

# Diploma in Financial Management & Accountability

*- a joint initiative of TISS & FMSF*

## Course Material



Control Systems  
Paper - VI

Module - III  
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## UNIT- 4

### MODEL FRAMEWORK OF INTERNAL CONTROL SYSTEM

#### 4.1. Introduction

The nature and extent of Internal Control can be developed on the basis of size and activities of the organization. It is very difficult to recommend any universal system for all organizations and therefore, it is important to understand the features and mechanism of Internal Control. All organizations should develop their own systems of Internal Control depending on their needs and resources.

However while designing an internal control system, the basics of Internal Control System and important features should be kept in mind and the following basics points should be considered while framing the internal control systems :

#### 4.2. Cash

4.2.1. Wherever possible cash function should be separated from accounts function.

4.2.2. The cashier must maintain a hand cash book recording therein all the receipts & payments.

4.2.3. Cash balance as per the hand cash book needs to be daily reconciled with the physical balance.

4.2.4. Periodically the head of the finance department shall also certify the physical verification of cash and its reconciliation with the book balance.

4.2.5. Withdrawal of cash from bank

- Based upon the monthly plan and the approved requisition from centres/ program Head, the cashier shall prepare a requisition for withdrawal of cash from bank.

- The approving authority, on the basis of such requisition & duly checked by the Accounts department, shall authorize the voucher and sign the cheque for payment or for withdrawal of cash from bank.

4.2.6. Wherever possible, adequate insurance coverage shall be taken for cash in safe and for cash in transit.

4.2.7. All the daily collection through Income generation programs, donations or any other receipts shall be deposited into the bank preferably on the next day or at fixed intervals. The amount required for incurring any expenses has to be met out of the withdrawal from the bank.

#### **4.3. Bank**

4.3.1. Bank account must be in the name of the organization / in the name of the project, and wherever possible saving bank account should be preferred in place of current bank account in order to earn interest on the money lying in the bank accounts.

4.3.2. The operation of the bank accounts must be under the joint signatories.

4.3.3. Wherever possible and permitted under the law, separate bank account should be maintained for each funding arrangement, for each Income Generation programme and for unrestricted funds.

4.3.4. The bank reconciliation statement on month to month basis has to be prepared for each bank account.

#### **4.4. Receipts**

4.4.1 Normally the nature of receipts includes:

- Grants
- Receipts from Income Generation Programs.
- Beneficiaries contribution
- Income from investments like interest and rent, etc.

#### 4.4.2. As regards receipt of Grant :

##### Receipts through cheques

- It is to be ensured that the grants are received in the name of the organisation and through a/c payee cheques/ Telegraphic Transfers/Bank Drafts.
- The grant should be received by the Head of the organization or by any person authorized by the Board and pre-numbered receipt should be issued for every grant received.

##### Receipts through cash

- In case where donations are received in cash it should be received by the head of the organization or by the persons authorized by the Board or authorized by head of the organisation.
- Pre-numbered receipt should be issued for every donation received and the amount collected should be handed over to the Cashier who will check the receipts from the counterfoil of the pre numbered receipts book.

#### 4.4.3. As regards Beneficiaries Contribution :

- All the contributions from the beneficiaries at various centers & at the Head office may be collected by the Center in charge/project in charge/any other authorized persons and it should be duly documented either by:
  - ❑ issuing a pre-numbered receipt, or
  - ❑ in case of small contributions through maintaining a contribution receipt register.

- The person on day to day basis or periodically will deposit the total cash collected to the cashier who will check the total collection made with the receipts issued.

#### 4.5. Expenses

##### 4.5.1 Processing & Authorisation of Vouchers

- It is recommended that every organization should formulate an authorization policy documenting the authorization process of each type of expenditure and financial transaction.
- At the time of formulating the authorization policy it is to be ensured that the project coordinators are also involved in the processing of vouchers concerning their projects and account heads should be given by the project coordinators. The role of the accounts department should be that of checking the correctness of accounts heads and completeness of the supporting and processes.
- The project head before passing a voucher for expenditure must ensure that all the expenses incurred are backed by budgetary provision and shall also ensure the propriety of the transactions.
- For the transaction in relation to internal project borrowings and loans the request should come from the accounts department on the basis of fund position and thereafter it should be authorized by the head of the organization before the fund is actually being transferred.
- All the disbursement must be documented through a voucher and supported by original invoices and supporting documents and the document to evidence the conduct of the programme/activity.

#### **4.5.2. Identification of expenses**

- It is required that all the requisitions, vouchers & the supporting must specify the name of the funding arrangement/ name of the programme, so that the expenses under a particular funding arrangement can be easily identified.
- It is also required that vouchers and the supporting after being paid must be stamped as PAID in order to avoid its re-use.

#### **4.5.3. Mode of payment**

- All the payments wherever possible should be paid by A/c Payee Cheques.
- The organization should define a limit beyond which cash payment can not be made.

#### **4.6. Advances**

- An advance has to be made only on approved requisition.
- The accounts department must maintain an individual ledger for advance taken and its adjustment.
- Separate ledger and sub ledger should be maintained for advance against salary and advance against project work.
- It is to be ensured to the extent possible, that second advances are given only after the first advance has been cleared.
- For advance for an amount below Rs. 1000.00 or the advance, which is going to be cleared within 3 days, the system of IOU may be followed. Under this system whenever a person is taking an

advance, he/she needs to sign a document confirming receipt of advance and at the end of the day when the advance is cleared this document is cancelled and the expenses are booked directly in the books of account. In such cases there is no need of maintaining the name wise advance register.

- It is to be ensured that, to the extent practicable, at the end of the financial year/project period no advances are carried forward.

#### **4.7. Fixed Assets**

**4.7.1. Definition:** A fixed asset is defined as “an asset held with the intention of being used for the purpose of producing or providing goods or services and is not held for sale in the normal course of business.”

##### **4.7.2. Procurement of fixed assets**

- Fixed assets, such as land, building, vehicle etc. should be procured/ purchased by organisation following the purchase policy if any.
- The fixed assets should always be recorded at the original cost plus any installation and other related capital cost incurred thereto.
- Sufficient insurance coverage for the assets should be taken wherever possible.

##### **4.7.3. Accounting of Fixed Assets purchased out of grants**

When fixed assets are acquired from restricted grant, the funds are shown to be utilized while reporting to the donors. It is therefore required that contra or corollary entries are made to record the acquisition as deduction from grant and recognizing the property as an asset and crediting to Property and Equipment Fund (a net asset account).

#### **4.7.4. Fixed assets register**

- a. Fixed assets register should be maintained incorporating therein the following details:

- i. Date of purchase
- ii. Description of assets
- iii. Quantity of assets
- iv. Value of the assets
- v. Location
- vi. Depreciation rate
- vii. Identification mark
- viii. Present use
- ix. Source of Fund
- x. Details of transfer from one Location to other
- xi. Any other information

- b. Separate fixed asset register should be maintained for head office and for each location.

#### **4.7.5. Depreciation**

- Depreciation is an allocation of the cost of a fixed asset over the period of its useful life.
- The rate of depreciation charged to the assets acquired should be at the rate as prescribed under statutory regulations or as stated in the Financial Policy or at the rates as may be approved by the Board.



#### **4.7.6. Sale/disposal of fixed assets**

- If an item of fixed asset gets permanently unusable or obsolete then the item can be sold.
- However in case of fixed assets acquired out of the grant, the condition attached with the acquisition of fixed assets as per the grant agreement must be looked into and must be complied with before the decision for sale of the fixed assets is being taken.
- The following procedures should apply for the sale of fixed assets:
  - i. A committee for the purpose of finalizing the sale of fixed assets should be formed.
  - ii. The committee will invite quotations for the sale.
  - iii. The committee will then evaluate the quotations and finally decide for the sale of the assets.

#### **4.7.7. Transfer of fixed assets from one location to another**

The fixed asset can be transferred from one office to another within the same organization. However, such transfer of Fixed Asset has to be authorized by the appropriate authority and all the terms & conditions attached as per the grant agreement at the time of acquisition of fixed assets should also be complied with.

#### 4.8. Investments

- The temporary surplus fund of the restricted grants can be kept in short term fixed deposits with the banks.
- Other surplus funds may be invested by the trust in the interest bearing fixed deposits and/or other securities.
- All NGOs should pay careful attention with regard to the investments. Firstly under section 11(5) of the Income tax Act 1961 investments are to be made in specified securities only.
- An investment register should be maintained incorporating therein :
  - the nature and description of the investments.
  - in the case of investments in companies, the name of company in which the investment has been made.
  - certificate numbers
  - distinctive numbers
  - cost, amount paid-up and face value
  - the names in which the investments have been made.
  - due dates for receipt of interest.
  - date on which dividends are ordinarily received.
  - maturity dates.
  - All the investments kept by an authorized official with adequate security measures.

- All investments should be periodically verified physically with the Register.
  - Periodic review of all investment income, to ensure timely receipt.
  - All transactions of investments should be authorized by the board or a person to whom power has been delegated.
- If the total investment to be made in one year exceeds Rs.25 lacs, a committee should be constituted by the Governing board for advising and monitoring the investments held by the organisation.

**SELF ASSESSMENT QUESTIONS:**

1. Design an Internal Control System for:
  - a) Withdrawal of cash from Bank
  - b) Processing of expenses for traveling.
  - c) Sale of Fixed Assets acquired by the organisation out of grant.
  - d) Receipt of donations in cash.
  - e) For maintaining identification of expenses of different funding arrangements.