The Regents of the University of California

COMMITTEE ON AUDIT
December 17, 2007

The Committee on Audit met on the above date at the Office of the President, 1111 Franklin Street, room 11326, Oakland.

Members present:	Regents Allen, Bugay, De La Peña, Lozano, Ruiz, Schilling, and Varner; Advisory member Croughan; Expert Financial Advisor Vining
In attendance:	Associate Secretary Shaw, Chief Compliance and Audit Officer Vacca, University Counsel Thomas, Vice President Broome, University Auditor Reed, and Recording Secretary Johns

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

1. **PUBLIC COMMENT PERIOD**

There were no speakers wishing to address the Regents.

2. **ADVISORY POSITIONS TO THE AUDIT COMMITTEE – FINANCE AND COMPLIANCE**

Committee Chair Ruiz informed the Committee that the search for the advisory positions to the Committee, for an Expert Financial Advisor and a Compliance Advisor, is still in process and names are being gathered. He requested recommendations from Committee members and noted that this search is not easy.

Senior Vice President Vacca observed that the Compliance Advisor position is new. She stated that several potential candidates are now being considered and that she anticipates bringing names forward at the next meeting. She opined that it will be more difficult to fill the Expert Financial Advisor position, to find someone who can appropriately replace Expert Financial Advisor Vining. She also solicited nominations of potential candidates.

Committee Chair Ruiz stated that the participation of alumni is preferred but that the positions are open to qualified individuals. He repeated his request for names of candidates. Regent Bugay asked if the timeline for filling the Expert Financial Advisor position will extend through June. Committee Chair Ruiz responded that he has asked Mr. Vining to be available until his position is filled. Mr. Vining confirmed that he will continue to serve until then. Mr. Vining suggested that an appointment could be made by June and noted that he plans to participate in one or two more meetings together with his successor, to pass on information and knowledge. He stated his wish to be involved in the October review of UC financial statements. Mr. Vining observed that even a financial expert may not be familiar with both Governmental Accounting Standards Board (GASB) standards and Financial Accounting Standards Board (FASB) standards, or be familiar with the requirements for UC medical center financial statements. He believed it would be wise for him to remain available during the first cycle of financial statement review.

University Auditor Reed opined that the compliance advisory position should ideally be filled by March, in conformance with the audit cycle. He recalled the audit process, noting that the external auditors will present annual audit plans at the March meeting, while the internal auditors will present their plans in May. The advisor should be involved at the beginning of the cycle.

3. **COMPLIANCE PROGRAM UPDATE AND EDUCATION**

Chief Compliance and Audit Officer Vacca began her presentation by emphasizing the importance of a common frame of reference in the development of the compliance and ethics program. She referred to the recent ethics training required for UC employees and proposed that ethics will now be integrated into UC's compliance program, with ongoing, integrated training. She emphasized that ethics will continue to be a focus and taken into consideration in the development of UC's compliance program.

Next she discussed the regulatory compliance drivers which are the impetus behind compliance program development and account for the nature of the program framework. Many people are familiar with the Sarbanes-Oxley Act, especially its Section 404 regarding internal controls implementation, and some of its other governance and accountability elements. She observed that Sarbanes-Oxley came "after the fact" and reinforced legal compliance requirements. Ms. Vacca also mentioned the governance standards for companies listed in the New York Stock Exchange and the NASDAQ Marketplace Rules.

Of all these regulatory compliance drivers, Ms. Vacca identified the Federal Sentencing Guidelines as most important to the University. She informed the Committee that she will use the Federal Sentencing Guidelines as a background because these Guidelines are accepted across all industries and widely recognized as a standard framework for compliance programs. Several elements of the Guidelines are also found in other regulatory drivers.

Other governmental agencies also serve as regulatory drivers. Ms. Vacca called attention to revised Federal Acquisition Regulations that stipulate that contractors with federal contracts of more than $5 million must have certain compliance and internal control elements in place. She cited this as an impetus for the University to develop its program with a standard recognized across the system. She noted the many enforcement activities related to compliance already occurring in the

University which concern government and management accountability and ensure that proper references and resources are available to employees.

The evolution of corporate governance related to compliance programs has developed in line with regulatory drivers. Ms. Vacca emphasized the crucial role of governance accountability. She stressed the need for the Committee's involvement and oversight in helping to enforce UC management oversight of enforcement activities to ensure that UC is a compliant organization.

Next Ms. Vacca turned to the seven elements of an effective compliance program, as identified in the Federal Sentencing Guidelines. The first element, standards and procedures, includes such issues as the business code of conduct, the academic code of conduct, and basic principles of conduct. For the University, many different items belong to the category of standards and procedures.

Regent Allen requested clarification of the meaning of the Federal Sentencing Guidelines. Ms. Vacca explained that the Guidelines were developed in 1991 to provide a standard of culpability for crimes, help determine appropriate penalties, and consider what factors might raise or lower culpability scores. Regent Allen asked whether this is a determination of culpability or the severity of a crime. Regent Schilling clarified that the Guidelines apply to sentencing by a judge after conviction and take into account factors such as the amount of money involved in a crime. She stated that there is no bargaining involved.

In response to Regent Allen's question, Ms. Vacca explained that UC is incorporating these seven elements from the Federal Sentencing Guidelines because they are the only existing standard or framework recognized across industries, in business, healthcare, defense, and research. In some cases compliance programs are mandated, but these programs use the seven elements as a guide. University Auditor Reed observed that when corporations are found guilty of violating federal laws, the presence of a compliance program can be a mitigating factor in determining the severity of the crime.

Committee Chair Ruiz pointed out that the issues raised by the implementation of a compliance program have always been relevant to the University. The current implementation effort simply reinforces their importance. Mr. Reed noted the absence of such guidelines in the professional literature or in laws and regulations and described the Federal Sentencing Guidelines as the "gold standard" for identifying the essential elements of compliance programs. Ms. Vacca added that the Guidelines do not provide direction on how elements are to be implemented, but recognize that an organization is making a good faith effort to be compliant if these elements are in place. University Counsel Thomas observed that Chapter Eight of the Guidelines concerns corporations and criminal conduct, and nonprofits like the University are not exempt from such guidelines.

Returning to the standards and procedures element, Ms. Vacca commented on the complex and extensive structure of the University, with its many campuses and other locations. The first step in approaching this large development task will be an inventory of current UC activities surrounding key risk elements. The Compliance Office will attempt to leverage existing activities and create a funnel of communication regarding these different activities.

Ms. Vacca briefly discussed the remaining elements from the Federal Sentencing Guidelines. She opined that the second element, oversight and leadership, relates to her appointment and role at UC. She stated that her reporting structure, directly to the highest level, the Regents, is critical in developing an effective compliance program, and that this has been demonstrated in different industries.

The third element, screening and delegation, refers to screening of agents of the University and appropriate delegation of authority. The fourth element, education and training, is well developed systemwide. These activities should be maximized and focused around key risks. The fifth element is represented by the auditing, monitoring and reporting mechanisms. Ms. Vacca referred to the whistleblower hotline and the ongoing audit program. She noted that the University does not have monitoring mechanisms in all areas and that an inventory will be critical. She identified the sixth element, corrective action, enforcement and discipline, as the crux of the whole program. She emphasized the importance of resolving gaps in controls and ensuring accountability for this. The program will not be effective in ensuring standards without appropriate corrective action and discipline. The seventh element is periodic risk assessment.

Vice President Broome asked if all the varied risk assessments carried out systemwide are being taken into account. Ms. Vacca replied affirmatively. She observed that many different UC functions have performed risk assessments and expressed her intention to leverage this information in order to narrow these categories down to four or five key risk areas for UC. She identified research as one of the principal risk areas. Based on her campus visits, Ms. Vacca reported that many campuses identify research as an area with need for processes and controls, and she stressed that this area needs strong focus. Ms. Vacca told the Committee she will present key identified risk areas at the March 2008 meeting, as well as the results of the planned inventory.

As an example of an inventory activity, Ms. Vacca noted UCSF's program on conflict of interest. This program could be leveraged, maximized, and made available to others. In this manner, model policies from across the system could be used as model templates to close the gaps in risk controls. She observed that training is fragmented systemwide, with different levels of awareness among units and departments. As her last goal, Ms. Vacca mentioned the development of a regulatory compliance model which she anticipated presenting at the March meeting. This will include the findings of the systemwide inventory, identified gaps, and a plan for moving forward for the systemwide compliance and ethics program. She stressed the need for communication and feedback from the Committee.

Ms. Vacca acknowledged the existing UC controls initiative, and that controllers are aware of risks. She described her effort as aimed at mutual integration rather than superimposing a model on existing procedures. She noted that she has met with Faculty Representatives Croughan and Brown and will continue to ensure that she is in communication with the academic side of UC.

Compliance programs have been shown to achieve certain outcomes. She noted that these outcomes are often measured less in decreases in penalties or litigation than in changes in organizational culture, accountability, and governance. The focus of UC's program will be on employee awareness of compliance and ethics, understanding of laws, regulations, and individual accountability. The University should expect a decrease in incidents of noncompliance and reductions in fines and penalties as UC becomes more compliant. Another measure of the effectiveness of such a program is that, as new UC initiatives are developed, the Compliance Office is proactively engaged when relevant compliance and ethics issues are involved in these initiatives.

Ms. Vacca again referred to the revised Federal Acquisition Regulations regarding contractors with federal contracts of more than $5 million and stressed that it is critical for UC to move with speed to integrate its overall efforts and present one systemwide model with the essential elements in place.

Committee Chair Ruiz observed that the compliance program was not in the UC budget plan for this year. He asked about plans for program funding. Ms. Vacca replied that she has spoken with Executive Vice President Lapp about a proposed budget for the compliance program. Core staffing needs have been identified. Ms. Vacca expressed the hope to have a deputy position in place by January 2008, to assist with program development and implementation. She anticipated several other positions in the Compliance Office related to implementation, analysis, education, and investigations. The plan for staffing will be presented at the March meeting.

Committee Chair Ruiz remarked that a reduction in fines and penalties and a decrease in incidents of noncompliance might be the greatest result or return on investment for a strong compliance program. He asked if there are concrete measures or specific goals for the program to measure its effectiveness. PricewaterhouseCoopers Lead Partner Joan Murphy observed that some metric would be desirable; she reported that her firm would measure this in terms of reduced litigation costs. Ms. Vacca noted that a new compliance program will bring about increased employee awareness and, in the first year, a likely increase in the number of penalties as employees start to report. She cited this as an example of the "Hawthorne effect." After an initial spike in the first year the number of penalties should decrease. She stressed the difficulty of using fines and penalties resulting from litigation as a benchmark of program effectiveness, and that they should not be used as the only such measure. Vice President Broome concurred, citing a similar rise in numbers of incidents when the risk management program introduced central processing of all property claims, with an eventual decrease in numbers because of the new emphasis and awareness. Ms. Vacca described the program as a diagnostic, preventive effort and compared it to medical diagnostic efforts to detect cancer.

Mr. Reed observed that there is not a reporting mechanism in every compliance area for benchmarking information. As an example, he noted that he cannot state precisely how many federal research dollars the University returned to federal agencies last year when it was discovered that funds were not spent in accordance with a grant or program. If there is no mechanism for capturing those numbers, it will be difficult to benchmark a decline.

University Counsel Thomas reported that the Office of the General Counsel is keeping track of its settlements with the federal government involving investigations by the Office of the Inspector General, fines, or paybacks of federal research dollars.

Committee Chair Ruiz stressed the importance to the University of identifying areas where it will benefit from having an excellent compliance program. He recalled that the Regents were originally responsible for implementing this program and that there were specific concerns which had led them to do so. He stated that the Regents are justified in expecting some kind of feedback on how this program will benefit UC, not only in monetary terms, but in reduction of significant issues.

Ms. Thomas referred to the new Federal Acquisition Regulations, noting that one of their features is the development and maintenance of a database on contract compliance. She emphasized that compliance is important not just for cost savings, but for enhancing the University’s reputation as an ethical recipient of federal research money.

Ms. Vacca observed that the effectiveness of some compliance elements is manifested in process rather than outcome and that in some cases the presence of an effective element itself serves as a measure. She anticipated that there will be direct measurable results in the first year in the area of compensation, where the Compliance Office is actively ensuring that appropriate monitors and controls will be in place. The compliance program will focus on process indicators as well as risks.

4. **LAWRENCE BERKELEY NATIONAL LABORATORY INTERNAL AUDIT PRESENTATION**

University Auditor Reed introduced Mr. Terrence (Terry) Hamilton, Manager of Internal Audit Services at Lawrence Berkeley National Laboratory (LBNL). He recalled that presentations to the Committee by campus and location audit programs are a new development, begun at the September 2007 meeting with presentations on the UCLA and UCB audit programs. This presentation on LBNL is a continuation of this plan.

Mr. Reed reviewed the change in the University's audit relationship to all three national laboratories in the last year and a half. When the Los Alamos and Livermore laboratories became part of limited liability companies (LLCs) managed by UC and its partners, the internal audit programs became part of the LLCs, and their employees are no longer UC employees. The audit programs of those laboratories are part of the Bechtel organization. They no longer report to the Office of the President, and information from their programs is no longer included in the UC quarterly report on Internal Audit activities. However, the University maintains a relationship with these audit programs. Mr. Reed informed the Committee that he and Vice President Broome serve on the audit committees of both LLCs. LBNL is still part of UC, like the campuses.

Mr. Hamilton began by noting that LBNL recently celebrated its 75^{th} anniversary at its location above the Berkeley campus, a 200-acre site. He reported that by the end of 2008, LBNL will begin moving several hundred administrative staff members from downtown Berkeley up to the site, bringing all administrative staff together in one place. This measure will result in cost savings, since LBNL will no longer lease buildings in downtown Berkeley, and effectiveness, since staff will be closer to the scientists they support.

Regent Schilling asked if any staff will be left in downtown Berkeley. Mr. Hamilton responded in the negative. He noted that there are scientific offsite locations in Oakland and Walnut Creek, and a new site being developed in Emeryville.

The Laboratory's staff of over 7,000 is broken down into 3,600 full time staff and about 3,400 participating guests involved in scientific research, who may stay at LBNL from one week to a few years. Scientists, engineers, faculty, students, and research staff make up 85 percent of the total staff; only a relatively small percentage, 15 percent, are administrative support staff. The Laboratory is proud of its eleven Nobel Laureates and its six members who recently shared the Nobel Peace Prize received by Al Gore for work on climate change. The size of LBNL's annual budget, $516 million, places it between those of UCSB and UCSC, and is equivalent to about one-third of the UCB budget.

Next Mr. Hamilton turned to LBNL's mission. He noted that Director Chu has updated the Laboratory's mission and put his own stamp on it in many ways. The mission focuses on solving pressing scientific problems, especially those related to the future of energy, building leading scientific facilities, and training the next generation of scientists and engineers. As a result of Mr. Chu's efforts, several construction projects are now under way, and there has been a new emphasis on safety, which is now built into the Laboratory's mission statement.

Mr. Hamilton presented a breakdown of the LBNL budget, noting that one large segment, $42 million, was devoted to work performed for the National Institutes of Health (NIH), and that in general the Laboratory's work is divided among a wide variety of programs.

Regent Allen asked about the Yucca Mountain operation. Mr. Hamilton explained that this is a nuclear waste storage project, a consortium of several groups, including UC and Sandia National Laboratories. The University exercises an oversight and scientific role. LBNL scientists have studied water permeability at the site, located in Nevada.

Ms. Thomas pointed to the percentage of the budget devoted to the category of non-Department of Energy (DOE) "Work for Others." She asked if this includes federal agencies and private industry. Mr. Hamilton responded that the largest part of this percentage is made up of projects undertaken for other universities. There is some work done for the private sector as well. As an example, he noted that Intel has used LBNL's Advanced Light Source in the development of computer chips.

Committee Chair Ruiz asked if the British Petroleum grant for the Energy Biosciences Institute is part of the current budget or the 2008 budget. Mr. Hamilton replied that the BP grant will begin with the fiscal year 2008 budget.

Next Mr. Hamilton discussed the organization of the LBNL Internal Audit department. There are seven full time employees including him, four auditors, one investigator, and one administrative staff member. He emphasized that this is a highly experienced staff, with CPAs, MBAs, and certified internal auditors. The staff is very well regarded for its audits and advisory services. The Internal Audit function reports both to Laboratory Director Chu and to University Auditor Reed. The Laboratory Director is also Chair of the LBNL Audit Committee. Mr. Hamilton stressed Director Chu's active interest and involvement in the follow-up of audit recommendations. The Audit Committee includes the heads of every major operating function at LBNL, with the exception of the Environment, Health and Safety division, and two scientific division directors.

Mr. Hamilton outlined the focus of LBNL Internal Audit activity. He enumerated risk-based audits, including a core audit program to evaluate compliance and controls; efforts to identify process improvements, which have produced significant cost savings in recent years; and an annual cost allowability audit required and reviewed by DOE. Mr. Hamilton underscored the importance and complexity of the cost allowability audit, which takes twice as long to perform as other audits, up to 800 hours per year. Mr. Hamilton noted that during his term as Audit Director since 1998, DOE has never changed or challenged LBNL's cost allowability audit, while it has rejected cost allowability audits at other sites. In response to Regent Allen's question, he explained that the audit examines LBNL expenditures to determine if any were not allowed by DOE or if the expenditures were made for a purpose not in the contract.

Next Mr. Hamilton outlined performance measures established for LBNL Internal Audit in DOE Contract 31. The performance of LBNL Internal Audit contributes to the LBNL business systems score and the overall Laboratory score, which determines whether UC needs to rebid its contract with DOE. The University could be forced to rebid this contract if a minimum score is not achieved. The performance measures include the expectation that Internal Audit will develop documentable cost savings methods, maintain professional certifications for its staff, and complete 100 percent of its audit plan, while the campuses are expected to complete only 70 percent. In addition, LBNL Internal Audit uses a customer feedback survey system for every audit. As a best practice, this procedure is being considered for wider implementation at UC.

Mr. Hamilton noted that Internal Audit received a score of A+ last year from DOE; this year, the University has submitted an A+ score to DOE, and DOE is in the process of reviewing this score. Mr. Reed observed that this score, first formulated by UC and then submitted to DOE, is based on many factors and is an honest assessment.

Mr. Hamilton reported on a value-added review carried out at LBNL in response to U.S. Office of Management and Budget (OMB) Circular A-123, which corresponds to Sarbanes-Oxley and concerns requirements for internal financial controls in federal agencies. This was an extensive inventory of controls and evaluation of risks that took over two years, approximately 1,600 hours, and identified almost 1,000 risk areas. He noted that other DOE sites called in outside consultants to perform this review, thus missing an opportunity to examine and better understand their controls. LBNL Internal Audit led training programs in internal controls and worked with department heads to educate employees about controls. Mr. Hamilton highlighted the result that LBNL is now in a better position than if an outside consultant had been brought in to perform this review.

Ms. Vacca noted that gaps in controls were brought to the attention of management and asked if there is an ongoing review process, and how management is being held accountable. Mr. Hamilton informed the Committee that there is a relevant quarterly meeting chaired by the Chief Financial Officer, and efforts are now being focused on combining and improving controls. Two hundred hours have been budgeted for that effort this year. He opined that LBNL cannot continue to invest that amount of time in the future; the essential benefit has been achieved. LBNL is more knowledgeable about controls, and 1,000 controls are listed on the Audit website.

Vice President Broome emphasized that the national laboratories had a very limited time frame of about eight months to comply with the OMB Circular and that this was a difficult task. Mr. Hamilton surmised that this is what caused other sites to hire outside consultants. At LBNL, two full-time positions were devoted to this task.

Mr. Hamilton concluded by emphasizing the effectiveness of LBNL Internal Audit's efforts in the follow-up process. There were no overdue high risk findings in fiscal year 2007. During the same year, Internal Audit issued 100 recommendations and closed 110 recommendations, with slight changes to two recommendations. The audit team is highly experienced, trained, automated, and transparent. Ms. Vacca concurred and reported her perception that LBNL management is very much held accountable for follow-up actions.

Committee Chair Ruiz underscored the importance of Laboratory Director Chu's participation in all LBNL Audit Committee meetings and suggested that chancellors should become more involved at the campuses. Expert Financial Advisor Vining noted a change in the private sector over the last few years, in that the CEO and senior officers of a corporation are involved in the audit committee operations and follow-up; Director Chu appears to be doing this. Mr. Vining observed that if the CEO sets the agenda and high risk items are put on job descriptions or to-do lists which are checked by the CEO, things tend to get done. He believed that, on the campuses, the only chancellors who chair or sit in audit committee meetings are those at UCLA and UCB. He opined that the correct model shown by LBNL could be moved into all UC locations. If chancellors are not supportive of audit, compliance, and financial control efforts, the Regents will not see implementation of the compliance and controls they are seeking.

Vice President Broome concurred and added that the chancellors' involvement is important to ensure a broad scope and coverage by campus internal audit programs. Faculty Representative Croughan suggested that campus deans should also be involved because they more often represent a direct line of communication to faculty. Mr. Vining agreed, stating that a CEO or chancellor needs to be present as a figurehead to ensure appropriate attention and emphasis, but that participation by deans, provosts, and other campus senior management is essential to the success of this process.

Mr. Reed observed that the membership of audit committees varies from campus to campus. Depending on the campus, executive vice chancellors, provosts, or deans serve on these committees and are active contributing members.

Mr. Vining recognized the independence of the campuses, but suggested that UC could work toward building a successful model in this area. Ms. Vacca commented that the UC compliance and ethics model could provide recommendations for leadership involvement with audit committees. Committee Chair Ruiz affirmed that this is clearly a best practice that the University should implement. Mr. Vining recalled that this issue was discussed by many of the Regents who are not members of the Committee on Audit, during the search process for the Senior Vice President/Chief Compliance and Audit Officer.

Mr. Hamilton noted that Mr. James (Jim) Krupnick was recently added to the LBNL Audit Committee. Mr. Reed informed the Committee that, under the new LBNL contract, UC was obligated to establish a contract assurance function. At the Office of the President, Vice President Foley has a contract assurance council with members from Laboratory administration and Office of the President functional specialists, including Vice President Broome, Mr. Reed, Associate Vice President Boyette, and Ms. Vacca. This council meets monthly with Laboratory representatives about their compliance efforts, their contract assurance function, issues management processes, and specific events in the areas of health and safety. The council oversees the Laboratory’s self-assessment process and communications with DOE. All these measures work together to enhance UC’s active management of the Laboratory.

5. PRESENTATION ON INTERNAL AUDIT QUARTERLY REPORT

University Auditor Reed discussed highlights from the report on Internal Audit activities for the quarter ended September 30, 2007. He enumerated reasons for slowed execution of the fiscal year 2007-08 audit plan, including continuing staff shortages, high investigation volume, and carryover work. Major investigations of the quarter concerning the UCSD Preuss School and the UCD Food Stamp Nutrition Education Program have been closed out. The distribution of time devoted to Internal Audit activities was 67 percent to audits, 14 percent to advisory services, and 19 percent to investigations. Mr. Reed described this distribution as less than ideal and expressed his wish that Internal Audit spend more time on advisory services and less time on investigations. The percentage of time spent on investigations, 19 percent, is higher than desired by about five percent.

Mr. Reed noted that Internal Audit completed audits of the five health sciences compliance programs. This included a review of their annual reports, which will be presented to the Committee early next year. Next he updated the Committee on high risk, past due Management Corrective Actions. Management Corrective Actions are audit recommendations that are tracked to completion systemwide. Over 2,000 such recommendations are issued systemwide every year. There were 12 high risk, past due Management Corrective Actions outstanding as of June 30, 2007, and these had not been cleared by November. During the quarter, 31 new items aged into this category, producing a new total of 43 open high risk, past due items as of September 30. These are the items receiving the most attention.

Committee Chair Ruiz asked whether this number of past due items was a cause for serious concern. Mr. Reed responded that the items in question are receiving daily attention and that most are complex issues requiring a systemwide solution. In some cases this is due to the complexity of a training rollout, when dissemination on a campus has not been completed. He emphasized that Internal Audit does not consider an issue resolved until the corrective actions have been completely implemented. He believed that UC management takes the issues seriously and affirmed that there are legitimate reasons for the fact that some issues take longer to resolve than others.

Mr. Reed next discussed recent themes or trends. One such theme was the need for Principal Investigators to carry out their fiscal responsibilities for research activities, responsibilities that are acknowledged in agreements signed with the federal government or other sponsors. Frequently these responsibilities are delegated to financial or administrative assistants. In some cases such assistants have been given excessive authority, there has been too little oversight, and inappropriate purchases have been made. In a decentralized system like UC, which is reliant on controls by individuals rather than system controls, the role of the Principal Investigator is critical for the approval of invoices and purchase transactions. Principal Investigators must understand the importance of their authorization of the expenditure of federal funds. In response to a recently investigated matter at the Davis campus, the Chancellor promised that, as a corrective action, training would be developed by June 30 to give Principal Investigators a better understanding of their fiscal and administrative responsibilities. Mr. Reed cited this as an example of training that might be leveraged across the UC system, transferable to other locations, and an area of critical control where the University needs improvement.

Mr. Reed informed the Committee of newly instituted reporting capabilities. Beginning this quarter, Locally Designated Officials, who receive hotline calls and whistleblower reports at campuses and locations, have begun to submit quarterly reports to UCOP. Previously, UCOP was informed only about those campus and location audits that were handed off to Internal Audit, approximately one third of the total. This new reporting provides substantial new information on investigation activity beyond Internal Audit, most often involving Human Resources matters, discrimination, sexual harassment, and sometimes research misconduct. Internal Audit is currently aware of 240 open investigations systemwide and is processing this information on the sources and nature of complaints and the outcomes of investigations. Based on this first quarter report, Mr. Reed noted that whistleblower investigations that are handed off to Internal Audit are sustained in about forty to fifty percent of cases; whistleblower allegations investigated by Locally Designated Officials and their staffs are sustained at a lower rate, but often enough to demonstrate that the University must take whistleblower allegations seriously. The new information will be a basis for improved reporting to the Committee.

Current challenges include personnel turnover at the Audit Director level. The UCB Audit Director recently retired and, after a national search, the UCSB Audit Director was appointed there. Recruitment for a new Director at the Santa Barbara campus will begin soon. The Office of the President will help UCSB on an interim basis; an Associate Director from UCOP will serve as Acting Director at UCSB for three days weekly. The UCI Audit Director has departed to take a position at Stanford. Mr. Reed anticipated that recruitment for the new UCI Audit Director would be completed in another week or two, with the new Director beginning in January.

Mr. Reed briefly discussed current activity aiming at integration of the audit and compliance programs, including frequent discussions with Chief Compliance and Audit Officer Vacca about this integration of the two programs and how it will influence the risk assessment program and next year's audit plan. An important effort is the search for ways to merge risk assessment efforts with other activities. Ideally, the University will have one collective view of risk to drive its risk management, control, and audit programs and better align these efforts. Mr. Reed concluded by noting that this first quarter report does not yet reflect the integration of the audit and compliance programs.

Faculty Representative Croughan stressed the willingness of faculty to offer collaborative advice on compliance issues since faculty members are often the subject of trainings. She found it bothersome that 100 percent compliance on training has not been achieved, and that campuses which have had more problems with ethical standards are the ones with the lowest compliance rates. She emphasized the availability of faculty volunteers who would be happy to serve on task forces.

6. EXTERNAL AUDITOR

Committee Chair Ruiz raised the issue of the Committee's responsibility for appointing and evaluating external auditors.

Vice President Broome responded that PricewaterhouseCoopers has served as the University's auditor for six years. UC has engaged three audit firms during the past 13 years. She reported that in past customer satisfaction surveys carried out at all UC locations, PricewaterhouseCoopers has always received positive evaluations reflecting a high degree of satisfaction. This year the same process will be carried out, but UC will also conduct a survey of all four nationally recognized accounting firms. The University will outline its extensive requirements, which include financial statements for UC, the medical centers, laboratory reviews, the health care and pension plans, and foundations and support groups. UC will indicate the extent of its requirements and ask the firms about their qualifications to meet these requirements. Ms. Broome stated that this Request for Qualifications (RFQ) is now being formulated in accordance with State procurement guidelines.

Expert Financial Advisor Vining opined that the process described by Ms. Broome is appropriate at this time, when UC is finishing its sixth year with PricewaterhouseCoopers. Based on his discussions with UC staff and other users of PricewaterhouseCoopers' services within UC, he emphasized his understanding that there is no question that PricewaterhouseCoopers is meeting the University's needs, especially compared to prior contractors. The current process is being implemented not because UC is unhappy with the services it is receiving, but because, as a public institution, the University must look outside periodically and decide whether to issue a Request for Proposals or to negotiate a new contract with its current vendor. Chief Compliance and Audit Officer Vacca opined that this process shows that the University has performed appropriate due diligence and identified proper steps for supporting PricewaterhouseCoopers' role.

Mr. Vining stressed that he was very impressed with the exceptionally smooth and professional transition from PricewaterhouseCoopers partner Mr. Mike Schini to Ms. Joan Murphy.

Committee Chair Ruiz asked who is in charge of the process and about the process timeline. Ms. Broome responded that Chief Procurement Officer Hisgilov will develop the RFQ using criteria that she and Assistant Vice President Plotts will provide. The RFQ will then be shared with Ms. Vacca, Mr. Vining, and Committee Chair Ruiz. The survey should be completed by February 2008, with a report to the Committee at the March meeting. Ms. Vacca stated that the RFQ would be issued in January.

Mr. Vining anticipated that ideally the University will approve the new contract in May, in time for the beginning of work in fiscal year 2008-09.

The meeting adjourned at 3:15 p.m.

Attest:

Secretary and Chief of Staff