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Financial Reporting Council
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For the attention of Jason Bradley

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Dear Sir,

Discussion document on Technological Resources: Using Technology to enhance audit quality

Thank you for producing the discussion paper on “Using Technology to enhance audit quality”. We welcome the opportunity to join the debate afforded by the paper. Our responses to the questions posed are attached.

If you would like further clarification of any comment in our response or have other queries, please do not hesitate to contact me by e mail as below.

Yours sincerely,



Dianne Simpson-Price

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TECHNOLOGICAL RESOURCES: USING TECHNOLOGY TO ENHANCE AUDIT QUALITY

RSM Audit UK LLP Responses

1. Do you agree that the increasing use of technological resources, including AI and other advanced tools, enhances the quality of audits, beyond the benefits derived from efficiency gains. If so, what are the indicators of enhanced quality?

- Yes, when used in the right place – at the right time.
- There are many cases where data analytics is not currently being used where its use could provide an increase in quality. In future we anticipate that growing familiarity and understanding of available tools and techniques will ensure that they are deployed in the majority of appropriate cases.
- There is no “one size fits all” approach to audit. Even in the future when common data models and more open source information make a suite of “standardised” routines appropriate, the interpretation of the results of the output data and underlying understanding of areas where manipulation is possible will underly the quality of the audit process.
- Ultimately the increase in quality can only be achieved by audit teams who understand the objective of the test and how the respective tool / technique enables them to achieve that objective.
- Key indicators of enhanced quality would be:
 - a greater understanding of client systems and processing of data, including consideration of segregation of duties and utilisation of audit trails
 - this knowledge can assist in providing a more tailored audit risk assessment
 - a reduction in the need to extrapolate results from a relatively small sample of a large population due to interrogation of the total population
 - the prospect of greater clarity in documentation based on common use cases of specific tools and techniques
 - use of tailored tools for client-specific tests and to add elements of unpredictability
 - for the SME audit market these approaches can add value to the audit by providing greater insights to share with management

2. Do you believe that challenger firms are currently at a disadvantage in the use of new technology? If so, what remedies would you suggest?

- Third party providers have identified that there are significant numbers of audit firms who did not have the appetite to engage in heavy investment (both financial and people resource) in bespoke, in-house development of audit analytic systems, although they were ready to employ such tools. Such providers have moved to meet this market demand, thus bringing cost-effective options within the reach of challenger firms.
- Even so, the need to “translate” the wide variety of client systems in a constantly evolving marketplace to any interrogating software is clearly a barrier to the promotion of competition between firms. The adoption of a common data model within the industry, and ideally by technology providers, would significantly reduce barriers to competition.
- Any move towards joint audits, as suggested by the CMA review, could well require the sharing of common platforms and methodology which could lead to the larger firms licensing the use of their platforms to their joint audit colleagues. The Institutes’ involvement in such licensing could facilitate this approach not just for joint audits, but for other assignments as well.

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3. Other than investment, what do you believe are the key challenges auditors face in the increasing utilisation of automated tools and techniques within the audit process? Again, what remedies would you suggest to overcome these challenges?

- As noted above, a move to common data models would promote more investment and intelligent innovation of auditing techniques. The open source common data model environment is more likely to promote development by entrepreneurial technology innovators.
- Losing the need for a data transformation process, which is currently a significant cost of any system, would enable small, agile, intelligent auditing application production for specific market use that could lower the barriers of entry to a significant number of audits for challenger firms.
- The lack of reference to data analytics throughout the ISAs can make it challenging to use these techniques. This means that auditors can find difficulty in interpreting the language used by the ISAs in the context of data analytics. Greater clarity would incentivise auditors to pursue this 21st century range of techniques. This would greatly assist engagement with training and transition for all firms.

4. Does the current assurance model or the auditing standards represent an obstacle to technological innovation? If yes, then what specific standards, objectives, requirements or guidance cause practitioners particular difficulties?

- No, it doesn't create an obstacle but the lack of reference to data analytics has led to its use as a marketing tool for the larger firms rather than a signifier of audit quality. ISAs could be used to encourage the use of data analytics appropriately by all, thereby acting to level the playing field.
- The ISAs generally ignore the use of data analytics as an audit technique and so it has been left to individual audit firms to try to shoe-horn their use of data analytics into an ISA compliant position when the position should be totally clear, given the increasing prevalence of these techniques.
- One of the key issues is the treatment of "outliers" identified in any technique in that some may read the ISAs as considering these as "errors" when they are just a specific part of a population requiring further auditor analysis or investigation. This may well be due to the definition of "outliers" not being adequately detailed. Several relatively easy data interrogations could well inform the audit team on elements of the client's information processing that a standard sampling technique across a whole population would not identify.
- Maybe ISAs should address how computer systems are intrinsic to the client's ability to process all transactions.
- The FRC's paper, "The Use of Technology in the Audit of Financial Statements", made it clear that data analytics gives greater insight and understanding of client systems. ISAs could possibly be developed to recognise this and encourage auditors' use of these techniques.

5. Do you believe the current level of training given to auditors – both trainees and experienced staff – is sufficient to allow them to understand and deploy the technological resources being made available?

- We firmly believe that in the future all auditors will require the ability to deploy data analytics in order to achieve the level of audit confidence required in a cost-effective manner.
- To do this, as noted above, a significant level of understanding in the processing of data undertaken by the entity being audited would be a prerequisite, and we see a distinct training requirement in this respect.
- Both professional bodies and training organisations are increasingly identifying this need and extending and refocusing their offerings to address this. However, we believe that there is still much to do.
- Looking to the future, we would anticipate that whilst a core syllabus will still be required for trainee accountants there will be the need to specialise by way of module selection or diploma options in specific

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5. (continued)

- fields which, in the case of auditing, could involve additional differentiation for those specialising in data science.
- It should not be left to audit firms to provide continuing professional development in data science post qualification. Those who have not specialised during initial training, or where their firms do not give that option, should have the ability to move into the field or extend their knowledge of data science through CPD options backed by the professional bodies.
- Internally, all firms must identify the data analytic techniques appropriate to their own methodologies and ensure that internal training reflects this.
- The key focus should not be “one size fits all”. Auditors need to utilise data analytics to achieve audit confidence and therefore the training needs to keep this in view as the required end result. Whilst some general underpinning knowledge will form the basic foundations, the requirements to reach an audit opinion should always be kept in mind.
- Ultimately, firms can provide their staff with as much training as possible, but unless audit teams understand the data systems and processes adopted by their clients, they will never be able to truly deploy appropriate testing outside of a traditional sample-based approach. The training needs to encourage and support achievement of that level of understanding.

6. What firm-wide controls do you believe are appropriate to ensure that new technology is deployed appropriately and consistently with the requirements of the auditing standards, and provides high quality assurance which the firm can assure and replicate more widely?

- Whether new technology is developed internally or purchased from an external provider, a rigorous assessment and testing process is required to ensure that confidence taken is well founded.
- Evaluation must always be in the context of the methodology utilised by the firm.
- A robust testing process, both on initial deployment and subsequent updates, would be required which would include (but not be limited to):
 - A core central testing team
 - Pilot programmes to involve the use of teams “on the ground” and obtain relevant feedback
 - Bite sized training for staff once the technology has been deployed – preferably in a hands-on format to encourage learning
 - Any training to focus on practical application as well as some theory – but not so much that audit teams lose track of how to apply the technique to their clients

7. Are you aware of the use of new technologies in analysing and interpreting information provided by auditors – including, for example, auditor’s reports? If yes, then do you foresee implications for the form and content of auditor’s reports?

- Various pieces of software are already doing this kind of analysis but are restricted due to the historic and current reporting requirements.
- The format of audit reports is driven by regulatory and legal requirement and, whilst this is the case, differentiation will always be limited and possibly restricted to the listed entities where additional requirements exist and could be enhanced due to requirements for greater transparency.
- Analysing listed reports could identify the use of “boilerplate” wording which investors may perceive as lacking specificity and act as a strong incentive for firms to differentiate to a greater degree than is currently the practice.
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7. (continued)

- Whether it would be necessary to adopt an ixbrl style audit report which can be easily “tagged” with key information is debateable given the developments in software such as machine learning identifying terms etc.

8. What do you see as being the main ethical implications arising from the greater use of technology and analytics in an audit?

- Confidentiality is the main ethical issue.
- Many of the enquiries that can be made digitally, and address issues of fraud inevitably involve interrogation of personal data and increasing consideration of non-financial, unstructured data such as email, telephone records, online activity etc. Auditors therefore have to be mindful of the legal and ethical framework when they work with and document their procedures on such information.
- Organisations may wish to anonymise data being interrogated but such procedures may compromise the results of the audit work being undertaken.
- With a push towards transparency for financial reporting it is vital that technological solutions can be found to these challenges. The ability to effectively audit adjustments to data, such as anonymisation, to ensure the processes have not sought to hide fraudulent activity will be important.
- For international audits, data residency will always be a challenge as sharing data across different jurisdictions brings legal challenge.
- Ethical and legal issues are totally intertwined as governments have sought to legislate in this area in protection of privacy which may, on occasion, bring some barriers to audit work that may lead to a restriction in scope that must be recognised.

9. Do you believe there is value in the UK having consistent data standards to support high quality audit, similar to that developed in the US?

- Whilst there are a number of common data standards, the AICPA model being just one, the lack of conformity in any country amongst the users and technology providers reduces their impact significantly.
- The question specifies common “data standards” rather than a common data model which would be of greater use to the profession.
- The lack of a common data model contributes to lengthy data extraction and cleansing times which inevitably act as a barrier to entry for smaller audit firms, and also act as a deterrent to stakeholders who may otherwise consider a move to an alternative audit firm but for the ever increasing cost of first year set up to obtain the required data from underlying accounting systems, or data lakes.
- The implementation of a common data model, such as that being developed by Engine B (which seeks to aggregate the work done by the AICPA and others as a foundation) would be a significant benefit to the accounting profession as a whole. As noted earlier, most of the time spent performing data analytics procedures is spent on cleansing and importing the data rather than running the required procedure. Ensuring a common data format would significantly increase the efficiency gains to be had through the use of technology – thereby driving audit and client team engagement.
- Not all systems will have the same depth of information captured which indicates the need for a scalable system. However, the starting point needs to capture sufficient information to achieve real value from the outputs. Therefore, the suggestion that a common data standard be narrowly scoped needs to be considered in this light.
- Care must be taken that limiting scope is not to the detriment of the proposition of the use of data analytics.

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10. Do you agree that threats to auditor independence may arise through the provision of wider business insights (not as part of the audit itself) drawn from the interrogation company data? If so, what measures would mitigate this risk from crystallising?

- If, in the course of the audit, the auditor obtains information that the client may find helpful in managing the company's affairs it is appropriate that the auditor shares this with the client. It is up to the client to decide whether the information is useful or not.
- Engagement as an auditor for an entity does not require, nor should it require, the analysis or consideration of data outside that required to support the audit opinion. That said, the increasing scope of audit requirements means that more information will come within the auditor's purview.
- Obviously, the auditor needs to act within the terms of the engagement, and wider audit standards, and sharing data found as part of this should not be forbidden, neither should it threaten independence.
- In the discussion paper reference was made to various learning models that rely on a "hands off" iterative data model which would come up with unspecified relationships or points. These models require constant input of transactional, up to date data, in order to function.
- Such an approach would not address specific audit requirements, neither would the data required be naturally available to the auditor until such time that "real time auditing" becomes the norm. As and when we move to continuous auditing, with real time interrogation of client data, any use of this "hands off" approach may well bring with it ethical challenges that could require some form of regulation.

11. Do you agree that audit documentation can be more challenging when an audit has been conducted with automated tools and techniques? If so, please identify specific areas where is a problem.

- The response very much depends on the tool and technique being utilised. Info, for example, includes the automated generation of working papers once audit work has been completed such that a full audit trail of the data ingestion, sample selection, and testing performed are fully documented in a consistent, firm (and regulator) approved format.
- The use of tools for data analytics that do not have a defined audit trail, such as Microsoft Excel, will always carry a greater degree of risk in terms of audit documentation as assumptions used and formulae can inadvertently or deliberately be altered inappropriately which is hard for the reviewer to ascertain without following a comprehensive process.
- Without following a comprehensive, independent validation process therefore what initially looks like a simple and easy solution can be fraught with unappreciated danger.
- A well designed, and clearly scoped, audit tool should be able to produce clear, unambiguous documentation on the test parameters used and results obtained.
- Whilst a number of tools for bespoke testing do have a trail, sometimes this is not user friendly, which can lead either to misunderstanding or lack of confidence in the use of the tool.
- A point should also be raised in respect of what needs to be documented. For example, if a "common" technique is detailed in a firm's audit methodology such that the underlying logic and process is understood then the audit file documentation need only include the outputs of said technique alongside the audit team's conclusion thereon without needing to explain how the technique provides assurance over the selected assertions.

12. Have you encountered challenges in dealing with the volume of 'exceptions' arising from the use of more complex or comprehensive data analytic procedures?

- We find that in practice you only get a large number of "exceptions" when there is a lack of audit team understanding over how a particular process or system works. Once the team have a more detailed

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12. (continued)

understanding, they are able to target their testing more effectively and the resultant level of “exceptions” is rarely a significant number.

- Basic data analytic procedures can throw up a very large number of exceptions, well designed more complex or comprehensive procedures allied to the requisite understanding usually do not, except in cases where the client has very basic data capture. However, over time the level of detail captured by financial systems has expanded primarily due to client demands of technology providers, and we foresee this being extended as auditors and users of accounts require greater levels of transparency.

13. Do you agree that the use of third-party technology vendors raises potential ethical challenges for auditors and, if so, which potential safeguards would you see as effective in reducing this threat to an acceptable level?

- In principle, this should, ethically, be no different to the use of an auditor’s expert, save for the volume of data being shared.
- Ethical challenges are inevitably greater when using a tool that includes data extraction and storage facilities, such as InFlo, which are hosted and maintained by third parties. “Simple” software tools such as IDEA which reside as a local installation on an auditor’s laptop don’t present such ethical concerns as this is effectively a tool entirely under the control of the auditor.
- When using third party vendors, provided a client has a chance to consider the vendor’s terms and conditions, and undertake their own evaluation then the risks are reduced.
- Use of third-party technology obviously involves data transmission and clients are used to sharing data through a variety of portals some of which are bespoke to the auditor, but many of these portals are tried and tested commercial applications. Any third-party technology provider needs to illustrate that they meet the appropriate encryption and other security standards.

14. Do you agree that the increasing usage of third-party providers presents challenges in audit documentation and, where relevant, how have you dealt with this?

- Our answer to this is very similar to our answer to question 11 above.
- A well-structured application will provide clear documentation and audit trail of the work done and, in a way that you could audit it on a different tool either of a bespoke nature, or from another supplier. However, to do this in every case cannot be sensible.
- It may be sensible to differentiate between new products and existing, well tried and tested technology with certain applications having a certification for their standard processes based on specific criteria.
- If the system does a matching of opening to closing trial balance through the total transaction data, then results of certain tests will meet the certification. Without this, individual firms must complete their own due diligence along these lines – but should not be expected to do this on every assignment.