

Audit and Assurance Alert

CANADIAN AUDIT STANDARDS (CAS)

JUNE 2021

The Consideration of Climate-Related Risks in an Audit of Financial Statements

This publication has been prepared to highlight areas of focus related to the consideration of climate-related risks when conducting an audit of financial statements in accordance with the Canadian Auditing Standards (CAS). This publication does not amend or override the CAS, the texts of which alone are authoritative. Reading this publication is not a substitute for reading the CAS.

What Is the Purpose of This Publication?

This Audit and Assurance Alert (*Alert*) is intended to help auditors understand what already exists in the CAS today and how that material relates to the auditor's consideration of climate-related risks in an audit of financial statements.

This *Alert* is based on *The Consideration of Climate-Related Risks in an Audit of Financial Statements* of the International Auditing and Assurance Standards Board (IAASB), published by the International Federation of Accountants in October 2020 and is used with permission of IFAC.

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Focus on Climate Change

Climate change is a topic which is increasingly front of mind for investors and other stakeholders as the effects of climate change are increasingly visible and because climate change has the potential to impact an increasing number of entities of all nature and sizes. Today, climate change affects businesses in various industries as global and local policy actions around climate change continue to evolve, and given the growing demand by investors for climate-related information for their economic decision making. For example, climate-related events or conditions may impact an entity in terms of its business model, its operations and processes, and its ability to raise finance or attract investment and customers.

While the phrase “climate change” does not feature in the CAS, the CAS require that the auditor identifies and assesses the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for the auditor’s opinion. Depending on the facts and circumstances of an entity, climate-related events or conditions may contribute to the susceptibility to misstatement of certain amounts and disclosures in an entity’s financial statements. The term “climate-related risks” is used in this *Alert* for ease of reference.

Support Materials for Entities and Their Auditors

In April 2019, the Australian Accounting Standards Board and Auditing and Assurance Standards Board issued a joint bulletin, [*Climate-related and other emerging risks disclosures: assessing financial statement materiality using AASB/IASB Practice Statement 2*](#). The focus of that publication was to illustrate how qualitative external factors, such as the industry in which the entity operates, and investor expectations may make climate-related risks “material” and warrant disclosure in the financial statements, regardless of their numerical impact. Subsequently, the International Accounting Standards Board (IASB) published [*IFRS Standards and climate-related disclosures*](#). This publication gives an overview of how the International Financial Reporting Standards (IFRS) address climate and other emerging risks. In addition, several climate-related disclosure frameworks have emerged across different jurisdictions in an effort to meet the growing demand for climate-related information.

The publication of these (and other) support materials and frameworks brings into view the need for additional guidance to address how auditors could be expected to consider and understand the implications of climate-related risks when auditing financial statements.

Scope of This *Alert*

This *Alert* focuses on the implications of climate-related risks for audits of financial statements conducted in accordance with CAS, i.e., the auditor expressing an opinion whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Climate change is an area of increasing concern and priority for investors which may affect how investors perceive climate-related risks in the entity’s financial statements



The majority of climate-related information is currently disclosed outside the financial statements of entities, for example, in management commentary intended to complement the financial statements, or as part of an entity’s sustainability information or corporate social responsibility reporting. In the context of an audit of financial statements, the auditor may have a responsibility in relation to such information in accordance with CAS 720¹ – which is highlighted in this publication. However, separate assurance engagements over information other than an entity’s financial statements or historical financial information, such as those that may be conducted in accordance with CSAE 3000² and CSAE 3001 are not addressed in this publication.



Entities That May Be Affected

Most, if not all entities, are likely to be impacted by climate change; directly or indirectly. Industries that are more likely to be directly affected by climate change include, for example, financial services (including banks and insurance groups), energy, transportation, construction, primary producers, agriculture and forestry industries.

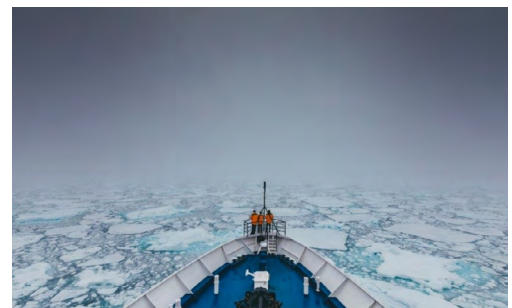
Other entities may be indirectly affected as climate change may affect supply chains, customers, financing, insurance and laws and regulations. For example, rising temperatures and droughts may affect coffee production and because of that, coffee will become increasingly difficult to grow and more expensive, impacting all entities buying and selling coffee.

Therefore, all entities need to consider what type of climate-related risks their businesses could be exposed to in the long-run.

What Are Management’s Responsibilities?

Management is responsible for preparing the financial statements of the entity in accordance with the applicable financial reporting framework.

Financial reporting frameworks have requirements that address the recognition and measurement of items in the financial statements (e.g., assets, liabilities, income, expenses and cash flows), as well as requirements for related disclosures. Management is required to make materiality judgments in preparing an entity’s financial statement.



¹ CAS 720, *The Auditor’s Responsibilities Relating to Other Information*

² Canadian Standards on Assurance Engagements (CSAE) 3000, *Attestation Engagements Other than Audits or Reviews of Historical Financial Information* and CSAE 3001, *Direct Engagements*

Financial reporting frameworks often discuss the concept of materiality in the context of the preparation and presentation of financial statements and user decision-making. If information, such as climate change, can affect user decision-making, then this information should be deemed as “material” and warrant disclosure in the financial statements, regardless of their numerical impact.

Currently, there is no mandatory international framework for reporting climate-related risks. However, there is growing support for climate-related financial reporting, generally within the financial statements or associated with the other information. Also, given the importance of climate-related risks to investors’ economic decision-making,³ entities may need to consider such risks in the context of their financial statements rather than solely as a matter of corporate social responsibility reporting or sustainability reporting.

For more information about the financial reporting implications of climate change risks in the context of IFRS, refer to the IASB publication *IFRS Standards and climate-related disclosures*.

What Are the Auditor’s Responsibilities?

The auditor’s objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement to enable the auditor to report on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.⁴ If climate change impacts the entity, the auditor needs to consider whether the financial statements appropriately reflect this in accordance with the applicable financial reporting framework (i.e., in the context of risks of material misstatement related to amounts and disclosures that may be affected depending on the fact and circumstances of the entity). Auditors also need to understand how climate-related risks relate to their responsibilities under professional standards, and applicable law and regulation. The next section highlights the auditor’s consideration of climate-related risks in respect of those CAS that are likely to be most relevant.

Which CAS May Be Most Relevant in Relation to Climate-Related Risks?

The tables below address some of the more significant areas that may need to be considered in relation to risk assessment and responses to assessed risks, audit evidence, and communication with those charged with governance and auditor reporting.

- 3 Examples include:
- The recommendations of the Financial Stability Board’s (FSB) [Task Force on Climate-related Financial Disclosures \(TCFD\)](#) have been endorsed by over 1,000 companies representing a combined market capitalization of over USD 12 trillion and USD 138.8 trillion assets under management.
 - [Climate Action 100+](#) sign on statement has been signed by more than 500 investors, who collectively manage more than USD 47 trillion in assets under management. Among other matters, the statement calls for enhanced corporate disclosures in line with the TCFD’s recommendations.
 - In 2018, [seven investor organizations](#) representing hundreds of investors worldwide with trillions of dollars in assets under management called for improved climate-related financial reporting.
 - In 2020, [CalPERS, Schroders and DWS](#) (over USD 1.9 trillion assets under management) asked companies and auditors to disclose climate-related risks in the financial statements and the auditor’s report, respectively, after British Petroleum disclosed climate-related risks in the financial statements and the auditor included a key audit matter in the auditor’s report.
 - In 2020, [investor groups](#) representing over USD 100 trillion of assets under management are calling out for information on the financial impact that climate change will have on companies.
- 4 CAS 200, *Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Canadian Auditing Standards*, paragraph 11



Risk Assessment and Responses to Assessed Risks

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 315, <i>Identifying and Assessing the Risks of Material Misstatement</i></p>	<p>In applying CAS 315,⁵ the auditor may consider the implications of climate-related risks when obtaining an understanding of the entity and its environment, including:</p> <ul style="list-style-type: none"> • The entity’s business model. Whether climate-related risks influence, or will influence, the entity’s business model, including the entity’s supply chain. When the entity’s structure includes subsidiaries, divisions or branches (i.e., a group), the auditor’s understanding of climate-related risks extends to the components within that group. In addition, the auditor may obtain an understanding of how management and those charged with governance consider the effects of climate-related risks.⁶ • Industry factors. Industry factors include industry conditions such as the competitive environment, supplier and customer relationships, and technological developments. Whilst the impact of climate change is entity dependent, industry factors are still an important consideration in respect of climate change. For example, new technological developments to address climate change may have a significant impact on the industry and in turn, the entity subject to audit. • Regulatory factors. The regulatory environment encompasses, among other matters, the legal and political environment and any changes thereto. Governments may change climate-related laws and regulations that could affect taxation or the entity’s business model through increased environmental requirements. For example, many governments have committed to meet the goals of the Paris Agreement and New Zealand’s government announced that it will mandate climate-related risks disclosures for banks, asset managers and insurers. • Other external factors. This may include the general economic conditions, interest rates and availability of financing, commodity prices and inflation or currency revaluation. For example, entities seeking financing may be impacted by banks’ lending decisions based on climate-related risks as banks may consider how the exposure to climate related risk affects the expected credit losses of its loans and investments. If a bank’s loan portfolio has significant exposure to, for example, fossil fuel-intensive projects, the bank may take into account increased regulatory risk or changing consumer preferences in making lending decisions.

⁵ The new CAS 315 including paragraph 19. CAS 315 is effective for audits of financial statements for periods beginning on or after December 15, 2021. Prior to this date, the previous CAS 315 standard, *Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment*, is applicable. References in this document are to the new CAS 315.

⁶ The United Kingdom Financial Reporting Council’s Financial Reporting LAB noted in its publication [Climate-related corporate reporting: Where to next?](#) that investors are interested in how Boards consider and assess climate-related issues.

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 315, Identifying and Assessing the Risks of Material Misstatement (continued)</p>	<p>With respect to the entity’s system of internal control, the auditor is required to obtain an understanding of, among other components of the system, the entity’s risk assessment process relevant to the preparation of the financial statements.⁷ Climate change may factor into understanding the entity’s process for identifying climate-related business risks relevant to its financial reporting objectives, assessing the significance of such risks (including the likelihood of their occurrence) and addressing the risks.</p> <p>Based on the risk assessment procedures, the auditor is required to identify and assess the risks of material misstatement at the financial statement level and at the assertion level for classes of transactions, account balances and disclosures.⁸ Climate-related risks may give rise to risks of material misstatement in respect of one or more relevant assertions, for example, accuracy, valuation and allocation, rights and obligations, and presentation for a class of transaction, account balance or disclosures.</p>
<p>CAS 320, Materiality in Planning and Performing an Audit</p>	<p>Climate-related risks may affect the auditor’s determination of materiality and performance materiality in accordance with CAS 320. For example, the standard recognizes that:</p> <ul style="list-style-type: none"> • The auditor’s determination of materiality is a matter of professional judgment and is affected by the auditor’s perception of the financial information needs of users of the financial statements.⁹ Given that some investors have specifically identified climate-related risks as being used in their economic decision-making, auditors of entities that are affected by climate-related risks may need to take that into account when determining materiality. • If the applicable financial reporting framework discusses the concept of materiality in the context of the preparation and presentation of financial statements, this provides a frame of reference to the auditor in determining materiality for the audit.¹⁰ In this regard, the IASB’s publication <i>IFRS Standards and climate-related disclosures</i> and IFRS Practice Statement 2, <i>Making Materiality Judgements</i> may provide additional guidance relevant to the auditor’s determination of materiality. • When considering whether misstatements in qualitative disclosures could be material, one of the factors that the auditor may consider is whether the qualitative disclosures are important to users of the financial statements because of the nature of an entity.¹¹ Climate-related risk disclosures may be important to users of the financial statements of entities that are affected by such risks. In this regard, the auditor may need to consider, for example, whether and how management has evaluated climate-related risks in their impairment assessments, and how climate-related risks have affected other judgments made in relation to the recognition or measurement of items in the financial statements.

7 CAS 315, paragraphs 22 and 23

8 CAS 315, paragraphs 28 to 37

9 CAS 320, paragraphs 4, 10 and 11

10 CAS 320, paragraphs 2 and 3

11 CAS 320, paragraph A2

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 330, <i>The Auditor’s Responses to Assessed Risks</i></p>	<p>CAS 330 requires the auditor to design and perform further audit procedures whose nature, timing and extent are based on, and are responsive to, the assessed risks of material misstatement at the assertion level.¹² Furthermore, the standard requires the auditor to conclude whether sufficient appropriate audit evidence has been obtained (also see guidance in relation to CAS 700¹³ below).¹⁴</p> <p>If the effects of climate-related risks form part of the reasons for the assessment given to the risk of material misstatement at the assertion level, the auditor’s further audit procedures are required to be responsive to these risks. The auditor shall obtain more persuasive audit evidence the higher the assessment of risk.¹⁵</p>
<p>CAS 250, <i>Consideration of Laws and Regulations in an Audit of Financial Statements</i></p>	<p>In addition to laws and regulations that have a direct effect on the determination of material amounts and disclosures in the financial statements (e.g., tax and pension laws and regulations), the auditor also has responsibilities in relation to other laws and regulations that do not have a direct effect on the determination of the amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operating aspects of the business, to an entity’s ability to continue its business, or to avoid material penalties.¹⁶</p> <p>The auditor is required to perform audit procedures to help identify instances of non-compliance with other laws and regulations that may have a material effect on the financial statements.¹⁷ In the case of climate-related risks, other laws and regulations may include environmental regulations. A breach of such regulations may have a material effect on the financial statements, e.g., a breach may result in a contingent liability for potential litigation and fines or penalties resulting from those regulations.</p>
<p>CAS 450, <i>Evaluation of Misstatements Identified during the Audit</i></p>	<p>CAS 450 requires the auditor to accumulate misstatements identified during the audit and, for uncorrected misstatements, the auditor is required to determine whether such misstatements are material, individually or in aggregate.¹⁸ In this determination the auditor takes into account that the circumstances related to some misstatements may cause the auditor to evaluate them as material, individually or when considered together with other misstatements accumulated during the audit, even if they are lower than materiality for the financial statements as a whole.¹⁹ Circumstances that may affect the evaluation include the extent to which the misstatement:</p>

12 CAS 330, paragraph 6

13 CAS 700, *Forming an Opinion and Reporting on Financial Statements*

14 CAS 330, paragraphs 25 to 27

15 CAS 320, paragraph 7

16 CAS 250, paragraph 6

17 CAS 250, paragraph 15

18 CAS 450, paragraphs 5 and 11

19 CAS 450, paragraph A21

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 450, Evaluation of Misstatements Identified during the Audit (continued)</p>	<ul style="list-style-type: none"> • Is an omission of information not specifically required by the applicable financial reporting framework but which, in the judgment of the auditor, is important to users' understanding of the financial position, financial performance or cash flows of the entity. For example, disclosures of sources of estimation uncertainty that fail to include climate-related risks in cases when it impacts the carrying amount of assets or liabilities. This may be the case for climate-related information, given investor statements on the importance of climate-related risks to their decision-making; or • Affects other information to be included in the entity's annual report that may reasonably be expected to influence the economic decisions of the users of the financial statements (also see guidance on CAS 720 below). This may be the case for climate-related information, given that the majority of climate-related information is currently disclosed outside the financial statements.



Audit Evidence

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 540, Auditing Accounting Estimates and Related Disclosures</p>	<p>Given the facts and circumstances of an entity, climate-related risks may have an impact on the entity's accounting estimates. Examples of accounting estimates often affected include:</p> <ul style="list-style-type: none"> • Impairment of property, plant and equipment, intangible assets and goodwill • Fair value of financial assets (investments and receivables) • Fair value of financial liabilities • Certain provisions and contingent liabilities • Mineral resources and reserves <p>With respect to climate-related risks, matters that the auditor may take into account in auditing accounting estimates include the following:</p> <p>Risk Assessment Procedures and Related Activities²⁰</p> <ul style="list-style-type: none"> • Regulatory factors, for example, governments may change climate-related laws and regulations that could affect the entity's cash flows and the recoverable amount of the entity's assets. • Whether management has assessed the continued use of previous methods, assumptions and data, and if not, whether the methods, assumptions and data used remain appropriate. For example, insurance entities may need to update their future claim models for the effects of changes in weather patterns and property valuers may need to update their valuation models for climate-related risks.

²⁰ CAS 540, paragraph 13

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 540, Auditing Accounting Estimates and Related Disclosures (continued)</p>	<p>Identifying and Assessing the Risks of Material Misstatement²¹</p> <ul style="list-style-type: none"> • The degree to which the accounting estimate is subject to estimation uncertainty may be impacted because of climate change. For example, climate change may: <ul style="list-style-type: none"> – Make it harder to make precise and reliable predictions about the future realization of a past transaction or about the incidence and impact of future events or conditions (e.g., the frequency of extreme droughts impacting harvests). – Affect the business environment in certain industries dramatically. Governments may discourage or restrict the use of fossil fuel energy, require entities to reduce their carbon dioxide emissions or encourage the use of sustainable energy sources. • The degree to which the accounting estimate is subject to complexity may be affected by climate change because: <ul style="list-style-type: none"> – New models may need to be developed to capture the effects of the changing climate. This may require the use of specialized skills or knowledge by management. – It may be more complex to derive data on which the accounting estimate is based due to the need to incorporate data from outside of the traditional accounting system. For example, a pension fund investing in a portfolio may rely on information disclosed by its investees. If those investees do not make adequate climate-related disclosures, it may be more complex to derive other data on which to base the accounting estimate. • The degree to which the accounting estimate is subject to subjectivity may be affected by climate change. This may particularly be the case for: <ul style="list-style-type: none"> – Assumptions with long forecast periods – Assumptions based on data that is currently unobservable – Balances where it is difficult to make reliable forecasts about the future <p>The IASB's publication <i>IFRS Standards and climate-related disclosures</i> also includes examples of accounting estimates that could be affected by climate change.</p>

²¹ CAS 540, paragraph 16

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 540, Auditing Accounting Estimates and Related Disclosures (continued)</p>	<p>Responding to the Assessed Risks of Material Misstatement²²</p> <ul style="list-style-type: none"> • When the auditor’s further audit procedures include testing how management made the accounting estimate or developing an auditor’s point estimate or range, such procedures are required to address, among other matters: <ul style="list-style-type: none"> – Whether the data is appropriate in the context of the applicable financial reporting framework and whether the data is relevant and reliable in the circumstances. For example, climate-related data may not be subject to the same internal control processes as accounting data, and the auditor needs to consider the relevance and reliability of such data.²³ – Whether significant assumptions are appropriate in the circumstances and in the context of the applicable financial reporting framework. Examples of how climate-related risks affect assumptions include: <ul style="list-style-type: none"> • The estimated useful lives of assets may change and therefore the amount of depreciation or amortization recognized each year. • Future estimated cash inflows and outflows used for recoverable amount calculations may change. • Valuation reports may need to take into account the effects of climate change.
<p>Disclosures (various CAS, including CAS 330 and CAS 540)</p>	<p>The auditor’s further audit procedures are required to be responsive to the assessed risks of material misstatement at the assertion level, considering the reasons for the assessment given to those risks.²⁴ This may include the effects of climate-related risks on the presentation of assets and liabilities and their related disclosures. With respect to accounting estimates, the auditor is required to design and perform further audit procedures to obtain sufficient appropriate audit evidence about disclosures related to accounting estimates, including disclosures in the financial statements about estimation uncertainty.²⁵</p> <p>Among other matters, disclosures help users of the financial statements understand the nature and extent of volatility and estimation uncertainty in the relevant amounts where the variables are difficult to predict. Even though the majority of climate-related information is currently disclosed outside the financial statements, it is expected that more and more climate-related disclosures will be included in the financial statements because of the increasing impact of climate-related risks on entities’ financial statements and the interest of investors therein.</p>

22 CAS 540, paragraphs 22 to 29

23 CAS 540, paragraph A107

24 CAS 330, paragraphs 6 and 7

25 CAS 540, paragraphs 26(b), 29(b) and 31

CAS Standard	Effect on Auditing Financial Statements
<p>Disclosures (various CAS, including CAS 330 and CAS 540) (continued)</p>	<p>The IASB's publication <i>IFRS Standards and climate-related disclosures</i> highlights, among other matters, requirements that may be relevant to climate-related disclosures. For example:</p> <ul style="list-style-type: none"> • IAS 1²⁶ requires disclosure in the notes of information that is not presented elsewhere in the financial statements but is relevant to an understanding of them. Information will be relevant if it could reasonably be expected to influence decisions made by investors. For example, a company may need to explain whether and how it has considered climate-related risks in its impairment calculations even though IAS 36²⁷ makes no requirement for such a disclosure. • IFRS 7²⁸ requires disclosure of the entity's exposure to market risks arising from financial instruments, its objectives in managing these risks and changes from the previous period. In relation to climate-related risks, this may affect investment funds and insurance entities as they could hold investments in industries that may be affected by climate-related risk and they would therefore be exposed to price risk in relation to these investments. Quantitative information, such as an analysis of investments by industry or sector, could specifically identify sectors exposed to climate-related risks and explain the entity's policy of managing its exposure to those sectors. • IFRS 13²⁹ requires companies to disclose key assumptions used where assets are recognized at fair value. When the fair value of an asset is affected by climate-related risks including the effect of and potential changes to laws and regulations with respect to managing such risks, a company may need to disclose how it factors climate-related risk into the calculations.
<p>CAS 620, Using the Work of an Auditor's Expert</p>	<p>Auditors of entities that are affected by climate-related risks may determine that the engagement team requires specialized skills or knowledge to appropriately identify and assess the risks of material misstatement or to respond to assessed risks. If expertise in a field other than accounting or auditing is necessary to obtain sufficient appropriate audit evidence, the auditor is required to determine whether to use the work of an auditor's expert.³⁰ For example, the auditor of an entity in an extractive industry may use the work of an auditor's expert to help calculate the provision recognized for decommissioning a plant or rehabilitating environmental damage due to regulatory changes or shortened project lives.</p>

26 International Accounting Standard (IAS) 1, *Presentation of Financial Statements*

27 IAS 36, *Impairment of Assets*

28 IFRS 7 *Financial Instruments: Disclosures*

29 IFRS 13 *Fair Value Measurement*

30 CAS 620, paragraph 7

CAS Standard	Effect on Auditing Financial Statements
CAS 570, <i>Going Concern</i>	<p>CAS 570 deals with the auditor’s responsibilities in the audit of financial statements relating to going concern and the implications for the auditor’s report and includes guidance if events or conditions have been identified that may cast significant doubt on the entity’s ability to continue as a going concern.³¹</p> <p>There may be certain instances when a climate-related risk could give rise to an event or condition that may cast significant doubt on the entity’s ability to continue as a going concern. For example:</p> <ul style="list-style-type: none"> • The effects of extreme weather events may be higher than before and may be relevant to the appropriateness of management’s going concern assumption. • Some entities face the risk of significant litigation claims which may impact the entity’s ability to continue its operations for the foreseeable future.



Communication with Those Charged with Governance and Auditor Reporting

CAS Standard	Effect on Auditing Financial Statements
CAS 260, <i>Communication with Those Charged with Governance</i>	<p>The auditor is required to communicate with those charged with governance, among other matters, the auditor’s views about significant qualitative aspects of the entity’s accounting practices, including accounting policies, accounting estimates and financial statement disclosures.³² For entities affected by climate change, this may include the effects of climate-related risks on these aspects.</p> <p>Such communications may include the appropriateness of the accounting policies to the particular circumstances of the entity, having regard to the need to balance the cost of providing information with the likely benefit to users of the entity’s financial statements.³³ It may also be relevant to draw attention to information on accounting policies used by similar entities in similar circumstances.</p>
CAS 700, <i>Forming an Opinion and Reporting on Financial Statements</i>	<p>CAS 700 requires the auditor to form an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.³⁴ This would include, as applicable, disclosures in the financial statements in relation to climate-related risks and any financial impact reflected in the financial statements.</p>

31 CAS 570, paragraph 1

32 CAS 260, paragraphs 16(a), A19 to A20 and Appendix 2

33 CAS 260, Appendix 2

34 CAS 700, paragraph 10

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 700, <i>Forming an Opinion and Reporting on Financial Statements</i> (continued)</p>	<p>In forming an opinion, the auditor is required to conclude whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, taking into account, among other matters, the auditor’s conclusion, in accordance with CAS 450, whether uncorrected misstatements are material, individually or in aggregate.³⁵ Climate-related risks that could give rise to material misstatements (if uncorrected), may relate to:</p> <ul style="list-style-type: none"> • Appropriateness or adequacy of disclosures. For example, the entity may not have appropriately disclosed the effect of climate-related risks in the financial statements while the decisions of users of the financial statements are likely to be affected by such disclosures. • Application of the entity’s accounting policies. For example, inappropriate recognition and measurement of assets because the related impairment calculations do not appropriately account for the effect of climate-related risks. <p>If the auditor concludes that, based on the audit evidence obtained, the financial statements as a whole are not free from material misstatement, the auditor is required to modify the opinion in the auditor’s report in accordance with CAS 705.³⁶</p>
<p>CAS 701, <i>Communicating Key Audit Matters in the Independent Auditor’s Report</i></p>	<p>When CAS 701 applies,³⁷ the auditor is required to determine key audit matters to be communicated in the auditor’s report (i.e., those matters that, in the auditor’s professional judgment, were of most significance in the audit of the financial statements of the current period).³⁸</p> <p>The degree to which climate-related risks require auditor attention in performing the audit, may result in determining such a matter to be a key audit matter. The auditor’s determination of matters that required significant auditor attention may be affected by the following:³⁹</p> <ul style="list-style-type: none"> • Significant auditor judgments. For example, for an entity in the energy sector, an area of significant auditor judgment may be around the potential impact of climate change and the transition to renewable energy sources, which may impact property, plant and equipment, goodwill, intangible assets and provisions. • Specific events or transactions. For example, there may be changes to laws and regulations with respect to the use of fossil fuels. This may significantly impact an entity in the transportation industry as these changes could affect the recoverable amount of the entity’s long-life assets.

35 CAS 700, paragraph 11

36 CAS 705, *Modifications to the Opinion in the Independent Auditor’s Report*, paragraph 6(a)

37 CAS 701, paragraph 5

38 CAS 701 paragraphs 8 to 10

39 CAS 701, paragraph 9

CAS Standard	Effect on Auditing Financial Statements
<p>CAS 720, The Auditor's Responsibilities Relating to Other Information</p>	<p>CAS 720 requires the auditor to read and consider the financial or non-financial information (other than the financial statements and the auditor's report thereon) included in an entity's annual report (i.e., other information).⁴⁰ Other information varies between jurisdictions and may include documents such as a management report, management commentary, operating and financial review, chairman's statement, corporate governance statement or internal control and risk assessment reports.⁴¹</p> <p>The majority of climate-related information is currently disclosed in other information. In reading the annual report, the auditor is required to consider whether there is a material inconsistency between:⁴²</p> <ul style="list-style-type: none"> • The other information, including any climate-related information contained therein, and the financial statements, and • The other information, including any climate-related information contained therein, and the auditor's knowledge obtained in the audit. <p>Material inconsistencies between the other information and the financial statements may indicate that there is a material misstatement of the financial statements or that a material misstatement of the other information exists. For example, the entity may include in the other information a scenario analysis that shows the potential future effects of climate change and related issues on the entity's operations. When such analysis shows that the entity could be significantly affected by climate change and the disclosures in the financial statements do not appropriately highlight this (i.e., in applying the requirements of the applicable financial reporting framework), it may indicate that there is a material misstatement of the financial statements or that a material misstatement of the other information exists (also see guidance on CAS 450 above).</p> <p>Determining the nature and extent of procedures to be performed with respect to other information is a matter of professional judgment.⁴³ The procedures may include:</p> <ul style="list-style-type: none"> • For climate-related information that is intended to be the same as information in the financial statements, comparing the information to the financial statements. • For climate-related information intended to convey the same meaning as disclosures in the financial statements, comparing the words used and considering the significance of differences in wording used and whether such wording could be interpreted differently than that disclosed in the financial statements. <p>The auditor is also required to remain alert for indications that the other information, not related to the financial statements or the auditor's knowledge obtained in the audit, appears to be materially misstated.⁴⁴</p>

40 CAS 720, paragraphs 12(a), 12(c) and 14

41 CAS 720, paragraphs A1 to A3

42 CAS 720, paragraphs 14(a) and 14(b)

43 CAS 720, paragraph A28

44 CAS 720, paragraphs 15

CAS Standard	Effect on Auditing Financial Statements
CAS 720, The Auditor’s Responsibilities Relating to Other Information (continued)	When climate-related information is presented in a document outside a document titled “annual report,” it may be important to determine whether the document containing the climate-related information nevertheless forms part of the annual report as defined for purposes of CAS 720. An example of a document which is not always part of the annual report is a sustainability report, which some jurisdictions are seeing an increase in entities issuing.

Other Resources

Other resources that the auditor may find useful include:

- IASB’s publication: [IFRS Standards and climate-related disclosures](#)
- Australian Accounting Standards Board and Auditing and Assurance Standards Board’s joint bulletin: [Climate-related and other emerging risks disclosures: Assessing financial statement materiality using AASB/IASB Practice Statement 2](#)
- The United Kingdom’s Financial Reporting Council’s Financial Reporting LAB’s publication: [Climate-related corporate reporting: Where to next](#)
- Institute of Chartered Accountants in England and Wales’ publication: [Reporting on climate risks and opportunities: A practical guide to the recommendations of the task force on climate-related financial disclosures](#)
- International Public Sector Accounting Standards Board’s staff questions and answers: [Climate change: Relevant IPSASB guidance](#)
- ClientEarth publication: [Risky business: Climate change and professional liability risks for auditors](#)
- International Federation of Accountants’ (IFAC) Point of View: [Climate Action](#)
- IFAC’s call for a [New Sustainability Standards Board alongside the IASB](#)

In December 2015, the FSB established the [Task Force on Climate-Related Financial Disclosures \(TCFD\)](#) to develop climate-related financial disclosures that could be voluntarily applied by preparers, to assist investors, lenders, and other stakeholders in understanding material risks. In June 2017, the Task Force provided a framework for companies and other organizations to develop more effective climate-related financial disclosures through their existing reporting processes. See the [TCFD’s website](#) for more information.

Feedback

If you have comments on this *Audit & Assurance Alert* or suggestions for future *Alerts*, please send them to:

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