

The image features a complex, abstract graphic design. The background is a light gray with a subtle hexagonal pattern. Overlaid on this are several large, overlapping circular and semi-circular shapes in various shades of green and blue. These shapes are filled with intricate patterns, including concentric circles, dashed lines, and solid blocks of color. The overall effect is a sense of depth and complexity, reminiscent of a technical or architectural drawing.

IS IT TIME TO
CHANGE THE
AUDIT FIRM

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Executive summary

Ashwani & Associates is pleased to present this white paper on why, when and how to find a new firm for your privately held company audit:

KEY POINTS ADDRESSED HEREIN:

- CFOs and their Audit Firms sometimes find them selves at odds, with Auditors no longer filling the company's needs. But when change is necessary, the process can be approached with more confidence if there is a clear plan and if all stakeholders understand their roles in the process.
- Key reasons why firms change auditors include: Audit Firm mergers, accounting disagreements, poor service, high staff turnover, lack of ideas from the auditor, fees, regulatory requirements and more.

A few critical first steps in making a change include putting together a needs assessment that will form the basis of your search for a new Audit Firm, and creating a short list of firms that you will invite to preliminary meetings.

Make sure your short list includes firms that have the size, expertise and compliance capability that your company needs.

Schedule meeting with each firm in your office so they can provide a formal presentation acquainting key members of your management team with their firms. This is an opportunity for them to acquaint you with the full breadth of their firms' capabilities and experience.

Key factors that can help insure that the selection of a new firm is successful: independence, size of the firm, industry specialty, compatibility, references, and fees.

Once the selection of a new Audit Firm is made, both the new firm and the incumbent firm should be notified as quickly as possible, and part of the transition process should include a meeting between your company's finance team and the entire audit team from your new CPA firm.

“The relationship between a company and its Audit Firm is a lot like a marriage.”

ashwani & associates

EARNING THE TRUST!

Expectations on both sides must be openly communicated. A common vision should be forged.

Confidential details will be shared, and over the long term, there should be anticipation of growth and prosperity.

But, like many a marriage, CFOs and their Audit Firms sometimes find themselves at odds, with auditors no longer filling the needs of growing, changing companies.

No company wants to go through the upheaval of changing Audit Firms. But when change is necessary, the process can be approached with more confidence if there is a clear plan and if all stakeholders, including the organisation's finance executives and Audit Committee or Board members, understand their roles in the process.

Do you have a compelling reason to change Audit Firms?

While highly-regulated entities such as public companies, financial institutions and nonprofit organizations are more likely to put their audit work out to bid regularly, private companies usually change Audit Firms only when there is a compelling reason. Reasons can range from fees that have gotten too high to lack of responsiveness or conflicts of interest. (See "Common Triggers for a Change in Audit Firms.")

Regulatory Requirements

Section 139(2) of the Companies Act 2013 prohibits the following categories of companies from appointing / reappointing an audit firm for more than 2 terms of 5 consecutive years, i.e. 10 consecutive years, after which such company would be required to mandatorily rotate its auditors in accordance with the Act:

- (i) listed companies;
- (ii) unlisted public companies having a paid-up share capital of INR 10 crores or more;
- (iii) all private limited companies having a paid-up share capital of INR 20 crores or more; and
- (iv) all companies (private and public) which do not meet the thresholds mentioned in (ii) and (iii) above, but have public borrowings from banks / financial institutions or public deposits of more than INR 50 crores.

Common Triggers for a Change in Audit Firm

- Change in company control or management
- Audit Firm merger
- Company cost reductions
- Audit fees that are higher than what was agreed upon
- Price too high for value received
- Disagreement on accounting matters
- Auditor independence impaired
- Scope limitation
- Poor service by Audit Firm
- Lack of responsiveness
- High Audit Firm staff turnover on the account
- Lack of new ideas from auditor

Know what's lacking in the current relationship with your Auditors

To understand what your company needs in a new Audit Firm, it's important to know what is lacking in the relationship with the current Audit Firm. The CFO and finance staff members are in the best position to know, as they have the closest working relationship with the external Audit Firm. Important factors to evaluate include:

Accessibility and pro-activeness

Does the Audit Firm meet with you regularly? Are the auditors always available by phone or email when needed? Do they initiate meetings with you to discuss new ideas and approaches?

Responsiveness

Do the auditors answer your questions in a timely manner with complete information? Do they go beyond the basic answer and offer alternative ideas?

Overall communication

Does the auditor share information with your Audit Committee freely, or does he or she seem protective of management? Does it appear that the auditor's independence is in any way compromised?

Technical expertise

Is the Audit Firm a recognised authority in your industry or field, and is its reputation deserved? Does the Audit Firm meet deadlines consistently and help your organisation meet regulatory requirements? Is the quality and accuracy of its work consistently excellent?

Approach

Are you satisfied with the Audit Firm's planning process and approach? Have there been differences of opinion regarding the scope and nature of the Audit Firm's testing?

Comfort with the Audit Team

Are the individuals from the Audit Firm who service your company easy to work with? Do their personalities mesh well with your staff's, and are they accountable? Has the audit team been stable, or has there been unacceptable turnover? Is cooperative work carried out with a spirit of professionalism and mutual respect?

Fees

Are the fees in line with the value received? Are they in line with what was agreed upon?

Professional services

Does the Audit Firm offer additional professional services – i.e. strategic planning, business consulting, retirement plan services, etc. – that your organisation needs? Any number of pain points may become obvious as these questions are asked and answered honestly.

“There are various factors which determine the need to evaluate a change if necessary. While the most important factors are ‘trust’ and ‘value’, another aspect which is concerning most companies these days is the regulatory requirement under Companies Act 2013 which requires rotation of the auditors.

Starting the search for a new Audit Firm

Once the pain points are identified, you can put together a needs assessment that will form the basis of your search for a new Audit Firm. You don't want old frustrations to be repeated with a new Audit Firm, and you want to make sure all of the company's needs – those that exist now, as well as those that are anticipated in the future – are met.

Your needs assessment will aid in the process of getting all internal stakeholders on board with the idea of switching Audit Firms, including the finance staff, the CEO and the Audit Committee. Once they are on board, the question of timing should be addressed. The company's fiscal year-end will help determine when the search for a new Audit Firm will take place. If your year-end is more than six months away, you likely have time to get a new Audit Firm in place to perform the current year audit.

Identify and reach out to firms that have shown interest in your company

In today's competitive environment, CEOs, CFOs and company Board members have likely been contacted and wooed by numerous Audit Firms. These firms will be the first group to consider in determining who is invited to bid on your company's audit work. They have shown an interest in working with your company, and they already know something about your needs.

With input from all stakeholders, create a short list of firms that you will invite to preliminary meetings to discuss their capabilities. Make sure they are firms that have the size, expertise and compliance capability that you need. The number of firms you meet with depends on you. How much time can you devote to the search? How many firms do you want to meet with before you feel comfortable narrowing down the field? After the initial meetings, you'll have a good sense of which firms you feel comfortable with. Narrow the field to three to five firms that will be invited to submit a formal proposal for your audit work.

Building your Request for Proposals (RFP)

If you decide to create a formal Request for Proposals (RFP), as many organizations do, the distinct needs that are identified during your internal needs assessment should be reflected in the RFP as questions to the bidding Audit Firms. (See "Building Your RFP.") Provide the RFP to the firms you have chosen to submit proposals, and give them a reasonable amount of time – at least one month – to respond.

Building your RFP

A Request for Proposal (RFP) includes these elements:

- Cover letter with brief description of your company and its search
- Clear deadlines for submitting proposals
- A date or timeframe for when a decision will be made
- Detailed description of the services you seek and the compliance requirements that apply to your company
- Clear, detailed list of information items that you require in submitted proposals
- Process for bidding firms to obtain needed information and documents (i.e. your previous year's financial statement)

Caveat: *There are a number of RFP templates available from web sites and professional associations. If you use one, be sure to add questions that will elicit tailored responses appropriate to your company's needs, and delete questions that are not relevant to you.*

First up: A formal presentation

Prior to receiving proposals from the Audit Firms, you'll want to schedule meetings with each firm in your office so they can provide a formal presentation acquainting key members of your management team with their firms. This is not a presentation of their proposals; rather, it is an opportunity for them to acquaint you with the full breadth of their firms' capabilities and experience and answer any questions that you have. It will also provide an opportunity for them to ask you to clarify any issues about your company that they would like to know so they can give you a truly tailored proposal.

These meetings are crucial to establishing a comfort level and rapport with a potential new Audit Firm. All members of your key management team should be comfortable with each firm that is selected to move forward.

You may want to receive proposals from all the firms, or you may want to narrow down to two or three at this point.

Reviewing and scoring proposals

Once the proposals are received, each should be reviewed and scored according to how well they addressed the points raised in the RFP. Who evaluates the proposals will depend on the company. In small companies, it's possible that the CFO and maybe the CEO will evaluate them together. In larger companies, a committee of the CFO, the Controller and a member of the Audit Committee or Board may evaluate them together. (See "Proposal Scoring.")

Proposal Scoring					
Does the Audit Firm's cover letter set the appropriate tone?	Excellent	Very good	Good	Fair	Poor
Are all RFP questions answered?	Exceeds expectations	Meets expectations	Average	Minor deficiencies	Major deficiencies
Question 1					
Question 2					
Question 3					
Question 4					
Question 5					
Question 6					
Question 7					
Question 8					
Question 9					
Question 10					
Does proposal provide detailed information about firm's complete capabilities?	Excellent	Very good	Good	Fair	Poor
Is proposal concise, well-written and free of typos and grammatical errors?	Excellent	Very good	Good	Fair	Poor
Is the proposal tailored to our company's needs and does it reflect issues discussed in face-to-face meetings?	Excellent	Very good	Good	Fair	Poor

Every company has different needs and should tailor its selection process accordingly. But a few key factors can help ensure that the selection of a new Audit Firm is successful:

INDEPENDENCE

Industry research has shown that the quality of an external auditor is based on the probability that the auditor will both discover and report a breach in an accounting system. While most companies want to work with an Audit Firm that they like and with whom they feel comfortable, you should remember during the selection process that you are essentially hiring a watchdog.

SIZE OF THE AUDIT FIRM

Many studies indicate that audit quality increases with Audit Firm size because of experience and industry knowledge. Typically, large or global companies benefit from the extensive resources offered by Big Four Audit Firms. Smaller companies usually don't require such resources, and benefit from the lower fees and personal attention afforded by local Audit Firms. It's important to understand your company's needs, and make sure the Audit Firms in your bidding process are well-matched for your needs.

COMPATIBLE PERSONALITY OF COMPANY AND AUDIT TEAM

The Board / Audit Committee, management, and personnel throughout the company all need to work closely with the external auditor, so personal compatibility among company personnel and the auditor's partners, managers and staff is important.

REFERENCES

Carefully checking the references of the Audit Firm finalists is a crucial step. Move beyond the "Bob is a great guy, and we've been with him for 20 years" conversation and ask probing questions about the reference's relationship with the Audit Firm, particularly how assertive the auditors have been about examining internal controls and making recommendations for change. Be sure to ask if the Audit Firm is providing any value-added, non-audit services, as well.

FEES

Minimising audit costs may be important, but it is essential to balance the proposed fees with the services, quality and expertise of the proposing firm. Some companies try to find an auditor whose price is within

a reasonable range for the services, but who maximises the value-added services for that price. That requires paying close attention to the proposing Audit Firms' capabilities beyond the exact services outlined in your RFP. Particular consideration should be given to services and capabilities that may be needed by your company in the future as it grows.

INDUSTRY SPECIALTY

Audit Firms with an industry specialty should provide higher quality audits for three reasons: better audit technologies, lower costs due to economies of scale and superior knowledge and technical expertise. In addition, industry experience should improve the detection of fraudulent reporting and task-level performance.

Making the transition to a new Audit Firm

Once the selection of a new Audit Firm is made, both the new firm and the incumbent firm should be notified as quickly as possible.

The new firm will probably have specified in its proposal that it has an expectation that work papers and other documents will be provided by the previous Audit Firm in order to effect a smooth transition. Your company – specifically, your finance staff – has an important role in making sure that happens.

Part of the transition process should include a meeting between your company's finance team, including the Audit Committee or Board members responsible for finance, and the entire audit team from your new CPA firm. This is an opportunity for all parties to get acquainted and share information about how the new engagement will proceed. It is an important part of setting off on the right foot.

Conclusion

Changing Audit Firms is a daunting task for any private company, but if you are unsatisfied with your current firm, there is no need to delay. Putting the right process in place and knowing which steps you must follow will help you embark on the search with confidence.

About us

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