

Changing Audit Firms: A Guide for the Privately-Held Company

CBIZ Tofias and Mayer Hoffman McCann P.C. - Tofias New England Division are pleased to present this whitepaper on why, when and how to find a new firm for your privately held company audit



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Mayer Hoffman McCann P.C.
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An Independent CPA Firm

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Executive Summary

CBIZ Tofias and Mayer Hoffman McCann P.C. - Tofias New England Division are pleased to present this whitepaper 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 themselves at a crossroads, with auditors no longer filling the company's needs. 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: poor service, high staff turnover, missed deadlines, lack of ideas and solutions from the auditor, surprises, fees 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 bid on your work.
- Make sure your short list consists of firms that have the size, expertise and compliance capabilities that you need.
- Schedule meetings with each firm at your office so they can provide a formal presentation acquainting key members of their firm with your management team. This is an opportunity for them to present you with the full breadth of their firm's capabilities and experience. In some situations these meetings are held before firms are asked to formally propose on the work, while in other situations these meetings are held with those firms that qualified after submitting their formal proposals.
- Key factors that can help ensure that the selection of a new firm is successful include independence, size of the firm, compatibility, references, fees and industry specialty.
- 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.

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The relationship between a privately-held company and its audit firm is an important one that should be nurtured. 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, CFOs and their audit firms can sometimes find themselves at a cross-roads, with auditors no longer filling the needs of growing, changing companies.

Not many companies want to go through the process of changing audit firms. However, when change is necessary, the process can be approached with confidence if there is a clear plan and if all stakeholders, including the organization’s finance executives and Audit Committee or Board members, understand their roles in the process.

Common Triggers for a Change in Audit Firm

- ✓ Poor service by audit firm
- ✓ Lack of responsiveness
- ✓ High audit firm staff turnover on the account
- ✓ Lack of new ideas and solutions from auditor
- ✓ Surprises from the auditor
- ✓ Missed deadlines by the audit firm
- ✓ Lack of industry knowledge by the audit firm
- ✓ Company outgrew the audit firm
- ✓ Audit fees that are higher than what was agreed upon
- ✓ Price too high for value received
- ✓ Change in company control or management
- ✓ Company in bankruptcy
- ✓ Auditor independence impaired
- ✓ Scope limitation

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Do You Have a Compelling Reason to Change Audit Firms?

While highly-regulated entities such as public companies, financial institutions and not-for-profit 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 poor service by the audit firm to lack of responsiveness or industry expertise. (See “*Common Triggers for a Change in Audit Firms.*”)

The Players

The key players in a company’s financial hierarchy should be involved in identifying needs and finding a new audit firm, including:

- ✓ Chief Executive Officer
- ✓ Chief Financial Officer
- ✓ Controller and Assistant Controller
- ✓ Accounts Receivable/Payable Supervisors
- ✓ Internal Auditor
- ✓ The Audit Committee
- ✓ Members of the Board who are regularly involved in financial issues

Know What is 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. (See “*The Players.*”)

Important factors to evaluate include:

- **Accessibility and Proactiveness** – 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 and solutions?
- **Overall Communication** – Do the auditors share information with your Board of Directors and/or Audit Committee freely, or do they seem protective of management? Does it appear that the auditors’ independence is in any way compromised?
- **Technical Expertise** – Is the audit firm a recognized authority in your industry or field, and is its reputation deserved? Does the audit firm meet deadlines consistently and help your organization 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?

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Know What is Lacking in the Current relationship With Your Auditors (Cont...)

- **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, 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, risk and control services, retirement plan services, valuation services, etc. – that your organization needs?



Any number of pain points may become obvious as these questions are asked and answered honestly.

Starting the Search for a New Audit Firm

Once the pain points are identified, your Board of Directors and/or Audit Committee and finance staff 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/Audit Committee members have likely been contacted by numerous audit firms. These firms should 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 likely already know something about your needs.

With input from all stakeholders, create a short list of firms that you will invite to propose on your work. Make sure they are firms that have the size, expertise and compliance capabilities that you need. The number of firms you reach out to depends on you. How much time can you devote to the search? How many firms do you want to propose on your work before you feel comfortable narrowing down the field?

After reviewing all of the responses to your request for proposal, you'll have a good sense of which firms you feel comfortable moving forward with. You can then narrow the field to three to five firms that will be invited to meet with you at your office and provide a formal presentation acquainting key members of their firms with your management team.

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Building Your Request for Proposal (RFP)

If you decide to create a formal 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

An RFP typically includes these elements:

- ✓ Cover letter with brief description of your company and its search
- ✓ Clear deadlines for submitting proposals
- ✓ 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 statements)

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.

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 of Directors may evaluate them together. (See “*Proposal Scoring.*”)

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Reviewing and Scoring Proposals (Cont...)

| Proposal Scoring | | | | | |
|--|----------------------|--------------------|---------|--------------------|--------------------|
| Does the audit firm's cover letter set an 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 firm to express an opinion about whether your financial statements are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles (or another financial reporting framework).

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 national and international audit firms. Smaller companies may not require such resources, and may also consider smaller regional or local audit firms in their search. 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.

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Reviewing and Scoring Proposals (Cont...)

Compatible Personality of Company and Audit Team – The Board of Directors and/or 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 audit firm’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 – Minimizing audit costs may be important, but it is essential to balance the proposed fees with the services, quality and expertise of the proposing firm. Fees should be clearly presented, state what is included and not included, should be fixed, and state that the firm will seek approval before any additional fees are incurred.

Industry Specialty – Audit firms with an industry specialty should provide higher quality audits due to tailored audit methodologies and superior knowledge and technical expertise.

The Formal Presentations

As previously mentioned, while some companies choose to hold formal presentations before selecting firms to proceed with the RFP, in most situations the formal presentations are held after reviewing all responses to the RFP. The meetings are scheduled with selected firms at your office so they can provide a formal presentation acquainting key members of their firms with your management team. This is an opportunity for firms to introduce the full breadth of their capabilities and experience and answer any questions that you have. It will also provide an opportunity for you to ask them to clarify any information included in their proposal as well as respond to those issues and needs that are most important to you.



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 the firm that is selected to move forward.

You may want to schedule meetings with all the firms you received proposals from, or you may want to narrow it down to three to five, or even two to three, at this point.

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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 the prior year audit documentation will be provided by the predecessor 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, and is an important step in getting off on the right track.

Conclusion

Changing audit firms can be 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, and assist in making the right selection for your company.



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About CBIZ Tofias and Mayer Hoffman McCann P.C.

We Help Our Clients Maximize Their Business Efficiency for Greater Financial Performance

CBIZ Tofias and Mayer Hoffman McCann P.C. - Tofias New England Division, a top ten national accounting and tax provider, uniquely combine national resources with local decision making by experienced, New England-based

professionals. Our specialists, skilled in accounting and auditing*, tax, and a range of consulting services, are dedicated to strengthening our clients' financial positions. When you choose CBIZ Tofias and Mayer Hoffman McCann P.C., you get proactive, accessible professionals who communicate in understandable terms, and deliver practical solutions on time, with no surprises, to help your organization thrive.

We are distinguished by the quality, credibility and insight of our accounting and auditing professionals who take the time to get to know each of our clients and the specific issues they face.

Our audit services are designed to:

- Examine your business to identify areas of financial statement risk.
- Reduce your risk of material misstatement.
- Provide informative financial statement results reporting to your management, audit committee or board.
- Deliver effective strategies and recommendations designed to enhance the value of your business.
- Keep you informed regarding pertinent accounting standards and assist in the implementation of applicable new standards.
- Ease the audit process by giving your accounting personnel adequate lead time to prepare required documentation.
- Meet all internal or external deadlines.

We utilize the audit process to provide ideas and recommendations that improve your financial position. For further information on our audit services for private companies, contact Marc Busny at 617.761.0565 or mbusny@cbiztofias.com.

**Audit and other attest services provided by Mayer Hoffman McCann P.C., an independent CPA firm.*

