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**ACHIEVING BETTER PROCESS
AND RESULTS WITH
CENTRALIZED
CONFIRMATIONS**

ACHIEVING BETTER PROCESS AND RESULTS WITH CENTRALIZED CONFIRMATIONS

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ACHIEVING BETTER PROCESS AND RESULTS WITH CENTRALIZED CONFIRMATIONS

Successful accounting firms that embrace change typically operate in a paperless environment and use technology tools to streamline workflow. Yet for decades, the process for managing audit confirmations in most firms has not changed. Findings from recent firm interviews reveal firms are now moving leaders to challenge the status quo of their current confirmation process and seek ways to improve the process – all in an effort to reduce costs while enhancing quality and fraud protection.

The purpose of this paper is to propose a key champion to improve the management and confirmation process – namely, centralized confirmations. Included in the discussion are the challenges in making a transition to centralized confirmations, what confirmation procedures are being shifted, and those that are not.

Specifically, this paper covers:



Current confirmation process steps



Pitfalls of current approach



Advantages of centralization

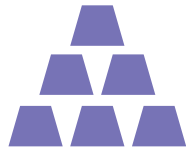
- Cost reduction
- Productivity improvement
- Quality improvement
- Scalability



Approaches to centralization



Implementing a centralized confirmation process



CURRENT CONFIRMATION PROCESS STEPS

The following table outlines the primary steps and associated tasks in the traditional confirmation process:

PRIMARY STEP	TASKS
Confirmation Assembly	<p>Obtain from client:</p> <ul style="list-style-type: none"> • Composition detail of balance sheet accounts • Determine accounts to be confirmed based on risk assessment and auditor judgment <p>Prepare confirmations:</p> <ul style="list-style-type: none"> • Identify correct confirmation template • Coordinate with client populating templates for each confirmation • Print each confirmation and have client sign all • Create confirmation log
Confirmation Mailing – 1st Request	<ul style="list-style-type: none"> • Review completeness of confirmations • Address and stuff envelopes for each recipient including return envelope with CPA firm's address • Update confirmation control log • Mail confirmations
Confirmation Receipt	<ul style="list-style-type: none"> • Distribute returned confirmations to one of the following: <ul style="list-style-type: none"> ◦ Client mail folder ◦ Staff folder assigned to client • Log receipt on confirmation control log • Place the confirmation in workpaper file
Address Exceptions	<ul style="list-style-type: none"> • Review the nature of the exception • Send exception to the client for resolution • Place the confirmation in the workpaper file • Note the exception on the confirmation log
Confirmation Mailing – 2nd and 3rd Requests	<ul style="list-style-type: none"> • Insert confirmations and return envelopes in envelopes • Update confirmation control log • Mail second confirmation requests • Complete "Confirmation Receipt" steps for second requests
Action Steps on Non-replies	<ul style="list-style-type: none"> • Perform alternative procedures for non-replies • Update confirmation control log

Costs

Confirmation processes organized in this traditional manner are inefficient, inconsistent and costly. These issues are magnified by the number of audits a firm conducts – yet most firms do not estimate time for the confirmation process or the cost per confirmation. Time is money, and if these routine tasks are performed manually by multiple staff assigned to a particular audit or by staff not associated with the audit, the cost of the audit is unnecessarily increased.



PITFALLS OF CURRENT APPROACH

Pitfall 1: Process inconsistency

Each audit team typically manages the confirmation process for each audit client. The common goal of each team is as follows:

- ① Send the confirmation requests
- ② Receive and log the confirmations
- ③ Place any documents in the file to support the audit

Despite the common goal, there is little process consistency in the management of a decentralized system. This results in excess time and effort being spent on an audit procedure that is relatively straightforward and could be systematized.

Pitfall 2: Poor direction

The senior auditor assumes overall responsibility to ensure confirmations are sent and returned from the third party. This person generally delegates these tasks to less experienced staff auditors with limited instructions, leaving staff auditors to devise their own methods to complete tasks.

Pitfall 3: Confirmation cost is greater than anticipated

Most firms require a time budget of some sort for each audit engagement. The extent of detail within the time budget varies widely across firms. Some firms base their budget by total hours for the engagement, while others budget hours by audit section. Firms generally do not create a budget for specific confirmation procedures and therefore don't know the overall cost of this process. Typically, the cost of the confirmation process is much greater than most firms realize. Research into the average cost of the process is \$70* per manual confirmation and because of inconsistency, varies depending on staff bill rates and the amount of follow-up work needed to address lost or inaccurate confirmations.

Pitfall 4: Duplication of effort

Lastly, the timing of receipt of the confirmation contributes to additional work and results in delays to the delivery of the audit report and financial statements. Often during fieldwork, expecting that a confirmation will not be returned, the audit team makes a decision to perform alternative procedures. These pitfalls can be remedied with a fresh look at the confirmation process.

* NEED THE COPY FOR THIS FOOTNOTE



ADVANTAGES OF CENTRALIZATION

Firms interviewed about their confirmation process indicated they recognize some benefit to centralization. They also acknowledged centralization would help better organize the process and reduce cost. However, the benefits are far beyond just cost. As Mauldin and Jenkins stated “[The value] is more the intangible because they like the accuracy. Who is getting it? [Is it the] right people? [It helps] reduce fraud and [improve] timeliness.”

Centralization of the confirmation process does present an opportunity to dramatically improve the entire process. Here are four reasons to centralize the confirmation process across all offices:

① Cost reduction

The most significant driver to move a firm to a centralized confirmation model is cost reduction. Moving confirmation functions into a centralized operating model typically saves 25 to 40 percent over the traditional model. Savings are realized through the centralization, standardization, simplification and automation of confirmation activities. Assigning confirmation tasks to salaried administrative staff trained in the systems eliminates the need to manage resourcing peaks and reduces salary costs.

② Productivity improvement

In a centralized confirmation process, audit teams know who is assigned to perform routine confirmation tasks, and this eliminates process inconsistencies and drives improved audit metrics. Individual auditors spend significantly less time organizing each set of audit confirmations. Confirmations are sent out earlier in the audit process and followed up as a matter of routine by administrative personnel, reducing the need for alternative procedures.

③ Enhanced quality

Since professional standards consider direct third-party verification as high-quality audit evidence, it is important to receive the majority of confirmations in a timely manner. A centralized confirmation process improves the timeliness, response rate, logging, follow-up and need for alternative, less high-quality procedures. Quality is further enhanced because trained administrative personnel who specialize in the confirmation process are better at identifying potential problems, such as unusual names or addresses.

④ Scalability

Centralizing confirmation processes inherently absorbs changes in the firm, including new audit engagements, mergers and staff turnover. A centralized capability allows a firm to expand and contract its scale and scope of confirmations swiftly and without significant increase in associated costs. Centralizing confirmation processes is scalable and can be deployed in any size firm. It is simply a matter of whether this operation is the full- or part-time effort of one or more administrative staff in the firm.



APPROACHES TO CENTRALIZATION

Establishing the right centralized operating model for the confirmation process starts with defining the following:

- ① What are the activities underpinning this process?
- ② Where within the firm should they reside?

In general, confirmation processes and activities are mechanical in nature and/or repetitive so they can be systematized and appropriately handled from a centralized location within the firm by administrative personnel. Use the following five key questions to make the decision to centralize:

KEY QUESTIONS	YES	NO
1 Do the confirmation processes technologically align with the other audit processes?		
2 Do the confirmation processes minimize cost while maximizing productivity, quality and scalability?		
3 Does the current confirmation process enhance the quality of the audit?		
4 Do you know the current average cost of a confirmation and what operational opportunities are available to reduce this cost?		
5 Are there resources available in the administrative team to handle centralized confirmation processes?		

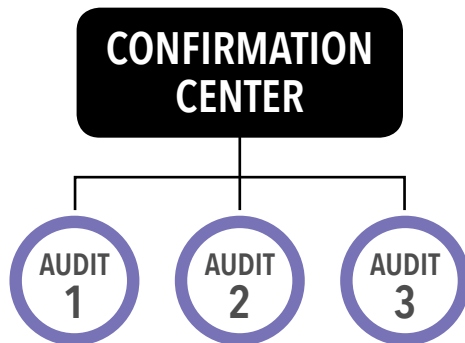
If the answer to 1, 2 or 3 are “no,” consider centralization. If the answers to 4 or 5 are no, find out the answers prior to considering centralization. This will ensure resources are available either internally or through a third party. Comparable estimated costs and targets are available to measure success, prepare future budgets, and optionally negotiate services with outside businesses.

The two centralization models are: 1. Direct Control Model and 2. Hub and Spoke Model

Under the Direct Control method, the Confirmation Center takes the lead in initiating the confirmation process for all audits. Under the Hub and Spoke Model, the audit team initiates the confirmation process and directs the Confirmation Center to commence these activities.

Direct Control Model

The following is an example of the Direct Control Model of centralization:



OVERVIEW

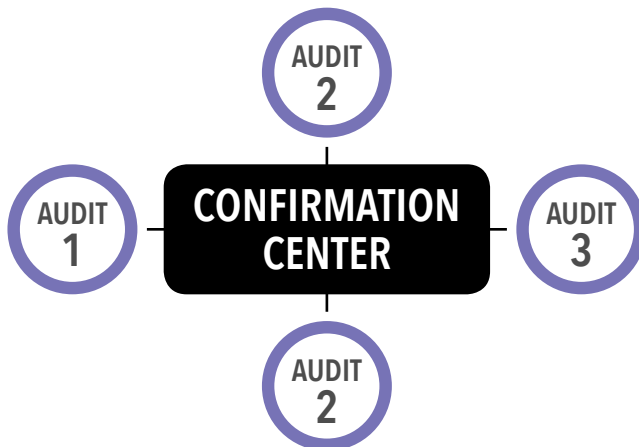
- Confirmation Center directs confirmation activities.
- Center keeps the audit file updated with confirmations sent.
- Center contacts client for name, address, and other information.
- Follow up with audit team to obtain confirmation selections (when sampling is being used, for example).

The Direct Control method allows the Confirmation Center to organize the entire process and assist in the smooth operation of the overall confirmation workflow across the firm.

See Appendix A - Centralization Models for complete Direct Control Model diagram.

Hub and Spoke Model

The following is an example of the Hub and Spoke model of centralization:



OVERVIEW

- Audit team initiates the confirmation process.
- Audit team instructs "Confirmation Center" to send confirmations.
- Primary client contact for the confirmation process is the audit team.
- Center places returned confirmations in the file and informs audit team when a confirmation identifies a difference.

See Appendix A - Centralization Models for complete Hub and Spoke Model diagram.

The Hub and Spoke approach is effective when the audit team proactively leads and initiates the confirmation process. Although this approach requires less culture change, it can result in an uneven workflow in the Confirmation Center.

Enhance the confirmation process with a third-party provider

In the case of both models, utilizing a third-party provider is a valid option to consider. By combining the services of a firm with an outside vendor to carry out the confirmation process, it creates a process that allows the firm to maintain control of the process and initiate all confirmation activities while supplementing and simplifying their workflow management needs. Employing a third party can fill the internal expertise gaps without spending the time, money and effort to add staff.

Consider the following when evaluating outside vendors:

- Identify third-party provider known for supporting firms in the confirmation process.
- Understand the relationship is based on support and cooperation.
- Know that overall responsibility for confirmation activities remains with the firm.
- Ensure providers undergo SOC 1, SOC 2, and SOC 3 examinations.

Knowledge of the client is retained within the firm with access to real-time, precise information on the progress of all confirmations in process from the third party. This access gives the Confirmation Center the ability to take timely corrective actions as needed.

Added Recommendations

Centralized process models have been successfully used for internal operating areas such as the information technology and human resources departments. There is also value in implementing centralized models in the audit process, including the confirmation process. Centralized confirmation processes can support cost reduction, productivity and quality improvements, and can be scaled to fit the size of the firm.

The most difficult challenge when transitioning to a centralized process is the need to change firm culture. Because the change is mandatory and no longer an option, management must ensure that all staff is aware of the benefits and that there is appropriate communication during the transition. To alleviate the resistance to change, it is important to delineate, document and communicate the change to staff as well as provide any necessary training and support of the new system.

Firms are encouraged to consider this fundamental opportunity to align with other technological innovations that are being utilized in the audit process. Leading firms aim to better manage audit risk more effectively and drive down cost. While recognizing that there are challenges in defining the right centralization model, the tide is definitely turning. Firms are increasingly asking “when and how” they can make this move – not “if.”



IMPLEMENTING A CENTRALIZED CONFIRMATION PROCESS: ADDITIONAL RESOURCES

The following resources are provided to help with a smooth implementation process:

Appendix A – Centralization Models

Appendix B – Steps to change the process

Appendix C – Frequently asked questions

Appendix D – Cost Toolkit (Web download) [\[NEED WEB LINK\]](#)

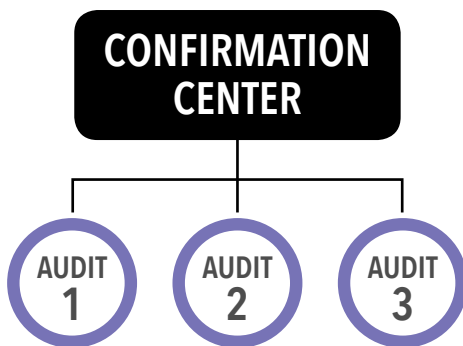
Appendix E – Process Steps (Web download) [\[NEED WEB LINK\]](#)

CENTRALIZATION MODELS



DIRECT CONTROL MODEL

The Direct Control method allows the centralized confirmation process through the Confirmation Center to organize the entire process and assist in the smooth operation of the overall confirmation workflow across the firm.



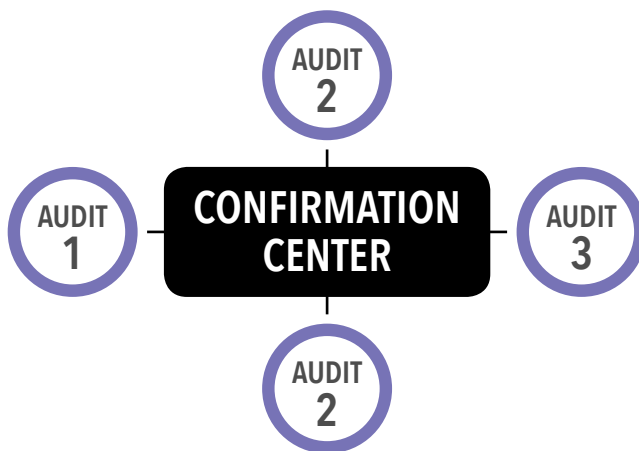
OVERVIEW

- Confirmation Center directs confirmation activities.
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- Follow up with audit team to obtain confirmation selections (when sampling is being used, for example).



HUB AND SPOKE MODEL

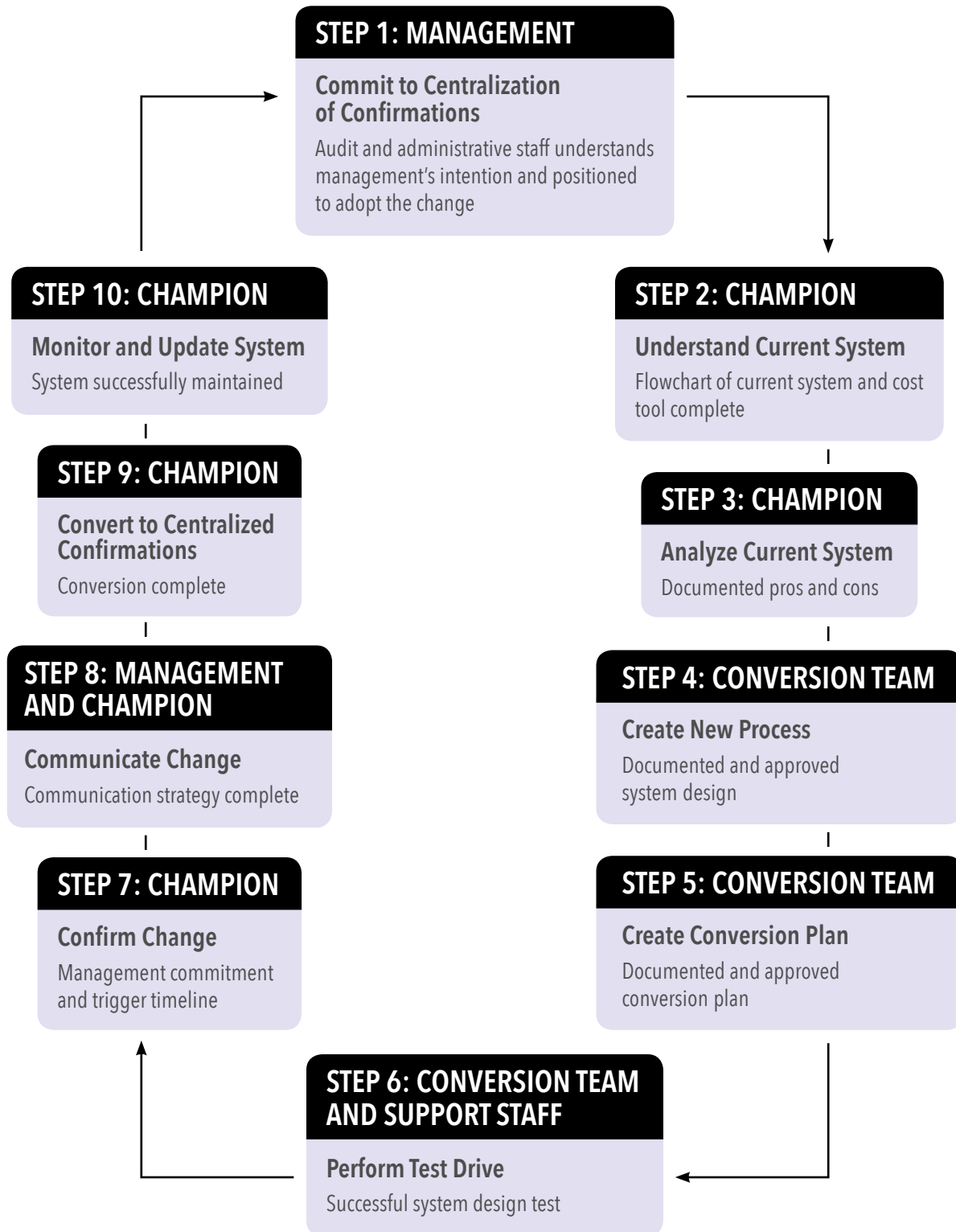
The Hub and Spoke method is effective when the audit team proactively leads and initiates the confirmation process, but can result in uneven workflow in the confirmation center.



OVERVIEW

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OVERALL STEPS IN THE PROCESS CHANGE





FREQUENTLY ASKED QUESTIONS OF MANAGEMENT

Q: Which department best handles the confirmation process?

A: Usually, it's an administrative person or group.

Q: Are we centralizing electronic and paper confirmations?

A: Yes. Both.

Q: Are administrative staff required to be independent of the client if they are involved in the process?

A: The team needs to be independent.

Q: Can we centralize electronic and paper confirmations and use a third-party provider, such as Confirmation.com?

A: Yes. Confirmation.com can be used for confirmations that are emailed, mailed and/or sent online.

Q: What happens when the responsible staff person is on vacation or ill?

A: Add a back up or cross training option in the toolkit.

Q: Is the firm the appropriate size and have the current staff to benefit from a centralized confirmation process?

A: It's more about whether a centralized confirmation process is one person's full-time job or a portion of their job. It depends on how many audits the firm handles. No matter what, it is more efficient and effective to centralize.

Q: How will the administrative staff be trained?

A: The champion can do the training. Combining this eBook with detailed, specific procedures would help.

Q: How will the process be routinely monitored for effectiveness and efficiency?

A: Following busy season, hold a debriefing on what worked, what didn't, and make process improvement changes as needed.

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