

The Regents of the University of California

**COMPLIANCE AND AUDIT COMMITTEE**

November 16, 2016

The Compliance and Audit Committee met on the above date at UCSF–Mission Bay Conference Center, San Francisco.

Members Present: Regents Brody, De La Peña, Elliott, Makarechian, Pérez, Sherman, and Zettel; Advisory members Chalfant and Monge; Chancellor Gillman; Staff Advisory Valdry; Expert Financial Advisor Juline

In attendance: Secretary and Chief of Staff Shaw, General Counsel Robinson, Chief Compliance and Audit Officer Vacca, Executive Vice President and Chief Financial Officer Brostrom, Executive Vice President and Chief Operating Officer Nava, and Recording Secretary Johns

The meeting convened at 1:35 p.m. with Committee Chair Zettel presiding.

1. **APPROVAL OF MINUTES OF PREVIOUS MEETING**

Upon motion duly made and seconded, the minutes of the meeting of September 14, 2016 were approved.

2. **ANNUAL REPORT ON INTERNAL AUDIT ACTIVITIES 2015-16**

[Background material was provided to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Deputy Audit Officer Matthew Hicks briefly mentioned certain key points of the Annual Report on Internal Audit Activities for 2015-16. The Internal Audit program identified no material deficiencies in internal controls related to financial matters, and no circumstances in which the program would feel that management was accepting an unreasonable level of risk. In key measures of productivity, compared to the prior year, the Internal Audit program had matched or improved on its performance. There was a slight decrease in the number of training hours per auditor, which might be the result of pursuing more targeted training, such as webinars, rather than conferences and full-day training.

Mr. Hicks presented a chart showing the most significant Internal Audit issues over a five-year period. Three issues had remained consistently important during this time: information technology security and information privacy, research compliance, and large-scale system implementations. The University was in the midst of a systemwide cyber security risk assessment. The results of this assessment would determine future targeted cyber security efforts.

Regent Pérez requested clarification of two other issues listed on this chart, “financial monitoring” and “general ledger/transaction review.” He recalled that many Regents had been surprised to learn of the structural deficit at UC Berkeley. He asked in which of these two categories this deficit would be placed. Mr. Hicks responded that the category of “financial monitoring” concerned broad-based systems of accountability. The Internal Audit program was moving its focus in this direction, whereas in the past it had focused more on targeted reviews of individual departments or units.

Regent Pérez asked about the status of financial monitoring as a priority in 2012-13 and 2013-14, and how the University might do a better job of capturing and analyzing campus data in order to be aware of looming problems. Mr. Hicks responded that the Internal Audit program has a focus on broad-based data analytics and ongoing monitoring. Chief Compliance and Audit Officer Vacca expressed the hope that the new focus on broad-based financial monitoring would identify situations like this in a timely manner. In the case of UC Berkeley, individual symptoms had been noticed, but not the harmful effect that a combination of symptoms would have.

Mr. Hicks provided examples of topics of concern for the Internal Audit program in research compliance and large-scale system implementations. Another issue listed on the chart was “affiliations, joint ventures, and partnerships,” and it was particularly relevant for the health sciences. He then presented a chart displaying the program’s effort distribution by area. Over half of Internal Audit’s time was spent in four areas: health sciences operations, financial management, information management and technology, and academic units and programs. The overall distribution of effort remained similar to the previous year, with some increase in activity in information technology, and in student affairs, in such areas as financial aid, admissions, and student fees.

Regent Makarechian requested an estimate of the cost per hour of the Internal Audit program’s activities. Ms. Vacca responded that this information could be provided.

Regent Pérez reiterated his concern about the structural deficit at UC Berkeley and expressed concern about audits of the Office of the President to be undertaken by the State Auditor. He stressed that the Board of Regents should be informed about State audit findings and the University’s responses before these become public. General Counsel Robinson responded that the statutory provisions pertaining to this last matter were ambiguous. In conversations with the State Auditor’s office, the University was informed that the State Auditor’s view was that the UC administration should not discuss the results of a State audit with the Board of Regents until the draft of the audit is produced. Ms. Vacca noted that there is only a short time period, five days, between the issuance of the draft audit and the final audit report. Mr. Robinson affirmed his view that there were arguments to support providing the Board of Regents with briefings on State audits as Regent Pérez was suggesting. The position of the State Auditor was that Board members could be briefed in offline discussions with less than a quorum.

Committee Chair Zettel asked if it would be possible for the Regents to convene special meetings for such briefings, in closed or open session. Mr. Robinson responded that the

State Auditor's position is that the law precludes any public discussion of a State audit prior to publication of the final audit report, and that any discussion of the draft audit can only take place after the draft has been produced.

Chancellor Gillman articulated the important question of whether the Compliance and Audit Committee should be informed about or exercise some kind of review regarding State audit activity at the University before audit information is passed on to the State. He expressed concern about governance issues, and about the possibility that the State audit process would not have the benefit of good judgments the Committee might provide about relaying information properly. Chancellor Gillman referred to the matter of the structural deficit at UC Berkeley and how the University would become aware of such situations. Many individuals on campus and at the Office of the President are responsible for the financial well-being of the campuses. He asked if the University's audit function was designed to monitor overall campus financial well-being, and how this compared to the responsibility of executive vice chancellors and chancellors. Ms. Vacca responded that controller positions in campus financial offices carry out ongoing monitoring. The audit function verifies that this work is taking place, but might not identify an issue if it is not raised as a risk issue by one of these controllers. Chancellor Gillman stated his view that the audit function was not the central function for identifying large-scale issues like the deficit at UC Berkeley, although Internal Audit plays an important role. Regent Makarechian emphasized that greater clarity in UC's financial statements and reports might help auditors and others identify problems like this.

Mr. Hicks then concluded his presentation with information on Management Corrective Actions (MCAs). There had been a 67 percent decrease in the number of outstanding MCAs over the previous seven years.

Staff Advisor Valdry reflected on the cost of compliance versus the cost of risk, and the question of whether certain training, such as cyber security training, is right and appropriate for specific faculty, staff, and student roles. He asked if there had been progress in monitoring these costs. Ms. Vacca responded that the Office of Ethics, Compliance and Audit Services had formed an education committee that would develop outcome measures. Mr. Robinson observed that the cost of risk is not entirely financial; some risk is reputational.

### 3. **ANNUAL REPORT OF EXTERNAL AUDITORS FOR THE YEAR ENDED JUNE 30, 2016**

[Background material was provided to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

PricewaterhouseCoopers (PwC) representative Michael Schini recalled that PwC had been engaged by UC late in the year, and that this had been challenging. He reported that PwC had completed its audits on time. PwC had detected no unrecorded adjustments or fraud. There were no disagreements with management. For 2015 there was a balance sheet reclassification of over \$500 million, but this would not affect 2016. The

Governmental Accounting Standards Board (GASB) introduced seven new accounting standards in the current year, and two of them were significant for the University. As part of implementing one of the new GASB Statements, the University now reports the Children's Hospital and Research Center Oakland blended with UCSF, whereas UC previously reported this as a discreet component unit; the other Statement concerned fair value disclosures for investments. The main area of concern in PwC's internal control report to the Regents, or Management Letter, was information technology security, in particular access to systems and segregation of duties. Management had been receptive to PwC's comments.

Committee Chair Zettel referred to the recent hiring of a director for cyber security and expressed the hope that the University's response to information technology security issues would become more robust.

#### 4. **UPDATE ON TRAVEL ABROAD SECURITY AND RESPONSE PROGRAM**

[Background material was provided to Regents in advance of the meeting, and a copy is on file in the Office of the Secretary and Chief of Staff.]

Chief Risk Officer Cheryl Lloyd explained that UC purchases an insurance policy through Chubb insurance for its travel abroad security and response program. Chubb subcontracts with two vendors: UnitedHealthcare Global, which responds to non-security-related issues, such as medical evacuation, and iJET, which provides pre-trip security analysis and security response. Following terrorist attacks in Paris, France in November 2015 and at the Brussels, Belgium airport in March 2016, the University was quickly able to track down students in those locations and ensure that they were safe. UC also responded to terrorist incidents in July 2016 in Bangladesh and in Nice, France, and to the death of a postdoctoral scholar in Ethiopia in October 2016.

UC provides travel risk assessment predictive intelligence tools and training to travelers. There is an online training tool specifically for UC Education Abroad Program travelers, including tools for addressing loneliness and depression. Ms. Lloyd reviewed the diverse categories of UC student, faculty, and staff travelers and their programs and projects, such as field researchers carrying out non-invasive observation study of primate populations in Indonesia. iJET can provide dedicated security assessments for regions of particular concern or risk, such as Afghanistan or Pakistan, including a pre-planned evacuation process. The UC Education Abroad Program is extensive. In 2015-16, there were about 5,700 participants in 43 countries, at more than 120 institutions. Death can occur when one travels abroad. However, out of 73 million U.S. travelers abroad in 2015, the rate of death was about 0.001 percent, based on statistics from the U.S. Department of State. UC tries to ensure that its travelers are risk-aware.

Regent Sherman asked if UC travelers carry tracking devices or if they would agree to such an arrangement. Ms. Lloyd responded that iJET had this capability, and that it had been tested by UC Davis travelers in Afghanistan. Whether travelers would agree to use this capability was another matter.

The meeting adjourned at 2:25 p.m.

Attest:

Secretary and Chief of Staff