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British Columbia Securities Commission
Manitoba Securities Commission
Securities Administration Branch, New Brunswick
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Department of Justice, Government of the Northwest Territories
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Registrar of Securities, Legal Registries Division, Department of Justice, Government of Nunavut
Ontario Securities Commission
Office of the Attorney General, Prince Edward Island
Commission des valeurs mobilieres du Quebec
Saskatchewan Securities Commission
Registrar of Securities, Government of Yukon

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Canadian Securities Administrators' Notice and Request for Comments on Proposals for a Harmonized Set of Continuous Disclosure Requirements

This letter expresses Accounting Standards Board (AcSB) staff comments on the proposed National Instruments and Companion Policy published on June 21 2002 as they relate to financial

accounting and financial statements. We understand that other groups within the CICA will be submitting comments on MD&A and assurance matters.

1. The use of US GAAP by Canadian companies, and reconciliation with Canadian GAAP (National Instrument 51-102, paragraphs 4.7 (2) and (3))

We accept that Canadian companies that are SEC registrants should be free to file financial statements prepared in accordance with US GAAP, rather than Canadian GAAP. However, we are concerned with the proposal to require no reconciliation with Canadian GAAP after a two-year transition period. We believe that a well-prepared reconciliation has important information value for external users that more than justifies companies' preparation costs. Further, these preparation costs are declining as unjustifiable differences between Canadian and US standards are being eliminated. The following briefly outlines the major considerations that we believe should be taken into account. We would be pleased to discuss these issues with representatives of the Canadian Securities Administrators.

(a) The mandate of the Accounting Standards Board (AcSB) is to develop and maintain accounting standards that reflect the best of US and international (IASB) standards. Under this mandate the AcSB is pledged to eliminate all significant differences with US GAAP, except where there is clear international agreement on a superior alternative to US GAAP (with superior information value for Canadian users) or in rare situations where there are unique Canadian circumstances that are not recognized by US GAAP. A determination to adopt a standard that differs from US GAAP is only taken after extensive study, due diligence, and an open process of consultation and exposure of proposals for public comment. Permitting a very important class of Canadian companies to adopt US GAAP with not even reconciliation accountability under Canadian GAAP could signal a lack of confidence in the usefulness and information value of Canadian GAAP and in the Canadian accounting standard setting process.

(b) Substantial progress has been made in eliminating significant unjustifiable differences with US GAAP. Recent examples include income taxes,[1] employee future benefits, interim financial statements, earnings per share, business combinations,[2] and foreign currency translation. In addition, current projects are underway to harmonize Canadian standards with those of the US on accounting for financial instruments and asset impairment.

(c) Looking to the future, significant unavoidable differences with US GAAP can be expected to be largely limited to a few matters of substance. Information on these differences and their effects can be expected to have information value to Canadian investors and other stakeholders in Canadian companies. It would be unfortunate if certain of Canada's largest and most prominent companies could avoid accountability under Canadian GAAP for at least a clear explanation and reconciliation of such differences. To take an example,

[1] The one significant difference that remains relates to the date that new tax legislation is considered to be effective for accounting purposes. Due to differences in legislative processes in the two countries the FASB rule does not yield sensible results in Canada.

[2] In this case a Canadian standard in place for many years was recognized world wide as being superior to the complex, but much more lenient, series of rules in place in the US. Recently, convergence was reached with the FASB, IASB, and several other prominent national standard setters on a common standard that is very close to the pre-existing Canadian requirements.

suppose that international agreement is reached, and an IASB standard issued, for expensing employee stock options at their fair value when granted, but that this requirement could not be put in place in the US, or is long delayed, for political or other reasons in that country. The AcSB could determine, with appropriate due process, that this accounting should be required under Canadian GAAP. It would seem unfortunate if a Canadian SEC registrant could report under US GAAP without explanation and reconciliation of the effects of such a difference with Canadian GAAP.

(d) It is to be hoped that US GAAP will be converged with international standards over time, so that the AcSB will have little need to consider differing from US GAAP. But this will depend on the success of FASB and international efforts to converge US and IASB standards. It is to be recognized that the IASB is charged with coordinating efforts with national standard setters to converge national standards to one universal set of (IASB) standards. The IASB is now a powerful and well-resourced body that could move out front of the FASB in developing some important improvements in accounting standards.

(e) A major concern in the past has been that the preparation of reconciliations can place an intolerable cost burden on Canadian companies and put them at a competitive disadvantage with their US peers. We are not aware of any rigorous evidence that the preparation of reconciliations to Canadian GAAP, after having prepared US GAAP financial statements, involves a major incremental cost that could adversely affect its competitive position. Moreover, as noted above, the number of unavoidable differences with US GAAP has been much reduced in recent years. If the CSA believes that there is a significant question in this regard, it is suggested that consideration be given to requiring high quality reconciliations for a reasonable trial period, during which preparation costs would be monitored – as the basis for a fully informed determination of the costs and benefits of continuing the requirement.

2. Improving the quality of reconciliation information

AcSB staff examination of Canada/US GAAP reconciliations currently provided indicates that many of them could be substantially improved. The information proposed to be required in notes to financial statements (National Instrument 51-102, paragraph 4.7(3)) should be helpful in this regard. We recommend, however, that the proposed requirement to quantify the effect of material differences not be limited to those "that relate to measurement", but also include recognition and presentation differences. We also suggest that further guidance may be useful in respect of the presentation and explanation of balance sheet and cash flow differences, as well as income effects.

AcSB staff would be willing to work with the CSA to develop supporting guidance to improve the quality of reconciliation information, if our recommendation for its provision on an ongoing basis is accepted.

3. Exemptions relating to foreign issuers (National Instrument 71-102 – Continuous Disclosure and Other Exemptions Relating to Foreign Issuers)

In general we accept that it is reasonable that Canadian investors in foreign companies issuing securities in Canada should be expected to become familiar with financial statements prepared on the basis of US or IASB standards, since these standards are widely accepted and recognized for purposes of cross-border listings. While it would be useful to Canadian users for such financial statements to be augmented by reconciliations to Canadian GAAP, we accept that it would not be practical to require this.

We are concerned, however, with the suitability of financial statements prepared on the basis of various other national accounting requirements and practices for filing by foreign issuers in Canada, at least without high quality reconciliation to Canadian, US or IASB standards - and make the following comments in this regard.

"Designated foreign issuers". It is not clear to us what the cost/benefit or other considerations may be that warrant creating a category of "designated foreign issuers" who would be permitted to provide financial statements for filing in Canada on the basis of their national disclosure requirements with no reconciliation to Canadian, US, or IASB standards. We believe that Canadian investors may reasonably expect that CSA acceptance of the financial statements of foreign issuers for filing in Canada indicates that Canadian securities regulators are satisfied that these statements will meet Canadian investors' basic financial information needs. We question whether financial statements prepared on the basis of the standards of certain of these jurisdictions will be sufficient to meet this expectation, and generally whether Canadian investors should be expected to understand what may be very significant differences with Canadian, US, or IASB standards – so as to be able to evaluate the information uncertainty that should be factored into the market prices of these issuers' securities. The fact that designated foreign issuers would only be able to issue a small proportion of their equity securities in Canada will not provide protection to a Canadian with a significant proportion of his or her portfolio invested in these securities.

Overall, we are not clear why it would be inappropriate to require all foreign issuers to provide financial statements on the basis of Canadian, US, or IASB standards, or at least to reconcile their financial statements to one of these bases - especially since many of the designated countries have committed to adopt IASB standards for consolidated statements within the next few years.

Other eligible foreign issuers. We agree in principle with the proposal that other eligible foreign issuers be permitted to provide financial statements prepared on the basis of national standards that "cover substantially the same core subject matter as Canadian GAAP" where they are accompanied by a reconciliation to Canadian GAAP. We have some practical concerns, however, relating to (a) how it will be determined that a particular country's national standards cover substantially the same core subject matter as Canadian GAAP, and (b) whether a complete and accurate reconciliation to Canadian GAAP has been prepared. A potential difficulty in these situations is that the foreign issuer may not have a sound understanding of Canadian GAAP, and Canadian advisors may not have a sound understanding of the accounting principles in the foreign country – which may lead to incomplete and inaccurate reconciliations. Special regulatory attention may be necessary in these situations.

4. Financial institution GAAP exemption

We support the proposal that the GAAP exemption for banks and insurance companies that exists in some jurisdictions be removed. It is our belief that external stakeholders are not best served by financial statements that depart from GAAP. Global accounting standards are striving to remove differences between national standards in order to facilitate comparability and the efficiency of global capital markets. Providing an exemption from those standards is counter to this objective.

5. Proposals for additional disclosures in financial statements – National Instrument 51-102

Additional information for development-stage issuers. (paragraph 4.10 and Companion Policy 51-102CP paragraph 3.5.)

While we are supportive of these additional disclosures, we are uneasy as to the CSA establishing arbitrary quantitative materiality rules. In particular, the absolute $25,000 minimum would seem to set a precedent that may result in unnecessary detail of disclosure. Are there particular difficulties with the application of the basic materiality concept for judgments to be made under GAAP in this one area that need to be singled out for special materiality rules?

Disclosure of outstanding share data. (paragraph 4.11)

We support the disclosures being proposed, while noting that at least the information to be provided under (3) (a) and (b) is already required under CICA Handbook Section 3240. We do not understand what is meant by the proposal that these disclosures be provided "as of the latest practicable date", and with the proposal of (c) that the information be provided "to the extent determinable upon reasonable inquiry".

6. Certain MD&A disclosure proposals that relate to financial statement disclosures (Form 51-102F2)

Transactions with related parties (paragraph 1.6)

We support efforts to improve disclosures of related party transactions. However, we have difficulty with the proposal to move beyond the CICA Handbook definition of "related parties" to parties "with whom you [the reporting issuer] have a relationship that enables you to negotiate terms of transactions that may not be available from other, more clearly independent third parties". We suggest that the intended relationships need to be better defined, and additional guidance provided, for this to be workable. For example, is some degree of economic power over some or all suppliers or customers due to an issuer's relative size or monopoly position to be included? What about the other side of economic dependence situations, where a company may be economically dependent on a supplier or customer? It may have no ability to negotiate terms of transactions, but may be forced to accept prices less advantageous than a fully efficient open market price. Disclosure of economic dependency is required by CICA Handbook Section 3841, and we suggest that consideration be given to the relationship and consistency of the CSA proposal with that standard. If a requirement extending the concept of party relationships to include broader economic dependency is put in place, we recommend that it be clearly distinguished from the concept of "related parties" defined in the CICA Handbook so as to reduce the likelihood of confusion with financial statement disclosures.

The proposed Instructions with respect to information to be disclosed would seem to overlap with some CICA Handbook Section 3840 requirements for disclosure of related party transactions, and would seem to need some clarification in order to avoid unnecessary differences and potentially confusing inconsistencies with the CICA Handbook requirements. In particular, Instruction (i) (D) would require "if disclosures represent that transactions have been evaluated for fairness, a description of how the evaluation was made and by whom". How is this intended to relate to the CICA Handbook requirement that no representation should be made that a related party transaction exchange amount is equivalent to a fair value (or an arm's length-equivalent value) unless the entity can demonstrate that it has undertaken equivalent transactions with arm's length parties at this value (paragraph 3840.55)?[3] We wonder whether the CSA proposal may suggest a lesser standard. Also Instruction (i) (E) would require disclosure of "ongoing" contractual or other commitments "resulting from the arrangement". We are not clear whether a different disclosure is intended from that required by CICA Handbook 3840.43(f), which requires disclosure of all contractual obligations (including commitments) with related parties.

We suggest that the need for the proposed general disclosure regarding relationships with unconsolidated, non-independent special purpose entities be evaluated against disclosures proposed to be required in a CICA Handbook Accounting Guideline on special purpose entities.

Critical accounting policies (paragraph 1.9)

We support the objective of improving disclosures of accounting policies and providing for disclosure of critical accounting policies. However, we believe that the proposed requirements are far too general and brief to be effective. In particular, we do not believe that a requirement to disclose "the likelihood that materially different amounts would be reported under different policies or using different assumptions" is reasonable or operational. We suggest that it is not reasonable to expect companies to identify and assess the impact of all possibly defensible alternative policies and assumptions, at least without considerable additional guidance. We recommend that this proposal be further studied and developed in coordination with the AcSB before being required. It would be desirable that standards for disclosure of accounting policies be made in the financial statements rather than in the MD&A.

Changes in accounting policies (paragraph 1.10)

We support this disclosure.

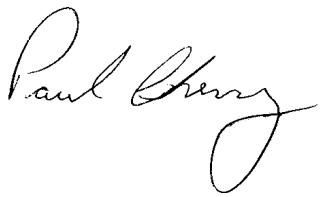
Financial instruments (paragraph 1.11)

We support the substance of these disclosures, which would complement and extend the disclosures currently required by CICA Handbook Section 3860.

We will be pleased to clarify or elaborate on any point raised in this submission.

[3] CICA Handbook Section 3840.55 further provides: "When such disclosures are made, the basis for determining fair value is disclosed."

Yours truly,



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