
Lessons Learned from Firms Implementing KAM Communications on Audits of TSX-Listed Entities

Identifying and Communicating KAMs
in the Auditor's Report

April 2021

This non-authoritative guidance has been prepared by staff of the Auditing and Assurance Standards Board (AASB). It does not form part of the CPA Canada Handbook – Assurance. Auditors are expected to use professional judgment in determining whether to apply the material in this guidance in the circumstances of their audit engagements.

Introduction

Communicating KAMs in the auditor's report is the biggest change to the auditor's report that the profession has seen in the last ten years. While KAM requirements have been in effect in jurisdictions around the world for about four years, it is a relatively new requirement for Canadian auditors and the last phase of the enhanced auditor reporting project.

Canadian accounting firms have been developing a KAM-implementation process and performing "practice runs" as they prepared to communicate KAMs in the auditor's report of entities listed on the Toronto Stock Exchange (TSX).

Firms that performed practice runs said it was a beneficial experience. They gathered initial feedback on their processes, including firm tools and guidance that has been developed to support implementing KAM communications. Firms indicated that management and the audit committee also benefited from the practice runs, helping them understand what to expect once the requirements become effective.

Staff of the AASB interviewed firm representatives from the department of professional practice, or the equivalent, to understand:

- the challenges faced during the practice runs;
- what went well when implementing the established processes; and
- what firms will do differently in the live setting.

The feedback was consistent from all firms: identifying and communicating KAMs is not easy!

Staff of the AASB leveraged the input received to create this guidance, which is broken down into two sections.

Section 1: Identifying KAMs

When identifying KAMs, the auditor starts with all matters communicated with those charged with governance. The auditor then exercises professional judgment to determine which matters were of most significance in the audit of the current period financial statements.

Figure 1 shows how to identify a KAM through a filtering process.

Section 2: Describing KAMs

The auditor exercises professional judgment to describe a KAM. The description of a KAM provides a succinct and balanced explanation that allows intended users of the financial statements to understand why the matter was one of most significance in the audit of the current period and how the matter was addressed in the audit.

The auditor seeks the right balance between providing too much information (which may confuse users) and too little information (which may affect users' understanding) when describing the KAM. This section outlines:

- requirements in the auditing standard for describing each KAM;
- related application material; and
- considerations for how to meet the requirements, based on the firms' practice runs

Overview

Canadian Auditing Standard (CAS) 701, *Communicating Key Audit Matters in the Independent Auditor's Report*, addresses the auditor's responsibility to communicate KAMs in the auditor's report.

This CAS applies to audits of complete sets of listed entities' general-purpose financial statements. It excludes listed entities required to comply with National Instrument (NI) 81-106, *Investment Fund Continuous Disclosure*.

This CAS also applies when the auditor decides to communicate KAMs in the auditor's report or when the auditor is required by law or regulation to communicate KAMs in the auditor's report.

Effective Date

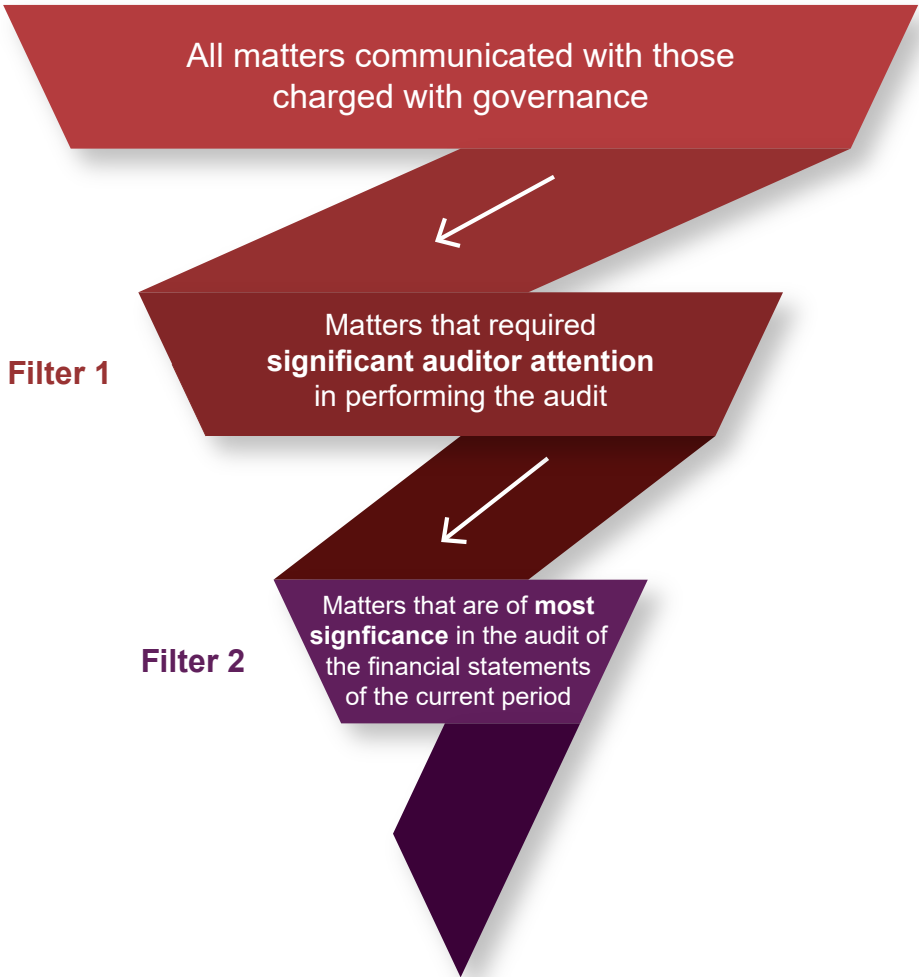
CAS 701 is effective for audits of financial statements of:

- TSX-listed entities, excluding listed entities required to comply with NI 81-106, for periods ending on or after December 15, 2020.
- Other listed entities,¹ excluding listed entities required to comply with NI 81-106, for periods ending on or after December 15, 2022.
- All entities for periods ending on or after December 15, 2018, when:
 - the auditor decides to communicate KAMs in the auditor's report; or
 - the auditor is required by law or regulation to communicate KAMs in the auditor's report.

¹ The CPA Canada Handbook – Assurance, Glossary of Terms, defines a "listed entity" as "an entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body." Other listed entities include all entities listed on exchanges other than the TSX (i.e., TSX Venture Exchange, Canadian Securities Exchange, Aequis NEO Exchange).

Section 1 – Identifying KAMS

Figure 1



Matters communicated with those charged with governance

Paragraphs 14-C17 of CAS 260, *Communication with Those Charged with Governance*, list matters the auditor is required to communicate with those charged with governance. Appendix 1 of CAS 260 identifies paragraphs in Canadian Standard on Quality Control (CSQC) 1, *Quality Control for Firms that Perform Audits or Reviews of Financial Statements, and Other Assurance Engagements*,² and other CASs that require the communication of specific matters with those charged with governance.

In addition to the required communications with those charged with governance, the auditor needs to identify any other matters communicated to determine the **entire population** of matters communicated with those charged with governance.

Filter 1: Matters that required significant auditor attention in performing the audit

To determine “significant auditor attention,” the auditor is required to consider the following items.

Areas of higher assessed risk of material misstatement

Paragraph 9 of CAS 701 requires the auditor, when identifying matters that required significant auditor attention, to consider the areas of higher assessed risk of material misstatement (which include significant risks). The higher the risk of material misstatement, the more persuasive the audit evidence needs to be. Therefore, more auditor attention is placed in areas of higher assessed risks of material misstatement. Paragraph 12(l) of CAS 315, *Identifying and Assessing Risks of Material Misstatement*, defines significant risk.

² The AASB approved 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* in January 2021. 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 be evaluated within one year following this date. They are required to evaluate their system within one year following this date.

Areas of significant risk of material misstatement

[Paragraphs A218-A220](#) of CAS 315 provide guidance for the auditor in determining significant risks. The determination of which of the assessed risks of material misstatement are close to the upper end of the spectrum of inherent risk, and are therefore significant risks, is a matter of professional judgment, unless the risk is of a type specified to be treated as a significant risk in accordance with another CAS. For example, [paragraphs 26-28](#) of CAS 240, *The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements*, provide requirements and guidance for identifying and assessing the risk of material misstatement due to fraud.

Significant auditor judgments relating to areas in the financial statements that involve significant management judgment

[Paragraph 9](#) of CAS 701 requires the auditor, when identifying those matters that required significant auditor attention, to consider the significant auditor judgments related to areas in the financial statements that involved significant management judgment. Certain accounting estimates subject to a high degree of estimation uncertainty may not be determined to be significant risks. Such estimates depend highly on management judgment and are often the most complex areas of the financial statements.

The effect on the audit of significant events or transactions that occurred during the period

[Paragraph 9](#) of CAS 701 requires the auditor, when identifying those matters that required significant auditor attention, to consider significant events and transactions.

Events or transactions that had a significant effect on the audit may be areas of significant auditor attention and may be identified as significant risks. Management may have made difficult or complex judgments related to recognition, measurement, presentation or disclosure of these events or transactions. For example, the auditor may have had extensive discussions with management and those charged with governance at various stages throughout the audit about the effect on the financial statements of significant transactions with related parties or significant transactions that are outside the normal course of business for the entity.

Significant economic, accounting, regulatory, industry or other developments that affected management's assumptions or judgments may also affect the auditor's overall approach to the audit and result in a matter requiring significant auditor attention.

Filter 2: Matters that are of most significance in the audit of the financial statements of the current period

Determine matters of most significance in the audit of the current period

After the auditor has identified those matters that required significant auditor attention, [paragraph 10](#) of CAS 701 requires the auditor to determine which of those matters were **of most significance in the audit** of the financial statements of the current period and, therefore, KAMs.

In assessing the relative significance of a matter communicated with those charged with governance, and whether the matter is a KAM, the auditor may consider the following:

- The nature and extent of communication about such matters with those charged with governance. If the auditor has robust, frequent and in-depth discussions with those charged with governance on a particular matter (e.g., a significant business combination), it is most likely a matter of most significance in the audit of the current period.
- The nature of the underlying accounting policy relating to the matter or the complexity or subjectivity involved in management's selection of an appropriate policy compared to other entities within its industry.
- The importance of the matter to intended users' understanding of the financial statements as a whole, in particular, its materiality to the financial statements.
- The nature and materiality, quantitatively or qualitatively, of corrected and accumulated uncorrected misstatements due to fraud or error related to the matter.
- The nature and extent of audit effort needed to address the matter, including:
 - The extent of specialized skills or knowledge needed to apply audit procedures to address the matter or evaluate the results of those procedures, if any.
 - The nature of consultations outside the engagement team regarding the matter.
- The nature and severity of difficulties in applying audit procedures, evaluating the results of those procedures, and obtaining relevant and reliable evidence on which to base the auditor's opinion, in particular, as the auditor's judgments become more subjective.
- The severity of any control deficiencies identified relevant to the matter.

- Whether the matter involved several separate, but related, auditing considerations. For example, long-term contracts may involve significant auditor attention with respect to revenue recognition, litigation or other contingencies, and may also affect other accounting estimates, for example, forecasted future cash flows used in impairment assessments.

Section 2 – Describing KAMs

| Requirement in CAS 701 | Application Material in CAS 701 | Consider These Lessons Learned from KAM Practice Runs |
|---|---|--|
| <p>N/A – Overall description of a KAM</p> | <ul style="list-style-type: none"> The auditor exercises professional judgment when describing a KAM. It is a succinct and balanced explanation that allows the intended users to understand why the matter was one of most significance in the audit of the financial statements of the current period and how the matter was addressed in the audit. | <ul style="list-style-type: none"> Include subheadings like: <ul style="list-style-type: none"> “Description of the Key Audit Matter”; “Why the Matter Is a Key Audit Matter”; and “How the Key Audit Matter Was Addressed in the Audit.” <p>Subheadings may help the auditor meet the requirements and may make the KAM clearer for the intended users.</p> Focus on the intended users. Use plain English and avoid auditor jargon. Make the KAM as entity-specific as possible. Relate it to the facts and circumstances of the audit of the financial statements of the current period. This may include tailoring the KAM to the entity by using product and subsidiary names, or unique entity factors in the description. Consider whether such detail is original information³ or has been used in another document. For example, if the KAM relates to a specific subsidiary’s goodwill impairment, use the name or other identifier in the description, provided the information is also in the financial statements or another public document, like the management discussion and analysis. |

³ Paragraph A35 of CAS 701: “Original information is any information about the entity that has not otherwise been made publicly available by the entity (e.g., has not been included in the financial statements or other information available at the date of the auditor’s report, or addressed in other oral or written communications by management or those charged with governance, such as a preliminary announcement of financial information or investor briefings). Such information is the responsibility of the entity’s management and those charged with governance.”

| Requirement in CAS 701 | Application Material in CAS 701 | Consider These Lessons Learned from KAM Practice Runs |
|---|---|---|
| <p>Paragraph 13 – Reference to the related disclosures, if any, in the financial statements</p> | <ul style="list-style-type: none"> • A reference to related disclosures helps the intended users better understand how management has addressed the matter in preparing the financial statements. • Management or those charged with governance may decide to include new or enhanced disclosures in the financial statements or in other documents, because the matter will be communicated in the auditor’s report as a KAM. Examples of such disclosures could be providing more robust information about the sensitivity of key assumptions used in accounting estimates or the entity’s rationale for a particular accounting practice or policy, when acceptable alternatives exist under the applicable financial reporting framework. | <ul style="list-style-type: none"> • Keep the titles of the KAM and the note disclosure consistent to help understanding and to cross-reference to the financial statement note. • Select parts of the note disclosure that are relevant to the KAM, so the description is tailored and focused. The auditor should not simply reiterate what is already disclosed in the financial statements. |

| Requirement in CAS 701 | Application Material in CAS 701 | Consider These Lessons Learned from KAM Practice Runs |
|--|---|---|
| <p><u>Paragraph 13(a)</u> – Why the matter was considered to be one of most significance in the audit of the current period and therefore determined to be a KAM</p> | <ul style="list-style-type: none"> • The KAM explains why the matter is considered one of most significance in the audit of the current period. The auditor may include factors that explain why the matter required significant auditor attention and was of most significance in the audit of the current period. • These factors may include: <ul style="list-style-type: none"> ○ economic conditions that affected the auditor's ability to obtain audit evidence, like illiquid markets for certain financial instruments; ○ new or emerging accounting policies, like entity- or industry-specific matters on which the engagement team consulted others within the audit firm; and ○ changes in the entity's strategy or business model that had a material effect on the financial statements. | <ul style="list-style-type: none"> • Insert the subheading “Why the Matter Is a Key Audit Matter.” • Identify the reason by referencing the three areas for identifying potential KAMs set out in <u>paragraphs 9</u> and <u>A9-A26</u> of CAS 701, and <u>Filter 1</u> on page 7. • Describe the most important factors in determining that the matters were of most significance in the audit of the current period set out in <u>paragraphs A27-A30</u> of CAS 701 and <u>Filter 2</u> on page 9. |

| Requirement in CAS 701 | Application Material in CAS 701 | Consider These Lessons Learned from KAM Practice Runs |
|---|---|--|
| <p><u>Paragraph 13(b)</u> – How the matter was addressed in the audit</p> | <ul style="list-style-type: none"> • Deciding on the detail included in the auditor’s report to describe how a KAM was addressed in the audit requires professional judgment. • The auditor may describe: <ul style="list-style-type: none"> ○ aspects of the auditor’s response or approach that were most relevant to the matter or specific to the assessed risk of material misstatement; ○ a brief overview of procedures performed; ○ an indication of the outcome of the auditor’s procedures; and ○ key observations with respect to the matter. • Avoid using auditing jargon to help intended users understand the basis for the auditor’s focus on particular matters during the audit. • Exercise care so that the language used in the description: <ul style="list-style-type: none"> ○ Does not imply that the matter has not been appropriately resolved by the auditor in forming the opinion on the financial statements. ○ Relates the matter directly to the entity’s specific circumstances and avoids generic or standardized language. ○ Considers how the matter is addressed in the related disclosure(s) in the financial statements, if any. ○ Does not contain or imply discrete opinions on separate elements of the financial statements. | <ul style="list-style-type: none"> • Insert the subheading “How the Key Audit Matter Was Addressed in the Audit.” • The amount of detail included in the KAM depends on the circumstances of the entity and the complexity of the audit procedures. When describing audit procedures, consider the following: <ul style="list-style-type: none"> ○ Avoid writing a “laundry list” of audit procedures performed. Focus on the primary procedures and those directed at evaluating management’s key assumptions, judgments or inputs. Include a lead-in sentence that indicates the procedures described are the primary but not all procedures performed to address the KAM. ○ Avoid using auditor jargon. For example, “cut-off testing”, “dual purpose testing”, “write-off”, “turnover, completeness”, “existence, classification and/or ownership and rights” may not be well understood by the intended user. ○ Describe the audit procedures performed in a logical manner to make the KAM clearer. For example, describe tests of controls first, followed by substantive procedures. ○ Describe the aspects of the audit procedures specific to the risk of material misstatement. For example, when assessing the appropriateness of the key assumptions used in management’s impairment analysis, it may not be enough to simply indicate the auditor assessed the appropriateness of the discount rate used. Consider including more detail to explain how the rate was tested. For example, include how the discount rate was compared to a discount rate independently developed using public data. ○ If an expert was involved in performing audit procedures relating to the KAM, consider including this detail in the KAM itself. |

Other Resources

The resources listed below provide further guidance on KAMs:

1. Australian Auditing and Assurance Standards Board. [Auditor Reporting FAQs, Australian AUASB website.](#)
2. CPA Canada. "Key Audit Matters." Chap. 13 in [Reporting Implications of the Canadian Auditing Standards](#), 4th edn. 2019.
3. International Auditing and Assurance Standard Board. [Auditor Reporting – Key Audit Matters](#). January 30, 2015.
4. New Zealand External Reporting Board and Financial Markets Authority. [Enhanced auditor reporting: A review of the third year of the revised auditor's report](#). May 2020.

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Lessons Learned from Firms Implementing KAM Communications on Audits of TSX-Listed Entities

Roadmap to Developing a Successful
KAM-Implementation Process

April 2021

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Introduction

Communicating key audit matters (KAMs) in the auditor's report is the biggest change to the auditor's report the profession has seen in the last ten years. While KAM requirements have been in effect in jurisdictions around the world for about four years, it is a relatively new requirement for Canadian auditors and the last component in the enhanced auditor reporting project.

Canadian accounting firms have been developing a KAM-implementation process and performing KAM "practice runs" as they prepared to communicate KAMs in the auditor's report of entities listed on the Toronto Stock Exchange (TSX).

Firms that performed practice runs said it was a beneficial experience. They gathered initial feedback on their established processes, including firm tools and guidance developed to support implementing KAM communications. Firms indicated that management and the audit committee also benefited from the practice runs, which helped them understand what to expect once the requirements are in effect.

Staff of the AASB interviewed firm representatives from the department of professional practice, or the equivalent, to understand:

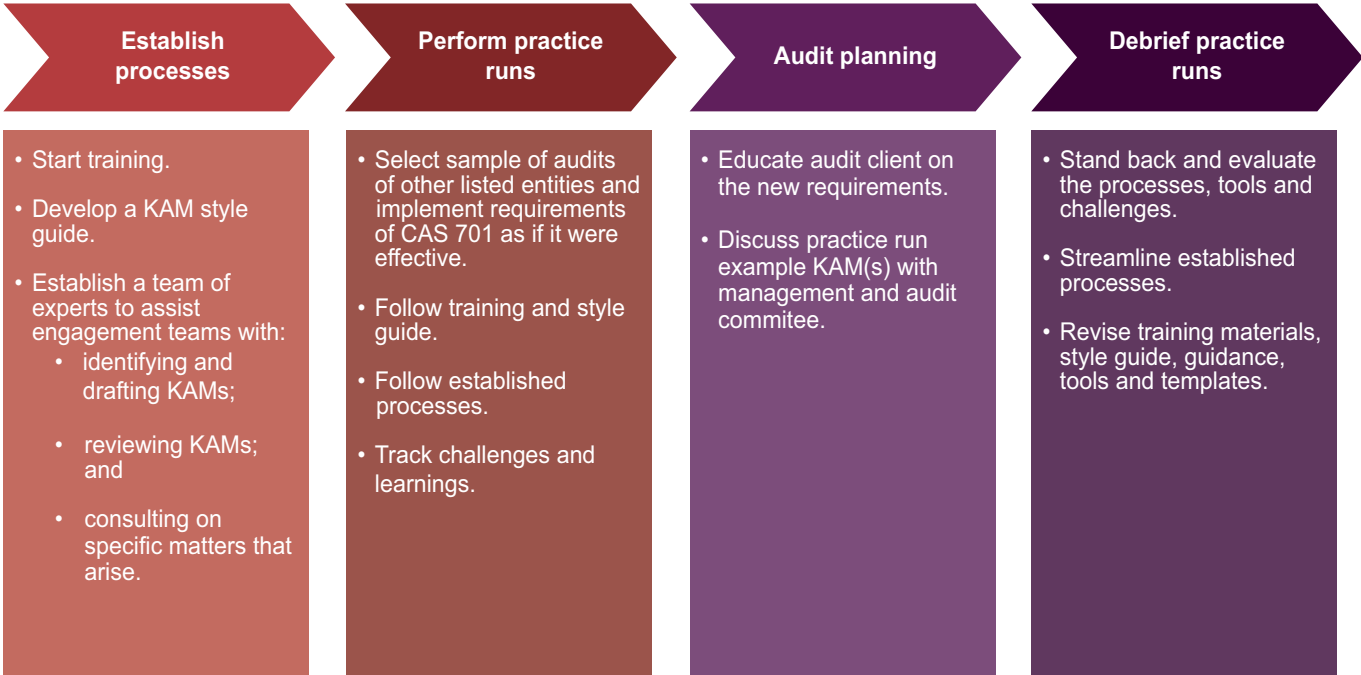
- the challenges faced during the practice runs;
- what went well when implementing the established processes; and
- what firms will do differently in the live setting.

Based on these interviews, staff created a general timeline for a firm to consider in communicating KAMs in the auditor's report. This timeline is designed for those performing audits of other listed entities¹, who will be communicating KAMs for audits of financial statements for periods ending on or after December 15, 2022.

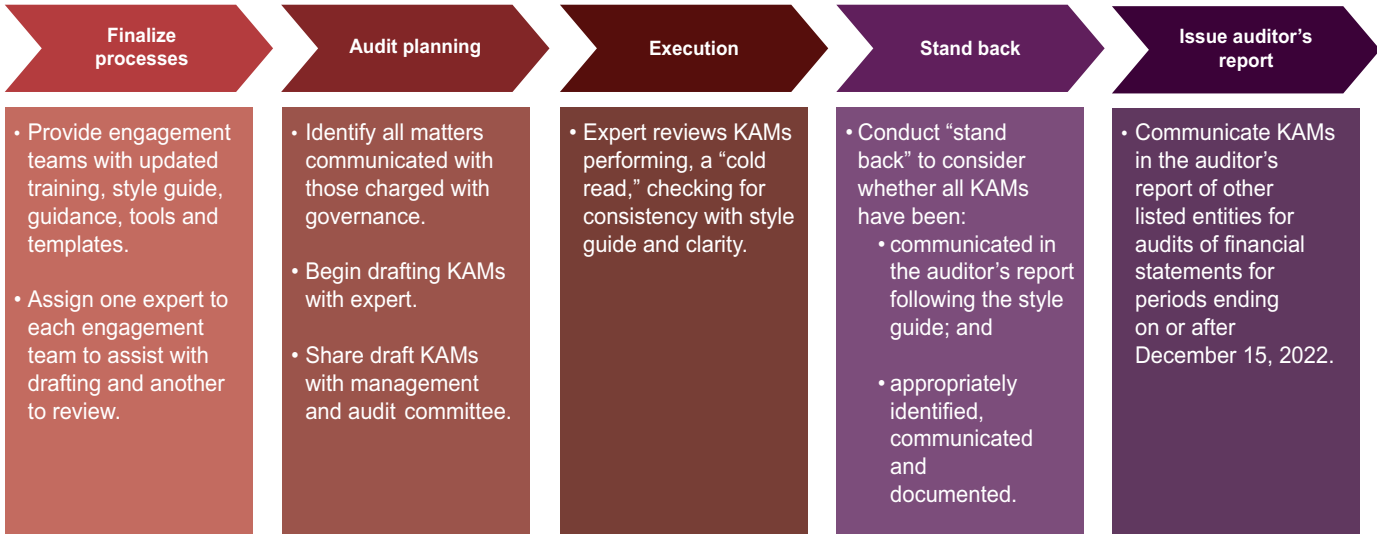
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Overview for Developing a Successful KAM-implementation Process

One Year Prior to Effective Date of Communicating KAM (2021)



Year of Effective Date of Communicating KAM (2022)



One Year Prior to Effective Date of Communicating KAM (2021)

Establish processes

Considerations and Lessons Learned from Practice Runs

- Train auditors involved in audits of other listed entities who will be communicating KAMs for audits of financial statements for periods ending on or after December 15, 2022.
- Develop a plain-language style guide for engagement teams to follow so the KAMs are drafted in a consistent manner across the firm and provide the intended user with a clear and understandable description of a KAM. The style guide may include:
 - using lists instead of long paragraphs;
 - using subheadings;
 - avoiding specific words (i.e., auditing jargon) in the description.
- Develop templates or other tools to make drafting consistent and clear.
- Be careful when creating sample KAMs for engagement teams. They may simply copy the wording and not tailor the KAM to the specific entity being audited.

Establish a team of experts to assume the following roles and responsibilities:

- **Assist engagement teams to identify and draft KAMs:** An expert will work with the engagement team to apply the firm's process for identifying KAMs. They will also work with the team, using the style guide to draft KAMs that meet the standard's requirements, are consistent with client terminology, and strike the right balance between breadth and depth for the intended user.
- **Review KAMs:** A different expert will do a "cold review" of the draft KAMs to ensure they comply with the style guide and are clear for the intended user.
- **Consultations:** Both teams will consult on specific matters that arise during the KAM-implementation process. For example, the firm may determine it appropriate for the engagement team to consult with the experts if the engagement team believes that there are no KAMs to communicate in the auditor's report of the current period financial statements. This may include a formal written document stating how the engagement team reached its conclusion, which is signed, and acknowledged by all parties involved in the conclusion.

Perform practice runs (mid-2021)

Considerations and Lessons Learned from Practice Runs

- Select a sample of audits of other listed entities whose auditors will be communicating KAMs for periods ending on or after December 15, 2022.
- Using the 2020 year-end audited financial statements as a basis, the engagement team identifies potential KAMs for the 2021 year-end audit. Following the style guide, the engagement team drafts the KAMs to communicate in the auditor’s report.
- Assign experts to assist the engagement team in drafting the KAMs. Both teams should follow the established processes.
- Assign an expert not involved in drafting the KAMs to perform a “cold review”. The engagement team needs to consult with the team of experts on specific matters, when applicable.
- Track the challenges both teams encounter while implementing the requirements and following the established processes.

Audit-planning meetings with clients for 2021 year-end audits

Considerations and Lessons Learned from Practice Runs

Educate audit client on the new requirements in CAS 701.

- Educate the client management and the audit committee on KAM communications. Discuss the nature of KAMs that may be communicated in the auditor's report if CAS 701 were effective for 2021 year-end audits.
- Consider providing the client with sample KAMs from TSX-listed entities in the same or similar industry. Be clear that these are **only for reference** and that KAMs communicated in the auditor's report will be tailored to the entity's specific circumstances.
- Discuss the practice-run KAMs with management and allow them to consider the appropriateness of the financial statement note disclosures relating to the matter(s) well in advance of the 2022 year-end.

Debrief practice runs (beginning of 2022)

Considerations and Lessons Learned from Practice Runs

- Engagement teams and experts stand back and evaluate the processes established, tools developed and challenges encountered during the practice runs.
- Discuss the challenges engagement teams encountered. Use the review and the challenges to:
 - streamline established processes;
 - revise training materials and/or develop further guidance to address the challenges; and
 - revise the KAM style guide, tools and/or templates.

Year of Effective Date of Communicating KAM (2022)

Finalize processes

Considerations and Lessons Learned from Practice Runs

- Provide engagement teams with updated training materials, new guidance, revised style guide, tools and/or templates based on the lessons learned from the practice runs.
- Assign experts to the engagement teams, one to help draft the KAMs and the other to review.

Audit planning

Considerations and Lessons Learned from Practice Runs

- Identify matters most likely to be areas of significant auditor attention in the audit of the financial statements of the current period and, therefore, may be potential KAMs.
- The earlier you begin identifying KAMs, the better. Engagement teams can plan the audit accordingly. For example, if the audit procedures to address a KAM involve a specialist, the engagement team may have the specialist review the description of the KAM, including the audit procedures performed. This adds more time and effort to the process.

Begin drafting KAMs.

- Draft KAMs to communicate in the auditor's report. The expert considers whether the appropriate KAMs are identified and whether they are drafted according to the style guide.

Discuss draft KAMs with management and the audit committee.

- Discuss the KAMs with management and the audit committee early in the process. Management will then have time to consider new or enhanced disclosures in the financial statements or elsewhere, related to the matter to be communicated as a KAM, before the KAM wording is finalized. If KAMs are discussed too late in the process, management may not have sufficient time to consider making enhanced disclosures.
- Work with management and those charged with governance to organize meetings so they are scheduled earlier than in the past. Robust two-way communication between the auditor and management is crucial to a successful KAM-implementation process.

Execution

Considerations and Lessons Learned from Practice Runs

Experts review KAMs.

- All KAMs are identified and the drafting of the KAMs is well underway, if not near completion.
- The expert does a “cold review” of all the drafted KAMs for consistency with the drafting convention/style guide and for clarity. The expert will also review the KAM for consistency with client terminology and the wording used in the related note disclosure.

Stand back

Considerations and Lessons Learned from Practice Runs

Do a stand back.

- Both teams consider whether all KAMs have been communicated appropriately in the auditor’s report using the style guide.
- Both teams consider whether all identified KAMs are:
 - appropriate;
 - communicated in accordance with the requirements in [paragraph 11](#) of CAS 701; and
 - documented in accordance with the requirements in [paragraph 18](#) of CAS 701.

Issue auditor's report

Considerations and Lessons Learned from Practice Runs

- Communicate KAMs in the auditor's report of other listed entities for audits of financial statements for periods ending on or after December 15, 2022.

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Key Audit Matters Insights for Stakeholders

Frequently Asked Questions (FAQs)

April 2021

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Introduction

Key audit matters (KAMs) are being communicated in the auditor's report as Canada enters the last phase of its enhanced auditor reporting project. Communicating KAMs in the auditor's report has important implications for the dialogue between auditors, management and audit committees.

This FAQ document addresses key questions that management, the audit committee and users may have related to KAM reporting requirements.

What are KAMs and how are they communicated?

KAMs are matters that, in the auditor's professional judgment, were of most significance in the audit of the financial statements of the current period. The auditor selects KAMs from all the matters communicated with those charged with governance of the entity.

KAMs are **not**:

- a substitute for appropriate disclosures in the financial statements;
- a substitute for the auditor expressing a modified opinion when required by the circumstances; or
- a separate opinion on individual matters.

They are communicated in the "Key Audit Matters" section of the auditor's report. When reading this section, you will notice every KAM includes:

- a separate subheading, a description of the KAM and a reference to the appropriate note disclosure in the financial statements;
- an explanation of why the matter was considered to be one of most significance in the audit of the current period and why it was determined to be a KAM; and
- an explanation of how the matter was addressed in the audit.

Who is required to communicate KAMs in the auditor's report?

Auditors of entities listed on the Toronto Stock Exchange (TSX), excluding those required to comply with National Instrument (NI) 81-106, *Investment Fund Continuous Disclosure*, are required to communicate KAMs in the auditor's report for audits of financial statements for periods ending on or after December 15, 2020.

Auditors of other listed entities,¹ excluding those required to comply with NI 81-106, are required to communicate KAMs in the auditor's report for audits of financial statements for periods ending on or after December 15, 2022.

How many KAMs are communicated in an auditor's report?

It depends.

No specific number of KAMs are required to be communicated in the auditor's report. The auditor judges the relative importance of matters that required significant auditor attention. If the auditor identifies no KAMs, the auditor's report will include a sentence to this effect in the KAM section of the auditor's report.

Will there be a KAM for all significant risks of material misstatement?

Not necessarily.

The auditor is required to presume there is a significant risk of fraud in revenue recognition and a significant risk of management override of controls. However, depending on the nature of the significant risks, they may not require significant auditor attention. So, the auditor may judge them to not be KAMs.

Should I expect the same types of KAMs in the auditor's report of entities in the same or similar industries?

Not necessarily.

The requirements for communicating KAMs depend on each entity's facts and circumstances. Several entities in an industry, may have the same or similar KAMs due to the industry's circumstances or the underlying complexity in financial reporting, however, the auditing standards do not prescribe KAMs for industries.

KAMs benefit users when they relate to the specific circumstances of the entity and the audit performed for the current period. A KAM is significant relative to other matters dealt with in the audit of the current period. When explaining why, the auditor may highlight aspects specific to the entity.

¹ The CPA Canada Handbook – Assurance, Glossary of Terms, defines a “listed entity” as “an entity whose shares, stock or debt are quoted or listed on a recognized stock exchange, or are marketed under the regulations of a recognized stock exchange or other equivalent body.” Other listed entities include all entities listed on an exchange other than the TSX (i.e., TSX Venture Exchange, Canadian Securities Exchange, Aequitas NEO Exchange).

Will the auditor communicate the same KAM(s) year after year?

It depends on the circumstances of each audit and the nature of the potential KAM.

Each year, auditors determine and communicate matters with those charged with governance. Those matters may change from year to year, therefore, different KAMs may be identified each year. However, it is not necessary (or required) that the auditor identify different KAMs each year. Even though the auditor may communicate a KAM for the same matter year over year, the reason for identifying the KAM and how it was addressed in the audit may vary from the previous year.

Will a description of the KAMs contain any original information about the entity?

No.

Original information is any information about the entity that management or those charged with governance has not otherwise made publicly available at the date of the auditor's report, or addressed in other oral or written communications, such as a preliminary announcement of financial information or investor briefing. The auditor will seek to avoid communicating original information by encouraging management and those charged with governance to disclose additional information.

However, management or those charged with governance may decide to include new or enhanced disclosures related to the KAM in the financial statements or other documents because the matter will be communicated in the auditor's report. For example, such new or enhanced disclosures may be included to provide more robust information about the sensitivity of key assumptions used in accounting estimates or the entity's rationale for a particular accounting practice or policy when acceptable alternatives exist under the applicable financial reporting framework.

Will KAMs include the outcome of the audit procedures performed?

Not necessarily.

The amount of detail to be provided in the auditor's report to describe how a KAM was addressed in the audit is a matter of professional judgment. The auditor may describe the outcome of the auditor's procedures or key observations with respect to the matter, however, the auditor is not required to.

Is management and/or the audit committee required to approve KAMs before the auditor's report is issued?

No.

Neither management nor the audit committee approve KAMs. KAMs are identified by the auditor and communicated in the auditor's report. However, the auditor is required to communicate KAMs with those charged with governance. Management and/or the audit committee will usually discuss the KAMs with the auditor before the auditor's report is issued.

What are the expected benefits of KAM communications?

Experience in jurisdictions that have implemented the KAM-communication requirements suggests that communicating KAM has benefited parties in the financial reporting ecosystem.

KAM reporting drives earlier, enhanced and more frequent dialogue among auditors, management and the audit committee throughout the year. Communication becomes more structured, requiring greater attention and preparation by everyone involved.

Academic and other literature reviews note that KAM communications promote focused and robust audit committee discussions with auditors and management about financial reporting risks. Audit committees report that these discussions put them in a stronger position to fulfill their responsibilities for accountability on behalf of investors.

Having to consider whether to communicate KAMs has helped many auditors re-emphasize matters in the audit that require judgment and significant attention. Discussions of these matters with management may result in management reassessing the adequacy of disclosures related to matters identified as KAMs. This improves audit quality and financial reporting.

Investors have indicated they gained more insight into the financial reporting risks of the companies they invest in, as well as the audit process.

In addition, indirect benefits noted from KAM reporting include company internal process improvements like strengthening internal controls, improving risk management, and identifying new risks.

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