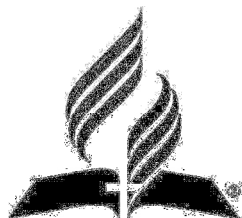


This document remains as a work-in-progress and is expected to be finalized and published at the upcoming 2011 GC Annual Council. Any use or distribution should keep this in mind.

General Conference of Seventh-day Adventists

# Transparency and Accountability in Financial Reporting

Our Global Leadership Commitment



SEVENTH-DAY  
ADVENTIST CHURCH

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*ADRA Audit Committee Chairperson*

## Executive Summary

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The Seventh-day Adventist Church and its family of institutions receive financial resources primarily in the form of tithe, offerings, donations, tuition, sales revenue and service fees. There is an expectation that every organization and their respective leaders will exercise proper stewardship for these financial resources. In the normal course of exercising proper stewardship an organization should regularly prepare and study financial statements based on the mission driven activities being pursued. To enhance the credibility of the financial statements, an annual financial audit is required to be performed by GCAS, or an approved external firm, so an opinion can be rendered on the fairness of the presentation.

When financial statements are prepared, studied, and audited they represent critical information to be used in making appropriate business decisions and holding leaders accountable for their stewardship. The controlling committee of an organization needs to make appropriate business decisions and risk analyses. The constituents of an organization need to hold leaders accountable. Committees and constituents can fulfill their role of governance only when they receive regular financial reports and require leaders to respond to issues identified in audit reports.

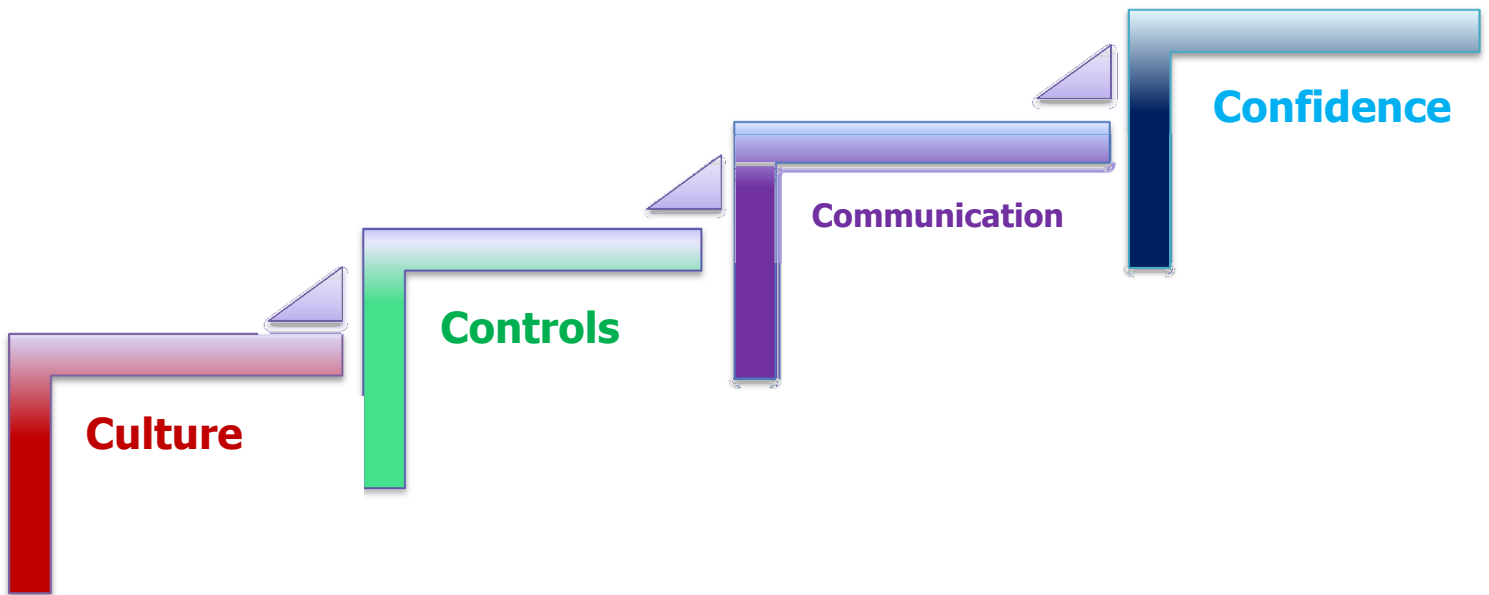
At the 2010 Annual Council of the General Conference Committee, GCAS presented a global annual report which included the frequency of certain audit findings and the recurring unresolved nature of those findings. In connection with this report, the GCAS Board expressed its concern regarding inadequacies related to transparency and accountability in financial reporting by many organizations in a letter to the General Conference Executive Officers. A consensus among Church leaders was reached to consider and implement a framework which would strengthen financial transparency and organizational accountability in the Seventh-day Adventist Church by including the following four recommendations made by the GCAS Board:

- Promote a culture of transparency and accountability that is modeled by Church leaders at every level of the denomination;
- Revise policies to incorporate best practices related to the receipt, response and resolution of issues identified in audit reports;
- Require the establishment of an Audit Committee for each denominational organization which is chaired by and includes persons not employed by the organization being audited; and
- Encourage denominational organizations to provide training to their respective boards and committees on how its members can effectively fulfill their governance role.

The continued flow of financial resources to the Seventh-day Adventist Church and its family of institutions in support of mission driven activities is largely dependent on the continued confidence of constituents and other stakeholders in organizational leaders and their stewardship. This document identifies organizational culture, organizational controls and organizational communication as being the key drivers for sustaining this confidence and the key disciplines to be expanded into a set of organizational policies.

# Confidence Matters!

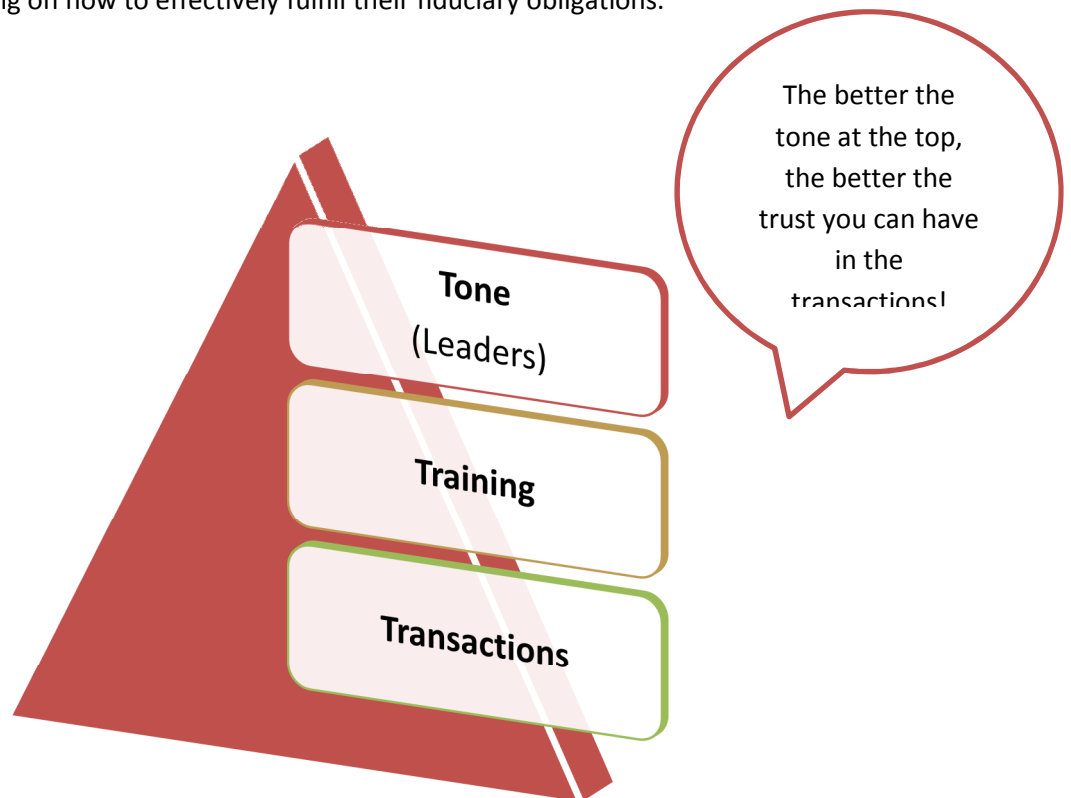
*Constituents and other stakeholders want to have confidence in organizational leaders and their stewardship*



## Organizational Culture

The Seventh-day Adventist Church and its family of institutions have unique organizational cultures which are a composite of individual attitudes and backgrounds. However, leaders in each organization are the persons who set the tone at the top of that culture as it relates to integrity, ethical values, stewardship and transparency. If leaders do not set an example in these areas there will be no moral compass to guide organizational decisions, and the behavior modeled by leaders will invariably be manifested in the actions of those whom they lead. As a Christian organization, there is a greater expectation for each person, but particularly leaders, to demonstrate exemplary behavior in transacting financial matters ensuring they conform to biblical principles, legal parameters, professional standards, and denominational policies.

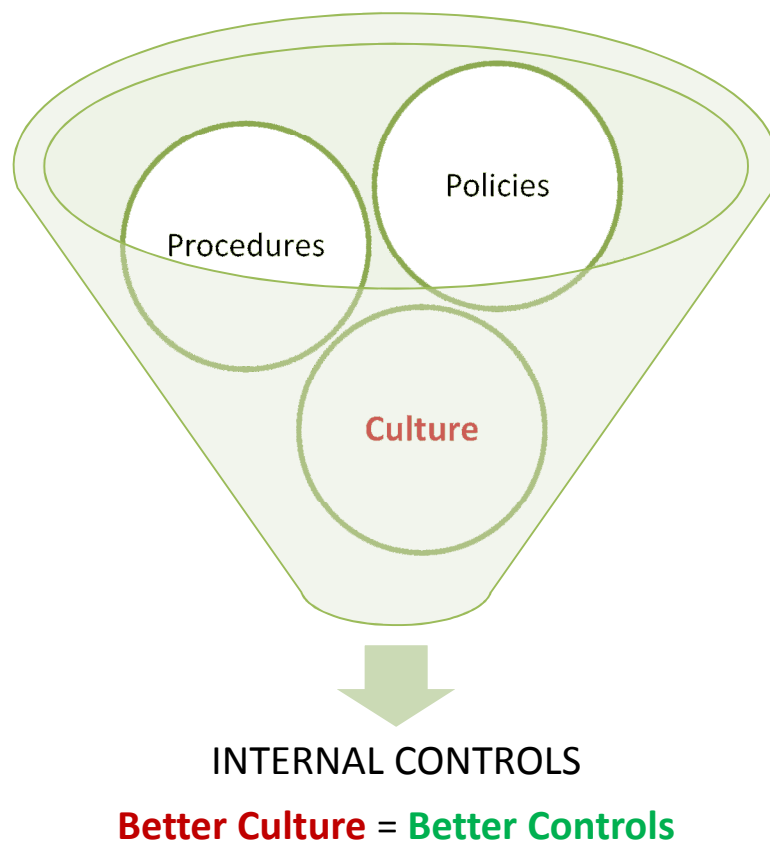
There is a principle that must be imbedded and instructive to any organizational culture within the Seventh-day Adventist Church and its family of institutions. This principle being that authority resides in groups more so than in individual office holders, and that controlling committees or boards are entrusted with the authority to govern. Regardless of the attitudes and backgrounds of the individuals who comprise each organization, there should be common evidence that the organizational culture promotes financial transparency and organizational accountability. As a demonstration of this evidence, officers of organizations must make themselves accountable to their respective controlling committee or board, persons serving on controlling committees or boards would function as trustees and be engaged in holding those officers accountable, and persons serving on controlling committees or boards would have access to training on how to effectively fulfill their fiduciary obligations.



## Organizational Controls

When the appropriate organizational culture is in place there is a greater appreciation for designing and implementing effective organizational controls. These controls consist of policies and procedures which collectively are referred to as **internal controls**. The internal controls of an organization should not be designed to target individuals but should focus on the objectives of providing reasonable assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with laws and regulations. The concept of reasonable assurance highlights the limitations that exist in designing internal controls for an organization. These limitations include the problem of cost versus benefit, possibility of collusion among employees, or the potential for management to override the same controls they were instrumental in designing. After taking all factors into consideration, these limitations should not provide an excuse for failing to design the best possible internal controls.

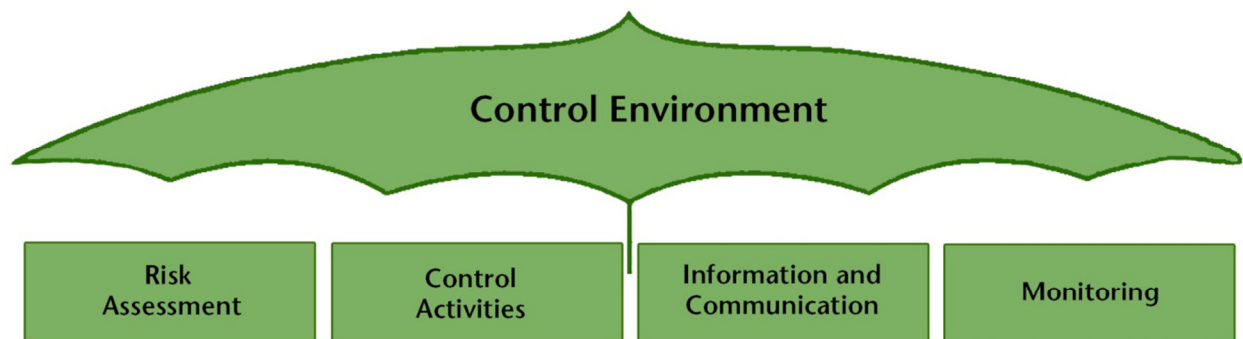
The Seventh-day Adventist Church and its family of institutions must each have internal controls which are designed, documented, implemented, communicated, and monitored by the highest level of governance in that organization. Part of an effective governance structure includes establishing an **audit committee** comprised of persons not employed by that organization.



## Components of Internal Control

Source: Auditing and Assurance Services 10<sup>th</sup> Edition, Alvin Arens | Randal Elder | Mark Beasley

Internal control includes five categories of controls that management designs and implements to provide reasonable assurance that management’s controls objectives will be met. These are called the components of internal control and are: (1) the control environment, (2) risk assessment, (3) control activities, (4) information and communication, and (5) monitoring. As the figure shows below, control environment is the umbrella for the four other components. Without an effective control environment, the other four other components are unlikely to result in effective internal control, regardless of their quality.



Components	Description of Component
<b>Control Environment</b>	Actions, policies and procedures that reflect the overall attitude of top management, directors and owners of an entity about internal controls and its importance
<b>Risk Assessment</b>	Management’s identification and analysis of risks relevant to the preparation of financial statements in accordance with the applicable financial reporting framework
<b>Control Activities</b>	Policies and procedures that management has established to meet its objectives for financial reporting including: adequate segregation of duties, proper authorization of transactions and activities, adequate documents and records, physical control over assets and records, and independent checks on performance
<b>Information and Communication</b>	Methods used to initiate, record, process and report and entity’s transactions and to maintain accountability of related assets
<b>Monitoring</b>	Management’s ongoing and periodic assessment of the quality of internal control performance to determine whether controls are operating as intended and are modified when needed

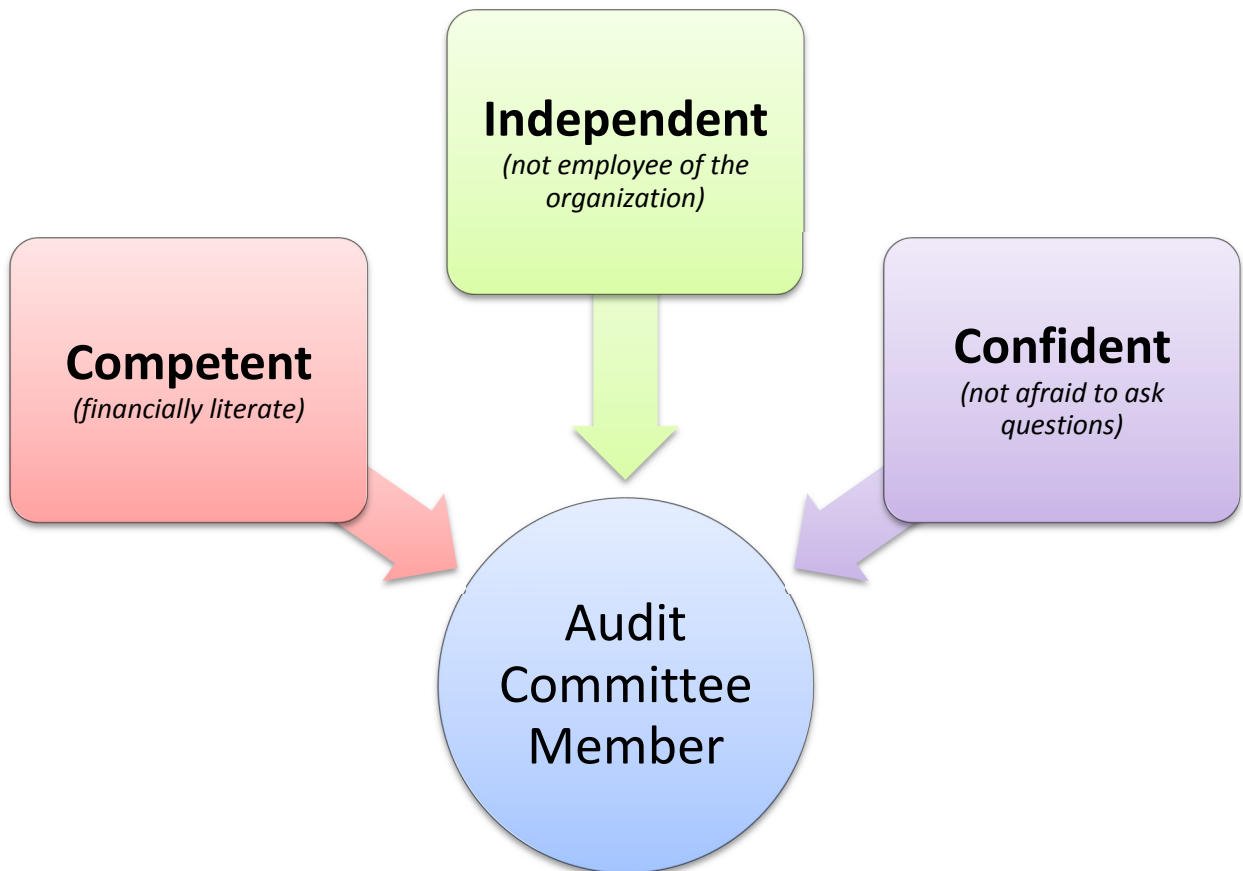
## Role and Function of an Audit Committee

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The audit committee operates under the authority and charter provided by an organization's controlling committee. This charter guides the operating activities of an audit committee and places on its members the responsibility for oversight of financial reporting and identification of related business risks. There are three core activities which define the breadth and scope of an audit committee:

1. Understand the risks related to the organization and its financial reporting
2. Oversee financial reporting processes for quality and reliability, including internal controls
3. Oversee audit activities with the internal and/or external auditor

An organization enhances credibility with constituents and other stakeholders when it establishes an audit committee that is proper in composition and proficient with the requirements of its charter. In selecting persons to serve as members on an audit committee there are three essential characteristics to ensure effectiveness:



## Organizational Communication

Communication is at the core of effective governance! The Seventh-day Adventist Church and its family of institutions should demonstrate their commitment to financial transparency and organizational accountability by embracing regular and open communication. This communication should take place within the organization and between the controlling committee, audit committee, GCAS/external auditor, constituents, other stakeholders, and next higher organization. It is important for communication channels to be open **inside** the organization and **outside** the organization with those involved in the governance process. Equally important, those involved in the governance process should have open communication with each other. A special emphasis should be placed on communicating with constituents and other stakeholders without any bias to the level or nature of their contribution. In designing any communication systems, it is critical to recognize the important role of constituents and other stakeholders to the continued viability of an organization by providing them with clear and complete communication.



## Communication Channels

Initiating Party	Nature of Communication	Receiving Party
<b>ORGANIZATION</b>	<ul style="list-style-type: none"> <li>• Provide monthly financial reports</li> <li>• Provide training on how to read and understand financial reports</li> </ul>	Controlling Committee (Executive Committee or Board)
	<ul style="list-style-type: none"> <li>• Address findings of the audit report</li> <li>• Respond to queries and recommendations related to internal control design and deficiencies</li> <li>• Respond to queries related to compliance with core policies</li> <li>• Respond to queries related to potential business risks</li> </ul>	Audit Committee
	<ul style="list-style-type: none"> <li>• Agree to terms of audit engagement</li> <li>• Provide responses and evidence to support assertions made regarding financial statement presentation and compliance with denominational policies</li> <li>• Receive an audit report along with any findings and recommendations</li> </ul>	GCAS/External Auditor
	<ul style="list-style-type: none"> <li>• Respond to queries related to the audit report received from GCAS/External Auditor</li> </ul>	Constituents and other Stakeholders
	<ul style="list-style-type: none"> <li>• Respond to queries regarding the audit reports received and stakeholder concerns received</li> </ul>	Next Higher Organization
<b>GCAS/External Auditor</b>	<ul style="list-style-type: none"> <li>• Provide an auditor's opinion</li> <li>• Provide a report on compliance with core policies</li> <li>• Provide an audit communication letter identifying significant deficiencies in internal controls</li> </ul>	Audit Committee & Controlling Committee (Executive Committee or Board)
	<ul style="list-style-type: none"> <li>• Provide a copy of the audit report along with a response from the organization</li> </ul>	Constituents and other Stakeholders
	<ul style="list-style-type: none"> <li>• Provide a copy of the audit report along with a response from the organization</li> </ul>	Next Higher Organization
<b>Audit Committee</b>	<ul style="list-style-type: none"> <li>• Present report regarding the results of the audit engagement</li> <li>• Present report regarding operational effectiveness of internal controls</li> <li>• Present report regarding compliance with core policies</li> <li>• Present report on potential business risks</li> </ul>	Controlling Committee (Executive Committee or Board)
	<ul style="list-style-type: none"> <li>• Present a report confirming the expectations enumerated in the charter have been met</li> </ul>	Next Higher Organization

# Let's Talk

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As a church leader, how can I promote as well as model transparency and accountability?



What policies, practices, procedures, or structures would you recommend to support transparency and accountability in our Church organizations?

## Quotations

“Therefore, since it is by God's mercy that we are engaged in this ministry, we do not lose heart. We have renounced the shameful things that one hides; we refuse to practice cunning or to falsify God's word; but by the open statement of the truth we commend ourselves to the conscience of everyone in the sight of God.”

**2 Corinthians 4:1-2.**

“The greatest want of the world is the want of men [*persons*] – *persons* who will not be bought or sold, *persons* who in their inmost souls are true and honest, *persons* who do not fear to call sin by its right name, *persons* whose conscience is as true to duty as the needle to the pole, *persons* who will stand for the right though the heavens fall.”

**Ellen G White – Education p. 57**

*“In every action of life the true Christian is just what he desires those around him to think he is. He is guided by truth and uprightness. He does not scheme; therefore he has nothing to gloss over. He may be criticized, he may be tested; but through all, his unbending integrity shines out like pure gold.”*

**Ellen G White – Heavenly Places, Chapter 237**

“This is a time when the work of God should be conducted with the strictest integrity by every conference [organization], a time when there should be the closest observance of the law of God on the part of every worker.”

**Ellen G White – Manuscript Releases Number 1445**

“For evils we might have checked, we are just as responsible as if we were guilty of the acts ourselves.”

**Ellen G White – Desire of Ages p.441**

“There are risks to a program of action. But they are far less than the long range risks and costs of comfortable inaction”

**John F Kennedy**