



**CANADIAN PUBLIC ACCOUNTABILITY BOARD
CONSEIL CANADIEN SUR LA REDDITION DE COMPTES**

**2013-2015
Strategic Plan**

Meeting the Regulatory Challenge in a Global Environment

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Executive Summary

During its first 10 years, the Canadian Public Accountability Board (CPAB) has made a significant contribution to audit quality in Canada. From a standing start, it moved quickly to engage subject matter experts and implement a risk-based inspection methodology. Driven by a culture of integrity, commitment and collaboration, CPAB has demonstrated that it can perform effectively and the organization has much to be proud of.

In 2009 when CPAB struck its strategic plan, it was at a key juncture in its evolution. At that time, the organization refined its vision and defined and began to deliver on a new value proposition for its key stakeholders. This was done when the global economy was facing numerous challenges across many sectors, including looming professional skills shortages and the introduction of new international accounting and auditing standards. Over the past three years, CPAB has evolved its inspection methodology, systems and processes, and people to provide effective audit oversight that stakeholders and the international community view positively.

The thrust of CPAB's 2013-2015 Strategic Plan is to build on these accomplishments and further enhance the organization's effectiveness in the face of heightened challenges to audit quality.

In April 2012, CPAB stated in its Public Report that the rate of audit deficiencies in Canada was too high. This conclusion was based on CPAB's 2011 inspections of complex files across audit firms of all sizes. While only a few restatements were required, CPAB concluded that the potential for additional restatements was too high.

In April 2013 CPAB stated in its Public Report that overall there was a 30 per cent decline in audit deficiencies in the audit files inspected, indicating a reduced risk of restatements.

While the 2012 inspection results were better than in 2011, there was considerable difference among firms in the degree of improvement. A number of firms still needed to make significant improvements. Since the inspection results were finalized in the late fall of 2012, CPAB has been actively involved with the leadership of these firms regarding the root causes of the inspection findings. CPAB believes that the recent remedial actions taken by these firms in response to CPAB's findings will produce the necessary improvements.

While the decrease in the number of audit deficiencies is encouraging, CPAB believes firms must commit to continuous improvement at all levels of their organizations to ensure that this trend continues. This includes, in some cases, a shift in audit firm culture to encourage collaboration and enhanced accountability in order to embed quality into the audit process. CPAB believes a multidisciplinary team approach to the audit, where different expertise is brought together and held accountable, would best serve the needs of both public companies and the investing public.

To address these concerns, CPAB required major firms to develop action plans to improve audit quality. CPAB's 2013 inspections indicate that these plans have resulted in some improvement, but the key question is whether the improvement is sustainable. Certain firms have devoted additional resources to embed quality into the audit process (such as pre-issuance quality monitoring review of audit files); whether these layered-on processes, which reduce margins, will continue in light of business pressures remains to be seen. While audit methodologies are generally sound, and the majority of audits are well done, consistent execution of the audit by the firms continues to be a challenge. These findings must be viewed against a backdrop of business and fee pressures, challenges dealing with the international operations of reporting issuers, and the dynamics of the global economy, which are dramatically increasing the complexity of audits. To achieve success, the action plans must be fully implemented and sustainable for the longer term. Feedback to CPAB also indicates there is room for us to materially enhance information we provide to stakeholders such as audit committees, to support their role in audit quality.

To effectively address these challenges, CPAB is undergoing a strategic shift which began in 2013. This shift will enable the organization to meet its regulatory mandate, through inspections of a selection of completed audits, and by enhanced contributions to sustainable improvement in the overall audit process, involving a broader range of stakeholders.

CPAB will focus on four priorities to address this strategic shift:

1. Thought Leadership
2. Stakeholder Engagement
3. Risk Management
4. Focused, Effective Inspections

These priorities will be operationalized by:

- Embedding risk analysis and assessment more deeply into the fabric of the entire organization. This means thinking about audit risk and the implications of risk in all aspects of CPAB's operations.
- Analyzing the root causes of audit deficiencies more effectively and then making more targeted interventions, with measures that will result in sustainable improvements.
- Making more value-added recommendations/requirements to/on audit firms.
- Providing greater transparency in CPAB's communication of inspection results and about the key drivers of audit quality to help key stakeholders in the audit process perform their roles more effectively.
- Proactively engaging key stakeholders, such as audit committees, in a dialogue on a range of issues designed to enhance audit quality.

CPAB will also continue to participate in the domestic regulatory agenda and will influence the development of the international audit regulatory framework through its leadership position in International Forum for Independent Audit Regulators (IFIAR).

CPAB has and will continue to focus on cost containment and productivity. CPAB has increased its activities in outreach and in inspections while maintaining its annual fees at 2% (of audit fees) to reporting issues.

An overview of the 2013-2015 Strategic Plan is found in Appendix 1. An operating plan detailing goals and actions for fiscal year 2014 is contained in a separate document.

Environment and Challenges to Audit Quality

The operating environment of the audit sector is in a state of flux. This is characterized by the:

- Globalization of audit firms and reporting issuer business structures and practices
- Rapid development of complex financial products
- Proposed changes to the auditing/regulatory framework
- Evolution of new audit standards to respond to changes
- Increasing expansion by Canadian reporting issuers internationally, and the associated audit challenges
- Lack of a cohesive international audit regulatory framework against which to assess audit quality
- Pressure on increasing the revenue and profitability of the audit business, which continues to conflict with audit quality considerations, and
- Ongoing skills shortages

Proposed regulatory changes are originating from Europe and the United States due, in part, to perceived auditing deficiencies in the lead-up to the 2008 financial crisis. Furthermore, the European debt crisis and accompanying volatile economic environment is affecting Canada, particularly financial institutions and their auditors.

Similarly, political, regulatory and other agendas in Europe and the United States will lead to changes in either auditing or regulatory standards that Canada will be obligated to adopt, or that will have a significant impact on Canada.

Audit risk typically increases during economic downturns, given the greater incentive for fraud and aggressive accounting. In addition, the number of foreign companies listing on Canadian stock exchanges has increased audit risks.

Commercial considerations, including the profitability of individual firms, partner performance evaluation and compensation, and the impact of global networks potentially conflict with professional conduct and public service. Long-term profitability is key to success, and quality is key to sustained audit firm profitability.

These developments are taking place against a backdrop of increasing complexity of financial reporting, which is calling into question the relevance of this reporting and the value of the audit process, including its structure, content and output. This has led to the IAASB and the PCAOB issuing proposals to dramatically change the auditor's report (e.g. requiring the auditor to identify key audit matters in the audit report and describe how they were addressed).

Notwithstanding efforts made by CPAB in recent years, audit committees and institutional investors lack an appropriate understanding of CPAB and its role and do not have access to CPAB insights on audit quality or audit inspection results. Furthermore, the audit is increasingly becoming a commodity, which puts audit quality at risk. These factors, in the aggregate, present an opportunity for CPAB to engage in more targeted outreach to and a dialogue with audit committees and other stakeholders. This outreach would include providing key stakeholders with more guidance and fostering an enhanced understanding of the value of the audit and of the value of CPAB's regulatory oversight.

Last, but of primary importance, competition for talent throughout the audit sector continues to be high. This has direct implications on the ability of individual firms to perform quality audits and on CPAB's ability to attract and retain qualified professionals.

Four Priorities

This Strategic Plan addresses four priorities:

1. Thought Leadership
2. Stakeholder Engagement
3. Risk Management, and
4. Focused, Effective Inspections

Actions on these priorities will reinforce each other to further enhance audit quality.

1. Thought Leadership

CPAB believes it can make a significant contribution to enhancing audit quality and investor protection by engaging in a dialogue and raising awareness among key stakeholders about all aspects of audit quality. This can be achieved through such means as research and publishing discussion papers. Topics could include the:

- Changing global audit regulatory framework
- Consistency of audit execution
- Rapid evolution of business models and financial products, and the related audit risks, and
- Impact of the structure and culture of audit firms on audit quality

In addition, CPAB continues to comment on areas where auditing standards need to improve. For example, CPAB is considering providing implementation guidance/expectations in areas where it believes the implementation of auditing standards needs to be improved. CPAB met with the CPA Auditing and Assurance Standards Board in 2013 to advise them of the need for further implementation guidance on certain auditing standards.

Convening roundtables and conferences, such as CPAB's Audit Quality Symposium, and publicizing their results, represents other significant opportunities to advance audit knowledge and practice.

Through its thought leadership, CPAB is in a unique position to contribute to the state of audit quality, audit committee effectiveness and international audit regulatory development.

2. Stakeholder Engagement

Audit firms and financial statement preparers are not the only part of the audit process. Audit committees, institutional investors and analysts also play important roles. By providing all stakeholders with better information on audit quality issues, and by engaging in a dialogue with them about CPAB's overall findings, all stakeholders, including CPAB, can perform their roles more effectively. There must be substantive engagement with key stakeholders on the implications of challenges to audit quality and the range of appropriate responses. CPAB continues to proactively engage with audit committees and other stakeholders, and is continuing to work effectively with senior firm leadership, to enhance audit quality.

3. Risk Management

An assessment of CPAB's internal risk universe identifies six principal categories of risk:

- Reputation (effectiveness)
- Quality/Operations
- Human Resources
- Technology
- Legal and Regulatory, and
- Financial and other

Strategically, it is important for CPAB to implement processes to keep abreast of the many risk factors affecting the organization and ensure we are, and are seen to be, effective in meeting our mandate to contribute to public confidence in financial reporting. These processes include: research and analysis of the reporting issuer population (specifically identifying outliers); ongoing environmental scanning (including media); root cause-focused inspections, and key stakeholder engagement. These measures will help embed risk discipline in the fabric of the organization. More specifically, gathering the right data (on the economy, changes in the profession, activities of reporting issuers,

media monitoring, and global influences), data analysis, and modeling risk scenarios enhances CPAB's risk capability. Further, better integration between Risk and Inspections enables CPAB to better focus its resources on the reporting issuers and firms that pose the greatest risk to the investing public.

Beyond these measures, CPAB fosters and promotes a culture of professional skepticism and intellectual rigour relative to risk management, which helps to elevate its focus, presence and impact as a regulator.

4. Focused, Effective Inspections

CPAB's current inspection methodology provides a sound basis for evaluating audit quality and is focused on reducing compliance burden. However, changes in the operating environment require this methodology to better evaluate underlying factors that are affecting audit quality, to ensure that regulatory requirements are targeted and effective. This will be accomplished through enhanced root cause analysis when deficiencies are identified, broader risk assessment, and effective recommendations/requirements in our inspection reports.

Enhanced transparency of inspection reporting to stakeholders presents an opportunity for CPAB. Audit committees requested more detailed and public reporting of inspection findings during cross-Canada roundtables CPAB convened in 2012. Direct communication to audit committees about emerging issues and factors impacting audit quality continues to be a focus. In 2013 CPAB has been working with the audit firms and audit committee members in developing a protocol to share CPAB's inspection findings with audit committees, beginning with the 2014 inspections. The protocol will be distributed for public comment in the Fall of 2013.

Overall, CPAB believes greater transparency in reporting will enhance audit quality, cause audit partners and firm leadership to focus more on continuous quality improvement, and raise awareness of noteworthy audit issues at the audit committee level. However, it is important this be done in a way that does not undermine CPAB's regulatory methodology and in a way that is useful to stakeholders.

Mission and Vision

CPAB's mission remains unchanged. CPAB will:

Contribute to public confidence in the integrity of financial reporting by public companies in Canada through effective regulation and the promotion of high quality, independent auditing.

This mission reflects the long-term nature of the need for CPAB's regulatory oversight and its mandate pertaining to the audits of public companies.

CPAB’s vision for the next two years encompasses a broad-based objective, which management believes is necessary to appropriately address the numerous factors in the operating environment. CPAB’s vision is:

Effective regulation – proactively identifying current and emerging risks to the integrity of financial reporting in Canada, assessing how auditors effectively respond to those risks, and engaging those charged with governance, regulators, and standard setters to develop sustainable solutions.

Fulfilling the mission and attaining this vision will ensure CPAB’s continued effectiveness in contributing to improved audit quality and investor protection, thereby helping to maintain the integrity of Canadian capital markets.

Core Issue and Strategic Shift

The core issue for this Strategic Plan is to ensure that audit firms achieve sustainable improvements in audit quality. Deficiencies in audit quality result primarily from inconsistent audit execution, which highlights the need for greater professional skepticism and better supervision and review throughout the audit process.

CPAB has concluded that it can best meet its regulatory mandate through after-the-fact inspections and by engaging a broader range of stakeholders in a discussion and better understanding of the audit process. Doing so will require a multi-faceted approach, including broader stakeholder engagement and improved inspection methodology, comprising enhanced root-cause analysis, broader risk assessment and expanded value-added recommendations. A more robust risk management mindset and skill set is being embedded within CPAB. This includes the development of insightful position papers, which will heighten stakeholder awareness and knowledge of emerging risks and matters related to audit quality.

In the aggregate, these initiatives will advance CPAB’s next strategic shift as depicted below.

Strategic Shift 2013-2015

| From | To |
|---|---|
| Compliance mindset | → Regulator mindset |
| Rigorous tactical risk assessment | → Comprehensive risk assessment and mitigation |
| Granular inspection focus | → Enhanced root-cause analysis/value-added recommendations/requirements |
| Periodic stakeholder communication | → Disciplined proactive stakeholder engagement |
| Responding to international regulatory developments | → Participating in shaping global regulatory framework |
| Standard inspection reporting | → Timely targeted stakeholder communication |
| Confidential disclosure | → Judicious transparency |
| Risk of being marginalized | → Participate in the domestic regulatory agenda |

Value Proposition, Critical Success Factors, Core Capability, Core Values

CPAB must continue to demonstrate to its key constituencies that it provides distinctive, superior and compelling value, and is worthy of their continued support. This value proposition, which reflects the core issue CPAB must address, is:

Penetrating insights that improve audit quality and mitigate risk.

Critical success factors are the measures an organization must implement or perform well to fulfill its mission, attain its vision, and deliver on its value proposition. CPAB's critical success factors are:

- ***Thought leadership***
- ***Strategic engagement***
- ***Broader risk-based inspection methodology***
- ***Enhanced assessment of quality processes and structures, and***
- ***Effective regulator mindset and practices***

A core capability is the combination of technical competencies and business processes that yield distinct competitive advantage, or, in the case of a regulator such as CPAB, long-term effective audit regulation. Core capability is vital to an organization's capacity to deliver on its value proposition. CPAB's core capability is:

Strategic inspection oversight: Risk and root-cause-oriented, rigorous, proactive, adaptable, value adding.

The need to improve risk assessment, root-cause analysis capabilities, proactivity and adaptability, together with the continued delivery of value-added recommendations, represent important activities for CPAB, which are reflected in the 2013-2015 strategic initiatives.

CPAB continues to adhere to its core values of *Excellence, Trust and Respect*. CPAB's core values have been complemented by a philosophy of *Proactivity*. From identifying emerging trends and risks, to engaging key stakeholders, to upgrading internal capabilities, proactivity in thought and action is another defining attribute of CPAB going forward.

Strategic Initiatives

CPAB has identified eight strategic initiatives for 2013-2015.

Thought Leadership

1. **Research, publish and promote dialogue on emerging issues affecting audit quality**

This initiative represents a significant change for CPAB. Increasing discussion, awareness of and insight into issues of audit quality with major stakeholders is fundamental to building a robust regulatory environment while maintaining/enhancing CPAB's effectiveness.

CPAB can raise the bar on overall audit quality by leveraging the information it acquires in its core inspection activities. This can be supplemented by research, interaction and dialogue with audit committees, institutional investors and other key stakeholders. Combined with similar data from international regulators and standard setters, CPAB's findings will yield significant information the organization can use to advise and influence standards formulation, risk identification, and business practices.

Stakeholder Engagement

2. Increase targeted outreach to key stakeholders (audit firms, audit committees, institutional investors, other regulators, and government bodies)

To address the core issue of enhanced audit quality, CPAB is communicating more strategically with key stakeholders to better influence change and cause sustainable improvement in audit quality. CPAB continues to clearly articulate its concerns to the audit firms and audit committees. Important elements of this engagement strategy include:

- Proactively sharing and discussing emerging risks with audit committees
- Redesigning and updating CPAB's website to make it the primary source of the latest information on audit quality
- Engaging in a dialogue with audit committees about the importance of audit quality and their role and responsibilities in this regard
- Increasing the transparency of CPAB's findings

CPAB roundtables with audit committees in 2013 yielded feedback that more transparent reporting of inspection results could help audit committee members exercise their audit oversight responsibilities more effectively, improving audit quality. Audit committees want to know if there are any audit quality issues with the audits of their reporting issuers.

Stakeholder engagement also encompasses targeted outreach to and dialogue with institutional investors, other regulators and standard setters, domestically and internationally, to ensure Canadian audit quality considerations remain top of mind.

Risk Management

3. Embed risk-based assessment practices and culture throughout the organization

Six major categories of risk comprise CPAB's risk universe: reputation (effectiveness); quality/operations; human resources; information technology; legal and regulatory, and financial. Each category, in turn, is composed of a discrete set of risks.

Strategically, it is important for CPAB to implement systems, processes and programs to keep abreast of the many risk factors. This includes more research and analysis of the reporting issuer population, environmental scanning, root-cause-focused inspections and key stakeholder engagement. Beyond those measures, CPAB is enhancing its organizational capability by promoting a culture of professional curiosity and skepticism through such means as investments in professional development relative to risk assessment/management, and leveraging CPAB's Management Team for ongoing discussions and updates on risks, findings and trends.

Inspections

4. Broaden inspection methodology to better assess drivers of audit quality through enhanced root-cause analysis, expanded risk assessment, and value-added recommendations that lead to sustainable improvement

CPAB has implemented a comprehensive inspection methodology that has enhanced audit quality. This has been achieved in an environment of increasing complexity and risk. Concurrently, the business/profitability interests in the audit firms continue to conflict with both audit quality and professional skepticism considerations.

To address this latter dynamic, and to reduce the high level of audit deficiencies, CPAB has enhanced its inspection methodology to better identify the root causes of quality shortfalls, including such factors as competence, accountability and organizational structure within the firms. This dictates the need for continued professional development within CPAB, as it shifts strategically from being a rigorous, traditional inspector to a discriminating effective regulator.

Standards

5. Ensure policies and practices remain current with continually changing standards

The evolution of standards means CPAB must continually modify its policies, practices and technical training.

CPAB has a unique opportunity to influence the evolution of auditing standards at the international regulatory level and to ensure that any Canadian views are appropriately

considered. CPAB continues to proactively voice its opinions in areas where auditing standards need to be improved. CPAB also plans to provide guidance where CPAB believes the implementation of auditing standards could be enhanced.

Organizational Capability

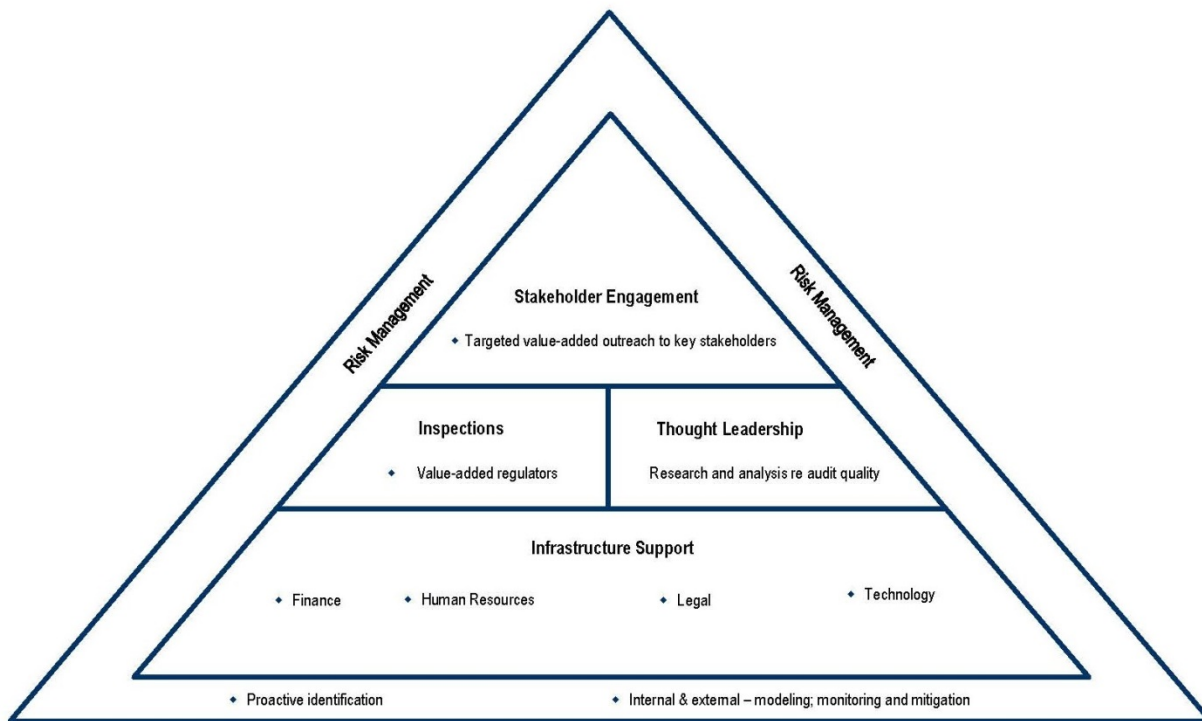
6. Foster an effective regulator mindset and culture

This is a broad-based, pervasive objective that starts with changes in the inspection methodology and better risk assessment, and extends through thought leadership, resulting in better stakeholder engagement and improved audit quality. This is a fundamental change in how CPAB exercises its mandate. CPAB will foster in all staff, through its core values, a set of beliefs and practices focused on identifying audit deficiencies and mitigating financial reporting risks to the investing public.

7. Redesign for optimum impact

To achieve these strategic initiatives, CPAB has modified its organizational design to align resources and accountabilities for maximum impact and to embed a more strategic, value-added, communicative and engagement culture. Organizationally, CPAB now has four lines of business: Thought Leadership; Stakeholder Engagement; Inspections, and Infrastructure Support. Each is receiving enhanced focus and resources, appropriate for an effective regulator committed to addressing the complexities of a rapidly changing and challenging operating environment. Risk management is an integral part of each line of business as indicated by the risk management triangle that surrounds the business lines.

CPAB's new organizational design graphically appears as follows:



The key principles of this new design are to:

- Advance an effective regulator mindset and practices
- Enhance risk capability that is embedded in the fabric of the organization
- Augment inspection methodology to drive improvement in audit quality
- Engage key stakeholders to enhance audit quality
- Foster communication, integration and knowledge management
- Enable an adaptable, high-performing, high-accountability culture
- Provide the opportunity for meaningful work, professional development and career progression

8. Invest in professional development and leadership succession

The shift CPAB is effecting, from inspector to effective regulator, has been noted. To achieve this, CPAB staff must understand and embrace the rationale for it, and policies, processes and practices must be aligned with this objective. Professional development will enable this shift through a variety of approaches, including discussion series, simulations, special projects, and secondments.

CPAB is also investing in succession planning to ensure future leadership is identified and developed. Performance appraisal, coaching and mentoring, assessment of potential, individual career development plans, and comprehensive leadership reviews provide a best-practice approach to attracting and developing talent and serve to

enhance CPAB's leadership capacity. CPAB may also need to strategically hire in some areas to effectively execute this Strategic Plan.

Strategic Outcomes

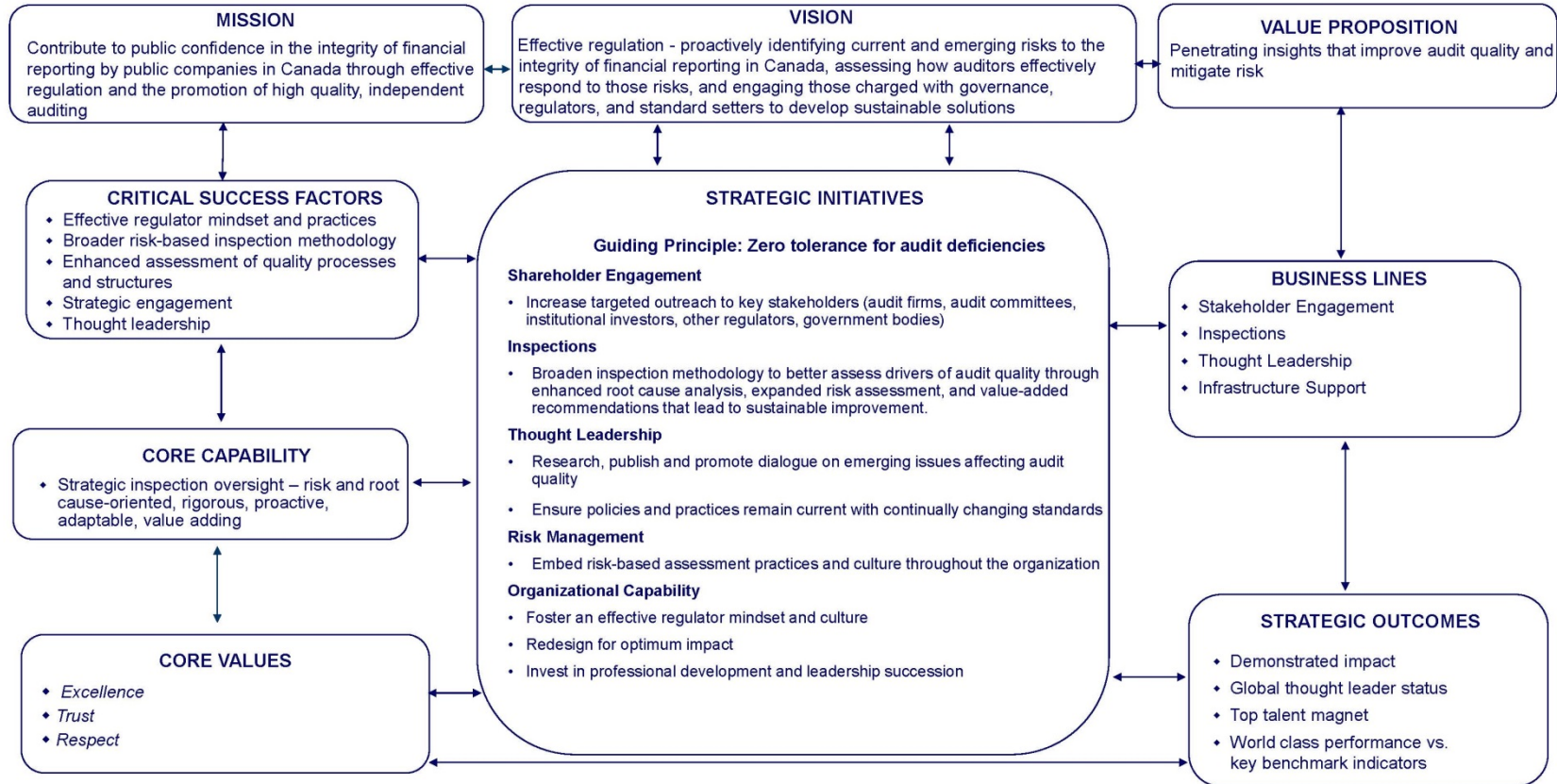
By 2015, CPAB will have positively affected the domestic and global audit sectors by demonstrably influencing the way audit quality is viewed.

This outcome will result from a number of factors, including an enhanced inspection methodology to better identify the root cause of quality outcomes, which will lead to high-impact recommendations. In addition, CPAB will continue to enhance relationships at the leadership level within Canadian audit firms, and will proactively establish relationships with audit committees, institutional investors and other domestic regulatory authorities. Furthermore, CPAB will assume a leadership role within the global audit regulatory system, through thought leadership and key roles in international regulatory portfolios.

In terms of business processes, as well as organization culture, CPAB has embedded a more robust risk capability and effective regulator mindset throughout the organization, complemented by enhanced engagement with key stakeholders.

In achieving these outcomes, CPAB will have caused sustainable improvement in audit quality, built its reputational capital, and become a magnet for top professionals who want to maintain their skills at the leading edge and be part of an organization making a profound difference on the Canadian and global audit regulatory landscape.

2013-2015 Strategic Framework



Appendix 2: Strengths, Weaknesses, Opportunities, Threats

- Among CPAB's greatest strengths are the quality of its people and the organization's reputation and credibility as a world-class audit regulator.
- Weaknesses include: having an inspector rather than an effective audit regulator mindset; being too inspection findings and compliance-focused, instead of being root-cause oriented; and being more reactive than proactive. Certain auditing standards dictate the need to enhance proactivity and to look at audit quality in a broader sense, which necessitates engaging key stakeholders through dedicated communication and outreach resources.
- CPAB's biggest opportunity is to assume a leadership role in engaging and influencing stakeholders, through such means as:
 - Commenting on standards
 - Seeking out ways to increase professional skepticism
 - Rebalancing inspection findings to emphasize value-added observations/actions, and
 - Increasing transparency of the reporting of audit quality issues
 - Raising CPAB's profile with audit committees, institutional investors and other regulators are also related and complementary opportunities.
- If CPAB does not drive improvement in audit quality, a perceived lack of relevance represents an overarching threat.
- Internal threats include:
 - Key-person risk as well as the broader challenge of building the skill set across the organization to bring about an effective regulator culture shift
 - Keeping pace with globalization and its inherent risks, which audit firms themselves have difficulty doing
 - Standards, which are increasingly international in origin
 - The challenges of effectively communicating with senior-level stakeholders
- In summary, the top three considerations from this assessment are:
 - The need for an expanded communication competency
 - Key stakeholder engagement
 - Achieving an effective regulator culture shift