Ontario Securities Commission
Alberta Securities Commission
Manitoba Securities Commission
Registrar of Securities, Government of Yukon
Registrar of Securities, Department of Justice, Government of the Northwest Territories
Securities Commission of Newfoundland and Labrador
Nova Scotia Securities Commission
Commission des valeurs mobiliéres due Québec
Saskatchewan Financial Services Commission
Office of the Attorney General , Prince Edward Island
Registrar of Securities, Legal Registries Division, Department of Justice, Government of Nunavut
Department of Justice, Securities Administration Branch, New Brunswick.

September 25, 2003

Dear Sirs:

Re: Investor Confidence Proposals

We are writing to provide comments on behalf of KPMG on proposed multilateral instruments 52-108, Auditor Oversight, 52-109, Certification of Disclosure and 52-110, Audit Committees.

KPMG supports the introduction of regulations that are consistent with similar requirements recently introduced in the United States. We believe that consistency with the US regulations is necessary to minimize the duplication of effort that those companies registered with both the SEC and a Canadian regulator would otherwise face and to demonstrate that Canada has an equally strong set of market regulations on which investors may rely. We also support appropriate flexibility in the regulations and/or exemptions necessary to recognize the needs of the many small Canadian issuers registered with the various venture exchanges.

The following comments identify specific concerns we have with the draft regulations and amendments that we believe should be considered:

Auditor Oversight

We support the need for CPAB to impose restrictions and sanctions in response to wrongdoing. We also support the concept of having various levels of restrictions/sanctions, depending on the severity of the wrongdoing, however, without any guidance on what action or lack of action will result in either restrictions or sanctions, it is difficult to assess whether the proposed "Notice" regulations in Part 3 are reasonable. Only when CPAB has issued this guidance including clarification on a Firm's right to appeal such penalties, will it be possible to determine whether the penalty is consistent with the offense.

Regardless, we believe the proposal in section 3.1 that a Firm must notify all of it's reporting issuer audit clients of all sanctions imposed by CPAB should be reconsidered. It is impossible to assess the reaction of a Firm's clients to such a communication. As a result the impact of the sanction may be much more severe than intended by CPAB. This proposal goes beyond established procedure for reporting actions involving professional service firms and is not a requirement included in the PCAOB proposed rules on "Investigations and Adjudications". Our fundamental concern is that for a system of restrictions/sanctions to be equitable, the firm being restricted/sanctioned should be able to reasonably assess the outcome or cost of the restriction/sanction. We are concerned that in today's environment a direct notification to all audit clients will leave the firm's ultimate cost/outcome in the hands of the marketplace.

We believe that only when the sanction imposed by CPAB results in a Firm being ineligible to issue future audit reports to issuers should a Firm be required to communicate a sanction directly with their issuer audit clients. Also, assuming that sanctions may be imposed on individual members of a firm rather than the firm in its entirety, we also believe that any required notices should depend on the extent of the sanctions imposed. For example, a sanction prohibiting a member of the firm from participating in the audit of an issuer should only be required to be communicated to those clients the member has been involved in auditing rather than all issuer audit clients of the Firm.

Any such communication to clients that is required by the final rules should allow more than the 5 business days for delivery proposed in section 3.1(3). A Firm with hundreds of issuer clients will need adequate time to draft, produce and deliver such an important communication. We recommend that the period for delivery be extended to at least 10 business days.

Further, we support the requirements for a firm to notify the regulator of sanctions or restrictions under sections 3.1 and 3.3, however, we suggest that the period allowed be the same for sanctions and restrictions and that it be 10 business days for both.

Public accounting firms in foreign jurisdictions

As the Commission is aware, in addition to the activities of the PCAOB in the United States, the EU and several countries have either adopted or proposed regulatory reforms in relation to audit firms. In many cases these reforms include new rules relating to registration, inspection and discipline of accounting firms.

Canadian and foreign market regulators need further time to co-operate and explore how they can best address the legal issues associated with registration as well as practical concerns associated with registration, oversight and discipline. This will enable regulators to ensure that the system provides for robust investor protection, but does not create a disproportionate impact in terms of the cost of regulation compared to the investor protection afforded by it. This is especially so in certain countries where there are a relatively small number of Canadian issuers.

Other comments

1. In those situations when reciprocity in relation to registration has not been achieved with other countries, we strongly encourage the alignment of registration deadlines and other requirements to the extent possible. This is especially relevant in relation to registration with the PCAOB due to the large number of Canadian public companies that are also issuers in the United States.

2. It is not clear from section 3.2 when the 12 month period for reporting sanctions in proposals to reporting issuers ends. We suggest that the requirement should be to include notification of any sanction issued against the firm by CPAB in any proposal issued to a reporting issuer within 12 months of the date the sanction was imposed.

3. As noted in the background material to the instrument, it is the intention of the CPAB to recover its costs from the participating firms. We note that is different from the PCAOB approach of recovering most of its operating costs from the SEC issuers. Although both approaches may ultimately result in the cost of auditor oversight being passed on to the issuers, CPAB may not appear as independent from the firms over which it is providing oversight. Further, discussions between CPAB and the PCAOB may result in the PCAOB relying on CPAB to perform oversight of Canadian SEC issuers. If this occurs, we believe Canadian SEC issuers should receive some relief from the fees they would otherwise be required to pay to the PCAOB.

Certification of Disclosure

We support the introduction of requirements relating to management's assessment and certification of internal controls and disclosure controls and procedures in a way substantially the same as introduced by the SEC. We note that the Commission continues to study the SEC requirement for auditor attestation to, and reporting on, management's assessment of internal controls. We believe that a requirement for auditor attestation will increase the discipline that is shown by management in performing their assessment and improve the level of confidence investors have in these important regulations. Also, without an auditor attestation requirement, the inclusion of management's assessment on internal controls in the annual MD&A may make it more difficult for auditors to comply with their responsibilities under CICA Handbook Section 7500, Auditor Association with Annual Reports, Interim Reports and Other Public Documents.

Inconsistencies with final US rules

We expect that the Commission may not have had an opportunity to review the final rules issued in late July by the SEC on "Management's Reports on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports" for the purpose of considering how changes from the SEC's draft rules may impact the Commission's proposal. If this is the case we strongly encourage this review to take place prior to the commission's rules being finalized. In this regard, we make specific reference to the following:

- Under the final SEC rules foreign private issuers need not begin complying with the rules on management's assessment of internal controls over financial reporting until the annual report for fiscal years ending on or after April 15, 2005. The transition rule in section 1.3 of the Instrument would require the evaluation of internal controls in annual filings on or after January 1, 2005. We believe the effective dates for this certification should be consistent especially in light of the exemption provided in section 4.1(1) of the Instrument.

- The SEC has removed the requirement to disclose corrective actions with regard to significant deficiencies. They have also removed reference to "other factors that could significantly affect internal controls" and amended the disclosures of changes in internal control over financial reporting to only cover those occurring during the most recent fiscal quarter covered by the certificate. We recommend that the Commission adopt these changes to the proposed annual and interim certificates as appropriate.

- The Sec has changed the terminology "that could adversely affect" in certification 5 (a) to "reasonably likely to adversely affect". We believe this change should also be adopted.

Need for additional guidance

We agree that providing an opportunity for companies to interpret the rules and adopt procedures that are appropriate for their circumstances is important as it recognizes the diversity in the size and complexity of Canadian issuers. Therefore, we do not believe it is necessary to be as prescriptive as the SEC has been in providing rules and interpretations for implementing those rules. However, we are concerned that the lack of background discussion on how management may achieve the stated objectives will create an environment of significant uncertainty for management and investors. To alleviate this uncertainty the Commission should consider providing general application guidance.

The guidance might include, for example, some of the following:

- A definition of the terms "internal controls" and "disclosure controls and procedures" consistent with the definitions of "internal control over financial reporting" and "disclosure controls and procedures" contain in the final SEC Rule to indicate the Commission and SEC rules are consistent in their concepts.

- The need for management to conclude on the effectiveness of internal control and the potential impact of significant deficiencies and material weaknesses identified during their evaluation on their conclusion.

- Guidance on the extent of work that may normally be required in documenting the design and assessing the operating effectiveness of internal controls and disclosure controls and procedures.

- Acknowledgment that the disclosure and internal controls required by a smaller issuer may be very different from those required by a larger issuer in order for both to reach the same positive conclusion on overall effectiveness.

Timing gap between filing and certification

We are concerned that in many instances an issuer's annual audited financial statements and MD&A will be filed for a considerable period of time prior to the annual certification being filed at the time of filing the AIF. It is unclear what actions management would be required to take should they become aware of new information relevant to the previous filings during the intervening period prior to filing their annual certificate. Until such time as all annual filings are required to occur simultaneously it may be desirable to adopt a certification process that requires a "bare" certification to be filed with the financial statements and MD&A and a full certification at the time of filing the AIF or, for venture issuers, the management information circular.

Interim evaluation

We believe the decision not to require an interim evaluation of internal and disclosure controls is consistent with the need to adopt a process that recognizes the challenges faced by the large number of smaller issuer's in Canada

Other comments

1. It is unclear why a company that is both a Canadian and SEC issuer would avail itself of the exemption under section 4.1(3) as this would require it to file interim certifications with the SEC that are not currently required. We do not believe that an issuer will voluntarily file quarterly certificates with the SEC unless required to under legislation.

2. We recommend that guidance be provided on the definition of consolidated subsidiary as used in the annual and interim certificates. It is unclear whether proportionately consolidated joint ventures are to be included as consolidated subsidiaries.

3. We note there is a typo in section 4 (b) of the proposed interim certificate; implement s/b implemented.

Audit Committees

Our main concerns with the proposals in this instrument relate to the disclosure requirements regarding "audit committee financial experts" and the categories of persons that are not considered independent for purposes of serving on an issuer's audit committee.

Audit committee financial experts

Although there is no requirement to include a financial expert on the audit committee, we expect that many issuers will see this as a "best practice" and will make every attempt to identify and appoint an audit committee member who satisfies the definition of an audit committee expert. However this process is likely to take some time in many instances. Rather than requiring companies to explain why they have not been able to identify and appoint a financial expert in accordance with the provision of item 9, Effective Date, we suggest that this requirement be deferred until filings occurring on or after July 31, 2005.

This date is consistent with the similar disclosure requirements for foreign private issuers contained in the SEC rules relating to listed company audit committees.

Audit committee independence

We acknowledge that the categories of persons that are not considered independent for purposes of serving on an issuer's audit committee are for the most part consistent with similar requirements issued by the SEC or proposed as listing requirements by the New York Stock Exchange (NYSE). However, it is our understanding the NYSE proposals have not been approved by the SEC. Until this approval is received, we are concerned that adopting these proposals in Canada may result in rules that are inconsistent with the final US rules for listed entities. We suggest that the OSC adopt the SEC criteria for audit committee member independence until the NYSE listing requirements are approved.

Regardless of what the NYSE adopts, we are concerned that the proposed NYSE restrictions on persons that were partners or employees of current or former internal and external auditors and their immediate family members may unnecessarily restrict the availability of persons otherwise meeting the financial literacy and financial expert definitions. As examples of changes that may address this concern, we provide two suggestions.

First, we recommend that the definition of immediate family be made consistent with the definition in the proposed independence standards developed by the Canadian Institute of Chartered Accountants as being "a spouse (or equivalent) or dependent". This would be consistent with the final SEC rules that consider fees received by "a spouse, a minor child or stepchild or a child or stepchild sharing a home with the member" to be received indirectly.

Second, we recommend that the restrictions in sections 1.3 (b) and (c) relating to former partners and employees of the current or former external auditors only apply to those persons who provided services to the issuer. It is this group who may have developed a relationship with management that could appear to interfere with the exercise of a member's independent judgment.

Pre-approval policies and procedures

We understand that the conceptual framework set out in the Instrument and the Companion Policy, read together, is clearly intended to parallel the approach adopted by the SEC in its independence rules 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 following characteristics:

- 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.

We are concerned that 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).

For greater clarity, we recommend that Section 2.3(4) be amended to state that the non-audit service pre-approval requirement *is* satisfied where the approval is obtained pursuant to pre-approval policies and procedures established by the audit committee which satisfy the requirements included in the three bullet points discussed above.

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 the following guidance from that release be adopted:

- 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.

In establishing the appropriate balance between specificity in the categories of service being pre-approved, and a streamlined and efficient process, we believe it is important that providing the appropriate level of detail for audit committee scrutiny not result in a burdensome process that undermines the purpose and intention of permitting pre-approval policies and procedures.

Other comments

1. We believe the background material should contain a discussion and possibly examples as to how the "prescribed period" should be determined in accordance with section 1.4(4).
2. Based on the effective date rules in Part 9, it is not clear whether the disclosures under sections 5.1 and 6.2 would be required in an AIF or management information circular filed after January 1, 2004 but in advance of the annual meeting held in 2004 or June 20, 2004, if earlier.
3. Under the SEC rules, disclosure of the audit committee charter is only required at least every three years. The disclosures under section 5.1 and 6.2 would require annual disclosure of the text of the audit committee's charter. We recommend that this disclosure requirement be consistent with the SEC requirement.
4. To provide additional clarity we recommend that section 2.3(4) require pre-approval of audit services as well as non-audit services.
5. The reference to Exemptions in item 4 of Form 52-110F1 should be to Part 8 not Part 7.

Please contact me should you wish to discuss any of the above comments.

Yours very truly

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