

# FINANCE 101: Audits at a Glance

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# Agenda

- ▶ Audit vs. Review vs. Compilation
- ▶ Audit Responsibility
  - ▶ Board and Staff
- ▶ Audit Reports
  - ▶ Clean vs. other than clean opinion
- ▶ Management Letter
- ▶ Basis financial statements
- ▶ Generally accepted accounting principles terminology
- ▶ Preparing and Filing Form 990

# Audit, Reviews, and Compilations

- ▶ Difference lies in the level of assurance given by the accountants who provide the service and the independence factor.
  - ▶ Audits:
    - ▶ Full Scope
    - ▶ Reasonable (not absolute) assurance that financial statements are presented fairly in all material respects in accordance with accounting principles generally accepted in the United States of America.

## Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of ABC Organization as of June 30, 20X1, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

- ▶ Must be independent.

# Audit, Reviews, and Compilations

## ▶ Reviews:

- ▶ Substantially less in scope than an audit:
  - ▶ Analytical procedures
  - ▶ Inquiries of management
- ▶ Limited assurance: No material modifications that should be made to the financial statements for them to be in accordance with accounting principles generally accepted in the United States of America.

### **Accountant's Conclusion**

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in accordance with accounting principles generally accepted in the United States of America.

- ▶ Must be independent.

# Audit, Reviews, and Compilations

## ▶ Compilations

- ▶ No procedures performed to verify the accuracy or completeness of information.
- ▶ No assurance or opinion is given.

Management is responsible for the accompanying financial statements of ABC Organization (a nonprofit organization), which comprise the statement of financial position as of June 30, 20XX, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements in accordance with accounting principles generally accepted in the United States of America. I (We) have performed a compilation engagement in accordance with Statements on Standards for Accounting and Review Services promulgated by the Accounting and Review Services Committee of the AICPA. I (We) did not audit or review the financial statements nor was (were) I (we) required to perform any procedures to verify the accuracy or completeness of the information provided by management. Accordingly, I (we) do not express an opinion, a conclusion, nor provide any form of assurance on these financial statements.

- ▶ Do not have to be independent.

# Audit Responsibility

- ▶ Board
  - ▶ Audit Committee
    - ▶ Choose the auditors
    - ▶ Oversee the audit
    - ▶ Approve the audit
- ▶ Management/Staff
  - ▶ Responsible for the books
    - ▶ Accounts must be reconciled
    - ▶ Provide information/supporting schedules to auditors

# Audit Reports

- ▶ Clean opinion
  - ▶ Unmodified opinion (Nonprofit term)

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of ABC Organization as of June 30, 20X1, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

# Audit Reports

- ▶ Other than a clean opinion
  - ▶ Modified opinion (Nonprofit term)
    - ▶ Scope limitation present - clean with the exception of:

## **Basis for Qualified Opinion**

No accounting controls are exercised over door-to-door cash collections prior to the initial entry of such contributions in the accounting records. We were unable to obtain sufficient appropriate audit evidence about the amount recognized for the door-to-door contributions collected by ABC Organization for the year ended December 31, 20X2, because there were no accounting controls. Consequently, we were unable to determine whether any adjustments to those amounts were necessary.

## **Qualified Opinion**

In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of ABC Organization as of June 30, 20X1, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.



# Audit Reports

- ▶ Other than a clean opinion
  - ▶ Adverse opinion (Nonprofit term).
    - ▶ Pervasive GAAP departure - failure to follow financial statement presentation requirements of FASB ASC 958.

## **Basis for Adverse Opinion**

As described in Note X to the financial statements, ABC Organization has not classified the difference between its assets and liabilities as unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets, based on the presence or absence of donor-imposed restrictions. Also, ABC Organization has not reported the changes in each of those classes of net assets in the statement of activities and has not disclosed information about expenses reported by their functional classifications in the statement of activities or the notes to the financial statements. Presentation of such information is required by accounting principles generally accepted in the United States of America. The effects on the financial statements of that departure from those accounting principles are not reasonably determinable.

## **Adverse Opinion**

In our opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion paragraph, the financial statements referred to above do not present fairly the financial position of ABC Organization as of June 30, 20X1, or the changes in its net assets or its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

# Audit Reports

- ▶ Other than a clean opinion
  - ▶ Disclaimer: No opinion is given.
  - ▶ Unable to obtain sufficient appropriate evidence.

## **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on conducting the audit in accordance with auditing standards generally accepted in the United States of America. Because of the matter described in the Basis for Disclaimer of Opinion paragraph, however, we were not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

## **Basis for Disclaimer of Opinion**

ABC Organization's promises to give amount is presented in the statement of financial position at \$XX,XXX as of June 30, 20X1, which represents XX percent of net assets. The management of ABC Organization requested that we not confirm promises to give by direct correspondence with donors. As a result, we were unable to determine whether any adjustments were necessary relating to the existence and carrying amount of promises to give.

## **Disclaimer of Opinion**

Because of the significance of the matter described in the Basis for Disclaimer of Opinion paragraph, we have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, we do not express an opinion on these financial statements.

# Management Letter

- ▶ Communicates internal control deficiencies to the board and management.
  - ▶ Deficiency: Exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.
    - ▶ Two Types
      - ▶ Material Weakness:
        - ▶ Reasonable possibility that a material misstatement of an Organization's financial statements will not be prevented, or detected and corrected, on a timely basis.
      - ▶ Significant Deficiency:
        - ▶ Less severe than a material weakness but important enough to merit the attention of those charged with governance.

# Financial Statements - Statement of Financial Position (Balance Sheet)

- ▶ Three components:
  - ▶ Assets
  - ▶ Liabilities
  - ▶ Net Assets: Unrestricted, temporarily restricted, and permanently restricted
- ▶ Nonprofit standards allow flexibility in preparing this statement as long as information about liquidity, financial flexibility, and relationships between assets and liabilities is presented in the statements or in the notes to the financial statements.
  - ▶ Most common format used is to present line items between current and noncurrent assets and liabilities, sequenced according to the nearness of conversion to cash or use of cash.
- ▶ Nonprofit standards require the three classes of net assets to be presented on the face of the statement of financial position.

# Financial Statements - Statement of Financial Position (Balance Sheet)

## CHILDREN'S SCIENCE MUSEUM, INC.

### STATEMENT OF FINANCIAL POSITION

AS OF JUNE 30, 2014, WITH COMPARATIVE  
TOTALS AS OF JUNE 30, 2013

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>2014 Total</u>	<u>2013 Total</u>
<b><u>ASSETS</u></b>				
<b>CURRENT ASSETS</b>				
Cash and cash equivalents	\$ 15,643	\$ 15,482	\$ 31,125	\$ 47,760
Grant receivable, Note A	39,152	—	39,152	38,712
Museum store inventory, Note A	3,514	—	3,514	3,459
Other current assets	6,831	—	6,831	2,448
Pledges receivable, Notes A and B	—	3,000	3,000	3,000
Total current assets	<u>65,140</u>	<u>18,482</u>	<u>83,622</u>	<u>95,379</u>
<b>PROPERTY AND EQUIPMENT, net, Notes A and C</b>	<u>1,007,862</u>	<u>—</u>	<u>1,007,862</u>	<u>1,023,861</u>
<b>INVESTMENTS, Notes D and K</b>	<u>251,025</u>	<u>—</u>	<u>251,025</u>	<u>238,017</u>
<b>OTHER ASSETS</b>				
Pledges receivable, Notes A and B	<u>—</u>	<u>3,000</u>	<u>3,000</u>	<u>6,000</u>
<b>TOTAL ASSETS</b>	<u><b>\$ 1,324,027</b></u>	<u><b>\$ 21,482</b></u>	<u><b>\$ 1,345,509</b></u>	<u><b>\$ 1,363,257</b></u>

# Financial Statements - Statement of Financial Position (Balance Sheet)

<b><u>LIABILITIES AND NET ASSETS</u></b>				
<b>CURRENT LIABILITIES</b>				
Accounts payable and accrued expenses, Notes A and G	\$ 59,019	\$ —	\$ 59,019	\$ 42,702
Line of credit, Note E	43,000	—	43,000	40,000
Deferred revenue, Note A	45,364	—	45,364	45,239
Other current liabilities	200	—	200	775
Notes payable, current portion	7,884	—	7,884	7,495
Total current liabilities	155,467	—	155,467	136,211
<b>LONG-TERM DEBT, Note E</b>	<b>314,088</b>	<b>—</b>	<b>314,088</b>	<b>321,972</b>
Total liabilities	469,555	—	469,555	458,183
<b>NET ASSETS</b>				
Unrestricted, Note A	854,472	—	854,472	858,908
Temporarily restricted, Notes A and I	—	21,482	21,482	46,166
Total net assets	854,472	21,482	875,954	905,074
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>\$ 1,324,027</b>	<b>\$ 21,482</b>	<b>\$ 1,345,509</b>	<b>\$ 1,363,257</b>

Present separate from unrestricted net assets



# Financial Statements - Statement of Activities (Income Statement)

- ▶ Nonprofit standards allow flexibility in the presentation of items in this statement.
- ▶ Present items in a relevant and understandable way to the users of the financial statements.
- ▶ Present expenses by function either on the face of the statement of activities or in the notes to the financial statements.
- ▶ One Requirement:
  - ▶ Totals for the change in unrestricted net assets, temporarily restricted net assets, permanently net assets, and the total change in net assets must be presented.
- ▶ Most common approach: Single Step
  - ▶ Groups components of change in net assets into three categories:
    - ▶ Revenues and Gains
    - ▶ Net Assets Released from Restriction
    - ▶ Expenses and Losses

# Financial Statements - Statement of Activities (Income Statement)

## Statement of Activities—Multiple Column Format

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
	<hr/>	<hr/>	<hr/>	<hr/>
REVENUES, GAINS, AND OTHER SUPPORT				
Contributions				
United Way Services	\$ —	\$ 156,275	\$ —	\$ 156,275
New men's shelter	—	46,193	—	46,193
Capital campaign	—	4,771	—	4,771
Equipment acquisition	—	30,000	—	30,000
Endowment	—	—	2,704	2,704
Other	89,736	—	—	89,736
Federal financial assistance	43,473	—	—	43,473
Program service fees	22,417	—	—	22,417
Investment return	5,766	497	—	6,263
Change in value of split-interest agreement	—	1,800	—	1,800
Other	2,777	—	—	2,777
Net assets released from restrictions	<u>183,343</u>	<u>(183,343)</u>	=	=
<b>TOTAL REVENUES, GAINS, AND OTHER SUPPORT</b>	<b>347,512</b>	<b>56,193</b>	<b>2,704</b>	<b>406,409</b>



# Financial Statements - Statement of Activities (Income Statement)

## EXPENSES

Program services				
Women and children	134,051	—	—	134,051
Men	94,231	—	—	94,231
Supporting services				
Management and general	55,629	—	—	55,629
Fund-raising	<u>13,541</u>	=	=	<u>13,541</u>
TOTAL EXPENSES	<u>297,452</u>	=	=	<u>297,452</u>
CHANGE IN NET ASSETS	<u>50,060</u>	<u>56,193</u>	<u>2,704</u>	<u>108,957</u>
NET ASSETS AT BEGINNING OF YEAR	<u>612,499</u>	<u>435,932</u>	<u>4,165</u>	<u>1,052,596</u>
NET ASSETS AT END OF YEAR	<u>\$ 662,559</u>	<u>\$ 492,125</u>	<u>\$ 6,869</u>	\$
				<u>1,161,553</u>

Required

# Financial Statements - Statement of Cash Flows

- ▶ Two Methods
  - ▶ Direct: recommended by GAAP but not required (2 page statement)
    - ▶ If used, must also present a reconciliation of the change in net assets to net cash flows from operating activities (Indirect Method).
  - ▶ Indirect: most common method used (1 page statement)
- ▶ Direct Method
  - ▶ Presents cash inflows and outflows from activities in three categories:
    - ▶ Operating Activities
      - ▶ Cash received from providing services, making or receiving contributions, etc.
      - ▶ Interest income reported on separate line.
      - ▶ Cash used in providing services, paying vendors, paying salaries, etc.
      - ▶ Interest paid reported on separate line.

# Financial Statements - Statement of Cash Flows

## ▶ Direct Method

### ▶ Investing Activities

- ▶ Lending money and collecting on loans
- ▶ Purchasing property
- ▶ Purchasing and selling of investments

### ▶ Financing Activities

- ▶ Borrowing money and repayment of loans

## ▶ Indirect Method

### ▶ Starts with change in net assets

### ▶ Adjust for

#### ▶ A) Non-cash items related to investing and financing activities

- ▶ Depreciation and amortization
- ▶ Net unrealized and realized gains (losses) on investments

#### ▶ B) Changes during the period in operating assets and liabilities

- ▶ Accounts receivable
- ▶ Accounts payable

# Financial Statements - Statement of Cash Flows

**BETHEL HOUSING CORPORATION  
STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012**

	<b>2013</b>	<b>2012</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Received from Tenants and Other Sources	\$ 103,153	\$ 102,466
Interest Received	64	142
Paid to Suppliers and Employees	(91,025)	(90,371)
Cash Transferred to Restricted Cash Account (Note 2)	(4,264)	(2,688)
Interest Paid	—	—
Income Taxes Paid	—	—
	<u>12,192</u>	<u>12,237</u>
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Principal Payments on Long-Term Debt	<u>(1,200)</u>	<u>(1,200)</u>
<b>NET CASH USED IN FINANCING ACTIVITIES</b>	<u>(1,200)</u>	<u>(1,200)</u>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	6,728	8,349
<b>CASH AND CASH EQUIVALENTS,</b>		
<b>BEGINNING OF YEAR</b>	<u>18,069</u>	<u>9,720</u>
<b>END OF YEAR</b>	<u>\$ 24,797</u>	<u>\$ 18,069</u>

# Financial Statements - Statement of Cash Flows

**BETHEL HOUSING CORPORATION  
STATEMENTS OF CASH FLOWS (CONTINUED)  
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012**

	2013	2012
<b>RECONCILIATION OF CHANGE IN NET ASSETS TO NET CASH PROVIDED BY OPERATING ACTIVITIES</b>		
Change in Net Assets	\$ (51,721)	\$ (52,301)
Adjustments to Reconcile Change in Net Assets to Net Cash Provided By Operating Activities:		
Depreciation and Amortization	60,088	60,120
Changes in Certain Assets and Liabilities:		
Restricted Cash	(4,264)	(2,688)
Restricted Deposits	(2,485)	2,981
Prepaid Expenses	3,136	1,268
Accounts Payable	3,174	(331)
Security Deposits	—	500
Total Adjustments	<u>59,649</u>	<u>61,850</u>
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<u><u>\$ 7,928</u></u>	<u><u>\$ 9,549</u></u>

# Generally Accepted Accounting Principles Terminology

## ▶ Reserves

- ▶ Liquid assets like cash, investments.
- ▶ Generally used in discussion by boards of wanting to build reserves to a certain level to be able to operate for certain time period.

## ▶ Designations

- ▶ Unrestricted net assets subject to limits that are self-imposed by an organization's governing body.
  - ▶ Earmarked for future programs, projects, contingencies, purchase or construction of fixed assets.
  - ▶ Present board designated net assets as separate line item on the statement of financial position.

## ▶ Donor Restrictions

- ▶ Temporary Restrictions
  - ▶ Purpose or time restriction imposed by donor.
- ▶ Permanent Restrictions
  - ▶ Contribution to be held in perpetuity by the organization.
  - ▶ Do not expire with the passage of time and cannot be removed or fulfilled by organization actions.

# Preparing and Filing Form 990

- ▶ Organization type determines type of 990 filed
  - ▶ Form 990 - Gross receipts of \$200,000 or more **or** total assets of \$500,000
    - ▶ Public charities - 501(c)(3)
    - ▶ Trade Associations - 501(c)(6)
  - ▶ Form 990 EZ - Gross receipts < \$200,000 **and** total assets < \$500,000
    - ▶ Public charities - 501(c)(3)
    - ▶ Trade Associations - 501(c)(6)
  - ▶ Form 990-PF
    - ▶ Private foundation status results from the nature of organization's support or the lack of public supervision of its activities
  - ▶ Form 990T
    - ▶ Return that must be filed if an organization has gross receipts of \$1,000 or more of unrelated business income
      - ▶ Common example: Advertising income

# Preparing and Filing Form 990

## ▶ Filing Requirements

- ▶ Due on the 15<sup>th</sup> day of the 5<sup>th</sup> month following the organizations year end

- ▶ Example: June 30, 2016 year end would be due November 15, 2016.

## ▶ Extensions

- ▶ 3 months

- ▶ Additional 3 months after 1<sup>st</sup> extension



# Q&A

- ▶ Questions/Comments?