

## AUDIT

A financial audit is different from an IRS audit. A financial audit is an examination of your accounting records and financial statements by an independent auditor—normally, a certified professional accountant (CPA). The auditor is an independent professional hired and paid by your nonprofit.

The independent investigation is to test the accuracy of your accounting records and internal controls. At the conclusion of the audit, the auditor issues a report in the form of a letter stating whether, in the auditor's professional judgment, your accounting records and year-end financial statements fairly represent your nonprofit's financial position according to generally accepted accounting principles (GAAP). The auditor's letter is attached to the front of your financial statements. A clean bill of health from an auditor shows the world that you're keeping your books in a responsible manner.

The IRS does not require nonprofits to obtain audits. However, if an affiliate is granted any federal or state funded grants, they may be required to have an audit. In addition to any audit requirements by the Federal and/or state governments, some funders may require an affiliate undergo an independent audit as a condition of funding. The primary purpose of this is to ensure that the funder's money was properly spent.

An audit seems like a good idea, but if it is not absolutely required by the government or an important funding source, it may not be worth the money, especially for nonprofits with smaller incomes. Audits can cost over \$5,000. An audit is generally unnecessary for small nonprofits because they engage in a low number of financial transactions each year, and the veracity of their books can be checked in cheaper ways.

There are two cheaper alternatives to a full-blown independent audit. The first is called a review, which is like a mini-audit. A CPA examines your financial records, but much less thoroughly than in a full-blown audit. Unlike an audit, the CPA does not express an opinion as to whether your financial statements are in accordance with GAAP. Instead, the accountant merely states whether he or she is aware of any material modifications that should be made to the financial statements for them to be in conformity with GAAP. A review costs about half as much as an audit. Many funders will accept a review instead of an audit, but a review is not an audit and it may not be referred to as such.

The cheapest alternative to an audit is a compilation. This is where an accountant assembles your financial statements from the information you provide. The accountant does not subject your financial records to any audit or review and thus can express no opinion at all as to whether they comply with GAAP.