



CANADIAN PUBLIC ACCOUNTABILITY BOARD  
CONSEIL CANADIEN SUR LA REDDITION DE COMPTES

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Tel 416.913.8260 Fax 416.850.9235 www.cpab-ccrc.ca

October 6, 2011

Office of the Secretary  
Public Company Accounting Oversight Board  
1666 K Street, N.W.  
Washington D.C. 20006-2803  
USA

Dear Sir:

**Request for Comment: Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards, PCAOB Rulemaking Docket Matter No. 34**

The Canadian Public Accountability Board (CPAB) is pleased to comment on the Public Company Accounting Oversight Board (PCAOB) *Concept Release on Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements and Related Amendments to PCAOB Standards* (the “Concept Release”). We believe now is the time for a fundamental review of the auditor reporting model (the “Reporting Model”) and we commend the PCAOB for engaging with stakeholders on how to enhance the quality, relevance and value of auditor reporting.

CPAB is Canada’s independent audit regulator responsible for overseeing firms that audit Canadian reporting issuers. Our mandate is to promote high quality independent auditing that contributes to public confidence in the integrity of reporting issuers’ financial reporting. We accomplish our mandate by inspecting audit firms and audit working paper files which provides us with insights into the application of auditing standards and how they might be improved.

**Transparency of the Audit**

Many investors are asking for more transparency from the auditor with respect to communications addressing the audit process and the auditor’s views on the underlying risks impacting the financial statements. The results of recent investor outreach show that many investors believe the current, largely boilerplate, audit report is not meeting their needs and they want deeper insights from the auditor. There is a perception that while the audit process is robust, the standard audit report does not adequately communicate the results of an extensive audit process.

In our view the status quo, with respect to auditor reporting, is not acceptable. Auditors need to provide greater value by sharing more information, related to the audit performed, directly with financial statement users (“Users”). Change needs to be responsive to the needs of Users, and

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should be implemented in a thoughtful, responsible way such that audit quality is enhanced and in no way diminished.

Since CPAB's mandate relates to listed entities in Canada our comments to follow are intended to apply solely to listed entities.

### **Auditor Commentary- Supplemental Reporting**

The Reporting Model should retain the current pass/fail opinion but should be expanded to include a supplemental auditor commentary (the "Commentary"). The Commentary should be targeted at areas that will provide the greatest insights to Users without negatively impacting the three-way interaction between the auditor, audit committee and management.

We suggest the following areas could be included in the Commentary:

- Comments on key areas of audit risk identified by the auditor, including a description of why the risks are significant, and the related audit approach;
- A summary of areas of significant auditor judgement, including the auditor's assessment of management's critical accounting judgements and qualitative aspects of the entity's accounting policies;
- A discussion of key inputs for significant assumptions and the basis for concluding that these were appropriate;
- A discussion of unusual transactions and significant non-recurring transactions, including the basis for the accounting adopted; and
- A description of the extent of reliance on auditors in foreign jurisdictions.

We believe the increased transparency provided by a Commentary as described above will improve audit quality and ultimately lead to improved disclosures in financial information, thereby benefiting Users. Clearly, the challenge will be to write reporting standards that provide appropriate guidance to auditors to ensure that any such Commentary does not become boilerplate over time or lead to investor confusion. Reporting standards will also need to be appropriately field tested prior to finalization.

We recognize many will resist this approach as being a substantive change from existing practice and there will be concerns with respect to consistency, legal liability and confidentiality. In our view this is a necessary change if audits are to continue to provide value and relevance to Users of financial reporting in the 21st century.

### **Emphasis of Matter Paragraphs in the Audit Report**

We support the expanded use of Emphasis of Matter paragraphs in areas of critical importance to the financial statements, including significant management judgements and estimates and areas of significant measurement uncertainty. This will assist Users in navigating their way through increasingly complex financial reporting by drawing attention to information within the financial statements that the auditor believes is critical to the Users understanding of the financial statements. We see the Emphasis of Matter Paragraphs as complementing and being cross-referenced to the more extensive Commentary described above. Emphasising these matters in the audit report should cause the auditor to focus more on the related audit procedures while focusing management more on the related significant judgements and disclosures, which should improve audit quality.

### **Other Information in Documents Containing Audited Financial Statements**

We support efforts to explore how the auditor can provide assurance on information outside the financial statements such as Management's Discussion and Analysis ("MD&A") or other information such as non-GAAP measures or key performance metrics. However, it is important that auditors have the necessary competence and skill set to provide such services in a cost effective and timely manner that adds value to Users. We see this as a longer term project that needs further study and should be incorporated into a more holistic review of the corporate reporting framework. In our view, the more pressing issue in the short term is determining how the auditor can provide Users with more relevant and better information related to the financial statement audit.

### **Global Auditor Reporting**

It is important for bodies such as the PCAOB, European Commission and International Auditing and Assurance Standards Board (IAASB) to work together to devise one global solution to the perceived deficiencies in auditor reporting. Since many audit reports are read globally; a more coordinated approach will improve consistency and mitigate investor confusion. Greater divergence in auditor reporting is not in the public interest.

In concluding we again commend the PCAOB for engaging with stakeholders on this important topic. Changes to the Reporting Model should be implemented in a cost effective way, ensuring that audit quality is enhanced and in no way diminished. In a global business environment that is continually changing and with increasingly complex financial reporting requirements, it is critical that auditor reporting evolves in a way that better meets the needs of financial statement users.

CPAB responded to the IAASB's Consultation Paper, *Enhancing the Value of Auditor Reporting: Exploring Options for Change*, and we attach a copy of our response for your information (see Attachment A). Our response to the IAASB Consultation Paper covered many of the areas where comments are requested in the Concept Release, and we believe these responses would be equally applicable to the Concept Release.

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We appreciate the opportunity to respond to the Concept Release, and would be pleased to discuss further any of the above comments.

Yours very truly,

A handwritten signature in black ink, appearing to read "Brian Hunt".

Brian Hunt, FCA  
Chief Executive Officer

cc. Mr. Bruce Winter, FCA  
Chair, Auditing and Assurance Standards Board (Canada)

Mr. Greg Shields, CA  
Director, Auditing and Assurance Standards  
The Canadian Institute of Chartered Accountants



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ATTACHMENT A

September 29, 2011

Technical Director  
International Auditing and Assurance Standards Board  
545 Fifth Avenue, 14<sup>th</sup> Floor  
New York, NY 10017  
USA

Dear Sir:

**Re: Consultation Paper on Enhancing the Value of Auditor Reporting: Exploring Options for Change**

The Canadian Public Accountability Board (CPAB) is pleased to comment on the International Auditing and Assurance Standards Board's (IAASB's) Paper *Enhancing the Value of Auditor Reporting: Exploring Options for Change* (the "Consultation Paper"). We believe now is the time for a fundamental review of the auditor reporting model and we commend the IAASB for engaging with stakeholders on how to enhance the quality, relevance and value of auditor reporting.

CPAB is Canada's independent audit regulator responsible for overseeing firms that audit Canadian reporting issuers. Our mandate is to promote high quality independent auditing that contributes to public confidence in the integrity of reporting issuers' financial reporting. We accomplish our mandate by inspecting audit firms and audit working paper files which provides us with insights into the application of auditing standards and how they might be improved.

**Corporate Reporting Framework**

While our comments focus on improvements to the auditor reporting model (the "Reporting Model"), we believe there is a need for a more holistic review of the corporate reporting framework in order to provide greater value to stakeholders. In our view, improvements to the Reporting Model should be part of a more comprehensive initiative to reform the corporate reporting framework which will require the active involvement of all stakeholders, including policy makers, investors, regulators, standard setters, corporate directors, company management and auditors.

## **Transparency of the Audit**

Many investors are asking for more transparency from the auditor with communications addressing the audit process and the auditor's views on the financial statements. The results of recent investor outreach show that many investors believe the current, largely boilerplate, audit report is not meeting their needs and they want deeper insights from the auditor. There is a perception that while the audit process is robust, the standard audit report does not adequately communicate the results of an extensive audit process.

In our view the status quo, with respect to auditor reporting, is not acceptable. Auditors need to provide greater value by sharing more information, related to the audit performed, directly with financial statement users ("Users"). Change needs to be responsive to the needs of Users, and should be implemented in a thoughtful, responsible way such that audit quality is enhanced and in no way diminished.

Since CPAB's mandate relates to listed entities in Canada our comments to follow are intended to apply solely to listed entities.

### **Auditor Commentary- Supplemental Reporting**

The Reporting Model should retain the current pass/fail opinion but should be expanded to include a supplemental auditor commentary (the "Commentary"). The Commentary should be targeted at areas that will provide the greatest insights to Users without negatively impacting the three-way interaction between the auditor, audit committee and management.

We suggest the following areas could be included in the Commentary:

- Comments on key areas of audit risk identified by the auditor, including a description of why the risks are significant, and the related audit approach;
- A summary of areas of significant auditor judgement, including the auditor's assessment of management's critical accounting judgements and qualitative aspects of the entity's accounting policies;
- A discussion of key inputs for significant assumptions and the basis for concluding that these were appropriate;
- A discussion of unusual transactions and significant non-recurring transactions, including the basis for the accounting adopted; and
- A description of the extent of reliance on auditors in foreign jurisdictions.

We believe the increased transparency provided by a Commentary as described above will improve audit quality and ultimately lead to improved disclosures in financial information, thereby benefiting Users. Clearly, the challenge will be to write reporting standards that provide appropriate guidance to auditors to ensure that any such supplemental commentary does not become boilerplate over time or lead to investor confusion. Reporting standards will also need to be appropriately field tested prior to finalization.

We recognize many will resist this approach as being too radical a change from existing practice and there will be concerns with respect to consistency, legal liability and confidentiality. In our view this is a necessary change if audits are to continue to provide value and relevance to Users of financial reporting in the 21<sup>st</sup> century.

### **Emphasis of Matter Paragraphs in the Audit Report**

We support the expanded use of Emphasis of Matter paragraphs in areas of critical importance to the financial statements, including significant management judgements and estimates and areas of significant measurement uncertainty. This will assist Users in navigating increasingly complex financial reporting by drawing attention to information within the financial statements that the auditor believes is critical to the Users understanding of the financial statements. We see the Emphasis of Matter Paragraphs as complementing and being cross-referenced to the more extensive Commentary described above. Emphasising these matters in the audit report will make the auditor focus more on the related audit procedures and focus management more on the related significant judgements and disclosures.

### **The Role of the Those Charged with Governance**

Audit committees have a key oversight role to play with respect to audit quality and high quality financial reporting. Continuous improvement in the two-way communications between the auditor and audit committees contributes significantly to audit quality, particularly given the increasing complexity and greater use of judgement in financial reporting. We believe it is important to further explore how communication between auditors and audit committees can be more forthright and transparent, particularly with respect to reporting of significant audit risks and related judgements. In our experience this is more of a challenge for smaller listed entities where corporate governance arrangements can be less formal.

In our view there is merit in considering having more transparent public reporting by audit committees on how they have discharged their responsibilities.

However, given the varying corporate governance models and practices used in different countries around the world it will be a challenge to implement an international model of enhanced corporate governance reporting to Users.

### **Other Information in Documents Containing Audited Financial Statements**

We support efforts to explore how the auditor can provide assurance on information outside the financial statements such as the Management's Discussion and Analysis ("MD&A") or other information such as non-GAAP measures or key performance metrics. However, it is important that auditors have the necessary competence and skill set to provide such services in a cost effective and timely manner that adds value to Users. We see this as a longer term project for the IAASB that needs further study and should be incorporated into a more holistic review of the corporate reporting framework. In our view, the more pressing issue in the short term is determining how the auditor can provide Users with more relevant and better information related to the financial statement audit.

## **Format and Structure of the Standard Auditor's Report**

We support the need to improve the format and structure of the existing standard audit report. We believe the explanations of management and auditor responsibilities should be retained within the audit report so that the report will be read with the appropriate context. However, the auditor's opinion should be given greater prominence and moved to the front of the audit report.

We agree that the technical language in the audit report could also be clarified, including terms such as "fair presentation", "materiality" and "reasonable assurance". Initially, such definitions should be included in the audit report with consideration to migration into a separate document or appendix over time.

## **Global Auditor Reporting**

It is important for bodies such as the IAASB, European Commission and United States Public Company Accounting Oversight Board to work together to devise one global solution to the perceived deficiencies in auditor reporting. Since many audit reports are read globally; a more coordinated approach will improve consistency and mitigate investor confusion. Greater divergence in auditor reporting is not in the public interest.

In concluding we again commend the IAASB for engaging with stakeholders on this important topic. Changes to the Reporting Model should be implemented in a cost effective way, ensuring that audit quality is enhanced and in no way diminished. In a global business environment that is continually changing and with increasingly complex financial reporting requirements, it is critical that auditor reporting evolves in a way that better meets the needs of financial statement users.

In addition to our comments above, our responses to the questions posed in the Consultation Paper are included in the Appendix to this letter.

We would be pleased to discuss further any of the above comments.

Yours very truly,



Brian Hunt, FCA  
Chief Executive Officer

cc. Mr. Bruce Winter, FCA  
Chair, Auditing and Assurance Standards Board (Canada)

Mr. Greg Shields, CA  
Director, Auditing and Assurance Standards  
The Canadian Institute of Chartered Accountants

## APPENDIX

### **1. Do respondents have any comments about the issues identified in Section II regarding the perceptions of auditor reporting today?**

Many investors are asking for more transparency from the auditor with communications addressing the audit process and the auditor's views on the audited financial statements. The results of recent investor outreach show that many investors believe the current, largely boilerplate, audit report is not meeting their needs and they want deeper insights from the auditor. There is a perception that while the audit process is robust, the standard audit report does not adequately communicate the results of an extensive audit process.

In our view the status quo, with respect to auditor reporting, is not acceptable. Auditors need to provide greater value by sharing more information directly with financial statement users ("Users") related to the audit performed. Change needs to be responsive to the needs of Users, and should be implemented in a thoughtful, responsible way such that audit quality is enhanced and in no way diminished.

### **2. If respondents believe changes in auditor reporting are needed, what are the most critical issues to be addressed to narrow the information gap perceived by users or to improve the communicative value of auditor reporting? Which classes of users are, in the view of respondents, most affected by these issues? Are there any classes of users that respondents believe are unaffected by these issues?**

#### **Auditor Commentary- Supplemental Reporting**

The auditor reporting model (the "Reporting Model") should retain the pass/fail opinion but should be expanded to include a supplemental auditor commentary (the "Commentary"). The Commentary should be targeted at areas that will provide the greatest insights to Users without negatively impacting the three-way interaction between the auditor, audit committee and management.

We suggest the following areas could be included in the Commentary:

- Comments on key areas of audit risk identified by the auditor, including a description of why the risks are significant, and the related audit approach;
- A summary of areas of significant auditor judgement, including the auditor's assessment of management's critical accounting judgements and qualitative aspects of the entity's accounting policies;
- A discussion of key inputs for significant assumptions and the basis for concluding that these were appropriate;

- A discussion of unusual transactions and significant non-recurring transactions, including the basis for the accounting adopted; and
- A description of the extent of reliance on auditors in foreign jurisdictions.

We believe the increased transparency provided by a Commentary, as described above, will improve audit quality and ultimately lead to improved disclosures in financial information, thereby benefiting Users. Clearly, the challenge will be to write reporting standards that provide appropriate guidance to auditors to ensure that any such supplemental commentary does not become boilerplate over time or lead to investor confusion. Reporting standards will also need to be appropriately field tested prior to finalization.

### **Emphasis of Matter Paragraphs in the Audit Report**

We support the expanded use of Emphasis of Matter paragraphs in areas of critical importance to the financial statements, including significant management judgements and estimates and areas of significant measurement uncertainty. This will assist users in navigating increasingly complex financial reporting by drawing attention to information within the financial statements that the auditor believes is critical to the users understanding of the financial statements. We see the Emphasis of Matter Paragraphs as complementing and being cross-referenced to the more extensive Auditor Commentary described above.

We believe these proposed changes will benefit all classes of users.

### **3. Do respondents believe that changes are needed for audits of all types of entities, or only for audits of listed entities?**

Our comments are made in the context of listed entities.

### **4. Respondents are asked for their reactions to the options for change regarding the format and structure of the standard auditor’s report described in Part A. Do respondents have comments about how the options might be reflected in the standard auditor’s report in the way outlined in Appendix 1 of this Consultation Paper?**

We support the need to improve the format and structure of the existing standard audit report. We believe the explanations of management and auditor responsibilities should be retained within the audit report so that the report will be read with the appropriate context. However, the auditor’s opinion should be given greater prominence and moved to the front of the audit report.

We agree that the technical language in the audit report could also be clarified, including terms such as “fair presentation”, “materiality” and “reasonable assurance”. Initially, such

definitions should be included in the audit report with consideration to migration into a separate document or appendix over time.

- 5. If the paragraphs in the current standard auditor’s report dealing with management and the auditor’s responsibilities were removed or re-positioned, might that have the unintended consequence of widening the expectations gap? Do respondents have a view regarding whether the content of these paragraphs should be expanded?**

See response to #4.

- 6. Respondents are asked for their reactions to the possibility that the standard auditor’s report could include a statement about the auditor’s responsibilities regarding other information in documents containing audited financial statements. Do respondents believe that such a change would be of benefit to users?**

We believe it would be appropriate for the audit report to explicitly address the auditor’s responsibility with respect to other information in documents containing audited financial statements. Many users may not understand the extent of auditor involvement with such information and clarification would benefit users.

- 7. If yes, what form should that statement take? Is it sufficient for the auditor to describe the auditor’s responsibilities for other information in documents containing audited financial statements? Should there be an explicit statement as to whether the auditor has anything to report with respect to the other information?**

There should be an explicit statement describing the extent to which the auditor has been involved with other information outside the financial statements. A starting point for developing such a statement should be ISA 720 “The Auditor’s Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements.”

- 8. Respondents are asked for their views regarding the auditor providing additional information about the audit in the auditor’s report on the financial statements.**

#### **Auditor Commentary- Supplemental Reporting**

Please see response to #2.

We recognize many will resist this approach as being too radical a change from existing practice and there will be concerns with respect to consistency, legal liability and confidentiality. In our view this is a necessary change if audits are to continue to provide value and relevance to users of financial reporting in the 21<sup>st</sup> century.

## **Emphasis of Matter Paragraphs in the Audit Report**

Please see response to #2.

### **9. Respondents are asked for their reactions to the example of use of —justification of assessments in France, as a way to provide additional auditor commentary.**

We support the use of a model that provides expanded use of Emphasis of Matters paragraphs in the audit report, similar to the justification of assessments in France but with expanded auditor commentary in a supplemental report. The challenge will be to ensure that the expanded disclosure adds value to Users without becoming boilerplate.

Please also see responses to #2 and #8.

### **10. Respondents are asked for their reactions to the prospect of the auditor providing insights about the entity or the quality of its financial reporting in the auditor’s report.**

Please see responses to #2 and #8.

### **11. Respondents are asked for their reactions to the options for change relating to an enhanced model of corporate governance reporting, as described in Section III, Part D.**

Audit committees have a key oversight role to play in ensuring both audit quality and high quality financial reporting. Continuous improvement in the two-way communications with audit committees contributes significantly to audit quality, particularly given the increasing complexity and greater use of judgement in financial reporting. We believe it is important to further explore how communication between auditors and audit committees can be more forthright and transparent, particularly with respect to the reporting of significant audit risks and related judgements. In our experience this is more of a challenge for smaller listed entities where corporate governance arrangements can be less formal.

In our view there is merit in considering having more transparent public reporting by audit committees on how they have discharged their responsibilities.

However, given the varying corporate governance models and practices used in different countries around the world it will be a challenge to implement an international model of enhanced corporate governance reporting to Users.

**12. To the extent that respondents support this model, what challenges may be faced in promoting its acceptance? Also, what actions may be necessary to influence acceptance or adoption of this model, for example, by those responsible for regulating the financial reporting process?**

Please see response to #11.

**13. Do respondents believe assurance by the auditor on a report issued by those charged with governance would be appropriate?**

Please see response to #11.

**14. Respondents are asked for their reactions to the need for, or potential value of, assurance or related services on the type of information discussed in Section III, Part E.**

Investors are increasingly using information outside the financial statements in their decision making. We believe there is merit in exploring how the auditor can provide assurance in areas such as the MD&A, non-GAAP measures or key performance metrics. However, it is important that auditors have the necessary competence and skill set to provide such services in a cost effective and timely manner that adds value to Users. For example, auditors may have limited expertise to provide assurance on such items as enterprise risk management and business models.

Standards will also need to be developed for auditors to provide assurance in these areas.

**15. What actions are necessary to influence further development of such assurance or related services?**

We see this as a longer term project for the IAASB which needs further study and should be incorporated into a more holistic review of the corporate reporting framework. In our view, the more pressing issue in the short term is determining how the auditor can provide Users with more relevant and better information related to the financial statement audit.

**16. Respondents are requested to identify benefits, costs and other implications of change, or potential challenges they believe are associated with the different options explored in Section III.**

These are addressed in the main body of the letter and our detailed responses above.

**17. Do respondents believe the benefits, costs, potential challenges and other implications of change are the same for all types of entity? If not, please explain how they may differ.**

Changes to the Reporting Model should be applied consistently across all listed entities. For smaller entities the reporting will generally be less complex. The challenges and costs will vary given differences in corporate governance structure and types of Users for smaller entities.

**18. Which, if any, of the options explored in Section III, either individually or in combination, do respondents believe would be most effective in enhancing auditor reporting, keeping in mind benefits, costs, potential challenges and other implications in each case? In this regard, do respondents believe there are opportunities for collaboration with others that the IAASB should explore, particularly with respect to the options described in Section III, Parts D and E, which envisage changes outside the scope of the existing auditor reporting model and scope of the financial statement audit?**

We believe Supplemental auditor reporting in the form of an **Auditor Commentary** and expanded use of **Emphasis of Matters paragraphs** in the Audit Report will be most effective in enhancing auditor reporting. Please also see our responses to #1 and #2 above.

We agree there should be greater collaboration with others by the IAASB. The IAASB, European Commission and United States Public Company Accounting Oversight Board should work more closely together to devise one global solution to the perceived deficiencies in auditor reporting. Since many audit reports are read globally; a more coordinated approach will improve consistency and mitigate investor confusion. Greater divergence in auditor reporting is not in the public interest.

**19. Are there other suggestions for change to auditor reporting to narrow the —information gap perceived by users or to improve the communicative value of the auditor’s report?**

We have no other comments.