

Management's role in audit success:  
During the audit

# Outline

- Key themes from January session
- Understanding the audit timeline
- Roles in the audit process
- Handling disagreements
- Keeping things on track
- Independence and objectivity during fieldwork
- Financial statement review for the non-finance manager
- Challenges for small organizations

# Preparing for an Audit - Recap

# What is a financial statement audit?

A financial statement audit is:

- An *independent assessment* of the financial statements,
- Which have been *prepared by management*,
- Are fairly stated *in all material respects*,
- In accordance with *prescribed accounting framework*
- Providing *reasonable assurance*

# Understanding the Audit Timeline

# Question

The auditors have contacted us to schedule the audit and the proposed fieldwork time is during the Lunar New Year, when the office is closed. It is difficult to get the auditors out here anyway, so I've told them that is fine, we will give them all our accounting records and they can get on with it, without being interrupted. Do we have to be in the office in case they have any questions?

compliance with governmental code policies.

**S 29 15 Participation on the Annual Audit**—The audit process is a collaborative effort on the part of the auditor and management of the organization. Management shall make the appropriate arrangements to be available during the course of the engagement and be responsive to requests made by the auditor. If at the close of scheduled audit procedures, management has not provided all the information requested by the auditor, the auditor shall inform management of the audit status and request a written engagement extension letter. At the close of the engagement, an exit interview will be conducted. The auditor shall supply a draft of the audit report for management to review before it is finalized. Since the financial statements are the responsibility of the organization, it is important for them to be reviewed and understood.

# Planning

- Understanding the entity and its environment
- Assessing risks, including fraud risks
- Establishing audit strategy
- Developing the audit plan and program

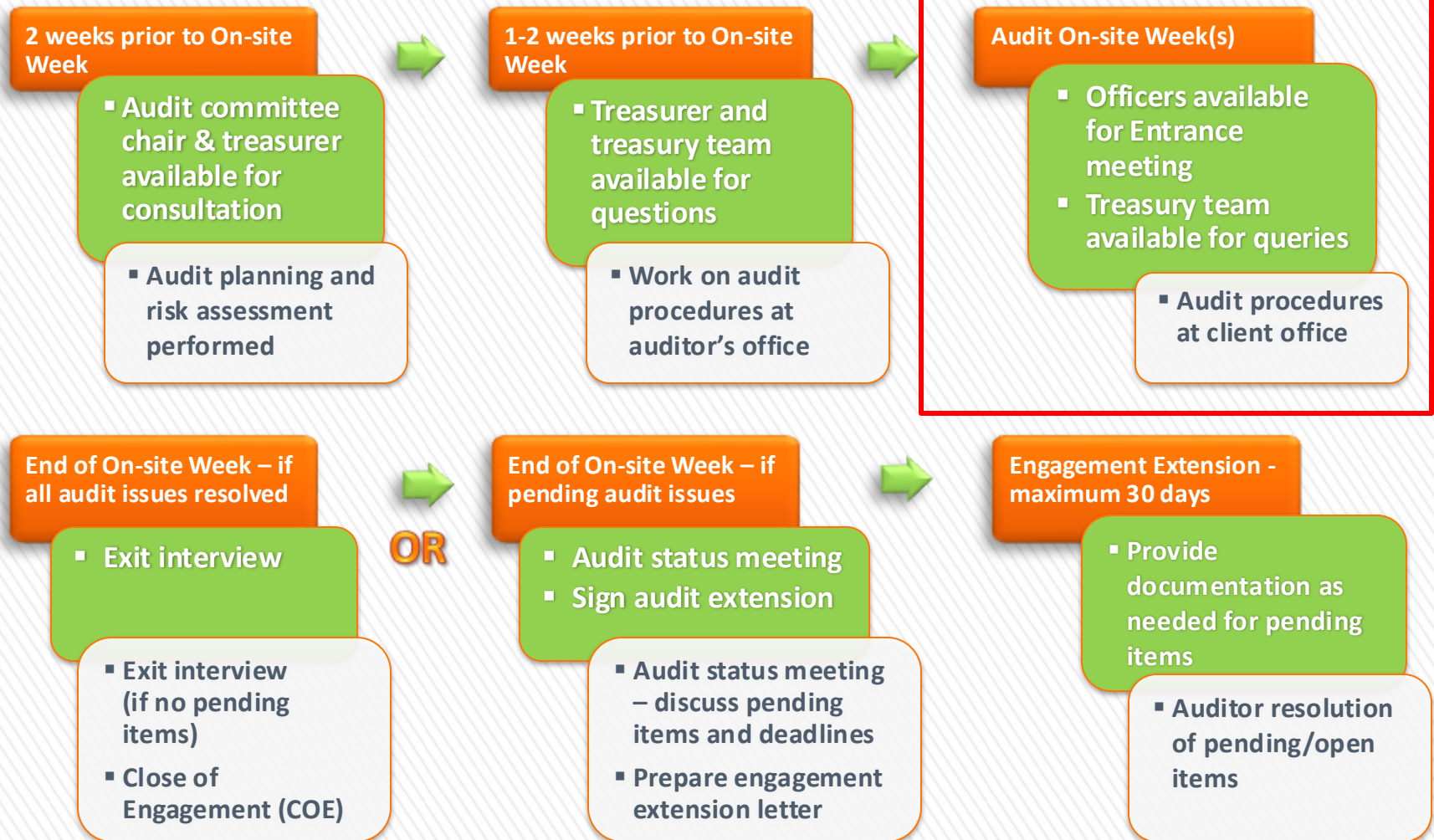
As part of the auditor's planning process, they will need to interview, *at a minimum*:

- Audit Committee Chair
- Officers
- Finance/Accounting personnel
- Legal counsel

Delays in responding to auditor questions at this stage can derail the entire audit timeline!







# Audit “field work”

# Remote Auditing

- Much of audit can be done remotely if:
  - You have reliable internet
  - All requested documents are uploaded to audit portal
  - All supporting documentation is in electronic form or can be scanned

Reduces cost

Beware:

- 'Out of sight, out of mind' delayed responses

Questions so far?

# Roles in the Audit Process

# Whose job is it anyway?

**Governance** – oversight and accountability

**Leadership** – ask the right questions

**Financial Management** – Coordinate, review, remediate

**Non-finance departments** – provide requested documents

**Accounting** – Prepare, reconcile, review

## Question

I am a newly-appointed member of the Audit Committee for our Adventist hospital and I heard that the auditors are here. I emailed the CFO to ask how things were going and what I could do to help. He indicated that everything was fine and I did not need to do anything until the Audit Committee meets to approve the reports.

However, when we finally met, the auditor was not present and the CFO presented the audit report very quickly, noting a qualified audit opinion, but not going through the auditor's findings which he said would be too technical to for the audit committee. An action was taken to accept the audit report and the meeting was concluded. In speaking with some other committee members afterwards, they indicated that this was always the extent of the Audit Committee's involvement. I feel like we were just rubber stamping the audit to comply with policy, but I don't see what the point is of my involvement. Is this acceptable protocol?

compliance with denominational core policies.

**S 29 15 Participation on the Annual Audit**—The audit process is a collaborative effort on the part of the auditor and management of the organization. Management shall make the appropriate arrangements to be available during the course of the engagement and be responsive to requests made by the auditor. If at the close of scheduled audit procedures, management has not provided all the information requested by the auditor, the auditor shall inform management of the audit status and request a written engagement extension letter. At the close of the engagement, an exit interview will be conducted. The auditor shall supply a draft of the audit report for management to review before it is finalized. Since the financial statements are the responsibility of the organization, it is important for them to be reviewed and understood.



# Purpose of An Audit Committee – GCWP S 34 05

- Selection of auditor (if not GCAS)
- Agree fees and scope
- Directly communicate with auditor
- Receive and discuss with auditor the audit reports **and management response**
- **Develop and review with management adequate internal controls**
- Develop and review 'whistleblower' program
- Discuss with management compliance with core policies
- **Identify, evaluate and respond to business and fraud risks**
- Understand emerging trends in accounting and how they impact Organization

# Purpose of An Audit Committee – GCWP S 34 05

- Review any serious difficulties encountered during audit
- Provide oversight for the conflict of interest
- Hold an **executive session where members of the management have been excused.**
- Present a report to the controlling board regarding the results of the audit engagement, operational effectiveness of internal control, compliance with core policies, and potential business risks. **This report should be accompanied by recommendations for the controlling board or executive committee to consider.**

# Handling Disagreements

# Question

The auditors gave my CFO a list of audit adjustments to record. One of the entries they are requiring us to record is to increase our net patient revenue and patient receivables because they think that the amount we are allowing for uncollectible patient accounts is too large. The hospital administration has discussed this with the Audit Committee chair and we think that the auditors' estimate is incorrect because they extrapolated their test of 25 patient receivables, which happened to only include accounts that were fully collected, what should we do?

# Implications of Audit Disagreements

- The 'Audited Financial Statements' are not the 'Auditor's Financial Statements'
- Management owns financial statements and can choose whether to post adjustments
- Depending on materiality, this may impact the audit opinion
- Audit Committee should be aware and agree with any decisions not to accept adjustments

# Keeping the Audit on Track

# Question

Our audit took place six months ago. However, we still have not seen the audit reports. The CFO says they don't know why the auditors are taking so long to issue the reports. What is going on and why does this keep happening to us?

# When Should Preparation Take Place?

- All year long!
  - Each monthly close is audit preparation
    - Are internal controls operating throughout the year?
  - Will result in cleaner and faster year-end close
  - Audit doesn't start when auditors arrive on site
    - Make sure preparation is complete per terms of Engagement Letter

**Governance/Leadership** – receiving regular and timely financial reports throughout the year are a good indicator of audit success. If not prepared, asking for these can help introduce the discipline and controls that will lead to positive audit outcomes.



# Communication is Key!

## **Internal:**

- With Treasury, Accounting/Finance, officers, other departments, make sure everyone knows what is expected and when
- Delegate - ask for help preparing by person most knowledgeable of each area
- Meet as a team to review audit preparation progress before and during fieldwork
- Communicate and monitor deadlines and responsibilities for each deliverable

# Communication is Key!

## External:

### Audit committee

- Should be aware of audit plan and updated on status, not just receive reports

### Auditors

- Read engagement letter - be aware of deadlines!
- Communicate frequently, at least weekly during fieldwork - make sure outstanding items are discussed
- Designate key point person for communication with auditors
- If you can't deliver, don't ignore, let the auditor know so they can plan

# Independence and Objectivity During Fieldwork

# Question

Our culture is famous for its hospitality, and it is normal practice to give guests a gift at the end of a visit. We always give each of the auditors a local souvenir and an envelope with cash. We also like to use the audit to appreciate our hard-working team, so we take turns in taking the auditors to dinner every day during the fieldwork. Is this acceptable?

# Auditor Independence

**298** / *Denominational Employees*

*GC Working Policy 2023-2024*

received financial benefits either directly or indirectly from any enterprise (excluding less than five percent [5%] ownership in any entity with publicly traded securities) which is or has been doing business with or is a competitor of the \_\_\_\_\_.

c. Neither I nor my family receive/received any payments or gifts, monetary or non-monetary (other than of nominal value) from other denominational entities, suppliers, or agencies doing business with the \_\_\_\_\_.

d. Neither I nor my family serve/have served as an officer, director, trustee, or agent of any organization affiliated with or subsidiary to the \_\_\_\_\_ in any decision-making process involving financial or legal interests adverse to the \_\_\_\_\_.

# Auditor's Independence

Auditor is required to be independent and objective:

- The auditor cannot participate in the **decision-making** processes of the client
- The auditor cannot have **financial or close personal relationships** with the client
- **The auditor cannot allow undue influence**
- The auditor cannot (*be part of the accounting system*):
  - **reconcile accounting information** or
  - **compile data for analysis**
  - be **responsible** for preparation of the financial statements or footnote disclosures (can assist\*)

Questions so far?

# Financial Statement review for the non-finance manager



# Question

I am the CEO of hospital, but I don't have any finance training. I don't really understand the audited financial statements and each year the auditors ask me to sign a representation letter stating that I believe the financial statements are fairly stated. How can I sign that in good conscience?

# Accounting

Accounting – to give an account

To whom?

The auditors?

The government?

The CFO?

Management?

Governance?

**S 29 15 Participation on the Annual Audit**—The audit process is a collaborative effort on the part of the auditor and management of the organization. Management shall make the appropriate arrangements to be available during the course of the engagement and be responsive to requests made by the auditor. If at the close of scheduled audit procedures, management has not provided all the information requested by the auditor, the auditor shall inform management of the audit status and request a written engagement extension letter. At the close of the engagement, an exit interview will be conducted. The auditor shall supply a draft of the audit report for management to review before it is finalized. Since the financial statements are the responsibility of the organization, it is important for them to be reviewed and understood.

# Review – Management Oversight

Multiple levels of Management should review on a monthly basis:

- Financial statements
  - Compare to expectations
  - Compare to prior year
  - Ask questions and understand what they mean
- Cost center detail
- Budget to actual variances

These steps will help to identify material misstatements in a timely manner

# Trend/YoY Analysis

- Comparing last year to this year and looking at large changes, particularly in the income statement are a good starting point to ask questions.

However:

- YoY analysis does not account for changes in volume/pricing. It will not identify misstatements that resulted in small variances from PY but should have (eg. what if FTEs dropped, but payroll expense did not?)
- Two points do not make a trend! Two years of data is insufficient to see the direction things are going in.

# Ratios

- Ratios assist in adjusting for fluctuations in volume:
  - Eg. Cost per discharge
  - Revenue per student
  - Gross profit margin
  - Net patient revenue
- Ratios make data comparable to external benchmarks
- Ratios can be used to analyze reasonableness between dependent and independent variables
  - Eg. Tuition revenue/student receivables

# Ask Why?

- Asking why is not a sign of ignorance!
- You don't have to have the answers, but you do need to ask the questions
- Foster a culture of 'no dumb questions'
- Allow time for questions in committee meetings
- Subcommittees (e.g. Audit Committees) are valuable because smaller groups allow more opportunity for questions and dialogue

Questions so far?



# Challenges for Small Organizations

# Question

We are a small clinic with just an accountant and treasurer. We barely have time to record all the transactions and keep up with our day-to-day duties and we don't have time to have the other person review every transaction and we only perform bank reconciliations just before the audit.

Each audit we get written up for lack of 'segregation of duties' and lack of review, but we explain that we just don't have the resources to hire more people. What do we do? Also, this year, the auditors found out that we do 12 months of bank reconciliations right before the audit takes place and they say that is an internal control deficiency. But we gave them what they wanted for the audit, so isn't this unfair to penalize us for something that we did?

# Small Organizations

## Challenges:

- Inadequate separation of duties
- Lack of independent review
- No financial or audit expertise on  
    Audit Committee
- Delayed accounting and reporting
- Cannot pay for audit

# Small Organizations

## Challenges:

- Inadequate separation of duties
- Lack of independent review
- No financial or audit expertise on Audit Committee
- Delayed accounting and reporting
- Cannot pay for audit

## Solutions:

- Split jobs, change workflow
- Retirees/committee members
- Lay members or non-board
- Automate, simplify
- Dialogue with higher org.

# Upcoming Sessions

March - Management's role in audit follow-up: After the Audit

April – Experiences from the front lines: From disclaimers to clean audits

Questions?