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Preparing for the first-time audit

Five considerations for emerging growth companies

For an emerging growth company (EGC), an independent financial statement audit may be the farthest thing from management's mind. All eyes are on raising capital, generating revenue, and scaling the business.

Eventually, many companies will reach an inflection point when an audit is called for. Often that happens when they take on outside investment—be it a bank loan, venture capital equity, or some other private investment vehicle—and an audit is part of the terms. Other times, the inflection point happens when the company reaches "critical mass," prompting founders and their advisers to think about laying the groundwork for the next stage of development—even a potential initial public offering or other exit strategy.

Either way, an accurate and transparent first-time audit of the company's financial statements, representing the company's official adoption of US generally accepted accounting principles (GAAP), is imperative. There are steps companies can take to help their first audit go as smoothly as possible.

1. Secure commitment from senior management
2. Use the EGC Knowledge Share tool
3. Organize accounting records and identify complexities
4. Know the different roles in an audit
5. Know the indicators of an effective first audit

1 Secure commitment from senior management

As a compliance exercise, an audit might invoke a different sense of urgency than tasks more closely tied to building the business. But it is important, particularly when lenders or investors are counting on it. Thus, ensure the audit is high on the agenda of key stakeholders in management.

2 Use the EGC Knowledge Share tool

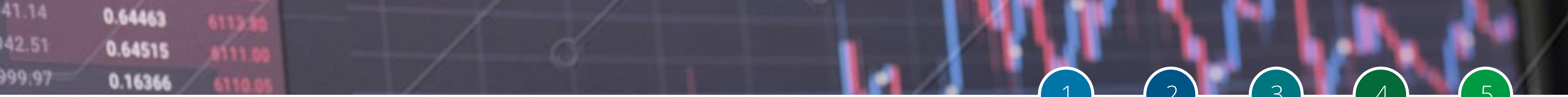
Save time and simplify data sharing in EGC audits with Deloitte's new tool, EGC Knowledge Share. Guided by your client coordinator, the tool conveniently enhances the efficiency of audit inquiries and neatly organizes the information in one place for everyone's access.

Watch the video about our new EGC Knowledge Share tool on the *Preparing for your first-time audit* Deloitte.com page >

3 Organize accounting records and identify complexities

For many EGCs without a finance or accounting department, the audit process may require more than collecting relevant records. It's essential to start maintaining these records in advance, ensuring a well-prepared and efficient audit.

Early identification of common accounting complexities for EGCs, such as revenue recognition, equity transactions, software development costs, and the presentation of gross margin, is crucial. These are often discovered during step 2 (EGC Knowledge Share).



4 Know the different roles in an audit

Understand how and who to engage for success:

- **Hands-on engagement** – GAAP accounting rules can be highly nuanced, requiring significant technical knowledge and judgment. Current audit preparation and reporting experience is essential. Ensure that at least one person knows GAAP and how it applies to the company.
- **Create bandwidth** – Employees can be responsible for financial reporting and other areas (facilities, HR, and IT systems). An audit can take a nontrivial amount of time, so create bandwidth for those supporting it.
- **Owning the results** – Stakeholders may need guidance on the areas of risk or other critical insights identified in the audit. They may also have questions about the business, the audit, and GAAP. If the audit reveals opportunities for improvement, the company should be able to carry them out. For all these reasons, someone within the company should take charge of the audit's conclusions.

5 Know the indicators of an effective first audit

Three outcomes are desirable:

1. Pre-audit planning, or "whiteboarding," in which the audit team (internal) and auditors (external) dive deep into the financial accounting practices of the company— transaction cycle by transaction cycle, area by area.
2. Meeting all deadlines and commitments as the audit process unfolds.
3. A good working relationship between the audit team and auditors at the end of the process.

Let the journey begin

An independent financial statement audit represents a significant advancement in the maturity level of an emerging growth company. At the same time, it also creates an expectation among the company's senior management, advisers, lenders, and investors that the audit process will repeat year after year.

The upshot is that financial statement audits are seldom "one and done." Instead, they are a commitment that requires an ongoing investment of time, resources, and labor. Through this investment, EGCs often experience improvements in many areas including record retention and segregation of responsibilities. By following these tips, growth companies may position themselves for a successful first audit and the ability to take on the demands of an effective ongoing audit process.

Contacts

Heather Gates
Managing Director
Deloitte Private
Enterprises and National
EGC Practice Leader
Deloitte & Touche LLP
hgates@deloitte.com
LinkedIn >

Bill Carey
Audit & Assurance Partner
GTS EGC Leader
Deloitte & Touche LLP
wcarey@deloitte.com
LinkedIn >

Deloitte.