Preparing for a Financial Statement Audit

The objective of a financial statement audit is to obtain reasonable assurance that an organization's financial statements are free from material misstatement. In order to achieve reasonable assurance that an organization's financial statements are fairly presented, in all material respects, an independent auditor needs to perform certain audit procedures on the financial statements and related notes. Working through a financial statement audit will help discover ways to improve efficiency and minimize errors.

This process can feel very overwhelming. Below are a few simple steps to perform to prepare for an audit:

1. Establish an "auditor" file for regulatory agency correspondence and for copies of new or modified documents for fixed asset additions and disposals, debt agreements, leasing arrangements, vendor contracts, lawsuits, complex transactions, technology modifications, and major customers and vendors.
2. Reconcile detail to general ledger account totals. For example, reconcile all bank accounts, accounts receivable, accounts payable and equipment lists.
3. Deadlines should be prepared to discuss significant estimates used in the financial statements, such as allowance for uncollectible accounts, warranty reserves, and percentage of completion.

Preparing for an audit

The financial officer of the organization or entity should discuss with the auditor the need for assistance and establish a high priority for agreed-upon items, while ensuring the time frame is fair to the staff.

Then, those expressed needs, as well as the audit procedures that will be performed should be discussed with management. Timing of the engagement is important. Determine contact people for specific areas under audit and avoid any potential scheduling conflicts, such as vacations, scheduled medical procedures, work schedules, out-of-town needs and holidays.

Information you may need to provide

Since auditors express an opinion on the broad financial statements, most of the detailed schedules they request are merely items your company should have as part of its accounting procedures.

The auditor systematically and objectively evaluates evidence about the basic financial statement assertions contained in account balances and transactions cycles:

- Existence or occurrence
- Completeness
- Rights and obligations
- Valuation and allocation
- Accuracy and classification

- Cutoff

The auditor may ask you to explain significant actual-to-budget and prior-year variances. Be prepared to discuss the results of the year based on your expectations going into the year.

You may be asked regarding any changes in the following:

- Governance, management, ownership
- Operations, raw materials, distribution
- Technology, personnel, union relations
- Economic/industry developments and their impact on your operations

<u>Communicating with your auditor</u>

Be open with the auditor about difficult areas you've encountered, concerns, questions and recommendations you may have about your job position, your business, or the industry.

Alert the auditor to any outside consultants, regulatory agency inquiries or future plans, and provide related reports and correspondence.

<u>Opinion</u>

You issue your financial statements, and the auditor tests them to determine whether the statements are materially stated. The auditor also looks at the systems and procedures used to generate the financial information to determine if they are free from material misstatements. After sufficient evidence has been gathered that your financial statements have been fairly stated, the auditor gives an opinion on those statements.

Ideally, auditors will provide an unqualified, or "clean," opinion on the organization's financial statements. An unqualified opinion will contain language such as "the financial statements present fairly in all material respects" and "in conformity with accounting principles generally accepted (GAAP) in the United States."