

## NOTES ON DOING A CHURCH AUDIT

*These notes were distributed at a workshop for treasurers of local Presbyterian churches. You may already have a copy. It is offered again as an assistance for those churches which are updating their financial review or audit procedures.*

*PSF Polity and Records Committee, 1997*

An "audit" in the sense that we will use it here is the attempt to test the accuracy of the annual financial statements as presented to the congregation at the annual meeting. To emphasize, you are not auditing the books but the financial statements. The implication of this is that you should constantly go back to the financials to see how transactions were reported.

We will divide the audit into two parts: an audit of the BALANCE SHEET and an audit of the INCOME STATEMENT.

### BALANCE SHEET

We begin with the Balance Sheet because it is simplest and allows us to establish beginning and ending points for our later consideration of the current year's activity. To properly do this, we need to consider the balances at two points: the beginning of the year and the end.

A. Look at the previous year's balances and the current year's balances. The same questions can be asked of each. Of course, if you also did the audit the previous year, less time will be needed for the previous year's review.

1. How many Cash Accounts does it show?
2. Were bank accounts opened/closed during the year? Are there proper authorizations in the minutes of session?
3. Does it show any liabilities?
4. Are any assets shown besides the cash accounts and fixed assets (the buildings, organ, furniture, etc.)?

B. To audit the cash accounts:

1. Find the bank reconciliation for each account. Does it tie into the bank statement and the general ledger (G/L)? If not, ask the bookkeeper to redo it so that it will. Make sure all the items on the bank reconciliation have been posted to the G/L.
2. Did the outstanding checks listed clear in January or February? If not, are they real, or do they need to be voided and the G/L adjusted?
3. If there are any cash receipts in transit, make sure that they cleared within the first few days of January. If not, follow up to see why not.



### C. To audit liabilities:

1. Compare last year's balances to this year's. Are they the same? If there are marked differences, follow up to see why. Look for confirmation statements from the creditors that back up the liabilities. If they are loans, check with the financial institutions to see their record of the balances as of the date in question.
2. Payroll taxes can be tested by reviewing the quarterly returns.
3. Accounts Payable vendors often send out statements. Or check to see if the invoices were paid in the new year.

### D. Other Assets:

1. Fixed Assets should be stated at cost. Some churches keep them on their books, others do not. If a current building fund is under way, major expenditures should be kept in a "Construction in Progress" account until the project is complete. At that time the project should be "capitalized" as a fixed asset such as "Building Renovation" etc. Also, check for assets that may not have been recorded (e.g. donations of fixed assets where the church had no cash outlay). You should also check for large expenditures in the "Repair and Maintenance" accounts that perhaps should be capitalized.
2. Prepaid expenses are amounts spent for future periods. An insurance premium paid for a year in advance is a prepaid. Prorate the portion already used up and expense it. The remainder should stay on the books as a current asset until it is used up.
3. Occasionally a church will have a receivable on the books. This should be tested by asking the individual or group for confirmation as to the amount and terms of the loan.

## INCOME STATEMENT

It is too time-consuming to review all transactions for a given year. So we can basically accomplish our objectives by testing a month or two and some key accounts.

### A. Testing a month:

1. You may want to review all cash disbursements greater than a certain amount, e.g. \$5,000. Make sure the disbursements were properly authorized and coded in the G/L.
2. Also, arbitrarily select a month or months to test.
3. Ask for a listing of all deposits made during that month. Make sure each deposit arrived at the bank in a timely manner. Ask for the weekly offering tally and tie it into the deposits made at the bank. See how the deposit was recorded in the G/L and test it for accuracy.



4. Ask for a listing of checks written during the month. For each check (except payroll) test that there was proper approval of the expenditure, that there was an invoice or check request describing the expenditure and that the canceled check agrees with the amount recorded on the G/L. (Payroll checks should be tested per B., Testing Accounts.)

5. Ask for a listing of journal entries. Review them to make sure they make sense to you. Make sure they were recorded properly on the G/L.

#### B. Testing Accounts

1. Select certain key expense accounts to see if the annual amounts expended make sense. Natural for this procedure are such accounts as payroll, utilities, insurance and other large ticket items. Also review the budget and select any accounts with a large variance budget to actual. For each account selected do the following:

a. Compare budget to actual and to prior year. If there is more than a 10% variance either way, try to determine why.

b. On salary and benefit accounts, look for board or congregation action approving the salary and benefits. Also look in the Personnel file for W-4's and test whether taxes were withheld properly.

#### C. Writing a report

In order to complete the process of an audit, it is necessary to write up your results. Since this is not a formal audit, the standard paragraphs of a CPA's audit need not be used. But a paragraph stating what entity and period you audited would be helpful. A second paragraph could describe in general terms the procedures you used. A final paragraph could state the results, namely whether you found the financial statements to be reasonably accurate. This statement could be conditional upon certain changes being made. If there were significant changes to be made, these could be described in a fourth paragraph; as you continue this process in succeeding years, you might indicate changes made in response to the previous year's suggestions.

Often accompanying an audit are certain recommendations as to changes in procedure. This is sometimes referred to as a management letter. If you found that some things could be done to improve the effectiveness or efficiency of the bookkeeping function, you may want to write them up in a few paragraphs to accompany the report.

#### D. Submitting the audit report (or financial review report) to the session

A brief, signed report, including the management letter if you write one, should be presented to your session and incorporated into the minutes by the Clerk of Session. Financial check lists and notes on conducting a church audit should not be included. The Book of Order calls for a financial review of the previous year reported in the current year's minutes. Thus your review of 1996 finances would be reported and included in the session minutes by the end of 1997 for the review of 1997 records in 1998.