



Financial Internal Controls

PREVENTING FRAUD AND EMBEZZLEMENT

Internal controls are the processes an organization has in place to detect and prevent fraud. An act of fraud happens when there are weaknesses in an organization's internal controls. According to the Association of Certified Fraud Examiners, three elements must exist for fraud to take place—**pressure or motivation, rationalization,** and **opportunity.** These three elements make up the **Fraud Triangle.**

A church organization's best chance at lowering its risk of fraud is to remove opportunities for fraud to transpire. A potential perpetrator may discover an opportunity when an innocent mistake slips through internal controls. Later, this discovery is acted on when financial pressure is felt, and rationalization found. Good financial risk management identifies exposures to loss and finds ways to prevent these losses from occurring. Good controls also protect the treasurer's reputation. Here are 8 internal controls to implement at your church.

Establish Controls

- 1. Careful Selection**—Properly screen all individuals for positions of financial responsibility. Individuals should have an attitude of transparency, willingness to train others, and readiness to allow other trained individuals to take over responsibilities in their absence.
- 2. Verify Cash Received**—Whenever possible, have two or more people present to count any collected money. This should be counted on site as soon as possible. Keep a written record of the count with the funds until the deposit is made into the organization's bank account. The group or individual who delivers the counted money to the treasurer should maintain a copy of the record for future verification.
- 3. Bank Statement Review**—Send monthly bank statements to an individual other than the treasurer, such as a pastor, principal, trusted board member, etc. This individual should verify if transactions seem reasonable before passing the statement on to the treasurer for reconciliation. Immediately verify inconsistencies, missing checks, or questions with accounting records.
- 4. Safeguard Checks**—Establish signature limits on the amount that a single individual can issue through a check. Once that limit is reached, require a second signature on the check. This prevents dishonest individuals from writing unauthorized checks for high



dollar amounts. It is also good to review a list of checks written at the board or finance committee.

- 5. **Timely Financial Reports**—Require financial statements be generated and rendered to the controlling committee or board on a timely basis. The treasurer or designated representative should be able to present the financial statement and answer questions concerning transactions that took place during the fiscal period.
- 6. **New Bank Accounts**—All bank and investment accounts should be authorized and approved by action of the controlling committee or board. Separate accounts in the name of the church established without proper authorization provides the opportunity for dishonest individuals to commit fraud or theft from the church.
- 7. **Investigating Questionable Transactions**—The controlling committee or board should note any questions that arise. Require a complete report at the next meeting or time specified. Until satisfactory answers are received, carefully investigate any failure to obtain answers to financial questions from the treasurer.
- 8. **Financial Audits**—It is the responsibility of the local conference to conduct the audit of the local church and school financial records. Audits should be conducted at a minimum of every two years. A written report should be presented to the controlling committee or board. If local audits are not being conducted on a regular basis, ask for the assistance of the conference treasurer to schedule an audit for your organization.

if mismanagement is happening or additional controls are needed.

- ▶ **Behavior Changes**
- ▶ **Personality changes due to pressure (moodiness)**
- ▶ **Lifestyle changes (lavish luxurious living)**
- ▶ **Never takes a vacation**
- ▶ **Likeable and generous**
- ▶ **Trusted employee**
- ▶ **Deceptive/good liars**

In Case of a Suspected Loss

Mishandling God’s funds is morally wrong and may include criminal actions. In the event of a possible loss, it is important to respond quickly and properly. If a church or school board has reason to suspect funds are being taken or misused by an individual, they should take the following action:

- 1. **Maintain Confidentiality**—Every effort must be made to keep fidelity situations from becoming common knowledge or gossip. Idle talk may give rise to potential defamation charges. The problem may only be poor recordkeeping or could stem from other causes.
- 2. **Remove the Individual(s)**—Once fraud is confirmed, the person(s) identified as responsible should be immediately removed from his or her position of trust. The insurance company will not cover any further loss due to an organization’s failure to remove an untrustworthy employee.
- 3. **Report Promptly**—Immediately report incidents to both the conference treasurer and the police department according to **NAD Working Policy S 04 48**.

Strict reporting requirements also exist with the insurance company (usually within four months from the date of discovery). Reporting beyond that time frame may result in not receiving any insurance settlement. Immediately report all potential claim situations to Adventist Risk Management,® Inc.

Red Flags That Could Indicate Fraud

One or more red flags do not mean fraud is taking place, but should alert leadership to take a closer look to see

REPORT YOUR CLAIM RIGHT AWAY
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