



HOAMCO

HOMEOWNERS ASSOCIATION MANAGEMENT COMPANY

YOU GET WHAT YOU PAY FOR

Choosing between Compilation, Review or Audit

By Schutte & Hilgendorf, PLLC

WE OFTEN RECEIVE CALLS AROUND BUDGET TIME asking what the differences are between financial statement compilations, reviews or audits. Homeowner's Associations must choose one of these annually to be performed by an outside CPA firm to be in compliance with Arizona law. Although it may seem to be a no-brainer to just choose the least expensive service and move on, it is important to know what you are receiving under the different levels of service. Let's review:

COMPILATIONS:

A compilation involves merely putting the financial information received from HOAMCO in an acceptable format (i.e. financial statements, footnotes and supplementary schedules) to satisfy professional standards governed by the American Institute of CPA's (AICPA). The information is considered the representation of management (HOAMCO and the Board). NO assurance is given as to whether the statements are in conformity with generally accepted accounting principles. In fact, no assurance is given that the numbers are even right!

Compilations that include footnotes are called "full disclosure" compilations. Footnotes are detailed

explanations of accounting policies and material balances contained in the financial statements. They are meant to help the reader better understand the statements. Limited compilations do not have any footnotes. The cost of a limited compilation is generally \$350-\$450. The cost of a full disclosure compilation is generally \$750-\$850.

REVIEWS:

A review takes the compilation to the next level. Instead of just slapping the numbers into a prescribed format, the CPA considers trends in the market and industry, calculates and compares relevant ratios, and questions management about balances, fluctuations, accounting practices and financial performance. A review is performed to determine whether the financial statements are plausible in the circumstances. Upon completion, a report is issued stating that a review is less in scope than an audit, and that the CPA did not become aware of any material modifications that should be made in order for the statements to be in conformity with generally accepted accounting principles. This is known as the expression of "limited assurance". The fee for a review generally starts at \$1,500 and increases with the size of the Association.

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AUDIT:

Audited financial statements are the product of a CPA's highest level of assurance services. In an audit, the CPA performs all of the steps indicated above regarding compiled or reviewed statements, but also performs verification and substantiation procedures that may include (but definitely are not limited to):

- **VALIDATING RECEIVABLES/PAYABLES THROUGH DIRECT CORRESPONDENCE WITH CREDITORS/DEBTORS,**
- **SUBSTANTIATING SPENDING OBLIGATIONS THROUGH INSPECTION OF MINUTES, CONTRACTS AND INVOICES.**
- **VERIFYING ACCURACY OF RECORDING THROUGH EXAMINATION OF CANCELLED CHECKS AND INVOICES**
- **SUBSTANTIATING PROPER RIGHTS OF OWNERSHIP THROUGH INSPECTION OF TITLE RECORDS AND INVOICES**

An audit also involves an evaluation of an Association's internal controls—the “checks and balances” in place to prevent and detect errors and fraud. When the audit is complete, the CPA's standard audit report states that an audit was performed in accordance with generally accepted auditing standards, and expresses an opinion that the financial statements present fairly the Association's financial position and results of operations. This is the expression of “positive assurance”. The fee for an audit starts at \$5,500.

SUMMARY:

So the level of service you decide on should first be based on the amount of assurance you want to have that your financial statements are free from material error. Take note that you don't have to choose the same level of service year after year (unless of course required by your bylaws or developer agreements—be sure to check first). This may help to balance the need for that warm, fuzzy feeling in your financial statements with your desire to keep the budget down. We recommend that all Associations have a review every 3-5 years at a minimum. The value of a review over a compilation far outweighs the difference in cost. Remember that a compilation gives NO assurance that the books are accurate, whereas a review gives at least limited assurance. Some boards decide to have an audit every year just to get the highest level of “warm, fuzzy”. For Associations with complex accounting issues, developer ownership, multiple developments, or commercial operations, we generally recommend regular audits either annually or alternating with reviews every 2-4 years.

For exact pricing or to help you decide what your next engagement will be, contact your HOAMCO community association manager or us directly. All mutually agreed upon procedures and pricing are summarized thoroughly in an engagement letter before beginning any engagement.

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