



# Maximising the benefit from your AIM advisors

## auditors & accountants

**In the fifth instalment of our series on AIM advisors, Barry Gamble explains how to make the most of your auditors and accountants**

“The best audits are done with people rather than to people,” are the words used by a leading accounting firm to sum up their approach. While some AIM boards might see the audit as a necessary evil that does not really contribute to shareholder value, the auditors provide the validation of published financial statements and other documents on which shareholders – the owners of the business – are entitled to place reliance.

Following the massive growth in the size of auditing firms, it is all too easy to overlook the scale of consolidation that has occurred within the accounting profession over the last decade. The consequence of this consolidation has been, in some respects, to ‘commoditise’ the offering. Following the number of corporate collapses and governance failures of recent years and the credit crunch we now face, a change in attitude to auditors just may be taking place. After seeing the introduction of the prescriptive Sarbanes-Oxley regime in the USA, it is salutary that we may be on the brink of a more regulated corporate environment here in the UK. More rigorous adherence

to existing codes and practices through more proactive engagement with the company’s auditors might be a more attractive option for AIM board directors.

A number of audit partners interviewed considered that many AIM companies could help the auditors more and, at the same time, help themselves. Skilled auditors position the directors so they become well aware of their obligations. Experienced boards work this out for themselves and set out to operate in an altogether more co-operative fashion, recognising the value of the role auditors undertake.

Not every AIM company needs the annual audit to be conducted by one of the top four firms, seen by some as billion-pound behemoths. Some of these firms are well-positioned to service AIM clients through specialist departments but there may be some hidden gems in the next tier down, which encompasses firms ranging in overall size from £50 to £500 million of fee income.

Auditors are required to report to the members of the company – the shareholders. In practice, this is achieved

through the shareholders’ agent – the board. So as with other AIM advisors, the effectiveness of the auditors depends to some degree upon the quality of the relationship between the auditors and the board – firstly, that between the executive directors, principally the finance director; and secondly, the relationship with the chairman of the audit committee. Management and auditors can both be subject to criticism that the relationship is too close, but without good empathy between the parties, the relationship may become stilted and even antagonistic. There are clearly times when the auditors might ask tough questions of management but hopefully, this will not be in default mode.

The auditors should recognise the importance of their planning, organisation, communication and approach in helping the company achieve ease of compliance. Lack of anticipation of the impact of changes can be particularly disruptive to company management. But of the chief financial officers on AIM – who may have limited resources – few consider audits as anything other than difficult

to achieve well. “Many AIM boards will have struggled with the implementation of IFRS – and not least through the sheer volume of disclosure now required in financial statements we now see,” notes audit partner Mark Harwood of Baker Tilly. Analysts may still tend to restate IFRS figures into EBITDA measures but at least the base data is now consistent across international markets – important for many AIM companies.

Directors should recognise that they and they alone have the responsibility for the maintenance of proper accounting records and diligent preparation of the financial statements. Boards should at no time fall into the trap of blaming the auditors if the accounting approach adopted or disclosures made fall short of what is required. Auditors may have difficulty communicating the increasing risk of a referral to the Financial Reporting Council. The financial director has a key responsibility here to ensure all members of the board fully understand their obligations in the preparation of the financial statements and facilitating the audit thereof. This emphasis resonates with the view of leading audit practitioners. “You cannot understand the organisation if you do not understand the board. Audit the board and it will tell you much of what you need to know,” is the refreshing philosophy of Mike Bishop, audit director of Smith & Williamson, who has responsibility for a number of AIM clients.

Good audit planning is essential to a smooth audit process. Company management should be thoroughly briefed on the impact of new accounting standards, changes in company law, and disclosure best practice. Requesting the auditors to undertake a review of the interim figures can be a good point at which to consider the impact of issues at the year end. It is never too early to mock up the year end statutory accounts to help this process. As well as company specific issues, there will often be more generic matters to consider in the planning process. Currently, these might well include banking covenants and renewal of facilities, as well as asset impairment – particularly intangibles.

The audit committee is now well engrained as a key board committee. Chaired by a non-executive director, it offers a level of oversight and detachment, a review of the corporate risk framework and often, the opportunity to consider

### Top tips:

- 1 Directors need to understand their responsibilities
- 2 Choose auditors who are appropriate to the size and needs of the AIM company
- 3 Be prepared to review the auditors periodically and consider inviting tender proposals
- 4 Develop an open and fully transparent relationship with the company's auditors
- 5 Brief auditors on key business changes and plans
- 6 Thoroughly plan the preparation of financial statements and audit process interface
- 7 Seek early warning on new accounting/ disclosure standards, practices and approach
- 8 A properly constituted audit committee will add value for directors and auditors
- 9 Use the annual report as a means of communicating corporate ethic and values

issues afresh. It is important that the audit committee fully explores its remit, so as to engage with external and internal audit alongside the executive directors. It must be prepared to go anywhere in the company to find the answers to questions. So often, these processes can be truly revealing of corporate ethic and values.

In this respect, the auditors' responsibility to ensure the statements in the annual report pass scrutiny is an important element of the communication with shareholders. So much can be gleaned from the tone and completeness of disclosure from these mostly narrative statements, not least in relation to corporate governance. Company boards and audit committees should also recognise that managing expectations as to timing of announcements is an important contributor to the trust and confidence built with shareholders.

“An audit committee that is properly engaged will help ensure a constructive and challenging audit that remains focused on shareholder interests,” says Stuart Barnsdall, audit partner at PKF. “Although the governance requirements for AIM companies are lighter than for a listed company, the accounting requirements are the same so it is important not to underestimate what is needed to achieve proper compliance.”

Governance best practice encourages a periodic review of auditors. Many things change in business over time – directors, staff, operational facilities, systems, customers and suppliers. As such, the needs of the business will likely change, so moving to a new firm of auditors may well bring a number of benefits. The process of putting the audit out to tender will often be quite illuminating. Different firms will vary the emphasis they place on audit approach. Timescales and cost proposals, for example, may all be markedly different. Boards may perceive the offering of the accounting firms to be broadly similar for a function framed by statute but the challenge for the audit firms is to provide some degree of differentiation.

The role of the reporting accountant will usually, but not necessarily, be undertaken by the incumbent firm of auditors. Due diligence for mergers and acquisitions, prospectus fundraisings, specialist reports to lenders and investigations into problem divisions can all be included within this remit. The approach will be tailored to the agreed brief. Here again, well-organised management will be able to save time, control costs and steer the process through good systems, good communications and clarity of purpose with a realistic timetable for delivery. If the ‘heavy lifting’ can be ahead of input from the reporting accountant, a much more efficient process will ensue.

As we have seen so far in this series, AIM boards should seek to develop a strong, open and trusting relationship with their advisors. The relationship with the auditors should be no different in character. ■

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