

# CPAs for NGOs

## Social Responsibility Programme

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Quick Guide Series



# Internal Control and Audit



Hong Kong Institute of  
Certified Public Accountants  
香港會計師公會

## Introduction

The Hong Kong Institute of CPAs has organized a series of “CPAs for NGOs” seminars to help local small- and medium-sized social service / non-governmental organizations improve their financial management and reporting, budget planning, internal control, and governance. Highlights of these seminars are captured in a series of quick guides designed to facilitate the implementation of best practices in your organization. For a full set of presentation slides, please go to [www.hkicpa.org.hk/CPAforNGO](http://www.hkicpa.org.hk/CPAforNGO).

## What are the common practices of internal control?

### • *Budgeting*

- Set up clear roles and responsibilities, announce the details and brief the responsible managers
- Document the basis and assumptions of budget and retain source documents for review
- Establish a review and follow-up mechanism
- Assign a budget and account code during purchase requisition which should be reviewed by relevant budget controller
- The code should be used throughout the entire accounting record process

### • *Procurement to payment*

- Emphasize staff stability for more routine reviews and leverage on specific knowledge or skills of professional firms for special projects
- Assessment panel/board should be responsible to review high value purchases
- Document justification for specific brand or sole supplier of valuable assets for independent review
- Review approved vendor list or bring in new vendors for selection
- Obtain pricing information from the market for sole vendor purchases
- Vetting criteria should be pre-set with weighting of each assessment criterion
- Apply two-envelope system for tendering
- Raising purchase order - Make it a rule for term contracts and bulk purchases for frequently purchased items
- Only accept original invoice for payment processing
- Approver’s payment request should be approved by an independent person
- Introduce vendor performance evaluation mechanism and suspend vendors with poor performance from future bidding for a period or remove from the vendor list

- **Cash management**

- Conduct ad hoc /surprise cash count by independent person
- Separate custody of cash and account recording
- Set time limit for claims of petty cash reimbursement or cash advance
- Reimbursement only upon submission of original invoice or receipt; Claim form should be signed by the responsible staff and the supervisor
- Auto-payment should be avoided
- Prior to payment by corporate credit card, itemized payment request form with original invoice should be prepared for the supervisor of the credit card holder to review and approve and then provided to finance team for checking
- Board resolution should cover all payment types including online banking
- Password and security token for online banking should not be shared with personnel who are not responsible for payment approval

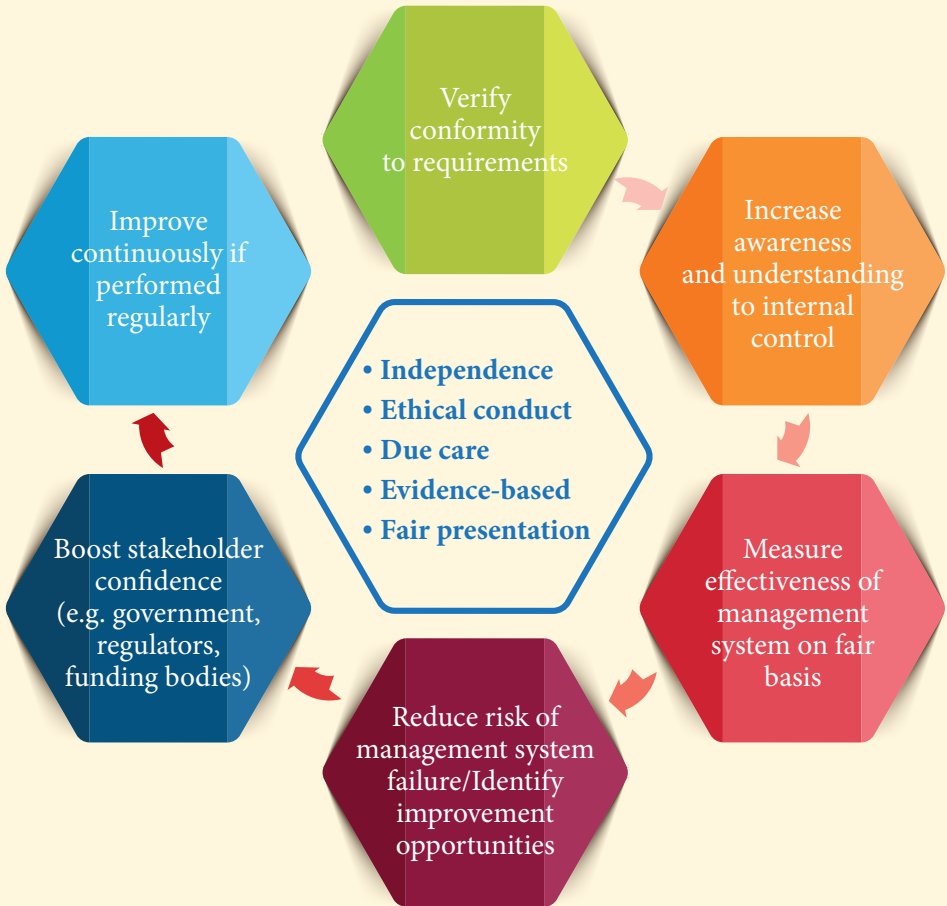
- **Financial close and reporting**

- Management should perform monthly reconciliation such as bank reconciliation and accounts receivable
- Financial statement close checklist and timetable should be designed to reflect:
  - ✓ Clear roles and responsibilities of involved parties
  - ✓ Company reporting timelines
  - ✓ Month-end closing activity level for daily monitoring
  - ✓ Documentation required to support management control and review

## **Why implement internal audit?**

- To serve as an independent appraisal function established by management
- To review the organization's internal control system
- To objectively examine, evaluate and report on the adequacy of internal control
- To monitor the proper, economic, efficient and effective use of the organization's resources

## What are the principles and values of internal audit?



## What types of internal audit are there?

- **Compliance audit**  
Assess the risk of non-compliance against the applicable rules, regulations and laws
- **Operational/performance audit**  
Assess the efficiency and effectiveness of operations and/or use of resources in achieving the organization's objectives
- **Information system audit**  
Assess controls of the information system throughout the entire business life cycle
- **Special assignment audit**  
Related to fraud, corruption investigations or other special services

## Which internal audit model to take?

- **Outsource (e.g. public sector)**
  - Benefit from the industry trend analysis or insights provided by the team outsourced to
  - Enjoy the flexibility of professional firms with worldwide resources
  - More cost-effective in terms of recruitment and training
- **Co-source (e.g. multinational companies with regional office based in Hong Kong)**
  - Emphasize staff stability for more routine reviews
  - Leverage on specific knowledge or skills of professional firms in special projects
- **In-house (e.g. publicly listed companies)**
  - Operate mainly in extremely niche industries where knowledge is not available in the market so the company needs to develop and train its own internal control team
  - Conglomerate organization which has resources for building up a sizable internal audit team for knowledge retention within a complex group

## How to perform internal audit?



## Internal audit in a governance structure

### 1<sup>st</sup> line of defence

*Responsible unit*

**Frontline  
Operations  
Units**

*Major functions*

- Responsible for identifying and managing risks directly (design and operation of controls)
- Responsible for conducting day-to-day operations and controls

### 2<sup>nd</sup> line of defence

*Responsible unit*

**Senior  
Management**

*Major functions*

- Provide advice and facilitate risk management activities
- Review the design and operation of controls in the first line of defence

### 3<sup>rd</sup> line of defence

*Responsible unit*

**Board of  
Directors**

*Major functions*

- Oversee the operations of the company
- Perform independent review with the assistance of external and internal auditors
- Optimize risk management function

## Challenges and benefits for NGOs with internal audit functions

Area	Challenges in setting up an internal audit function	Benefits of a well-established internal audit function
<b>Organization culture</b>	✓ Stable management team	
	<ul style="list-style-type: none"> <li>- Conservative to changes</li> <li>- Strong resistance to internal audit activities</li> </ul>	<ul style="list-style-type: none"> <li>- More welcoming of innovative ideas</li> <li>- Familiar with internal audit approach</li> </ul>
<b>Internal control environment or system</b>	<ul style="list-style-type: none"> <li>- Remote support from governance team</li> <li>- Unclear tone at the top</li> <li>- More deficiencies within internal control system</li> </ul>	<ul style="list-style-type: none"> <li>- Effective support from the board</li> <li>- Clear tone at the top</li> <li>- Become mature after years of revolution</li> </ul>
<b>Area of focus</b>	<ul style="list-style-type: none"> <li>- Focusing on reputational risk, relationships with government, public, privacy issues</li> </ul>	
	<ul style="list-style-type: none"> <li>- More effort to promote internal control</li> </ul>	<ul style="list-style-type: none"> <li>- More effort in different audit approaches</li> </ul>

### Disclaimer:

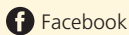
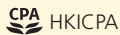
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### Hong Kong CPAs Making a Difference

The Hong Kong Institute of CPAs, the only statutory body for professional accountants in Hong Kong, takes its social responsibility seriously through mobilizing and empowering members to proactively and positively contribute to the development and well-being of the community with their professional skills, expertise and knowledge. “CPAs for NGOs” is one of the Institute’s core social responsibility projects. CPAs volunteer in various programme activities, including seminars, workshops and advisory sessions, to advise small- and medium-sized social service / non-governmental organizations on the best practices to strengthen their financial system and governance to achieve sustainable development.



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