Audit Readiness Lessons Learned
Four Tips for Achieving a Smooth Audit

It seems obvious: Prepare well and prepare ahead of time and the year-end audit does not have to be the painful experience most organizations expect. But time and again, audits do not go as planned. For numerous reasons, fees are often higher than expected, disruption becomes business as usual, companies lose key talent, and there are never enough hours in the day.

In this article you will discover key insights around the challenges of achieving a smooth audit.

Having been in the trenches with our clients as they prepare for and execute on the audit process, we have developed several tips on how to make the process as smooth as possible. Audit readiness has its benefits. With improvements in planning, communications, and data quality, a company can reduce the headaches and often lower the costs associated with a yearly audit.

Benefits of Audit Readiness
- Reduce audit preparation time and cost
- Decrease external audit fees
- Fill critical resource voids
- Enable strategic resource deployment
- Prevent staff burnout
- Meet tight reporting deadlines
- Improve auditor relationships
- Eliminate independence conflicts

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Audit Readiness Tip #1

Be proactive and fully understand what your financial information is saying before the auditors walk through the door.

If it doesn’t make sense to you, it almost certainly won’t make sense to your auditors. There is no substitute for the benefits provided by audit process experience. Team members with prior audit experience who have been through the drill before can help facilitate the process by anticipating what information auditors will request, as well as what red flags to look for in advance. Early in the process, your auditors should provide a schedule request list, often referred to as the Prepared by Client (PBC) list. If you feel that you are not receiving this list in a timely manner, speak up. Don’t try to guess what the auditors will want to see.

As the PBC documents are being assembled, anticipating what questions auditors may ask can be an important step in avoiding difficult questions on the back end. Think like an auditor. Ensure that reconciliations are tied to the general ledger. Understand and be able to explain large reconciling items. Perform a preliminary fluctuation analysis to identify unusual trends in the financial statements that may be the result of erroneous transaction posting. Ensure that high-risk areas such as revenue recognition, equity, and goodwill are consistent with generally accepted accounting principles (GAAP).

One of the biggest mistakes that a financial executive can make is providing a PBC schedule to the auditors just to check the box that it was delivered without truly understanding what the schedule says. A good auditor—and most of them are good—will pick up on unusual information in schedules very quickly.

Detailed data must be collected and repeatable processes established to ensure that an audit trail exists for all information submitted to auditors. A best practice is for companies to allocate time and resources to walk through the entire PBC cycle and create a package for the auditor that includes all journal entries and every financial document. Sometimes it is as simple as assigning a resource or bringing in outside support to delve deeper into areas that may have already been audited in the past, but where in-depth analysis was not conducted. An hour spent up front can save you two hours or more in auditors’ fees. Typically if your auditors are in the building and you are not prepared, there is a high likelihood that they will remain there for the long haul.

Anticipating what questions auditors may ask can be an important step in avoiding difficult questions on the back end.
Meeting deadlines is a critical component of audit readiness, and one of the biggest causes of missed deadlines is a lack of quality data or the inability to access that data quickly. These factors drive up auditors’ fees, create fire drills and distractions, and cause unnecessary rework. We find that the biggest causes of poor data quality and untimely access are the absence of reliable reporting systems, a lack of qualified resources, and overreliance on spreadsheets.

Spreadsheet dependence is a fact of life, but few spreadsheets are controlled well, which can lead to an increased risk of poor data quality. Staff turnover, lack of governance, inconsistent application of formulas, and other factors contribute to this risk. Inaccurate data identified in a spreadsheet creates a tremendous amount of work for auditors and management to ensure that additional errors do not occur.

Audit preparation also requires robust staff support to collect and verify data, work with management to confirm accuracy, and ensure that deadlines are met in a timely fashion. With finance organizations being decimated by cutbacks in recent years, many organizations find themselves lacking the capacity, institutional knowledge, and technical capabilities needed to ensure that a quality product is provided to auditors. As a result, data is often inaccurate or incomplete when auditors arrive.

For every question raised by the audit, you can expect a deeper dive into that specific area than would have otherwise occurred.

To mitigate the risk of insufficient access to data or poor data quality, management should evaluate known shortcomings from past audits as early as possible and develop a plan to remediate them going forward. This may involve implementing a basic business intelligence tool, becoming more aware of the process to gather the data, or creating a risk matrix to identify accounts or issues that require a heightened focus.

In a recent MorganFranklin survey, 39% of respondents considered data quality and timeliness to be the biggest challenges when preparing for a year-end audit.
Without question, enhanced communication between client and auditor is possibly the easiest means to reduce uncertainty or frustrations and eliminate inefficiencies in the audit cycle. Proactive communication from auditors is crucial.

According to the results of a 2010 MorganFranklin LinkedIn survey, the majority of respondents did not view proactive communication as a challenge when preparing for an audit. This is good news. Companies that communicate well are able to break down barriers such as lack of trust, different communication styles, and unclear expectations. Any one of these barriers can lead to an inefficient and often costly audit experience.

Without good communication, you leave yourself open to unplanned and certainly unexpected issues—such as new accounting pronouncements or unforeseen audit adjustments—that will cause headaches and ultimately drive up audit fees.

Whether you assign someone internally or look for support externally, it is important to have an auditor liaison in place to avoid these barriers. When the nature of an auditor’s question is not understood, it can lead to unnecessary headaches and the exchange of incorrect or irrelevant information. Many times, we have found that even the most senior executives and the most junior staff members can get tongue-tied when interacting with external auditors. This is rarely intentional, but it often leads to confusion as the auditors proceed with their work. With an experienced liaison acting as an extension of management, the rest of the team can spend more time handling the day-to-day tasks of running the business and less time addressing audit-related issues.

Audit Readiness Tip #3

Communicate with your auditors early, frequently, and as openly as possible.

21% of survey respondents did not consistently complete auditors’ requests in a timely manner.
**Audit Readiness Tip #4**

Spend adequate time addressing prior-year audit recommendations. They’re coming back!

If the client has not addressed recommendations from the past year’s audit, you can bet that the auditor will focus their attention right back on those issues.

For many companies, it all boils down to not having enough resources with the right skills and adequate bandwidth to remediate issues and findings from the previous year’s audit. It is also surprising how quickly these issues can fall back to the bottom of the priority list once the audit is complete.

Auditors use prior-year issues and recommendations as critical planning tools to gauge a client’s potential audit issues, overall abilities, and risk matrix for the upcoming year’s audit. If the client has not addressed recommendations from the past year’s audit, you can bet that the auditor will focus their attention right back on those issues. Often the ability to address past recommendations comes down to bandwidth or prioritization.

Failure to mitigate such risks can result in additional write-ups, internal control deficiencies, or at worst a qualified opinion. However, a small investment of time to address these issues early on can reduce the amount of time auditors will need to spend the next time around.

Companies should establish performance measures related to year-end audit recommendations to assess performance and create incentives for improvement. Hold your team accountable for implementing any relevant year-end audit recommendations. You are paying your auditor for these recommendations, so why not benefit from them? A lack of measures aligned to the objectives of reducing manual work and compliance costs can result in apathy among your staff relative to potential audit process improvements, recurring audit issues, and the perception of a weak internal control structure in the eyes of the auditor.

*MorganFranklin conducted a survey on LinkedIn during Q1 of 2010. Survey respondents were identified as SEC registrants. Survey results were as follows:

**What is the biggest challenge when preparing for a year-end audit?**
- Data quality and timeliness .............. 39%
- Balancing other priorities ............... 24%
- Lack of resources ......................... 14%
- New accounting pronouncements ....... 10%
- Proactive communication from auditors .. 9%

**How would you describe your ability to complete audit requests from your auditor in a timely manner?**
- Always on schedule ....................... 31%
- Always ahead of schedule .............. 30%
- Sometimes ahead of schedule ....... 18%
- Sometimes on schedule ............... 17%
- Never on schedule ......................... 4%

**How often do you complete all of your auditor’s year-end recommendations before the next audit?**
- Always ...................................... 57%
- Sometimes .................................. 22%
- Rarely ...................................... 13%
- Never ......................................... 8%