



University of Toronto

OFFICE OF THE GOVERNING COUNCIL

Appendix "A" to Report Number
150 of the Business Board (May
29, 2006)

TO: Audit Committee

SPONSOR: Louis R. Charpentier
Secretary of the Governing Council

CONTACT INFO: 416-978-2118 – l.charpentier@utoronto.ca

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AGENDA ITEM: 7

ITEM IDENTIFICATION:

Audit Committee Terms of Reference: Amendment

JURISDICTIONAL INFORMATION:

The Audit Committee may make recommendations to the Business Board for amendments to its terms of reference. Amendments must ultimately be approved by the Governing Council.

PREVIOUS ACTION TAKEN:

The terms of reference were reviewed by a working group consisting of: Mr. Louis Charpentier (convener), Mr. Mark Britt, Ms Sheila Brown, Ms Paulette Kennedy, Mr. Richard Nunn, Ms Catherine Riggall and Ms Martha Tory. The working group held one meeting and a smaller group then drafted the attached proposal.

As a basis for its work, the working group reviewed a summary, prepared by Mark Britt, of recommendations concerning audit committee charters for not-for-profit organizations. The recommendations were those of the American Institute of Certified Public Accountants, KPMG Canada LLP, and the Institute of Internal Auditors Research Foundation.

HIGHLIGHTS:

Proposed changes are as follows.

1.1 Composition. Pursuant to current thinking, it is specified that membership of the Audit Committee be independent (i.e. not University faculty, staff or students) and be members of the Governing Council or the Business Board. There are two exceptions.

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First, the Business Board may appoint a senior member of the teaching staff of the University with expertise in accounting (tenure is deemed to confer independence). Second, where an insufficient number of members as specified above are available to serve, other independent members with financial expertise may be co-opted.

1.2 Term. Unchanged.

1.3 Chair and Vice-Chair. Unchanged.

2. Quorum. Redefined as one half of the voting membership other than *ex officio* members.

3. Subcommittees. Unchanged.

4. Function. Unchanged.

5. Areas of Responsibility.

Ordering. The Committee's specific responsibilities are grouped into the following categories: financial reporting, external auditors, internal auditor, financial controls and control environment, risk management, and other.

5.1.1. Financial Reporting

(a) Review of the University's audited financial statements. It is proposed to specify certain duties in connection with the review of the statements. The Committee reviews the signed statement of administrative responsibility. As part of its review, the Committee reviews relevant written communications from the external auditors, including any schedule of unadjusted differences.

(b) Review of accounting policies and practices. Again, it is proposed to specify certain duties in connection with the periodic review of accounting policies. The Committee is called on to assess the quality as well as the acceptability of the University's accounting. It is to be advised of all alternative treatments considered and judgements made in the presentation of financial information.

(c) Review of report on legal actions. To satisfy itself with respect to the note on contingent liabilities and to assist it in monitoring risk exposures, the Committee would continue to review an annual report on legal actions. It would no longer review a report on the use of legal services. That report is primarily a summary of the use of legal services and the legal fees paid to various firms, and it is not relevant to those duties.

(d) Review of an annual financial report on the pension plans. The contents of the annual report are no longer specified. The Committee is called upon to review management's assessment of the financial soundness of the pension plans.

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(e) Review of an annual report on the endowment. The terms of reference would reflect the Committee's practice in reviewing an annual report on the endowment. The Committee is called upon to review management's assessment of the financial soundness of the endowment funds.

(f) Review of an annual report on borrowing. The terms of reference would reflect the Committee's practice in reviewing this report. The Committee is called upon to review management's assessment of the financial soundness of the University's borrowing.

(g) Review of an annual report on the insurance program. The terms of reference would reflect the Committee's practice in reviewing this report. The Committee is called upon to review management's assessment of the financial soundness of the University's insurance protection.

(h) Other financial reports. This is a combination and simplification of items (c) and (o) of the current terms of reference.

5.1.2. External Auditors

(a) Recommendation of the appointment of the external auditors. Largely unchanged, but the Committee is specifically called upon to review with management the performance of the external auditors, to ensure appropriate partner rotation, and to consider the need for audit firm rotation.

(b) External auditors' engagement, plan and fees. Largely unchanged, but the Committee is specifically called upon to consider the co-ordination of the work of the external and internal auditors.

(c) Non-audit services. Specific reference is made to the new Policy on Non-Audit Services. Reference is removed for a Committee duty to "consider whether the nature or extent of such [non-audit] services could detract from the audit firm's independence in carrying out the audit function." That is taken care of in the Policy.

(d) *In camera* meeting with the external auditors before voting on the financial statements. No substantive change.

(e) Review of management letter, including *in camera* meeting with the external auditors. It is specified that the Committee is to review the management letter addressed to it. The Committee is, therefore, not called upon to review the management letter addressed to management, containing detailed recommendations not thought by the external auditors to require the Committee's attention.

(f) Reports to the Committee on differences of opinion between management and the external auditors. Unchanged.

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(g) Reports on seeking alternative accounting advice. The section on “opinion shopping” is unchanged.

5.1.3. Internal Auditor

(a) Review of the internal audit policy. No substantive change.

(b) Review of the internal audit plan. The section refers to the review of annual audit plans. Consistent with current practice, reference to the review of a long-term plan is omitted. Adds a provision for review of the department’s structure and the qualifications of its staff.

(c) Review of internal audit reports. Specifies that the Committee reviews interim and annual reports. The previous terms of reference spoke of reviewing reports, which might have been understood to suggest a review of each audit report. Specifies that reports deal with controls over, and security of, electronic information systems.

(d) *In camera* meetings with the internal auditor. Provision specified here rather than in the “procedures” section.

(e) Review of internal audit services. New, but reflects established practice.

(f) Review of circumstances of any dismissal or resignation of the Director of Internal Audit. Unchanged.

5.1.4. Financial Controls and Control Environment

(a) Review of management reports on controls and assessment of the control environment. On the basis of reports from the auditors, assesses the effectiveness of controls. New. Reflects current practice, wherein the Committee has received reports over the years on such matters as controls over capital projects and investments, and regularly evaluates the controls on the basis of the reports of the internal auditor.

(b) Reports on financial problems. Unchanged.

(c) Review of program of accountability reports. New in the terms of reference. Reflects long-established practice.

(d) Review of “whistle blower” procedure and its operation. New.

(e) Reports on financial audits carried out by granting councils, regulatory agencies, etc. Unchanged.

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5.1.5. Risk Management.

Largely unchanged. The Committee is, under the current terms of reference, called upon to focus on “the adequacy of key controls over those vital risks considered to be . . . more significant and likely to occur.” It is proposed to amend that section to call for focus on “the adequacy of key controls over, and mitigations of,”

5.1.6. Other

(a) Monitors other financial matters. It is proposed to ask the Business Board to rescind its 1996 direction to the Audit Committee to carry out the board’s stewardship responsibility with respect to the incorporation business ancillary operations. One of those operations, the Innovations Foundation, has ceased to be an incorporated ancillary. Instead, its functions are being carried out within the Office of the Vice-President, Research and Associate Provost. In the case of the University of Toronto Asset Management Corporation, the Business Board itself monitors investment performance, and the Audit Committee reviews only UTAM’s financial statements. Because UTAM’s revenue and expense amount to only \$3.7-million, a separate review of its very simple financial statements seems superfluous. The Committee would continue, as part of its review of the University’s financial statements, to review assurances concerning the presence and valuation of the invested assets. The Committee would also continue, as part of its review of controls, to receive periodic reports (perhaps every five years) on UTAM’s controls. That would leave only the University of Toronto Press, and it is recommended that the Press make its annual report directly to the Business Board. Because the annual report and financial statements are approved by the Press’s Board, the Business Board would receive the report only for information. If it were to have concerns about the Press, it would presumably transmit those to the President and the Executive Committee of Governing Council, implying the need for a new Board of Directors.

(b) Provision for regular review of the terms of reference. New.

5.2. Responsibility of Administration. Unchanged.

6. Procedures. The provision for *in camera* meetings with the external and internal auditors is included in “areas of responsibility” and therefore deleted in this section. The section is otherwise unchanged.

Since the Committee’s previous review of the proposal, section 6.2 on Access has been strengthened to provide the external and internal auditors unambiguously with access to the Chair of the Committee on all “matters within the scope of their duties” rather than only “serious” matters “that cannot be resolved through normal administrative reporting lines.”

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FINANCIAL AND/OR PLANNING IMPLICATIONS:

No direct financial implications.

RECOMMENDATION:

That the Audit Committee recommend to the Business Board:

- (a) THAT the proposed revised terms of reference of the Audit Committee be approved; and
- (b) THAT the Business Board rescind its instruction, made on October 15, 1996, that the Audit Committee carry out the Board's stewardship responsibility with respect to the incorporated business ancillary operations, and that the Board itself receive for information the annual reports and audited financial statements of those operations.