

Canada in a Global Context – Questions 2 and 4

1. *How important are company headquarters to Canada's economic prospects and ability to create jobs and opportunities for Canadians? How important are global divisional head offices? What factors influence their location?*

It is, of course, vitally important for Canada to continue to attract and retain its share of company headquarters. Any country benefits when it hosts the head office of an international organization – in terms of top-quality jobs, market access, investment and decision-making clout.

We believe that one of the under-appreciated factors that impacts on investment and head offices is the liability regime of the country. Currently, Canada is saddled with an antiquated system known as joint and several legal liability. Under such a system, a party that is found to be just one per cent responsible for a financial loss can be held to account for fully 100 per cent of a claim.

This risks a tremendous negative impact on doing business in a jurisdiction as it increases the threat of being held responsible for disproportionately heavy costs in a legal case. This is especially relevant to the audit profession and is increasingly threatening to shut off access to vital financial and accounting services for businesses of every size and, with it, access to the investment capital they need to grow and create jobs, owing to the needless risk posed by joint and several liability.

The current regime also acts as a restraint on Canada's ability to attract and retain top professional talent, due to the fear of exposure to an unreasonable degree of legal liability.

Audit firms – not just the large firms but also smaller practices in smaller communities (*See Appendix A – An Issue for Bay Street and Main Street*) – are often the targets of huge and growing claims even though they may have little responsibility for a financial loss. Essentially, they are being asked to “insure” our country's capital markets by being available as a “deep pocket” for investor lawsuits.

Our members tell us that the current liability scheme is:

- *driving them out of the marketplace for their services because of skyrocketing insurance costs and exposure to disproportionate liability*
- *shutting off access to vital audit services for enterprises of every size, which in turn deprives those companies of the investment capital they need to compete, grow and create jobs, and*
- *pushing Chartered Accountants and other financial professionals out of the audit and assurance field and, sometimes, right out of Canada.*

(For examples of the types of problems this causes Canadian business, see *Appendix B – Real Businesses – Real Impacts*).

How does joint and several liability hurt our competitiveness when pursuing or retaining head offices? Many companies, including international audit firms, are becoming increasingly wary of litigation costs and are looking for safe harbours for conducting their work. By that standard, the increasingly litigious environment in Canada can look like a daunting place to establish or maintain an organization.

The competitive situation for Canada is not getting better. Currently, our major trading partners in the U.S., U.K., Europe and Australia and elsewhere have acknowledged the problem and are at various stages of addressing the liability issue with reforms, such as moving to a proportionate liability system. Under proportionate liability, responsibility for a financial loss is apportioned according to the extent of an individual's responsibility for that loss.

Reforms already underway in other jurisdictions will ultimately lead investors to ask: Why would I place my head office in Toronto, Halifax or Vancouver? Why take that risk? This is particularly true in the Ontario context, where neighbouring Great Lakes States (and many others) have already moved to various forms of proportionate liability – creating a distinct competitive disadvantage for this province in one of the most wealthy and concentrated consumer markets in the world (*See Appendix C – Keeping up with the Neighbours*).

In the case of international audit firms, the temptation to establish your business and the high-paying jobs that come with it outside of Canada will only grow if we fail to address this crucial business issue. The reality is that, in a tightly interconnected world, high value financial services for a client in Montreal can often be provided by professionals in Memphis or Mumbai.

Canada needs a well-designed liability regime that protects the interests of investors, professionals, the business community and the general public.

2. Do Canada's economic policies appropriately reflect our increased integration with the North American and global economy? How might these policies be changed to better reflect this new competitive environment?

From a global standpoint, Canada is seen as an anomaly in that its economic policies are set at various levels by our federal, provincial and territorial governments. In contrast with the United States and the European Union, Canada's economic policies are often a confusing and occasionally conflicting maze of legislation and bureaucratic red tape that hampers the business community's ability to compete.

As an example of this in action, the Institute would like to highlight our inconsistent and, in some jurisdictions, non-existent standards for public accounting qualification and conduct in Canada.

Public accounting is the business of expressing independent assurance on financial statements and other financial information of enterprises of every size, to ensure that the information truly reflects their financial condition. Large and small investors, financial institutions and other third parties then use that assurance to help them make informed investment and lending decisions. Many of those decisions involve investments in RSPs, mutual or pension funds – making the practice of public accounting relevant to nearly all Canadians.

Naturally, international investors also rely on financial statements when they are deciding on whether to allocate capital, resources and talent to a particular country. When they view statements from most of our peers in developed nations, they have the assurance that those financial statements have been signed off by auditing and assurance professionals who have met the highest standards for education, experience and conduct.

In Canada, it is not that simple. While Chartered Accountants in every province and territory must meet the CA profession's uniformly high and internationally recognized standards, there is an underlying "patchwork quilt" of 13 differing forms of regulation for entry into the field of public accounting by people who are not Chartered Accountants.

In some provinces, notably Ontario and Quebec, where the majority of our public companies reside and the bulk of securities trading take place, the standards for conducting public accounting are high and recognized internationally. In other provinces, however, regulations allow people with accounting designations that are not internationally recognized to practice public accounting and, in some Canadian provinces, anyone who can get a client can sign off on financial statements, even if they have no relevant designation, education or professional standards oversight whatsoever.

Some have argued that if low (so-called "minimum") or non-existent standards suffice in some jurisdictions, perhaps these should be the starting point for benchmarking nationally consistent standards. However, this ignores Canada's obligations to investors and the general public, both at home and abroad, and risks starting a "race to the bottom" that will render Canadian standards for the practice of public accounting unacceptable to other major industrialized

nations. It would also risk nullifying our international trading partner commitments with respect to public accounting services, which are founded on Mutual Recognition Agreements (MRIs) between major accounting bodies in each jurisdiction. These MRIs serve to certify that public accounting qualification and conduct standards among signatory jurisdictions have been found to be substantially equivalent in depth, breadth and rigour.

To ensure our competitiveness and ability to attract investment, Canada needs internationally recognized, nationally consistent standards for qualification and conduct for both CAs and non-CAs who wish to practice public accounting, in order to safeguard our existing international trading partner commitments. (*See Appendix D - Proposed National Standards: A Principled Approach*). Those commitments currently are anchored by Mutual Recognition Agreements between Canadian CA Institutes and their peer accounting bodies in our major trading partners. These agreements determine “substantial equivalence” in standards among the bodies, thereby ensuring that the qualification and conduct standards for public accounting are internationally recognized.

As an example of how this works in practice today, we would draw the Panel’s attention to the system in Ontario. Our province’s competitiveness benefits from internationally recognized high standards for public accounting that are mandated in legislation – the *Public Accounting Act, 2004* – that was passed with support of all parties in the Legislature (*See Appendix E - Chronology: The New Public Accounting Act, 2004*).

The Act sets out the required qualification and conduct standards for public accountants. They are benchmarked against internationally recognized standards to ensure financial statements signed off on in Ontario are accepted in other jurisdictions across Canada and around the world.

Competition between accounting designations is allowed on the basis that, once the standards set out in the Act are met, other accounting bodies in Ontario will be allowed to license their members to practice public accounting alongside CAs.

The *Public Accounting Act, 2004* complements the U.S. *Uniform Accountancy Act*, which extends consistent public accounting standards across more than 40 U.S. States and territories in similar ways for the same reason.

To compete globally, our country needs nationally consistent public accounting standards that match those of our international competitors. Investors, in Canada and abroad, deserve nothing less than the reassurance that they can trust the education, experience and conduct of the professionals who are doing vital audit and assurance work.