



LOCAL CHURCH AUDIT GUIDE

Prepared for churches of the
Canadian Baptists of Ontario and Quebec

This booklet is given to you as a service of the Canadian Baptists of Ontario and Quebec. We hope you will find it useful. If you have suggestions for making it better, please telephone, write or email us at:

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DISCLAIMER

The Canadian Baptists of Ontario and Quebec are not responsible for the conduct of local church audits, nor do they provide legal or financial advice to local churches through this booklet. Local churches should seek assistance and advice from their local advisers when specific issues arise. This guide is provided to you as a service; it should be used to increase knowledge of auditing principles within your local church, including the understanding of why audits should be conducted and the uses to which they can be applied by local church officials.

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What Is an Audit?

The word *audit* is derived from a Latin word meaning *to hear*. It is the auditor's job to hear and judge the accuracy of various kinds of testimony or evidence. In the modern context, the auditor is usually faced with written testimony, often in the form of financial reports or schedules. The objective of the audit then becomes an assessment of, and an expression of opinion on, the accuracy and fairness of the information presented in those reports or schedules.

There are different kinds of audits available to churches and other organizations. The most formal and structured type is an independent audit of financial statements performed by a Chartered Accountant (CA). These audits are conducted according to uniform national standards and result in an objective opinion on the fairness of the organization's financial statements. Chartered Accountants and other certified accounting professionals can also conduct a *review* which does not adhere to the same standards as a formal *audit* and thus is of minimal benefit. Local churches incorporated under the Canada Not-For-Profit Corporations Act (CNCA) are required to have an independent external audit. The level of financial review requirements depend on whether the incorporated church is a soliciting or non-soliciting corporation as per the chart listed below.

Level of Financial Review			
Type of Corporation	Gross Annual Revenues	Appointment of Public Accountant (PA)	Review Engagement or Audit
Soliciting	\$50,000 or less	Members must appoint a PA by ordinary resolution at each annual meeting. Exception – Members may waive appointment by annual unanimous resolution.	PA must conduct review engagement , but members may pass an ordinary resolution to require an audit instead. (If no PA is appointed, then compilation only.)
	More than \$50,000 and up to \$250,000	Members must appoint a PA by ordinary resolution at each annual meeting	PA must conduct an audit, but members can pass a special resolution to require a review engagement instead.
	More than \$250,000	Members must appoint a PA by ordinary resolution at each annual meeting	PA must conduct an audit.
Non-Soliciting	\$1 million or less	Members must appoint a PA by ordinary resolution at each annual meeting. Exception – Members may waive appointment by annual unanimous resolution.	PA must conduct review engagement , but members may pass an ordinary resolution to require an audit instead. (If no PA is appointed, then compilation only.)
	More than \$1 million	Members must appoint a PA by ordinary resolution at each annual meeting.	PA must conduct an audit.

Lastly, there is the *internal audit*, conducted by members of the congregation and may have different, possibly broader, objectives than an independent audit. It is this type of audit, which is the subject of this guide.

For the purposes of this Guide then, here is our practical, working definition of an internal audit for the local church:

A local church audit is an internal independent (from those responsible for the financial records) evaluation of the financial reports and records and the internal controls of the local church by a qualified person or persons for the purpose of reasonably verifying the reliability of financial reporting, determining whether assets are being safeguarded, and whether church policies and procedures are being followed.

Who should be on the Audit Committee?

Audits can be performed by anyone, but certain types of audits require certain characteristics and qualifications. Audits of financial reports require that the individuals performing the audit have a reasonable familiarity with the terms, concepts, and practices of the financial world. It is presumptuous of anyone to publicly express an opinion on the accuracy of something that they themselves do not understand. Accordingly, appointments to the Audit Committee should be made with this in mind.

Without a doubt, however, the single most important characteristic for an auditor to possess is integrity. For an audit to be useful and effective, the person or persons performing it must do so in an objective and impartial fashion, and with the highest degree of integrity. The Audit Committee has the task of lending public credibility to the financial reports of the church. This cannot be done if the membership perceives the Committee as biased or lacking in knowledge or ability.

Merely *having* an Audit Committee will not accomplish the objectives desired by the church's governing body. Some Audit Committees are very ineffective, because they function as little more than a rubber stamp of approval for whatever is presented to them. To be truly effective, an Audit Committee must be given the resources of talent, time, and access. Only then will the Committee's report in the church's annual report to its membership have any true meaning.

It is important within the church's financial structure to maintain a separation of duties. For this reason, persons who are related to the treasurer or the financial (envelope) secretary should not serve on the Audit Committee.

In some smaller churches, there are often only one or two individuals who have the financial experience required and so it is likely that they are already acting as treasurer, finance committee chair or envelope steward. Churches are encouraged to think creatively as to how an audit might be accomplished within this scenario. Perhaps another local church treasurer would be willing to audit your church records in return for you acting as their auditor. Or, perhaps a local retired accountant would be willing to do the work on a pro-bono basis.

What is the Role of the Audit Committee?

The Audit Committee represents the interests of the membership of the church, as well as those of the clergy, the church governing body, and the BCOQ. The Audit Committee is entrusted to perform a task that none of these individuals or groups can perform, primarily because they do not have access to the financial information and transactions of the church on a daily basis. The members and other interested parties are not in a position to judge the accuracy and fairness of any summarized financial reports which the church produces.

The Audit Committee has the task of attempting to verify the truth and accuracy of the information contained in the church's financial reports, and by expressing an opinion on such information, make them more believable and acceptable to all interested parties. Such credibility can be achieved only if the Committee itself is believable. It is often said that the cornerstone of any audit is *independence*, meaning that the auditors must be unbiased and impartial regarding the material which is the subject of their audit. Only then can they offer a fair opinion on what they have examined. Perception can be just as important as reality in meeting this test, for an individual may be the most honest and objective person alive, but if the membership of the church *perceives* that person to be biased or to have a vested interest in the subject matter of the audit, any report they might give will not be credible. Thus it is not appropriate for a church's treasurer or financial secretary to serve on the Audit Committee. Certainly these individuals will play a central role in the audit, and they must be readily available to the Committee. The audit and the audit report, however, must be produced by individuals who are not now, and have not been, involved in the accounting or record keeping for the church during the year under audit.

The church and its leadership have a stewardship responsibility to see that the resources made available are used in the service of Christ and in the manner designated by the church leadership and the membership. This responsibility also extends to managing special gifts that may be restricted by the donor, and thus are available only for a specific purpose. A properly functioning Audit Committee will help the church to fulfill its stewardship responsibility by helping to assure that resources have been used in the proper fashion.

The church Audit Committee has a uniquely challenging task because of the environment in which it must operate. Churches are typically, and appropriately, characterized by a high degree of trust among the staff and employees. Nonetheless, prudence dictates that the church leadership must remain ever vigilant in order to fulfill the responsibilities given to it. No individual is above temptation. Jesus Himself was tempted by Satan. And yet who among mortals has the strength of Christ to withstand all such assaults? The Audit Committee is sometimes perceived as superfluous or unnecessary because of the trust placed in the church's treasurer and/or financial secretary. In the vast majority of cases that trust is well deserved. In other cases, the Committee is viewed by those whose work comes under scrutiny as an attempt to discredit or devalue their work. Indeed, the treasurer or financial secretary should not view the Audit Committee as a vehicle by which the church is expressing distrust or suspicion. On the contrary, the Audit Committee in a church should celebrate the good work of the treasurer and financial

secretary and hold it up high for all the membership to see!

The purpose for an annual audit then is:

- To protect the persons the local church elects to offices of financial responsibility from unwarranted charges of careless or improper handling of funds;
- To build the trust and confidence of the financial supporters of the church in the way their money is being accounted for (trust and confidence lead to improved patterns of financial support);
- To set habits of fiscal responsibility to assure that when there is turnover in personnel there will be continuity in accountability and nothing will fall through the cracks;
- To assure that gifts made to the church with special conditions attached are consistently administered in accordance with the donors' instructions, and thus let donors know their gifts are used as intended;
- To provide checks and balances for sums received and expended.

In order to make the task more manageable, some churches have opted to have a six-month review. This allows for some work to be done mid-year and to identify potential problems before they reach crisis level.

Conducting an audit is not a symbol of distrust.

It is a mark of responsibility.

It is good stewardship demonstrated for all to see.

It is a message to local church donors that you care about their gifts.

The Committee's Objectives

The objectives of the church Audit Committee are somewhat narrower than those of a public accountant auditing financial statements of a business. Most businesses must conform to a set of required accounting principles when presenting financial statements to the public, and auditors therefore gear their work toward reporting on whether the business' statements are in conformity with such acceptable accounting principles.

For many churches, especially smaller ones, generally accepted accounting principles (GAAP) are usually a non-issue. Compliance with such principles would only become important if the church had a need to publish its financial statements to outside parties, such as a lending institution, and was therefore required to have the statements audited by an independent outside auditing firm. Statements prepared for internal use by the church and its members need not conform to generally accepted accounting principles, although they certainly can be so prepared if the church wishes. It is usually much simpler for the church to prepare just those statements and schedules that it finds most useful.

Since most churches find that the information they need most often revolves around cash receipts and cash payments, the reports they have developed focus on these aspects of the church's operations. Accordingly, the principal objectives of the church Audit Committee will also concentrate on these areas. In general terms, the Committee must be able to satisfy itself that all cash received by the church has been recorded properly and deposited into a bank account where access is limited. Similarly, it should be satisfied that all cash payments have been properly authorized by the appropriate body within the church, properly documented and recorded. Finally, the Committee must be satisfied that all of these receipts and payments are correctly summarized and reported in the annual financial reports of the church, and that the information contained therein agrees with the underlying records of the church.

The Audit Committee's responsibilities will extend to other areas as well. For example, if the church has investments in securities such as stocks and bonds, the Committee will seek to assure itself that any purchase or sale transactions during the year have been properly authorized and recorded, and that the list of investments in the year-end financial reports is complete and accurate, properly representing what the church owns at year-end. On the other hand, if the church has any outstanding debts such as mortgages or loans, the Committee will want to assure itself that all required payments have been made during the year, and that the balances reported in the church's financial statements are accurate as of the date of the statements.

There are other areas that should get the Committee's attention too. These include the payroll area where the Committee will want to make sure that all employees and staff are being paid at the rate approved by the church governing body and that appropriate payroll remittances have been made. Additionally, the Committee should satisfy itself that the church has adequate insurance coverage for all of its property and potential liabilities. Also, the Committee may wish to conduct a periodic inventory of the church's property such as office equipment, audiovisual equipment, furniture, and similar items, comparing results with previous inventories to make certain that no assets have become

missing.

One final area which should be of concern to the Audit Committee is often overlooked in the rush to “crunch the numbers” in the church’s annual financial reports. This area is the daily, weekly, and monthly accounting *practices and procedures* employed in the church, and it is vital to the accuracy of the ultimate financial reports. If the procedures and practices used on an ongoing basis are not sound, there may be errors which will be beyond the ability of the Audit Committee to discover. Items may be overlooked and never recorded, or they may be lost. It is the validity of the ongoing practices and procedures that will provide some assurance that all events get recorded and nothing is lost along the way. The Audit Committee can be helpful here by reviewing the practices and procedures in use and making constructive suggestions when necessary. To assist in this function, the section of this handbook on practices and procedures contains a questionnaire which will help the Committee to identify potential weaknesses in the church’s accounting practices and procedures.

The audit in a local church may involve more than just the main church books. Individual groups within the church may maintain their own bank accounts and accounting records and therefore these should be included in the process. Examples of other groups might include:

- Sunday School
- Baptist Women
- Youth groups
- Memorial Fund
- Mid-week groups
- Special programs (food banks, day camps, etc.)

Throughout the process, the Audit Committee should document its work. All good auditors do this in the form of audit schedules or work papers, which form the basis and provide the evidence for the auditor’s conclusions. Church auditors should be no different in this regard. The Audit Committee is ultimately going to issue a report on the soundness of the annual financial reports, so it should have a well-documented basis for doing so.

Cash Receipts and Cash Balances

Much of the Audit Committee's work will revolve around the cash transactions of the church. This section will examine the audit objectives associated with cash receipts transactions and with the year-end cash balances which appear in the church's financial reports. There is also a suggested "audit program", a list of steps and tests which the Committee should consider while performing its work.

Since the majority of the church's cash receipts will occur as offering taken at worship services, the Committee should test a sample of such collections. As is true in most audit situations, the Audit Committee will not be able to check *every event and transaction* that occurred during the year, so the alternative is to choose a sample and draw conclusions from the examination of this sample. The size and extent of the sample is a matter of judgment and will depend upon the time and other resources which the Committee has available. Regardless of how large or small a sample is chosen, however, the sample should be as representative of the whole year's activity as possible. In other words, if the Committee decides to test six Sunday collections, the sample should not consist of six consecutive Sundays in the middle of the summer season. The sample should be chosen so as to represent the entire period's activity, the high points and the low, the busy and the slack.

Once the sample is chosen, the Committee should examine the document(s) produced by the person(s) who performed the count on the date of the collection. This should be some type of count sheet which identifies the gifts as cash or cheque and also as pledge or loose offering receipts. It should be signed by the person(s) who performed the count. The total should be verified by addition, and then should be traced to both a bank deposit slip and to the next subsequent bank statement to establish that all cash received was deposited into the church's bank account. Additionally, the total collected should be traced to an entry in the accounting records to establish that the amount collected was properly included in the church's cash receipt records. Time permitting, the Committee may also wish to trace some of the individual donor amounts identified by pledge # to the donor's pledge card or pledge record to establish the validity of the pledge records.

If any discrepancies are found, the Committee should request an explanation from the Treasurer or Financial Secretary, whichever is responsible for the transaction in question. The Committee must exercise judgment in assessing the validity of the explanation given, and if satisfied, may consider the matter closed. If, however, the Committee remains unsatisfied with the explanation received, it may wish to consider consulting with the church's governing body. Before taking this step, the Committee should be certain that it has fully investigated the transactions in question and documented its work so that a full description may be presented to the governing body.

The Committee will also want to verify the total receipts for the year, and this may be done by listing and adding the totals of the weekly entries to produce a yearly total. This should be compared to the total of pledge and loose income presented in the annual financial reports. It will likely not be in exact agreement due to minor corrections and

adjustments, but it should be close. This gives the Committee reasonable assurance that the total pledge and loose offering income in the financial reports is fairly stated. Once established, these annual totals should also be compared to budgeted amounts for the year and to similar amounts for prior years. The Committee should seek explanations for any significant unexpected variations.

It is important to understand that the Audit Committee cannot achieve 100% certainty as to the correctness of the annual totals of income and expense in the financial reports. This is so because the Committee cannot possibly examine every individual transaction which occurred during the year, and because of the possibility of human error on the Committee's own part. The goal of the Committee, therefore, is to reach a level of *reasonable certainty that there are no significant errors* contained in the totals.

The Committee must now turn its attention to the year-end cash balances which are presented in the annual financial reports. It should begin by identifying all the separate, individual bank accounts and listing them, with account numbers, and indicating whether they are chequing or savings accounts. This list should be maintained by the Committee and compared to the previous year's list with any changes being noted. Any change in the list of bank accounts should be traceable to the minutes of meetings of the church governing body where such an account opening or closing should have been authorized.

For any savings accounts, the passbook or statement should be examined and the balance determined as of the date of the fiscal year-end. This balance should be agreed to the balance shown in the church's annual financial reports. The minutes of the governing body should be scanned for any indication of new bank accounts opened during the year, and any such accounts should be traced both to the list of accounts and the annual financial reports.

All chequing accounts should be reconciled monthly by the treasurer, and the Committee will want to examine at least the reconciliation coinciding with the fiscal year-end. Items listed on the reconciliation and used to bring the bank balance to agreement with the chequebook balance are called reconciling items. Routine reconciling items such as deposits made at month-end but not yet credited by the bank (deposits in transit), or cheques written and recorded but not yet charged by the bank (outstanding cheques) should be verified as legitimate by tracing them to the next subsequent bank statement. Deposits in transit should appear without delay. A deposit supposedly made on the last day of the final month of the fiscal year and listed as a deposit in transit on the reconciliation should normally appear on the bank statement on the first business day of the next month. Any significant delay in the deposit appearing on the bank statement should be investigated. The Committee must note the possibility here that cash received on the last day or days of the month may be held in the church safe or other secure location for a short period before being deposited. This cash might be listed as a "deposit in transit" even though it might not have been deposited prior to the end of the month. While this practice is not ideal, it may provide a reasonable explanation for a short delay in the deposit reaching the bank.

Similarly, cheques listed as outstanding cheques on the reconciliation should normally clear the bank and be listed on the bank statement during the subsequent month. Any

outstanding cheques which do not clear the bank during the subsequent month should be investigated.

Any reconciling items which appear to be non-routine or unusual should also be investigated, with the Committee seeking both an explanation and documentation to verify the legitimacy of the items. It is most important that the Committee satisfy itself that the bank's records are in agreement with the records of the church. Reconciling items which appear month after month on the reconciliation are always suspect and should be investigated and resolved. By their nature, reconciling items are temporary differences between the banks and the church's records and normal processing should resolve them in short order. Thus any reconciling item which appears continually is likely an indication of an uncorrected error which must be investigated by the Committee and resolved.

One final area which may require attention is that of petty cash. If the church has a petty cash fund, the Committee should determine the basis on which it is operated. Ideally, it should be an "imprest" fund meaning that the governing body initially sets an amount as the size of the fund. That amount of cash is withdrawn from the bank to start the fund, and any expenditures are documented with petty cash vouchers (and other supporting documentation such as cash register receipts or invoices) which are placed in the fund box or drawer. The governing body should also set an absolute limit on the size of individual expenditures to be made from the fund, with any larger expenditures requiring normal cash payment processing. No additional cash is added to the fund until it is nearly exhausted. At that point, all vouchers are summarized and recorded in appropriate expense or other categories, and a corresponding amount of cash is withdrawn, upon approval of the appropriate authority, and placed in the fund. Barring a shortage or overage, this returns the fund to its initial size. Should a shortage or overage occur, they should be treated as miscellaneous expense (shortage) or miscellaneous income (overage). When this system is used, control is established over the fund and expenditures made through it. At any time, the fund should contain a combination of cash and vouchers equal to the preset size of the fund. This allows assurance that all petty cash expenditures are documented and recorded, and allows for easy verification counts of the fund at any time. If the church has a petty cash fund which is not kept on this basis, the Committee should recommend to the governing body that this method be adopted.

What follows is an "audit program" or list of specific procedures to be performed by the Audit Committee during its consideration of cash receipts and cash balances. It is not intended to be all inclusive, nor will all steps be relevant in every church. It will, however, give the Audit Committee a base from which to work in designing its own series of tests. The Committee must exercise its own judgment in tailoring this program to the situation in its own church.

Suggested Audit Program

Cash Receipts & Balances

1. Obtain a list of dates of Sunday and other services during the year at which collections were taken.
2. From this list choose a representative sample of dates. For each date chosen, obtain the documentation prepared by the tellers.
3. Verify by addition the total amount recorded on the count sheet for each date. Note the amounts designated as pledge income and loose offering income.
4. Trace these amounts into the accounting records as cash receipts and note any discrepancy.
5. Optional: For one or more dates chosen, trace a sample of individual pledge gifts into the donor's pledge card or other pledge record to establish the accuracy of the pledge cards. Note: In some churches the pledge records are considered too confidential and will not be available for this type of test.
6. For each date, trace the total amount collected to a bank deposit slip and to the next subsequent bank statement. Note any discrepancy.
7. Obtain a summary of collection amounts by week, and verify by addition the yearly total of all weekly collections. Compare this total to the total pledge and loose offering income in the annual financial reports. Investigate any *significant* discrepancies.
8. Optional: Obtain the pledge cards or other pledge records and verify by addition the total amounts listed as contributed. Compare this to the amounts on the weekly summaries and to the amounts in the annual financial reports as total pledge income. Note: In some churches the pledge records are considered too confidential and will not be available for this type of test.
9. Obtain a summary of restricted or designated contributions by week, and verify by addition the yearly total of all weekly contributions. Compare this total to the total recorded in the annual financial reports or alternately trace a sample of weekly amounts to the accounting records.
10. Obtain or prepare a list of all bank accounts owned by the church and compare to last year's list, noting any changes. Trace any openings or closures to the minutes of the church governing body.
11. Obtain the passbook or year-end statement for all savings accounts and determine the fiscal year-end balance. Compare this balance to the balance listed in the annual financial report and investigate any differences. Optionally, request a confirmation of closing bank account balances for each account and compare these balances to those recorded in the financial report.
12. For each chequing account, obtain the year-end bank reconciliation and the bank statements for the last month of the year and the first month of the new fiscal year. Trace the "bank balance" from the reconciliation to the bank statement.
13. Trace any normal reconciling items such as deposits in transit or outstanding cheques to the first bank statement of the new fiscal year, looking for any undue delays in clearing.
14. Investigate any unusual or non-recurring reconciling items, obtaining documentation of legitimacy. If such items exist, examine prior months' reconciliations to see if the items have been carried forward from month to

- month.
15. Once reconciling items are verified, compare the “book balance” from the reconciliation to the balance in the accounting records as of the fiscal year-end and to the balance reported in the annual financial reports.
 16. Count the petty cash fund and determine that the fund is intact.
 17. Choose one prior reimbursement of the fund and examine the documentation in order to establish the validity of items and amounts expended from the fund.

Cash Payments

In the area of cash payments, the Audit Committee is faced with the task of satisfying itself that the recorded expenditures are legitimate and accurate and that they were properly authorized. As mentioned in the previous section, the Committee cannot possibly examine every expenditure made during the year so it should once again plan on using a sample for purposes of its audit. Once again, the sample should be chosen so as to be representative of the entire year’s expenditure transactions; in other words, the sample should not consist of 20 or 30 consecutive payments from a single month.

Before beginning its examination of individual transactions, however, the Committee should obtain a list of all bank accounts from which payments are made. For each one, it should also obtain a list of those persons who are authorized to sign cheques or make withdrawals. These lists should be compared to the prior year’s list and verified with the church governing body. The Committee should also determine the approval process in use and satisfy itself that all expenditures are subjected to an adequate review and approval before payment. This process will vary among churches and in some will involve the church governing body in almost all expenditures except routine recurring ones. In other churches, the governing body will only approve major items with other items left to the approval of the treasurer or financial secretary.

In order to begin its testing, the Committee should obtain the listing of all disbursements for the year. This may take the form of a disbursements journal, a series of cash summaries, or simply a chequebook. From this listing, a sample of individual expenditure items is chosen. For each one, the Committee must establish that the item is a legitimate church obligation, that its payment was approved, that it was recorded and charged to an appropriate account, and that it has been included in the correct category in the annual financial reports.

To accomplish these goals, the Committee will want to obtain and examine the supporting documents and the canceled cheque for each of the expenditures chosen in the sample. The invoice or other documents should provide evidence that the item is a church purchase and not a personal item, as well as verifying the amount of the expenditure. The invoice should bear evidence of approval for payment, perhaps in the form of a stamp, a signature, or initials. The cheque should be made out to the appropriate vendor indicated on the invoice, should be signed by one of the approved cheque signers for the church, and the endorsement on the cheque should be consistent with the payee indicated by the invoice. This process should allow the Committee to establish the legitimacy of each of the expenditures chosen in its sample.

The Committee must also determine the appropriate account category for each of its sample expenditures and determine that the item was charged to that appropriate account. This is necessary to establish the accuracy of the reported financial information in the annual financial report. Therefore each item chosen should be traced to an entry in the accounting records as a cash payment and as a charge to the appropriate account category.

Beyond the individual payments chosen for examination, the Committee should also scan the numerical sequence of cheques recorded and investigate any missing numbers. They may be voided cheques, and if so, the voided cheques should be obtained and examined. Voided cheques should not be destroyed, but rather should be marked "Void" and retained.

Unexplained gaps in the recorded sequence of cheques or "voided" cheques which cannot be produced for examination could be evidence of unrecorded and possibly non-approved disbursements of church funds.

Suggested Audit Program - Cash Payments

1. Obtain a list of all bank accounts used to make payments and a list of persons authorized to sign cheques or make withdrawals for each account. Compare the list to that from prior years and verify the authorized cheque signers with the church governing body.
2. Obtain the cash disbursements journal or other listing of all disbursements for the year and choose a sample of disbursements for examination.
3. For each item chosen, obtain all supporting documentation and the canceled cheque.
4. Examine supporting documents for evidence that the item is a legitimate obligation of the church, and for evidence of approval for payment.
5. Examine the canceled cheque noting the authorized signature and the payee, and determine that the endorsement is consistent with the payee.
6. Determine the appropriate account to be charged for each item and trace each item to an entry in the accounting records to determine that the correct account was charged.
7. Scan the numerical sequence of cheques issued during the year. Investigate any missing numbers.
8. Examine all checks listed as "Void" in the chequebook or disbursements journal.
9. Scan cancelled cheques for irregularities (i.e. second endorsements).
10. Investigate and ensure financial statements reflect long-term commitments such as leases and contingencies such as lawsuits.

Payroll

The area of payroll will differ in significance from one church to the next. In some churches, the minister may be the only paid individual, whereas in other churches there will be associate and/or assistant ministers, secretaries, youth leaders and other paid staff members. Since many churches do their own payroll as opposed to using a payroll service, the Audit Committee may want to test some transactions in this area.

The Committee's objectives in this area overlap with those in the cash payments area. It must attempt to satisfy itself that all payroll payments are to actual church employees, at approved rates of pay. Additionally, it should be determined that all required deductions for payroll taxes are being made, and that any other deductions have been properly authorized by the employee. These might include withholding deductions for the BCOQ pension plan, optional group life insurance and other local savings plans. All voluntary deductions should be authorized in writing by the employee.

If payroll taxes or other items are being withheld, the Committee must satisfy itself that amounts withheld are being remitted to the proper governmental or other organization on a timely basis. Federal and Provincial payroll taxes withheld require the filing of monthly or quarterly remittances to the Receiver General. The Committee will have to determine that the forms are being filed as required.

The area of pastor's compensation is a complex and delicate area, and this discussion is not intended to be a thorough discussion of the subject. In general, most churches are required to withhold income tax on only a portion of the pastor's salary. The Audit Committee should request to see documentation from the pastor as to how much he or she is claiming for the Clergy Residence Deduction. Income Tax should be withheld and remitted on the balance of compensation. The church should have provided a T1223, to support the pastor's eligibility to claim the Clergy Residence Deduction, in addition to the T4.

Suggested Audit Program – Payroll

1. Choose one or more employees and compare actual rates of pay with authorized rates from the church governing body.
2. Examine withholdings and deductions from pay cheque of chosen individuals and examine documents authorizing any voluntary deductions.
3. Examine payroll tax returns and compare amounts reported thereon for one- or more employees to the amounts reported on the employee's T-4 form. Investigate any discrepancies.

INVESTMENTS

Many churches do not have funds to invest however even the employment of surplus cash can be deemed to be “investing”. Churches operating in Ontario are obligated to have an approved investment policy that meets the requirements of the Trustee Act. The Audit Committee’s objectives in this area will be to ensure that investments have been made according to approved policy, that investment decisions have been properly recorded and that transfers between accounts have been handled appropriately.

To accomplish this goal, the Committee will want to acquire a copy of the investment policy, a copy of all investment statements, and a copy of the minutes of investment committee meetings. Details of investments not held with a financial institution (i.e. BCOQ Certificate Loans) should also be acquired. If very few transactions have occurred during the year the Committee may want to analyze each one, otherwise a sample of transactions should be chosen. For each one, the Committee must establish that the investment meets the criteria of the policy, that the decision to buy or sell the investment instrument was appropriately documented within the minutes and that the instruction to buy or sell was authorized by those approved in the policy.

It is assumed that final balances in investment accounts will have been checked against the balance shown in the church’s annual financial records. If not, this should be done within this section. The amount of interest income earned from investments should be totaled from the investment statements provided and agreed to the church’s financial statements. If the income is disbursed to a number of different accounts, the basis upon which this disbursement is made should be rationalized and the allocations checked.

Suggested Audit Program - Investments

1. Obtain copies of the church’s approved investment policy, investment statements, and a copy of the minutes from investment committee meetings.
2. Verify that the balances on the investment statements match those recorded in the accounting records and the balance reported in the annual financial reports.
3. For one or more transactions chosen, analyze the investment to ensure that it meets the criteria of the investment policy, that the decision to buy or sell the investment was appropriately documented within the minutes and that the transaction was authorized appropriately.
4. For one or more transactions chosen, trace the correct recording of capital and interest in the accounting records.

Property, Insurance & Miscellaneous Items

In most cases, the largest and most valuable property that the church owns will be the church building, which is obviously central to the mission of the church. There may, however, be other properties such as a parsonage, a classroom building, or a youth center. Additionally, there will be numerous pieces of personal property which are important to the operation of the church including such things as office equipment (computers, copiers, furniture), audio visual equipment for educational programs and Sunday School, and portable furnishings for a church hall (tables, chairs, partitions).

The objectives of the Audit Committee regarding this type of property are to satisfy itself that all such property belonging to the church has been catalogued and listed, that all listed property is present, and that any changes in the list from last year to this year (purchases or dispositions) have been properly authorized by the church governing body. Additionally, the Committee should determine that property, especially the real property, owned by the church is adequately insured and that the coverage is up to date. In compiling the list of property, the church may, as a convenience, set a minimum amount for items to be listed. For example, it may decide to list only property with a value of at least \$100. The point of this is to avoid having to list inconsequential items like pencils and coffee mugs.

Practice differs from church to church as to whether real and personal property is presented in the annual financial reports of the church. Among those churches which do present such property, there will be even more divergence of practice regarding the recording of depreciation on the property. The Audit Committee will have to tailor its approach to the individual needs of its own church. It should, however, be governed by the overriding audit objectives of existence, ownership, and completeness. In other words, does all reported or listed property belong to the church, does it all exist within the church, and does any such listing or reporting include all such property belonging to the church?

Often the ownership of real property creates the financial responsibility of a mortgage or other debt, often with the property pledged as collateral for the loan. Whether or not the property is reported in the church's financial reports, such debt should be acknowledged because church leaders, as well as members, need to be aware of the obligations imposed by such debt. Successfully meeting monthly mortgage or loan payments requires planning which can only be accomplished if the leaders and planners are fully aware of the obligations. The Committee should seek to make certain that all such debt is fully communicated in the financial reports of the church. Further, it should determine that all payments on such debt are up to date, and if not, should communicate this fact immediately to the church governing body.

Suggested Audit Program Property, Insurance & Miscellaneous

1. Obtain a master list of all real and personal property owned by the church and compare to last year. Determine that any additions or disposals were properly authorized.
2. For any new items on the list, examine the items to determine that they are present. Spot check older items to be certain they are present.
3. Examine current insurance policies for dates and amounts to determine that adequate coverage exists.
4. Obtain year-end statements for any mortgages or loans and determine the correct year-end balance. Trace this amount to the annual financial report.
5. Determine for all mortgages and loans that payments are up to date.

Accounting Practices & Procedures

As mentioned earlier in this guide, the area of accounting practices and procedures often receives very little attention from the Audit Committee, which seems much more concerned with getting the year-end numbers right. Unfortunately, such an approach ignores the possibility that inherent weaknesses in the church's practices and procedures could produce problems and errors which might be impossible for the Audit Committee to uncover.

The practices and procedures referred to here are what a business calls an internal control system. While the church will likely not have anywhere near as extensive a system as most businesses, it should recognize the importance of the objectives of such a system: 1) to safeguard the resources of the entity; 2) to promote accuracy in the financial data produced; and 3) to promote operational efficiency. The first two of these are just as important to churches as they are to businesses and therefore a church should be aware of the basic principles of internal control. The Audit Committee can assist in this area by reviewing the practices and procedures and making constructive suggestions. This will likely have the dual benefit of better protecting the church's resources and also making the Committee's job easier in future years.

One of the easiest and most effective ways to evaluate the practices and procedures of the church is through the use of an internal control questionnaire. This method is commonly used by public accountants while conducting audits of businesses. It is attractive because it is accomplished by carrying out an interview during which the auditor works from a printed questionnaire and asks the treasurer or financial secretary a series of questions. Every question produces a yes, no or not applicable answer which is recorded on the questionnaire. The questions are constructed in such a way that each affirmative answer represents an acceptable practice while each negative answer represents a potential weakness and likely basis for a constructive suggestion.

What follows below is a suggested accounting practices and procedures questionnaire for use by the Audit Committee in evaluating the practices and procedures of its own church. It is based in large measure on a discussion of the subject by Richard Vargo in his book *Effective Church Accounting*, and Committee members are encouraged to obtain and read this volume for much more extensive discussion of church accounting issues and practices. This book and several others are referenced in the next section of this handbook.

**FIRST CHURCH OF
“ANYTOWN” AUDIT
COMMITTEE**

**ACCOUNTING PROCEDURES
CHECKLIST/QUESTIONNAIRE**

Date Completed:	Person Completing:		
	YES	NO	N/A OR COMMENT
QUESTION			
1. Does the church have an up-to-date accounting procedures manual?	_____	_____	
2. Are the duties of financial secretary and treasurer segregated? Are the incumbents unrelated by blood, marriage or employment relationship?	_____	_____	
3. Are facilities locked when not in use?	_____	_____	
4. Are the accounting records safeguarded at all times?	_____	_____	
5. Is an internal Audit Committee operational?			
6. Are the accounting records and underlying internal controls audited annually?	_____	_____	
7. Are all employees who have access to cash bonded?	_____	_____	

QUESTION	YES	NO	N/A OR COMMENT
8. Are members encouraged to use offering envelopes?			
9. Are members encouraged to use cheques in making their offerings (or other gifts)?	_____	_____	
10. Are at least two unrelated tellers appointed to count each collection, not including the financial secretary who may be present but does not have counting responsibility?	_____	_____	
11. Are collections counted in a secure area?	_____	_____	
12. Do the tellers verify that the contents of the offering envelopes are identical to the amounts written on the envelopes by members?	_____	_____	
13. Are all cheques received restrictively endorsed as soon as possible?	_____	_____	
14. Is cash deposited as soon as possible after receipt?	_____	_____	
15. Is ALL cash received deposited in the bank?			
16. Is cash safeguarded in a safe, lockbox, or protective container when at the church?	_____	_____	
	_____	_____	

QUESTION	YES	NO	N/A OR COMMENT
17. Are collection reports given to the financial secretary and treasurer for entry into the accounting records?	_____	_____	
18. Are incoming mail and in-office contributions handled by people who are not responsible for the accounting records?	_____	_____	
19. Has the bank been instructed, in writing, never to cash third party cheques made payable to the church?	_____	_____	
20. Are contributions records maintained for members?	_____	_____	
21. Are members instructed to report any discrepancies in their notices of contributions to the Audit Committee?			
22. Are the contribution records reconciled to the total contributions in the accounting records?	_____	_____	
23. Are requisition slips prepared for cash disbursements that do not have standing authorization?	_____	_____	
24. Are pre-numbered purchase orders used for all purchases that do not	_____	_____	
	_____	_____	

QUESTION	YES	NO	N/A OR COMMENT
25. Are invoices for goods and services approved by a person in authority before payment is made?	_____	_____	
26. Are invoices checked for accuracy before being paid?	_____	_____	
27. Is the approval and check for accuracy documented?	_____	_____	
28. Are all disbursements, except for minor items, made by serially numbered cheques?	_____	_____	
29. Are pre-numbered cheques used or is there some means of numbering control for manually numbered or computer produced cheques?	_____	_____	
30. Are at least two signatures required for all cheques?	_____	_____	
31. Do all cheque signers inspect all supporting documentation before signing?	_____	_____	
32. Are invoices and supporting documents marked paid when cheques are issued?	_____	_____	
33. Are all void cheques so marked and retained?	_____	_____	
	_____	_____	

QUESTION	YES	NO	N/A OR COMMENT
34. Is preparing a cheque made payable to "Cash" prohibited?	_____	_____	
35. Are blank unused cheques safeguarded at all times?	_____	_____	
36. Is a petty cash fund used for all minor disbursements of cash?	_____	_____	
37. Are vouchers prepared for all disbursements from the petty cash fund?	_____	_____	
38. Are transfers between bank accounts always properly authorized?	_____	_____	
39. Are reconciliations of all bank accounts prepared or approved monthly by an individual who is not involved in handling cash or writing cheques?	_____	_____	
40. Is the petty cash fund reconciled on a surprise basis at least once per year?	_____	_____	
41. Are the account balances in the books reconciled with the amounts presented in the financial reports?	_____	_____	
42. Are valuables (securities, important documents) afforded protection in a bank safe deposit box?	_____	_____	

QUESTION	YES	NO	N/A OR COMMENT
43. Are two signatures required for access to the safe deposit box	<hr/>	<hr/>	
44. Is an updated inventory of securities, valuables, equipment and other non-cash assets maintained?	<hr/>	<hr/>	
45. Are regular reviews made to determine if insurance coverage is adequate?	<hr/>	<hr/>	
46. Does the church have an approved investment policy?	<hr/>	<hr/>	