

BASIS FOR CONCLUSIONS CANADIAN AUDITING STANDARD (CAS) 260, Communication with Those Charged with Governance

September 2009

This Basis for Conclusions has been prepared by staff of the Auditing and Assurance Standards Board (AASB). It relates to, but does not form part of, Canadian Auditing Standard (CAS) 260, *Communication with Those Charged with Governance*.

Background

In November 2006, the International Auditing and Assurance Standards Board (IAASB) issued its Exposure Draft of International Auditing Standard (ISA) 260 (Revised and Redrafted), *Communication with Those Charged with Governance* (ED-ISA 260). The IAASB approved final ISA 260 in September 2007 subject to confirmation by the Public Interest Oversight Board (PIOB) that due process was followed. This confirmation was received in December 2007.

In January 2007, the AASB issued its Exposure Draft to adopt proposed ISA 260 as CAS 260 (ED-CAS 260) to replace Section 5751, COMMUNICATION WITH THOSE HAVING OVERSIGHT RESPONSIBILITY FOR THE FINANCIAL REPORTING PROCESS. There were 11 respondents to ED-CAS 260 (identified below).

The AASB approved CAS 260 in January 2008. The Auditing and Assurance Standards Oversight Council reviewed due process followed by the AASB in the development of this CAS prior to its issuance in the CICA Handbook – Assurance.

Purpose of this Basis for Conclusions

This Basis for Conclusions has been prepared to make Canadian stakeholders aware of the following.

- (a) A Basis for Conclusions for ISA 260 prepared by IAASB staff is available on the IAASB web site, and provides information on how the IAASB dealt with comments received on significant matters in response to the ED-ISA 260.
- (b) Information on how the AASB dealt with significant matters arising from comments received in response to its ED-CAS 260 is also available. This information is set out below.

Significant Matters

AASB's Consideration of Amendments to ISA Wording

1. CAS 260 contains no amendment to the ISA wording.
References to the International Federation of Accountants' Code of Ethics
2. ED-CAS 260 proposed an amendment to the wording in ISA 260 to replace references to the International Federation of Accountants' *Code of Ethics* (IFAC Code) with references to relevant independence and other ethical requirements set out in rules of professional conduct / code of ethics applicable to the practice of public accounting issued by the various professional accounting bodies. No respondent raised an objection to the proposed amendment. In its final consistency review of all ISAs (including ISA 260), the IAASB removed the references to the IFAC Code and changed the wording to state that "the auditor is required to comply with relevant ethical requirements, including those pertaining to independence, relating to financial statement audit engagements." Accordingly, no amendment to the wording in ISA 260 was necessary in finalizing CAS 260.

Independence Communications

3. Some respondents suggested that the communication of independence should not be limited to listed entities. The IAASB considered this issue and concluded that extending the requirement for communication of independence beyond listed entities would not be appropriate as part of the clarity project but would be considered again when changes to the International Federation of Accountants' *Code of Ethics* have been finalized. The AASB supported the IAASB's decision on not expanding the requirement at this time. The AASB also noted that CAS 260 does not prohibit auditors from communicating their independence to non-listed entities other than listed entities and auditors may choose to do so as good practice.

Definition of Listed Entity

4. Some respondents suggested an amendment regarding the definition of "listed entity" since that definition would not necessarily conform to definitions in Canadian laws and regulations. The issue was discussed at the IAASB meeting and the IAASB concluded that the ISA is not meant to help auditors comply with or supersede national laws and regulations. Accordingly, definitions of certain terms in the ISA may differ from the definitions used in certain national laws or regulations. The ISAs and CASs recognize the need for auditors to comply with relevant laws and regulations. The AASB concurred with the IAASB's view on this issue.

Reporting Misstatements

5. Some respondents suggested that non-corrected errors should be communicated to those charged with governance. The IAASB questioned the practicality of a requirement to communicate material corrected misstatements that were brought to the attention of management as a result of audit procedures. The IAASB noted that such an approach would assume that complete financial statements are available when the audit starts, when in reality, preparing and auditing financial statements is an iterative process. For example, while management is preparing the financial statements, the auditor may detect a misstatement that the entity's internal controls would otherwise have identified later in the process. The IAASB discussed whether it is the corrected misstatement or the underlying weakness in internal control that allowed the misstatement to occur that is important to those charged with governance. The IAASB concluded that the requirement here should be to communicate material weaknesses in design, implementation or operating effectiveness of internal control that have come to the auditor's attention, rather than corrected misstatements. The AASB concurred with the IAASB's views on this matter.

Oral vs. Written Communication

6. One respondent expressed the view that for audits of listed entities, all matters should be communicated in writing. The IAASB believes that apart from matters regarding auditor independence and certain other matters specified in other auditing standards, it should be left to the auditor's professional judgment to determine which matters need to be communicated in writing and which may be communicated orally. Furthermore, the ISA contains specific requirements on documentation when the communication is made orally. The AASB concurred with the IAASB's views on this matter.

Establishing a Mutual Understanding with Those Charged with Governance

7. A respondent suggested that the wording in paragraph 14, "the auditor shall communicate with those charged with governance the form, timing and expected general content of communication" does not seem appropriate as it would require the auditor to communicate what he or she is going to communicate. The respondent suggested that the requirement be reworded to "the auditor shall seek to establish with those charged with governance a mutual understanding of the form, timing and expected content of communication."
8. The IAASB considered this matter and concluded that the wording in paragraph 14 is appropriate because:
- (a) "shall seek to establish ... a mutual understanding ..." is too weak a requirement; and
 - (b) the auditor cannot be made responsible for the actions of those charged with governance and, therefore, the requirement cannot state "shall establish ... a mutual understanding ..." as this involves an action by those charged with governance. The AASB concurred with the IAASB's views on this matter.

Communications with Smaller Entities

9. Some respondents suggested that CAS 260 seems to contain too many requirements in the context of communications with smaller entities. The AASB concluded that the requirements are appropriate in the context of communications with smaller entities. The AASB also noted that CAS 260 provides guidance that in the case of audits of smaller entities, the auditor would communicate in a less structured manner with those charged with governance than in the case of listed or larger entities.

Other Suggested Amendments

10. Some respondents suggested that CAS 260 include amendments from the wording in ISA 260 to deal with matters that include:
- sample independence letters;
 - hierarchy of relevant persons to communicate; and
 - various specific matters to be communicated.
11. The AASB considered whether amendments relating to one or more of these suggestions would meet the AASB's criteria for amendments and concluded that its criteria would not be met. In particular, the AASB concluded that there are no circumstances relating to these matters particular to the Canadian environment where such amendments would be required to serve the Canadian public interest or maintain the quality of auditing and reporting in Canada.

Other Matters

None.

List of Respondents to ED-CAS 260

BDO Dunwoody LLP

Browning Milgram LLP

Canadian Public Accountability Board

Deloitte & Touche LLP

Institute of Chartered Accountants of British Columbia

Malinsky & Associates

Office of the Auditor General of Canada

Ordre des comptables agréés du Québec

Provincial Auditor Saskatchewan

Vérificateur général du Québec Ville de Montréal – Bureau du vérificateur général

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