

HOW IS SARBANES-OXLEY AFFECTING THE PUBLIC SECTOR?

**Presentation by
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To
The Midwestern Intergovernmental Audit Forum
April 25, 2007**

I. INTRODUCTION

- A. The University of Wisconsin System is one of the largest systems of public higher education in the country.
- B. UW System at a Glance:
 - 1. Enrollment: 163,000
 - 2. Faculty and staff: 32,000
 - 3. Institutions:
 - a. 2 campuses (Madison and Milwaukee) offer both undergraduate and graduate degree programs, including doctoral and professional programs.
 - b. 11 comprehensive campuses provide students both undergraduate and master's degree programs in smaller, more individualized academic settings.
 - c. 13 UW Colleges deliver freshman-sophomore courses for students seeking a foundation for a bachelor's degree.
 - d. UW-Extension works with all 26 campuses, all 72 Wisconsin counties, and a wide variety of other educational partners to bring UW expertise to all corners of the state.

4. Annual Budget: \$4.315 billion
 - a. \$ 2.645 billion (61.3%) is restricted funding: gifts, grants and contracts, federal funding, specific purpose tax dollars.
 - b. \$1.670 billion (38.7%) is core instructional and student services funding. Of that amount:
 - (1) \$910 million (54.49%) comes from tuition and
 - (2) \$760 million (45.51%) comes from state tax dollars.
 5. Economic Impact: \$9.5 billion annually
- C. Organization of the UW System
1. Board of Regents (16 appointed by the Governor and 2 ex-officio)
 2. System President (appointed by the Board of Regents)
 - a. Executive Senior Vice President
 - b. Senior Vice President for Academic Affairs
 - c. Vice President for Finance (responsible for internal audit function)
 - d. General Counsel
 - e. Associate Vice Presidents for Budget and Planning and Human Resources
 - f. Executive Director of Communications & External Relations
 3. Chancellors of four-year campuses and statewide extension services
 4. Deans of two-year colleges
- D. UW System Audit Functions
1. The state of Wisconsin's Legislative Audit Bureau is the UW System's primary external auditor.

2. The Vice President for Finance is responsible for the System's internal audit function through the Office of Operations Review and Audit. That office:
 - a. Provides review and analysis to assure that programs, policies, and practices are conducted in accordance with state law and Board of Regents policy.
 - b. Reviews status of Board of Regents policy implementation.
 - c. Reviews effectiveness with which the UW institutions or UW System Administration have implemented state or federal legislative requirements.
 - d. Conducts research and analysis in other operational areas of interest to the Board of Regents or the UW System institutions.
 - e. Recommends necessary changes in programs, policies, or practices at the UW System or institution level.
 - f. Works with the audit offices at the UW System institutions to provide assurances to the Board of Regents that necessary financial and management controls are present.

II. THE ACT DOES NOT APPLY TO PUBLIC HIGHER EDUCATION, BUT ...

- A. The concerns that Sarbanes-Oxley addresses also apply to higher education.
 1. Auditor independence
 2. Board responsibility
 3. Enhanced financial disclosures
 4. Accountability
 5. Certification of financial results
- B. Higher education governing boards (whose members are typically referred to as trustees or regents) often are comprised of people who are becoming accustomed to the letter and spirit of Sarbanes-Oxley in their private corporate activities.
- C. Several states are considering adopting variations of Sarbanes-Oxley and applying it to some of the not-for-profit organizations in their jurisdictions.

- D. A new AICPA standard (Statement on Auditing Standard (SAS) No. 112) aligns certain definitions and concepts with standards of the Public Company Accounting Oversight Board, which was created by Sarbanes-Oxley. SAS No. 112, which is applicable to all financial audits, also lowers the threshold for when a concern would be classified as a material weakness or significant deficiency and when communication with the governing board is required.
- E. The Government Accountability Office has considered Sarbanes-like requirements for recipients of federal funding, although these changes have not been implemented.

III. UW SYSTEM INITIATIVES IN RESPONSE TO SARBANES-OXLEY

- A. In 2003, the National Association of Colleges and University Business Officers (NACUBO) issued recommendations regarding issues raised by Sarbanes-Oxley. The NACUBO report stated that institutions of higher education should look at the Sarbanes-Oxley Act as a framework to help evaluate overall financial risks and recommended “best practices” for higher education institutions.
- B. The UW System Board of Regents considered the NACUBO recommendations and suggestions of individual regents and, in the context of its governance structure, took the following initiatives:
 - 1. Expanded the name of the Business and Finance Committee to include audit to reflect the Board’s commitment.
 - 2. Designated the Business, Finance and Audit Committee Vice Chair as audit liaison with the Office of Operations Review and Audit.
 - 3. Clarified the process whereby Board members can directly request audits.
 - 4. Strengthened the reporting lines between the System President and Operations Review and Audit Director.
 - 5. Gave the Operations Review and Audit Director unfettered access to the System President and required at least quarterly private conferences between the two.
 - 6. Required periodic updates from the Operations Review and Audit Director to the Business, Finance and Audit Committee on internal and external audits.

7. Requested presentations to the Business, Finance, and Audit Committee on the annual financial report, during which time the external auditors are present and available to comment on the audit and answer Board questions.
- C. In addition to the actions of the Board of Regents, UW System administration and certain institutions have taken the following initiatives:
1. Conduct an integrated System-wide risk assessment, to align limited resources with risks and goals.
 2. Move to risk-based audit planning at the System and campus level.
 3. Conduct follow-up reviews to previous audit findings and recommendations.

IV. SARBANES-OXLEY INFLUENCES IN PUBLIC HIGHER EDUCATION GOVERNANCE

A. Positive influences of Sarbanes-Oxley:

1. Emphasis on avoiding conflicts of interest
2. Increased attention to the governing board's fiduciary duties
3. Enhanced focus on risk management
4. Trustees are encouraged to get information independent of management

B. Negative influences of Sarbanes-Oxley:

1. In an effort to engage more purposefully in issues facing their institutions, some governing board members may cross the line between policy setting and management.
2. Private meetings of governing board members trustees or regents without their president or senior officers, under the guise of acting more independently, can result in misguided efforts.

V. CONCLUSION

APPENDIX A

KEY REQUIREMENTS OF THE SARBANES-OXLEY ACT AND THE BOARD OF REGENTS OR UW SYSTEM'S POSITION ON THOSE REQUIREMENTS

Key Sarbanes-Oxley Act Requirements	Board of Regents or UW System Position
Public accounting firms are prohibited from performing non-audit services, such as bookkeeping, actuarial services, and legal services, to financial statement audit clients.	The UW System's primary external auditor is the Legislative Audit Bureau (LAB). While LAB occasionally serves in an advisory role, non-audit services as formally defined are not provided.
The lead audit partner of the public accounting firm must rotate off the audit after five years, with a five year time-out period.	Because LAB does not have the same relationship with the UW System that a private accounting firm may likely have, this may be considered in the future but is not a critical requirement to the UW. The National Association of College and University Business Officers recognized the different relationship and recommended that a seven-year rotation be used, if a firm is selected through a competitive bidding process.
<p>The public accounting firm must report to the audit committee:</p> <ul style="list-style-type: none"> • All critical accounting policies and practices discussed with management and the accounting firm's preferred treatment; • Other material written communication between the accounting firm and management, such as the management letter and schedule of unadjusted differences. 	<p>The audit engagement letters and post-audit communication letters from LAB are addressed to the audit committee. The post-audit letters contain:</p> <ul style="list-style-type: none"> • information on significant adjustments made during the course of the audit; • any disagreements with management; • unadjusted differences; and • identified material control and compliance weaknesses.
<p>The CEO and CFO shall certify along with the annual audit report that:</p> <ul style="list-style-type: none"> • they have reviewed the report; • based on their knowledge, the statements are not misleading; • they are responsible for establishing and maintaining internal controls; • they have evaluated the effectiveness of the internal controls; and • they have disclosed to the auditors all significant deficiencies and material weaknesses. 	<p>Annual certifications for the financial and compliance audits are signed by the UW Vice President for Finance and Associate VP for Financial Administration and contain the statements that are applicable and significant to higher education.</p> <p>In addition, each institution's chief business officer sub-certifies the financial information that is submitted to UW System Administration.</p>

<p>Each annual report shall contain an internal control report that assesses the effectiveness of the internal control structure and procedures. The public accounting firm shall attest to and report on the internal control assessment made by management.</p>	<p>The National Association of College and University Business Officers does not recommend auditor attestation of internal controls because it would be expensive and time-consuming, given the decentralized nature of universities. However, UW System Administration has evaluated and documented its critical business processes; each campus is in the process of doing the same; and a system-wide risk assessment is on-going.</p>
<p>Each member of the audit committee shall be a member of the Board and shall otherwise be independent (i.e., not receive consulting or advisory fees). At least one member of the audit committee should be a “financial expert.”</p>	<p>The Business, Finance, and Audit Committee oversees audit issues for the Board and has no voting management representatives. Many committee members have significant financial and audit experiences.</p>
<p>Each company must disclose whether it has adopted a code of ethics for its senior financial officers and the contents of the code of ethics.</p>	<p>Sections 19.45(11)(b) and 36.23, Wis. Stats., mandate that the Board establish a code of ethics for unclassified UW staff, which includes senior financial officers. As described in Chapter 8 of the UW System administrative code,</p> <ul style="list-style-type: none"> • every unclassified UW staff member at the time of appointment must make a personal commitment to professional honesty and integrity; • it is a violation of this commitment to seek financial gain for themselves, their immediate families, or organizations with which they are associated through activities that conflict with the interests of the UW System; and • Each unclassified staff member engaging in reportable outside activities shall annually file a report of outside activities with his or her appropriate administrator.
<p>The audit committee shall establish procedures for:</p> <ul style="list-style-type: none"> • the receipt, retention, and treatment of complaints regarding accounting, internal controls, and audit matters; and • the confidential, anonymous submission of questionable accounting or auditing matters. 	<p>UW-La Crosse recently established an institutional audit/fraud hotline. As additional experience is gained in this area, other campuses may choose to establish similar reporting mechanisms.</p>