

# **PASSING THE PLATE: A SURVEY OF INTERNAL CONTROLS IN LOCAL CHURCHES**

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*Anita Collins worked for the NY Archdiocese for eight years, but a saint she was not. Collins has been charged with stealing \$1 million from the NY Archdiocese through what authorities and church reps have called a “sophisticated fraud”.*

**J. Scott (2012), Forbes**

## **ABSTRACT**

An increasing number of cases of fraud and embezzlement at churches have been reported by the popular press and there is good evidence to suggest that a primary reason for these defalcations may lie in a lack of internal control or lapses in enforcement of existing controls. Churches appear to be particularly vulnerable to fiscal abuse, given the large amounts of donations and collections that are received in cash. A survey is conducted to evaluate procedures that exist in sixteen local churches located in New York, Indiana and Michigan. Results of the survey identify specific weaknesses that exist within the local church’s internal control structure. Based on the findings, suggestions are offered as to the steps that churches may take in order to improve their internal control systems and thereby improve the organization’s financial reporting, strengthen the safeguarding of assets and minimize the misappropriation of church assets.

## **INTRODUCTION**

Misappropriation of assets and accounting fraud have occurred since time immemorial, but it wasn’t until the failures of major public companies like Enron, Adelphia Communications, Tyco, and WorldCom that the public became painfully aware of its devastating effects. While fraud in publically traded companies has been widely publicized, less publicized are reports of fraud occurring in churches and church-related organizations.

Anita Collins embezzled over \$1 million from the NY Archdiocese. Quiet and unassuming, the “church lady” knew that checks under \$2,500 did not require supervisor approval. So Collins issued herself over 450 checks for amounts under the threshold and billed the Archdiocese for

nonexistent services. The embezzlement was eventually detected by the independent auditors. (Scott, 2012).

Religious organizations and churches are vulnerable to misappropriation and fraud since monitoring by church members or by the government rarely occurs (Taylor, 1982). There is a degree of trust in religious organizations and churches due to the expectation of employees' commitment to the mission of the church. Additionally, these entities may not have outside, independent audits.

Unethical acts that violate fiduciary responsibility or public trust for personal or organizational gain are unsettling, particularly when they occur in a church setting. "Often, it's one of the most trusted people in the church who's pilfering from the collection plate, or diverting funds from the church budget or investment accounts" (Brotherhood Mutual Insurance Company, 2015).

Much of the fraud goes unreported. Barrett worked with accounting fraud experts on his initial study who estimated that as much as 95% of fraud within churches goes undetected or unreported (Palvo, 2013). Similar studies of corporate fraud estimate that over 66% of these misappropriations are not reported (Palvo, 2013). Fraud in churches and church based organizations continues to grow. Brotherhood Mutual Insurance Company (2015) estimated that fraud in churches is growing at a rate of 6% annually, with losses expected to reach nearly \$6 billion by 2025.

A common element in asset misappropriation and fraud, regardless of whether it occurs in the corporate or not-for-profit (NFP) sectors, is that the internal controls over the accounting system that should have prevented, deterred or detected the fraud were circumvented, were deficient, or did not exist. One consequence of the major corporate frauds was the enactment of the Sarbanes Oxley Act of 2002 (SOX). One aspect of this legislation requires publicly held

companies to enhance their systems and standards of internal control. Given the rise in church related frauds, religious institutions must also review and enact stronger systems of internal control.

Internal controls are important because they address risks the organization faces regarding its financial reporting process and the internal controls provide assurances to donors and church governing bodies that the resources donated are properly accounted for, disbursed according to management and donor intentions, and assets are protected. Internal controls do not guarantee an environment where errors and fraud do not occur. Rather effective internal controls provide “reasonable assurance” that errors and or fraud have not occurred. There is a cost-benefit relationship, where the costs of providing greater assurances must be less than the expected benefits. Churches, especially small churches, face particular challenges regarding internal controls because they may not have the resources or manpower to effectively deter risks of fraud or misappropriation.

For this research, we developed a survey instrument. Sixteen local church treasurers participated in the survey to determine the extent to which the churches follow accepted standards for internal controls as they relate to contributions. The challenges and issues that churches face in dealing with matters of internal control over contributions is the focal point of the survey. The results of the survey will shed light on the extent to which our sample of local churches have appropriate internal control procedures in place and are in compliance with existing internal control guidelines. The survey represents a starting point for further research aimed at internal controls in churches. The results of this research, we hope, will be helpful to church leaders in establishing better systems of internal controls and help to stem the tide of fraud in local churches.

The remainder of this paper is organized as follows: a review of the literature is presented, followed by the research approach and finally our findings.

## LITERATURE REVIEW

The existing literature on internal controls for NFP organizations, including churches, demonstrates the necessity of strong internal controls as a way to safeguard the assets and to maintain the trust of the donating public. Since NFP organizations are generally not as heavily regulated or closely monitored as for-profit corporations, appropriate internal controls are of particular importance. The responsibility to build and maintain a strong internal environment in order to ensure the efficient use of resources and protect against inappropriate use of its assets lies with the Treasurer and Chief Financial Officer (CFO) of the organization. The activities of the CFO/Treasurer consist of keeping financial records, preparing accurate and meaningful financial statements, budgeting and anticipating financial problems, safeguarding and managing financial assets, and complying with federal and state reporting requirements. Additionally, the Treasurer/CFO is instrumental in setting the “the tone at the top” for the entire organization by ensuring the financial legitimacy of nonprofit entities (Gross, Larkin, & McCarthy, 2000).

There has been increased scrutiny of fraud in the nonprofit sector. The regulatory bodies have recommended ways to deter frauds in this area. One of the main recommendations is to attempt to engage financial experts, or at least financially knowledgeable individuals, to serve on the finance committee. Even though segregation of duties may be difficult in small organizations, segregation of duties is especially critical in fighting embezzlement and fraud when cash is handled. Churches face the challenge that qualified assistance may not always be readily available and it is often difficult to find someone who will be of continued support (McNeal & Michaelman, 2006).

Internal controls are systems of policies and procedures that protect the assets of an organization, create reliable financial reporting, promote compliance with laws and regulations and achieve effective and efficient operations. In order for the system of internal control to be effective, it is imperative that management is committed to developing and sustaining ethical values and processes throughout the organization (McNally, 2013). The Committee of

Sponsoring Organizations of the Treadway Commission (COSO) Framework states that the internal control process provides assurances that the following objectives are met: (1) operational effectiveness, (2) reliability of financial reports, and (3) compliance with regulations (COSO, 2008). Internal controls, in addition to relating to accounting and reporting, also relate to the organization's communication processes, internal and external, and include procedures for (1) handling funds received and expended by the organization, (2) preparing appropriate and timely financial reporting, (3) conducting the annual audit of the organization's financial statements, (4) evaluating staff and programs, (5) maintaining records of real and personal property, and (6) implementing organizational policies (Cuomo, 2007).

### **Lapses of Internal Controls at Churches and Resulting Frauds**

The popular press is replete with examples of lapses in internal controls at churches resulting in fraud. For example, a Southern Baptist church in Mississippi discovered that a member/employee had embezzled more than \$700,000 over a three-year period. The church had over 1,000 resident members and an average attendance of over 400 parishioners each Sunday morning. It was discovered that the church's undesignated gifts were embezzled during this period, ranging from \$600,000 to \$800,000 per year. For a three-year period, that one trusted individual embezzled approximately 33% percent of the church's income without being detected. The embezzlement occurred due to poor internal controls over cash receipts (Duncan & Flesher, 1999).

A church treasurer stole more than \$45,000 by placing the funds in a separate account from the church designated building fund. The treasurer was able to create false financial statements to cover up fraudulent transactions since he alone was responsible for keeping the church's books and reconciling its bank account (Slaybaugh, 2005). This embezzlement illustrates the results of poor internal controls and lack of segregation of duties.

A former employee of the United Methodist Church was sentenced to two years in prison for embezzling more than \$158,000 from the church. The employee worked in the finance department and court documents show she began stealing money in 1999. She wrote approximately 70 checks either directly to herself or to pay credit card bills and phone bills. The church's denominational governing body (conference) discovered she had written three checks totaling about \$12,000 which she repaid, but a subsequent audit uncovered the additional missing funds. This employee was responsible for the books and reconciling the bank accounts (Adams, 2004).

In February 2009, Father Magaldi pleaded guilty to one count of embezzling \$120,000 from St. Anthony Church. The priest forged a total of five checks and coerced a St. Anthony volunteer worker to send him \$2,500 from weekly mass collections. In this case, there was evidence of collusion to override the system of internal controls (Podles, 2008).

These scenarios provide antidotal evidence that internal controls often are weak in churches. There is some historical evidence that the avoidance of mixing the sacred mission with the profane activity of accounting led to insufficient internal controls in churches (Laughlin, 1988). Laughlin (1988) also conjectures that as long as contributions were sufficient to cover the expenses of the sacred trust, there were few questions about the finances of the church. To date, minimal research on the connection between internal controls and fraud in churches is found in academic literature and little on the subject as it relates to NFP organizations in general. One notable exception is Holtfreter's (2008) study of fraud in 128 NFP agencies. The study identifies fraud involving the physical theft of organization assets as occurring more frequently; however, the biggest losses occur from wrongfully misappropriated funds or property entrusted to the care of institutional workers.

Holtfreter's (2008) analysis also indicates that a significant predictor of financial loss is the lack of adequate internal controls. However, even when greater levels of internal controls exist,

losses can still occur (Holtfreter, 2008). Duncan & Flesher (2002) studied the internal controls of churches, addressing the types of internal controls actually in place and functioning in church accounting systems. Their research found that many churches had several controls in place related to cash receipts. However, most churches indicated that they lacked the elementary controls prescribed in accounting literature. Large churches tended to have more control procedures in place, but all the churches in the Duncan & Flesher study could improve their existing internal control systems. They concluded that although a strong system of internal control may cause inconvenience from time to time, the existence of such a system is well worth the effort in the long run (Duncan & Flesher, 2002).

In their study of religious NFP organizations, Wooten, Coker & Elmore (2003), found a positive correlation between organization size and the strength of internal controls largely due to the resources available and greater accountability required by the constituents. They also found that internal controls over receipts of tithes and offerings were stronger than the controls over disbursements. Wooten et al. (2003) suggest that the stronger internal controls over receipts can be linked to tax-deductibility of charitable contributions for member-donors.

### **Implications on Internal Control from the Sarbanes Oxley Act (SOX)**

While SOX applies to public companies, the legislation has increased public attention on potential issues of fraud in NFPs. In particular, two provisions of SOX have direct implications to both public and private entities: whistleblower protection and document destruction policies. SOX provides extensive protections for whistleblowers, and also requires the adoption of a written policy regarding the procedures for disposing and archiving corporate records (A Guide to the Sarbanes-Oxley Act, 2002).

The increased scrutiny on corporate governance has resulted in the development of best practices based on SOX rules. Though not required for churches, compliance with these



practices would appear appropriate in order to strengthen the internal controls for churches. A summary of the recommendations made by SOX for NFP organizations includes establishing an audit committee tasked with overseeing accounting and financial reporting processes; having annual audits of all financial statements; prohibiting the practice of providing personal loans to officers (i.e. if it is necessary to extend a loan, the NFP board should formally approve the loan); evaluating whether strengthening internal controls is feasible and cost-effective; evaluating whether strengthening disclosures is feasible and provides an accurate picture of its financial condition to anyone who requests them; and finally, adopting a code of conduct which include enforcement policies.

Churches should be encouraged to analyze their practices and methods of operation. Many may need to conduct a top-down review of their practices and re-evaluate certain relationships, such as with their auditors. Here is where the governing body of the church organization needs to be involved; to effectively update policies and procedures, organization documents and structures need to be evaluated and updated to reflect SOX indicated best practice. It is important to note that, for churches, self-regulation and proactive behavior usually proves more powerful than defensive policies. Auditors play an important role in establishing the rules and procedures that need to be followed at the local church level and should recommend practices and procedures that may be cost efficient for particular church organizations (Metropolitan Corporate Counsel, 2009).

Strong internal controls provide reasonable, not absolute, assurance to prevent and detect errors, but they cannot guarantee that errors will never happen. Some limitations include human error, carelessness, management override, and collusion. However, the separation of duties is an important step in implementing a strong system of internal control.

The initial custody of cash is vitally important and an unavoidable component as it relates to the internal controls of finances. Cash is the primary target of fraud; consequently, the inherent risk

for cash is generally highest among all assets. Cash is not easily identifiable as company property and it is highly portable; therefore, controls over cash must be unusually strong (Whittington, 2009).

## METHODOLOGY

Based on the objectives and goals of this research, a survey instrument is the best tool to obtain the necessary data. Surveys are useful in describing the qualities of a population, especially when there may be high levels of variations. Standardized questions make measurement more precise by enforcing uniform definitions upon participants and also ensure that the data can be interpreted comparatively. Qualities of a good survey instrument include identifying the purpose and properly pinpointing the information needed to develop questions that gather the important data. Question sequence is an important aspect of survey instrument development. A logical flow of questions can make the respondent feel more comfortable and focus less on the time spent (Parker & Rea. 1992).

Our survey instrument consists of a mix of predominately close-ended questions paired with some open-ended questions to gather the type of data necessary to completely understand the existing controls in each church. The survey was administered utilizing a personal interview rather than a mail survey. By conducting personal interviews, a degree of reliability was added along with the expectation that the church treasurer would feel free to share complete information. Also, we felt personal interviews provided some assurances that the information provided was an accurate indication of the procedures and systems actually in place. This method allowed us to ask follow-up questions, clarify answers that were unclear and overall garner a better indication of the emphasis placed on internal controls within the church.

Each church had a written set of policies and procedures to assist with the continuity and sustainability of a strong system of controls. The primary basis of the survey questions was the audit program used by the Protestant denomination when auditing local churches. The internal

controls section of the audit program provided valuable insight regarding the controls of particular relevance to churches. Supplemental questions relevant to internal controls were added to provide a richer basis for data analysis. In addition to the background information collected on the participants, other sections of the survey related to the chronological flow of the church offerings and donations (i.e. cash, checks) from the time of collection until the time that funds are deposited in the bank, recorded and reviewed. Given that cash is an asset susceptible to embezzlement, and given the number of individuals involved in collection activities, we viewed the controls over cash as extremely important. The need for exemplary controls over cash is magnified since church members may be likely to suspend future contributions should theft of offerings occur.

Questions on disbursement procedures were also included the survey followed by a number of other miscellaneous control-related items. A copy of the survey is found in the Appendix.

## **EXPLANATION OF MAJOR SURVEY ELEMENTS**

### **Background information**

Background information covered the attributes of the church and was used to compare churches in the sample and to analyze any trends that may exist with churches possessing similar characteristics.

### **Collections & deposits**

These questions covered the internal control practices over the initial custody of cash and checks as they were collected until deposited in the bank.

### **Accounting record-keeping**

This section of the survey covered policies and procedures in place to insure the integrity of the accounting function.

### **Cash disbursements**

This section of the survey covered the procedures and practices relating to cash disbursements. Cash disbursements are another area vulnerable to a potential of misuse of church funds. Proper authorization is a key element behind proper control over the disbursement of cash.

### **Reconciliation, External review and other**

The questions in this section covered reconciliations and audit focusing on the separation of duties and frequency of audits.

### **Data Collection**

A sample of sixteen local churches, affiliated with a Protestant denomination were included in the study. The churches were located in southwest Michigan, Northern Indiana and New York City. Prior to beginning the research study, the survey was approved by the university's Institutional Review Board and permission was granted by the church governing bodies (conferences) to survey the church treasurers. Two of the three conferences provided sample of audit programs, church manuals, and/or guidelines for procedures to be followed by their given church entities.

## DATA ANALYSIS AND RESULTS

Given the small sample size, no statistical tests were performed. Data analysis primarily involved determining and reporting upon relevant patterns found in the study data. A summary of results follows.

Six of the churches had 150 members or less, seven of the churches reported membership between 151 to 300 members and three churches reported 300 members to 600 members. Weekly tithes and offerings ranged between \$7,000 and \$10,000. Member contributions are valuable to churches as tithes and offerings are the primary sources of support for all the church activities and functions.

Cases of theft involving the initial custody of cash occur in various types of organizations. Within the local church environment, a secure room to count funds is of high importance. Counting money in an unsecured location is not utilizing adequate safety controls and creates minimal deterrence for criminally-minded individuals. All the survey participants described their cash collection process and have reasonable control over the initial custody of cash. A minimum of two individuals counted the money, with an average of 2.8, with two other individuals being on duty and present.

Figure 1 shows an overview of controls over cash. In just over 80% of the churches, checks were endorsed immediately while the money was counted. In 94% of the churches, all cash was deposited. Only 27% of the churches used requisition slips to request money; however, 94% of the churches made all disbursements by check. Half the churches required two signatures on checks; just 19% of the churches used a petty cash fund. We discuss this further below.

**Figure 1. Overview of controls over cash**

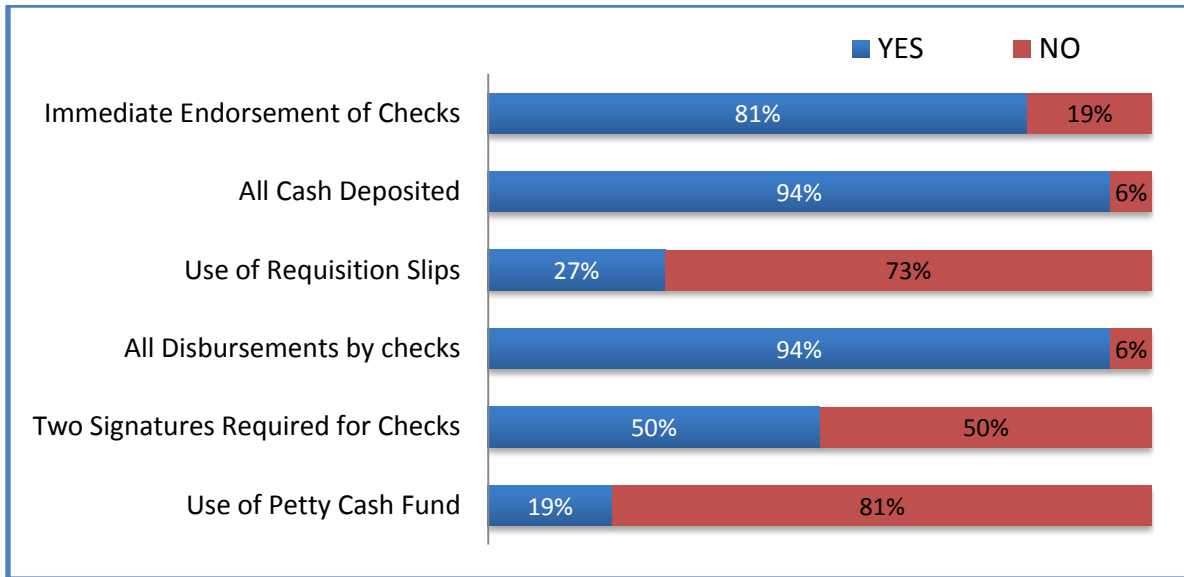
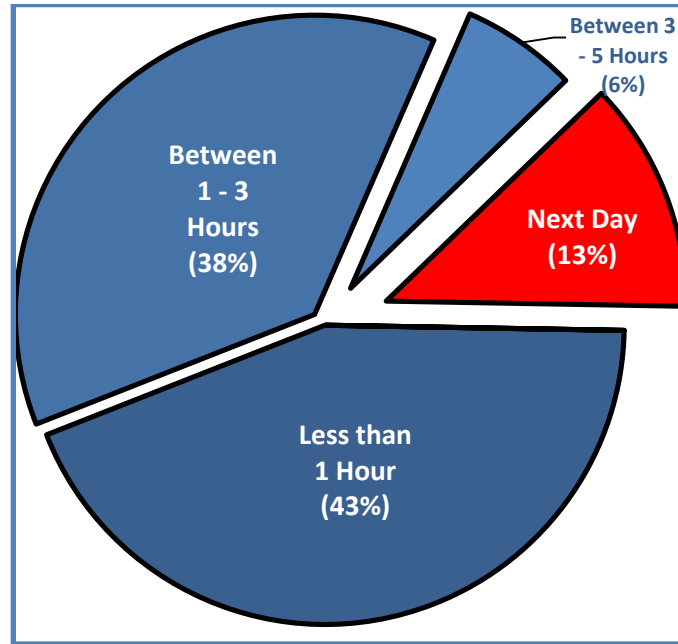


Figure 2 shows the results of the timeliness of counting the money. All churches reported counting the money within a day of collection and approximately 87% of the churches counted the money the same day. Forty-three percent of the churches counted funds within one hour of collection and 44% between one and five hours of collection. Thirteen percent of the respondents indicated that offerings were not counted until the next day.

Figure 2. Timeliness of cash counts



### Timeliness of Bank Deposits

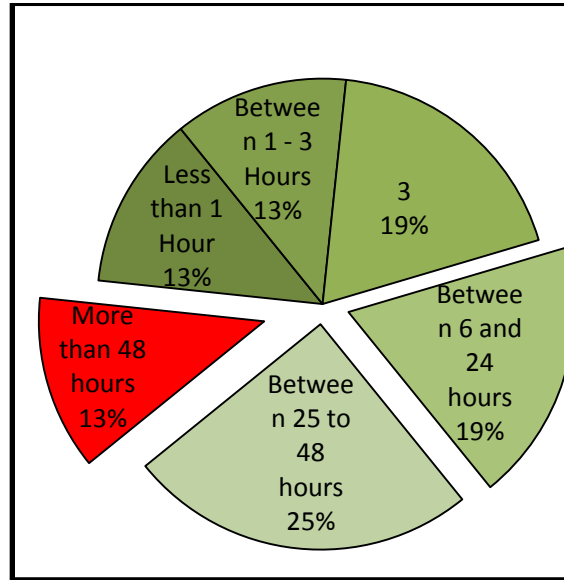
Figure 3 presents the timeliness of bank deposits. Approximately 45% of churches in the study deposit cash collections within 24 hours of collection; 19% have policies in place not to deposit funds on the day of worship, but to make the deposit on the following day. In fact, 38% report that deposits are made more than one day after collection. Waiting several days before depositing cash and checks represents a major vulnerability of cash fraud.

### Security of Church Funds

The security of church funds refers to safeguarding of money between the time of count and the time of deposit. Ideally, funds should be deposited immediately and at a night deposit if the bank is not open. When there is a delay between counting and depositing the money, it should be stored in a safe, lockbox or other secure place that only the treasurer or cashier has access to. In the situation where funds are deposited the same day, the funds may only be in the safe

for a few hours. However, in cases where funds are not deposited the same day, it is vitally important that they are stored in a locked safe.

**Figure 3. Timeliness of deposits**



### **Check endorsement and cash deposited**

An important factor is the immediate endorsement and deposit of checks. Cashiers should stamp or sign checks as soon as they are received to minimize misuse of members' contributions; approximately 81% of the local churches held to this practice (see Figure 1). Though checks were endorsed immediately, there were variations in the timeliness of the bank deposits and the security over collection funds until they were deposited.

### **Accounting and Record Keeping**

Results of the study showed that approximately 62% of the churches had an updated accounting procedures manuals. Treasurers and church officers change from time-to-time



making it vital to practice sound financial principles and consistently apply the guidelines and procedures. A manual helps to provide this level of stability.

An important aspect of internal control is to separate the recording and custody functions. Approximately 44% of the church treasurers in the sample had duties that combined the recording, custody or authorization functions. Treasurers are placed in a position of high responsibility which translates into high trust; however, there should be help available to treasurers to maintain a proper separation of duties. In smaller churches, maintaining separation of duties may be more difficult due to lack of personnel or relying upon volunteers to assist with treasury functions.

### **Cash disbursements**

The requirement to have two signatures on checks was split 50/50 among the participant churches. This was not a requirement for all churches, but it provides an additional control to help ensure that all disbursements are properly approved. Another area of control is to retain all voided checks; all respondents followed this practice.

### **Petty cash**

A number of churches in the study used a petty cash fund for minor disbursements, while others did not keep cash on hand. Different churches operate under different circumstances and have to adjust procedures to meet their particular needs.

## **Review and reconciliation procedures**

Reconciling the differences between the bank's records and the cash accounts at regular intervals and taking appropriate action with respect to any differences, is especially important to the entire process. To maintain an effective system of internal control, segregation of the duties of reconciling bank accounts and check writing is essential. Only 38% of the churches prepared monthly bank reconciliations by a person not involved in writing checks; in approximately 62% of the churches, the bank reconciliations were prepared by an individual who also signed checks and/or maintained the books. This practice provides prime opportunity for embezzlement with the ability to effectively conceal the theft.

## **Periodic Audit**

A yearly audit is an important function of the review process. Results of the survey indicated that 62% of church treasurers reported both the accounting records and internal controls were regularly audited, while the remaining 38% replied that only the accounting records were audited. However, only 50% of the churches had had any sort of audit within the past year.

## **Other practices**

All churches participating in the study encouraged members to use offering envelopes. By utilizing offering envelopes, members are eligible to receive Charitable Tax Deduction statements for their tax returns. Offering envelopes also provide increased control over cash contributions versus contributions that are "loose offerings" in the collection plate. Members should be made aware that offering envelopes assist the treasury in record-keeping and provide the option to designate fund allocation and ensure that the money is used as designated.

Other common practices found in all surveyed churches include: mailing or distributing annual contribution receipts to donors; retaining voided checks, and having at least two individuals to count the money (i.e. joint custody). These common practices are essential to effective cash handling.

## **DISCUSSION AND CONCLUSIONS**

A number of control weaknesses were noted. The first involved cash collections. While 43% of the cash counts occurred within the hour after collection, 44% of the participant churches reported that they counted the money later on (more than one hour) after collection, but on the same day. Overall, 87% of the churches reported counting the offerings on the day collected. Thirteen percent did not count the collection until the next day. The longer the time gap between the collection and counting of cash, the greater the chance that a mishap occurs.

Nearly 19% of the surveyed churches have policies in place to not deposit funds on the day of worship, but to deposit it the following day, within 24 hours. There were 37% of the responding churches that deposited the funds more than 24 hours later and 13% deposited more than 48 hours later. This represents a major vulnerability of cash fraud. Leaving funds in the church building or taking the funds to a treasurer or cashier's home creates increased opportunity for funds to be lost, stolen, or misused. Given that cash is highly portable, controls over cash must be particularly strong. Therefore, once funds are collected and counted, deposits should be made as soon as possible, utilizing a bank drop box or night deposit box where necessary. In the rare instances when this is not possible, an in-church safe is recommended to secure the funds until deposits may be made. This safe should be locked with access only available to the treasurer (or certain treasury staff).

Many of the churches in the study had procedures in place relating to the security of cash receipts. However, as may be expected, the larger churches had more controls in place. Most of the churches (approximately 63%) can improve on their internal control systems in one or more

of the following areas: obtaining & following accounting procedures manual, counting money in secure room immediately after collection, immediate deposit of funds, and monthly reconciliation by independent party.

Besides making contributions via the offering plate donors can use their bank's bill-pay option to have their contributions sent directly to the church. Some church websites offer online giving which provides the ability to pay with a credit card or checking account. Online giving reduces handling of funds which decreases the opportunity for theft as well as providing some reduction in the workload of treasury staff. Members should be made aware of online giving, reminded of this option and encouraged to use it.

Cash disbursements appears to be another vulnerable area for churches in the study. Only 27% of the churches used requisition slips (ie purchase order forms) for disbursements. When using requisition slips documentation should be attached. This provides a way to track anticipated disbursements, ensure the proper payee and and that the amount paid is correct. Dual authorization should be in place for requisitions of amounts of a preestablished amount, such as \$2,000 (Best Practices for Church Financial Internal Controls, 2013) and the church finance committee should pre-approve large expenditures.

The requirement to have two signatures on checks was split 50/50 among the participant churches. It is highly recommended that all churches implement procedures requiring approval with two signatures on checks and authorization limits set at minimal dollar amounts. These changes will provide additional controls over cash disbursements.

Another area of concern was the separation of duties between the recording function and the authorization function. In 44% of the churches, the person responsible for authorizing transactions was the same person who signed the checks. Treasurers are placed in a position of

high responsibility and high trust and there should be help available to treasurers to maintain a proper separation of duties. Ideally, the four functional responsibilities should be performed by four different staff members. These include: [1] authorization to execute transactions, the authority and responsibility for initiating or approving transactions; [2] recording transactions (refers to the accounting and record-keeping functions); [3] custody of assets - in church organizations this would include the deacons, cashiers and treasurers who have physical possession of cash at some point during the process between the offering collection and the deposit at the bank; and [4] periodic reconciliation of existing assets to recorded amounts, such as bank reconciliations that should be performed monthly (Louwers, Ramsay, Sinason, & Strawser, 2008).

Segregation of duties relating to cash is an area where most of the churches surveyed should improve. Only 38% of the churches conducted monthly bank reconciliations by a person not involved in writing checks; 62% of the church's bank reconciliations were prepared by an individual who also signed checks and/or maintained the books. It is highly recommended that the custody, reconciliation and authorization functions be segregated. For churches that do not have paid staff or a sufficient number of volunteers to separate these duties, the pastor or someone from the finance committee should review the bank reconciliations on a monthly basis to help ensure that the process is up to date and accurate.

While audits are an important part of the review process there appears to be a deficiency in the regularity and timeliness of church audits for the participants in the study. In this denomination there are conference auditors who audit the local church books on a regular basis, but because of limited audit staff, audits may occur only once every two or three years.

While we report some weaknesses in internal controls, overall our findings support Wooten et al.'s (2003) findings that internal controls are stronger for receipts than disbursements. Eighty-seven percent of the churches surveyed counted the offerings by the end of the day when they

were collected. Sixty-two percent deposit the offerings in the bank within 24 hours after counting, while 19% had a policy for not depositing on the day of worship. The controls over disbursements were not as widely practiced. A little over a quarter (27%) of the churches used requisition slips for disbursements. In 62% of the churches the bank reconciliations were prepared by someone who signed checks or maintained the accounting records.

One purpose of this study is to establish a platform for future research. Our results point to major weaknesses in internal controls over cash disbursements and the need for improvement. The results also provide guidance for church leaders on changes that should be implemented.

The research represents a study thus the sample size is small. A larger sample would enrich the data and make the findings more applicable to a broader group of church based organizations.

This study indicates a need for more research on fraud and the relationship to internal controls in churches and church-based settings. This is particularly relevant given the estimates of the growing problem of fraud and its significance to church entities.

## **Conclusion**

While churches are built upon a system of faith, hope, and love, the stark reality is that instances of fiscal misconduct within church based organizations are on the rise. Unless proper internal controls are in place and are enforced, churches become opportunities for misappropriate funds and fraud to occur.

As former President Ronald Reagan said, "Trust, But Verify!" Thus, church leaders must take cost-effective precautionary measures to create a secure internal control environment. Yes, trust the treasurers, but audit their work. It will be well worth it in the long-run.

## Appendix

### Survey Questions - Evaluating Internal Controls at Local Churches

#### Background

1. What is your current church membership?
2. What is the average church attendance?

<input type="checkbox"/> Less than 50	<input type="checkbox"/> 451-600
<input type="checkbox"/> 50-150	<input type="checkbox"/> 601-750
<input type="checkbox"/> 151-300	<input type="checkbox"/> 751+
<input type="checkbox"/> 301-450	
3. On a given day of worship, what is the average collection of Tithes & Offerings in total?

<input type="checkbox"/> Less than \$500	<input type="checkbox"/> \$10,001-\$12,000
<input type="checkbox"/> \$501-\$1,500	<input type="checkbox"/> \$12,001-\$15,000
<input type="checkbox"/> \$1,501-\$3,000	<input type="checkbox"/> \$15,001-\$20,000
<input type="checkbox"/> \$3,001-\$5,000	<input type="checkbox"/> \$20,001-\$25,000
<input type="checkbox"/> \$5,001-\$7,000	<input type="checkbox"/> \$25,000+
<input type="checkbox"/> \$7,001-\$10,000	
4. How many deacons are on duty on a typical day of worship?
5. What percentage of total funds collected, on a typical day of worship, is received in currency? In checks?

_____ Currency
_____ Checks
6. Are member encouraged to use offering envelopes?

<input type="checkbox"/> Yes
<input type="checkbox"/> No

#### Collections & Deposits

7. How many individuals are normally on duty to count the money? How does this vary from week to week?
8. Where are funds counted?
9. How soon after funds collected are they counted?

<input type="checkbox"/> Less than 1 hour	<input type="checkbox"/> Next day
<input type="checkbox"/> Between 2-3 Hours	<input type="checkbox"/> During the following week
<input type="checkbox"/> Most times between 3-5 hours	<input type="checkbox"/> Other _____

10. How soon after funds are collected are they deposited in bank?

- Less than 1 hour
- Between 2-3 hours
- Most times after 3-5 hours
- Next day
- At least 2 days after

11. Where are funds kept between the time they are counted and the time they are deposited in the bank?

- Church Office
- Secure Safe Box
- Other \_\_\_\_\_

12. Who deposits funds in the bank? (check all that apply)

- Assistant Treasurer
- Deacon
- Treasurer
- Pastor
- Other \_\_\_\_\_

13. Is all cash received deposited in the bank?

- Yes
- No

14. Are checks restrictively endorsed as soon as received?

- Yes
- No

### **Accounting Record-Keeping**

15. Does the church have a written, up-to-date accounting procedures manual?

- Yes
- No

16. Do the financial secretary(s) of treasurer's activities involve only keeping the records of cash collections and preparing the support for disbursements?

- Yes
- No

17. Where are the accounting records stored?

18. Who has access to these files?



19. Are contribution records maintained for members?

- Yes
- No

### **Disbursements**

20. How often do members receive notices of contributions?

- Only when solicited
- Yearly
- Quarterly
- Monthly
- Weekly

21. Are requisition slips prepared for anticipated disbursements

- Yes
- No

22. Are all disbursements made by serially numbered checks?

- Yes
- No

23. Are at least two signatures required for all checks?

- Yes
- No

24. Are all voided checks marked and retained?

- Yes
- No

25. Is a petty cash fund used for minor disbursements of cash?

- Yes
- No

26. Are vouchers prepared for petty cash disbursements?

- Yes
- No

### **Reconciliation and External Review**

27. Are reconciliations of all bank accounts prepared monthly by a person not involved in writing checks?

Yes

No

28. Is the petty cash fund reconciled on surprise basis at least once a year?

Yes

No

29. When was the last time your church was audited?

In 2008

In 2007

In 2006

Other \_\_\_\_\_

30. What is normally audited?

Accounting Records Only

Internal Controls Only

Both Accounting Records and Internal Controls

Other \_\_\_\_\_

31. Are financial statements audited yearly?

### **Other**

32. Do you do background checks on all employees?

33. Do you require 2 week rotations of all employees?

End of survey, thank you.

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