

# Delivering Value Through World Class Audit Regulation



CANADIAN PUBLIC ACCOUNTABILITY BOARD  
2010 ANNUAL REPORT

# Delivering Value

The Canadian Public Accountability Board (CPAB) delivers value to its various stakeholders through world class audit regulation. Through its inspection of firms that audit reporting issuers in Canada, CPAB contributes to public confidence in the integrity of financial reporting by promoting high-quality, independent auditing. As CPAB continues the next stage of development, the organization will enhance its capability as a high-quality regulator in four key areas.

- **Rigorous, consistently applied methodology**

Delivering value means imparting useful and insightful inspection findings to firms, including comments on the root causes of deficiencies that provide firms with unique insight into their performance and into audit risk matters and practices. CPAB strives to report, on a timely basis, findings based on high-quality inspections that are risk-based, conducted efficiently, based on current standards and predicated on a rigorous, consistently applied methodology.

- **An accountability mindset**

As it evolves as a regulator, CPAB continues to more fully assume the accountability incorporated in its mandate. To succeed, CPAB must increase accountability across the organization so that the roles, responsibilities and interdependencies of each division and each person are clear. There must also be reward and consequence for how these accountabilities are put into operation.

- **An advanced skill set for broader risk assessment**

Having successfully recruited top talent, CPAB must now focus on the further development and retention of staff. Staff skills must move from those of auditors to those of effective audit regulators.

- **Identification of key risks in audit practices**

CPAB has enhanced its risk assessment capabilities, and now uses a more robust risk analysis process to identify higher-risk firms and engagements. Going forward, CPAB's inspection methodology must become more strategic, provide better risk assessment, and add more relevance to participating firms.

## TABLE OF CONTENTS

2	REPORT OF THE CHAIR
5	CPAB BOARD MEMBERS
6	REPORT OF THE CHIEF EXECUTIVE OFFICER
12	CPAB MANAGEMENT COMMITTEE
13	INSPECTION ACTIVITY
16	MANAGEMENT'S DISCUSSION AND ANALYSIS
20	2011 CPAB OPERATING BUDGET
22	STATEMENT OF MANAGEMENT'S RESPONSIBILITY
23	INDEPENDENT AUDITOR'S REPORT
24	FINANCIAL STATEMENTS
31	CORPORATE INFORMATION

## CPAB'S MISSION:

TO CONTRIBUTE TO PUBLIC CONFIDENCE IN THE INTEGRITY OF FINANCIAL REPORTING OF REPORTING ISSUERS IN CANADA BY EFFECTIVE REGULATION AND PROMOTING QUALITY, INDEPENDENT AUDITING.

# ... to our stakeholders

Building relationships with key stakeholders is critical to CPAB's success. CPAB is developing a comprehensive program to enhance its communications and outreach to its stakeholders, including the investor community, Audit Committees, audit firms, and regulators.

## INVESTOR COMMUNITY

High-quality audits mean all investors, from large institutional investors to individuals, can have confidence in the integrity of financial statements issued by public companies in Canada. In performing an audit, the auditor gains an in-depth understanding of the business and related systems and processes. Through its inspection activity, CPAB develops recommendations that, when implemented by participating audit firms, will add value to audit quality. This should reduce the possibility of audit deficiencies.

## AUDIT COMMITTEES

Audit Committees are an important oversight and entity-wide control feature of corporate governance. CPAB believes continuous improvement in the two-way communications between audit firms and Audit Committees enhances audit quality. CPAB enhanced its outreach to Audit Committees in 2010 and will continue to do so in the coming year.

## AUDIT FIRMS

Annually, CPAB inspects all audit firms that audit more than 100 reporting issuers, representing 99.5 per cent of the total market if measured by market capitalization. There are now 15 firms in this category. CPAB also regularly inspects firms that audit fewer than 100 reporting issuers. These firms account for \$6.9 billion, measured by market capitalization.

## REGULATORS

CPAB works in cooperation with a variety of national and provincial regulators in Canada, including the Office of the Superintendent of Financial Institutions, provincial securities regulators, federal and provincial departments and ministries, and national and provincial accountants' institutes and associations. CPAB also participates in the International Forum of Independent Audit Regulators (IFIAR), which helps develop cooperative arrangements with other national auditor oversight authorities and encourages dialogue on auditor inspection techniques, results and remediation.



# Delivering Value

**The Canadian Public Accountability Board delivers value to its various stakeholders through world class audit regulation. Its stakeholders are investors, other users of financial statements, and the Canadian public generally, who benefit from integrity in financial reporting that supports vibrant, efficient capital markets. Through its inspection of firms that audit reporting issuers in Canada, CPAB contributes to public confidence in the integrity of financial reporting by promoting high-quality, independent auditing.**

During its first six years of operation, CPAB focused primarily on developing and implementing an inspection methodology that added significant value to the firms auditing reporting issuers. In 2009, CPAB moved to the next stage of its development. The organization's strategic plan identified a new vision: To be viewed domestically and internationally as a world class audit regulator. CPAB has in the first year of the strategic plan taken a number of steps to realize this vision, including significant investments in human resource management, inspection methodology, technology and systems, stakeholder relations and regulatory affairs.

Based on its strategic plan, CPAB is delivering on a new value proposition for its key stakeholders. The organization is operating at a more strategic level and is demonstrating relevance in the form of added value to many of the audit firms it oversees.

Since its incorporation in 2003, CPAB has issued seven annual Public Reports on its inspection results. The first five Public Reports summarized inspection findings.

Two years ago, CPAB changed its approach to focus on the root causes of audit deficiencies and to highlight the key recommendations that, if implemented, would have the greatest impact on improving audit quality. CPAB has also enhanced its risk assessment capabilities, and now uses a more robust risk analysis process to identify higher-risk audit firms and audit engagements.

In the seven years that CPAB has been conducting inspections, the organization has seen numerous examples of high-quality audit work. Many firms have significantly improved audit quality by implementing CPAB's recommendations while others have undertaken their own initiatives to improve audit quality. Overall, CPAB believes that audit quality in Canada continues to be sound.

In general, investors can have confidence in the integrity of public company financial statements that have been audited in Canada. In particular, audit quality is generally sound for the major audit firms' largest and most complex clients. But audit quality is not uniformly high across all engagements in all firms, and, even for major firms, there can be occasional lapses that result in reduced quality.

Similarly, smaller and mid-sized audit firms with focused engagement clientele in sectors that they fully understand also demonstrated sound audit quality in engagements reviewed by CPAB. Audit quality issues for these firms are more likely to arise in instances where they either audit very few public companies or else undertake audits of a few reporting issuers outside their comfort zone. This can also happen in major firms where certain offices or partners may, on occasion, also deal with audits that pose complexities outside their comfort zone.

CPAB BELIEVES THAT  
AUDIT QUALITY  
IN CANADA  
CONTINUES TO  
BE SOUND

CPAB believes that public company auditors in Canada should strive for continuous improvement in audit quality. However, overall, CPAB saw little improvement in audit quality from 2009.

CPAB is also concerned that a number of factors, including the fee pressure on audit firms, economic uncertainty, looming professional skills shortages and the transition to new accounting and auditing standards, may negatively affect audit quality.

### Strategic Plan Update

In November 2010, CPAB's Board of Directors and management reviewed its strategic plan to assess progress made during the year and to confirm that the plan's basic direction remains appropriate.

The Board has reconfirmed CPAB's mission and vision statement, and expanding the organization's mandate is not a current priority. From a brand perspective, CPAB took a number of steps in 2010 to raise its profile, including participating in round tables with Audit Committees and commissioning a survey of firms on CPAB's performance as a regulator. More work needs to be done to raise CPAB's profile, as the organization is not well known or understood by members of the business community, reporting issuers and the investing public. As well, the integrity of financial reporting and the quality of the audit depend on efforts by reporting issuers and their Audit Committees, not just on audit firms and CPAB.

ATTRACTING,  
DEVELOPING AND  
RETAINING TOP  
TALENT IS CRITICAL  
TO CPAB'S SUCCESS



CPAB's approach to enterprise risk management has a guiding principle of zero tolerance for reputational risk to CPAB. This risk resides in three main areas: inspection failure; data security; and human capital. CPAB is constantly working to mitigate these risks. CPAB does not expect that an audit failure will never occur, but it does expect that its inspections will identify weaknesses that, once corrected, will greatly reduce the likelihood and impact of audit deficiencies. Data security pertains to the protection of audit firm and reporting issuer information stored in CPAB's information technology system. From a human capital perspective, attracting, developing and retaining top talent is critical to CPAB's success, and the organization made significant progress in this area in 2010.

As is the case for any organization, CPAB requires a financing and resource base to fulfill its mission and mandate and to implement its strategic and operational plans. CPAB will need to demonstrate value and relevance in its core inspection activities, as well as transparency and efficiency in its resource utilization. While CPAB increased the rate charged to auditors of reporting issuers in 2010, the organization anticipates being able to achieve excellence in its core activities without any further increase.

## Governance

CPAB made a number of changes to its governance structure in 2009 to enhance the organization's accountability, effectiveness and collaboration with provincial regulators of public accounting. These changes have been fully implemented. CPAB welcomes the oversight of its effectiveness by the Council of Governors and specific securities commissions, pursuant to legislation. CPAB's primary accountability is to its Board, which is fully independent from the audit profession that CPAB regulates. During 2010, under the auspices of Ontario legislation, the Ontario Securities Commission (OSC) conducted a review of CPAB with respect to its mandate and its governance. The OSC provided a favourable report to the Council of Governors and to the Ontario legislature that CPAB was fulfilling its mandate. The OSC's suggestions that CPAB disclose Board and Executive compensation and include its budget with commentary in its Annual Report have been adopted for this Annual Report.

As CPAB becomes a recognized body under legislation in other provinces, this type of oversight will increase.

CPAB favours a coordinated approach by the various provinces, to ensure the effectiveness of the process.

Wendy Dobson and Ron Gage, FCA, left the Board of Directors in 2010, at the conclusion of their terms of office. I thank them for their significant and thoughtful contributions to CPAB. The organization also welcomed a new director, Sheryl Kennedy, to the Board in 2010.

## Conclusion

I would like to thank my colleagues on the Board of Directors for their support and hard work in 2010. I would also like to express my appreciation to Chief Executive Officer, Brian Hunt, the management team and staff for their outstanding efforts and ongoing commitment to delivering value as a world class audit regulator.



**Nick Le Pan**  
BOARD CHAIR

# CPAB Board Members

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**Nick Le Pan**

*BOARD CHAIR*

FORMER SUPERINTENDENT OF FINANCIAL INSTITUTIONS, OFFICE OF THE SUPERINTENDENT OF FINANCIAL INSTITUTIONS, OTTAWA, ONTARIO



**Ian Bourne**

CHAIR, BALLARD POWER INC.; DIRECTOR, SNC-LAVALIN GROUP, CANADA PENSION PLAN INVESTMENT BOARD, WAJAX CORPORATION AND CANADIAN OIL SANDS LIMITED; AND RETIRED CFO, TRANSALTA CORPORATION, CALGARY, ALBERTA



**Ken Crump**

FORMER CHAIR, BOARD OF TRUSTEES, COAST WHOLESALE APPLIANCES INCOME FUND; VICE CHAIR, BOARD AND CHAIR, FINANCE AND AUDIT COMMITTEE, BOARD OF COMMUNITY LIVING BRITISH COLUMBIA, VANCOUVER, BRITISH COLUMBIA

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**Guy Fréchette**

FORMER VICE CHAIR AND MEMBER, EXECUTIVE COMMITTEE AT ERNST & YOUNG LLP AND FORMER MANAGING PARTNER FOR THE PROVINCE OF QUÉBEC, MONTRÉAL, QUÉBEC



**Sheryl Kennedy**

CEO, PROMONTORY FINANCIAL GROUP CANADA AND FORMER DEPUTY GOVERNOR OF THE BANK OF CANADA, TORONTO, ONTARIO



**Gary Porter**

FORMER DIRECTOR AND CHAIR, INVESTMENT COMMITTEE OF THE ONTARIO TEACHERS' PENSION FUND AND RETIRED CO-FOUNDER OF PORTER HÉTU INTERNATIONAL, BROCKVILLE, ONTARIO

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**Jocelyn Proteau**

CHAIR, BOARD OF BTB REAL ESTATE INVESTMENT TRUST AND FORMER CHAIR, BOARDS OF STANDARD LIFE ASSURANCE COMPANY OF CANADA, STANDARD LIFE FINANCIALS INC. AND STANDARD LIFE TRUST, MONTRÉAL, QUÉBEC



**Alain Rhéaume**

A FOUNDER AND MANAGING PARTNER, TRIO CAPITAL INC., FORMER DEPUTY MINISTER OF FINANCE, QUÉBEC AND FORMER PRESIDENT AND COO, MICROCELL TELECOMMUNICATIONS, MONTRÉAL, QUÉBEC



**Peter W. Roberts**

FORMER CHAIR, RISK OVERSIGHT AND GOVERNANCE BOARD, CICA, FORMER CFO, SIERRA WIRELESS INC. AND PAST PRESIDENT OF ICABC, WEST VANCOUVER, BRITISH COLUMBIA

# World Class Audit Regulation

**Over the past year, CPAB has enhanced its capability as a high-quality regulator and made significant progress toward realizing its vision of being recognized, domestically and internationally, as a world class audit regulator.**

CPAB made considerable progress in implementing its strategic plan in 2010 and reviewed and updated the plan during the year to reflect accomplishments to date. This necessitated a change in strategic emphasis, as the organization moves to achieve its vision by 2012. This change in emphasis is primarily in two areas: organizational development and human resources.

In 2010, CPAB implemented a new organizational structure, which established a new management formation with clear roles and responsibilities for staff at various levels. Management also developed core values for the organization: Excellence, Trust and Respect. In the area of human resources, management's focus in 2010 was on recruiting staff to ensure that the skills and capabilities defined in the organizational structure were available to CPAB. CPAB has been very successful in attracting top talent. As a direct result of these efforts, CPAB's focus in 2011 will shift from recruiting to developing staff, and from developing core values to ensuring that they permeate the organization. Management will also focus on the consistent application of inspection policies and methodology.

CPAB's Management Committee reflected extensively on the organization's core issue, and reaffirmed it as the need to make recommendations to participating firms and other key stakeholders that add value to audit quality. CPAB's value proposition continues to be disciplined inspections and penetrating insights that appreciably enhance audit quality to benefit investors, other users of financial statements, capital markets and Canadians more generally.

Delivering value means imparting useful and insightful inspection findings to firms, including comments on the root causes of deficiencies that provide firms with unique insight into their performance and into audit risk matters and practices. It also includes articulating appropriately tough but fair findings as necessary and imposing the related consequences on firms.

The Management Committee also reviewed and updated the factors critical to CPAB's success. These are:

- Leading-edge technical/professional skills
- Rigorous inspection methodology
- Clear accountabilities and performance measurement
- Strong stakeholder relationships
- A significantly expanded legislative base

CPAB's strategic plan also outlines ten major initiatives, which represent key deliverables for 2010-12. These initiatives fall into four key areas: Organization, Stakeholders, Infrastructure and Regulatory. While important progress was made on each of these ten initiatives in 2010, management's goal over the next year is to shift emphasis and focus to the next phase of their implementation.



## Ten Major Strategic Initiatives – 2010-12

### Organization

1. *Define and increase accountability in all areas of the organization*
2. *Implement best-in-class human resource management*
3. *Recruit, develop and retain leading accounting, auditing and IFRS professionals*
4. *Build a consultative, high-performance, high-engagement culture*

### Stakeholders

5. *Implement state-of-the-art risk-based inspection methodology*
6. *Elevate regional and national profile*
7. *Expand risk-based inspections activity of all firms*
8. *Develop strong relationships with Audit Committees, the investor community and international counterparts*

### Infrastructure

9. *Build robust internal control and reporting/ measurement systems and advanced database management capability*

### Regulatory

10. *Establish pan-Canadian legislative base and international reciprocity*

## Organization

### ***Define and increase accountability in all areas of the organization***

As it evolves as a regulator, CPAB continues to more fully assume the accountability incorporated in its mandate. To succeed, CPAB must increase accountability across the organization so that the roles, responsibilities and interdependencies of each division and each person are clear. There must also be reward and consequence for how these accountabilities are put into operation.

In 2010, CPAB developed profiles for each position in the organization and established a performance measurement system linked to compensation. CPAB has also designed an accountability framework, to be implemented in 2011, that defines interdependencies between positions. Work has been substantially completed on a career progression and development program, which will be implemented in 2011-12.

These measures should help clarify roles and responsibilities in the organization, which should result in greater accountability and clearer career paths for CPAB staff.

### ***Implement best-in-class human resource management***

CPAB is a human capital knowledge organization, and, as CEO, I am committed to providing professional and career development that is second to none. Investment in the key elements of human resource management is critical to the organization's success. These include:

- *Core:* Recruitment and selection, compensation and benefits, human resources policies, performance appraisal, employee engagement, professional development
- *Value-adding:* Organizational, leadership and professional development

CPAB has accelerated its investment in human capital in anticipation of the new Canadian Auditing Standards

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(CAS) and International Financial Reporting Standards (IFRS). Professional development curriculum is being established to provide staff with best-in-class learning experiences related to the organization's new competency profile and their own career progression.

The introduction of a new performance appraisal system and updated human resources policies, and the engagement of staff in CPAB's evolution as a regulator, are well underway. Significant work on both career development and succession planning was completed in 2010. The organization's focus in 2011 will move more from design to implementation.

***Recruit and develop leading accounting, auditing and IFRS professionals***

CPAB required a significant recruitment effort in 2010 to fill several new positions created by the new organizational structure, to minimize systemic and specific risk and to prepare for IFRS. CPAB's 2010 recruiting initiatives were very successful. A robust onboarding program, 90-day probationary performance reviews, and pursuit of staffing reciprocity agreements with other regulators round out this recruitment initiative.

Having successfully recruited top talent, the organization must now focus on the further development and retention of staff. Staff skills must be developed from those of auditors to those of effective audit regulators. CPAB will also pursue certain secondments with other

audit regulators as a way of building capability and providing staff development opportunities. In 2011 CPAB will second staff to the UK and Australia in an effort to ensure that sufficient IFRS experienced personnel are available for inspections in 2012.

***Build a consultative, high-performance, high-engagement culture***

To achieve the stature and impact envisioned in its strategic plan, CPAB's culture must shift to one that incorporates more consultation. Internally, this must occur between Inspections and Standards & Consultation. Externally, enhanced consultation with other audit regulators and with the firms themselves is required. Significant progress was made in 2010, but more must be done.

The organization is implementing processes and mechanisms to drive high performance, through investments in professional development, performance appraisal and compensation systems. Staff will help develop these systems and will participate in an active exchange with senior management about them.

**Stakeholders**

***Implement state-of-the-art risk-based inspection methodology***

CPAB's inspection methodology must become more strategic, provide greater risk assessment, and add more relevance to participating firms. CPAB's stakeholder survey shows that while progress has been made, more is necessary and achievable.

The transition to this approach includes: meetings with various Canadian audit firms to discuss the impact of the economy on audit quality; greater focus on the consistency and effectiveness of inspections; more rigorous risk analysis of participating firms and of the files being selected for inspection; instituting a database of inspection report findings; increasing interaction with foreign regulators; inspecting more



firms; and increasing communication with participating firms throughout the year.

An enhanced ability to make key judgments on significant inspection matters is central to a more strategic inspection process. This ability has been identified in CPAB's new set of core competencies and, accordingly, is referenced in a number of position profiles.

In 2010, CPAB repositioned its risk model to better address the weighting of risks in regard to audit quality. CPAB's risk assessment process helps it allocate its resources effectively, and the organization is well positioned to move its risk assessment to the next level in 2011.

#### ***Elevate regional and national profile***

To fulfill its mission of oversight to protect the public interest, CPAB must raise its profile. Stakeholders require a better understanding of CPAB's contributions to the quality of audits of public company financial statements in Canada, as well as a better understanding of what we do and don't do.

As an important first step in raising its regional profile, CPAB established offices in Québec (Montréal) and Western Canada (Vancouver) in 2010. These offices are led by resident Regional Directors, who are senior audit professionals and experienced leaders. Their role is to build CPAB's presence in the regional marketplace and to be directly responsible for their staff.

In 2010, CPAB also participated in roundtable discussions with Audit Committees in Vancouver, Calgary, Toronto and Montréal. Hosted by participating audit firms, these roundtables were an excellent opportunity to discuss a variety of issues, including CPAB's role and activities, audit fees, relationships between auditors and Audit Committees, audit partner rotation and the financial literacy of Audit Committees.

By building its profile and brand, CPAB will elevate the importance of quality auditing and strong audit oversight, and will enhance its reputation in the auditor

community as a destination employer for top talent. This initiative will receive higher priority in 2011.

#### ***Expand risk-based inspection activity of all firms***

CPAB is committed to expanding its risk-based inspection activity of firms of all sizes. From a base of 53 inspections of 2009, CPAB inspected 69 firms in 2010 (including follow-up inspections).

In 2010, CPAB enhanced its risk assessment capabilities and now uses a more robust risk analysis process to identify higher-risk audit firms and engagements, thereby improving the effectiveness of its inspections. CPAB has also increased the frequency of its inspections of firms that audit fewer than 100 reporting issuers. In 2011, this will include more than 20 desk inspections of reporting issuer audits by smaller firms/practitioners. In a desk inspection, the firm submits the reporting issuer's audit file to CPAB's regional office for inspection. Desk inspections focus solely on the quality of the audit, unless further inspection procedures are deemed necessary.

#### ***International partnerships***

CPAB participates in the International Forum of Independent Audit Regulators (IFIAR), which helps develop cooperative arrangements with other national auditor oversight authorities. IFIAR also encourages dialogue on challenges facing audit regulator organizations. More than 100 countries have established organizations such as CPAB and more than a third of them are members of IFIAR.

At its September 2010 meeting in Madrid, Spain, IFIAR members discussed Core Principles for IFIAR. CPAB has also encouraged IFIAR to be more proactive in recruiting new members, given that a number of G20 countries are not IFIAR members.

CPAB is also active in the Global Public Policy Committee (GPPC)/IFIAR Working Group. The Working Group, which includes international accounting networks and IFIAR members, has established a

framework for discussing topics on audit quality that are of interest to both the GPPC and IFIAR members. I chair this Working Group.

CPAB works with other audit regulators around the world to increase audit oversight efficiencies by entering into agreements that allow for reliance on each other's work. In a major step forward, the European Commission in February 2010 approved CPAB equivalency pursuant to Statutory Audit Directive 2006/43/EC. The European Union, on behalf of its Member States, has worked with CPAB to exchange information on mandate, vision, inspection methodology, staff competencies and capabilities. The decision allows European Union Member States to enter into bilateral agreements with CPAB on the exchange of audit inspection working papers.

CPAB is also pursuing a recognition agreement with the Japanese audit oversight body. CPAB has reviewed a draft agreement prepared by the Japanese and expects the agreement to move forward in 2011. CPAB has also been helping the Cayman Islands and Bermuda establish an audit oversight body. CPAB has offered advice on draft legislation and draft regulations that their security commissions have prepared. CPAB is also in the process of entering into a memorandum of understanding with the audit regulator in Australia.

In October 2010, CPAB met in Washington DC with senior staff from its main international partner, the Public Company Accounting Oversight Board (PCAOB). CPAB and the PCAOB agreed to enhance co-ordination of the 2011 inspections they conduct

jointly, including Big Four firm inspections. The two bodies will also define their sharing of information, including signing an updated memorandum of understanding for a new information-sharing model that reflects the *Dodd-Frank Act* in the United States.

### Infrastructure

#### ***Build robust internal control and reporting/ measurement systems and advanced database management capability***

To upgrade its infrastructure, CPAB will establish a performance scorecard that aligns the overall organization, from strategic initiatives through to divisional and, ultimately, individual actions and outcomes.

Part of the measurement process will incorporate stakeholder value analysis, which may include interviews and electronic surveys of key stakeholders to determine what they value in a regulator such as CPAB and how CPAB is performing relative to these value propositions.

In 2010, CPAB retained a professional market research firm to conduct a survey of the registered audit firms. The purpose of the survey was to obtain feedback on a range of issues affecting the audit profession, but particularly on perceptions of the performance of CPAB. Specifically, the survey examined various aspects of the working relationship between CPAB and audit firms, from the firms' perspective.

Overall the survey results were positive, with 77 per cent of respondents saying they believe CPAB's performance as an effective regulator is high and indicating that this has increased in the past year. Respondents gave CPAB high ratings on professionalism, communication during the inspection process, knowledge and technical competence of staff and on the opportunity for an audit firm to explain its position on an issue.

The survey responses confirm that CPAB is moving in the right direction, although more work needs to be

CPAB WILL ESTABLISH  
A PERFORMANCE  
SCORECARD THAT  
ALIGNS THE OVERALL  
ORGANIZATION

done. The survey results suggest that additional effort is required to provide greater consistency and higher-quality inspection findings, as well as more focused, value-added recommendations to improve audit quality. CPAB plans to conduct the survey again in the next two years to assess progress.

## Regulatory Issues

### ***Establish pan-Canadian legislative base and international reciprocity***

A robust regulatory framework is critical to CPAB's ability to perform as a strategic regulator.

Ontario has passed legislation stating that CPAB, without breaking solicitor-client privilege, may require the provision of information or the production of documents that are, "the subject of solicitor-client privilege if access to the information or the documents is absolutely necessary to the purpose of the review of the audit." CPAB worked with audit firms in implementing the new legislation and appreciates their contribution. It is CPAB's view that access to privileged information in the audit working papers that supports the audit opinion is absolutely necessary to the purpose of the review of the audit. The "absolutely necessary" provision has worked very well in practice with CPAB's 2010 inspections, as CPAB obtained access to 100 per cent of the information needed to assess the quality of the audit process.

CPAB is in discussions with Québec to attain legislative amendments that would give CPAB access to privileged information in the auditor's working papers on the same "absolutely necessary" basis.

CPAB legislation is now in force in British Columbia. CPAB is working with the British Columbia Securities Commission to finalize, in the first quarter of 2011, recognition of CPAB as an auditor oversight body in that province.

CPAB has also been discussing CPAB legislation with other Canadian jurisdictions. Given the developments

in Québec and British Columbia, we anticipate that significant progress will be made in these other jurisdictions by late 2011 or early 2012.

## Financial Strategy

Through its strategic plan, CPAB focused on enhancing the organization's capabilities in a number of key areas in 2010. This required additional financial resources. As a result, CPAB increased its fees to reporting issuers from 1.6 per cent to 2.0 per cent of their audit fees. These additional resources were used to implement significant organizational restructuring, provide IFRS training to staff, increase risk assessment capabilities and increase inspection activity levels. They were also used to rebuild reserves, which were affected by organizational restructuring. The 2011 level of funding and expense is required for CPAB to effectively fulfill its mandate under its strategic plan.

## Conclusion

In conclusion, I would like to thank Board Chair, Nick Le Pan, the Board of Directors, management and staff for their support and assistance over the past year.

As CPAB moves through the next stage of its development, the organization will continue to build on its achievements to date and to enhance its capabilities as a strategic regulator. This includes a shift to a more rigorous, consistently applied methodology, an accountability mindset, advanced skill sets and inspection reporting that focuses on key risks in audit practices. Building awareness of CPAB's role and activities – via outreach to key stakeholders, education and more effective communications – is another key focus for the organization in 2011.

This transition will evolve over the next two years, as CPAB continues to deliver value through world class audit regulation.



**Brian A. Hunt**, FCA  
CHIEF EXECUTIVE OFFICER

# CPAB Management Committee

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**Brian A. Hunt**, FCA  
CHIEF EXECUTIVE OFFICER



**Kenneth J.A. Vallillee**, FCA  
SENIOR VICE PRESIDENT  
OF INSPECTION ACTIVITY



**Galt Arthur**, FCA  
VICE PRESIDENT AND  
CHIEF INFORMATION OFFICER



**Glenn Fagan**, CA  
VICE PRESIDENT



**Kam Grewal**, CA, CPA  
VICE PRESIDENT OF STANDARDS



**Marial Stirling**, CA, LLB  
VICE PRESIDENT AND GENERAL COUNSEL

# Enhancing Audit Quality

## Introduction

**As at December 31, 2010, there were 309 participating audit firms registered with CPAB. During 2010, 38 firms registered with CPAB and 23 terminated their registration of their own accord.**

In 2010, CPAB inspected 69 firms (2009 – 53 firms) and reviewed 232 audit engagements (2009 – 212 audit engagements) to assess the effectiveness and implementation of audit firms' policies and procedures, relative to accounting and auditing standards. CPAB conducted:

- Inspections of Canada's Big Four firms and reviews of 120 audit engagements carried out by those firms
- Inspections of 11 firms inspected annually (Annual Firms) and reviews of 57 audit engagements carried out by those firms
- Inspections of 25 Regional and Local Firms and reviews of 55 audit engagements in those firms
- Twenty-nine follow-up inspections, which are carried out to ensure that CPAB's recommendations have been implemented. In addition to the inspections CPAB conducted, provincial accounting bodies inspected over 70 firms that audit reporting issuers

CPAB uses a number of risk analysis processes to identify higher-risk reporting issuer audits and allocates its inspection resources accordingly. The

2010 inspections were focused reviews that drilled deeply into the audit work in high-risk areas such as valuations, impairments, revenue recognition, complex financial instruments, income taxes and going concern. In addition, CPAB inspected files of two early adopters of IFRS, monitored firm readiness for IFRS and evaluated how the firms assessed their clients' readiness for conversion to IFRS. CPAB also assessed the firms' plans for adoption of the new CAS.

During 2010, CPAB's 29-member inspection staff was supported by 11 contract consultants, who specialize primarily in the areas of taxation, IFRS, information technology, Generally Accepted Accounting Principles (GAAP) and valuations.

## Results of Inspections

In the seven years that CPAB has been conducting inspections, the organization has seen numerous examples of high-quality audit work. Many firms have significantly improved audit quality by implementing CPAB's recommendations while others have undertaken their own initiatives to improve audit quality. Overall, CPAB believes that audit quality in Canada continues to be sound.

In general, investors can have confidence in the integrity of public company financial statements that have been audited in Canada. In particular, audit quality is generally sound for the major audit firms' largest and most complex clients. But audit quality is not uniformly high across all engagements in all firms, and, even for major firms, there can be occasional lapses that result in reduced quality.

Similarly, smaller and mid-sized audit firms with focused engagement clientele in sectors that they fully understand also demonstrated sound audit quality in engagements reviewed by CPAB. Audit quality issues for these firms are more likely to arise in instances where they either audit very few public companies or else undertake audits of a few reporting issuers outside their comfort zone. This can also happen in major firms

2010 INSPECTIONS  
WERE FOCUSED  
REVIEWS THAT  
DRILLED DEEPLY  
INTO AUDIT WORK IN  
HIGH-RISK AREAS

where certain offices or partners may, on occasion, also deal with audits that pose complexities outside their comfort zone.

CPAB believes that public company auditors in Canada should strive for continuous improvement in audit quality. However, overall, CPAB saw little improvement in audit quality from 2009.

The 2010 inspection reports highlighted the top recommendations that, if implemented would have the greatest impact on improving audit quality. CPAB believes that if the firms implement the recommendations – particularly in the area of enhanced engagement supervision and review – many of its inspection findings may have been avoided.

CPAB believes that audit firms must seriously consider its recommendations in light of their own commitment to audit quality, and take the steps necessary to rigorously focus on continuous improvement in this area.

### Big Four Firms

Canada's Big Four firms audit reporting issuers in Canada that represent more than 92 per cent, if measured by market capitalization.

CPAB's 2010 inspections of the Big Four firms were risk-based, with increased emphasis on larger, more complex engagements. CPAB also focused on smaller, high-risk reporting issuers that were audited by offices

outside the major centres in Canada and on partners who had not been previously inspected.

CPAB used several external databases to identify high-risk engagements and then compared the engagements identified to the firm's own lists and investigated any differences. Once the engagement files were chosen, CPAB conducted a review of the financial statements and related public information to decide which specific audit risks within the financial statements would be the subject of a focused review.

CPAB saw many examples of high-quality audit work by the Big Four firms in the files reviewed in 2010. However, there continues to be room for improvement. In particular, a disproportionately high number of the more serious audit file deficiencies occurred in the smaller offices and in the files of partners CPAB inspected for the first time.

The major systemic issues and areas for improvement that CPAB noted most often in 2010 included:

- Lack of partner supervision and review
- Ineffective involvement of the engagement quality control partner
- Lack of application of professional skepticism
- Inadequate substantive analytical procedures
- Insufficient or inappropriate audit evidence
- Lack of transparent communication with Audit Committees

### Annual Firms

Many of the major issues CPAB identified in the inspections of the Big Four firms also applied to the Annual Firms. CPAB also noted two additional issues with respect to Annual Firms:

- The need for senior leadership of the firms to strengthen their messages about audit quality
- A lack of resources devoted to audit quality

CPAB SAW MANY  
EXAMPLES OF  
HIGH-QUALITY  
AUDIT WORK

### Regional and Local Firms

In 2010, CPAB conducted more inspections of smaller firms, which up to now had been inspected primarily by provincial regulatory authorities.

Many of the major issues CPAB identified in its inspections of the Big Four and Annual Firms were also evident in its inspections of Regional and Local Firms. CPAB also noted two additional major issues with respect to Regional and Local Firms:

- Lack of evidence of the resolution of significant issues
- Lack of consultation on complex, non-routine transactions

### Remedial Actions

As a result of its 2010 inspections, CPAB placed requirements on three firms. Requirements placed on two firms as a result of CPAB's 2009

inspections will remain in place, pending further follow-up reviews by CPAB.

### Reporting

CPAB issues to each firm inspected a private report that includes recommendations for that firm. Each recommendation requires a response from the firm within a prescribed period of time, which is typically 180 days. CPAB follows up to ensure that its recommendations have been implemented.

CPAB reports publicly at least annually on the results of its inspections but does not identify either individual firms or companies. If CPAB did impose the most serious level of sanctions on an audit firm, that would be reported to the relevant securities commissions and to the audit firm's reporting issuer clients. No such sanctions were imposed in 2010.

The 2010 Public Report will be issued in April 2011 and will be available for viewing at [www.cpab-ccrc.ca](http://www.cpab-ccrc.ca).

## OVERVIEW AND SCOPE

*CPAB's mandate is to effectively regulate and promote high-quality external audits of entities that are reporting issuers in Canada. In carrying out that role, CPAB conducts inspections of the firms subject to its oversight, either directly or in cooperation with provincial or foreign regulatory authorities.*

*Each year, CPAB reviews all firms that audit 100 or more reporting issuers. There are now 15 firms in this category. CPAB also reviews, at least every two years, firms with between 50 and 99 reporting issuer audit clients. Over three years, the majority of firms registered with CPAB that are also registered with the PCAOB are inspected. For the remaining Canadian participating audit firms, CPAB primarily relies on its reviews of the quality inspections carried out by the relevant provincial accounting bodies, i.e., Institutes of Chartered Accountants or Associations of Certified General Accountants, although it may, and has, elected to review some of those firms directly. In 2011 CPAB will conduct more than 20 desk inspections of reporting issuers audited by smaller practitioners.*

*When a registered firm is domiciled in another country, CPAB will, depending on the robustness of the audit regulatory activity in that country, endeavour to rely on that regulator. However, at a minimum, CPAB will carry out some review of the audit files relating to Canadian reporting issuers.*

# Operating Results, Outlook, Principal Risks and Uncertainties

*The following is a review of CPAB's operating results for the year ended December 31, 2010.*

*This section also includes the outlook for 2011 and principal risks and uncertainties that could affect the organization.*

## Overview

CPAB is an independent, federally incorporated, not-for-profit corporation without share capital. Established in 2003, CPAB's mission is to contribute to public confidence in the integrity of financial reporting of reporting issuers in Canada by effective regulation and promoting quality, independent auditing. National Instrument 52-108 of the Canadian Securities Administrators requires that auditors of Canadian reporting issuers' financial statements be registered with and in good standing with CPAB. CPAB carries out its mandate by conducting inspections of the firms subject to its oversight either directly or in cooperation with other regulatory bodies in Canada and abroad.

As at December 31, 2010, 309 public accounting firms were registered with CPAB as participants in good standing. At year-end in 2009 this number was 294. This 5 per cent increase is due primarily to the registration of new foreign accounting firms that audit Canadian reporting issuers or that expect to in the future.

IN 2010, 309 PUBLIC  
ACCOUNTING FIRMS  
WERE REGISTERED  
WITH CPAB AS  
PARTICIPANTS IN  
GOOD STANDING

## Operating Results

### Revenues

CPAB derives all of its funding from Canadian reporting issuers. CPAB invoices audit firms a fee, which the firms in turn bill to their reporting issuer clients. The fee amount is designed to cover CPAB's annual operating costs and to provide a reasonable reserve for contingencies. CPAB's 2010 fee levy rate for Canadian audit firms was 2.0 per cent of the audit fee these firms charge their reporting issuer clients, with a minimum fee of \$1,000. In 2010, 96 Canadian audit firms paid the minimum fee. CPAB charges foreign participating audit firms the same annual participation fee of 2.0 per cent of a firm's audit fees that it does for domestic firms, subject to the same minimum fee of \$1,000. However, firms in certain country jurisdictions that have audit regulatory oversight in place are charged only 0.2 per cent of the firm's audit fees.

In 2010, CPAB increased its fee levy rate from 1.6 per cent (\$12.7 million) to 2.0 per cent (\$15.6 million) and the levy for firms in certain country jurisdictions from 0.1 per cent (\$0.4 million) to 0.2 per cent (\$0.8 million). CPAB increased the levy to continue to develop the organization and its capabilities, increase inspection activity, maintain risk tolerance at an acceptable level and ensure CPAB continues to fulfill its mandate.

### Operating Expenses

To implement its strategic plan and to address the challenges posed by an uncertain economic environment and the introduction of new international auditing and accounting standards, CPAB made significant investments in its inspection methodology, systems and processes, and people in 2010.

CPAB's changes to its inspection methodology are designed to provide a better risk assessment of and

add more relevance to participating firms. CPAB's risk assessment process helps it allocate its resources effectively, and the organization is well positioned to move its risk assessment to the next level in 2011.

In 2010, CPAB expanded its inspection activity to include more Regional and Local Firms and also deepened its inspection coverage in the Big Four firms and other firms inspected annually. CPAB inspected 69 firms in 2010, compared to 53 inspections in 2009, an increase of 30 per cent (including follow-up inspections). Inspection activity is expected to increase further to include more foreign firms and smaller firms that are currently inspected by the provincial audit regulators. CPAB will use a risk-based approach to inspect these firms. Much of this activity was, and is, expected to be accomplished through rebalancing inspection staff and productivity gains.

Salaries and benefits for inspection and administrative staff continue to be CPAB's largest expense, totalling \$10.4 million or 71.2 per cent of 2010 total expenses of \$14.7 million (2009 – \$8.7 million or 66 per cent), before restructuring expenses.

Excluding salaries and benefits and restructuring expenses, operating expenses decreased approximately 5.9 per cent, to \$4.2 million in 2010 from \$4.5 million in 2009. This decrease was related to reductions in professional services expenses, largely due to lower recruiting costs, and legal services expenses. These decreases were partly offset by an increase in continuing education costs for IFRS training. Excluding restructuring expenses, the excess of revenue over expense in 2010 was \$1.8 million, compared to zero in 2009 (see chart on page 19).

Restructuring expenses in 2010 of \$0.4 million (2009 – \$1.4 million) consisted of severance payments for management changes related to human resources initiatives undertaken by CPAB.

In 2010, CPAB replaced its registration system with a newly developed Firm Information and Registration

IN 2010, CPAB  
EXPANDED ITS  
INSPECTION ACTIVITY  
TO INCLUDE MORE  
REGIONAL AND  
LOCAL FIRMS

Management System. This system, which resides within CPAB's secure IT environment, provides enhanced information about participating audit firms and their reporting issuer audit clients.

### Cash Flows and Liquidity

The net cash used in 2010 was \$1.1 million (2009 – \$3.0 million), primarily for the net purchase of short-term investments of \$1.7 million. At December 31, 2010 CPAB had a strong working capital position of approximately \$3.9 million (2009 – \$2.7 million).

### Director and Executive Compensation

CPAB strives to offer Director and Executive compensation comparable to organizations at similar levels. CPAB conducts annual compensation surveys and aims to have its compensation levels fall in the mid-range of compensation offered by organizations with a similar mission and mandate.

Board Members' 2010 compensation included fees of \$0.6 million (2009 – \$0.6 million) for governance responsibilities. Board members' fees included a \$150,000 annual retainer for the Board Chair, a \$30,000 annual retainer for all other Board Members and an additional \$4,000 for Committee Chairs. Meeting attendance fees included \$1,500 per day for each Board and Committee meeting. The Board Chair does not receive meeting attendance fees.

Executive compensation in 2010, which included all amounts paid to the CEO, CFO and next three highest-paid members of the Management Committee, totalled \$2.2 million (2009 – \$2.0 million). Executive total compensation includes salaries, bonuses, and Registered Retirement Savings Plan (RRSP) contributions.

### Outlook for 2011

CPAB's strategic plan supports an increase in 2011 inspection activity and advancements in its inspection methodology, systems and processes, and people. CPAB will continue to make significant investments in human resource management, inspection methodology, technology and systems, stakeholder relations, and regulatory affairs to ensure the organization is positioned to continue to deliver value as a world class audit regulator.

Downward pressure on audit fees as a result of the ongoing economic environment has eroded CPAB's fee base for 2011. At the same time, investments to train and develop staff, change inspection methodology, participate in national and international consultations on matters affecting audit quality and to advance CPAB's legislative and regulatory affairs agenda continue. The implementation of IFRS and the new CAS will also continue to have an impact on CPAB's operating costs.

For 2011, revenues are budgeted at \$15.9 million to cover operating expenses, as compared to revenues

of \$16.4 million in 2010. CPAB's operating expenses for 2011 have been budgeted at \$15.5 million. This represents an increase of 5.4 per cent from total operating expenses of \$14.7 million, before restructuring, in 2010. Costs are expected to increase for one-time IFRS training requirements, legislative initiatives and for regional offices in Vancouver and Montréal, which CPAB opened in 2010.

CPAB anticipates capital expenditures in 2011 of approximately \$0.2 million to replenish its IT infrastructure and reporting systems.

### Principal Risks and Uncertainties

CPAB's most important assets are its human capital and its reputation as an effective regulator. Significant risks include political, economic, human capital and technological forces that could have a material impact on CPAB's mission, vision, or critical success factors.

Political risks revolve around impact of legislation that does not support CPAB in meeting its mandate.

Current economic uncertainties increase the possibility of risks associated with failures in corporate governance, financial reporting and in audits. These have the consequent risk of loss of confidence in CPAB.

Human capital risks include an aging accounting workforce and a shortage of IFRS-experienced personnel.

Technologically, data security is an overarching consideration. Central to CPAB's ability to fulfill its mandate are database design, management and security, development of and support for the participating firms' registration information system, connectivity to support the Internet, the Extranet utilized by provincial regulators, and the Intranet and other services utilized by remote users.

As stated in the Reports of the Chair and CEO, CPAB's guiding principle is zero tolerance for reputational risk

CPAB'S MOST  
IMPORTANT ASSETS  
ARE ITS HUMAN  
CAPITAL AND ITS  
REPUTATION AS  
AN EFFECTIVE  
REGULATOR

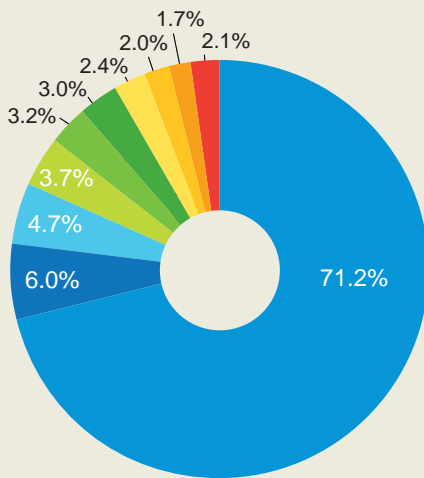
MANAGEMENT'S DISCUSSION AND ANALYSIS

and the organization is constantly working to mitigate risk. In 2010, the organization enhanced its risk assessment capabilities and now uses a more robust risk analysis process to identify higher-risk audit firms and engagements. CPAB's inspection methodology must become more strategic, provide greater risk assessment, and add more relevance to participating firms. From a human capital perspective, CPAB made significant progress in attracting top talent in 2010. Going forward, the organization's focus will shift to retention and development. In the area of technology,

a major opportunity in IT includes implementing new software for inspections.

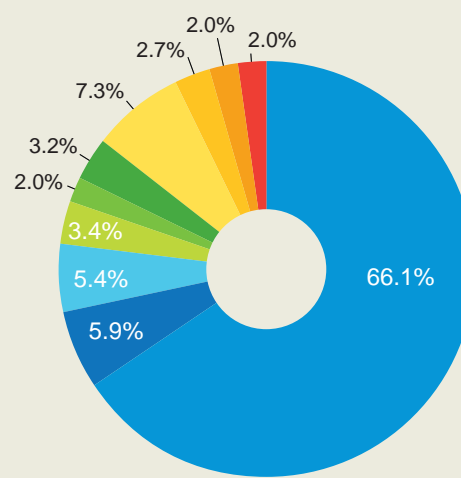
As CPAB evolves as a regulator, it more fully assumes the accountability incorporated in its mandate. This involves increased focus on accountability across the organization to ensure that roles, responsibilities and the interdependencies of each division and person are clear. CPAB continues to manage its resources to enhance its ability to address risks, to achieve its mission and mandate and to realize its vision of being recognized as a world class audit regulator.

MAJOR EXPENSES, BEFORE RESTRUCTURING\*, BY TYPE (\$000'S)



2010

Salaries and Benefits	\$10,439
Travel	\$880
Directors' Fees and Expenses	\$695
Administrative and General	\$538
Continuing Education	\$474
Occupancy Costs	\$443
Professional Services	\$357
Legal Services	\$294
Insurance	\$244
Amortization	\$305
*Restructuring	\$432



2009

Salaries and Benefits	\$8,736
Travel	\$780
Directors' Fees and Expenses	\$712
Administrative and General	\$452
Continuing Education	\$262
Occupancy Costs	\$424
Professional Services	\$971
Legal Services	\$361
Insurance	\$266
Amortization	\$267
*Restructuring	\$1,392

# CPAB Statement of Operations

(UNAUDITED)

<i>Year Ended December 31 (000's),</i>	<i>2010 Actual</i>	<i>2011 Budget</i>
<b>REVENUE</b>		
Fees from participating audit firms	\$ 16,366	\$ 15,890
Intent to Participate fees from applicant firms	44	–
Interest income	12	30
	16,422	15,920
<b>EXPENSES</b>		
Salaries and benefits	10,439	10,730
Travel	880	935
Directors' fees and expenses	695	890
Administrative and general	538	542
Continuing education and professional memberships	474	568
Occupancy costs	443	497
Professional services	357	451
Legal services	294	250
Insurance	244	233
Amortization of property and equipment	305	373
Restructuring	432	–
	15,101	15,469
<b>Excess (Deficiency) of Revenue Over Expenses for the Year</b>	<b>\$ 1,321</b>	<b>\$ 451</b>

# Commentary on the 2011 CPAB Operating Budget

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**The 2011 Operating Budget (Budget) shows CPAB continuing to fulfill its mandate effectively during challenging times, which include increasing complexity in financial reporting and the transition to IFRS and the new CAS. To address these challenges, CPAB must further develop its capabilities and increase its inspection activity.**

In 2010 CPAB, through its strategic plan, focused on enhancing the organization's capabilities in a number of key areas. In order to enhance these capabilities additional financial resources were required. CPAB increased its fees to reporting issuers from 1.6 per cent to 2.0 per cent of their audit fees. These additional resources were utilized to implement significant organizational restructuring, provide IFRS training to staff, increase our risk assessment capabilities as well as increase inspection activity levels and finally to rebuild our reserves which were impacted by the organizational restructuring. Organizational restructuring in 2009 and 2010 cost approximately \$1.8 million, in aggregate.

CPAB derives its funding from Canadian reporting issuers. CPAB invoices audit firms a fee, which the firms in turn bill to their reporting issuer clients. CPAB's fee levy rate will remain at 2.0 per cent of the audit fee that firms charge their reporting issuer clients.

CPAB is increasing its 2011 Budget expense by 5 per cent over its 2010 budget. The 2011 Budget reflects anticipated increased costs for one-time IFRS training requirements and legislative initiatives.

In 2010 CPAB worked to ensure that it is well positioned for the transition to the CAS and to IFRS. CPAB recruited employees with IFRS expertise,

increased IFRS training for all inspection staff and worked with other international auditor oversight organizations to initiate secondments. In 2011, CPAB will second two staff members to jurisdictions that currently utilize IFRS. These staff members will return to CPAB in 2012 and use the experience they have gained in CPAB's inspections of 2011 audits. Secondments to the Australian auditor oversight organization will continue in 2011-2012, giving CPAB access to additional expertise.

CPAB's strategic plan supports an increase in inspection activities in 2011 and advancements in its inspection methodology, systems and processes, and its people. CPAB inspected 40 firms in 2010 (excluding follow-up inspections) and has set a target of 50 firm inspections a year by 2012. CPAB's 2011 inspection activity will include more Regional and Local Firms. It will also include, based on a risk-based, targeted review, additional inspections of foreign firms and firms inspected by the provincial audit regulators. Opportunities to improve the inspection process include developing policy documents and controls to enhance consistency across inspections. CPAB will continue to invest in technical training of staff in standards and industry knowledge, and in strategic and lateral thinking on how inspections are, and can be, conducted. This initiative should enhance risk identification capabilities and the effectiveness of internal consultations.

CPAB will also continue to make significant investments in human resource management, technology and systems, stakeholder relations, and regulatory affairs to ensure CPAB is positioned to deliver value as a world class audit regulator.

# Statement of Management's Responsibility

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The annual financial statements and all financial and other information contained in this Annual Report are the responsibility of the management of the Canadian Public Accountability Board.

Management has prepared the financial statements in accordance with Canadian Generally Accepted Accounting Principles, applying best estimates and judgments based on currently available information. The significant accounting policies are described in Note 2 to the financial statements. Financial information contained in this Annual Report is consistent with that shown in the financial statements.

Management is responsible for the integrity and reliability of financial information, and has established systems of internal procedural and accounting controls designed to achieve this. These systems also reasonably ensure that assets are safeguarded from loss or unauthorized use.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board has created an Audit Committee to help it with these responsibilities. The Audit Committee met with the auditors, both with and without management present, to review the activities of each, as well as to review the financial statements.

Cowperthwaite Mehta has been appointed by the Provincial Audit Regulator Members as CPAB's auditors to express their opinion on the fair presentation of the financial statements. Cowperthwaite Mehta has had full and unrestricted access to the Board of Directors and management to discuss matters pertaining to their audit. The Audit Committee undertakes annually a formal review of the auditor's performance and makes a recommendation to the Board of Directors, which in turn makes a recommendation to the Provincial Audit Regulator Members, with respect to their reappointment for the coming year.



**Brian A. Hunt**, FCA  
CHIEF EXECUTIVE OFFICER



**John Mastrella**, CA  
DIRECTOR, INTERPROVINCIAL RELATIONS  
AND CHIEF FINANCIAL OFFICER

# Independent Auditor's Report

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*To the Members,*

*Canadian Public Accountability Board / Conseil canadien sur la reddition de comptes*

## **Report on the Financial Statements**

We have audited the accompanying financial statements of the Canadian Public Accountability Board/Conseil canadien sur la reddition de comptes, which comprise the statement of financial position as at December 31, 2010, and the statements of changes in net assets, operations and cash flows for year then ended, and a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian Generally Accepted Accounting Principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian Auditing Standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the financial statements present fairly, in all material respects, of the financial position of the Canadian Public Accountability Board/Conseil canadien sur la reddition de comptes as at December 31, 2010, and its financial performance and its cash flows for the year then ended in accordance with Canadian Generally Accepted Accounting Principles.

*Conqurthwite Mehta*

*CHARTERED ACCOUNTANTS  
LICENSED PUBLIC ACCOUNTANTS*

*FEBRUARY 14, 2011  
TORONTO, ONTARIO*

# Statement of Financial Position

<i>As at December 31,</i>	<i>2010</i>	<i>2009</i>
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 372,974	\$ 1,426,418
Short-term investments (note 4)	4,700,000	3,000,000
Accounts receivable (note 4)	19,838	19,270
Goods and services tax recoverable	58,539	58,538
Prepaid expenses	116,467	106,172
	5,267,818	4,610,398
Property and equipment (note 5)	920,154	906,702
	<b>\$ 6,187,972</b>	<b>\$ 5,517,100</b>
<b>LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	\$ 1,378,704	\$ 1,954,762
Unamortized tenant inducements	264,651	338,492
	920,154	906,702
Invested in property and equipment	920,154	906,702
Unrestricted	3,624,463	2,317,144
	4,544,617	3,223,846
	<b>\$ 6,187,972</b>	<b>\$ 5,517,100</b>

APPROVED ON BEHALF OF THE BOARD:



, DIRECTOR

**Nick Le Pan**, CHAIR



, DIRECTOR

**Ken Crump**

# Statement of Changes in Net Assets

Year Ended December 31,			2010	2009
	<i>Invested in property and equipment</i>	<i>Unrestricted</i>	<i>Total</i>	<i>Total</i>
Net assets beginning of year:	\$ 906,702	\$ 2,317,144	\$ 3,223,846	\$ 4,606,948
Excess (Deficiency) of revenue over expenses for the year	(304,728)	1,625,499	1,320,771	(1,383,102)
Purchase of property and equipment	318,180	(318,180)	Nil	Nil
<b>Net Assets, End of Year</b>	<b>\$ 920,154</b>	<b>\$ 3,624,463</b>	<b>\$ 4,544,617</b>	<b>\$ 3,223,846</b>

# Statement of Operations

Year Ended December 31,			2010	2009
<b>REVENUE</b>				
Fees from participating audit firms			\$ 16,365,711	\$ 13,137,507
Intent to Participate fees from applicant firms			44,000	73,005
Interest income			12,091	28,796
			<b>\$ 16,421,802</b>	<b>\$ 13,239,308</b>
<b>EXPENSES</b>				
Salaries and benefits			10,438,791	8,735,705
Travel			879,868	780,088
Directors' fees and expenses			694,632	712,266
Administrative and general			538,237	451,540
Continuing education and professional memberships			474,074	262,301
Occupancy costs			443,006	424,106
Professional services			357,267	971,278
Legal services			293,945	361,090
Insurance			244,446	265,693
Amortization of property and equipment			304,728	266,702
Restructuring (note 8)			432,037	1,391,641
			15,101,031	14,622,410
<b>Excess (Deficiency) of Revenue Over Expenses for the Year</b>			<b>\$ 1,320,771</b>	<b>\$ (1,383,102)</b>

# Statement of Cash Flows

<i>Year Ended December 31,</i>	<i>2010</i>	<i>2009</i>
<b>OPERATING ACTIVITIES</b>		
Excess (Deficiency) of revenue over expenses for the year	\$ 1,320,771	\$ (1,383,102)
Add back (deduct) non-cash items:		
Amortization of property and equipment	304,728	266,702
Amortization of tenant inducements	(73,841)	(64,707)
Net change in non-cash working capital items (note 9)	(586,922)	1,589,218
Cash generated from operations	964,736	408,111
<b>INVESTING ACTIVITIES</b>		
Purchase of short-term investments	(12,300,000)	(3,000,000)
Redemption of short-term investments	10,600,000	–
Purchase of property and equipment	(318,180)	(399,665)
Cash used in investing activities	(2,018,180)	(3,399,665)
Cash and cash equivalents used in the year	(1,053,444)	(2,991,554)
Cash and cash equivalents, beginning of year	1,426,418	4,417,972
<b>Cash and Cash Equivalents, End of Year</b>	<b>\$ 372,974</b>	<b>\$ 1,426,418</b>

# Notes to the Financial Statements

DECEMBER 31, 2010

## 1. The Organization

Canadian Public Accountability Board/Conseil canadien sur la reddition de comptes is a corporation without share capital incorporated under the *Canada Corporations Act*.

The mission of CPAB is to contribute to public confidence in the integrity of reporting issuers in Canada by effective regulation and promoting quality, independent auditing. CPAB fulfills its mission principally by establishing participation requirements for public accounting firms that audit reporting issuers in Canada and by operating an effective system of quality inspections of participating audit firms.

## 2. Significant Accounting Policies

Management is responsible for the preparation of these financial statements in accordance with Canadian Generally Accepted Accounting Principles applied on a basis consistent with prior years. Outlined below are those policies considered particularly significant:

### *Cash and cash equivalents*

Cash and cash equivalents consists of cash and guaranteed investment certificates, with maturities not exceeding 90 days, with insignificant risk of changes in value.

### *Revenue recognition*

CPAB charges two types of fees to public accounting firms: an Intent to Participate fee that is collected from public accounting firms on their initial application to become participating audit firms, and an annual participation fee that is collected from participating audit firms. All fees are established to recover CPAB's costs and to provide working capital for contingency purposes.

The Intent to Participate fee is a flat fee based on the number of reporting issuer clients of the applicant firm at the date of registration. Intent to Participate fees are recorded in the accounting period in which the firm is registered and fees are received.

The annual participation fee is based on audit fees paid by a participating audit firm's reporting issuer clients. This fee is billed annually and recognized as revenue in the year to which it relates. The fee for 2010 was set at 2.0 per cent of the audit fees charged by each participating firm to its reporting issuer clients or a minimum of \$1,000. Firms in certain foreign jurisdictions are charged a rate of 0.2 per cent.

### *Property and equipment*

Property and equipment is recorded at cost. Amortization is provided on a straight line basis over the estimated useful lives of the assets commencing on the date when the assets are placed into service.

The estimated useful lives are as follows:

<i>Office equipment and furniture</i>	<i>3 – 10 years</i>
<i>IT Infrastructure and networks</i>	<i>4 – 5 years</i>
<i>Computer software</i>	<i>3 years</i>
<i>Office and computing equipment</i>	<i>2 years</i>
<i>Leasehold improvements</i>	<i>Over the life of the lease</i>

*Investments*

CPAB classifies fixed income securities as held-for-trading. Held-for-trading securities, which are purchased for redemption in the near term, are reported at estimated fair value. Realized and unrealized gains and losses are recognized as investment income when they arise. Transaction costs related to financial instruments classified as held-for-trading are expensed as incurred.

*Leases*

All of CPAB's leases are operating leases. The benefit of the seven month initial rent free period and cash inducement received at the inception of the Toronto office lease has been deferred and is being recognized on a straight line basis over the term of the lease.

*Use of estimates*

The preparation of these financial statements in conformity with Canadian Generally Accepted Accounting Principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods.

Actual results could differ materially from those estimates and assumptions. Estimates and assumptions are reviewed periodically and, as adjustments become necessary, they are reported in the year in which they become known.

**3. Financial Instruments and Risks**

CPAB classifies its financial assets and financial liabilities into the following categories:

Held-for-trading – This category comprises cash and fixed income guaranteed investment certificates with a major Canadian chartered bank. The cost of the guaranteed investment certificates, plus accrued interest income, approximates the fair value of these instruments.

Other financial assets and liabilities – Other financial assets and liabilities are carried at cost, which approximates their fair value due to their short term nature.

It is management's opinion that CPAB is not exposed to significant interest, currency or credit risks.

**4. Short-Term Investments**

Short-term investments include fixed income guaranteed investment certificates (GICs) with maturities exceeding 90 days and consist of:

	2010	2009
GIC – 0.75%, matures August 11, 2011	\$ 900,000	\$ –
GIC – 1.00%, matures October 19, 2011	2,000,000	–
GIC – 1.00%, matures November 15, 2011	1,800,000	–
GIC – 1.1%, matures December 23, 2010	–	2,000,000
GIC – 0.5%, matures June 23, 2010	–	1,000,000
	4,700,000	3,000,000
Accrued interest	9,448	14,129
	<b>\$ 4,709,448</b>	<b>\$ 3,014,129</b>

NOTES TO THE FINANCIAL STATEMENTS

Investments in guaranteed investment certificates are classified as held-for-trading and recorded at fair value. Accrued interest income of \$9,448 (2009 – \$14,129) is included in accounts receivable.

## 5. Property and Equipment

Property and equipment, recorded at cost, is as follows:

	<i>Cost</i>	<i>Accumulated Amortization</i>	<i>2010 Net</i>	<i>2009 Net</i>
Office equipment and furniture	\$ 565,516	\$ (340,980)	\$ 224,536	\$ 207,412
IT Infrastructure and networks	1,048,552	(618,364)	430,188	343,103
Computer software	125,988	(115,169)	10,819	1,993
Office and computing equipment	116,152	(93,991)	22,161	56,874
	<b>\$ 1,856,208</b>	<b>\$ (1,168,504)</b>	687,704	609,382
Leasehold improvements, net			232,450	297,320
			<b>\$ 920,154</b>	<b>\$ 906,702</b>

## 6. Bank Credit Facility

CPAB has a bank Credit Facility of \$2,000,000 bearing interest at bank prime. Amounts owing under the Credit Facility are payable on demand. No assets have been pledged by CPAB as collateral for the Credit Facility and no charges are incurred until the facility is drawn down. At December 31, 2010 and 2009 the amount owing under the Credit Facility was \$nil.

## 7. Net Assets Invested in Property and Equipment

The excess of expenses over revenue charged to net assets invested in property and equipment is composed of the following item:

	<i>2010</i>	<i>2009</i>
Amortization of property and equipment	<b>\$ 304,728</b>	<b>\$ 266,702</b>

## 8. Restructuring

During 2010, CPAB recorded restructuring expenses of approximately \$0.4 million (2009 – \$1.4 million), consisting primarily of severance charges, relating to the implementation of a human resources initiative and other strategic initiatives. At December 31, 2010 approximately \$0.2 million (2009 – \$1.1 million) of these charges remain unpaid and are included in accounts payable and accrued liabilities.

## 9. Change in Non-Cash Working Capital Items

Changes in non-cash working capital items are detailed as follows:

	2010	2009
Accounts receivable	\$ (568)	\$ 22,634
Goods and services tax receivable	(1)	(16,470)
Prepaid expenses	(10,295)	(42,855)
Accounts payable and accrued liabilities	(576,058)	1,625,909
	<b>\$ (586,922)</b>	<b>\$ 1,589,218</b>

## 10. Management of Capital

In managing capital, CPAB focuses on liquid resources available for operations. CPAB's objective is to have sufficient liquid resources to continue operating despite adverse events with financial consequences and to provide it with the flexibility to take advantage to advance its purposes. The need for sufficient liquid resources is considered in the preparation of an annual budget and in the monitoring of cash flows and actual operating results compared to the budget. As at December 31, 2010, CPAB had met its objective of having sufficient liquid resources to meet its current obligations with cash and cash equivalents of approximately \$0.4 million (2009 – \$1.4 million) and short-term investments of \$4.7 million (2009 – \$3 million).

## 11. Commitments

CPAB entered into a ten year lease for office space in Toronto in 2004. There are no asset retirement obligations associated with the lease or improvements made to the premises. The annual rent is approximately \$165,000 for the first five years and \$180,000 for the second five years. CPAB's share of the building's operating costs is currently estimated at \$272,000 per annum.

CPAB entered into additional leases for office space in 2010 in Vancouver, which expires February 29, 2012, and Montréal, which expires October 31, 2013. The annual rent for these leases is approximately \$103,000 per year.

## 12. Income Tax Status

CPAB is exempt from income tax in Canada as a not-for-profit organization under Section 149(1)(L) of the *Income Tax Act (Canada)*.

# Corporate Information

## CPAB Executive Team

### Brian A. Hunt

CHIEF EXECUTIVE OFFICER

MR. HUNT WAS INVOLVED WITH CPAB'S CREATION AND SERVED AS A DIRECTOR SINCE ITS INCEPTION. PRIOR TO HIS CURRENT POSITION AT CPAB, MR. HUNT WAS PRESIDENT AND CEO OF THE INSTITUTE OF CHARTERED ACCOUNTANTS OF ONTARIO.

### Kenneth J.A. Vallillee

SENIOR VICE PRESIDENT OF INSPECTION ACTIVITY

BEFORE JOINING CPAB, MR. VALLILLEE SERVED THREE YEARS AS SENIOR VICE PRESIDENT, FINANCE WITH A MAJOR CANADIAN BANK. PRIOR TO THAT, HE SPENT TEN YEARS AS A PARTNER AND AS THE DIRECTOR OF ACCOUNTING STANDARDS IN CANADA FOR AN INTERNATIONAL ACCOUNTING FIRM.

### Galt Arthur

VICE PRESIDENT AND CHIEF INFORMATION OFFICER

MR. ARTHUR IS A RETIRED PARTNER OF DELOITTE & TOUCHE LLP, WHERE HE SPECIALIZED IN DELIVERING ASSURANCE SERVICES TO INSURANCE AND INVESTMENT COMPANIES AND IN PROVIDING COMPUTER AUDIT AND ASSURANCE SERVICES. HE LED THE FIRM'S ENTERPRISE RISK SERVICES PRACTICE IN BRITISH COLUMBIA.

### Glenn Fagan

VICE PRESIDENT

BEFORE JOINING CPAB IN 2010, MR. FAGAN SPENT ALMOST TWELVE YEARS AS VICE PRESIDENT, FINANCE OR CFO FOR A NUMBER OF PUBLIC AND PRIVATE COMPANIES IN THE MANUFACTURING, CONSTRUCTION AND SERVICE SECTORS. PREVIOUSLY, MR. FAGAN WAS AN ASSURANCE PARTNER WITH LEGACY PRICEWATERHOUSECOOPERS LLP.

### Kam Grewal

VICE PRESIDENT OF STANDARDS

PRIOR TO JOINING CPAB, MR. GREWAL PRACTISED IN THE NATIONAL OFFICE OF PRICEWATERHOUSECOOPERS LLP, WHERE HE PROVIDED ADVICE ON ACCOUNTING, ASSURANCE AND FINANCIAL REPORTING MATTERS. HE HAS EXPERIENCE ACROSS MARKET SEGMENTS, INCLUDING TECHNOLOGY, COMMUNICATIONS AND MANUFACTURING. MR. GREWAL IS RESPONSIBLE FOR STANDARDS AT CPAB.

### Marial Stirling

VICE PRESIDENT AND GENERAL COUNSEL

MS. STIRLING IS A LAWYER AND CA. PRIOR TO JOINING CPAB, HER DIVERSE EXPERIENCE INCLUDED POSITIONS WITH OSLER, HOSKIN & HARCOURT LLP, THE CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS (ACCOUNTING

STANDARDS), THE OFFICE OF THE AUDITOR GENERAL OF CANADA AND SEVERAL YEARS WITH AN INTERNATIONAL ACCOUNTING FIRM.

### John Mastrella

DIRECTOR, INTERPROVINCIAL RELATIONS AND CHIEF FINANCIAL OFFICER

BEFORE JOINING CPAB IN 2007, MR. MASTRELLA SERVED AS A SENIOR FINANCE EXECUTIVE WITH A NUMBER OF PUBLIC COMPANIES IN THE DISTRIBUTION, REAL ESTATE, AEROSPACE, TECHNOLOGY AND HOSPITALITY INDUSTRIES. PRIOR TO HIS POSITIONS IN INDUSTRY, MR. MASTRELLA PRACTISED WITH KPMG LLP IN TORONTO.

## Directors

### Nick Le Pan

BOARD CHAIR

FORMER SUPERINTENDENT OF FINANCIAL INSTITUTIONS, OFFICE OF THE SUPERINTENDENT OF FINANCIAL INSTITUTIONS, OTTAWA, ONTARIO.

### Ian Bourne<sup>2</sup>

CHAIR, BALLARD POWER INC.; DIRECTOR, SNC-LAVALIN GROUP, CANADA PENSION PLAN INVESTMENT BOARD, WAJAX CORPORATION AND CANADIAN OIL SANDS LIMITED; AND RETIRED CFO, TRANSALTA CORPORATION, CALGARY, ALBERTA.

### Ken Crump<sup>1</sup>

FORMER CHAIR, BOARD OF TRUSTEES, COAST WHOLESALE APPLIANCES INCOME FUND; VICE CHAIR, BOARD AND CHAIR, FINANCE AND AUDIT COMMITTEE, BOARD OF COMMUNITY LIVING BRITISH COLUMBIA, VANCOUVER, BRITISH COLUMBIA.

### Guy Fréchette<sup>1</sup>

FORMER VICE CHAIR AND MEMBER OF THE EXECUTIVE COMMITTEE AT ERNST & YOUNG LLP AND FORMER MANAGING PARTNER FOR THE PROVINCE OF QUÉBEC, MONTRÉAL, QUÉBEC.

### Sheryl Kennedy<sup>1</sup>

CEO, PROMONTORY FINANCIAL GROUP CANADA AND FORMER DEPUTY GOVERNOR OF THE BANK OF CANADA, TORONTO, ONTARIO.

### Gary Porter<sup>2</sup>

FORMER DIRECTOR AND CHAIR, INVESTMENT COMMITTEE OF THE ONTARIO TEACHERS' PENSION FUND AND RETIRED CO-FOUNDER OF PORTER HÉTU INTERNATIONAL, BROCKVILLE, ONTARIO.

### Jocelyn Proteau<sup>2</sup>

CHAIR, BOARD OF BTB REAL ESTATE INVESTMENT TRUST; VICE CHAIR, BOARD AND LEAD DIRECTOR OF 20/20 TECHNOLOGIES INC.; DIRECTOR OF RICHELIEU HARDWARE, CO2 SOLUTION AND FAMILIPRIX. FORMER CHAIR, BOARDS OF STANDARD LIFE

ASSURANCE COMPANY OF CANADA, STANDARD LIFE FINANCIALS INC. AND STANDARD LIFE TRUST, MONTRÉAL, QUÉBEC.

### Alain Rhéaume<sup>2</sup>

A FOUNDER AND MANAGING PARTNER, TRIO CAPITAL INC., FORMER DEPUTY MINISTER OF FINANCE, QUÉBEC AND FORMER PRESIDENT AND CHIEF OPERATING OFFICER, MICROCELL TELECOMMUNICATIONS, MONTRÉAL, QUÉBEC.

### Peter W. Roberts<sup>1</sup>

FORMER CHAIR, RISK OVERSIGHT AND GOVERNANCE BOARD, CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS, FORMER CHIEF FINANCIAL OFFICER, SIERRA WIRELESS INC. AND PAST PRESIDENT OF THE INSTITUTE OF CHARTERED ACCOUNTANTS OF BRITISH COLUMBIA, WEST VANCOUVER, BRITISH COLUMBIA.

## Corporate Contact

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## Auditors

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187 GERRARD STREET EAST,  
TORONTO, ONTARIO M5A 2E5

## Corporate Counsel

### Fasken Martineau DuMoulin LLP

66 WELLINGTON STREET WEST, SUITE 4200,  
TORONTO DOMINION BANK TOWER, BOX 20,  
TORONTO-DOMINION CENTRE, TORONTO,  
ONTARIO M5K 1N6

SHERYL KENNEDY WAS APPOINTED AS A BOARD MEMBER ON FEBRUARY 8, 2010.

WENDY K. DOBSON AND RONALD G. GAGE REACHED THE END OF THEIR EXTENDED TERMS OF OFFICE AS DIRECTORS ON FEBRUARY 16, 2010.

GALT ARTHUR RETIRED AS VICE PRESIDENT AND CHIEF INFORMATION OFFICER ON DECEMBER 31, 2010.

GLENN FAGAN IS RESPONSIBLE FOR HUMAN RESOURCES AND, AS OF JANUARY 1, 2011, INFORMATION TECHNOLOGY.

- 1 MEMBER OF THE AUDIT COMMITTEE
- 2 MEMBER OF THE HUMAN RESOURCES AND GOVERNANCE COMMITTEE

TO BE MORE ENVIRONMENTALLY FRIENDLY, CPAB HAS CHOSEN NOT TO PRINT HARD COPIES OF THIS ANNUAL REPORT FOR GENERAL DISTRIBUTION. THE REPORT IS AVAILABLE FOR VIEWING AT WWW.CPAB-CCRC.CA.