



University of Toronto

BUSINESS AFFAIRS

TO: Audit Committee

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AGENDA ITEM: 5

ITEM IDENTIFICATION:

Policy on Use of the External Auditor for Non-Audit Services

JURISDICTIONAL INFORMATION:

The Governing Council approves the appointment of the external auditor on the recommendation of the Business Board and Audit Committee.

PREVIOUS ACTION TAKEN:

Governing Council approved the appointment of Ernst & Young as the external auditor for the fiscal year ended April 30, 2006 at its meeting of June 29, 2005.

The Audit Committee reviewed the external auditor's engagement letter and plan, including a report on non-audit services provided by the external auditor, at its meeting of November 23, 2005.

The Audit Committee receives an annual report from the external auditor regarding non-audit services provided by the external auditor.

HIGHLIGHTS:

In the United States, the Sarbanes-Oxley Act of 2002, which applies to Securities and Exchange Commission registrants, prohibits public accounting firms from performing certain non-audit services to financial statement audit clients.

Sarbanes-Oxley is not applicable to U.S. universities. However, on November 20, 2003, the National Association of College and University Business Officers (NACUBO), published an advisory report in which it provided emerging best practice guidance for higher education institutions. (There is no similar guidance for Canadian universities.)

The NACUBO report of November 20, 2003 noted the following Sarbanes-Oxley prohibitions (Title II, 201):

- 1) Bookkeeping or other services related to the accounting records or financial statements;
- 2) Financial system design and implementation;
- 3) Appraisal or valuation services, fairness opinions or contribution-in-kind reports;
- 4) Actuarial services;
- 5) Internal auditing outsourcing services;
- 6) Management or human resource functions;
- 7) Broker or dealer, investment advisor, or investment banking services;
- 8) Legal services and expert services unrelated to the audit;
- 9) Any other service the Accounting Oversight Board determines, by regulation, is impermissible.

The NACUBO report further noted that Sarbanes-Oxley specifies that “a registered public accounting firm may engage in any other service, including tax services for an audit client, but only if the Audit Committee approves the activity in advance.”

NACUBO’s advice for U.S. universities was as follows:

“It [NACUBO] believes that institutions of higher education should look at the Sarbanes-Oxley Act as a framework to help evaluate overall financial risks and not simply comply with accountability concepts that stem from structures and circumstances that differ fundamentally from the stewardship responsibilities and public obligations they face.”

In the area of non-audit services, NACUBO recommended that “institutions should prohibit their independent auditors from providing the non-audit services prohibited by the Act unless extenuating circumstances exist and the audit committee approves the work in advance”.

In Canada recent legislation for publicly listed companies (Multilateral Instrument 52-110 for Ontario Securities registrants) requires that the Audit Committee pre-approve all non-audit services provided by the external auditors of the organization.

At this time, this is not a requirement for organizations that are not OSC registrants. While the University of Toronto Asset Management Corporation is registered with the OSC, this registration does not apply to the University of Toronto as a whole.

In Canada, the CICA requires that external audit firms comply with the new Canadian Independence Standard which provides additional comfort beyond that contemplated by NACUBO when it prepared its guidance. The Guide to the New Canadian Independence Standard includes the following prohibitions with respect to non-audit services with respect to audits of public companies only:

- “5. Members and firms may not provide:
- bookkeeping and accounting services;
 - financial information systems design and implementation;
 - actuarial services;

- valuation services;
- internal audit services;

unless it is reasonable to conclude that the results of the services will not be subject to audit procedures.

6. Members and firms may not provide the following services, even if not subject to audit:
- expert services including litigation support;
 - legal services;
 - management functions;
 - human resources services;
 - corporate financial services.”

While this section of the standard applies to publicly traded companies, it is very similar to Sarbanes-Oxley, with which NACUBO has concurred as best practice for U.S. universities, as noted above. It provides the best practices standard that the accounting profession requires our external auditor to use in determining whether they can accept individual assignments for their public clients. While these standards for public companies are more restrictive than for non-public companies, the external auditor may choose to apply some or all of the more restrictive standards to their non-public clients. We intend to use the more restrictive public sector Canadian standards to formulate our policy. The full Guide to the New Canadian Independence Standard is attached as Appendix B for the information of Audit Committee members.

The policy, attached as Appendix A, delegates to the Chair of the Audit Committee the authority for the approval of non-audit services. The chair would have the authority to a) approve the service, b) consult with the Audit Committee before approving the service, or c) refer the service to the Audit Committee to recommend to the Business Board and Governing Council for approval.

The policy also delegates to the Chief Financial Officer the authority to engage the external auditor for specific categories of pre-approved non-audit services – tax consultation, participation in the risk assessment process, professional services regarding advice on accounting for individual transactions and professional services regarding advice on financial statement disclosures.

The Audit Committee will continue to receive an annual report from the external auditor on the non-audit services.

FINANCIAL AND/OR PLANNING IMPLICATIONS:

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RECOMMENDATION TO BUSINESS BOARD:

That the policy on the use of the external auditor for non-audit matters attached as Appendix A be approved.