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Innovation is Key to Improving Audit Excellence

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WITH CONTINUING economic uncertainty and increasing fee resistance from clients, CPA firms are under pressure to manage the efficiency of their audits. Market pressures are also increasing the risk of fraud as companies seek to show strong financial performance in accord with the apparent economic recovery. These factors are causing many firms to revisit how they can increase the efficiency and effectiveness of their audits—their audit excellence.

Audit excellence, or a firm's ability to maximize the profitability of its audit engagements and value provided to its clients while minimizing its audit failure risk, is the key to managing the performance of its audit department. Audit excellence has several aspects:

- **Communications Management** – Managing internal (e.g. within the audit team members) and external (e.g. with the client, third-parties, subject matter experts, etc.) communications.
- **Data & Document Management** – Managing the work papers, information received from others, and the final deliverables associated with the engagement.
- **Engagement Management** – Managing the engagement as a whole, from proposal, to timekeeping and expenses, through to final billing.
- **Process Management** – Managing the audit process and the execution of the audit methodology.
- **Project Management** – Managing of the scope, timeline, and execution of the audit plan.
- **Quality Management** – Ensuring that the engagement is compliant with applicable standards and managing the risk of defects in its deliverables.
- **Risk Management** – Managing the risk of an audit failure or engagement failure.
- **Staff Management** – Determining which staff to assign to an audit, as well as the staff's tasks and schedule for the audit.
- **Value Management** – Ensuring the engagement delivers value to the client and to the firm.

These aspects all play a role in contributing to the success of each audit and the performance of the audit team—in other words, they drive audit excellence.

Audit Innovation

So how does a firm achieve audit excellence? It must be innovative in its approach to managing the efficiency and effectiveness of its audits.

Innovation may seem antithetical to audits, a process steeped in strict standards and theoretically tied to conservatism. However, technology provides opportunities for increasing both the efficiency and effectiveness of audits in many of the aspects above, while maintaining the high quality and reliability required to sustain the integrity of the audit service.

There are currently innovative initiatives in progress at the American Institute of Certified Public Accountants (AICPA), state CPA societies, CPA software vendors, and at the CPA firms themselves to improve audit services and the technology supporting delivery of those services. Innovation is presented in two categories¹:

- **Evolutionary Innovation** – Minor or incremental changes; usually low risk; approximately 90% of innovation falls into this category.
- **Revolutionary Innovation** – Broad, disruptive, radical changes; usually high risk; approximately 10% of innovation falls into this category.

The majority of firms are most likely more focused on evolutionary innovation, changing the way they are addressing the audit standards or trying different audit procedures—which may help them gain some minor efficiencies. **However, to truly gain a competitive advantage, firms must rethink their method to approaching the audit and embrace a more revolutionary innovation.**

¹ Adapted from “Managing Innovation: Harnessing the power of finance”, CGMA, 2013



TECHNOLOGY'S ROLE IN AUDIT INNOVATION

THE INCREASINGLY INTEGRATED ROLE OF TECHNOLOGY within society, both personally and professionally, presents opportunities to leverage innovative solutions and the data associated with it to support the aspects of audit excellence. The following questions are essential to ask when considering how technology can support innovation on the audit.

AUDIT EXCELLENCE ASPECT	QUESTIONS TO CONSIDER
Communications Management – Managing internal (e.g. within the audit team members) and external (e.g. with the client, third-parties, subject matter experts, etc.) communications.	<ul style="list-style-type: none"> • How have we leveraged private social media technologies for intra-team communication? • How do we move communications with clients out of e-mail (in individual mailboxes) into a shared collaboration platform? • How can we better communicate with third parties and subject matter experts supporting the audit?
Data & Document Management – Managing the work papers, information received from others, and the final deliverables associated with the engagement.	<ul style="list-style-type: none"> • How do we collect all the source documents and work products associated with the audit in one place that is accessible when and where I need it? • How do we easily exchange documents with third parties and subject matter experts that are supporting the audit? • How do we maintain the security of all documents? • How do we ensure compliance with records retention requirements?
Engagement Management – Managing the engagement as a whole, from proposal, to timekeeping and expenses, through to final billing.	<ul style="list-style-type: none"> • How do we monitor the engagement budget? • What is the amount of time and expense that has been spent on the engagement? • What can be billed to the client and what has been billed to the client? • Has the client paid us and what is the payment amount? • How adaptable is our audit software to the different methods of engagement management?
Process Management – Managing the audit process and the execution of the audit methodology.	<ul style="list-style-type: none"> • How adaptable is our audit software for the different ways we may run different engagements? • How do we capture the audit plan? • How does the audit software support the audit programs for the different audit areas? • How do we integrate the procedures performed in different audit areas with the audit objectives? • How agile is our audit software in supporting changes to the plan or procedures mid-stream?
Project Management – Managing the scope, timeline, and execution of the audit plan.	<ul style="list-style-type: none"> • How are we controlling the scope of the audit? • What are our milestones? • Where are we in the audit process? • What other tasks need to be accomplished for us to complete the audit? • Is the delivery of the audit report and other deliverables on schedule?
Quality Management – Ensuring the engagement is compliant with applicable standards, and managing the risk of defects in its deliverables.	<ul style="list-style-type: none"> • Have we addressed all standards and requirements? • Have we managed our audit risk appropriately? • How does the audit software support our internal review process? • Will this audit pass peer review? • How do I provide access to this audit to my peer reviewer?



AUDIT EXCELLENCE ASPECT	QUESTIONS TO CONSIDER
Risk Management – Managing the risk of an audit failure or engagement failure.	<ul style="list-style-type: none">• What are the risks of the audit?• How are we managing the risks of an audit failure?• What are the risks of the engagement?• How are we managing the risk that the engagement as a whole may fail?• Are we managing the risks at a tolerable level for the firm?
Staff Management – Determining which staff to assign to an audit, as well as the staff's tasks and schedule for the audit.	<ul style="list-style-type: none">• What staff resources are available for the audit?• Who do we need on the audit?• Who is assigned to the audit?• What are their scheduled tasks and when are they scheduled?
Value Management – Ensuring the engagement delivers value to the client and to the firm.	<ul style="list-style-type: none">• What value are we delivering to the client via the audit?• How does the audit provide value to the firm?• How does the audit provide value to the assigned staff?

WHEN EVALUATING THE SOFTWARE supporting its audits, a firm should map which software(s) is/are supporting each of the above excellence aspects and how well the questions to consider are addressed. When a gap or deficiency exists between what is being provided by the software and the needs of the firm, the firm should consider whether there are other options or better software to meet its needs. Sometimes the change in software is an evolutionary step and sometimes it is more revolutionary.

Some firms may feel that adopting revolutionary technology is too advanced or risky for them because they're too small or aren't technologically savvy. However, research we conducted on audit automation conveyed that it's really more about the firm's approach to technology rather than its size or tech-savvy that determines its ability to improve its audit excellence through technology.



AUDIT AUTOMATION STUDY¹

TO HELP FIRMS that are interested in increasing the efficiency and effectiveness of their audits, we interviewed a variety of firms, both large and small, that were both successful and unsuccessful in utilizing technology to automate their audit processes. Our goal was to identify the strategies and factors that helped or hindered the successful deployment of technology to support key audit processes. We also looked at firms that had broad adoption (e.g. used automated tools on all their engagements) and those that used tools inconsistently (e.g. only using electronic confirmations when required by the receiving party).

Firm Size Doesn't Matter

An interesting finding from the research was that neither the size of firm nor the level of technology adoption (e.g. bleeding edge vs. laggard) were factors in the successful implementation of audit automation tools. **Firms of all sizes, at varying levels of technology adoption have been able to realize the value of audit automation tools.**

Traditional vs. Progressive Firms

Our research showed that firms perceived as leaders in their area had certain characteristics and methods in which they approach the use and management of technology in their firms. The elements that help a firm move from “ordinary” to “excellent” are identified in the table below. Examples of how a more traditional firm utilizes these elements are provided in the “Traditional CPAs, Inc.” column. Elements of leading firms are described in the “Progressive CPAs LLC” column.

EXCELLENCE ELEMENT	TRADITIONAL CPAS, INC.	PROGRESSIVE CPAS LLC
IT Steering Committee	IT Steering Committee is focused on firm infrastructure (e.g. e-mail, office servers, MS Office, practice management) and upgrades to existing software.	IT Steering Committee is focused on firm infrastructure, but also looks at keeping the firm tapped into emerging technologies and how to increase staff efficiencies and client collaboration using those technologies. Larger firms may have additional sub-committees for each line of business, focused on the applications and services used specific to the line of business. Reports up to IT Steering Committee and to Line of Business leadership.
Audit Workflow Management	Low level of audit workflow standardization across the firm. Audit workflow varies depending on the partner/manager in charge of the audit. Audit workflow is not monitored or monitored on an ad-hoc basis by each partner/manager.	Audit workflow is standardized across the firm (with limited localization allowed for larger firms with regional offices). Automated tools are deployed to help manage and track workflow, including time from completion of fieldwork to delivery of audit report.
Staff Performance & Audit Cost Management	Staff performance is measured by “billable-hour” and engagements by performance against budget. Views staff as a fixed cost and doesn't analyze the opportunity cost of staff assignments.	Uses other measures (e.g. meeting of delivery targets, client satisfaction) in addition to “billable-hour” to measure staff performance. Looks at both revenue potential and cost basis aspects of staff. Seeks to push work down to lower level staff when possible to reduce cost and provide opportunity for more senior staff to generate additional revenue.
Audit Technology Usage & Training	Audit technologies made available to staff, but usage not mandated. Usage is typically dictated by the engagement partner/manager preference. Training is not standardized and is usually provided by other staff or managers as needed.	All existing staff provided with training during new tool rollout. New staff provided with training on firm's audit technologies during on-boarding. Usage mandated by policy with exceptions allowed only under select circumstances.



INNOVATION IS KEY TO AUDIT EXCELLENCE

FIRMS OF ALL SIZES should consider how they can incorporate evolutionary and revolutionary audit innovations to improve the efficiency and effectiveness of their audits. Leveraging the innovations provided by technology to support different aspects of audits will allow firms to improve their audit excellence.

ABOUT THE AUTHOR

DONNY SHIMAMOTO, CPA/CITP, CGMA, is the founder of IntrapriseTechKnowlogies LLC, a CPA firm focused on organizational development and advisory services for the middle market. An active CPA, Certified Information Technology Professional (CITP), and Chartered Global Management Accountant (CGMA), Donny helps many organizations by bridging accounting and IT to strengthen organizational governance and risk management, improve business processes through IT, and increase the effectiveness of decision making through business intelligence. Donny also serves as an outsourced IT Audit “Partner” and advisor for smaller regional/local firms and internal audit departments who lack in-house IT management and IT audit expertise, helping with IT risk assessments and enabling increased staff proficiency with IT tools supporting internal and client engagements.

Donny is the chair of the AICPA’s Information Management and Technology Assurance Executive Committee, and is a former member of its Governing Council and Assurance Services Executive Committee (ASEC). Donny was recognized from 2012 – 2014 as one of the Top Thought Leaders in “Public Accounting by CPA Practice Advisor and was named to Accounting Today’s Top 100 Most Influential People list in 2013. He received the 2009-2010 President’s Award from the Hawaii Society of CPAs, was named to CPA Technology Advisor’s 40 Under 40 list in 2007 & 2009.

Endnotes

ⁱ “This section was excerpted from “Automation is Key to Improving Efficiency and Effectiveness of Audits”, Donny Shimamoto, CPA2Biz, 2012