Canadian Public Accountability Board
Conseil canadien sur la reddition de comptes

MARCH 2020

2019 ANNUAL REPORT

Reinforcing public confidence in Canada's capital markets

CPAB-CCRC.ca

Our Vision

The Canadian Public Accountability Board (CPAB) is a leading audit regulator that reinforces public confidence in Canada's capital markets.

Our Mission

CPAB promotes sustainable audit quality through proactive regulatory oversight, facilitating dialogue with domestic and international stakeholders, and publishing practicable insights to inform capital market participants.

Our Strategic Commitments

One

Cultivate a proactive, adaptive and innovative culture that elevates our regulatory effectiveness.

Two

Drive targeted, systemic changes to accelerate audit quality improvements.

Three

Impact how the future audit is performed and regulated.

Four

Influence global audit quality consistency.

Contents

A message from Benita Warmbold, Chair

In 2019, it was my honor to accept the role of Chair of CPAB. I would like to thank Nick Le Pan for his enormous contribution to the organization. As CPAB's former Chair, Nick's relentless pursuit of better-quality audits, regulatory effectiveness and continuous improvement spanned 11 years, significantly impacting how we think about audit regulation in Canada and around the world.

A core value proposition of the audit profession is that statutory audits enhance confidence in the reliability of corporate reporting, contributing to financial stability. That value is predicated on the public's trust in auditors to perform high quality audits. As this country's public accounting firm regulator, improving the integrity and reliability of Canada's audits is our first priority.

In 2019 CPAB launched its 2019-21 strategic plan; early progress indicates leadership is advancing well in the execution of our four strategic commitments. The board's primary focus in 2019 was providing oversight of CPAB's management team in its delivery against the strategic and annual operating plan and of CPAB's enterprise risk management program. The board evaluated management's assessment of the impact of various issues on audit quality, and the potential implications for CPAB's mandate and risk profile. Key issues included innovation, technology, emerging industries, and audit firm culture and governance. In addition, we provided oversight of management's new audit quality assessment model, and the successful integration of key senior leaders into new and transitioning roles.

CPAB advanced discussions regarding its approaches to regulatory innovation, transparency of inspection findings, and discipline and enforcement. The organization also continued to build the next generation of regulatory leadership, adding more diversity of thought and experience, and expanding capabilities in emerging and complex technologies and industries. These types of competencies will be critical for regulators of the future — developing that capacity continues as a top priority for CPAB.

Good governance requires effective board renewal and the CPAB board made progress on its director succession commitments. I would like to thank Jocelyn Proteau who retired this year for his exemplary service, particularly in his role as Vice Chair. This year we also welcomed new directors Sheila Fraser, Kevin Kelly and Renaud Caron who bring deep expertise from the government, financial institution and technology sectors and reflect our skills-based approach to renewal — with a focus on gender, geographic and professional diversity.

Finally, a sincere thank you to my board colleagues and the CPAB management team and staff for their contributions to driving our strategy forward and continued dedication to enhancing audit quality in Canada.

B Warmbold

Benita Warmbold, FCPA, FCA
Chair

A message from Carol Paradine, CEO

CPAB has been intently focused on steps that can be taken to encourage high quality audits and heighten awareness of the role that all stakeholders play in strengthening investor confidence in Canada's capital markets.

As I reflect on the past year and look forward to 2020, it's hard not to consider events in other parts of the world, and in particular several studies, reports and regulatory changes to the auditing landscape in the UK, the Netherlands and Australia. All of these developments are relevant to our activities in Canada; each one exploring ways to enhance confidence in financial reporting and auditing – the fundamental purpose of a quality audit.

Our assessment program is at the centre of what we do. Fundamental to our regulatory effectiveness, it combines risk-based individual audit engagement file inspections with broader, more holistic evaluations of firmwide quality management systems to identify gaps and good practices in the work of external auditors. In CPAB's view, greater attention to strong, centralized firm quality management systems helps firms deliver more consistent quality audits. Our assessments of these systems at the country's four largest public accounting firms are intended to improve firm leadership's focus on risk management practices. In 2019 these firms made significant strides in improving their quality management systems and I am pleased with the progress to date.

The overall inspection results for 2019 were disappointing and in many instances much greater attention to audit quality is needed. This year, the crypto-asset and cannabis industries have been a challenge for many auditors. While we saw some progress in inspection results in traditional industries, auditors still struggle to adapt to emerging business models and novel scenarios. CPAB published a second report on risks identified in crypto-asset sector audits based on our inspections findings.

We are seeing increased stakeholder focus on whether auditors are doing enough to detect fraud and identify and report on companies at risk of insolvency — two other areas with significant potential impact on the investing public. Our review of auditors' response to fraud and going concern standards this year told us that, overall, their work is compliant. However, while there are examples of good practices, areas for improvement exist.

In 2019 we made important progress in gaining access to audit work in foreign jurisdictions. The Canadian Securities Administrators' (CSA) proposed amendments will enhance CPAB's access, and better protect the interests of the investing public in Canada while not unduly increasing the efforts of audit firms, reporting issuers or regulators. We look forward to coordinating with the CSA on implementing changes in 2020.

Looking ahead, CPAB will advance our firm audit quality management systems assessments across the large public accounting firms. We also strongly encourage all firms to meet a target of 10 per cent or fewer files with significant findings no later than 2021. We'll continue to provide our perspectives on the benefits, challenges and risks created by the growing use of new technological tools and by reporting issuers operating in new and emerging industries.

Finally, a very sincere thank you to the CPAB board of directors for its overall guidance on our strategic direction and the entire CPAB staff for their enormous contributions to the successful execution of our 2019 operating plan — I look forward to all we will achieve in our pursuit of higher quality audits in 2020.

Carol Paradine, CPA, CA
Chief Executive Officer

CPAB Leadership Team

Carol Paradine
Chief Executive Officer

Jennifer Cooper
Senior Director, Discipline & Enforcement

Malcolm Gilmour
Vice President, Inspections

Kristina Heese
General Counsel & Corporate Secretary

Adrienne Jackson
Senior Director, Communications

Jeremy Justin
Chief Risk Officer and Vice President, Strategy

Margo Longwell
Senior Director, Quality, Firm Risk and Registration

M. Philippe Thieren
Regional Vice President Eastern Canada and CFO

Lily Watson
Director, Talent

CPAB Board of Directors

Benita M. Warmbold
Chair,
Toronto, Ontario

Sheryl Kennedy
Vice Chair
Toronto, Ontario

Ian Bourne[2]
Calgary, Alberta

Renaud Caron[2]
Montreal, Quebec

Julie Dickson[1]
Ottawa, Ontario

Sheila Fraser[2]
Ottawa, Ontario

Guy Frechette[1]
Montreal, Quebec

Bruce C. Jenkins[1]
Toronto, Ontario

Kevin Kelly[1]
Toronto, Ontario

Alice Laberge[2]
Vancouver, British Columbia

1 Member of the Risk and Audit Committee
2 Member of the Human Resources and Governance Committee

GOVERNANCE REPORT

Responsible corporate governance

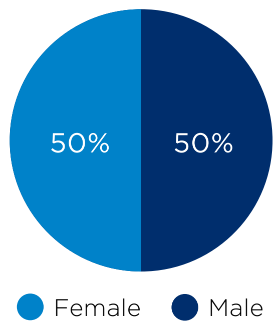
Responsible corporate governance is critical to CPAB's regulatory oversight mandate and to reinforcing public confidence in the integrity of financial reporting by public companies. This is reflected in our structure and operating practices.

The Board of Directors has overall responsibility for supervising the management of CPAB's activities and affairs. All Directors are appointed by CPAB's Council of Governors (see Member classes below for more detail). CPAB's Rules require that the board comprises a combination of professional accountant, non-accountant experience and audit oversight regulation and regulatory experience. The Council of Governors ensures these requirements and criteria are met in appointing board members and seeks diversity of expertise and industry experience as well as geographical and gender representation.

While CPAB is not subject to any legislative or legal obligations to set gender targets, the board takes gender representation into account in recommending the composition of its membership to the Council of Governors and when filling executive positions. In 2019, five out of ten board members were women.

Benita Warmbold became Chair, Sheryl Kennedy became Vice Chair, and Sheila Fraser and Kevin Kelly became directors effective March 18, 2019. Renaud Caron was appointed to the board on August 28, 2019.

Board of Directors



Annual board meetings

Thirteen board and committee meetings and one strategic planning meeting were held during the fiscal year ended December 31, 2019.

	Board of Directors Meetings	Risk and Audit Committee Meetings	Human Resources and Governance Committee Meetings
Benita Warmbold*	5/5	3/3	4/4
Sheryl Kennedy*	5/5	4/4	3/3
Ian Bourne	5/5	N/A	4/4
Renaud Caron**	2/2	N/A	2/2
Julie Dickson	5/5	4/4	N/A
Sheila Fraser***	4/4	N/A	3/3
Guy Fréchette	5/5	4/4	N/A
Bruce C. Jenkins	5/5	4/4	N/A
Kevin Kelly***	4/4	3/3	N/A
Alice Laberge	5/5	N/A	4/4

* meetings attended as of role effective date
** joined CPAB board in August 2019
*** joined CPAB board in March 2019

Director compensation

In 2019, directors were compensated by a retainer of $48,000 and a per-meeting-attended fee of $1,500. The Chair of each Committee's annual retainer was $7,250. The Chair of the board's annual retainer is $175,000; the Chair does not receive meeting-attended fees.

Compensation of the directors and the Chair of the board is reviewed annually and adjusted from time to time based on analysis of peer group compensation and increases in inflation. In November 2019, on the recommendations provided by an external consultant based on a benchmarking analysis and assessment of CPAB's director compensation, the board increased director retainers to $50,000 and added a Vice Chair retainer of $7,500 per year, beginning in 2020.

Board committees

The board's two standing committees — Risk and Audit, and Human Resources and Governance — actively support the board's oversight of CPAB.

The Risk and Audit Committee assists the board in fulfilling its obligations and oversight responsibilities related to financial budgeting and reporting, the system of corporate controls and the external audit. It also provides guidance and oversees CPAB's activities and affairs related to risk management, including establishing risk tolerance and identifying and monitoring key risks and risk mitigation strategies.

The Human Resources and Governance Committee approves certain matters, and reviews and makes recommendations to the board on issues related to human resources, corporate governance, board composition and succession, the formation and membership of committees, the objectives, performance and compensation of CPAB's CEO and other officers, and the content and application of CPAB's Codes of Ethics. It also oversees the annual evaluation of the board, the Chair, and committees, and provides guidance and oversight of CPAB's talent management strategies.

Member classes

The Council of Governors has oversight responsibility for CPAB and appoints our directors annually, as well as the Chair and Vice Chair of CPAB's board. The Council is composed of the Chair of the Canadian Securities Administrators (CSA), the Chair of the Ontario Securities Commission, the Chair of the *Autorité des marchés financiers*, the Superintendent of Financial Institutions of Canada, a fifth Governor selected by the CSA, and a person selected by the other five Governors who is a professional accountant and has audit oversight regulatory experience. The Council carries out an annual assessment of CPAB's performance against our mandate in adherence with our governance practices.

The Provincial Audit Regulator Members (provincial audit regulators who oversee audit firms whose aggregate Canadian audit fee revenue from reporting issuers in a province is at least $7 million per provincial audit regulator) and the Council of Governors vote on any proposed amendments to CPAB's By-Law and receive our annual financial statements. The Provincial Audit Regulator Members appoint CPAB's external auditor.

Independence

Independence is critical to our role. CPAB has policies and procedures to minimize even the perception of potential conflicts. The positions of Chair of the board and CEO are separate, and the CEO is not a member of the board. Board members are independent and cannot have current positions or material relationships with audit firms regulated by CPAB. They must report any financial interests or other relationships that might affect or appear to affect their independence or objectivity, and generally do not receive any identifying information from management regarding participating firms or reporting issuers.

Our inspectors have significant technical auditing and accounting expertise, often gained at the large accounting firms. CPAB has in place comprehensive disqualification requirements with respect to which firms or reporting issuers an inspector may inspect and when. We prohibit CPAB inspectors from reviewing audits performed by a firm with which they were previously associated at any time during the ten preceding years. For a period of five years after joining CPAB, inspectors are also prohibited from participating in decision making that may have a material direct or indirect effect on such a firm.

CPAB's whistleblower hotline is available through our website to enable the anonymous reporting of matters related to CPAB, its employees, public accounting firms we inspect, or Canadian reporting issuers. The Ethics Hotline Whistleblower Policy protects any staff or consultant who reports through the hotline from retaliation.

STRATEGIC COMMITMENTS PROGRESS: DRIVING REGULATORY EFFECTIVENESS

STRATEGIC COMMITMENT 1

Cultivate a proactive, adaptive and innovative culture that elevates our regulatory effectiveness.

Highlights

- Delivered year one of a multi-year organization-wide learning curriculum, with a significant focus on emerging technologies.
- Commenced a comprehensive review and started to implement changes to our enforcement and discipline mechanisms.
- New Learning and Innovation Leader introduced to enhance experiential learning and innovation program.

STRATEGIC COMMITMENT 2

Drive targeted, systemic changes to accelerate audit quality improvements.

Highlights

- Full implementation of quality management systems assessments at Canada's four largest public accounting firms.
- Met with more than 180 reporting issuer audit committee chairs across a range of market capitalization and industries.
- Coordinated seven industry forums and co-hosted 2019 Canadian Audit Quality Roundtable with the Office of the Superintendent of Financial Institutions.
- Advanced investor outreach.

STRATEGIC COMMITMENT 3

Impact how the future audit is performed and regulated.

Highlights

- Implemented technology action plan: hired additional IT expertise, reviewed audit firm cyber-risk preparedness and began assessment of new technology tools being implemented by audit firms.
- Engaged with key stakeholders to explore recommendations with respect to key topics such as transparency and CPAB's regulatory effectiveness.
- Advanced efforts to gain access to working papers for audits performed on Canadian-listed companies with operations outside of Canada. (For a detailed list of jurisdictions where CPAB is unable to access working papers, please visit www.cpab-ccrc.ca).
- Required audit firms to develop action plans to address the significant root causes of identified audit quality findings.

STRATEGIC COMMITMENT 4

Influence global audit quality consistency.

Highlights

- Published audit quality insights for audit committees, encouraged standard setters to innovate and enhance their responsiveness, and provided our perspectives on current and emerging areas such as audit quality indicators (AQIs), auditing in the crypto-asset space, use of data analytics in the audit, IFRS 9 and auditor responsibility in detecting and reporting on fraud and going concern.
- Led discussions within the International Forum of Independent Audit Regulators (IFIAR) on how audit regulators can work together in evaluating emerging technology tools and worked with other IFIAR board members to explore changes to the audit industry's structure, new standards and independence requirements.

Our full 2019-21 strategic plan is available at www.cpab-ccrc.ca.

2019 OPERATIONAL HIGHLIGHTS

Audit quality insights: 2019 annual audit quality assessments

All public accounting firms that audit a reporting issuer must register with CPAB. Securities legislation defines what constitutes a reporting issuer; each of the 13 Canadian securities commissions maintains a list of the reporting issuers in their jurisdictions. At December 31, 2019, 267 public accounting firms were registered; 95 of those firms do not currently audit reporting issuers.

Each year, CPAB inspects all firms that audit 100 or more reporting issuers. There are currently 14 firms in this group which audit over 7,000 reporting issuers. These firms, and their foreign affiliates, audit approximately 99.5 per cent of all reporting issuers as measured by market capitalization.

Based on our inspections findings, we provide mandatory recommendations to improve audit quality which the audit firm must implement within a defined period — usually 180 days; this deadline is much shorter for more serious findings, particularly where there may be a potential restatement of the financial statements. Our Rules provide a framework of remediation and disciplinary mechanisms to address audit quality deficiencies at the firm and file levels (see CPAB Discipline Overview on page 21).

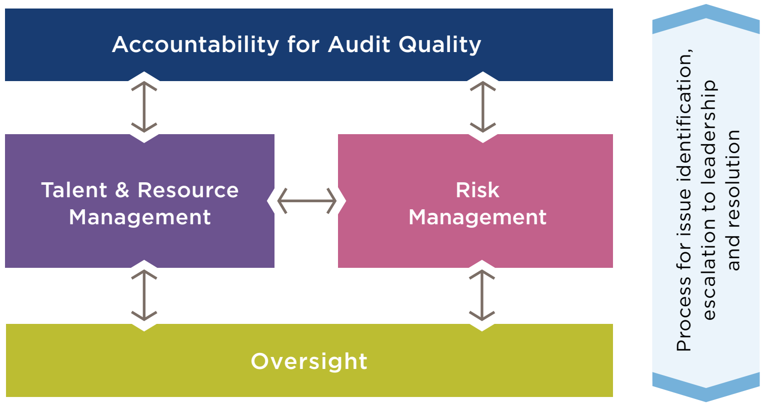
During 2019 CPAB inspected 35 firms (2018:32) and 142 engagement files (2018:139).

Quality management systems assessments: strengthening audit quality

CPAB expects firms to have quality management systems that manage risk, emphasize strong governance and accountability, and deploy highly trained professionals with skillsets tailored by industry and areas of expertise.

In alignment with this expectation, and to help accelerate improvement, CPAB has evolved our audit oversight methodology (supplementary to our audit engagement file inspections) to assess the effectiveness of the quality management systems at the country's four largest public accounting firms (Deloitte LLP, Ernst & Young LLP, KPMG LLP and PwC LLP).

CPAB's FIRM QUALITY MANAGEMENT SYSTEMS MODEL: CRITERIA FOR ASSESSING QUALITY



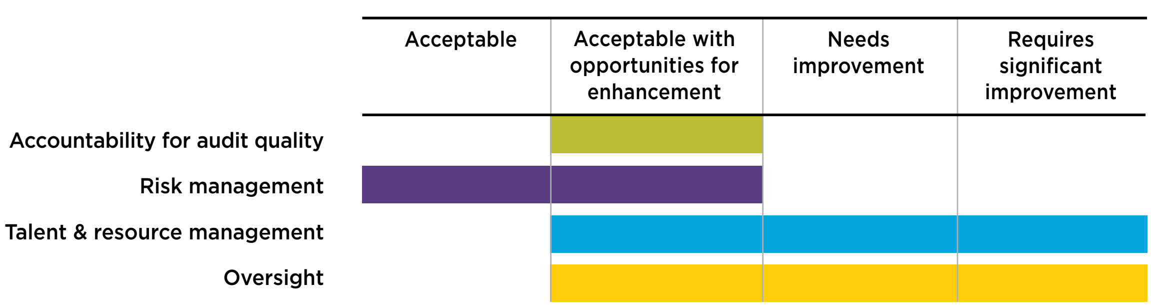
Progress made in 2019

In 2019, each firm made a significant effort to address our observations related to their quality management systems including documenting, amending and in certain cases, implementing new controls and processes, and linking them to our assessment criteria. The journey to establish robust quality management systems takes time and each firm is at different stages of maturity with respect to the formality of their systems, how closely existing processes and controls align to CPAB's evaluation criteria, and the quality of evidence available to demonstrate the identified controls are operating effectively.

Our 2019 assessments focused on firm process documentation specific to CPAB's criteria, evaluating firm assessments of risk, evaluating control design and where possible, firm testing to support operating effectiveness. We considered the objective, resources, methodologies, type of risk, frequency and robustness of the process or control relative to the risk, and severity of findings related to each control.

Because many firm processes and controls were implemented in 2019 or were still being developed at the time of our assessments, not all gaps previously identified have yet been fully addressed and newly implemented controls could only be assessed for design but not operating effectiveness. Below we provide a range for our assessments by criteria to illustrate the progress firms have made in certain areas while recognizing it will take time to fully embed these changes to achieve consistently executed, high quality audits.

RANGE OF QUALITY MANAGEMENT SYSTEMS RATINGS BY CRITERIA



2019 QUALITY MANAGEMENT SYSTEMS ASSESSMENTS BY CRITERIA

ACCOUNTABILITY FOR AUDIT QUALITY

Why it's important
Clearly defined roles with responsibilities for audit quality at the leadership and engagement levels supports a culture of shared accountability and responsibility for audit quality that encourages escalation of issues.

CPAB assessment
The four firms have been evaluated as **acceptable with opportunities for enhancement**. Improvements in the development and communication of detailed roles and responsibilities to include accountability for audit quality (at all levels) have been observed and the firms are implementing organizational changes to build a more consultative and collaborative culture.

Enhancements recommended
The firms are continuing to develop and refine leadership roles and integrate them into their performance management processes. For controls and processes which require issue escalation to leadership there is a need for formalized structure rather than relying on informal communications.

RISK MANAGEMENT

Why it's important
Robust policies, procedures and controls to identify, monitor and respond to risks identified across the firm's portfolio supports informed decision-making, including the initial acceptance or the decision to continue with existing clients. Leadership monitoring and intervention ensures that reporting issuer clients are allocated sufficient resources with the appropriate capabilities and experience, including specialists.

CPAB assessment
Evaluations ranged from **acceptable** to **acceptable with opportunities for enhancement**. Of each of CPAB's criteria, risk management processes and controls were the most established at all firms, particularly related to monitoring risk and the decision to accept new or continue with existing clients.

Enhancements recommended
Certain firms had challenges providing suitable evidence to demonstrate the operating effectiveness of controls regarding the identification, review and intervention of high-risk engagements and evidence of challenge of annual continuance assessments.

2019 QUALITY MANAGEMENT SYSTEMS ASSESSMENTS BY CRITERIA

TALENT AND RESOURCE MANAGEMENT

Why it's important
Strong controls and processes to support firm leadership's monitoring of talent capacity and competency help improve the timeliness and effectiveness of intervention to support engagement teams when there are changes in scope, risk, and staff availability and client delays. Timeliness and effectiveness of interventions by leadership is critical to supporting the execution of quality audits by engagement teams.

CPAB assessment
Evaluations ranged from **acceptable with opportunities for enhancement** to **requires significant improvement**. In general, firms have mature controls and processes to manage assignments and re-alignments from a capacity and competency perspective for audit partners and senior managers, however the processes and controls for audit managers, staff and specialists are less robust.

Enhancements recommended
Certain firms have designed and implemented new controls for the 2019 year-end audits to help address these findings, such as more formalized and timely monitoring and intervention for team members with excessive overtime. These controls will be evaluated for design and operating effectiveness in 2020.

OVERSIGHT

Why it's important
Systems that provide leadership with visibility into the progress of audit work and quickly initiate issue resolution are critical to audit quality. Effective oversight includes both monitoring by leadership and escalation mechanisms that support engagement teams when circumstances arise that may require additional resources or the decision to delay the issuance of the audit opinion.

CPAB assessment
Evaluations ranged from **acceptable with opportunities for enhancement** to **requires significant improvement**. All firms have developed or are developing systems to provide leadership with more visibility into the status and changes in risks of individual engagements, which allows the firm to initiate intervention, where necessary.

Enhancements recommended
There is a need for formal escalation and oversight mechanisms at certain firms to provide sufficient evidence to demonstrate operating effectiveness.

Looking forward

We expect that strong, well-executed quality management systems will lead to long term sustainable audit quality and improve the overall consistency of audit execution. We have seen improvement in the firms' quality management systems compared to last year; however, in many cases our file-related significant inspection findings continue to indicate deficiencies exist in the firms' quality management systems.

In our 2019-21 strategic plan CPAB commits to measuring firm progress based on our file inspections and our assessment of firm quality management systems using two indicators:

1. Percentage of firm quality management systems with a rating no lower than 'acceptable with opportunity for enhancement' (phased implementation with a target of 90 per cent of the firms' quality systems components achieving this rating by 2021).

2. Percentage of audit files inspected with no significant findings (target of 90 per cent with no significant findings by 2021).

Our 2019 quality management system assessments are a positive indicator that the first target is achievable; firms are currently meeting the target for two of the four criteria. However, it is important they continue to evolve processes, demonstrate controls are operating effectively and advance their self-assessment processes for all of CPAB's assessment criteria.

With respect to the second target, improvement is required at three firms to reduce the findings to an acceptable level.

QUALITY MANAGEMENT SYSTEMS – CREATING A DIALOGUE

To improve the dialogue on how the firm's quality management systems support audit quality, audit committees could consider these illustrative questions for the engagement team.

1. **Does the audit team expect to consult with the firm's national office or experts outside the engagement team?**

2. **If your company operates in a new or emerging industry, how does the auditor ensure all relevant risks to the financial statements are identified and appropriately mitigated?**

3. **If the firm uses automated audit tools (data analytics, machine learning, etc.) are there sufficient firm resources to support the engagement team in implementing and interpreting the outputs of these tools to maintain audit quality?**

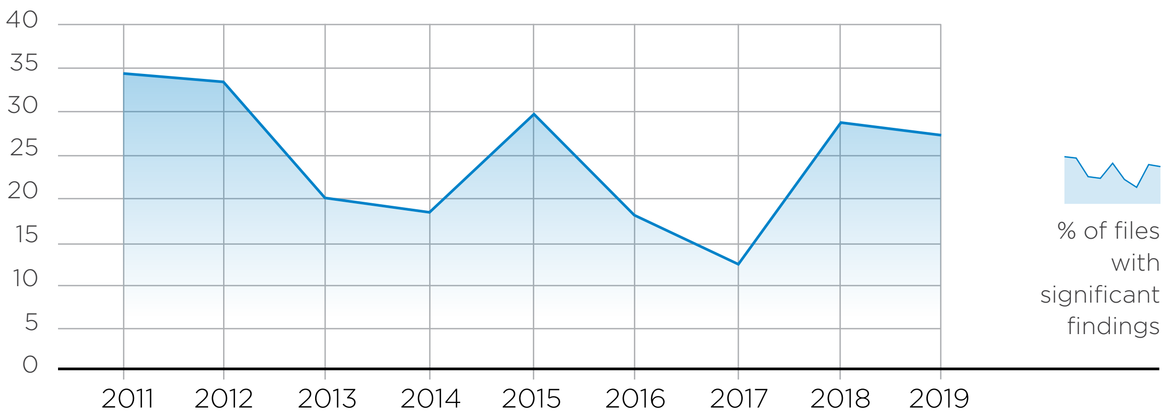
4. **What actions have been taken at the firm and engagement team levels to align and re-align, where necessary, talent to respond to new circumstances or changes in risk?**

5. **How does the firm support engagement teams so that talent with sufficient capacity and competency at all staff levels, including industry experts and specialists (i.e. valuations, tax and IT), is assigned to execute on quality audits?**

Audit engagement file assessments

Twenty-seven per cent of the files we inspected at the 14 public accounting firms reviewed annually had significant findings (2018:28 per cent).

SIGNIFICANT FINDINGS: NINE YEAR TREND

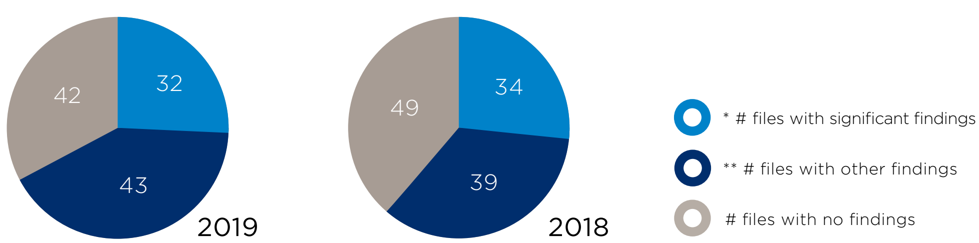


The level of total findings at certain firms was impacted by the expansion of the number of reporting issuers in the crypto-asset and cannabis sectors and associated audit challenges presented that were not appropriately addressed. In response, we inspected 24 files in these sectors (2018:13) and identified significant findings in 14 of those files (2018:8). Firms that choose to audit reporting issuers operating in these industries need to invest in enabling tools, training and resources so that the competencies required to achieve an acceptable level of audit quality are in place.

2019 ANNUAL FIRM INSPECTIONS SNAPSHOT

CPAB inspected 14 annual firms in 2019 (2018:14) and 117 engagement files (2018:122) and identified significant findings in 32 (2018:34). Improvement is required by 11 of the firms to achieve the target of 90 per cent of files with no significant findings.

- Four largest firms: 72 engagement files; 12 with significant findings.
- Ten other annual firms: 45 engagement files; 20 with significant findings.



*Significant findings – A significant inspection finding is defined as a deficiency in the application of generally accepted auditing standards related to a material financial balance or transaction stream where the audit firm must perform additional audit work to support the audit opinion and/or is required to make significant changes to its audit approach. CPAB requires firms to carry out additional audit procedures to verify there was no need to restate the financial statements due to material error, or to substantiate that they had obtained sufficient and appropriate audit evidence with respect to a material balance sheet item or transaction stream to support their audit opinion.

**Other findings – A noted deficiency in the application of generally accepted auditing standards related to a material balance sheet item or transaction stream where CPAB is able to conclude, without the engagement team performing additional procedures to support the audit opinion, that the deficiency is unlikely to result in a material misstatement. These findings, while not significant, indicate areas for improvement.

Firm-specific results

Deloitte LLP, Ernst & Young LLP, KPMG LLP, PwC LLP

CPAB inspected 72 (2018:80) audit engagement files across Canada's four largest public accounting firms − Deloitte LLP, Ernst & Young LLP, KPMG LLP, PwC LLP − and identified significant inspection findings in 12 (2018:16) of those files. Results at three firms, including the two with a higher level of significant findings in 2018, improved in 2019 with one firm having met the target of 90 per cent of files with no significant findings for both years; one firm experienced an increase in significant findings over the prior year.

The two firms with increased findings in 2018 acted upon CPAB's recommendations and developed or updated detailed action plans to address their quality issues. Successful implementation of longer-term initiatives, including planned enhancements to the firms' quality management systems, will be critical to achieving improved sustained audit quality.

The firm with increased findings in 2019 had met the target of 90 per cent of files with no significant findings in the previous year. CPAB has recommended the firm perform a root cause analysis on this year's findings to identify underlying factors impacting audit quality and consider the implications on the effectiveness of its quality management systems to develop specific action items to address this year's results.

Remediation work being performed by audit firms has either been completed or is in process; no restatements have been required since our 2018 annual report. Where a restatement is required, the firm works with the reporting issuer and its securities legal counsel to effect the restatement as soon as possible — usually within the next quarterly reporting period.

BDO LLP, Davidson & Company LLP, DMCL LLP, Grant Thornton LLP, Manning Elliott LLP, McGovern Hurley LLP, MNP LLP, Raymond Chabot Grant Thornton LLP, RSM Canada LLP, Smythe LLP

In 2019, CPAB inspected 45 (2018:42) audit engagement files across these ten annually inspected firms; 20 had significant findings (2018:17). Twelve of those 20 significant findings were in the crypto-asset and cannabis sectors which contributed to the overall unacceptable inspection results for four firms. These firms had significant findings in over 50 per cent of files inspected in both 2019 and 2018. We have recommended a number of actions to these firms in order to achieve acceptable audit quality.

Four other firms had significant findings in over 25 per cent of the files inspected in both 2019 and 2018. These firms need to do more to understand the underlying factors leading to an increase in significant inspection findings and identify targeted actions to ensure consistent high-quality auditing across their reporting issuer audit practice.

CPAB will continue to monitor the progress of the eight firms in addressing and resolving the factors that impacted their respective 2019 inspection results. Specific recommendations for improvement have been provided to each of these firms, with actions including completing an in-depth root cause analysis of the inspection findings, enhanced training and supervision, hiring more staff or staff with greater expertise, additional quality reviews and completion of audit quality action plans. We are encouraging these firms to begin early implementation of the new international quality management standards.

Failure to address our recommendations and improve audit quality will result in an escalation of our regulatory intervention and may result in the disciplinary mechanisms outlined in the CPAB Discipline Overview on page 21 of this report.

Two firms continued to have stable inspection results, with zero or one significant finding in both 2019 and 2018.

These ten firms audit about one per cent of Canadian reporting issuers by market capitalization (approximately 1,650 public companies). Two restatements have been required since our 2018 annual report.

Non-annual firms

CPAB identified 15 (2018:8) files with significant findings out of the 25 files (2018:18) inspected across the 21 non-annually inspected firms (2018:18) in 2019. Five of the files inspected were in the cannabis sector, four of which had significant findings. No restatements have been required since our 2018 annual report.

CPAB executes a tailored inspection methodology to assess quality management systems at non-annual firms. Common inspection findings and potential causal factors leading to significant findings are incorporated into our risk analysis of these firms and the companies they audit. This facilitates proactive outreach to understand how the firms will manage these risks along with strategic intervention through select file inspections.

Failure to implement our recommendations or continued unacceptable levels of significant findings will result in an escalation of our regulatory intervention, as outlined in the CPAB Discipline Overview section on page 21 of this report. Actions taken on certain firms include Restrictions limiting the acceptance of new reporting issuers, required enhanced engagement quality control reviews or in-flight reviews, requirement to undertake additional training for specific accounting or audit topics, and required action plans to improve audit quality and hiring additional resources.

Common inspection findings

Emerging industries

Auditors must design audit procedures that respond to emerging industry risks, including rapid growth and innovative cultures; many traditional audit procedures can be less effective in these kinds of business environments.

In November 2019, CPAB published **Auditing in the crypto-asset sector** outlining the five most common engagement file deficiencies in this sector and highlighted the technical challenges that need to be addressed.

Cannabis company inspection findings were primarily related to insufficient understanding of complex business arrangements. Estimating fair value of biological assets is complicated by market uncertainty and volatility related to volume and price of expected sales — the fair value amounts are often highly sensitive to relatively small changes in these key inputs and auditors are not always appropriately assessing the potential impact of such changes.

Auditing estimates remains a challenge

More than half the significant findings in 2019 were related to the audit of estimates. Auditors did not adequately address the risks associated with auditing financial statement amounts that could not be directly observed. Revisions to the auditing standards to help auditors better respond to the risks will be effective for audits of financial periods beginning on or after December 15, 2019.

Assessing estimates of fair value continues to be a challenge for auditors. We observed this most often in the audits of fair value estimates of asset acquired, liabilities assumed, and non-cash consideration transferred in business combinations. Fair values of biological assets and investments were also common findings as noted above.

As in prior years, the audit of revenue recognition based on the percentage of work completed continues to be a concern; we are finding that some auditors do not obtain sufficient and appropriate evidence to support the estimate of progress achieved.

Responding to changes in the business

The current business environment requires companies to constantly evolve the nature of their products and services or internal operations. Our inspection findings are often in areas where there has been a significant change at the reporting issuer in the year. For example, a business may decide that instead of performing a full inventory count at a point in time it is more effective to count small portions throughout the year. To respond to this business process change, the auditor is required to perform different audit procedures and to perform them throughout the year. Significant inspection findings arose when auditors did not make the appropriate audit procedure changes.

2019 INSPECTIONS SCOPE

How CPAB chooses files to review

CPAB's risk-based methodology for choosing files (and the specific areas of those files) for inspection is not intended to select a representative sample of a firm's audit work. Instead, it is biased towards higher-risk audit areas of more complex public companies or areas where the audit firm may have less expertise, so there is a greater likelihood of encountering audit quality issues. Our inspections do not look at every aspect of every file and are not designed to identify areas where auditors met or exceeded standards. Results should not be extrapolated across the entire audit population, but instead viewed as an indication of how firms address their most challenging situations.

Registered firms

At December 31, 2019, 267 audit firms were registered as a Participating Audit Firm with CPAB. During the year, twenty-three new firms registered (five Canadian and 18 foreign firms). Twenty-eight firms withdrew from registration with CPAB and one firm's registration was terminated for failing to comply with administrative requirements. Audit firms who voluntarily participate in the Protocol for Audit Firm Communications of CPAB Inspection Findings with Audit Committees (Protocol) share significant file-specific inspection findings with their reporting issuers' audit committees. A significant inspection finding is a significant deficiency in the application of generally accepted auditing standards related to a material financial balance or transaction stream where the audit firm must perform additional audit work to support the audit opinion and/or is required to make significant changes to its audit approach. Twelve of the 14 annually inspected firms participate in the Protocol – a complete list is available at www.cpab-ccrc.ca.

How firms respond to CPAB findings

The majority of CPAB's inspection findings in 2019 required the audit firm to carry out additional audit procedures to verify there was no need to restate the financial statements due to material error. The remaining findings required the audit firms to add considerable evidence to the audit file to show they had obtained sufficient and appropriate audit evidence with respect to a major balance sheet item or transaction stream. For the 14 annually inspected firms, two restatements have been required since our 2018 annual report or one per cent of files inspected (2018: five restatements or four per cent of files inspected).

CPAB DISCIPLINE OVERVIEW

CPAB actively engages with firms throughout the inspections cycle to resolve issues as they arise during our reviews. Our Rules provide a framework of remediation and disciplinary mechanisms to address audit quality deficiencies at the firm and file levels. This allows us to respond quickly when we believe more work is required to support the audit opinion. For example, CPAB operates under the principle that, within 10 days of determining a file deficiency, we notify the firm; we then require their remediation plan within another 10 days. CPAB expects that firms will remediate file deficiencies before their reporting issuer's next quarterly report or next audit committee meeting.

CPAB also has the authority to commence an investigation when it considers that a Violation Event may have occurred, and it wishes to seek information and the cooperation of the firm with respect to such matters. A Violation Event is defined in CPAB's Rules as: (i) an act or omission in violation of CPAB's Rules or chartered professional accountant standards; (ii) a failure to supervise a person to prevent such violations, and the person has committed the act or omission; (iii) a failure to cooperate with the terms of an inspection or investigation; or (iv) a failure to comply with the terms of any Requirement, Restriction or Sanction imposed by CPAB. No investigations were conducted in 2019.

What happens when a firm does not show improvement?

If a firm fails to improve, CPAB has the authority to impose discipline at three levels: Requirement, Restriction and Sanction. This can include publicly naming a firm and restricting it from auditing public companies and helps to ensure that firms act quickly and appropriately to resolve deficiencies. Finally, where CPAB imposes a disciplinary action related to a defect in the firm's system of quality control, and the firm fails to address it to CPAB's satisfaction within a specified time period, the firm must notify the audit committees of all its reporting issuers.

Requirements typically involve CPAB mandating the firm to take an action to make a change to its audit practices to improve audit quality. Requirements are generally private, unless notification is required by the securities commissions. If audit quality has not improved during a follow-up inspection with an audit firm with a Requirement on it, or if CPAB feels the performance of the firm and the severity of the lack of audit quality in the first instance requires so, CPAB would impose a Restriction.

Restrictions characteristically involve CPAB limiting the audit firm's practice in some way, and CPAB will specifically notify the securities commissions of the Restriction, in addition to the notification that may be required otherwise under National Instrument 52-108. If there is demonstrated continued lack of improvement of audit quality with an audit firm with discipline already in place, or if in the first instance there is demonstrated egregious behavior, CPAB would impose a Sanction.

With the imposition of a Sanction, CPAB would severely limit the audit firm's practice and obligate the firm to notify the audit committees of its reporting issuer clients. CPAB would also notify the securities commissions.

The power of public censure

CPAB's power to impose a Requirement, Restriction or Sanction includes a public censure in the event that CPAB considers a Violation Event has occurred. A public censure is intended to be a strong public statement of disapproval of a firm's conduct. While CPAB has not yet publicly censured a Participating Audit Firm, CPAB may impose this sanction when commensurate with the circumstances of the case. CPAB considers the seriousness of the Violation Event, the firm's response and risk of harm to the investing public.

A public censure may be published on CPAB's website or, in serious cases, announced via a news release. CPAB would only impose a public censure while respecting the confidentiality obligations imposed on it by its Rules or legislation. CPAB will not identify any individual, except insofar as those names are part of a Participating Audit Firm name. CPAB will not share specific information relating to a reporting issuer, or the business, affairs or financial condition of a Participating Audit Firm or the client of any such firm.

Participating Audit Firms have the right to petition for a review hearing before a public censure is imposed, as is the case with all Requirements, Restrictions or Sanctions.

2019 disciplinary actions

As at December 31, 2019 there were Requirements on one firm (2018:3) and Restrictions on one firm (2018:2). Of the two firms operating with Requirements or Restrictions, CPAB has limited the acceptance of new reporting issuers for both firms, and for one or both firms required enhanced engagement quality control reviews or in-flight reviews, additional training for specific accounting or audit topics, and action plans to improve audit quality and consider hiring additional resources. There were no Sanctions in 2019.

How does a firm request a review proceeding?

A firm may petition for a review proceeding in the following three situations: 1) when CPAB intends to make public the weaknesses, deficiencies and recommendations in the system of quality control, or deficiencies in specific engagements, not addressed or remedied to CPAB's satisfaction; 2) when CPAB proposes to impose Requirements, Restrictions and Sanctions in the case of a Violation Event; 3) in connection with an application for membership not accepted by CPAB.

No review proceedings were conducted in 2019.

In conversation with our stakeholders

180 public company directors

7 audit committee roundtables

Accountability for sustainable audit quality lies with all stakeholders involved in the audit including auditors, audit committees and management. To keep audit quality matters at the top of the agenda, CPAB continued its discussions with key stakeholders and provided our insights and perspectives to help accelerate improvements in quality, with a primary focus on audit committees.

In 2019, CPAB leaders met more than 180 public company directors from a range of industries and company size. Management also has significant impact on the execution of high-quality audits; consistent with this view, several of our discussions included the company's Chief Financial Officer or other senior financial executives. We hosted seven audit committee roundtables in Vancouver, Calgary, Toronto and Montreal covering the mining, energy, real estate and banking and insurance sectors, helping to support the role of these important stakeholders.

During the year we initiated a strategy to engage more proactively with investors, beginning discussions with seven institutional investors and investor organizations.

In addition to meetings and events, in 2019 we published our insights and perspectives on several audit quality matters including current and emerging industries and technologies such as the crypto-asset sector and the use of data analytics in the audit. To support the expanded application of audit quality indicators by auditors, management and audit committees CPAB reported our key learnings on the use of and benefit of audit quality indicators.

We also examined the role of auditors in detecting fraud and reporting on going concern. To provide a starting point for our work, we performed thematic reviews of auditor responsibilities in these two areas during 2019. This included reviewing the auditor's fraud risk discussion, fraud risk assessment and responses to assessed risk of fraud in more than 100 files inspected. We published our initial observations on both of these reviews in early 2020.

2019 CANADIAN AUDIT QUALITY ROUNDTABLE

New risks and opportunities continue to emerge in the public company audit environment. In October 2019 CPAB and the Office of the Superintendent of Financial Institutions (OSFI) co-hosted the first Canadian Audit Quality Roundtable to explore ways to enhance public confidence in audit quality. More than forty of Canada's public accounting and regulatory leaders came together to share ways to support continued financial system stability. CPAB and OSFI have established multi-stakeholder teams that will address four priority actions:

1. Develop a forum to accelerate our ability as a collective group to identify emerging issues and address risks and challenges resulting from novel/emerging industries or emerging trends in the broader corporate reporting environment (including accounting, disclosure, auditing) in a nimble/agile and timely manner.

2. Explore what can be done to better prevent and detect corporate fraud by management, audit committees, auditors, standard setters and regulators.

3. Explore what actions can be taken by all relevant stakeholders to reduce 'surprise' business failures, including assessment of whether current standards (auditing, accounting, corporate reporting) are fit for purpose, and whether incremental corporate disclosure, standards, procedures and education are required.

4. Review barriers to the application of professional skepticism by auditors and develop an action plan for steps that can be taken in the Canadian audit environment to enhance professional skepticism, including actions by auditors, management, audit committees, standard setters and regulators.

Influencing global audit quality

CPAB continued our commitment to influencing global audit quality as part of our 2019-21 strategic plan, including enhancing the ability to access audit work of Canadian reporting issuers performed in foreign jurisdictions, building on our international presence as an authoritative thought leader on audit quality matters, and collaborating with domestic and international regulators.

CPAB is actively involved in issues related to auditing and audit policy internationally through our leadership in the International Forum of Independent Audit Regulators (IFIAR) and our publications.

In 2020 CPAB will continue to dedicate resources to actively support IFIAR. A key focus will be the establishment of methodologies to assess data analytics, artificial intelligence and other technological tools used by auditors as a member of IFIAR's Technology Task Force.

Building the team of the future

CPAB continues to implement its talent strategy to support the delivery of our 2019-2021 strategic plan. Our people, including their professional knowledge, skills and experience, are critical to our effectiveness as an audit regulator.

Investing in skills and accelerating our team's professional and personal development have been essential components of CPAB's 2019 talent approach. We created a new Learning and Innovation role to lead CPAB's learning strategy and to advance our innovation culture. We delivered training on key audit quality matters including audit issues raised by emerging industries, use of technology in the audit and business skills via internal and external subject matter experts.

We increased our headcount by 10.2 per cent. We leveraged vacancies and new positions that arose to broaden and diversify our skills and experience base to align with current and anticipated needs such as learning and innovation, discipline and enforcement, and technology.

Workplace and gender diversity are central to CPAB's culture, and we aim to attract, develop and retain the most capable employees from diverse backgrounds. In 2019, visible minorities comprised 33 per cent of our total staff (2018: 24 per cent). The percentage of women on our leadership team increased to 60 per cent (2018: 44 per cent).

Recognizing the importance of strategically managing risks and the competition for top talent, we refined our succession planning and leadership development work.

Our communities

The health and well-being of our communities matters to CPAB. Our people engage personally and professionally in a variety of activities that make our communities better places to live.

As part of our Community Matters program, staff annually volunteer their time with a locally-chosen charitable organization individually and at an organizational level. In 2019 we launched a campaign to raise awareness about mental health through educational sessions, and our employees participated in CPAB's charitable donation matching program and fundraising activities dedicated to this cause. In addition, CPAB staff across the country volunteered at their local food banks.

In 2020, CPAB will continue to support mental health awareness through fundraising, internal education, and fostering a healthy, safe and inclusive workplace.

CPAB COMMUNITY matters

MANAGEMENT'S DISCUSSION AND ANALYSIS

Overview

CPAB is an independent, federally incorporated, not-for-profit corporation without share capital. Established in 2003, CPAB reinforces public confidence in the integrity of financial reporting of public companies in Canada through effective regulation and by promoting quality, independent auditing. National Instrument 52-108 of the Canadian Securities Administrators requires that auditors of Canadian reporting issuers' financial statements be registered and in good standing with CPAB.

Our core work combines annual assessments of firm quality management systems and risk-based audit file inspections either directly or in co-operation with other regulatory bodies in Canada and abroad.

This management's discussion and analysis (MD&A), prepared as of February 11, 2020, is a review of CPAB's operating results for the year ended December 31, 2019. It should be read in conjunction with the audited financial statements for the year ended December 31, 2019 and related notes which have been prepared in accordance with Canadian accounting standards for not-for-profit organizations. It also includes the outlook for 2020, principal risks and uncertainties that could affect the organization and forward-looking information that describes CPAB's budget, estimates and forecasts. Forward-looking information can be identified by the use of conditional or forward-looking terminology, such as budgets, estimates, anticipates, will, and should.

Forward-looking statements involve risks and uncertainty and reflect CPAB's view at the date of this report. Forward-looking information is based on assumptions and estimates including the timing of recruiting, travel requirements that depend on the selection of files to be inspected, and the extent of international travel for inspections of component auditors. Revenue has been assessed based on audit fees as reported by Participating Audit Firms, subject to CPAB internal review. Actual results may vary from the forward-looking information.

All amounts are expressed in Canadian dollars.

Operating results

CPAB is committed to prudent fiscal management and innovation in how we deliver on our regulatory mandate. Our current operating environment continues to bring significant technological change with impacts on both the public company accounting firms we regulate and our effectiveness as a regulator. In response, CPAB invests in information technology applications, upskilling existing staff and recruiting for the required new skills.

Key financial data

(in $'000)	For the year ended December 31, 2019	For the year ended December 31, 2018
Total fees revenue	$ 17,030	$ 16,750
Investment income	168	120
Salaries and benefits	12,413	11,236
Other operational expenses (net of other revenue)	4,924	4,319
Excess of revenue over expenses (expenses over revenue)	(139)	1,315
Cash and investment	8,342	7,886
Total assets	10,286	9,485
Total liabilities	2,787	1,848
Net assets	7,498	7,637

The decrease noted in our excess of revenue over expenses in 2019 is aligned with our budget reflecting increased staff levels and information technology expenses.

Revenues

CPAB derives its revenue from Canadian reporting issuers. Each year, CPAB invoices Participating Audit Firms, which in turn, bill their reporting issuer clients. The fee is designed to cover CPAB's annual operating costs and to provide a reasonable reserve for contingencies.

Annual Participation fee revenue increased by 1.7% from $16.7 million in 2018 to $17 million in 2019. In 2019, CPAB implemented a new revenue-neutral funding model that is more equitable for reporting issuers as it is based on the total audit fees billed to the reporting issuer, as publicly reported on SEDAR/EDGAR (public company reporting systems used by securities regulators in Canada and the US, respectively). In 2019, CPAB's fee rate was 1.22% of the total global audit fees charged to Canadian reporting issuers with a cap of $75,000 for foreign reporting issuer companies (2018:2.0% of the local audit fees Canadian and foreign participating firms charged to their reporting issuer clients).

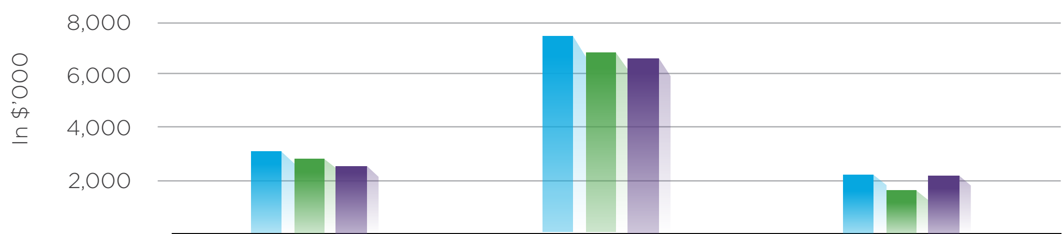
Operating expenses

In 2019, salaries and benefits for inspections and corporate staff was CPAB's largest expense, totaling $12.4 million or 72% of total expenses of $17.3 million (2018:$11.2 million or 72%).

The increase of 10% or $1.2 million in salaries and benefits is mainly due to successfully filling existing vacancies and staffing newly created positions in 2019. As at December 31, 2019, CPAB had 54 employees compared to 49 as at December 31, 2018.

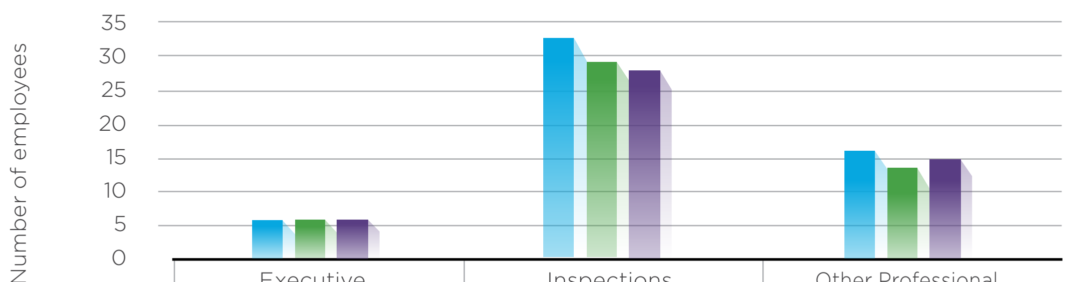
The following tables show the evolution of CPAB's headcount over the last three years by executive, inspections and corporate staff.

Salaries by category



	Executive Staff	Inspections Staff	Other Professional Staff
2019	2,913,715	7,316,867	2,182,608
2018	2,720,778	6,874,519	1,640,270
2017	2,700,000	6,600,000	2,200,000

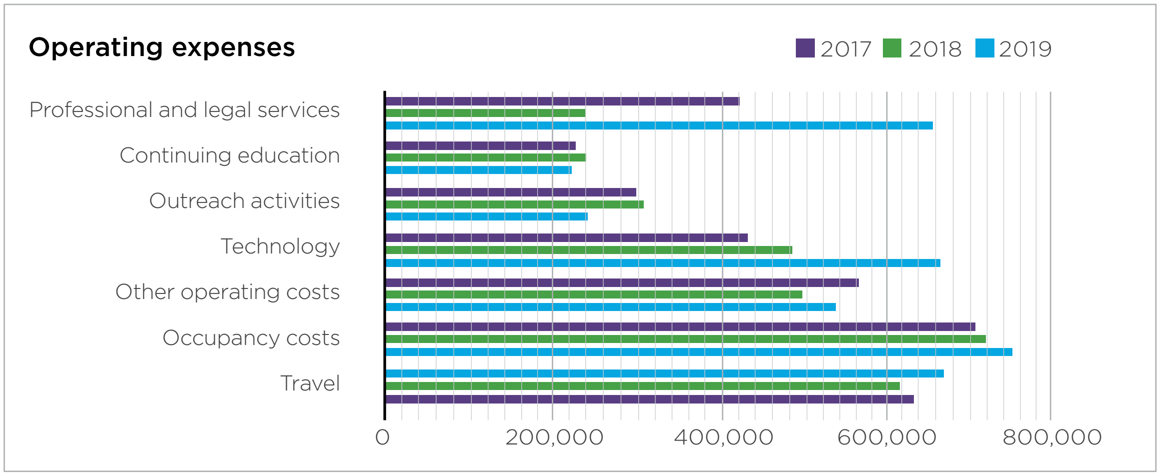
Number of employees by category



	Executive Staff	Inspections Staff	Other Professional Staff
2019	6	32	16
2018	6	29	14
2017	6	28	15

Overall, operating expenses amounted to $17.3 million (2018:$15.6 million), an overall increase of $1.7 million or 11% from 2018 mainly attributed to increases in headcount, technology expenses and professional and legal services fees.

The following table shows the composition over the last three years of the operating expenses excluding salaries, directors' fees, and amortization.



In 2019, operating expenses increased in technology and professional and legal services. The former reflects the expenditure CPAB is currently incurring in technology and communication and software upgrades, now renewed under annual licenses. Professional and legal services increased from $0.2 million in 2018 to $0.7 million in 2019, mainly attributable to an increase in recruitment fees of $0.27 million and legal fees of $0.15 million. In 2019, management used external legal counsel services to advise on improving access to component audits and disciplinary actions.

The other operating costs include subscriptions and memberships, insurance and other administration costs.

Financial position

The following table presents CPAB's condensed statement of financial position as of December 31:

(in $'000)		2019		2018
Cash and investments	$	8,342	$	7,886
Accounts receivable and prepaid expenses		553		530
Accounts payable and accrued liabilities		(2,319)		(1,442)
Net working capital	**$**	**6,576**	**$**	**6,974**
Property, equipment and intangible assets		1,390		1,069
Unamortized tenant inducements		(468)		(406)
Net Assets	**$**	**7,498**	**$**	**7,637**

At December 31, 2019, CPAB had a working capital position of approximately $6.6 million (2018: $6.9 million). CPAB has established a guideline for an appropriate reserve of approximately four to six months of operational costs; this would be used to ensure business continuity should there be fluctuations in revenue and to maintain consistency in the Annual Participation fee.

The increase in property, equipment and intangible assets is mainly attributable to the leasehold improvement following the renewal of the Montreal office lease agreement, the new website launched in early 2020 and the replacement of computer equipment.

Accounts payable and accrued liabilities increased as a result of an unpaid balance of $0.2 million on leasehold improvements in Montreal for which certain work was not completed and accepted at year end.

CPAB's investment policy requires that excess cash be invested in accordance with criteria assessing risk, yield and liquidity. Investments may be made in short-term government of Canada treasury bills, Canadian Chartered Bank Term notes and top-rated Certificates of Deposit, with maturities of up to one year. Commencing in 2020, the investment policy has been updated to include money market funds, direct obligation of the Canadian governments and fixed income securities with an investment grade of AAA or better.

Segmented information

Our core operations are organized into three segments:

1. Inspections: Costs related to our inspection program of all participating firms.
2. Other regulatory activities: Costs related to CPAB's regulatory oversight program to improve audit quality. Includes stakeholder engagement initiatives, thought leadership projects, enterprise risk management program, registration, legal, and communication costs.
3. International: Costs related to our participation in the International Forum of Independent Audit Regulators and other international audit quality work.

Except for payroll-related costs that are allocated based on a best estimate of time spent, the cost allocation among segments is based on actual expenses. For purposes of segmented information management groups certain costs for analysis which may have a different presentation and classification from those in the financial statements. Costs that cannot be allocated to a specific segment are considered general expenses. These costs mainly relate to governance, finance and the corporate team.

(in $'000)	Inspections		Other Regulatory		International		Total	
	2019	2018	2019	2018	2019	2018	2019	2018
Human capital								
Salaries and related costs*	$ 9,953	$ 8,757	$ 1,837	$ 1,675	$ 89	$ 265	$ 11,879	$ 10,697
Travel expenses	372	300	38	49	95	148	505	497
Outreach activities								
Stakeholder engagement	–	–	68	84	–	–	68	84
Thought leadership	–	–	133	98	–	–	133	98
IFIAR meetings	–	–	–		–	124	–	124
Operational costs								
General	150	136	230	93	83	82	463	311
Information technology	666	487					666	487
Total operational expenses	**$ 11,141**	**$ 9,680**	**$ 2,306**	**$ 1,999**	**$ 267**	**$ 619**	**$ 13,714**	**$ 12,298**
General costs								
Salaries and related costs							1,049	868
Travel							127	121
General							483	336
Occupancy							751	717
Amortization							347	326
Directors' fees and expenses							877	889
Total expenses							**$ 17,348**	**$ 15,555**

*Salaries and related costs include salaries and benefits, continuing education and recruitment fees

Outlook for 2020

2019 marked the first year of implementation of our 2019-21 strategic plan which is accessible at www.cpab-ccrc.ca. We made solid progress on our commitments — specific milestones are highlighted on page 10 of this report.

CPAB is committed to managing its finances efficiently while focusing on developing our people and investing in IT resources and technology. We will continue to promote sustainable audit quality through our audit quality assessment program and participate in discussions related to audit quality and audit policy domestically and internationally, including through our leadership at IFIAR.

2020 CPAB operating budget (unaudited)

YEAR ENDED DECEMBER (in $'000)	2019 ACTUAL	2019 BUDGET	2020 BUDGET
REVENUE			
Fees	$ 17,030	$ 16,494	$ 17,435
Interest income	168	100	150
Other income	11	-	-
	17,209	**16,594**	**17,585**
EXPENSES			
Salaries and benefits	12,413	12,070	12,725
Directors' fees and expenses	877	866	948
Travel	632	767	697
Occupancy costs	751	749	790
Administration and general	394	365	392
Information technology	666	621	693
Outreach activities	244	273	282
Continuing education	224	280	270
Insurance	143	143	150
Professional services	428	220	303
Legal services	228	85	150
Amortization of property and equipment	347	320	450
	17,348	**16,759**	**17,850**
EXCESS OF EXPENSES OVER REVENUE	**$ (139)**	**$ (165)**	**$ (265)**

Commentary on the 2020 operating budget

For 2020, revenues (which cover operating expenses) are budgeted at $17.6 million, compared to actual and budgeted revenues of $17.2 million and $16.6 million respectively in 2019. For 2019, revenues were estimated using the new fee model at a rate of 1.22% of the audit fees as published on SEDAR/EDGAR. The expected increase comes from the increase in audit fees charged to reporting issuers in 2019.

CPAB's operating expenses for 2020 are budgeted at $17.8 million. This amount represents a 3% increase compared to the 2019 actual operating expenses. In 2020, CPAB will continue investing in the development of our employees, information technology and hiring additional resources.

CPAB anticipates capital expenditures of approximately $0.9 million over the next year mainly related to information technology infrastructure, data management upgrades and certain leasehold improvements for our Toronto office.

Over the next five years, management anticipates increases in operating costs. Investment in technology and new skillsets will be required due to increased adoption of complex technology in audits. In addition, the lease agreement for our Toronto office will end in 2024. Based on the current downtown Toronto real estate market condition, management expects a significant increase in its occupancy costs. Therefore, management anticipates that the Participating Audit Firm fee rate may be adjusted in future years.

Director and executive compensation

CPAB utilizes Mercer Canada's Professional Services Industry Compensation Survey and their consultancy services in establishing compensation ranges. CPAB also monitors public comparative information provided by provincial securities regulators. Taken together, these practices support our efforts to provide compensation that continues to be comparable and competitive.

Executive compensation in 2019, which includes all amounts paid to the CEO, Senior Vice President, Audit Firm Regulation (who left the organization in May 2019), Chief Risk Officer, Chief Financial Officer and Regional Vice President Eastern Canada, Vice President, Inspections and Regional Vice President Western Canada totaled $2.9 million (2018:$2.7 million). This includes salaries, accrued bonuses, registered retirement savings plan contributions and benefits.

2019 director compensation included fees of $0.9 million (2018:$0.9 million). These fees included a $175,000 annual retainer for the Chair of the board, $48,000 annual retainers for each of the other board members, and $7,250 for each committee Chair. Meeting attendance fees were $1,500 for each board and committee meeting.

The board met five times in 2019 (2018:5 total meetings). All board members attended every meeting as well as CPAB's strategic planning session in September.

Principal risks and uncertainties

Significant risks include economic, human capital, technological and legislative forces that could have a material impact on CPAB's mandate and critical success factors.

Current economic uncertainties increase the risks associated with reporting issuer failures in corporate governance, financial reporting and audits. These could create a consequent risk of loss of confidence in CPAB. The organization manages its risk through an enterprise risk management (ERM) program led by our Chief Risk Officer; this program supports the allocation of resources to mitigate risks.

Human capital risks include challenges in attracting qualified personnel. CPAB manages this risk by actively working to be an attractive career destination for highly qualified professionals.

From a technology perspective, data security is an overarching consideration. Central to CPAB's ability to fulfill its mandate is: database design, management and security; development of and support for the participating firms registration information system, and connectivity to support our websites and other services used by remote users. CPAB manages this risk in various ways including, but not limited to: appropriate firewalls; regularly engaging third parties to perform ethical hack and security assessments on CPAB's infrastructure and application controls; internal phishing training for our people; use of hard-drive encryption and internet protocol-based global positioning system tracking tools on all laptops and smartphone devices; managing laptops and servers through the use of systems to ensure all critical patches are deployed regularly, and maintaining offsite Disaster Recovery and Backup facilities.

Our risks include legal or other limitations on CPAB's access to audit working papers in certain countries. CPAB is continuing to pursue legislative change to support its work as an independent audit regulator. During 2019 we worked with Canadian Securities Administrators to improve CPAB's access to audit work performed by component auditors in foreign jurisdictions. We anticipate finalization of the applicable rule changes in 2020.

CPAB's risk management plan, including crisis and business recovery plans, addresses all aspects of its operations. The Board of Directors oversees this plan, which is also actively reviewed by the Risk and Audit Committee of the board. CPAB reviews and updates the plan at least annually. Based on the risks identified, CPAB develops and implements mitigation strategies.

FINANCIAL STATEMENTS

Responsibility for Financial Reporting

The annual financial statements and all financial and other information contained in this annual report are the responsibility of the management of CPAB.

Management has prepared the financial statements in accordance with Canadian accounting standards for not-for-profit organizations, applying best estimates and judgments based on currently available information. The significant accounting policies are described in note 2 to the financial statements. Financial information contained in this report is consistent with that shown in the financial statements.

Management is responsible for the integrity and reliability of financial information and has established systems of internal procedural and accounting controls designed to achieve this. These systems also reasonably ensure that assets are safeguarded from loss or unauthorized use.

The board of directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The board has created a Risk and Audit Committee to assist with these responsibilities. The Risk and Audit Committee met with the auditors, both with and without management present, to review the activities of each, as well as to review the financial statements.

Fuller Landau LLP has been appointed by the Provincial Audit Regulator Members as CPAB's auditors to express their opinion on the fair presentation of the financial statements. Fuller Landau LLP has had full and unrestricted access to the board of directors and management to discuss matters pertaining to their audit. The Risk and Audit Committee undertakes annually a formal review of the auditor's performance and makes a recommendation to the board of directors, which in turn makes a recommendation to the Provincial Audit Regulator Members, with respect to their reappointment for the coming year.

Carol Paradine

Carol Paradine, CPA, CA
Chief Executive Officer

Philippe Thieren

Philippe Thieren, CPA, CA
Chief Financial Officer

Independent Auditors' Report

To the Members of Canadian Public Accountability Board/ Conseil canadien sur la reddition de comptes

Opinion

We have audited the financial statements of **Canadian Public Accountability Board/Conseil canadien sur la reddition de comptes**, which comprise the statement of financial position as at December 31, 2019, and the statements of changes in net assets, operations, and cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the **Canadian Public Accountability Board/Conseil canadien sur la reddition de comptes** as at December 31, 2019, and the results of its operations and its cash flows for the year then ended in accordance with Canadian Accounting Standards for Not-For-Profit Organizations.

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the organization in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with Canadian Accounting Standards for Not-For-Profit Organizations, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the organization's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the organization or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the organization's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the organization's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the organization's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the organization to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit. We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

Fuller Landau LLP

Chartered Professional Accountants
Licensed Public Accountants

Toronto, Ontario
February 11, 2020

STATEMENT OF FINANCIAL POSITION
As at December 31

	2019	2018
ASSETS		
Current assets		
Cash and cash equivalents	$ 2,706,731	$ 2,757,005
Investments (note 4)	5,635,635	5,129,380
Accounts receivable (note 5)	231,851	132,649
Prepaid expenses	320,952	396,689
	8,895,169	8,415,723
Property, equipment and intangible assets (note 6)	1,390,448	1,069,545
	$ 10,285,617	**$ 9,485,268**
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities (note 7)	$ 2,319,568	$ 1,442,303
Unamortized tenant inducements	467,915	406,107
	2,787,483	1,848,410
NET ASSETS		
Invested in property and equipment	1,390,448	1,069,545
Unrestricted	6,107,686	6,567,313
	7,498,134	7,636,858
	$ 10,285,617	**$ 9,485,268**

See accompanying notes.

Approved on behalf of the board:

B Warmbold

________________________, Director
Benita Warmbold, FCPA, FCA, Chair

________________________, Director
Bruce Jenkins, FCPA, FCA

STATEMENT OF CHANGES IN NET ASSETS
For the years ended December 31

			2019	2018
	Invested in property and equipment	*Unrestricted*	*Total*	*Total*
Net assets, beginning of year:	$ 1,069,545	$ 6,567,313	$ 7,636,858	$ 6,321,551
Excess of revenue over expenses (expenses over revenue) for the year	-	(138,724)	(138,724)	1,315,307
Purchase of property and equipment	667,435	(667,435)	-	-
Amortization of property and equipment	(346,532)	346,532	-	-
Net Assets, end of year	**$ 1,390,448**	**$ 6,107,686**	**$ 7,498,134**	**$ 7,636,858**

See accompanying notes.

STATEMENT OF OPERATIONS
For the years ended December 31

	2019	2018
REVENUE		
Fees (note 8)	$ 17,029,778	$ 16,750,237
Investment income	168,326	119,687
Other income	11,100	-
	17,209,204	**16,869,924**
EXPENSES		
Salaries and benefits	12,413,191	11,235,567
Directors' fees and expenses	876,569	888,561
Travel	632,506	618,127
Occupancy costs	751,080	716,506
Administrative and general	394,486	351,636
Information technology	665,715	487,120
Outreach activities	244,082	308,180
Continuing education	224,134	237,928
Insurance	142,634	142,634
Professional services	428,747	152,014
Legal services	228,252	90,817
Amortization of property and equipment	346,532	325,527
	17,347,928	**15,554,617**
EXCESS OF REVENUE OVER EXPENSES (EXPENSES OVER REVENUE)	**$ (138,724)**	**$ 1,315,307**

See accompanying notes.

STATEMENT OF CASH FLOWS
For the years ended December 31

	2019	2018
OPERATING ACTIVITIES		
Excess of revenue over expenses (expenses over revenue)	$ (138,724)	$ 1,315,307
Add back (deduct) non cash items:		
Gain on sale of property and equipment	(7,600)	-
Amortization of property and equipment	346,532	325,527
Amortization of tenant inducements	(62,542)	(56,723)
Net change in non-cash working capital items (note 10)	747,342	(516,734)
Cash generated from operations	**$ 885,008**	**$ 1,067,377**
INVESTING ACTIVITIES		
Purchase of short-term investments	(14,800,000)	(13,400,000)
Redemption of short-term investments	14,300,000	12,600,000
Sale of property and equipment	7,600	-
Purchase of property and equipment (note 10)	(442,882)	(150,200)
Cash used in investing activities	**(935,282)**	**(950,200)**
Cash and cash equivalents (used) generated in the year	**$ (50,274)**	**$ 117,177**
Cash and cash equivalents, beginning of year	2,757,005	2,639,828
Cash and cash equivalents, end of year (note 10)	**$ 2,706,731**	**$ 2,757,005**
Additional information		
Interest received	124,627	73,196

See accompanying notes.

NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2019 and 2018

1. THE ORGANIZATION

The Canadian Public Accountability Board/Conseil canadien sur la reddition de comptes (CPAB/CCRC) is a corporation without share capital incorporated under the *Canada Corporations Act*. CPAB is exempt from income tax in Canada as a not-for-profit organization under Section 149(1)(L) of the *Income Tax Act* (Canada).

As Canada's public company accounting firm regulator, CPAB oversees firms that audit the financial statements of Canadian reporting issuers. We promote sustainable audit quality through our robust audit quality assessment program, commenting on accounting and auditing standards, engaging with key stakeholders including audit committees, public company financial management, other regulators and institutional investors to accelerate improvements in audit quality domestically and abroad, and providing practicable insights that inform capital market participants and contribute to public confidence in the integrity of financial reporting.

2. SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared in accordance with Canadian accounting standards for not-for-profit organizations. These financial statements are presented in Canadian dollars which is also the functional currency of the organization. The significant accounting policies are as follows:

Cash and cash equivalents
Cash and cash equivalents consist of cash and guaranteed investment certificates, with maturities not exceeding 90 days, and insignificant risk of changes in value.

Revenue recognition
CPAB charges two types of fees to public accounting firms: an Intent to Participate fee that is collected from public accounting firms on their initial application to become Participating Audit Firms, and an Annual Participation fee that is collected from Participating Audit Firms. All fees are established to recover CPAB's costs, and to provide working capital for contingency purposes.

The Intent to Participate fee is a flat fee based on the number of reporting issuer clients of the applicant firm at the date of registration. Intent to Participate fees are recorded in the accounting period in which the firm is registered, and fees are received.

The Annual Participation fee is based on audit fees paid by Participating Audit Firms' reporting issuer clients. This fee is billed annually and recognized as revenue in the year to which it relates.

In certain circumstances, CPAB charges additional fees to Participating Audit Firms to recover costs incurred to monitor those firms. These fees are included in other fees and are recognized in the accounting period in which the work is performed.

Property, equipment and intangible assets
Property, equipment and intangible assets are recorded at cost less accumulated amortization. Amortization is calculated on a straight-line basis over the estimated useful lives of the assets commencing on the date when the assets are placed into service.

The estimated useful lives are as follows:

Office equipment and furniture	3 – 10 years	Computing equipment	2 years
IT infrastructure and networks	4 – 5 years	Leasehold improvements	Over the life of the lease
Computer software	3 – 5 years		

Investments
Investments are purchased for redemption in the near term and are accounted for at fair value. Realized and unrealized gains and losses are recognized as investment income when they arise. Transaction costs are expensed as incurred.

Leases
All of CPAB's leases are operating leases. Benefit tenant inducements received at the inception of a lease are deferred and recognized on a straight-line basis over the term of the lease.

Use of estimates
The preparation of financial statements in conformity with Canadian accounting standards for not-for-profit organizations requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the balance sheet date and the reported amounts of revenues and expenses during the year. CPAB has not made any significant estimates or assumptions in these annual financial statements.

3. FINANCIAL INSTRUMENTS AND RISKS

CPAB's financial assets include cash and fixed income guaranteed investment certificates (GICs) with major Canadian chartered banks. The cost of the GICs, plus accrued interest income, approximates their fair value. Other financial assets and liabilities are carried at cost, which approximates their fair value due to their short-term nature.

It is management's opinion that CPAB is not exposed to significant interest, currency or credit risks.

4. INVESTMENTS

Investments consist of fixed income GICs with maturities exceeding 90 days. GICs maturing within 12 months from the year end date are classified as current.

	2019	**2018**
GICs	$ 5,600,000	$ 5,100,000
Accrued interest	35,635	29,380
	$ 5,635,635	**$ 5,129,380**

GICs and short-term investments have interest rates ranging from 1.6% to 1.95% (2018: 1.2% to 1.95%).

5. ACCOUNTS RECEIVABLE

	2019	**2018**
Trade accounts receivable	$ 170,300	$ 85,181
Sales taxes recoverable	61,551	47,468
	$ 231,851	**$ 132,649**

6. PROPERTY, EQUIPMENT AND INTANGIBLE ASSETS

	Cost	*Accumulated Amortization*	*2019 Net*	*2018 Net*
Office equipment and furniture	$ 868,831	$ (690,291)	$ 178,540	$ 102,755
IT infrastructure and networks	2,263,121	(2,048,555)	214,566	313,561
Computing equipment	209,381	(88,011)	121,370	9,492
	3,341,333	(2,826,857)	514,476	425,808
Leasehold Improvements	2,029,165	(1,313,888)	715,277	617,013
Property and equipment	**5,370,498**	**(4,140,745)**	**1,229,753**	**1,042,821**
Software	311,186	(277,736)	33,450	26,724
Website	127,245	-	127,245	-
Intangible assets	**438,431**	**(277,736)**	**160,695**	**26,724**
Property, equipment and intangible assets	**$5,808,929**	**$(4,418,481)**	**$1,390,448**	**$1,069,545**

Intangible assets include the development costs of CPAB's external website ($127,245) launched in January 2020.

7. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	2019	**2018**
Trade accounts payable	$ 154,292	$ 84,001
Salaries, vacation and bonuses	1,888,551	1,305,931
Other accrued liabilities	276,725	52,371
	$ 2,319,568	**$ 1,442,303**

8. FEES

	2019	**2018**
Annual participation fees	$ 16,938,278	$ 16,642,862
Intent to participate fees	16,000	39,000
Other fees	75,500	68,375
	$ 17,029,778	**$ 16,750,237**

9. BANK CREDIT FACILITY

CPAB has a bank Credit Facility of $2,000,000 bearing interest at bank prime. Amounts owing under the Credit Facility are payable on demand. No assets have been pledged as collateral for the Credit Facility and no charges are incurred until the facility is drawn down. At December 31, 2019 and 2018 the amount owing under the Credit Facility was nil.

10. CASH FLOWS

Changes in non-cash working capital items are detailed as follows:

	2019	2018
Accounts receivable	$ 39,231	$ (35,245)
Accrued interest	(6,255)	(18,018)
Sales tax recoverable	(14,083)	(5,959)
Prepaid expenses	75,737	(208,203)
Accounts payable and accrued liabilities	652,712	(249,309)
	$ 747,342	**$ (516,734)**

Cash and cash equivalents are composed of:

	2019	2018
Cash	$ 519,534	$ 604,535
Short-term investments	2,187,197	2,152,470
	$ 2,706,731	**$ 2,757,005**

Non-cash transactions:

Investing activities:
In 2019 CPAB acquired property and equipment for a total of $667,435 of which $224,553 remained unpaid as at December 31, 2019. The unpaid balance is considered as non-cash transaction and is excluded from the cash flow statement.

Financing activities:
In November 2019, CPAB renewed its lease agreement for its Montreal office. As part of its new lease agreement, CPAB is entitled to receive a leasehold improvement allowance of $124,350. As at December 31, 2019, this allowance not received from the landlord is included in the trade accounts receivable. The allowance is considered as a non-cash transaction and is excluded from the cash flow statement.

11. COMMITMENTS

Commencing January 2017, CPAB entered into a ten-year four-month lease for office space in Vancouver. The annual rent expense is $57,450, and operating cost is estimated to be $67,535 per annum.

In February 2013, CPAB entered into an 11-year six-month lease for its Toronto head office. The annual rent expense is $306,475 for the term of the lease, and operating cost is estimated to be $305,393 per annum.

Commencing November 2019, CPAB entered a 10-year lease for office space in Montreal. The annual rent expense is $53,471, and operating cost is estimated to be $60,672. The organization has issued an unsecured letter of credit to the landlord for an amount of $21,270.

There are no asset retirement obligations associated with the leases.

CPAB's lease commitments within the next five years are as follows:

Within one year	$ 850,996
From two to five years	3,253,928
Over five years	951,574
	$ 5,056,498

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