



# Discussion Paper

## Canadian Auditing Standards

# Exploring Standard-Setting Options for Audits of Less Complex Entities

**September 2021**

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**COMMENTS TO THE AASB MUST BE RECEIVED BY  
December 10, 2021**

**COMMENTS TO THE IAASB MUST BE RECEIVED BY  
January 31, 2022**

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We value your input and look forward to your feedback on this Discussion Paper. Comment on this document by taking part in the [Connect.FRASCanada.ca](https://connect.frascanada.ca) project or submitting a comment letter addressed to:

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This Discussion Paper is intended to obtain input from stakeholders on possible options that might be explored in Canada to address the challenge of applying the Canadian Auditing Standards (CASs) to audits of less complex entities. The Discussion Paper also seeks views on the concept of a separate standard for the audit of less complex entities as well as views on the International Auditing and Assurance Standards Board's (IAASB) Exposure Draft "Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities."

Individuals and organizations are invited to send written comments on this Discussion Paper. Comments are most helpful if they relate to a specific paragraph or group of paragraphs in the Discussion Paper. Challenges raised should clearly explain the problem and include a suggested alternative, supported by reasoning. All comments received by the AASB will be available on the website shortly after the comment deadline unless confidentiality is requested. The request for confidentiality must be stated explicitly within the response.

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## INTRODUCTION

1. The Auditing and Assurance Standards Board (AASB) is issuing this Discussion Paper to:
  - (a) seek views on possible options that the Board might explore in Canada to address the challenges of applying the Canadian Auditing Standards (CASs) to audits of less complex entities (LCEs); and
  - (b) encourage Canadian stakeholders to provide views to the Board on the International Auditing and Assurance Standards Board's (IAASB) Exposure Draft, "[Proposed International Standard on Auditing for Audits of Financial Statements of Less Complex Entities](#)" (ED-ISA for LCE).
2. The challenges of applying the CASs have historically been around the difficulty experienced in audits of smaller entities that are less complex. We have since shifted to refer to LCEs (rather than smaller entities) to reflect that the entity's complexity is not solely determined by its size. Some smaller entities can be more complex, and some larger entities can be less complex. Therefore, this Discussion Paper refers to LCEs when describing entities whose operations and financial statements are less complex. However, the AASB recognizes that LCEs may also have some elements of complexity, the nature of which may vary from year to year.
3. The CASs, adopted from the International Standards on Auditing (ISAs), are principles-based, and apply to audits of entities of all sizes and complexities. However, some stakeholders have told the AASB they face challenges applying the CASs to the entity's less-complex elements.
4. The AASB's [2022-2025 Strategic Plan](#) outlines its commitment to "provide solutions that respond to the environment for small and medium-sized entities and allow practitioners to apply standards in a scalable and proportional way on the less complex elements of an entity." Scalability and proportionality describe the standards' ability to be consistently applied and be globally operable across entities of all sizes and in all regions, and allow the practitioners to apply judgment and thoughtful consideration to the varying circumstances of the audit at hand.
5. Small and micro-entities make up a substantial segment of the Canadian economy.<sup>1</sup> The AASB believes the practitioners' ability to apply the CASs to LCEs in a scalable and proportional way is critical to performing high-quality, cost-effective audits that serve the public interest. This Discussion Paper is an essential step in obtaining stakeholder perspectives to help the Board design solutions to achieve its strategic objectives in this area.
6. This Discussion Paper explores three possible options that the AASB might consider undertaking. The Board is seeking views from stakeholders to help make an informed decision on the direction of its future work. The Board invites all interested stakeholders to respond, including:
  - practitioners and audit firms of all sizes;
  - lenders and other users of financial statements;
  - regulators, including provincial CPA bodies;
  - developers of audit tools and methodologies; and
  - academics.

To read more about the work done to date on this project, visit the [project page](#).

Please review "[Comments requested](#)" in Section III for information on preparing a response to this Discussion Paper.

<sup>1</sup> Innovation, Science and Economic Development Canada, [Key Small Business Statistics](#) (Ottawa, ON: ISED, November 2020). As of December 2019, of the 1.23 million businesses in Canada, 97.9 per cent were small businesses (fewer than 100 employees) and 54.9 per cent were micro-businesses (one to four employees).

## SECTION I – BACKGROUND

### What the AASB has done

7. Over the last few years, the AASB's main activities on this initiative included:
  - (a) conducting outreach activities on the challenges practitioners face when auditing LCEs;
  - (b) listening and contributing to international deliberations on this topic, including attending the 2017 and 2019 IAASB SMP/SME Working Conferences in Paris, France;
  - (c) monitoring the IAASB's progress on this initiative, including providing feedback on the IAASB's meeting agenda papers to the IAASB members from Canada;
  - (d) seeking broad Canadian stakeholders' input on the IAASB's 2019 [Discussion Paper, "Audits of Less Complex Entities: Exploring Possible Options to Address the Challenges in Applying the ISAs."](#) and submitting a [response letter](#) shaped by that feedback;
  - (e) establishing the [Audits of LCE Advisory Group](#) to support the AASB in reviewing and responding to materials issued by the IAASB; and
  - (f) providing input to CPA Canada's implementation guidance to help address the challenges in identifying and assessing risks while emphasizing the scalability of the standard with a focus on LCEs – [Implementation Tool for Auditors, "The Risk Assessment Process: Tips on Implementing Revised CAS 315<sup>2</sup>."](#)

### Public interest considerations

8. The AASB's previous consultations were with a broad range of stakeholders, including practice reviewers, practice advisors, developers of audit tools and methodologies, regulators, and practitioners from firms of various sizes. The feedback some of these stakeholders provided has raised the following concerns:
  - (a) The CASs have become complex, lengthy, overly detailed and challenging to navigate.
  - (b) The CASs are not explicit enough when requirements are scalable or proportionate for an entity's less-complex elements.
  - (c) Specific requirements in the CASs are particularly challenging to apply in LCE audits, as set out in [Appendix I](#).
  - (d) The CASs are unclear on the required documentation when specific audit procedures have not been performed because they are ineffective or do not apply.
9. The public interest considerations based on the concerns raised by some stakeholders are listed below:
  - (a) Practitioners may not consistently apply the CASs in LCE audits, which may affect the performance of high-quality audits.
  - (b) Practitioners may spend unnecessary time and effort performing procedures that may be ineffective or create redundant documentation, which may affect the performance of cost-effective audits. If conducting audits is not cost-effective (i.e., the cost of the requirements that the standard imposes exceeds expected benefits from compliance with those standards), it may become a barrier in engaging auditors.
10. Some stakeholders have raised several other challenges of performing audits not related to standard-setting, as listed below:
  - (a) Users may not understand an audit's value and, therefore, clients might question the cost-benefit of the audit work performed and pressure practitioners to reduce audit fees.

2 CAS 315, *Identifying and Assessing the Risks of Material Misstatement*

- (b) People with the right skills and relevant experience in performing high-quality audits are challenging to attract, train and retain.
  - (c) Practitioners are reluctant to exercise professional judgment in scaling or modifying the requirements in the CASs when they audit LCEs, primarily because of a perceived inspection risk.
  - (d) Practitioners rely on “off-the-shelf” tools and methodologies, often with generic forms and templates that can be challenging to customize to achieve an efficient audit.
11. While examining these other challenges is outside the scope of its work as a standard-setter, the AASB recognizes that they may influence the feedback it receives.

See [question 1](#) about the public interest considerations in “[Comments requested](#)” in Section III.

## Where does the AASB go now?

12. In Canada, the AASB’s policy is to adopt the IAASB’s ISAs and its International Standards on Quality Management. The AASB’s decision to adopt other international standards the IAASB issues is made on a case-by-case basis. For example, ED-ISA for LCE will not be part of the ISAs when finalized. Therefore, the AASB’s decision to adopt it in Canada will be based on whether it meets Canadian stakeholders’ needs and serves the Canadian public interest.
13. Before the IAASB commenced the development of ED-ISA for LCE, the AASB asked Canadian stakeholders for their views about the concept of a separate standard for LCE audits. At that time, stakeholders’ support for a separate standard for LCE audits was mixed. However, the Board believes reviewing ED-ISA for LCE provides an opportunity for stakeholders to closely examine what a separate standard for LCE audits may look like and consider whether their previous views have changed.
14. The AASB believes it needs to seek feedback from stakeholders on different options for moving forward in Canada. Such information will inform the Board on whether to pursue a separate standard for LCE audits (for example, by adopting the ISA for LCE that will result from the IAASB’s project) or undertake other options. These views will also inform the Board’s response to the IAASB’s Exposure Draft.

## SECTION II – POSSIBLE OPTIONS IN CANADA

15. Paragraphs 8-9 set out stakeholders’ concerns raised and the public interest considerations specific to applying the CASs to LCE audits. The AASB is exploring three possible options to address these issues. The most appropriate way forward may be one option, a combination of options or only parts of the options. It may also include other options identified by respondents. What follows is a description of the possible options, including their benefits and drawbacks.

### Option 1 – Separate standard for LCE audits

16. Option 1 involves having a separate Canadian standard for LCE audits, including assessing whether ED-ISA for LCE is appropriate to:
- (a) adopt in Canada; or
  - (b) serve as a basis for developing an equivalent Canadian standard, where the wording of ED-ISA for LCE may be amended to reflect the Canadian environment and address concerns raised by Canadian stakeholders.

17. The benefits and drawbacks of a separate standard for LCE audits, using ED-ISA for LCE as an example, are set out below.

### Benefits

- (a) A separate standard for LCE audits serves the public interest (see paragraph 18 of the IAASB's Explanatory Memorandum).
- (b) The IAASB developed ED-ISA for LCE to help practitioners understand the flow of an audit with clear and understandable requirements (see paragraph 30 of the IAASB's Explanatory Memorandum). Therefore, ED-ISA for LCE may be more effective and efficient for audit firms to develop methodologies and training for LCE audits.
- (c) ED-ISA for LCE is tailored to the nature and circumstances of LCE audits. As a result, practitioners who perform LCE audits may not need to spend time identifying what is applicable and what is not when the entity is less complex. Therefore, practitioners could invest more time executing appropriate procedures that more effectively target LCE audits (see paragraph 100 of the IAASB's Explanatory Memorandum).
- (d) ED-ISA for LCE may clarify documentation requirements and help practitioners avoid creating redundant documentation.
- (e) ED-ISA for LCE may provide a comprehensive solution by addressing matters that may arise during the phases of LCE audits.
- (f) Anecdotal evidence in Canada suggests that some practitioners have moved away from performing audits because they are not cost effective. The IAASB developed ED-ISA for LCE as a cost-effective global solution to providing a reasonable assurance opinion for LCE audits.
- (g) Because ED-ISA for LCE will be a global standard, Canadian LCE audits will be more consistent with their international counterparts in terms of audit benefits and cost.
- (h) Under its transparent and rigorous due process, the IAASB carefully considers stakeholders' views when developing new standards. Therefore, if there is Canadian support for a separate standard for LCE audits, there may be no need to duplicate the IAASB's efforts.
- (i) ED-ISA for LCE is based on the ISAs' (and the CASs') core requirements. Therefore, for practitioners already familiar with the CASs, ED-ISA for LCE may be relatively easy to implement.

### Drawbacks

- (a) ED-ISA for LCE requires practitioners to exercise a significant amount of judgment in deciding whether it can be used. If a practitioner applied ED-ISA for LCE when it was inappropriate to do so (for example, if they used the standard in the audit of an entity with both complex and less-complex elements), they would not have obtained sufficient appropriate audit evidence to support the reasonable assurance opinion.
- (b) ED-ISA for LCE requires the auditor's report to state compliance with the ISA for LCE. As a result, the public may perceive an audit conducted using ED-ISA for LCE as providing a lower level of assurance than an audit conducted using the ISAs (and the CASs), which may create confusion and exacerbate users' expectation gap.
- (c) The core requirements in the ISAs (and the CASs) are included in ED-ISA for LCE as they are needed to obtain a reasonable assurance opinion (see paragraph 101 of the IAASB's Explanatory Memorandum). As a result, ED-ISA for LCE may not substantially reduce the work effort to perform an LCE audit. Therefore, practitioners may not achieve significant efficiencies.
- (d) The guidance provided in essential explanatory material (EEM) in ED-ISA for LCE is much more limited than is the application material provided in the ISAs (and the CASs) (see paragraph 88 of the IAASB's Explanatory Memorandum). Therefore, practitioners may lack sufficient guidance to perform high-quality audits.
- (e) The need for education, training and maintenance of audit methodologies will increase for practitioners and firms using both the CASs and the separate standard for LCE audits.

- (f) ED-ISA for LCE requires the practitioner, during the audit, to evaluate whether ISA for LCE continues to be appropriate for the nature and circumstances of the entity being audited. If complex matters or circumstances are identified during the audit indicating that continuing to use the standard is not appropriate, the practitioner may need to revert to the CASs midway through the audit. If such circumstances arise frequently, they may deter practitioners from using the separate standard for LCE audits.

See [questions 2-7](#) about Option 1 in “[Comments requested](#)” in Section III.

## Option 2 – Limited targeted revisions to the CASs

18. Under Option 2, the AASB would choose not to adopt the ISA for LCE that may result from the IAASB’s project nor use the ISA for LCE as a basis for developing an equivalent Canadian standard. Therefore, there would be no separate standard for LCE audits in Canada.
19. Option 2 involves broadening the criteria set out in [Appendix II](#) to permit limited, targeted Canadian amendments to the ISAs when adopting them as CASs to support stakeholders’ need for more effective scalability and proportionality in the CASs. Any revisions the AASB makes to its Canadian amendment criteria will be within the constraints of its commitment to continue adopting the ISAs as CASs. The Board believes the global alignment of the ISAs is critical to maintaining stakeholder confidence as their needs evolve.
20. Limited, targeted Canadian amendments to support the need for scalability and proportionality may involve the following:
- (a) Where practitioners experience significant challenges in applying a particular requirement in a CAS to an entity’s less-complex elements, the CAS could be revised to deal with the particular challenges. Several such challenges have been identified in previous consultations with stakeholders, as set out in [Appendix I](#). The revision to the CASs may include additional application and other explanatory material focused on describing considerations specific to LCEs. For example, the recently revised [CAS 315](#) includes boxes, tables and other explanatory material to help practitioners apply specific requirements to LCE audits. Revisions to the CASs may be complemented by non-authoritative guidance material.
  - (b) Where ED-ISA for LCE includes material that supports stakeholders’ need for more effective scalability and proportionality in the CASs, a revision could be made to the corresponding CAS to incorporate such material.
21. The benefits and drawbacks of making limited, targeted revisions to the CASs are set out below.

### Benefits

- (a) Revising the CASs would be a practical solution to address the specific areas of the CASs that cause practitioners significant challenges when applying to LCE audits.
- (b) Revisions to the CASs are authoritative. Therefore, such revisions may be more effective than non-authoritative guidance in changing practice where needed.
- (c) The AASB will maintain the current approach where the CASs are principles-based and apply to audits of entities of all sizes and complexities. Therefore, Option 2 will avoid the possible drawbacks of a separate standard for LCE audits in Option 1.

### Drawbacks

- (a) The AASB will require time and effort to revisit its amendment criteria set out in [Appendix II](#) to determine what changes are needed to permit Canadian amendments to the ISAs to support more effective scalability and proportionality of the CASs.

- (b) If the number of Canadian amendments increases, maintaining close ties between the CASs and the ISAs may be difficult. As well, tracking the differences between the CASs and the ISAs may become cumbersome.
- (c) The revisions to the CASs will be limited, targeting specific areas where practitioners experience significant challenges in LCE audits. Therefore, Option 2 will not be a comprehensive solution to addressing the phases of an LCE audit.
- (d) Adding LCE considerations will lengthen the CASs. This may exacerbate the challenges some stakeholders raised about the CASs already being lengthy, overly detailed and challenging to navigate.
- (e) Existing CASs will be revised over time and may take longer than adopting the ISA for LCE that may result from IAASB's project. The ED-ISA for LCE presents a solution that the IAASB intends to finalize on an accelerated timeline. Therefore, the time to implement a solution for LCE audits may be longer under Option 2 compared to Option 1.
- (f) If the IAASB issues an ISA for LCE, future new or revised ISAs (and the CASs) may not deal comprehensively with matters impacting LCE audits. Therefore, the AASB will need to spend more time and effort addressing LCE considerations in the CASs and exposing them for public comment. As a result, issuing CASs may take more time and impact the AASB's 2022-2025 Strategic Goal of delivering timely standards.
- (g) The CASs' core requirements apply to LCE audits and are needed to obtain a reasonable assurance opinion. As a result, limited, targeted revisions may not substantially reduce the work effort to perform an LCE audit. Therefore, practitioners may not achieve significant efficiencies.

See [questions 8-10](#) about Option 2 in "[Comments requested](#)" in Section III.

### Option 3 – Targeted non-authoritative guidance

- 22. Under Option 3, the AASB would choose not to adopt the ISA for LCE that may result from the IAASB's project nor use the ISA for LCE as a basis for developing an equivalent Canadian standard. Therefore, there would be no separate standard for LCE audits in Canada. As well, the AASB would decide not to make limited, targeted revisions to the CASs to support the need for effective scalability and proportionality.
- 23. Option 3 involves developing (or supporting other groups, such as CPA Canada, in developing) targeted non-authoritative guidance, including tools, to assist practitioners in applying the CASs to LCE audits. Such non-authoritative guidance would not be part of the CASs and would not impose additional requirements on practitioners.
- 24. Options for guidance may include:
  - (a) **Implementation material for new or revised CASs focused on the LCEs.** This area may include tools, slide presentations, webinars or videos to educate and help practitioners implement new or revised CASs. For example, in June 2021, CPA Canada developed guidance, with input from the AASB's Audits of LCEs Advisory Group, to help practitioners understand the scalability of revised CAS 315 with a focus on LCEs. See [Implementation Tool for Auditors, "Risk Assessment Process: Tips on Implementing Revised CAS 315."](#)
  - (b) **Targeted guidance and tools focused on addressing the significant challenges in applying specific requirements in the CASs to the LCEs.** CPA Canada developed guidance like this, for example:
    - ["Audits of Not-for-Profit Organizations: Risk Assessment under Canadian Auditing Standards"](#) (2015); and
    - [Implementation Tool for Auditors, "Testing Journal Entries and Other Adjustments: Responding to the Risk of Management Override of Controls"](#) (2015).

25. The benefits and drawbacks of developing targeted non-authoritative guidance are set out below.

### Benefits

- (a) Non-authoritative guidance can be developed, issued and modified as necessary quicker than authoritative pronouncements because non-authoritative guidance does not have to follow the due process required for authoritative pronouncements.
- (b) Non-authoritative guidance can be more flexible as it can include practical examples and flowcharts and use plain language. Therefore, it may better support practitioners in applying the CASs to LCE audits.

### Drawbacks

- (a) Developing guidance will add more materials for practitioners to read and consider.
- (b) The non-authoritative guidance will target specific areas in the CASs where practitioners experience significant challenges in LCE audits. Therefore, Option 3 will not be a comprehensive solution to addressing the phases of an LCE audit.
- (c) Non-authoritative guidance may be less effective than authoritative pronouncements in changing practice where change is needed.
- (d) Non-authoritative guidance is not part of the CPA Canada Standards and Guidance Collection. Therefore, updating such guidance may be less of a priority when the CAS that it relates to is revised or practice evolves.

See [questions 11-12](#) about Option 3 in the “[Comments requested](#)” in Section III.

## SECTION III – COMMENTS REQUESTED

### Responding to the IAASB’s Exposure Draft

- 26. The IAASB’s Exposure Draft is available on the [IAASB website](#). In addition to the text of ED-ISA for LCE, the Exposure Draft includes the Explanatory Memorandum, providing background and explaining proposals.
- 27. Canadian stakeholders who comment on the IAASB’s Exposure Draft are asked to provide the AASB with a copy of their response. Alternatively, respondents may share their comments directly with the AASB on the [Connect.FRASCanada.ca project page](#) or by [submitting comments](#) via an online form. The AASB will take these comments into account when drafting its response to the IAASB’s Exposure Draft.
- 28. Comments are most helpful if they relate to a specific paragraph or group of paragraphs. Any statements expressing disagreement with the IAASB’s Exposure Draft proposals should clearly explain the problem and include a suggested alternative supported by specific reasoning. When a respondent agrees with proposals in the IAASB’s Exposure Draft, it will be helpful for the AASB to be made aware of this view. Respondents are free to address only questions relevant to them or all questions.
- 29. Respondents are asked not to include comments on matters particular to the Canadian environment in their responses to the IAASB. Such comments should be included only in responses sent to the AASB. Please refer to the “Guide for Respondents” in the IAASB’s Exposure Draft and respond to the specific questions.

## Providing comments to the AASB

30. The AASB would appreciate responses to the questions set out below, in addition to receiving a copy of the response to the IAASB's Exposure Draft, if a response is provided.
31. In responding to the IAASB's Exposure Draft questions and to the AASB's questions below, the AASB invites practitioners and firms of all sizes to field test the requirements in ED-ISA for LCE and to communicate the outcome in its response letter. Field testing may focus on all or certain phases of an audit or specific requirements in ED-ISA for LCE. Lessons learned from field testing will provide the Board with a better understanding of the proposals' practical implications.
32. The AASB seeks responses to the questions set out below.

### Public interest considerations

1. Do you agree with the concerns stakeholders raised in the AASB's previous consultations in [paragraph 8](#) and with the public interest consideration in [paragraph 9](#)? Are there other concerns or public interest considerations not identified in these paragraphs?

### Option 1 – Separate standard for LCE audits

2. The AASB is particularly interested in views on the questions below in the IAASB's [Explanatory Memorandum](#) about ED-ISA for LCE:
  - (a) Questions 3-6 relating to the Authority (or scope) of ED-ISA for LCE (Part A of the proposed standard).
  - (b) Question 7(d) relating to the approach to the EEM. Specifically, do you believe ED-ISA for LCE includes sufficient EEM to help an auditor perform a high-quality audit?
  - (c) Question 13 relating to transitioning between ED-ISA for LCE and the ISAs. Specifically:
    - (i) Do you agree with the view in paragraph 131 that it should be relatively rare for an audit of an entity to need to transition after engagement acceptance or continuance from using ED-ISA for LCE to using the ISAs?
    - (ii) Do you support the premise in paragraphs 26 and 133 that relevant ISA requirements cannot be used to "top-up" ED-ISA for LCE to address circumstances not contemplated in ED-ISA for LCE? For example, where ED-ISA for LCE does not contemplate an element of complexity that arises during the audit, the ISAs cannot be used.
    - (iii) Paragraph 139 sets out a list of matters the practitioner needs to consider if they determined that ED-ISA for LCE is no longer appropriate for use in an audit engagement. Is this list appropriate and complete?
3. Consider the Authority of the Standard in Part A of ED-ISA for LCE. If the proposed ISA for LCE was adopted in Canada:
  - (a) Will practitioners be able to use the proposed standard in the Canadian environment?
  - (b) In addition to the prohibitions already included in Part A of ED-ISA for LCE, are there specific types of entities or industries in Canada that you believe should be explicitly prohibited from using the proposed standard? Are there specific types of entities or industries in Canada that should be explicitly allowed to use the proposed standard?
  - (c) Are there specific thresholds or criteria you believe would be appropriate to establish in Canada for when the proposed standard may be used?
4. If the AASB were to adopt ED-ISA for LCE in Canada:
  - (a) Do you believe users' perception may change in terms of the level of assurance provided in an audit engagement performed using the proposed standard compared to the CASs?

- (b) How would performing an audit under the proposed standard differ, if at all, from performing an audit under the CASs? Do you anticipate specific efficiencies or benefits? Please explain why or why not.
  - (c) What implementation support do you believe would be required for the proposed standard (e.g., further guidance, training or tools) initially and on an ongoing basis?
5. Do you believe that a separate standard for LCE audits for use in Canada is an appropriate solution? Please explain why or why not.
  6. If you believe that a separate standard for LCE audits for use in Canada is an appropriate solution, do you support the adoption of ED-ISA for LCE? Please explain why or why not.
  7. If the AASB were to adopt ED-ISA for LCE in Canada, would you suggest any Canadian amendments? If so, what would they be?

### **Options 2 – Limited, targeted revisions to the CASs**

8. Do you believe that making limited, targeted revisions to the CASs is an appropriate solution? Please explain why or why not.
9. Do you believe that the requirements identified in the AASB's previous consultations, set out in [Appendix I](#), are significantly challenging to apply in LCE audits? Are other requirements in the CASs significantly challenging to apply in LCE audits that may need revisions? If so, what are they?
10. What limited, targeted revisions to the CASs, including incorporating elements from ED-ISA for LCE (e.g., EEM), would address the significant challenges you believe exist in applying the CASs to LCE audits?

### **Option 3 – Targeted non-authoritative guidance**

11. Do you believe that developing targeted non-authoritative guidance is an appropriate solution? Please explain why or why not.
12. If the AASB focused on developing targeted non-authoritative guidance, for which areas or specific requirements in the CASs would it be most helpful? What guidance should the Board prioritize, and why?

### **Other**

13. What other options or matters, if any, should the AASB consider as it deliberates the direction of its work in this area?
  14. If the most appropriate way forward is a combination of options, how should the AASB prioritize them?
33. We value your input and look forward to your feedback on this Discussion Paper. Comment on this document by taking part in the [Connect.FRASCanada.ca project](https://connect.frascanada.ca) or by [submitting a comment letter](#) addressed to:

Eric Turner, FCPA, FCA  
Director, Auditing and Assurance Standards  
Auditing and Assurance Standards Board  
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Toronto ON M5V 3H2

The deadline for providing your comments to the AASB on the above is December 10, 2021.

## APPENDIX I

### List of standards and their requirements identified in previous consultations with Canadian stakeholders as challenging to apply in LCE audits

#### **CAS 315, *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and its Environment***

The paragraphs refer to CAS 315 in the Archived Pronouncements.

**Preliminary analytical review – CAS 315.6(b):** This paragraph requires the auditor to perform analytical procedures as a risk assessment procedure. Stakeholders indicated such a procedure is often ineffective for an audit where the entity's financial information requires year-end adjustments (e.g., cut-off adjustments, amortization, etc.) to comply with the applicable financial reporting framework. Although stakeholders acknowledged that the guidance in CAS 315.A17 provides considerations specific to smaller entities, they thought it does not allow enough flexibility for the auditor to decide not to perform the procedure or combine the procedure with final analytical procedures.

**Risk assessment procedures – CAS 315.13:** This paragraph requires the auditor to perform procedures in addition to inquiry to understand controls relevant to the audit. Stakeholders thought inquiry alone should be sufficient to obtain this understanding when taking a fully substantive audit approach.

**Understanding internal controls – CAS 315.14-19 and CAS 315.22-24:** These paragraphs require the auditor to understand the components of internal control. Stakeholders thought the understanding required in this section is too granular and does not reflect a less-complex environment. Such an environment is typically less formal and focuses more on monitoring and oversight controls than on process controls. Further, stakeholders thought this section seems onerous in circumstances where a fully substantive approach is taken.

**Responding to risks arising from information technology (IT) – CAS 315.18 and CAS 315.21:** These paragraphs require the auditor to understand the information system and related controls relevant to financial reporting. Stakeholders thought the standard is unclear as to the extent of work required when the auditor decides specific controls over IT applications will be irrelevant to the audit. For example, IT risks for an entity using "off-the-shelf" commercial accounting packages that the entity cannot change should present a low risk to financial reporting. Still, practitioners struggle to understand what evidence is needed to support this judgment.

#### **CAS 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements***

**Identification and response to fraud risk – CAS 240.27:** This paragraph presumes there is always a risk of material misstatement due to fraud related to revenue recognition. Stakeholders indicated this requirement is challenging to apply to audits of entities with a single revenue source (e.g., government grants) that is not susceptible to fraudulent financial reporting. Although rebuttal of the presumed risk of fraud is permitted, the work effort to support and document the rebuttal is not well understood and believed by some to be a high hurdle to overcome.

**Incorporate an element of unpredictability in the selection of procedures – CAS 240.30(c):** This paragraph requires the auditor to incorporate an element of unpredictability in the design and selection of the nature, timing and extent of audit procedures. Stakeholders indicated this can be challenging when taking a fully substantive audit approach, where many (if not all) transactions and balances are examined. In such circumstances, it can be difficult to determine what may be an effective unpredictability procedure.

**Journal entry testing – CAS 240.33(a):** This paragraph requires the auditor to design and perform procedures to test the appropriateness of journal entries throughout the period and at the end of the period. Stakeholders indicated this requirement is not well understood when a fully substantive audit approach is taken. For example, when many of the entity’s journal entries have already been tested in a substantive audit approach, it is unclear how much additional testing is required.

### **CAS 260, *Communication with Those Charged with Governance***

**Frequency and substance of communications – CAS 260.14-16:** These paragraphs list matters the practitioner is required to communicate with those charged with governance. Stakeholders indicated they are sometimes challenged in complying with the requirements to communicate specific matters throughout the audit in less-formal oversight structures, where a board of directors does not exist or meets infrequently.

### **CAS 230, *Audit Documentation***

**Documentation:** This CAS lacks clarity on what needs to be documented when specific audit procedures have not been done because they are ineffective or do not apply. Practitioners indicated they spend unnecessary time and effort documenting what they have not done and why this was an appropriate course of action. They do so to avoid being challenged by practice reviewers about applying professional judgment when determining that a requirement is ineffective or does not apply. A lack of clarity about scalability in the standards may be causing inappropriate interpretations. [CAS 200.22\(b\)](#)<sup>3</sup> states “the auditor shall comply with each requirement of a CAS unless, in the circumstances of the audit the requirement is not relevant because it is conditional, and the condition does not exist.” It is unclear how to interpret this requirement. Is conditionality a matter of professional judgment (i.e., the practitioner determines the procedure would be ineffective and, therefore, the requirement is not relevant), or is conditionality required to be explicitly defined in the requirement (as in [CAS 220.21](#) where the requirement is conditional for listed entities)?

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3 CAS 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Canadian Auditing Standards*

## APPENDIX II

### Criteria for amending ISAs when adopting them as CASs

With respect to adopting ISAs, the AASB's overriding goal is to adopt ISAs into the CPA Canada Handbook – Assurance without amendment. However, there may be circumstances when amendments are required. The following sets out the limited circumstances when the Board will amend ISAs.

1. The AASB will limit additions to an ISA to those required to comply with Canadian legal and regulatory requirements.<sup>4</sup>
2. The AASB will limit deletions from, or other amendments to, an ISA to the following:
  - (a) The elimination of options (alternatives) provided for in the ISA.
  - (b) Requirements or guidance, the application of which Canadian law or regulation<sup>4</sup> does not permit, or which require amendments to be consistent with law or regulation.
  - (c) Requirements or guidance, where the ISA recognizes that different practices may apply in different jurisdictions and Canada is such a jurisdiction.
3. The AASB may amend an ISA with respect to requirements or guidance that do not fall within 1 or 2 above when it believes there are circumstances particular to the Canadian environment where such amendments are required to serve the Canadian public interest and maintain the quality of auditing and reporting in Canada.
4. To the extent possible, amendments that are:
  - (a) Additions to an ISA will not be inconsistent with the current requirements or guidance in the ISA; and
  - (b) Deletions from, or other amendments to, an ISA will be replaced by an appropriate alternative that achieves the objective of the deleted requirement.

Proposed amendments to an ISA will be highlighted in exposure drafts of proposed Canadian standards. The AASB will indicate the reasoning for the amendments and stakeholders will be invited to comment on them, including when the amendment will not result in convergence with the ISA in accordance with the IAASB's guide for national standard setters. Amendments to ISAs will be separately identified in the final Assurance Handbook material.

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4 Canadian incorporating and other governing legislation often require entities to prepare financial statements in accordance with Canadian generally accepted accounting principles (GAAP). Accordingly, if Canadian GAAP necessitates a different audit response in Canada, these differences fall within the definition of a legal or regulatory requirement.

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