

Notice of National Instrument 52-108 *Auditor Oversight*

Introduction

National Instrument 52-108 *Auditor Oversight* (the “Instrument”) is an initiative of the Canadian Securities Administrators (“CSA” or “we”). The Instrument was first published for comment as a multilateral instrument. Since publication, however, British Columbia has decided to participate in this initiative and the Instrument is now being adopted as a national instrument and will take effect in all jurisdictions.

The Instrument is expected to be adopted as a rule in each of Alberta, British Columbia, Manitoba, Newfoundland and Labrador, Nova Scotia, Ontario and Québec, as a Commission regulation in Saskatchewan and Nunavut, as a policy in New Brunswick, Prince Edward Island and the Yukon Territory, and as a code in the Northwest Territories.

In Alberta, the Instrument and other materials were delivered to the Minister of Revenue. The Minister may approve or reject the Instrument. Subject to Ministerial approval, the Instrument will come into force on March 30, 2004. The Alberta Securities Commission will issue a separate notice advising whether the Minister has approved or rejected the Instrument.

In British Columbia, the Minister of Competition, Science and Enterprise gave his approval in principle of the Instrument on July 25, 2003. The Instrument will be adopted as a rule and come into force in British Columbia on March 30, 2004, subject to obtaining final Ministerial approval.

In Nova Scotia, the Instrument will be delivered to the Minister for non-objection by the Governor in Council in accordance with Nova Scotia securities law after it is adopted as a rule by the Commission. If the Instrument is not objected to by the Governor in Council, it will come into force on March 30, 2004.

In Ontario, the Instrument and other required materials were delivered to the Minister of Finance on January 14, 2004. The Minister may approve or reject the Instrument or return it for further consideration. If the Minister approves the Instrument or does not take any further action by March 15, 2004, the Instrument will come into force on March 30, 2004.

In Québec, the Instrument is a regulation made under section 331.1 of *The Securities Act* (Québec) and must be approved, with or without amendment, by the Minister of Finance. The Instrument will come into force on the date of its publication in the *Gazette officielle du Québec* or on any later date specified in the regulation. It must also be published in the Bulletin.

Provided all necessary ministerial approvals are obtained, we expect to implement the Instrument on March 30, 2004.

Substance and Purpose

The purpose of the Instrument is to contribute to public confidence in the integrity of financial reporting of reporting issuers by promoting high quality, independent auditing.

Where a reporting issuer files its financial statements accompanied by an auditor's report, the Instrument will require the reporting issuer to have the auditor's report signed by a public accounting firm that is:

- a participant in the Canadian Public Accountability Board ("CPAB") oversight program for public accounting firms that audit reporting issuers (the "CPAB Oversight Program"), and
- in compliance with any restrictions or sanctions imposed by the CPAB.

In addition, other than in Alberta, British Columbia and Manitoba, the Instrument will require a public accounting firm that prepares an auditor's report with respect to the financial statements of a reporting issuer to:

- be a participant in the CPAB Oversight Program;
- be in compliance with any sanctions or restrictions imposed by the CPAB, and
- provide notice, in certain situations, of any restrictions or sanctions imposed by the CPAB to their audit client and to the securities regulator in each jurisdiction in which the audit client is a reporting issuer.

Refer to the section of this notice dealing with "Application and Transition" for a discussion of situations in which public accounting firms in Alberta, British Columbia and Manitoba or elsewhere may still be required to follow the above requirements.

Background

The CPAB was created to address concerns relating to investor confidence in the credibility of auditors and audited financial information. Established in July 2002, a key mandate of the CPAB is to promote high quality external audits of reporting issuers. One of the ways it will achieve this is through registering and inspecting public accounting firms that prepare auditors' reports with respect to the financial statements of reporting issuers.

The CPAB has begun registering public accounting firms that prepare auditors' reports in connection with the financial statements of reporting issuers. To date, approximately 240 accounting firms have indicated they intend to participate in the CPAB Oversight Program and we expect that most of these will complete the registration process by February 29, 2004.

The CPAB registration process involves two phases. The first phase required public accounting firms to file an 'intent to participate form' and a 'quality control report' with the CPAB by December 31, 2003. The second phase requires public accounting firms (other than foreign

public accounting firms) to file with the CPAB by February 29, 2004 an initial registration form and a signed participation agreement. Foreign public accounting firms will have until July 19, 2004 to file these documents. The participation agreement sets out requirements with which participating firms must comply, such as adhering to quality control standards established by the CPAB and submitting to regular inspections. A copy of the participation agreement, together with further information about the registration process, can be obtained from the CPAB website at www.cpab-ccrc.ca.

Summary of Written Comments Received by the CSA

The Instrument was first published for comment on June 27, 2003 by all CSA jurisdictions except British Columbia. It was published for comment on September 3, 2003 for 60 days in British Columbia. During the comment periods, we received submissions from 18 commenters. We have considered the comments received and thank all the commenters. The names of all the commenters are contained in Appendix A of this notice and a summary of their comments, together with the CSA responses, is contained in Appendix B of this notice. All of the changes made since the publication of the materials are reflected in the blacklined version of the Instrument contained in Appendix C of this notice.

After considering the comments, we have made amendments to the Instrument. However, as these changes are not material, we are not republishing the Instrument for a further comment period.

Summary of Changes to the Instrument

Set out below are notable changes made to the Instrument since it was published for comment.

1. National Instrument

As a result of British Columbia's decision to participate, the Instrument is now a national instrument and will take effect in all jurisdictions in Canada.

2. Part 1 - Definitions

(a) “Participant in Good Standing”

The definition of “participant in good standing” has been deleted from the Instrument. The substantive requirements of the definition have been incorporated into sections 2.1 and 2.2, and modified such that a public accounting firm must be a participating audit firm and be in compliance with any restrictions or sanctions imposed by the CPAB as of the date of the auditor’s report.

(b) “Participating Audit Firm”

The definition of “participating audit firm” has been amended to ensure that a public accounting firm is a participant in the CPAB Oversight Program at each date on which it signs an auditor’s report with respect to the financial statements of a reporting issuer. This change reflects the fact

that even though a participating audit firm may have entered into a participation agreement, its status as a participant in the CPAB Oversight Program may be terminated by the CPAB in accordance with CPAB By-Law No. 1.

(c) “Public Accounting Firm”

The definition of “public accounting firm” has been amended to capture the various forms of legal entities under which public accountants may organize their business.

3. Part 1 - Application and Transition

Section 1.2 has been amended to clarify both the Instrument’s application and transition.

With respect to the application of the Instrument, we note that section 2.2 is being adopted in each jurisdiction in Canada. Accordingly, this section applies to every issuer that is a reporting issuer and that files its financial statements in at least one Canadian jurisdiction.

In contrast, because the securities commissions in Alberta, British Columbia and Manitoba do not have authority to make rules imposing obligations directly on auditors, section 2.1 and Part 3 are not being adopted in Alberta, British Columbia and Manitoba.

It should be emphasized, however, that while section 2.1 and Part 3 do not apply in Alberta, British Columbia and Manitoba, a public accounting firm situated in one of these provinces or elsewhere may still be subject to the requirements in section 2.1 and Part 3 by virtue of the fact that one of its clients is a reporting issuer in one of the other jurisdictions in Canada.

For example, a public accounting firm situated in British Columbia that prepares an auditor's report for a client situated in British Columbia that is a reporting issuer in British Columbia, Alberta, Ontario, and Quebec, would be subject to the requirements of each of the provinces in which its client is a reporting issuer. Under British Columbia and Alberta securities law, the public accounting firm would not be required to comply with section 2.1 and Part 3. However, because it is preparing an auditor’s report with respect to the financial statements of an issuer that is also a reporting issuer in Ontario and Quebec, the public accounting firm would be required to comply with section 2.1 and Part 3 under Ontario and Quebec securities law. In other words, it is the client's reporting issuer status in a jurisdiction, not the physical location of a client or the physical location of a public accounting firm that determines whether the Instrument applies to a public accounting firm.

With respect to transition, subsection (3) makes it clear that once the Instrument takes effect it does not apply to either a public accounting firm or a reporting issuer unless:

- (a) the deadline for that public accounting firm to register with the CPAB has expired, and
- (b) the auditor’s report prepared by the public accounting firm is dated on or after March 30, 2004.

For example, if a Canadian public accounting firm prepares an auditor’s report dated March 29, 2004 respecting the financial statements of a reporting issuer, the Instrument will not apply. This

is because, despite the fact that the February 29, 2004 registration deadline prescribed by the CPAB will have expired, the auditor's report is dated before March 30, 2004. The outcome will be the same even if the financial statements are filed on or after March 30, 2004.

If the auditor's report is dated March 31, 2004, then the Instrument will apply. As a result, the reporting issuer filing its financial statements will have to ensure that, as of March 31, 2004, the auditor's report accompanying those financial statements is signed by an auditor that has registered with the CPAB and is in compliance with any CPAB restrictions or sanctions.

In situations where a foreign public accounting firm has prepared the auditor's report, the Instrument will not apply until after the CPAB prescribed registration deadline of July 19, 2004 has expired.

4. Part 2 - Auditor Oversight

Part 2 of the Instrument has been amended to clarify which obligations are imposed on public accounting firms and which obligations are imposed on reporting issuers. We have also removed the references to "the time period prescribed by the CPAB." These references were intended to clarify that the Instrument did not apply to a public accounting firm or a reporting issuer until such time as the registration deadline set by the CPAB had expired. However, as a result of the transitional provision that is now built into subsection 1.2(3), these references are no longer necessary.

Subsections 2.1 and 2.2 have been amended to require that, as of the date of its auditor's report, a public accounting firm must be a participating audit firm and in compliance with any restrictions imposed on it by the CPAB. This change was made in response to a comment and is intended to remove any ambiguity as to when the conditions in paragraphs (a) and (b) have to be met.

Subsection 2.2 has also been amended to clarify that the requirements with respect to appointing a public accounting firm apply in connection with the reporting issuer's own financial statements only and not, for example, to financial statements of another issuer that the reporting issuer might file as a condition of an exemptive relief order provided in connection with an exchangeable security transaction.

5. Part 3 - Notice

We have rearranged the provisions under Part 3 so that the sections on notice of restrictions appear before the sections on notice of sanctions.

We have also changed the references respecting the auditor having been "engaged" to now refer to the auditor being "appointed". We believe these changes better align the Instrument with the fact that auditors usually act as the auditors of reporting issuers until they either resign or are no longer re-appointed.

We have also increased the notice periods set out in subsection 3.2(3) and 3.3(3) from five to ten business days. These changes have been made in response to commenters' recommendations

that the notice periods be extended to provide more time for public accounting firms to prepare and deliver the required notices.

Section 3.4 was amended to clarify that, before a public accounting firm can accept an appointment, it must ensure it has provided notice to a reporting issuer client and the regulator of (a) any failures to address defects in its quality control systems to the satisfaction of the CPAB if these failures occurred within the 12-month period immediately preceding the expected date of appointment, and (b) any sanctions imposed by the CPAB within the 12-month period immediately preceding the expected date of appointment.

Finally, the notice provisions in Part 3 were amended to clarify that where a reporting issuer does not have an audit committee, the applicable notice should be delivered to the issuer's board of directors or the person or persons responsible for reviewing and approving the reporting issuer's financial statements.

6. Part 5 - Effective Date

The effective date for the Instrument has been changed to March 30, 2004.

Questions

Please refer your questions to any of:

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National Instrument

The text of the Instrument follows.

Dated: January 16, 2004