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April 15, 2004

John Stevenson, Secretary
Ontario Securities Commission
20 Queen Street West
Suite 1900, Box 55
Toronto, Ontario, Canada M5H 3S8

Re: Comments on Proposed Multilateral Policy 58-201

Dear Mr. Stevenson:

Further to our letter of September 25, 2003, The Institute of Internal Auditors (IIA) continues to support the Ontario Securities Commission (OSC) and the other participating members of the Canadian Securities Administrators (CSA) in your initiatives to promote effective corporate governance in Canada. Following on the heels of the final rules (52-108, 52-109, 52-110) released in January 2004, this new proposal continues to make excellent strides in strengthening governance practices, in communicating the value of basic fundamentals, and in improving the international perception of the Canadian marketplace.

The IIA, representing over 93,000 members worldwide including 3,700 Canadian members in 11 chapters, is the principal voice of the internal auditing profession. Internal Auditors are well positioned to offer unique insights into issues related to improving corporate governance, risk management, and control processes. The IIA maintains the *International Standards for the Professional Practice of Internal Auditing (Standards)*, which are recognized around the globe and support the internal auditing profession.

Good governance and accurate financial reporting emanate from the balanced interaction of board members, executives and their management and staff, internal auditors, and external auditors. In December 1999, The IIA adopted the following definition of internal auditing that acknowledges the role of internal auditing in corporate governance:

Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

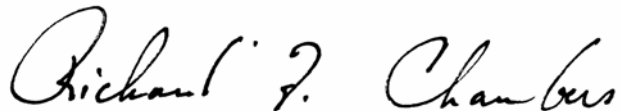
Since the adoption of this definition, The IIA has intensified its efforts to contribute to the reform of governance practices of public companies around the world. These efforts included reviewing and providing comment on the 2003 CSA proposed rules that were recently adopted. The IIA is also pleased to provide our views regarding the proposed policy, released January 16, 2004, for public comment. Leading Canadian IIA members, including prominent chief audit executives, have contributed to developing our input for your consideration.

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From our perspective as a contributor to corporate governance, and as an independent observer of that process, The IIA offers its detailed comments on the Proposed Policy and Proposed Instrument, as well as other areas where we believe the OSC/CSA can enhance its final rules to further improve governance processes, in the attached document.

We appreciate the opportunity to express our views on these important matters and welcome further discussion at any time.

Best regards,

A handwritten signature in cursive script that reads "Richard F. Chambers". The signature is written in black ink on a white background.

Richard F. Chambers, CIA, CGAP, CCSA

Attachment: Detailed Comments on Proposed Multilateral Policy 58-201

Response Team Members:

Brian G. Brown, CIA, Chief Audit Executive, Agricore United, Canada
Noreen Foh, CA, VP Internal Audit, Intesa Bank, Canada.
Alphonse Galluccio, CIA, Chief Audit Executive, Le Groupe Jean Coutu (PJC) Inc., Canada
Larry Harrington, Chief Audit Executive, Staples Business Depot, Canada
Libby MacRae, Research Associate, CCAF, Canada
Carman Lapointe-Young, CIA, Past Chair of The IIA, Vice-President, Internal Audit & Evaluation,
Export Development, Canada
Paul Striowski, CIA, Risk Management and Internal Audit Consultant, Grant Thornton LLP, Canada
Dan Swanson, CIA, AVP Professional Practices, Institute of Internal Auditors
Archie Thomas, CIA, Director, Institute of Internal Auditors

THE INSTITUTE OF INTERNAL AUDITORS
Detailed Comments on Proposed Multilateral Policy 58-201

April 2004

1. General Support

The Institute of Internal Auditors (IIA) continues to support the efforts of the Ontario Securities Commission and the Canadian Securities Administrators to improve the level of Corporate Governance in Canada. The rules and policies recently released and proposed will help those charged with governance responsibilities and increase the confidence of stakeholders. The IIA has, in recent years, continually encouraged regulatory bodies to promulgate a strong, uniform code for corporate governance and require board reporting on the extent of compliance with the code. These practices improve transparency and help to restore investor confidence.

2. Best Practices - Internal Auditing

The IIA recommends a requirement that all publicly held companies establish and maintain an independent, adequately resourced, and competently staffed internal auditing function to provide boards of directors (through their audit committees) and management with ongoing assessments of governance, risk management, and internal control practices in accordance with The IIA's *Standards*. While companies should decide how best to provide this service based on individual needs, structure, complexity and size, disclosure should be required in the absence of an internal auditing function, including the rationale.

Policy 58-201 proposes Best Practices for Effective Corporate Governance. Restoration of investor confidence must be founded on strong principles of corporate governance that create checks and balances effected by appropriate distribution of authority among management, shareholders, and regulators. Effective organizational control is best achieved when the four cornerstones of good governance — boards, management, internal auditors, and external auditors — are competent, adequately resourced, and coordinated in their efforts.

Internal auditors and audit committees are mutually supportive. Consideration of the work of internal auditors is essential for audit committee understanding of the effectiveness of operations. Internal auditing also provides independent assurance on the quality of management systems and practices, the accuracy and completeness of reporting, and compliance with laws, regulations and policies. Contemporary internal auditing focuses on identifying the strategic, market, credit, operational, and financial risks, and assessing controls designed to manage or mitigate those risks, including:

- Related-party transactions, joint ventures, and partnerships;
- Restructurings, mergers and acquisitions;
- New business lines, products, and systems;
- Outsourcing of critical functions;
- Vulnerability to interest or exchange rate or cash flow volatility;
- Security and integrity of information and operating systems;
- Business continuity and contingency planning; and,
- Exposure to reputational risks.

Internal auditing monitors and reports on the effectiveness of controls to help boards avoid situations like those underlying recent governance and quality of earnings catastrophes.

Audit committees, in overseeing internal auditing activities, should ensure that the function is structurally situated to achieve organizational independence, avoid scope limitations, and permit unrestricted access to top management, the audit committee, and the board. The IIA's *Standards* require that the chief audit executive (CAE) report to a level within the organization that allows the internal audit activity to fulfill its responsibilities. Ideally, the CAE should report functionally to the audit committee, and administratively to the chief executive officer of the company to ensure adequate consideration of internal audit results.

3. *Mandatory Standards*

Proposed Policy 58-201 contains recommended best practices, encourages issuers to adopt the suggested measures, and requires certain disclosure (Form 58-101F1) and filings. While the policy is intended to provide issuers with flexibility, leaving implementation optional sends unclear signals to the marketplace.

The markets and other stakeholders are seeking leadership, standards, consistency, and transparency regarding effective corporate governance practices. Voluntary guidelines, as demonstrated by the low adoption rate of guidelines recommended in the Dey Report¹, will result in inconsistent implementation by market participants and lack of comparability for stakeholders in the global marketplace. By contrast, most of the recommended best practices appear as mandatory standards in competing international markets², and are considered fundamental elements of good governance.

The proposed best practices would therefore more appropriately reflect market expectations if they were mandatory.

4. *Monitoring, Assessment, and Feedback*

To assist Boards in fulfilling their mandate, the Policy on Effective Corporate Governance would be significantly enhanced if the Policy required timely monitoring, assessment, and feedback on the effectiveness of each of the proposed best practices. Monitoring is a key component of internationally accepted internal control frameworks, such as COSO or CoCo.

A strong internal auditing function would be well positioned to provide regular and timely assessments of these practices on behalf of boards and management, and support external reporting of their effectiveness.

5. *Specific Request for Comment - Responses*

Following are our responses to your *Specific Request for Comment*: on the Proposed Policy and Proposed Instrument.

1. The Proposed Policy and Proposed Instrument reflect many current best practices, and incorporate a number of the previous Toronto Stock Exchange (TSX) guidelines.
 - a. While we agree these initiatives will provide solid guidance to issuers, experience dictates that the proposed best practices would be significantly more effective were they mandatory.
 - b. We agree these initiatives will provide meaningful disclosure to investors; however, such disclosure would be enhanced if ongoing monitoring, assessment, and feedback processes, such as can be provided by internal auditing, were also required.
 - c. In our view, greater clarity, consistency, and comparability of practices would result from a requirement to disclose and describe specific practices relative to best practices described in the Policy, rather than descriptions relative to categories of governance principles.
 - d. In our opinion, publishing best practices in Canada will provide aspirational goals for market participants, but will not accomplish meaningful adoption and confidence of investors unless mandatory.

¹ *Five Years to the Dey*; 1999, Institute of Corporate Directors and TSX.

² Such as in Australia, England, France, South Africa, and the United States.

2. Ideally, boards should be required to adopt and disclose codes of business conduct and ethics; nevertheless:
 - a. Disclosure of the text of the code of ethics would contribute to clarity and transparency.
 - b. Disclosure of waivers from the code will provide useful disclosure for investors, and in addition, could effectively create a deterrent.
 - c. Since there is no requirement for a code of ethics, the obligation to disclose the text of any adopted code may indeed discourage adoption. However, mandatory adoption of a code of ethics and disclosure of the text would promote more consistent acceptance of best practices, and in addition, would create comparability and choice for investors.
3. Ideally, issuers should be required to have a compensation committee composed of independent directors with a charter that must be disclosed; nevertheless:
 - a. Investors would be well served by a requirement to disclose the process used to determine compensation, regardless of whether it has a compensation committee. Such disclosure would promote accountability, and discourage compensation practices that undermine stewardship obligations.
 - b. Disclosure of the text of the compensation committee's charter would be useful in informing investors about accountability with respect to compensation. However, establishing accountability alone in the absence of a description of the process used to determine compensation would be of limited value in discouraging inappropriate compensation practices or in creating transparency or confidence on the part of investors.
4. Ideally, issuers should be required to have a nominating committee composed of independent directors with a charter that must be disclosed; nevertheless:
 - a. It would be useful to investors for the issuer to disclose the process by which candidates are selected for board nomination, regardless of whether it has a nominating committee. Such disclosure would provide useful information about how directors' qualifications are determined, and promote rigor and due care in the nomination of qualified candidates that will lead to improved confidence by investors.
 - b. Disclosure of the text of the nominating committee's charter would be useful in informing investors about accountability with respect to nominations. However, establishing accountability alone in the absence of a description of the process used to determine qualifications and selection of appropriate candidates would be of limited value in discouraging inappropriate nominations or in creating transparency or confidence on the part of investors.
5. Ideally, position descriptions should be required for the roles of the board, committee chairs and CEO. In addition, it would be useful to investors for the issuer to disclose the assessment process for these roles. Position descriptions alone provide information only about expectations and accountability for these roles; disclosure of the assessment process would promote due diligence in establishing rigorous processes for evaluating performance against expectations, leading to greater transparency and ultimately creating confidence on the part of investors.

Concluding Remarks

The Institute of Internal Auditors expresses our appreciation for the opportunity to comment on these important proposals. We encourage the OSC/CSA to continue developing enhanced governance practices for Canadian issuers.