CPAB Real Estate Industry Forum Highlights

CPAB held its Real Estate Industry Forum on October 18, 2018 in Toronto for audit committee chairs and CFOs of Canadian real estate companies.

Moderated in Toronto by Joanne Ferstman, audit committee chair of Dream Unlimited, the Forum featured roundtable discussions about matters that are top of mind for audit committees and CFOs of Canadian real estate companies.

Issues facing audit committees of real estate companies in Canada

Estimates

**Valuation**

Participants discussed how audit committees could better oversee the fair value assessment of properties, citing the value of independent valuators, external specialists, and specialists from their audit firms and ensuring that if using both internal and external valuators, the valuations should align. Valuation challenges included monitoring the quality of internal controls and the lack of historical data points in a rapidly changing real estate market. One participant noted the advantage of using a large external valuation specialist organization due to their access to a larger pool of data.

**Tenant quality**

To mitigate risk, real estate companies may have a goal of having a diverse mix of tenants from various industries. Some participants noted that management has a considerable amount of information related to releasing rates and vacancy levels, which can be leveraged to better disclose how estimates are created.

Key Performance Indicators (KPIs)

Investors rely on KPIs and non-GAAP measures reported by real estate companies to inform investment decisions. Several key performance indicators (KPIs) are commonly disclosed by real estate companies including net operating income (NOI), funds from operations (FFO), and adjusted FFO (AFFO). While some standardization guidance exists in this area, there can be differences in application.

Participants discussed common issues real estate companies experience in this area, including defining occupancy and aligning with other companies in the industry. One participant suggested that occupancy should be defined in the MD&A with clear disclosures on how the rates are calculated. Since real estate company boards are ultimately responsible for disclosure, participants also noted the value of educating the entire board on these issues. Analyst presentations to the Board and periodic industry checks were cited as useful in these areas. Participants also highlighted the importance of knowing whether their company was in line with others in the industry and suggested that the auditor could provide insight in this area.

KPIs are an evolving area and real estate companies should ensure they have specific disclosures in place to ensure they are applied consistently.
Developments in audit quality

Trust in audit

When international regulators asked CEOs of the world’s largest public accounting firms what is currently top of mind, trust and integrity were at the forefront. In today’s global audit community, there is no shortage of examples where audit quality has been questioned. Discussions are continuing in some jurisdictions such as the UK around changes that can improve audit quality including steps to increase competition for large audits and reduce the potential for conflicts of interest.

Audit quality management systems

CPAB believes increased focus on centralized quality control systems at the firm level is important to improve the consistency of audit quality. While most audits we inspect comply with the required standards, recurring inspection themes indicate that weaknesses in quality management systems persist, leading to inconsistent audit execution. Firm policies and processes – at both the leadership and engagement team levels – that manage risk and get the right people working on the right things at the right time are essential to delivering high quality audits, consistently. In 2018, CPAB implemented new methodology to assess existing audit quality management systems to help accelerate improvements.

Audit quality indicators

Audit quality is a challenge for audit committees to measure and evaluate. Audit Quality Indicators (AQIs) are a response to this and provide quantitative measures about the external audit process. They facilitate collaboration among key stakeholders (auditors, management and the audit committee), and provide more in-depth information to assist in evaluating and achieving sustained audit quality. CPAB believes that AQIs have significant potential to positively impact audit quality. CPAB recently wrapped up a two-year pilot project with audit committees and management exploring the value of audit quality indicators (AQIs). We recently published a final report on our findings and launched an AQI Network to enable information sharing and support for current and future AQI users.

Emerging industries and disruptive enablers

CPAB is keeping an eye on emerging industries, including cryptocurrency and cannabis, with great interest and believes there is an urgent need for guidance on how auditors should be responding to typical audit risks associated with these clients. We recently published our perspectives on auditing in the crypto-asset sector to help address some of these risks.

Auditor use of data analytics and technology is also a growing area of change. CPAB will continue to watch the development and implementation of new tools and procedures and provide our perspective on how they can enable better quality over time.
Thank You

CPAB thanks everyone for their participation. We encourage ongoing dialogue and look forward to continuing the audit quality discussion at future events across Canada.

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