ProSystem *fx*® Knowledge Coach
Addresses Common Auditing
Deficiencies Found in Peer Review

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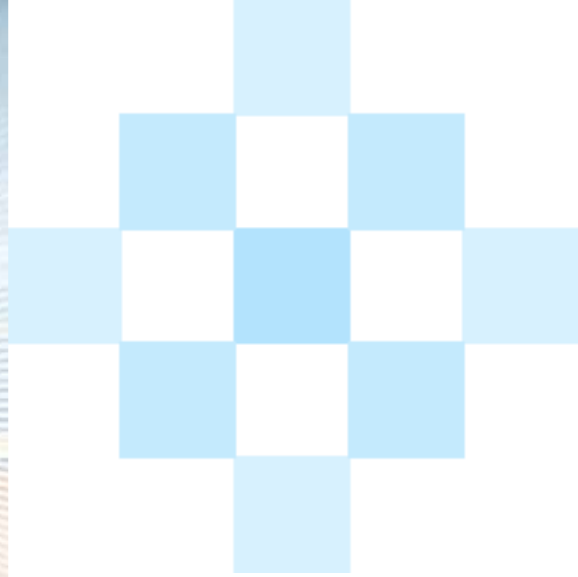
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In his article on common auditing deficiencies, published in the July 28 online edition of *Accounting Today*, Dan Hevia highlights some of the most common issues identified during peer review.

By streamlining CCH's Knowledge-Based Audit™ (KBA) methodology, ProSystem *fx*® Knowledge Coach takes a unique approach that helps auditors avoid these deficiencies and conduct more accurate, higher-quality audits. To explain how Knowledge Coach addresses the most common deficiencies, we asked two of CCH's experts on this solution to share their experience and perspectives from the field.

Deficiency #1: Inadequate Internal Controls Assessments

How Does Knowledge Coach Help Accurately Assess Internal Controls?

Stephanie Lanke: When conducting an audit today, many auditors often don't go outside of the accounting department to evaluate controls. However, just because someone is not a member of the accounting department does not mean they don't participate in the accounting of a transaction. By only talking to the accounting department, it is possible to miss what can go wrong in the business — whether in sales, information technology, the warehouse, or security checkpoints.

Knowledge Coach's control evaluation forms include a comprehensive list of examples that go through the questions auditors should be asking when talking to clients. Using these practice aids encourages the auditor to engage the client with thought-provoking questions that also elevate the skill set of less experienced staff. Many read these and say, "I never thought to ask that," when they read these examples. The questions are specifically designed to identify what can go wrong and to help the auditor evaluate and document their understanding of the client's internal controls.

Robin Penney: In addition, some firms don't test controls or simply set the control risk at maximum. Knowledge Coach helps auditors evaluate and properly document whether this is appropriate. Auditors are required to consider how deep of an understanding of controls they need to get in certain areas, and then to document the design of controls and whether or not they are effective in their design. After that is completed, they may proceed with the testing of the controls. Knowledge Coach can help auditors get more out of evaluating controls and make a better assessment of control risk. Setting control risk to maximum without really understanding the controls at all can actually create more work for the auditor by forcing them to pick more samples and evaluate more procedures because they haven't fully evaluated the client's controls.

Stephanie Lanke: Additionally, when you think of the phrase "Knowledge-Based Audit," the control evaluation process is an excellent opportunity to gain critical knowledge. Lack of understanding the client almost always leads to over-auditing. At times, our clients have told us that other products sometimes generated a disconnect between the evaluation of the design of the internal controls and the controls being tested. As a reviewer, it can be a challenge to see the clear documentation of controls when they are documented in a narrative form, because the reviewer can't easily see the key controls, the relevant assertions, and what procedures were performed to address those assertions and controls in the control testing process.

Knowledge Coach brings it all together in a central location. It provides an extensive matrix that lays out the information clearly and connects the documentation and what ends up getting tested. In testing controls, each test must be tied to an assertion. The Knowledge Coach Activity-Level Controls Evaluation worksheet ties together the evaluation of what can go wrong for each relevant assertion and control objective. It also helps to identify key controls that address what can go wrong, evaluating whether or not those controls are designed effectively and are implemented, and finally to the selection of controls for control testing and the results of the testing.

Deficiency #2: Failure to Link Risk Assessments to Audit Procedures

How Does Knowledge Coach Link Risk Assessments to Audit Procedures?

Robin Penney: The desire to more clearly link risk assessments and audit procedures is one of the most common reasons firms consider Knowledge Coach for their practices. To meet the requirements of the AICPA's risk assessment standards, CCH developed a specific feature designed to directly and clearly link audit procedures to risks identified by the auditor. Unlike other solutions, Knowledge Coach requires auditors to link selected program steps back to either a specific risk, a financial statement level risk or a relevant assertion. If steps are not connected, the auditor will receive a diagnostic that highlights an unaddressed risk, an unaddressed assertion or a program step not linked to a risk.

Stephanie Lanke: In other systems, auditors often have to go out of their way to link the program steps and risks, because there is nothing that requires them to do this explicitly. Even taking the extra step of writing a memo to establish the linkage does not fully protect against inconsistencies. Knowledge Coach enables the auditor to easily see which steps address which risks, ensuring a complete and accurate audit. All the links flow into one central Summary of Risk Assessments document and into a handy Risk Pane, so that staff and reviewers can see, at a glance, how all of the risks are being addressed. This summary stays up to date as changes are made, so that the auditor always knows it's accurate.

Robin Penney: Another key design of Knowledge Coach is that the audit programs are actually blank to start with, and the auditor adds program steps from a Program Step Library based on some tailoring questions and on his or her knowledge of the risks and entity. This is fundamentally different from some other systems where the audit programs are pre-populated for the auditor. Having a pre-populated set of steps naturally makes it harder for the auditor to truly design the steps as they should. In fact, many practitioners have told us that they felt very nervous when removing a step from these pre-populated programs because they hadn't gained a solid understanding of the risks and they felt that it might look bad to a peer reviewer if a step was removed. Knowledge Coach's approach is philosophically different, and encourages auditors to design their own audit programs based on knowledge. The auditor is only doing a step because it's actually necessary, not because it's in the checklist. Again, professional judgment is exercised throughout the engagement by the auditor, not by the system. This helps establish the crucial link between audit steps and risks because the auditor is forced to select steps from the library or write their own, making sure they are covering the risks at the right level.

Deficiency #3: Failure to Identify or Implement New Standards

How Does Knowledge Coach Identify or Implement New Standards?

Stephanie Lanke: Knowledge Coach has the capability to update content to the latest version of industry titles whenever the auditor desires. Auditors can either update information during the binder roll-forward process or they can roll the binder forward first and then update on-the-fly in an active engagement. In a merging process, Knowledge Coach can keep things like answers to questions, sign offs, workpaper references, custom rows, and edits to program steps, but brings in the new content as well, keeping the auditor up-to-date and current. In the past, practitioners had to wait for the latest content to come out and often worried about missing an update. With Knowledge Coach, auditors can start planning whenever they want without worry and update content at any time, on-the-fly.

Robin Penney: Like other vendors, the titles are updated once each year, so practitioners will still need to monitor new pronouncements between updates. To help with this monitoring, there is seamless integration to CCH's Accounting Research Manager® (ARM) directly from the Knowledge Coach workpapers. Auditors can click on a reference to a standard and learn all about it in ARM. One nice feature on ARM is an Effective Date Checklist that lists all new pronouncements and when they kick in, whether early adoption is permitted, and other key information about the pronouncement.

Deficiency #4: Not Understanding Specialized Industry and Reporting Situations

How Does Knowledge Coach Deal with Specialized Industry and Reporting Situations?

Robin Penney: CCH recognizes the importance of specialized industry knowledge.

To that end, CCH has created a variety of industry-specific titles, including:

- Commercial
- Compilations & Reviews
- Construction
- Employee Benefit Plans
- Financial Institutions
- Government
- Health Care
- International
- Non-Traditional Engagements
- Not for Profit
- PCAOB
- Real Estate
- Single Audit

CCH has a number of new titles scheduled for release within the next year, including:

- Common Interest Realty Associations
- Housing and Urban Development

Each CCH specialized title is tailored to the specific industry, including the program steps, reports, different correspondence letters, and what needs to be handled during planning and financial statement disclosure checklists. CCH is constantly monitoring industry developments to keep clients up-to-date and current with the latest requirements.

Stephanie Lanke: In addition, users are actively encouraged to customize Knowledge Coach for their clients. If CCH does not cover a specific industry yet, users can add their own custom audit steps and that will flow throughout the auditing process.

For example, one client we work with serves a number of school districts. He started with the Government title and then customized his engagements from there. Since Knowledge Coach enables customization, he was able to use much of his work with his other school district clients.

Deficiency #5: Inadequate Tailoring of a Firm's Quality Control System

How Does Knowledge Coach Help Tailor a Firm's Quality Control System?

Stephanie Lanke: The reality is that very real business risks can indeed happen and peer review is only part of the quality control process. We have seen customers with clean peer reviews still feel that there were inconsistencies with their risk assessment process. They felt that they were only able to monitor the obvious risks, leaving the firm exposed.

Robin Penney: Used properly, the forms and practice aids in the KBA methodology will aid the auditor in meeting the quality control requirements. While Knowledge Coach does not address certain matters such as auditor independence and staff training, the KBA methodology does include a document that covers Meeting Quality Control Standards, which covers the main steps auditors need to be taking with regard to quality control as they relate to specific engagements. The document lists the quality control requirement that affects the performance of the specific engagement and the workpaper where that requirement is addressed.

The Consequences of Non-Compliance

How Does Knowledge Coach Guard Against the Inappropriate Use of Third-Party Practice Aids?

Stephanie Lanke: The fact of the matter is that some third-party practice aids can be misused in the field. Most often, they are either over-relied upon or simply bypassed altogether. If an auditor grows to over-rely on a practice aid, he or she can adopt a "checklist mentality," in which critical thinking stops in favor of simply going through a series of pre-defined steps, whether they make sense or not.

On the opposite end of the spectrum, some practitioners can feel that practice aids are overkill or don't allow for the customization required in their specific client engagements. As a result, they stop using them entirely, missing out on the efficiencies they can deliver.

What sets ProSystem *fx* Knowledge Coach apart is that it forces the auditor to rely on their expertise and rethink what they've done in the past. We don't make professional judgments for the auditor. Instead, we guide them, provide recommendations and highlight potential errors, but the ultimate decisions remain with the professional.

We do this through the KBA methodology, which helps auditors collect information and build their knowledge of their client's business and practices. The KBA methodology helps ensure that the auditor designs the appropriate audit steps based on what is learned about the entity. This helps protect against both under- and over-auditing. While the KBA methodology assists the auditor in gathering and organizing information, the auditor makes all of the decisions related to identifying risks and designing the appropriate program steps. And if new information is gained during the engagement, that knowledge can be incorporated, new risks can be identified and addressed, and it all flows through the KBA documentation very naturally.

Robin Penney: One example of practice aid misuse we've seen in the field is in the area of financial statement assertions. Our audit clients need to assess risk at the assertion level, and we've had a number of clients tell us that other products obscured the connection between assertions and the program steps selected to address them. With Knowledge Coach, the auditor has to consciously select their relevant assertions for each audit area. Once the auditor selects their assertions, they assess inherent and control risk at the assertion level. Then they build their program steps to address each assertion, paying attention to the diagnostics that keep track of unaddressed assertions and unaddressed risks. As a result, they must ask themselves:

- Why am I picking this step?
- Am I addressing each assertion and risk?
- Am I over-addressing any assertions?

Knowledge Coach helps make sure that the auditor covers all relevant points to gain a better understanding of the business, as well as the thinking behind how each step supports the audit objectives.

Stephanie Lanke: That's one of the biggest benefits we've seen from Knowledge Coach — it creates a deeper understanding of the audit process and the client's business. Under the risk assessment standards, audit procedures need to be linked to each risk, but if a set of steps is chosen by a practice aid and staff don't understand why, they are missing the main point of the audit. We've had people who have implemented Knowledge Coach and used it on engagements successfully connect the dots between what they're doing and why, and exclaim, "I've been doing this for over 20 years, and I finally understand what I'm doing."

Robin Penney: Over time, this knowledge leads to improved efficiency. Once you understand the methodology, you can contribute more as a business advisor to your clients because you truly know the inner workings of their businesses. We're seeing many customers roll out Knowledge Coach to their smaller engagements due to the efficiencies they've gained from the methodology. Using Knowledge Coach, they have found that they can cut down on their fieldwork because they are conducting more effective pre-planning assessments. The KBA methodology has helped make their entire auditing process more efficient.

Dan Hevia is a shareholder with Gregory, Sharer & Stuart. He is an experienced peer review team captain and chair of the AICPA Peer Review Board. His article, "Significant and Pervasive Audit Deficiencies within Accounting Firms" can be found in the July online edition of *Accounting Today*.