



AUDIT &  
ASSURANCE  
FACULTY

# Improving audit quality using root cause analysis

What, why, how, who and when?

**A PAPER FOR EXTERNAL AUDITORS**



# What is RCA and what is it for?

Root cause analysis (RCA) is a technique for identifying the underlying key cause (or causes) behind review findings, whether specific to one audit or firm wide, so that an appropriate and achievable action (or actions) can be taken to prevent recurrence of negative outcomes and to promote recurrence of positive ones.

Most attention on RCA to date has been in connection with negative review findings and so this paper's main focus is on RCA being used for those. But RCA can also be useful as a means to identify and nurture positive outcomes and aspects identified in individual audit engagements, or across types of audit engagement.

In an audit quality control context, RCA can be a valuable technique to prevent recurrence of the same issues (whether weaknesses or failings) year after year in monitoring or compliance reviews.

It can also be useful to make use of RCA outside of purely monitoring or compliance reviews. Circumstances where it might be beneficial include: if a firm has a professional indemnity issue; as part of a continuous improvement programme; or as part of evidence gathering for training-need identification.

RCA is about identifying the cause of an issue, rather than just looking at the symptom of review findings. Dealing with the symptom (ie, the problem as it manifests itself) is a 'sticking plaster' approach. It may address the immediate issue, but identifying and addressing the underlying or root cause is likely to be a far more effective way to reduce future recurrence of similar findings.

RCA does not have to be complicated, yet it can be very powerful if done well. In simple terms, it is a matter of asking 'why?', possibly several times. A well-structured and systematic approach will help to formalise the firm's thinking and is more likely to bring about a successful result than an unstructured reaction.

In the audit arena, addressing compliance failings through additional training might be a common knee-jerk reaction to a range of review findings. But without first exploring the root cause, there is a danger that the time and effort spent on developing additional training will be wasted, and the real underlying problem left unresolved.

Training on technical matters may be the right answer, but there could be a range of other behavioural or organisational factors worth considering. For example, were the right staff allocated to the job? Was there a difficult or complex issue that should have been foreseen? Was the team under time pressure, or pressure from client management? Or did someone simply have a bad day? These questions could all lead down differing avenues to different root causes and, as a result, different actions to address them.

RCA can be used by firms of all sizes. The hope is that it will help firms towards more effective ways of identifying solutions and improving quality than just a review and a standard one-size-fits-all response. There is a need for a nuanced approach and tailoring to the firm's circumstances. Also firms need to think about what they are uncovering and take an analytical approach. Thoughtful consideration of relevant facts in the context of the specific circumstances is a key component of effective RCA.

Here we have covered **what** RCA is, the sections that follow cover: **why** we are issuing a paper on RCA; **how** you can do it; **who** should do it; and **when** RCA should be performed. We have also included an illustrative list of issues that might be root causes as **Appendix 1**, and a graphic as **Appendix 2** to provide an example of RCA in practice. The paper is brief as we want firms to do their own thinking and not just try to fit their RCA into a few standard templates.

# Why this paper on RCA?

The Audit and Assurance Faculty has become aware that many audit firms would welcome practical help on how to carry out effective RCA.

RCA as a technique is well established in many industries and there are many quality assurance websites offering tips on how to conduct RCA (for example [mindtools.com](http://mindtools.com), [isixsigma.com](http://isixsigma.com) and [asq.org](http://asq.org)). There is plenty of advice available for internal auditors where RCA is used quite commonly. But there is currently an absence of material aimed at RCA in connection with external audits. We hope that this paper helps to fill that gap.

RCA as applied to audit is a very topical issue across the globe and in recent times has been **commented on extensively by regulators and standard-setters**. Our motivation in providing this paper is to help auditors and their firms to use RCA to improve the quality of their audits and to provide them with net benefits rather than burdening them with additional requirements and costs.

It is not mandatory to follow the suggestions in this paper and it has simply been issued for any firms seeking such help. However, all audit firms should already review their performance and the faculty believes that, if they do it well, RCA is a way to help them do this more effectively and efficiently.

## Who is the paper aimed at?

The paper is aimed at all auditors and particularly those individuals within firms (of all sizes) and networks responsible for improving audits within the firm/network (NB: future references are just to firms, but the matters apply just as much to networks too). We hope that audit firms in all countries will find it helpful. RCA is performed in the context of the firm and its specific circumstances. We believe that thoughtful RCA is a scaleable activity that, if performed well, can be of benefit to all sizes of firm and even the very smallest firms can benefit from RCA, without needing to devise or perform excessive formal processes and documentation.

## What is in the paper?

The paper draws on the experience of firms already doing RCA and provides pointers based on that experience about the key matters they have encountered and what they have found works in practice. We are not providing case studies or templates as we hope auditors will think about the best way to do the analysis given their specific circumstances.

## How we hope you will use the paper

We hope that the paper will help firms to perform RCA effectively and that, as stated above, this will help them to improve the quality of their audits. Remember that it is increasingly likely that those firms perceived as valuing high quality in their audit work will be the most commercially successful.

In this paper we are making suggestions and not seeking to impose specific ways of performing RCA. Flexibility and judgement are key, taking account of the firm's specific circumstances. It is likely that as firms become more adept at RCA their procedures and ideas will become more sophisticated, more precisely targeted and increasingly more effective.

## The bigger audit quality picture

The suggestions in this paper should be considered within a much bigger audit quality picture. Effective RCA will not produce perfect audit quality and the paper does not, for example, cover design of appropriate actions to address review findings. There is much material available on what is needed overall and the many different factors involved in enhancing audit quality, for example see the IAASB's '[A Framework for Audit Quality: Key Elements that Create an Environment for Audit Quality](#)'.

The need for RCA has been referred to extensively by the International Forum of Independent Audit Regulators (IFIAR) in recent reports. For example, IFIAR's ['Report on 2015 Survey of Inspection Findings'](#) states: 'Audit firms should continue to pursue initiatives to improve audit quality and the consistency of audit execution across their firms. This often begins with a thorough evaluation and understanding of the root causes undermining consistent audit quality.'

The IAASB has recently consulted on audit quality as part of its [major project](#) on the topic. One matter the IAASB is considering is whether RCA should be covered in some way in its standards. The IAASB summarises the position of regulators: 'Audit regulators expect firms to investigate and understand the root causes of inspection findings, and to use them as the basis for determining remediation activities and assessing the effectiveness of those actions.'

The FRC in the UK has now issued [a thematic review on RCA](#) carried out by the six largest UK audit firms.

We will draw on the key matters and pointers from this paper in making our representations to the IAASB and any other bodies considering issuing requirements and formal guidance in this area. It is important that any policy and standards adopted on RCA take into account the practical experience of auditors already doing it and the lessons they have learned.

It is likely that the regulatory spotlight, and the call for effective RCA, will soon fall on a greater range of firms given the new challenges they will face in the future. Factors here include changes in the audit regulation regime (and the number of firms caught in the 'public interest' net) and changing financial reporting requirements, with more entities subject to increasingly challenging accounting requirements. For example greater use of 'fair values' will require firms to demonstrate their scepticism, including challenging the fair values adopted as appropriate.

This paper is part of a wide range of activities the faculty is engaged in on audit quality. Related guidance includes our ['Quality Control in the Audit Environment'](#) publication and a number of [webinars on audit quality topics](#).

# How might RCA be performed?

Before beginning RCA, firms might ask themselves some preliminary questions to frame the basis for their actions, for example:

## Should the exercise be performed for every review and every finding?

If not, which reviews/findings should be selected? There are a number of ways in which the review findings can be filtered. For example you might select:

- high-risk jobs only (size and public interest will be factors here);
- particular types of review only (eg, internal monitoring programme 'cold' reviews, EQCRs, regulatory reviews);
- reviews with disappointing results (however, it may be worth analysing why an engagement that received a good review result was successful – there may be valuable lessons to be learned); or
- those reviews highlighting themes that seem common to a number of engagements.

It is clearly more work to analyse all findings, but if firms wish to find evidence about why people behave as they do, it may be more telling to look at a wider body of evidence than just a few serious findings. It is for the firm to decide which, if any, filter will be the most relevant to its own circumstances.

## How will the results of the RCA be considered?

- Individually?
- Together?
- In combinations?

It is important to remember that review findings may have multiple contributing causes, even at their root – and some prime issues may be the root cause of more than one review finding. For example issues in the exercise of leadership can have wide-ranging impacts.

## How much of a framework should the firm provide?

The strongest RCA exercise may be one with no predetermined categories, however, embarking on an exercise with a blank sheet of paper may be a daunting task. It may be helpful to provide some framework, for example suggestions of potential usual suspect root causes, even if the people conducting the exercise are free to go off-piste should they need to.

## What approach should be used to perform the RCA?

There are a number of ways in which RCA might be performed, and different processes might be applied to different types of issue. It is likely that effective RCA exercises will involve tailoring and specificity rather than general procedures, therefore this is not an exhaustive list, but possible procedures might include combinations of the following procedures:

**Discussions with the individual who identified the issue.** This, of course, would cover the internal support team for external regulatory reviews. These discussions would aim to understand the specifics of the matter raised, for example, or to get their views on whether it related to a guidance, execution or another cause.

**Asking engagement teams to complete a questionnaire.** This could include obtaining their perspective on possible root causes, as well as gathering data about the engagement which can be used for subsequent analysis. This could include, for example, how many years have members of the engagement team been involved on the audit.

**Discussions with individuals involved in the engagement.** For larger engagements of bigger firms this may include individual members of the engagement team, ranging from the engagement partner and manager to more junior members of staff responsible for issues highlighted in the review findings, and the engagement quality control reviewer. Discussions may cover those matters which have given rise to either specific or thematic actions, or a combination of both.

**Review of working papers in the engagement file.** For example, to understand whether engagement teams appropriately executed required procedures, or whether documented procedures are unclear.

**Review of supporting documents.** Review of guidance, work plans or templates used by engagement teams at the time of their work.

**Discussions with those responsible for methodology and training.** To identify whether there have been any subsequent changes to guidance issued, or whether any gaps in guidance or training have been identified that could have contributed to the issue.

**Analysis of data collected.** To consider whether there are correlations with the findings.

**Discussion with other contributors.** Discussions with any specialists or experts who contributed to the review findings to understand their perspective. These can include those involved in tax or pensions matters where the issues relate to these areas.

Where discussions and reviews take place, it is important to ask (others and yourself) 'why' to drill down to the real root cause. The graphic in [Appendix 2](#) illustrates this process. It is a matter of judgement as to how far you drill down and in how many directions, depending on the specific circumstances you encounter. But we suggest that it is unproductive to over complicate the process and the suggested rule of thumb is to keep to a maximum of five levels.

#### **An effective RCA exercise will:**

- not seek to establish a blame culture;
- challenge superficial answers about why things went wrong;
- challenge preconceived notions;
- avoid the temptation of the 'quick-fix' answer and not shy away from identifying matters that might be difficult to fix;
- identify root causes linked directly to one or more review findings;
- stop when it is appropriate to go no further with the RCA; and
- feed into an action plan to remedy the identified root causes with clear responsibilities and a feeling of ownership of the actions.

RCA that is not sufficiently robust may not identify the real root causes for findings. For example, an assumption could be made that a failure to properly check a cash flow statement was due to a lack of knowledge while in fact poor project management had resulted in rushed, last minute work. If the wrong cause is identified, the wrong remedial action will be taken. In this example, training might be recommended, instead of the need to agree a better timetable with the client.

Useful RCA will identify the real key factors and it needs to reach a conclusion to have true impact. [Appendix 1](#) lists some of the issues that might be root causes.

#### **Top tip**

The key to creating a successful RCA is to identify what approach is appropriate for your firm or your particular circumstances and plan accordingly.

# Who should perform the RCA?

In identifying who performs the analysis, firms could consider factors including the required level of skill and experience, objectivity and authority. Below are some thoughts on who might be involved.

**The audit team itself** (plus, possibly, the engagement quality control reviewer) – Some form of self-assessment may be useful, but may not be sufficiently rigorous and objective, particularly if performed close to the time of the review (see comments in the next section on the timing). It may help to use a questionnaire to gather data to analyse for correlation with the inspection or review findings. For example details of engagement hours or the number of years that key team members have been involved on the audit.

**Members of a central function** – More relevant for larger firms, these individuals could be part of quality, methodology, or training function. Such individuals will need to maintain an open mind, and recognise that root causes may lie in areas for which they have direct responsibility. For example, if gaps in the firm's methodology or training are identified as root causes.

**The person who carried out the review** – The analysis might be built into the review process or performed later. Combining it with the review may make it difficult for the audit team to provide candid answers if they are still challenging the review findings.

**Someone outside the audit function** – A non-auditor may be able to offer different perspectives, but may not have sufficient technical knowledge about the audit issues to be able to ask sufficiently probing questions.

**A third party** – Small firms in particular need to consider whether they have a suitable person available within the firm and may decide that a sufficiently objective view can only be obtained from someone from outside the firm. One downside of this option is the potential loss of ownership by the firm. The competence of the third party must also be considered. While they do not necessarily need to be an expert auditor, this decision will depend on the objective of the RCA and the nature of the underlying issues.

## Skills and seniority

It is important that the individual or team performing the RCA has the necessary technical knowledge to understand the issues and, where applicable, the experience to identify suggested solutions. But, perhaps more importantly, they need to display professional scepticism and have strong personal skills, as well as sufficient experience and seniority to be able to ask challenging questions of the audit team. At the same time they need to demonstrate empathy with the team which will help to obtain candid answers to those difficult questions.

Senior staff members are likely to have the necessary skills and experience, but may seem intimidating to junior members of the audit team. Involving less senior staff can have benefits, but firms need to ask whether they have enough background knowledge of the firm's operations and staff dynamics to identify root causes that emanate from those areas. Do they have the analytical skills to perform the task effectively? Also, the nature of the engagement might be a factor in determining how senior the person should be. For example, if the engagement is an audit of a listed entity it might require a more senior staff member.

The individual or team performing the RCA must have sufficient time to explore the root causes in sufficient depth. It may be an iterative process requiring a number of discussions with audit teams, as well as, for example, a review of guidance and training materials.

Sometimes the results of the RCA may make uncomfortable reading. But even if finding suitable solutions in this situation is very difficult (or impossible), it is important that matters are reported to the firm's leadership. The person making the report must be sufficiently assertive to do this and be strong enough to not be deterred from doing so.

### Top tip

Where RCA is being performed by different individuals or teams, covering a range of internal and external inspections, there needs to be sufficient high-level oversight to ensure consistency.

# When should the RCA be performed?

It is important that firms consider what timing will enable the RCA exercise to be fully informed and effective.

Audits are typically performed on a yearly cycle and the ideal situation is to aim for any quality review findings identified at the last inspection to be corrected in time for the following year's audit. It could be that the matters identified are relevant to a range, or all, of the firm's audits and ideally action is needed before the next audit cycle. This will depend on the firm's lead time for the necessary actions, for example, changing methodology might need a significant period of adjustment.

There are a number of factors that might affect the ability of the audit firm to perform RCA in time to make a difference to the next audit cycle, such as when the internal or external quality review inspections take place in the audit cycle and how quickly feedback is obtained from the quality review inspector. Also, it is possible that on occasions RCA might be most effective when the 'dust has settled' and there has been sufficient time for reflection by all involved. There is a balance to be struck and it is important that the RCA is done properly.

Once the review finding has been identified, the RCA can be broken down into two stages: information gathering and root cause identification.

## Information gathering

The key factor in this stage is that RCA should be performed as soon as possible after the review finding is identified (although it could be delayed for good reasons as highlighted above). If information gathering is performed too long after the review, important details may be missed and the root cause may never be discovered.

Information gathering should take place quickly if possible, irrespective of whether the review finding is identified by internal or external monitoring. Information about what went wrong should be obtained directly from those involved in the audit and quality monitoring. If information is not gathered promptly there is a risk that audit team members may have moved on from either the department, office or firm.

Prompt information capture is the best way to avoid the possibility of information becoming unavailable. It also prevents loss or alteration of the data and information. Information is fresh in the minds of the audit team and quality review inspectors and auditors are more likely to remember what they think caused the issue.

## Root cause identification

Once information is gathered and the team performing the RCA understand exactly what went wrong, then it is equally important that root causes are identified quickly.

If the team performing the RCA can ask 'why?' and drill down to the underlying reasons behind the quality failure, this is more likely to be successful if they can question the people who performed the work at a time when they can still remember what they did and the reasons for their actions or inaction.

### Top tip

The RCA should be conducted at a point where informed conclusions can be made, realistic action plans can be formulated and the process can drive real change in the short, medium and longer term.

## Appendix 1

# What sort of issues might be root causes?

Issues that have the potential to be root causes of review findings may be internal, which the firm may be able to influence, or external, which the firm is less likely to be capable of influencing.

It is important to identify whether root causes are internal or external to understand why findings have occurred, despite the likelihood that external causes identified may not be able to be resolved by the firm itself (or alone).

Firms need to consider these issues in connection with the specific nature, type and complexity of the audits they are doing.

This list of potential root causes is provided for illustrative purposes only and is not intended to be comprehensive.

### Resource issues:

- Competencies of staff (this may also have an impact on personal, ethical and attitude issues).
- Experience of staff (this may have an impact on personal, ethical and attitude issues).
- Engagement team dynamics (eg, toxic combinations, skills or experience gaps, lack of continuity and over familiarity).
- Time available (rushed jobs are rarely successful).
- Numbers of staff available (understaffed jobs are rarely successful).
- Lack of clarity on competencies and responsibilities.

### Personal, ethical and attitude issues:

- A mindset that is prepared to cut corners (perhaps due to laziness or a desire to keep to original timetables and budgets) meaning that certain processes are not carried out. This mindset can also accept insufficient evidence to support assertions, possibly due to a poor attitude to the work.
- Unwillingness to acknowledge or learn from mistakes.
- Being unwilling or unable to direct, supervise or review effectively, even when resource is available and procedures require this.

### Process issues:

- Issues arising from the firm's policies and procedures – are they well framed, are there gaps, are they well understood? (This issue may also be bound up with personal, ethical and attitude issues.)
- Does on the job mentoring and reviewing happen in the way it should? (This could be connected with personal, ethical and attitude issues.)
- Are adequate policies and procedures complied with? If not, why not?
- Does the staff appraisal system drive improvement or is it cosmetic?
- Failure to consult when appropriate. (This could be connected with personal, ethical and attitude issues.)
- Poor project management, including leaving big issues to the end of the audit. (A poor attitude to the job that gives rise to this.)
- Where safeguards have been identified as necessary, are these applied effectively?

### Leadership issues:

- Do staff receive appropriate leadership?
- Is change effected when required?
- Is leadership cosmetic or real? (Do actions belie words?)

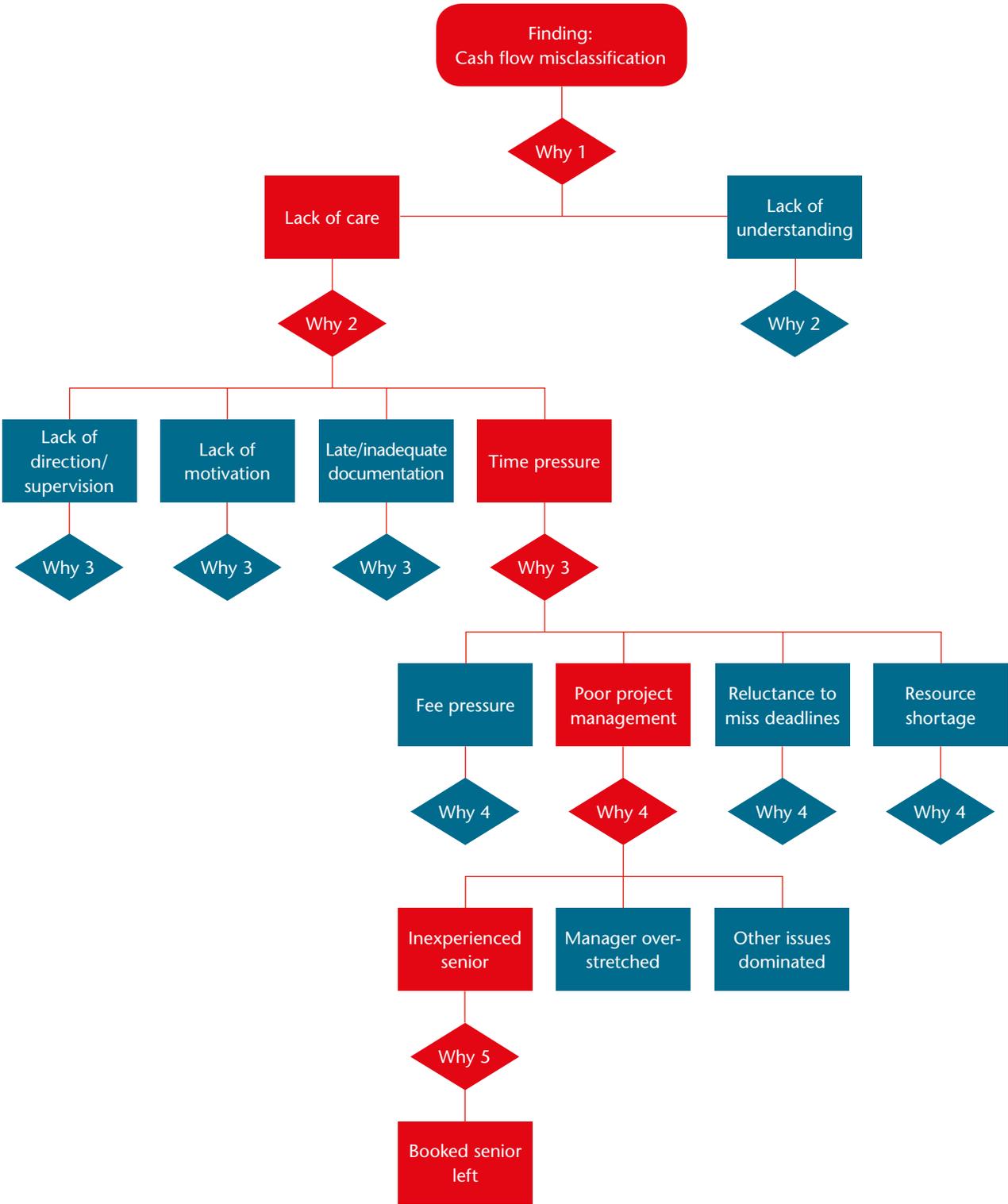
### Client issues:

- Can the firm be fairly expected to serve its client base? (Considering: competence, resources and specialisms.)
- Are review findings rooted in difficulties with client interaction? For example, fee pressure, an unreasonable client-imposed deadline to complete the audit, poor quality, or information arriving late from the client. (These are most likely to be external factors.)

# Appendix 2

## RCA example

Failure to identify cash flow misclassification\*



\*Note – this is only an example of the type of responses that may be given to the ‘why’ questions.

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