

DO NONPROFITS BENEFIT FROM BEING AUDITED BY ISSUER AUDIT PARTNERS?

Zimmerman Aleksandra, Gvinjilia Megi, Zappin Brooklyn, Zawodzinski Peyton

INTRODUCTION

In the auditing profession, practitioners must serve clients across diverse economic sectors. However, little is known about how these differing sectors can impact the outcome for different clientele. This study examines if nonprofit organizations benefit from being audited by a partner who also audits a public company. Key motivations include:

- **Cross-sector auditing:** Conventionally, the auditor industry favors specialization. However, a growing number of auditors are serving for both non-profit and for profit clients
- **The information intermediary role:** We propose the idea that serving both sectors might allow partners to act as information intermediaries, which would benefit non-profits and their delivery. This specifically means that these partners help with things like tax planning, internal controls, and development decisions.
- **Extension of past research:** We built on previous research to include unrelated audit clients across economic sectors
- **Benefits and costs of client diversification:** We looked into how diversifying the clients you are serving as an audit partner can help or hurt the clients you serve.

NUMBER OF ORGANIZATION OBSERVATIONS BY AUDIT FIRM TYPE/SIZE

Partner Type	Big 4	Next 4	Smaller Firms	Total Entity-Year Obs
Issuer partners	534	245	828	1,607
(Unique Partners)	84	36	117	
Non-Issuer partners	1,460	2,036	14,573	18,069
Total	1,994	2,281	15,401	19,676

METHODS

Design: Mixed-method approach combining interviews and archival analysis.

Interviews

- 10 nonprofit executives
- 10 audit partners with issuer audit experience
- Provide insight into auditor selection and whether public-company experience is considered

Archival Data

- U.S. nonprofit audit data (2015–2019)
- 19,676 nonprofit-year observations
- 5,818 nonprofits and 1,888 audit partners
- Issuer partners identified using PCAOB Form AP disclosures

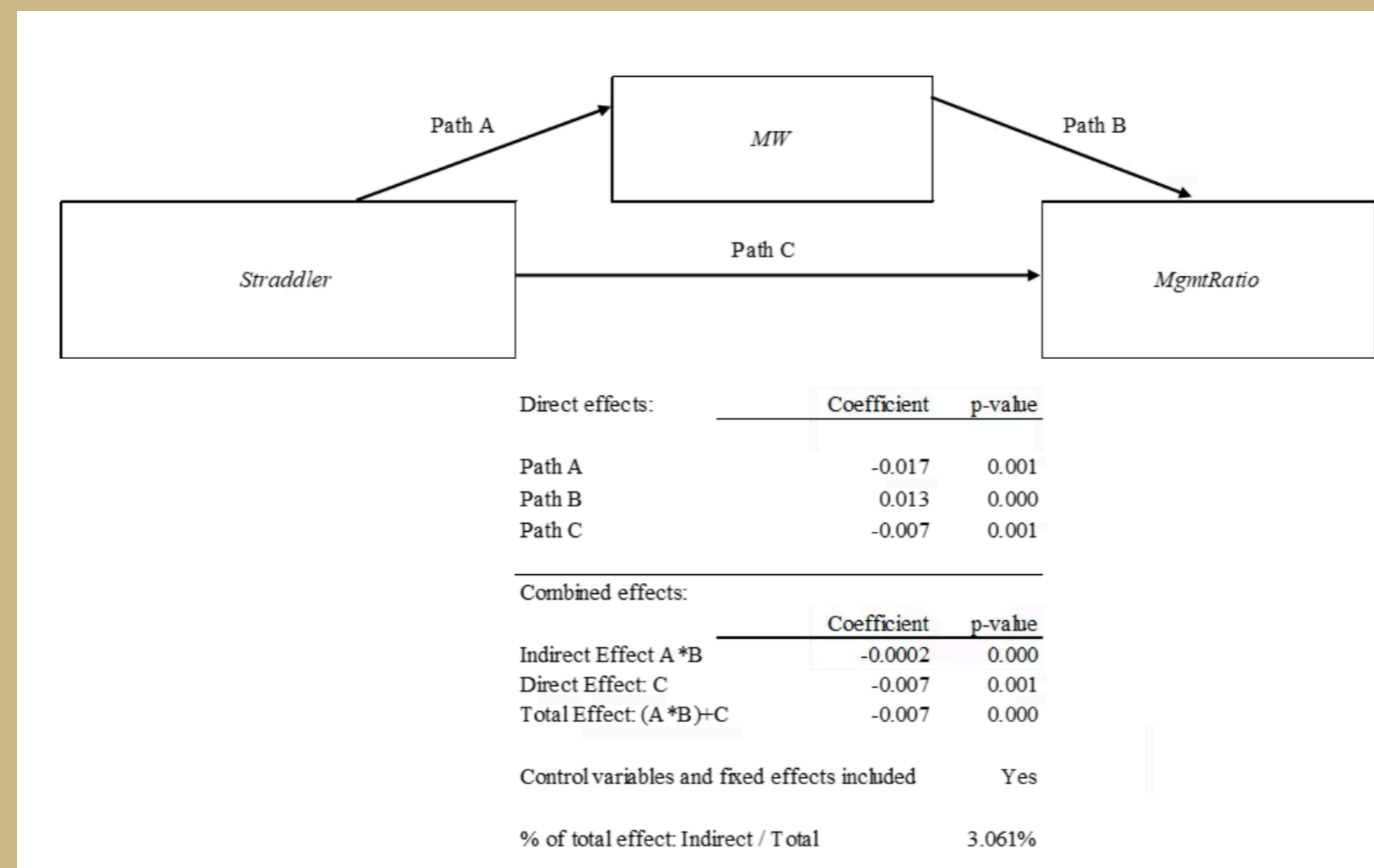
Key Measures

- Internal controls: material weaknesses
- Operating efficiency: management expense ratio and program ratio
- Trade-offs: audit report lag and accounting/audit fees

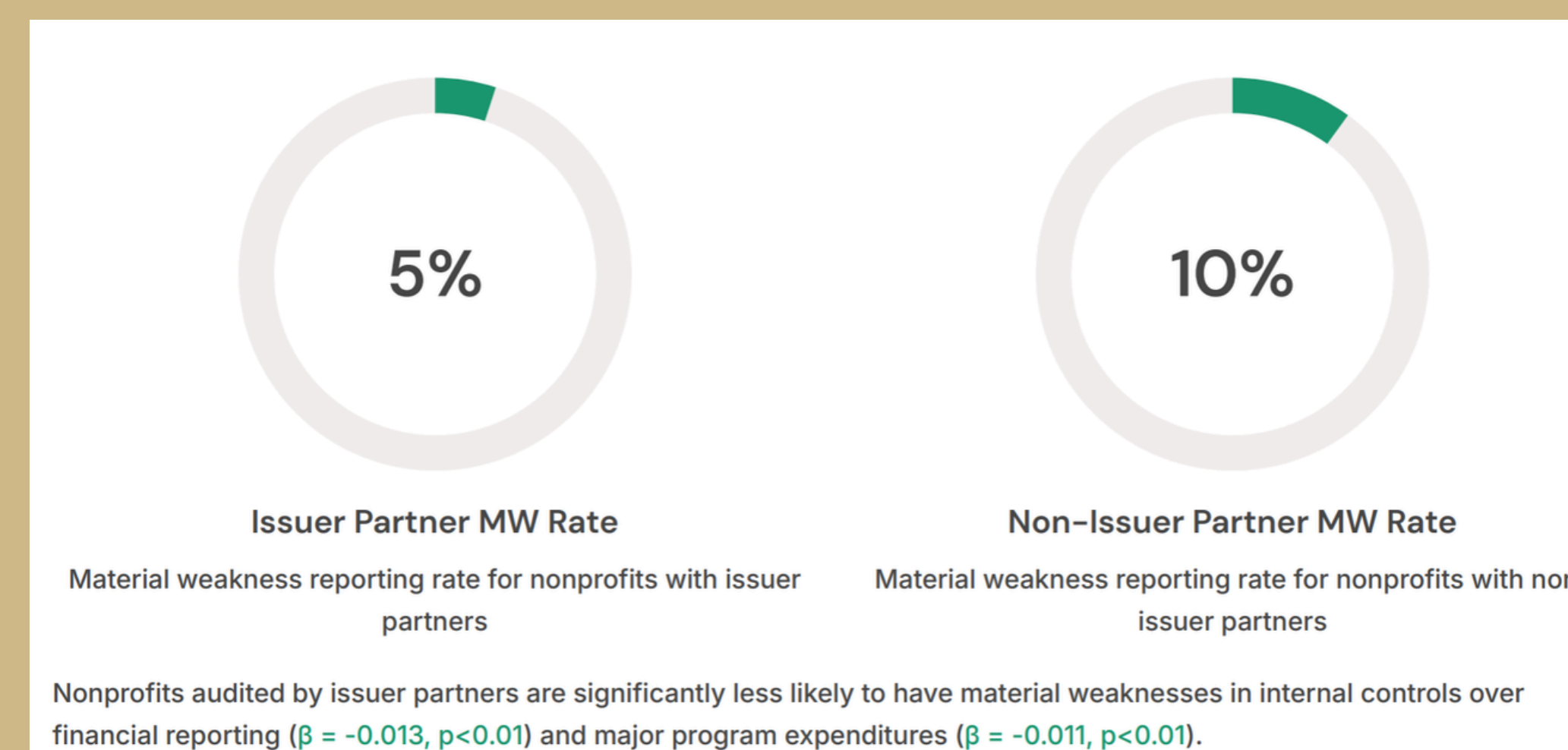
Analysis

- Statistical models with standard controls
- Robustness tests including balancing and partner-switch analyses

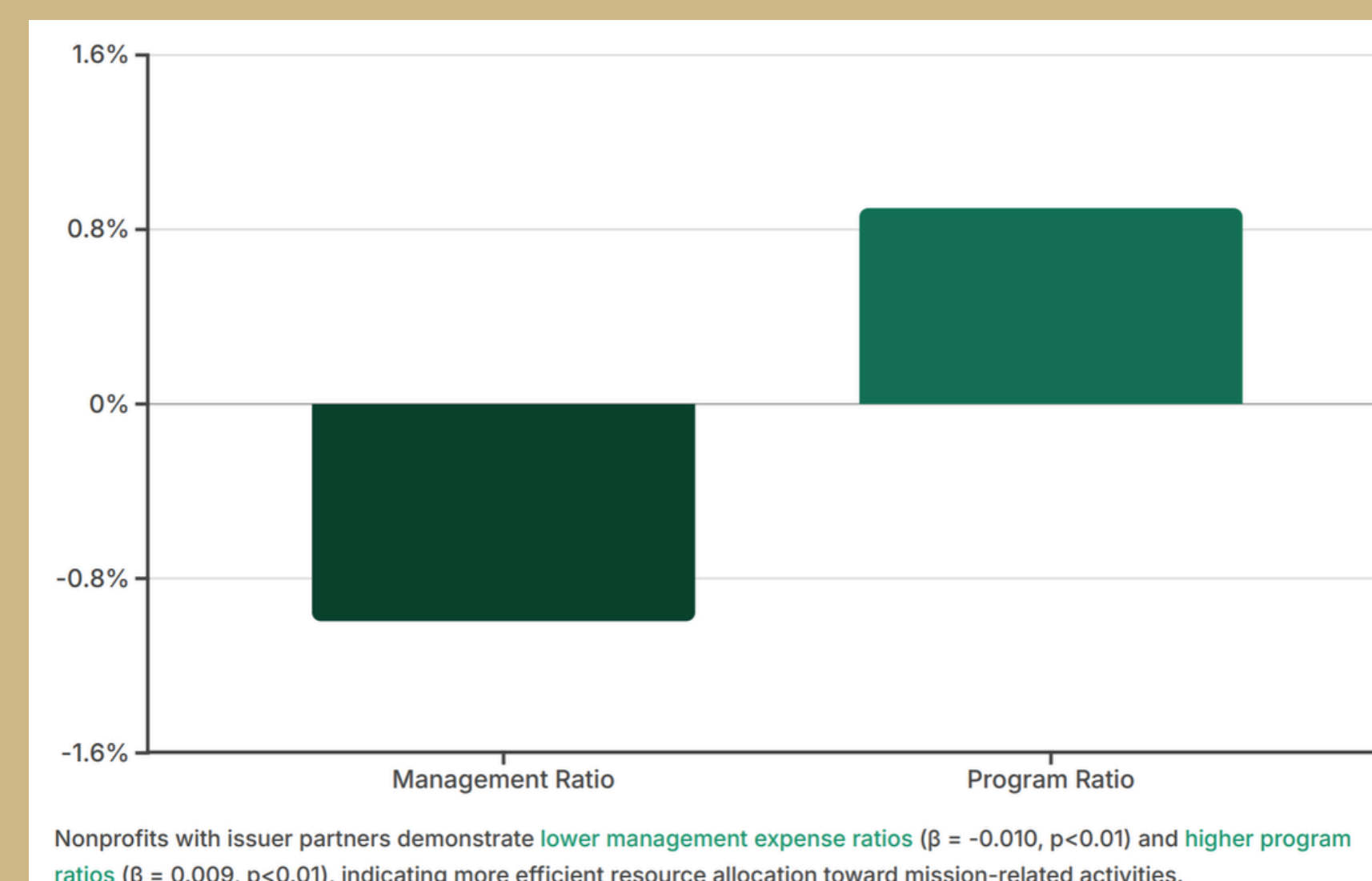
PATH ANALYSIS



MAIN RESULTS: INTERNAL CONTROLS



MAIN RESULTS: OPERATIONAL EFFICIENCY



RESULTS

Stronger Internal Controls

- Nonprofits audited by issuer audit partners show fewer material weaknesses.
- 5% material weakness rate (issuer partners) vs. 10% (non-issuer partners).
- Indicates stronger financial oversight and improved control quality.

Greater Operational Efficiency

- Lower management expense ratios (reduced administrative spending).
- Higher program expense ratios (more resources directed to mission activities).
- Overall, a larger share of funds supports core programs.

Effects of Switching to Issuer Partners

- Within the same nonprofit, switching to an issuer partner is associated with:
 - Lower management costs.
 - Higher program spending.
- Suggests improvements are not driven solely by organizational differences.

Additional Evidence

- Benefits are stronger when partners audit multiple public companies, consistent with knowledge transfer.
- Audit report lag increases by ~7 days.
- Audit fees do not increase.
- Results are robust across multiple tests.

CONCLUSION

Overall Insight: Nonprofits benefit from audit partners with public-company experience, even though boards rarely prioritize this expertise.

Benefits:

- Stronger internal controls
- More efficient resource use
- Greater spending on mission activities
- Partner Switching: Improvements persist when nonprofits switch to issuer partners, supporting a causal interpretation.

Trade-Offs: Audits take slightly longer, but audit fees do not increase.

Key Takeaway: Public-company audit experience transfers best practices that improve nonprofit governance and efficiency without higher cost.

REFERENCES

