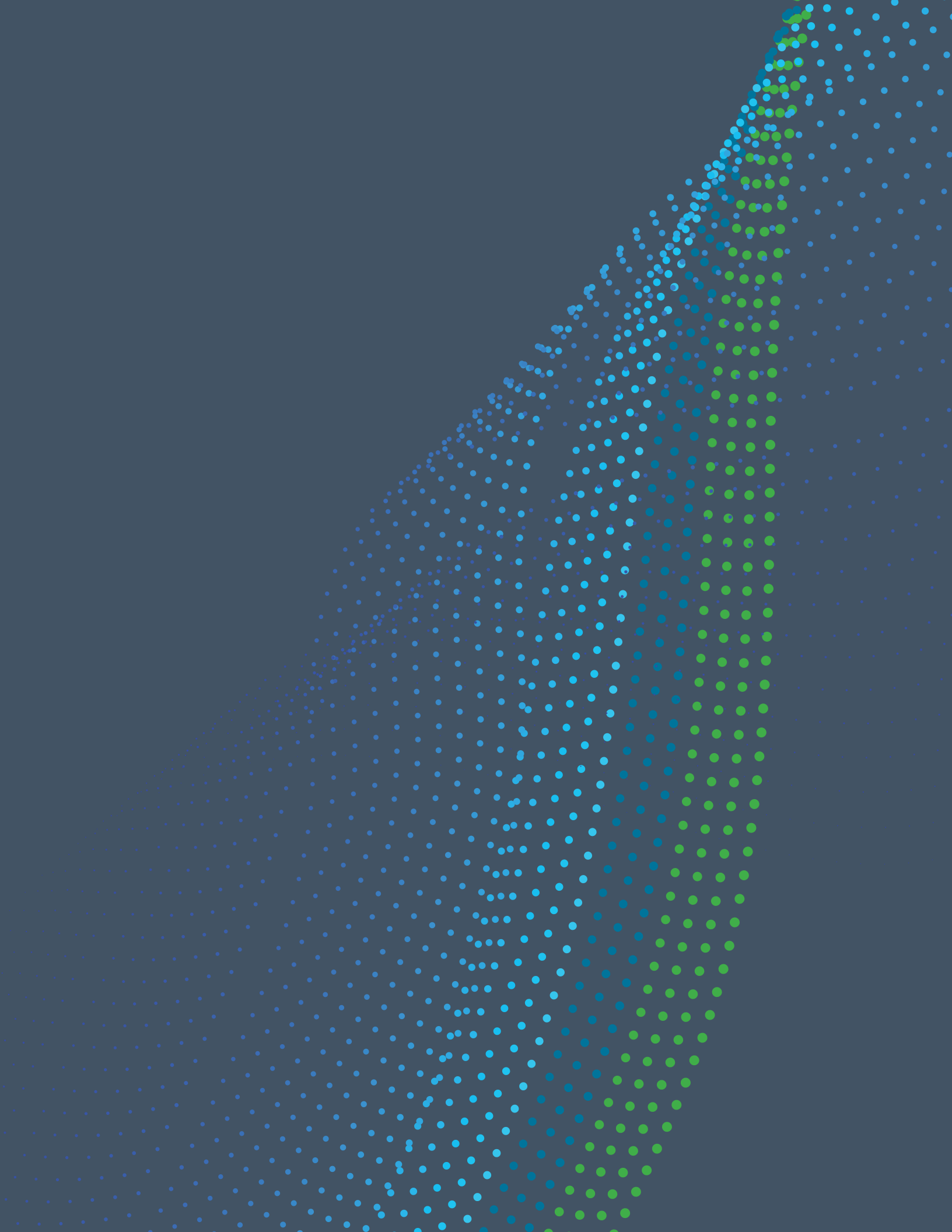


UPHOLDING HIGH STANDARDS TO PROTECT THE PUBLIC

MANAGING AUDIT QUALITY 2023





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OUR MANDATE

We are a community of over 100,000 CPAs and over 20,000 students across the province committed to innovation, ethics and upholding the highest standards of the profession.

The professional accounting profession is a provincial responsibility governed by the *Chartered Professional Accountants of Ontario Act, 2017* and the *Public Accounting Act, 2004*.

Through this legislation and delegated authority from the government, CPA Ontario is the regulatory body responsible for overseeing CPAs and accounting firms in Ontario.

Like our Provincial, Territorial, and Bermudian (PTB) CPA body partners across Canada, the critical work we do protects the public, enables us to advance the profession and enables CPAs to lead business and society forward.

Going forward, we will continue to work in collaboration with our partners across the country as one CPA designation to deliver on these important responsibilities that government has entrusted to us:

SHAPE THE FUTURE OF THE PROFESSION by attracting the next generation of talent and seizing opportunities for innovation.

GOVERN AND REGULATE CPAS AND ACCOUNTING FIRMS IN ONTARIO which includes compliance and disciplinary processes.

ENSURE THE CPA PIPELINE MEETS MARKET DEMANDS through recruitment activities within PSIs and high schools, and by supporting new entrants to Canada.

EDUCATE AND ASSESS CPA STUDENTS by delivering a world-class professional education program.

FACILITATE COMMON ENTRY INTO THE PROFESSION by working with our PTB CPA counterparts.

GRANT CPA DESIGNATIONS AND PUBLIC ACCOUNTING LICENCES while maintaining the rigour and high standards that set the profession apart.

ENHANCE THE SKILL AND KNOWLEDGE OF MEMBERS through professional development and thought leadership.

SUPPORT STANDARD SETTING WITHIN CANADA and at the international level.

ENABLE MOBILITY OF CPAS through agreements with PTBs as governed by provincial laws.



OUR PURPOSE

We **PROTECT** the public.

We **ADVANCE** the profession.

We **ENABLE** CPAs to lead
business and society forward.

OUR VALUES

How we do things is just as important as what we do.

Values guide the way we work and the decisions that we make. They reflect who we are as an organization and what we believe is right. Our values align with our purpose and enable us to deliver our strategy in a way that we can all be proud of.

These values embody how we aspire to behave in all situations with each other, members and students, and other stakeholders. They set the expectations we have of each other.

WE ACT WITH INTEGRITY

We always do the right thing and take accountability for our decisions and work.

WE ARE THOUGHTFUL

We are considerate in the way we make decisions, and how we engage with the public, employers, our members, students, and colleagues.

WE WORK TOGETHER

We are a supportive and inclusive team and empower each other to achieve our personal and professional goals.

WE MAKE AN IMPACT

We strive to make a meaningful difference to our stakeholders and the profession, delivering results with excellence.

WE ARE FORWARD-THINKING

We are curious, innovative and data-driven, and ensure our work benefits business and society.

OUR STRATEGIC PRIORITIES

Our strategy defines our priorities as an organization and clearly sets out the work we need to do. Since the strategy was last revised, the world around us has changed in incredible ways.

And so, our strategy has evolved with the environment and in line with the needs of members, students and firms, as well as the broader business community.

Five strategic pillars focus our efforts. Everything we do supports these pillars and ensures that our work helps us achieve this purpose. We are committed to working closely with our counterparts across Canada to deliver on these priorities as a unified profession.

PROTECT

the public interest ensuring our members, students and employees maintain the highest standards of integrity.

ADVANCE

the profession by developing CPAs who can lead in an ever-evolving world.

BUILD

a robust pipeline of high-calibre individuals.

CREATE

a strong brand and demand for CPAs.

CULTIVATE

an environment that enables our people to thrive together.

WHY IS AUDIT QUALITY ESSENTIAL?

Ontario is home to Canada's capital markets and the majority of Canada's public companies, as well as Canada's largest stock exchange, the Toronto Stock Exchange. Approximately half of Canada's equity market value comes from issuers registered in Ontario.¹

Trust in our capital markets is essential for the growth and integrity of the Canadian economy and our national prosperity. One of the cornerstones of that trust is the audit, which ensures transparency in financial reporting and provides crucial information that the public and investors rely on.

Confidence in the audit comes from knowing that audit firms have designed, implemented and consistently applied policies and procedures that promote and support audit quality in accordance with professional standards and applicable legal and regulatory requirements.

As the largest CPA body in Canada and the qualifying and regulatory body of over 100,000 Chartered Professional Accountants (CPAs), including over 4,000 Public Accounting Licence (PAL) holders, it is our role to protect the public and the integrity of our capital markets by ensuring that firms, and our members and students, meet the highest standards of integrity and technical expertise. Where these standards are not met, it is also our responsibility to address it.

WHAT IS AUDIT QUALITY?

CPA Ontario's view is that audit quality is dependent on a firm establishing a system of quality management that ensures audits are planned and performed consistently and to the high standards of the profession.

This includes:

- The establishment of appropriate values, ethical standards and attitudes.
- The development of required knowledge, skills and experience.
- The allocation of sufficient time and resources to perform audit work.
- The implementation of a rigorous audit process and quality management system that comply with professional standards and applicable legal and regulatory requirements.

In Ontario, these requirements include the CPA Code of Professional Conduct (the Code), the *Public Accounting Act, 2004*, the *Chartered Professional Accountants of Ontario Act, 2017*, CPA Ontario's by-law and regulations and the profession's quality management standards, such as the Canadian Standards on Quality Management (CSQM) 1 and 2.

¹ The Ontario Securities Commission: Ontario's Capital Markets
<https://www.osc.ca/en/about-us>

STANDARDS: THE FOUNDATION OF AUDIT QUALITY

The CPA Code of Professional Conduct (the Code) and the Student Code set out the principles that guide members, students and firms in their fundamental responsibilities. The Code encompasses key areas that support audit quality which are addressed in detail through provincial legislation and CPA Ontario's by-law, regulations and the standards of our profession:

Compliance with governing legislation, by-law and regulations:

- The *Chartered Professional Accountants of Ontario Act, 2017* and the *Public Accounting Act, 2004* govern members, students and firms. CPA Ontario's by-law and corresponding regulations support the implementation of these Acts.

Compliance with Professional Standards:

- Consistent performance of engagements in accordance with professional standards is critical to audit quality. A key driver of this is the design, implementation and operation of a firm's system of quality management.
- Canadian Standard on Quality Management (CSQM) 1, *Quality Management for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements* deals with the firm's responsibility for having a system of quality management. CSQM 2 builds upon CSQM 1 by including specific requirements for engagement quality reviews, an important part of the firm's system of quality management.

Professional Competence:

- Robust Continuing Professional Development that emphasizes technical competence, builds on ethical principles and emerging issues creates a foundation that, combined with experience, develops the necessary and critical skills that underly audit quality.

CONTINUING PROFESSIONAL DEVELOPMENT

The requirements for Continuing Professional Development (CPD) are prescribed in CPA Ontario Regulation 7-2, *Continuing Professional Development*.

Under this regulation, members must complete at least 20 hours of CPD annually and 120 hours in every rolling three-year period. Of this, 10 hours and 60 hours must be verifiable, respectively. Included in these hours must be four hours of ethics each triennial period.

All CPD must be relevant to professional responsibilities as a CPA, be quantifiable, and contain significant intellectual or practical content.

To be eligible to apply for a new PAL or renew an existing PAL, these hours must be in activities directly related to the competencies needed to engage in the Practice of Public Accounting. Additionally, CPD must be based on the learning outcomes as set out in International Education Standard 8 (IES 8), *Professional Competence for Engagement Partners Responsible for Audits of Financial Statements (Revised)*.

FIVE FUNDAMENTAL PRINCIPLES OF ETHICS

These underly the CPA Code of Professional Conduct:

**PROFESSIONAL
BEHAVIOUR**

**INTEGRITY
AND DUE CARE**

OBJECTIVITY

**PROFESSIONAL
COMPETENCE**

CONFIDENTIALITY

OUR REVIEW

WHY DID CPA ONTARIO CONDUCT A REVIEW OF AUDIT QUALITY?

Protecting the public. It is the core of what we do at CPA Ontario and our regulatory continuum of advising, compliance, inspecting, investigation, enforcing and imposing discipline helps us identify members, students or firms who are falling short of the standards expected of them.

Over the last two inspection cycles, the CPA Ontario Practice Inspection team has identified concerns with audit quality in a number of registered firm practicing offices.

In these cases, inspections have resulted in an unacceptable outcome, being a reinspection or referral to our Professional Conduct Committee, at a rate of 9-15% in each of the last six years.

Twelve practicing offices were referred to the Professional Conduct Committee in the last year, although none of these firms were subject to this review of audit quality as these 12 firms did not, at the time of this review, audit reporting issuers and were therefore out of scope.

Some of these referrals were due to practitioners adding or altering documents more than 60 days after the corresponding reports were issued and backdating those documents to make it appear as if they had been completed on or before the date of the corresponding report, presenting a risk to the public and to the profession.

At the same time, last year's shift from quality control to quality management through CSQM 1 requires firms to take a new approach. This new approach to quality is risk-based, focused on achieving quality objectives and grounded in a risk assessment that identifies quality risks specific to firms and the engagements they perform.

Firms that conduct audits or reviews of financial statements or other assurance engagements were required to have designed and implemented their system of quality management by December 15, 2022, and within one year perform an evaluation of that system.

It is our role, as the regulator, to monitor and ensure implementation of these new standards.

Our recent inspection findings, along with the shift in standards from quality control to quality management, made it the right time to undertake this review.

OUR APPROACH

In the Fall of 2022, CPA Ontario began a focused review of public accounting firms that conduct audits of reporting issuers. Fifteen firms were selected who collectively audit over 99% of the reporting issuers in Ontario.

The selected firms were required to respond to a Request for Information from CPA Ontario to provide details on how they manage audit quality to meet the standards and expectations of our profession.

In parallel with its review of firms, CPA Ontario also conducted a review of 146 individual PAL holders, 34% of which were employed by the national firms. This review was to assess whether their CPD meets the requirements of the Code and CPA Ontario regulations, including international technical competence and ethical standards.

This review occurred as part of the PAL renewal cycle, and renewal applicants were asked to provide details and supporting documentation for CPD taken for the triennial period 2019-2021, including the ethics requirement.

EXECUTIVE SUMMARY

“Audit provides a key pillar of trust in our capital markets, and it is the responsibility of firms to maintain that trust by ensuring that their audits continue to be of the highest quality. Protecting the public is the foundation of the CPA designation, and the cornerstone of our role as the regulator of the profession in Ontario.”

Carol Wilding, FCPA, FCA, ICD.D

President and CEO,
CPA Ontario

“Our review identified areas of risk that, if left unaddressed, could present a threat to audit quality. That is why these areas of risk will be included in our in-depth review of quality management in our next practice inspection cycle. Firms must ensure that they are executing to the high standards of the profession.”

Janet Gillies, CPA, CA

Executive Vice-President,
Regulatory and Standards,
CPA Ontario

Firms must execute to the highest standards of the profession to ensure quality and protect the public. Through our review, CPA Ontario identified five areas of risk that, if left unaddressed, could present a threat to audit quality.

01 Governance & Decision-Making

02 Ethical Mindset

03 Talent & Technology

04 Working Papers

05 Monitoring Activities

By no means do these quality risks apply to every firm that was subject to this review, but their presence indicates the need for firms to remain vigilant to ensure the highest possible standards of audit quality are being met.

This is why, commencing in 2023, CPA Ontario's Practice Inspection team is conducting in-depth reviews of quality management systems. This will include all five areas of unidentified or unaddressed quality risks identified in our review. Over the next inspection cycle, all fifteen firms included in this report will undergo this enhanced review.

Our review also identified four firms, representing audits of less than 1% of reporting issuers, with deficiencies warranting a referral for further review by the Practice Inspection team this year.

Firms subject to these reviews by Practice Inspection may be required to develop an action plan, undergo further reinspection, or be referred to the Professional Conduct Committee for investigation.

Included in these four firms were cases where the parallel review of individual PAL holders uncovered CPD deficiencies that demonstrated a strong disconnect between what these firms had described as robust learning and development policies and our findings around the specific CPD activities. Deficiencies of this severity call into question the firm's overall system of quality management.

CPA Ontario has also enhanced the documentation requirements for CPD reporting by members applying for a new PAL; these review and oversight procedures are now an integral part of the application process.

In addition to identifying risks, the responses provided by the firms also revealed a series of effective practices firms are employing to drive audit quality. These best practices are shared throughout the report and should serve as a road map for firms as they conduct their review of their system of quality management within one year of implementation, as per CSQM 1.

Upholding high standards and protecting the public is the responsibility of firms, just as holding the profession to those standards is the responsibility of their regulator. As firms continue their implementation of CSQM 1 and 2, this report will be shared with firms to provide them with an important lens they can use to evaluate their quality management practices and processes.

CPA Ontario will continue our focus on audit quality to ensure that trust in Ontario's capital markets – a key plank in the foundation of Canada's economy and prosperity – remains strong. This would include further oversight of this important area, and we will take appropriate regulatory action for non-compliance, where necessary.

KEY THEMES

Every firm and practice is unique, which is why every firm must develop its own quality management system including processes, policies, procedures and cultural practices that comply with the legislative and regulatory frameworks to ensure audit quality.

In alignment with CSQM 1, five areas of unidentified or unaddressed quality risks emerged through our review: Governance & Decision-Making, Ethical Mindset, Talent & Technology, Working Papers, and Monitoring Activities.

While these risks do not apply to every individual firm, it is the responsibility of all firms to focus on identifying and responding to quality risks that arise given the nature of their firm and the engagements they perform.

WHAT IS A FINDING?

Under CSQM 1, a system of quality management addresses eight components by establishing quality objectives for the firm in each area: the firm's risk assessment process, governance and leadership, relevant ethical requirements, acceptance and continuance of client relationships and specific engagements, engagement performance, resources, information and communication, and the monitoring and remediation process.

As part of the firm's risk assessment, the firm:

- Establishes quality objectives specified under CSQM 1 and any additional quality objectives considered necessary by the firm.
- Identifies and assesses quality risks by understanding and evaluating the nature and circumstances of the firm and of the engagements performed by the firm.
- Designs and implements responses to address those quality risks.

A deficiency in the firm's system of quality management exists when either:

- A quality objective is not established.
- A quality risk or combination of quality risks is not identified or properly assessed.
- A response or combination of responses does not reduce the likelihood of a related quality risk occurring.
- Another aspect of the system of quality management is absent or not properly designed, implemented or operating effectively, such that a requirement of CSQM 1 has not been addressed.

01 | GOVERNANCE & DECISION-MAKING

Senior leadership within a firm are ultimately responsible and accountable for quality and must demonstrate the values, ethics and behaviours that support a culture of quality in auditing through their actions and decision-making.

CPA Ontario asked firms how they incorporate external viewpoints into strategic and operational decision-making, how they establish a quality-first mindset around client acceptance and continuance decisions, and how they set clear and appropriate responsibility for audit quality.

OVERSIGHT WITH PERSPECTIVE: GETTING A SECOND OPINION

An outside view can bring with it fresh perspectives and foster transparency.

Independent non-executives often play this role on boards and advisory committees. They are removed from daily operations, which puts them in a unique position to constructively challenge views with external experience and expertise while facilitating issues such as disagreements between partners, conflicts of interest and ethics reporting.

For small- and medium-sized firms that do not have boards or advisory committees, engaging with external resources or consultants can help provide the oversight with perspective needed to protect audit quality.

WHAT WE FOUND

Many firm responses featured oversight by boards that included independent directors or independent advisory panels.

However, some firms identified oversight by partners, or management committees comprised solely of partners of the firm.

This lack of external perspective in decision-making increases the risk that decisions about priorities may not be adequately considering the importance of quality.

Many smaller firms cited their participation in local or global networks of independent firms as the means for obtaining an external perspective on its work by incorporating them into its internal monitoring on a rotational basis.

These networks also collaborate on new and emerging issues and standards, staff training, and share best practices on everything from file preparation to practice management. This approach is one way a smaller firm can ensure its audit quality practices are being viewed with fresh, independent eyes.

EXAMPLES OF EFFECTIVE PRACTICE INCLUDE:

Having external board directors with previous public company experience to provide perspective for decision-making.

Relying on peer firms within the firm network to review and discuss developments in the profession, practices, and modifications.

Retaining external consultants and subject matter specialists when an independent third party is required for perspective or to meet ethical requirements.

ACCEPTING CLIENTS: SHARING A COMMITMENT TO QUALITY

A strong sense of direction on quality allows a firm to make timely and effective decisions regarding which clients it works with and which industries it works in, based on the firm's values, strategic priorities, risk appetite, assessment process, technical competencies and available resources.

Working with clients that share the firm's focus on quality can help ensure a shared commitment to transparency.

At the same time, it is important to understand the essential role audit plays in the capital markets ecosystem. Firms must balance their strategic decision-making with a responsibility to serve and protect the capital markets and the public. This is especially true in complex and emerging markets, where the risk to take on a client or audit may be elevated or even outside the firm's usual risk appetite.

These are also areas where the role of audit has never been more important. A quality-first mindset will support a firm as it evolves to address complex reporting matters such as sustainability, cybersecurity, and digital currency.

WHAT WE FOUND

Stronger responses from firms included parameters around the types of clients they will work with and included conversations around exiting clients where pressures impact quality such as unmitigated fee and timing or resource concerns. One firm noted that by exiting clients where team members had identified unrealistic fee pressure and felt the client did not see the value of a high-quality audit, employee satisfaction and engagement improved.

This speaks to an important point: if a firm's leadership demonstrates audit quality is a priority, the quality of engagement will improve.

AUDIT COMMITTEES

Audit committees have oversight responsibilities over financial reporting, which can serve to hold company leadership accountable for a culture of quality, including prioritizing and cooperating with the audit.

Inadequate fees can introduce the risk of an inadequate audit. There may be instances where an effective audit can be obtained for a lower fee, but it can also create internal pressures to limit the impacts of low or reduced fees on margins.

The existence of an audit committee does not preclude the need for boards of directors to take responsibility for financial reporting, and that includes ensuring that audit fees are not set at a level that could lead to compromised quality.

Several firms also demonstrated a willingness to invest in the specialized knowledge and expertise required to serve clients that might otherwise not be within the scope of their risk profile, demonstrating that the profession can continue to fulfil its role in protecting capital markets in emerging sectors of the economy.

However, some weaker responses identified quality as a strategic priority, but they did not effectively reinforce its priority through firm policy, or through actions taken by leadership. These responses cited templates and checklists used to document client acceptance and continuance decisions but were not otherwise considered as part of the firm's overall strategy. To be effective, quality objectives must be reinforced through policy, clear action and direction driven from the very top.

RESPONSIBILITY FOR QUALITY: TAKING THE LEAD

While each firm is responsible for ensuring quality, ultimate responsibility and accountability for the system of quality management must lie with those who have the authority, influence, experience and knowledge to hold the rest of the organization to account.

For smaller firms, that could be a single managing partner. For larger firms, operational responsibility might be broken up and assigned to different people. Whatever the case may be, lines of responsibility should be clear and accessible, the message consistent and unwavering.

WHAT WE FOUND

Responsibility for quality often lies with the CEO or Managing Partner of the firm. But how roles are assigned to manage that responsibility differs between firms.

Stronger firm responses identified one individual who is both accessible to staff and connected to the engagement teams, laying out a clear structure for operationalizing quality management, while demonstrating clear and frequent communication from the individual responsible.

Some firms described firm-wide communications from their CEO on topics ranging from news headlines related to regulatory matters, to the importance of ethics, as well as support mechanisms for raising both quality and ethical concerns. This approach demonstrates a clear desire from the very top to reinforce the importance of quality to every member of the team.

However, some weaker responses identified one or more committees or groups responsible for quality with unclear structures, some of which were inaccessible to staff.

Consistency between responsibility and messaging reinforces the importance of audit quality, as does making the resources available within the firm to support engagement teams. When this does not happen, there is a risk that quality will not be prioritized in a firm's culture.

02 | ETHICAL MINDSET

Ethical behaviour is the foundation of trust, which is why any quality management system must be underpinned by a culture that recognizes and reinforces the importance of professional ethics, values and attitudes.

Codes of conduct and corporate policies lay out expectations around quality and ethics, but those are table stakes. Firms must go further to understand and evaluate compliance with these codes so they can identify gaps between firm requirements and how employees interpret those policies. Clear mechanisms are required for ensuring these behaviours are lived and incorporated into day-to-day practice.

We asked firms about the policies they have in place to support the reporting of concerns about ethical violations or compliance with professional standards and how they address fear of reprisal. We also inquired about policies surrounding academic integrity, and mechanisms put in place to prevent or detect possible breaches.

ENCOURAGE WHISTLEBLOWERS: DOING THE RIGHT THING

Whistleblowing plays a vital role in safeguarding the public and is an effective way to detect unethical conduct, but it is not without risk to the one blowing the whistle. Policy simply isn't enough. Encouraging staff to expose wrongdoing also means protecting them from reprisal as well as providing the necessary resources to create a safe system for reporting.

WHAT WE FOUND

The weaker responses from firms did not report any policies around whistleblowing, while others could not demonstrate a path for staff to report ethical concerns or violations other than through direct managers, which exposes the whistleblower to the potential of reprisal.

WHISTLEBLOWER HELPLINES

Whistleblower helplines that engage external third-party service providers can, with the appropriate structure, create secure, anonymous, confidential and accessible reporting helplines available to both internal and external parties involved with the firm.

A whistleblower helpline can also be established internally, so long as the safety and protection of the whistleblower is considered in determining who is responsible for receiving, reviewing, and resolving issues.

A truly independent system will always need to be broader than simply independent from management, as a whistleblower is likely to perceive other internal parties to be acting in the interest of the firm rather than in their interest.

The majority of responses referenced general whistleblower policies or codes of conduct, without any clear systems to support them. Failing to establish support for whistleblowers and address fear of reprisal creates a risk that concerns about ethical violations and compliance with professional standards that impact audit quality will not be raised.

The stronger responses demonstrated how policies have been implemented, reinforced and monitored within the firm. Some firms are encouraging partners and staff alike to speak up by allocating resources towards ensuring safety and anonymity in reporting ethical concerns or violations, often through dedicated whistleblower helplines.

One firm described a speak up campaign that previewed the firm's ethics helpline, introduced an ethics group available for consultation and encouraged all professionals to report unethical conduct at any time, demonstrating a clear link between the tone at the top and the firm's culture.

Embedding a strong whistleblower process within a culture of open dialogue around mistakes, where staff and others feel free to come forward with problems, increases the likelihood that wrongdoing is uncovered or, better yet, caught before it becomes a serious issue.

EXAMPLES OF EFFECTIVE PRACTICE INCLUDE:

Acknowledging whistleblower reports in a timely manner, sometimes even within 24 hours.

Creating internal training courses on whistleblower policies which must be completed, with a high score required for successful completion.

Engaging an external third party to provide an appropriate structure for a secure, anonymous, confidential reporting helpline.

Appointing a Complaints or Ethics Officer who ensures confidentiality and protection for any team member.

Providing annual certification for personnel on Code of Conduct and other policies.

Obtaining feedback through an annual ethics survey to gauge uptake of the firm's ethical culture.

ACADEMIC DISHONESTY: PASSING THE ETHICS TEST

Whether during professional exams or internal tests, plagiarism and cheating are breaches of professional conduct, an ethical violation and undermine the credibility and integrity of the CPA designation.

In short, they are unacceptable.

Because firms are required to have policies around ethical behaviour and controls to identify and prevent breaches, this behaviour also calls into question the firm's quality management practices and culture.

WHAT WE FOUND

Firm responses frequently identified academic integrity policies and controls to detect possible breaches, but stronger responses included methods to *inform*, *prevent*, *detect*, and *monitor*.

TO INFORM

These systems start with attestations embedded within knowledge assessments and training to remind staff of their responsibility to complete assessments independently, prohibiting the use or distribution of answers.

TO PREVENT

Enhancements have been added to re-order assessments, which makes answer-sharing no longer worth it or to only share a result or outcome at the end of an examination rather than providing an answer key.

TO DETECT AND MONITOR

Systems have been established to compare time spent on courses and assessments against expected length and completion times.

EXAMPLES OF EFFECTIVE PRACTICE INCLUDE:

Tracking how long it takes to complete training or an assessment, repeated attempts to pass an assessment and performance on assessments.

Retaining training and tests with the national office, and no longer sharing answer keys following the completion of an exam.

Testing that requires analysis and application-based questions, instead of relying on just recall and shuffling questions so responses are in a different order.

Including a warning that an assessment is to be completed on an individual basis and answers are not to be shared.

Adding attestations to the beginning of all curriculums and annual compliance confirmations.

Introducing discipline up to and including termination from the firm for anyone found to have engaged in cheating or failed to reporting cheating.

Some larger firms have their national office retain all training and tests for in-house programs to reduce any risk around answer sharing. Small and medium firms may not have in-house programs or assessments, however controls should still be considered for courses provided by third parties, including how those third parties monitor learning and assessments.

Some firms proactively identify pressures that might result in unwanted behaviours like cheating and answer sharing and made efforts to mitigate those pressures directly.

One firm described adjusting the learning system to not overly penalize assessment takers who fail to pass on the first attempt, emphasizing learning objectives and providing for additional attempts. Another example encouraged the use of application-based questions to assess competence, rather than recall.

Lastly, some firms identified time pressures as contributing to the issue and adjusted deadlines around internal training, allowing for it to be spread throughout the year.

03 | TALENT & TECHNOLOGY

Audit quality must be reinforced in the way firms invest in and allocate resources, including people and technology. This means embedding quality into how firms recruit and develop talent, assess performance, provide feedback and compensate their people.

The right talent also requires the right tools to ensure consistency in the performance of quality engagements, which is why investing in innovation and technology is critical.

We asked firms how they allocate resources to support quality and compliance with CPD requirements, and how they are investing in software and technology to support audit quality management.

COMPENSATION TIED TO QUALITY: REWARDING PERFORMANCE

Regardless of firm size, quality should be built into performance at all levels.

There must be a clear link between high-quality audits and reward, including remuneration, promotion and other incentives. Equally as important is reinforcing consequences where breaches arise, or where low-quality work is completed.

The link between compensation and quality extends to attracting and retaining diverse, sufficiently trained and experienced staff to service clients. Firms need trained people at all levels to deliver high-quality audits. CPA Ontario has received feedback from post-secondary institutions that compensation is a top issue for students. As clients are expected to appropriately value audit work and compensate firms for high-quality audits, firms need to recognize the importance of people in the delivery of high-quality audits and compensate them accordingly.

WHAT WE FOUND

Weaker firm responses reported a vague link between compensation or financial reward and achieving some form of quality outcome as part of the overall performance appraisal for more senior people. Some responses did not demonstrate a link between compensation and quality at any level, often citing standard annual appraisal processes with salary increases stipulated at market rates.

Without a clear tie between compensation and quality, there is no incentive to put audit quality first. Stronger responses tied compensation for staff at all levels, including partners, directly to quality outcomes with clear and specific rewards or penalties for meeting, or failing to meet, both internal and external standards.

Several firms linked partner compensation to specific ratings of performance on quality metrics, based on real-time monitoring.

For other professionals, best practices linked feedback received on quality at the engagement level to promotion and compensation decisions.

There are metrics available to small and medium firms to help them assess quality. These include external monitor results, the results of regulatory reviews or monitoring instances of identified breaches in firm policy, such as missed archiving deadlines or inadequate professional development being completed.

Quality can also be linked to compensation indirectly by prioritizing and supporting appropriate project management and accurate billings across the firm to mitigate the risk of cutting corners on engagements due to capacity, timing issues or fee pressure.

With respect to attraction and retention, some firm responses identified increased compensation, more flexible work and reduced utilization pressures that emphasize wellbeing as leading to a reduction in turnover rates. Others have responded by finding more ways to recognize contributions with meaningful rewards, such as executing mid-year pay

increases as part of a commitment to competitive pay and mid-year promotions to recognize professionals already performing at the next level.

As with the overall system of quality management, feedback is also essential for attraction, retention and talent management. Some of the stronger responses emphasized coaching and 360-degree feedback, with some firms rolling out surveys to measure satisfaction, engagement, and commitment on a regular basis.

EXAMPLES OF EFFECTIVE PRACTICE INCLUDE:

Putting strategic performance outcomes specified by service line and level in place, including a monetary penalty for partners who fail inspections.

Tying partner compensation to a rating, with income partners rated as “needs improvement” receiving a reduction in their incentive compensation and/or base salary.

Determining promotion and compensation decisions using quality feedback at the engagement level and other quality considerations such as learning compliance.

Creating a steering committee to ensure that attributes of quality are given appropriate recognition in the compensation process for partners.

Designing an audit quality dashboard that factors into the key metrics for partner performance.

DEVELOPING TALENT: LOOKING TO THE FUTURE

Firms have a responsibility to be forward-looking and committed to building the future of the profession. Investing in technical skills, building specializations and supporting knowledge sharing serves to attract, retain and develop leaders within the firm which in turn supports the delivery of high-quality audits.

Learning is essential to quality and goes far beyond meeting the CPD requirements for maintaining membership and licensure.

Firms should embrace a comprehensive approach with an emphasis on continuous learning by:

- Providing sufficient time for professional staff to engage in and complete training courses and assessments.
- Training in technical competencies of assurance and financial reporting as well as focused areas, such as emerging industries and digital upskilling.
- Sharing results of inspections and monitoring, both internal and external, across the firm to promote dialogue around quality.

Larger firms offer in-house learning curriculums spanning technical accounting and auditing, professional standards, regulatory requirements, ethics and independence, emerging trends, and leadership development.

Small and medium firms typically do not offer in-house learning and development, but many identified the use of firm networks for the delivery of training opportunities

PUBLIC ACCOUNTING LICENCE HOLDERS

CPA Ontario's review of CPD hours for PAL holders identified concerns with the mechanisms that firms have put in place to ensure that CPD requirements are met. Relevant CPD is required to ensure a PAL holder has the depth and breadth of competencies necessary for the practice of public accounting; the learning outcomes and competencies for PAL holders are detailed in International Education Standard (IES) 8.

The most common concern that required follow-up or resulted in guidance or referral was with respect to CPD hours taken in tax. Hours in taxation, such as annual personal and corporate tax updates, do not count towards CPD for licensure unless they meet the learning outcomes identified in IES 8, directly. Tax under IES 8 is limited to evaluating procedures performed to address the risks of material misstatement in the financial statements in respect of taxation, and the effect of the results of these procedures on the overall audit strategy.

Additionally, where CPD course selections can be mapped to IES 8, the proportion of CPD taken in specific areas must be appropriate. Concentrated hours in one learning outcome will not achieve the breadth required. We noted high concentrations in tax and personal development with less focus on technical accounting and assurance competencies, which is concerning given the nature of public practice and the risk to capital markets.

Members and PAL holders alike are also reminded that they are obligated to complete four verifiable hours in professional ethics for each triennial period. Ethics is foundational to maintaining the public trust, which is why it is the responsibility of every member to ensure that they are maintaining a focus on learning and understanding the nuances of ethical practice.

or have made use of external professional development course offerings. Firms can further capitalize on these sessions by offering debriefs to discuss how learnings can be integrated and applied within the firms work.

The responsibility for complying with CPD requirements lies with each member, but appropriate CPD is a critical component of a firm's quality management system. CPD deficiencies can be an indicator that the firm's quality management system may not be robust and may pose a potential risk to audit quality.

WHAT WE FOUND

Most firms identified policies around annual professional development and compliance, but the strongest responses demonstrated how the firm integrated learning into the workday, building non-chargeable learning time into both scheduling and utilization rate targets. Some firms tag specific days for learning and incorporate dashboards to monitor compliance with learning and development.

However, weaker responses only identified policies around CPD consistent with the regulatory requirements to maintain membership without any clear link to the specific requirements for licensure or any programs and practices to encourage continuous learning and development.

Without allocating resources in a way that supports compliance as well as learning and competency development, engagement teams may not be up to date on current pronouncements, emerging issues and relevant standards.

Some responses noted that their firm pivoted to incorporate learning into regular communications and online webinars to engage professional staff on an ongoing basis during the pandemic. This approach has proven effective, even under new hybrid working environments.

The method of delivery may vary significantly across firms, but dedicating the time and the resources to developing talent is the strongest indicator of a successful culture of learning.

EXAMPLES OF EFFECTIVE PRACTICE INCLUDE:

Dedicating one day a month to learning, blocking calendars to create time in busy schedules to learn, develop, grow, and encourage the completion of CPD.

Implementing learning models where all training can be conducted during the workday.

Factoring non-compliance with learning requirements into the assessment of annual performance, promotions, and compensation.

Staggering training deadlines throughout the year to reduce pressure on staff to complete a high volume of training at the end of the year.

Using a people leader dashboard to monitor completion status of mandatory courses for direct reports.

Booking required learning time into the scheduling system, with additional time booked for staff with many outstanding learning or assessments close to the due date.

INVESTING IN TECHNOLOGY: USING THE RIGHT TOOLS

Strategic investment in software and technology can help firms manage the consistency and performance of engagements, including tracking progress, supervising and reviewing work and timely file assembly – all of which are critical to audit quality.

WHAT WE FOUND

Some of the larger firms reported developing their own methodologies or use methodologies procured from their international networks. Others use a common third-party off-the-shelf software with embedded audit methodology solutions and optional enhancements to tailor the audit approach to the engagement.

As part of its review of audit quality, CPA Ontario reviewed third-party software and found that available preventive and detective controls can vary depending on whether the desktop, cloud-based or hybrid system is used. Nevertheless, firms should ensure they are taking advantage of any available controls.

Cloud-based solutions can help streamline working paper preparation and ensure audits are assembled and archived automatically within the permitted time frame. Since the date and time stamps typically cannot be altered in this version they help mitigate audit quality risks, such as working papers being modified after the date of the audit report or backdated through manual override. As mentioned in this report, instances of backdating have been identified through the work of our Practice Inspection team, presenting a risk to the public and the profession, and are never acceptable.

The use of technology should never replace professional skepticism and judgement, two of the foundational skills of a CPA. Software-based standardized checklists and working papers may be efficient but they often do not allow enough flexibility, scalability or tailoring for auditors to demonstrate the work performed and the conclusions reached in complex entities and engagements.

04 | WORKING PAPERS

A firm's system of quality management is embedded throughout every phase of an audit engagement: planning, execution, review, supervision, consultation, and communication of audit results.

Critical to this process is the documentation of the audit working papers, which supports the audit opinion.

Effective use of software and technology, combined with strong prevention and detection controls, can assist with timely lockdown and archiving and help reduce underlying pressures that can lead to backdating working papers and manual override.

We asked firms how they control lockdown and archiving and deal with quality risks such as modified working papers, backdating and manual override, as well as how resources such as software and technology are used to support quality in these areas of engagement performance.

LOCKDOWN AND ARCHIVING: ASSEMBLING THE FILE

For audits conducted under the Canadian Auditing Standards (CAS), an appropriate time limit within which to complete the assembly of the final engagement file is ordinarily not more than 60 days after the date of the audit report.

Automating the lockdown process and reducing the time permitted between issuing the audit report and locking down the file encourages the audit team to ensure that all audit evidence has been obtained and documented in the file prior to issuing the audit report.

EXAMPLES OF EFFECTIVE PRACTICE INCLUDE:

Implementing tracking for all engagements not locked down and archived after internal deadline.

Introducing a manual lockdown at which time the file becomes read-only and cannot be modified, documents cannot be added or deleted.

Introducing a quality dashboard, which includes the number of days left until file needs to be locked down.

Assembling and archiving within 30 days from the audit report date.

Monitoring through an archival tool that sends reminders and archiving reports, which are run quarterly by business units.

Evaluating partners based on compliance with archiving policies as part of their annual assessments, which impacts compensation.

Reopening a locked down file requires any changes to be documented in the document assembly.

Including an attestation that no completed files have been modified after the lockdown/archive date without an appropriate memo being added to the file in the annual declaration.

WHAT WE FOUND

Most firm responses reported using a combination of automatic and manual lockdown processes, with the window between engagement completion and lockdown ranging from 30 to 60 days, which is considered the maximum appropriate under the current standards.

Firms requiring a 60-day timeframe within their policies may be at a far greater risk of missing lockdown deadlines as required by the standards, as the internal policy leaves no room for failure due to administrative, technological, or other extenuating circumstances.

Stronger responses saw firms taking steps to ensure that all required documentation was in the file and complete prior to issuing the audit report. The most effective practices saw automated lockdown set to occur immediately after file completion or within 10 to 15 days of issuing the audit report.

It was noted by these firms that the accelerated file assembly period changed behaviours, encouraging completion of working papers in a timely manner, resulting in minimal hours being incurred by the engagement team following the audit report date.

However, several firms did not report having controls in place to prevent and detect instances of failure around lockdown and archiving. In some cases, we found software features that could identify dating issues, such as the engagement history log, were not enabled.

The engagement history log feature tracks file and working paper access and signoff and, since it cannot be altered, may be an effective detective control. It exists in all versions of frequently used third-party audit software but can be disabled by firms.

Systems only work if you monitor their effectiveness. Some firms identified thorough use of tracking and review, including review of the engagement history log, to identify

issues. They also used compensating controls, such as manual tracking and monitoring in spreadsheets to identify and follow up on upcoming or missed lockdown deadlines.

DOCUMENTATION: PUTTING CONTROLS IN PLACE

Using software and technology as an audit tool relies on communication and enforcement of the highest ethical standards within the firm. Simply stating that manual override of system generated controls is not permitted is not enough. Firms are responsible for ensuring that these policies and controls are implemented, tested, and working effectively.

They must also ensure compensating controls are in place to prevent or detect failures including unauthorized access, manual override, or backdating of working papers.

Backdating working papers and manual override are ethical violations under the CPA Code. There is never an excuse for it.

WHAT WE FOUND

Several weaker responses identified reliance on policy or system controls that are not operating effectively or have not been tested. This is wholly inadequate for maintaining and supporting a firm's commitment to audit quality.

Firms using proprietary software may have more options available to embed system controls than those that employ off-the-shelf software. However, where a tool allows unwanted changes, compensating controls can and should be used to reduce or remove this risk.

A strong commitment to oversight around performance of the audit engagement, including progression through the phases of the audit, monitoring of time spent and work papers completed, and timely review and resolution of issues by leadership can reduce both the opportunity and pressure that might lead to inappropriate behaviours such as backdating or manual override.

EXAMPLES OF EFFECTIVE PRACTICE INCLUDE:

Implementing an audit quality milestones program requiring engagement teams to complete certain activities related to execution, supervision, and review by specified dates throughout the audit engagement, with compliance monitored by leadership.

Putting in place a system control that requires documentation of an explanation to support why a date other than the current date is being used for a signoff.

Monitoring chargeable hours after signoff and lockdown to identify areas where modification or manual override may have occurred.

Integrating working papers into the software platform to reduce the possibility of manual override.

05 | MONITORING ACTIVITIES

In-depth and rigorous internal monitoring is critical to measuring the overall effectiveness of the system of quality management.

Firms need to establish clear communication around the analysis and remediation of any deficiencies, ensuring information sharing within engagement teams and across the firm. Effectively measuring compliance allows a firm to identify and respond to quality risks quickly and effectively.

CYCLICAL MONITORING AND REAL-TIME FEEDBACK: STRIKING THE BALANCE

The goal of robust internal monitoring processes should be striking the proper balance between pre-issuance reviews for timely feedback and cyclical internal inspections that look at overall compliance and emphasize remediation with a view to improving audit quality.

Depending on firm size and available resources, monitoring may be entirely internal, wholly outsourced to an external monitor or use a hybrid approach, depending on the expertise and independence requirements on any given file. Some firms make effective use of their firm networks to complete peer reviews in addition to standard monitoring.

WHAT WE FOUND

Weaker firm responses identified periodic inspection of completed files using a structured, checklist-style approach. Stronger responses emphasized timing, frequency, and complexity in determining which files are selected as part of cyclical monitoring and when, placing a greater emphasis on addressing quality risks and determining the root cause for any significant findings.

Audit is a dynamic environment and long periods of time between monitoring could result in issues going unaddressed. Furthermore, each audit's considerations are complex and vary by file, making the use of standardized forms and checklists less desirable to facilitate understanding and issue remediation.

Some firms reported going so far as to incorporate an element of unpredictability, selecting partners and files more or less frequently than the standard period, which can help to both detect and deter quality issues in every file completed.

Repeated instances of failure to comply with internal policy and procedure – identified as part of the firm's own cyclical monitoring activities and not remediated – were also identified. It should be understood that effective remediation of deficiencies is at the core of the monitoring process. Repeated and unaddressed deficiencies identified in previous monitoring cycles is unacceptable.

The best approaches to monitoring audit quality incorporate a timely feedback loop to gauge performance within the audit practice and encourage a culture of continuous improvement by openly discussing mistakes as a learning and actioning corrections prior to issuing the audit report.

Many firms have taken steps to develop indicators to assist with measuring the audit process, including:

- Timing
- Audit milestones
- Use of specialists
- Experience of the engagement team
- Audit hours by areas of significant risk
- Deliverables

These indicators can lead to important conversations about investing in the resources, the people, the policies, and the technology to support positive quality outcomes. Some firms have also found it useful to monitor

key performance indicators for excessive hours, estimated hours and missed vacation time, noting that as hours go up risk often goes up too. Where excessive hours are identified or predicted, firms can act in a timely manner to ensure audit quality is upheld.

Lastly, some firms are employing real-time monitoring while an audit is in progress. This approach helps firms pivot when these “hot” checks indicate that additional communication or support may be needed around higher-risk areas, or to encourage adoption of new standards or respond to issues identified in internal and external monitoring.

These reviews can also help teams identify common themes and challenges and get assistance working through complex areas in a live file. Some firms reported taking this concept even further, requiring engagement teams to formally consult on specific or complex issues during the audit to facilitate information sharing and real-time solutions. Larger firms often cited reliance on national practice advisory groups for consultation, but small and medium firms typically use other team members, external advisors, or colleagues in their firm networks.

EXAMPLES OF EFFECTIVE PRACTICE INCLUDE:

Instituting a process of peer reviews annually with partner firms, covering one completed engagement for each engagement partner.

Ensuring coverage across engagement types, new and recurring clients, with at least one type of engagement for each partner for each type of authorization.

Presenting the results of internal monitoring to the entire practice and leadership.

Setting up root cause meetings with engagement teams and groups.

Milestone monitoring to track engagement team achievement of key metrics as they progress through audits.

Internal independent reviews of areas of focus on in-progress audit engagements to provide direct real-time support and coaching before the reports are signed.

CONCLUSIONS

CPA Ontario undertook this review to address specific concerns with audit quality, as identified through practice inspection findings at a number of registered firm practicing offices. These findings, coupled with the move from quality control to quality management standards, meant that the time was right to review audit quality in Ontario.

This review revealed a recognition among firms that audit quality must remain a top priority. However, it also uncovered deficiencies.

A deficiency exists in the quality management system when a quality risk is not identified or properly assessed, or processes do not reduce the likelihood of a quality risk occurring.

When unidentified, or left unaddressed, quality risks can have a pervasive effect on the design, implementation, and operation of the system of quality management.

It can call into question whether the objectives of the system are being achieved, which can then significantly impact audit quality.

Throughout our review, we looked at any unidentified, unaddressed or under-addressed quality risks, along with the firm's description of their evaluation and remediation process, in determining whether a deficiency may be present.

Where deficiencies were present and pervasive enough to challenge the overall quality objectives, the firm was referred to CPA Ontario's Practice Inspection team for additional, regulatory review of identified quality risk areas this year.

Four firms, representing less than 1% of reporting issuers in Ontario were identified as having deficiencies in their quality management system.

These deficiencies warranted referral to Practice Inspection, as follows:

- Did not adequately identify and address quality risks around:
 - Ethical violations not being raised due to fear of reprisal
 - Academic dishonesty
 - Lockdown and archiving of working papers
 - Manual override and backdating of working papers
 - Learning and competency development
 - Compliance with CPD requirements
 - Non-compliance with firm policies and procedures
- Did not provide sufficient detail about the internal monitoring processes to establish that quality risks are being adequately identified and addressed through the system of quality management and that deficiencies are being remediated.

The review by the Practice Inspection team of these areas of focus could lead to an action plan to remediate identified deficiencies in the quality management system, reinspection or, in the case of significant conduct issues, referral for investigation by the Professional Conduct Committee.

In the Continuing Professional Development review of Public Accounting Licence (PAL) holders, approximately 70% of the reviews were considered satisfactory, requiring no follow-up.

The rest required follow-up for clarification as to how the CPD related to the competencies specified in IES 8. Eleven per cent of the PAL holders selected for review were provided specific guidance to address compliance concerns or required further regulatory action.

In two of the reviews, individual PAL holders demonstrated compliance issues of significant concern, causing a strong disconnect between what these firms had described as robust learning and development policies and our findings around the specific CPD activities.

Deficiencies of this severity call into question the firm's overall system of quality management. While other deficiencies were present in these two reviews, the severity of the CPD deficiencies resulted in immediate referral to CPA Ontario's Practice Inspection team.

WHERE WE GO FROM HERE

The responsibility for audit quality rests with every member of the profession. It's about more than just the reputation of CPAs – it's about the public's trust in our capital markets, and the very foundation of the Canadian economy.

This review was in response to concerns surrounding a decline in audit quality, identified through our Practice Inspection process, as well as the implementation of new standards.

Through this review, we identified several areas where a risk to quality is present that, if left unaddressed, could contribute to an overall decline in the quality of audits. We uncovered deficiencies that warranted further attention, and as the regulator of the profession it is the role of CPA Ontario to protect the public and ensure these deficiencies are properly addressed and corrected.

This task will be undertaken by our Practice Inspection team this year and going forward, as they conduct an in-depth review of quality management systems, including a review of all five areas of unidentified or unaddressed risk.

However, our review also uncovered recognition and understanding among the firms that audit quality must remain a top priority for the profession. Many firms have put in place effective policies and practices that put quality management at the very heart of their work.

As CSQM 1 and CSQM 2 became effective for audits and reviews of financial statements or other assurance engagements as of December 15, 2022, firms were required to have designed and implemented their system of quality management by this date and within one year perform an evaluation of that system.

This evaluation is an opportunity for firms to consider the findings in this review and use it as one lens by which to evaluate the effectiveness of their own practices. The examples we have included should serve as a road map for firms to continue raising the bar on audit quality and fulfilling their duty to protect the public.

