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April 25, 2008

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**Subject: CSA Concept Paper 52-402**  
**Possible changes to securities rules relating to International Financial Reporting Standards**

Dear Mrs. Hait and Mrs. Anctil-Bavas:

We have read the attached response letter dated April 7, 2008, and submitted by Canadian National Railway ("CN") with respect to CSA Concept Paper 52-402, "Possible changes to securities rules relating to International Financial Reporting Standards." We are in full agreement with the responses and the examples discussed in that letter. In particular, we strongly feel that Canadian companies that have prevailed themselves of the choice given to them by the Canadian regulators of filing US GAAP financial statements should be allowed to continue to do so until time as U.S. domestic companies are required to adopt IFRS.

We thought that it would be more efficient and convenient for you by expressing our response in this manner and we trust that you will consider our comments in the final version.

Yours truly,



Picklu Datta, C.A.  
Controller

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April 7, 2008

**BY EMAIL**

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**Subject: CSA Concept Paper 52-402**  
***Possible changes to securities rules relating to International Financial Reporting Standards***

Dear Mrs. Hait and Mrs. Anctil-Bavas:

Thank you for the opportunity to provide our comments on the proposed rule "Concept Paper 52-402 Possible changes to securities rules relating to International Financial Reporting Standards" (the "Concept Paper") issued by the Canadian Securities Administrators ("CSAs") on February 13, 2008.

The railway industry in North America is mainly represented by five major companies in the U.S. and two in Canada. Canadian National Railway Company, together with its wholly-owned subsidiaries (collectively "CN"), is the largest railway in Canada with a market capitalization of about \$23 billion and ranks third in market capitalization among North American railways. CN's shares are publicly traded on both the Toronto and New York Stock Exchanges.

Shortly after its privatization in 1995, CN realized the importance of issuing comparable financial statements with most of the other major North American railways in the industry. Consequently, since 1998, CN's primary internal and external financial reporting has been under U.S. generally accepted accounting principles (US GAAP). Initially, from 1998 to 2005, CN produced two sets of financial statements: one under Canadian generally accepted

accounting principles (Canadian GAAP) with a reconciliation to US GAAP to meet the regulatory requirements and one under US GAAP to facilitate comparability with its competitors. In 2004, CN welcomed the initiative by the CSAs to reduce certain financial reporting costs by allowing SEC issuers to file US GAAP financial statements in Canada. Since 2005, CN has been using US GAAP as its sole reporting base to shareholders, mainly due to the fact that the U.S. market is CN's main source of financing. Also, its shareholders and analyst groups generally review CN's performance against that of other Class I railroads in the U.S.

The CSA National Instrument 52-107, which permitted CN and other SEC issuers the opportunity to prepare one set of financial statements in accordance with US GAAP was a great initiative for Canadian companies to reduce costs, increase their competitiveness and attract a wider base of investors. As a result of this change, CN has significantly reduced its financial reporting costs, one of the main reasons cited by the CSAs in adopting National Instrument 52-107, and eliminated any confusion that might result from dual reporting. In fact, since 2005, there has not been a single request made to CN for Canadian GAAP financial statements.

CN supports the harmonization of accounting principles for financial reporting. As globalization progresses rapidly, the initiative to move towards one common set of accounting standards worldwide has to be commended. The major challenge is how to achieve that objective without causing detrimental effects on Canadian companies, including implementation and financial reporting costs. CN's main concern with the Concept Paper centers on the implementation timeline. The CSAs' tentative conclusion that would, after the year 2013, disallow a SEC issuer, like CN, the option to prepare one set of financial statements under US GAAP, would, in our view, be a step backwards and needs to be reviewed considering all factors. In particular, it is important for CN to be allowed to change to IFRS reporting at the same time as the substantial majority of its competitors (i.e., other U.S. based Class I railroads) are required to adopt IFRS. To impose additional financial reporting costs on CN, when the harmonization objective should be coordinated with the U.S., seems inefficient and unfair. We believe that those Canadian companies that have availed themselves of the choice given to them by the Canadian regulators of filing US GAAP financial statements should be grandfathered until such time as U.S. domestic companies are required to adopt IFRS. It would be unfair and harmful to take away a choice already granted by Canadian regulators. Such action would effectively impose additional costs on those companies that availed themselves of the option to report in US GAAP, without any real benefits to society or the investment community as CN is analyzed in comparison with its U.S. competitors that would continue to report in US GAAP.

There are also implementation issues that regulators must consider when moving from Canadian or US GAAP to IFRS. One example of a difference between US GAAP and IFRS, which is expected to be very costly for not only the railway industry, but also for other industries using the group method of accounting for properties, is the requirement to use "componentization accounting" under IFRS. Such a change would require significant system changes for railway companies. Componentization accounting for properties has been a topic

that created a significant amount of debate when it was being reviewed by the U.S. regulators. Following several years of discussion, the topic was put on hold (or dropped) for US GAAP purposes. Not knowing how this difference between US GAAP and IFRS will be resolved is an important issue. It will be costly and inefficient to force the railway industry to use componentization accounting for properties through the required adoption of IFRS, when there exists a real possibility that the discussions leading to the implementation of IFRS for U.S. companies may result in componentization no longer being required under IFRS.

From a market demand perspective, CN and other SEC issuers in Canada will need to continue reporting under US GAAP until the United States Securities and Exchange Commission ("SEC") adopts IFRS-IASB for U.S. domestic filers. Therefore, the proposed CSA rule requiring financial statements under IFRS-IASB would have the effect of substantially increasing the financial reporting costs of Canadian companies that are SEC filers; costs that had been effectively eliminated by National Instrument 52-107. In CN's case, it would mean going back to producing two sets of financial statements, as U.S. traded Canadian companies that do not also report in US GAAP would run the risk of having investors discount the value of their shares due to the lack of comparable accounting and financial information with U.S. companies. When faced with such increasing costs, Canadian companies will be asked to explore options to eliminate such costs. The results may lead to undesirable consequences.

Canadian companies that currently use US GAAP face additional challenges, as they will not be able to rely on the Canadian Institute of Chartered Accountants (CICA) for guidance on differences between US GAAP and IFRS. Consequently, we urge our Canadian regulators to work with the accounting professions in both Canada and the U.S. to ensure an even playing field for companies competing within North America and determine an appropriate timeline for the orderly conversion to IFRS of all such North American companies.

The CSAs have been instrumental in bringing about many positive outcomes for Canadian issuers in recent years. Considering however, the convergence of Canadian and U.S. business activity, the continuous investor benchmarking of financial performance within North American industry groups, the reliance by Canadian companies on U.S. capital markets for liquidity and financing and the cost of preparing additional sets of financial statements, it is our view that a Canadian company, which is also an SEC issuer should be permitted to retain the option to file one set of financial statements in accordance with US GAAP, and this beyond the year 2013 or until U.S. domestic companies are required to use IFRS. This will permit Canadian issuers to be competitive and comparable with similar U.S. companies.

In conclusion, it is our strongly held view that the most appropriate course of action is for the CSAs to continue to permit SEC issuers in Canada to prepare and file their financial statements using US GAAP until such time as the SEC adopts IFRS-IASB for its domestic filers in the United States, particularly for those companies that are currently filing under US GAAP. The Canadian and U.S. economies are so inter-twined that we propose that the accounting regulators in both Canada and the U.S. work together to maintain an even playing field in both countries by ensuring that all North-American SEC filers convert to IFRS at the same time.

For your convenience, we have also attached to this letter an appendix with answers to those specific questions included in the discussion paper.

If you wish to discuss our comments please feel free to contact me or Serge Pharand, Vice-President and Corporate Comptroller, at (514) 399-4784.

Yours truly,



Claude Mongeau

cc: Fred Snell, Chief Accountant, Alberta Securities Commission  
John Carchrae, Chief Accountant, Ontario Securities Commission  
Marion Kirsh, Associate Chief Accountant, Ontario Securities Commission

## Appendix A

**Question 1: Do you agree we should allow a domestic issuer to adopt IFRS-IASB for a financial year beginning on or after January 1, 2009? If not why?**

- CN generally favors early adoption of accounting rules. Consequently, if practical for certain companies and given the long-term objective, we agree with giving this option to a company.

**Question 2: Are there additional factors, not discussed in this paper, to consider in deciding whether to allow a domestic issuer to adopt IFRS-IASB before 2011?**

- Some domestic issuers might decide to list in the U.S. only.
- Any requirement to use Canadian GAAP during the early adoption period would need to be amended to also allow IFRS.

**Question 3: Do you agree we should not allow a SEC issuer to use US GAAP for financial years beginning on or after January 1, 2009, with the exception that SEC issuer filing US GAAP financial statements in Canada for its most recent financial year ending on or before December 31, 2008, could continue doing so until 2013? If not, why do you disagree, and how if at all would you modify existing rules?**

- We believe that an SEC issuer filing US GAAP financial statements in Canada for its most recent financial year ending on or before December 31, 2008 should be allowed to continue using US GAAP financial statements until all domestic U.S. companies are required to file under IFRS. Most of those companies compete with companies that will be required to use US GAAP. Consequently, not allowing our Canadian companies to use US GAAP may result in investors discounting the value of their shares, unless such companies incur the additional costs associated with also producing US GAAP financial statements.

**Question 4: Are there additional factors, not discussed in this paper, to consider in deciding whether to allow a SEC issuer to use US GAAP?**

- While the objective of one set of accounting rules covering the world is an objective that CN supports, the CICA's shift in direction from US GAAP to IFRS is alarming. Is there a risk that the CICA changes direction again a few years down the road (i.e., reverting back towards US GAAP)? Consequently, the key question, at this time, is when will U.S. issuers be required to report under IFRS rather than US GAAP.

- One example of a difference between US GAAP and IFRS, which is expected to be very costly for the railway industry, is the requirement to use componentization accounting under IFRS. Such a change would require significant system changes for railway companies. Componentization accounting has been a topic that created a lot of debate when it was being reviewed by the U.S. regulators. Following several years of discussion, the topic was put on hold (or dropped) for US GAAP purposes. Not knowing how this difference between US GAAP and IFRS will be resolved is a significant issue. It would be frustrating for the railway industry to be forced to use componentization accounting through a required adoption of IFRS with a risk that this IFRS requirement be reversed as a result of discussions leading to the implementation of IFRS for U.S. companies.
- Canadian investors and analysts can only make informed investment decisions if an entity is benchmarked against its competitors, which in most instances for CN are in the U.S. (i.e., five out of six of the Class I Roads are U.S. and publish US GAAP financial statements). Therefore, if CN is required to adopt IFRS it might have a negative impact on the company because when investors and analysts compare CN against its U.S. competitors they would not get comparability of financial statements due to the differences between US GAAP and IFRS. CN would therefore be forced to produce both IFRS and US GAAP financial statements, in addition to a further required set of financial statements that must be produced under the Canada Transportation Agency rules. This consequence would be contrary to the spirit of the original NI 52-107, which was intended to reduce costs, increase competitiveness and attract a wider base of investors.
- The preparation of financial statements is a cost that must be borne by the company and is an expensive undertaking. If CN were required to adopt IFRS then it would likely have to produce two sets of financial statements for an extended period of time. The preparation of two sets of financial statements for CN can place a significant cost burden on the company and put the company at a disadvantage with respect to its U.S. peers, who will not be required to file under IFRS until such time as the SEC adopts IFRS, and therefore only have to incur costs for one set of statements at any time.
- While there have been significant improvements in IFRS over the past few years, the IFRS guidance does not provide the same in-depth guidance and rigorous consistent application as found in US GAAP. Therefore, there is a need for improved guidance on complex topics such as derivatives, stock based compensation, pensions and income taxes, to be equivalent to the guidance found in US GAAP.
- CN shareholders in both Canada and the U.S. have come to understand and depend on US GAAP financial statements issued by the company. If CN's financial statements were to be converted to IFRS it would create an atmosphere of unfamiliarity and confusion for our shareholders because our shareholders have limited exposure to IFRS. Although Canadian shareholders will over time become familiar with IFRS, our U.S. shareholders will not until the SEC adopts IFRS. CN will have to continue to support its U.S. shareholder base by providing US GAAP financial statements even though it adds significantly to the cost of financial reporting.

**Question 5: Is the proposed transitional period of five years from 2009 to 2013 appropriate?**

- The answer will depend on the harmonization program between US GAAP and IFRS. Today one can argue that US GAAP and Canadian GAAP are very similar. As a result the Canadian investment, accounting, education and government communities may be very familiar with both GAAPs. IFRS however appears to have major differences with both Canadian and US GAAP. Normally, a five-year time period is a sufficient time period to implement accounting systems and controls, educate preparers and perform testing under an IFRS environment. However, because of the major differences between Canadian GAAP and IFRS, we suggest that the CSA regularly review the progress on converting to IFRS by Canadian companies, investors, analysts, auditors, educators and governments.
- Canadian companies that currently use US GAAP face additional challenges, as they will not be able to rely on the Canadian Institute of Chartered Accountants (CICA) for guidance on differences between US GAAP and IFRS. Consequently, the transitional period should be directly linked with the transitional period that will be required for U.S. domestic companies to convert to IFRS. There should be no time limit until that decision is made in the U.S. Otherwise, we are putting certain Canadian companies at a cost and competitive disadvantage.

**Question 6: Do you agree that we should require a domestic issuer to prepare its financial statements in accordance with IFRS-IASB and require an audit report on such annual financial statements to refer to IFRS-IASB? If not, why?**

- A domestic issuer should prepare its financial statements in accordance with IFRS-IASB and require an audit report on such financial statements to refer to IFRS-IASB because continued usage of Canadian GAAP will give the impression that Canada has a specific version of IFRS. To allow the impression that Canada has a specific version of IFRS goes against the objective of uniform accounting standards throughout the world, which is to adopt a single set of high-quality accounting standards accepted globally.

**Question 7: Are there additional factors, not discussed in this paper, to consider in deciding whether securities rules should refer to IFRS-IASB rather than Canadian GAAP?**

- We would like to see the establishment of a special committee, which would be comprised of Canadian and U.S. accounting representatives. This special committee would not only work on a coordinated implementation schedule but would also issue specific guidance addressing situations that are unique to Canada or the U.S. This guidance would help the implementation of IFRS in unique situations and would effectively be generally accepted under IFRS.