



AUDIT COMMITTEE FORUM

CPAB Audit Committee Forums Highlights

The Canadian Public Accountability Board (CPAB) hosted four forums in June 2020 for audit committee chairs of Canadian reporting issuers to discuss the impact of COVID-19 on the financial reporting and audit process.

We are pleased to provide the following overview of the conversation.

What's top of mind

COVID-19 audit considerations

The global COVID-19 pandemic continues to significantly impact Canadian reporting issuers and their auditors. With increased challenges and more time spent on the audit, audit committees can expect the audit process will look different this year. Audit committees should invite conversations with management and auditors on what has changed and how audit quality is impacted.

The risk of fraud is now higher. There is a need for heightened awareness and discussion of stakeholder efforts to prevent and detect fraud.

Audit committees can help auditors better understand the impact of COVID-19 on their organizations and how their audit approaches might need to adjust for changing risks and conditions.

Remote work

Audit committee chairs commented positively on how management and auditors are responding to the COVID-19 pandemic. People and processes have rapidly adapted to remote work arrangements. Teams can mobilize quickly when needed, and in some cases, the quality of information has improved. However, we are currently at the beginning of what could be a long journey. Auditors and directors will need to continue to monitor how people are coping with the strain of longer work hours and balancing the needs of work and home. Frequent pulse surveys may be helpful to organizations in identifying early signs of mental fatigue.

Supervision and review

Corporate and audit firm management require new ways to effectively communicate regularly with staff. They are supervising and mentoring teams that may have irregular hours of work and could be under significant stress.

Auditors will need to use high levels of professional judgment to plan and execute the audit as the nature of evidence changes. Junior staff will need support to critically evaluate what they are reviewing. These factors will increase the importance of supervision and review by audit firm partners and senior staff in providing oversight and support to less experienced staff, including the use of technology for virtual meetings.

Audit committees may want to consider whether there are leading indicators, such as staff turnover on the engagement, that can help them to understand how staff and audit teams are coping in the current environment. Audit committees should also think about asking their auditor how they are instilling a skeptical mindset among their team members.

Internal controls

An increased focus on internal controls is critical right now:

- Businesses are more vulnerable to fraud in this environment.
- Remote work has led to significant changes to internal controls. Businesses are identifying opportunities to improve processes and accelerate the shift towards greater automation as a result of the crisis.
- Many businesses are facing increased financial burdens and resource constraints. This has led to staff reductions, making it more difficult to appropriately segregate duties and design an effective control environment.
- Cybersecurity risks are on the rise due to remote work.

Forum participants noted that sufficient testing has not yet been carried out this year to assess the effectiveness of internal controls. Management also may find it difficult to demonstrate the effectiveness of compensating controls, such as management supervision and oversight, when the business is operating remotely.

Given the potential magnitude of changes to internal controls, audit committees should consider encouraging earlier control testing by management and their internal and external auditors this year. This early approach can also allow additional time to remediate identified control deficiencies.

What are audit committees doing differently?

Audit committee's role

Audit committees have had to rapidly adjust to COVID-19. Participants commented on the current challenges of balancing their oversight and advisory roles. Audit committees are meeting more frequently, and chairs are interacting more often with chief financial officers (CFOs) and controllers to provide support and understand the issues they are facing. Management is also providing more frequent updates and reports to audit committees as conditions change. Audit committee focus has shifted towards greater oversight of forward-looking issues, including liquidity, cashflows, hedging strategies and capital allocation.

Audit committee chairs are also meeting more frequently with their auditors to understand how they are adapting to the crisis and to ensure they have access to the information they need to work effectively.

“The crisis is a stress test of the audit committee.”

– Audit committee chair

Accounting estimates

It is difficult to assess the reasonableness of assumptions and forward-looking information in the COVID-19 environment. Participants commented on the challenges they experience in their oversight of estimates, and the risks of being either overly conservative or optimistic in interim and annual reporting. Some noted the benefits of proactively involving the auditor earlier in the quarterly process and leveraging industry experts to support the review of material judgments and estimates.

Audit committee chairs expect impairment to be a significant issue this year. Forum discussions noted the importance of understanding potential impairment triggers, professional skepticism, and considering the long-term in assessing fair value estimates.

Audit committee chairs should consider meeting directly with their auditor's experts to understand their perspectives to help in their oversight.

Liquidity and going concern

Participants discussed the impact of the second quarter on trailing debt covenants and how banks might respond, including the possibility of covenant easing. Companies dealing with significant liquidity issues may need to enhance their liquidity disclosures.

Disclosures could provide boards with an opportunity to be more comprehensive and transparent in describing to stakeholders what is happening and their plans to address the challenges.

Audit committees should consider being proactive in raising going concern as a potential issue for discussion with management and their auditor. They should also consider how specific and meaningful their going concern disclosures about material uncertainty and significant judgments are to the reporting issuer. For close calls, where there is no material uncertainty for going concern, but considerable discussion was required to arrive at this conclusion, audit committees should consider whether significant judgment was applied that should be clearly and transparently disclosed.

Project management

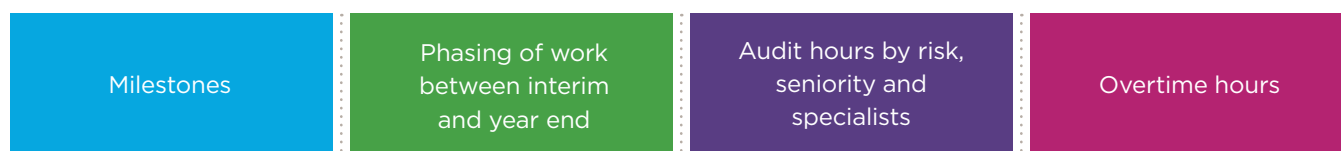
“Will management, audit committees and auditors be ready for year end?”

– Audit committee chair

Participants discussed what could go wrong in the audit process this year and how they can support a quality audit. More frequent communication will be important to identify early warning signs and prevent surprises.

Audit quality indicators (AQIs) could be helpful to support robust audit planning and execution, generate timely discussions and facilitate more collaboration. For example, audit firms and management can share and track the achievement of milestones throughout the audit to give better visibility into progress and to monitor for unexpected delays.

AUDIT QUALITY INDICATORS TO CONSIDER



Audit committees should consider getting involved earlier in the audit process and obtaining regular reporting of key indicators or dashboards to ensure there is an appropriate response to changing circumstances and increased workload for all involved.

Key audit matters

US-listed companies report on critical audit matters. TSX-listed companies will start reporting on key audit matters for periods ending on or after December 15, 2020. Audit committee chairs discussed how they will engage with management and auditors on key audit matters reporting early in the audit process in 2020. The potential for COVID-19 to dominate key audit matters reporting was discussed along with the need for disclosures to be specific in order to be useful to users.

Disclosures and non-GAAP measures

Participants commented that COVID-19 disclosures were more qualitative in the first quarter but expect to see more quantitative disclosures during the rest of the year. Companies are making operational and financing adjustments and could also be benefiting from efficiencies during COVID-19.

Participants discussed the nature of COVID-19 disclosures and the impact COVID-19 could have in or outside the financial statements.

There is no clear definition of a COVID-19 adjustment. Participants asked whether restructuring costs, the increase in the financial cost to access capital or the costs of suspending operations could be interpreted as COVID-19 costs. Depending on the duration of the pandemic, adjustments could also be one-time or recurring. It will be important to differentiate between pre- and post-COVID-19 adjustments.

Participants noted the recent guidance released by securities regulators to support robust and transparent COVID-19 disclosures. Proactive dialogue with the auditor to evaluate these types of issues could be beneficial.

CANADIAN AND DUAL-LISTED REPORTING ISSUERS MAY WANT TO CONSIDER THIS RECENT DISCLOSURE GUIDANCE:



- Canadian securities regulators remind issuers of importance of disclosure in financial reporting
- SEC - COVID-19 - Disclosure considerations regarding operations, liquidity and capital resources
- IOSCO statement on importance of disclosure about COVID-19

What audit committees should consider

Audit committees should consider the following for overseeing audits this year:



- How are auditors instilling a skeptical mindset in the current remote work environment?
- Are there leading indicators that might give insight into how staff and audit teams are coping?
- Are there key audit quality indicators or dashboards that could enhance communication, support the timeliness of the audit and help identify early warning signals?
- Could earlier control testing be helpful to allow for more time to remediate control deficiencies?
- Could it be useful to engage with the auditor's experts to hear their perspectives on work performed in complex or subjective areas?
- Could going concern be an issue to raise proactively with management and the auditor?
- Where going concern is an area of significant judgment, is this being clearly and transparently disclosed? Are going concern disclosures specific to the reporting issuer and meaningful to stakeholders?

Thank you

We would like to thank **Jocelyn Proteau**, Chair, BTB REIT and Richelieu Hardware and former Vice Chair of CPAB's board, **John Gordon**, audit committee chair of TORC Oil & Gas Ltd., and **Richard Graff**, audit committee chair of Yamana Gold Inc. for their advice and support in planning and moderating the forums. We are grateful for their involvement.

CPAB thanks everyone for their participation. We encourage ongoing dialogue and look forward to continuing the audit quality discussion at future events.

Have a view?

We'd like to hear from you. Please reach out to us at stakeholderengagement@cpab-ccrc.ca.

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