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What Canadian audit committees should consider at the beginning of 2022 and beyond

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This 2022 edition of our annual review of issues affecting audit committees during the year-end audit cycle summarizes key considerations for audit committees. With the changing risk landscape, the audit committee's role continues to grow more demanding and complex amid the pandemic and a dynamic business environment. This report will assist audit committees to proactively address developments in risk management, financial reporting, tax, and the regulatory landscape.

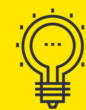
CONTENTS

02 Risk management
10 Financial reporting
14 Tax and other policy-related developments
22 Regulatory developments
32 Questions for audit committees to consider

1 RISK MANAGEMENT

After a protracted period of operating in survival and stabilization mode, organizations are now turning their attention to enhancing enterprise resilience, growth and transformation. A recent EY study noted that 68% of organizations plan a major investment in data and technology in the next 12 months, and 61% plan to undertake a major transformation initiative.

Boards and audit committees are revisiting risk management practices to see that risks are managed effectively across the organization. They're also building more resilience toward low likelihood and high-impact risks, including the ability to rapidly restore business operations. Given the likely continued waves of disruption ahead, leading organizations are making investments to drive resilience into their long-term strategies and operating models.



OVER THE LAST 18 MONTHS, RESILIENCE ACROSS EXISTING AND NEW RISK DIMENSIONS HAS BECOME A DEFINING CHARACTERISTIC OF LONG-TERM SUCCESS AND A KEY BUSINESS IMPERATIVE FOR ORGANIZATIONS GLOBALLY.

A growing focus on enterprise resilience

The rapidly changing economic conditions, including inflationary pressures and ongoing supply chain disruption, have made understanding the current business environment and predicting future conditions challenging – especially since the economic recovery remains uneven across geographies and sectors. Over the last 18 months, resilience across these existing and new risk dimensions has become a defining characteristic of long-term success and a key business imperative for organizations globally. Financial and operational resilience were rigorously tested, and those who had built greater and higher-quality capital and liquidity were in stronger positions going into the pandemic. The need for greater technological resilience was driven by greatly accelerated moves to transform digitally. Human capital issues, workforce resilience and employee well-being became key focus areas. At the same time, societal and environmental resilience became an elevated focus as organizations paid closer attention to diversity and equity in society and the accelerating impacts of climate change.

Whether due to growing regulatory pressure or the disruptions caused by COVID-19, risk management has climbed higher on the board agenda. We recently surveyed 510 global directors to uncover the views and perceptions of directors on enterprise risk management within their organization and the hallmarks of effective risk management, and identify the actions boards can take to improve risk oversight.

SOME NOTABLE SURVEY HIGHLIGHTS INCLUDE THE FOLLOWING:

- COVID-19 was not only a major risk event in itself – it was also an accelerator of risks that were already present, including cybersecurity attacks, supply chain disruption, geopolitical tension, and other external threats. Nearly 83% of board members believe market disruptions have become increasingly impactful, and 87% believe they have become increasingly frequent.
- Core attributes of high-performing risk management leaders include three key behaviors: risk is viewed through a long-term horizon (ideally more than five years); risk management priorities are aligned with business strategy; and there is a greater focus on managing emerging risks, atypical risks and external risks.
- Directors rank unfavorable economic conditions, technology and digital disruption, and changing customer expectations as the top three risks that will moderately impact their business during the next 12 months. Additionally, changing customer expectations, climate change and sustainability, and changes in the regulatory environment are noted as the top three risks that have grown in importance as compared with the prior year.
- Directors noted a misalignment between corporate culture and strategy as the greatest workforce-related risk management challenge. Given the hypercompetitive labor market and the need to contend with business transformations, it is not surprising that board oversight of talent and culture has risen in importance. In fact, our study shows that 80% of companies considered leaders on risk management often or always talk at board meetings about the culture needed to support the organization's strategy.
- Despite the criticality of risk management, many board members lack confidence in their organization's capabilities. For example, just 18% believe that their organization's disaster response and contingency planning is highly effective, and only 13% believe that their organization is highly effective at embedding risk and compliance activities.

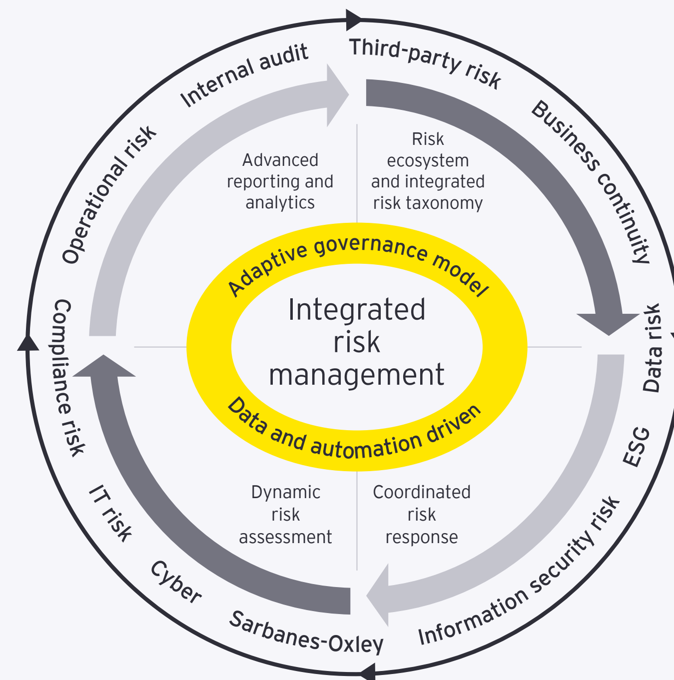
As companies build enterprise resilience and revisit their risk management practices, audit committees and boards should continue to monitor the risk landscape and assess implications to the company.

How data and technology are enabling integrated risk management

Despite its elevated importance, organizations' risk monitoring and mitigation efforts currently fall short of boards' expectations. In fact, just 49% of CEOs say their risk assessment processes are adequately data-driven. Organizations that prioritize the development of an integrated risk management platform effectively embrace the momentum created by data and technology to drive agility and enhanced risk-based decision-making into their risk management approach. The outcome is a coordinated and proactive view of the top risks faced by the organization. We highlight trends and ways that organizations are leveraging data and technology to enable and enhance integrated risk management efforts:

- Leading organizations are leveraging automation technology to process low-value manual tasks, such as risk model verification and simple data processing, allowing the risk function to focus on value-adding activities (e.g., evaluating new business models or assessing threats associated with their organization's deployment of new technology). Automated data collection and monitoring are enabling these organizations to identify real-time potential issues to risk and business teams much sooner and provide a broader and connected perspective on control effectiveness and risk.
- Businesses are utilizing artificial intelligence (AI) to assist in modeling and understanding connections between risks (e.g., using AI to automate basic risk research, identify important risk statements in unstructured documentation and undertake casual analysis to identify risk interdependencies). These insights can then be presented in easy-to-comprehend formats via dashboards to senior management and boards. Importantly, an improved understanding of the intricacies of risk helps to develop more effective mitigation measures and improved coordination for deploying resources across risk functions.
- Integrated risk management platforms and cloud infrastructure are enabling teams to analyze risk trends more easily and providing risk teams the data storage capacity and analytics firepower needed to conduct horizon scanning, scenario planning and stress testing based on multiple variables. Boards and audit committees who are looking for teams to effectively detect weak signals of an atypical and distant threat before it materializes into a major risk are seeking this type of analysis.

Boards and audit committees should assess whether management has a robust strategy for an integrated risk management program leveraging data and technology, with a particular focus on talent and skillsets that may be required.



ORGANIZATIONS THAT PRIORITIZE THE DEVELOPMENT OF AN INTEGRATED RISK MANAGEMENT PLATFORM EFFECTIVELY EMBRACE THE MOMENTUM CREATED BY DATA AND TECHNOLOGY TO DRIVE AGILITY AND ENHANCED RISK-BASED DECISION-MAKING INTO THEIR RISK MANAGEMENT APPROACH.

How oversight of cybersecurity continues to evolve

As the cyber attack surface increases, threats and incidents continue to intensify, creating more pressure than ever for companies. According to the **EY Global Information Security Survey 2021**, 81% of executives say the COVID-19 pandemic forced organizations to bypass certain cybersecurity processes or controls.

In this environment, boards and audit committees should remain vigilant and enhance their oversight over cybersecurity by:

- **Setting the tone.** Establish cybersecurity as a key consideration in all board matters.
- **Staying diligent.** Address new issues and threats stemming from remote work and the expansion of digital transformation. Assess how data protection and governance can be improved.
- **Determining value at risk.** Reconcile value at risk in dollar terms against the board's risk tolerance, including the efficacy of cyber insurance coverage.
- **Embedding security from the start.** Embrace a "trust by design" philosophy when designing new technology, products and business arrangements.
- **Independently assessing the cybersecurity risk management program.** Obtain a recent and rigorous third-party assessment of the cybersecurity risk management program with the external independent advisor's direct feedback presented to the board.
- **Understanding escalation protocols.** Include a defined communication plan detailing when the board should be notified, including ransomware incidents.
- **Managing third-party risk.** Understand management's processes to identify, assess and manage the risk associated with service providers and the supply chain.
- **Updating cybersecurity and integrity training for employees and contractors.**
- **Testing response and recovery.** Enhance enterprise resilience by conducting rigorous simulations, including restoring off-site backups and testing recovery time and arranging protocols with third-party specialists before a crisis.
- **Monitoring evolving practices and the regulatory and public policy landscape.** Stay attuned to evolving oversight practices, disclosures, reporting structures, metrics, and regulatory and public policy developments.

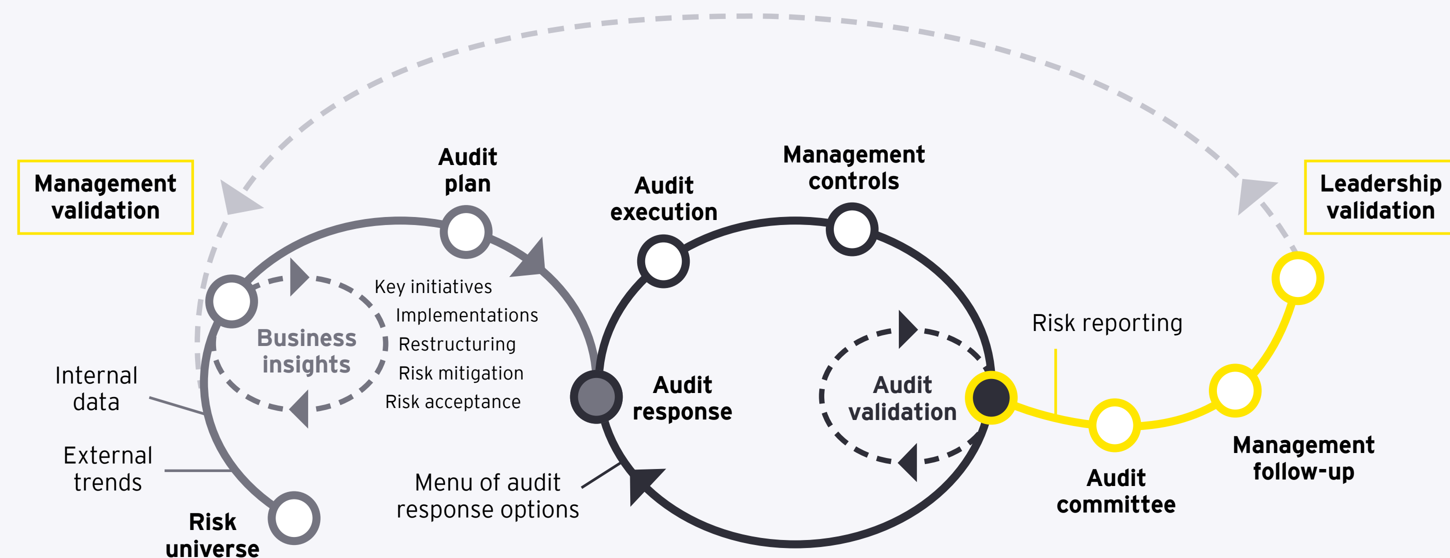
How internal audit (IA) functions are transforming

Increasingly, boards and audit committees will not be content with an IA function that continues to do business as usual while dynamic shifts are occurring throughout the organization. Typically the growing "digital and data divide" between IA and the business within organizations will continue to challenge the relevance of IA and compliance functions.

Both executives and audit committees are evaluating the effectiveness of their IA function and exploring changes to the way the function operates in the future. Since the pandemic, a different picture of IA has been emerging as the function becomes more dynamic and draws on an expanded skill set. Traditional audit methods such as on-site visits, sample-based testing and documentation reviews are giving way to remote audits, analytics-based testing and digital audit techniques. The COVID-19 disruption is accelerating the transformation of IA to become an agile, forward-looking and technology-enabled business partner that provides strategic insight on risk across the organization. In particular, leading IA functions are performing the following:

- **Disrupting the risk assessment process:** shifting from a static, single point-in-time view of risk to dynamic, technology-enabled risk identification and prioritization that is refreshed continuously in real time. IA functions are also leveraging collaboration tools to facilitate efficient and timely feedback from key stakeholders and exploring the use of tools and enablers to identify outside risks.
- **Adopting continuous monitoring:** broadening the focus from detection based on past results to also predicting control failures and risk triggers in real time. Additionally, leading IA functions are implementing a data analytics platform that monitors key risk indicators throughout the organization and enhances risk management by enabling the first and second lines to continuously monitor baseline risk. This is allowing IA to optimize its audit approach and focus on emerging risks.
- **Communicating with impact:** transforming the way that IA communicates with its stakeholders by focusing on delivering insights over simply reporting results. IA functions are focusing their communications of findings on the root cause of the issue, providing the business with valuable wisdom and insight that can be used to enact real change and improvement. Progressive IA functions are also using interactive reporting dashboards, which allow for quicker turnaround of results, better engagement with the user and more impactful conversations than traditional audit reports.

A DYNAMIC IA FUNCTION – DIGITALLY ENABLED AND AGILE



Sharpening the focus on culture, ethics and compliance-related risks

In the current environment, businesses may have been forced to take quick actions without following normal protocols and due diligence. Governments around the world are sending aid to companies with minimal safeguards. Many employees are working remotely with less security and supervision while under far more stress, increasing the opportunities for fraud. Organizations without a strong antifraud program and appropriate cybersecurity may face increased compliance risks, such as legal action and regulatory fines.

All types of occupational fraud rose in 2020, and 90% of certified fraud examiners expect a further increase in 2021, according to a global ACFE survey.[1] Examiners cited cyber fraud as the top risk, with payment fraud, bribery, corruption, and employee embezzlement also on the increase. As the post-crisis landscape promises some relief as well as more change, audit committees should assess how fraud risks may have grown during the pandemic and assess whether the current control environment is sufficient. Audit committees should verify that organizations are looking beyond short-term fixes and enhancing current processes and policies to make them stronger long after the pandemic ends. We offer the following practices for audit committees and management to consider:

- Identify areas that are most likely to be impacted by fraud and prioritize them for improvement, such as third-party controls and lack of cybersecurity for remote workers.
- Maintain a strong culture of corporate integrity, understanding that adjustments may be needed to engage and support a remote workforce.
- Closely monitor and keep a pulse on how culture can affect internal controls and compliance – this includes consideration of analytics of cultural trends, benchmarking to other entities or standards, "lessons learned" analyses, reviews of behavioral trends, and surveys of risk attitudes and risk awareness.
- Consider how AI, advanced analytics and automation can be leveraged to stay ahead of sophisticated cyber threats and detect patterns that indicate wrongdoing.
- Evaluate changes to third-party risk due to the changing environment, considering new controls, contracts, and other measures to improve data protection and stem corruption.
- Evaluate the effectiveness of the organization's whistle-blower reporting processes.
- Stay abreast of evolving regulations to maintain compliance and reduce penalties should data breaches and other wrongdoing occur.

ADDITIONAL RESOURCES

> EY Global Board Risk Survey

> How cybersecurity risk disclosures and oversight are evolving in 2021

[1] "Fraud in the wake of COVID-19: Benchmarking report – December 2020 edition," Association of Certified Fraud Examiners (ACFE), December 2020.

Questions for audit committees

- How is the company using new technologies and data to enhance stress testing and scenario analyses to better prevent surprises and significant variability in operating performance?
- Do scenario analyses consider an appropriate range of extreme and even improbable scenarios, including existential threats? Do they incorporate the potential compounding effects of various risks?
- How can the organization build resilience while remaining lean and agile enough to respond to unforeseen risks? Are contingency and response plans related to risks, including cybersecurity and supply chain, periodically simulated and reviewed with the board?
- How is the company revisiting and adapting its risk management strategy and management's approach to the three lines model in response to potential changes in the external and internal environment, changes in strategy and risk landscape and the company's operating model?
- How is the company managing critical third-party and systemic risks, including those related to financial and operational resilience, IT security, data privacy, and the company's supply chain?
- Has the board considered how the organization's technology strategy is evolving, including how AI and other emerging technologies can be used to review and validate data and information to unearth insights into enterprise risks and opportunities?
- Have the company's information security measures and other controls been reviewed and adapted to be responsive to ongoing digital acceleration efforts, technology changes and the shifting business environment?
- How has the company's cybersecurity risk management program evolved to address the post-pandemic context, in which attackers are targeting a larger surface area and using increasingly unpredictable tactics? How is cybersecurity proactively integrated into all major strategy or tactical decisions, such as transactions, alliances, new products or services, and technology upgrades?

2

FINANCIAL REPORTING

Companies are continuing to re-evaluate their disclosures as stakeholders seek to understand the impact of various external developments on the business. This includes the continued global COVID-19 pandemic-driven economic uncertainty, climate and other environmental, social and governance (ESG) factors, and evolving geopolitical developments.

> "
> Companies should continue to discuss the impacts of COVID-19 on their business and operations to the extent applicable.
>
> *– Ontario Securities Commission*

Continue to focus on accounting and disclosure issues related to the pandemic

As organizations adapt to the uneven economic recovery and variants of the pandemic within and outside of Canada, we anticipate audit committees will continue to evaluate these evolving impacts and changes in the business environment on their financial reporting processes. Key considerations may include the following:

- Evaluate and consider thorough disclosures in areas such as changes in internal control over financial reporting, management discussion and analysis (e.g., impacts of labor shortages and labor market conditions, inflationary pressures), risk factors, critical accounting estimates, liquidity, and current vulnerabilities due to certain concentrations (e.g., customer, supplier, geographic).
- Reevaluate earnings and other performance or financial position guidance previously provided and the ability to provide future guidance.
- Reevaluate the use of non-GAAP measures and consider whether any changes in non-GAAP financial measures (or key performance indicators) are appropriately disclosed and consistently applied in all periods.

Companies should continue to update their disclosures about the effects of the pandemic, current market conditions and their expectations for the future. It will be important for audit committees not only to understand management's view of future economic conditions, but also validate that the organization provides transparent disclosures regarding these views.

Non-GAAP financial measures

National Instrument 52-112, *Non-GAAP and Other Financial Measures Disclosure*, which now contains legally binding disclosure requirements, supersedes prevailing Staff Notice 52-306, *Non-GAAP Financial Measures*, with much more standardized and specific definitions and disclosure requirements.

NI 52-112 addressees the disclosure requirements for non-GAAP financial measures, non-GAAP ratios and other financial measures (e.g., capital management measures, supplementary financial measures and total of segments measures, as defined in the national instrument). The instrument has substantially incorporated the previous disclosure guidance while introducing new disclosure requirements if such financial measures are disclosed outside of the financial statements.

Disclosures for non-GAAP financial measures that are historical information must apply a number of criteria.

ISSUERS ARE LIKELY TO CONTINUE TO FIND THE FOLLOWING AREAS THE MOST CHALLENGING:

- Presentation with no more prominence than that of the most directly comparable financial measure that is disclosed in the primary financial statements
- An explanation of how the measure provides useful information
- A quantitative reconciliation, in the permitted format, to the most directly comparable financial measure for the current period that is disclosed in the primary financial statements, and if included within an MD&A or earnings release, the comparative period must be included as well.

Audit committees can continue to play an important role in understanding how management uses non-GAAP financial measures and how they supplement the GAAP financial statements. Audit committees that display strong interest in non-GAAP financial measures can have a positive effect on the quality of disclosures.

NI 52-112 applies to all reporting issuers except investment funds, SEC foreign issuers and designated foreign issuers. It also applies to non-reporting issuers, in particular to documents prepared by such issuers in connection with certain prospectus-exempt offerings or other transactions (such as, but not limited to, an offering memorandum, long-form prospectus or a filing statement/listing statement).

Forward-looking information

Securities regulators continue to focus on deficiencies in forward-looking information (FLI). Issuers are required to:

- Specifically identify the FLI and avoid boilerplate disclosures.
- Describe their policy for updating FLI or state that they undertake no obligation to publicly release any revisions to FLI.
- Present FLI in a manner that allows an investor to readily identify it.

Particular attention is being paid to multi-year FLI. Where issuers are using multi-year FLI in a prospectus or otherwise, the FLI must be based on assumptions that are reasonable in the circumstances (including consideration for COVID-19). Assumptions for quantitative data should be specific and comprehensive, such that each investor or user is able to clearly understand how each assumption was used in developing the FLI. Like non-GAAP measures, audit committees can play an important role in understanding the company's FLI and how FLI is described in the company's disclosures and prospectuses.

ADDITIONAL RESOURCES

- > CSA Staff Notice 51-362 – Staff Review of COVID-19 Disclosures and Guide for Disclosure Improvements
- > 52-112 Non-GAAP and Other Financial Measures Disclosure
- > OSC Staff Notice: 51-732 - Corporate Finance Branch 2021 Annual Report | OSC

Questions for audit committees

- How is the organization proactively assessing opportunities to enhance stakeholder communications, including corporate reporting, to address changes in operations and strategies as well as changing stakeholder expectations?
- Have there been any material changes to internal controls over financial reporting or disclosure controls and procedures to address the changing operating environment? Have any cost saving initiatives and related efforts impacted resources or processes that are key in internal controls over financial reporting? If so, has management identified mitigating controls to address any potential gaps?
- What approach has management taken to consider multiple scenarios related to its projections and underlying assumptions that are expected to have a material impact on the results of operations or capital resources? Have there been material changes in controls and processes to evaluate the reasonableness of the assumptions and key estimates?
- Does the audit committee understand how management uses non-GAAP financial measures and how they supplement the GAAP financial statements?

3

TAX AND OTHER POLICY-RELATED DEVELOPMENTS

The tax landscape is in flux. Multinational companies are navigating a range of policy shifts, including potential major tax legislation, continuing progress on the Organisation for Economic Co-operation and Development (OECD) BEPS 2.0 project and a growing focus on the role of tax in the ESG agenda.

Add in the ongoing human and economic effects of COVID-19, and the result is a challenging and dynamic tax environment for businesses. Boards and audit committees should oversee their organizations' preparedness for and responses to these issues, all of which could affect business models, supply chains and decisions. Businesses should consider modeling and analysis to map out future scenarios and prepare for added complexity. This increased complexity could also lead to businesses facing more tax controversy. Audit committees will want to make sure that all tax matters related to COVID-19 and the broader tax landscape have been appropriately assessed and considered.

Canadian tax policy developments

DIGITAL SERVICES TAX

In its 2020 fall economic statement and again in the 2021 budget, the federal government proposed a digital services tax (DST) as a precautionary measure against the G7, G20 and the Organisation for Economic Co-operation and Development (OECD) not being able to reach consensus on the OECD's "two-pillar solution" to address the tax challenges arising from the digitalization of the economy.

By the fourth quarter of 2021, the OECD was able to obtain agreement by 137 jurisdictions, along with endorsement by the leaders of the G20, on its statement of the core design and implementation plan of its two-pillar solution.

The first pillar of the solution, expected to come into effect in 2023, provides new profit allocation and nexus rules for large profitable multinational enterprises (i.e., those with greater than €20 billion in worldwide revenues and profitability before tax above 10%), including large digital corporations, to provide that they pay a fair share of tax in the jurisdictions in which their users and customers are located.

Under the agreed statement, the multilateral convention through which part of the first pillar will be implemented will require all parties to remove all DSTs and other relevant similar measures with respect to all companies and that no new DSTs or other relevant similar measures will be imposed on any company from October 8, 2021 until the earlier of December 31, 2023 and the coming into force of the multilateral convention.

In response, on October 8, 2021, Canada announced that it would proceed with introducing its own DST legislation, but that the new tax would not be imposed earlier than January 1, 2024 and only if the multilateral convention implementing the first pillar has not come into force within the expected timeline. In the event that pillar one does not come into force prior to January 1, 2024, Canada's DST will be payable in respect of revenues earned as of January 1, 2022, but will be imposed no earlier than January 1, 2024.

On December 14, 2021, the federal government tabled the *Digital Services Tax Act* in the House of Commons. The DST is proposed to apply to certain types of large businesses, both domestic and foreign, operating in the digital space in a calendar year where their:

- Total consolidated group revenue from all sources is at least €750 million during a fiscal year that ends in the preceding calendar year; and
- The total of all Canadian digital services group revenue is greater than CDN$20 million in the calendar year.

The DST is proposed to apply a rate of 3% to taxable Canadian digital services revenue in excess of CDN$20 million, which is based on the following four sources:

- Canadian online marketplace services revenue
- Canadian online advertising services revenue
- Canadian social media services revenue
- Canadian user data revenue

Impacted businesses should review the Notice of Ways and Means Motion to amend the *Income Tax Act* (NWMM) and consider the potential consequences and tax cost to their operations. Since the DST, if implemented, will be payable in respect of taxable Canadian digital services revenue earned on or after January 1, 2022, potential taxpayers should determine whether, and to what extent, they would be required to make provision in their financial statements for this potential tax.

The Canadian Government has invited comments on the proposed legislation. Impacted businesses should take the opportunity to raise any technical issues of concern with the NWMM by making submissions to the federal Department of Finance during the public consultation period, which ends on February 22, 2022.

International tax updates from the 2021 federal budget

RULES TO ADDRESS HYBRID MISMATCH ARRANGEMENTS

The 2021 federal budget, released in April 2021, contained two significant proposals to address perceived offensive cross-border tax structures.

The proposed rules to address hybrid mismatch arrangements align Canada's legislation with the OECD's initiatives to address arrangements resulting in:

- Deduction/non-inclusion mismatches
- Double deduction outcomes
- Imported mismatches
- Branch mismatch arrangements

The legislation was scheduled to be introduced in two packages. The first, set to be effective no earlier than January 1, 2022, was meant to address deduction/non-inclusion mismatches. The second, addressing the other arrangements, was set to come into effect no earlier than January 1, 2023. As of the time of writing, no draft legislation has been released.

LIMITATIONS ON "EXCESSIVE" INTEREST DEDUCTIONS

The proposed federal rules to address excessive interest deductions complement the existing thin capitalization regime and align with the OECD's Action 4 to limit base erosion through the use of excessive leverage.

The 2021 federal budget proposed to introduce a new earnings-stripping rule consistent with OECD recommendations and many similar regimes in other jurisdictions. The new rule would limit the amount of net interest expense a corporation may deduct in computing its taxable income to no more than a fixed ratio of "tax EBITDA." Tax EBITDA is described to be a corporation's taxable income before taking into account interest income and expense, income tax, and deductions for depreciation and amortization, where each of these items is as determined for tax purposes.

The new earnings-stripping rule is to be phased in with a fixed ratio of 40% of EBITDA for taxation years beginning on or after January 1, 2023 but before January 1, 2024 (the transition year) and 30% for taxation years beginning on or after January 1, 2024. The proposed measure also includes a "group ratio" rule that would allow a taxpayer to deduct interest in excess of the fixed ratio of tax EBITDA where the taxpayer is able to demonstrate that the ratio of net third-party interest to book EBITDA of its consolidated group implies that a higher deduction limit would be appropriate.

The rules should generally allow for the results among a Canadian group to be effectively combined.

This combining measure may have limited application to Canadian banks and life insurance companies, which may not be able to combine their net interest income from their regulated banks or insurance businesses against net interest expense for other members of their corporate group that are not regulated banking or insurance entities.

Interest denied under the earnings-stripping rule would be able to be carried forward for up to 20 years or back for up to three years.

No draft legislation has been released as of the time of writing.

US tax policy changes and developments

Audit committees will need to anticipate possible tax policy changes at both the federal and state levels and understand the potential business implications arising from these developments:

US TAX LEGISLATION – DEADLINES APPROACHING

At the time of publication, the Biden administration and US congressional Democrats were aiming to enact significant tax legislation as part of their social spending bill, the Build Back Better Act (BBBA) but negotiations have stalled. Despite current challenges, the BBBA is still a top priority of President Biden and fellow Democrats in Congress so audit committees should continue to monitor developments closely.

The legislative process for the BBBA has required a delicate balancing act and several rounds of changes to try to satisfy both progressive and moderate groups within the Democratic party whose support will be needed if the measure is to pass.

Although further modifications may be made to the $1.47t of tax increases in the bill,[2] the House-passed legislation contains the following key tax changes:

- A 15% corporate alternative minimum tax based on book income for companies with more than $1b in profits, effective January 1, 2023
- New interest deduction limitations on excessive interest for US corporations that are part of multinational financial reporting groups
- Modifications to the Base Erosion and Anti Abuse Tax (“BEAT”) regime
- Broadening and expansion of tax incentives in the green energy sector
- Substantial changes to the US global intangible low-taxed income (“GILTI”) international tax regime
- Modifications to the wash sale rules

The BBBA also includes $80b for the IRS to invest in “compliance, technology and taxpayer services,” which could result in expanded audit capabilities in the near future.[3]

STATE OUTLOOK

Anytime the federal tax law changes, there will be state tax implications since most state income tax systems start with US federal taxable income. The US federal tax legislation currently being developed in Congress (notably the international tax provisions) has the potential to impact state income taxes for businesses.

Unrelated, but equally important, a growing number of states are also enacting pass-through entity (PTE) taxes. These PTE taxes, which states have employed as a “workaround” to the Tax Cuts and Jobs Act’s federal state and local tax deduction limitation, differ from state to state, creating complexities for owners of businesses with multistate activities. States are also on the forefront of taxing the digital economy, employing new taxes on digital advertising services, expanding sales and use tax bases to include digital goods, streaming services and platform companies and targeting new areas such as non-fungible tokens and cryptocurrencies for taxation.

AUDIT COMMITTEES WILL NEED TO ANTICIPATE POSSIBLE TAX POLICY CHANGES AT BOTH THE FEDERAL AND STATE LEVELS.

[2] “Distributional Effects Of The Revenue Provisions Of Title XIII – Committee On Ways And Means, Of H.R. 5376, The “Build Back Better Act,” As Passed By The House Of Representatives,” Joint Committee on Taxation, November 23, 2021, (JCX-47R-21).

[3] “Estimated Revenue Effects of Increased Funding for the Internal Revenue Service in H.R. 5376, the Build Back Better Act,” Congressional Budget Office, November, 18 2021. The CBO estimates that the funding for tax enforcement activities would increase outlays by $80b and revenues by $207b, decreasing the deficit by $127b through 2031.

Other policy and global developments

Audit committees should continue to monitor the new tax policies, regulations, and other developments.

MOBILE WORKFORCE

In response to COVID-19, businesses have adopted various work-from-home options, including working remotely (in your home province, interprovincially or internationally) and hybrid in-office/remote models. Remote workers can impact employers' (as well as employees') tax responsibilities (e.g., withholding, unemployment taxes, corporate income and franchise taxes) and create taxable presence for a business in new jurisdictions.

THE ENVIRONMENT

Governments are introducing business incentives and penalties in their drive toward sustainability. Recently, at COP26, nearly 200 countries signed the Glasgow Climate Pact, the key summit agreement which sets out the actions and commitments that each country will follow to limit global warming to 1.5°C above pre-industrial levels. The collective activity across governments and the private sector during the conference demonstrates that environmental sustainability and ESG continue to be top issues, thus boards and audit committees need to be aware of the risks and opportunities that could affect their businesses.

Increasingly tax intersects with ESG matters, particularly around a company's approach to taxation: its carbon footprint and climate mitigation strategies, its decisions around using available tax incentives and credits and its overall tax transparency and reporting. Tax is often used as a lever to drive (and fund) economic and policy change, and a company's decisions around tax engagement, tax incentives and tax disclosures have implications for its ESG strategies. Varied and vast ESG reporting metrics can mean that a company may report different facts and figures to different groups, which can increase its tax and reputational risk.

OUTSIDE THE US, MANY OTHER COUNTRIES ARE ALSO MOVING AHEAD WITH THEIR OWN TAX REFORMS. PRESENTLY, 137 COUNTRIES HAVE AGREED TO A TWO-PILLAR SET OF GLOBAL CORPORATE TAX CHANGES BEING DEVELOPED THROUGH THE OECD/ G20 INCLUSIVE FRAMEWORK THAT WOULD REFRAME THE LONG-STANDING INTERNATIONAL TAX ARCHITECTURE.

TAX REFORM ON A GLOBAL SCALE

Outside Canada and the US, many other countries are also moving ahead with their own tax reforms.[4] As previously mentioned, presently, 137 countries have agreed to a two-pillar set of global corporate tax changes being developed through the OECD/G20 Inclusive Framework that would reframe the long-standing international tax architecture. Known as "BEPS 2.0," the OECD proposals involve a new global minimum tax framework at a 15% rate and revisions to existing nexus and profit allocation standards, which could significantly alter where a company's income is taxed.

On December 20, 2021, the OECD released its model rules on the Pillar Two global minimum tax. The model rules cover the scope and the various mechanics collectively referred to as the Global Anti-Base Erosion (GloBE) rules. The model GloBE rules provide details on how to calculate the effective tax rate of each jurisdiction, how to calculate the top-up tax, if any, and how to determine the liability for the top-up tax (i.e., who pays the liability and to which jurisdiction). Multinational entities are encouraged to review these rules to analyze their potential applicability.

There is still much technical work to be completed on the substantive details of the new rules. Despite the release of the model GloBE rules, the timeline remains ambitious, with most provisions targeted to take effect in 2023. As the remaining details are filled in, attention will focus on country-level activity to implement the agreed rules through domestic legislation and bilateral and multilateral tax agreements.

Because these changes may result in higher taxes for multinational companies, it will be important for boards to monitor the details and implementation action by countries. This is also the time to consider providing feedback to country policymakers as the rules are being implemented.

TRADE ISSUES

US trade policy under the Biden Administration has been focused on addressing existing bilateral issues and supporting broader administration concerns with China, supply chain resilience and ESG matters.

The Biden Administration has, for the most part, retained policies adopted during the Trump Administration, particularly for China. The overall emphasis on a "worker-centric" trade policy has, in practice, resulted in a continuation of the more protectionist policies of the prior administration.

A significant development across the major trading blocs is the emphasis on supply chain resilience and government efforts to promote stronger, more diversified domestic production of key strategic products.[5] Trade policies are being pursued that actively support these efforts.

Regionalization is expected to continue in response to supply chain pressures driven by the pandemic and the aforementioned trade policies. The trading system's emerging architecture reflects this as the multilateral-based World Trade Organization (WTO) continues to face challenges, and countries like the UK, China and Taiwan express interest in regional agreements like the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP).

A SIGNIFICANT DEVELOPMENT ACROSS THE MAJOR TRADING BLOCS (US, EU AND CHINA) IS THE EMPHASIS ON SUPPLY CHAIN RESILIENCY AND GOVERNMENT EFFORTS TO PROMOTE STRONGER, MORE DIVERSIFIED DOMESTIC PRODUCTION OF KEY STRATEGIC PRODUCTS.

4 For example, in September, Colombia enacted tax reform legislation that included an increase in the corporate income tax to 35% beginning in 2022. Argentina has upcoming elections that may also lead to possible changes in tax policy, and there has been proposed tax reform in Brazil. See the EY Americas tax policy update, October 8, 2021.

5 In the US, an Executive Order supply chain report with numerous executive and legislative recommendations was published with the intent of driving a national supply chain strategy. The EU is pursuing its own "open strategic autonomy," and China has its "dual circulation" policy, all of which are designed to drive policies that enhance domestic production of key products.

Questions for audit committees

- Did the organization use any COVID-19-related tax benefits in 2021? How were those benefits identified and documented?
- Has the organization reviewed its approach to tax controversy management in light of the ongoing pandemic and the shifting economic, trade and tax policy environment?
- What systems are in place to keep the organization informed of tax policy changes and related developments?
- Has the company performed modeling and scenario planning reflecting potential tax policy changes and trade developments?
- What role does tax play in the organization's ESG strategy?

4 REGULATORY DEVELOPMENTS

Securities regulators continue to focus on company disclosures and investor protection. Given the changing regulatory landscape, audit committees and reporting issuers should keep abreast of the evolving CSA, and if applicable SEC, agenda and the impact that such changes have on the organization.

The rapidly evolving significance of environmental, social and governance (ESG) disclosures to investors, employees, customers and other key stakeholders (including regulators) is causing audit committees and boards to deepen their understanding and oversight of ESG policies and disclosures.

Environmental, social and governance

Current securities regulation in Canada requires disclosure of certain climate-related information in a company's regulatory filings if such information is material. Forward-looking companies and boards are shifting their frame from ESG disclosure compliance and/or public relations to robust ESG policies as a strategic differentiator.

In September 2020, the IFRS Foundation issued its Consultation Paper on Sustainability Reporting for comment. Feedback to the paper confirmed an urgent need for sustainability reporting standards and support for the IFRS Foundation to play a role in their development.

The IFRS Foundation's board of trustees is working on establishing an international sustainability reporting standards board within the existing structure of the IFRS Foundation. The strategic direction of the new board will:

- Focus on information that is material to investors, lenders and other creditors
- Prioritize climate-related matters while also working towards meeting the information needs of investors on other ESG matters
- Build on the well-established work of the Financial Stability Board's Task Force on Climate related Financial Disclosures (TCFD), as well as work with the alliance of standard-setters in sustainability reporting focused on enterprise value
- Aim to provide a globally consistent and comparable sustainability reporting baseline, while also providing flexibility for coordination on reporting requirements that capture wider sustainability impacts

MANDATORY CLIMATE CHANGE DISCLOSURE MOVES TOWARDS GLOBAL ADOPTION

Reporting on ESG factors affecting corporations continues to evolve as various standardized reporting frameworks for ESG become more widely adopted. However, the big developments heading into 2022 relate to mandatory requirements around climate change disclosure in Canada, the US and Europe.

While there will be differences between new requirements emerging in each of the above-mentioned jurisdictions, the overall frameworks being proposed by local regulators are aligning quite closely with the TCFD's previously issued framework. Companies that currently plan or issue their disclosure around the TCFD framework will likely be in the best position to comply with new rules.

CANADIAN DEVELOPMENTS

On October 18, 2021, the Canadian Securities Administrators (CSA) published for comment proposed National Instrument 51-107, *Disclosure of Climate-related Matters*. The public comment period for the proposals expires February 16, 2022.

This proposed National Instrument is similar to the TCFD requirements and includes two key components:

- Companies must describe their processes for oversight of climate-related risks and opportunities by the board of directors and management.
- Companies must provide detailed climate change disclosures related to strategy, risk management processes, and the metrics and targets used to manage climate related risks.

Meeting these requirements includes explicitly stating what material climate-related risks face the company in the short, medium and long run. A company would also disclose the metrics it uses to assess climate-related risks as well as data on its greenhouse gas (GHG) emissions under the classifications of Scope 1 (direct), Scope 2 (indirect emissions arising from its consumption of electricity, heat or steam) and Scope 3 (all other indirect emissions created by their business, including emissions by suppliers and customers). If a company does not disclose this data, it would need to disclose why it cannot do so.

The CSA is also considering an alternative approach that would make disclosure of Scope 2 and Scope 3 emissions voluntary.

Disclosures required under the proposed National Instrument could be included in the management information circular, if one is issued, or the annual information form or the MD&A. In all circumstances, the disclosures would likely be incorporated by reference in short-form prospectuses and caught by legal requirements related to liability for prospectus disclosures.

The CSA acknowledged concerns regarding the regulatory burden and costs imposed on issuers because of mandatory climate related disclosure requirements. The CSA has tried to address the concerns in three ways:

- Issuers are not required to disclose scenario analysis, including a 2°C or lower scenario.
- Issuers will be permitted to disclose their GHG emissions or explain why they have not done so.
- The rules will be phased in over a one year period for non venture issuers and over a three year period for venture issuers. The proposed instrument is not anticipated to come into force prior to December 31, 2022.

These proposed new CSA rules are in addition to an ongoing focus by Canadian securities regulators on the clarity and fulsomeness of the discussion of climate change risks in MD&A.

The overall effect of these regulatory developments, as well as increasing investor analysis and expectations of climate-related disclosures, is that companies will need to ensure they have robust processes for addressing sustainability issues, particularly climate change risk. Much greater transparency will often be required about potential business impacts. Information that is disclosed will need to be supported by effective disclosure controls.

The increase in sustainability data in the MD&A is also increasing the finance function's accountability for this data. Most companies are re-examining their internal processes and accountability frameworks to ensure they can meet these challenges. It is also important that any new disclosures integrate with the company's overall communication plan for all its communication channels. This will provide a clear picture of the impact of climate change and other sustainability issues on shareholder value.

US DEVELOPMENTS

Early in 2021, US President Biden signed an Executive Order encouraging financial regulators to strengthen supervision of climate-related risks, including consideration of increased disclosure requirements. This Executive Order affects the regulation of banking and other financial institutions as well as public securities.

For the securities market, the SEC had traditionally taken the view that its existing disclosure requirements around material business risks adequately covered climate change risks from the investors' perspective. In 2010, the SEC published guidance illustrating how climate-related risks should be better addressed under these requirements.

In 2021, in response to the Executive Order, the SEC began a program of more strict enforcement of compliance with existing rules, including its 2010 guidance, as well as a study of what new rule-making was required.

A new SEC Enforcement Division has been created to follow up on potentially misleading disclosures related to climate change risk. The SEC staff have also been issuing numerous comment letters on registrants' climate change disclosures included in periodic financial filings and prospectuses. A common theme is a request for greater elaboration of physical and transitional risks of climate change to the business's operations and financial results. To assist registrants in better complying with existing rules, a generic illustrative comment letter has been posted on the SEC's website.

Companies are increasingly making disclosures around commitments to reduce or achieve net-zero emissions. These companies should anticipate that the SEC, as well as investors, will be looking for commentary on the financial and other business impacts of pursuing these new targets. Some large investors are indicating that transparency of reporting and disclosure around climate change-related impacts and costs will impact their proxy voting decisions with respect to the appointment of audit committee members and auditors.

With respect to rule-making, it is anticipated that new SEC requirements will come into effect at some point under the Biden Administration. The SEC received over 550 comment letters on its initial outreach on this topic in March 2021, approximately 75% of which were supportive of increased disclosure requirements. The form of these new rules remains under debate, but they will likely be similar to the TCFD framework and rely on definitions used in existing sustainability reporting frameworks. Whether the new reporting will be required to be included in the annual 10-K filing is still under debate. Discussions and consultation are also ongoing as to whether auditor attestation of climate risk or other data will be required.

A draft of the proposed SEC rules is expected to be published in early 2022 and will be subject to further public comment.

INVESTORS ARE HOLDING BOARDS ACCOUNTABLE FOR HOW COMPANIES CREATE LONG-TERM VALUE AND ACT AS RESPONSIBLE STEWARDS OF NATURAL AND HUMAN CAPITAL.

EUROPEAN DEVELOPMENTS

The European Commission is rolling out new climate-related risk disclosures for most public companies. These build off existing requirements for very large European companies and include writing new disclosure standards to be prepared by the European Financial Reporting Advisory Group. These requirements will be applied universally across the European Union and will capture around 50,000 companies. They will apply to EU-listed entities and other large entities operating in the EU that are governed by laws of EU member states, even if the parents of the entities in question are foreign entities,

The first round of these new reporting standards is expected by mid-2022. The European Parliament decided that the new rules, while still subject to final amendments, could be effective as early as reporting periods ending in 2023. Auditor attestation will be required, but reporting will be on a "limited assurance" basis at the time of adoption.

Key ESG issues in the boardroom

As standards and disclosure requirements continue to develop, current key issues in boardroom discussions include:

- Understanding which ESG topics are of highest priority to a company and its stakeholders
- Integrating ESG into the firm's strategy, purpose and risk management processes
- Setting appropriate goals and measuring progress
- Allocating oversight responsibilities at the board level

To the extent ESG metrics are key performance indicators disclosed in a public filing, it is critical that audit committees consider and understand:

- Data quality and controls
- Disclosure processes and controls
- Consistency in disclosures and a cohesive communication across the company's various external reporting outlets (e.g., public filings, earnings releases, the annual report and shareholder letter, and the sustainability report)
- The role of internal and external audit

ADDITIONAL RESOURCES

> Applying IFRS Accounting for Climate Change | EY - Global

> IFRS Foundation establishes International Sustainability Standards Board | EY - Global

> SEC Response to Climate and ESG Risks and Opportunities

CPAB Big Four firm inspection findings

The Canadian Public Accountability Board (CPAB) issued its **2021 Interim Inspections Report** in October 2021 and noted that, to date, 73 of 75 planned file inspections had been completed across Canada's four largest audit firms and significant inspection findings had been identified in five of those files. This compares to six significant inspection findings across 72 inspections in 2020. All four firms had fewer than 15% of files with significant findings.

The CPAB noted in its report that the current economic environment has increased the level of estimation uncertainty on critical accounting estimates, including going concern assessments/liquidity evaluations, complex valuations, impairment evaluations and estimating expected credit losses. The most common inspection findings the CPAB identified related to auditing estimates involving significant assumptions and judgements about future conditions or events.

The CPAB published **Auditing accounting estimates: Strengthening audit quality**, a communication to all audit firms registered with the CPAB in September 2021, which includes more detail on the nature of the deficiencies. Examples of inspection deficiencies included:

- Deficiencies in management's estimate approach were not effectively challenged.
- Point estimates or ranges were developed without sufficient understanding of how management assessed and addressed the level of estimation uncertainty.
- There was insufficient or no consideration of contradictory evidence.
- No assessment was made of the impact of deficiencies on internal controls.

The CPAB encourages audit committees to consider the following questions related to auditing accounting estimates with higher estimation uncertainty:

- Did the auditor identify any deficiencies or gaps in management's analysis of significant estimates? If so, how was the impact of these deficiencies on internal control evaluated?
- How did the auditor evaluate for management bias in auditing complex estimates? Were there any potential indicators identified and how were these resolved?

> "The audit work over accounting estimates continues to be an area with deficiencies and opportunities for improvement.
>
> *– Canadian Public Accountability Board*

CSA changes to auditor oversight rules

On January 13, 2022 the Canadian Securities Administrators ("CSA") published the following:

- **Amendments to National Instrument 52-108 Auditor Oversight (the "Amendments")**
- **Changes to Companion Policy 52-108 Auditor Oversight (the "CP Changes")**

These amendments require actions by reporting issuers and participating audit firms that will assist the Canadian Public Accountability Board ("CPAB") in accessing audit working papers of significant component auditors, particularly in certain foreign jurisdictions.

What has changed?

- Written notification is required to be provided by the reporting issuer to the significant component auditor on or before the audit report date permitting CPAB access to the component auditor's records relating to their audit work if requested *(Written notification can be provided indirectly to the significant component auditor by the group auditor through the reporting issuer's engagement letter)*.
- Failure to provide CPAB access could lead to the group auditor being prohibited from engaging the significant component auditor for future audit work (unless the significant component auditor satisfies CPAB that access is prohibited under local law).

The CP Changes provide additional guidance on how to interpret and apply the Amendments.

These changes are effective for audit reports issued on or after March 30, 2022.

PCAOB outlook and developments

The SEC **appointed** a new Chair and three other new Board Members to the PCAOB in November 2021: Erica Williams as Chairperson and Christina Ho, Kara Stein and Anthony (Tony) Thompson as Board members.

Audit committees, external auditors and SEC registrants should keep abreast of the new Board's strategic priorities and standard setting agenda as it develops in the coming months and the impact that such changes can have on the execution of audits and overall audit quality.

The PCAOB's inspection findings, enforcement matters, and areas of inspection focus should be considered by registrants, external auditors and the audit committee. In October 2021, the PCAOB issued its *Staff Update and Preview of 2020 Inspection Observations*[6], highlighting both good practices observed during audit inspections and areas of recurring deficiencies. Consistent with prior years, some of the recurring deficiencies were in the areas of assessing risks of material misstatement relating to revenue and related accounting, estimates, inventory, critical audit matters, Form AP, and ICFR. Audit committees may find the observations useful as they engage with auditors.

AUDIT COMMITTEES, EXTERNAL AUDITORS AND SEC REGISTRANTS SHOULD KEEP ABREAST OF THE NEW BOARD'S STRATEGIC PRIORITIES AND STANDARD SETTING AGENDA AS IT DEVELOPS IN THE COMING MONTHS AND THE IMPACT THAT SUCH CHANGES CAN HAVE ON THE EXECUTION OF AUDITS AND OVERALL AUDIT QUALITY.

[6] **"PCAOB spotlight: Staff update and preview of 2020 inspection observations,"** Public Company Accounting and Oversight Board, October 2021.

SEC's regulatory agenda

SEC Chairman Gary Gensler's priorities have been reflected in the SEC's semi-annual regulatory agenda that lists the short- and long-term regulatory actions it plans to take. Key SEC rulemaking areas include special purpose acquisition company mergers, disclosures about climate-related and other ESG matters (e.g., board diversity, human capital), and cybersecurity risk governance.

The SEC is also reconsidering certain proxy-related rules. For example, the SEC's Division of Corporation Finance issued Staff Legal Bulletin 14L, *Shareholder Proposals*, setting forth its views on the application of Rule 14a-8 of the Securities Exchange Act, which allows companies to exclude shareholder proposals from their proxy statements in certain circumstances. In addition, the SEC recently adopted **amendments** to its rules that require the use of universal proxy cards in all non-exempt solicitations involving contested elections of directors. Companies will need to comply with the amended rules for a shareholder meeting involving a contested director election after August 31, 2022. The SEC also **proposed** changes to rescind two conditions it added in 2020 to its proxy solicitation rules on exemptions that proxy voting advice businesses typically rely on to avoid the information and filing requirements (i.e., Securities Exchange Act of 1934 Rules 14a-2(b)(1) and (b)(3)).

It also plans to address unfinished rulemaking mandated by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, including finalizing pay vs. performance rules and clawback policies. In October 2021, the SEC requested public comments on its 2015 clawback proposal that would direct national securities exchanges to establish listing standards that would require companies to develop and implement policies to recover incentive-based compensation after an accounting restatement.

Chair **Gensler** and senior SEC staff also have laid out their approach to enforcement, emphasizing the need to restore trust in the public capital markets. One area of focus is holding market participants accountable as appropriate for not living up to their obligations. This includes gatekeepers such as lawyers, accountants and directors, all of whom the SEC views as the first line of defense against wrongdoing. To reinforce this accountability, the SEC Division of Enforcement expects to use tools such as **admissions of wrongdoing** in order to reach settlements with defendants, where appropriate. Senior SEC staff also have **highlighted** the importance of auditor independence and the shared responsibility of the auditor, management and audit committee in protecting it.

Given the dynamic regulatory environment, audit committees should continue to monitor information from the SEC and other regulatory authorities, including how the potential rulemaking may impact reporting requirements and related disclosures.

KEY SEC RULEMAKING AREAS INCLUDE SPECIAL PURPOSE ACQUISITION COMPANY MERGERS, DISCLOSURES ABOUT CLIMATE-RELATED AND OTHER ESG MATTERS (E.G., BOARD DIVERSITY, HUMAN CAPITAL), AND CYBERSECURITY RISK GOVERNANCE.

Mandatory compliance date for recent SEC amendments to Regulation S-K

As a reminder, the SEC's November 19, 2020, amendments to Regulation S-K Items 303, MD&A, will be mandatory for fiscal year ending on or after August 9, 2021 (e.g., effective for an annual report for a year ending on or after September 30, 2021). The amendments add objectives to the requirements for MD&A and change or clarify the requirements for a number of items such as liquidity and capital resources, known trends and uncertainties, critical accounting estimates and off-balance sheet arrangements.

Registrants with off-calendar year-end dates should be mindful of the effective dates and prepare for timely compliance of the amended rules. Key considerations for audit committees may include the following:

Evaluate whether sufficient disclosures, both quantitative and qualitative, have been provided to help investors understand the impact of estimation uncertainty on a registrant's financial condition or operating results. To the extent material and reasonably available, such disclosure must include how much any critical accounting estimate has changed over a relevant period and a sensitivity analysis.

Review the discussion of a company's liquidity and capital resources and assess whether it includes descriptions of material cash requirements, their general purpose and the anticipated source of the funds needed to satisfy them. It also should assess whether sufficient discussions have been included to avoid a material loss of information for investors if the company chooses to eliminate the contractual obligation table.

If the company chooses to remove the selected quarterly financial data table, assess whether such removal is appropriate (e.g., whether there has been a material retrospective change affecting comprehensive income).

Questions for audit committees

- Does the company have sufficient controls and procedures over nonfinancial data? Is IA providing any type of audit coverage on ESG-related data or is the company obtaining any external assurance?
- In anticipation of CSA and SEC rulemaking on disclosure of ESG-related matters, what steps will be taken to evaluate and adopt processes and controls related to potential new disclosure requirements?
- What process does the audit committee have in place for regulatory updates and is the committee sufficiently engaged in dialogue providing views and input as needed on the related impacts?
- In light of the changing environment, what additional voluntary proxy disclosures might be useful to shareholders related to the audit committee's time spent on certain activities, such as cybersecurity, data privacy, business continuity, corporate culture and financial statement reporting developments?
- External auditors: were there material changes to materiality assessments, scope, physical inventory counts and the overall planned audit approach? Were there any "close calls" or areas that were particularly challenging as a result of the current environment and remote workforce? What additional procedures has the external auditor performed to gain comfort regarding key assumptions, estimates and prospective financial information? How has the engagement team considered the potential increase in errors due to work-from-home distractions or changes to the incentive, opportunity and rationalization of the fraud triangle? Has there been a reevaluation of key audit matters and how will auditor reporting requirements be impacted?

Questions for audit committees to consider

RISK MANAGEMENT

- How is the company using new technologies and data to enhance stress testing and scenario analyses to better prevent surprises and significant variability in operating performance?
- Do scenario analyses consider an appropriate range of extreme and even improbable scenarios, including existential threats? Do they incorporate the potential compounding effects of various risks?
- How can the organization build resilience while remaining lean and agile enough to respond to unforeseen risks? Are contingency and response plans related to risks, including cybersecurity and supply chain, periodically simulated and reviewed with the board?
- How is the company revisiting and adapting its risk management strategy and management's approach to the three lines model in response to potential changes in the external and internal environment, changes in strategy and risk landscape and the company's operating model?
- How is the company managing critical third-party and systemic risks, including those related to financial and operational resilience, IT security, data privacy, and the company's supply chain?
- Has the board considered how the organization's technology strategy is evolving, including how AI and other emerging technologies can be used to review and validate data and information to unearth insights into enterprise risks and opportunities?
- Have the company's information security measures and other controls been reviewed and adapted to be responsive to ongoing digital acceleration efforts, technology changes and the shifting business environment?
- How has the company's cybersecurity risk management program evolved to address the post-pandemic context, in which attackers are targeting a larger surface area and using increasingly unpredictable tactics? How is cybersecurity proactively integrated into all major strategy or tactical decisions, such as transactions, alliances, new products or services, and technology upgrades?

FINANCIAL REPORTING

- How is the organization proactively assessing opportunities to enhance stakeholder communications, including corporate reporting, to address changes in operations and strategies as well as changing stakeholder expectations?
- Have there been any material changes to internal controls over financial reporting or disclosure controls and procedures to address the changing operating environment? Have any cost saving initiatives and related efforts impacted resources or processes that are key in internal controls over financial reporting? If so, has management identified mitigating controls to address any potential gaps?
- What approach has management taken to consider multiple scenarios related to its projections and underlying assumptions that are expected to have a material impact on the results of operations or capital resources? Have there been material changes in controls and processes to evaluate the reasonableness of the assumptions and key estimates?
- Does the audit committee understand how management uses non-GAAP financial measures and how they supplement the GAAP financial statements?

Questions for audit committees to consider

TAX

- Did the organization use any COVID-19-related tax benefits in 2021? How were those benefits identified and documented?
- Has the organization reviewed its approach to tax controversy management in light of the ongoing pandemic and the shifting economic, trade and tax policy environment?
- What systems are in place to keep the organization informed of tax policy changes and related developments?
- Has the company performed modeling and scenario planning reflecting potential tax policy changes and trade developments?
- What role does tax play in the organization's ESG strategy?

REGULATORY DEVELOPMENTS

- Does the company have sufficient controls and procedures over nonfinancial data? Is internal audit providing any type of audit coverage on ESG-related data or is the company obtaining any external assurance?
- In anticipation of CSA and SEC rule-making on disclosure of ESG-related matters, what steps will be taken to evaluate and adopt processes and controls related to potential new disclosure requirements?
- What process does the audit committee have in place for regulatory updates and is the committee sufficiently engaged in dialogue providing views and input as needed on the related impacts?
- In light of the changing environment, what additional voluntary proxy disclosures might be useful to shareholders related to the audit committee's time spent on certain activities, such as cybersecurity, data privacy, business continuity, corporate culture and financial statement reporting developments?
- External auditors: were there material changes to materiality assessments, scope, physical inventory counts and the overall planned audit approach? Were there any "close calls" or areas that were particularly challenging as a result of the current environment and remote workforce? What additional procedures has the external auditor performed to gain comfort regarding key assumptions, estimates and prospective financial information? How has the engagement team considered the potential increase in errors due to work-from-home distractions or changes to the incentive, opportunity and rationalization of the fraud triangle? Has there been a re-evaluation of key audit matters and how will auditor reporting requirements be impacted?

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