

INTERNAL FINANCIAL CONTROLS CHECKLIST FOR MUNICIPALITIES



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Internal Financial Controls Checklist for Municipalities

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Introduction

This checklist was created to help VLCT member municipalities assess internal financial controls. This document is meant to be used by municipal officials whose responsibilities include oversight and handling of municipal assets as well as accounting for municipal finances. Ideally, this checklist will be used by all such officials, working together to assess and improve the accuracy, transparency, and security of municipal finances and assets. Please read this introduction (pages 2-6) before using the checklist that appears at pages 7-30 of this document. It includes important information.

What are Internal Controls for Finance?

Internal controls for finance are systems and processes that are designed to ensure that the financial statements of an organization accurately present the operating results and financial position of that organization. In the municipal context, internal controls help to assure that public funds are administered and expended in compliance with applicable statutes and regulations; that funds are used for purposes for which they were authorized and intended; and that there is accurate reporting regarding the use of those funds. The basic principles of internal control are routinely used in business and government accounting.

According to the Committee of Sponsoring Organizations¹ (COSO), a joint initiative of five private sector accounting and financial management organizations:

Internal control is a process, effected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in three fundamental categories:

- Effectiveness and efficiency of operations,
 - Reliability of financial reporting, and
 - Compliance with applicable laws and regulations.
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One of the primary goals of internal controls is to create a separation of accountability and custodianship, i.e. to assure that municipal officials or employees who have responsibility for keeping records of municipal finances are not also the same individuals who have custody of its assets. In the accounting world, the principle of separation of accountability and custodianship dictates that a person who handles bank deposits or keeps cash books, should not also receive bank statements or make bank reconciliations. In addition, the same individual should not disburse payment and also confirm receipt of or authorize payment (sign selectboard's order) for merchandise.

¹ The members of COSO are the American Accounting Association, the American Institute of CPAs, the Financial Executives International, the Institute of Management Accountants, and the Institute of Internal Auditors.

Are Municipalities Legally Required to Adopt Internal Controls?

State law does not mandate the implementation or use of internal financial controls.² In fact, State law gives very little guidance regarding municipal financial management. As such, internal controls may vary significantly from municipality to municipality. Controls in small towns with few employees will naturally be different from controls in larger towns that have more employees in the financial function. However, the standards of any internal control system are generally the same.

Why are Internal Controls Important?

From an accounting and risk management standpoint it is considered best practice for each municipality to have an internal control system to help assure the dependability of the town's financial record keeping and reporting. An internal control system can be implemented through the adoption of written financial policies. Such policies can have a number of benefits for Vermont municipalities:

- a. **Education.** Financial policies help educate those municipal officials who may not have a background in government financial management. In Vermont, many elected and appointed municipal officials have no background or expertise in government finance. Nevertheless, these officials may be responsible for the administration of municipal budgets comprising hundreds of thousands or even millions of dollars. Written financial policies can help inform officials, regardless of their educational or professional background, of good financial practice, making it more likely that these good practices will be implemented and followed.
- b. **Prevention and Resolution of Conflicts.** Financial policies may help prevent and resolve conflicts in local government. The responsibilities of Vermont's municipal officers frequently overlap and clear lines of authority can be hard to identify. As a result, the administration of Vermont local government can seem complex, even in the smallest town. The key to effectively navigating this complexity is effective communication and cooperation among local officials. Financial policies can clarify both the responsibilities of local officials and lines of authority. The process of adopting written financial policies can also afford local officials the opportunity to engage in communication and develop common financial goals for their municipalities. Active participation in the process makes it more likely that all the parties involved in financial decision-making will abide by a common set of rules.
- c. **Continuity and Efficiency.** Financial policies can provide continuity and efficiency in the town's financial operations. Elected officers often serve relatively short terms and new officers may not be experienced in dealing with financial issues. Financial policies can eliminate the need to

² It should be noted however, that the State or Federal government may require that municipal use of State or Federal grant funds requires certain internal financial controls.

reinvent responses to recurring situations, thereby increasing efficiency by standardizing operations and retaining institutional knowledge built up over the years.

- d. **Guidance.** Financial policies can fill some of the gaps in Vermont's rudimentary municipal finance laws. Vermont is a Dillon's Rule state, meaning that our municipalities have only those powers specifically delegated to them by the Legislature and such additional functions as may be necessary to exercise those authorities. For this reason, municipal officials often turn to Vermont statutes for guidance when questions arise. Unfortunately, Vermont's municipal finance statutes have not kept pace with modern financial practices and often fail to provide local officials adequate guidance on the finance issues they commonly face. Well-crafted local financial policies can overcome some of these shortcomings in Vermont's municipal finance laws.
- e. **Transparency and Confidence.** The adoption of financial policies can foster confidence in local government by increasing transparency, accountability, and consistency in municipal decision-making. The policies can help local officials make more informed decisions about providing services, acquiring and managing capital assets, safeguarding a town's resources, and promoting financial stewardship, all of which may result in a more stable tax rate.

Who has the Authority to Adopt Internal Controls?

There are multiple municipal officials with varying degrees of authority to adopt policies regarding financial controls. The selectboard (or other legislative body) of the municipality only has the authority to adopt financial controls that apply to municipal officials *who are appointed or hired* by the legislative body. The legislative body does not have authority to dictate the use of financial controls by officials who are independently elected such as clerks, treasurers, and tax collectors. Elected clerks, treasurers, and tax collectors are legally independent from the legislative body and from one another, and therefore have authority to adopt their own financial controls and to dictate the use of financial controls by their statutorily appointed assistants.

Despite this legal independence, it is to the advantage of the municipality as a whole when elected officials work together to see that there is a comprehensive system of internal financial controls that is adopted and adhered to. Working cooperatively on these matters is also logical since the respective responsibilities of elected officials frequently overlap. In many instances, several boards or officers may be involved in a particular financial transaction or function. In that case, VLCT recommends that the applicable policy or procedure should be adopted jointly by all of the officials involved. For example, the law provides that money received by the treasurer on behalf of the town may be invested and reinvested by the treasurer with the approval of the selectboard. Accordingly, a town's investment policy should be jointly crafted and adopted by the treasurer and selectboard. On the other hand, the purchase of goods and services is the sole responsibility of the selectboard, and therefore the selectboard would adopt a purchasing policy addressing such things as prior authorization of certain purchases and bidding requirements.

Municipal officers are not required to follow any special procedure when adopting financial policies, except that a policy adopted by a municipal board (e.g., selectboard, board of auditors) may only be

adopted by a majority of board members at a meeting held in accordance with Vermont's Open Meeting Law. Technically the voters of the municipality have no authority to demand or to refuse financial policies. Unlike ordinances, there is no permissive referendum process for municipal policies.

It should be noted that the town treasurer has an independent obligation to report on internal controls pursuant to 24 V.S.A. § 1571(d) which states that the town treasurer "shall annually, on or before June 30, complete and provide to the selectboard a copy of the document made available by the Auditor of Accounts pursuant to 32 V.S.A. § 163(11) regarding internal financial controls." A copy of the State Auditor's Financial Management Questionnaire for Towns and Cities is made available on the website of the Vermont State Auditor.

The Five Elements of Internal Control

The Committee of Sponsoring Organizations (COSO) identifies five elements of internal control which are briefly described below.

1. The **Control Environment** in a municipality should be one in which the elected officials and appointed managers support strong financial controls and show a commitment to maintaining competence through good hiring practices and training. In addition, the municipality should have a clear and unambiguous organizational structure with appropriate policies and procedures. VLCT has published five policies particularly applicable to internal controls: Model Accounting, Auditing, and Financial Reporting Policy; Model Purchasing Policy; Model Cash Receipts, Petty Cash, and Returned Check Policy; Model Credit Card Policy; and Model Fraud Policy. The Model Fraud Policy explains fraudulent activities and the role of employees who discover them. These policies may be found on the VLCT website <https://www.vlct.org/resource/model-municipal-financial-policies>. In addition, the VLCT Model Conflict of Interest Policy can help municipal officials manage conflicts of interest that may arise in the context of financial transactions and financial management. The Conflict of Interest Policy can be found here: <https://www.vlct.org/municipal-assistance/municipal-topics/ethics-and-conflict-interest>.
2. **Risk Assessment** is the process of identifying potential weaknesses in the way finances are managed and accounted for. Risk Assessment helps to identify the activities carried out by municipal officers and employees that may create a risk of mistake, misrepresentation, fraud, or embezzlement. Once those risks are identified municipal officials will have a better handle on what internal control activities are needed to eliminate or mitigate those risks.
3. **Control Activities** are specific actions municipalities can take to prevent or mitigate the risks that have been identified in their operations. The VLCT Municipal Checklist for Internal Controls, which follows this memo, is a key component of determining appropriate financial control activities.
4. **Information and Communication** is critical to internal control, and by extension, critical to the proper functioning of all the other activities in the municipality. Effective and timely communication of relevant and accurate financial information helps ensure that the municipality is able to meet its objectives and comply with laws and regulations. In addition, it assures that elected officials and voters have accurate information about municipal finances and are able to make informed decisions

based on that information. For these same reasons, it is also important that financial policies and procedures are documented and accessible and that financial control efforts are transparent.

5. The final element, **Monitoring**, is the review of the effectiveness of all five elements of internal control. This requires looking at the municipality's activities and transactions to assess the quality of performance over time and to determine whether controls are effective. Any financial policy that is adopted should be reviewed annually to insure that it remains current. This may involve minor edits or major revisions resulting from economic or legislative changes. Of course, a policy adopted by one board or officer can be rejected or modified by the next officer or board. But annual review will help insure that all officials subject to the policy agree with its terms.

Internal Financial Controls Checklist for Municipalities

Before you start working on the checklist, please read the introduction (pages 2-6) and list of supporting documents (page 30). Guidance and additional information are included with the checklist questions to help you complete it.

The Municipal Checklist for Internal Controls is a modified version of the Vermont State Auditor's Internal Control Checklist for Vermont Towns.³

A. GENERAL CONTROLS

Question A.1: Do municipal officials with control over municipal assets and accounts understand their various responsibilities for implementing and following an adequate system of internal controls?	Yes	No	Unsure
	☐	☐	☐

Guidance for Question A.1: *It is important for local officials who have authority over town assets and accounts to establish and follow a system of internal financial controls appropriate for their municipality.*

This system should address all five elements of internal control: the control environment, risk assessment, control activities, information and communication, and monitoring. The adoption of appropriate financial policies regarding accounting, reporting auditing, purchasing, and fraud prevention will help assure that town assets are appropriately expended or preserved and that financial statements are free from accidental or purposeful misstatement. In addition to using this Checklist, a municipality may want to hire a professional auditor to do a full financial assessment.

Question A.1 Response Notes:

Question A.2: Has a system of internal financial controls been adopted and are those controls well-documented? Are the duties of municipal employees who have access to municipal assets and accounts clearly defined and in writing?	Yes	No	Unsure
	☐	☐	☐

Guidance for Question A.2: *A municipality should have proper documentation of its financial policies, procedures, and control practices.*

Such documentation should explain the duties and responsibilities of each employee in the municipality and how they interrelate with one another. Among the policies that a town should consider adopting are

³ VLCT's Model Financial Policies are available on the VLCT website here: <https://www.vlct.org/resource/model-municipal-financial-policies>

an accounting, auditing, and financial reporting policy; a purchasing policy; and a cash receipts policy. When policies, procedures, and control activities are in writing, employees will know what is expected of them as they carry out their duties. In addition, written procedures will be indisputable in the case of employee absences or when a new employee is hired.

Question A.2 Response Notes:

Question A.3: Are financial policies retained, accessible, and adequately communicated to newly-elected officials and newly-hired staff?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question A.3: *Newly elected officials should be oriented to financial policies and procedures that are applicable to their position in municipal government.⁴ Officials who manage or supervise employees should see that those employees are educated about proper financial management and reporting.* A strong system of internal controls includes a commitment to competence. To make sure that municipal financial systems are functioning properly, it is important that municipal officials and staff are familiar with municipal policies and have the opportunity to get the training they need to maintain and improve their skills. Policies should be retained in a manner that is accessible and should be communicated to newly elected municipal officials and to municipal staff.

Question A.3 Response Notes:

Question A.4: Has the selectboard adopted a fraud prevention policy (such as the VLCT Model Policy) and has it been communicated to municipal employees during the last year?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question A.4: *Municipalities should adopt a fraud prevention policy that outlines what is expected of all employees in terms of their personal conduct, as well as their role and responsibility in reporting suspected inappropriate actions by others.* A fraud prevention policy informs employees that fraudulent acts will not be tolerated and explains that each employee has a duty to report any activity that appears to violate any law, regulation, or policy. The policy should also clearly outline the process that is available to report any suspected violation and assure employees that complaints will be investigated confidentially and without retaliation of any kind.

Question A.4 Response Notes:

⁴ Depending on his or her position within municipal government, an independently-elected official may have the authority to revise or reject an existing financial policy or procedure.

Question A.5: Does the municipality have an independent professional audit done on an annual basis?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question A.5: *While VLCT continues to support the election of auditors and their work, we recommend that all towns obtain periodic or regular audits from a certified public accountant.* Ideally, a town would have an outside audit conducted annually. However, if that is not possible, VLCT recommends that the outside audit should be conducted at least every three years.

Question A.5 Response Notes:

Question A.6: Does the selectboard regularly receive and review financial reports from the treasurer regarding actual revenue and expenses as compared with budgeted revenue and expenses?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question A.6: *The selectboard should regularly receive and review financial reports from the treasurer (or municipal finance manager) regarding actual revenue and expenses as compared with budgeted revenue and expenses.* Selectboards and municipal managers must make employees aware that they are paying attention to the financial affairs of the municipality. Employees should be properly supervised and their work regularly reviewed. Reports should be regularly prepared and distributed, and managers should review any unusual issues with accounting staff. Employees are less likely to commit fraudulent activities if they think they might be caught. Selectboards and municipal managers should regularly review budgets and projections and compare actual results to expectations. An employee who commits a fraudulent act typically needs to manipulate the accounting records to hide the action. In many cases, a careful review of the accounts will expose that kind of activity.

Question A.6 Response Notes:

Question A.7: Are municipal officials bonded or covered by liability insurance?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question A.7: *Elected officials and employees who handle municipal funds should be appropriately bonded or covered by liability insurance to ensure that the taxpayers do not absorb the cost of embezzlement if it does occur.*

Question A.7 Response Notes:

Question A.8: Are financial and accounting duties segregated so that no individual is able to perform all related elements of a financial transaction?	Yes ☐	No ☐	Unsure ☐
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Question A.9: Are all employees encouraged to take annual vacations, and are their accounting functions performed by other employees when they are on vacation?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions A.8 and A.9: *Although not required by law, it is best practice to segregate duties so that no single individual performs all related elements of an individual transaction.* Officials and employees who have responsibility for keeping records of municipal finances should not also be the same individuals who have custody of its assets. Personnel who are involved in the accounting function should be encouraged to take annual vacations, and other employees should perform their functions in their absence. Routine cross training among positions will facilitate this process. It is often when someone else performs an accounting function that an incidence of fraud is discovered.

Questions A.8 and A9 Response Notes:

B. CONTROLS OVER FINANCIAL RECORDS

Question B.1: Have the selectboard and treasurer jointly adopted an accounting, auditing, and financial reporting policy such as the VLCT Model Policy?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question B.1: *An accounting, auditing, and financial reporting policy sets the tone for fulfilling the selectboard's stewardship role over municipal finances. Every town should aspire to establish and maintain high standards for its accounting practices.* Such standards inspire confidence in the financial information produced and presented to voters. They enable the voters, selectboard, and other officials to make sound decisions in preparing and adopting the town budget and managing town finances.

Although the elected treasurer technically has authority to adopt his or her own policies, VLCT strongly recommends the joint adoption of one single policy by the treasurer and selectboard since each bear some responsibility over the management and reporting of the town's finances.

Question B.1 Response Notes:

Question B.2: Does the treasurer have written documentation of the accounting procedures used by the treasurer, the assistant treasurer, and financial or accounting staff?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question B.2: *Municipalities should maintain written documentation regarding accounting procedures and allows for accurate recording of financial transactions.*

Any systems that are put in place should allow easy retrieval of data for analysis, and generation of timely reports to maintain accountability for the assets of the municipality. The system should include detailed cash receipts and cash disbursements journals, as well as a detailed general ledger and subsidiary ledgers where appropriate. The system should also require that subsidiary ledgers (a detailed list of outstanding taxes receivable, for example) should be regularly reconciled with the general ledger to ensure that transactions were recorded properly and that all transactions have been included.

Question B.2 Response Notes:

Question B.3: Does the treasurer have a useful and descriptive chart of accounts?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question B.3: *The use of a chart of accounts is recommended as a best practice in financial management and accounting.* A chart of accounts is a listing of the names of the accounts that a company has identified and made available for recording transactions in its general ledger. The chart is usually sorted in order by account number, to ease the task of locating specific accounts. The accounts are usually numeric, but can also be alphabetic or alphanumeric. The chart of accounts organizes financial information so that financial reports are organized and easier to read. The use of a descriptive chart of accounts (a chart that assigns a unique number to each type of transaction) will provide a system for recording revenues and expenditures that fits the organizational structure of the municipality.

Question B.3 Response Notes:

Question B.4. Does the municipality maintain its financial records using a computerized accounting system?	Yes ☐	No ☐	Unsure ☐
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Question B.5. Does the accounting system allow for timely recording of financial transactions, easy viewing of transaction data, and timely creation of financial reports?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions B.4 and B.5: *The use of a computerized accounting system is recommended as a best practice in financial management and accounting.* A computerized accounting system makes financial operations faster and more accurate and allows for the automatic generation of financial reports. Perhaps most importantly, the use of a computerized accounting system allows officials to see the real-time state of the municipality's financial position.

Questions B.4 and B.5 Response Notes:

Question B.6. Are detailed cash receipts journals and cash disbursements journals maintained?	Yes ☐	No ☐	Unsure ☐
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Question B.7. Are subsidiary ledgers (e.g., taxes receivable, accounts payable) regularly reconciled with the general ledger?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions B.6 and B.7: *It is best practice for a municipality to maintain detailed cash receipts journals, cash disbursements journals, and subsidiary ledgers (a detailed list of outstanding taxes receivable, for example) which are regularly reconciled with the general ledger to ensure that transactions were recorded properly and that all transactions have been included.*

Questions B.6 and B.7 Response Notes:

Question B.8: Are account reconciliations and account analysis regularly performed and reviewed by a knowledgeable person other than the preparer?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question B.8: *Although not required by law, it is best practice to segregate duties so that no single individual performs all related elements of an individual transaction. No individual should be able to (a) authorize a transaction, (b) record the transaction in the accounting records, and (c) maintain custody of the assets resulting from the transaction.* For example, individuals responsible for the data entry of accounts payable should not be able to authorize transactions. For a small town with a limited number of staff, this will require that those staff persons alternate certain duties to ensure that there is a second set of eyes for each type of transaction. For towns without any staff, this will require that the treasurer allow for another town official to assist with recording or reconciling financial transactions.

Bank reconciliations should be performed by someone who is not involved in the cash receipt or cash disbursement process. For instance, reconciliation may be carried out by an assistant treasurer, if there is one, a hired bookkeeper, or another town official. Reconciliations should be prepared on a timely basis,

preferably immediately on receipt. A responsible and knowledgeable official other than the preparer should review the completed bank reconciliation.

In addition to the bank reconciliation, other reconciliation procedures should be performed monthly. Regularly reconcile accounts receivable balances to the original invoices and receipts and accounts payable balances with actual invoices. Reconcile payroll withholdings with payroll reports and invoices for benefits, and reconcile property tax receivable balances with property tax bills. These reconciliations will indicate if the subsidiary information contains errors or irregularities.

Question B.8 Response Notes:

Question B.9. Are all adjusting journal entries approved in writing by someone in management?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question B. 9: *It is best practice to have adjusting journal entries reviewed and authorized by someone other than the person making the entries.* An "adjusting journal entry" is an accounting term referring to an entry made to correct an account or to book other transactions to the general ledger, usually at the end of a period (month or quarter). An example of an adjusting journal entry would be a reclassification of an expense that was incorrectly coded when the payment was initially booked. Such entries should be reviewed to reduce the risk of fraudulent or incorrect entries being booked.

Question B.9 Response Notes:

Question B.10. Are financial recording documents (checks, receipts, purchase orders) prepared in duplicate and pre-numbered?	Yes ☐	No ☐	Unsure ☐
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Question B.11. Are all checks, receipts, and purchase orders regularly accounted for as issued or voided?	Yes	No	Unsure
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Question B.12. Are all accounting records adequately protected against fire, theft and manipulation?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions B.10, B.11, and B.12: *All financial recording documents should be prepared, used, and stored in a way that prevents misuse and allows for clear tracking and safekeeping.*

Documents such as checks, receipts, and purchase orders should be pre-numbered, and all forms should be accounted for. Receipts should be issued in duplicate for all cash transactions and a copy of each

receipt should be maintained by the municipality. Checks that are voided should be retained rather than destroyed. Accounting records should be safeguarded against fire, theft, and manipulation. Records should remain on town property, preferably in a safe or vault.

Questions B.10, B.11 and B.12 Response Notes:

C. CONTROLS OVER CASH

"Cash" includes all items that are acceptable for deposit in a bank, such a paper money, coins, checks, and money orders.

Question C.1: Have the selectboard, treasurer and tax collector(s) jointly adopted a cash receipts policy such as the VLCT Model Policy?	Yes ☐	No ☐	Unsure ☐
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Question C. 2: Has the selectboard specified which of their employees and appointees have authority to accept payments on behalf of the town?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions C.1 and C.2: *The selectboard, treasurer, and tax collector(s) should establish adequate processes for safeguarding cash that is received.* Although the elected treasurer and tax collector(s) technically have authority to adopt their own policies, VLCT strongly recommends the joint adoption of one single cash receipt policy by all officials who handle cash. A cash receipt policy should specify at least the following:

- which officials and employees are authorized to accept payments on behalf of the municipality;
- written receipts are prepared in duplicate for all transactions;
- all funds collected by persons other than the treasurer must be remitted to the treasurer promptly;
- no expenditures are made from cash collected;
- checks are restrictively endorsed ("for deposit only") immediately upon receipt;
- cash is physically safeguarded until deposit;
- deposits are made on a timely basis; and
- checks that are received are not cashed but are deposited intact.

Questions C.1 and C.2 Response Notes:

Question C.3: Does the municipality use a pooled cash account (one bank account) for most receipts?	Yes ☐	No ☐	Unsure ☐
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Question C.4: Does the municipality allocate monthly interest to the various funds using the pooled cash account? (If the municipality pools its cash, is interest being allocated to various funds that are using that pooled cash account in the accounting records?)	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions C.3 and C.4: *If a pooled cash account is used, monthly interest should be allocated to the various funds using the pooled cash account.* In addition, interfund transactions should be reconciled on a regular basis to insure that payables and receivables between funds are accurate and match known transactions.

Questions C.3 and C.4 Response Notes:

Question C.5: Are bank accounts covered by FDIC insurance or otherwise collateralized?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question C.5: *All bank accounts should be covered by FDIC insurance or otherwise collateralized.*

Question C.5 Response Notes:

Question C.6: Are receipts issued in duplicate for all cash transactions?	Yes ☐	No ☐	Unsure ☐
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Question C.7: Are duplicate receipts compared to cash journals during the reconciliation process?	Yes ☐	No ☐	Unsure ☐
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Question C.8: Are receipts recorded in the accounting system in a timely manner?	Yes ☐	No ☐	Unsure ☐
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Question C.9: Are copies of receipts turned over to the treasurer daily and recorded in the accounting system in a timely manner?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions C.6, C.7, C.8, and C.9: *Receipts should be issued in duplicate for all cash transactions and should be compared to cash journals during the reconciliation process. Copies of receipts should be turned over to the treasurer daily and receipts should be recorded in the accounting system in a timely manner.*

Questions C.6, C.7, C.8, and C.9 Response Notes:

Question C.10. When funds are received by municipal officials are they deposited (rather than being cashed) and if so, are they deposited intact (without taking funds out for other purposes)?	Yes ☐	No ☐	Unsure ☐
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Question C.11: Are checks restrictively endorsed upon receipt (stamped with "for deposit only")?	Yes ☐	No ☐	Unsure ☐
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Question C.12: When funds cannot be deposited daily are they securely stored?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions C.10, C.11, and C.12: *Checks should be restrictively endorsed upon receipt and deposited daily or stored secured until they can be deposited.* Checks should never be cashed and cash should never be disbursed before being deposited.

Questions C.10, C.11, and C.12 Response Notes:

Question C.13: Does the same employee accept funds, document or deposit them, and record the activity in the accounts?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question C.13: *Every municipality should establish and maintain a segregation of duties that will promote accuracy and limit opportunities to commit fraud.* Persons involved in purchasing and receipt of goods should be different municipal officials or staff members than those involved in the payment of invoices.

Question C.13 Response Notes:

Question C.14: Is petty cash controlled through an imprest petty cash system?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question C.14: *Petty cash should be handled on an imprest system.* An imprest system requires that the general ledger account "Petty Cash" will remain dormant at a set amount. For example, if the petty cash custodian is entrusted with a locking bag containing \$50 of currency and coins, then the Petty Cash account will always report a debit balance of \$50. This \$50 is the "imprest balance." As long as \$50 is adequate for the town's small disbursements, then the general ledger account Petty Cash will never have an entry again. Under the imprest system, the petty cash custodian should at all times have a combination of coins, currency, and petty cash receipts equal to \$50, the imprest amount.

Question C.14 Response Notes:

D. CONTROLS OVER ACCOUNTS RECEIVABLE AND COLLECTIONS

Question D.1: Have the selectboard, treasurer, and tax collector(s) established adequate processes for collecting and recording accounts receivable?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question D.1: *The selectboard, treasurer, and tax collector(s) should establish adequate processes for collecting and recording accounts receivable.* Although the elected treasurer and tax collector(s) technically have authority to adopt their own policies, VLCT strongly recommends the joint adoption of policies by municipal officials.

Question D.1 Response Notes:

Question D.2: Is the accounts receivable system capable of preparing an aged listing of outstanding accounts receivable?	Yes ☐	No ☐	Unsure ☐
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Question D.3: Are invoices prepared by various town departments forwarded to the treasurer or finance office for entry into the accounts receivable ledger?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions D.2 and D.3: *Invoices that are prepared by various town departments should be forwarded to the treasurer or finance office for entry into the accounts receivable ledger so that action can be taken on unpaid balances.*

Questions D.2 and D.3 Response Notes:

Question D.4: Are all accounts receivable recorded in the general ledger?	Yes ☐	No ☐	Unsure ☐
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Question D.5: Are subsidiary ledgers reconciled to the general ledger control account on a regular basis?	Yes ☐	No ☐	Unsure ☐
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Question D.6: Are accounts receivable reconciled to detailed invoices and receipts on a regular basis?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions D.4, D.5, and D.6:

All receivables (taxes, utility charges, other miscellaneous receivables) should be recorded in the general ledger. Subsidiary ledgers should be reconciled to the general ledger control account on a regular basis.

Questions D.4, D.5, and D.6 Response Notes:

Question D. 7: Are billing, collection and posting performed by separate employees or departments?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question D.7: Every municipality should establish and maintain a segregation of duties that will ensure that account balances are accurate and that opportunities to commit fraud are limited.

Duties involving billing, collection and posting should be performed by separate employees or departments.

Question D.7 Response Notes:

Question D.8: Are penalties and interest assessed on overdue taxes and water and sewer charges as allowed by law?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question D.8: The assessment of penalties and interest on overdue taxes is controlled by 32 V.S.A. §§ 1674, 4873, and 5136. The assessment of penalties and interest on overdue water and sewer charges is controlled by 24 V.S.A. § 5151, and 32 V.S.A. § 5136.

Question D.8 Response Notes:

Question D.9: Do taxpayers or ratepayers receive regular statements for outstanding balances due or overpayments (other than taxes)?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question D.9: *Although not required by law, sending periodic statements to all customer accounts showing any unpaid amounts as well as recent payments is recommended as a method to encourage payment and assist in such collections.*

Question D.9 Response Notes:

Question D. 10: Has the Collector of Delinquent Taxes adopted a policy regarding the collection of delinquent taxes?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question D.10: *Although not required by law, it is advisable for the Collector of Delinquent Taxes to adopt and follow a policy regarding the collection of delinquent taxes.* Neither the selectboard nor any other municipal official have authority to approve or disapprove of such policy. However, it is advisable for the delinquent tax collector to present the policy to the members of the selectboard so that they understand and support it.

Questions D.10 Response Notes:

Question D.11: Does the Collector of Delinquent Taxes send regular notices of delinquent taxes?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question D.11: *Although not required by law, sending regular notices of delinquent amounts may encourage payment and assist in such collections.*

Questions D.11 Response Notes:

Question D.12: Are penalties and interest assessed on overdue accounts (other than taxes and water and sewer charges) as allowed by law?	Yes ☐	No ☐	Unsure ☐
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Question D.13: Does the municipality have a written policy regarding adding penalties and interest to delinquent accounts (other than taxes and water and sewer)?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions D.12 and D.13: *It is best practice to have a written policy regarding the assessment of penalties and interest to delinquent accounts (other than taxes and water and sewer) to provide clarity and predictability, and protect the municipality from allegations of discriminatory assessment.*

Questions D.12 and D.13 Response Notes:

Question D.14: Does the municipality have a policy regarding writing off delinquent accounts (other than taxes and water and sewer)?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question D.14: *A written policy regarding the forgiveness of delinquent accounts (other than taxes and water and sewer) provides clarity and predictability, and protects the municipality from allegations of discriminatory assessment.* Note that delinquent taxes, and water and sewer charges may only be abated by the local Board of Abatement after a hearing.

Question D.14 Response Notes:

E. CONTROLS OVER PURCHASING AND DISBURSEMENTS

Question E. 1: Has the selectboard adopted a purchasing policy that includes a conflict of interest provision such as the VLCT model policy?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question E.1: *The selectboard should adopt and follow a policy that allows for the procurement of goods and services in an efficient, timely, and cost-effective manner, and encourages*

the most open, competitive purchasing process practicable to acquire these goods and services at the best possible value. Such policy should describe the lines of authority for approving purchases and indicates when to use competitive bidding. No one person should be involved in the purchasing, receiving, and payment functions.

If the municipality does not already have a separate conflict of interest policy, it is important for the purchasing policy to address the conflicts of interest that may arise in the context of municipal purchasing and contracting. At a minimum, the policy should define a procedure for public disclosure of the potential conflict and the level of participation permitted when discussion or voting related to the purchase of an item where the conflict exists takes place. It is not uncommon for a board member or the family member of a board member to own a local business that supplies materials and/or services to a municipality. In such instances, however, the board member should not be involved in the selection, award, or administration of the purchase or contract.

Question E.1 Response Notes:

Question E.2: Are the functions of purchasing, receipt of goods, and payment of invoices performed by different municipal officials or staff members?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question E.2: Every municipality should establish and maintain a segregation of duties that will ensure that purchasing and payment are carried out accurately and that opportunities to commit fraud are limited. Persons involved in purchasing and receipt of goods should be different municipal officials or staff members than those involved in the payment of invoices.

Question E.2 Response Notes:

Question E.3: Does the municipality maintain an approved vendors list and perform procedures to detect fictitious vendors?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question E.3: Every municipality should employ procedures to detect fictitious vendors and prevent duplicate payment of invoices. The procedures should include tax identification number matching on the IRS website to assure that each company or individual you are paying has a legitimate tax ID number. There should also be regular review of vendors to detect any suspicious activity.

Question E.3 Response Notes:

Question E.4: Does the municipality use purchase orders?	Yes ☐	No ☐	Unsure ☐
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Question E.5: Are all expenditures supported by original invoices and other related supporting documentation?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions E.4 and E.5: *The municipality's purchasing policy should mandate the use of a purchase order system to document purchasing details and demonstrate that policies were adhered to. A copy of every purchase order and all receiving documents for payment should be maintained in the municipal files.*

Questions E.4 and E.5 Response Notes:

Question E.6: Are orders drawn on the treasurer prepared for all purchases and approved in writing by the appropriate elected official or specifically authorized employees before payment is made?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question E.6: *All invoices must be approved by the appropriate authority before payment is made by the treasurer.* In most cases, the appropriate authority is the selectboard (or other legislative body). The selectboard may delegate some purchasing authority to other municipal officials, although this delegation should be documented in the municipality's written purchasing policy.

Question E.6 Response Notes:

Question E.7: Are all disbursements, except for small petty cash items, made by check or direct deposit?	Yes ☐	No ☐	Unsure ☐
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Question E.8: Are checks produced using an automated accounting system?	Yes ☐	No ☐	Unsure ☐
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Question E.9: Are checks pre-numbered and used consecutively?	Yes ☐	No ☐	Unsure ☐
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Question E.10: Are unused checks controlled and adequately protected from misuse or theft?	Yes ☐	No ☐	Unsure ☐
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Question E.11: Are voided checks accounted for?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions E.7, E.8, E.9, E.10, and E.11: All disbursements, except for occasional small petty cash items, should be made by check or direct deposit transactions. Checks should be pre-numbered, unused checks should be stored in a secure location, unused checks controlled and adequately protected from misuse or theft, and voided checks accounted for. Checks should be made payable to a specific individual, never to “cash.”

Questions E.7, E.8, E.9, E.10 and E.11 Response Notes:

Question E.12: Are checks prepared by a separate person from the signer?	Yes ☐	No ☐	Unsure ☐
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Question E.13: Are duties segregated so that the person who writes checks does not also open the bank statements?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions E.12 and E.13: *Every municipality should establish and maintain a segregation of duties that will ensure that payment functions and account reconciliation are carried out accurately and that opportunities to commit fraud are limited.* Persons involved in writing checks should be not be involved in the reconciliation of accounts.

Questions E.12 and E.13 Response Notes:

F. CONTROLS OVER PAYROLL

Question F.1: Has the selectboard established and maintained adequate systems for ensuring accuracy and oversight over payroll?	Yes ☐	No ☐	Unsure ☐
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Question F.2: Does the selectboard or town manager maintain personnel records for all employees that include hiring and compensation information and authorization for all deductions?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions F.1 and F.2: *The selectboard should establish and maintain adequate systems for ensuring accuracy and oversight over payroll.* A personnel file should be maintained for each employee that includes hiring and compensation information and authorization for all deductions taken. The selectboard should annually adopt salary and wage information for all employees.

Questions F.1 and F.2 Response Notes:

Question F.3: Does the municipality have a personnel policy that addresses benefits and the accumulation and use of leave time?	Yes ☐	No ☐	Unsure ☐
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Question F.4: Does the municipality have accurate records of accumulated leave balances of employees?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions F.3 and F.4: *The selectboard should adopt written policies regarding leave time and benefits. Adequate records should be maintained to document the accumulation and use of leave time.*

Questions F.3 and F.4 Response Notes:

Question F.5: Are salary and wage rates approved by the selectboard?	Yes ☐	No ☐	Unsure ☐
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Question F.6: Are withholding taxes remitted promptly?	Yes ☐	No ☐	Unsure ☐
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Question F.7: Are payroll withholdings reconciled to payroll reports?	Yes ☐	No ☐	Unsure ☐
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Question F.8: Are fees paid to elected officials disclosed in the municipality's accounting records and reported to the IRS?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions F.5, F.6, F.7, and F.8: *Salary and wage rates should be approved by the selectboard. Withholding taxes should be remitted promptly, payroll withholdings should be reconciled to payroll reports, and fees paid to elected officials disclosed in the municipality's accounting records and reported to the IRS.*

Questions F.5, F.6, F.7 and F.8 Response Notes:

Question F.9: Are payroll changes authorized by someone who does not process payroll?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question F.9: *Every municipality should establish and maintain a segregation of duties that will ensure that payroll additions, removals, or changes should be authorized by someone other than the employee who processes payroll.*

Question F.9 Response Notes:

Question F.10: Is direct deposit used for payment of net pay (where authorized by law)?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question F.10: *Where allowed by 21 V.S.A. § 342 (i.e. where there is a prior agreement between the municipality and the employee or a personnel policy that addresses the issue) the municipality should use direct deposit for payment of net pay. This will help to prevent fraudulent payments.*

Questions F.10 Response Notes:

G. CONTROLS OVER THE GRAND LIST AND TAX RECORDS

Question G.1: Do the listers or assessor receive timely notice of all zoning permits that are issued?	Yes ☐	No ☐	Unsure ☐
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Question G.2: Do the listers or assessor receive timely notice from the board of civil authority, Vermont Tax Department or Superior Court regarding decisions that affect tax assessments?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions G.1 and G.2: *Municipal officials should establish and maintain adequate processes to ensure that the grand list and records of the listers are accurate and up-to-date.* A system should be in place to make certain that the listers or assessor receive prompt notice of zoning permits and land use decisions that affect the valuation of taxable property. Other systems should assure that the listers or assessor receive prompt notice of decisions from the board of civil authority, Vermont Tax Department, or Superior Court that relate to valuation of property.

Questions G.1 and G.2 Response Notes:

Question G.3: Have the selectboard, treasurer, and tax collector(s) established adequate processes for collecting and recording tax payments?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question G.3: *The selectboard, treasurer, and tax collector(s) should establish adequate processes for collecting and recording taxes.* As stated above, although the elected treasurer and tax collector(s) technically have authority to adopt their own policies, VLCT strongly recommends the joint adoption of policies and procedures by municipal officials.

Questions G.3 Response Notes:

Question G.4: Are decisions of the board of abatement regarding the abatement of taxes communicated to the treasurer and collector(s) of taxes in a timely manner?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question G.4: A system should be in place to make certain that the treasurer and tax collector(s) receive timely notice of decisions of the board of abatement regarding the abatement of taxes and that those adjustments are made to the appropriate tax accounts upon notification.

Question G.4 Response Notes

Question G.5: Are receipts issued in duplicate for all tax payments that are received?	Yes ☐	No ☐	Unsure ☐
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Question G.6: Are checks received for the payment of taxes restrictively endorsed upon receipt ("for deposit only by the town of ___")?	Yes ☐	No ☐	Unsure ☐
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Question G.7: Are cash receipts for tax payments deposited daily to a financial institution or retained in a secure location until they can be deposited?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions G.5, G.6, and G.7:

Paper receipts should be issued in duplicate for all tax payments that are received. Checks should be restrictively endorsed upon receipt and all funds received for tax payments should be deposited daily to a financial institution or retained in a secure location until they can be deposited.

Questions G.5, G.6 and G.7 Response Notes:

Question G.8: Are tax receipts reconciled to tax receivables, and are tax receivables reconciled to the grand list on a regular basis by someone other than the collector of taxes?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question G8: *Tax receipts and billing should be reconciled to tax receivables, and tax receivables reconciled to the grand list on a regular basis. Where possible, an individual other than the tax collector (current and/or delinquent) should reconcile taxes.*

Question G.8 Response Notes:

H. CONTROLS OVER MUNICIPAL PROPERTY AND EQUIPMENT

Question H.1: Are capital asset schedules maintained for municipal property and equipment?	Yes ☐	No ☐	Unsure ☐
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Question H.2: Are periodic inventories taken and compared with such schedules?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions H.1 and H.2: *The selectboard should establish and maintain adequate systems and processes to ensure that asset schedules are accurate and inventory is secure.* They should see that capital asset schedules are prepared so as to maintain control over significant assets and conduct and compare periodic inventories with the capital assets schedule.

Questions H.1 and H.2 Response Notes:

Question H.3: Is all property and equipment properly secured?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question H.3: *Proper security – such as locks and the use of security cameras and alarm systems – should be maintained over all property and equipment as necessary.*

Question H.3 Response Notes:

Question H.4: Is insurance coverage reviewed regularly to determine its adequacy?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question H.4: *The selectboard should periodically review insurance coverage to determine its adequacy, consulting with insurance providers as necessary.*

Question H.4 Response Notes:

I. CONTROLS OVER INFORMATION SYSTEMS

Question I.1: Is access to financial information limited to those who specifically require access?	Yes ☐	No ☐	Unsure ☐
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Question I.2: Is access to financial information protected by the use of passwords that are regularly changed?	Yes ☐	No ☐	Unsure ☐
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Guidance for Questions I.1 and I.2: *The selectboard and other officials with control over financial information should establish and maintain adequate systems and processes to ensure that financial data is secure.* To prevent accidental or intentional changes to data, access to financial records should be limited to those who require specific access. Passwords should be used to protect all financial information and those passwords should be changed regularly and not shared with other officials or employees.

Questions I.1 and I.2 Response Notes:

Question I.3: Are computer records regularly backed up, and are back up copies stored off site?	Yes ☐	No ☐	Unsure ☐
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Guidance for Question I.3: *Financial computer records should be backed up daily, and the back-up copies should be stored off-site in different secure locations.*

Question I.3 Response Notes:

This Internal Controls Checklist was completed by:

Name

Date

Supporting Documents

The documents listed below are referenced in the checklist. It may be helpful to gather them (if applicable in your municipality) before starting to work on the checklist.

Municipal Policies

Financial Reporting

Purchasing

Cash Receipts

Fraud Prevention

Personnel

Delinquent Tax Collection

Conflict of Interest

Other Resources

Audit Report

Accounting Procedures

Chart of Accounts

Vendor List