

ASSURANCE FOR NOT-FOR-PROFITS:

A guide for funding organisations

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**AUDITING &
ASSURANCE
STANDARDS**



**NOT FOR PROFIT
ACCOUNTING
STANDARDS**

The External Reporting Board (XRB) is the independent Crown Entity responsible for accounting and assurance standards in New Zealand. The New Zealand Auditing and Assurance Standards Board (NZAuASB) has delegated authority from the XRB Board to develop or adopt, and issue auditing and assurance standards.

All XRB standards are designed to give New Zealanders trust and confidence in the financial reporting of our organisations, across the profit, public and not-for profit sectors.

Introduction

Assurance engagements give stakeholders' confidence in the credibility of an organisation's information. The most commonly used and best-known assurance engagement is an audit of financial statements, but there are also many other options available. This document provides funding organisations with an overview of the different assurance options and how to choose the right one.

Some not-for-profit (NFP) organisations are required by law to have their financial statements audited or reviewed, but not all. In determining which organisations must have assurance the Government has considered the needs of users of the organisations financial reports, and whether the benefits outweigh the costs.



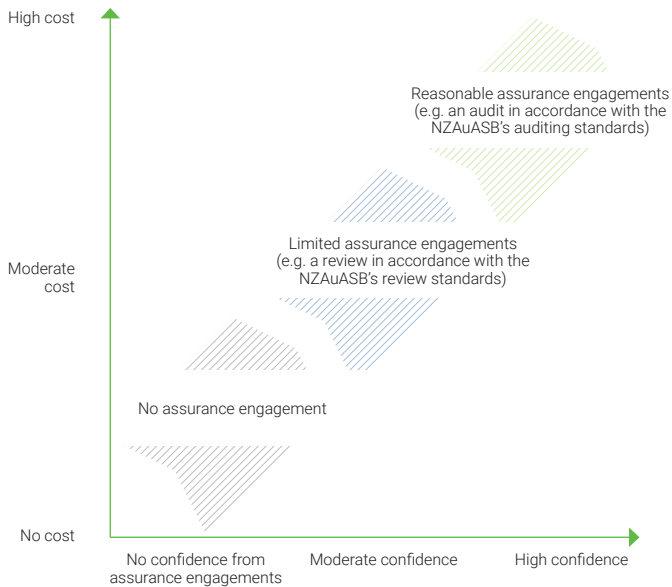
Funding organisations include any organisation that provides funding for the not-for-profit sector, such as philanthropic funding organisations, city councils and government departments.



Assurance engagements are only one link in the chain involved in the provision of high quality financial reporting. High quality information is best achieved when all participants in the financial reporting chain play their roles as best they can. See page 9 for more information.



All assurance engagements that are required by law (statutory assurance engagements) must be carried out by an accredited accountant and to standards issued by the NZAuASB. See page 10 for more information.



Requesting assurance from a NFP

Funding organisations need to have confidence in the credibility of the information supplied by NFP organisations when applying for funding. Many funding organisations request audited financial statements from NFPs, including those smaller organisations which do not have a statutory requirement to have their financial statements audited or reviewed. This can be an added financial burden on that organisation, which may not be necessary. It is important that the funding organisation has a clear understanding of why it is requesting assurance, and is confident that the type of assurance it is requesting provides the best solution to funders assurance needs.

The first thing you need to consider is whether an audit or review of the NFP's financial statements will provide the information you need. The following pages provide an overview of what you can expect from an audit and a review of an NFP's financial statements. We also provide some information about other types of assurance engagements which might be more appropriate.

There are also non-assurance services available which can address funding organisations specific concerns, such as agreed-upon procedures. However, non-assurance services over the financial statements are not included in the NZAuASB's mandate, more information is available from Chartered Accountants Australia and New Zealand (www.charteredaccountantsanz.com).

What is an audit?



What is an audit engagement?

An audit engagement is where an independent auditor provides their opinion as to whether the financial statements are prepared in accordance with the applicable financial reporting framework. The purpose is to increase the confidence of users in the credibility of the financial statements.

The auditor obtains reasonable assurance (not absolute assurance) about whether the financial statements, as a whole, are free from material misstatement due to either fraud or error. The auditor examines, on a test basis, evidence supporting the amounts and disclosures in the organisation's financial statements, assessing the accounting principles used and significant estimates made by the organisation. The auditor will also evaluate the overall financial statement presentation. The independent auditor's opinion is expressed as a positive opinion statement. For example: "In our opinion, the financial statements present fairly, in all material respects, ..."

What can be reasonably expected of an audit engagement?

An audit is not an absolute guarantee. The auditor cannot practically test all or even a majority of the transactions recorded by the organisation. This would simply take too long and be too expensive. Instead, the audit is designed to provide a level of assurance that is reasonable but not absolute.

The auditor does not provide any opinion on the efficiency or effectiveness of how the NFP has spent its resources. That assessment needs to be done by the users of the financial information. Similarly, the auditor does not necessarily verify whether funds are being used for the intended purposes.

The auditor also considers the NFP's financial controls and procedures to ensure appropriate audit procedures are designed and performed. This is not for the purpose of expressing an opinion over the effectiveness of the NFP's

internal controls. If an audit opinion expresses that financial statements are appropriately prepared (i.e. a clean audit report), it does not mean that the NFP has implemented effective controls and procedures over its operations and financial affairs.

While an auditor is required by the NZAuASB's auditing standards to consider fraud, an audit of financial statements is not a fraud detection engagement (which is usually referred to as forensic accounting). A clean audit report does not guarantee "no fraud".

Which NFPs must have their financial statements audited?

- All registered charities with annual expenditure over \$1m
- Not-for-profit friendly societies with annual expenditure over \$30m
- Not-for-profit friendly societies with annual expenditure less than \$30m (unless they opt out of preparing financial statements, or operating payments are less than \$125,000 and the entity's rules don't require an audit)
- Community trusts under the Community Trust Act 1999
- Corporate societies under the Gambling Act 2003

What is a review?



What is a review engagement?

A review engagement is less thorough and detailed than an audit. The reviewer provides a conclusion as to whether anything has come to their attention to indicate that the financial statements have not been prepared in all material respects, in accordance with the applicable financial reporting framework. The purpose of a review is still to provide the users of the financial statements with confidence.

The reviewer obtains a meaningful level of assurance that the financial statements as a whole are free from material misstatement, whether due to fraud or error. The reviewer's conclusion is expressed as a negative opinion statement. For example: "Based on the work performed, as described in the report, nothing has come to our attention ..."

What can be reasonably expected of a review?

A review provides a lower level of assurance than an audit. Therefore, there is a greater risk that material misstatements will not be identified in a review as compared to an audit.

The procedures performed for a review are substantially less than those performed for an audit. They mainly consist of enquiry and analytical procedures, after obtaining an understanding of where material misstatements are likely to arise in the financial statements.

As reviews generally require less work to complete, they may be less costly and time consuming compared to an audit.

Which NFPs require a review of their financial statements?

All registered charities with annual expenditure less than \$1m but more than \$500k are required to have a review of their financial statements at a minimum. These entities can opt up to an audit if they choose to do so.

What are the alternatives?



There are other assurance options which may provide more meaningful information for funders. The NZAuASB provides a full suite of standards which are flexible and scalable, and can be applied to a wider range of matters other than audits or reviews of financial information.

These assurance engagements can cover areas such as:

- the controls in place at an NFP to deter and/or detect the misappropriation of the NFP's resources
- whether an NFP has spent its funding in accordance with the criteria set by the funding organisation
- whether an NFP's policies, procedures and management processes are appropriate to meet its objectives and desired outcomes
- whether an NFP has been effective and efficient in delivering a funded plan/program/activity.

These assurance standards can be customised by a suitably qualified assurance practitioner to apply to a wide range of matters. They can be delivered to provide either reasonable assurance (high level of assurance but not absolute, with a positively expressed opinion similar to an audit) or limited assurance (a meaningful level of assurance but less than reasonable assurance, with a negatively expressed conclusion, similar to a review).

When is an assurance engagement most likely to be effective?

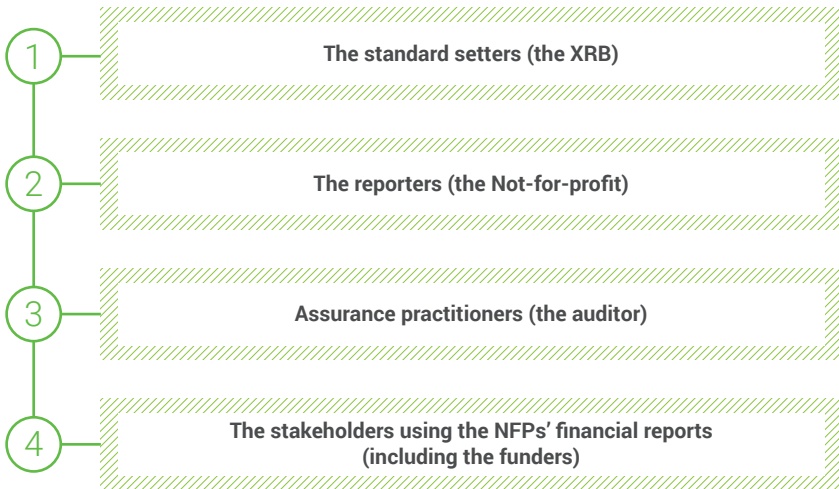


A chain is only as strong as its weakest link.

The aim of any assurance engagement is to provide confidence in NFPs information. This is best achieved in an environment where all participants:

- understand their responsibilities and fulfill them as best as they can, and
- assist other key participants in undertaking their role.

High quality financial reporting involves a chain of participants that begins with the organisation which sets the standards and ends with the users of the financial report. Audit or review engagements are important links in this chain but these are unlikely to be effective if other links are broken. An overview of the financial reporting chain is provided below.



1

The standard setters (the XRB)

The External Reporting Board (XRB) is the independent Crown Entity responsible for accounting and assurance standards in New Zealand.

The XRB delegates responsibility for standards to its two key boards:

- the New Zealand Accounting Standards Board (NZASB), responsible for accounting standards; and
- the New Zealand Auditing and Assurance Standards Board (NZAuASB), responsible for auditing and assurance standards.

Standards for the not-for-profit sector have been developed to ensure accountability to funders and members and to instill confidence in the organisation and sector, while still being cost effective to use.

The XRB website (www.xrb.govt.nz) provides details of which accounting standards an organisation needs to apply.

2

The reporters (the Not-for-profit)

The group of individuals entrusted with the governance of the NFP play a vital role. This group is often referred to as the board, trustees, or management committee. They are responsible for preparing the NFP's financial reports.

This governance group is responsible for ensuring that the NFP's financial reports are prepared in accordance with the right financial reporting standards.

They must implement internal controls to ensure that the NFP's financial affairs are prudently conducted (e.g. risk of fraud is appropriately managed) and that all the relevant financial information is captured in the NFP's accounting records and summarised in its financial reports to external stakeholders.

3

Assurance practitioners (the auditor)

If an NFP is required by law to have its financial statements audited or reviewed, the statutory audit or review must be undertaken:

- to the standards issued by the NZAuASB; and
- by an appropriately accredited accountant.

There are two types assurance practitioners that can undertake statutory audit or review engagements:

- **Licensed auditors:** This is the highest level of statutory recognition for assurance practitioners in New Zealand. A licensed auditor can audit or review (in accordance with the NZAuASB assurance standards) the financial statements of Financial Market Conduct (FMC) reporting entities.
- **Qualified auditor:** Chartered Accountants Australia and New Zealand (CAANZ) and CPA Australia members who are recognised as qualified auditors can carry out an audit or review in accordance with the NZAuASB assurance standards.

Other NFPs with no statutory requirement for an audit or a review may opt to require an audit or review of their financial statements in accordance with the NZAuASB standards.

4

The stakeholders using the NFPs' financial reports (including the funders)

There are a range of stakeholders who use the financial reports developed by NFPs, this includes funding organisations.

Users of financial reports need to have a reasonable level of financial knowledge, and have the time to engage properly with the report.

Users need to understand the key elements included within the statements and the relationships between those elements.

They also need to have a reasonable understanding of business and economic activities relevant to the NFP, to ensure they have the context to be able to interpret NFP's financial information.



The NZAuASB is a committee of the XRB established under Schedule 5 of the Crown Entities Act. The NZAuASB has delegated authority from the XRB to develop, or adopt and issue auditing and assurance standards for assurance practitioners (including professional and ethical standards).

NZAuASB standards

Assurance standards issued by the NZAuASB are provided across three key categories:

- 1. Professional and ethical standards** – these standards specify the ethical principles and quality control requirements that all assurance practitioners must adhere to.
- 2. Standards for assurance engagements over financial statements** – these are the two most common assurance engagements – audit and review of the financial statements. These have been developed to provide greater confidence in the information included in the financial statements.
- 3. Standards for assurance engagements other than audits and reviews** – these standards can be customised by an expert assurance practitioner to apply to a wide range of matters other than annual financial reports.

www.xrb.govt.co.nz