



FINANCIAL INSTITUTIONS

TORONTO • JANUARY 20, 2017

CPAB Industry Forum Highlights Financial Institutions

CPAB held its first Financial Institutions Industry Forum on January 20, 2017 for audit committee chairs serving the boards of banks and insurance companies in Canada.

Co-hosted by Alan MacGibbon, audit committee chair, TD Bank Group, the Forum featured a roundtable discussion about matters relevant to audit committees of banks and insurance companies in Canada. The Forum included a presentation by CPAB about current and emerging developments in audit quality in Canada and abroad, and audit partner perspectives from Bill Schlich, banking partner, EY LLP, and Claire Cornwall, insurance partner, PwC LLP. Read on for highlights from the three-part event.

Issues facing audit committees of banks and insurance companies in Canada

Keeping up with changes to accounting and regulatory requirements

- Participants discussed training strategies for keeping up with changes to accounting and regulatory requirements including having combined meetings of audit and risk committees to discuss common issues.
- Most participants indicated that training was a key priority for all directors.
- Challenges were discussed related to the adoption of IFRS 9 including increased measurement uncertainty under the expected credit loss model for estimating the allowance for loan losses and implementation challenges related to new systems, processes and internal controls required at adoption.
- An audit partner expressed the view that adoption of expected credit loss accounting will be the most complex accounting change they have experienced.

IT strategy including cybersecurity

- Cybersecurity is regarded as a key priority for the boards for all participants.
- New standards¹ expected in the US on enhanced cybersecurity risk management will broaden the mandate of audit committees of Canadian banks with US operations.

- Some participants said increased expertise will be required at the board level to understand and effectively challenge the adequacy of cybersecurity protocols implemented by management.
- Participants agreed that the interconnectedness of the financial system meant that system-wide enhancements to cybersecurity should be addressed through increased cooperation among all financial institutions, OSFI, and other federal agencies.

Data analytics

- Data analytics was viewed as a powerful tool because it shifts audit work away from routine audit areas into riskier areas identified by the tools.
- Participants commented that more progress is needed for internal and external auditors to take advantage of the benefits of data analytics. More progress has been seen in other areas of the business including compliance functions like AML monitoring.

¹ The three federal banking regulatory agencies in the US (Federal Reserve Board, FDIC, OCC) issued an advance notice of proposed rulemaking on October 19, 2016 inviting comment on potential enhanced cybersecurity risk management and resilience standards that would apply to large and interconnected entities under their supervision.

Breadth of the mandate for audit committees

- The mandate of audit committees is becoming progressively broader reflecting increasing risk and complexity of financial institutions.
- New requirements that expand the responsibilities of internal auditors, including a responsibility to evaluate the strength of the entity's risk governance and culture, further broaden the mandate of audit committees given their oversight capacity over the internal audit function.
- Several participants agreed it is becoming more challenging to balance the demands of more routine compliance requirements with the more strategic areas of the mandate.
- Participants described strategies for optimizing the use of audit committee members' time including a consideration of the timing and frequency of in-camera sessions.

Developments in audit quality

CPAB overview

- CPAB has a risk-based file selection process focused on industry and reporting issuer risks.
- Continued need for audit firms to improve consistency of execution as many files show a high level of audit quality but others require significant improvement; audit committees can assist.
- Audit firms provide CPAB's significant inspection findings in writing to audit committees under the Protocol for Sharing Inspection Findings with Audit Committees (Protocol).
- CPAB seeks to increase awareness of audit quality matters among audit committees through 1:1 meetings and presentations and publications that assist them in their oversight role.

Relevance of the audit

- The focus of investors and equity analysts on other information outside of the financial statements (i.e., KPIs including non-GAAP measures) raises questions about the relevance of the audited historical financial information, including:
 - What information do investors use to make decisions?
 - What is the responsibility of management, internal auditors, external auditors, and the audit committee in relation to the integrity of this information?
 - Should this information be audited?

Audit Quality Indicators (AQIs)

- Use of AQIs can positively impact audit quality.
- In 2016, CPAB sponsored a pilot project with audit committees of six public companies to explore the usefulness of applying an AQI framework.
- No predefined set of AQIs were prescribed. Pilot participants selected AQIs based on specific circumstances and areas of focus. Significant variation in AQIs was observed across pilot participants. Context is important in understanding and use of AQIs.
- One participant commented that the greatest benefit of an AQI framework was the dialogue it encouraged among audit committees, audit firms, and management.
- AQI pilot will continue in 2017 with a call for new participants.

Expanded auditor reporting

- Expanded auditor reporting would include a requirement for auditors to describe key audit matters that were of most significance in the audit of the current period financial statements. This is expected to make the audit more relevant and understandable to stakeholders.
- IAASB approved standards that expand auditor reporting for 2016 calendar year-end audits.
- The AASB is waiting for clarity around the PCAOB's proposed expanded auditor reporting standards before finalizing the Canadian standards.

Expanded audit committee reporting

US

- In 2013, several national governance organizations put out a call to action for audit committees to voluntarily improve their disclosures.
- In July 2015, an SEC Concept Release proposed an expansion to audit committee reporting; responses were mixed and SEC is considering next steps.

Canada

- CSA is exploring whether additional reporting from an audit committee would provide useful information to investors and positively impact audit committee activities and performance.
- Concept Paper expected in mid-2017.

Audit partner perspectives on areas of audit focus

Banks

Key areas of audit focus:

- Allowance for loan losses
 - Audit focus is on controls, governance, and models.
- Fair value estimates for derivatives
 - Complex fair value estimates include the funding and credit valuation adjustments.
- Other estimates

Insurance companies

Key areas of audit focus:

- Actuarial estimate of claims liabilities
 - Importance of internal specialists
- Fair value estimates for investments
- Other estimates

Thank You

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

Learn More

Visit us at www.cpab-ccrc.ca and join our mailing list. Follow us on Twitter — @CPAB-CCRC

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