Center for Government Innovation

Office of the Washington State Auditor
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Best Practices for Bank Reconciliations

If there is one accounting task you should not skip, it is completing your bank account reconciliation. When you perform this important task, you ensure bank transactions mirror those in your own accounting records. This critical step can identify fraud, flag bank errors and highlight your own mistakes; ultimately leading to more accurate accounting records and financial information. Use this guide to help you understand and apply best practices for reconciling your bank accounts.

Getting started

- **Adopt a bank account reconciliation policy.** Create minimum expectations for bank account reconciliations, refer to Appendix A for a bank reconciliation example and Appendix B for potential policy topics. If you have multiple decentralized accounts, adopt an overarching control policy and consider recommending departments also maintain their own detailed, written procedures – especially for unique or complex reconciliations.

A bank account means any account holding cash or investments, including money held by your county treasurer or fiscal agent.

- **Adopt a reconciliation frequency based on your risk.** In Washington state, the Budgeting, Accounting and Reporting System (BARS) Manual requires all local governments to reconcile their bank accounts at least monthly. However, some local governments may need to reconcile certain bank accounts daily to reduce risk to an acceptable level. Consider these items as they may affect your risk:
  - Review your banking agreement terms and conditions for how quickly you must report fraud or errors
  - Check your insurance policy requirements for any stipulations
  - Consider the transaction types permitted for the bank account in question. Any bank account used for automated clearing house (ACH) transactions and wire transfers is higher risk. You have little to no window for reporting fraud for these transaction types.

- **Consider automating your reconciliation.** Today, some enterprise resource planning (ERP) and standalone software systems can import daily banking data, automatically reconcile most or all of it – handling even complicated tasks like matching one-to-many relationships. Some can also automatically record journal entries for banking fees or interest earned. If you use an automated reconciliation, periodically verify the program works as expected – especially after any system updates.

One city automated its disbursement account bank reconciliation, using its ERP system's cash management module. The system automatically reconciles checks and some account transfers and then flags any remaining items for staff to manually research. The city is working on automatically reconciling the remaining transaction types.

Use bank services to reduce fraud risk, and take some pressure off reconciliation procedures

- **Place blocks on your bank accounts, as appropriate.** You can block check activity, ACH transactions, wire transfers and international wire transfers on any account. In this way, you can lower your risk on certain bank accounts, which can then affect your reconciliation frequency.

- **Use Positive Pay with Payee Name Validation, on all check-writing accounts.** After you sign up for this bank service, you submit detailed payment information to the bank so they can compare it to checks presented for payment. Banks typically compare payee name, date, check number and dollar amount. They do this to detect counterfeit and altered checks, before they allow the check to clear the account. They may ask you to review exceptions. You will still have to reconcile cleared checks as part of your bank reconciliation procedures for two reasons:

    1. You will need to calculate outstanding checks; it is a reconciling item to the bank reconciliation.

    2. This service detects most, but not all kinds of check fraud. You should still watch for certain things like forged, missing or improper check endorsements. To learn more about check fraud and this service, as well as what risks it doesn't cover, review this guide on protecting your organization from check fraud by J.P. Morgan Chase (PDF).

- **Use an ACH filter (also known as ACH positive pay).** Use this tool to screen ACH activity and block incoming charges before the bank deducts them from your account. This tool will also send notifications of any activity outside of the parameters that you set up for payees (such as name, dollar limits and timeframe).

- **Use a dedicated bank account for ACH transactions or wire transfers.** Maintain a zero balance and restrict this account from processing any other payment types.

Establishing key controls for the reconciliation

- **Provide adequate training.** If you lack internal resources, contract with a third party to train both your preparer and reviewer. Some topics to address include:
  - Understanding the bank activity (transaction types, how they originate, how they get recorded in your general ledger).
  - How to read bank statements (refer to our Follow the Money (PDF) resource for help in learning to read bank statements).
  - How to complete a reconciliation (both the preparer and reviewer should have the ability to complete a reconciliation from start to finish).
  - How to identify, respond to, and report discrepancies or red flags.

A bank reconciler identified and documented the same "deposit in transit" for five consecutive months. The employee did not understand "deposits in transit" should appear as actual deposits in the bank account within a few days; anything longer indicates a potential theft. The employer had not provided adequate training.

- **Segregate duties.** Assign duties so the bank account reconciler cannot perpetrate fraud and conceal it. For more information about how to segregate duties, or implement compensating controls if you cannot, read the banking chapter in our Segregation of Duties Guide (PDF).

One small government contracted with a local accounting firm to reconcile the bank account, as they could not segregate duties. They recognized the importance of this task, and dedicated resources accordingly.

- **Implement security controls over tools or applications used for reconciliation purposes.** For example, if you use a spreadsheet, protect the file with a password, use check figures and lock cells to protect formulas. If you use an application, ensure it appropriately restricts user access and maintains an audit trail.

- **Establish timeframes for key steps in the bank reconciliation process.** This includes reconciliation completion, outstanding item resolution and final review. Without direction, staff may not prioritize these critical tasks.

Setting up your general ledger

- **Record all transactions promptly in the general ledger.** Record transactions as they occur, based on the source records. Do not record transactions based on the bank statement – that is not a source record (except for bank-imposed transactions like bank fees or interest earnings).

- **Maintain one-to-one relationships to save time and reduce complexity.** Ideally, a deposit on the bank statement would reconcile to a single transaction in your accounting system; or, one bank account would correspond to a single general ledger account.

- **Use general ledger tracking ability to aid in the reconciliation.** For example, if you deposit remote cash receipts into one bank account, consider tracking them separately in your corresponding general ledger cash account, using a unique identifier. In this way, you can quickly identify and reconcile this transaction type.

Performing the reconciliation

- **Read the bank statement.** It is not enough to merely reconcile numbers, take time to read and understand the activity as part of your oversight procedures. To learn more about reading the bank statements, review our Follow the Money (PDF) resource.

The bank statement listed fraudulent transfers in another employee's name, but the person reconciling the account didn't read it – she only focused on the numbers – and missed the fraud.

- **Cash-basis governments should also reconcile revenues and expenditures to banking activity.** If you report on a cash-basis, then most cash inflows you receive typically count as revenue (or other increases) on your financial statements. The same is true of cash outflows, these typically count as expenditures (or other decreases) on your financial statements. Therefore, comparing the bank activity to your general ledger activity can further help you identify accounting errors.

  We provide an optional Excel tool for you: our Global Reconciliation Worksheet. Or, you may create your own.

- **Clearly document reconciliations, so others can verify your work.** Prepare a schedule showing the bank account and general ledger cash balances, how they compare, as well as any reconciling items. Document your reconciliation with enough detail and clarity so that someone else can follow and understand it.

A new finance director used checkmarks on various documents to indicate he performed some sort of reconciliation, but he did not document the reconciliation itself. During the audit, no one could verify his work. (Their policy should have required a documented reconciliation.)

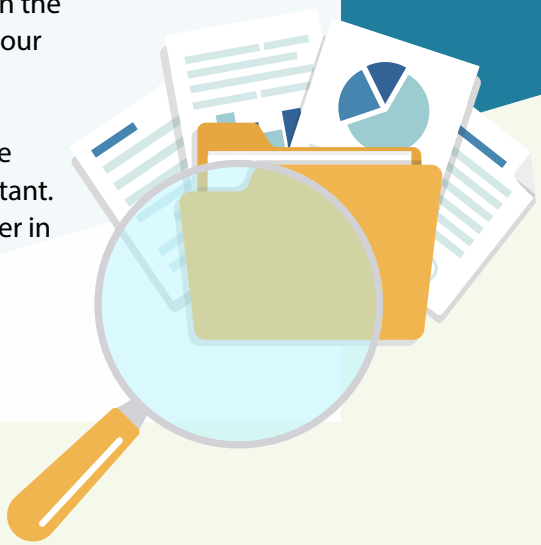
- **Support each reconciling item.** All reconciling items should have support, and most should clear on the next month's bank statement (all deposits in transit become actual deposits next month and most outstanding checks become cleared checks next month). Other than bank fees or interest earnings, staff should carefully evaluate and support any other type of reconciling item.

  Note: Our Office receives many questions on how to handle stale-dated checks, that the beneficiary has not cashed after a period of time. This qualifies as unclaimed property and requires special handling and reporting; refer to the Department of Revenue's Guide for Local Government Unclaimed Property (PDF) for guidance.

Monitoring

- **Independently review bank account reconciliations.** If you have fully segregated duties, the reviewer may perform spot checks of key items on the completed reconciliation, and ensure the reconciler completed it on time. The reviewer should also read the bank statement that they obtained directly from the bank, and compare it to the one used in the reconciliation. For some tips on reading bank statements, refer to our Follow the Money (PDF) resource.

  If you cannot fully segregate duties, then consider outsourcing the bank reconciliation to someone else, such as a contracted accountant. For compensating control possibilities, refer to the banking chapter in our Segregation of Duties Guide (PDF).



- **Periodically review and update your policy.** You may need to update your policy and procedures as circumstances change over time. For example, you may have new accounting software, different receipting or payment processes, new types of electronic payments, or staff turnover. Refer to policy topics in Appendix B.

- **Evaluate your bank account structure annually.** Here are some steps you might take:

  - Reevaluate your open accounts; assess whether you can reduce risk by adding or closing an account. For example, you may want to separate deposits from payments, placing the latter in zero-balance bank accounts.
  - Review blocks for each open account; making sure you have the correct ones in place. You can block checks, ACH transactions, wire transfers and international wire transfers on any account.
  - For each open bank account, verify the mailing address, authorized signers, those authorized to execute wire transfers or ACH transactions, and people granted online access. Also, you might check for any inappropriately issued debit cards.
  - Search for any open accounts unknown to you. To do this, inquire with your bank and possibly others about any bank accounts with your government's name or your federal identification number. You should also scan bank statements for transfers to an unfamiliar bank account and review payments made to other banks.

- **For small cash-basis governments, consider sharing your bank reconciliation with your board.** Help your board participate in their oversight duties. Your financial reports will show ending cash and investments, an important figure in assessing financial health. Show your board members the support for this figure by demonstrating that it agrees to the amount reflected in the completed bank account reconciliation. For very small governments especially, board members may want online read-only access to the bank account, so that they can independently check the account balance and detect unusual activity.

Related resources

- *Budgeting, Accounting, and Reporting System* (BARS) Manual: BARS cash manual, BARS GAAP manual
- Office of the Washington State Auditor: see the banking chapter in the Segregation of Duties Guide (PDF)
- Office of the Washington State Auditor: Global Reconciliation Worksheet
- Office of the Washington State Auditor: Follow the Money (PDF)
- Government Finance Officers Association: Getting Unstuck: How to Get Through Your Bank Reconciliation
- Government Finance Officers Association: Bank Account Fraud Prevention
- J.P. Morgan Chase: Your guide to protecting your company from check fraud (PDF)
- Washington State Department of Revenue: Guide for Local Government Unclaimed Property (PDF)

Questions? Concerns?

This resource was developed by the Center for Government Innovation at the Office of the Washington State Auditor. Please send questions, comments or suggestions to Center@sao.wa.gov.

Disclaimer

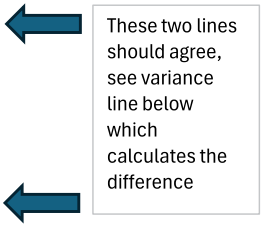
This resource is provided for informational purposes only. It does not represent prescriptive guidance, legal advice, an audit recommendation or audit assurance. It does not relieve governments of their responsibilities to assess risks, design appropriate controls and make management decisions.

Appendix A: Example bank account reconciliation

A bank reconciliation compares ending cash balances per the bank records, to that of your general ledger records, to verify accuracy. As you can see, this bank account in **Figure 1** reconciled with zero variance, as expected.

Figure 1: Example bank account reconciliation

(1) Per bank records		
Ending cash balance per bank	$	250
Plus deposits in transit		50
Less outstanding checks		(100)
Adjusted ending cash, per bank	**$**	**200**
(2) Per general ledger records		
Ending cash balance per general leder	$	195
Plus interest earnings		10
Less bank fees		(5)
Adjusted ending cash balance, per general ledger	**$**	**200**
Variance	$	-



These two lines should agree, see variance line below which calculates the difference

In (1) we adjusted the ending cash per the bank statement. The two most common adjustments are:

- Deposits in transit: money you received that the bank records do not yet reflect. You may have the last day of the month's deposit in the safe, or you might have done a night depository on the last day of the month. These should show up in the first few days of next month's bank activity.

- Outstanding checks: money you spent, but some vendors or employees have not yet cashed or deposited. Therefore, the bank has not yet taken money out of your bank account.

In (2) we adjusted the ending cash per the general ledger. Your general ledger keeps a running total of ending cash throughout the month, as transactions occur. The two most common adjustments are:

- Interest earnings: we learned about this miscellaneous revenue from reading the bank statement, as the bank posted it on the last day of the month. We have not yet recorded it in our general ledger, but it relates to the prior month and so we will post it back to that period.

- Bank fees: we learned about this expenditure from reading the bank statement, as the bank posted it on the last day of the month. We have not yet recorded it in our general ledger, but it relates to the prior month and so we will post it back to that period.

Appendix B: Policy topics for your bank statement reconciliation

Your policy should address expectations for bank account reconciliations. For example, some topics the policy might cover include:

- The types of accounts staff should reconcile, and the corresponding frequency (daily, weekly or monthly)
- The position designated to reconcile the bank statement, how they will obtain it from the bank and if they should sign and date it upon completion. You might also address the conflicting duties this position should not perform. Refer to the banking chapter in the Segregation of Duties Guide (PDF) for a list.
- The position assigned to reconcile the bank account when the designated person is absent (your policy should restrict anyone from holding work during employee absences)
- The number of days allotted for completing the reconciliation, after receipt of the bank statement
- Whether you will expect the reconciler to use a prescribed tool or software application such as an automated reconciling system
- Expectations for documenting the reconciliation and whether you have a prescribed format
- Standards for documenting reconciling items, especially unusual ones. You might also address the timeframe for resolving outstanding reconciling items.
- The position designated to review the bank account reconciliation, how they should obtain the bank statement and how they should document their approval
- Guidelines for bank account reconciliation review, such as when the reviewer should complete it and any other expectations you might have. For example, you might require them to verify reconciling items and/or periodically reperform it.

- Process for reporting issues, red flags or concerns if identified. (Remember that you must report known or suspected losses to our Office in accordance with RCW 43.09.185.)
- Whether you will allow any variance to remain unresolved (between the bank statement and the general ledger)
- Where you will store completed reconciliations and the supporting documentation, and for how long
- Whether you will require detailed, written procedures for any bank account reconciliations (such as for decentralized locations where complexities exist)

Example online policies include:

- University of Houston Bank Account Reconciliation Policy
- University of Rochester Bank Reconciliation Policy (PDF)
- Florida A&M University Bank Reconciliation Procedures (PDF)

The Municipal Research Services Center also maintains a sample document library that may have helpful policy examples.