A Friendly Audit

Somehow, through a combination of interest, pressure, time available, guilty conscience about doing your share, etc., you've been appointed an auditor of some Meeting's financial books and been told it's a simple task.

You're not quite sure what that involves and would like to show up not quite completely ignorant at the time of the audit. You would also like to know a little of what you're expected to do or look for. This sheet will give you a rough start.

The primary tasks and responsibilities of an auditor are:

- Make sure all the assets claimed on the closing date are there, in the proper accounts.
- Check that the bank accounts have been reconciled on a monthly basis.
- Check if there are any liabilities on the closing date.
- Check to make sure that there is some system of checks and balances for income and expenses.

Balance Sheet:

The person (treasurer) whose books you are auditing should have prepared a financial statement (balance sheet) showing all the assets for which he/she is responsible at a given date (often 12/31 or 6/30). He/she should also have a similar statement one year earlier (or when he/she became responsible) which lists the assets and their values on the opening dates. He/she should be able to explain to you how the assets and their values on the opening sheet get to the assets and their values on the proposed closing sheet.

Assets:

The checking account usually has the most transactions and deserves attention. Look at the monthly bank statements, particularly the one at the closing date and make sure that the bank's balance is the same as the one the treasurer claims. Often the two do not quite match because there may be outstanding checks or deposits not yet received by the bank. The treasurer will explain this and his explanation is called a reconciliation.

A savings account or a money market fund is similarly handled.

Other financial assets, such as securities (investments: stocks, bonds, mutual funds) should show the number of shares and values on opening and closing dates. Mutual funds will send periodic statements that show these and so it is easy to check any changes that occurred during the period. Statements of banks, brokers or other custodians will show what securities (and changes in quantities) they hold. If the treasurer holds securities in a safe deposit box (rare these days) the safe deposit box should be visited and a list made for comparison.

Still other assets, such as real estate, leases, buses, etc., probably are not on relatively simple books and so are not dealt with here. If they do appear, ask the treasurer how he/she obtained the opening and year end values and if he/she applied any depreciation or amortization. Nod your head knowingly or ask more questions such as "What does that mean and is it realistic?" Then you can nod your head knowingly at the answer.

Trusts (over which the Meeting controls the investment management): These should be included on some investment account statement somewhere. This might be a Friends Fiduciary, bank or brokerage account statement. When reviewing, try to apply the ideas gleaned from above.

Accounts Receivable: hopefully none, but there might be the case where you have always received the income from a trust on Dec 31 but this year Dec 31 is on a Friday and the income doesn't actually arrive until Tuesday, Jan 4. In that case, in order to make a good consistent comparison with prior years it might show up as a receivable. (Alternatively, it can be shown as received on 12/31, sometimes known as keeping the books open until Jan 4th).

Liabilities:

Hopefully the books are on a cash basis, as opposed to an accrual basis. Look to see if the proposed liability really belongs in the accounting period. Example: If the treasurer has determined that a contractor is due a certain payment as of 12/31 but has not paid it by year end, it is a liability. But: If the electric bill comes in 12/20 for the period ending 12/10 but is not due until 1/5 it is not a liability. (It should, however, have been handled the same way last year). If there's a mortgage on the property, the current value of the mortgage will show as a liability. If you owe on an installment plan for some other asset, that unpaid balance is a liability.

Net Assets:

Net assets are the total of the assets minus the total liabilities. Sometimes there are restricted and unrestricted net assets and these should be listed separately. An example of a restricted asset might be the graveyard fund, while the checking account or general investment account is unrestricted.

Dealing with Restricted or Designated Funds:

Restricted funds are those funds that the donor or some legal document restricts. Designated funds are designated for use by the Meeting and the Meeting can change this designation.

Income only may be used for the Mary Brown Fund. If that is the case, then the principal of the fund is permanently restricted but the portion of the assets that represents the unspent income (probably checking account) is unrestricted. Suppose the Alfred Williams Fund permits only the income to be used and only for the Graveyard upkeep. Then the principal of that fund is permanently restricted and that portion of the assets that represents the unspent income is temporarily restricted, until it is spent on the graveyard. Suppose the Helen Enead Fund is available, principal and income, for scholarships. Then both the principal portion (probably investments) and the income portion (probably checking account) are temporarily restricted assets. In this case, the principal portion may be on the books for decades but it's still temporarily restricted. (Foundation grantors often restrict their grants for special programs and require careful accounting of expenditures. Often, too, they allow up to a certain percentage for overhead, which you may put into your organization's unrestricted general fund.)

Your meeting receives $20,000 as an unrestricted bequest. The meeting minutes its decision to use this gift for a new bathroom. This is then a designated fund. The money remains in the unrestricted assets but the treasurer should be tracking the use of this gift.

Statement of Revenues and Expenses:

The treasurer should also have a statement of revenues and expenses. Revenues will usually consist of gifts or contributions, interest, dividends, capital gains distributions, rent, or grants. Expenses include payments for utilities, building maintenance, babysitting, reimbursements for supplies, etc. The total expenses for the year will include recurring items and some one-time events. They should be compared to last year's totals and any major differences should be explained.

If you receive contributions from an individual of $250 or more, make sure that an acknowledgement goes out stating that no goods or services were supplied in return. A copy should be kept on the premises. Although the IRS does not require receipts for contributions below $250, it is a good practice to send receipts for all gifts.

Be careful about mortgage receipts; they are usually part interest and part return of capital (principal, or investment). In addition, when you sell an investment, part of the total receipt is return of your investment and part is either a gain or loss. Often, but not always, short term gains are considered income and long term gains are returned to principal.

Sample Monthly Meeting Income Statement

<Sample not available>

Sample Monthly Meeting Balance Sheet

<Sample not available>

Checking Account Expenditures:

Look at the endorsements on the backs of the canceled checks (or facsimiles). Spot check if there are numerous checks. Many banks, however, no longer return canceled checks, reducing bank charges. If there are checks written for large amounts to nonrecurring payees, ask for more documentation as to purpose. You might also want to check with the payee to confirm that they, in fact, received and cashed the check. If a check is made out to the treasurer or another signer on the account, ask for documentation or an "OK" from another responsible meeting member.

Payrolls are always a pain. If your organization has any sense it will use a payroll service, like Paychex, which will handle all the complexities, particularly the Federal, State, and Local tax reporting, and will prepare the paychecks as well as the Federal, State, and Local tax checks. There is a considerable risk of liability here if one is not up on all tax laws, forms, and changes in them.

Comments:

Don't hesitate to ask questions on what, why, how, when etc. Ask for examples of routine transactions and see how they're handled. Ask if there were any unusual transactions during the year (such as adding or disposing of an asset, a special emergency expenditure, acquiring a computer, or transferring cash to or from an investment account). Look at how they were handled. Ask how gains, realized and unrealized were handled. Listen to the treasurer's concerns: record retention, bonding, succession, security, asset mix, strategy, etc.

Be sure to find out where the books are kept in case a truck hits the treasurer. The "books" include ledgers, bank statements, IRS tax exempt number, wills, etc. If the records are kept on computer, please make sure that a back-up is regularly done (monthly would be good) and kept offsite. If the records are kept manually, copies of the account balances and statements should be kept offsite and updated regularly as well.

Prepare your auditor's report:

Often the Treasurer will have a draft ready for you to sign. It should say at a minimum that you have examined the treasurer's books, that you have verified the bank balances, naming the amounts, and that you have seen evidence of the value of the investments.

Final Comments:

Much of the above sounds dreadfully complicated but that's only because I have mentioned many items that are unlikely to show up on any particular audit. (I have also omitted many possibilities.) Most books have their own characteristic patterns as to what shows up on them year after year. In most cases, a given transaction has probably been handled the same way at some previous date, which can serve as a model. Don't sound too know-it-all or the next thing you know you will be the next treasurer. Being an auditor can be fun and you can get a much better understanding of your organization.

Prepared by Jack N. Childs, Jr.

Germantown Monthly Meeting, 9/2005