

# Getting Ready For A Financial Audit

## How to Get Ready for A Financial Audit

The number of Americans calling themselves Christians has dropped sharply in recent years, according to a new Pew Research Center survey—while the population of religiously unaffiliated adults is on the rise. This trend is driven by Millennials, around one-third of whom claim to be religiously unaffiliated, according to Time Magazine.

One of the best ways you can earn the trust of Millennials is with how your church handles its money. Millennials live in a world where they can directly donate via their phone to thousands of organizations that connect directly to their heart. No longer do they need the United Way and/or the local church to find partnerships that connect to their heart, they just find it on their own through their phones. Unfortunately, the word *Christian* is often not one that connects to their heart.

One of the best ways for your church to earn the community's trust is to hire an independent CPA firm to audit your books. So how does a church get ready for an audit?

### 1. Hire an Audit Firm

Your elder board needs to hire an audit firm. Yes, the church's board is responsible for hiring the auditors, not the staff. Be sure the staff and the board of your church understands that. If you are not part of the board, you can still help guide them in the process by going through a bidding process to find a potential auditing firm, presenting the firm to the board for their review and approval. Please don't forget to allocate budget funds for the audit; it is not cheap but well worth the money. When bidding out an audit, be sure to interview at least three firms to ensure you feel comfortable with the price that you are paying. Choose a firm that has experience auditing churches and that will give you key insights. These independent, unbiased insights could help your church really understand the financial numbers, helping to add value to the decision making at the church. Ask the CPA firms for permission to interview a few of their clients and then ask those clients how the firm has helped them be a better church.

### 2. Meet with the Auditors Before the Audit

The ideal is to have an annual audit performed by independent CPAs. Generally, however, only large churches can afford this extra expense. External audits of smaller churches often are done on a non-GAAP basis – the statements do not conform to the full accrual method with depreciation recognized. Non-GAAP audits of smaller churches often are acceptable to banks and other agencies that require audited financial statements. (GAAP stands for Generally Accepted Accounting Principles.)

### 3. Know Your Responsibilities in the Audit

Remember that these are ultimately your church's financial statements. If you don't feel comfortable on how the auditor is presenting the numbers, let him know and ask him to explain it to you. The auditors are attesting that your financial statements are accurate, but it's not an IRS audit. So please, don't rely on the auditing firm to ensure that you are following IRS regulations for the housing allowance or something of that nature. The auditors' role is to ensure that what you are reporting financially is accurate. If you don't know how to write a financial statement, learning how to do it is a great goal to have. The easiest way to learn is by reading one of your church's previous financial statements, if one is available. If it's not, there are plenty of ECFA-accredited churches that share their financial statements on their website. Start with the Statement of Financial Position, also

known as a balance sheet. Pick a number and try to find that same exact number in your church accounting software. Once you find that number, try to find a source document(s) that proves that number is what it says it is. That is a great start to learning how to create a financial statement.

Unfortunately, if you are feeling overwhelmed as a church accountant, you may have a hard time finding CPA volunteers to help you—CPAs often already work many hours for their firm. If you do find one that is willing to assist you, organize all the paperwork and books ahead of time. The easier you make it for the CPA to do what they do best, the more you will get out of the partnership. Partnering with a CPA will really help you gain valuable insights on your church so you can take all the ideas in your head and put them into action. Try scheduling a lunch with a CPA and show them your financial statements. See if they can share with you any insights. I firmly believe that you learn so much when you go outside your normal network to seek insight to a situation.

At the end of the day, the church creates and owns the financial statements, not the auditors. They are an independent witness to your books who attest that your books are what you say they are. So, try to learn what is yours.

If your church isn't doing this already, consider filing all your documents electronically. By doing this, you can keep all of your files organized electronically and map them to the bank statements. Ask your auditors what they have used in the past and create similar workpapers to justify each number. Have a pre-audit folder that saves all these files—that way, you can see what the auditors were looking for last year and recreate them for the current year. Be sure to review your methods from previous audits before doing the same thing every year. Over time everything changes, so be aware of potentially new and better ways to prove that your numbers are correct.

#### **4. Create Internal Controls**

Create your church's Internal Controls, and make sure they are up to date every year before the audit. Internal Controls are what CPAs do to ensure that: (1) What we want to happen will happen, and (2) What we don't want to happen won't happen. Often times people ask me, "Do you trust me?" It's not about trust, it's about doing things in a way that no one would question ... "and I trust you so much that I am willing to tell you how everything financially works at this church."

Creating your Internal Controls is a simple but time-consuming exercise. Once you write them all out, the auditors will test them to see if they are accurate. Strong Internal Controls are something every auditor looks at to ensure that the church's numbers are accurate. It also helps the church in case of an emergency. If something should happen to you, they would know how to write a check or where to find the password to open the accounting software.

After completing an audit, a great question to ask is "When was the last time the leadership team made a decision based on the generally accepted accounting principles (GAAP) financial statements?" The role of a great leader is to help present the GAAP financial statements that the auditor has verified through the lens of marginal data where decisions are made. You must communicate the connections so you can show how both have value so key decisions can be made with this report as a church. For example, if you have rapidly declining value on your equipment, I would highly recommend setting aside budget funds and staff time to replace these aging pieces of equipment. If you anticipate this, you can save for this through your operating budget rather than asking the church to pay for every large piece of equipment that breaks. It will help you focus on the spiritual matters while fixing the equipment that enhances ministry.

## **Concluding Thoughts**

In conclusion, auditing your church's financial statements is one of the best ways your church can earn the trust of your community. It is also one of the best ways you can be complimented for doing a great job as church accountant by an outside independent source.

You can do it; you don't need to be a CPA, just lean into God's call for your life and don't forget to ask for help.

## **About the Author::**

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### ***Disclaimer***

The information contained in this Toolbox series is of a general nature. It is not offered as specific legal or tax "advice." Each person and local church board should evaluate their own unique situation in consultation with their local legal and tax advisors.

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