CPAB
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CANADIAN PUBLIC ACCOUNTABILITY BOARD

World Class Audit Regulation

2011 Annual Report

Delivering Value

The Canadian Public Accountability Board (CPAB) is Canada's audit regulator, dedicated to protecting the investing public's interests and to delivering value to its various stakeholders through world class audit regulation. As a world class audit regulator, focused on excellence, CPAB delivers value by promoting high-quality, independent auditing. As a champion of audit quality, CPAB contributes to public confidence in the integrity of financial reporting, which supports Canada's capital markets.

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.

As CPAB continues the next stage of development, the organization will enhance its capability as a strategic regulator in five 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 and related recommendations that provide unique insight into audit risk matters and practices. CPAB strives to conduct strategic inspections that are risk-based, conducted efficiently, delivered on time, 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. CPAB is increasing accountability across the organization so that the roles, responsibilities and interdependencies of each division and each person are clear. There are also rewards and consequences for how these accountabilities are put into operation.

An advanced skill set for broader risk assessment

Having successfully recruited top talent, CPAB is now focusing on the further development and retention of staff. Staff skills must evolve from those of auditors to those of a strategic audit regulator.

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 even more strategic, provide greater risk assessment, and add more relevance to participating firms.

Outreach to key stakeholders

CPAB is in a unique position to provide Audit Committees and other stakeholders with information and thought leadership on current audit developments, which will enhance their efforts to meet their governance objectives with respect to audit quality.

… 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 other 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. CPAB believes this knowledge could be better utilized to bring greater value to investors and other users of financial statements.

Audit Committees

Audit Committees are an important oversight and entity-wide control feature of corporate governance. Through its inspection work and thought leadership on audit reporting and related topics, CPAB can assist Audit Committees in their efforts to enhance audit quality. CPAB expanded its outreach to Audit Committees in 2011 and will continue to do so in 2012.

Audit Firms

Annually, CPAB inspects all audit firms that audit more than 100 reporting issuers, representing 99.5 per cent of the total market capitalization. There are now 14 firms in this category. CPAB also regularly inspects firms that audit fewer than 100 reporting issuers. These smaller firms account for $9.5 billion 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, 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 encourages dialogue on auditor inspection techniques, results and remediation.

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Report of the Chair

Nick Le Pan
BOARD CHAIR

The Canadian Public Accountability Board (CPAB) is dedicated to protecting the investing public's interests and to maintaining public confidence in financial reporting, by promoting high-quality audits of public company financial statements audited in Canada. This year we continued to focus on what it takes to maintain and enhance our position as a world class audit regulator.

Investors should continue to have confidence in the integrity of public company financial statements audited in Canada. However, audit quality is not uniformly high across all engagements in all audit firms. Even for major firms, there are lapses that result in an unacceptably high risk of material financial misstatements. The improvements necessary are outlined in this report and in our Public Reports on inspection findings. We will continue to promote continuous improvement—both in auditing and at CPAB.

High-quality auditing depends on everyone in the financial reporting chain: preparers of financial statements; their Audit Committees; audit firms and their partners and staff; audit and accounting standard setters; and the analyst and investor community.

The 2010–2012 strategic plan, established by the Board, makes outreach to other participants in audit quality a priority.

The three-year strategic plan the Board established in 2009 makes outreach to other participants in audit quality a priority. This outreach complements CPAB's traditional inspection program by providing other participants with useful information, in order to enlist them in the process of continuous improvement. We believe this approach levers our effectiveness as an audit regulator and helps others better perform their role.

I am very pleased that we have made major progress on this front in 2011, particularly with outreach to Audit Committee chairs and members. This culminated in CPAB's Audit Quality Symposium held in early December, which has catalyzed a number of follow-up actions with the audit profession, regulators, standard setters and private-sector participants. We are carrying this focus into 2012. The Board, together with management, will also examine how we can enhance the transparency of our inspection results for Audit Committees and investors, while maintaining our ability to issue timely and focused reports, recommendations and requirements to regulated audit firms.

We have also focused on enhanced risk assessment to drive our inspection program. This has enabled us to achieve better inspection findings, which now identify the root cause of audit deficiencies noted at audit firms.

CPAB's ultimate strength, and what I believe makes us a world class audit regulator, is our people—their pursuit of excellence, dedication, initiative, judgment, willingness to listen to the views of regulated firms, and expertise.

Over the past year we have significantly enhanced our human resource capability, attracting new talent and providing more effective training to all staff to better address today's challenges. CPAB's regional offices in Montréal and Vancouver became fully staffed in 2011. This human resources effort has been a major Board priority. In 2011 and into 2012 we have shifted our focus to staff retention, succession planning and further training and development.

It is also essential that CPAB fulfill its mandate in an effective and efficient way. In 2011 the Board focused on performance measures for CPAB, in preparation for a 2013 stakeholder survey assessing our performance.

There was no increase in the fee rate charged to audit firms and reporting issuers in 2011, and none is contemplated for 2012.

CPAB is now in the third and final year of its current strategic plan. In 2012 the Board will develop a strategic plan for 2013–15, which will be designed to further enhance our capability as a world class audit regulator.

In July 2011 CPAB welcomed a new director, Benita M. Warmbold, FCA, to the Board. Ms. Warmbold is Senior Vice President and Chief Operations Officer at the Canada Pension Plan Investment Board.

I would like to thank my colleagues on the Board of Directors for their support and efforts in 2011. I also very much appreciate the outstanding work done over the past year by Chief Executive Officer Brian Hunt, the management team and staff.

Nick Le Pan
BOARD CHAIR

CPAB's ultimate strength, and what I believe makes us a world class audit regulator, is our people.

CPAB Board Members

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; 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

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; FORMER DEPUTY GOVERNOR OF THE BANK OF CANADA, TORONTO, ONTARIO

Gary Porter

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

Jocelyn Proteau

CHAIR, BOARD OF BTB REAL ESTATE INVESTMENT TRUST; 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; FORMER PRESIDENT AND COO, MICROCELL TELECOMMUNICATIONS, MONTRÉAL, QUÉBEC

Peter W. Roberts

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

Benita M. Warmbold

SENIOR VP AND COO, CANADA PENSION PLAN INVESTMENT BOARD; DIRECTOR, CANADA DEVELOPMENT INVESTMENT CORPORATION, QUEEN'S SCHOOL OF BUSINESS ADVISORY BOARD, TORONTO FINANCIAL SERVICES ALLIANCE AND ALZHEIMER'S SOCIETY, TORONTO, ONTARIO

Report of the Chief Executive Officer

Brian A. Hunt, *FCA*
CHIEF EXECUTIVE OFFICER

During 2011 CPAB made significant progress in both expanding and focusing its inspection activity of firms auditing reporting issuers in Canada. As part of this process, in addition to its more traditional inspections, CPAB completed its first targeted review of firms auditing companies operating in foreign jurisdictions. CPAB also made significant strides in implementing its 2010–12 strategic plan and in support of its vision of being a world class audit regulator.

Inspection Results

CPAB's 2011 inspection results are disappointing, demonstrating that greater focus is needed on audit execution, especially in higher-risk areas of the audit. CPAB is concerned that, in many cases, the same systemic inspection findings are identified year after year without significant improvement. Firms have responded positively to CPAB's call to action and are implementing action plans for improvement.

2011 inspection results disappointing

In 2011 CPAB found deficiencies in Generally Accepted Auditing Standards (GAAS) in firms of all sizes. A GAAS deficiency is defined as a failure to obtain sufficient, appropriate audit evidence to support a financial statement assertion for a material account balance or transaction stream. The Big Four firms, which audit 94 per cent of reporting issuers by market capitalization, had a GAAS deficiency rate of 20–26 per cent on the files inspected by CPAB. This rate was considerably higher in the case of other National and Regional and Local firms. It should be noted that the deficiency rate indicated will not necessarily be consistent across all reporting issuers or industry sectors, as accounting and audit complexity vary. These deficiencies indicate too high a risk of material financial misstatements.

In almost all cases, when audit firms performed additional audit work to remedy deficiencies noted by CPAB, there was no restatement of the financial statements. However, this does not mean that there was no risk of a restatement. In major corporations, with strong internal controls, the chances of a material misstatement going undetected may be low; however, the risk is still real. Therefore, because of the risk of restatement, CPAB believes these inspection results are unacceptable and would not expect Audit Committees and the investment community to tolerate such a high deficiency rate.

Investor confidence

While there has been little progress in terms of improved audit quality, CPAB believes investors should continue to have confidence in the integrity of public company financial statements audited in Canada. CPAB inspections did not lead to many restatements and firms are progressing on their remedial action plans. The largest and most complex clients of the major audit firms generally demonstrate good audit quality. However, this cannot be said for all engagements in all firms and, even for major firms, there are performance lapses that result in reduced quality. So continued vigilance by all those responsible for the financial statements: preparers, their Audit Committees, and auditors, as well as by investors, is called for.

Audit execution is the root cause

While CPAB generally finds that the firms' audit methodologies comply with GAAS requirements, and the firm's risk assessment is generally appropriate, inspections continue to identify problems in the execution of the audit work. It is disconcerting to note that the majority of audit deficiencies relate to basic audit procedures, not the audit of complex transactions.

In the increasingly complex world of financial reporting, and with the transition to International Financial Reporting Standards (IFRS), senior engagement personnel need to spend more time with their staff to ensure that audit risks are appropriately identified and that the audit strategy to address such risks is properly executed. This needs to become a greater area of focus for firm management. It should be viewed as equal to or greater in importance than business development when firm management evaluates the performance and contribution of its partner and manager group.

Deficiencies similar to those found by other regulators—not just a Canadian problem

This is not just a Canadian problem. CPAB's findings are consistent with those noted by other audit regulators around the world. In particular, they have also raised concerns about a lack of professional skepticism, inadequate supervision and review, ineffective substantive analytical procedures, and the poor quality of audit evidence in the audit files. Reported deficiency rates in several major countries are similar to CPAB's. Matters of greatest concern to regulators are not country-specific, but relate to the profession at large.

Firms required to develop action plans to improve audit quality

As a result, CPAB has required certain firms to develop meaningful and measurable action plans to improve audit quality. Such plans must contain short-term actions to deal with 2011 year-end audits and longer-term actions designed to permanently change behaviours. CPAB expects to see significant improvement in the quality of audit work on 2011 year-end audits. However, it will take a year or two for the full benefit of the action plans to be realized. CPAB needs and expects real cultural change at the firms if the desired results are to be achieved and maintained.

Among other things, the action plans require the firms to identify measurable milestones, with timelines, and to allocate implementation responsibilities to individuals with appropriate authority within the firm. Firms must also implement a self-monitoring mechanism to ensure key elements of the plan are executed effectively and on time.

CPAB is pleased to report that the firms recognize that the status quo is not acceptable and have responded positively to these recommendations. CPAB will closely monitor the action plans throughout 2012 and into 2013 to assess that they are implemented effectively.

Auditing in foreign jurisdictions

CPAB has been monitoring the extent to which Canadian reporting issuers have operations in foreign jurisdictions. Foreign operations can present challenges to the conducting of high-quality audits of financial statements.

In 2011 CPAB undertook a special review of 24 reporting issuers, each of which had extensive foreign operations. While CPAB monitors reporting issuers with operations in all foreign jurisdictions, the focus of this initial review was Canadian public companies with extensive operations in China. This was a result of the significant concerns expressed by analysts, investors, securities regulators, and other audit regulators about the quality of financial reporting by Chinese companies. CPAB has identified additional reporting issuers with substantial operations in other foreign jurisdictions and will complete inspections of those audit files in 2012.

CPAB was disappointed by the results of its review of Canadian reporting issuers with significant operations in China. In too many instances, auditors simply did not properly apply procedures that would be considered fundamental in Canada. CPAB also found a lack of professional skepticism when auditors were confronted with evidence that should have raised red flags regarding potential fraud risk.

CPAB does not believe this issue is unique to the audits of companies based in China. CPAB believes it reflects a general failure on the part of auditors to recognize that the differences in the business environments of foreign jurisdictions require modification to the nature, timing and extent of their audit procedures.

Fundamentally, CPAB believes Canadian auditors have the talent and capabilities to perform quality audits in foreign jurisdictions. However, they must execute these audits with a high degree of professional skepticism and a thorough understanding of the business environment, to ensure their audit procedures adequately address risks arising from the foreign jurisdiction's business customs and practices.

CPAB's Progress in 2011

CPAB's strategic plan includes 10 major strategic initiatives, including key deliverables, for 2010–12. These initiatives are organized into four areas: Organization, Stakeholders, Infrastructure and Regulatory. CPAB successfully implemented the majority of its objectives for 2011. Implementation will continue in 2012, as will the development of a new set of strategic initiatives for 2013–15.

There are four key areas where CPAB made significant advancements and that are highlighted in this report: Human Resources; Inspections; Outlook and Thought Leadership; and Outreach to Audit Committees.

Human Resources

In 2010 CPAB implemented a new organizational structure, which established clear roles and responsibilities for staff at all levels. As part of this process, management developed core values for CPAB (Excellence, Trust, and Respect) and recruited staff with the skills and capabilities needed in the new organizational structure. The focus in 2010 was on recruiting and CPAB was very successful in attracting top talent. In 2011 management's focus shifted to developing staff and to implementing the core values. The year was marked by a significant change in the organization's culture. I am very pleased to report that CPAB has been able to attract quality staff who are in mid-career, who are excited to be with the organization and who are building their careers while helping CPAB achieve its strategic objectives. Through their actions, staff members are clearly demonstrating pride in the organization.

Fundamentally, CPAB believes Canadian auditors have the talent and capabilities to perform quality audits in foreign jurisdictions.

Providing exceptional career and professional development for CPAB staff is one of our top priorities. CPAB is making substantial investments in core human resources programs and policies, value-added professional development, including leadership development, and initiatives to evaluate organizational design and the return on human capital. Success in these areas is critical to CPAB's overall success in fulfilling its mandate and achieving its vision.

In 2010 CPAB formed a Leadership Council, comprising the Management Committee, Senior Directors, Regional Directors, General Counsel and the Chief Financial Officer. The Leadership Council, which met four times in 2011, discusses strategic and operational matters and facilitates communications to staff at all levels of the organization.

In 2012 CPAB will continue to move from auditor-focused inspections to regulatory-focused inspections.

Professional development has been part of all staff training sessions and key staff members completed leadership programs during 2011, with more planned in 2012. The Leadership Council and other CPAB leaders participated in a 360-degree feedback program during the year. Retention efforts have been successful, with very limited staff turnover.

CPAB's Western (Vancouver) and Eastern (Montréal) Regional Offices are now fully staffed, which was a key objective for 2011. In 2012 more emphasis will be placed on staff development, as well as outreach initiatives, in those locations.

During 2011 CPAB seconded two members of its staff to international regulators: one to the Financial Reporting Council in London, England, and another to the Australian Securities and Investments Commission (ASIC) in Australia. Both secondees will return to CPAB in early 2012 and will provide significant hands-on IFRS experience during upcoming inspections. In 2012 CPAB will send another secondee to the ASIC.

Inspections

In 2011 CPAB began moving from auditor-focused inspections to regulatory-focused inspections. The most visible aspect of this change is seen in the nature of CPAB's recommendations to firms, which focus on the root causes of audit deficiencies and measures to enhance audit quality.

CPAB launched a new inspection methodology in April 2011, which reflects the new Canadian Auditing Standards (CAS). Given its new organization and staff, together with its new inspection methodology, CPAB has moved to a new level of inspection competency and capability. The organization continues to improve the quality of its inspection findings, focusing its recommendations to firms on key issues that enhance audit quality and provide value.

In 2012 the inspection methodology will be updated to reflect recommendations arising from the 2011 inspections and to incorporate changes resulting from the introduction of IFRS. In the fall of 2011 CPAB developed a quality review process, which was made possible by the new inspection methodology. The first quality monitoring reviews based on the new process were conducted in February 2012. Results from the reviews will be incorporated, as appropriate, in 2012 training. CPAB has also implemented a new engagement file review protocol intended to drive enhanced consistency and quality across CPAB inspections. This has been well received by staff and the firms.

CPAB conducted extensive work on risk in 2011, including developing documents relating to: CPAB's risk universe; enterprise risk identification and monitoring; and a composite inspection risk model. This has helped CPAB identify priority risk areas for 2012, including audit risks in foreign jurisdictions. Among other benefits, CPAB's enhanced risk assessment process improved the quality of information provided to inspection staff. In 2011 CPAB used its risk assessment information to allocate inspection activity resources to a greater extent than ever before.

The enhancement of CPAB's risk assessment capabilities and the further integration of risk into the inspection process resulted in a significantly improved focus of the inspections.

Outlook and Thought Leadership

Outlook

In 2011 CPAB undertook several initiatives to broaden the ways in which it contributes to enhancing audit quality. To help direct its activities on a number of fronts, including communications, talent recruitment, accounting industry-related research, and international activities, CPAB developed a communications plan. This plan identifies target audiences, key messages, possible value-added information CPAB could provide, and vehicles and opportunities to deliver these messages and this information. An important part of enhancing outreach has been building a database of key stakeholders and contact information, and surveying stakeholders.

The audit process involves many participants—preparers, their Audit Committees, audit firms, provincial and national regulators, investors, professional accounting bodies and standard setters. Financial policy-makers also have an interest.

Each group expects different things from CPAB. Those who are most directly affected by CPAB's work—particularly the large audit firms and accounting industry associations—have said they want more value-added from the organization. This means spending more time providing guidance about findings and root cause considerations.

Other groups familiar with CPAB but less actively engaged with the organization, such as government and other financial regulators, have said they need to be updated on CPAB's work but do not require frequent interaction.

CPAB Management Committee

Brian A. Hunt, FCA
CHIEF EXECUTIVE OFFICER

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

Glenn Fagan, CA
VICE PRESIDENT

Kam Grewal, CA, CPA
VICE PRESIDENT OF STANDARDS

Audit Committees, on the other hand, have little or no awareness of CPAB. They require information about CPAB's oversight role and how the organization helps improve audit quality. They would also welcome information about industry trends and news that would help them in their work, as well as more information about CPAB inspection findings.

Thought leadership

CPAB's credibility as a thought leader, both domestically and internationally, grew significantly during the past year. It is important that CPAB's on-the-ground experience relating to audit quality be used to assist policy-makers and standard setters. CPAB's views are now sought—and taken seriously—by standard setters and other regulators. A demonstration of the organization's progress in this area was CPAB's first annual Audit Quality Symposium, which attracted thought leaders and policy-makers from across Canada and around the world.

The symposium, which was a resounding success, focused on issues relating to audit quality, current proposals to address these issues and specific action required in Canada. While the solutions put forward by various groups and jurisdictions participating in the symposium differed, there was remarkable consensus around the major challenges that currently exist, and around certain solutions.

These challenges include making financial reporting and the audit more relevant, enhancing the role of Audit Committees and improving the interaction among regulators, auditors and Audit Committees. There was also significant discussion about the need for audit firms to embrace a culture of independence, professional skepticism and commitment to audit quality.

CPAB believes Canada must proactively address current concerns and proposals around audit quality. This means developing Canadian-made solutions and influencing international developments. In today's global economy, measures implemented in one jurisdiction can have far-reaching effects elsewhere. Canadian regulators typically "punch above their weight" internationally and should be a strong voice in discussions relating to financial reporting and audit quality.

CPAB supports reform and has responded to the proposals put forward by the EU, US and other jurisdictions. The next step is to work with other Canadian stakeholders to identify priority issues, their root causes and to develop a made-in-Canada solution. As Canada's audit regulator, dedicated to protecting the investing public's interests, CPAB's goal is to ensure any changes are implemented in a way that demonstrably improves audit quality and disclosures in financial information.

Outreach to Audit Committees

A key focus in 2011 was outreach to Audit Committees.

On this front, CPAB both coordinated and participated in a number of Audit Committee roundtable discussions during the year, including eight in Vancouver, Calgary, Toronto and Montréal. These discussions enabled CPAB to enhance its role as an audit regulator. They also provided an opportunity to share information to help Audit Committees, within their governance role, to be more effective in enhancing audit quality. In 2012 CPAB will further its outreach to Audit Committees and other stakeholders by providing information to them on matters of interest, which will assist them in meeting their governance objectives.

International partnerships

In April 2011 CPAB signed an updated agreement with the Public Company Accounting Oversight Board (PCAOB) under the new *Dodd-Frank Act* provisions. This agreement has strengthened both CPAB and the PCAOB by allowing the two bodies to share inspection methodologies and inspection findings. This is an important step forward in CPAB's relationship with the PCAOB. As this new agreement is implemented and updated, CPAB and the PCAOB will be able to more effectively utilize inspection activity resources.

Late in 2011 CPAB finalized a protocol with the ASIC regarding procedures for cooperating in the oversight of auditors subject to the regulatory oversight of both CPAB and the ASIC. Pursuant to the Protocol, CPAB will conduct inspections of three participating firms in Australia in early 2012. In addition, CPAB is in discussions with auditor oversight authorities in both Japan and the Netherlands and hopes to finalize Memoranda of Understanding (MOUs) shortly. Authorities in Germany are interested in entering into a similar arrangement. CPAB is considering other jurisdictions where it would be beneficial to seek MOUs and will pursue this in 2012.

In 2011 CPAB became the first audit regulator to sign a Participation Agreement with the International Organization of Securities Commissions (IOSCO) providing CPAB with access to the IFRS decisions database. This will greatly assist CPAB in its 2012 inspections, as it evaluates the transition to IFRS in Canada.

CPAB continues to help the Cayman Islands and Bermuda as they establish their own auditor oversight bodies. This includes providing advice on draft legislation and draft regulations prepared by their securities commissions.

CPAB actively participates in the International Forum of Independent Audit Regulators (IFIAR), which encourages dialogue on auditor inspection techniques, results and remediation. More than 100 countries have now established organizations such as CPAB. More than a third of them are members of IFIAR, and this number continues to grow.

CPAB was elected to the Advisory Council of IFIAR in March 2011 and continues to chair the IFIAR Global Public Policy Committee Working Group.

Regulatory Issues

CPAB requires an effective regulatory framework to perform as a world class audit regulator. Significant progress was made in 2011, with the enactment of new auditor oversight legislation in several provinces that formally recognizes CPAB. Early in the year, CPAB was recognized as an auditor oversight body in British Columbia. Similar legislation was introduced in August in Manitoba and in December in Saskatchewan. With the progress made in 2011, CPAB is now recognized as an auditor oversight body under legislation in Québec, Ontario, Manitoba and British Columbia.

CPAB is continuing discussions with the Québec Law Society regarding legislative amendments that would provide clear language concerning CPAB's access to privileged information in the auditor's working papers on the same "absolutely necessary" basis as in Ontario, Manitoba and British Columbia. CPAB believes that access to privileged information in the audit working papers that supports the audit opinion is absolutely necessary to the purpose of the review

CPAB actively participates in the International Forum of Independent Audit Regulators, which encourages dialogue on auditor inspection techniques, results and remediation.

of the audit. The "absolutely necessary" provision worked very well in CPAB's 2011 inspections. We anticipate that new language will be proposed shortly to the Québec Government.

We will be discussing CPAB legislation with other Canadian jurisdictions in 2012.

Financial Strategy

In 2010, CPAB increased fees to reporting issuers from 1.6 per cent to 2.0 per cent of their audit fees. This increase was necessary to support CPAB's restructuring, enhance IFRS training, improve risk assessment capabilities and increase inspection activity. These additional fees were also used to build reserves.

CPAB achieved its financial objectives in 2011, earning a small surplus of $440,000 on revenues of approximately $16 million. As forecast in last year's Annual Report, no rate increase was required in 2011 and none is planned for 2012.

Conclusion

CPAB's vision is to be and be viewed by key stakeholders as a world class audit regulator.

Led by a strong team and buttressed by a solid regulatory foundation, CPAB is contributing to higher-quality public company audits. It has gained the respect and confidence of its stakeholder community and is developing a reputation for being purposeful, independent and fair.

CPAB's investments in organizational structure, human resource policies and systems aligned with its core values, technical training and professional development is making it a career destination for top talent.

In 2012 CPAB will continue the implementation phase of its strategic plan, notably in the areas of organizational development and human resources. It will also become more outward-looking, by reaching out to and adding value for key stakeholders.

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

Brian A. Hunt, FCA
CHIEF EXECUTIVE OFFICER

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 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***

Auditors in the Spotlight

Overview and Scope

As at December 31, 2011, there were 303 participating audit firms registered with CPAB. During 2011, 30 firms registered with CPAB and 36 terminated their registration of their own accord.

Each year, CPAB inspects all firms that audit 100 or more reporting issuers. There are now 14 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 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.

During 2011, CPAB inspected 88 firms (2010–69) and reviewed 245 audit engagements (2010–232) 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, including 114 audit engagements carried out by those firms
- Inspections of 10 firms inspected annually, and reviews of 41 audit engagements carried out by those firms
- Inspections of 53 Regional and Local Firms, including 84 audit engagements carried out by those firms (of which 27 were "desk inspections" of smaller firms as well as 14 firms which were part of CPAB's special review)
- Inspections of three foreign firms, including three engagements
- Eighteen follow-up inspections (to ensure that CPAB's recommendations have been implemented), including three additional engagements

In addition to the inspections CPAB conducted, provincial accounting bodies inspected more than 60 smaller firms that audit reporting issuers. These bodies shared their findings with CPAB.

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 inspections of the audit files relating to Canadian reporting issuers. In 2011, based on its risk analysis, CPAB carried out inspections of audits performed by three foreign firms.

CPAB uses a number of risk analysis processes to identify higher-risk reporting issuer audits and allocates its inspection resources accordingly. The 2011 inspections comprised focused reviews that examined the audit work in high-risk areas such as valuations, impairments, revenue recognition, complex financial instruments, and going concern. In addition, CPAB monitored firm readiness for IFRS and evaluated how the firms assessed their clients' readiness for conversion to IFRS. CPAB also assessed the firms' implementation of the new Canadian Auditing Standards (CAS).

During 2011, CPAB's 33-member inspection staff was supported by seven contract consultants who primarily specialize in the areas of taxation, IFRS, information technology, Generally Accepted Accounting Principles (GAAP) and valuations.

Results of Inspections

CPAB's 2011 inspection results are disappointing because they show little improvement from the previous year. In fact, the Big Four firms had a GAAS deficiency rate of 20–26 per cent on the audit files inspected in 2011. In the case of other National and Regional and Local firms, CPAB found deficiency rates that were considerably higher. Many of the deficiencies are similar to those identified in last year's inspections. CPAB's findings are also consistent with those noted by other audit regulators around the world. While there were only a few financial restatements resulting from these audit deficiencies, they represent a risk of material misstatement that CPAB believes is too high.

For more information, CPAB's Public Report on its 2011 inspections is available at www.cpab-ccrc.ca.

Reporting

CPAB gives each firm a report on each file inspected, as well as an overall report on the firm as a whole. A participating audit firm's inspection report will, in most cases, include a number of recommendations arising from deficiencies related to engagement performance. These recommendations are applicable to either systemic/firm-wide processes or specific engagement files that were inspected. Deficiencies noted in the other elements of quality control may also result in recommendations. The inspection report separately identifies CPAB's top three to five recommendations that, when implemented, would improve audit quality.

CPAB's recommendations must be implemented by the audit firm within 180 days of the date of the inspection report. Failure to implement the recommendations to CPAB's satisfaction would give rise to disciplinary action being placed on the audit firm in the form of a Requirement, Restriction or Sanction. Disciplinary action starts with a Requirement, which limits the scope of the audit work the firm can undertake until the identified deficiencies have been corrected, within a specified timeframe. In more serious cases, or should the Requirement not be sufficient, then CPAB would place a Restriction on the firm. This elevates the disciplinary measure that requires action by the firm and includes notifying the relevant provincial securities regulators that CPAB has placed a Restriction on the firm. The third level of discipline, for more serious situations, is a Sanction, which in addition to the securities regulators, requires the Audit Committees of reporting issuer clients of the firm to be notified.

In 2011, based on risk analysis, CPAB carried out inspections of audits performed by three foreign firms.

Depending on the severity of the finding, the deadline for implementing CPAB's recommendations may be less than 180 days. This is particularly true where there may be a potential restatement of financial statements as a result of CPAB findings. Requirements, Restrictions or Sanctions take effect immediately unless the firm requests a review proceeding. In all cases, before disciplinary measures are lifted, CPAB follows up to ensure that the recommendations have been implemented satisfactorily.

Following the 2011 Inspections, CPAB has Requirements on seven firms (2010–five) and for one of these firms the Requirement was converted to a Restriction in 2012 (2010–nil). All remain in effect at year-end. During 2011 CPAB did not place a Sanction on a participating firm (2010–nil). No review proceedings or any other proceedings were conducted relating to CPAB's disciplinary decisions in 2011 or 2010.

Management's Discussion and Analysis

Operating Results, Outlook, Principal Risks and Uncertainties

The following is a review of CPAB's operating results for the year ended December 31, 2011. This section also includes the outlook for 2012 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 through effective regulation and by 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. It also undertakes other activities in support of its mandate, including: commenting on accounting and auditing standards most important to audit quality; participating in international activities related to enhancing audit quality and dealing with international audit firm networks; and conducting outreach to other Canadian participants in the audit process, such as Audit Committees.

As at December 31, 2011, 303 (2010–309) public accounting firms were registered with CPAB as participants in good standing. The 2 per cent decrease in the number of firms registered was due primarily to the withdrawal of participating audit firms that either had no Canadian reporting issuer clients or did not expect to have any in the future.

In 2011 CPAB inspected 88 firms, compared to 69 in 2010, an increase of 27.5 per cent (including follow-up inspections). In its overall inspection report, to each firm, CPAB provides three to five major recommendations which are focused on improving the quality of a firm's audit work.

As at December 31, 2011, 303 (2010–309) public accounting firms were registered with CPAB.

When CPAB finds that the number and nature of audit deficiencies is unsatisfactory and that the investing public could be at risk, disciplinary action is taken. Such action can escalate from a Requirement to a Restriction to a Sanction. Deadlines, which depend on the severity of the finding, are established. In all cases CPAB follows up to ensure that the recommendations have been implemented satisfactorily before disciplinary measures are lifted. Requirements, Restrictions or Sanctions take effect immediately unless the firm requests a review proceeding.

Following the 2011 Inspections, seven firms have Requirements (2010–five) placed on them and for one of these firms the Requirement was converted to a Restriction in 2012 because the firm did not comply with the Requirement. During 2011 CPAB did not place a Sanction on a participating firm (2010–nil) and there were no review proceedings or any other proceedings conducted in respect of CPAB's disciplinary decisions in 2011 or 2010. No investigations were carried out during the year and there were no appeals, applications for judicial review or arbitrations in respect of decisions made by a review panel.

CPAB continued to make significant investments in its inspection methodology, systems and processes, and people in 2011.

Additional information about CPAB's disciplinary powers is available in CPAB's Public Report of its 2011 inspections at www.cpab-ccrc.ca.

Operating Results

Revenues

CPAB derives its revenue from Canadian reporting issuers. Each year, CPAB invoices the firms registered with it a fee, which they may, in turn, bill to their reporting issuer clients. The fee is designed to cover CPAB's annual operating costs and to provide a reasonable reserve for contingencies. In 2011 CPAB's base fee rate was 2.0 per cent of the audit fees both Canadian and foreign participating firms charged their reporting issuer clients, with a minimum fee of $1,000. In 2011, 90 firms paid the minimum fee. The only exception to this rule is for firms in certain foreign jurisdictions that have audit regulatory oversight bodies in place. These reporting issuers are charged only 0.2 per cent of the firm's audit fees. These rates did not change from 2010.

CPAB had revenues of $15.9 million in 2011 compared to revenues of $16.4 million in 2010. The 3 per cent decrease was primarily due to a reduction in the audit fees firms charged to Canadian reporting issuers.

Operating Expenses

CPAB continued to make significant investments in its inspection methodology, systems and processes, and people in 2011 to effectively implement its strategic plan and address the challenges posed by an uncertain economic environment and the introduction of new international auditing and accounting standards.

Salaries and benefits for inspection and administrative staff continue to be CPAB's largest expense, totalling $11.0 million or 71.1 per cent of 2011 total expenses of $15.5 million (2010–$10.9 million or 72.0 per cent).

Excluding salaries and benefits, operating expenses increased approximately 5.7 per cent, to $4.47 million in 2011, from $4.23 million in 2010. This increase can be principally attributed to greater inspection activity during the year and costs associated with the Audit Quality Symposium CPAB hosted in December 2011. These increased costs were partly offset by a decrease in professional services and legal expenses.

Overall, operating expenses amounted to almost $15.5 million (2010–$15.1 million), increasing $0.36 million or 2.4 per cent over 2010. Of total operating expenses in 2011, 78 per cent related to inspection activity (2010–77 per cent).

The excess of revenue over expenses in 2011 was $0.44 million, compared to $1.32 million in 2010. CPAB currently has a reserve of $4.9 million, which represents four months of operating expenses. This complies with the guideline established by the Board.

During the year, CPAB made additional investments in its inspection methodology to enhance its risk assessment capabilities and better focus its inspection processes. CPAB's risk assessment approach helps it allocate its resources effectively, and the organization is well positioned to further enhance its risk assessment capabilities in 2012. Inspection activity in 2012 will include increased emphasis on foreign audit firms auditing reporting issuers in Canada, and on audits conducted by Canadian audit firms in foreign jurisdictions.

Cash Flows and Liquidity

Cash used in 2011 was $0.03 million (2010–$1.05 million). At December 31, 2011 CPAB had a strong working capital position of approximately $4.45 million (2010–$3.89 million).

CPAB investment policy requires excess cash, held from time to time, to be invested in accordance with sound investment management principles. At all times, investments will be made based on the requirements of safety, yield and appropriate liquidity. Investments may be made in Canadian Chartered Bank Term Notes and Certificates of Deposit.

Director and Executive Compensation

CPAB endeavours to offer Executive compensation that is comparable to organizations of similar mandate, size and complexity. Each year, CPAB evaluates the market by reviewing compensation surveys conducted by the Canadian Institute of Chartered Accountants and the Toronto Board of Trade. In addition, CPAB participates in and subscribes to the *"CA Professional Services Industry Compensation Survey"*. CPAB also monitors public comparative information provided by provincial securities regulators. Taken together, these practices ensure that compensation continues to be comparable and competitive.

Board Members' 2011 compensation included fees of $0.7 million (2010–$0.6 million) for governance responsibilities. Board members' fees included a $150,000 annual retainer for the Board Chair, $37,500 annual retainers for all other Board Members and an additional $4,000 for Committee Chairs. Meeting attendance fees were $1,500 per day for each Board and Committee meeting. The Board Chair does not receive meeting attendance fees.

The Board met five times in 2011. All Board Members attended every meeting, either in person or by phone. All Board Members attended the Board's strategic planning session in September.

CPAB will continue to build on its premium reputation for being purposeful, independent and fair.

Executive compensation in 2011, which included all amounts paid to the CEO, CFO and next three highest-paid members of the Management Committee, totalled $2.3 million (2010–$2.2 million), which includes salaries, accrued bonuses and Registered Retirement Savings Plan contributions by CPAB on behalf of staff.

Outlook for 2012

CPAB's goal in 2012 is to be viewed by key stakeholders as a world class audit regulator.

CPAB intends to be more outward-looking in 2012. Building on the progress made through its 2011 initiatives, CPAB will enhance its outreach to key stakeholders in 2012, including Audit Committees, investors and standard setters. CPAB will continue to provide information that is useful to these stakeholders in their contribution to audit quality, which will help lever CPAB's effectiveness. To succeed in this outreach, CPAB must further develop a number of key capabilities, the most significant of which are an effective communication strategy and competency in its implementation. This is essential to providing value-added information to key stakeholders, particularly Audit Committees and the investing community.

Led by a progressive and aligned leadership team, and enabled by a solid regulatory and inspection approach, CPAB is well placed to contribute to the evolution of higher-quality public company audits, and to have the respect and confidence of its stakeholder community as a world class audit regulator.

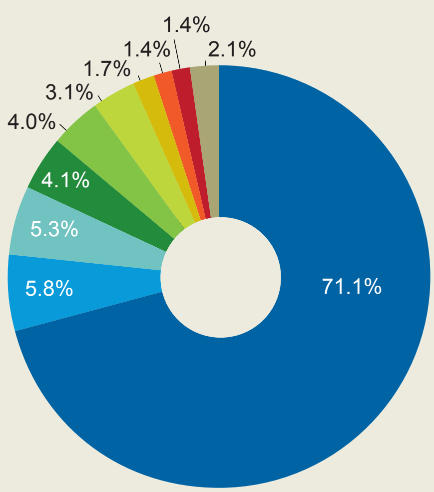
Committed to operational excellence and stakeholder value, CPAB will continue to build on its premium reputation for being purposeful, independent and fair.

From a human resources perspective, CPAB will make further investments in its organizational structure, policies and systems, technical training and professional development. These will be aligned with CPAB's core values, making it a career destination for top talent.

Powered by an evergreen technology platform, CPAB will enhance its management reporting and risk analysis capability.

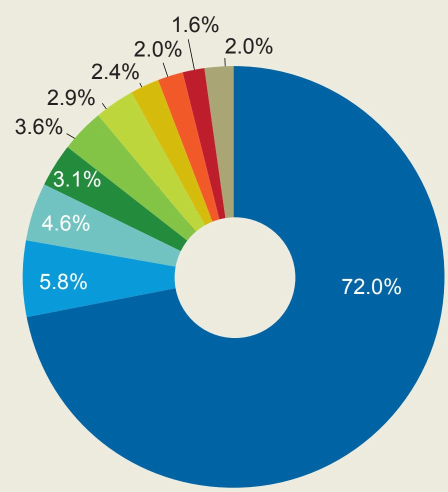
An upgraded performance framework, which tracks performance against key indicators, will be put in place across the organization. In addition, CPAB's reward system will continue to recognize staff for their contribution to the organization's success. This

MAJOR EXPENSES BY TYPE ($000'S)



2011

Salaries and Benefits	$10,990
Travel	$894
Directors' Fees and Expenses	$826
Continuing Education	$628
Administrative and General	$610
Occupancy Costs	$482
Professional Fees	$269
Legal Services	$220
Insurance	$219
Amortization	$321



2010

Salaries and Benefits	$10,871
Travel	$880
Directors' Fees and Expenses	$695
Continuing Education	$474
Administrative and General	$538
Occupancy Costs	$443
Professional Fees	$357
Legal Services	$294
Insurance	$244
Amortization	$305

environment of increased accountability will lead to a more effective organization.

For 2012, revenues are budgeted at $16.15 million (2011–$15.9 million) and operating expenses are budgeted at $16.25 million (2011–$15.46 million). In percentage terms, revenues are expected to increase by 1.6 per cent, while costs will increase by about 5.1 per cent, resulting in a small deficit for the year. The increase reflects the cost of additional outreach activities and one-time IFRS training requirements. Fees charged to reporting issuers will remain unchanged at 2 per cent of the audit fees charged by the audit firm (or 0.2 per cent for reporting issuers from certain foreign jurisdictions).

CPAB anticipates capital expenditures in 2012 of approximately $0.3 million, which will be necessary to replenish the organization's information technology 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 economic, human capital and technological forces that could have a material impact on CPAB's mission, vision, or critical success factors, as well as legislative risk.

Current economic uncertainties increase the possibility of risks associated with reporting issuer failures in corporate governance, financial reporting and audits. These could have a consequent risk of loss of confidence in CPAB. CPAB manages its risk through its risk analysis, which supports the allocation of resources and focus in its audit inspection program.

Human capital risks include an aging accounting workforce and a shortage of IFRS-experienced personnel. CPAB manages this risk by actively working to be an attractive career destination for high-quality staff. Legislative risks revolve around the impact of legislation that may not support CPAB in meeting its mandate. CPAB is continuing to pursue legislative change in a few jurisdictions to support its standing as an audit regulator.

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. CPAB manages this risk in various ways.

CPAB's guiding principle is zero tolerance for reputational risk, and the organization is constantly working to mitigate this risk.

CPAB's guiding principle is zero tolerance for reputational risk, and the organization is constantly working to mitigate this risk. In 2011, the organization further enhanced its risk assessment capabilities and continues to use a more robust risk analysis process to identify higher-risk audit firms and audit engagements. CPAB's inspection methodology must continue to become more strategic, providing greater risk assessment, and adding more relevance to participating firms.

CPAB Statement of Operations

(UNAUDITED)

Year Ended December 31 (000's),	*2011 Actual*	*2011 Budget*	*2012 Budget*
REVENUE			
Fees	$ 15,848	$ 15,890	$ 16,100
Interest income	52	30	50
	15,900	15,920	16,150
EXPENSES			
Salaries and benefits	10,990	10,730	11,034
Travel	894	935	845
Directors' fees and expenses	826	874	931
Continuing education and professional memberships	482	532	605
Administrative and general	447	462	556
Occupancy costs	482	497	503
Professional services	269	344	329
Legal services	220	250	200
Insurance	219	233	220
Stakeholder communications	309	239	637
Amortization of property and equipment	321	373	390
	15,459	15,469	16,250
Excess (Deficiency) of Revenue Over Expenses for the Year	**$ 441**	**$ 451**	**$ (100)**

Note: Certain 2011 expenses in this statement have been reclassified from the audited financial statements to align with the presentation in the 2012 Budget.

Commentary on the 2012 CPAB Operating Budget

The 2012 Operating Budget (the "2012 Budget") shows CPAB continuing to fulfill its mandate effectively during challenging times, while looking more outward as an organization.

For 2012, revenues, which cover operating expenses, are budgeted at $16.2 million, as compared to actual and budgeted revenues of $15.9 million in 2011. This revenue primarily comes from Canadian reporting issuers. CPAB invoices audit firms a fee (based upon 2 per cent of the audit fees charged to Canadian reporting issuers), which the firms generally pass on to their reporting issuer clients. CPAB's fee will remain unchanged.

CPAB's operating expenses for 2012 have been budgeted at $16.3 million. This represents an increase of 5 per cent from total actual and budgeted operating expenses of $15.5 million in 2011. The largest increases in the 2012 Budget relate to increased costs for communications with key stakeholders regarding audit quality and preparing our inspection staff for the challenges arising from the adoption of International Financial Reporting Standards.

In 2010, CPAB established a new management structure with clear roles and responsibilities for staff at various levels and developed core values for the organization (Excellence, Trust, and Respect). Since that time, management's focus has moved from recruiting to developing and retaining staff and on accountability and consistency of application of policies/methodology.

CPAB needs to be more outward-looking in 2012. Building on the work done through the branding initiative in 2011, CPAB will continue to reach out to key stakeholders this year. In this regard, a number of key capabilities will need to be developed, including an effective communication strategy and competency. These capabilities are needed so CPAB can provide value-added information to its key stakeholders, particularly, Audit Committees and the investing community.

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

Statement of Management's Responsibility

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 accounting standards for not-for-profit organizations, applying best estimates and judgments based on currently available information. These are CPAB's first financial statements prepared in accordance with these new standards, which have been applied retrospectively. No restatement of previously reported amounts was required since the adoption of the new accounting framework had no impact on the previously reported assets, liabilities and net assets of CPAB. The presentation and disclosures in the financial statements this year include the presentation of the opening amounts as of the date of the transition, being January 1, 2010, and all disclosures required under the new accounting framework. The significant accounting policies are described in Note 3 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 auditors' 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

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 statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010, and the statements of changes in net assets, operations and cash flows for years ended December 31, 2011 and December 31, 2010, 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 accounting standards for not-for-profit organizations, 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 audits. We conducted our audits in accordance with Canadian Generally Accepted 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 in our audits 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, the financial position of the Canadian Public Accountability Board/Conseil canadien sur la reddition de comptes as at December 31, 2011, December 31, 2010 and January 1, 2010 and its financial performance and its cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with Canadian accounting standards for not-for-profit organizations.

Cowperthwaite Mehta

CHARTERED ACCOUNTANTS
LICENSED PUBLIC ACCOUNTANTS

FEBRUARY 14, 2012
TORONTO, ONTARIO

Statement of Financial Position

	December 31, 2011	December 31, 2010	January 1, 2010 (note 2)
ASSETS			
Current assets			
Cash and cash equivalents	$ 343,349	$ 372,974	$ 1,426,418
Short-term investments (note 5)	5,400,000	4,700,000	3,000,000
Accounts receivable (note 5)	50,914	19,838	19,270
Sales tax recoverable	87,230	58,539	58,538
Prepaid expenses	161,867	116,467	106,172
	6,043,360	5,267,818	4,610,398
Property and equipment (note 6)	722,550	920,154	906,702
	$ 6,765,910	**$ 6,187,972**	**$ 5,517,100**
LIABILITIES			
Current liabilities			
Accounts payable and accrued liabilities	$ 1,589,705	$ 1,378,704	$ 1,954,762
Unamortized tenant inducements	190,809	264,651	338,492
NET ASSETS			
Invested in property and equipment	722,550	920,154	906,702
Unrestricted	4,262,846	3,624,463	2,317,144
	4,985,396	4,544,617	3,223,846
	$ 6,765,910	**$ 6,187,972**	**$ 5,517,100**

APPROVED ON BEHALF OF THE BOARD:

, DIRECTOR

Nicholas Le Pan, *CHAIR*

, DIRECTOR

Kenneth Crump

Statement of Changes in Net Assets

	Invested in property and equipment	*Unrestricted*	*Total*
Net assets as at January 1, 2010	**$ 906,702**	**$ 2,317,144**	**$ 3,223,846**
Excess of revenue over expenses for the year	–	1,320,771	1,320,771
Purchase of property and equipment	318,180	(318,180)	–
Amortization of property and equipment	(304,728)	304,728	–
Net Assets as at December 31, 2010	**$ 920,154**	**$ 3,624,463**	**$ 4,544,617**
Excess of revenue over expenses for the year	–	440,779	440,779
Purchase of property and equipment	123,673	(123,673)	–
Amortization of property and equipment	(321,277)	321,277	–
Net Assets as at December 31, 2011	**$ 722,550**	**$ 4,262,846**	**$ 4,985,396**

Statement of Operations

Year Ended December 31,	*2011*	*2010*
REVENUE		
Fees	$ 15,847,820	$ 16,409,711
Interest income	52,543	12,091
	$ 15,900,363	**$ 16,421,802**
EXPENSES		
Salaries and benefits	10,989,600	10,870,828
Travel	893,940	879,868
Directors' fees and expenses	825,563	694,632
Continuing education and professional memberships	628,264	474,074
Administrative and general	610,108	538,237
Occupancy costs	482,479	443,006
Professional services	268,870	357,267
Legal services	220,384	293,945
Insurance	219,099	244,446
Amortization of property and equipment	321,277	304,728
	15,459,584	15,101,031
Excess of Revenue Over Expenses for the Year	**$ 440,779**	**$ 1,320,771**

Statement of Cash Flows

Year Ended December 31,	*2011*	*2010*
OPERATING ACTIVITIES		
Excess of revenue over expenses for the year	$ 440,779	$ 1,320,771
Add back (deduct) non-cash items:		
Amortization of property and equipment	321,277	304,728
Amortization of tenant inducements	(73,842)	(73,841)
Net change in non-cash working capital items (note 8)	105,834	(586,922)
Cash generated from operations	794,048	964,736
INVESTING ACTIVITIES		
Purchase of short-term investments	(10,500,000)	(12,300,000)
Redemption of short-term investments	9,800,000	10,600,000
Purchase of property and equipment	(123,673)	(318,180)
Cash used in investing activities	(823,673)	(2,018,180)
Cash and cash equivalents used in the year	(29,625)	(1,053,444)
Cash and cash equivalents, beginning of year	372,974	1,426,418
Cash and Cash Equivalents, End of Year	**$ 343,349**	**$ 372,974**

Notes to the Financial Statements

DECEMBER 31, 2011 AND DECEMBER 31, 2010

1. The Organization

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

The mission of CPAB 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. 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. Adoption of Accounting Standards for Not-For-Profit Organizations

Effective January 1, 2011, the organization elected to adopt the Canadian accounting standards for not-for-profit organizations. These are the first financial statements prepared in accordance with this new framework which have been applied retrospectively.

Management reviewed the exemptions provided on transition to the Canadian accounting standards for not-for-profit organizations and has elected to designate all investments to be subsequently measured at fair value, which is consistent with the accounting policy in place at the time of the transition. The adoption of Canadian accounting standards for not-for-profit organizations had no impact on the previously reported assets, liabilities and net assets of the organization, and accordingly, there has been no restatement of previously reported amounts as at the date of the transition, being January 1, 2010. The presentation and disclosures in the financial statements reflect the requirements under the new accounting framework.

3. Significant Accounting Policies

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 currently 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 2011 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:

Office equipment and furniture	*3 – 10 years*
IT Infrastructure and networks	*4 – 5 years*
Computer software	*3 years*
Computing equipment	*2 years*
Leasehold improvements	*Over the life of the lease*

Investments

Investments, 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 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.

4. Financial Instruments and Risks

CPAB's financial assets include cash and fixed income guaranteed investment certificates (GICs) with a major Canadian chartered bank. The cost of the GICs, plus accrued interest income, approximates the fair value of these instruments. 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.

5. Short-Term Investments

Short-term investments consist of fixed income GICs with maturities exceeding 90 days from the date of purchase and consist of:	*2011*	*2010*
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 – 1.00%, matures March 9, 2012	1,000,000	–
GIC – 1.00%, matures May 14, 2012	1,000,000	–
GIC – 1.00%, matures August 8, 2012	1,000,000	–
GIC – 1.00%, matures November 8, 2012	2,400,000	–
	5,400,000	4,700,000
Accrued interest	20,211	9,448
	$ 5,420,211	**$ 4,709,448**

Accrued interest income is included in accounts receivable.

6. Property and Equipment

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

	Cost	Accumulated Amortization	2011 Net	2010 Net
Office equipment and furniture	$ 570,647	$ (398,223)	$ 172,424	$ 224,536
IT Infrastructure and networks	1,136,590	(786,424)	350,166	430,188
Computer software	133,488	(120,634)	12,854	10,819
Computing equipment	135,434	(115,908)	19,526	22,161
	$ 1,976,159	**$ (1,421,189)**	554,970	687,704
Leasehold improvements, net			167,580	232,450
			$ 722,550	**$ 920,154**

7. 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, 2011 and 2010 the amount owing under the Credit Facility was $nil.

8. Change in Non-Cash Working Capital Items

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

	2011	2010
Accounts receivable	$ (31,076)	$ (568)
Sales tax recoverable	(28,691)	(1)
Prepaid expenses	(45,400)	(10,295)
Accounts payable and accrued liabilities	211,001	(576,058)
	$ 105,834	**$ (586,922)**

9. Commitments

CPAB entered into a 10 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 $180,000 for the remaining term of the lease. Currently, CPAB's share of the building's operating costs is an estimated $272,000 per annum.

In 2010, CPAB entered into leases for office space in Vancouver and Montréal, which expire March 31, 2013 and October 31, 2013, respectively. The annual rent for these leases is approximately $105,000.

Corporate Information

CPAB Executive Team

Brian A. Hunt
CHIEF EXECUTIVE OFFICER

MR. HUNT WAS INVOLVED WITH CPAB'S CREATION AND HAS 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 SPENT THREE YEARS AS SENIOR VICE PRESIDENT, FINANCE WITH A MAJOR CANADIAN BANK. PRIOR TO THAT, HE SPENT 10 YEARS AS A PARTNER AND AS THE DIRECTOR OF ACCOUNTING STANDARDS IN CANADA FOR AN INTERNATIONAL ACCOUNTING FIRM.

Glenn Fagan
VICE PRESIDENT

BEFORE JOINING CPAB IN 2010, MR. FAGAN SPENT ALMOST 12 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.

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.

Directors

Nick Le Pan
BOARD CHAIR

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

Ian Bourne[2]
CHAIR, BALLARD POWER INC.; DIRECTOR, SNC-LAVALIN GROUP, CANADA PENSION PLAN INVESTMENT BOARD, WAJAX CORPORATION AND CANADIAN OIL SANDS LIMITED; RETIRED CFO, TRANSALTA CORPORATION, CALGARY, ALBERTA.

Ken Crump[1]
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[1]
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[1]
CEO, PROMONTORY FINANCIAL GROUP CANADA; FORMER DEPUTY GOVERNOR OF THE BANK OF CANADA, TORONTO, ONTARIO.

Gary Porter[2]
FORMER DIRECTOR AND CHAIR, INVESTMENT COMMITTEE OF THE ONTARIO TEACHERS' PENSION FUND; RETIRED CO-FOUNDER OF PORTER HÉTU INTERNATIONAL, PRESCOTT, ONTARIO.

Jocelyn Proteau[2]
CHAIR, BOARD OF BTB REAL ESTATE INVESTMENT TRUST; DIRECTOR, RICHELIEU HARDWARE INC., CO2 SOLUTIONS INC., FAMILIPRIX INC.; VICE CHAIR AND LEAD DIRECTOR, 20/20 TECHNOLOGIES INC.; FORMER CHAIR, STANDARD LIFE OF CANADA, MONTRÉAL, QUÉBEC.

Alain Rhéaume[2]
A FOUNDER AND MANAGING PARTNER, TRIO CAPITAL INC.; FORMER DEPUTY MINISTER OF FINANCE, QUÉBEC; FORMER PRESIDENT AND COO, MICROCELL TELECOMMUNICATIONS, MONTRÉAL, QUÉBEC.

Peter W. Roberts[1]
FORMER CHAIR, RISK OVERSIGHT AND GOVERNANCE BOARD, CANADIAN INSTITUTE OF CHARTERED ACCOUNTANTS; FORMER CFO, SIERRA WIRELESS INC.; PAST PRESIDENT OF THE INSTITUTE OF CHARTERED ACCOUNTANTS OF BRITISH COLUMBIA, WEST VANCOUVER, BRITISH COLUMBIA.

Benita M. Warmbold[2]
SENIOR VICE PRESIDENT AND COO, CANADA PENSION PLAN INVESTMENT BOARD; DIRECTOR, CANADA DEVELOPMENT INVESTMENT CORPORATION, QUEEN'S SCHOOL OF BUSINESS ADVISORY BOARD, TORONTO FINANCIAL SERVICES ALLIANCE AND ALZHEIMER'S SOCIETY, TORONTO, ONTARIO.

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BENITA W. WARMBOLD WAS APPOINTED AS A BOARD MEMBER ON JULY 4, 2011.

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

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