



Nonprofit Audits:

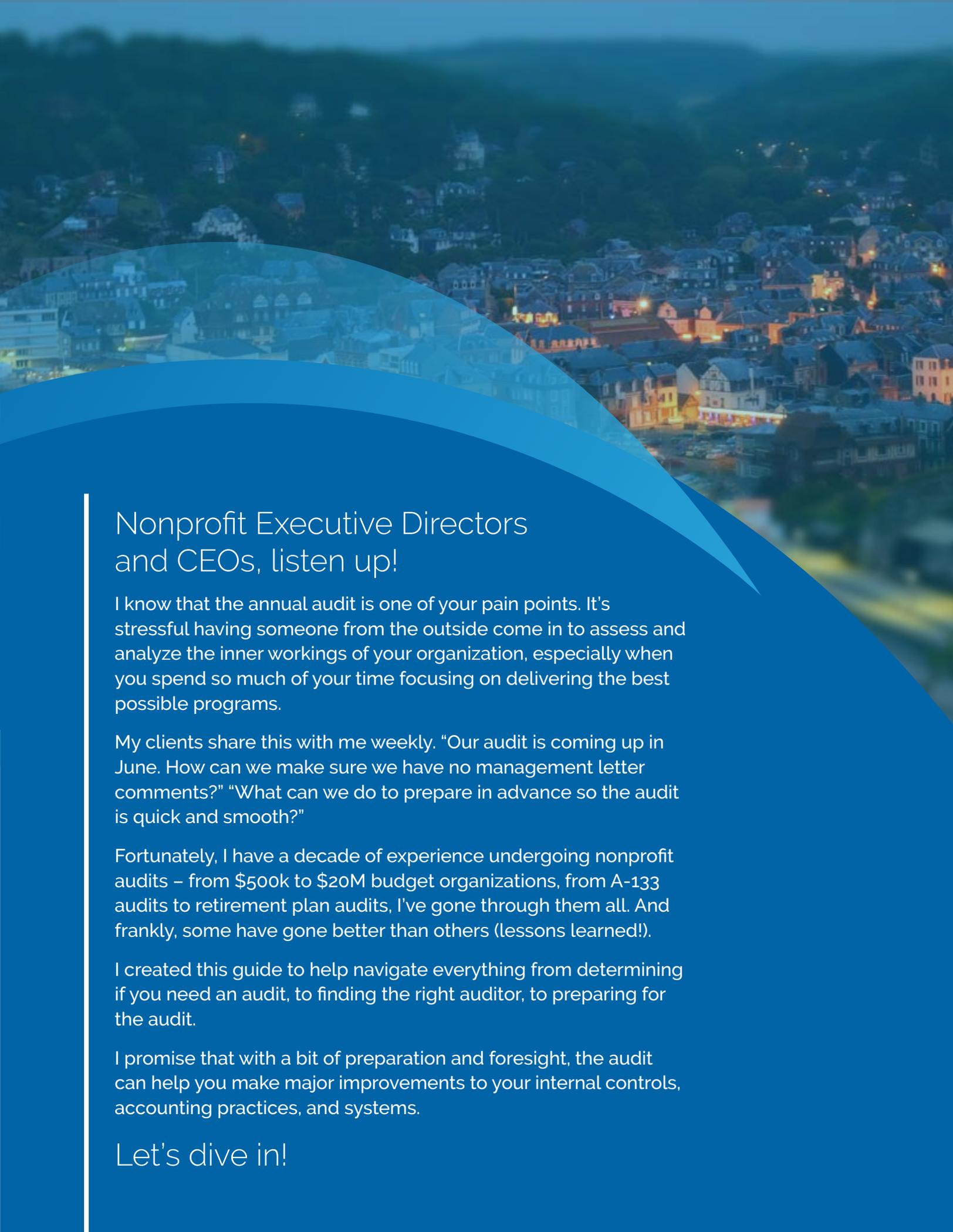
EVERYTHING YOU NEED TO KNOW

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Nonprofit Executive Directors and CEOs, listen up!

I know that the annual audit is one of your pain points. It's stressful having someone from the outside come in to assess and analyze the inner workings of your organization, especially when you spend so much of your time focusing on delivering the best possible programs.

My clients share this with me weekly. "Our audit is coming up in June. How can we make sure we have no management letter comments?" "What can we do to prepare in advance so the audit is quick and smooth?"

Fortunately, I have a decade of experience undergoing nonprofit audits – from \$500k to \$20M budget organizations, from A-133 audits to retirement plan audits, I've gone through them all. And frankly, some have gone better than others (lessons learned!).

I created this guide to help navigate everything from determining if you need an audit, to finding the right auditor, to preparing for the audit.

I promise that with a bit of preparation and foresight, the audit can help you make major improvements to your internal controls, accounting practices, and systems.

Let's dive in!



What is an audit?

Is it when the big, scary IRS comes in and rifles through all your files and you're in trouble? No way! This is when a nonprofit organization chooses an independent auditor to come in and assess not only your books but also your policies and internal controls, then they hand you a neatly compiled set of financials that you can then share with donors, funders and other stakeholders. Also, you pay them.

Does my organization really need an independent auditor?

There are a few factors to consider here:

- What state are you incorporated/registered in? Each state has different audit requirements, oftentimes based on annual revenue or annual expenses.
- Are you registered to fundraise in any other states, besides the one you operate in? Oftentimes, organizations will register in a number of states in order to fundraise there and those states may require audited financials. [Here is a great guide](#) of state-by-state audit requirements and links to statutes. [Please always consult your legal counsel before making any decisions - sites like this could be outdated!]
- Who are your funders? Many private foundations and government agencies will require audited financials along with grant or contract applications. If they don't require an up-front audit, they may require one when you spend above a certain threshold of federal funds in a year ([currently \\$750,000](#)).

Remember, the annual audit and the 990 are two different things. You can think of the 990 as the organization's tax return. The IRS requires nonprofits to complete the [990](#) but does not require an independent audit. Part XII Financial Statements and Reporting of the 990 asks whether or not the organization has had an independent audit and, as you probably know, this form is public information.

Now that you've done the research and discovered that your organization does or does not technically need an audit, here's why it is a best practice:

1. You'll gain the credibility and confidence of funders by promoting financial transparency of the organization.
2. Your organization will potentially be eligible for new and different sources of funding as well as ratings by the important charity watchdog organizations ([Charity Navigator](#), [Guidestar](#), etc).
3. Finally, and maybe most importantly, it's an opportunity to do a deep dive into your policies and procedures to ensure you're using your limited resources most efficiently.

HERE AT
100 DEGREES CONSULTING,
WE ARE ALL ABOUT
BEST PRACTICES!



Finding an auditor: the RFP process

Now you're ready for an audit (or a review) but you need to find someone to conduct it for you.

Not only do we need an audit firm that specializes in nonprofits, but we also want someone we connect well with. You will likely be communicating with that auditor not only during the annual audit process, but also throughout the year as questions come up. The auditor will also meet with your board's audit/finance committee or perhaps even present at a board meetings, so it's important that the audit firm's culture meshes well with yours.

I recommend an RFP (Request for Proposals) process to appropriately do your due diligence and get an auditor that will work best for your organization. I promise it's not complicated!



Form a committee of stakeholders. Who will be interacting with the audit team? Perhaps the ED, your lead finance person, and a board member would be a good place to start.



Determine what you're looking for in an audit firm and write it down. This will be the basis of your RFP document. Here are some things to think about: What size firm do you want? What is their expertise? How many staff will work on your engagement? What is their average turnaround time? How much do they cost? Are they available when you want them to come? [Here is a sample.](#)



Identify who you want to send the RFP to. This is where your network comes in! I suggest reaching out to colleagues, peers, and board members and finding out which audit firms they recommend - you'll have a much better experience than simply Googling "nonprofit auditor [your location]". Come up with a list of maybe 10 firms and their contact information.



Send the RFP out. Send both a paper and email copy to the contacts you identified with specific instructions on how to submit the proposal.



Review the proposals, select your two or three finalists, and invite them into the office for a meeting to discuss their proposal. Don't forget to discuss fees!



Make your final decision and hire your new audit firm. Let the fun begin!

With the proper due diligence, this new audit firm will serve as an ongoing sounding board for your organization. For example, if you begin a new project and aren't sure exactly how to book the revenue, call your auditor for advice rather than waiting for them to find potential mistakes during the audit.

On the contrary, if the audit firm didn't live up to your expectations, remember that the relationship isn't forever - simply go through the RFP process again to find a better fit.



How to prep for a stress-free audit

Now that you've determined you need or want an auditor and found a great firm, we're ready to prepare.

I had a few alternative titles for this section:

- Audit Prep: You're Already Behind the Eight Ball
- Audit Prep: Shape Up So They Can Ship Out
- Audit Prep: No Management Letter Comments, No Cry

Joking aside, without adequate preparation, the audit can be one of the most stressful weeks (or months!) of a nonprofit leader's year. Not only are you expected to make sure every single journal entry is properly booked, but you've got HR files and donor letters and receipts from a year's worth of expenses to be sure are coded, organized, and easily accessible. Not to mention the things that can be just plain confusing: temp restricted net assets, anyone?

The auditor's arrival to your office does not have to be the worst moment of your year. I am here to change your mindset – auditors are here to help!

Use this checklist to ensure the audit is as smooth as can be:



Prior year. As soon as the auditors send you the final report and management letter from the prior year's audit, you should start tackling their comments right away to make institutional changes to fix any issues. If you didn't jump on that, jump now! You need to demonstrate you've taken their recommendations seriously and have made substantial effort to correct any issues. This is important to all stakeholders to ensure we're maximizing and being good stewards of our resources to further our mission.



Scheduling the audit. Think strategically about when to schedule your audit. If you have a June 30th year end, I strongly suggest you not schedule the auditors to arrive on July 15th. Give yourself at least a month after year-end close to make sure the books are in order, paperwork is organized, and you've prepared as much documentation as humanly possible.



Ongoing communication. This should not be the first time you have spoken with your auditor since they walked out last year. Most good firms will be in communication throughout the year on new regulations and best practices, and be available to answer your questions as they come up. Audit week is NOT the time to ask how to track your temp restricted net assets - be prepared for an auditor brain explosion if you ask her.



PBC list. If you haven't already, ask your auditor now (seriously, GO EMAIL HER NOW!) for the PBC, or Provided By Client, list. This is a comprehensive list of everything the auditor needs both prior to on-site and when they arrive. Here's a great [sample list](#).



Create a game plan. As soon as I have the PBC list in my hands, I schedule a team meeting and assign a person responsible and a deadline to each item. We also have a year-end close deadline list (e.g. soft close on January 15th, review reports and fix any issues by January 21st, hard close on January 22nd) which helps determine when PBC list items can be completed. The final part of the game plan is our brief weekly check-ins on the status of each item until the auditors arrive.



Start early. If you've got enough capacity in your finance team to do so, I recommend tackling as many items as you can simultaneously with closing the books for the year. You'll likely be asked for personnel and finance policies, employee lists, check registers and other items that can be sent immediately.



Wait to send schedules. I think we can all relate to this: we work really hard to complete the temp restricted net asset schedule quickly this year, send it off to the auditor before we officially close the books and realize that there was an edit which throws off the whole balance. While you can send many items early, you should wait until your books are absolutely final to send all your schedules. Remember, everything must agree - general ledger vs. schedule vs. balance sheet and income statement - and a surefire way to ensure this is to wait until your books are solidly closed. You don't want to show the auditors fifteen different reconciliations later to show how you made the changes.



Stay organized. Once you've begun preparing schedules and other PBC list items, it's critical to keep them organized so your auditor isn't asking for the same document seven times. It's very tempting to just drop the bank statements in an email but that email could easily get lost in the shuffle (I mean, how many emails do you receive each day?!). Set up a Google Drive or Dropbox folder, share with stakeholders, and create a filing system that ties directly with the PBC list. You've just eliminated about 50 emails a day and created a cloud-based record of your audit to reference next year.

NOW YOU'RE READY!
PREPARATION IS CRUCIAL TO A
SMOOTH AUDIT - STAY ORGANIZED
AND YOU'VE GOT THIS!