

SAN BRUNO

Community Foundation

Board of Directors

Nancy A. Kraus, *President* • John P. McGlothlin, *Vice President* • Emily Roberts, *Secretary* • Ben Cohn, *Treasurer*
Patricia Bohm • Frank Hedley • Regina Stanback Stroud
Leslie Hatamiya, *Executive Director*

AGENDA

SAN BRUNO COMMUNITY FOUNDATION

Special Meeting of the Audit Committee

June 23, 2015

4:30 p.m.

Meeting Location:

San Bruno Senior Center Library, 1555 Crystal Springs Road, San Bruno

In compliance with the Americans with Disabilities Act, individuals requiring reasonable accommodations or appropriate alternative formats for notices, agendas, and records for this meeting should notify us 48 hours prior to meeting. Please call the City Clerk's Office at 650-616-7058.

1. Call to Order

2. Roll Call

3. Conduct of Business

- a. Elect Audit Committee Chair
- b. Review and Approve Request for Proposal for Audit Services and Provide Direction to Executive Director on Next Steps in the Auditor Selection Process

4. Public Comment: Individuals are allowed three minutes, groups in attendance, five minutes. If you are unable to remain at the meeting, contact the President to request that the Board consider your comments earlier. It is the Board's policy to refer matters raised in this forum to staff for research and/or action where appropriate. The Brown Act prohibits the Board from discussing or acting upon any matter not agendized pursuant to State Law.

5. Adjourn

SAN BRUNO

Community Foundation

Memorandum

DATE: June 22, 2015
TO: Audit Committee, San Bruno Community Foundation
FROM: Leslie Hatamiya, Executive Director
SUBJECT: Election of Chair

Article VII, Section 5, of the San Bruno Community Foundation's Bylaws establishes an Audit Committee consisting of at least two members of the Board of Directors.

On March 19, 2015, the San Bruno Community Foundation Board approved the appointment of Vice President John McGlothlin and Board Member Patricia Bohm to the Audit Committee. At that time, the Board did not designate a Committee chair.

Identifying a Committee chair would help ensure the proper functioning of the Committee, including providing guidance in the development of the Committee's meeting agendas and running the Committee's meetings. At its first meeting on June 23, 2015, I recommend that the Committee elect one Committee Member to serve as its chair.

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Memorandum

DATE: June 22, 2015

TO: Audit Committee, San Bruno Community Foundation

FROM: Leslie Hatamiya, Executive Director

SUBJECT: Request for Proposals for Audit Services

Article XIII, Section 4, of the San Bruno Community Foundation's Bylaws states that the Foundation "shall retain an[] independent auditor and conduct annual independent audits (commencing with Section 12586(d) of the California Government Code)." Article VII, Section 5, of the Bylaws establishes an Audit Committee whose duties include "[a]ssisting the Board in choosing an independent auditor and recommending termination of the auditor, if necessary."

The Foundation received and spent funds for the first time during the 2014-2015 fiscal year, which concludes on June 30. As a result, it is now time for the Audit Committee to begin the process of securing the services of an independent certified public accounting (CPA) firm to provide audit and related services.

Nonprofits generally require annually the following from an auditor:

- Conduct an audit of the organization's records, internal controls, and financial statements in accordance with auditing standards generally accepted in the United States,
- Communicate with the Audit Committee as appropriate, before, during, and after audit fieldwork,
- Complete an audit report of Foundation financial statements with appropriate accompanying notes,
- Complete a report to management, which includes recommendations on strengthening internal controls and/or operations,
- Present the audit report and the report to management to the organization's Board of Directors, and
- Complete federal and state tax forms (IRS-990, CA-199, and RRF-1) by the applicable deadlines.

I recommend that the Foundation follow this typical process for hiring an auditor:

- Draft a Request for Proposals (RFP) for Audit Services
- Send the RFP to CPA firms that provide nonprofit audit and related services, including firms recommended by other nonprofit organizations

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Memorandum

- Receive, by a set deadline, responses to the RFP
- Review the responses and select a small number of finalists for consideration
- Interview finalists, request additional information as needed, and check references
- Make a recommendation to the Board for selection of a CPA firm for audit and related services

Consistent with this process, I am proposing the following timeline for the selection of the Foundation's first independent auditor:

- June 23: Audit Committee finalizes an RFP for Audit Services and prepares list of CPA firms to receive RFP
- June 29: Audit Committee shares the RFP and reports on the timeline to the Board
- June 30: Executive Director begins sending RFP to list of CPA firms
- July 31: Deadline for receiving responses to RFP
- August-early September: Audit Committee reviews RFP responses, selects list of finalists, conducts interviews, and checks references
- September: Audit Committee makes recommendation to the Board for approval

The audit and preparation of tax returns would then take place from late September through early November. The federal and state tax forms are due on November 15 (the Foundation may request a three-month extension if additional time is needed).

As the first step in the process, I have prepared the attached first draft of an RFP for audit services for the Audit Committee to review and edit at its June 23 meeting. The draft RFP provides background information on the Foundation, a list of expected annual audit and tax services deliverables, the list of information sought from responding CPA firms, and the deadline for responses. The goal for the Committee will be to finalize the RFP for presentation to the full Board at its June 29 special meeting.

Also attached is the beginning of a list of Bay Area CPA firms to whom the Foundation may want to send the RFP. These firms have been recommended by other nonprofit organizations or are known to have nonprofit audit practices. The Committee will have the opportunity to edit the list of CPA firms at the Committee meeting.

As background information related to the Audit Committee's role and the purpose of an audit, I have attached several articles to inform the Committee's discussion:

- "Get the Most Value from Your Audit," from *Blue Avocado*, August 29, 2011.
- "The Sarbanes-Oxley Act and Implications for Nonprofit Organizations," by BoardSource and Independent Sector, revised 2006 (summary and full report).

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Community Foundation

REQUEST FOR PROPOSAL

June __, 2015

The San Bruno Community Foundation (“Foundation”) requests a proposal for the annual audit of its financial statements and preparation of state and federal information returns (IRS-990, CA-199, and RRF-1).

The Foundation is a nonprofit entity incorporated in California, with federal income tax exemption issued under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended. The Foundation is classified as a public charity and, under Section 509(a)(3), as a Type I supporting organization.

The Foundation is the organization created by the San Bruno City Council to administer the \$70 million in restitution funds resulting from the devastating 2010 gas pipeline explosion in San Bruno’s Crestmoor neighborhood. As stated in the Foundation’s bylaws, the primary purpose of the Foundation is “to benefit the San Bruno community through enduring and significant contributions to, and investments in, charitable and community programs, and publicly owned community facilities, over the long term.”

A seven-member Board of Directors appointed by the City Council governs the Foundation. The Board has a two-member Audit Committee that is overseeing the auditor selection process. The Foundation’s fiscal year runs from July 1 to June 30.

The Foundation was founded in 2013 and began independent operations in early 2015. In 2013-2014, the Foundation reported revenues and expenses of \$0, as the City has held the restitution funds in a custodial account. For 2014-2015, total revenue is projected at \$491,031 (receipt of the first tranche of restitution funds), and total projected expenses are \$315,552 (which included reimbursement to the City for costs incurred in the formation of the Foundation through January 2015). The Foundation expects to receive the balance of the restitution funds in 2015-2016, with total revenue for that fiscal year budgeted at \$69,627,658 and total expenses currently projected at \$335,774. The Foundation is in the process of determining its initial program and investment strategies and will likely amend the 2015-2016 budget in the fall to reflect adoption of those strategies.

Currently, the Foundation employs one full-time staff person and one part-time contractor (accounting consultant/full charge bookkeeper). In the four months since bank accounts were opened, vendor and reimbursement payments have averaged less than 10 per month. In addition to savings, payroll, and general checking accounts, the Foundation has a credit card account in the name of SBCF and the Executive Director.

EXPECTED ANNUAL AUDIT & TAX SERVICES DELIVERABLES

The selected auditor or CPA firm will be expected to do the following annually:

1. Conduct an audit of the Foundation's records, internal controls, and financial statements in accordance with auditing standards generally accepted in the United States of America.
2. Communicate with the Audit Committee as appropriate, before, during, and after audit fieldwork.
3. Complete an audit report of Foundation financial statements with appropriate accompanying notes.
4. Complete a report to management, which includes recommendations on strengthening internal controls and/or operations.
5. Present both reports mentioned in numbers 3 and 4 above to the Foundation Board of Directors at its October meeting.
6. Complete IRS-990, CA-199, and RRF-1 by November 1, thereby allowing for timely filing of these forms on or before November 15.

INFORMATION AND/OR RESPONSES TO BE PROVIDED

In order to assist the Board of Directors in its search for an auditor to provide the services described above, please provide, by July 31, 2015, a proposal that includes responses to the following:

1. Please describe your firm's background, history, and areas or industries of specialization. In particular, please highlight your experience with 501(c)(3) nonprofit organizations, particularly those with assets of at least \$50 million. Please include the names of any principals of the firm and their backgrounds. Also, please provide a copy of your firm's annual report (if any) and/or other literature about your firm.
2. Please provide the location of your office(s) and the names and titles of personnel that are expected to be involved in the Foundation's annual audit and tax services.
3. Please provide a proposed timeline for fieldwork and final reporting for all services requested.
4. Does your firm have a written Code of Conduct, Ethics Policy, or Conflict of Interest Policy? If so, please provide a copy of each.
5. Please describe the level of coverage for errors and omissions and professional liability insurance your firm carries. List the insurance carrier(s) supplying the coverage.
6. Has your firm, or anyone in your firm, provided any gifts, travel and room expenses, entertainment, or meals to any Foundation Board member or employee during the past 12 months? If yes, please describe in detail.
7. What do you feel makes your firm superior to other firms that the Foundation may be considering?
8. Provide a list of other non-profit 501(c)(3) clients for whom your firm provides annual audit services. Also, please provide a sample of your audit reports for such organizations.
9. Please provide a reference to three of your non-profit 501(c)(3) clients who have hired your firm for annual audit services during the past five years.
10. What will be your fee for completing all services described above in the "Expected Annual Audit & Tax Services Deliverables" section of this RFP? Will these fees be constant for two or more years? If not, what is your normal fee increase from year to year? Do you provide

any financial incentives for clients who are particularly well prepared and organized in preparing for the audit?

11. Does the fee described above differ from fees charged to other clients? If yes, please explain.
12. Describe any other potential fees that the Foundation may be subject to based upon common situations with other clients.
13. Include a copy of your firm's pre-audit requests for information that your clients are required to provide, including any worksheets and questionnaires. How far in advance of the site visit must the information be submitted to your firm?
14. Include a copy of your firm's most recent peer review report, the related letter of comments, and the firm's response to the letter of comments.
15. Provide any additional information that you believe to be relevant to the Request for Proposal and your capability to provide the services requested.

Basis for award of contract will include but not be limited to responsiveness to the RFP, interview performance, quality and timeliness of service, and price.

Only licensed Certified Public Accountants or firms may respond to this RFP. The Foundation reserves the right to reject all proposals or request additional information from one or more proposers. All costs incurred in the preparation of a proposal responding to this RFP will be the responsibility of the proposer and will not be reimbursed by the Foundation.

The successful proposer agrees to execute a professional services agreement for the work in a form substantially similar to that attached hereto.

Submit proposals by July 31, 2015, to:

San Bruno Community Foundation
Attn: Audit Committee
901 Sneath Lane, Suite 209
San Bruno, CA 94066
lhatamiya-sbcf@sanbruno.ca.gov

Questions? Please contact Leslie Hatamiya, Executive Director, at lhatamiya-sbcf@sanbruno.ca.gov or (650) 922-1223.

SAN BRUNO

Community Foundation

AGREEMENT FOR PROFESSIONAL SERVICES

This agreement (“Agreement”) is entered into by and between the San Bruno Community Foundation, the “Foundation,” a California 501(c)(3) nonprofit corporation, and _____, a [insert form: corporation of __, limited liability corporation, sole proprietor], with offices located in _____ (“Contractor”). Its purpose is to clearly define the responsibilities and compensation of the Contractor.

1. **Relationship.** During the term of this Agreement, Contractor will provide professional services (the “Services”) to the Foundation as described on Exhibit A attached to this Agreement. Contractor represents that Contractor is duly licensed (as applicable) and has the qualifications, the experience and the ability to properly perform the Services in a manner commensurate with community professional standards. Contractor shall use Contractor’s best efforts to perform the Services such that the results are satisfactory to the Foundation. Contractor shall maintain a City of San Bruno business license during the term of this Agreement.

2. **Fees.** As consideration for the Services to be provided by Contractor and other obligations, the Foundation shall pay to Contractor the amounts specified in Exhibit B attached to this Agreement at the times specified therein.

3. **Expenses.** Contractor shall not be authorized to incur on behalf of the Foundation any expenses without the prior consent of the Foundation’s Executive Director, whose consent shall be evidenced in writing for any expenses in excess of \$100.00. As a condition to receipt of reimbursement, Contractor shall be required to submit to the Foundation reasonable evidence that the amount involved was expended and related to Services provided under this Agreement.

4. **Term and Termination.** Contractor shall provide Services to the Foundation for a period commencing on _____, and terminating on _____. However, the Relationship shall terminate prior to such date if Contractor shall have been paid the maximum amount of fees as provided in Exhibit B, unless otherwise agreed to in writing.

Notwithstanding the above, either party may terminate this Agreement at any time upon two weeks’ written notice. In the event of such termination, Contractor shall be paid for any portion of the Services that have been performed prior to the termination.

5. **Background Check.** Contractor agrees to undergo credit and criminal background checks, and this Agreement is contingent on the successful completion of such checks.

6. **Independent Contractor.** Contractor’s relationship with the Foundation will be that of an independent contractor and not that of an employee.

a. **Method of Provision of Services.** Contractor shall be solely responsible for determining the method, details and means of performing the Services. Contractor may, at Contractor’s own expense, employ or engage the service of such employees or subcontractors as Contractor deems necessary to perform the Services required by this Agreement. Such employees or

subcontractors are not employees of the Foundation, and Contractor shall be wholly responsible for the professional performance of the Services by his employees and subcontractors such that the results are satisfactory to the Foundation.

b. **No Authority to Bind Foundation.** Neither Contractor nor any partner, agent, or employee of Contractor has authority to enter into contracts that bind the Foundation or create obligations on the part of the Foundation without the prior written authorization of the Foundation.

c. **No Benefits.** Contractor acknowledges and agrees that Contractor (or Contractor's employees, if Contractor is an entity) will not be eligible for any Foundation employee benefits and, to the extent Contractor (or Contractor's employees, if Contractor is an entity) otherwise would be eligible for any Foundation employee benefits but for the express terms of this Agreement, Contractor (on behalf of itself and its employees) hereby expressly declines to participate in such Foundation employee benefits.

d. **Tax Indemnification.** Contractor shall have full responsibility for applicable withholding taxes for all compensation paid to Contractor, its partners, agents or its employees under this Agreement, and for compliance with all applicable labor and employment requirements with respect to Contractor's self-employment, sole proprietorship or other form of business organization, and Contractor's partners, agents and employees, including state worker's compensation insurance coverage requirements and any U.S. immigration visa requirements. Contractor agrees to indemnify, defend and hold the Foundation harmless from any liability for, or assessment of, any claims or penalties with respect to such withholding taxes, labor or employment requirements, including any liability for, or assessment of, withholding taxes imposed on the Foundation by the relevant taxing authorities with respect to any compensation paid to Contractor or Contractor's partners, agents, or its employees.

e. **Liability Indemnification.** Contractor shall indemnify, defend, and hold the Foundation, its Board of Directors, officers, agents, employees, and the City of San Bruno harmless from any and all claims, damages, losses, causes of action, and demands, including reasonable attorney's fees and costs, incurred in connection with or in any manner arising out of Contractor's performance of the work contemplated by this Agreement. Acceptance of this Agreement constitutes that the Contractor is not covered under the Foundation's general liability insurance, employee benefits, or worker's compensation insurance. It further establishes that the Contractor shall be fully responsible for such coverage.

f. **Insurance.** Contractor shall return an executed copy of this Agreement with proof of insurance and endorsements to insurance coverage satisfactory to the Foundation that shows that on or before beginning any of the services or work called for by any term of this Agreement, Contractor, at its own cost and expense, shall carry, maintain for the duration of the Agreement insurance coverage naming the Foundation, its officers, officials and employees, as well as the City of San Bruno, as additional insureds, as follows: i) statutory Workers' Compensation Insurance and Employer's Liability Insurance for any and all persons employed directly or indirectly by Contractor with limits not less than \$1,000,000, [If the Contractor has no employees, it need not carry worker's compensation and employer liability insurance and this may be deleted] ii) Commercial General and Automobile Liability insurance in an amount not less than \$1,000,000 per occurrence, and c) [If there is no standard professional liability insurance or errors or omissions insurance generally available for the particular service then this may be deleted] professional liability

insurance for licensed professionals performing work pursuant to this agreement in an amount not less than \$1,000,000 covering the licensed professionals' errors and omissions. Contractor shall not allow any subcontractor to commence work on any subcontract until all insurance required of the Contractor has also been obtained for the subcontractor.

7. **Supervision of Contractor's Services.** All of the Services to be performed by Contractor, including but not limited to the Services, will be as agreed between Contractor and the Executive Director. Contractor will be required to report to the Executive Director concerning the Services performed under this Agreement. The nature and frequency of these reports will be left to the discretion of the Executive Director. The Executive Director is responsible for the retention of Contractor's services and agreement on scope of work.

8. **Assignment and Subcontracting.** Contractor shall not assign this Agreement or any portion thereof to a third party without the prior written consent of the Foundation, and any attempted assignment without such prior written consent in violation of this Section shall automatically terminate this Agreement. Unless otherwise specified in Exhibit A, Contractor shall not subcontract any portion of the performance contemplated and provided for herein without prior written approval of the Foundation.

9. **Discrimination and Harassment Prohibited.** Contractor will comply with all applicable local, state, and federal laws and regulations prohibiting discrimination and harassment.

10. **Confidential Information.** Contractor agrees at all times during the term of this Agreement and thereafter to hold in strictest confidence and not to use, except for the benefit of the Foundation to the extent necessary to perform under this Agreement, or to disclose to any person, firm, corporation, or other entity, without written authorization of the Board of Directors of the Foundation, any Confidential Information of the Foundation. Contractor further agrees not to make copies of such Confidential Information except as authorized by the Foundation. As used in this Agreement, the term "Confidential Information" means information pertaining to any aspects of the Foundation's business which is either information not known by the general public or is proprietary information of the Foundation or its affiliates, whether of a technical nature or otherwise.

11. **Ownership of Documents.** All work product produced by Contractor or its agents, employees, and subcontractors pursuant to this Agreement is the property of the Foundation. In the event this Agreement is terminated, all work product produced by Contractor or its agents, employees, or subcontractors shall be delivered at once to the Foundation.

12. **Retention of Records.** Contractor shall maintain all records related to this Agreement for no less than three years after the Foundation makes final payment or after termination of this contract and all other pending matters are closed. All records shall be subject to the examination and/or audit by agents of the Foundation.

13. **Conflict of Interest.**

a. **In General.** Contractor represents and warrants that, to the best of the Contractor's knowledge and belief, there are no relevant facts or circumstances that could give rise to a "conflict of interest," as that term is defined in the Political Reform Act, as codified at California Government Code Section 81000, et seq., on the part of the Contractor, or that Contractor has already disclosed all such relevant information in writing.

b. **Subsequent Conflict of Interest.** Contractor agrees that if an actual or potential conflict of interest in the part of the Contractor is discovered after award, the Contractor will make a full disclosure in writing to the Foundation. This disclosure shall include a description of the actions, which the Contractor has taken or proposes to take, after consultation with the Foundation to avoid, mitigate, or neutralize the actual or potential conflict and shall take all such steps within thirty (30) days.

c. **Interests of Foundation Officers, Board Members, and Staff.** No officer, board member or employee of the Foundation shall have any pecuniary interest, direct or indirect, in this Agreement or the proceeds thereof. Neither Contractor nor any member of the Contractor's family shall serve on any Foundation board or committee or hold any such position which either by rule, practice, or action nominates, recommends, or supervises Contractor's operations or authorizes funding Contractor.

14. **Conflicts with this Agreement.** Contractor represents and warrants that neither Contractor nor any of Contractor's partners, employees, or agents is under any pre-existing obligation in conflict or in any way inconsistent with the provisions of this Agreement. Contractor represents and warrants that Contractor's performance of all the terms of this Agreement will not breach any agreement to keep in confidence proprietary information acquired by Contractor in confidence or in trust prior to commencement of this Agreement. Contractor warrants that Contractor has the right to disclose and/or use all ideas, processes, techniques and other information, if any, which Contractor has gained from third parties, and which Contractor discloses to the Foundation or uses in the course of performance of this Agreement, without liability to such third parties. Notwithstanding the foregoing, Contractor agrees that Contractor shall not bundle with or incorporate into any deliveries provided to the Foundation herewith any third party products, ideas, processes, or other techniques, without the express, written prior approval of the Foundation. Contractor represents and warrants that Contractor has not granted and will not grant any rights or licenses to any intellectual property that would conflict with Contractor's obligations under this Agreement. Contractor will not knowingly infringe upon any copyright, trade secret, or other property right of any former client, employer, or third party in the performance of the Services required by this Agreement.

15. **Miscellaneous.**

a. **Amendments and Waivers.** Any term of this Agreement may be amended or waived only with the written consent of the parties.

b. **Sole Agreement.** This Agreement, including the Exhibits hereto, constitutes the sole agreement of the parties and supersedes all oral negotiations and prior writings with respect to the subject matter hereof.

c. **Notices.** Any notice required or permitted by this Agreement shall be in writing and shall be deemed sufficient upon receipt, when delivered personally or by courier, overnight delivery service or confirmed facsimile, 48 hours after being deposited in the regular mail as certified or registered mail (airmail if sent internationally) with postage prepaid, if such notice is addressed to the party to be notified at such party's address or facsimile number as set forth below, or as subsequently modified by written notice.

d. **Choice of Law.** The validity, interpretation, construction and performance of this Agreement shall be governed by the laws of the State of California, without giving effect to the principles of conflict of laws.

e. **Severability.** If one or more provisions of this Agreement are held to be unenforceable under applicable law, the parties agree to renegotiate such provision in good faith. In the event that the parties cannot reach a mutually agreeable and enforceable replacement for such provision, then (i) such provision shall be excluded from this Agreement, (ii) the balance of the Agreement shall be interpreted as if such provision were so excluded and (iii) the balance of the Agreement shall be enforceable in accordance with its terms.

f. **Counterparts.** This Agreement may be executed in counterparts, each of which shall be deemed an original, but all of which together will constitute one and the same instrument.

g. **Alternative Dispute Resolution.** If any dispute arises between the parties that cannot be settled after engaging in good faith negotiations, the Foundation and Contractor agree to resolve the dispute in accordance with the following:

i. Each party shall designate a senior management or executive level representative to negotiate any dispute.

ii. The representatives shall attempt, through good faith negotiations, to resolve the dispute by any means within their authority.

iii. If the issue remains unresolved after ten (10) days of good faith negotiations, the parties shall attempt to resolve the disagreement by negotiation between legal counsel. If the above process fails, the parties shall resolve any remaining disputes through mediation to expedite the resolution of the dispute.

iv. The mediation process shall provide for the selection within 15 days by both parties of a disinterested third person as mediator, shall be commenced within 30 days and shall be concluded within 15 days from the commencement of the mediation.

v. The parties shall equally bear the costs and fees of any third party in any alternative dispute resolution process.

vi. The alternative dispute resolution process is a material condition to this Agreement and must be exhausted as an administrative remedy prior to either Party initiating legal action. This alternative dispute resolution process is not intended to nor shall be construed to change the time periods for filing a claim or action specified by Government Code § 900, et. seq.

h. **Advice of Counsel.** EACH PARTY ACKNOWLEDGES THAT, IN EXECUTING THIS AGREEMENT, SUCH PARTY HAS HAD THE OPPORTUNITY TO SEEK THE ADVICE OF INDEPENDENT LEGAL COUNSEL, AND HAS READ AND UNDERSTOOD ALL OF THE TERMS AND PROVISIONS OF THIS AGREEMENT. THIS AGREEMENT SHALL NOT BE CONSTRUED AGAINST ANY PARTY BY REASON OF THE DRAFTING OR PREPARATION HEREOF.

[Signature Page Follows]

The parties have executed this Agreement on the respective dates set forth below.

SAN BRUNO COMMUNITY FOUNDATION

By: Leslie Hatamiya

Title: Executive Director

Signature: _____

Address: 901 Sneath Lane, Suite 209, San Bruno, CA 94066

Date: _____

NAME OF CONTRACTOR

By: _____

Title: _____

Signature: _____

Address: _____

Date: _____

EXHIBIT A

DESCRIPTION OF SERVICES

EXHIBIT B

COMPENSATION

Suggested Bay Area CPA Firms with Nonprofit Practices

As of June 22, 2015

Armanino - San Francisco
Bedinger & Company - Concord
Cook & Company - San Francisco
Crosy & Kaneda - Oakland
Frank, Rimerman + Co. LLP - Palo Alto/San Francisco
Harrington Group - San Francisco/Pasadena
Hood & Strong – San Francisco
Lamorena & Chang CPA - San Francisco
PMB Helin Donovan - San Francisco
Seiler LLP - San Francisco/Redwood City

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Get the Most Value from Your Audit

Get the Most Value from Your Audit

[Board Cafe](#) [1] • [Finance & Strategy](#) [2] • By Dennis Walsh, CPA • August 29, 2011 • [Email](#) [3]

[Print](#) [4]



*Audits are expensive in terms of money, staff time, and board attention. CPA **Dennis Walsh** tells us how to wring the most value from them:*

An IRS tax audit has been described as an autopsy without the benefit of death. The financial statement audit -- done by an independent CPA, not the IRS -- can be seen by nonprofits as only slightly more appealing.

Many nonprofits have annual CPA audits, but the executive director and/or the board's finance or audit committee may be unsure whether they are getting the most out of the audit. A worthwhile question for the board to ask might be: "Are we getting the most out of this significant investment of money and time?"

We have developed two questionnaires to help you answer this question. The first looks at whether your auditor is doing a good job for you. The second questionnaire looks at whether your nonprofit is doing its part in utilizing the audit. (The questionnaires can also be downloaded as a Word document; see link at end of article.)

But first, why have an audit, anyway?

Benefits of a good audit relationship

An unqualified audit opinion -- a "clean audit" -- is a statement by the auditor that the financial statements are a fair and accurate representation of your organization's financial situation. As Jeanne Bell of CompassPoint Nonprofit Services pointed out in a [Blue Avocado article](#) [5], an audit can have the following major benefits:

- Enhances donor and community confidence
- Demonstrates commitment to fiscal accountability
- Moves the nonprofit toward best financial practices (through auditor feedback)
- Encourages accounting discipline
- Provides limited deterrent to fraud

The better the relationship with your audit firm, as expressed by the following indicators of a good audit relationship, the more of these benefits you can expect to realize:

- Trust
- Independence
- Communication
- Competence
- Timeliness
- Value

These two questionnaires are tools to help you sample for the presence of these qualities. It is not a checklist for a clean audit report or intended to assign blame for shortcomings, but rather looks for qualities inherent in a well-functioning audit relationship.

It's important that you be willing to invest some time finding out what's at the core of any "no" answers.

Is our auditor doing a good job for us?

- | | | |
|----|---|--|
| 1 | Does audit planning begin well in advance of fiscal year-end? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 2 | Does the auditor prepare an audit engagement letter that is discussed in advance of the audit? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 3 | Are changes in the audit fee (from the prior year) adequately explained in advance? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 4 | Has the auditor informed you of any audit-related tasks that can be performed by your staff or outsourced at lower, non-audit rate? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 5 | Does the auditor give your staff enough time and adequate instruction to gather and prepare documents, where permissible, to assist in audit field work? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 6 | Is audit field work conducted without frequent interruptions and delays? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 7 | Does the auditor make it clear through words and behaviors that the client is the board, not the staff? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 8 | Is the audit firm sensitive to timely completion of IRS Form 990, grantor reports, and government agency filings prepared in conjunction with the audit? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 9 | Does the auditor demonstrate proficiency with nonprofit issues such as accounting for pledges and multi-year grants, donated goods, recognition of qualifying volunteer services, classification of restricted donations, etc.? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 10 | Does the auditor explain the reasons for any proposed adjustments to the financial statements and anything you should do differently in the future related to those adjustments? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 11 | Does the auditor give you the chance (and the time) to respond to the draft audit, footnotes, and management letter? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 12 | Has the auditor been willing to consider changes in above based on a discussion? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 13 | If the auditor makes changes to your preferred financial statement format (such as the level of detail on the balance sheet, horizontal or vertical presentation, and so forth), have you discussed the changes in advance? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 14 | Does the auditor meet with the board (or a board committee) without staff present? | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |
| 15 | Is the audit report issued by the date | <input type="checkbox"/> yes <input type="checkbox"/> no <input type="checkbox"/> don't know |

Reluctance to change auditors

Whatever their past audit experience, however, organizations are often reluctant to tamper with what feels like a successful service relationship. After all, if it isn't broken, why fix it?

A common attitude among small organizations in particular is that although we get written up for accounting deficiencies, we still receive an unqualified audit opinion from year to year. But an unqualified opinion along with what seems like a good relationship with the auditors doesn't guarantee that the organization is getting what it is paying for in the audit experience.

Assessing your answers

The greater the number of "no" answers, the more the board should address audit matters with priority. Consult with your CPA audit principal to determine underlying reasons for "no" answers and develop an action

- specified in the audit engagement letter? yes no don't know
- 16 Does the auditor press for implementation of solutions to recurring accounting and internal control deficiencies? yes no don't know
- 17 Is there low or moderate turnover in the audit team from year to year? yes no don't know
- 18 If an audit is not mandated by one of your funders, has the audit partner indicated a willingness to explain to the board from time to time whether a different type of service – such as a review – might accomplish your governance and accountability needs? yes no don't know
- 19 As your organization has changed, do you feel the planning and conduct of your audit has kept up with the changes? (examples: different activities, larger staff, smaller staff, changes in funding sources) yes no don't know

Are we doing a good job managing our audit?

- 1 Does the board (as opposed to management staff) lead the decision in choosing an auditor? yes no don't know
- 2 Do senior staff (as opposed to the auditor) make all decisions on accounting methods, such as basis of accounting, depreciation methods, asset useful life, when to reclassify restricted grants, when to recognize pledges, and so forth? yes no don't know
- 3 Do one or more board members understand the reasons for the choices made above? yes no don't know
- 4 Does the board (or a board committee) meet annually with the auditor without staff present? yes no don't know
- 5 Is the substance of that meeting reported to the full board? yes no don't know
- 6 Are we satisfied that neither we nor the auditor is becoming complacent with the relationship? yes no don't know
- 7 Does the staff exhibit a proper distance from the auditor (as opposed to a complacent relationship)? yes no don't know
- 8 In addition to evaluating audit expense, has the board (or a board committee) considered the size, nonprofit audit experience, and other credentials of the audit firm? yes no don't know
- 9 Are copies of the audit and the management letter given to all members of the board? yes no don't know
- 10 Does the board review the audit relationship every three years, or more often if there are any problems? yes no don't know
- 11 Has the staff responded appropriately to comments in the management letter? yes no don't know
- 12 Not part of the audit but related: Does senior staff other than finance staff review the draft 990 before it is finalized (in particular to look at areas such as Program Accomplishments)? yes no don't know

plan to remedy the issues, with consideration to any contributing factors from the organization as well as what the audit firm can do to help spur you on to better practices.

Identifying causes of perceived complacency in the audit relationship can be much thornier. Since the audit depends on a cooperative partnership among the board, staff, and audit team, there is usually some degree of shared responsibility where expectations aren't met. Here in particular, board and management must resist the temptation to point fingers and remember that the board, not the audit firm, is ultimately responsible for the quality of the audit relationship.

Bear in mind that recurring deficiencies due to structural issues such as unwillingness to invest in accounting systems, training, or staffing, for example, will take more time and resources to remedy than adjusting the timing of audit field work to lessen disruptions to your activities.

Tip: If your organization's staff struggle to prepare GAAP financial statements prior to the audit, consider having the statements initially prepared (compilation engagement) by a second CPA firm at a lower, non-audit billing rate. This can also enhance audit firm independence, reduce overall cost, and help avoid the common management letter comment regarding inadequate accounting

personnel.

If you decide that issues with the current audit firm can't be worked out, then it's time to look for a successor. But be careful, deliberative, and if you must, part with your current auditors gracefully. (And watch for an upcoming *Blue Avocado* article on finding a new auditor.)

Concluding thought

Although some nonprofits dread the annual audit as something to be endured, the audit is an exercise in good governance and accountability. In practical terms, this means that the financial statements are judged to portray the organization's financial condition fairly and completely. And valuable management advice is a natural by-product of a good audit relationship. You consume considerable resources being accountable to your stakeholders: get the most from it.

[To download a free copy of this article in Word to make it easy for you to adapt the questionnaire to your own organization, click [here](#) [6].]

Thanks to Dane Byers, CPA, of [Bassett & Associates, PA](#) [7], in Raleigh, NC, and Steve Zimmerman, CPA, of [Spectrum Nonprofit Services](#) [8] in Milwaukee, WI, for their feedback in the development of this article.

Dennis Walsh, CPA, volunteers his post-retirement time helping North Carolina nonprofits with accounting concerns, work for which he recently received the Community Service Award from the [Guilford Nonprofit Consortium](#) [9]. He shares his expertise nationally with nonprofits through [Blue Avocado](#). Through the [Deborah and Dennis Walsh Foundation](#) [10], he has also published "Legal & Tax Issues for North Carolina Nonprofits" and [Man From Macedonia](#) [11], a memoir by civil rights leader Aaron Johnson. To right you can see him discussing an audit of Civil War expenses with Mr. Lincoln.



See also in *Blue Avocado*:

- [Is It Time for an Audit?](#) [5] by Jeanne Bell
- [Seven Ways to Reduce Your Audit Costs](#) [12] by Dennis Walsh

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Sarbanes-Oxley Act and Implications for Nonprofits

Created to rebuild public trust in the corporate community in the wake of corporate and accounting scandals, the federal legislation that has become known as the Sarbanes-Oxley Act requires publicly traded companies conform to new standards in financial transactions and audit procedures. As state officials explore ways to apply elements of the law to the nonprofit sector, BoardSource and Independent Sector offer the publication, *The Sarbanes-Oxley Act and Implications for Nonprofit Organizations*, which provides nonprofit leaders practical recommendations on promoting effective oversight of their organizations.

Independent Sector and BoardSource recommend that nonprofits voluntarily incorporate certain provisions of the Act that make good governance sense.

A checklist for nonprofits and foundations includes:

1. Insider Transactions and Conflicts of Interest

- Understand and fully comply with all laws regarding compensation and benefits provided to directors and executives (including "intermediate sanctions" and "self-dealing" laws).
- Do not provide personal loans to directors and executives.
- In cases in which the board feels it is necessary to provide a loan, however, all terms should be disclosed and formally approved by the board, the process should be documented, and the terms and the value of the loan should be publicly disclosed.
- Establish a conflict of interest policy and a regular and rigorous means of enforcing it.

2. Independent and Competent Audit Committee

- Conduct an annual external financial audit (the boards of very small organizations, for whom the cost of an external audit may be too burdensome, should at least evaluate carefully whether an audit would be valuable).
- Establish a separate audit committee of the board.
- Board members on the audit committee should be free from conflicts of interest and should not receive any compensation for their service on the committee.
- Include at least one "financial expert" on the audit committee.
- The audit committee should select and oversee the auditing company and review the audit.
- Require full board to approve audit results.
- Provide financial literacy training to all board members.

3. Responsibilities of Auditors

- Rotate auditor or lead partner at least every five years.
- Avoid any conflict of interest in staff exchange between audit firm and organization.
- Do not use auditing firm for non-auditing services except tax form preparation with pre-approval from audit committee.
- Require disclosure to audit committee of critical accounting policies and practices.
- Use audit committee to oversee and enforce conflict-of-interest policy.

4. Certified Financial Statements

- CEO and CFO should sign off on all financial statements (either formally or in practice), including Form 990 tax returns, to ensure they are accurate, complete, and filed on time.
- The board should review and approve financial statements and Form 990 tax returns for completeness and accuracy.

5. Disclosure

- Disclose Form 990 and 990-PF in a current and easily accessible way (also required of all nonprofit organizations by IRS law).
- File 990 and 990-PF Forms in a timely manner, without use of extensions unless required by unusual circumstances.
- Disclose audited financial statements.
- Move to electronic filing of Form 990 and 990-PF.

GOVERNANCE RESOURCES

PRINCIPLES FOR GOOD

PRINCIPLES RESOURCE CENTER

IRS FORM 990



6. Whistle-Blower Protection

- Develop, adopt, and disclose a formal process to deal with complaints and prevent retaliation.
- Investigate employee complaints and correct any problems or explain why corrections are not necessary.

7. Document Destruction

- Have a written, mandatory document retention and periodic destruction policy, which includes guidelines for electronic files and voicemail.
- If an official investigation is underway or even suspected, stop any document purging in order to avoid criminal obstruction.

For a discussion of the law and recommendations for nonprofits and foundations, see the BoardSource-Independent Sector publication, [The Sarbanes-Oxley Act and Implications for Nonprofit Organizations](#) (PDF).

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Formerly the National Center for Nonprofit Boards



The Sarbanes-Oxley Act and Implications for Nonprofit Organizations

BoardSource and Independent Sector wish to thank Dan Moore, Vice President for Public Affairs, GuideStar; Tom Hyatt, Principal, Ober Kaler; and Paul Nelson, President, Evangelical Council for Financial Accountability, for sharing their professional insights and expertise on this document.

Information and guidance in this document is provided with the understanding that BoardSource and Independent Sector are not engaged in rendering professional opinions. If such opinions are required, the services of a certified public accountant or an attorney should be sought.

This paper was revised in January 2006 to reflect changes in laws relating to, and practices of, nonprofit organizations.

The Sarbanes-Oxley Act was signed into law on July 30, 2002. Passed in response to the corporate and accounting scandals of Enron, Tyco, and others of 2001 and 2002, the law's purpose is to rebuild public trust in America's corporate sector. The law requires that publicly traded companies adhere to significant new governance standards that broaden board members' roles in overseeing financial transactions and auditing procedures.

While nearly all of the provisions of the Act apply only to publicly traded corporations, the passage of the bill served as a wake-up call to the entire nonprofit community. Indeed, several state legislatures have already passed or are considering legislation containing elements of the Sarbanes-Oxley Act to be applied to nonprofit organizations. In many instances, nonprofit organizations have adopted policies and altered governance practices in response to the Act.

Nonprofit leaders should look carefully at the provisions of Sarbanes-Oxley, as well as their state laws, and determine whether their organizations ought to voluntarily adopt governance best practices, even if not mandated by law. This report will review those provisions and assess their relevance to nonprofit organizations.

Finally, it is important to note that two provisions of Sarbanes-Oxley apply to all entities, including nonprofit organizations. This report will also review those features of the Act that require immediate nonprofit compliance.

MAIN PROVISIONS OF THE SARBANES-OXLEY ACT

With two notable exceptions, the Sarbanes-Oxley Act affects only American publicly traded companies and regulates what boards must do to ensure auditors' independence from their clients. The Act also creates and defines the role of the Public Company Accounting Oversight Board, an entity empowered to enforce standards for audits of public companies. The Act explains processes for electing competent audit committee members and for ensuring that adequate reporting procedures are in place. In addition, it calls for regulations, and closes most of the loopholes, for all enterprises — for-profit and nonprofit — relating to document destruction and whistle-blower protection.

The following sections cover each of the major provisions of the law and discuss their relevance to nonprofit organizations. In addition, BoardSource and Independent Sector offer recommendations for how nonprofit leaders should implement various provisions of the law.

INDEPENDENT AND COMPETENT AUDIT COMMITTEE

SUMMARY OF SARBANES-OXLEY PROVISION

The Sarbanes-Oxley Act requires that each member of a company's audit committee be a member of the board of directors and be independent. "Independence" in the Act is defined as not being part of the management team and not receiving any compensation (either directly or indirectly) from the company as a consultant for other professional services, though board service may be compensated.

In addition, a company must disclose whether it has at least one “financial expert” serving on its audit committee. If it does not have such an expert, it must disclose the rationale behind that decision. Who qualifies as a “financial expert” is still being debated. The Securities and Exchange Commission (SEC) proposes a definition that relies on an individual’s education and experience as a public accountant, auditor, or principal accounting officer. At present, however, the company’s board seems to retain the final right to establish specific qualifications for a financial expert.

The audit committee is directly responsible for hiring, setting compensation, and overseeing the auditor’s activities. It sets rules and processes for complaints concerning accounting and internal control practices.

RELEVANCE TO NONPROFIT BOARDS

While not all nonprofits conduct outside audits, most nonprofit boards have established one or more financial committees (e.g., finance, audit, and/or investment). In those organizations that undertake annual audits, particularly medium to large nonprofit organizations, the board is likely to have a separate audit committee or subcommittee. In California, the Nonprofit Integrity Act of 2004 requires that any charity registered with the attorney general and receiving annual gross revenues of \$2 million or more must form an audit committee. Several other states have adopted similar rules, albeit at varying gross revenue thresholds.

It is good practice for nonprofit organizations to take steps to ensure the independence of the audit committee. While most nonprofit board members serve as volunteers without any compensation and staff members do not participate as voting members, all nonprofit organizations should review their practices to ensure the independence of the audit committee. Also, many states provide additional liability protection for volunteer directors that may be lost if the directors are compensated for their service.

Because of recruitment priorities to create a well-balanced and diverse board, finding people with financial savvy may be challenging for boards. Nonprofit organizations need to ensure that board members of the audit committee have the financial competency to understand financial statements, to evaluate accounting firm bids to undertake auditing, and to make sound financial decisions as part of their fiduciary responsibilities. A nonprofit that has a limited number of financial experts on its board may struggle with filling the treasurer’s position, a finance committee, and an audit committee.

RECOMMENDATIONS

While it is too onerous to demand that all nonprofit organizations undertake a full audit, the board is responsible for assessing the potential benefits and costs of an independent audit. Nonprofits that expend more than \$500,000 of federal funds are required to conduct an annual audit. In addition, participating in the Combined Federal Campaign requires an audit at \$100,000. Any other charitable organization with \$1 million or more in total annual revenues (excluding houses of worship or other organizations that are exempt from filing Form 990) should have an audit conducted of their financial

statements and consider attaching a copy to their Form 990 or 990-PF. Smaller charities with revenues of at least \$250,000 should choose a review or at least have their financial statements compiled by a professional accountant. The boards of nonprofit organizations that forego an audit should evaluate that decision periodically.

All nonprofit organizations that conduct outside audits, particularly medium to large organizations, should consider forming an audit committee and should separate the audit committee from the finance committee.

The audit committee should be composed of individuals who are not compensated for their service on this committee and do not have a financial interest in or any other conflict of interest with any entity doing business with the organization. Most nonprofit organizations have volunteer board members. Nonprofit organizations that do compensate board members should not compensate audit committee members for their additional service. In addition, all nonprofits should ensure that no members of staff, including the chief executive, serve on the audit committee, although it is reasonable to have the chief financial officer provide staff support to the audit committee. The chair of the audit committee should be a board member and it is reasonable to expect that the majority of the committee members are board members.

The audit committee should ensure that the auditing firm has the requisite skills and experience to carry out the auditing function for the organization and that its performance is carefully reviewed.

The audit committee should meet with the auditor, review the annual audit, and recommend its approval or modification to the full board. The full board should review the annual audit and the audit committee's report and recommendations. Ideally the full board would also desire to meet with the auditor before formally accepting or rejecting the audit.

At least one member of the audit committee should meet the criteria of financial expert and have adequate financial savvy to understand, analyze, and reasonably assess the financial statements of the organization and the competency of the auditing firm. This may be a non-director advisory member where permitted by state law.

Orientation of board members should include financial literacy training.

To support the accounting field and help ensure that nonprofit boards have available financial expertise, professional accreditation and membership organizations of accountants should require CPAs to participate in a pro bono nonprofit board service program.

RESPONSIBILITIES OF AUDITORS

SUMMARY OF SARBANES-OXLEY PROVISIONS

The Sarbanes-Oxley Act requires that the lead and reviewing partner of the auditing firm rotate off of the audit every five years. This does not necessarily mean that the auditing firm must be changed, although that may be the most direct way to comply with this requirement.

In addition, the Act prohibits the auditing firm from providing most non-audit services to the company concurrent with auditing services. This prohibition applies to bookkeeping, financial information systems, appraisal services, actuarial services, management or human resource services, investment advice, legal services, and other expert services unrelated to the audit. The board's audit committee may, however, pre-approve certain services (not included in the above categories), such as tax preparation, which can then be carried out by the auditing firm. In addition, the pre-approval requirement is waived for non-auditing services if the value of the non-auditing services is less than five percent of the total amount paid by the organization to the auditing firm for auditing services.

The Act also requires that the auditing firm report to the audit committee all "critical accounting policies and practices" that are used by the organization, discussed with management, and represent the preferred way management wants these policies and practices treated. These critical accounting practices include methods, assumptions, and judgments underlying the preparation of financial statements according to generally accepted accounting principles (GAAP) and assurance that any results would be disclosed in case of changed assumptions.

RELEVANCE TO NONPROFIT BOARDS

Changing auditors (partner or firm) every five years should be considered on a regular basis. The rationale: Auditing firms may grow accustomed to the financial procedures within one organization after a certain number of years, and bringing in a new firm helps ensure that all practices are closely examined.

Nonprofit organizations would be well served to adopt the Sarbanes-Oxley rule of preventing auditing firms from providing non-auditing services, as this provision precludes a conflict of interest between the auditing firm and the client. At a minimum, application of the rule should be considered in each case. At the same time, certain services can be pre-approved by the audit committee, and there is no reason why tax services and preparation of the Form 990 or 990-PF (for private foundations), for example, could not and should not be undertaken by a nonprofit's auditing firm. This can also ensure that certain economies are achieved for the client.

Finally, the provisions about disclosure to the audit committee of critical accounting policies and discussions with management also seem to follow good practice. Greater disclosure of these internal control practices and management's views on them will foster more informed judgments by the audit committee, enhanced oversight by the board, and greater transparency. The critical accounting practices would include processes for segregation of duties, policies to use restricted funds for intended purposes, processes to review off-balance sheet transactions, and procedures for monitoring inventory fluctuations. In addition, the audit committee may be an effective committee for overseeing implementation and enforcement of the governing body's conflict-of-interest policy.

RECOMMENDATIONS

Large nonprofits should consider rotating at least the lead and reviewing partners of the audit firm every five years.

Nonprofit organizations should be cautious when using their auditing firms to provide non-auditing services except for tax preparation, which should be approved in advance, while the firm is contracted to provide auditing services.

The audit committee should require each auditing firm to disclose to the committee all critical accounting policies and practices used within the organization as well as share with the committee any discussions with management about such policies and practices.

CERTIFIED FINANCIAL STATEMENTS

SUMMARY OF SARBANES-OXLEY PROVISIONS

The chief executive and the chief financial officers must certify the appropriateness of financial statements and that they fairly present the financial condition and operations of the company. There are criminal sanctions for false certification, but violations of this statute must be knowing and intentional to give rise to liability.

In addition, to avoid conflicts of interest, the CEO, CFO, controller, and chief accounting officer cannot have worked for the auditing firm for one year preceding the audit.

RELEVANCE TO NONPROFIT ORGANIZATIONS

Any CFO who is responsible for generating timely and accurate financial statements for the company or organization should feel comfortable about certifying document integrity.

In a for-profit company, a positive bottom line is the CEO's responsibility. Business acumen, capacity to interpret financial statements in detail, and skillfulness in convincing the board and shareholders that the corporation is meeting all expectations are obvious characteristics in a manager. Likewise, a nonprofit chief executive may be handicapped without adequate financial skills. He or she may be hired, however, primarily for other qualities. Nonprofit CEOs may excel in fundraising, knowledge of the organization's field of interest, or a variety of other skills. Lack of superior financial prowess must be complemented by a skillful financial officer; without that person, the organization cannot convince donors and funders that their money is properly managed. Nevertheless, it is still the responsibility of the CEO to ensure good stewardship of the organization's resources.

Under Sarbanes-Oxley, CEO and CFO certification carries with it the weight of the law, but part of the underlying rationale is to ensure that both the CEO and CFO know and understand the financial statements. For a nonprofit organization, CEO and CFO sign-off on financial statements would not carry the weight of law (although some states are now considering adopting a similar requirement), but it

would signal the importance that the CEO, in particular, attaches to understanding the nonprofit's financial condition.

For nonprofit organizations, a key financial document is the Form 990 or 990-PF. The form requires a signature from an officer of the organization. Research from a number of studies reveals that the accuracy of these forms leaves much to be desired. Many of the errors in the Form 990 and 990-PF relate to failures to complete all forms, including Schedule A. Other problems include presenting an inaccurate report on fundraising costs, thereby distorting the required financial picture of the organization's operations. Thus, it is critical that nonprofit organizations examine their financial systems, policies, and reporting to help improve the accuracy and completeness of these forms.

There is, in all likelihood, considerably less staff movement in the nonprofit world between accounting firms and client organizations than there is in the for-profit world. Furthermore, because nonprofit executives do not receive lucrative stock options, the relevance of possible conflicts of interest from an auditor joining the executive staff of a nonprofit client is correspondingly less.

RECOMMENDATIONS

CEOs or CFOs, while they need not certify the financial statements of the organization, do need to fully understand such reports and make sure they are accurate and complete. Signing off provides formal assurance that both the CEO and the CFO have reviewed them carefully and stand by them.

The CEO and CFO should review the Form 990 or 990-PF before it is submitted to ensure that it is accurate, complete, and filed on time.

Regardless of whether the CEO and CFO certify the financial report, the board has the ultimate fiduciary responsibility for approving financial reports. Just as the financial and audit reports are reviewed and approved by the audit committee and the board, the Form 990 or 990-PF should also be reviewed and approved. At a time when the Form 990 and 990-PF are published on the Internet by third parties, it is more important than ever that directors be familiar with the contents of the organization's 990 each year.

INSIDER TRANSACTIONS AND CONFLICTS OF INTEREST

SUMMARY OF SARBANES-OXLEY PROVISION

The Act generally prohibits loans to any directors or executives of the company.

RELEVANCE TO NONPROFIT ORGANIZATIONS

Nonprofits are currently highly regulated with respect to financial transactions that take place within the organization. Private inurement, excessive personal benefit, and self-dealing all cause serious penalties for any nonprofit that steps out of line. "Intermediate sanctions" laws specifically address compensation and excess benefit transactions with "disqualified" individuals, generally board members and executive staff.

Providing private loans to insiders — the specific item included in the Sarbanes-Oxley Act - is not a common practice in the nonprofit sector. However, when it has occurred, it has caused problems either from the perception of a conflict of interest or because it has not been appropriately documented as part of executive compensation. In addition, in some states, nonprofit law expressly prohibits loans to directors and officers.

RECOMMENDATIONS

Because the practice of providing loans to nonprofit executives has been a source of trouble in the past and because this practice is specifically prohibited under Sarbanes-Oxley and in some states, it is strongly recommended that nonprofit organizations not provide personal loans to directors or executives.

If such loans are provided, they should be formally approved by the board, the process for providing the loan should be documented, and the value and terms of the loan should be disclosed.

To guide the board and staff in independent decision making, the organization must have a conflict-of-interest policy with board members annually disclosing their potential conflicts of interest, and this policy must be enforced without fail.

DISCLOSURE

SUMMARY OF SARBANES-OXLEY PROVISION

The Sarbanes-Oxley Act requires a number of disclosures, including information on internal control mechanisms, corrections to past financial statements, and material off balance sheet transactions (adjustments). The Act also requires companies to disclose information on material changes in the operations or financial situation of the company on a rapid and current basis.

RELEVANCE TO NONPROFIT ORGANIZATIONS

While nonprofit organizations do not file most of the reports that publicly traded companies are required to file, they should nevertheless provide their donors, clients, public officials, the media, and others with an accurate picture of their financial condition. Current law already requires tax-exempt organizations to make their Forms 990 or 990-PF freely available to anyone who requests them in writing or in person. These information returns, as mentioned before, need improvements both in accuracy and in timeliness of disclosure. One way to achieve that objective is through electronic filing, something the Internal Revenue Service is currently pursuing and the nonprofit community generally endorses.

RECOMMENDATIONS

Nonprofit organizations should improve the timeliness, accuracy, and completeness of the Forms 990 or 990-PF by filing electronically when that option is available to them. Nonprofits should strive for greater disclosure and transparency.

Nonprofits should not rely on automatic extensions for filing Forms 990 and 990-PF without cause.

Audited financial statements should be easily accessible for review.

Two provisions of the Sarbanes-Oxley Act apply to all entities because they are amendments to the federal criminal code, so all nonprofit organizations need to comply with them.

WHISTLE-BLOWER PROTECTION

SUMMARY OF SARBANES-OXLEY PROVISION

The Sarbanes-Oxley Act provides protections for whistle-blowers and imposes criminal penalties for actions taken in retaliation against those who risk their careers by reporting suspected illegal activities in the organization. It is illegal for any entity — for-profit and nonprofit alike — to punish the whistle-blower in any manner.

RELEVANCE TO NONPROFIT ORGANIZATIONS

Nonprofits must start by protecting themselves. They must eliminate careless and irresponsible accounting practices and benefit from an internal audit that brings to light weak spots and installs processes that are not vulnerable to fraud and abuse. Written policies that are vigorously enforced by executive staff and the board send a message that misconduct is not tolerated. These policies should cover any unethical behavior within the organization — including sexual harassment.

Each organization must develop procedures for handling employee and volunteer complaints, including the establishment of a confidential and anonymous mechanism to encourage employees and volunteers to report any inappropriateness within the entity's financial management. No punishment for reporting problems — including firing, demotion, suspension, harassment, failure to consider the employee for promotion, or any other kind of discrimination — is allowed. Even if the claims are unfounded, the organization may not reprimand the employee. The law does not force the employee to demonstrate misconduct; a reasonable belief or suspicion that a fraud exists is enough to create a protected status for the employee.

RECOMMENDATIONS

Nonprofits must develop, adopt, and disclose a formal process to deal with complaints and prevent retaliation.

Nonprofit leaders must take any employee and volunteer complaints seriously, investigate the situation, and fix any problems or justify why corrections are not necessary.

DOCUMENT DESTRUCTION

SUMMARY OF SARBANES-OXLEY PROVISION

The Sarbanes-Oxley Act addresses destruction of litigation-related documents. The law makes it a crime to alter, cover up, falsify, or destroy any document (or persuade

someone else to do so) to prevent its use in an official proceeding (e.g., federal investigation or bankruptcy proceedings). The Act turns intentional document destruction into a process that must be monitored, justified, and carefully administered.

RELEVANCE TO NONPROFIT ORGANIZATIONS

Common sense dictates that individuals, nonprofit organizations, and companies regularly need to shred or otherwise dispose of unnecessary and outdated documents and files. Like their for-profit counterparts, nonprofit organizations need to maintain appropriate records about their operations. For example, financial records, significant contracts, real estate and other major transactions, employment files, and fundraising obligations should be archived according to guidelines established by the organization. Because of current technology, electronic files and voicemail can become complicated as we come to understand the relevance of the delete button as a permanent method of file removal.

RECOMMENDATIONS

A nonprofit organization should have a written, mandatory document retention and periodic destruction policy. Such a policy also helps limit accidental or innocent destruction.

The document retention policy should include guidelines for handling electronic files and voicemail. Electronic documents and voicemail messages have the same status as paper files in litigation-related cases. The policy should also cover back-up procedures, archiving of documents, and regular check-ups of the reliability of the system.

If an official investigation is underway or even suspected, nonprofit management must stop any document purging in order to avoid criminal obstruction charges.

CONCLUSION

The Sarbanes-Oxley Act has now been in force for several years. The legal climate has intensified in the nonprofit sector as Congressional committees and state legislatures are actively proposing new legislation to regulate organizations. Individual nonprofits have begun to identify loopholes - and figure out how to eliminate them. Watchdog agencies and other nonprofit field-building organizations are reconsidering assumptions and standard operating procedures in an effort to identify guidelines, standards, and best practices in the sector.

Regardless of the present scope of existing and potential new legislation at the state and federal level, nonprofit organizations have heard the wake-up call. For all of us in the sector, the Sarbanes-Oxley Act spearheaded a renewed realization that nonprofit organizations rely on - and must protect - the indispensable and unequivocal confidence and trust of our constituents. Self-regulation and proactive behavior will always prove more powerful than compulsory respect of laws.

ADDITIONAL RESOURCES

Press Release from the Office of New York State Attorney General

www.oag.state.ny.us/press/2003/mar/mar12a_03.html

“Strengthening Transparency, Governance, Accountability of Charitable Organizations, a Final Report to Congress and the Nonprofit Sector, June 2005.” Panel on the Nonprofit Sector, www.nonprofitpanel.org/final.

Summary of the Sarbanes-Oxley Act

www.aicpa.org/sarbanes/index.asp.

Recommendations from the National Association of Corporate Directors

Concerning Reforms in the Aftermath of the Enron Bankruptcy

www.nacdonline.org/nacd/enron_recommendations.asp

“Corporate Governance. The Wall Street Journal Reports.” *Wall Street Journal*, February 24, 2003.

“Raising the Bar on Governance: Board Committee Performance in the New Era of Accountability.” American Governance & Leadership Group, 2002.

Hamel, W. Warren. “What Corporate Governance Legislation Means to You.” *Association Management*, March 2003.

Heinz, Patrice A. “The Financial Reporting Practices of Nonprofits”. Alliance for Children and Families, 2003. www.alliance1.org/Home/SOX_final_8-03.pdf

Kokourek, Paul F., Christian Burger, and Bill Birchard. “Corporate Governance: Hard Facts about Soft Behaviors: Seven steps to fixing what Sarbanes-Oxley can’t.” *strategy+ business*, Issue 30, Spring 2003.

McLaughlin, Thomas A. “For-Profit Spillover: New Regulation of Independence.” *NonProfit Times*, February, 1, 2003.

Michaelson, Martin. “A New Era of Corporate Governance Bears Down on Higher Education.” *Trusteeship*, January/February 2003.