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Audit Documentation

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Learning Objectives

At the end of this session, you will be able to:

- Recognize the documentation standards for financial statement audits and other audits
- Define reliable audit evidence
- Identify retention requirements and best practices



Why does it matter?

- The AICPA Peer Review Program determined that a **lack of proper audit documentation** is the most common form of non-conformity with professional standards.



Objective of Audit Evidence

The auditor should obtain Sufficient and Appropriate Audit Evidence to be able to draw reasonable conclusions on which to base the audit opinion.



What is Required?

- Sufficiency is the measure of the **quantity** of audit evidence. The quantity of audit evidence needed is affected by the auditor's assessment of the risks of misstatement (the higher the assessed risks, the more audit evidence is likely to be required) and also by the quality of such audit evidence (the higher the quality, the less may be required).
- Appropriateness is the measure of the **quality** of audit evidence (that is, its relevance and reliability in providing support for the conclusions on which the auditor's opinion is based). The reliability of evidence is influenced by its source and nature and is dependent on the individual circumstances under which it is obtained.



Sufficiency

- Sampling learned about earlier



Appropriateness

- Relevance
 - Relevance relates to the logical connection with, or bearing upon, the purpose of the audit procedure and, when appropriate, the assertion under consideration.
 - Example: Testing recorded accounts payable existence and valuation
 - Testing for Overstatement – relevant
 - Testing for Understatement – not relevant (need to test subsequent disbursements, unpaid invoices, etc.)



Appropriateness

- Reliability
 - The reliability of information to be used as audit evidence and, therefore, of the audit evidence itself is influenced by its source and nature and the circumstances under which it is obtained, including the controls over its preparation and maintenance, when relevant.



Reliability of Audit Documentation

- When using information produced by the entity, the auditor should evaluate whether the information is sufficiently reliable for the auditor's purposes, including, as necessary, in the following circumstances:
 - Obtaining audit evidence about the accuracy and completeness of the information
 - Evaluating whether the information is sufficiently precise and detailed for the auditor's purposes



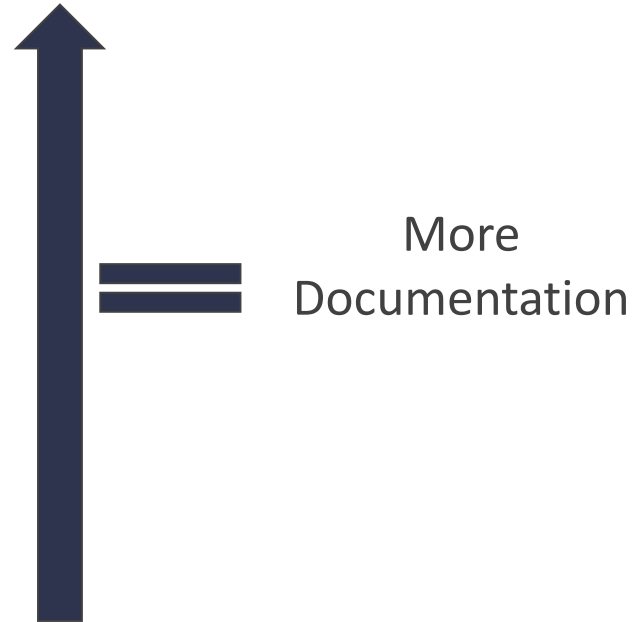
Reliability of Audit Documentation

- Documentation should be prepared on a timely basis
 - Helps enhance audit quality
 - Facilitates effective review before auditor's report is finalized
 - Increases likelihood that documentation will be accurate

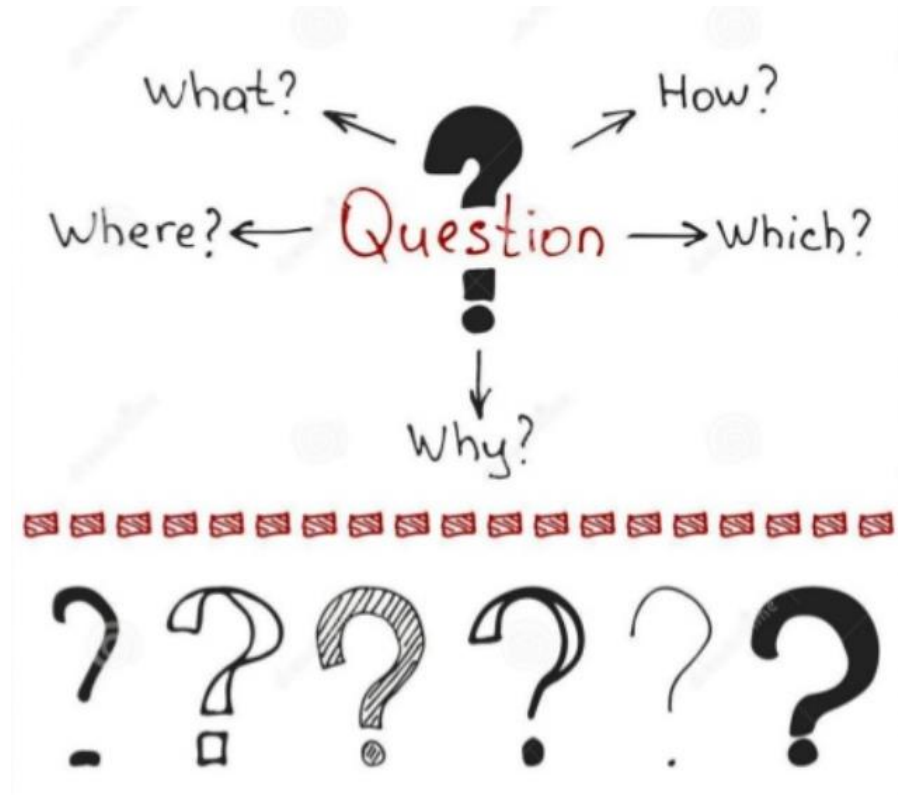


How much do you need?

- Risk
- Judgement
- Need of Analysis
- Conclusion Less Apparent
- Significant Evidence
- Materiality



What is documentation?



What is Documentation?

- AU-C Section 220: Audit Documentation
 - The record of audit procedures performed, relevant audit evidence obtained, and conclusions the auditor reached
- AU-C Section 500: Audit Evidence
 - Information used by the auditor in arriving at the conclusions on which the auditor's opinion is based. Audit evidence includes both information contained in the accounting records underlying the financial statements and other information.



What is Documentation?

- Auditor's record of
 - Procedures performed
 - Relevant evidence obtained
 - Conclusions reached
- Examples
 - Audit plans and checklists, including risk assessment
 - Analyses and memos
 - Confirmations and representation letters
 - Correspondence (including email) concerning significant findings/issues



Workpapers



What is Required?

- Experienced auditors with no connection to the audit should understand:
 - Nature, timing and extent of procedures performed
 - Results and evidence obtained
 - Significant findings, issues and professional judgments
- Applies to **any procedure** that provides audit evidence necessary to support the opinion



Nature and Timing

- The nature and timing of the audit procedures to be used may be affected by the fact that some of the accounting data and other information may be available only in electronic form or only at certain points or periods in time.
 - For example, source documents, such as purchase orders and invoices, may exist only in electronic form when an entity uses electronic commerce or may be discarded after scanning when an entity uses image processing systems to facilitate storage and reference.

Extent (Form and Content)

- The form, content, and extent of audit documentation depend on factors such as
 - the size and complexity of the entity.
 - the nature of the audit procedures to be performed.
 - the identified risks of material misstatement.
 - the significance of the audit evidence obtained.
 - the nature and extent of exceptions identified.
 - the need to document a conclusion or the basis for a conclusion not readily determinable from the documentation of the work performed or audit evidence obtained.
 - the audit methodology and tools used.
 - the extent of judgment involved in performing the work and evaluating the results.



Sources

Audit procedures to obtain audit evidence can include inspection, observation, confirmation, recalculation, reperformance, and analytical procedures, often in some combination, in addition to inquiry. **Inquiry alone ordinarily does not provide sufficient audit evidence!**

1. Inspection

- It consists of examining records and documents to varying degrees of reliability.
- It also consists of examining tangible assets with respect to their existence but not necessarily as to their ownership.

2. Observation

- It consists of looking at a process or procedure being performed by others.



Sources

3. Inquiry

- It consists of seeking information of knowledgeable persons within or outside of the entity. It can be in form of written inquiries or informal oral inquiries.

4. Confirmation

- It consists of response to an inquiry to corroborate information contained in the accounting records.

5. Recalculation

- It consists of checking the mathematical accuracy of source documents and accounting records.

6. Analytical Procedures

- It consists of the analysis of significant ratios and trends including the resulting investigation of fluctuation.



Sources

- Information obtained from a source independent of the entity may increase the assurance that the auditor obtains from audit evidence that is generated internally
 - Accounting records alone do not provide sufficient appropriate audit evidence on which to base an audit opinion
- The absence of information (for example, management's refusal to provide a requested representation) is used by the auditor and, therefore, also constitutes audit evidence.

Oral Documentation

AU-C 230.A7



If requirements of AU-C 230 **are met**, oral explanation may be **appropriate**.



If requirements of AU-C 230 are **not met**, oral explanation is **not sufficient**.



Documentation for Testing

- For each required procedure, auditor should record

✓ **Identifying characteristics of items tested**

✓ **Who performed and date of performance**

✓ **Who reviewed and date/extent of review**

Documenting Sample Selections

- **Purchase orders**
 - identify the documents selected for testing by their dates and unique purchase order numbers.
- All items **over a specific amount** from a given population
 - record the scope of the procedure and identify the population (for example, all journal entries over a specified amount from the journal register for the period being audited).
- **Systematic sampling** from a population of documents
 - identify the documents selected by recording their source, the starting point, and the sampling interval (for example, a systematic sample of shipping reports selected from the shipping log for the period from April 1 to September 30, starting with report number 12345 and selecting every 125th report).
- **Inquiries** of specific entity personnel
 - record the inquiries made, the dates of the inquiries, and the names and job designations of the entity personnel.
- **Observation** procedure
 - record the process or matter being observed, the relevant individuals, their respective responsibilities, and where and when the observation was carried out.



Documenting Populations

Audit documentation that is used for performing audit procedures needs to be sufficiently complete and accurate.

- Ex: The effectiveness of an audit procedure, such as applying standard prices to records of sales volume to develop an expectation of sales revenue, is affected by the accuracy of the price information and the completeness and accuracy of the sales volume data.
- Ex: Testing controls over the preparation and maintenance of the information. *However, still need to determine the completeness of the populations of controls being tested.*

Redundant and Unnecessary

- Timely removal- not only permitted but encouraged during the audit and during the “file assembly” period, but not after a subpoena (or notice of regulatory investigation) arrives
- Client correspondence that is not related to the audit may be retained in separate correspondence or desk files, but not in audit workpapers
- Superseded, redundant, and other unnecessary material





Findings

Documenting Findings and Issues

- Judging significance requires an objective analysis
- Consider extent to which professional judgment is exercised
- Document discussions of significant findings or issues with management, those charged with governance, and others, including
 - Nature of findings or issues discussed
 - When and with whom discussions took place
- Document how inconsistencies were addressed
 - Procedures in response to the information
 - Differences in professional judgment



Documenting Findings and Issues

- More detail documented within the finding can make for a more efficient close to your audit
 - Specific details on the findings
 - Who and what documentation the finding came from
 - When and where the information was obtained
 - Provide preliminary findings in status updates, not draft reports



Documentation Retention

Retention Requirements – AICPA

- Document report release date in the audit file
- No more than 60 days to lock the audit file down
- Keep all documentation in audit file for **5 years** from release date

Other Retention Requirements

- **IRS** – 3, but really 7 Years
- **CMS** (Medicare managed care program providers) 10 years
- **IIA** – “retention requirements must be consistent with the organization’s guidelines and any pertinent regulatory or other requirements.”



Electronic WP Retention

- Data backups – Test your data
- Offsite storage
- Due Diligence on workpaper software provider
- Encryption



Paper WP Retention

- Locked room
- Sprinkler System
- Alarms/Security Cameras
- Logs for accessing finalized binders



Additional Resources

- <https://www.aicpa.org/eaq/peer-review-documentation-resources.html>



Thank you



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