CANADIAN SECURITIES ADMINISTRATORS NOTICE NO. 1

AUDIT COMMITTEES

INTRODUCTION

1. Increasingly the Canadian Securities Administrators are being asked their views concerning the role and the responsibilities that should be adopted by audit committees. The Administrators strongly support the efforts of audit committees which significantly improve the quality of financial reporting. This notice sets out certain practice standards which should be followed if an audit committee is to discharge its responsibilities in an effective way.

2. An audit committee is a committee of the board of directors to which the board delegates its responsibility for oversight of the financial reporting process.

3. The objectives of an audit committee, as stated in a research study published by the Canadian Institute of Chartered Accountants, are as follows:

(a) to help directors meet their responsibilities, especially for accountability;

(b) to provide better communication between directors and external auditors;

(c) to enhance the external auditor's independence;

(d) to increase the credibility and objectivity of financial reports; and

(e) to strengthen the role of the outside directors by facilitating in depth discussions between directors on the committee, management and external auditors.

4. A number of recent reports, such as the Report of the Commission to Study the Public's Expectations of Audits (the MacDonald Commission), have concluded that an audit committee can make a major contribution towards improving the quality of financial reporting. This relates to a fundamental requirement of securities regulation and the Administrators agree with this conclusion.

5. Audit committees are a relatively recent development and it is emphasized that their role is continuing to evolve. Boards of directors or reporting issuers should adapt the responsibilities of their audit committees to their particular circumstances. It is also emphasized that no published set of practices can substitute for the active commitment to high standards by every party having responsibility for the corporate disclosure system.

6. The practices outlined in this notice complement the requirements for audit committees set out in the

corporate law statutes and, in the view of the Administrators, can be followed without conflict with those requirements.

7. The Administrators consider that fulfilment of the responsibilities set out in this notice will result in an audit committee becoming more informed, vigilant and effective.

8. Boards of directors of reporting issuers are encouraged to incorporate these matters in the terms of reference for their audit committees. Consideration should be given to disclosing the terms of reference to shareholders annually.

INTERIM FINANCIAL STATEMENTS.

9. The Administrators gave particular consideration to the matter of audit committee review of interim financial statements. Financial statement users rely heavily on interim financial statements but interim reporting is subject to fewer controls than annual reporting. While the external auditor may review quarterly results, any such review is frequently part of the annual audit which is conducted after the end of the fiscal year, at which time it is too late to take corrective action.

10. The Administrators recommend that audit committees review interim financial information before it is released to the public.

MEMBERSHIP OF AUDIT COMMITTEES

11. The Administrators strongly encourage boards of directors of reporting issuers to select independent directors as members of audit committees and to limit membership to such directors whenever possible.

12. The chairperson of the audit committee should be an independent director.

13. An audit committee should normally consist of no fewer than three persons.

MEETINGS

14. Meetings of the audit committee should be scheduled to take place on a regular basis.

15. Opportunities should be afforded periodically to the external auditor, the internal auditor and to senior management to meet separately with the independent members of the audit committee.

16. Minutes should be kept of all meetings of the audit committee.

RESPONSIBILITIES OF AUDIT COMMITTEES

17. The audit committee should periodically report the results of reviews undertaken and any associated recommendations to the board of directors.

18. Audit committee practices intended to preserve the independence of the external auditor should include the following:

(a) review management's recommendations for the appointment of an external auditor;

(b) review the terms of the external auditor's engagement, the appropriateness and reasonableness of the proposed audit fees and any unpaid fees;

(c) when there is to be a change of auditor, review all issues related to the change, including the information to be included in the notice of change of auditor called for under national Policy 31, and the planned steps for an orderly transition;

(d) review all reportable events, including disagreements, unresolved issues and consultations, as defined in National Policy 31, on a routine basis, whether or not there is to be a change of auditor; and

(e) review any engagements for non-audit services to be provided by the external auditor's firm or its affiliates, together with estimated fees, and consider the impact on the independence of the external auditor.

19. Audit committee practices related to audits and financial reporting should include the following:

(a) review the audit plan with the external auditor and with management;

(b) review with management and with the external auditor any proposed changes in major accounting policies, the presentation and impact of significant risks and uncertainties, and key estimates and judgements of management that may be material to financial reporting;

(c) question management and the external auditor regarding significant financial reporting issues discussed during the fiscal period and the method of resolution;

(d) review any problems experienced by the external auditor in performing the audit, including any restrictions imposed by management or significant accounting issues on which there was a disagreement with management;

(e) review audited annual financial statements, in conjunction with the report of the external auditor, and obtain an explanation from management of all significant variances between comparative reporting periods;

(f) review the post-audit or management letter, containing the recommendations of the external audit, and management's response and subsequent follow-up to any identified weaknesses;

(g) review interim unaudited financial statements before release to the public;

(h) review all public disclosure documents containing audited or unaudited financial information before release, including any prospectus, the annual report, the annual information form and management's discussion and analysis;

(i) review the evaluation of internal controls by the external auditor, together with management's response;

(j) review the terms of reference of the internal auditor;

(k) review the reports issued by the internal auditor and management's response and subsequent follow-up to any identified weaknesses; and

(l) review the appointments of the chief financial officer and any key financial executives involved in the financial reporting process.

20. The responsibilities outlined in this notice are not intended to be comprehensive. Boards of directors of reporting issuers should consider any additional areas which may require oversight when determining the responsibilities to be assigned to the audit committee.