

# Internal Audit Review for FYE June 30, 2013

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## Charge

In August 2013, the Board approved a standing "Charge for Internal Audit Committee" (Appendix 1). The duties stipulated in this charge are:

As requested, assist the Board in carrying out its responsibilities in monitoring compliance with the Board's financial policies and the finance related provisions in the Church Bylaws.

Upon Board approval, perform the annual review/audit function set out in Article XII, Section 8 of the Church's By-laws. Arrange and direct the external audits/reviews in years with such an audit/review.

Article XII Section 8 of the bylaws state:

The Board of Trustees, through an internal audit committee, shall direct an annual review or audit of a type and nature it deems appropriate, except that every two (2) years the Church shall conduct either a review or an audit by an outside auditor.

On January 5, 2014, John Bohman, Chair Board of Trustees, appointed Board members David McTaggart, Gretchen Menn and Ken Marshall to serve as an internal audit committee (Audit), with David McTaggart as Chair. He further directed the Audit to perform an internal audit for Fiscal Year Ending June 30, 2013. External audits had previously been prepared by E. Cohen & Company, CPAs for FYE 2009, 2010, 2011 and 2012.

## Detailed Checklist

The Audit prepared an Internal Audit Checklist (Appendix 2) of concerns and questions for investigation and response by staff. Staff was able to address these concerns and present compliant evidence to the satisfaction of the Audit as noted in the appended document.

## Summary Report

### **1. Financial Statements**

The Audit is satisfied that the appended Financial statements prepared by staff and the Treasurer's report accurately reflect the financial affairs of the Church as of June 30, 2013.

Balance Sheet for Fiscal Year Beginning 7/1/2012 (Appendix 3)

Budgeted Financial Statement for Fiscal Year Beginning 7/1/2012 (Appendix 4)

UUCA Capital Campaign Sources and Uses of Funds Through June 30, 2013 (Appendix 5)

Treasurer's Annual Report 2013 (Appendix 6)

The Audit verified that BB&T lender statements of 6/20/2013 agree with reported liabilities:

Mortgage Principal Balance:	\$1,978,691.03
Line of Credit Principal Balance:	\$1,553,748.17

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The balance sheet reports booked value of Land, Buildings and Equipment at \$7,715,000. In contrast, Real estate appraisers Sapperstein & Associates (by report dated May 30, 2012) valued the Church property at \$14,200,000 upon completion of capital improvements by June 1, 2013. It is interesting to note that the same report valued the "as-is" May 11, 2012 property at \$9,800,000 implying that the improvements would appreciate the market value by \$4,400,000.

The Audit verified bank statement reconciliations for two separate randomly-picked months for both the operating and construction accounts. No irregularities were found and the reconciliation process appears to be adequate.

The Audit pulled and reviewed random checks from the Operating Account and the Construction Account. The voucher protocol was followed in all cases. The authorization process appears to be adequate and uniformly followed. In addition, seven (7) CN Register Entries for contributions and eleven (11) Journal Entries (JE) concerning fund transfers (from account to account) were randomly picked and reviewed and found to be accurately entered.

## **2. Bookkeeping Procedures**

Staff updated its bookkeeping procedures this spring in a document titled "UUCA Procedures for Cash Disbursements and Receipts" (Appendix 7). This document supersedes similar procedures prepared by the previous administration.

The Audit is satisfied that these procedures comply with the following Executive Limitations:

4.5.8 The Executive shall not...Receive, process, or disperse funds without documented controls sufficient to meet the Board appointed auditor's standards, other governmental standards, or regular business standards and practices;

4.7.2 The Executive shall not...Operate without adequate accounting controls and procedures that are maintained and documented;

## **3. Accounting Basis**

The Church uses a modified cash basis of accounting which, as described by E. Cohen & Associates in its FY2012 audit report, "is a comprehensive basis of accounting other than generally accepted accounting practices (GAAP). Revenue is recognized when received and expenses are recognized when paid." Assets are capitalized on the balance sheet rather than depreciated.

There has been recurring discussion as to whether the Church ought to continue with its modified cash basis or to depreciate assets. The Treasurer offered this opinion on the relative merits (paraphrased) in a March 14, 2014 email:

GAAP is the more correct way of accounting. It would improve the accuracy of the balance sheet and the estimated value of assets. However, said accuracy provides very little value to the operation of the Church. If the bookkeeping burden is trivial, then we should do it; if the bookkeeping burden is significant, we should not.

**\*\*\*What is the burden in terms of bookkeeping days per year and software licensing? Brian**

**\*\*\*The Audit recommends that the Board consider...**

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## **4. Designated Funds**

The Church maintains an accounting of all funds designated for the operation of specific ministries including: Chalice Theatre, Peace Camp, VOICE, Choir, Day Alliance, Fellowship X, Young Adults, OWL, OWL cook, Memorial Garden, PAG, Clerestory Press, Choir Concert, Piano fund, Fall Retreat, Poker Club, ...etc. There are over three dozen such accounts.

Recognized lay leaders of all ministries budget and manage their cash flow under the supervision of Executive staff. Core ministries such as Choir, Peace Camp and VOICE (a congregational ministry commitment) have line-item support from the operating budget. Some receive GTP support. Some, including VOICE and Chalice Theater, have on occasion contributed surplus funds to the Church. Most are revenue neutral in that they are self supporting, raising and spending monies for their chartered purpose. Funds residing in designated accounts are reported on the monthly balance sheet; all inflows and outflows are recorded as operating revenue/expense in the Church books.

The Audit is satisfied that this manner of operation is appropriate for the Church.

## **5. Investment Management**

The Audit is confident that the investments of reserve funds are being prudently managed by lay professionals under the supervision of the Executive. However, the organizational structures and operating procedures remain ill-defined.

Specifically, the Audit is not satisfied that the investment management functions comply with the following Executive Limitation:

4.5.8 The Executive shall not...Operate without written policies guiding the prudent investment of Church reserves and restricted funds;

Although this Executive Limitation was written subsequent to FY 2013, the Treasurer's Report and legacy financial committee charters appended to the minutes of Board Meeting July 17, 2012 describe a confused situation that persists to this day. Refer to "Treasurer's Report to the Board of Trustees" dated July 17, 2012 (Appendix 8)

## **6. Personnel Matters**

The Audit checked employment agreements, tax information and direct deposit records for high-salary employees and found that employment agreements for some employees appear to be missing.

Personnel files are locked up and maintained securely and confidentially.

The employee handbook appears adequate in scope and available to employees.

## **7. Insurance**

The Church has an insurance policy with GuideOne Mutual Insurance Company. The current policy was effective April 1, 2014 and expires on April 1, 2015. It reflects kinds and classification of coverage and amounts for each coverage.

The policy protects the church from theft, although there is a deductible. The Policy Holder Notice does

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not mention embezzlement, although it does discuss the concept of employee dishonesty coverage.

The over all coverage and limits includes Employer Liability (\$500,000 each accident or employee illness) as well as policy limitation. The Policy's Commercial General Liability has a \$3,000,000 aggregate limit with a \$1,000,000 limit for each occurrence. It also has a \$1,000,000 limit for damage to premises rented to UUCA and the same limit for directors and officer's liability. Sexual misconduct insurance is included under the General Liability.

The Audit determined that this amount of insurance coverage matches or exceeds that recommended by the Northeast Synod of the Presbyterian Church, the Lutheran Church - Missouri Synod, and the Anglican Church of North America as well as AIG, a private insurance company. Furthermore, staff reports that the current insurance sales agent does not recommend additional insurance.

The Audit is satisfied that these procedures comply with the following Executive Limitations :

4.5.8 The Executive shall not...Fail to insure reasonably against theft and casualty losses, corporate liability, and personal liability of Board members, Officers, and staff;

## **8. Computer File Backup**

Computer records are backed up daily to a local server located in a waterproof and fireproof "data vault" on the lower level. At the Audit's request, staff demonstrated that data could be readily retrieved.

Staff is planning to update the operating systems on all computers in the near future. At that time, the cost of off-site secure "cloud" backup will be assessed. The Audit will follow up on the findings of this investigation.

## **9. Audit Policy**

Ambivalence persists in governance policy as to whether the Church ought to perform a) a financial review or audit, b) in house or by an outside accounting firm, and c) annually or biannually.

Church Bylaws (Article XII, Clause 8) stipulate an external review or audit every two years.

Executive Limitations 4.6.8: The Executive shall not...Fail to budget for an annual audit by an outside accounting firm;

The director of non-profit services at E. Cohen & Company, CPAs (previous church auditors) advises "There is no reason to do a financial statement review in the off audit year unless the board wants financial statements in which case they may want to consider a compilations which is the lowest level of financial statement services and the least cost to the organization."

The Audit questioned the audit policies of four other metro UU churches. All Souls in D.C. And Fairfax Unitarian Universalist have the most rigorous policy. All Souls conducts alternating internal and external yearly audits while Fairfax conducts an annual financial review by an outside accounting firm. Two others, Cedar Lane UU and River Road UU, both in Maryland, rely on internal reviews although River Road conducts an external financial review every five years.

The Audit recommends the Church adopt a policy of conducting an internal review and external audit in alternating years. The Bylaws may stand as written. Executive Limitations ought be revised accordingly.

The Audit will solicit proposals for a full professional audit for FYE June 30, 2014 to start in August.

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## Appendices

1. Charge for Internal Audit Committee
2. Internal Audit Checklist
3. Balance Sheet for Fiscal Year Beginning 7/1/2012
4. Budgeted Financial Statement for Fiscal Year Beginning 7/1/2012
5. UUCA Capital Campaign Sources and Uses of Funds Through June 30, 2013
6. Treasurer's Annual Report 2013
7. UUCA Procedures for Cash Disbursements and Receipts
8. Treasurer's Report to the Board of Trustees dated July 17, 2012