PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Chartered Accountants
145 King Street West
Toronto, Ontario
Canada M5H 1V8
Telephone +1 416 869 1130
Facsimile +1 416 863 0926
Direct Fax 416-941-8481

September 25, 2003

Alberta Securities Commission
Manitoba Securities Commission
Department of Justice, Securities Administration Branch, New Brunswick
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Department of Justice, Government of the Northwest Territories
Nova Scotia Securities Commission
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 mobilières du Québec
Saskatchewan Financial Services Commission
Registrar of Securities, Government of Yukon

John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario
Email: jstevenson@osc.gov.on.ca

Denise Brosseau, Secretary
Commission des valeurs mobilières du Québec
Stock Exchange Tower
800 Victoria Square
P.O. Box 246, 22nd Floor
Montréal, Québec
Email: consultation-en-cours@cvmq.com

Subject: Proposed Multilateral Instruments 52-108, *Auditor Oversight*, 52-109, *Certification of Disclosure in Companies Annual and Interim Filings* and 52-110, *Audit Committees* (the "Investor Confidence Initiatives")

PricewaterhouseCoopers appreciates the opportunity to comment on the Proposed Multilateral Instruments comprising the Investor Confidence Initiatives by Canadian securities regulatory authorities.

We fully support the Canadian Public Accountability Board and mandatory participation by auditors. We have no specific comments on the CSA proposals related to auditor oversight.

Our detailed concerns on the proposed certification and audit committee requirements are included in Appendix A to this letter.

If you wish to discuss our comments, please contact Michael A. Tambosso (michael.a.tambosso@ca.pwc.com or 416-941-8388) or Vicki Kovacs (vicki.kovacs@ca.pwc.com or 416-941-8363).

Yours very truly,

(signed) ***"PricewaterhouseCoopers LLP"***

Chartered Accountants

Appendix A

1. Certification of Disclosure in Companies Annual and Interim Filings

(a) Internal controls, and disclosure controls and procedures

The Request for Comments queries whether the Proposed Instrument should formally define "internal controls" and "disclosure controls and procedures". We note that SEC Rule 302 defines "disclosure controls and procedures" and contains a cross-reference to an AICPA definition of internal control. We believe that these terms should also be separately defined in the Proposed Instrument.

We do not believe that the current approach in the Proposed Instrument (i.e. describing the outcomes that these controls are designed to achieve) is sufficient. For example:

- As currently drafted, "internal controls" might be taken to relate to internal controls broadly, whereas in the Proposed Instrument it should perhaps be interpreted more narrowly to relate to internal controls over reporting financial data.
- While the term "internal controls" is used in conjunction with a specified outcome in Item 4(b) of the proposed annual certification, it is not clear in Item 4(c) whether the reference therein to "internal controls" is also limited to the controls subject to the outcome specified in Item 4(b).
- It is questionable whether the proposed certification is intended to be the equivalent of the SEC Rule 302 certification, or whether it also covers the SEC Rule 404 certification.

(b) Significant deficiencies and material weaknesses

The Proposed Instrument uses the terms "significant deficiencies" and "material weaknesses" although neither term is defined in the Instrument or under Canadian generally accepted auditing standards ("GAAS"). CICA Handbook Section 5220, *Internal Control in the Context of an Audit – Weaknesses in Internal Control*, uses the term "significant weakness in internal control". Literature in the United States, SAS 60 in particular, uses the phrase "reportable conditions" which are also described as "significant deficiencies (in the design or operation of internal control)" and also defines "material weakness". There was some talk of dropping the term "reportable conditions" under U.S. GAAS and only using the terms "significant deficiencies" and "material weaknesses". It might be useful for the Proposed Instrument to use the same terms as in the U.S. requirements as well as to define those terms within the Canadian Instrument.

(c) Fair presentation

Item 3 of the proposed annual and interim certifications deals with fair presentation of the entire disclosure record (i.e. financial statements together with other financial information included in the annual and interim filings such as management discussion and analysis) without limitation to generally accepted accounting principles (GAAP). The background material in the Request for Comments, however, indicates the following:

> *...the Proposed Instrument will require CEOs and CFOs to certify, annually and on an interim basis, that their issuer's financial statements "fairly present" the financial condition of the issuer for the relevant time period. This representation is not qualified by the phrase "in accordance with generally accepted accounting principles" which Canadian auditors typically include in their financial statement audit reports. This qualification has been specifically excluded from the annual and interim certificates to prevent management from relying entirely upon compliance with GAAP procedures in this representation, particularly where the results of a GAAP audit may not fairly reflect the overall financial condition of a company.*

We are concerned that this background material is inconsistent with the proposed annual and interim certifications in that it is directed at the financial statements and not the disclosure record as a whole. We believe clarification is needed that "fair presentation" on its own does not apply only to the financial statements and that it is not intended to apply to the financial statements on a stand-alone basis as indicated by this material. We are concerned that to imply otherwise may force MD&A disclosure and other information into the financial statements, an outcome which is not appropriate for companies and their auditors.

We understand that the intention was to address the disclosure record as a whole and not the financial statements on a stand-alone basis. We request that this be clarified in the final material.

(d) General

Generally, we find this Proposed Instrument difficult to comprehend. In particular, it is cumbersome to relate the exemptions listed in Part 4 to the certification requirement from which one is exempt. It would be better to describe the exemption in the same place as the particular rule to which it relates. In addition, we did not find the material in the Request for Comments to be written in a user-friendly format. The questions therein launch into the various parts of the certification requirements without any meaningful discussion.

2. Audit Committees

(a) Financial expert

The definition of "audit committee financial expert" in Item 1.1 lists several criteria an expert must possess including having "an understanding of financial statements and the accounting principles used by the issuer to prepare its financial statements".

We are uncertain as to how this criterion applies in circumstances when, for example, an issuer's primary financial statements are prepared in accordance with one GAAP and reconciled in a note to another GAAP. We are aware of at least one legal analysis which indicates that this criterion relates to an understanding of the GAAP used in the primary financial statements. This would imply that an individual could be a financial expert without knowing anything about the other GAAP in the GAAP reconciliation. Some clarification in this regard would be helpful.

On a related note, we understand that, from a U.S. perspective, when financial statements are prepared in accordance with non-U.S. GAAP and include a reconciliation to U.S. GAAP,

internal controls over financial reporting for SEC Rule 404 certification purposes should include controls over U.S. GAAP for purposes of the GAAP reconciliation. We note this for your attention in drafting your equivalent of the SEC Rule 404 certification.

(b) Pre-approval of non-audit services

(i) Pre-approval policies and procedures

Section 2.3 (4) of Proposed Instrument 52-110 requires audit committee pre-approval of all non-audit services to be provided to the issuer by is external auditors, but comment on the manner in which that requirement may be satisfied is left to Section 5.1 of Companion Policy 52-110CP:

> "In our view, ***it may be sufficient*** for an audit committee to adopt specific policies and procedures for the engagement of non-audit services where
>
> - the pre-approval policies and procedures are detailed,
> - the audit committee is informed of each non-audit service, and
> - the procedures do not include delegation of the audit committee's responsibilities to management." [emphasis added]

We understand that the conceptual framework set out in these sections, read together, is clearly intended to parallel the approach adopted by the SEC in Sections 210.2-01 (7)(i)(A) &(B) in its Final Rule of January 28, 2003. Those sections require either audit committee pre-approval of each specific non-audit service engagement provided by the auditor, or pre-approval through pre-approval policies and procedures with the same characteristics set out in the three bullet points above.

We are concerned that by segregating the sanctioning of policies and procedures to satisfy the preapproval requirement in the Companion Policy, and by using the phrase "it may be sufficient" in the Companion Policy, there is room for uncertainty whether pre-approval policies and procedures ***will*** indeed satisfy the audit committee pre-approval requirement imposed in Section 2.3(4) of Proposed Instrument 52-110.

We believe that the use of pre-approval policies and procedures should be made explicit in the Rule, with guidance offered in the Companion Policy. Section 2.3(4) should state that there should be preapproval of each specific service or through pre-approval policies and procedures established by the audit committee which satisfy the requirements included in the three bullet points in the current text of Companion Policy Section 5.1. The phrase "it may be sufficient" should be removed.

Also, the SEC's August 2003 release of Frequently Asked Questions on the Application of the January 2003 Rules on Auditor Independence suggests that additional guidance on pre-approval procedures will be useful. Accordingly, we also recommend that a new Companion Policy Section 5.1 be adopted, stating that in satisfying the three requirements:

- the use of monetary limits alone does not constitute a sufficient basis for a pre-approval policy;
- the appropriate level of detail for an issuer's pre-approval policy will differ depending upon the facts and circumstances of the issuer;
- that such detail, however, need not constitute an individual engagement-by-engagement approval but be constructed to ensure that the principle of audit committee supervision of the independence of the audit is satisfied.

(ii) What must be pre-approved/fee disclosures

Item 2.3(4) of the Proposed Instrument requires that an audit committee of an issuer must pre-approve all non-audit services to be provided to the issuer or its subsidiary entities by its external auditors (i.e. the "principal auditors") or the external auditors of the issuer's subsidiary entities. Item 7 of Proposed Form 52-110F1, *Information Required in an AIF*, requires disclosure of external auditor service fees (but without reference to subsidiary entities and their auditors, which in some instances may be different than the auditors of the issuer).

We understand that the U.S. requirements are that audit services provided to the issuer and its subsidiaries, by the auditor of each entity, must be pre-approved by the audit committee of the issuer. Services provided by the auditor of an entity subject to significant influence by the issuer need not be pre-approved. Non-audit services provided by an auditor of a subsidiary, where that auditor differs from the auditor of the issuer, are not subject to pre-approval by the audit committee of the issuer. For fee disclosure purposes, services to be included are those provided by the principle auditor, whether provided to the issuer or to any of its subsidiaries. We suggest that the Canadian rules should be written to lead to the same result, i.e.:

- The audit committee of the issuer should approve all audit services provided to the company, whether by the principal auditor or other external auditors of subsidiaries.
- Non-audit services provided to subsidiaries by non-principal external auditors are not subject to pre-approval by the audit committee of the issuer.
- Fee disclosure requirements include fees for audit, audit related, and other services provided by the principal auditor of the issuer. Fee disclosure requirements do not include fees of nonprincipal external auditors of subsidiaries for audit services provided to subsidiaries (even though the audit services are approved by the audit committee of the issuer), or for audit-related and other services provided to subsidiaries.

Our understanding of the current Canadian proposals as compared to U.S. requirements, including the fee disclosure requirements, is set out in the following table. If we are incorrect in our analysis of the Canadian proposals, we suggest that clarification is required. We also suggest that a table in the Canadian requirements would be useful to include in the Companion Policy.

	Pre-approval required by issuer's audit committee		Fee disclosure required by issuer	
	Canada	**U.S.**	**Canada**	**U.S.**
Audit services of issuer's external auditor (principal auditor) (the audit committee of the issuer must recommend the appointment of the auditor)	Yes	Yes	Yes	Yes
Non-audit services of principal auditor	Yes	Yes	Yes	Yes
Audit services of non-principal external auditors of subsidiaries (SEC rules relating to listed companies on NYSE, ASE or NASDAQ)	No	Yes	No	No
Non-audit services of non-principal external auditors of subsidiaries	Yes	No	No	No
Audit services of auditors of affiliates (e.g. equity accounted investees or joint ventures)	No	No	No	No
Non-audit services of auditors of affiliates	No	No	No	No

(c) de minimus non-audit services

As currently drafted, Item 2.4(a) of the Proposed Instrument does not appear to extend the pre-approval exception to de minimus non-audit services provided to subsidiary entities by its own external auditors. We agree that this is appropriate assuming that non-audit services provided to subsidiary entities by its own external auditors are not subject to pre-approval themselves. However, as currently drafted, Item 2.3(4) requires pre-approval of such services provided to subsidiaries. If Item 2.3(4) remains unchanged in the Final Instrument (refer to our previous comments in section 2(b)(ii) of this Appendix), then Item 2.4(a) should be amended to extend the de minimus exception to non-audit services provided to subsidiary entities by its own external auditors as well.