

UNIVERSITY OF TORONTO
THE GOVERNING COUNCIL
REPORT NUMBER 93 OF THE AUDIT COMMITTEE

May 12, 2010

To the Business Board,
University of Toronto.

Your Committee reports that it met on Wednesday, May 12, 2010 at 4:00 p.m. in the Board Room, Simcoe Hall, with the following members present:

Mr. W. John Switzer (In the Chair for
items 1 - 3)
Ms Paulette L. Kennedy (In the Chair
thereafter)
Professor Ramy Elitzur
Mr. J. Mark Gardhouse
Ms Shirley Hoy
Mr. Joseph Mapa

Ms Catherine J. Riggall,
Vice-President, Business Affairs
Mr. Mark L. Britt, Director,
Internal Audit Department
Ms Sheila Brown, Chief Financial Officer
Mr. Louis R. Charpentier, Secretary
of the Governing Council

Mr. Neil Dobbs, Secretary

Regrets:

Mr. George E. Myhal

In Attendance:

Mr. Pierre G. Piché, Controller and Director of Financial Services
Ms Martha J. Tory, Ernst & Young

The meeting was called to order by the Secretary of the Governing Council, who advised that the Chair would be unable to attend and the Vice-Chair had another commitment that would prevent her arrival until later in the meeting. With the agreement of the Committee, Mr. Switzer assumed the Chair *pro tem*.

Members were referred to the revised agenda for the meeting, which had been placed on the table. The same items appeared in an amended order.

ALL ITEMS ARE REPORTED TO THE BUSINESS BOARD FOR INFORMATION.

1. Report of the Previous Meeting

Report Number 92 (December 8, 2009) was approved.

REPORT NUMBER 93 OF THE AUDIT COMMITTEE – May 12, 2010**2. Internal Audit: Annual Report, 2009-10**

Mr. Britt presented the Annual Report of the Internal Audit Department for 2009-10. He reported that the Department had delivered 108% of the hours included in the revised audit plan. The revisions had been required to enable special reviews: two in response to management requests and eight others arising from allegations of misappropriation. (Mr. Britt had reported on the special reviews at the December meeting.) The time required for the special reviews had resulted in a reduction of the time for departmental audits and continuous auditing. Mr. Britt was pleased to report that the Department had been at its full staffing level for much of the year, with functions being carried out by a committed and satisfied staff.

Mr. Britt summarized the substantive matters in his report.

- **Departmental audits.** The Internal Audit Department had worked with the risk categories used in the University's risk-assessment profile from 2009. The outcome of the audit reviews were summarized in Appendix "A" to the report. In its reviews, the Department had studied the effectiveness of the internal controls and other steps taken to mitigate the particular risks. The findings or issues that had emerged were listed in the column headed "risk indicators." Those factors led to a conclusion concerning the level of residual risk arising from the review. There were five areas where the risk level was highest in the units reviewed: financial risk, information systems / information technology risk, environmental and individual health and safety risk, legal risk and research risk. Mr. Britt concluded that those were likely also the areas of highest risk in divisions and departments across the University. In the particular units where risks had been identified, the Internal Audit Department worked with management to promote remediation and mitigation of the risk. Management was asked to prepare an action plan to deal with the concerns identified, and their compliance with the plan was monitored by a follow-up review conducted nine to twelve months later. The Internal Audit Department prepared reports on the outcome of those reviews.
- **Continuous auditing.** Given limitations of resources, the Internal Audit Department was limited in the number of departmental audits it could conduct. The continuous audit, an examination of specific types of transactions University-wide, provided a very effective means to obtain broad audit coverage. The Department reviewed a monthly sample of transactions of particular types processed by the University's information systems. The outcome was reported in Appendix "B" to Mr. Britt's report. For the most recent continuous audit, a sample of 207 transactions had been reviewed. Of those transactions, exceptions to appropriate completion of procedures had been noted in 89 cases or 43% of the sample. Those exceptions included one or more indicators of non-compliance with University or external (usually research-sponsor) procedures. Mr. Britt stressed that the transactions reviewed had not been selected randomly. Nor had they been selected to provide a representative sample. Rather, they had been selected in areas where, in the Department's judgement, there was a higher risk of non-compliance. Therefore, it would not be appropriate to extrapolate from the outcome the level of non-compliance with procedures across the University. In addition, Mr. Britt stressed that 65 of the exceptions

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were of a minor or “housekeeping” nature – such things as incorrect account or tax coding or untimely action. However, the continuous audit process did provide a good indicator of the level of strict compliance with procedures and guidelines and did help to identify types of transactions with higher levels of non-compliance.

- **Information-system audits.** Working with the new Chief Information Officer and his team, the Internal Audit Department had made real inroads in the area of mitigating information-system risk. The Department had completed a number of reviews and had provided consulting advice on a number of matters. The Department had provided advice concerning the next-generation student information system, information security concerning credit card payments, application security in the Convocation Office, desk-top encryption, and disaster / business recovery planning. Activity in many of those areas would continue into 2010-11, and hours had been set aside in the Department’s plan to provide for that work.
- **Follow-up reviews.** At the previous meeting, the members had urged that the Internal Audit Department make a special effort to complete follow-up reviews when original reviews had led to the conclusion that the departments compliance to appropriate procedures needed improvement. Pursuant to that urging, the Department had completed follow-up reviews of the procedures for tendering and administration of capital projects and for the operations of the Office of Environmental Health and Safety. Most internal audit recommendations were being implemented in the two departments, but in both cases one recommendation either (a) required additional work, or (b) was rejected, with the department deciding to accept the risks identified.
- **Administrative accountability reporting.** Employees with financial management responsibility were required to complete an annual report, signing off that their activities had been in compliance with University policies and procedures and that they had completed certain required functions. For 2009-10, accountability reports had been required from 44 employees in the units reviewed, and they had been submitted in all cases but one. In that case, the individual was not aware that report was required for his position. Mr. Britt noted that because of the audit program for 2009-10, the sample size had been small. Audit reviews had been concentrated in central administrative divisions rather than in academic divisions. In the latter, accountability reports were often more numerous, being required of Principal Investigators – faculty members who were responsible for grant-funded research programs.
- **Special reviews.** As noted, the Internal Audit Department had been engaged in ten special reviews over the year: two requested by management and eight arising from allegations of financial mismanagement or misappropriation. In response to a question, Mr. Britt said that none of the special reviews involved large amounts of money. The largest amount involved was \$50,000, and the matter was resolved and the full amount recovered. Of the ten special reviews, two were still in progress. Of the eight that were completed, five had resulted in the termination of the employment of the staff member concerned.

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Among the matters that arose in questions and discussion were the following.

(a) Risk assessment. A member asked how the Department distinguished between matters it would regard as major ones and those it would regard as minor. Mr. Britt said that at the initiation of each audit, the Department performed a risk assessment to determine the components of the unit's operations that were critical to it. For example, in an academic department that relied a great deal on external research funding, a substantial level of non-compliance with the requirements of one of the three research granting councils or with the requirements of the Canada Foundation for Innovation would represent a moderate to high risk. The assessment would also depend on the actions taken to mitigate that risk. Was there an appropriate level of segregation of duties between the principal investigators in the department and the departmental administrator? What was the level of knowledge of the departmental administrator of the granting council and C.F.I. requirements? A second example: in departments that handled cash, was the revenue stream a large one? If so, were there proper cash-handling procedures in place? Was there an appropriate segregation of duties and a proper reconciliation of cash balances with cash-register tapes or receipts? Again, if the amount was large, the risk would be regarded as moderate to high, particularly if measures to mitigate the risk were not firmly established.

(b) Improvements in the Department. A member asked how the operations of the Department had improved over the past year. Mr. Britt replied that he believed the improvement to have been significant. First, the Department had initiated use of the "Teammate" proprietary software to manage its workflow. It permitted better management of the audit process and a more seamless transition from field-work to review to report, permitting more timely review and assessment of audit results. Second, the Department had aligned its audit planning with the University's risk-assessment profile, ensuring focus on appropriate areas. Third, it had made inroads with the leaders of academic and administrative divisions, who felt greater comfort in calling on the Department for assistance or to report concerns. Finally, reporting had become more streamlined and user-friendly.

(c) Sampling techniques for audit testing. In response to a question, Mr. Britt said that the Department continued to rely on a judgmental sampling technique. It was working on moving to a monetary-unit sampling technique (as reported at the previous meeting), but was facing some challenges in doing so. Those challenges had to do with the lack of homogeneity of the departments being audited. The attributes to be tested differed in the various units. The results produced using trials with the monetary-unit technique had not appeared sufficient to enable extrapolation of the outcome to the entire population of units within the University. The Department continued to work with a statistical consultant on the matter. In the meanwhile, it used its backup judgmental technique, employing data-mining software to identify transactions for testing. The software performed tests according to fifteen rules or criteria. For example, it sought out transactions to obtain goods or services valued at over \$5,000 that were not backed by a purchase order. It sought out transactions that had the characteristics of a split transaction – seeking to overcome requirements for large purchases by splitting the purchase into two or more parts. The primary deficiency of the judgmental method was that it did not permit extrapolation from the results of individual reviews to the University as a whole.

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(d) External auditors' reliance on internal audit results. A member asked whether the external auditors relied on the outcome of internal audit reviews. Was it a matter of concern that, for example, the rate of exceptions in the continuous audit program was so high (albeit including many exceptions that were considered minor)? Ms Tory replied that the external auditors were aware of the results of the Internal Audit testing and considered it. However, the external auditors were concerned with the risk that existed at the entity level rather than only in individual departments. In their work, the external auditors went into some of the larger units to understand controls and to confirm that they were in operation, for example comparison of budget to actual spending. The external auditors were interested in controls that would monitor the University's financial affairs and detect problems. The Internal Audit Department was interested in controls that would prevent problems. Internal Audit sought to ensure that controls were in place going forward; the external auditors sought to ensure that controls had been in place to ensure the quality of financial information looking back. An important factor from the point of view of the external auditors was the requirement for manual signature of all cheques for amounts over \$50,000. Given the level of materiality, it would require a large number of cheques for a lower amount to make a material difference.

(e) More minor exceptions to appropriate procedures. A member said that it was important to focus not only on the economic implications of malfeasance but also to bear in mind the risk to the reputation of the University that could arise from behaviour that might cause lesser financial loss.

Another member referred to the exceptions to appropriate procedures classified as not significant. He asked whether there was a maximum tolerance for such exceptions. His organization, for example, had ceased to provide reimbursements for expenses that were not fully and properly documented.

(f) Conclusion about level of financial or operational risk. A member cited the conclusion in the report that "the audit results do not indicate an unreasonable level of financial or operational risk to the University in the light of its size and complexity of operations." Had Mr. Britt reached that conclusion by comparing his findings to a benchmark established for other organizations of a similar size?

Mr. Britt explained that his conclusion had been drawn in the light of the high level of decentralization and the large number of units in the University. Finding problems in one or two units should not be regarded as the basis for concern that there was a material problem that would create a high level of risk for the whole organization. He was well aware of reputational risk, and it was especially important to ensure appropriate compliance for funds supplied by the granting agencies who had their own monitoring procedures and could be unforgiving of even small exceptions. However, Internal Audit had found no problems that were pervasive and therefore a danger to the University

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A member observed that financial risk and compliance risk might best be seen as two separate categories. The problem in a situation of financial risk was fraud or inappropriate administration of finances. The problem of compliance risk involved failure to adhere to regulations. Mr. Britt agreed with the observation and said that he would separate the categories of risk in the future.

(g) Capital projects: Contractor prequalification program. A member referred to the information on the follow-up review of the process for contract tendering and administration for capital projects. The auditors had recommended that contractor pre-qualification calls be advertised nationally, in conformity with the Agreement on Internal Trade (A.I.T.) The administration had apparently decided not to implement the recommendation.

Ms Riggall replied that the University had requested a legal opinion on the matter. If it was permissible to do so, the University would prefer not to advertise nationally for contractors. She cited an instance in which a contractor had failed to complete a project according to the terms of the contract. The project had been completed late and at a cost well above its budget. The University would prefer, therefore, to invite only contractors it knew well to be of high quality to seek pre-qualification. If, however, the University were advised that national advertising was required under the law, the University would comply and seek in other ways to protect against misadventure.

(h) Prioritization of concerns. A member asked which of the concerns that had emerged from the internal audit program for the year were the greatest. Mr. Britt replied that his greatest concern was compliance with government requirements. The accountability framework for special grants such as research grants was being made more rigorous by both the federal and provincial governments. The second area of concern had to do with health and safety matters. He was not concerned that the University was an unsafe place to work or study. However, the approach used to identify health and safety risks was not as comprehensive as would be desirable. The third area of concern was risk arising from organizational restructuring. As further budget pressures forced even more restructuring, there was a growing risk to appropriate segregation of financial duties.

Ms Brown commented on compliance risk with respect to research grants. The Vice-President, Research had about one year ago established and filled the position of Executive Director, Research Oversight and Compliance. That Office was doing excellent work in making a broad range of staff in the academic divisions aware of the requirements of the granting councils and other funding agencies. The initiative was proving to be of very great benefit in the University's highly decentralized environment.

3. Internal Audit: Audit Plan, 2010-11

Mr. Britt presented the Internal Audit Plan for 2010-11. The plan was based on the risks identified in the 2009 Risk Assessment Profile. It assumed the completion of 8,000 audit hours. The Department's appointed staff resources for 2010-11 would be slightly lower, with a senior

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auditor having left the Department to accept a position at the University of Toronto Mississauga. The amount paid to that auditor would be used to engage contract auditors for specialized work. The objectives of the plan were consistent with the Department's mandate and with the Internal Audit Policy. The Department would work to assist management and the Audit Committee by providing analyses, appraisals, recommendations, and information concerning: significant operational and financial risks; the effectiveness of the systems of internal control and risk management; compliance with policies, procedures, contracts, and statutory requirements; the safeguarding of assets; and the development and implementation of effective administrative policies and procedures. The scope of the plan included academic, administrative and student-service departments on all three campuses and included information-systems auditing and consultation, continuous auditing, follow-up reviews and special reviews as well as assisting the external auditors with the annual financial-statement audit. The specific audits planned would include a substantial number of reviews of central administration activities, in part continuing reviews begun in 2009-10 but not completed and also responding to requests from the senior administration. There would also be some emphasis on information-systems reviews. The outcome would, however, be consistent with the risks that merited most attention.

Discussion centred on special reviews and on the consequence to other internal audit work of spending substantial time on special reviews. That discussion focused on the following themes.

(a) Time required for special reviews. In response to questions, Mr. Britt said that special reviews could be very demanding of time depending on the nature of the matter, the success of the person responsible in hiding the inappropriate behaviour, the clarity of the records, and therefore the level of detailed work required. Where an individual was suspected of a defalcation, it became appropriate to review all of the activities of that individual, who may have been responsible for other inappropriate actions. A total of 900 hours had been allocated in the 2009-10 plan, but 2,243 hours had been required. A total of 1,000 hours had been set aside in the plan for 2010-11. The need to complete ten special reviews in 2009-10 was highly unusual – far greater than in any previous year in Mr. Britt's lengthy experience in the University.

(b) Nature and concerns arising from special reviews. In response to a question, Mr. Britt said that the problems arising in the special reviews had originated from the absence of appropriate segregation of financial duties and from inadequate oversight or monitoring of the individual's work or of the accounts for which the individual was responsible. The nature of the problems was presented in staff development and training sessions to make appropriate University officers aware of the risks.

A member asked whether the problems had occurred at the working level or at a higher level in the organization. She noted that the Committee had typically taken comfort from the requirement that staff with financial responsibility complete the annual compliance reports. If, however, the problems occurred at more senior levels, then the Committee should take less comfort from that program. Mr. Britt said that the level varied. It was clear that some more

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senior officers, including department heads, should have been more diligent in carrying out their financial administrative duties. The problems had typically arisen when long-term employees had received substantial delegations of authority in an environment of trust, and the busy officers at one level up did not review financial administrative activities adequately. That led to the opportunity for defalcation.

(c) Consequences to individuals. A member expressed concern about the number of problems and about the time required to deal with them. Were actions taken to make it clear that the University would not tolerate misappropriation? Mr. Britt said that in all five cases that involved proven misappropriation, the employment of the individuals had been terminated for cause without any financial incentive to resign. While such action could be challenged through grievance procedures, the University had demonstrated a clear lack of tolerance for financial dishonesty.

(d) Consequences for other internal audit activity. A member asked whether the time required for special audits had left sufficient time for the discharge of other audit responsibilities. Mr. Britt was concerned about the discharge of the Department's full responsibilities. While the Department had done everything possible to take care of its responsibilities other than special audits, Mr. Britt was not pleased that it had proven necessary to carry forward so much work from the 2009-10 plan. While the special audits did sometimes result in the recovery of money, they added less value than the preventive result arising from other work.

A member said that the basic question remained: was the time left for other work sufficient? The Chair said that it was the Committee's duty to satisfy itself that the Internal Audit Plan for 2010-11 was sufficient, or if it were not to make its reservations known. A member said that she would not wish to see the current trends continue and to find that so large an amount of time was required for special audits again in 2010-11. In part, the problem was the highly decentralized nature of the University. That fact resulted in the on-going opportunity for small acts of fraud. On the other hand, many major risks were not being adequately addressed. Perhaps the Committee should ask Mr. Britt to report on an on-going basis on any problems in the achievement of the Internal Audit plan that might arise from the need to devote more time than planned to special audits. Another member commented that problems appeared to be inevitable because the Department was already behind in completing work from the previous year's plan.

A member suggested that the best solution might well be the provision of enhanced resources to the Department. There was a real risk of damage to the reputation of the University if a problem emerged that should have been prevented by appropriate internal audit activities. The failure to devote appropriate resources to the internal-audit function would not be accepted as good reason for a major problem that might arise. The member asked whether it might be possible to charge back to the Department the cost of any special audit required. A member said that if internal audits led to substantial improvements in administrative procedures, the department concerned would ultimately benefit and should be willing to pay the cost of gaining that benefit. Mr. Britt observed that it might be appropriate to bring in contract auditors to deal with particular

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problems. He was aware of situations in some organizations where departments that were subjects of contract auditing paid some or all of its cost. Ms Riggall expressed concern that if departments were aware that they would have to pay some or all of the cost of special audits, they might not disclose problems or request assistance.

A member said that it was the responsibility of the Committee to require that any serious problem be dealt with. How it would be dealt with was a decision for the University's administrators. It would at a minimum be important to track the time requirements for special audits going forward to determine whether the matter required action during the year. Mr. Britt stressed that 2009-10 had been a very unusual year. The unusually high number of problems could be the result of a number of factors: the difficult economic times creating pressures on individual staff members; the gaps in University's administrative organization caused by financial pressures, leading to problems that would otherwise have been prevented by a middle level of management; or simply greater effectiveness of the Internal Audit Department, making units more willing to seek help. A member noted a similar experience in his organization; the more good work that was done by the internal auditors, the more problems emerged. It would be very important to track the situation going forward.

Two members referred to the possibility of using contract auditors to deal with any future need for an unusually large number special audits. It might well be the case that external specialists, with appropriate skills and experience, could deal with such situations in a more efficient manner than the University's own department. Mr. Britt agreed that co-sourcing could be considered, but he noted that he was a certified fraud examiner and that the Department was well able to deal with such matters itself and to do so in an efficient manner.

4. Internal Auditor: Private Meeting

The Chair stated that an *in camera* meeting with the Internal Auditor was a regular, annual procedure. Members of the University's administration, the Secretariat and the external auditors absented themselves. Mr. Britt was invited to report on "any problems encountered, any failure to provide appropriate information or any restrictions on internal audit work, the general co-operation received in the performance of internal audit duties, and any matters requiring discussion arising from the auditor's findings." [Terms of Reference of the Audit Committee, item 5.1.3(d).]

Following the *in camera* meeting, members of the administration, the secretariat and the external auditors resumed their attendance. The Chair instructed the Secretary to arrange for an additional meeting of the Committee early in the fall. The objective would be to permit the Committee to continue its *in camera* discussion and to give further consideration to the Committee's role and its agendas, the role of the internal auditor, and the risk assessment.

REPORT NUMBER 93 OF THE AUDIT COMMITTEE – May 12, 2010**5. Risk Assessment, 2010**

The Chair stated that the Audit Committee terms of reference called upon the Committee to review “an annual management report on significant business, financial and regulatory risks and [to] monitor the University’s processes for identifying and controlling those risks. In carrying out this responsibility, the Committee focuses primarily on the adequacy of key controls over, and mitigations of, those vital risks considered to be, currently or in the future, more significant and likely to occur, [and] meets with management and the internal or external auditors to come to a fuller understanding and better assessment of management’s response to controlling important risk situations. . . .”

Ms Riggall reported that the current report was the third the administration had presented in the current format. To provide for continuity, the matters reported in 2009 continued to be shown in the report, along with the matters added to the report for 2010. The matters included in the 2008 report had not been carried forward unless they were of particular on-going relevance. The report from 2009 had been reviewed by the President and Vice-Presidents, and the sections of the report for 2010 had been prepared by the senior administrator responsible for each risk area. Those sections had then been compiled, and they had been reviewed by the President and the Vice-Presidents. Two areas of risk were of particular concern: compliance with Provincial compensation-restraint legislation and the pension-plan deficit. Neither matter was wholly in the University’s control. Apart from those areas, the administration was fairly comfortable with its understanding of the risks facing the University and with the actions taken to mitigate the University’s risk exposures.

The following matters arose in questions and discussion.

(a) Shared ownership of risk areas. A member said that he was concerned that for some of the risk categories, there was more than one stated “owner.” He regarded that as a cause for concern and stated his preference that there be one individual with an unambiguous responsibility for management of each area risk. Ms Riggall replied that there was more than one owner stated in three cases. First, in the case of financial risk, she was ultimately responsible, but Ms Brown as Chief Financial Officer in fact oversaw most of the activity undertaken to mitigate financial risk. Both she and Ms. Brown spent a great deal of time together and with Mr. Piché on management of financial risk. Second, in the case of Physical/Facilities risk, Ms Riggall was responsible for policy in the area and for management of the risks on the St. George Campus, but the Principals and Vice-Presidents of the Scarborough and Mississauga campuses were responsible for the management of the risks on their own campuses. Finally, in the case of information-technology risk, the Vice-President and Provost, Professor Misak, was ultimately responsible, but the Chief Information Officer again in fact oversaw the activity undertaken to manage the risk. The member said that he was satisfied in the cases where another officer reported directly to a Vice-President, the matter of ownership of the risk was clearly that of the Vice-President.

(b) Information / information-technology risk. A member observed that information-technology risk was the one area where no committee of the Governing Council was identified as having responsibility. Ms Riggall said that there had to date been no report on the overall

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management of the area. The management of information and information technology in the University was very decentralized, with the appointment of the Chief Information Officer a relatively recent development. Another member stressed that information security and information technology were areas of great potential risk, and there should be a governance body responsible for policy and strategy in the area. Ms Riggall said that there were two areas where governance oversight might well be appropriate. The first was the infrastructure of the information systems, and it appeared to her that the Business Board might well be the appropriate governance body to receive reports and consider overall policy. The second area concerned the appropriate information technology to enable the University to deliver its academic and research programs. That matter was clearly of interest to the Academic Board. The Chair proposed, and the Committee AGREED that the Committee consider the matter further at its first meeting of the 2010-11 year – the additional meeting the Committee had agreed to hold. She proposed that the Director of Internal Audit might well provide advice on the subject of oversight of information-technology security and controls. Standard protocols were in place in other organizations.

(c) Emergency preparedness. A member asked whether the University's administration was satisfied that it was prepared to deal with sudden emergency situations, including managing the response, communicating with members of the University, and communicating with the outside community. The member noted that the level of risk of emergencies was growing. Ms Riggall replied that the University had an emergency-response procedure in place. An executive officer of the University was designated as being on-call twenty-four hours a day for each week of the year to assume responsibility in the event of an emergency. Protocols for emergency response were in place to be supervised by that officer. Ms Riggall described how that arrangement had been implemented in the tragic case of a fatal construction accident at the University of Toronto at Scarborough.

6. Audited Financial Statements for the Year Ended April 30, 2010: Draft Notes

The Chair said that the full financial statements would come before the Committee at the June 16, 2010 meeting, at which time the Committee would consider a motion for their approval. The current review of the notes provided an opportunity for members to comment on proposed changes before they were included in the final draft of the statements.

Mr. Piché summarized the major changes to the notes. In some cases, the changes were required in response to changes in accounting standards. In other cases, the University chose to make changes to enhance the clarity and value of the note disclosures.

- **Note 2(a) – Change in accounting policies** (page 1). The University had adopted retroactively a requirement concerning the cash-flow statement that required the separate presentation of investing and financing activities. (In the course of discussion, a member noted his surprise that the separation had not been required at an earlier date.)

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6. Audited Financial Statements for the Year Ended April 30, 2010: Draft Notes (Cont'd)

- **Note 2(c) –Derivative financial instruments** (pages 2-3). The new note described the accounting treatment of hedge contracts when they ceased to be required as a hedge or when they were terminated or sold. The provision would affect the University's accounting for forward contracts entered into to hedge against interest-rate changes on certain floating-rate loans at such time as those loans were repaid.
- **Note 5 – Investments: Risk management** (page 8). An additional note disclosure, which was not required by external accounting standards, described the financial risks to which the University's investments were exposed, and it described certain steps taken to mitigate those risks. Those steps included foreign-currency hedging and minimum credit-quality standards for fixed-income investments. Comparable notes were included in the financial statements of many other universities and corporations.
- **Note 25 – Comparative financial statements (page 20)**. The notes stated that comparative financial statements had been reclassified for the statements previously presented in order to conform to the 2010 statement presentation. The most significant change had to do with the presentation of certain revenue in terms of gross revenue, along with the separate presentation of expenses incurred in earning that revenue. In particular, the statements presented gross investment income as revenue and recorded investment-management fees as expenses. Previously, the statements had presented only the net revenue after fees. The new form of presentation had been used in the most recent annual report on the endowment funds.

A member asked about the status of discussions of financial statement reporting standards associated with the adoption of International Financial Reporting Standards (I.F.R.S.) for the private sector. Mr. Piché replied that the Canadian Institute of Chartered Accountants (C.I.C.A.) had issued an exposure draft on accounting standards for not-for-profit organizations. The Ontario universities, working with the Canadian Association of University Business Officers, would submit a response. The exposure draft would permit the universities to use the new International Financial Reporting Standards if they wished to do so, but adoption of those standards would be very costly. The alternative would be the adoption of accounting standards for private entities along with section 4400 of the C.I.C.A. *Handbook*. The Ontario universities favoured the latter alternative. The major problem was that the financial statements of the publicly supported universities in some other Canadian Provinces were consolidated with those of the Province itself. The universities in those Provinces would have to adopt the same reporting standards as the Provincial Government, which would mean that the statements of all Canadian universities would not be comparable. The universities would raise that concern with the C.I.C.A.

Ms Tory agreed that the private corporation standards, as modified by section 4400 of the *Handbook*, would be the most appropriate choice for universities and hospitals. The I.F.R.S had no special rules for not-for-profit organizations. The complication was that the universities and hospitals in different jurisdictions could wind up using different standards.

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While the C.I.C.A Accounting Standards Board supported giving the universities and hospitals the choice of standards they would find most appropriate, Government standard-setters might well be unwilling to agree, thinking that their own standards were superior. The differences could be very significant. For example, in the government reporting standards, investments were recorded at cost rather than marked to market.

7. Report of the Administration

Ms Riggall stated that there were no matters, other than those on the agenda, that should be drawn to the attention of the Audit Committee at this time.

8. Date of Next Meeting

The Chair reminded members that the next regular meeting of the Committee was scheduled for Wednesday, June 16, 2010. The major item of business would be the review of the audited financial statements.

The meeting adjourned at 5:40 p.m.

Secretary

Chair

June 1, 2010

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