

EXTERNAL AUDITOR INDEPENDENCE

BRD 315

PURPOSE

Policy BRD 310, *Terms of Reference for the Audit & Finance Committee* (the “Committee”), assigns to the Committee the responsibility of reviewing the planning and results of external audit activities, and for overseeing the ongoing relationship with the external auditor.

The Committee recommends engagement of the external auditor to the Board of Directors of Northern Health (the “Board”). As specified in BRD 310 section E “External Audit”, it is also required to:

- *review and receive assurances on the independence of the external auditor; and*
- *review the internal audit services and non-audit services to be provided by the external auditor’s firm or its affiliates (including estimated fees) and consider the impact on the independence of the external audit*

The objectivity and integrity of the external auditor is fundamental to the public confidence in the reliability of the external auditor’s report and hence the public accountability of Northern Health.

Since the external auditor is required to have a relationship with the client, absolute independence is not possible. The significance of economic, financial and other relationships must therefore be evaluated in the light of what a reasonable and informed third party would conclude as acceptable.

The purpose of this policy is to establish principles and controls designed to provide reasonable assurance that the external auditor maintains an adequate degree of independence to ensure objectivity and integrity.

The principles and controls set out below concern the engagement of the external auditor, the justification of non-audit services, and the hiring of audit staff.

ENGAGEMENT OF THE EXTERNAL AUDITOR

1. The external auditor’s independence can be influenced by a number of threats including, but not limited to:
 - a. Self-review threats that occur when an external auditor provides assurance on his or her own work

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- b. Self-interest threats that occur when an external auditor could benefit from a financial interest in a client or when there is an undue dependence on an assurance¹ client
 - c. Advocacy threats that occur when an external auditor promotes a client's position or opinion
 - d. Familiarity threats which occur when an external auditor becomes too sympathetic to a client's interests
 - e. Intimidation threats which occur when an external auditor is deterred from acting objectively by actual or perceived threats from a client
2. It is expected that the external auditor will maintain a quality control system which recognizes these and other threats and provides reasonable assurance that his or her independence is not impaired.
 3. The external auditor is required to give the Committee annual assurances concerning independence.
 4. The external auditor is expected to adhere to a rotation policy that provides a balance between effectiveness, efficiency and independence. This rotation must be at intervals of no more than seven years for the lead partner responsible for the audit.

An exemption on an annual basis from these requirements can be granted by the Committee if circumstances require such an exemption. Where there is only one partner engaged, the Committee may request that a partner from another location of the same firm be utilized in at least one year.

5. The external auditor should not hire and involve any of the following individuals to participate in the audit within twelve months of the cessation of their employment with Northern Health:
 - a. Individuals who were previously employed as senior management of Northern Health, or
 - b. Individuals who were previously employed as participants in processes or areas subject to external audit procedures.
6. Once the Committee is satisfied that the external auditor recognizes and accepts these principles and responsibilities it will authorize the Board Chair and the President and Chief Executive Officer (the "CEO") to jointly co-sign the letter of engagement.

¹ An 'assurance client' is a client who is receiving external audit services

INTERNAL AUDIT SERVICES

1. Internal audit services encompass assurance and consulting activities undertaken by the Internal Audit department of Northern Health. Internal Audit may, during the course of the year, seek assistance on projects through contract relationships with qualified individuals or firms.
2. The Chartered Professional Accountants of British Columbia (CPABC) Code of Professional Conduct specifically prohibits performance of an external audit engagement if:
 - “... during either the period covered by the financial statements subject to audit or review or the engagement period, the member, the firm or a network firm or a member of the firm or network firm provides an internal audit service to the entity or a related entity unless, with respect to the entity for which the internal audit service is provided:*
 - (i) the entity designates an appropriate and competent resource within senior management to be responsible for internal audit activities and to acknowledge responsibility for designing, implementing and maintaining internal controls;*
 - (ii) the entity or its audit committee reviews, assesses and approves the scope, risk and frequency of the internal audit services;*
 - (iii) the entity’s management evaluates the adequacy of the internal audit services and the findings resulting from their performance;*
 - (iv) the entity’s management evaluates and determines which recommendations resulting from the internal audit services to implement and manages the implementation process; and*
 - (v) the entity’s management reports to the audit committee the significant findings and recommendations resulting from the internal audit services.”*
3. The external auditor should not provide internal audit services where the services comprise a significant portion of the internal audit activities.
4. Certain internal audit activities may impair the independence of the external auditor and should not be undertaken by the external auditor:
 - a. Performing ongoing monitoring or quality control activities that relate to the execution, accounting for, or approval of transactions
 - b. Determining which, if any, recommendations for improving the internal control system should be implemented
 - c. Reporting to the Board or the Committee on behalf of management or Internal Audit

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- d. Approving or being responsible for the overall internal audit work plan, including the determination of the internal audit risk and scope, project priorities, and frequency of performance of audit procedures
5. The licensed firm is required to identify threats to its independence and either apply safeguards to reduce the threats to an acceptable level or refuse to accept the external audit engagement.²
6. A proposal by Internal Audit to engage the external auditor for any internal audit services must be approved in advance by the Committee. The proposal will provide an estimate of fees and a description of safeguards to ensure independence of the external auditor is maintained. The proposal must be accompanied by a statement by the external auditor that such services:
 - a. Will not be provided by external audit staff members participating in an external audit of Northern Health within twelve months of the provision of internal audit services
 - b. Will be supervised and reviewed by an external audit partner other than that responsible for the provision of external audit services
 - c. Will exclude audit items covered in the annual external audit
 - d. Will exclude activities outlined in #4 above
7. The total fees incurred in the provision of internal audit services by the external auditor will not exceed 25% of the regular external audit fee for the year as approved by the Board.

NON-AUDIT SERVICES

1. External audit services are those related to the formulation of an opinion on financial statements prepared by management and include advice on accounting policies. Non-audit services are those services other than external or internal audit services.
2. Non-audit services undertaken by the external auditor create actual and/or perceived self-review, self-interest or advocacy threats to the independence of the external auditor. The degree of the threat depends on the nature, scale and scope of the non-audit services.
3. In relation to the provision of non-audit services, the term external auditor shall be interpreted as meaning the external auditor and any of its affiliates. The term affiliates will be interpreted by reference to the substance of a relationship with the audit firm but will generally include any entity controlled by the audit firm or under common control, ownership or management.

² Ibid, 204.2.

4. The external auditor may be engaged to provide non-audit services where there are good reasons and the services to be provided do not create a material threat to the independence of the external auditor. Good reasons for the external auditor to be appointed to perform non-audit services include:
 - a. It is economical in terms of skill and effort for the external auditor to provide such services as a result of his or her intimate and specialised knowledge of the business
 - b. The information required is a by-product of the audit process
 - c. The services are required by legislation or regulation
5. Certain categories of non-audit services are considered to be potentially incompatible with the independence of the external auditor and should normally be avoided. These categories include:
 - a. Performance of management functions or making management decisions
 - b. Financial statement preparation services and bookkeeping services
 - c. Valuation services
 - d. Actuarial services
 - e. Designing or implementing a hardware or software system
 - f. Designing or implementing internal controls over financial reporting
 - g. Legal services
 - h. Recruiting services
 - i. Certain corporate finance activities that create an unacceptable advocacy or self-review threat including making investment decisions or having custody of assets such as securities
6. A proposal by Northern Health management to engage the external auditor for any services in the categories set-out in #5 above must be approved in advance by the Committee. In the review of such proposals the Committee will, where further detailed guidance is considered necessary, refer to standards and guidelines issued by CPA Canada and CPA British Columbia.
7. Except for those services set out in #5 above, management may arrange the provision of non-audit services by the external auditor provided that:
 - a. A formal procurement is followed in accordance with NH procurement policies
 - b. The costs of such services do not exceed an amount equal to 25% of the regular external audit fee for the year as approved by the Board
 - c. The costs of the service to be provided, combined with the cost of any other non-audit or internal audit services provided by the external auditor in the same year do not exceed an amount equal to 50% of the regular audit fee

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- d. All such services are reported to the Committee at the next scheduled meeting along with the reasons therefore
 - e. Any proposal to engage the external auditor for the provision of non-audit services, the costs of which will exceed the limits set out in 7(b) and (c), must have the prior approval of the Committee. Where the need for such services is time sensitive, the CFO may request the Chair of the Committee to convene a special meeting of the Committee.
8. Taxation services comprise a broad range of services, including compliance, planning, provision of formal taxation opinions and assistance in the resolution of tax disputes. Such assignments are generally not seen to create threats to external auditor independence.

HIRING OF EXTERNAL AUDIT STAFF

1. Any individual that was employed by the external audit firm and participated in the external audit within the last three months will not be hired to a position at the Regional Director level or above.

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