Year-end Closing of Books: Cutoffs, Accruals, Transfers and Pre-audit Issues

Be Audited, the Smart Way

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Objectives

- Identify tools to be audited the “smart way vs the hard way”
- Understand items that need to be done before your audit date
- Understand transfers and their impact on the financial statements
- Identify accruing entries that need to be done before the audit

1. Pre-audit Items: Audit Dates

- Selecting audit dates that work best for the treasury team as a whole not just the treasurer.
- Select in advance dates for exit conference to get the officers in the exit conference.
- Audit dates should be free of conflicts with payroll and board meeting dates.
- To minimize auditing stress, it may be a good idea to schedule the audit after vacation.

2. Reviewing Prior Year's Audit Reports

- Review the following:
- Audit Communication Letter (Management letter) and focus on auditors' "write ups" and try to resolve the concerns and recommendations.
- Accounting Letter items: small items that are of lesser concern for the audit.
- Policy Compliance Report: Policy violations

3. Selecting a Coordinator for the Audit

- Select an individual in the treasury team to be an in-charge person for the audit. The person should be the one who understands the whole items in the financial statements both operating, plant and other funds.

4. Pre-audit: Work with other Departments

- Work with other departments such as secretariat or HR to get service record, conflict of interest statements and minutes.

Pre-Audit: Reviewing Minute Excerpts

Date	Type	Action	Entity Name	Description	Source of Funds	Amount	Comments
3/19/16	Executive	N/A	Wilma Church	Kitchen Remodel	CURF	20,000	Expensed, delayed maint
5/21/16	Executive	N/A	Linthicum Ch	Replace HVAC	CURF	6,500	Expensed, delayed maint
5/21/16	Executive	N/A	CrestLane Sch	Repairs	CURF	15,000	Expensed, delayed maint
5/21/16	Executive	N/A	Dover Church	School Construction	CURF	300,000	Construction started 2015
5/21/16	Executive	N/A	Baltimore Sp Ch	Gym Constr	CURF	340,000	Per Pastor, church cancelled project

Building Auditors' Confidence

Maintain and strengthen the internal control such as:

- Reconcile accounting records
- Attempt to prepare GAAP Financial Statements, including footnotes
- Review accounting records and show evidence of review.
- Having adequate supporting documentation for journal vouchers
- Understand the concepts of Due to/from, temporarily restricted net assets, agency accounts (trust accounts) and transfers and their effects on the financial statements.

Closing Books: Reconcile Accounting Records

- Bank accounts be reconciled regularly at least monthly,
- Petty cash be reconciled regularly
- Payroll accounts and taxes
- PPE and Subsidiary accounts
- Beginning net assets must always match the audited statements.
- Accounts receivable and subsidiary ledgers and related allowance for doubtful accounts.

Closing: Net Assets Reconciliation

- Always the beginning net assets MUST match the ending net assets of each fund in the Prior-year Audited Financial Statements.
- For example, you can run AASI net assets accounts for each fund and compare with the Prior year Audited Statements.
- See Sample of beginning net assets reconciliation, next slide.

EXAMPLE – BEGINNING NET ASSET RECONCILIATION

OPERATING FUND ACCOUNT #	ACCOUNT NAME	AMOUNT
501100	Unallocated Net Assets	$ 3,163,512.31
502100	Allocated Net Assets	1,673,014.42
505100	Temporary Restricted Net Assets	500,215.75
519100	Temporary Restricted Net Assets- Prior Period Adjustment	51,504.59
Total Beginning(2016) Net Assets	-Per GL	5,388,247.07
Net Assets Total, 2017	-Per GCAS Audited Statement	5,388,246.00
	DIFFERENCE	**1.07**

Why Net Assets not Matching Prior Year Audited Statements?

- Audited adjusting entries not recorded
- Entries recorded the wrong way
- Entries not received from auditors

Closing: "Release To and Release From"

- Releases are financial activity accounts that are used to move Temporarily Restricted Funds from restrictions to Unrestricted.
- **Release to and release from must always balance. Always make sure that the proper codes "7 or 2" are used when using AASI ledger.**

Closing: Temporarily Restricted Net Assets: Releases

- You cannot Release more than the restricted income or net assets
- You cannot Release until either time or purpose restriction has been met.
- You cannot Release more than expenses relating to the restricted net assets
- For example, you have received a restricted income for scholarship of $20,000. You spent only $5,000 on scholarship. You can only release $5,000.

Closing: Bank Reconciliation and Review

- All Bank Accounts Must be Reconciled to the General Leger
- There should be evidence of review by someone other than the preparer.
- Evidence could be a reviewer's signature or initials as long as it is consistently applied.

Closing: Accounts Receivable and Allowance for Bad Debt

- Accounts receivables are recorded at Net Realizable Value
- You must make a provision for allowance based on risk of collectability.
- Your analysis for the allowance must be documented and reasonable.
- Allowance is always based on management JUDGEMENT and should be reasonable. For example, payment plan in place, statements are sent regularly, payment history, length of time of A/R outstanding, etc.

Closing: Remittances Receivable

- Remittances received after the close of the year-end should be accrued as well as the related remittance payable to higher organizations.

Due To/Due From

- **Due to/from**: Is one fund borrowing from another fund with the intention to pay back. It is asset and a liability depending on the Fund asset is borrowed. Due to/from is a balance sheet item which must net to zero in the combined financial statements.
- There should be a plan for the borrowed "Fund" to pay back the amount borrowed.

Accrued Payables

- Make Accruals for retirement for employees older than 56 years.
- Make Accruals for vacation time. Vacation carryover must be approved by ADCOM or governing body.
- Invoices received after year-end, usually 2 months after year-end should be reviewed for possible accruals.
- IBNR should be recorded only to the extent of the actual medical expense not recorded.

Accrued Liability: IBNR

- IBNR (Incurred But Not Reported medical claim): Care must be taken to ensure that IBNR and actual medical costs are not recorded twice at year-end.

Inter-fund Transfers

- **Transfers (In and Out)** are the flow of allocated resources from the operating fund to the plant fund.
- Transfers not revenue or expense. In addition, because these transactions reflect movement of resources within the organization, not inflows or outflows with third parties, they do not increase or decrease the total resources held by the organization as a whole.
- **the total transfers out of one fund must be equal to the total transfers into the other fund**. As a result, the final total of transfers for the whole entity will be reported as **zero.**

Long-term Payables: Leases

A lease is classified as a Capital (finance) lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership. Operating lease is a financial activity that is expensed. **Operating lease will no longer be used in 2018.**

Long-term Payables :Capital Lease

- Capital Lease should be recorded as Asset and liability and should be depreciated over the useful life of the leased asset.
- **Criteria for capital lease**

(a) Transfer ownership

(b) Useful term is at least 75% of the useful life of leased asset

(c) Bargain of purchase

(d) Present value of the leased payments is at least 90% of the FMV of the asset.

Current Vs Long-term Liabilities

- Break the long-term liabilities into current and long-term using amortization schedule (or excel).

Payroll Reconciliation

- Reconcile G/L Payroll accounts to the Subsidiary Ledger.
- Payroll W-3 must match 941s.
- Evidence of payroll tax payments should be kept.

Church and School Capital Projects

- Remember to record capital additions such as renovations, land improvements etc.
- Send quarterly emails to the local pastors, treasurers and business managers about capital projects.

Plant Fund: Capitalization Policy

- Develop a capitalization policy and apply it consistently. For example, an entity may have its policy like this "The Organization's capitalization policy is to capitalize all plant asset purchases above $5,000 with a useful life of 3 or more years. Church and school building and renovations are capitalized above $10,000".

Plant Fund: Unexpended

- **Unexpended**: record resources that are available for use in acquiring land, buildings and equipment.
- Assets include Cash, investment, A/R.
- Liabilities Include: Accounts payable or amounts due to other funds.

Plant Fund: Net Invested

- To record the cost and accumulated depreciation of land, land improvements, buildings, and equipment, as well as any long-term liabilities related to those assets.

Plant Fund: Properties Purchased by Local Church

- Real estate properties such as land, land improvement and building should be recorded by the Conference since the Conference holds legal title to the property
- The cost and related donated property (revenue) are recorded in Net Invested Plant fund.
- Depreciable donated property should be depreciated over its useful life
- Significant additions (renovations) be capitalized based on capitalization policy.

Plant Fund: Construction inn Progress (CIP)

- CIP is an asset that is not ready for its intended use. Typically, it represents building under construction.
- CIP should be capitalized and should not be depreciated until the asset is ready for its intended use. It’s recorded in Net Invested Plant fund.

Attempt to prepare GAAP Financial Statements

- It is very useful to prepare your own GAAP financial statements before the audit. Some of the benefits of preparing the financial statements are
- (1) It gives you greater understanding and control of all the items in the financial statements.
- (2) It helps you to find errors and correct them before the audit to avoid material misstatements and auditors' write up.
- (3)It helps you to reclassify accounts appropriately and provide reasons for changes in significant accounts.
- (4) It gives you confidence and helps you to prepare for the audit.

Evidence of Review

- Sign on the bank reconciliation statement: It could be just your initials or signature and date.
- Sign on all payroll and other reconciliations.
- Sign on all journal vouchers.

Areas of Major Concern for Auditors

- Beginning net assets not matching the prior year's audited ending net assets.
- PPE G/L not matching the subsidiary ledger.
- Temporarily restricted income recording as agency funds.
- Payroll accounts not reconciled
- Over/under release of restricted income

Remember: Auditors

- They are very nice and should be treated such as.
- Provide them decent working space during the audit.