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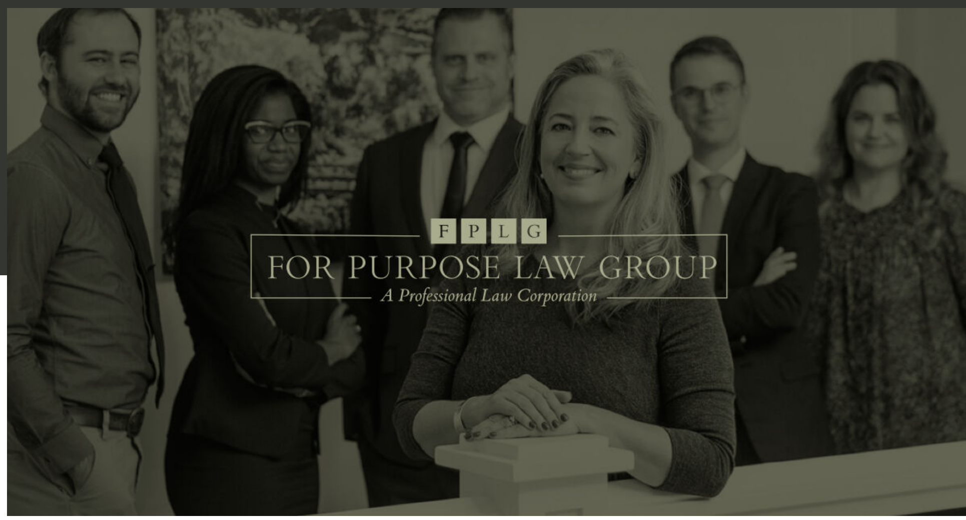
NONPROFIT

Common Accounting Errors of Small Nonprofits

08.29.17 | Linda J. Rosenthal, JD



There's no one-size-fits-all for an accounting set-up for nonprofits. Needs and best practices may vary widely depending on the organization's size, financial situation, and purposes and activities. However, even a new small organization must create and maintain a basic accounting system sufficient to keep adequate records and to generate data for any required tax or regulatory filings. It's the board's responsibility to learn the basics of nonprofit accounting and to set up – or get help in setting up – a workable system.

Avoid Common Accounting Mistakes

Nonprofit accounting experts explain that, in addition to having a good accounting system, directors of small organizations should watch out for – and avoid – certain common errors. Some of these are:

- ***Not Following Established Procedures***

"Even the smallest nonprofit should set formal, documented and detailed procedures for managing financial and bookkeeping chores." It should "include all aspects of managing your organization's money — how to accept, document and deposit donations, pay bills, and handle every step in between." But having a system in place without following it scrupulously defeats that purpose. "Put these procedures in writing and make sure you follow each step, every time."

- ***Making Clerical Errors***

Particularly for board members who are volunteers with little experience in accounting matters, it's easy to "wreak havoc on your accounts by entering a $500 payment as $50 or transposing numbers." The remedy for this all-too-likely occurrence is to "check and double-check every entry every time [...and...] [r]econcile accounts against bank statements immediately."

- ***Not Having a Budget***

Creating an accounting system is a key step in getting an organization off the ground, but establishing annual budgets is critical as well. "Budgets don't have to be intricate to be useful," but they are a necessary step in the ongoing planning and operation of the organization. There should be revisions and refinements on a regular basis.

- ***Not Assigning Appropriate Categories***

In particular, "if you accept donations that may be earmarked for certain programs," it's important to account for them in proper detail. That may include setting up an initial chart of accounts and defining how items should properly be assigned.

- ***Not Managing Petty Cash***

"Small expenditures like picking up a few office supplies or buying a pizza for volunteers is much easier to do with a petty cash fund. Handle the cash with care, though. Lock it up, authorize only a few people to make disbursements and require receipts for all expenditures."

Establish Internal Controls

Unfortunately, nonprofits are not immune from the problem of fraud and – particularly – embezzlement. "Financial mismanagement, or worse yet, embezzlement can occur within any organization – it does not only happen in certain types of organizations, explains Bennett Napier in *Board members must oversee finances* (May 10, 2017) *Tallahassee Democrat*. "Such activity can happen in large staff run organizations, small staff organizations, or all volunteer run organizations. Furthermore, it does not solely occur in organizations with large budgets."

In *Charities and Embezzlement* (August 9, 2017), we touched on this topic, relaying a troubling incident that rocked the small Clinton Township outside of Detroit. There was a theft: the Clinton Valley Little League was robbed of $300,000: "The embezzler was an unlikely criminal; the elementary school's library clerk who was active in her church. She was 'like everyone's grandma in town.' "

But, "as a volunteer, she handled the cash and was able to misappropriate small amounts over the six years that she had handled the money. She pleaded guilty and was sentenced to five years' probation and restitution, 'but the incident has left the town traumatized and divided.'"

According to one observer, "[t]he whole township was broken up by it: 'It was a nightmare. [The perpetrator] kept no books for the league finances over the six years of her tenure. During that time, her personal money and the league's were commingled. A full 380 of the group's checks were made payable to the couple, who, records showed, moved $318,000 through local casinos, depositing checks and withdrawing money through casino ATMs.'"

In *Charity Embezzlement: Thwart It With Good Controls* (November 17, 2016), we discussed certain precautions that can and should be taken by each and every organization. They include a recommendation that could have helped in the Clinton Little League situation; that is, making sure that at least two unrelated people are responsible for handling cash.

Conclusion

Simple mistakes in the money-management aspect of a nonprofit can cause outsized havoc and trouble. It's as critical to know what to do right as it is to learn about what can go wrong, and take steps to prevent the foreseeable pitfalls that have plagued other groups like yours.

— Linda J. Rosenthal, J.D., FPLG Information & Research Director