

## Audit Committee “Spot Checks”

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With the new audit standards issued a few years ago, organizations can no longer rely on their annual audit as its only check of internal controls. It is now the Audit Committee (or those tasked with that function) responsibility to ensure there are adequately designed internal controls that are operating effectively.

Many times we are asked for guidance to help the Audit Committee understand its role in this area. Here are some simple steps you might consider:

Step 1: Read and understand the controls that are in place now – management may already have some written policies and procedures to review. Update your understanding by asking staff to walk-through some of the procedures.

Step 2: Identify the highest risk areas to test – this is an opportunity to look at the organization holistically. After you've got a good idea of how the internal controls work, think about where fraud or errors could occur. Maybe it's in the credit card statement controls or in the grants management controls. It's up to you to identify which areas you want to focus on. Some other examples of key areas are receipts coming into the organization, disbursements going out of the organization, payroll, and bank reconciliations.

Step 3: Design a procedure to test the areas where risk is higher - It can be simple, like “We will select 2 credit card statements over the past 6 months and review each for complete documentation, accuracy and authorization.”

Step 4: Perform the procedure – Be sure to write down the steps you've taken, which samples you selected and your findings.

Step 5: Report your procedures and findings to the Board – Basically the board will want to know what you did: that you read and understood the current internal controls, identified the 3 riskiest areas, designed and performed procedures to test the controls, and found no concerns or the following issues.

Step 6: If issues were found – Be sure to monitor and re-check the area in the future and report back to the Board.

The Audit Committee can also delegate this responsibility to others, including staff and volunteers, as long as there is no conflict of interests. For example, you would not want a staff member evaluating and testing controls in an area in which they work or are responsible for.

Spot checks do not have to be elaborate, and you can set a schedule to do various checks on various areas throughout the year. Best practices suggest rotating through different control areas for better coverage.



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## State of WA Excise Tax Concerns

As the State of Washington has been hit by lean times, more and more nonprofit organizations are being subjected to State audits by the Department of Revenue. Make sure your organizations has addressed these primary issues before they come knocking on your door!



In Washington State, there is no business income tax. There is however a “gross receipts” tax, commonly referred to as the business and occupation or B&O tax. The good news is that organizations don’t have to worry about calculating net income for state tax purposes; the bad news is all gross receipts, unless there is a specific exemption or deduction, is taxable. There is no generic exemption for all nonprofit organizations. Almost ALL nonprofit organizations are subject to this tax.

**THE ASSUMPTION SHOULD BE THAT  
ALL RECEIPTS ARE TAXABLE UNLESS  
YOU CAN PROVE OTHERWISE.**

Gross receipts is defined as the value of products, gross proceeds of a sale or gross income of a business. This definition includes any cash or non-cash payments received or earned by the organization. For nonprofit organizations, examples include contributions, gross sales from event registrations, government contracts, dues, fees, other fees for services, and reimbursements for expenses.

It is equally important to understand exemptions and deductions.

**Exemptions** are items that Washington allows businesses to exclude from the gross receipts reported. Common exemptions include fundraising activities (donations, special events, etc.), interest income, and government grants to health and social welfare organizations.

**Deductions** must be reported as gross receipts, but then are listed as a qualified deduction, which lowers the B&O taxable amount. Common deductions include income received for membership dues (that aren’t in exchange for significant services), certain income received by arts and cultural organizations, and trade show booth fees (if the trade show is not open to the general public).

For more information, see the attached WAC regarding nonprofits: <http://apps.leg.wa.gov/wac/default.aspx?cite=458-20-169> . There is a full list of exemptions and deductions starting at 82.04.310: <http://apps.leg.wa.gov/rcw/default.aspx?Cite=82.04>

It is highly recommended that you scan through your organization’s sources of income and make sure you can specifically identify an exemption or deduction that keeps each income line from being taxable.

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Should you have any questions about the content of anything in this newsletter, please contact us.

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