THE CHURCH BENEFITS ASSOCIATION
CFO ROUNDTABLE SUMMARY

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The 2006 agenda in large part was centered around accounting and auditing guidance that affects the presentation of financial statements, how alternative investments will be audited, and how auditors will examine and rely on an entity's internal controls.

The Valuation and Audit of Alternative Investments

In July 2006, the AICPA issued the practice and "Alternative Investments—Audit Considerations" that addresses the challenges associated with auditing investments for which a readily determinable fair market value does not exist. These investments typically include private equity, real estate funds, venture capital, commodity funds, offshore funds, and hedge "fund of funds".

This practice aid anticipates that an auditor's client will perform rather extensive work around the initial due diligence process (including the determination of valuation methodologies), ongoing monitoring and, the review of financial controls for investment managers who engage in alternative investing. This process should be thoroughly documented by the client.

AU 9332 which more specifically addresses the valuation of alternative investments and essentially strengthens AU Sections 328 and 332 which state that:

- the auditor's client is responsible for making the fair value measurement and disclosures included in the financial statements;

- the auditor must understand the client's valuation methodology, making sure it is in accordance with generally accepted accounting principles and, test the entity's fair value measurements and disclosures and;

- the auditor must be satisfied that the securities listed in its client's financial statements both exist and are valued correctly.

Challenges

- Investment hedge fund managers are reluctant to expose investment positions for fear of losing a competitive edge.

- Clients very often lack resources to pursue this data.

- Covenants (loan) may be in danger if an unqualified opinion can not be rendered.

The following observations were made:

1. That auditor approaches to implementation of AU 9332 vary both inter-firm and intra-firm,
2. The further away the client's year end is away from the investment manager's year end, the more the audit firm would be concerned about risk related to the valuation of alternative investments.
3. There are concerns about potential delays with the completion of the audit.
4. It will be potentially difficult to get investment managers to sign confidentiality agreements with the client and the client's audit firm.
5. It is prudent to meet with auditors well in advance of the audit to understand their requirements.
6. Alternative investments ranged from 0% to 35% among Roundtable participants.
7. There is an increase of staff time related to the audit.
8. One participant's audit costs will be increasing 20 to 30%.
9. This audit requirement could potentially influence asset allocation to alternative investments in the future.

FASB—158 Employers' Accounting for Defined Benefit Plans and Other Post Retirement Benefits.

This statement moves retirement plan funding deficits or surpluses from the footnotes of the financial statements onto the face of the sponsoring employer's balance sheet (statement of financial position). Not-for-profits must adopt this Statement no later than fiscal years ending after June 15, 2007.

Essentially, the Financial Accounting Standards Board wants to address the difference between plan assets and plan obligations, which is typically different from the amount on the balance sheet.

Items of Note

- An organization cannot offset one plan's net benefit assets against another plan's net benefit liabilities.

- A single net asset is reported for the aggregate of all over funded plans and a single net liability is recorded for the aggregate of all unfunded or under funded plans.

- No later than 2008, the organization must use the balance sheet date as the measurement date for plan assets and obligations.

A number of organizations are following FASB 35 and FASB 60 and do not consider FASB 158 to be an issue at this time.

SAS 112—Communicating Internal Control Related Matters Identified in an Audit

In May of 2006, the AICPA issued SAS 112 which incorporates the Public Company Account Oversight Board's (PCOAB) definition of significant deficiencies and material weaknesses which now includes publicly traded companies.

Under this audit standard, it is possible that more control deficiencies will be considered severe. The auditor is now mandated to look at a combination of deficiencies in determining whether there are good internal controls over financial statement reporting. The auditors will have less latitude in determining the severity of a control deficiency under SAS 112.

A number of participants address their internal control structure on a regular basis. It is also believed that it will promote quality assurance with process management. One entity will be conducting a separate internal control audit. Another entity is being encouraged by their auditors to engage in an enterprise-wide risk management analysis.

State Tax Withholding

Some of the pension boards have implemented or are in the process of implementing a state tax withholding mechanism either internally or on an outsourced basis. One noted that they were currently addressing the issue with their third party provider of members receiving multiple check, EFTs, and 1099Rs.

Performing Due Diligence on Outsourced Processes

The process of performing due diligence on third party providers vary from Board to Board. Diligence includes the review of the TPA's SAS 70-Report on Internal Controls, reviewing scorecards with TPAs, conducting quarterly meetings and, looking at a providers financial health.

Addressing Potential Security Threats

The roundtable was presented with a proposal from Artemis Consulting Group which assesses an organization's security threats. The proposal included scope of services along with a fee schedule. This consultant will be leading a seminar on security issues with one of the pension boards during 2007.

Other Items

As a matter of due diligence, it was recommended that pension boards request a copy of the auditor's peer review report to determine how well they are auditing.

One board is considering a comprehensive tax risk assessment which includes but is not limited to unrelated business income tax, sales tax, and Social Security withholding.