



Compilation, Review and Audit

A Comparative Overview

A compilation, review or audit – which does my organization need? The level of service is determined by the needs of the nonprofit organization and what your donors and/or creditors require. The higher the level of service required, the more time the CPA needs to complete the engagement and therefore the more costly the engagement. However, the organization may want to have an audit when it has grown in complexity, has experienced a major change in financial management, is preparing for a large fundraising campaign or simply wants a periodic evaluation of financial health.

When an organization is considering an audit, the general rule-of-thumb is when income reaches approximately \$1 million and staff size is about five or more.



Assurance

A CPA can obtain a level of “assurance” about whether the financial statements are in accordance with the financial reporting framework (i.e., GAAP or other basis of accounting such as cash basis). The CPA obtains assurance by obtaining evidence. There are different levels of assurance ranging from no assurance at all (compilation) to the highest level of assurance (audit).

Material Misstatement

A misstatement is a difference between a reported financial statement item and what is required for the item to be reported in accordance with the applicable financial reporting framework. A misstatement may result from error or fraud. A material misstatement is one where the amount or nature of the difference would cause a user to form an incorrect conclusion about a financial statement.

Compilation

- Compiled financial statements represent the **most basic level of service** CPAs provide with respect to financial statements. The CPA prepares financial statements

based on the accounting records the organization provides; however, the CPA does not verify the accuracy or completeness of the information.

- In a compilation engagement, the CPA must have an understanding of the industry in which the organization operates, obtain knowledge about the organization, and read the financial statements to consider whether such financial statements appear appropriate in form and free from obvious material errors.
- The CPA issues a compilation report which states that the CPA did not audit or review the financial statements and accordingly does not express an opinion, a conclusion or provide any assurance on them.

Review

- Reviewed financial statements **provide the user with “limited assurance.”** The CPA performs analytical procedures, inquiries and other procedures to provide the user with a level of comfort on the accuracy of the financial statements.
- In a review engagement, the CPA is required to understand the industry in which the organization operates, and knowledge about the organization itself – including the accounting principles and practices generally used in the industry and by the organization – sufficient to

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Comparative Snapshot			
	Compilation	Review	Audit
Level of assurance	No assurance	Limited assurance	High level of assurance
CPA's independence	CPA does not have to be independent	CPA must be independent	CPA must be independent
Procedures performed	Inquiry and other procedures not required unless issues are identified	Inquiry and analytical procedures required plus additional procedures if issues are identified	Inquiry and analytical procedures as well as verification and substantiation procedures required
Obtain an understanding of internal control and assess fraud risk.	Not required	Not required	Required

identify areas in the financial statements where it is more likely that material misstatements may arise.

- A review is substantially narrower in scope than an audit. A review does not obtain an understanding of the entity's internal control, assess fraud risk, test accounting records or perform other procedures ordinarily done in an audit.
- The CPA issues a review report that includes a conclusion as to whether, based on the review, the CPA is aware of any material modifications that should be made to the financials in order for them to be in accordance with the applicable financial reporting framework.

Audit

- Audited financial statements **provide the user with the highest level of assurance service that a CPA performs** – that is, provide the user comfort on the accuracy of the financial statements. The CPA performs procedures in order to obtain “reasonable assurance” (defined as high

but not absolute assurance) about whether the financials are free from material misstatement.

- In an audit, the CPA is required to obtain an understanding of the entity's internal control and assess fraud risk. The CPA is also required to corroborate the amounts and disclosures included in the financial statements by obtaining audit evidence through inquiry, physical inspection, observation, third-part confirmations, examination, analytical procedures and other procedures.
- The CPA issues an audit report that expresses an opinion on whether the financial statements are presented fairly, in all material respects, in accordance with the applicable financial reporting framework. In addition, the CPA is required to report to the organization any significant or material weaknesses in the system of internal control that are identified during the audit.

