

The Regents of the University of California

COMMITTEE ON AUDIT

July 16, 1999

The Committee on Audit met on the above date at UCSF-Laurel Heights, San Francisco.

Members present: Regents Davies, Parsky, Taylor, and Vining

In attendance: Regents Atkinson, Connerly, Hopkinson, O. Johnson, S. Johnson, Kozberg, Lansing, Lee, Montoya, Pannor, and Preuss, Regent-designate Kohn, Faculty Representatives Coleman and Dorr, Secretary Trivette, General Counsel Holst, Treasurer Small, Provost King, Senior Vice President Kennedy, Vice Presidents Broome, Gomes, Gurtner, and Hopper, Chancellors Berdahl, Bishop, Carnesale, Greenwood, and Vanderhoef, Chancellor-designate Tomlinson-Keasey, University Auditor Reed, and Recording Secretary Nietfeld

The meeting convened in Closed Session at 8:40 a.m with Committee Chair Vining presiding.

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The Committee went into Open Session at 9:40 a.m.

The Regents were informed that, due to the lack of a quorum, the meeting would be held as a briefing for the Regents present.

INVESTIGATION OF FINANCIAL DISCREPANCIES, SAN FRANCISCO CAMPUS

Committee Chair Vining reported that all matters directly related to the investigation, including personnel matters, recovery efforts, and criminal or civil litigation prospects, were discussed in the closed session meeting of the Committee. Specific internal control issues that allowed the embezzlement to occur and to go undetected, as well as the corrective actions taken or planned, were also covered in the closed session.

It will be necessary to be cautious in the open session in order not to influence the investigation that is currently in progress. The Committee will be permitted to discuss the historical situation at UCSF, the current situation, and any systemwide implications of the internal control issues that were brought up by the investigation at UCSF.

Chancellor Bishop reported that the financial discrepancies which have been uncovered could have occurred only due to inexcusable failures of performance within the campus' financial system. He noted that he had followed the investigation closely and that he would personally review all proposals for disciplinary action. Steps will be taken to ensure that such a fraud can never again occur at UCSF.

Vice Chancellor Barclay informed the Regents that an ongoing investigation at UCSF has determined that the campus has suffered a cash loss in the amount of approximately \$4.5 million. The loss was discovered in May, following an extensive review by accounting staff and outside auditors in response to a fiscal 1997-98 year-end audit report from the University's external auditors, Deloitte & Touche. The auditors' report had noted that campus depository bank statements had not been reconciled in a timely fashion nor reviewed by an appropriate level of management. Upon learning of the loss, the campus took immediate corrective actions. Because of ongoing investigations, these actions cannot be described in detail; however, over one dozen actions have been taken to strengthen controls and procedures and to provide adequate management oversight. Mr. Barclay assured the Regents that University assets are now secure. He stressed that the loss has no connection with losses suffered by UCSF Stanford Health Care.

Vice Chancellor Barclay announced that the position of campus controller had been offered to a Certified Public Accountant who serves as the controller at a major research university. With the support of Vice President Broome, the campus will conduct a comprehensive review of financial management to correct any other internal control deficiencies that might exist. Training efforts will be increased, building on the successful systemwide Business Officers Training Program, with special emphasis on internal controls. Vice Chancellor Barclay assured that Regents that there would be serious consequences for the individuals associated with this matter.

University Auditor Reed reported that his role is to assure that similar situations do not exist at other campus locations. He and Vice President Broome have separately communicated with the directors of internal audit and with the campus controllers regarding this matter. He has assessed all of the local audit programs' recent coverage of cash-handling operations and cash reconciliations and inquired into audit efforts to verify the corrective action taken in response to recommendations made by Deloitte & Touche in its 1998 management letter. Mr. Reed reported that he was satisfied that the University's cash and account reconciliation audit activities elsewhere have been adequate. He noted that while the University's policies and procedures are being complied with elsewhere in the system, such compliance will be improved through the sharing of information about the UCSF situation. There are certain locations, however, where current audit efforts are needed in these areas, and he will ensure that supplemental audits are added in the near term to the internal audit plan that was approved by the Board in June. In addition, each audit director has been asked to work with the controllers to ensure that the University's policies for cash handling are being complied with and that all balance-sheet accounts are clearly assigned to appropriate personnel and are reconciled in a timely manner. Mr. Reed stated that he would review the University's risk-assessment process to assure that appropriate risk is recognized in these areas and that appropriate weight is given to the need for more prudent audit coverage.

Vice President Broome reported that, as indicated by University Auditor Reed, she has had extensive discussions with the campus controllers, all of whom have reviewed the cashiering function and the related general accounting practices. The controllers did not find any violations of control. The administration is committed to performing a more extensive review of this function. Ms. Broome recalled that approximately two years ago the administration undertook a control initiative. Prior to that time, the campuses did not

have a controller position. At present there is a controller in place on each campus, with the exception of UCSF. A major initiative for the controller has been to conduct a control self-assessment.

Regent Preuss requested that Ms. Broome present a report in the near future indicating the degree of any similar weaknesses on the other campuses. Vice President Broome agreed to present a status report at the September meeting.

In response to a question from Regent Hopkinson, Vice President Broome stated that a complete control review of the San Francisco campus would be appropriate. University Auditor Reed added that, in addition to the report on the investigation, there will be a detailed audit report that will address the internal audit control weaknesses at the San Francisco campus. The overall review will also address such cashing issues as surveillance cameras. Regent Hopkinson asked that this report also be presented at the September meeting.

At President Atkinson's request, Vice President Broome gave a brief description of the controller position, recalling that several years before it had become evident to Senior Vice President Kennedy that there was no single individual who was responsible for internal controls on a campus. The controller position has a solid-line reporting responsibility to the vice chancellor for administration and a dotted-line reporting responsibility to the Vice President for Financial Management. The administration has developed a model which is in use at each campus to assess the control environment, which represents a significant undertaking on large campuses such as UC San Diego, where it could take as many as five years to cover the entire campus. She noted that there are approximately 3,000 separate businesses at the University of California.

Regent Hopkinson commented that the University should vigorously pursue those individuals responsible for the fraud and encourage the district attorney to move forward rapidly. Chairman Davies agreed, noting that the Regents' outrage at the events must be expressed through cooperation with the district attorney's office. He observed that the Regents look forward to charges being brought, consistent with the rights of the suspects.

Regent Taylor requested that the administration report on the University's procedures with respect to records retention and what steps might need to be taken to ensure that policies are being followed.

In response to a question from Regent Lee regarding loss recovery, Vice President Broome explained that the University had notified its insurance carrier of the investigation. A claim will be filed once the investigation has been completed. University Auditor Reed added that an attempt has been made to identify the use of the funds and any assets that may constitute restitution. The University has a \$300,000 deductible in its insurance policy.

The meeting adjourned at 10:00 a.m.

Attest:

AUDIT

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Secretary