Confidential

Cabinet Submission

Legislation and Regulations Committee

Establishing an Audit Committee

TREASURY BOARD SECRETARIAT

Office of the Provincial Controller Division

DRAFT: FOR DISCUSSION PURPOSES ONLY

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I Request

Treasury Board Secretariat is requesting the Legislation and Regulations Committee of Cabinet to recommend for approval an amendment to the Auditor General Act establishing an Audit Committee; an advisory agency of independent experts to provide advice to the Government of Ontario and the Auditor General (AG).

II Background

The Government's transformational agenda and continuing commitment to modernizing government are fostering a new environment in the OPS, one in which risk management and fiscal accountability take centre stage. At the same time, the rising emphasis on transparency and efficiencies in government operations means that the Government faces an ongoing challenge to ensure that its control and accountability mechanisms are effective.

The Government addresses these challenges through an established governance and oversight function which includes the following three components:

1. ***Corporate Audit Committee***

   The Corporate Audit Committee (CAC) assists the Deputy Ministers' Council (DMC) in discharging their governance, accountability and controllership responsibilities by advising that Ministry and Agency risks are being appropriately addressed through a strong governance, risk, control and compliance framework; appropriate stewardship; and an adequate and effective internal audit function.

   The CAC acts as a forum for communication between the Deputy Ministers, senior management, and the Ontario Internal Audit Division (OIAD).

   Within the Ontario Public Service (OPS), Office of the Provincial Controller Division (OPCD) and Ontario Internal Audit Division (OIAD) maintain the key relationships with the Auditor General (AG).

2. ***Ontario Internal Audit Division***

   OIAD provides risk and business consulting services, and independent and objective assurance services to ministries and agencies of the Government. It is responsible for:

   - Audit services for OPS under direction of Corporate Audit Committee though its
     - Enterprise-Wide Audit Service Team
     - Enterprise-Wide I and IT Audit Service Team
     - Corporate Financial Assurance Audit Service Team:
   - Audit services to ministries and agencies through Ministry Audit Service Teams:

- Specialized forensic and fraud investigations services to ministries and agencies though its Forensic Investigations Team:

OIAD liaises between the AG and clients ministries and agencies on Value for Money audit and special reports.

3. ***Office of the Provincial Controller Division***

   OPCD is responsible for maintaining the Public Accounts and preparing the Annual Report and Consolidated Statements and the Public Sector Salary Disclosure. OPCD also supports the preparation of the multi-year fiscal plan, Results-based Plan and the provincial Budget, as well as the Pre-Election Report on Ontario's Finances.

   OPCD works with the AG during the audit of Public Accounts. The AG considers internal control, accounting policies, accounting estimates and control over assets as well as the overall presentation of the consolidated financial statements. OPCD also liaises with the AG, as well as other jurisdictions and the accountancy bodies, on the development of government accounting standards.

Working relationship with the AG

There have been significant disagreements between professional staff and the AG regarding a number of financial accounting and reporting issues. Both OPCD and OIAD have noted instances where the efficiency and effectiveness of the auditing and reporting process could be improved. In addition, senior staff from several line ministries, have expressed concerns regarding the AG's requests for access to data and/or handling of sensitive issues.

Mostly recently, during the 2015-16 Public Accounts process, the Auditor General and the government's professional accounting staff disagreed regarding the application of Public Sector Accounting Standards (PSAS) to pension assets related to two pension plans that the Province jointly sponsors – Ontario Teachers' Pension Plan and Ontario Public Service Employees' Union Pension Plan.

The failure to resolve key issues resulted in:

- The government passing a time-limited regulation to align the accounting for these pension assets with the interpretation of the Auditor General. This time-limited regulation enabled the professional accounting staff to take responsibility for the preparation of the Public Accounts in accordance with legislation and PSAS.
- The government releasing an annual report and unaudited financial statements on October 3, 2016, and concurrently announcing that an advisory panel would be formed to review the application of PSAS to these pension assets.
- The Auditor General issuing a qualified report on the 2015-16 Public Accounts on October 5, 2016. While the 2015-16 results were accepted by the Auditor General, the audit opinion was qualified because the comparative financial balances were not restated for the prior year to write off the pension assets.

The Pension Asset Expert Advisory Panel reported on 13th February, 2017 and supported the government opinion that the pension funds met the definition of an economic resource, and should thus be accounted as government assets.

While the Province has publicly committed to adopting the recommendations of the Expert Panel, the AG continues to disagree with this treatment.

The creation of an Audit Committee would assist in enhancing the relationship between the professional staff and the AG by providing a forum where both parties can have a discussion on a contentious issue and benefit from the wisdom of independent expertise.

III Key Considerations / Business Case

Purpose

The Audit Committee will be an advisory agency of independent experts to provide advice to the Government of Ontario and the AG,

The purpose of the Audit Committee will be to enhance the integrity and efficiency of the Public Accounts Audit and the system of reporting performance, by providing an independent forum for communication and discussion where OPS professional staff and the AG could discuss concerns. Specifically the Audit Committee will provide professional staff and the AG:

- Access to independent experts who could provide advice and wise counsel on the planning of the Public Accounts Audit;
- A neutral space to discuss significant financial accounting and reporting issues where there might be disagreement between the AG and the professional staff of government; and
- A forum where independent experts in the field of auditing and accounting could provide an appropriate challenge to either party.

Authority

An amendment to The Auditor General Act will authorize the establishment of an Audit Committee, and provide the authority to exercise its responsibilities.

The Audit Committee, within the scope of its roles and responsibilities, will be authorized to:

- review the planning, performance and reports relating to the Public Accounts Audit, Value for Money Audits and Special Reports.
- seek independent / legal advice after they have reviewed the matter and agrees that seeking a second opinion is beneficial.
- call witnesses as required.

Mandate and Implementation:

The Audit Committee will have the mandate to review:

- Public Accounts
- Value for Money Audits
- Special Reports.

The Audit Committee will focus on Public Accounts in year one, and expand the scope of their activity each year until it achieves its full mandate at the end of year 3:

- Year 1: Public Accounts only
- Year 2: Public Accounts and Special Reports only
- Year 3: Public Accounts, Value for Money Audits and Special Reports.

The implementation plan will be included in through regulations.

NOTE: Confirm with legal how this will be affected in legislation and regulation and then articulate in document

NOTE: Focus has been on the role of the Audit Committee wrt Public Accounts, details of their role wrt VFM audits and Special Reports will be fleshed out during the implementation phase.

Composition and Tenure

The Audit Committee will consist of up to seven members, with one member appointed as Chair.

Members will be appointed by the Province for an initial period of up to three years, and may serve for up to two terms.

Members, taken collectively, will have a broad range of skills, knowledge and experience. They will comprise accounting experts, and legal experts in the field of public sector accounting and auditing standards.

Each member will bring a unique skillset and perspective. Proposed appointees will be assessed against a competency map (Appendix II) which includes knowledge in areas such as:

- Public accounting/standard setting, including Pension Law and Accounting
- Government
- Academia

Members' employment or involvement in other activities must not place them in a conflict of interest position.

Members must take an Oath of Confidentiality.

Meetings and Attendance

In year 1 the Audit Committee will meet:

- Quarter 4: Audit Planning for Public Accounts Audit
- Quarter 2: Interim Meeting for Public Accounts Audit
- Quarter 3: Final Audit Report for Public Accounts Audit and Auditor General's Report
- Ad hoc if requested

The meeting schedule will be reviewed in year 2 and 3 as the Audit Committee increases the scope of its work.

The Chair of the Audit Committee may also call a meeting to review any matter at the request of either the AG or the President of the Treasury Board.

Audit Committee members shall attend/participate in the meetings; no substitutes or alternates should attend in place of a member.

Reporting and Accountability:

The Audit Committee must provide an annual report to Government regarding substantive matters dealt with and actions taken.

The Audit Committee must disclose the charter and a summary of how they discharged the responsibilities contained in the charter.

The Audit Committee must evaluate their performance annually.

Agency and Appointment's Directive

Being an advisory body, the Audit Committee must comply with the requirements of the Agency and Appointment's Directive.

Impact on OPS or government operations

The Audit Committee is anticipated to accelerate the timeliness of Public Accounts as it will provide a forum for discussion of contentious issues which should facilitate the resolution process resulting in a smoother Public Accounts Audit which is completed earlier.

NOTE: NOTE: Focus has been on the role of the Audit Committee wrt Public Accounts, details of the impact wrt VFM audits and Special Reports will be fleshed out during the implementation phase.

IV Jurisdictional Scan

In the private sector, Audit Committees have long since provided oversight by offering objective advice and recommendations to the board on whether the organization's governance, risk management, and internal control processes are suitably designed and working as intended to achieve its objectives.

Independent Audit Committees are now also being established within public sector organisations to meet increasing demands for transparency and accountability. Audit Committees provide government with an independent source of assurance and advice to on key aspects of its operations. The distinguishing feature of a public sector Audit Committee is its independence from management.

Alberta

Within Canada, only Alberta has a functioning, and long standing, Audit Committee. Alberta's Auditor General Act stipulates the roles and functions of the Committee, and ensures that the government has insight into the AG reports before they are released.

Alberta's Audit Committee reviews and advises on both performance audits and the Public Accounts, specifically:

- Issues relating to financial statement presentation and disclosure, accounting policies and pronouncements, and non-financial performance information,
- Matters related to the AG's report to the Legislative Assembly prior to its publication and any other reports made by the AG,
- Any matters related to the financial affairs of the Crown in accordance with a request of the President of Treasury Board and Minister of Finance.

Alberta's Audit Committee plays an advisory role, and does not have decision-making authority. It has proven to be successful in bridging the communication between the AG and provincial government. In particular, the AG is very supportive of the audit committee and considers it to be helpful to both parties.

Saskatchewan

The Provincial Audit Act in Saskatchewan mandates, and stipulates the roles and functions of the Audit Committee.

There is not currently an operating Audit Committee nor has one been appointed for many years, however, Saskatchewan is currently seeking to appoint new members.

Newfoundland and Labrador

Newfoundland and Labrador is currently developing a charter for its internal Audit Committee to include roles and responsibilities for: Internal Audit, Public Accounts, Advocacy, Ethics and Values, General Matters.

Canada

The Independent Accounting and Financial Auditing Advisory Committee provides advice to the Federal AG on his audits of the financial statements of the Government of Canada, Crown corporations, and various other public sector entities.

Members of the Committee are selected by the AG, who is the Chair, and the Committee members report as personal advisors to him.

International Jurisdictions

The available guidance for public sector audit committees is more limited than for businesses, however, some of the Big 4 audit firms have published guidance for public sector entities that wish to form an audit committee. Much of the guidance is similar and all of the organizations publishing guidance recommend government entities use an audit committee.

In Australia, audit committees are considered a critical component of corporate governance. This is reflected in the legislative requirements included in the Financial Management and Accountability Act, and the Commonwealth Authorities and Companies Act that require Australian Government public sector entities to establish an audit committee.

In New Zealand, the New Zealand Institute of Internal Auditors and KPMG published a survey of current practice characteristics in public sector audit committees in New Zealand (IIA New Zealand, 2005).

In the UK, public sector audit committee guidance is available through the Audit Committee

Handbook (UK Treasury, 2007).

Although there is no all-encompassing legislation or regulation in the USA that requires audit committees in the public sector, several prominent USA professional organizations[1] recommend or encourage that audit committees be created for government entities.

V Options

The following options were considered:

Option 1: Legislation (Recommend)

Establishing the Audit Committee through legislation, provides the Audit Committee with legislative weight. Key functions and powers of the Audit Committee can also be included in the legislation, for example, the power to call meeting, to call witnesses, when reports have to be presented, etc.

Establishing the Audit Committee by legislation places a legal obligation on government staff and the AG to cooperate and interact with the Audit Committee.

Option 2: Minister's Order

An alternative is to establish the Audit Committee as an advisory committee providing specific advice to the Minister by Minister's Order. However, given the AG's reaction to the report of The Pension Asset Expert Advisory Panel there is a high risk that the AG will choose to perceive the Audit Committee primary function as providing support to the government and thus of being biased. The AG may not feel compelled to interact with the Audit Committee and/or to disregard its advice and recommendations.

Option 3: Status Quo

There has been increased tension in the working relationship between professional staff and the AG. If government does not act, the tension is likely to continue and the relationship with the AG may deteriorate further, resulting in more disagreements and qualified audit opinions in the future.

Establishing the Audit Committee is just one element of a wider TBS strategy to improve the working relationship with the AG.

Additionally, OIAD has been requested to prepare an analysis of potential opportunities to enhance public service collaboration with the OAGO, specifically as it relates to where OIAD/CAC/DMC may provide enhanced support. OIAD's analysis focuses on the AG's value for money (VFM) audit processes.

Recommendation

To amend to the Auditor General Act to establish an Audit Committee to strengthen and

[1] These include the Governmental Finance Officers Association (GFOA, 2008), the National Association of College and University Business Officials, the Institute of Internal Auditors (IIA, 2009), the Governmental Accountability Office, and the Office of Management and Budget.

improve the transparency and accountability of the government, serve as a vehicle for communication between the provincial government and the AG, and play an independent oversight and advisory role to assist both the government and Auditor General.

This is also in line with Alberta's Auditor General Act and The Provincial Audit Act in Saskatchewan which mandate the establishment of an Audit Committee (see section IV for further details).

Ontario would be the second jurisdiction in Canada, after Alberta, to establish a provincial Audit Committee.

VI Financial Implications / Analysis

Per diems

Audit Committee members will be compensated at market rates because of the time requirement expected of committee members and the ability to attract quality candidates for the committee.

The proposed per diem of $627 for the Chair and $491 for other members is above the maximum remuneration provided for part-time Advisory Agencies as set out in Schedule A of the Agencies and Appointments Directive.

Note: Waiting for confirmation from OIAD whether there are external members on CAC and what they are paid.

The proposed rates are in line with special advisors and appointees to short-term advisory boards for appointees with specific knowledge, and expertise/technical knowledge. Other experts sitting on Provincial Advisory Panels have been remunerated at similar rates including

- Committee to evaluate drugs: $355-$1000 per diem, the Chair is on retainer.
- Building Code Commission: $398-$627 per diem.
- Physician payment review board: $398-$664 per diem.
- Ontario Financing Authority: Max $500 per diem.

The chair received a higher per diem than other members, as this person will likely have interaction with the media and must become fluent with all the aspects of the Audit Committees. Any under-expenditure on per diem costs may be reallocated to procurement costs in the approved budget.

Other expenses and costs

Audit Committee members will be reimbursed for travel costs to attend the meetings, and other reasonable expenses incurred in connection with their duties in accordance with Treasury Board/Management Board of Cabinet Directives and Guidelines.

The Audit Committee budget also includes a provision for ODOE, and for the procurement of services, including advice from such counsel, staff, or expertise considered necessary in the performance of its duties at reasonable remuneration approved by TB/MBC.TBS will follow TB/MBC Directives and Guidelines and other applicable government policies in obtaining these services.

Audit Committee Support

The Province will identify two ministry staff to support the Audit Committee:

- 1.0 FTE AFA21 Senior Policy Advisor
- 1.0 FTE OAD11 Administrative Assistant

The two staff members will work collaboratively with the Audit Committee to provide information as requested/required, to conduct research as needed, to help write reports, and administrative support.

The Province will be responsible the costs of these individuals.

Annual Costs

Based on these rates, the total annual budget is estimated at $0.8M, which is comprised of:

		#people	Per diem	# meeting / year	# days / meeting	Total Cost (rounded)
Audit Committee Costs						
Chair		1	627	4	15	38,000
Members		6	491	4	10	118,000
		Total Per Diems				156,000
		Travel Budget: 10% per diem per meeting				62.000
		ODOE Costs: 15% of per diems				23,000
		Total Budget: Chair and Members				241,000
Additional OPS Staff Costs – 2.0 FTE						
AFA21	Salary & Wages (mid-point scale)				94,000	
	Employee Benefits at 15%				14,000	
						108,000
	ODOE at 15%					16,000
OAG11	Salary & Wages (mid-point scale)				56,000	
	Employee Benefits at 19%				11,000	
						67,000
	ODOE at 15%					10,000
Procurement Costs						400,000
		Total Estimated Annual Costs				**842,000**

NOTE: While $$ Costs will be managed within OPCD/TBS Budget, we will need approval for the 2.0 FTEs requested.

The budget is consistent with the goal of resolving risky/contentious accounting issues earlier such that fiscal planning can be completed with more certainty regarding accounting issues.

Additional costs may arise for others:

- The AG is likely to incur some costs and may request additional funding
- Other ministries may also incur costs if they are required to be present at the committee meetings, depending on the scope of the committee (e.g. if the committee focuses on VFM audits, the audited ministry would be at the meeting.)

OPCD/OTB will managed additional costs within their funding envelope. No additional funds will be required.

The costs for Option 1 and 2 will be the same regardless of whether the committee is established via changes to legislation or a Minister's Order.

Option 3 will incur no cost as no committee will be established. Funds that would be directed towards the Audit Committee will instead be directed to other OPCD / TBS priorities.

VII Risks and Mitigating Strategies

Note: Cindy has had initial discussion with Communication, and we will be seeking their input on mitigating strategies.

Risks	**Mitigating Strategies**
• Establishing an Audit Committee will be seen as an increase in bureaucracy and cost with little or no benefit to Ontario. • There is a contraindication in the government establishing a new committee while, at the same time, trying to reduce the number of committees.	• Establishing an Audit Committees is in line with Best Governance practice • The costs of the Audit Committee will be managed within the government's existing budget. • The costs of permanent Audit Committee which will lower than the costs associated with short term advisory body like the Pension Asset Expert Advisory Panel.
• The Audit Committee may be seen as usurping authority from an independent legislative officer, and thus undermining the role of the	• The Audit Committee is an advisory body, and there is no requirement that the AG follow the Audit Committee's advice • The AG retains independence to make

AG. • Placing a legal obligation on the AG to cooperate and interact with the Audit Committee may be seen as usurping authority from an independent legislative officer, and thus undermining the role of the AG.	own decisions.

VIII Performance Measurement

Note: Working to identify performance measurement items

IX Legislative and Regulatory Requirements

Note: Have had initial discussion with Paul Kaufman, Legal Services Branch. He is expecting to receive the draft Cabinet Submission for his review/comment shortly.

X Stakeholder Engagement

Note: Cindy has had initial discussion with Communication, and we will be seeking their input on mitigating strategies.

STAKEHOLDER	CONCERN / ISSUE	MITIGATING STRATEGY
Auditor General	• Unlikely to be supportive • May be seen as an attempt to hamper independence	• Committee is an advisory body, like the Pension Asset Expert Advisory Panel appointed 2016/2017 • AG retains independence to make own decisions, as there is no requirement that the AG follow the Audit Committee's advice • Establishing an Audit Committees is in line with Best Governance practices • May be possible to leverage support from both the controller and AG in Alberta to provide Ontario AG with a basis to support the creation of this

		committee
Other Independent Officers of the Legislature: Ombudsman, Integrity Commissioner, Fairness Commissioner, Etc	• May be some concern that the Audit Committee will impact the role of the AG, and similar bodies may be created to affect other Independent Officers of the Legislature	• Committee is advisory body, like the Pension Advisory Committee established 2016/2017. • Establishing an Audit Committees is in line with Best Governance practices.
Federal and provincial AGs	• Interest, rather than concern, regarding Ontario moving forward with a leading edge / best practice	• Establishing an Audit Committees is in line with Best Governance practice. • Ontario will be the third province to enact legislation to establish an Audit Committee and the second province to establish one.
OPCD / OIAD	• Staff may have concerns regarding how the Audit Committee will impact their work and relationship with the AG	• Establishing an Audit Committees is in line with Best Governance practice. • The Audit Committee in Alberta works well for both staff and the AG and both parties consider it helpful.

XI Recommendation

That Legislation and Regulations Committee of Cabinet recommend for approval an amendment to the Auditor General Act establishing an Audit Committee, which would be advisory agency of independent experts to provide specific advice to the Government of Ontario and the Auditor General (AG)

That Legislation and Regulations Committee of Cabinet recommend to the Lieutenant Governor in Council a remuneration Order in Council for panel members.

XII Communication and Issues Management

NOTE : Cindy has had initial discussion with TBS communications (Sofie DiMuzio). They are expecting to receive the draft Cabinet Submission for review/comment shortly.

XIII Proposed Minute

Note: Working with TBS Corporate Services / Business Planning and Financial

Management (Elena Wagner) to draft proposed minute

Appendix I: Roles & Responsibilities

NOTE: Working on completing the above table to make explicit the different roles of government, the AG and the Audit Committee. Table will be 'back pocket' item or an appendix but including here while the paper is a WIP

	Government	Auditor General	Audit Committee
Public Accounts			
Value for Money Audits			
Special Reports			

Appendix II: Member Competencies

NOTE: Working on competency map