KPMG

CURRENT DEVELOPMENTS

Canadian Securities & Auditing Matters

Q1 2021

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This edition provides a summary of newly effective and forthcoming regulatory and auditing matters in Canada in the quarter ended March 31, 2021.

Canadian securities: New guidance

Confidential filing

In January 2021, the Ontario Securities Commission (OSC) issued best practices when filing a confidential pre-file prospectus. To streamline the review process issuers were reminded that:

- Pre-filed prospectuses should contain all financial and non-financial disclosure that would be included in the actual prospectus filing, and missing disclosure can result in review timelines being extended.
- A deal timeline should be included in the filed cover letter to assist staff in understanding when the review should ideally be completed. The OSC expects that the issuer will file a preliminary prospectus shortly after the completion of the review of the pre-filed prospectus.
- Any legal or accounting questions where OSC staff input is required should be highlighted.

Audit firms were reminded that the financial statements included in a draft prospectus must, as prescribed for preliminary prospectuses under securities legislation, be audited (or be accompanied by an Auditor's Comfort Letter regarding Audited Financial Statements) or reviewed, as applicable.

The OSC stated that staff will not review pre-files of non-offering prospectuses, other than non-offering prospectuses pre-filed in connection with cross-border financings or where there is a specific legal or accounting matter requiring staff input. Pre-files of prospectuses that solely qualify the issuance of securities on conversion of convertible securities, such as special warrants, will also not be reviewed.

COVID-19 disclosures

In February 2021, the Canadian Securities Administrators (CSA) published Staff Notice (SN) 51-362 *Staff Review of COVID-19 Disclosures and Guide for Disclosure Improvements*. The SN summarizes the results of an issuer-oriented review to assess issuers' disclosures of the current and anticipated impacts of COVID-19. Staff reminded that meaningful disclosures about the business impacts and potential uncertainties regarding COVID-19 are needed for investors to make informed investment decisions. The notice summarizes key review findings and includes some disclosure examples.

Key observations related to MD&A included:

- **Discussion of measures taken to reduce impact.** Many issuers provided "lists" of measures employed to manage operational and liquidity risks, but did not provide adequate discussion to address the anticipated impact to the issuer.
- **Analysis of overall performance and operations.** Most issuers that quantitatively disclosed variances related to COVID-19 (e.g. impact to sales) did not explain the methodology used in determining fluctuations that were isolated to COVID-19. Several issuers provided limited disclosure of known trends or events related to COVID-19 that are likely to affect future performance.
- **Liquidity and capital resources.** Many issuers with material liquidity risks did not disclose in detail their ability to meet working capital requirements, planned growth initiatives or to fund developmental activities and capital expenditures. There was a lack of disclosure regarding trends or expected fluctuations in liquidity that took into account events or uncertainties related to COVID-19.
- **Risk factor disclosure.** Several issuers provided "lists" of risks without discussion or general disclosures that touched on general economic or societal impacts of COVID-19 and did not describe entity-specific COVID-19-related risks.

Key observations related to financial statement disclosures included:

- **General.** Some issuers failed to adequately update their disclosures and assumptions impacted by COVID-19 in the context of testing impairments of goodwill and intangible assets, measuring fair value and estimating expected credit losses.
- **Significant judgements and measurement uncertainties.** Some issuers failed to include entity-specific disclosure for significant judgements or measurement uncertainties or only included this disclosure in their MD&A but not in their financial statements.

- **Impairment of non-financial assets**. A few issuers did not identify reasons for impairments or just noted "negative economic impacts of COVID-19" as an impairment indicator for all cash generating units but did not elaborate on those impacts.
- **Going concern**. Some issuers breached financial covenants during the reporting period but did not disclose the implications of breaches on the issuer's ability to continue as a going concern. Some issuers disclosed "close call" situations but did not disclose the mitigating actions that impacted their determination that there were no material uncertainties that cast significant doubt on the issuer's ability to continue as a going concern (e.g. successful negotiation of credit facilities subsequent to period end).
- **Government assistance.** Over half of the issuers reviewed recognized, or disclosed in subsequent events, COVID-19 related government assistance. Some issuers did not disclose the nature and extent of the government assistance or the accounting policy adopted including the methods of presentation.
- **Expected credit losses (ECL).** Only a few issuers disclosed the use of COVID-19-induced overlays to their ECL models.
- **Financial Instrument Risk Disclosure.** Some issuers that experienced material adverse impacts of COVID-19 did not provide an entity-specific update to their risk disclosure.
- **COVID-19 related amendments to IFRS 16 *Leases* for Lessees.** Some issuers did not disclose whether they applied the practical expedient to either all or some of their rent concessions.

Other areas where observations were provided included non-GAAP financial measures, forward looking information, material change reporting and promotional disclosures.

Crypto assets reporting issuers

In March 2021, the CSA published CSA Notice 51-363 *Observations on Disclosure by Crypto Assets Reporting Issuers.* Crypto assets reporting issuers includes reporting issuers dealing in digital assets, such as cryptocurrencies, tokens, stablecoins, and similar digital assets relying on blockchain technology. The notice outlines several disclosure observations based on the annual filings by reporting issuers (other than investment funds) that engage materially with crypto assets.

Concerns regarding an issuer's financial condition and the sufficiency of proceeds from a prospectus offering

In March 2021, the CSA published revised CSA SN 41-307 *Concerns Regarding an Issuer's Financial Condition and the Sufficiency of Proceeds from a Prospectus Offering.*

Securities legislation provides that the authorized decision maker must issue a receipt for a prospectus unless it appears to the decision maker that it is not in the public interest to do so or for motives enumerated in securities legislation. An issuer may face potential receipt refusal where:

- It appears that the prospectus inadequately discloses an issuer's financial condition and going concern risk; or
- There is adequate disclosure about the issuer's financial condition, but it appears that either (i) the sufficiency of proceeds from the prospectus offering, along with the issuer's other resources, will be insufficient to accomplish the purpose of the issue stated in the prospectus or (ii) it is not in the public interest to issue receipt.

When conducting prospectus reviews, staff may consider the anticipated proceeds from a prospectus offering to be insufficient if they are raised:

- for a specific purpose but do not address the issuer's short-term liquidity requirements;
- through a best efforts offering without a minimum subscription, or a minimum subscription that does not appear to be sufficient to satisfy the issuer's short-term liquidity requirements; or
- through a shelf prospectus offering that can be drawn down in small increments that, when considered separately, may not be sufficient to satisfy the issuer's short-term liquidity requirements.

When considering short-term liquidity requirements, staff considers the circumstances of the issuer, in particular:

Type of Issuer	Consideration
Exploration stage issuer	Sufficient resources to meet completion stage of next phase of a project
Development stage issuer	Sufficient resources to achieve the issuer's next significant milestone
Research & development stage issuer	Sufficient resources to achieve progress on the development of a key product
Issuer with active operations	Ability to continue for the short-term, generally at least 12 months

The SN highlights 5 areas of focus that may raise comments:

- missing information regarding offering amount and pricing;
- offering structure;
- use of proceeds disclosure;
- risk factor disclosure; and
- representations to support ability to continue operations.

Auditing matters

Audits of less complex entities

In February, the Auditing and Assurance Standards Board (AASB) discussed the Audits of Less Complex Entities (LCE) Advisory Group's recent work. During the AASB's previous activities, stakeholders identified several matters in archived Canadian Auditing Standard (CAS) 315 *Identifying and Assessing the Risks of Material Misstatement Through Understanding the Entity and Its Environment* that were challenging to apply in audits of LCEs.

At its March meetings, the AASB provided input to the IAASB members from Canada on the International Audit and Assurance Standard Board's (IAASB) project to develop a separate standard for audits of LCEs.

Key issues discussed included:

- the conventions used in drafting the separate standard;
- the proposed description of the characteristics of an LCE to consider when deciding when to apply the separate standard;
- the proposed approach to maintain alignment of the separate standard with the International Standards on Auditing (ISAs); and
- the additional matters that the project should explore, including how to transition from the separate standard to the ISAs when an entity no longer qualifies as an LCE.

The AASB also discussed how to proceed in Canada in relation to the IAASB's issuance of an exposure draft of a separate standard for audits of LCEs.

The AASB will continue its discussion on the way forward in Canada at its May meeting.

Fraud and going concern

The AASB reviewed a draft response letter to the IASB's discussion paper *Fraud and Going Concern in an Audit of Financial Statements: Exploring the Differences Between Public Perceptions About the Role of the Auditor and the Auditor's Responsibilities in a Financial Statement Audit*.

Future-oriented financial information

The AASB discussed elements of a possible project proposal to revise or replace Assurance and Related Services Guideline (AuG) 16 *Compilation of a Financial Forecast or Projection*, including the benefits of establishing a task force and a reference group to supplement the activities of a task force.

The AASB plans to review a proposal for AuG-16 at a future date.

Quality management for firms

In January, the AASB unanimously approved:

- Canadian Standard on Quality Management (CSQM) 1 *Quality Managements for Firms that Perform Audits or Reviews of Financial Statements, or Other Assurance or Related Services Engagements* (CSQM 1);
- CSQM 2 *Engagement Quality Reviews*;
- CAS 220 *Quality Management for an Audit of Financial Statements*; and
- related conforming amendments to other CASs.

CSQM 1 is effective as follows:

- Firms are required to design and implement their system of quality management for audits or reviews of financial statements or other assurance engagements by December 15, 2022. They are required to evaluate their system within one year following this date.
- Firms are required to design and implement their system of quality management for related services engagements by December 15, 2023. They are required to evaluate their system within one year following this date.

CSQM 2 is effective for:

- audits and reviews of financial statements and other assurance engagements for periods beginning on or after December 15, 2022; and
- related services engagements beginning on or after December 15, 2023.

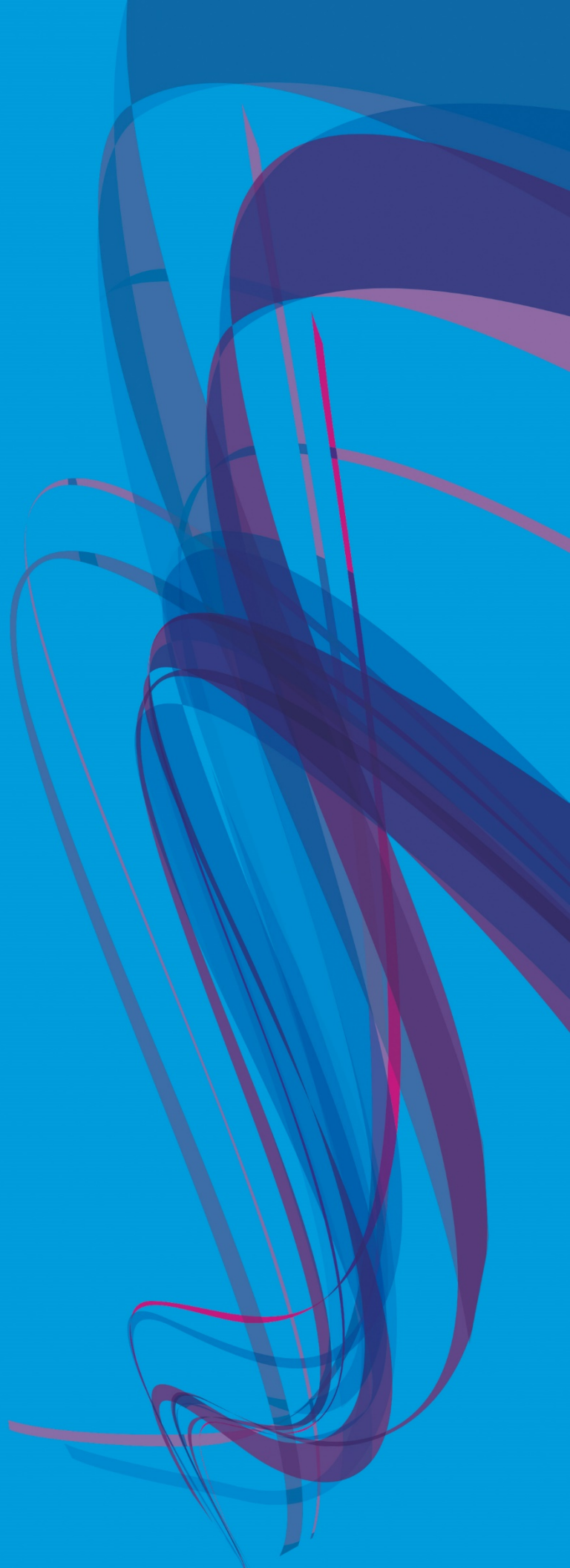
CAS 220 is effective for audits of financial statements for periods beginning on or after December 15, 2022.

In March, the AASB discussed matters related to its proposed exposure draft addressing conforming amendments to other Canadian standards, resulting from the January 2021 approval of CSQM 1.

The AASB expects to review an exposure draft at its April meeting.

Audit standards issued but not yet effective

Standard	Effective for years ending December 15,		
	2022	2023	Beyond
CAS 315 (Revised) *Identifying and Assessing the Risks of Material Misstatement*	✓		
CAS 700 *Forming an Opinion and Reporting on Financial Statements*; paragraphs C30 and C40C(c)	✓		
CAS 220 *Quality Management for an Audit of Financial Statements*		✓	
ISA 600 *Special Considerations – Audits of Group Financial Statements (Including the Work of Component Auditors)*			✓



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