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To whom it may concern,

We appreciate the opportunity to comment on the Auditing and Assurance Standards Board (AASB) Exposure Draft - Proposed Amendments to Canadian Auditing Standard (CAS) 240 – Fraud CAS (CAS 240).

We are generally supportive of the proposals in CAS 240, *The Auditor's Responsibilities Related to Fraud in an Audit of Financial Statements* and believe most of the new guidance will enhance audit quality. We do, however, have concerns relating to some of the specific questions asked by the International Auditing and Assurance Standards Board in your request for comment and these concerns are outlined in our responses to those questions below.

Does ED-240 clearly set out the auditor's responsibilities relating to fraud in an audit of financial statements, including those relating to non-material fraud and third-party fraud?

It is not clear how to interpret and apply paragraph A18 of the standard, which states that “depending on the nature and circumstances of the entity, certain laws, regulations or aspects of relevant ethical requirements dealing with corruption, bribery or money laundering may be relevant to the auditor's responsibilities to consider laws and regulations in an audit of financial statements in accordance with ISA 250”.

We believe that additional clarification and guidance is necessary to address whether the proposed wording expands an auditor's responsibilities beyond the scope currently required in CAS 250, *Consideration of Laws and Regulations in an Audit of Financial Statements*. This guidance should better explain the requirements in the standard, and whether the proposed CAS 240 will require an auditor to find information on all instances of non-compliance with laws or regulations to consider whether any of these issues are related to corruption, bribery, or money laundering. Without clear guidance in the proposed standard, there may be confusion on the application of this guidance and the depth at which an auditor must assess noncompliance with laws and regulations.

Does ED-240 appropriately enhance transparency about matters related to fraud in the auditor's report?

One of the objectives of the amendments to the standard is to provide additional transparency to stakeholders on fraud-related procedures conducted by the auditor and to 'clarify the role and responsibilities of the auditor for fraud in an audit of financial statements'¹.

We are concerned that the proposals in CAS 240, specifically the use of Key Audit Matters (KAM), may not meet these objectives and could widen the expectations gap over the auditor's role. The changes in the definition of a KAM would result in a significant change in current practice in Canada, may result in inconsistencies between other disclosure documents and KAMs, and may be challenging for auditors to implement. We are also concerned that there could be significant legal implications if auditors report on any form of suspected or alleged fraud. We believe the current definition, interpretation, and application of KAMs is appropriate and provides users with information about matters relating to fraud requiring significant auditor attention.

Should the standard require additional disclosures related to fraud, we believe that identified and assessed fraud risks and the auditor's response should be outside the KAM section of the Independent Auditor's Report unless the fraud risk meets the definition of a KAM. For most entities, this disclosure would focus on significant fraud risks associated with revenue recognition and management override of controls, among other fraud risk factors where applicable. These disclosures should be entity-specific to avoid boilerplate language on an auditor's approach to fraud, as previously observed in the United Kingdom². We believe that auditors should be able to apply their professional judgement in determining whether meaningful disclosure can be made related to these matters. By describing the significant fraud risks associated with entity specific financial reporting matters and the auditor's response when an entity-specific circumstance has occurred, this disclosure would meet the objective of increasing the transparency of the auditor's work associated with fraud, while not widening the expectations gap of the auditor's responsibility for detecting fraud.

We highlight our specific concerns with the KAMs approach below:

¹ ED CAS 240: EXPLANATORY MEMORANDUM paragraph 5 (a) and (d).

² We believe that the proposed language in the standard could lead to an increase in boilerplate disclosure related to fraud risks. The Association of Chartered Certified Accountants (ACCA) in their "*Key Audit Matters: Unlocking the Secrets of the Audit*" publication [March 2018] noted that "in the first year of implementation in the UK, most audit reports did include the risk of misstatement due to fraud in revenue recognition as a KAM. The FRC's first year review was critical, noting that it was unhelpful for there to be KAMs that are generic rather than specific and that such disclosure did not comply with the requirement for KAMs to be 'of most significance... in the current period'. As a result, disclosure of fraud in revenue recognition as a KAM dropped significantly in the second year and subsequent years in the UK. ... The feedback from participants at roundtables supported the infrequent mention of fraud. It would be appropriate in those circumstances where it had been one of the most important areas of the audit in the period, but otherwise participants did not expect it to be included within the KAMs". Link: https://www.accaglobal.com/content/dam/ACCA_Global/professional-insights/Key-audit-matters/pi-key-audit-matters.pdf

Key Audit Matters in Canada

It is unusual for the independent auditor's report of a Canadian public company to report fraud-related matters as a KAM. This is because fraud-related matters rarely meet all the conditions required to report a KAM under CAS 701, *Communicating Key Audit Matters in the Independent Auditor's Report*³.

The statement in the proposed amendments to CAS 240 that it would be rare that the auditor would not determine at least one KAM related to fraud in the audit of a complete set of general-purpose financial statements for a listed entity is inconsistent with the Canadian experience in applying CAS 701 and will result in a significant change in practice. Importantly, the basis for determining KAMs has not changed, other than consequential amendments to CAS 701 removing paragraph A21, which references fraud related risks as an example that not all significant risks require KAM disclosure⁴.

If these proposals are adopted, we believe the research related to the conclusion that there should be at least one fraud-related KAM should be shared as part of a broader educational outreach to familiarize practitioners and users with this change.

Expectations Gap

The financial reporting disclosure standards relating to fraud are limited, and management may interpret current guidance as not requiring disclosure of fraud-related matters in financial statements unless they are quantitatively material, as is current practice. In some cases, management may meet any disclosure obligations of fraud-related matters through other disclosure documents, such as press releases or the management, discussion & analysis (MD&A). Without explicit disclosure of fraud in the financial statements, we are concerned that fraud related KAMs may be inappropriately referenced to other disclosure documents and extend the auditor's responsibilities to information beyond the financial statements.

³ Based on a review of all companies on the TSX, TSX-V and CSE that reported KAMs, there were only two filers which provided disclosure on a fraud investigation or any other fraud related KAMs in calendar 2022. This was based on an analytical review of KAMs filed using the platform AuditAnalytics, which generates its data through a review of all financial information in the Canadian market. The data generated was filtered by exchange (included TSX, TSX-V and CSE), and then a search was conducted for all KAMs with the word "fraud" in their title or description. As of April 11, 2024, this generated two KAMs. The CCAQ also reviewed Critical Audit Matters (CAMs) reported on the AuditAnalytics platform for fiscal 2022 on April 29, 2024, and noted that there were two KAMs that directly referenced fraud, one that referenced a whistleblower complaint, four that mentioned insufficient audit evidence over internal controls, and 15 that noted a material weakness in internal controls.

⁴ Current guidance in CAS 701 paragraph A21 is as follows: "*However, this may not be the case for all significant risks. For example, ISA 240 presumes that there are risks of fraud in revenue recognition and requires the auditor to treat those assessed risks of material misstatement due to fraud as significant risks. ...Depending on their nature, these risks may not require significant auditor attention, and therefore would not be considered in the auditor's determination of key audit matters in accordance with paragraph 10.*"

Revised wording would change that guidance to the following: "ISA 240 (Revised) presumes that there are risks of fraud in revenue recognition and requires the auditor to treat those assessed risks of material misstatement due to fraud as significant risks. ...The auditor may determine these matters to be key audit matters related to fraud because risks of material misstatement due to fraud are often matters that both require significant auditor attention and are of most significance in the audit. However, this may not be the case for all these matters. The auditor may determine certain risks of material misstatement due to fraud did not require significant auditor attention, and, therefore, these risks would not be considered in the auditor's determination of key audit matters".

The proposed amendments to CAS 240 will require that when an auditor determines that there are no KAMs related to fraud to communicate, the auditor include a statement to this effect in the KAMs section of the auditor's report. There is no requirement for the auditor's report to specifically reference that there are no KAMs related to other commonly reported matters, such as impairments or revenue recognition, as the current wording required is "we have determined that there are no [other] key audit matters to communicate in our report."

We are concerned that users may misinterpret the statement to mean that there is additional assurance being provided over the existence of fraud further contributing to the expectations gap. It may also be confusing to a user, and exacerbate the expectations gap, if a fraud is disclosed in a press release, or the MD&A, however the auditor reports that there are no key audit matters to communicate related to fraud.

Comparability

Given the number of audits conducted under the Public Company Accounting Oversight Board (PCAOB) auditing standards in Canada, it would be useful for the AASB to highlight differences in reporting KAMs with Critical Audit Matters (CAMs) relating to fraud in the standard's basis for conclusion to reduce misunderstanding and improve comparability.

Weighing the Public Interest

Paragraph A176 of the proposed CAS 240 indicates that it will be extremely rare for a matter determined to be a key audit matter not to be communicated in the auditor's report. There is a presumed public interest benefit in providing greater transparency about the audit and associated fraud risks. However, disclosure is omitted when adverse consequences to the entity or the public could occur because the impact of the communication of the fraud or suspected fraud is viewed as so significant that the consequences of disclosure would be expected to outweigh the public interest benefits of communicating the matter.

We are concerned with the practical application of this requirement and believe additional guidance, including practical examples, would benefit both auditors and preparers in determining whether adverse consequences to the entity outweigh the public interest benefits of disclosure.

Do you believe that the IASB has appropriately integrated scalability considerations in ED-240 (i.e., scalable to entities of different sizes and complexities, given that matters related to fraud in an audit of financial statements are relevant to audits of all entities, regardless of size or complexity)?

We are concerned that the scalability considerations as provided in the proposed CAS 240 will not be sufficient guidance for Canadian practitioners serving entities listed on the TSX-V or private enterprises. Most conditional items apply to entities irrespective of size or complexity but given the nature of the entities may require additional judgement and consideration by the

auditor. There is also a risk that KAMs or other disclosures may become boilerplate for smaller entities as the preparer and the auditor responses to fraud risk factors will be common.

We believe that further consideration should be given to providing explanatory materials for auditors on the scalability of fraud risk factors more prevalent in TSX-V reporting issuers and private entities to ensure that the guidance provided is clear and properly incorporates the circumstance of smaller, less complex entities.

Other Matters

We believe that the illustrative examples provided in the standard as it relates to the rebuttal of fraud risk in revenue recognition should be expanded on to include more nuanced, complex examples to provide practitioners with application guidance to determine if a fraud risk rebuttal is appropriate.

We appreciate the work done by the IAASB and the AASB on this critical area and the opportunity to comment on these proposals. If you have any questions or require additional information, please contact me at michael.walke@ccaq-ccqa.com.

Yours very truly,



M. C. Walke

The Canadian Centre for Audit Quality (CCAQ) is an independent not-for-profit Canadian corporation dedicated to supporting Canadian audit firms and public accountants in fulfilling their public interest role, and investors and other stakeholders with public policy and public interest issues. The CCAQ's founding members are the seven largest Canadian independent registered CPA accounting firms.