

HCCA AUDIT AND COMPLIANCE CONFERENCE 2019 TEN AUDIT ISSUES FOR AUDIT COMMITTEE AND BOARD MEMBERS

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New York Charities Bureau

- Mandated Independent Audit Reports for charitable nonprofits (exceptions for hospitals) with IRS 990
- Review of mergers, sales of substantially all assets provides window to entity financial reporting
- Focus on best practices (AUDIT COMMITTEE REQUIREMENTS AND RESPONSIBILITIES-9/18)
<https://www.charitiesnys.com/pdfs/AuditCommittees.pdf>
- Investigations after embezzlements, business failures, governance disputes, fundraising fraud
- Coming-search capability for audit report text (2020)

Heroic volunteer firefighter/ Mahopac treasurer Michael Klein saves cat
(photo from Putnam Daily Voice)



Mahopac VFD IRS 990

- 2014 Return \$2 million in revenue, \$2 million in expenses
- Signed by thief Mike Klein (treasurer and embezzler)
- Signed by preparer, CPA JER
- Did the organization become aware of a significant diversion of its assets during the year? No.
- Document meetings? No
- Conflict of interest policy? No
- Only two officers-no directors

Auditor Edmond Brady and the Breast Cancer Survivors' Fund (2018)

- Complaint and judgment against accounting firm for aiding and abetting fraud
- MCENERNEY, BRADY, & COMPANY, LLC, and EDMOND BRADY
- “disregarding basic professional standards for auditors”
- “failing to report significant internal control failures”
- Auditors of Breast Cancer Survivors Fund- never spoke with the board or the chair-only with professional fundraiser
- BCSF dissolved; chair publishes apology

New York's Approach- from Duty to Rule

- Primary regulation by private parties
- Positive obligations with consequences
 - Independent audit committee /work plan
 - Auditor/preparer
 - Related party transactions requirements
 - Loans to officers

Reliance on CPA/Auditor Work in Audits, Reporting, Internal Controls

- Auditor opinion that the financial statement and balance sheet present fairly the financial operations and position of the organization.
- Funding agencies require management letters
- Auditor opinion that financial statements comply with:
 - GAAP
 - GAAS
 - “all pronouncements . . . that establish accounting principles relevant to not-for-profit corporations” of FASB and AICPA

Relevant Audit Standards

- AU-C Section 240 - Consideration of Fraud in Financial Statement Audit
- AU-C-Section 250 - Consideration of Laws and Regulations in an Audit of Financial Statements
- AU-C-Section 260 - The Auditor’s Communication with Those Charged with Governance
- AU-C “Clarified Statements on Auditing Standards” from AICPA

TEN AUDIT ISSUES FOR BOARD MEMBERS

- 1) An independent audit is responsible for evaluating a fair presentation of financial statements, for the benefit of the board, external stakeholders, and the charitable beneficiaries.
- Audit Committee selects the auditors, not management.
- Auditors design the audit work plan, not management, and discuss scope and planning with Audit Committee
- Auditors report is to the Audit Committee and the Board, not management

What AU-C-260 requires: Scope and Planning

- PLANNING THE AUDIT - Establish and apply the working principles governing the audit:
 - ___ Auditor should communicate to those charged with governance:
 - ___ the method of two way communication
 - ___ fraud issues
 - ___ the auditor's intentions with respect to documentation of communications with those charged with governance
 - ___ auditor's views on quality of significant accounting practices, and the process used by management in formulating sensitive accounting estimates
 - ___ significant difficulties, if any, encountered during the audit
 - ___ disagreements with management, if any

TEN AUDIT ISSUES FOR BOARD MEMBERS

- 2) An independent audit must be conducted consistent with governing professional standards-significant room for professional judgment, but auditor review and work papers must document and support the judgment. (Auditing Standards Board of AICPA)

TEN AUDIT ISSUES FOR BOARD MEMBERS

- 3) It's not just about the independent audit-what other documents do the auditors prepare or sign? Who reviews? What standard?
- Engagement letter-describe scope and fees
- Management/internal control letters-proxy for audit quality
- IRS 990 reported information
- Preparer declaration on 990:"I have examined this return, including accompanying schedules and statements. . . To the best of my knowledge it is true, correct, and complete. "
- Contract reviews/special procedures
- State charities/nonprofit/Health filings
- Timely submission of other documents for board review.

TEN AUDIT ISSUES FOR BOARD MEMBERS

- 4) SALY (Same as Last Year) is suspect.-(same footnotes, same numbers, same Schedule O on IRS 990)

TEN AUDIT ISSUES FOR BOARD MEMBERS

- 5) Please, auditors, discuss the management representations and disclosures to the auditors upon completion of the audit
- Are you comfortable that they were accurate and complete? Did you discover any information potentially inconsistent with management representations? How did you address these issues?

AU-C 580: Management Representations and AU-C Section 240: Considerations of Fraud

- Written representations about completeness of information, related party transactions, amounts receivable from or payable to third parties
- Management's acknowledgment of its responsibility for the design and implementation of programs and controls to prevent and detect fraud.
- Knowledge of fraud or suspected fraud affecting the entity involving (1) management, (2) employees who have significant roles in internal control, or (3) others where the fraud could have a material effect on the financial statements. Knowledge of any allegations of fraud or suspected fraud affecting the entity received in communications from employees, former employees, analysts, regulators, short sellers, or others.

TEN AUDIT ISSUES FOR BOARD MEMBERS

- 6) the auditor and the audit committee should reach an understanding regarding the nature, form, and extent of communications with the committee about fraud/misappropriations perpetrated by employees, vendors, or contractors

TEN AUDIT ISSUES FOR BOARD MEMBERS

- 7) Does the audit firm believe that they have any professional obligation to make additional disclosures concerning illegal acts that have come to its attention to those charged with governance, or to a funding agency or other specified agency in accordance with requirements for the audits of companies that receive governmental financial assistance AU-C-Section 250

TEN AUDIT ISSUES FOR BOARD MEMBERS

- 8) Does the auditor believe that the organization has any obligation to report, refund, and explain any overpayments to government healthcare programs under the Affordable Care Act Section 6402?
- Credit balances-USA ex rel. Kane v. HealthFirst (NY) (SDNY August 2015)

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- 9) The auditor must communicate in writing to management and the audit committee all significant deficiencies and material weaknesses in internal controls identified during the audit (management letters)
- Tell us about issues you considered for significant deficiencies and material weaknesses-how were they resolved? How do they differ from last year? Did management address significant deficiencies and material weaknesses from last year?

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- 10) If the auditor believes there is substantial doubt about the entity's ability to continue as a going concern for a reasonable period of time, he should (1) obtain information about management's plans that are intended to mitigate the effect of such conditions or events, and (2) assess the likelihood that such plans can be effectively implemented.
- The Audit Committee needs to know about the plans and about the auditor's assessment of them
- Management must evaluate going concern issue and report to auditor in management representations

Core Planning for Audit Committee Members

- Access to legal, accounting expertise where needed
- Training on duties when elected
- Accurate minutes of meetings
- Reporting to full board
- Knowledgeable about accounting and financial reporting processes of the corporation

Resources

- New York Charities Bureau guidance
<https://www.charitiesnys.com/guides>
 - Right From the Start - Responsibilities of Directors of Not-for-Profit Corporations
 - Internal Controls and Financial Accountability for Not-for-Profit Boards
 - Whistleblower Policies Under the Nonprofit Revitalization Act of 2013
 - Accounting from the Inside Out – Internal Controls and External Accountability (New York Council of Nonprofits)
 - Influentials email list-monthly updates on nonprofit issues