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PREVIEW EDITION

FINANCIAL INTEGRITY for NONPROFITS

A Compliance Guide for Boards & Management

Produced by The Aleph Institute's Project 432

Praise for the Guide

“This pamphlet is concise, informative, and easy for a layperson to understand. It is a valuable resource with practical advice and actionable takeaways that can be easily implemented. I recommend that all members of the Board of Directors read it.”

Benjamin Berger, CPA
Partner at Bernath + Rosenberg, PC

“Excellent study and compliance guide. A must read for nonprofit Torah observant board members, officers and management.”

Jacob I. Friedman, Esq.
Partner at Proskauer Rose LLP

“Yaakov “Jake” Goldstein’s Compliance Guide is an outstanding work that will be very helpful in assisting non-profits in complying with the law and avoiding the potentially devastating legal consequences of financial misconduct. It is a highly practical guide by a knowledgeable, experienced practitioner that deals with the nuts and bolts of proper financial management. Every non-profit board and management team should closely read this work and apply the principles and techniques described in the Guide.”

Rabbi Dr. Yakov Yellin, Esq.
Former Chief Compliance Officer at Disney

Financial Integrity for Nonprofits is a publication of Aleph Institute's Project 432.

Project 432 is Aleph Institute's awareness and education initiative to promote ethical behavior, integrity, and fidelity to the law within our communities.

The Aleph Institute is a Jewish humanitarian organization that provides religious, emotional, and financial support, and advocates for the needs of justice impacted individuals.

Learn more at p432.org

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Preface

Several weeks ago I spoke in Boro Park before a large crowd of frum Jews. The topic was billed as Dina Demalchusa Dina – The Law of The Land is The Law. Ostensibly this means that the Laws of the United States must be followed. Sounds simple enough but it truly is not.

As an experienced criminal defense lawyer who also happens to be an Orthodox Jew, I am often astonished by how many in our community either don't understand this concept or do understand it but choose to ignore it until the draconian consequences of doing so manifests itself often with very dire results.

I stressed that one's own emails and texts can often end the case as these carelessly drafted missives can demonstrate "intent" or even a reckless disregard for truthfulness or accuracy. Even "one" cavalierly inserted or omitted word can change an innocuous comment into an incriminating one. I stressed that before one hits the “send” button read the email carefully. It can sometimes end a career if poorly drafted. Hard to argue lack of “intent” when the black and white printed word strongly suggests otherwise.

I hope my message resonated well. Only time will tell whether my words had the intended impact or were heard but later ignored.

This written guide is done well. It should be read carefully and then followed scrupulously.

Ben Brafman, Esq.
Brafman & Associates

A Note from the Author

This Guide emphasizes the crucial role of financial oversight and controls in schools, shuls, and nonprofits. There are 3 main reasons why board members may neglect financial oversight:

1. They are unaware of their fiduciary duty.
2. They find these tasks complex and uninteresting, preferring to focus on the organization's mission.
3. They fear it suggests distrust of employees they know and trust.

In Parshas Mattos, it states 'v'hiyisem nekiyim m'Hashem um'Yisroel.' Chazal infer that in addition to the "eyes of Hashem"; one must also remove any suspicion in the eyes of people. Thus, the officers handling donated funds for the Beis Hamikdash entered the treasury barefoot and wore clothing without hems, wide sleeves, pockets, or cuffs, making it impossible to hide any coins and avoid suspicion of theft.

Financial controls do not imply dishonesty among staff; most employees act with integrity. Yet even ethical individuals might succumb to theft when they face a financial crisis, rationalizing it as temporary borrowing. Consistent controls prevent such situations honesty.

Board members also risk personal financial and legal liability if they neglect oversight duties. Even with D&O liability insurance, policies often exclude criminal offenses like fraud. Ignoring fiduciary duties can lead to gross negligence charges. Implementing strong financial controls <u>and being able to demonstrate it</u>, is vital to protect board members, management, and staff.

Yaakov 'Jake' Goldstein, CPA

Introduction

Nonprofit boards often comprise members with diverse skills but limited financial management expertise. This booklet is written in layman's terms to ensure clarity and ease of understanding. It includes policies and procedures that offer high value in preventing financial misconduct.

Section 1 "Common Methods of White-Collar Crimes," lists actual cases of fraud and embezzlement in nonprofits to highlight the risks and vulnerabilities.

Section 2 "Monthly Financial Oversight Checklist," provides a 3-hour process for an effective internal audit by a board committee.

Section 3 "Compliance and Risk Management," covers basic board governance practices, regulations, and insurance considerations.

Section 4, "Financial Controls and Oversight – Best Practices," outlines staff procedures and control policies. Board members are responsible for compliance and strong financial control.

While a nonprofit with weak controls might never experience fraud, the benefit of minimizing risks outweighs the cost.

- For the organization, financial misconduct can lead to loss of trust, fundraising difficulties, and damaged reputations.
- For perpetrators, it means severe financial loss, community ostracization, and emotional suffering, affecting their families even more deeply.

Our Sages teach us "Arba Chashuvim K'meisim" that certain situations render a person like a dead person. We'd add that a Yid in jail is also in this category, impacting their family as if they were widows and orphans, but with added public humiliation. Therefore, providing proper financial controls and oversight is the greatest gift nonprofit leaders can give their employees to prevent these tragedies.

1: COMMON METHODS OF WHITE-COLLAR CRIMES

Fundraising Fears

An Aleph client story, names and details changed for privacy

Ehud Ben-Shoshan was a charismatic youth rabbi on an American campus. Despite his success, Ehud struggled with fundraising. Noam, a senior coleague introduced him to a questionable matching funds scheme. Under financial pressure, Ehud rationalized his participation, which promised increased donations through unethical means.

“Every dollar we received went directly toward our programming, not to my pocket. If a bit of finagling was the way to receive larger amounts, I told myself that this wasn't hurting anyone." However, the moral and psychological toll eventually led Ehud to abandon the scheme.

Ehud's life took a dramatic turn when the FBI implicated him in Noam's fraudulent activities, resulting in severe charges and a guilty plea. The scandal shattered his career, and the legal consequences strained his family relationships.

He now sees his mistakes as a test from Hashem, emphasizing the importance of integrity and hard work. "Do everything by the book. Don't cut corners. That is where the bracha is."

The following is a list of common methods of fraud and embezzlement grouped by the financial process of a typical back office. The quotes below each method are copied from news articles of actual cases.

1. Receipts/Donations:

a. Depositing check donations into a fake bank account and issuing fake tax receipts to the donor.

> "She fraudulently used the congregation's checks to pay personal expenses, endorsed and converted checks that were meant for the congregation and drew the congregation's checks and diverted funds to her own personal accounts."

b. Colluding with vendors on fraudulent schemes

> "Donors regularly made large charitable contributions to be written off their taxes. In one case, 90 percent of the money was secretly funneled back to the donor, keeping 10 percent for himself. One donor got his donation returned in the form of $1 million in gold, prosecutors said."

2. Purchasing:

a. Colluding with vendors to overcharge and get kickbacks or "finders fees".

> "The insurance company would inflate the insurance rates by hundreds of thousands of dollars, which he and his co-conspirators would then keep for themselves."

b. Submitting fake invoices for phony services or goods.

> "The employee had access to critical financial systems, and she created fake invoices in the names of legitimate groups. She approved the invoices for payment, and when the checks were ready, she cashed them herself."

3. Disbursements/Spending:

a. Writing checks from the organization to oneself or paying directly for personal items.

> "She forged signatures of nonprofit executives on checks, which she made payable to herself."

b. Using the organization's credit card or debit card for personal expenses.

> "He would use the organization's credit cards to make personal purchases, falsely characterizing their purchases as legitimate expenses. At the end of the

year, he would allocate his personal expenses to the departments that had not exceeded their budgets."

4. Payroll:

a. Paying unapproved salaries.

"The director raised her salary without receiving board approval."

b. Payroll fraud.

"The school paid its employees in a manner that grossly underrepresented their employees' "on the books" income."

5. Online Banking and Electronic Payment Portals:

a. Online banking transfers from the organization's bank account to a personal bank account.

"$500,000 had been wired from the shul's bank account to the director's personal account."

b. Electronic payments from the organization's payment processing portal to a personal account.

"He allegedly used the school's PayPal and Stripe accounts to transfer school funds into his own personal PayPal account."

2: MONTHLY FINANCIAL CHECKLIST FOR AUDIT COMMITTEES

Lessons Learned

An Aleph client story, names and details changed for privacy

Yosef Sholom was inspired to open a new Cheder where children were respected as individuals. His commitment to helping others, however, led him into a legal entanglement when he failed to verify the legitimacy of a contractor's government billing, resulting in serious charges and potential imprisonment.

"One always needs to do one's due diligence whenever one is involved with any sort of business deal. If you don't ensure that what you are getting involved with is kosher, don't expect anybody else to do it for you."

Facing the prospect of significant time away from his large family and enduring the long-term consequences of a felony conviction, Yosef Sholom's story serves as a cautionary tale about the high costs of negligence and misplaced trust. His experience underscores the need for thorough scrutiny in all dealings, no matter how well-intentioned or seemingly trustworthy the circumstances appear.

Ideally, an audit committee should be established to perform these tasks that take only a few hours each month to complete. Even a few basic oversight procedures can serve as an effective deterrent for dishonest behavior by removing opportunity for one tempted to go down that road. Most of the steps are simple and straightforward. With a little training, even board members with no financial background could provide effective financial oversight.

General		
1	Upon completion of the following monthly financial oversight steps, confirmation of completion should be documented in an email to the Board.	☐

Banking		
2	Review monthly bank statements (original) and canceled checks for reasonableness. Seek explanations for: • Unexplained debits and credits. • Checks with no check numbers or numbers clearly out of sequence. • Duplicate check numbers. • Transfers to unknown accounts. • Any other unusual or unexplained transactions.	☐
3	Review monthly bank reconciliations for reasonableness: • Ensure balances tie out to the ending book and bank statement balances. • Seek explanations and resolutions for unusual activity.	☐

- The bank reconciliation detail should include a list of cleared checks by vendor.
- On a select basis, verify that the vendor listed on the cleared check list matches the name on the cleared check image.

Cash Receipts - Donations and Tuitions		
4	Review a monthly report of all non-cash transactions (or audit trail report), including: • Write-offs. • Accounts marked deceased/inactive. • Deleted transactions. • Discounts. • Credits applied for goods and services. Look for unusual items, transactions without explanations, or non-authorized entries.	☐

Purchasing Goods and Services		
5	Review monthly credit card statements for appropriateness, reasonableness and proper authorization. Seek explanations for any unusual activity.	☐

Cash Disbursements (Payments and Spending)		
6	Review the monthly payment detail report sorted by vendor for appropriateness and reasonableness. Seek explanations for: • Any unusual activity. • Large payments. • Unfamiliar vendors. On a select basis, request original paid invoices. Occasionally pick out a large payment and contact the relevant staff person to make sure the expense was authorized.	☐
Payroll		
7	Review the payroll summary for each pay period. Perform an analytical comparative review for reasonableness and consistency.	☐
Online Banking and Electronic Payment Portals		
8	Download monthly "All Transaction" reports and review for unusual or irregular outgoing 3rd party electronic payments, refunds, etc.	☐
9	Review and ensure every transfer of funds is going into one of the organization's bank accounts. Randomly cross reference to the credit on the organization's bank statement.	☐
10	Periodically go online and check the linked external bank accounts (fund transfers) and credit card accounts and ensure they are the organization's accounts.	☐

3. COMPLIANCE & RISK MANAGEMENT FOR BOARDS

Just This Once

An Aleph client story, names and details changed for privacy

Ari Silverstein's dedication to Mazon LaMishpacha, a vital soup kitchen for Holocaust survivors, was marred by a fateful decision to accept undisclosed commissions. Initially seen as a gesture of gratitude, these cash payments escalated, and entangled Ari in a multimillion-dollar fraud scheme that involved inflated vendor bills.

"Instead of saying, ‘no, you don't owe me commissions,’ or ‘wait, I got to go to my board and let them decide if it's appropriate for me to get commissions and how to pay taxes,’ I accepted his offer of paying me these commissions in cash."

He ultimately accepted a plea deal, leading to a period of incarceration where his faith became a cornerstone of survival. "The private aveira can be spun into so much more that you're best avoiding the aveira altogether."

This is a short list of basic board governance practices, government regulations and insurance considerations.

Governance

1 Board members should be trained in financial management. ☐

The Board should establish an Audit Committee and at least one member of that committee should have professional background in finances. ☐

2 The Audit Committee should assist in budget preparation, and review the monthly reports for reasonableness, consistency and accuracy. ☐

The Audit Committee should meet at least quarterly to review the expanded financial reports with senior management. ☐

3 The Board must formally adopt the annual budget and the annual audited financial statement before the finalization and acceptance of these reports. ☐

4 Donations should not be used for anything outside the mission of the organization, even if the nature of the donation is charitable. ☐

5 Ensure parsonage is properly administered and that the recipient is aware of the housing allowance regulations. ☐

6 Staff should have a safe way to report improper conduct directly to a board member. ☐

State Regulations

1 Ensure the organization's Articles of Incorporation and Bylaws accurately describe ☐

what is actually happening procedurally. This includes:

- The number of board members.
- Properly documented board minutes.
- Resolutions.
- Other formal actions.
- Terms of office, etc.

2 Ensure the documented conflict of interest policy is signed by each board member annually. ☐

3 Ensure the organization has a current copy of the organization's IRS Determination Letter (501(c)(3) Letter), Sales Tax Exemption Certificate, etc. ☐

Federal Regulations

1 The annual audit of the organization's financial statements and Form 990 should be reviewed and adopted by the board before finalizing with a client rep letter or signing the return. ☐

2 Adopt a written document retention and destruction policy. ☐

For consideration: Periodically review compliance to these policies.

Insurance and Risk Management

1 Review the organization's risk management and insurance policies with respect to: ☐

- Risk exposure.
- Coverage.
- Cost efficiency.

- Liabilities and obligations, including areas like Workman's Comp, Property, General Liability, Employment Practice, Abuse/Misconduct, Fiduciary Liability, D&O, Cybersecurity, etc.

2 There should be daily backups of all data. ☐

3 Local computers and software programs should be individually password protected. ☐

4 Conduct a periodic compliance audit of emails to ensure there are no communications that expose the organization to financial, legal or reputational risk. ☐

Human Resources

1 Perform background checks and fingerprinting on all new hires which can reveal undisclosed criminal records and prior instances of fraud. ☐

Carefully check employee references and job history as permitted by applicable law.

2 Retain all employee documentation in a personnel file, including: ☐

- Employment contract or written terms of employment.
- I-9 (employment eligibility verification).
- W-4 (payroll withholdings), etc.

3 Staff involved in financial transactions should take at least one week of uninterrupted vacation in order to permit transactions to clear properly in their absence. ☐

4 Ensure all new hires are provided with: ☐

- An employee handbook.
- Disciplinary procedures.
- Evaluation and appraisal procedures.
- Sexual Harassment/Anti-Discrimination Policy.
- Whistle-blower policy, etc.

Staff should confirm in writing their understanding of these policies every year.

4. FINANCIAL CONTROLS & OVERSIGHT BEST PRACTICES

Pressure Cooker

An Aleph client story, names and details changed for privacy

Effy Pinkowitz had the daunting task of managing a rapidly expanding school's finances. Tasked with overseeing a massive operational overhaul, Effy faced mounting financial strain from day one. Pressure from his board and driven by a desire to keep the school afloat, led him down a slippery slope of ethical compromise when applying for government programs.

"I don’t remember if I willfully convinced myself that we could qualify, or if I decided to submit the claims anyway. But in hindsight, it was fraudulent, and I knew that."

The FBI uncovered the school's fraudulent claims, and the ensuing legal battle tarnished his reputation and cast him as a pariah in the community. Despite pleading guilty in court and emphasizing his altruistic intentions, Effy faced harsh sentencing and personal humiliation. After he served his sentence, he reflected on the costly lessons learned, concluding, "If you don't feel that something is legal, don’t do it. It’s really that simple. I just had to learn that the hard way."

This section outlines staff procedures and control policies. Board members are responsible for compliance and strong financial control.

A. FINANCIAL REPORTING AND BUDGETS

1 Develop an annual budget process that projects incoming revenue and outgoing costs for the year. ☐

Budgets must be approved by the board and reflected in the board minutes. ☐

2 Prepare bank reconciliations every month immediately after month-end for every bank account, even for small accounts (i.e. Petty Cash, etc.). ☐

3 The one who prepares bank reconciliations should not issue or sign checks (access to assets) or process cash receipts and deposits (accounting duties). ☐

4 Upon completion of the monthly close, prepare monthly financial reports (P&L, Cash Flow and Balance Sheet) and present them to the Board. ☐

Seek explanations for unusual trends, variances and balances. ☐

5 Quarterly financial reports should analyze actual results to the budget and prior period. ☐

Full explanations for large variances and unusual items should be presented to the Board. See Compliance section. ☐

6 Arrange for annual audits (or reviews) performed by outside independent auditors. ☐

- Ensure the books are prepared on the full accrual basis (GAAP). *See Appendix A for further explanation.*
- Take proper action on qualified opinions or issues specified in the management report. See Compliance section.

7 Once the audited financial statements have been adopted by the Board, ensure no further transactions are recorded in that fiscal year. ☐

Password protect the fiscal year in the accounting system. ☐

B. CASH RECEIPTS - DONATIONS AND TUITIONS

1 Restrictively endorse all checks at the time of receipt. ☐

2 Keep paper or digital copies of a checks in a secure location for verification purposes if ever needed. ☐

3 To verify the integrity of staff, consider sending in a donation anonymously to ensure complete and proper processing. ☐

4 Actual cash received should be recorded in a dual-copy pre-numbered cash receipt book. ☐

A different staff person should record the cash received into the system and be sure to count it again. ☐

5 Entries in the cash receipts books should be cross-referenced to the donors account periodically and unannounced. ☐

6 The following should be approved in writing with noted reasons: 1) write-offs, 2) deleted transactions, and 3) credits to donor accounts. ☐

7 Lock cash and checks in a safe, secure location (i.e. a safe, etc.) overnight. ☐

Install security cameras in the area where cash and checks are processed and where they are kept overnight. ☐

8 Provide donors with an annual statement of contributions after the calendar year-end to substantiate their charitable contributions for the year. ☐

C. PURCHASING GOODS AND SERVICES

Ordering Goods and Services

1 Centralize the purchasing function. Only one or two people should be authorized to make purchases on behalf of the organization. ☐

2 For purchases of goods and services, a Purchase Requisition Form (PRF) should be prepared by the requesting party. It should include: ☐

- Detailed description.
- Quantity.
- Approximate cost.

The PRF must be approved in writing by the authorized staff person before the purchase is made. ☐

3 These 3 tasks are conducted by separate staff: ☐

- Purchasing (access to assets).
- PRF written approval (management duties).
- Cash disbursement (accounting duties) .

4 All reimbursed expenses should be pre-approved and only reimbursed upon submission of original receipts. ☐

5 All contracts above a predetermined amount are subject to at least three bids and approval by a Board member uninvolved in the transaction. ☐

Credit Card Purchases

1 Ensure the organization's credit or debit card is always kept in a secure location. ☐

2 Only the authorized purchaser may use the credit or debit card (access to assets) and only after the PRF is properly authorized and approved. ☐

The person approving purchases (management duties) may not use the credit (or debit) card. ☐

The authorized purchaser may not record the credit card transactions into the books (accounting duties). ☐

Safeguarding Assets

1 Tag or engrave all equipment and fixed assets with ID numbers and reference to the fixed ☐

asset listing especially if purchased with government grant funds.

2 Perform a periodic inventory on all the fixed assets (computers, equipment, furniture, etc.) at least once a year to ensure completeness. ☐

3 Ensure supplies are kept in a secure location and distributed with proper oversight. ☐

D. CASH DISBURSEMENTS (PAYMENTS AND SPENDING)

Check Payments

1 Before entering invoices into the books: ☐

- Ensure the PRF was authorized and matches the original invoice.
- Review the invoice for calculation errors.
- Ensure proper confirmation of receipt of goods or performance of services is noted on the invoice.

2 The staff person who enters the invoice into the books may not be a signatory on the checking account. ☐

Bank account signatories may not have access to the bookkeeping program. ☐

3 *For consideration:* Separate the following tasks: ☐

- Entering invoices into the system.
- Printing checks.

4 Before signing any check the authorized check signer should ensure: ☐

- The PRF was authorized.
- Proper confirmation of receipt of goods or performance of services is noted on the original invoice.

5 Ensure dual signatures on all checks with ideally one being a board member. ☐

Signature stamps should not be used. ☐

6 Attach a check stub to all paid invoices (or stamp "paid" on the invoice) as evidence of payment after the payment is processed. ☐

7 Checks should not be stuffed and mailed by the check preparer or signer. ☐

8 A W-9 should be received before issuing payments to subcontractors in order to timely file 1099's. ☐

Check Safeguards

1 Ensure all blank checks are locked in a safe location. Access to these checks should be restricted, perhaps even from the bookkeeper. ☐

Checks may never be pre-signed. ☐

2 Checks should be in prenumbered, sequential order to provide an audit trail and ensure completeness. ☐

3 Checks should never be made out to 'cash'. ☐

4 Properly account for all voided checks (mark accordingly on the check, keep a list, etc.). ☐

5 Consider using the bank's "Positive Pay" service which adds an extra layer of security. Typically, it requires submitting a list of "authorized" checks into the bank portal and only checks on this "authorized" list will be processed. ☐

E. PAYROLL

1 Timesheets should be reviewed and approved by the authorized staff person (management duties). ☐

A different staff person should process and prepare the payroll (accounting duties). ☐

2 Ensure dual signatures on all payroll checks unless using a 3rd party payroll company. ☐

3 A new staff form must be completed for all new hires and include all the necessary information to add the new staff to the payroll. ☐

All new staff forms must be approved in writing by the authorized staff person (management duties) before being entered into the payroll program. ☐

4 Prior to the first payroll cycle, cross-reference salary/wage information from the payroll program to the approved supporting documentation (new staff forms, contracts, ADP new hire sheets, etc.) ☐

Ensure accuracy and proper authorization for each employee. ☐

5 Ensure compliance with: ☐

- Timely federal payroll tax deposits.
- Workman's Compensation requirements.
- W-2 vs. 1099 classifications.

6 Using direct deposit for payroll is safer and more efficient than using checks. ☐

F. ONLINE BANKING AND ELECTRONIC PAYMENT PORTALS

Account Management

1 Four main steps provide a high level of oversight: ☐

1) Alert notifications email/text.
2) Review transactions online.
3) Dual controls on specific tasks.
4) Managing user privileges (privileged access management.)

2 All staff that have access to online accounts should be set up with separate login username and passwords. ☐

All staff should follow these protocols: ☐

- Passwords are never shared.
- Two-step verification for online activity. (Two-step verification adds an extra layer of security. In addition to your username and password, you'll enter a code that is sent via text or email upon signing in or performing sensitive tasks.)

3 Use the online accounts 'manage users' functionality to set up employee privileges. Separate duties as much as possible. ☐

4 For important account changes (user rights, adding emails, etc.), set up Dual Control. One staff initiates and another approves from a different computer. ☐

5 If practical, one dedicated computer should be used for all online banking where email and web browsing is blocked. ☐

6 On a daily basis, a designated staff person should check all online activity for any unusual transactions. Be on the lookout for small transactions that don't appear authorized. ☐

Even a small deposit in a checking or savings account, if unexpected, could be a sign criminals have learned your account information and are trying to link your account to theirs so they can fraudulently withdraw money, perhaps your entire balance.

7 *For consideration:* Restrict bank accounts by purpose and permitted transactions. For example: ☐

(1) "Main" account for deposits only. No debits are allowed other than internal transfers. This account funds the other accounts.

(2) "Payroll" account to process direct debit paychecks.

(3) "Checking" account restricted to processing check payments only. No deposits, wires, ACH transactions, etc.

(4) "Electronic" account restricted to processing all electronic transactions.

Only fund the three accounts in the amount needed to cover payments. Establish maximum payment and transfer thresholds by account.

Electronic Transactions

1 Offer donors an online payment portal for donations or payments due to the organization. ☐

2 Use "Push" transactions for electronic payments with "Dual Control". One staff initiates and another approves from a different computer. If practical, "Pull" transactions (initiated by the vendor) should not be used. ☐

3 If "Pull" transactions are necessary, set up a "Whitelist" of approved vendors with the bank. Any attempt by a vendor not on the list is automatically blocked. ☐

For consideration: For approved vendors, consider setting max dollar amounts on a vendor-by-vendor basis.

4 Before sending outgoing wires or receiving incoming wires, ensure the recipient / payer verbally confirms the proper wiring information. ☐

5 Set up automated electronic alert notifications for any attempted or actual misuse of: ☐

- Balance threshold violations.
- Wire notifications.
- New vendor online bill pay.
- Positive pay exceptions.
- Newly linked external accounts, etc.

APPENDIX A

RECOGNIZING INCOME ON THE CASH BASIS

Boards for schools and non-profit organizations utilize budgets and financial reports for analytical and decision-making purposes. The data provided in these reports only has significance if it leads to fact-based decisions that enable the organization to meet its financial obligations.

GAAP requires using the accrual basis of accounting. This requires revenue to be recognized when "earned". For tuition income, this is only after the service (i.e. education) is provided. However, the timing of the performance of the service does not necessarily correspond with the actual receipt of tuition payments. As such, accrued tuition revenue does not accurately reflect the school's ability to meet its financial obligations. The same is true in recognizing 'promises to give' as donation revenue. Even when all the conditions are met to recognize 'promises to give' as donation revenue, it still does not reflect actual cash received.

When the financial report shows a surplus based on revenue from accrued tuition and 'promises to give', it may not be understood that this does NOT mean they are running a CASH surplus. In fact, they may be insolvent. It is for this reason that revenue from tuition and promises to give should only be recorded when the cash is received, not when "earned".

This is the premise for using the modified cash basis of accounting for internal financial reports. It recognizes revenue when cash is received (cash basis) and expenses upon receipt of an invoice after goods are delivered or a service performed (accrual basis). It also excludes recording non-cash provisions like depreciation and allowance for doubtful accounts. Financial reports based on this method are straightforward and easy to understand. This is especially helpful for Board members that do not have a strong financial background. Most importantly, such a report provides an accurate financial picture of an organization's ability to meet its financial obligations.

It should be noted that this accounting method is not in accordance with Generally Accepted Accounting Principles (GAAP) which requires using the full accrual basis. As such, accrual journal entries are required in preparing audited annual financial statements which must conform with GAAP.

AUTHOR BIO

Yaakov 'Jake' Goldstein graduated from Yeshiva University with a B.S. in Accounting in 1987 and became a CPA in 1991. He has worked at several multi-national corporations including Bank Leumi, Arthur Andersen, and PricewaterhouseCoopers.

Specializing in the high-tech industry, Yaakov helped his clients build up their finance departments, designed financial controls, trained staff, and handled SEC reporting and IPOs, aiding clients in securing financing.

In 2000, Yaakov joined Torah Institute during a time of financial distress. He overhauled the finance office, established controls, cut costs, and launched a fundraising campaign, eliminating over $1 million in residual operating debt and subsequently paying off a long-term construction loan nine years ahead of schedule. The school remains debt-free as of today.

Since 2012, Yaakov has helped schools and nonprofits revamp and bolster their finance offices, noting that most boards lack necessary financial oversight. This booklet aims to raise awareness and help boards fulfill their fiduciary duty including financial oversight.

Yaakov speaks to yeshiva high schools, yeshiva gedolas and nonprofits on behalf of The Aleph Institute's Project 432. He can be reached at 443-414-6432 or ygoldstein@aleph-institute.org


PROJECT
432
Honesty.
Integrity.
Peace of Mind.
POWERED BY
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