



# YOUR CFO FOR RENT Gene Siciliano

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*We Thought You'd Like to Know...*  
**Management Ideas for the Nonprofit Organization**

## For your audit committee: When the auditor has to go...

**W**ith California's passage of the Nonprofit Integrity Act of 2004 ("the Act"), boards of directors got a new opportunity to look at the relationship between their organization and their auditors. Many directors are finding that change is long overdue.

On top of that, foundation grant review committees are looking carefully at the way organizations manage change, in addition to all the things they traditionally look for, as they review grant applications that always seem to exceed the funds available.

By now everyone reading this article has heard of the Act, and most generally knows its provisions. But applying these new rules still requires judgment to achieve the results that the Act and boards of directors are striving for: *sound financial management of California's not-for-profit organizations and the best possible use of donor contributions.*

For example, while the Act broadly defines the role of an audit committee, it (*thankfully*) doesn't attempt to legislate good judgment in the management of the auditor relationship. Questions that remain for the board to answer, both directly and through its audit committee, include these:

- How do you choose an auditor – price, timetable, reputation, chemistry, or simply a strong referral from an associate?
- How do you assess the tradeoff between lower fees and possibly a lower level of service or capability?
- What should you expect from your auditor by way of suggestions for better financial management practices? General business practices? Your core services?
- Compliance aside, what is the lasting value you should expect from your auditor when they have finished their work?
- How do you judge whether your auditor is doing a good job or not?
- *How many years should you retain the same auditing firm?*

demonstrated how significantly it can affect the others.

We have a client, a mid-sized organization that had engaged the same auditor for over 30 years, in a long-term relationship that was built on familiarity and mutual trust. Hey, what could be bad about that? Read on.

Because of the long-term relationship, *and* a finance director who was underpowered for the job, the auditor had long ago stopped questioning repetitive flaws that never seemed to get resolved. Perennial audit issues included internal control weaknesses, missing or misfiled documents, weeks of waiting for analyses that should have been done every month, dozens of audit adjustments at year end, and more.

The treasurer, a long-time board member and retired CPA, exerted significant influence over the activities of the finance department, compensating in many ways for the staff and auditor weaknesses and ensuring reports got delivered to the board on time every month and questions got answered, albeit often by time consuming special project work that might not have been needed with adequate internal systems.

It was clear that this relationship was not the best management practice, and

*Audit... continued on page 2*

## “How do you know when it's time to make a change?”

None of these questions is simple to answer. So let's just look at that last one for this article. It might not be one you would have added to your list, and a recent engagement



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we believe it had the effect of weakening the effectiveness of the ED and gave the organization less on-staff financial muscle than was needed to support its operations.

We asked ourselves:

1. Would another audit firm have taken aggressive written exception to these issues until they were corrected?
2. Did the finance director decide to relax because the auditor no longer pressed for corrections?
3. Should the treasurer be spending more time in the finance office, or less?
4. Or, *did the finance director and the auditor survive in their respective roles because the treasurer picked up the slack?*

Our conclusion: it was time for a change. In part through our efforts, and those of a determined ED and board of directors, an audit committee was formed and properly authorized, and both the

finance director and the audit firm were replaced with stronger players. The end result gave both the board and the ED tools to do a better job in their respective roles of oversight and management. Needless to say, a critical part of this solution was the change of auditors.

**So how do you know when it's time to make a change?**

Regardless of how happy you are today with your current auditors, *we recommend you put that assignment up for competitive bidding every 3 to 5 years.* To do so more often can rob the organization of the valuable insights they can get from an auditor who knows the lay of the land.

But to do so *less* often runs the risk of an auditor gradually slipping into complacency, and no longer questioning financial practices that have been written up in the past and not corrected. It risks having an auditor overlook operational weaknesses because he or she has

simply learned to work around them over the years, and they are no longer troublesome enough to make an issue of them, to "rock the boat," so to speak. It risks losing all the insight that can come from "*a fresh pair of eyes.*"

Please don't misunderstand. *This is not an indictment of auditors.* Strong audit firms take pains to teach their staff to be alert for things that aren't quite right, and their internal reviewers routinely re-visit the findings of the field staff if they think something's been missed. That's part of the professional practice of auditing.

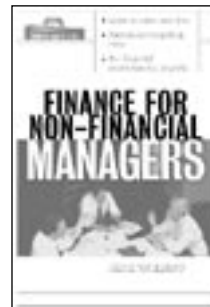
But *you can't be sure* that's always happening – that the training is getting done, that it's effective, that the reviewers will catch what the field auditor didn't, etc. You can't be sure that your finance director will fix it if the auditor doesn't put it into the management letter. *The message: don't take that chance. Periodically get that "fresh pair of eyes."*

OK, last step in the process – let's suppose you put the audit up for bidding and your current firm is the consistent low bidder, not an unlikely possibility. If your current auditor wins that competition twice in succession, perhaps they should be ineligible to participate the next time around. We think an audit firm should be changed at the outside every 8 to 10 years, even a good one. Well, you might say, doesn't that penalize the best firm? Perhaps, it does. But the risk to your organization from losing that fresh pair of eyes is, in our opinion, the greater and more important consideration. And besides, a really good firm already has more business than they can handle. They'll be fine, trust me.

If you would like to discuss your situation, or hear more of our reasons for these recommendations, or any other aspect of your audit firm relationship, just pick up the phone and dial 888-788-6534. We welcome your call.

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