

September 29, 2021

VIA EMAIL: consultation@cpab-ccrc.ca

Canadian Public Accountability Board

RE: Joint submission on potential changes to the Canadian Public Accountability Board (“CPAB”) regulatory disclosures

Deloitte LLP, Ernst & Young LLP, KPMG LLP and PricewaterhouseCoopers LLP are pleased to respond to CPAB’s July 19, 2021 request for input into the potential changes on regulatory disclosures. We are supportive of CPAB’s efforts to increase transparency, and provide the following comments with the goal of working collaboratively with CPAB to ensure that regulatory changes improve sustainable audit quality and protect the public interest.

As noted by CPAB, any changes to CPAB’s regulatory disclosures will require reviews and revisions of the relevant provisions of the *Canadian Public Accountability Board Act* (“**CPAB Act**”) and CPAB Rules, as well as other applicable rules and legislation. In addition, we note that changes may necessitate revisions of client engagement terms, including for example, any confidentiality or reporting provisions. For these reasons, if CPAB decides to move forward with its proposed changes, including amending its Rules, after this initial consultation and after considering the consequences of such proposed changes, we would appreciate the opportunity to participate in discussions and provide further submissions.

1. *Disclosure Principles*

a. *Comments on CPAB proposed disclosure principles including any other principles CPAB should consider.*

We support CPAB’s disclosure principles of improvement in audit quality, timeliness of CPAB’s reporting and remediation of audit deficiencies, public accountability, and the costs versus benefits of any potential changes. We believe that increasing transparency around audit practices will assist in delivering high quality audits and enhancing trust. This will drive greater accountability for auditors, reporting issuers, and regulators, and boost the public’s understanding of the role and independence of audit firms.

We provide the following comments in regard to the principles for consideration:

- i. Meaningful and relevant disclosure: As CPAB notes in its consultation proposal, there is a risk that the nature and extent of CPAB’s review will be misunderstood. We agree that this is a significant risk and believe that countering it should be a priority in the development of any format or process for CPAB disclosure. It should be a primary objective of any disclosure changes that disclosed information is put clearly in context and in a manner that the user can understand. In particular, we agree that as part of any disclosure, CPAB should explain that its risk-based methodology for choosing files for inspection is not likely to be representative of a firm’s entire audit engagement portfolio and instead focuses on the most complex sections of a file with greater risks of material misstatement.

- ii. Consistency of disclosure: In comparing any proposed CPAB disclosure changes to other Canadian and international regulators, it will be important to consider not only the disclosure standards of other regulators, but also the underlying processes utilized by those regulators. For example, a regulatory system involving more formalized and quasi-judicial hearing and adjudication processes may warrant very different disclosure than a more flexible, informal, consultation-based regulatory oversight system and may therefore not be properly comparable.
- iii. Protecting confidentiality of audit clients: In a reflection of CPAB's mandate to oversee audit firms, while we support changes to the disclosure of CPAB's oversight work, we believe that it is of the utmost importance that any regulatory disclosures maintain the confidentiality of reporting issuers and our clients. Protecting audit clients' confidentiality will guard against potential harms, including the release of confidential information, market disruption, and exposures to private or class action litigation based on any reported deficiencies. By extension, protecting confidentiality will help ensure that reporting issuers and our clients continue to have confidence in the regulatory process, and by extension in the audit process, and to provide full and frank disclosure to their auditors. All of this promotes audit quality. We are also mindful of audit firms' duties to maintain confidentiality under the CPAB Act¹, the *Chartered Professional Accountants of Ontario Act, 2017*², and the CPA Code of Professional Conduct³. Engagement agreements between the audit firms and their clients also often contain confidentiality provisions. For all these reasons, we believe that it is critical that any disclosure changes ensure that confidentiality of reporting issuers will be protected. These protections should encompass both the risk of express disclosure of the identity of reporting issuers and the risk of indirect or "constructive" disclosure of identifying information that would permit third parties to identify a reporting issuer.

Overall, we are committed to the above disclosure principles to help ensure public confidence in the effective and independent oversight of Canadian audit firms and, in turn, the Canadian financial reporting system.

2. Communication to audit committees

- a. ***Should CPAB pursue amendment of its Rules to make the sharing of the results of individual audit file inspections with the audit committee (or others charged with governance if there is no audit committee) of that reporting issuer mandatory?***

We are supportive of CPAB amending its Rules to make the sharing of results of individual audit file inspections with the audit committee mandatory across all audit firms. As voluntary participants in CPAB's Protocol for Audit Firm Communication of CPAB Inspection Findings with Audit Committees (the "**Protocol**"), we believe that transparent communications with the audit committee is important.

- b. ***Should this sharing of information be mandatory for all reporting issuers? Why or why not?***

¹ *Canadian Public Accountability Board Act (Ontario), 2006*, S.O. 2006, c. 33, Sched. D, s. 11(2).

² *Chartered Professional Accountants of Ontario Act, 2017*, S.O. 2017, c. 8, Sched. 3, s. 60(1).

³ *Chartered Professional Accountants, Code of Professional Conduct*, s. 208.

We believe the proposed sharing of information should be mandatory for all reporting issuers. We do not believe that differences with respect to reporting issuers, such as the size of an issuer, the exchange the issuer is listed on, or the nature of the entity, significantly change the importance of audit quality, the role of the audit committee or equivalent body, and the importance of the auditor's role. Although there may be varying levels of financial reporting sophistication of reporting issuers, the disclosure of inspection results would at minimum prompt a discussion of the inspection process and findings with the reporting issuer and those charged with governance, and would promote a focus on efforts to improve audit quality.

3. Disclosure of the results of CPAB's regulatory oversight activities

a. Should CPAB pursue amendments of its Rules to allow for disclosure of findings by individual firm? Please explain.

We agree that there is an increased desire for more transparency around inspection results in Canada for firms. We believe meeting the desire for enhanced transparency is necessary to maintain trust and confidence in the profession in Canada, and for this reason we support the proposed disclosures of findings by individual firm.

Although we are supportive of this proposed change, there are a few considerations we would note. First, as stated above, disclosure should not include findings that would identify any given reporting issuer, whether expressly or based on inference from the other disclosed information. In addition to the reasons we noted above in our discussion of disclosure principles regarding confidentiality and openness, disclosure of information at the reporting issuer level may also result in higher costs from including another level of detailed information and reduced timeliness in the completion of CPAB's reviews.

Second, disclosure on an individual firm level must be made consistently across all audit firms. This means that if CPAB discloses firm-level findings, it must do so for all firms and a firm cannot elect to refrain from publicly reporting their inspection results. If CPAB discloses firm-level findings for some firms and not others, this could lead to inconsistent disclosure and a lack of comparability, thereby undermining investor confidence. Additionally, if CPAB discloses firm-level findings for some firms and not others, investors may incorrectly assume that firms for which no disclosure was made are of superior quality with no negative findings. This would have a negative effect on both audit quality and market confidence.

Third, before any public disclosures of findings by individual firm, firms should be permitted and be given sufficient time to respond to the results of the findings. Currently, an inspected audit firm has 30 days to respond to CPAB's draft inspection report.⁴ The audit firm then has 15 days to review and respond once the CPAB provides a revised draft inspection report.⁵ We believe that in considering disclosure changes, CPAB should consider that there is a connection between the extent of disclosure of findings, and the procedural fairness of the process used to arrive at those findings. In the event that CPAB publicly discloses inspection findings of any individual firm, such firm should be permitted to respond to the disclosure to provide context to the public. Concurrently with this proposed change, CPAB should also consider the reasonableness of the time for firms to respond and weigh this against the need for timely reporting and remediation.

⁴ Canadian Public Accountability Board Act Rules, r. 409 [CPAB Rules].

⁵ CPAB Rules, r. 410.

Finally, if CPAB discloses the results of inspections findings on an individual firm level, the audit firms should be able to disclose those same inspection findings in their own reports to their clients in order to facilitate dialogue with its stakeholders.

b. What type of information would be most useful and how would this information be used?

The information that would be useful to disclose to the public includes the number of reporting issuers audited by the audit firm and the number of files with significant inspection findings. We also believe that the disclosure of themes and issues across the firms is important information to identify possible systemic or emerging issues and the specific audit deficiencies being identified.

Consistent with the Protocol, we believe that only significant inspection findings should be included in any public disclosures. If non-significant findings are disclosed, investors and the public may not be able to assess or differentiate the significance of the inspection findings, which may lead to confusion.

While disclosure of a firm's system of quality management ("QMS") evaluations may provide useful information, the incorporation of QMS into CPAB's inspection methodology is still relatively new. Additionally, the impending move to International Standard on Quality Management ("ISQM 1") will create additional change that would have to be addressed in any disclosure model. As such, we believe that the results of QMS should not be included in CPAB's reporting or public disclosures at this time and we suggest that further consideration is required as to the nature and extent of such disclosures.

c. Should these disclosures be provided for all inspections of Participating audit firms?

If CPAB publishes inspection findings on an individual firm level, the disclosures should be provided for all inspections of Participating Audit Firms in order to provide consistent and relevant information.

4. Disclosures related to CPAB's enforcement actions

a. How would the information about CPAB's enforcement actions be used?

While we understand this question to have not been primarily directed to audit firms, we note that we would consider disclosed information about CPAB's enforcement actions against other firms to identify any issues or considerations related to the performance of audits, audit quality, and professional requirements. We would also use this information to determine if additional focus in terms of training, monitoring, or guidance is required.

b. Should CPAB's disclosures about enforcement actions apply to all enforcement action or be focused on specific (categories/types) breaches of professional standards?

We believe CPAB should not disclose all enforcement actions. Disclosing all breaches without any consideration of the severity and the risk of harm to the investing public could lead to several unintended consequences, including increased costs, delays in finalizing conclusions, and disclosure of information that is not meaningful or that could be misinterpreted or misunderstood.

As CPAB notes in its consultation notice, if a firm engages in conduct which violates professional standards that may impact audit quality, CPAB has the authority to impose enforcement actions, including a “Requirement, Restriction or Sanction”. While we support the disclosure of such enforcement actions, we suggest that CPAB provide additional guidance on the three enforcement actions, including information about the differences between the three actions, in order to clarify what types of enforcement actions and breaches will be disclosed.

Any disclosures should be designed to protect procedural fairness, and it is possible that the changes under consideration may require amending the Rules to ensure enhanced procedural fairness mechanisms. For example, under the current CPAB Rules, if CPAB considers a “violation event” has occurred, CPAB may propose requirements, restrictions or sanctions for the audit firm.⁶ If there are enhanced enforcement disclosures, a “violation event” should be proven instead of being determined to have occurred by the CPAB alone. Further, procedures relating to review proceedings under Section 700 of the CPAB Rules should be reviewed and considered. CPAB should consider disclosing enforcement actions only after a matter has been finally adjudicated. CPAB would also need to provide more clarity on the arbitration rules and appeal rights. In comparison, the Public Company Accounting Oversight Board (“**PCAOB**”) Rules require a statement of allegations, an ability for the audit firm to provide a responding defence, discovery-related procedures, and set procedural rules relating to hearings.⁷

5. Any other comments about potential unintended consequences or other costs from changes to CPAB’s disclosures.

CPAB should consider whether enhanced disclosures may have impacts on audit firms’ willingness to take on riskier clients or industries, the competitiveness of the audit market, and the profession’s ability to retain and attract quality candidates.

6. Other areas where CPAB should consider changes to our disclosures.

CPAB should consider a further or enhanced review/appeal process for audit firms that do not agree with a particular finding or disclosure.

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We appreciate this opportunity to submit our responses to CPAB’s proposed disclosure changes. We would be pleased to participate in any further consultations and provide submissions as requested.

Best regards,

Deloitte LLP, Ernst & Young LLP, KPMG LLP and PricewaterhouseCoopers LLP

⁶ See CPAB Rules, r. 601.

⁷ See PCAOB Rules, “Section 5. Investigations and Adjudications”.