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Financial Controls:
A Safeguard Against Misuse of Public Funds

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ABSTRACT

Financial controls assist school administrators in safeguarding and evaluating the efficient and effective use of financial resources. In this article, I discuss two methods of financial controls used by school districts: internal control and financial audits.

Financial control techniques assist building principals and other school administrators in acquiring, allocating, and evaluating the use of financial resources—cash, accounts receivable, accounts payable, inventories, purchases, and long-term debt. Regardless of their size, school districts must be able to pay short-term obligations and long-term debts. They must also protect the school district's revenue from theft, unlawful conversion, and misuse. Control of financial resources in individual schools and school districts is implemented primarily through two methods: internal control and financial audits.

Internal Control

Internal control is an accounting function and responsibility. Through the efforts of the school district's accounting unit headed by the CFO, policies and procedures are adopted to safeguard assets and verify the accuracy and reliability of accounting data. The characteristics of effective internal control include the following (American Management Association, 2010; Pinedo, 2011).

1. Formal organization should be clear. Definitions of job responsibilities must be estimated so as to fix accountability for each and every aspect of a financial transaction. The organizing function of administration must be the primary source for this important aspect of internal control.

2. Financial accounts must be set up for each division or other unit of administration. When expenses and income are readily traceable to specific administrators, they are more easily controlled. Such communication between accounts and divisions or building units is especially important in both the preparation of budgets and the evaluation phase of the accounting system.
3. Employees who handle assets should not also be responsible for record keeping on these assets. For example, employees who receive and store materials should not also verify the receipt of those materials.
4. No one person should have complete control over all phases of an important transaction. For example, the same individual should not be responsible for preparing purchase orders and for making out the checks in payment of those purchases.
5. The flow of work from employee to employee should not be duplicative, but the work of the second employee should provide a check on the work of the first. For example, the check drawn to pay for supplies and materials should be cosigned by a second employee who verifies the accuracy and legitimacy of the transaction.

Effective internal control procedures can be established for each distinct financial resource. Cash, accounts receivable, interest, inventories, accounts payable, payrolls, and purchases must be safeguarded through procedures that conform to the five aforementioned characteristics of effective internal control.

Financial Audits

Another major financial control technique is the *financial audit***,** an independent appraisal of a school district's accounting, financial, and operational systems. Audits are of two types: external and internal (Carmichael, 2010).

External Audit

An *external audit* is conducted by experts from outside the school district such as, bank examiners or certified public accountant (CPA) firms. Their main purpose is not to prepare the school district's financial reports but to verify that the district, in preparing its own financial statements, has followed generally accepted accounting principles and applied them correctly (American Institute of Certified Public Accountants, 2010). External audits are so important that some states require all public school districts to have their financial records examined and certified by outside accountants, as assurance to taxpayers that the school district's financial reports are accurate.

Internal Audit

An *internal audit* is performed by employees of the school district who are trained to examine the accuracy of the school district's accounting and financial reports. Large school districts may have an accounting staff assigned to the internal audit function. Like external audits, internal auditors verify the accuracy of financial and accounting procedures used by the school district. Internal audits also focus on the efficiency and appropriateness of the financial and accounting procedures. Besides appraising the accounting and financial operations of the school district, internal auditing sometimes involves assessment of operations generally, such as policies, procedures, use of authority, quality of management, effectiveness of methods, special problems, and other phases of general operation (Hooks, 2011).

Both external and internal audits should be thorough. Some of the areas examined by auditors include the following (American Institute of Certified Public Accountants, 2010).

1. *Cash flow.* Confirm bank balances; review cash management procedures.
2. *Accounts receivable.* Obtain verification from vendors concerning amounts owed and anticipated payments; confirm bank balances.
3. *Inventory*. Count physical inventory to verify the accuracy of the school district's financial reports.
4. *Fixed assets.* Check physical evidence of fixed assets (buildings, equipment); evaluate depreciation; determine whether insurance is adequate.
5. *Loans.* Review long- and short-term loan agreements; summarize the school district's obligations.
6. *Revenues and expenditures.* Evaluate proper matching; safeguard assets; prevent or detect fraud or theft.

Conclusion

Financial controls assist school administrators in safeguarding and evaluating the efficient and effective use of financial resources. Control of financial resources in school districts is implemented primarily through two methods: internal control and financial audits.

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