

It Pays to Manage Payment Risk
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Alas! how deeply painful is all payment!
- Lord (George Gordon) Byron

Paying the bills is just something that we all have to do. As Lord Byron suggests above, it can be a deeply painful experience, but it can be particularly so if you pay more than necessary due to negligence, error or even fraud. And, the risk of doing so is much greater than you might think.

Setting aside the possibility of fraud for a moment (but, just for a moment!), one might wonder: just how difficult is it to correctly pay an invoice? Of course, it's really rather simple ... unless the goods were returned, or not even delivered ... or, the pricing was incorrect ... or, an agreed discount was not applied ... or, the quantity was incorrect ... or, the invoice is a duplicate ... or, the payment is the responsibility of another party ... or, well, you get the idea. It's not really that simple at all.

And, let's *not* set aside the possibility of fraud ... by a staff member, by a volunteer, by a supplier, by any unscrupulous party *pretending* to be a supplier. This we don't like to think about, but it is surely our responsibility to recognize the reality of fraud and to take reasonable steps to avoid it. But, the good news is, there are many simple, inexpensive steps you can take to significantly reduce the risk of fraud and error in your payments system.

Let's also be mindful that this is not just a large organization issue (and, happily, these are not just large organization solutions!) -- every organization, no matter how small, is at risk for incorrect payments, and every organization should be taking at least some of these steps to address that risk. For very small organizations, the use of volunteers in some of these steps is a simple way of adapting the process to your circumstances -- for very large organizations, it may not be the executive director that needs to be involved, but another member of the management team, or of divisional management.

So, here are eight practical, realistic steps you can take in your organization to ensure that all payments are accurate and justified.

Buying on trust is the way to pay double.
- Source Unknown

1. All invoices should be approved (and initialed and dated to show this) by the individual most proximate to the expenditure. So, for office supplies, that might be the office manager or admin assistant (not the executive director); for the audit fees, the director of finance or Treasurer; etc. This ensures that the person who knows the most about the expenditure agrees with what was invoiced. This person, as part of that approval process, should: verify pricing, confirm satisfactory receipt of the goods or services, and confirm the identity of the supplier.

2. All expenditures should be recorded in the accounting system, allocated in detail to the most relevant accounts, and compared to budgets for these accounts. Comparing detailed financial reports by program, department or activity to budgeted and prior year amounts is a quick way to highlight unusual changes in amounts (both higher and lower). Of course, this is only useful if these reports are being reviewed, on a timely basis, by knowledgeable people in the organization, and if questions and anomalies are promptly followed up on!

3. All (except possibly very small) cheques should be signed by two authorized signing officers.

In doing so, both cheque signers should ensure that the invoice(s) being paid are attached to the cheque for review. The first signer should verify that the invoice has been properly approved (see above), that the amount and payee are in agreement, and that any relevant discounts or adjustments have been taken into account. The second cheque signer should ensure that the first signer is doing her job!

4. Once cheques have been signed, they should NOT be given back to the cheque preparer for mailing out. Once signed, a cheque could be modified by changing the payee or the amount (the banks really don't look very closely at the billions of cheques they process!). The cheque preparer would be in the best position to cover their tracks, while someone independent of the preparation process wouldn't be able to do so.

Honesty pays, but it doesn't seem to pay enough to suit some people.

- Kin Hubbard

5. Use a "positive pay" system with your bank. Using this system provides the bank with a separate listing of cheques that they are authorized to process -- if a cheque isn't on the list, it won't get cleared, and you'll be alerted to a fraud or error situation very promptly.

6. Accounting department employees should be required to take their vacations regularly. It's not just that all work and no play makes for burned out, dissatisfied, and error-prone employees (though it does!). If an employee were involved in a fraudulent activity, or were simply trying to cover up a significant mistake, doing so might require their continued attendance to cover up a problem -- taking a vacation of at least a full week in duration may help any such continuing situation come to light.

7. Bank statements and paid cheques should be returned directly to the executive director for review. Bank statements, in the unopened envelope directly from the bank, give someone independent of accounting an opportunity to see first hand what transactions have gone through the bank. A quick review of the returned cheques and overall cash activities and balances in the back should reveal any major problems. A supplier that is not recognized? A payment that you thought was processed months ago? An overdraft when you thought there was cash on hand? Again, the key is to follow up promptly!

8. Review supplier statements. If you have major, recurring suppliers, you (the executive director) should periodically review a statement (not an invoice) from the supplier. This will show you what invoices and amounts the supplier thinks is outstanding. If a payment from many months ago has gone astray, some suppliers will simply apply subsequent payments to the oldest outstanding items, and will therefore never escalate (or potentially be aware of) an unpaid invoice. You should ensure that suppliers are showing their accounts as being fully paid and follow up if they show any balance that you think has already been paid.

Mistakes are part of the dues one pays for a full life.

- Sophia Loren

Each of these steps is likely simple, straightforward and inexpensive to implement. As noted above, if staff resources are stretched thin (and who isn't?), or if you simply don't have enough staff to properly segregate some of these key duties from one another, there may be a very simple and well-defined role for a volunteer to play, so long as they can do so on a reasonably timely basis.

What is important is that enough of these steps are introduced into the regular, ongoing and recurring processes and procedures of the organization. Worrying about incorrect or fraudulent payments is only one tiny thing on a very long to-do list for most nonprofit organizations, and that's why building routines (kind of like good habits) is so important.

Which steps will be right for your organization? Every organization is unique, and so there is no universally right answer. One source of advice may be your auditor -- you can ask their advice as to steps that they believe would strengthen the internal control environment in your organization. But, however you do so, finding out how to make your payments process more robust and resistant to fraud and error is a task that will pay you handsomely, both in money and in peace of mind!

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