

February 1st, 2021

International Auditing and Assurance Standards Board  
529 Fifth Avenue  
New York  
NY 10017

**Subject: DP/2020/09 – *Fraud and Going concern in an audit of financial statements***

The Canadian Securities Administrators Chief Accountants Committee appreciates the opportunity to comment on the International Auditing and Assurance Standards Board's ("IAASB" or the "Board") Discussion Paper *Fraud and Going concern in an audit of financial statements* (the "Discussion Paper"). The Canadian Securities Administrators ("CSA") is an organization of Canada's provincial and territorial securities regulators whose objective is to improve, coordinate and harmonize regulation of the Canadian capital markets. The CSA Chief Accountants Committee ("CAC") is comprised of the Chief Accountants from the provinces of Alberta, British Columbia, Ontario and Québec.

We support the IAASB's effort to address issues and challenges related to fraud and going concern in audits of financial statements and the role of auditors in these areas. We provide the following comments about a few key aspects of the preliminary views outlined in the Discussion Paper that we believe could be further explored.

## **I. Expectation gap**

### ***Question 1(a) and (b) – Main cause of the expectation gap relating to fraud and going concern in an audit of financial statements***

#### **(a) Fraud**

Within the knowledge gap component of the expectations gap, we agree that the current wording prescribed for an auditor's report does not clearly explain the nature, extent and limitations of the auditor's responsibilities in relation to fraud. The statement "the risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control," (per Appendix C1 of ISA 700 – *Forming an opinion and reporting on financial statements*) does not explicitly state that the standards do not require the auditor to detect fraud. Related to this knowledge gap, in response to the evolution gap, the IAASB should consider expanding the requirements and enhancing procedures in the auditing standards targeted at the identification of risks relating to fraud for better detection of fraud. However, the IAASB should ensure that the costs to implement and apply any new requirements do not outweigh the benefits. It appears auditors themselves are considering changes to address the evolution gap, as highlighted by the response to the Wirecard scandal

by EY Global Chairman Carmine Di Sibio, where he noted: “Many people believe that the fraud at Wirecard should have been detected earlier and we fully understand that. Even though we were successful in uncovering the fraud, we regret that it was not uncovered sooner”<sup>1</sup>.

With respect to the performance gap, page 11 of the Discussion Paper states that for the purposes of the Discussion Paper, the IAASB is limiting its consideration of the performance gap to issues resulting from an auditor not doing what is required because the requirements are not clear or leave room for misinterpretation. We agree that the performance gap may be the result of auditors not having sufficient understanding in the area of fraud. However, in the table on page 13, the examples in the first and fourth bullets of “aspects that require further consideration” relating to the performance gap are where the auditors do not meet the existing standards due to time and client pressures. These bullets raise additional considerations (e.g., quality control procedures, audit fee pressures) that are not within the scope of this Discussion Paper, and therefore we have not commented on these issues even though we agree these are concerns. We note that if an auditor knowingly does not meet existing standards, changing the terminology used in the audit standard (as proposed in the Discussion Paper) or changing the requirements in the audit standards will not address this type of performance problem. We recommend to the Board to pursue these types of performance concerns separately.

Relating to the evolution gap, we agree that users of financial statements are looking for enhanced procedures in relation to fraud that are not currently required by auditing standards. Based on the public response to the high-profile corporate failures highlighted in the Discussion Paper, we think users expect the auditor to more rigorously identify, assess, and carry out audit procedures responsive to, the risks of material misstatement due to fraud. Technological advances have contributed to the evolution gap and we think stakeholders expect auditors to be able to leverage new technologies in the financial statement audit. We recommend the IAASB consider modernising the standards to reflect technological advances, for example where an auditor can use technology (e.g., data analytics, data mining, or other forensic techniques) for fraud detection, to increase the coverage of audit samples or to reduce some of the more mundane or routine procedures that have to be done so that auditors can focus on the areas of greatest risk and on key judgments that management is making.

(b) Going Concern

We think the expectation gap relating to going concern is largely due to the knowledge gap resulting from the unclear wording in the auditor’s report relating to going concern in conjunction with an emphasis of matter paragraph. The wording, “when a material

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<sup>1</sup> <https://markets.businessinsider.com/news/stocks/cy-chairman-expresses-regret-over-wirecard-audit-failures-2020-9-1029591270>

uncertainty exists relating to events or conditions that may cast significant doubt on an entity's ability to continue as a going concern," is vague and in some cases, not understood by users of the financial statements. The term "going concern" itself may not be well understood by users. We think the existing auditor responsibilities with respect to going concern are clear; however, the auditor's report does not highlight that the auditor does not make a positive assessment of going concern. To close the knowledge gap relating to going concern, we think the IAASB could require communications of the auditor's responsibilities relating to going concern, as listed on page 21 of the Discussion Paper in the auditor's report in all instances. In addition, if there is no emphasis of matter paragraph in the auditor's report, the IAASB could consider adding wording consistent to the wording at the bottom of page 22 of the Discussion Paper: "The absence of any reference to a material uncertainty about the entity's ability to continue as a going concern in an auditor's report cannot be viewed as a guarantee as to the entity's ability to continue as a going concern".

## **II. Fraud**

### ***Question 2(a) – Should the auditor have enhanced or more requirements with regard to fraud in an audit of financial statements?***

As discussed in section 1(a), the evolution gap suggests the IAASB should consider expanding requirements and enhancing procedures in the standard targeted at the identification of risks relating to fraud for better detection of detect fraud, subject to the cost-benefit considerations noted above.

With respect to current requirements, we think there is an opportunity for enhanced education, training and development of professional skepticism for audit staff/teams. *ISA 300 – Planning an audit of financial statements* requires the involvement of key engagement team members in the audit planning and they have to establish the audit strategy with the appropriate experienced resources for high risk areas. To guide auditors, we think the Board should clarify the appropriate experience requirements for high risk areas. Specific requirements may be helpful to enhance education, training and development of professional skepticism when performing an audit.

### ***Question 2(c) – Enhanced fraud identification by inclusion of a “suspicious mindset”***

We have some concerns about the use of the term “suspicious mindset” as this term is not defined in the Discussion Paper. The introduction of a new term could exacerbate the expectations gap. Furthermore, since the “professional skepticism” concept, as described in *IAS 200 – Overall objectives of the independent auditor and the conduct of an audit in accordance with Canadian Auditing Standards*, already covers the identification and the

assessment of material misstatement, whether due to fraud or error, it is unclear how using the term “suspicious mindset” would contribute to enhanced fraud identification. However, we do think that there is an opportunity for the IAASB to enhance and evolve the concept of “professional skepticism” and reconsider how it should be applied throughout the audit. Notwithstanding the above, if a “suspicious mindset” concept is proposed in the standard, it should be well defined and clearly distinguished from the term “professional skepticism.”

***Question 2(d) – More transparency needed about the auditor’s work in relation to fraud***

We support the view of the IAASB that a non-material misstatement related to fraud may be indicative of a bigger issue. In that context and because the primary responsibility for prevention and detection of fraud rests with both those charged with governance of the entity and management<sup>2</sup>, we are of the view that the communication with those charged with governance, as required by *ISA 260 – Communication with those charged with governance*, could be enhanced to include all instances of fraud (including for non-material fraud).

We are of the view that only adding more disclosure in the auditor’s report may not be sufficient to reduce the expectation gap, rather the focus should be placed on enhanced procedures and more specific requirements in the current auditing standards. After concluding on any changes to the auditing standards in regards to expanded requirements or procedures relating to the detection of fraud (as discussed in our response to question 2(a)), the IAASB should revise the wording in an auditor’s report to more clearly communicate the nature, extent and limitations of the auditor’s responsibilities.

**III. Going concern**

***Question 3(a) – Should the auditor have enhanced or more requirements with regard to going concern in an audit of financial statements?***

**(a) Consideration of the Accounting Framework**

We think that any changes to the auditing standards should be considered in tandem with the relevant responsibilities of issuers in the applicable accounting framework. In this regard, we note that the auditor’s requirements for “close call” going concern situations in *ISA 570 – Going Concern* do not adequately align with the accounting and disclosure requirements in IFRS.

As part of the auditor reporting project that was concluded in 2015, the IAASB revised *ISA 570 – Going Concern* regarding the auditor’s work effort in relation to the IFRS framework (i.e., auditors are required to evaluate the adequacy of

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<sup>2</sup> *IAS 240 – The auditor’s responsibilities relating to fraud in an audit of financial statements*

disclosures in the “close call” situations in view of the requirements of the applicable financial reporting framework<sup>3</sup>). However, because the requirement for issuers to disclose the close calls is only explicitly expressed in an IFRIC agenda decision (which has less prominence compared to the authoritative standards), we have found that some auditors do not adequately assess these disclosures and are concerned that entities may not be aware they need to provide them. Indeed, in the course of our regulatory reviews, we have observed limited instances of “close call” judgements disclosure in the financial statements. As a next step, we think that the IASB should revise the main body of IAS 1 – *Presentation of financial statements* to explicitly require close call significant judgements disclosure. We note that U.S. GAAP contains explicit requirements in this regard, and that the New Zealand Accounting Standards Board has proposed clarifications along these lines.

(b) Auditor Requirements

We note that throughout most of the duration of the IAASB’s auditor reporting project that was concluded in 2015, the suite of standards contained a proposed requirement for auditors to provide an explicit, direct statement about whether a material uncertainty had been identified, and the appropriateness of management’s use of the going concern assumption. However, that proposed requirement was ultimately excluded from the final suite of standards. Given the current market conditions combined with the heightened public attention that the topic of going concern in financial statement audits continues to receive, we think that the IAASB should re-consider whether such disclosure should now be required. We think such disclosure would improve the quality of financial reporting and provide decision useful information to investors. Greater transparency in the auditor’s report could also lead to different behaviors by management. For example, greater transparency may result in higher accountability as issuers may expect their judgements to be scrutinized more comprehensively.

***Question 3(c) – More transparency needed***

(c) User Needs

We support the IAASB’s view that challenges pertaining to going concern are best addressed through a multi-stakeholder approach. In particular, we think that the role of users (i.e., investors) should be actively considered and explored in order to better understand their needs in terms of going concern in the context of a financial statement audit.

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<sup>3</sup> The IAASB developed paragraph 20 of ISA 570 – *Going Concern* with reference to a specific IFRS IC agenda decision. Requiring the auditor to evaluate the adequacy of disclosures in “close call” situations in view of the requirements of the applicable financial reporting framework was made in reference to the respective July 2014 IFRIC Agenda Decision. For further context, please refer to the IAASB publication. [https://www.ifac.org/system/files/meetings/files/Supplement\\_to\\_Agenda\\_Item\\_D\\_Auditor-Reporting-on-Going-Concern\\_final.pdf](https://www.ifac.org/system/files/meetings/files/Supplement_to_Agenda_Item_D_Auditor-Reporting-on-Going-Concern_final.pdf)

Yours truly,

**The CSA Chief Accountants Committee**

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