



AUDIT COMMITTEE FORUM

CPAB 2020 Audit Committee Highlights – A Year-end Review

The Canadian Public Accountability Board (CPAB) has been meeting regularly with audit committee chairs during the pandemic to understand the changes in the environment, facilitate a dialogue and contribute our perspectives. Earlier this year, we published **COVID-19 implications for audit committees**, summarizing our earlier one-on-one discussions, followed by **highlights** from the forums we hosted during the summer.

This fall, we continued our one-on-one outreach and hosted eight forums to share our perspectives and discuss the issues top of mind for audit committees as we approach the end of the year and look ahead to 2021.

The following summarizes our recent conversations.

Managing through economic uncertainty

Audits are taking longer. Management teams and auditors are spending more time navigating a process that is new and different. Increased complex accounting issues require deeper review, consultation and support from specialists. Audit committees play an essential role in overseeing management and the auditor through this turbulent period.

Focusing on liquidity and solvency

“ The challenge today is to predict what will happen in three, six and nine months.”

Audit committee chair

Management at companies hit hard by the pandemic are providing more thorough information and analysis to audit committees and auditors on their companies' long-term prospects. To assess whether their companies can continue as a going concern, audit committees are reviewing reverse stress tests – bottom-up scenario analyses to identify what could give rise to adverse outcomes such as a covenant breach. They are evaluating whether breaches could happen and how they could be prevented or mitigated.

Audit committees play a role in ensuring auditors have access to the information they need to support their assessment of going concern and are exercising sufficient levels of skepticism in challenging management's analysis.

Making challenging estimates

Audit committees are focused on how judgment is applied to make estimates. Inputs and assumptions could have wide ranges that significantly affect valuations. Audit committees can set the tone for a strong challenge process by encouraging management teams and auditors to engage in subjective areas of the audit.

Direct interaction with the auditor's valuation specialists at audit committee meetings can provide valuable perspectives on the reasonableness of valuations. Examples of areas for discussion include whether valuation reports are being qualified, and how estimates compare to industry peers, market information and other external evidence.

Adapting to significant changes in how audits are performed

Auditing in a remote environment is new. We continue to inquire about the quantity and quality of interactions between management and the auditor due to remote work. Some have observed that planning and preparation has improved, resulting in better communication and more productive meetings. We have also heard that the change to remote meetings and elimination of travel and other commitments can allow partners and senior members of the audit team to be more involved in engagement meetings and oversight.

Considering the risks of a remote audit, engagement teams also need to be aware that an increasing proportion of the audit conducted electronically underscores the importance of assessing the reliability of information sources and authenticating evidence.

Increased partner and manager involvement

Less experienced audit team members may find it difficult to gain the proper competencies and experience, build constructive relationships and absorb the culture of their firms at a critical stage in their careers. To respond to the increased risk and the need to supervise less experienced team members, partners and other senior staff need to dedicate more time to the audit to mentor and supervise their teams and provide on-the-job training.

Working with component auditors

Auditors working in different countries may also need to substantially change their audit approach. Group auditors unable to visit the local audit and management teams in person may find it more challenging to understand and evaluate how the audit approach has changed and to evaluate whether sufficient evidence has been obtained by the component auditors.

Audit committees should consider interacting directly with significant component auditors to understand their issues and challenges and ensure audit quality is maintained.

Heightened fraud risk

“ A lot of us are trained to think skeptically. The story is not written yet. It will be several months before a problem surfaces that brings to light a weakness we didn't see. And it might be because it is so obvious we didn't see it right in plain view. ”

Audit committee chair

The changing environment creates additional incentives and opportunities that increase the risk of fraud. Audit committees are asking how management and auditors are responding to the risk of override, collusion and aggressive practices. Audit committee chairs have observed emerging practices:

- Comprehensive ethics and cybersecurity training and annual staff and supplier attestations to instill greater awareness and set expectations for proper conduct.
- Management integrating fraud risk management into their internal controls and internal auditors incorporating fraud risk considerations into their plans and control testing.
- Participation by the audit committee in corporate whistleblower programs including receiving complaints directly and monitoring what management is doing to follow up and conclude.

Audit committees should consider inquiring how their external auditors have incorporated management's fraud risk management program and whistleblowing practices into their risk assessments and asking how effective they are.

Technological changes

Businesses are adopting technology faster. Auditors are investing in advanced information technology (IT) tools to assess risk and enhance their audit work. Audit firms are encouraging greater use of tools to assess fraud, automate routine work and standardize processes. They are also considering how to leverage machine learning and artificial intelligence into the audit. Audit committees may want to consider exploring with their auditors the tools that would improve audit quality but which they are not yet using or are using sub-optimally.

Audit committees are also stressing the importance of IT understanding and expertise across the audit team.

“ Audits are performed in a system, not around a system. ” *Audit committee chair*

Internal controls

Businesses are focused on reducing overhead in their efforts to contain costs and manage liquidity. This could put significant pressure on the control environment. New people in control roles may find it harder to become proficient in a virtual setting or be less inclined to ask for help. Similarly, companies could be affected by service organizations that experience delays in reporting due to changes in their control environment. Audit committees should focus on the impact of the pandemic on the quality of internal controls and whether there could be significant deficiencies that may take time to surface.

“ Some of the key controls are year-end controls. Could we have problems at year end because new people may not be on top of these controls as they were before? ” *Audit committee chair*

“ Tell me what controls you think have changed and to what extent you have changed your reliance on internal audit? ” *Audit committee chair*

Overseeing the audit

Audit quality indicators

Audit committees are asking management and auditors for audit quality indicators to serve as an early warning of possible future challenges — this could include information about the amount of time spent by partners, quality control reviewers, senior staff and specialists on key risk areas. Other indicators include significant changes in control deficiencies, reliance on internal controls by the external auditor, including IT, and measures that help understand how much or how little external auditors are relying on the work of internal auditors compared to the past.

Taking the appropriate time

In preparing for the upcoming year-end audits, management, auditors and the audit committee should all have the time they need to perform their role effectively given the risks and complexity of this year's audits. Audit committees should be asking if the work is on track or if additional time is needed. Taking additional time prior to finalizing the approval of financial statements and completion of the audit may be necessary to avoid future errors.

WHAT AUDIT COMMITTEES SHOULD CONSIDER



- How are auditors remotely instilling a skeptical mindset on their team?
- How is the risk of fraud considered in the audit process?
- Are there indicators that might give insight into the skills and experience of staff and audit teams and how they are working together?
- Could it be useful to meet with or invite experts and component auditors to the audit committee meeting to hear their perspectives on work performed in complex or subjective areas?
- Is the auditor getting the information they need to review management's assessment of going concern?
- 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 the following audit committee chairs for their advice and support in moderating our events this year:

- **Joanne Ferstman**, audit committee chair, ATS Automation Tooling Systems Inc., Dream Unlimited Corp., Cogeco Communications Inc. and Osisko Gold Royalties Ltd.
- **Garry Foster**, audit committee chair, SmartCentres REIT and Real Matters Inc.
- **John Gordon**, audit committee chair of TORC Oil & Gas Ltd. and Topaz Energy Corporation.
- **Richard Graff**, audit committee chair, Yamana Gold Inc.
- **Sara Lewis**, audit committee chair, Sun Life Financial.
- **Alan MacGibbon**, audit committee chair, The Toronto-Dominion Bank and past audit committee chair, CAE Inc.
- **Kathleen O'Neill**, audit committee chair, ARC Resources Ltd. and audit and actuarial committee chair, Ontario Teachers' Pension Plan Board.
- **Jocelyn Proteau**, past audit committee chair, Familiprix and Quincaillerie Richelieu and former vice-chair of CPAB's board.
- **Pierre Seccareccia**, audit committee chair, Ivanhoe Cambridge.

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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