasonableness of all transactions.

Guide to Pre-Audit Procedures and Necessary Items

- a. Obtain a preliminary understanding of the accounting systems (both manual and computer) that generate significant financial statement items and of related principal internal accounting controls.
- b. Obtain copies of the minutes of the Vestry meetings for the period under examination. This should include the minutes of any committee authorized to receive and disburse monies. Read the minutes regarding the election of officers, compensation of personnel, bonding of the treasurer, budget approvals, contracts entered into, and items purchased, monies borrowed, purchase and sale of securities, resolution confirming clergy housing allowance for tax purposes, etc. This should be done before the actual examination of any accounting records. You may need to see the minutes of the previous year if they contain authorizations for expenditures in the year being audited.
- c. Obtain a copy of the previous audit complete with the Committee Audit Findings on Policies and Procedures. This provides a firm set of starting balances which may differ from the Treasurer's reports. It will also offer the chance to check on the progress of corrections of management control deficiencies, an important part of the teaching process.
- d. Obtain a copy of the annual financial statements as prepared and presented by the treasurer.
- e. Review the procedures being used to account for church monies. Identify by name and

position the individuals with responsibility for financial operations and decisions and verify with them that all the funds of the congregation are included in the statements.

f. Identify all bank accounts and authorized check and withdrawal signers, including those under separate treasurers.

g. Request that all accounting records of all funds be presented together including:

- 1) Chart of Accounts and Organization Chart
- 2) General Ledger
- 3) Cash Receipts Journals
- 4) Cash Disbursements Journals
- 5) Bank Statements including canceled checks
- 6) Paid Invoices
- 7) Individual payroll records including Forms W-4 and I-9
- 8) Passbooks and evidence of other investments
- 9) Pledge Records by individual and total

h. Meet with members of the Finance Committee to discuss the annual financial statements.

Inquire about the occurrence during the year of any significant matters of which the auditor should be informed. Also, inquire into significant variances noted on the financial statements.

i. Request a location in which to perform the audit. The audit can be more thoroughly and efficiently performed if it is conducted where the records are located.

3. Receipts:

a. Plate offerings: Cash receipts journal entries should be traced to weekly cash receipts records on a test basis.

b. Pledge receipts:

Pledge receipts should be verified by tracing cash receipt entries to individual pledge records on a test basis. A minimum of 10% of postings should be traced. Results will indicate if a broader sampling is necessary.

Adding machine tapes should be made of the individual pledge records with the total agreeing with the total pledge payments reported.

Random selection of individual pledge records should be tested for accurate total and balance. A minimum of ten percent should include the same individuals as above.

If the auditor is engaged before year end and if the church sends statements to the pledgors, the auditor can save time and effort by supervising the mailing of the year end statements. The auditor can then use this mailing to obtain direct confirmation.

The auditors should always review the pledge receipts of the congregation personnel involved in money transactions.

The decision regarding the size of the representative sample of postings and pledge records for examination depends on the dollars involved and the sophistication of the parish records.

c. Contributions from congregation organizations: Receipts must be listed separately for each organization and amounts entered in the cash receipts journal, traced to the weekly cash receipts records. These listed amounts shall be confirmed with their sources.

d. Contributions from the Diocese: Receipts must be listed and amounts entered in the cash receipts journal, traced to weekly cash receipts records.

e. Investment and endowment income: Income from securities should be verified by an examination of the brokerage house statement. Income from investment accounts should be verified by an examination of the statements provided or confirmed by the trustee or agency. Income from savings bank deposits should be confirmed by the bank.

f. Restricted income: Income received for special purposes should be noted by the auditor who should trace the cash receipts journal entries to the weekly cash receipts records. The auditor should also be satisfied that the income was used for the purpose for which the gift was made.

g. Non-income receipts: Verify all cash receipts journal entries by tracing them and ascertaining that the proper authorization has been given for any transfer or inter-fund

borrowing, or for the sale or redemption of any investments or property.

h. All cash receipts records should be traced to duplicate deposit slips or bank statements to ascertain that these receipts are deposited intact.

i. Petty cash: The auditor should be satisfied that a proper imprest system is being maintained. Petty cash is not to be used to cash personal checks. Cash flow and size of fund over audit period should be checked for possible misuse.

j. All receipts should be compared to budgeted amounts and material variances should be explained.

k. Contributions of tangible assets or services. Refer to Chapter III (Bookkeeping) for discussion and proper treatment of these contributions.

l. Verify the totals in the cash receipts records for two to three months. Check postings of monthly totals to the general ledger or to the monthly financial statements.

4. Disbursements:

a. Tests are to be made to satisfy that disbursements have been accurately classified, and that invoices supporting the disbursements have been properly approved and canceled or marked "PAID".

b. The committee must be familiar with the financial statement expenditure categories listed on the congregation's chart of accounts.

c. All disbursements should be compared to budgeted amounts and material variances should be explained.

d. Testing of Disbursements: Select a sample of disbursements. A minimum of 10 percent of postings should be traced. Results will indicate if a broader sampling is necessary. Test the disbursements to invoices as follows:

1) Compare invoices with the recordings in the cash disbursements journal for a sufficient number of items to assure the committee that they are fairly recorded and classified. Comparison should include vendor's name, date and amount billed.

2) Examine invoices for verification signature that the items were received or services

performed for a sufficient number of items so the committee may be satisfied that goods and services were acknowledged by a person authorized to do so.

3) Check the arithmetic on invoices and vendors' monthly statements for a sufficient number of items to assure the committee that invoiced amounts were properly recorded on the statements.

4) Travel and business expense reimbursements should be checked to see that they are in accordance with the qualified reimbursement policy of the congregation. Reference Chapter IV (Taxes) for discussion of a qualified reimbursement policy.

e. Verify the totals of the cash disbursements records for two to three months. Check postings of monthly totals to the general ledger or to the monthly financial statements.

5. Bank Accounts:

a. The committee should ascertain the number of bank accounts maintained and the purpose for which each is maintained.

b. The committee should examine the canceled checks for:

1) Authorized signature(s)

2) Proper endorsement

3) Comparison with the cash disbursements journal for proper recording of payee and amount. If fewer than ten checks are written each month then all items should be examined. If more than ten per month, a random sampling of two to three months would suffice if a good system of accounting were evident.

c. The auditor should account for all voided checks.

d. Outstanding checks from the previous period should be examined to determine proper bank clearing and amount. Any check outstanding for a period longer than three months from the balance sheet date should be questioned for satisfactory explanation.

e. The auditor should verify bank balances at the end of the period being audited and should check that the closing cash amount is correctly stated.

Examine the January bank statement following the close of the audit year for items

impacting the audit year.

f. Determine whether transfer of funds occurred between bank accounts near the date of the Statement of Financial Position. Determine that the transfers were recorded in the books in the same accounting period and that any transfers not recorded by the bank in the same accounting period appear in the appropriate bank reconciliation.

6. Investments:

a. Obtain or prepare a list of securities owned showing:

1) The description of each security

2) The serial number of bonds or securities

3) The denomination of each security or its par value

4) The interest rate of each bond

5) The cost of each security and the amount recorded on the books

6) The interest and dividends received during the year

7) The market value of each bond or security as of December 31 of the year being audited

b. Review the investment summary for reasonableness, consistency of amounts between years and obvious omissions.

c. Compare the securities listed with ledger accounts and/or with the statement. Whenever practicable, serial numbers should be compared with records of security purchases or gifts in order to obtain positive identification and to avoid the possibility of substitution.

d. Examine securities listed or obtain confirmation from the holders if any are held by depositories. It is preferable for this examination to occur as close to the examination date as possible. Insure that the securities are registered in the name of the congregation or are endorsed appropriately to be transferable to the congregation. Examine the coupons on bonds to ascertain that unmatured coupons are intact.

e. Examine all transactions for verification of acquisitions and disposition.

f. Trace acquisitions to disbursement records and sales (dispositions) to receipts records.

- g. Examine broker statements and compare with investment ledger where applicable.
- h. The auditor should be satisfied that the securities are being adequately safeguarded.
- i. Examine securities for ownership, certificate number, dates, endorsements, assignments, etc.
- j. Verify any income that has not yet been distributed.
- k. Determine, by reference to dates of purchase and disposal of investment, interest rates and published dividend records, whether income earned and accrued income receivable have been appropriately recorded.

7. Restricted Funds:

- a. Obtain or prepare a list of restricted funds showing:
 - 1) The source and date;
 - 2) Terms governing the use of principal and income;
 - 3) To whom and how often reports of condition are to be made, and
 - 4) How the funds are to be invested.
- b. Examine the donor letter, or trust or agency agreement, for each new gift and contribution received during the fiscal year.

8. Loans:

- a. Obtain or prepare a schedule of all loans to include:
 - 1) The name of the lending institution
 - 2) The date or origin
 - 3) The original amount of loan
 - 4) The interest rate and payment schedule
 - 5) The monthly payment
 - 6) The unpaid balance
 - 7) The purpose of loan
 - 8) The authorizing body
 - 9) The collateral for the loan

10) The restrictions placed by the lender

- b. Review balances for reasonableness, consistency of amounts between years and obvious omissions.
- c. Determine that any loans from the year being examined had the proper authorization and were recorded in the minutes of the Vestry or mission committee.
- d. Verify, by direct communication with any lender, the outstanding indebtedness at the year-end as well as the terms of the indebtedness.
- e. Reconcile the unpaid balance of all loans as reported by the congregation records to the figure reported by the lending institutions.

9. Property and Equipment:

- a. Obtain a list of fixed assets of significant amounts showing the cost and date of purchase, if known.
- b. Review balances for reasonableness, consistency of amounts between years, and obvious omissions.
- c. Examine all the deeds and titles of ownership related to the properties owned by the congregation. Review them for the proper recording of the name of the owner and to determine if any encumbrances or liens exist.
- d. Determine if any inventory identification procedure is in effect.
- e. The congregation must have a physical inventory of capital assets. A sampling test of this inventory is to be made by the committee.
- f. Ensure that all property and equipment is adequately insured.
- g. If depreciation of property is recognized, review entries for accuracy.

10. Payroll Records:

- a. Examine the individual earnings records for name, address, social security number, number of exemptions, rate of pay, and effective date.
- b. Ensure that the salary paid is authorized and proper by comparing with the amount budgeted.

- c. Trace the individual earnings record postings to the check register.
- d. Reconcile total wages paid and total withholding taxes with the quarterly Form 941 and end-of-year Form W-3, checking that they were remitted on time.
- e. Determine if a current signed Federal Form W-4 and a Form I-9 (Immigration and Naturalization Service) is on file for each employee hired after November 6, 1986.
- f. Determine if a Form W-2 has been given to each employee (including the clergy) and that the Forms W-2 are correct and properly filed.
- g. Determine if Forms 1099 are being provided for all individuals who are not employees and unincorporated entities paid \$600 or more annually and all recipients of educational scholarship funds of \$600 or annually.

1998 Instructions for Forms 1099, 1098, 5498, and W-2G, Department of the Treasury, Internal Revenue Service, (p. 23, Scholarships) reads,

“Do not use Form 1099-MISC to report scholarship or fellowship grants. Scholarship or fellowship grants that are taxable to the recipient because they are paid for teaching, research, or other services as a condition for receiving the grant are considered wages and must be reported on Form W-2. Other taxable scholarship or fellowship payments (to a degree or non-degree candidate) are not required to be reported by you to the IRS on any form.”

- h. Test the payroll to be sure that a real employee exists for every payroll check written.

11. Receivables and Payables:

- a. Prepare a schedule of accounts receivable as of the date of the Statement of Financial Position. These may include pledge payments which were made after the end of the year in which the money was pledged or authenticate obligations owed to the congregation at year end.
- b. Prepare a schedule of accounts payable as of the date of the Statement of Financial Position. These may include monies owed by the congregation to vendors at year-end for

goods and services received during the year being audited. Discuss with the treasurer any old or disputed payables

12. Insurance: A schedule should be prepared listing the name of carrier, description of coverage, period of insurance, premium amount and date of premium payment for the following policies which the committee is to review:

- a. Fire insurance on buildings and equipment
- b. General Liability (Public Liability and Property Damage)
- c. Burglary
- d. Fine Arts
- e. Malpractice
- f. Worker's Compensation
- g. Fidelity Bond
- h. Automobile coverage on cars owned by the congregation
- i. Non-ownership liability insurance for cars owned by others when used for congregation business
- j. Directors' and Officers' Liability
- k. Umbrella Liability
- l. Other special policies held by the church

13. Discretionary Fund: Check that the discretionary fund is in the congregation's name, that the congregation's Federal Employer's Identification Number is the number used to identify the account at the bank, and that the fund has not been used for operating fund expenses or for the personal expenses of the clergy. If a separate checking account has been authorized, all monies for the discretionary fund must pass through the congregation's general bank account and subsequently a check should be written to transfer the monies to the separate discretionary fund checking account. Reference Chapter V (Clergy Discretionary Funds) before proceeding.

14. Work Papers: The committee should retain a file of the work papers that were prepared

during the audit. When the next year's audit is performed, these papers could be an invaluable guide. The next auditor should be provided with a copy of the work papers. These work papers should include such things as: the complete audit and internal control check lists; lists of bank accounts, restricted funds, investments, insurance accounts and loans; the schedules prepared; the procedures followed in performing the audit and memoranda describing significant issues raised during the audit.

15. Audit Committee Certificate: The Audit Committee Certificate states that steps have been taken to ensure that the financial statements are presented fairly in all material respects. The Audit Committee Certificate should identify exceptions when the audit committee questions any aspect of the financial statement. When this occurs, the audit committee should carefully describe the condition raising the question. Such a statement does not nullify the accuracy or the importance of the audit, but it does alert the reader that the financial statements may be affected in some way because of the noted variance.

16. Audit Committee Findings on Policies and Procedures: The Audit Committee should comment in a separate letter to the Vestry regarding the internal control procedures in effect at the congregation. This letter should be made a part of the minutes.

Exceptions to adequate procedures should also be noted in these comments. Repeat items from previous years should be noted. Good business practices and policies, as well as safeguards, should be recommended. A copy of this letter should accompany the audit report. The Audit Committee should look for opportunities to educate the Treasurer, Vestry and bookkeeper by teaching the accrual method of accounting.