



INTERACT: IT'S GOOD TO TALK

Identifying who is charged with governance, ensuring appropriate communication takes place and demonstrating this on the audit file are vital to the success of smaller entity audits, as **Adrian Gibbons** outlines

Communicating effectively throughout the audit can improve its technical quality and cost effectiveness for entities of all shapes and sizes. It is important to understand that communication is not something you have to do because various International Standards on Auditing (ISAs) require it; it is something you should want to do in order to improve the audit approach.

The level and purpose of communication during an audit is dealt with directly by ISA 260 *Communication with those charged with governance* (other ISAs also highlight specific communication requirements).

Paragraph A31 in ISA 260 says: “In the case of audits of smaller entities, the auditor may communicate in a less structured manner with those charged

with governance than in the case of listed or larger entities.” Unfortunately, some practitioners interpret “less structured” to mean not recorded on the audit file. Whichever format the communication takes, if it is relevant to the audit then it must be recorded on the audit file.

Many audit files that I review give good evidence of communication with management at the completion stage. This is a mix of formal documentation (such as management letters) and informal notes (of meetings, emails and phone conversations). But ISA 260 requires the audit team to establish effective two-way communication throughout the audit process. This means that the audit file should demonstrate a consistent level of communication throughout, not just at the stage when you send the bill.

WHO ARE WE COMMUNICATING WITH?

The short answer is: those charged with governance of the entity being audited. However, the auditor must identify who this is and ensure that an appropriate level of communication/interaction takes place.

Many audit files demonstrate communication with the finance chief (CFO or FD), the bookkeeper or other staff within the organisation. This is not necessarily the same as those charged with governance. The CFO may be a board director: but the board as a whole is charged with governance of the entity. If you speak to only one director, can you be sure that your issues and questions are passed to the full board?

Charity audit files often evidence communication with the charity’s accountant rather than the trustees. It is fair to say that many trustees do not want to speak to the auditors (in fact many directors do not want to speak to the auditors). However, if they are ‘charged with governance’ then they should engage with the audit process. Our job as auditors is to help them see the benefit of two-way communication.

WHAT ARE WE COMMUNICATING?

Paragraphs 14 to 17 of ISA 260 include the following main headings:

- The auditor’s responsibility in relation to the financial statement audit;
- Planned scope and timing of the audit;
- Significant findings from the audit; and
- Auditor independence.

The application material that supports these paragraphs suggests the following information would be part of communication with the client:

- Background information - to help the audit team understand the entity and the risk issues.
- Sources of audit evidence - useful when designing appropriate audit tests.
- Information on specific transactions and events - this helps with the assessment of risk and audit approach.
- How those charged with corporate governance have fulfilled their responsibility for the financial statements.

While the above gives a technical overview of the communication, your interaction

with the client should be much more. The aim is to engage the client in the process and help them to recognise the benefits resulting from the exercise.

An example might be discussing the risk profile that is created as part of the audit planning exercise. Smaller entities do not generally have detailed risk profiles; so it may be beneficial to the entity's management team to understand what a risk profile is and the ways in which they can use the risk information.

WHEN SHOULD WE COMMUNICATE?

Communication is ongoing. It should start with pre-audit communication covering independence issues and the scope of the audit. At the planning stage, it should focus on risk. At completion, it should focus on the issues identified and the audit opinion.

Agreeing a clear agenda with the client will help them to appreciate that the communication is beneficial. As smaller entities may be reluctant to communicate for fear it increases the audit fee, the timing of the communication should suit the client.

WHERE SHOULD WE COMMUNICATE?

The best communication is face-to-face and at the client's premises.

Communication is always better when you can see the other party and understand their body language. A meeting on client premises not only makes the client feel more relaxed but also means they are more likely to have access to the information they will need for the discussion.

However, audits of smaller entities often have insufficient budget to justify a face-to-face meeting at their premises, so alternative methods are required.

At the pre-audit planning stage, for example, telephone the client to update the background information and cover key issues that may affect risk and the audit approach.

At the audit planning stage email can be used. It introduces an element of formality and is useful in communicating issues such as: the scope of the audit; and its timing, extent and limitations. Always remember to file a copy of the email on the audit file.

The completion/wrap up meeting

usually takes place at the client's or the firm's office. For the majority of audits, during this face-to-face meeting you will communicate the results of the audit and its key benefits to the client.

BEST OF YOUR ABILITY

Many years ago, I carried out visits to schools and colleges to talk about careers in accountancy. Students would approach me and say: "I am good at maths and I want to be an accountant". I would then explain that there is not much maths in accountancy; rather, a key skill is the individual's ability to communicate with the client.

This article has been about your ability to communicate with the client. The auditing standards require a lot of ground to be covered through communication. You and your team's ability to do this has significant benefits for the quality and cost effectiveness of the audit approach.

Communicating in a less formal way with smaller audit clients has its risks and cost implications. However, the rewards, in terms of the technical information on the file and the relationship you build with the client, make the exercise more than worthwhile. ■

WEBINAR INTERACTION

Interactions with management on smaller entity audits will also be the subject of a faculty webinar, to be given by Adrian Gibbons on 23 September (see page 5), which will reprise the well-received external audit lecture he gave on this subject at Chartered Accountants' Hall in June.



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