The Community Foundation requires that all organizations that submit applications to our competitive grant programs must receive a financial audit or a financial review. These are both terms used to describe levels of financial analysis completed by an "auditor," meaning someone external to the nonprofit organization (generally a CPA or accounting firm).

Here is more detailed information on what is meant by these terms:

Comparison of a Financial Audit and Financial Review

Attribute	Audit	Review
Engagement performed for the purpose of providing an opinion or report about whether the financial statements are presented fairly in conformity with generally accepted accounting principles	The auditor obtains a high, but not absolute, level of assurance about whether the financial statements are free of material misstatement	Accountant obtains limited assurance that no material modifications should be made to the financial statements
CPA obtains an understanding of internal control over financial statements	Yes	No
CPA tests the effectiveness of internal control	Frequently, but not always. The nature and extent of internal control testing depends on the auditor's judgment and conclusions pertaining to risk assessment	No
CPA verifies certain balances and transactions with third parties	Yes	No
CPA performs procedures to obtain reasonable assurance that financial statements are free of material misstatements whether caused by fraud or error	Yes	No
Financial statements are the responsibility of management	Yes	Yes
Financial statements are prepared by and are the responsibility of management	Yes, but CPA may assist in drafting	Yes, but CPA may assist in drafting
CPA guarantees that the financial statements are accurate and free of fraud	No	No
CPA evaluates the entity's policy decision and use of resources	No	No
CPA reports material weaknesses in internal control over financial reporting noted during the engagement to management or audit committee	Yes	Not required, though may be done if matters come to the CPA's attention
CPA acts as a whistleblower internally and reports identified fraud to management or audit committee	Yes	Yes, unless clearly inconsequential
CPA acts as a whistleblower externally and reports fraud and other matters to third parties, such as the IRS or state attorneys general	No	No
Cost	The cost of an audit or review will vary depending on many factors	

What is an audit?

The financial statements for nonprofit organizations (NPOs) are prepared by and are the responsibility of the NPO's management. The auditor's responsibility is to express an opinion on those financial statements based on the audit. Generally Accepted Accounting Standards (GAAS) require that the auditor plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud. Though this is a reasonable or high level of assurance, an audit does not provide a guarantee of accuracy.

An audit includes obtaining knowledge about and an understanding of the industry in which the entity operates. It includes acquiring information on key aspects of the entity, including operating methods, products and services, material transactions with related parties, and internal controls. Auditors make inquiries concerning financial statement related matters, such as accounting principles and practices; recordkeeping practices, accounting policies, actions of the governing board, and changes in business activities. Auditors apply analytical procedures designed to identify unusual items or trends in the financial statements that may need explanation. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Essentially, many of the preceding procedures are designed to determine whether the financial statements make sense, prior to applying additional audit procedures.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Typical audit procedures might include confirming balances with banks or creditors, observing inventory counting, and testing selected transactions by examining supporting documents. In addition, the auditor contacts other sources outside of the client to gather information that may be more objective than that obtained from internal sources. For example, the auditor may decide to obtain written confirmation from an NPO's donors about promises to give. While accumulating this type of evidence, the auditor tries to reduce the risk that the financial statements will be materially misstated.

Because an audit must be performed at a reasonable cost, an auditor tests a portion of the transactions and does not examine 100 percent of all transactions. The auditor must exercise skill and judgment in deciding what evidence to look at, when to look at it, and how much to look at. The auditor must also exercise skill and judgment in evaluating and interpreting the results of the tests performed. Additionally, because management in preparing its financial statements must use estimates and because estimates are inherently imprecise, an audit cannot guarantee exactness.

The auditor plans and performs the audit with an attitude of professional skepticism; that is, the auditor designs the audit to obtain reasonable assurance that material errors or fraud are detected. An audit, however, does not and cannot provide a guarantee that fraud does not exist. For example, the auditor may not find fraud concealed through forgery or collusion, because the auditor is not trained to catch forgeries, nor will customary audit procedures detect all conspiracies. Procedures the auditor performs pertaining to consideration of fraud in a financial statement audit include, but are not limited to, the following:

- Discussion among the engagement personnel regarding the risks of material misstatement due to fraud
- Identifying risks that may result in a material misstatement due to fraud
- Assessing identified risks after taking into account an evaluation of the entity's programs and controls
- Responding to the results of an assessment
- Evaluating audit evidence
- Communicating about fraud to management, the audit committee, and others

What is a review?

During a review performed in accordance with Statements on Standards for Accounting and Review Services (SSARS), an accountant obtains limited assurance that material changes to the financial statements are not necessary in order for the financial statements to be in conformity with Generally Accepted Accounting Principles (GAAP).

The end product of a review is the CPA's report on the accompanying financial statements. The CPA's report states the scope of the CPA's work (for example, which financial statements have been reviewed) and provides a statement that the CPA is not aware of any material modifications that should be made to the financial statements in order for them to be in conformity with GAAP.

As with all levels of service the financial statements are the responsibility of the NPO's management. The primary difference between a review and an audit is that in an audit, the auditor verifies management's amounts and disclosures with evidence provided by third parties. In a review, the CPA ordinarily does not verify management's amounts and disclosures with outside evidence unless the CPA believes that the amounts and disclosures are materially inaccurate.

In performing a review, the CPA performs inquiries and analytical procedures designed to identify unusual items or trends that may need further explanation by management. Essentially, the review is designed to determine whether the financial statements make sense without applying audit-like procedures. A review of financial statements does not require that the CPA obtain an understanding of the entity's internal control, assess control risk, test accounting records and responses to inquiries by obtaining corroborating evidential matter, or perform certain other procedures ordinarily performed during an audit. A review does include assessing the accounting principles used and significant estimates, made by management, as well as evaluating the overall financial statement presentation.