

Proactive and Preventive Best Practices In the Wake of Wounded Warriors

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Proactive & Preventive Best Practices

- Risk management for non-profit organizations
- Proactive and preventive best practices
- A holistic view and some thoughts on addressing specific risks

Best Practices cont'd

- Holistic approach -- integral to understanding and addressing risk
- Structural challenges -- different from those in the for-profit realm
- "Non-profit" tells us what an entity isn't
- What is the affirmative definition of a non-profit?

Best Practices cont'd

- Non-profits existed for millennia
 - "For-profit" relatively new
- Charitable or educational mission
- Missions and entities come in all shapes and sizes

Best Practices cont'd

- Entrusted resources-serve the mission
 - Other people's money
- Conflicting ideals:
 - Confidentiality and transparency

NPO Stakeholders

- Board of directors–audit committee
- Executive leadership
- Staff (paid/volunteer)
- Service recipients (clients, students/parents, "participants")
- Donors/sustainers
- Stakeholders – many hats

NPO Stakeholders cont'd

- Risk management: Collaboration between BOD and executive leadership
 - Audit, Legal, Insurance, IT
- BOD and executive leadership
 - Differing roles

NPO Stakeholders cont'd

- Oversight v. Operations
- NPO stakeholders – not stockholders
- Risk-management sees "cons" *and* "pros" with entrusted resources

NPO Stakeholders cont'd

- Owning Risks
 - BOD and executive leadership are not “owners”
 - Risks heightened by mission and entrusted resources
 - Reputational risk
 - Non-confrontational organizational culture vs “bruising workplace”
 - “Emperor with no clothes”

NPO Stakeholders cont'd

- Wounded Warriors-case study in the mismanagement of structural risks
- Executive leadership-poor judgment with "entrusted resources"
- Where was BOD? Reactive not proactive
- Mission v. Intramural concerns
 - "Eye off the ball"
- Result: Reputational harm/catastrophic loss of good will among donors

NPO Stakeholders cont'd

- Holistic risk management:
“Murphy's Law”
- What risks aren't regularly addressed?
- What are the metrics of success / failure?

NPO Stakeholders cont'd

- **BOD**
 - Composition
 - Background
 - Strengths/weaknesses
 - Training
 - Policies and procedures
 - Tenures
 - Who knows what
 - Who has reliable view of peer organizations and your organization's context
- **Who on BOD manages risks? How?**

NPO Stakeholders cont'd

- Executive leadership
 - Background
 - Strengths/weaknesses
 - Areas of responsibility
 - Who knows what
 - Time limitations
- Who in leadership manages risks? How?
- BOD, leadership--manage risk together?
 - Oversight v. Operations

NPO Stakeholders cont'd

- Who is the "driver"?
 - Volunteer/inexpert BOD v. "Professional" executive leadership
- What risks are particular to your organization?
- Checks and balances: Risk review
- Subverting aspects of the institution to the mission

Regular Review of Key Documents

- BOD handbook
- Employee handbook
- BOD annual review of executive leadership
- Stakeholder handbooks
- Contracts
- Releases

Addressing Specific Risks

- Volunteer programs
- Data breaches
- Schools and other programs serving youth
- Programs serving the disabled and other vulnerable persons
- Financial risk: Audit committee

Addressing Specific Risks cont'd

- Litigation risk
- Conflicts of interest
- Fiduciary breaches – directors/officers
- General reputational risk
- Succession planning
- Financial distress
- Hitting the fan -- crisis management

Addressing Specific Risks cont'd

- Systematic review of risk management function
- BOD reps and executive leadership reps
- Input from outside professionals

Let's be careful out there.
Hill Street Blues

Thank you for your time.

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Expertise that Works

Audit Committees – Roles and Responsibilities Not-for-Profit Summit

Presented by Mike Young



Source

All information within originated from:

**AICPA's Audit Committee Toolkit
Not-for-Profit Entities, 3rd Edition**

Audit Committee Member Roles & Responsibilities

- **Assists the board in its oversight of:**
 - **integrity of the organization's financial statements;**
 - **internal controls including internal control over financial reporting;**
 - **independent auditor's qualifications, independence, and performance;**
 - **internal audit function's qualifications, independence, and performance;**
 - **the organization's risk management and overall governance process;**
 - **the organization's ethics and compliance program, which includes legal and regulatory requirements; and**
 - **the review of (or delegation thereof) IRS Form 990.**

Audit Committee Member Roles & Responsibilities - Continued

■ Audit Committee Process and Procedures

- Develop an audit committee charter and obtain approval from the Board.
- Conduct annually: review of the audit committee charter; self-assessment of effectiveness and efficiency of the audit committee.
- **Set agenda for the audit committee meetings based upon the charter and relevant issues. Consider developing an annual calendar based upon the charter.**
- Ensure meeting minutes are prepared.
- Provide audit committee reporting responsibilities to the board of directors.
- **Educate the other Board members on the understanding of the financial statements, financial statements risks, and internal controls over financial reporting.**
- Prepare annual audit committee report.
- **Conduct regularly scheduled and documented meetings with the independent external auditor, leader of the internal audit function, general counsel, CEO, CFO, senior management, and others as needed.**

Audit Committee Member Roles & Responsibilities - Continued

- **Oversight of the Financial Reporting Process**
 - Review critical accounting policies, practices, judgments, estimates, significant issues, significant transactions, adjustments, unusual items, complex issues, and business arrangements.
 - Understand complex accounting and reporting areas and how management addresses them.
 - Understand significant judgments and estimates used by management and their impact.
 - Review annual and interim financial statements and management's discussion and analysis.
 - Review annual audited financial statements (and A-133 reports as applicable).
 - Review IRS Form 990.
 - Question management and the independent auditor on significant financial reporting issues.
 - **Review comparative data from other organizations within the industry (reasonableness test).**
 - Facilitate the resolution of disagreements between management and the independent auditor.
 - Determine when a subject matter expert is required and hire advisers when needed.
 - **Review the independent auditor's management letters (recommendations and responses).**
 - Determine that adequate procedures are in place for the review of the entity's disclosures.

Audit Committee Member Roles & Responsibilities - Continued

- **Oversight of Financial Reporting Process**
 - **Oversee adequacy of the entity's system of internal controls.**
 - **Determine if the entity has adopted an internal control framework, such as COSO, in the establishment of their system of internal controls.**
 - Review development and implementation of a sub-certification process over internal controls and compliance with related Sarbanes Oxley section 404 attestations.

Audit Committee Member Roles & Responsibilities - Continued

- **Oversight of the Independent Auditor
(If Applicable)**
 - **Review audit plan and scope of audit to be conducted by the independent auditor.**
 - **Provide pre-approval of all audits, permitted non-audit services, and proposed fees.**
 - **Appoint or replace the independent auditor, including the periodic rotation of the audit partner.**
 - **Conduct evaluations of the independent auditor. Meet periodically with tax, IT, actuarial, and other specialists.**

Audit Committee Member Roles & Responsibilities - Continued

- **Oversight of Risk Management**
 - **Oversee system of risk assessment and risk management as determined by the board of directors. The audit committee should be focused primarily on financial risk.**
 - Oversee and respond to enterprise risk management activities.
 - Periodically reassess the list of top enterprise risks, determining who in the management committee is responsible for each risk.

Audit Committee Member Roles & Responsibilities - Continued

■ Oversight of Ethics and Compliance

- Oversee system for compliance with legal and regulatory requirements.
- **Ensure that management exhibits ethical behavior and reported violations receive action.**
- **Ensure that a code of conduct has been developed, reviewed, and updated as needed, and that all employees are given the code of conduct, understand it, and receive training on a regular basis.**
- Ensure that a chief ethics and compliance officer or equivalent has been appointed and that they have direct access to the board.
- Review the entity's procedures for reporting problems, including whistleblower hotline and other communication methods.
- Establish a process for audit committee special investigations, including but not limited to whistleblower allegation, anti-fraud plan compliance, discovery of error, and illegal acts.

Audit Committee Member Roles & Responsibilities - Continued

- **Limitation of Audit Committee's Role**
 - **NOT** the responsibility of the audit committee to plan or conduct routine audits or to be the primary determinant that the entity's financial statements and disclosures are complete and accurate and are in accordance with generally accepted accounting principles and applicable rules and regulations.

Financial Expert

Typical attributes of financial expertise:

- **Understanding of generally accepted accounting principles, generally accepted auditing standards, and financial statements**
- **Ability to assess the general application of such principles and standards in connection with the accounting for estimates, accruals, and reserves**
- **Experience preparing, auditing, analyzing, or evaluating financial statements that present a similar breadth and level of complexity of accounting issues, or experience actively supervising one or more people engaged in such activities**
- **Understanding of internal controls and procedures for financial reporting**
- **Understanding of audit committee functions (roles and responsibilities)**
- **General understanding of the financial issues and specific knowledge of the sector (for example, not-for-profit, education, etc.)**
- **General knowledge of the sector's current concerns or regulatory issues**
- **Understanding of the past 3–5 years of the entity's financial history**

Responding to the Identification of Material Weaknesses

Whether a material weakness is identified by management, internal audit, or the auditor, management should have a plan in place to correct the weakness(es), and the audit committee should be engaged in the review and approval of that plan.

Responding to the Identification of Material Weaknesses - Continued

- Discussions with **MANAGEMENT TEAM**:
 - Interview members of the management team (CFO, controller, etc.) about the weakness.
 - **Who identified the weakness, and in what context, such as routine internal audit or management review was it identified? What is the nature and root cause? How long has it existed? What are the implications (financial statement, regulatory, compliance, etc.)? What is the plan to correct?**
 - Explore with the management team how much was known about the weakness when the CEO and CFO prepared the financial statements and made certifications regarding those financial statements.
 - **In subsequent years, ask management team for an update on the status of the current year weakness.**

Responding to the Identification of Material Weaknesses - Continued

- Discussions with **Independent Auditor:**
 - **In executive session, discuss the findings, implications, and recommendations with the independent and internal auditors.**
 - Collect information from the independent auditor based on his or her knowledge of internal controls and experiences with other clients.
 - After meeting with the management team, those charged with governance and the independent auditor, address whether the weakness could have resulted from an illegal act.
 - **In subsequent years, ask the independent auditor for an update on the status of the current year weakness.**

Responding to the Identification of Material Weaknesses - Continued

- **Additional considerations:**
 - Consult experts from outside the entity about the weakness and the steps to correct.
 - **Work with management to develop a plan to correct.**
 - Review with management:
 - its plan to communicate to key stakeholders (donors, board members, employees, etc.) the results of the adverse opinion and reassure about corrective action plans, if appropriate.
 - its communications plan for the business press who might be interested in the plans to correct, if applicable.
 - **Inquire of management if they have considered other potential implications of the adverse report (debt covenant compliance, federal funds or other sources who may be interested).**

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