PREPARE FOR AUDIT

TIPS FROM THE AUDITOR FOR NOT-FOR-PROFIT BOOKKEEPERS & ACCOUNTANTS

BY

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A. Purpose of the E-book

"The price of good quality accounting records is eternal vigilance."

The purpose of this e-book is to assist bookkeepers and accountants new to NFPs in preparing accurate accounting records. It will also ensure that your accounts will be audit ready with the minimum amount of effort.

As the Auditor of many NFPs, from small to large, I found that certain issues or mistakes are very common.

Collins & Co Audit Pty Ltd always seeks to add value in our audits by pointing out potential risk areas that are hidden in seemingly immaterial account balances.

Larger audit firms that focus only on the material balances tend to ignore these risk areas associated with immaterial balances, which seldom get resolved unless the NFPs management is proactive.

These common risks can be prevented and detected by regularly reviewing potential problem areas, which can then be addressed and managed in a timely fashion.

The users of this e-book may find that some of the issues highlighted are very simple and common sense to any accountant or bookkeeper. Nonetheless these seemingly small issues are important and could be an indicator of a much larger problem.

I hope this e-book helps your NFP improve the quality of its accounting records and to ensure accurate financial statements that are audit ready.

I would love your feedback on whether you found this e-book useful and whether there are other topics in this area that may be of interest to you.

Please feel free to contact me on re@collinsco.com.au.

We also keep our NFP clients up to date with the quarterly Collins NFP Advisor newsletter, as well as other communication on specific issues as they arise.

Please email partner@collinsco.com.au if you are interested in receiving these.

Author's notes:

a. Throughout the text, 'Not-For-Profit NFPs' will be abbreviated to 'NFPs'.

b. At the end of the e-book, you will find a glossary with definitions of some of the terms used.

c. Working Papers 58A & 58B, refer to in this e-book, can be obtained in Excel format, by emailing the author at re@collinsco.com.au

B. Before you start preparing for the audit

1. **Ensure that the prior year net surplus or deficit per the accounting software agrees to the prior year audited financials.**

2. **Ensure that the opening retained earnings per the accounting software agrees to the prior year audited financials.**

   Do not assume that the comparatives information in the accounting software is correct.

   I find too often that the NFP's prior year balances vary from the financial statements we audited in the prior year.

   If the opening balances are incorrect, then the chances are that the current year closing balances are incorrect as well.

Next steps if you find a problem:

If you find that there are differences, do the following:

a) **Ask your auditor for a copy of the prior year final audited trial balance and compare the balances to the prior year closing balances in your accounting software.**

b) **Ensure that you have posted the prior year audit adjustments.**

c) **Check if any other adjustments have been made that would have changed the comparative information and the opening retained earnings.**

We recommend that the NFP accountant or bookkeeper ensure that they receive the audit adjustment journals and agree the adjusted balances in the accounting software to the audited financial statements as soon as possible after the conclusion of the annual audit to avoid the above issue.

However, sometimes errors can creep in during the financial year, which will create a problem.

We recommend that the NFP accountant or bookkeeper "lock" the financial year after the audit adjustments had been posted to ensure transactions cannot be backdated to the prior audited financial years and therefore create issue with changes in the opening retained earnings and other account balances.

C. General Comments

1. **Ensure that a detailed general ledger for the year under audit is downloaded from the accounting software or can be made available to the auditor by inviting them as a user to the NFP's accounting software file.**

2. **Ensure that you understand every account balance on the balance sheet, whether it is material or not, and that you ask and consider the following questions:**

   a. Do you know what this account balance means?

   b. What do you expect this account balance to represent?

   c. Is this account reconciled?

   d. Does the fact that this account balance is not reconciled or regularly reviewed indicate the existence of a deeper problem?

3. **The process to follow when an account balance is not reconciled, is as follows.**

   Every account in the balance sheet should be supported by a reconciliation, sub ledger or supporting schedule that explains how the balances were calculated.

   If an account is not reconciled:

   a) Ask the auditor if he/she received or prepared a reconciliation of the said account's closing balance as part of the prior year audit.

   b) Review the transactions in the general ledger for the last three months and see if you can work out what the balance consists of.

   c) If the account cannot be reconciled, highlight the issue with the auditor.

4. **Regular Reconciliations of Key Accounts**

   It is important that all key accounts are reconciled on a regular basis, whether it is monthly or quarterly.

   Such key accounts will include: all bank accounts, accounts receivable, accounts payable, fixed assets, GST, PAYGW, superannuation payable, sundry or other debtors, sundry or other creditors, provisions for employee entitlements, salaries and wages, etc.

5. **Immaterial account balances can hide serious issues.**

   Immaterial account balances, which are not reconciled, can hide problems, which never are identified or addressed due to the auditor's materiality concept.

   For example, the superannuation payable account balance is small, however, the balance is not what you expected the balance to be. This could mean that some employees' historical superannuation had not been paid.

D. Cash & Cash Equivalents (Bank Accounts & Term Deposits)

1. **Ensure that all the bank accounts and term deposits are reconciled at the end of each month and at the end of the financial year.**

   Ensure the bank reconciliation reports are not **<u>out of balance</u>** in the accounting software.

2. **Agree the bank account balances to the last bank statement of the financial year.**

   If the bank account balances does not agree to the last bank statement, obtain a bank reconciliation report from the accounting software to ensure the bank account has been properly reconciled.

3. **Agree the term deposit balance to the last roll over document or bank statement of the financial year.**

   If the term deposit balances does not agree to the last bank statement, obtain a bank reconciliation report from the accounting software to ensure the term deposit bank account has been properly reconciled.

4. **Review the bank reconciliation report, where applicable, for long outstanding items, i.e., older than three months.**

   If the bank reconciliation report shows long outstanding items, review and investigate the outstanding items.

   Especially look out for long outstanding deposits and direct payments.

   A deposit should not be an outstanding item unless it is banked within a week after month's end.

   The accountant/bookkeeper should also investigate all direct payments (EFTs) shown as outstanding.

5. **The use of general journals in control accounts (such as bank accounts) could have been utilised to hide fraudulent activities – or are just poor bookkeeping.**

<u>Next steps if you find a problem:</u>

If the bank reconciliation report is out of balance:

a) **Do a quick check, going month end by month end in the accounting software bank reconciliation reports, from financial year end working backwards, to work out where the issue started.**

b) **It may be necessary to check and agree the bank transactions in the accounting software to the bank statements on a line-by-line basis for the period when the error occurred.**

c) **Investigate and correct the problem in the accounting software.**

E. Petty Cash and Cash on Hand

1. **Are the cash on hand balances correct and do they still exist?**

2. **Obtain a written confirmation of the financial year end balance of the cash held from each staff member that controls petty cash.**

F. Trade Debtors/ Accounts Receivable

1. **Agree the Trade Debtors/ Accounts Receivable balance with the Detailed Aged Trial Balance Sub Ledger Report from the accounting software.**

   Ensure that you have provided the auditor with the correct report, especially if the NFP uses MYOB (i.e., remember to provide the auditor with the detailed reconciliation report at year end).

   If the balance does not agree to the sub ledger, investigate and correct.

   General journals posted to the general ledger account could cause imbalances.

2. **Establish the reasons behind the long outstanding invoices, i.e., older than three months.**

   Why is the invoice still outstanding? (Payment plan in place, unrecoverable, slow paying, etc.)

   Questions that management need to consider are:

   - How old is the invoice?
   - Why is it still outstanding?
   - Is the debt recoverable?

3. **Do you need to make a Provision for Doubtful Debts based on the review of long outstanding invoices?**

4. **Review the credit notes issued after year end to ensure the outstanding invoices at year end have not been cancelled and should be provided as part of the Provision for Doubtful Debts.**

5. **The use of general journals in control accounts (such as trade debtors) could have been utilised to hide fraudulent activities – or are just poor bookkeeping.**

G. Sundry/ Other Debtors & Prepayments

1. **Where the NFP has a Prepayments balance at balance date in the prior year, ensure that you consider whether the NFP should also have a balance for Prepayments for the current year.**

   Remember that prior year prepayments are normally brought into the current year's expenses on a month by month or quarterly basis until all the relevant balances have been expensed.

   It is good practice to make copies of invoices/ supporting documentation of all expenses that you consider to be prepayments during the year and have added to the Prepayments schedule.

2. **Where the NFP have Sundry Debtors or Other Debtors balances, ensure that you understand what these balances consist of.**

3. **Rental Bonds or Security Deposits for Leased Premises needs to be held in an interest bearing account in trust for (ITF) the NFP.**

   Security deposits/rental bonds for commercial properties are sometimes not kept in an interest-bearing account by the landlord or real estate agent (in Victoria) in trust, or in the name of the NFP.

   Under section 24 of the Victorian Retail Leases Act 2003, a landlord, or an estate agent acting on behalf of a landlord, is required to hold a security deposit in an interest-bearing account.

   A security deposit is an amount of money paid by a tenant as surety to a landlord. A security deposit provides the landlord with some level of protection, as it covers a landlord for performance of a tenant's obligations. The security deposit requested by a landlord is usually equivalent to one or two months' rent. The dollar amount of a security deposit is not regulated by retail leases legislation, and landlords and tenants should negotiate a mutually agreeable amount.

   The landlord must account to the tenant for interest earned on the deposit, but the landlord is entitled to keep the interest and deal with it as money paid by the tenant to the landlord to form part of the security deposit. This means that the interest generated by the security deposit is to be passed on to the tenant, as with the initial payment, provided the tenant complies with their obligations under the lease.

   In an instance where the landlord or real estate agent does not act in accordance with their legislative obligations, the security deposit of the NFP may be at risk of not being recoverable.

   Commercial property rental bonds can be easily embezzled if not kept in a separate interest-bearing account.

H. Investments in Listed Shares or Managed Funds

1. Agree the investments to the Investment Portfolio Report at balance date, if applicable.

a) Obtain the investment documentation for the full year under audit.

b) If the investments are in a managed fund/ portfolio, is an audit report available that covers the annual investment statement/ year end reporting pack.

c) If no audit report is available, your auditor will need to confirm the name of the investor (ownership), the number of shares/ units held and the market values of shares/ units at balance date using Share Registries.

2. If the investments consist of separate shareholdings managed by the NFP, obtain:

a) All Dividend statements or Distribution statements for the full year under audit.

b) The shareholder investor number (HIN) so that your auditor can confirm the name of the investor (ownership), the number of shares/ units held and the market values of shares/ units at balance date using Share Registries.

3. Establish whether the investments are recorded in the accounts at cost or market value.

Investments can be recorded at their historical cost or at the market value at quarter or year end, especially for investments that are listed on the Australian Stock Exchange or where other reliable sources of market value information are available.

I. Fixed Assets

1. **Ensure the organization has a detailed fixed asset register for the year being audited.**

2. **Agree the opening cost and accumulated depreciation balances to the prior year closing balances.**

   Often NFPs delete obsolete assets or scrapped assets from the fixed asset register, which leads to opening balances that do not agree.

   These obsolete and scrapped assets should be removed from the fixed asset register by “disposing” of the assets in the accounting software or having two lines for the “disposed” asset in the Excel spreadsheet that the NFP accountant or bookkeeper may be using.

3. **Agree the closing cost and accumulated depreciation balances per the accounts to the detailed fixed asset register closing balances.**

4. **Ensure the new additions are recorded in the fixed asset register at the GST exclusive amounts.**

5. **A complete review may need to be undertaken in respect of the NFP's asset register and depreciation schedules, to ensure:**

   - Existence of assets recorded on the schedules;
   - Completeness of the schedules, i.e. all identifiable assets are recorded;
   - Accuracy of the asset schedules;
   - Appropriate depreciation charges; and
   - Impairment to fixed assets, if any, are accounted for.

   Each fixed asset should also be assigned a unique location identification number to enable the management to conduct an effective stocktake of the fixed assets at regular intervals.

   Inventory lists that list all the relevant fixed assets in each room would assist with the stocktake process.

   Smaller assets such as laptops, PDAs and iPads can be recorded in an inventory list, then ‘booked out to staff members’, who are then held responsible for the safekeeping of that asset.

J. Loans Receivable

1. **Obtain a loan confirmation from the person or entity that borrowed the money from the NFP.**

2. **Enquire about the terms and conditions of the loan, i.e., interest rate, repayment terms or repayable on call, existence of a loan agreement, etc.**

   Have the conditions and terms of the loan been met?

3. **If interest is payable on the loan, recalculate the interest amount for the year being audited.**

4. **Establish whether the loan is recoverable.**

   Why do management think the loan is recoverable?

K. Loans Payable

1. **Obtain a loan confirmation from the person or entity that the NFP borrowed the money from.**

2. **If the loan is from a financial institution obtain the loan statements for the full financial year and tie in the interest paid amount to these loan statements.**

3. **Enquire about the terms and conditions of the loan, i.e., interest rate, repayment terms or repayable on call, existence of a loan agreement, etc.**

   Have the conditions and terms of the loan been met?

L. Trade Creditors/ Accounts Payable

1. **Agree the Trade Creditors/ Accounts Payable balance with the Detailed Aged Trial Balance Sub Ledger Report from the accounting software.**

   Ensure that you have provided the auditor with the correct report, especially if the NFP uses MYOB (i.e., remember to provide the auditor with the detailed reconciliation report at year end).

   If the balance does not agree to the sub ledger, investigate and correct.

   General journals posted to the general ledger account could cause imbalances.

2. **Consider the reasons behind the long outstanding unpaid invoices i.e., older than three months.**

   Did the NFP forget to allocate a payment already made against an outstanding invoice?

   Is there a valid reason why the supplier invoice has not been paid and will it be payable in future?

3. **Review the supplier invoices paid after year end to ensure no material unrecorded liabilities exist.**

   Does the NFP record the accounting entries on invoice or payment date?

   If the NFP records the accounting entries on payment date, there may be an unrecorded liabilities issue.

4. **Be on the lookout for invoices paid twice or duplicate invoices recorded via the Accounts Payable.**

5. **Where the NFP have suppliers from whom they make frequent purchases, we recommend that the supplier's month end statement should be reconciled to the supplier's accounts payable sub ledger to ensure all invoices have been recorded.**

6. **The use of general journals in control accounts (such as trade creditors) could have been utilised to hide fraudulent activities – or are just poor bookkeeping.**

7. **If a journal is used to record an estimate of outstanding invoices yet to be received instead of using the Accounts Payable or Trade Creditors by recording each invoice through the financial year, please ensure a schedule of the closing balance and supporting documentation is prepared for the Auditor.**

M. Sundry Creditors & Accruals and Income/ Income Received in Advance

Accrued Expenses/ Accruals

If during the course of the NFP's operations certain expenses are incurred, but no invoice is received by balance date, then these expenses are referred to as accruals/ accrued expenses.

These expenses (or an estimate of the expenses) should still be included in the Income Statement. When the actual invoice is received, an adjustment can be made to correct the estimate.

Accrued expenses/ accruals are normally reversed at the start of the next financial year so that when the actual invoices for these expenses are paid, the expense are offset by the reversal to the expense accounts.

Please ensure a schedule of the year end Accrued Expenses/ Accruals and supporting documentation is prepared for the Auditor.

How to perform a Superannuation Payable Reconciliation?

NFPs can make inaccurate payments of their employee's Superannuation Guarantee Charge (SGC) contributions.

1. Does the bookkeeper/accountant perform a Superannuation Payable Reconciliation?

2. What do you expect the balance to be at year end?

    - For NFPs that make quarterly Superannuation payments, the expected Super Payable balance would be the SGC deductions for the last quarter.

    - For NFPs that make monthly Superannuation payments, the expected Super Payable balance would be the SGC deductions for the last month.

What can go wrong?

a) Manual journal adjustments were posted to the Superannuation Payable Account during the financial year.

b) The first Superannuation payment of the financial year did not clear the carried forward opening balance, which indicates an historical issue.

c) Ensure the Superannuation payments posted to the Superannuation Payable Account for the financial year were correct and off sets against the SGC Deductions for the month/ period to which it relates.

d) The Superannuation liabilities for the prior periods have not been paid yet.

Ensure balance has been subsequently paid.

Failure to pay may indicate a cash flow issue.

Income Received in Advance

Grants & Funding Received in Advance

When the NFP documents the Income in Advance information, the auditor requires the supporting agreements and need a summary of the Income in Advance Balance, which clearly document:

a) Source of each Funding/ Grants in Advance amount

b) What project does it relate to?

c) What is the timeframe for the project, i.e., 1 January 2020 to 31 December 2020?

d) On which basis is the deferred revenue calculated, i.e., unspent funding, number of months, etc.

e) Why is the income being deferred?

f) Keep a copy of the agreements or documentation for the Auditor of each Funding stream/Grant.

AASB 15 Revenue from Contracts with Customers became effective on 1 January 2019 for NFP's. A key principle of AASB 15 is that revenue is recognised when performance obligations/ specific promises are fulfilled. Where specific promises have not been met, the revenue from that contact should be deferred.

Deposits for Events/ Services Received in Advance

Please note that where deposits are received for future events may consist of a refundable and non-refundable portion, which impact on the treatment of GST on such income and the timing of the payment of the GST.

N. Reconciliations of GST & PAYGW Payable

Why do we do annual GST & PAYGW Reconciliations?

An annual GST and PAYGW Reconciliation needs to be performed for each NFP, irrespective of whether the account balances are material or not.

Purpose of Working Paper 58A

We recommend you use **Working Paper 58A** to reconcile the information for the GST and PAYGW as lodged per the financial year's BAS & IAS Statements with the information per the accounting software's the Payroll Reports to ensure the following:

a. The correct **adjusted gross wages** amounts (W1) have been declared to the ATO for the financial year.
b. The correct PAYGW amounts have been declared to the ATO for the financial year.

The above exercise will allow you to detect and correct possible PAYGW errors that occurred during the reporting to the ATO, so that you can advise the NFP about these issues.

You will also be able to detect any over or under payments in relation PAYGW, which I found in the past can happen very easily.

Did the NFP declare the correct Wages amount under Label W1?

Include at W1 total gross payments from which the NFP is usually required to withhold amounts.

W1 do not include:

- amounts subject to salary sacrifice arrangements, i.e. FBT Exempt entities
- employee salary sacrifice super contributions

Purpose of Working Paper 58B

We recommend you use **Working Paper 58B** to reconcile the information for the GST as lodged per the financial year's BAS Statements with the information per the accounting software's GST Liability Reports to ensure the following:

a. No changes were made to prior quarter's information by backdating a transaction, which means that the information is now incomplete/ incorrect, i.e. we suggest the temporary lock of the prior BAS quarters.

The above exercise will allow you to detect and correct possible GST errors that occurred during the reporting to the ATO, so that you can advise the NFP about these issues.

You will also be able to detect any over or under payments in relation to GST, which I found in the past can happen very easily.

I also found in the past that the GST treatment of suppliers was not consistent throughout the financial year, especially when the supplier's GST registration status remained unchanged. Review the GST treatment of all invoices for each supplier and check consistency.

<u>How to perform a GST Reconciliation – Accruals Basis</u>

The basic principle for the Reconciliation of the GST Account when the NFP reports GST on the Accruals Basis is as follows:

GST payable on Accruals Basis per June 2020 BAS = GST Account Balance

<u>What can go wrong?</u>

a) **You used the GST Collected and GST Paid per the Cash Basis Reports in the accounting software to complete Working Paper 58B, instead of the Accruals Basis Reports.**

b) **Working Paper 58B shows that the NFP overstated or understated the GST Collected.**

c) **Working Paper 58B shows that the NFP overstated or understated the GST Paid.**

d) **Manual journals were posted to the GST Accounts during the financial year, which are not reflected on the GST Reports.**

e) **The first GST payment of the financial year did not clear the carried forward opening balance, which indicates an historical issue, which may go back for many years.**

f) **Ensure the GST (BAS) payments posted to the GST Accounts for the financial year were correct by comparing the information to the BAS lodged during the financial year and the information as reflected on the ATO Integrated Client Account.**

Do not solely rely on the Xero GST Reconciliation as it can be incorrect, i.e., garbage in = garbage out.

Review the income and expenses labelled as GST Free or Non-Taxable items to ensure the GST was reasonable and make sense.

How to perform a GST Reconciliation – Cash Basis

The basic principle for the Reconciliation of the GST Account when the NFP reports GST on the Cash Basis is as follows:

GST payable on Cash Basis per June 2020 BAS

Add: GST included in Accounts Receivable: June 2020

Less: GST included in Accounts Payable: June 2020

= Expected GST payable on Accruals Basis at June 2020

What can go wrong?

a) **You used the GST Collected and GST Paid per the Accruals Basis Reports in the accounting software to complete Working Paper 58B, instead of the Cash Basis Reports.**

b) **Working Paper 58B shows that the NFP overstated or understated the GST Collected.**

c) **Working Paper 58B shows that the NFP overstated or understated the GST Paid.**

d) **Manual journals were posted to the GST Accounts during the financial year, which are not reflected on the GST Reports.**

e) **The first GST payment of the financial year did not clear the carried forward opening balance, which indicates an historical issue, which may go back for many years.**

f) **Ensure the GST (BAS) payments posted to the GST Accounts for the financial year were correct by comparing the information to the BAS lodged during the financial year and the information as reflected on the ATO Integrated Client Account.**

Do not solely rely on the Xero GST Reconciliation as it can be incorrect, i.e., garbage in = garbage out.

Review the income and expenses labelled as GST Free or Non-Taxable items to ensure the GST was reasonable and make sense.

Please keep in mind that not all Accounts Receivable and Accounts Payable amounts will include GST.

Please email the author at re@collinsco.com.au to obtain an Excel Version of **Working Papers 58A & 58B**.

How to perform a PAYGW Reconciliation

By performing a PAYGW Payable reconciliation when such payments are due to the ATO, the NFP will ensure that each employee's PAYGW tax has been paid correctly and that the general ledger liability only reflects future PAYGW payable amounts.

The way to approach the PAYGW Reconciliation is as follows:

1. Did the NFP perform a PAYGW Reconciliation?
2. What do you expect the balance to be at year end?
    - For NFPs that only lodge Business Activity Statements (BAS), the expected PAYGW balance would be the PAYGW deductions for the last quarter.
    - For NFPs that lodge both Business Activity Statements (BAS) and Instalment Activity Statements (IAS), the expected PAYGW balance would be the PAYGW deductions for the last month.
3. Have the PAYGW liabilities for prior periods been paid prior to the financial year end?
4. Review the ATO Integrated Client Account for the financial year to ensure that you can reconcile the closing balance at financial year end with the GST and PAYGW accounts information.

What can go wrong?

e) Manual journals were posted to the PAYGW Account during the financial year, which are not reflected on the Payroll Reports.

f) The first PAYGW payment of the financial year did not clear the carried forward opening balance, which indicates an historical issue.

g) Ensure the PAYGW (IAS & BAS) payments posted to the PAYGW Account for the financial year were correct by comparing the information to the IAS & BAS lodged during the financial year and the information as reflected on the ATO Integrated Client Account.

h) The PAYGW liabilities for the prior periods have not been paid yet.

O. Provision for Employee Entitlements

When you calculated the amounts owed to employees at the end of the financial year, you need to ask yourself the following questions:

a. Did the NFP use the employees’ pay rate applicable for the last period in the current financial year?

b. Are you confident the NFP accurately recorded the annual leave entitlements hours that accrued during the financial year and the actual annual leave hours taken?

c. Did the NFP include 17.5% leave loading for all the employees that are entitled to leave loading?

d. Are you confident the NFP accurately recorded the actual hours worked by each employee to enable you to calculate their Long Service Leave Entitlements?

e. What Long Service Leave entitlements are staff entitled to - 8.6666 weeks per year or more generous per their Award?

f. Did the NFP need to provide for any Time in Lieu, which will be payable to employees in the next financial year?

g. Did the NFP need to provide for Personal/ Carer’s Leave or what is the NFP’s accounting policy for Personal/ Carer’s Leave?

h. Did the NFP register eligible staff for the Portable Long Service Benefits Scheme (in Victoria) from 1 July 2019?

i. Employees should be encouraged to take leave during the period in which it is accrued. This minimises the level of provisions required at balance date, ensures that annual leave is paid at the same rate at the time it is earned and represents good OH&S practice.

<u>What are the Next Steps?</u>

1. Obtain a leave entitlement report from the accounting software.
2. Prepare the Provision for Long Service Leave calculation.
3. It is important to extract from the payroll system each employees’ hours worked for that year to ensure the NFP can track the hours worked for employees for the purposes of the calculation of the employees’ long service leave entitlements.

   The average weekly hours used for the long service leave entitlement calculation is the greatest of the below three calculations:

   a. Average of the hours worked during the last 52 weeks, i.e., 1 year;

   b. Average of the hours worked during the last 260 weeks, i.e., 5 years; and

   c. Average of the hours worked during the entire period of employment.

P. How does Portable Long Service Benefits Scheme impact on the Provision for Long Service Leave?

What is the Portable Long Service Benefits Scheme (PLSB Scheme)?

- Victoria's Portable Long Service Benefits Scheme began in July 2019 to ensure eligible workers in the community services could build up long service benefits based on service to the industry as a whole, rather than years with a single employer.
- Community services employees are required to be a part of the scheme starting 1 July 2019. From 1 January 2020, NDIS and children's services employees, including childcare are also required to be part of the PLSB Scheme.
- The PLSB Scheme applies to all employees who are classified as community service workers under the test – full time, part time and casual staff are all required to be part of the PLSB Scheme.
- There is no recognition of prior service for community services staff before 1 July 2019 or 1 January 2020, depending on when the employees were registered with the PLSB Scheme.
- The Victorian Government has identified the following awards as the main awards applying to the community services sector based on extensive consultation with the sector and unions:
  - Social, Community, Home Care and Disability Services Industry Award 2010
  - Children's Services Award 2010
  - Educational Services (Teachers) Award 2010
  - Labour Market Assistance Industry Award 2020
  - Supported Employment Services Award 2020
- The PLS Authority (PLSBA) will only reimburse employees for the period of time that they have been registered in the scheme, i.e., from 1 July 2019 or 1 January 2020 or any other eligible date.

  For example, if the worker has worked for the NFP employer for 8 years, but only has 18 months recorded with the PLSBA, the PLSBA will only reimburse the employer for the long service leave associated with the 18 months of service.

  The employer will be liable to pay the balance.
- NFP employers will not be reimbursed for payments to the PLSB Scheme, this includes after an employee leaves the NFP to work at another eligible NFP and if the employee exiting the community services sector.
- Employees can choose to have their entitlement paid by their employer or the PLSA. If they choose to be paid by their employer, the employer can then seek reimbursement from the PLSA.

  Please beware that these reimbursements from the PLSA will not include superannuation, but only the long service leave amount owed by the PLSA.

- It is my understanding that where the employees' LSL entitlements under an award is more generous than the statutory long serve leave requirements, the PLSA will reimburse an employer at the higher rate if staff are employed on a fair work instrument.

<u>How to account for Portable Long Service Leave?</u>

a. Impact on the Employee's Long Service Leave Liability

The number of hours accrued will be frozen as at 30 June 2019, 31 December 2019 or any other eligible date when the employee is registered for the PLSB Scheme, depending on their circumstances.

The employee's Long Service Leave Liability will increase each year to reflect an increase in wage rate every year.

Where any employee takes LSL, the NFP will need to access whether the LSL needs to reduce the employee's long service leave entitlements and how much, if any, should be paid by the PLSA.

b. Profit & Loss Impact of Payments to Portable Long Service Authority

All payments made to the PLSA are expensed in the financial year in which it is accrued or paid.

c. Changes in the Employee's Employment on their Long Service Leave Entitlements

- Joe started with the NFP on 1 July 2015 and was registered with the PLSB Scheme from 1 July 2019.

  He will have a Long Service Leave Entitlement with the NFP for the years of service between 1 Jul 2015 and 30 June 2019 and after that he will fall under the PLSB Scheme.

- If Joe left the NFP to go to another NFP before his seven years of service has been achieved, the impact on his Long Service Liability Entitlements are as follows:

  1. Joe loses his entitlement to his long service leave liability for the four years before he was registered with the PLSB Scheme.

  2. Joe's new employer, who is also an NFP in the community services, may accept the transfer of his previous employer's LSL liability for the four years for Joe and pay out his previous employer.

- If Joe left the NFP to go to another NFP after his seven years of service has been achieved, then the NFP will pay out his full Long Service Leave Entitlements and claim back the relevant LSL back from the PLSA.

d. Importance of Tracking Employee's Hours of Worked

It is important to extract from the payroll system each employees' hours worked for that year to ensure the NFP can track the hours worked for employees for the purposes of the calculation of the employees' long service leave entitlements, even if they are partly or wholly covered by the PLSB Scheme.

Q. Revenue

1. Revenue Recognition

It is very important to the future sustainability of any NFP that the revenue that was received during the financial year is recorded in the right financial year or are recorded as a liability on the balance sheet, when not all the conditions for the release of that revenue have been met.

We recommend you read the grant or funding agreements to ensure you understand the conditions attached to these revenue items. Consider:

a) Source of each Funding/ Grants amount

b) What project does it relate to?

c) What is the timeframe for the project, i.e., 1 January 2020 to 31 December 2020?

d) On which basis is the deferred revenue calculated, i.e., unspent funding, number of months, etc.

e) Why is the income being deferred?

f) Keep a copy of the agreements or documentation for the Auditor of each Funding stream/Grant.

2. Reconciling stand-alone software information to accounting software information

NFPs do not always reconcile the financial information generated by a stand-alone software package (such as a Childcare Management Software such as Qkkids or Raisers Edge, Stripe, Square, Trybooking, VETTRAK, etc.) with the information that ends up in their accounting software as the NFP's financial results.

The biggest risk with not reconciling the sources of financial information used to establish the NFP's financial results is the opportunity for someone – most often a trusted employee – to commit fraud.

A major issue is the accounting for cash receipts into stand-alone software packages and the subsequent banking and recognition in the accounting software.

The financials records of the NFP may be inaccurate and incomplete if the NFP's management does not know what information in their stand-alone software package has not been taken up in the accounting software.

The NFP's management should ensure the following:

a) Establish the sources of financial information used to prepare the financials.
b) Ensure you understand what financial information is supplied by the stand-alone software packages and how will this information be used in the accounting software to prepare the financials.
c) Ensure that the cash inflows (whether cash, EFT or cheque receipts) into the stand-alone software packages are also accounted for in the accounting software, as well as any cash outflows like refunds or credit notes.

The above is achieved by reconciling the information in your standalone software package with your accounting software.

You therefore need to reconcile the monies banked and recorded in your accounting software from that income for the financial year versus the income receipted per the stand-alone software for the financial year.

R. Expenses

1. Verifying ABN and GST registration for suppliers

NFPs do not often verify the ABN and GST registration of their new contractors and suppliers.

Suppliers may provide ‘tax invoices’ to the NFP but are not actually registered for GST. This results in the NFP being overcharged for services rendered or goods provided and defrauds the Commonwealth of Australia.

The ABN provided may also be for a totally different NFP unrelated to the supplier.

A GST input credit is claimed in error because the tax invoice received from the supplier is invalid.

The NFP is also required to withhold 49% of the supplier’s invoice amount where the ABN provided to the NFP is invalid or not provided.

The ABN and GST registrations for all new suppliers, especially small suppliers, and subcontractors, should be checked when they come on board as a supplier to the NFP.

Also, where a supplier is a contact in the accounting software with a GST rate at 0%, and the invoice is material in nature - re-check the ABN as their status may have changed.

The web link for the ABN Lookup is: https://abr.business.gov.au/

ABN Lookup is the public view of the Australian Business Register (ABR). It provides access to publicly available information supplied by businesses when they register for an Australian Business Number (ABN).

Invoices supplied by catering and small cleaning service suppliers are especially at risk of being treated incorrectly for GST.

2. Check if there are 12 payments/ invoices for rent, telephone, internet, etc.

S. Payroll

1. **Obtain the Payroll Report showing the gross wages, tax deducted, superannuation deducted and other deductions (salary sacrifice benefits) for the whole financial year.**

2. **Reconcile the Payroll Report (showing the employees) with the Salaries and Wages & Superannuation Expenses for the year.**

What can go wrong?

a) **Manual journals were posted to the Salaries & Wages and Superannuation Accounts during the financial year, which are not reflected on the Payroll Reports.**

b) **Did the NFP accrue Salaries & Wages and Superannuation at the end of the prior year, which need to be brought into account?**

c) **Did the NFP accrue Salaries & Wages and Superannuation at the end of the current year, which need to be brought into account?**

d) **Some of the Payroll expense were allocated to other accounts, i.e., fringe benefits, salary sacrifice, allowances, tutors, etc.**

e) **The NFP reallocated expenses to other accounts using manual journals.**

3. **Establish whether the NFP is a FBT Exempt or FBT rebatable employer by looking up the NFP's ABN on the ABN Lookup website: https://abr.business.gov.au/**

   An FBT Exempt Employer, such as a Public Benevolent Institution or Health Promotion Charity, employees' can salary sacrifice up to $15,900 of private expenses (rent, mortgage, credit card, etc.) and $2,649 of meal entertainment for each FBT year (01.04 to 31.03).

   Ask the Auditor if you are unsure.

4. ***Did the NFP declare the correct Wages amount under Label W1?***

   Include at W1 total gross payments from which the NFPs are usually required to withhold amounts.

   W1 do not include:

   - amounts subject to salary sacrifice arrangements, i.e. FBT Exempt entities
   - employee salary sacrifice super contributions

5. Employee Documentation

Some NFPs do not maintain adequate employee documentation, which may expose the NFP to future legal action by an employee.

Developing employment documentation and maintaining employment records is not only good business practice but is also a legal requirement under the Federal Fair Work Act 2009 and the Fair Work Regulations 2009.

Documentation is needed so the employer has an accurate view of an employee's employment history. For example, a written contract of employment clarifies whether an employee is permanent or casual, their classification and wage, and when the employment commenced. This can reduce the risk of misunderstandings and disputes regarding employment conditions and status.

Appropriate documentation and records can also protect employers from costly unfair dismissal, unlawful termination, or discrimination claims.

An employer that has maintained and documented performance warnings, disciplinary interviews and the steps taken to ensure procedural fairness, have a stronger defense against unfair dismissal or unlawful termination claims compared with where no documentation has been kept.

A well-thought-out employee file should be kept for each employee, with the following minimum documentation to ensure transparency:

- A signed letter of offer of employment or employment contract
- Any formal notification of a change in working hours/ conditions of employment
- Any formal notification of a change in pay rate, promotion, or employee category
- Any formal notification of disciplinary action or warnings
- Leave application forms
- Signed acknowledgement by employee of their understanding of the NFP’s policies

T. Comments on Fraud Detection and Prevention

Fraud will take place at NFPs more often than one realise.

Fraudulent activities in the NFP sector can include appropriation of assets (financial, fixed and intellectual property), false accounting (financial statements, contracts and acquittals) falsifying of documents (qualifications, experience and identification) and corruption (bribery, kickbacks and conflict of interest).

In most instances, the staff member was given the opportunity to access the NFP's bank account as part of their role and gave into the temptation.

Often it is trusted and long serving employees that are the culprits.

There are specific fraud risks that apply to NFP's:

1. One person has too much control over the NFP's finances, other activities and crucial decisions.
2. Due to limited number of staff, it is difficult or nearly impossible to have strong internal controls such as segregation of duties.
3. The NFP board consisting of volunteers have little to no financial background or limited input in or access to the NFP's finances.
4. Income from donations and other discretionary receipts that are not formally acknowledge create a situation where it is easier to misappropriate cash.
5. Volunteers have access to confidential information and they may not have been properly cleared using police checks, etc.
6. Not all instances of fraud are reported to police and the relevant authorities due to fear of negative publicity or the alleged fraudster is not properly held responsible for their actions due to lack of resources and funds.
7. A fraudster will take steps to avoid anyone else from taking over their duties, by avoiding taking sick days and annual leave.
8. Two or more staff members can collude to defraud the NFP, and no one may be the wiser.

<u>Financial Fraud can be perpetrated in various ways:</u>

Invoices

Any arrangement in which a person causes his or her employer to issue a payment by submitting invoices for fictitious goods or services and/or inflated invoices.

Expense Reimbursements

Any arrangement in which an employee makes a claim for reimbursement of fictitious or inflated business expenses.

Payment Tampering

Any arrangement in which a person steals his or her employer's funds by intercepting, forging or altering a cheque drawn or EFT payment, on one of the NFP's bank account.

Payroll

Any arrangement in which an employee causes his or her employer to issue a payment by making false claims for compensation.

Cash

Any arrangement in which cash is stolen from an NFP before it is recorded on the NFP.

Any arrangement in which cash is stolen from an NFP's books and records.

Any arrangement in which an employee makes false entries on a cash register to conceal the fraudulent removal of cash.

Any arrangement in which the perpetrator misappropriates cash kept on hand at the victim NFP's premises.

Non-Cash Misappropriations

Any arrangement in which an employee steals or misuses non-cash assets of the NFP.

Revenue Fraud

Any arrangement in which an employee steals his or her employer's funds by misstating discounts and adjustments and making false claims.

Any arrangement to over inflate the NFP's revenue entitlements from government funding sources.

Internal Controls that can assist with the detection and prevention of fraud:

Detection

Due to their limited resources, many small NFP's cannot afford to implement robust preventive controls.

Ongoing review and external oversight through detective controls can provide the safety net such NFPs need. These controls include**:**

1. **Management Review** - The Board of Management should consider reviewing a monthly list of all payments made, along with a review of the month's bank statements, credit card statements and request invoices and supporting documentation if they have concerns.
2. **External Audits** – NFPs should consider the value of external audits of financial statements, as well as of the review of internal controls over financial reporting.
3. **Internal Audits** - Internal audits of financial statements (comparing actual to budget and investigating any variances), as well as credit card charges, expense reports, payroll records, and petty cash by someone who is not involved with recording financial transactions in the accounting software.

Prevention

1. **Dual Authorisation** - Electronic payments made by staff at NFPs should have a dual payment/approval step so that 1 individual is not solely responsible for the payment of outgoing monies.
2. **Segregation of Duties** - The staff member who initiates a transaction should not approve that transaction, and the staff member who approves the transaction should be different from the staff member who records it.

   While collusion can negate this control, the above checks-and-balances significantly reduces the chances of fraud.
3. **Credit Card Policies** - Credit card accounts are akin to cash and should only be assigned to employees who have a clear need to use them, such as senior management. Other employees, with no need to make business purchases, should not have credit cards.

   When individual cards are required, consider a strict but clear credit card policy for employees outlining spending authorisation, responsibilities and rules and restrict accounts with spending limits.

U. Glossary

Accounts Payable:

The amounts owed to a supplier or a creditor for delivered goods or completed services.

Accounts Receivable:

The amounts that are owed to a NFP by its customers/ members.

Accruals or Accrued expenses:

If during the course of the NFP's operations certain expenses are incurred, but no invoice is received by balance date, then these expenses are referred to as accruals.

These expenses (or an estimate of the expenses) should still be included in the Income Statement.

When the actual invoice is received, an adjustment can be made to correct the estimate.

Income can also be accruals where the expected income had not been received by balance date.

Accrual Accounting:

Under the accrual accounting method, revenue is recorded/ processed during the financial year the revenue is earned, whether or not it has been received.

Similarly, expenses are recorded/ processed during the financial year the expenses are incurred, whether or not the expense has been paid.

The Income Statement and Balance Sheet is therefore prepared on an accruals basis.

Audit:

The systematic examination and verification of a NFP's accounts, transaction records, other relevant documents by qualified accountants aka auditors, to ensure the financial records are in line with the NFP's policies, processes and procedures.

Audits are performed to ascertain the validity and reliability of information; also, to provide an assessment of a system's internal control. The goal of an audit is to express an opinion on the NFP or system (etc.) in question, under evaluation based on work done on a test basis.

Audit Adjustment

The correction of a financial information misstatement identified by the auditor, whether recorded or not.

Bad Debts Provision:

An account used to record an estimate of bad debts for the year (usually the amounts of the long outstanding invoices deemed bad and totally irrecoverable by Management).

Cash Accounting:

Under the cash accounting method, revenue is only recorded when received and expenses when it has been paid.

The Income Statement and Balance Sheet is therefore prepared on a cash basis.

Doubtful Debts Provision

An account used to record an estimate of doubtful debts for the year (usually the amounts of the long outstanding invoices deemed possibly irrecoverable by Management).

Income in Advance/ Deferred Revenue:

Refers to amounts/funding/grants received for services which have not yet been delivered.

Going Concern :

Assumption that a business can remain solvent, i.e. pays all amounts owed, until the next reporting period. It is one of the fundamental accounting concepts underlying the preparations of financial statements.

Accounts are prepared on a going concern basis with assets shown at their cost to the business. The alternative basis would be to prepare accounts using “break up “values.

Immaterial Balance:

A balance in the financial statements that will not change decisions made by the users when they make decisions based on the financial information.

Income Statement:

A statement listing the total incomes and total expenses incurred during a specific accounting period. (Also known as the Profit and Loss Account or Statement of Financial Performance).

Material Balance (**materiality)**

Account balances or Information important enough to change the users’ decision when they make decisions based on the financial information.

Materiality includes the absolute value and relationship of an amount to other information.

PAYGW = ‘Pay as you Go Withholding Tax’

This is the name given to the income tax system where employees pay their income tax due every pay run during the year, based on estimates calculated by the ATO.

When they submit their income tax returns for assessment by the ATO, these PAYG payments are deducted from the final tax figure.

Prepayments or prepaid expenses

An expense that covers a period that extend into the future past the balance date, paid in advance, e.g. rent, insurance, etc.

Reconcile (reconciliation)

A schedule establishing agreement between separate sources of information, such as accounting records reconciled with the financial statements.

Statement of Financial Performance

Also known as the Income Statement.

Statement of Financial Position

Also known as the Balance Sheet.

Subsidiary Ledger/ Sub Ledger

The detailed information that totals to the balance in the general ledger account.

The total of all customer accounts receivable included in the subsidiary ledger of accounts receivable is the balance in the general ledger accounts receivable account.

The total of all supplier accounts payable included in the subsidiary ledger of accounts receivable is the balance in the general ledger accounts payable account.

Vouch

The auditor’s method to proof accuracy of accounting entries by tracing amounts to supporting documents.

T. Checklist of Common Issued Found

	The NFP is:	How to Check
1.	Not checking the ABN or GST registration of new contractors/ suppliers.	ABN Lookup
2.	Claiming GST input credits on invalid tax invoices	ABN Lookup/ Supplier invoices
3.	Inconsistent GST treatment of same supplier.	Detailed GST Report from software
4.	Not ensuring that the GST Collected and GST Paid accounts are correctly cleared every quarter.	GST Reconciliation
5.	Incorrect Declaration of Salaries and Wages on BAS (especially salary sacrifice arrangements)	GST Reconciliation
6.	Incorrect calculation of Superannuation during payroll activities	Payroll Slip
7.	Not ensuring that all Superannuation calculated is paid over every quarter/ month	Agree to last month or quarter
8.	Not ensuring that all PAYGW withheld is paid over every quarter/ month	Agree to last month or quarter
9.	Security Deposits/ Rental Bonds for Commercial Properties not kept in interest bearing account by landlord or agent in Victoria	Review lease agreement and ask NFP.
10.	Security Deposits/ Rental Bonds interest bearing account is not in the name of the NFP	Review bank statement
11.	Outstanding cheques and deposits on bank reconciliations are not cleaned up at least annually	Review Bank Reconciliations
12.	Not ensuring that the aged trail balance for trade debtors is reviewed to provide	Review Trade Debtors Aged TB and ask the NFP.

	for unrecoverable debt	
13.	The NFP capitalises fixed assets that belongs to someone else, e.g. Council or church	Knowledge of NFP's business
14.	The NFP does not maintain a detailed fixed asset register or library of small electronic equipment	Ask the NFP
15.	The NFP does not properly accrue for pre yearend expenses where they prepare accounts on the accrual basis	Review payments made after yearend
16.	The NFP does not reconcile the creditor invoices to creditor statements on a regular basis	Ask NFP staff
17.	The NFP does not record creditor transactions on invoice date, but rather on payment date (accruals basis)	Review NFP detailed general ledger
18.	Where the NFP does not utilise the accounting software correctly to record transactions, the cash flow functionality cannot be used.	Review NFP detailed general ledger
19.	The NFP does not record the invoice numbers for supplier invoices, which could have fraud implications	Review NFP detailed general ledger
20.	The NFP annual leave and long service leave provisions are incorrect or out of date	Detailed Employee Entitlement Reports
21.	The NFP's long service leave provision has not been calculated correctly	Review award under which staff accrues leave
22.	The NFP uses journals in the bank accounts/trade debtors/ trade creditors	Review NFP detailed general ledger