

IMPLEMENTING THE NEW CANADIAN AUDITING STANDARDS: After Busy Season — What You Need to Do Now

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INTRODUCTION

For Canadian practitioners, the world of auditing is about to change! For all audits of financial statements with period ends on or after December 14, 2010, the suite of 36 new Canadian Auditing Standards (CASs) apply.

Do these new rules apply to you? If you perform audits of financial statements, the answer is a clear and resounding "yes". The CASs apply to the audits of all financial statements. This includes audits that are both large and small, for public companies, private companies, not-for-profits, and government. In a nutshell, regardless of size or industry, the CASs rule.

Is this a significant change? That depends. The CASs certainly encompass more requirements than we've ever had before. The extent of real change in many cases, however, will depend on how closely the practitioner has been following best practice by performing truly risk-based audits. The CASs are focused on requiring auditors to plan, perform and report their audits using a risk-based approach. For public accounting firms that fully implemented the changes required by the last Canadian overhaul of Generally Accepted Auditing Standards (GAAS) in 2006, the CASs may not require further substantial change, other than some notable differences.

For firms that have not yet moved to a risk-based audit approach as outlined by the current Assurance Handbook, the move to auditing under the CASs could be extensive. As we transition to auditing in this new CAS environment, firms should use this opportunity to update their audit practices to be in line with the requirements of risk-based auditing.

TRANSITION

The new Canadian Handbook has been divided into two parts. Part I includes the new CASs, along with the CSQC 1 requirements (*Quality Control for Firms that Perform Audits and Review for Financial Statements*) that came into effect on December 15, 2009. Additionally, other standards for engagements other than audits of financial statements are also contained in Part I. Part II holds current GAAS. Depending on the year end of the financial statements being audited, you must select the correct part of the Handbook to follow.

Be careful. Remember, early adoption of the CASs is not permitted. This means that there will be a point in time in 2010 where some auditors will need to perform different audits using the two different audit platforms...at the same time!

As auditors are finishing up an audit using current GAAS, and planning audits under the new CASs, it is critical to ensure that relevant rules are applied.

BRINGING YOUR FIRM UP TO SPEED

The October 2009 CA Practice Advantage article *Implementing the New Canadian Auditing Standards—What You Need to Do Now for a Successful Transition* gave practitioners three “To Dos” to get ready. Many firms have already started implementing them. Here are some reminders of things to focus on now that the busy season is almost behind us, and you begin to implement the To Dos:

1. Appoint one person within the firm to lead the change initiative and be held accountable for the successful transition to the CASs.

This is a critical step to ensure your firm is ready in time to meet the impending deadline. With competing firm priorities, anchor this initiative with a strong firm leader to ensure a successful transition.



2. Develop a plan to address your firm’s methodology, processes, and staff training and assess the impact on specific audit engagements.

Firm methodology and processes

Auditors must start by reading the actual CASs to identify differences in requirements from current standards. Firms must identify necessary changes in their firm methodologies, including the audit approach and processes, to put a plan in place to make the necessary amendments. Firm standard audit programs, checklists and templates must all be analyzed and amended where necessary.

Staff training

Staff will require training to efficiently implement CASs. All engagement team members should be encouraged to read and understand the standards themselves and to discuss implementation issues that they see. Hands-on training with revised firm audit methodologies, programs and tools will help minimize difficulties and inconsistencies when putting the standards into practice. Offices will have to decide if they are able to provide training with in-house resources, through Institute or other vendor provided courses, or perhaps collaborate with colleagues in joint office sessions.

Specific audit engagements

Firms should consider their audit client base and determine which engagements will be affected most by the requirements of the new CASs. How can auditors make that determination? It can only come from a client-by-client, individual engagement assessment. Auditors are encouraged to act now. Auditors can debrief their busy season audits while they are still top of mind. Any audits still in process should also be tackled immediately. Create CAS focused planning memos for next year’s audits complete with the identification of specific CASs that will represent the most change.

3. Communicate with Clients

Audit deliverables and coordination

The CASs will not go unnoticed by clients. The auditor's primary deliverable, the audit report, has changed. There will also be changes in communication requirements, timing of audit work, the amount of client assistance required and various audit letters of communication.

Auditors have heightened requirements for communicating specific matters to management and those charged with governance throughout the audit process. All parties should be notified in advance of what to expect and when to expect it.

In some cases, the timing of the audit work performed may change. To be effective, auditors may have to do more planning, and do more of it at the client site. Auditors may require more or different client schedules and have deadlines for schedules that differ from previous years.

Finally, the various letters of communication used throughout the audit, for example, management representation letters and engagement letters, will likely encompass new language and new terms to comply with the new CASs.

The CASs provide an excellent opportunity for auditors to educate their clients upfront and early and partner with their clients for a smooth transition to the new CAS environment.

Consider distributing this CAS brochure to your clients which provides a concise, practical look at the changes and how the changes will affect them. Download for free from www.cica.ca/clientdev-CAS

Audit fee considerations

It is almost inevitable that at least some clients will be concerned with the impact of the CASs on audit fees. Firms should expect there will be additional costs associated with complying with the CASs. There will be, for example, training costs and administrative changes to firm forms and processes. Additionally, it will be necessary to amend various communication reports and letters with clients such as the audit report, the engagement letter and management representation letter.

The good news is that these increased costs will be a one-time hit for many practitioners, and it will be a business decision for each firm to determine which engagements, if any, will have increased audit fees.

As with any change, auditors should look at the adoption of the new standards as an opportunity to review their existing firm policies and engagement files to look for efficiencies and improvements that often get overlooked when we continue to "do what we did last year".



AREAS OF POTENTIAL BIG IMPACT

The audit process in the CAS environment—understanding the entity and its environment, performing risk assessments and responding to risks of material misstatement—is largely unchanged from current GAAS. There are, however, CASs dealing with specific areas of the audit that contain a number of new requirements that may have a big impact on you and your clients. The following table highlights some of the most common areas. Of course, there may be others depending on the circumstances of the engagement.

	Audit Area	How it Might Affect Your Audit	How it Might Affect Your Client
Audit Report CAS 700	This is one of the most notable changes from current Handbook requirements. The Audit Report is noticeably longer with six paragraphs instead of the current three. It is also more explicit regarding the responsibilities of management and the auditor. Under the CASs, there is a broader range of reporting options and more flexibility in the form of the report.	In most cases where general purpose financial statements are prepared in accordance with GAAP, there will be limited change to audit work effort. In other situations, for example for financial statements currently receiving Section 5600 reports, auditors will be required to do more work to determine the appropriate form of the audit report under the new reporting model.	Clients need to be made aware of this change so they can be ready to advise all key stakeholders such as the Board of Directors, shareholders, and banks.
Subsequent events and dating of the auditor's report CAS 560/700	The current Handbook concept of dating the audit report on the date of "substantial completion" of the audit does not exist in the new CAS environment. The CASs state the audit report should be dated when the auditor has obtained <i>sufficient appropriate audit evidence</i> .	Auditor's reports will in many cases be dated later than under current Canadian GAAS. Where an Engagement Quality Control Review is performed, it will need to be completed by the date of the auditor's report rather than the report issue date. Subsequent events procedures may need to be extended to the later audit report date.	Clients may wish to reduce the time between the completion of the financial statements by management and their approval by the Board of Directors to speed up the audit completion process. Management representations will be required up to the later audit report date.
Going concern CAS 570	Current existing GAAS has no standard equivalent to CAS 570.	Auditors must consider going concern issues in the pre-engagement phase and when understanding the entity and its environment and performing risk assessment procedures. When potential issues are identified, additional procedures, as outlined in CAS 570, should be performed.	The preparation of the financial statements require management to assess the entity's ability to continue as a going concern. The auditor's report may contain an Emphasis of Matter paragraph if the use of the going concern assumption is appropriate but a material uncertainty exists. The auditor must communicate with those charged with governance events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern.

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Related Parties and Related Party Transactions (RPTs) CAS 550	<p>CAS 550 is consistent with the overall thrust of requirements in the existing Handbook but is much more explicit and prescriptive in what the auditor must do with respect to RPTs.</p>	<p>The auditor must explicitly consider and evaluate RPTs throughout the audit and ensure audit documentation captures the assessments and judgments made. Additional procedures include:</p> <ul style="list-style-type: none"> • Discussion of RPTs in the engagement team discussion of the susceptibility of the entity's financial statements to misstatement • Obtaining an understanding of controls over RPTs and significant transactions outside of the ordinary course of business • For identified significant business transactions outside the normal course of business, evaluate the business rationale and inspect underlying contracts and agreements. 	<p>Management will be asked about controls it has in place over RPTs, including significant transactions outside the normal course of business.</p> <p>Management and, where appropriate, those charged with governance will be asked to provide specific written representations with respect to RPTs.</p> <p>The auditor has specific communication responsibilities to those charged with governance with respect to RPTs.</p>
Management Estimates CAS 540	<p>CAS 540 provides more requirements and application material than existing GAAS. It focuses the auditor's work on estimates that have a risk of material misstatement and, in particular, those that have high estimation uncertainty.</p>	<p>Auditors must perform risk assessment procedures specific to any significant management estimates. For example, auditors are required to obtain an understanding of how management makes accounting estimates and an understanding of the data on which they are based.</p> <p>Auditors must also review the outcome of accounting estimates made in prior periods to evaluate management's estimation abilities and determine if there is any bias.</p>	<p>Management may be asked to provide more information to the auditor concerning, among other things, how it identifies those transactions, events and conditions that may give rise to the need for accounting estimates to be recognized or disclosed in the financial statements.</p>
Group Audits CAS 600	<p>This CAS applies to audits where financial information about components (such as an entity or business activity) is included in the financial statements being audited. This would include financial information for the following components or combination of components:</p> <ul style="list-style-type: none"> • subsidiaries, joint ventures, or investees accounted for by the equity or cost methods of accounting • a head office and one or more divisions or branches • a function, process, product or service (or group of products or services), or geographical location. 	<p>The biggest issue here is applicability. Auditors must act as early as possible to evaluate their upcoming audit engagements to determine if these criteria apply.</p> <p>For engagements where this CAS applies, the group engagement partner is responsible for the direction, supervision and performance of the group audit engagement.</p>	<p>Where audit engagements are identified to meet the criteria of a group audit, auditors should take care to ensure clients are informed of the key requirements of this standard. Clients should be notified that more work will be performed in this area compared to previous years. They will be asked to provide additional schedules when necessary. There will be increased interaction and coordination across group auditors who may be at different geographical locations. The group partner may determine it prudent to travel to other locations to meet with group engagement teams.</p> <p>The group auditor will communicate with the group audit committee and management regarding such things as deficiencies in internal control that are group wide or specific to components of the entity and fraud.</p>

IMPLEMENTING THE NEW CANADIAN AUDITING STANDARDS: After Busy Season — What You Need to Do Now

	Audit Area	How it Might Affect Your Audit	How it Might Affect Your Client
Auditor Communications CAS 260/265/450	<p>Auditors have heightened requirements for communicating with management and those charged with governance on a timely basis. Auditors must establish a communication process and communicate the form, timing, and expected general content.</p>	<p>CAS 260 requires auditors to communicate matters in writing related to their independence and fees for audit and non-audit services for listed entities only.</p> <p>For audits of non-listed entities, although the auditor is not required by CAS 260 to communicate independence matters with the audit committee, provincial Rules of Professional Conduct may require such communication in writing at least annually. This is consistent with CAS 260, para A21, which requires the auditor to comply with relevant ethical requirements.</p> <p>The auditor must communicate all significant deficiencies in internal control in writing to those charged with governance on a timely basis. The classification of a significant deficiency is a matter of judgment.</p> <p>CAS 450 provides more detailed requirements for evaluating and communicating misstatements identified during the audit.</p>	<p>Management and those charged with governance should be made aware that they will be receiving a proposed communication process from their auditors.</p> <p>They should be made aware that auditors will use judgment to determine which deficiencies, if any, are significant deficiencies. The concept of a material weakness does not exist in the CASs.</p> <p>Management will be requested to correct all misstatements accumulated during the audit. Those charged with governance will be requested to correct any remaining uncorrected misstatements.</p>

CONCLUSION

The CASs apply to all financial statement audits ending on or after December 14, 2010. The deadline is fast approaching. The time to act is now! There is a need to become aware of plenty of requirements, and the implications to some firms may be substantial. Firms must make it an immediate priority to understand the impact of the CASs on their firms and their clients, and communicate changes to clients to ensure a smooth transition to the new auditing environment!

Visit www.cica.ca/cas often to check for new resources to assist your firm with the transition to the CASs.



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