

NONPROFIT AUDIT WORKSHOP 2018

Preparing for a Smooth, Successful Audit



1

**AUDIT
BASICS**

2

**PREPARING FOR
AN AUDIT**

3

**ROLES DURING
AN AUDIT**

4

**WHAT YOU
CAN EXPECT**

Introduction

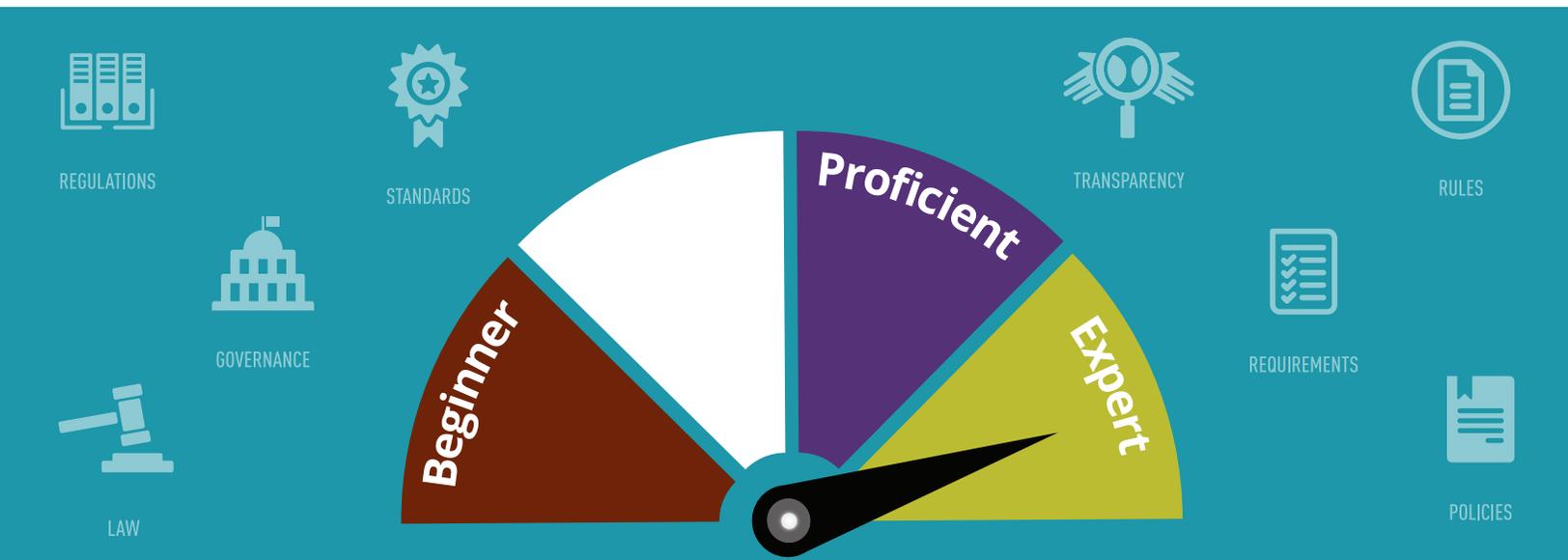
“AUDIT” doesn’t have to be a dirty word at your nonprofit! A thorough financial audit gives you a clear picture of how well your organization manages and tracks its funds, which in turn makes you more effective in carrying out your mission. Passing your audit with flying colors builds confidence among donors and staff. Plus, preparing for your audit and remediating any issues it uncovers can only strengthen your financial practices.

Still, audits can feel like a real burden, costing lots of money and weeks of staff time to complete. That’s why we’ve put together this guide – your audit workshop for 2018 – to help you prepare for a smooth, successful audit. In it, you will learn:

- What an audit should achieve
- How to prepare for an audit
- Roles of staff members, board members, and auditors
- The role of technology in supporting audits
- What you can expect during and after your audit
- How to fully prepare for next year

Your finance team members deserve to sleep well at night, knowing they’ve done everything they should to create an efficient and painless audit experience. Read on to find out how!

Please note: We suggest you always consult a certified public accountant (CPA), independent auditor, or auditing firm to discuss specific questions you may have about audit procedures and practices.



Click the sections below to navigate

← BACK NEXT PAGE →

1
AUDIT BASICS

2
PREPARING FOR AN AUDIT

3
ROLES DURING AN AUDIT

4
WHAT YOU CAN EXPECT

Chapter One: Audit Basics

Why Financial Audits Are Useful

Your organization might not be required by law to conduct an audit or one of the other financial reviews explained below. So why do it at all? It comes down to three things:

- Knowing you're doing right by donors and grant-making organizations by exercising good stewardship over the funds they give you
- Assuring your supporters you're managing your operations well
- Giving your board members and executives the accurate financial data they need to make informed, confident decisions for your nonprofit

Having your financials audited or reviewed by unbiased outside accounting professionals helps ensure you're keeping good track of the money that comes into your organization, where it's allocated, and how effectively your internal controls govern your finance operations.

Passing your annual audits – and using each one as an opportunity to hone your practices – gives greater confidence to everyone who interacts with your nonprofit, from donors to government agencies to staff members. Over the long run, that improves your ability to raise money, run effective projects, and carry out your organization's mission.

Other Types of Financial Reviews

There are two common types of financial reviews that are distinct from audits.

1 Compilation Report
This report, typically prepared by an independent accountant at substantially lower cost than an independent financial review or audit, is simply a compiled report of an organization's financial position, including related statements of activities, functional expenses, and cash flows. A compilation report merely provides an organization with formatted financial statements and records that can be easily reviewed and consumed by third parties, such as your board or bank. Because it is not an audit, it offers no opinion or assurances about whether the financial statements accurately reflect the organization's financial position, or if they are in accordance with generally accepted accounting principles (GAAP).

2 Financial Review
Falling somewhere between a compilation report and an audit, a financial review covers a nonprofit's statement of financial position, statement of activities, and cash flows. The independent accountant who conducts it will make inquiries to the organization's management and apply analytical procedures to management's financial data in accordance with Statements on Standards for Accounting and Review Services, issued by the American Institute of Certified Public Accountants. These standards require the accountant to perform procedures to obtain limited assurance – substantially less than in an audit – that there are no material modifications that should be made to the financial statements. Nonprofit leaders will typically have a financial review conducted to provide a degree of assurance to a regulatory body, insurance company, or lender that their organization's financial statements have been reviewed by a CPA.

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter One: Audit Basics (continued)

Other Types of Financial Reviews Independent Audits vs. Single Audits: What's the Difference?

Audits themselves come in two varieties that require a little more explanation.

Independent Financial Audit

As the name implies, this type of audit – and the focus of this guide – is carried out by a certified public accountant (CPA) who is not otherwise affiliated with the organization being audited. This auditor or firm is contracted to provide an unbiased outside opinion of whether your financial statements are, in accounting parlance, “free from material misstatement.”

An independent audit typically examines your organization's statement of financial position, related statement of activities, cash flows for the year ended, and related notes to the financial statements. The audit is conducted in accordance with GAAP, and involves a range of procedures, selected at the auditor's discretion, intended to obtain accurate data about the amounts and disclosures in the financial statements, and to assess the risks of material misstatements arising from either fraud or error. An audit also evaluates the appropriateness of accounting policies used, the reasonableness of significant accounting estimates made by management, and the overall presentation of the financial statements.

An audit represents the highest level of assurance an auditor can provide and an organization can receive on a set of financial statements. When the audit is complete, the auditor's work is submitted

to your board of directors or audit committee as an Independent Auditor's Report, also known as an opinion letter because it expresses the auditor's professional opinion on all aspects of your financial statements.

Single Audit

This is a special type of audit applied to nonprofits that expend \$750,000 or more in federal or state funds in a single fiscal year. The Code of Federal Regulations requires this kind of audit so the government can have assurance that an organization's use of federal funds complies with the government's funding requirements. Single audits differ depending on the recipient and which federal program provides the funds, but in general they cover the entire scope of an organization-wide independent financial audit, along with a compliance-based audit.

Auditors are required to perform compliance audits in both the planning and fieldwork stages of these federally-funded projects. In the planning stage, the auditor must determine whether there is a high risk that the nonprofit will not comply with applicable laws and regulations, plus identify the relevant federal program and evaluate the program itself. In the fieldwork stage, the auditor again audits the program, along with its use of federal or state funds. According to the Office of Management and Budget (OMB), the auditor must “perform a compliance audit that scrutinizes operations of the specific government-funded program, examining files, documents, contracts, checks, etc. These functions are compared with the laws and regulations applicable to the program to see if they comply or not.”

Click the sections below to navigate

[← BACK](#) [NEXT PAGE →](#)

1

**AUDIT
BASICS**

2

**PREPARING FOR
AN AUDIT**

3

**ROLES DURING
AN AUDIT**

4

**WHAT YOU
CAN EXPECT**

Chapter One: Audit Basics (continued)

What Goes on During an Audit?

Later sections of this guide give more details about every aspect of an independent financial audit, but in a nutshell there are three stages:

1 Stage One: Planning and Preparation

During this stage, your auditor will likely send you an engagement letter (essentially a vendor agreement), along with a detailed “Prepared by Client” (PBC) list that outlines the supporting schedules and other documentation the auditors need your organization to prepare so they can perform the audit.



2 Stage Two: Fieldwork

While the audit is actually under way, a team from the auditing firm will work on site at your organization long enough to review all the information needed to issue an opinion on your financial statements. During this phase, the auditors are likely to have regular conversations with key staff members to clear up any questions they have.

3 Stage Three: Post Work

Finally, the auditors will complete their analysis and submit their final report, or opinion letter, to your board of directors or audit committee.



Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter One:

Audit Basics (continued)**New Audit Regulations for 2018**

Stephen Harris leads the audit practice for the firm REDW in Phoenix; he's worked extensively with nonprofits across his 30-plus years as an auditor. He notes that organizations will have some new regulations to deal with in the next couple of years. The Financial Accounting Standards Board (FASB) has alerted nonprofits to new rules in three areas particularly.

1. Revenue Recognition

Every nonprofit should look at its revenue sources to determine how its recordkeeping will be affected by FASB's new standards. The rule change focuses on determining if you have a contract with a customer. If you don't have a contract, nonprofits will continue to use existing rules to record revenues. However, you should pay close attention to contract and grant income to make sure your finance team is recording revenues properly under the new rules.

2. Lease Standards

For auditing purposes, *capital leases* – for example, a large piece of equipment – have traditionally been treated almost like a purchase: You put the asset on your balance sheet, then recognize a corresponding liability for the lease payments. By contrast, *operating leases* have been treated more like renting an item: You note the expense on your financial statements, then disclose the specifics of term and payments in the notes. Under FASB's new regulations, though, operating leases will be treated more like capital leases: You'll record the leased item as an asset on your balance sheet, along with an offsetting liability for the payments.

There's a key thing to watch out for here, Harris says. If your organization uses bank financing, it may come with certain stipulations about your ratio of assets to liabilities. The new rule potentially changes the numbers used to compute that ratio, so you want to make sure the math still works to satisfy your bankers when the new FASB standard kicks in.

3. Financial Statement Preparations

Harris notes that FASB's current standards in this area have often confused his clients, because they call for as many as three columns (or "buckets") for classifying net assets – unrestricted, temporarily restricted, and permanently restricted. To fix that, the new standards will present net assets in two classes. One of the classes will be for net assets with donor restrictions and the other will be for net assets without donor restrictions.

Ask your auditor or accountant when these standards will begin to apply to your organization. Harris says they will go into effect for most of his clients in 2020, though he is advising all of them to get up to speed on the rules now, so they have plenty of time to understand the impacts of the rules and make any needed changes in their accounting practices.

Keep up-to-date on new or upcoming regulations by following the FASB website: fasb.org.

Click the sections below to navigate

← BACK NEXT PAGE →

1

**AUDIT
BASICS**

2

**PREPARING FOR
AN AUDIT**

3

**ROLES DURING
AN AUDIT**

4

**WHAT YOU
CAN EXPECT**

Chapter Two: Preparing for an Audit

Selecting the Right Auditor

Searching for an auditor requires input from your board and plenty of work by staff members. You'll need to establish timelines, perform research in your sector, perhaps develop a request for proposals (RFP), and evaluate the proposals of candidate auditing firms. Given all of that, you should conduct thorough internal planning before beginning your auditor search.



Fiscal Management Associates (FMA), in its Nonprofit Auditor Selection Guide, suggests these five planning steps:

- 1** Ensure that the board's audit committee is involved in the selection process from the beginning. If your organization doesn't have a separate audit committee, the finance committee should take on this role. Identify one individual from the committee to manage the process and coordinate with members of management.
- 2** Clarify the logistics of the selection process and determine a timeline to complete the process and finalize the decision.
- 3** Conduct initial research, for example by getting recommendations from peer nonprofits.
- 4** Identify key attributes that you want in an auditor and determine a method for evaluating auditor proposals.
- 5** Throughout the process, keep in mind your organization's strategic objectives.

Nonprofit audits require unique expertise, so you'll want to look for an auditor who specializes in them. In particular, you should look for firms that have experience working with your specific type of nonprofit. For example, a firm with plenty of experience in auditing nonprofits that operate primarily from memberships and donations might not be a good fit if your organization relies heavily on grant funding. If you want to use an RFP process to solicit proposals and narrow the field, you'll find plenty of examples and templates online by searching keywords such as "nonprofit audit RFP."

Regardless of how you find your auditor candidates, you should conduct in-person interviews. One key thing you want to learn from this process is the level of detail your auditor will provide. Some firms merely offer the basics, while others will conduct detailed analytic procedures to produce year-over-year analysis and uncover any anomalies. A comprehensive audit will also analyze how contributions are used, computing the relative percentages of each type of income distribution and comparing that with nonprofits of similar scale and type in your area.

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

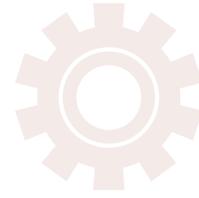
3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Two: Preparing for an Audit (continued)



As you're interviewing auditors, also be sure to ask them what happens if they find fraud. Will they simply alert you, as any auditor would, about anomalies they've discovered, or will they help you gather evidence and assist in the investigation? Do they have personnel who specialize in fraud? (Most auditors don't.) Can they guide you through next steps, or connect you with a fraud examiner to further the investigation?

Planning for an Audit

Stephen Harris has simple but deep wisdom for any organization facing an audit: "You want to plan as much ahead of time as you can." Ideally, you already have some measures in place to ensure you're preparing for your audit year-round. If not, by the time you finish reading this guide you'll know exactly what to do.

As lead auditor on large projects, Harris likes to sit down with clients well in advance to discuss how the audit will proceed and what's needed to make it successful. It starts by establishing a timeline for the whole project, which is usually pegged to the final deliverable, for example, the date when the Independent Auditor's Report is due to the board of directors. From there, auditor and client can work backwards to set calendar milestones for each part of the work.

Harris also supplies the client with a "Prepared by Client" (PBC) list – discussed further below – which enumerates what he calls "the menu of items we'll need to complete the audit." The PBC list will include items such as:

- Bank account reconciliations
- Property, plant, and equipment listings
- Detailed general ledger
- Trial balance

About two or three weeks before the audit is scheduled to begin, Harris reviews the process with the client again, trying to answer questions such as, "Are they ready to go?" "Do they need help with anything?" And, "Do they have an outside CPA firm we need to coordinate with?" Answering these questions allows everyone to hit the ground running when the audit starts.

Suzanna Braun is a CPA and former auditor based near Washington, D.C. She heads Capitol Nonprofit Solutions, a longtime Abila Business Partner. Drawing on her earlier years of experience as an auditor, she counsels organizations not to overcomplicate this part of the process. "My belief is, it needs to be simple," she says. "In all fairness to the auditors, it needs to be simple.

She adds that members of a nonprofit's finance team should not ask for an "incredible amount of information" from the auditor, for example by looking for things as specific as which members of the auditing firm's staff will be working on the audit. It's enough to meet the accounting partner who will run the audit – someone like Harris – and hammer out the basics of timeline, documentation, workflow, and staff interactions. With that knowledge in hand, you can prepare your *people, processes, and paperwork* in earnest.

TIP!

Don't delay! The sooner you start collecting audit-related documents, the less likely you'll end up in a crunch to get everything together on time.

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Two:

Preparing for an Audit (continued)

People

If you want your audit to proceed smoothly and efficiently, make sure you designate a well-organized person – perhaps your controller or one of his or her deputies – to help make it happen. This person, perhaps backed by a small team on larger audits, will be tasked to:

- Coordinate the auditors' scheduling
- Organize documents for the auditors, in line with the "Paperwork" section below
- Manage the details of the actual onsite visit; the auditors will need parking, a quiet, private space such as a conference room or spare office where they can work, strong WiFi access, and a point-person to handle any other logistical issues that come up

Later, we'll discuss more specifics about the roles that staff members, board members, and the auditors themselves will play during the audit.

Processes

As discussed throughout this guide, auditors primarily examine your financial records and practices to assess your organization's financial position. The audit will go a lot more smoothly if you can easily:

- Demonstrate strong internal controls over access to financial resources and related recordkeeping
- Provide an audit trail that clearly tracks transactions to sources of revenue
- Produce reports that quickly and efficiently show how funds are used and other relevant financial activities

It helps if you have financial systems in place designed to facilitate these processes – with granular control over how people access financial systems, auditability of your general ledger and system logs, configurable alerts, and other robust capabilities. If your systems don't make it easy to do these things, be prepared for some extra effort on your part to get ready for the audit. You might also find that the auditors have concerns about your internal controls. These issues are discussed further in the section, "Technology's Role in a Smooth Audit" below.

Red Flags

These warning signs could mean your audit will be rough, or even put you at risk for material misstatements:

- ! You don't have supporting schedules.
- ! Your numbers don't add up or don't agree.
- ! Your internal controls are weak or not documented.
- ! You have large "Miscellaneous" or "Other" expense categories, indicating a possible classification issue.
- ! You're unorganized, handing your auditor the dreaded jumbled box of documents.

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Two: Preparing for an Audit (continued)

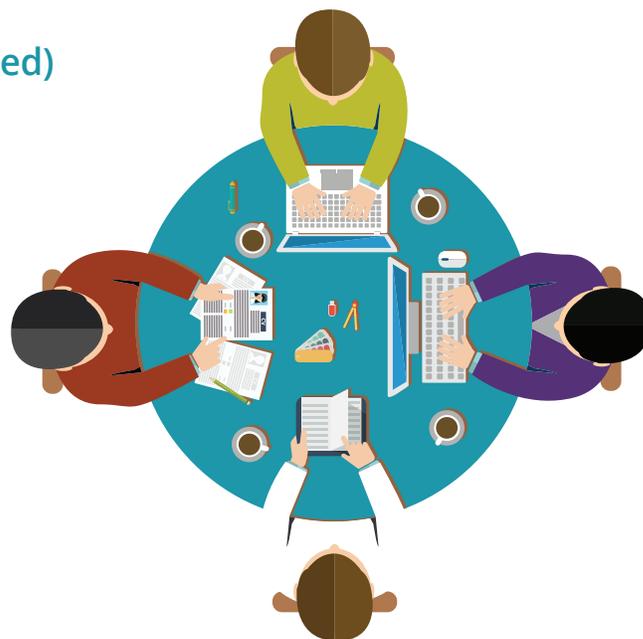
Paperwork

Even before your auditors supply you with their PBC list, you can start to pull together the necessary documentation using the National Council of Nonprofits' basic list of items for audits:

- Bank statements and reconciliations
- Investment summary showing YTD transactions and year-end balances
- Documentation of donor pledges, donated securities, and grant funds received
- Fixed asset and depreciation schedules
- Year-end accounts payable and expenses

Braun has two suggestions to help you simplify your approach to audit paperwork. The first is to ask your auditors for a copy of the **work paper** from the previous year's audit, so you can see the format they use. If you're using [true fund accounting™](#) software, it's simple to pull the needed information straight from your database in exactly the format they want. You drop it into Excel ("I find both accountants and auditors love Excel," Braun says) and that's it.

This process gets even easier in subsequent years, because usually auditors' audit schedule lists will barely change from year to year. Except in cases where they need additional information, or maybe if a new staff member doesn't understand the format wanted, it can be as simple as making a quick change to the relevant date ranges and producing the necessary document for the new year.



Braun's second suggestion is to prepare an **"audit binder"** in both electronic and hard copies. This is especially easy for standard items that auditors ask for every year – things like:

- Final bank statements for the old year, initial bank statements for the new year, and reconciliations for every account
- Investment accounts with related purchases, tied to year-end statements
- Prepaid expenses, with a schedule of what has been paid per vendor
- Accounts receivable aging
- Check registers with receiving
- Fixed assets with repairs and maintenance
- Accounts payable trial balances
- Payroll register, with a schedule tying it back to Forms 941

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Two: Preparing for an Audit (continued)

As Braun puts it, there's no reason not to put these together systematically when your audit is approaching. You print them out for every account and put them in the binder, organizing the corresponding electronic files in parallel. When the auditors arrive, you hand over the binder and the thumb drives as soon as they walk in the door.

You should also provide the auditors with thorough documentation of your accounting procedures and internal controls. This material should answer questions such as, "How do you process money coming in?" "How do you process money going out?" And, "How do you handle cash?" If you don't document this, your auditors will have to gather the information through interviews with your staff.

You can also save the auditors time by explaining up front any large variances they're sure to uncover in their analysis. For instance, if your nonprofit added a program during the fiscal year that required the purchase of two new delivery trucks, you should document that for the auditors so they will know why your fixed assets went up by a significant amount.

Following this approach enables you to be prepared with everything the auditors will need. At the same time, it structures the documentation to make the work much easier for them.



Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Two:

Preparing for an Audit (continued)

Keeping Audit Costs Down

A small, two-person firm that provides a small nonprofit with minimum assurance that there are no material misstatements in its financials may charge as little as \$5,000 to conduct an independent audit. On the other end of the spectrum, a detailed audit for a large nonprofit with multiple operations and significant revenue could cost into the millions. Regardless of the scope, there are a few simple things you can do to control your audit costs.

Work Around the Auditor's Busy Season

Just like a CPA handling individuals' tax returns in April, auditors can get very busy during their peak periods, which drives up the cost of your audit. So, plan ahead and work with your auditors to take that pressure off of them by doing your audit earlier or later.

Make it Easy for Them

Stephen Harris notes the internet has completely revolutionized the way audits are conducted. When he started more than 30 years ago, everything was done with pencil and paper. "Now you can do so much of the audit remotely," he notes, adding that processes of documentation are much more efficient, as well. "It can make a world of difference for what you have to charge to do an audit."

If your finance staff operates efficiently and proactively, they will facilitate the audit so it goes quickly, for example, by collecting relevant information year-round, or by proactively supplying the documentation mentioned above. Conversely, if your finance team is slow to gather information or



hamstrung by systems that don't allow it to quickly produce information that the auditors need, the time and expense of the audit can mount.

Don't Change Auditors Without a Good Reason

It's expensive to change auditors: You have to start all over again with your selection process, and then get up to speed with all of the preferences of the new auditor, who will be seeing your financial books for the first time. According to Suzanna Braun, not only does this cost extra time and money, it can also harm the morale of staff members.

Braun notes that some organizations adopt the practice of changing auditors on principle every so often – say, every five years. Her advice, however, is to avoid changing auditors too frequently, simply for the sake of change. If you have a good reason to make the change, go right ahead; if you don't have a good reason, spare yourself the grief and the extra expense.

Click the sections below to navigate

[← BACK](#) [NEXT PAGE →](#)

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Three: Roles During an Audit

Having run many audits in her career, Suzanna Braun strongly recommends holding a **kickoff meeting** at the start of the audit process. In line with what Stephen Harris said above about clarifying points with clients ahead of time, Braun notes that auditors are usually very good about setting their own expectations; conversely, a kickoff meeting for the whole team held by your CFO or controller is a vital opportunity to clarify *your* expectations.

This meeting gives the auditors a chance to explain exactly what they are trying to accomplish, which helps staff members better support them. But, it also gives you the chance to manage the engagement. You can review the timeline, so everyone has a common understanding of milestones, including:



The kickoff meeting is also your chance to establish ground rules about how the auditors and your staff will interact. To take one key example, you can make it clear that members of the audit team should not interrupt the finance team’s work by stopping in at random times to ask individual questions. Instead, there should be a systematic process by which the audit team accumulates questions and gives them to the controller at regular intervals – perhaps mid-morning, early afternoon, and end of day. You can also emphasize that any requests for additional information should be made in writing to prevent misunderstandings.

Taking the time to plan and hold a kickoff meeting like this will repay you many times over as the audit progresses.

TIP!
Clear the decks! Don’t schedule other major events at the same time as your audit, and make sure everyone knows when and where it’s taking place.

Click the sections below to navigate

← BACK NEXT PAGE →

1
AUDIT BASICS

2
PREPARING FOR AN AUDIT

3
ROLES DURING AN AUDIT

4
WHAT YOU CAN EXPECT

Chapter Three:

Roles During an Audit (continued)

The Finance Staff's Role

Let's start with the fundamentals. As the client, your finance team is on the hook to prepare and fairly present your financial statements according to GAAP. This includes the design, implementation, and maintenance of adequate internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement.

Once the audit is under way, your finance team will be focused on tactical concerns related to specific documents and project timelines. Your organization's controller plays a vital role in this. First, the controller should know which information auditors need and collect it systematically year-round. During the fieldwork portion of the audit, your controller will probably also be the best person to serve as the single point of contact for any questions or issues that arise.

If your staff establishes a good working relationship with your auditors, your controller should be able to work with them to discuss any audit adjustments before they are formally proposed. It doesn't reflect well upon a finance organization if they receive a lot of audit adjustments, so you'll want to know what they are ahead of time and clarify anything you can.

Auditors also typically don't know what your financial software can do, and thus don't understand the depth of the audit trail for software such as [MIP Fund Accounting™](#). Your staff members can work with the auditors to clarify how the controls within the software work and which reports can be generated automatically rather than produced manually. This may help the auditors with their evaluation of your internal controls.

Braun points out that, no matter how proactive the finance staff is, there may occur misunderstanding of facts by the auditors that won't show up until they hand over a draft of the full audit. Working with them closely and methodically throughout the process, however, should minimize surprises and make it easy to correct any misunderstandings.

TIP!

Stephen Harris suggests using a secure electronic accounting portal such as Suralink that can be accessed by both auditors and clients. The auditor can populate it with the PBC list, then easily track what's been supplied and what's still needed as the client uploads items.

The Board's Role

As Braun points out, "Being a nonprofit is a tax status. It's not a business plan." Your board will no doubt represent a mix of professional and personal backgrounds, probably including members with senior management experience. But Braun emphasizes that it's also important to have board members with a real background in finance. Stephen Harris, for example, brings his decades of finance expertise to his service as a board member for a nonprofit in Phoenix.

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Three: Roles During an Audit (continued)

Besides the part that finance committee or audit committee members will play in selecting your auditor, board members with finance expertise can provide guidance on important matters of investment management and financial operations. Beyond that, they will be able to analyze the organization's financials – and the Independent Auditor's Report – to determine how well your operations align with your strategic planning in support of your overall mission.

The Auditor's Role

Braun believes auditors are all too often put into an adversarial relationship with clients. In fact, though, it's not actually their job to nail you for irregularities or to uncover fraud. Rather, they're trying to help you make sure you're taking the steps you should to handle your financials correctly and present them accurately.

A thorough audit will carefully analyze your accounting tools and processes to ensure you're exercising appropriate care to avoid unethical accounting practices and costly mistakes. This includes closely examining your system of internal controls – the policies and safeguards you have in place to protect your cash and financial records from fraud or mismanagement. The auditors will also review your procedures for producing accurate and timely financial reports.

Keep in mind, the auditor's report will *not* include an opinion on your nonprofit's internal controls. That's a common misconception. Certainly, as part of their work they're checking that your internal controls are designed and implemented appropriately, but they won't render an official opinion on it.

It's also not their purpose to detect fraud. Sometimes a thorough audit does turn up evidence of fraud as the auditors review financial statements and interview your personnel. But that's not its purpose, and auditors don't have any formal responsibility to uncover fraud.



TIP!

For a comprehensive overview of fraud detection in nonprofits, see Abila's recently published guide, "[Follow the Clues: A Nonprofit Sleuth Uncovers Fraud.](#)"

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Three:

Roles During an Audit (continued)

Technology's Role in a Smooth Audit

For some nonprofits, particularly small ones, out-of-the-box accounting software might be all that's needed to organize, track, and report financials. However, if you find yourself using one-off spreadsheets to manage your programs, that could leave you open to error and inadvertent financial mismanagement – and a rocky audit. Using a true fund accounting™ system can help you better track funds, meet compliance and reporting requirements, make informed financial decisions, and prepare for your audit. A true fund accounting™ system provides you with:

A fully-auditable general ledger – If any modifications are made throughout the fiscal year to invoices, for example, you and your auditor will have full visibility into the entire trail of changes. By contrast, if you're using generic accounting software or Excel spreadsheets, there's no way to know if entries are deleted or modified, creating a potential security risk.

Help with compliance – You can easily generate a Statement of Activities for your auditors so they can examine and test expenses back to each individual grant. Your fund accounting software-generated Statement of Activities will show exactly what was expensed, without having to track down figures from multiple spreadsheets.

The ability to classify net assets – You can easily classify your net assets as permanently restricted, temporarily restricted, or unrestricted within the software, then provide that information to your auditors, saving them time on reconciliation. (Remember the mantra for keeping audit costs down: "Make it easy for them.") And, because you're starting

the new year reconciled, you'll save yourself time by not having to reclassify assets all over again.

The capability to easily pull grant information – Your true fund accounting™ system will help you track grants by funding source, group them by state or federal grantors, and even assign attributes to each grant. When your auditor asks for grant-specific details, you can swiftly pull that information into a report. This is especially helpful when determining if you require a single audit, because it clearly shows whether your organization passes the monetary threshold.

Easy access to documentation – Because you can easily scan and attach invoices when you enter them into your software, your auditor can pull them directly out of the system.

Robust security controls – Within your fund accounting software, you have complete control over which users have access to what. For example, each program manager can be given access to budgets only for their own programs. You can even enable your auditors access to self-service during the fieldwork stage. You can also create a report for your auditor that clearly specifies who has access to what, demonstrating a key facet of your internal controls.

Stronger internal control processes – Purpose-built software enables you to define which expenses can be allocated where. It also inhibits intentional or unintentional misappropriation of funds because you can configure the system to control transaction entries and define which segments can or cannot be combined. Additionally, you can automate business rules to prevent certain kinds of errors.

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

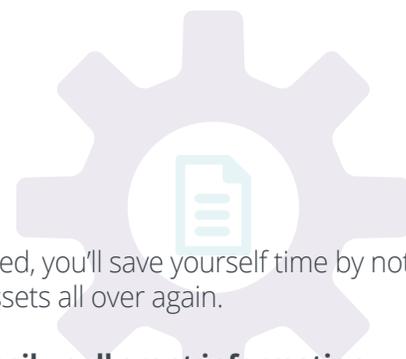
PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT



Chapter Four:

What You Can Expect During and After an Audit

During the Audit

The best advice is to step back, stand by, and stay cool. Once you've done everything above – scheduled the audit, collected all the paperwork, gotten the auditors and your finance team synced – the only thing left to do is get out of the way. The auditors will let you know when they need something.

And, what are the auditors doing, exactly? As touched on above, they're reviewing all of the items from the PBC list to ensure your organization's financial statements accurately reflect your actual financial state, based on GAAP. They're examining your internal controls for weaknesses that might increase the risk of error or fraud. They're looking at how money comes in and goes out, and whether you handle it appropriately in between. As they carry out their tasks, they should follow the processes you laid out in the kickoff meeting to ask any questions or raise any issues they have.

TIP!

Stop worrying! Just remember an “unqualified or unmodified opinion” report – the kind everyone hopes for – is the most common outcome of any audit.

A word to the wise: Don't be terribly concerned if anomalies are uncovered during your audit; it's not an uncommon occurrence, and in many cases solving the problem is straightforward. Significant irregularities could point to a high risk of material misstatements in your financials, and thus the risk of a bad report from the auditors. But most issues are minor – indicating room for improvement, not disaster, for your organization.



What the Auditors Will Prepare for You

After they have completed their work, the audit team will share a draft of their report and letter to management. This is an opportunity for you to ask questions and have the auditors explain any concerns and recommendations in detail. If the auditors have been working closely with your controller as explained earlier, your finance team should already have some awareness of their findings; at this stage, the auditors' conclusions can also be shared with the leadership team and the audit or finance committee of the board.

Based on feedback from the client, auditors will work to correct any errors they have made or incorporate any relevant information they may have missed that will affect their final report.

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

4

WHAT YOU
CAN EXPECT

Chapter Four:

What You Can Expect During and After an Audit (continued)

After the Audit

If your auditor raised issues, consider possible initiatives to address them. Auditor concerns typically center on process weaknesses or operating inefficiencies. These may be minor, earning the organization a “qualified opinion” report, or more serious, leading to an “adverse opinion.”

Either way, you’ll need to address the weaknesses. The specifics will obviously vary depending on your organization and what your audit report shows, but here are a couple of examples:

- If auditors cite weak internal controls, how can you shore those up? For example, would an accounting system with auditable system logs provide better transparency for financial activities? Do you need a more proactive fraud detection system?
- If auditors cite operating inefficiencies, what would help you improve your finance operations? Do you need better tracking of funds by grant in your general ledger to avoid the risk of double dipping, for instance?

TIP!

Ask for help! Enlist your auditors’ support for new initiatives to improve controls and operations.

Once the auditors’ work is done, present the final report to your board. Board members should receive copies of the audit report and management letter well in advance of the meeting in which they will be discussed. You should be prepared for questions, or at least for a discussion of the findings.

Getting Ready for Next Time

Once your annual audit is complete, you can return to your normal finance routines ... *if* you got a good report and you’re already keeping your records audit-ready 12 months a year.

In any event, consider what you learned from the audit process, especially in terms of areas for improvement, and commit yourself to being proactive, so you can avoid the stress of last-minute audit preparations.

Here are a few ideas to start being proactive right now:

- Keep an “audit file” in which you routinely put copies of documents related to fixed assets, loan agreements, or other areas typically examined in audits.
- Maintain a file in which you record restricted donations throughout the year, so the documentation is ready for the auditors at year-end.
- Segregate cash and non-cash donations in the general ledger throughout the year, rather than waiting to separate them out at the end of the year.
- Continually evaluate your recordkeeping systems to identify opportunities for improving controls and increasing efficiency.

In Closing

Now that you’ve “attended” our Nonprofit Audit Workshop, you have all the tools and information you need to sail through your next audit. And always remember, your auditors are friends, not foes. Because, a thorough audit of your nonprofit’s financials gives you – and just as importantly, your donors and community – a clear picture of how well your organization handles and tracks its funds. This, in turn, builds confidence and support in your nonprofit’s work, enabling you to achieve and grow your mission.

Click the sections below to navigate

← BACK NEXT PAGE →

1

AUDIT
BASICS

2

PREPARING FOR
AN AUDIT

3

ROLES DURING
AN AUDIT

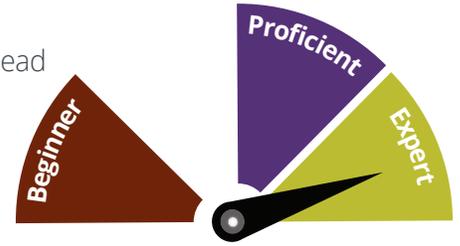
4

WHAT YOU
CAN EXPECT

More Resources

Learn more about how a true fund accounting™ system can help you stay ahead of the audit process, so when next year rolls around, you're audit-ready like never before.

- [Nonprofit Audit 101: A Guide to the Fundamentals and More](#)
- [Preventing Fraud E-book: A Nonprofit Finance Sleuth Uncovers Fraud](#)



About the Experts



Stephen T. Harris, CPA - Principal

Steve Harris has been performing auditing and tax services for more than 30 years and leads REDW's audit practice in Phoenix. He has extensive experience within a broad range of industries, but his specialties lie in tribal gaming, hospitality, and retail. His auditing experience includes performing audits of school districts, community college districts, counties, state agencies, nonprofit entities, and Native American communities in Arizona, California, and New Mexico. Prior to joining REDW in 2012, Steve helped to build Miller, Allen & Co., P.C., into a successful CPA firm in Phoenix, known for its outstanding services to tribes, and was head of its gaming practice for 15 years. Miller, Allen merged with REDW in November 2012.



Suzanna Braun, CPA, MBA

Suzanna is a California certified public accountant and works exclusively with nonprofit and governmental organizations throughout the mid-Atlantic region. She is the managing member at Capitol Non Profit Solutions, LLC, providing consulting services in the metropolitan Washington, D.C. area. Suzanna has nearly 16 years' experience as an Abila Business Partner serving nonprofit and government organizations.

About Abila

Abila, a member of the Community Brands family, is the leading provider of software and services to associations, nonprofit organizations, and government agencies that help them improve decision making, execute with greater precision, increase engagement, and generate more revenue. Abila combines decades of industry insight with technology know-how to serve nearly 8,000 customers across North America. For more information, please visit www.abila.com.

About Community Brands

Community Brands is a technology-driven company that delivers purpose-built solutions to more than 17,000 of the world's leading associations, nonprofits, and K-12 private schools to thrive and succeed in today's fast-paced, evolving world. Our focus on accelerating innovation and bringing to market modern technology solutions helps power social impact and create opportunity. With Community Brands software and services, organizations better engage their members, donors, volunteers, and students; raise more money; effectively manage revenue; and provide professional development and insights to power their mission. For more information, please visit www.communitybrands.com.

LEARN MORE

(800) 811-0961 • www.abila.com

©2018 Abila, Inc. All rights reserved. Abila, the Abila logos, and the Abila product and service names mentioned herein are registered trademarks or trademarks of Abila, Inc., or its affiliated entities. All other trademarks are the property of their respective owners. 03-21-2018

abila™
part of the **communitybrands** family