



**TABLE OF CONTENTS
FOR
AUDIT, COMPLIANCE, AND MANAGEMENT REVIEW
COMMITTEE**

Committee Meeting: 2/11/2015

Board Meeting: 2/12/2015
Austin, Texas

Brenda Pejovich, Chairman
Wallace L. Hall, Jr.
R. Steven Hicks
Jeffery D. Hildebrand
Robert L. Stillwell

	Committee Meeting	Board Meeting	Page
<p>A. CONVENE AUDIT, COMPLIANCE, AND MANAGEMENT REVIEW COMMITTEE MEETING IN OPEN SESSION TO RECESS TO EXECUTIVE SESSION PURSUANT TO TEXAS GOVERNMENT CODE, CHAPTER 551 <i>(Conference Room, Ashbel Smith Hall, 9th Floor)</i></p> <p>Personnel matters relating to appointment, employment, evaluation, assignment, duties, discipline, or dismissal of officers or employees - Section 551.074</p> <p>U. T. System: Discussions with the Chief Audit Executive and Interim Systemwide Compliance Officer concerning personnel matters relating to appointment, employment, evaluation, assignment, duties, discipline, or dismissal of individual System Administration and institutional officers or employees involved in internal audit and compliance functions</p>	<p>9:00 a.m. <i>Chairman Pejovich</i></p>		
<p>B. RECONVENE IN OPEN SESSION TO CONSIDER AGENDA ITEMS <i>(Board Room, Ashbel Smith Hall, 9th Floor)</i></p>			
<p>1. U. T. System Board of Regents: Discussion and appropriate action regarding Consent Agenda items, if any, referred for Committee consideration</p>	<p>9:20 a.m. Action</p>	<p>Action</p>	<p>35</p>
<p>2. U. T. System Board of Regents: Discussion and appropriate action regarding amendment of Regents' Rules and Regulations, Rule 20401 (Audit and Compliance) to more accurately reflect current responsibilities of the U. T. System Chief Audit Executive</p>	<p>9:21 a.m. Action <i>Chairman Pejovich</i></p>	<p>Action</p>	<p>36</p>
<p>3. U. T. System: Report on the Systemwide internal audit activities, including status of Priority Findings and discussion of audit coverage in the area of procurement</p>	<p>9:31 a.m. Report/Discussion <i>Mr. Peppers</i></p>	<p>Not on Agenda</p>	<p>41</p>

	Committee Meeting	Board Meeting	Page
C. CONVENE JOINT MEETING WITH FINANCE AND PLANNING COMMITTEE			
4. U. T. System: Report on the Fiscal Year 2014 Annual Financial Report, including the report on the U. T. System Annual Financial Report Audit, and audits of U. T. M. D. Anderson Cancer Center, U. T. Southwestern Medical Center, U. T. Medical Branch - Galveston, and U. T. Health Science Center - Tyler financial statements and for funds managed by The University of Texas Investment Management Company (UTIMCO)	9:45 a.m. Report/Discussion <i>Mr. Wallace</i> <i>Ms. Tracey Cooley,</i> <i>Deloitte & Touche</i> <i>Mr. Peppers</i>	Not on Agenda	53
D. ADJOURN JOINT MEETING	10:15 a.m.		

1. **U. T. System Board of Regents: Discussion and appropriate action regarding Consent Agenda items, if any, referred for Committee consideration**

RECOMMENDATION

The proposed Consent Agenda is located at the back of the book.

2. **U. T. System Board of Regents: Discussion and appropriate action regarding amendment of Regents' *Rules and Regulations*, Rule 20401 (Audit and Compliance) to more accurately reflect current responsibilities of the U. T. System Chief Audit Executive**

RECOMMENDATION

The Chancellor concurs in the recommendation of the General Counsel to the Board and the Vice Chancellor and General Counsel that the Regents' *Rules and Regulations*, Rule 20401, regarding Audit and Compliance, be amended as set forth in congressional style on the following pages to more accurately reflect current responsibilities of the U. T. System Chief Audit Executive.

BACKGROUND INFORMATION

These proposed Regents' Rule amendments clarify the duties of the U. T. System Chief Audit Executive to include assuring that an effective internal audit function is in place Systemwide. This oversight is exercised primarily through the establishment and review of audit standards and practices at U. T. System Administration and at all U. T. System institutions and apprising the Audit, Compliance, and Management Review Committee of significant noncompliance with those standards and practices.

**The University of Texas System
Rules and Regulations of the Board of Regents**

Rule: 20401

1. Title

Audit and Compliance Programs

2. Rule and Regulation

Sec. 1 Audit Program. The Chancellor, as chief executive officer of the U. T. System, is responsible for ensuring the implementation of appropriate audit procedures for the U. T. System. Accordingly, the U. T. System Chief Audit Executive (CAE) prepares an executive summary of all internal audit activity by the U. T. System internal auditors and the institutional internal auditors for the Chancellor.

1.1 U. T. System Chief Audit Executive's Responsibilities. The U. T. System ~~Chief Audit Executive~~ CAE is charged with assuring that an effective internal audit function is in place Systemwide is responsible for coordinating the effective auditing of the U. T. System as set out in Section 1.1 (b) below. The U. T. System CAE accomplishes this through oversight of the following activities at U. T. System Administration and all U. T. System institutions:

(a) Proposing a charter for the Audit, Compliance, and Management Review Committee (ACMRC) to be reviewed and approved by the Committee.

(b) Developing a Systemwide internal audit plan based on a comprehensive risk assessment and coordinating the implementation of the audit plan with the chief audit executives at all U. T. System institutions.

(c) Providing support and advice to each institution's internal audit committee. This includes:

(i) interviewing all candidates for an open institutional CAE position,

(ii) participating in the annual performance review for each institution's CAE, and

(iii) participating, with the institution's president and chair of the institution's audit committee, in any

**The University of Texas System
Rules and Regulations of the Board of Regents**

Rule: 20401

decision to terminate the employment of an institution's CAE.

(d) Establishing the standards and methodology to be followed by all U. T. System internal auditors in:

(i) preparation of the annual institutional audit plan,

(ii) documentation required for all internal audit work papers,

(iii) establishment of a standard internal audit reporting format, and

(iv) provision of direction concerning findings that must be reported to the ACMRC.

(e) Establishing a quality assurance and improvement program that includes monitoring and assessments, to the extent considered necessary by the CAE, to evaluate the internal auditors' conformance with prescribed standards.

(f) Providing The Chief Audit Executive provides audit assistance to the Chancellor, the Executive Vice Chancellors, and the Vice Chancellors in the exercise of their responsibilities.

(g) Providing information to the ACMRC in Executive Session concerning personnel matters relating to appointment, employment, evaluation, assignment, duties, discipline, or dismissal of individual U. T. System employees involved in internal audit functions.

1.2 Appointment and Evaluation of the CAE. ~~(a)~~ The Chief Audit Executive shall be appointed by the ACMRC ~~Audit, Compliance, and Management Review Committee~~ after nomination by the Chancellor. The Chief Audit Executive shall hold office subject to the pleasure of the ACMRC ~~Audit, Compliance, and Management Review Committee~~ and the Chancellor. The Chancellor's actions regarding the Chief Audit Executive are subject to review and approval by the ACMRC ~~Audit, Compliance, and Management Review Committee~~.

**The University of Texas System
Rules and Regulations of the Board of Regents**

Rule: 20401

~~(b) The primary responsibilities of the Chief Audit Executive include developing a Systemwide internal audit plan based on a Systemwide risk assessment and coordinating the implementation of this plan with the institutional internal auditors. This Systemwide audit plan is submitted to the Audit, Compliance, and Management Review Committee for review and approval after the Chancellor's review and approval. Responsibilities of the Chief Audit Executive also include conducting audits of the System including the revenue produced from the Permanent University Fund lands and formulating policies for the internal audit activity at each institution.~~

1.34.2 The U. T. System internal auditors are the internal auditors for the U. T. System and augment the audit work of the institutional internal auditor and the State Auditors at the institutions of the U. T. System.

Sec. 2 Compliance Program. The Chancellor, as chief executive officer of the U. T. System, is responsible for ensuring the implementation of a compliance program for the U. T. System. Accordingly, the Systemwide Compliance Officer prepares an executive summary of all compliance activity of the institutions, The University of Texas Investment Management Company (UTIMCO), and System Administration.

2.1 Systemwide Compliance Officer's Responsibilities. The Systemwide Compliance Officer is responsible, and will be held accountable for, apprising the Chancellor and the ACMRC Audit, Compliance, and Management Review Committee of the institutional compliance functions and activities at System Administration, UTIMCO, and at each of the institutions as set out in Section 2.1 (b) below. The Systemwide Compliance Officer provides institutional compliance assistance to the Chancellor, the Executive Vice Chancellors, the Vice Chancellors, and the Chief Compliance Officer of UTIMCO in the exercise of their responsibilities.

(a) The Systemwide Compliance Officer shall be appointed by the Chancellor. The Systemwide Compliance Officer is the senior compliance official of the U. T. System; provides assistance and advice covering all institution, UTIMCO, and System

**The University of Texas System
Rules and Regulations of the Board of Regents**

Rule: 20401

Administration compliance programs; and shall hold office without fixed term, subject to the pleasure of the Chancellor.

- (b) The primary responsibilities of the Systemwide Compliance Officer include developing an infrastructure for the effective operation of the U. T. System Institutional Compliance Program; chairing the Systemwide Compliance Committee and the Compliance Officers Council; and prescribing the format for the annual risk based compliance plan and the quarterly compliance status reports to be submitted by each institution, UTIMCO, and System Administration.

3. **U. T. System: Report on the Systemwide internal audit activities, including status of Priority Findings and discussion of audit coverage in the area of procurement**

REPORT

Chief Audit Executive Peppers will report on Systemwide Priority Findings. A PowerPoint presentation is set forth on the following pages. Chief Audit Executive Peppers will also discuss internal audit coverage in the area of procurement.

BACKGROUND INFORMATION

The significant findings process previously reported to the Audit, Compliance, and Management Review Committee was suspended at the end of FY 2012 while a workgroup comprised of chief audit executives and System Audit Office management members was given the charge to reevaluate the process surrounding this level of finding, including the term used, the definition and criteria used, and related reporting. The term Priority Finding was selected and a more robust definition and criteria for this level of finding was developed.

A Priority Finding is defined as "an issue identified by an audit that, if not addressed timely, could directly impact achievement of a strategic or important operational objective of a U. T. System institution or the U. T. System as a whole." A Priority Findings Matrix was developed to aid chief audit executives in the determination of a Priority Finding. The matrix provides three categories of standard factors to consider, each alone with the potential to result in a Priority Finding. They are: Qualitative Risk Factors (evaluates the probability and consequences across seven high risks), Operational Control Risk Factors (evaluates operational vulnerability to risks by considering the existence of management oversight and effective alignment of operations), and Quantitative Risk Factors (evaluates the level of financial exposure or lost revenue).

U. T. Systemwide Priority Findings

Mr. J. Michael Peppers, U. T. System Chief Audit Executive

U. T. System Board of Regents' Meeting
Audit, Compliance, and Management Review Committee
February 2015



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Priority Finding Definition

- An issue identified by an audit that, if not addressed timely, could directly impact achievement of a strategic or important operational objective of a U. T. System institution or the U. T. System as a whole.

43



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Priority Finding Criteria

- A Priority Findings Matrix was developed to aid chief audit executives in the determination of a Priority Finding.
- The matrix provides three categories of standard factors to consider, each alone with the potential to result in a Priority Finding.
 - Qualitative Risk Factors: evaluates the probability and consequences across seven high risks,
 - Operational Control Risk Factors: evaluates operational vulnerability to risks by considering the existence of management oversight and effective alignment of operations, and
 - Quantitative Risk Factors: evaluates the level of financial exposure or lost revenue.
- The classification of a Priority Finding is validated by the institutional audit committee and the U. T. System Audit Office.



Priority Finding Organizational Areas

General

- Governance
- Finance
- Information Technology
- Research
- Human Resources
- Facilities Management
- Property Management
- Supply Chain
- Legal
- Risk Management
- Public Services

Academic

- Admissions
- Student Services
- Academic Support
- Instruction
- Colleges
- Athletics
- University Relations
- University Development
- Auxiliary Services

Health

- Medical School
- Basic Science
- Clinical Science Education
- Clinical Programs
- Medical Ethics – Law
- Clinical Care
- Physician Care
- Biomedical
- Pharmacy
- Quality
- Medical Data & Clinical Reporting Management
- Revenue Cycle
- Medical Staff
- Provider
- Practice Plan
- Compliance

45



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Priority Finding Risk Factors

- Reputation
- Information Security
- Compliance
- Accomplishment of Management's Objectives
- Effectiveness and Efficiency
- Capital Impact
- Life Safety
- Management Oversight
- Operational Alignment
- Designed Controls
- Payments/Expenditures
- Lost Revenue

46

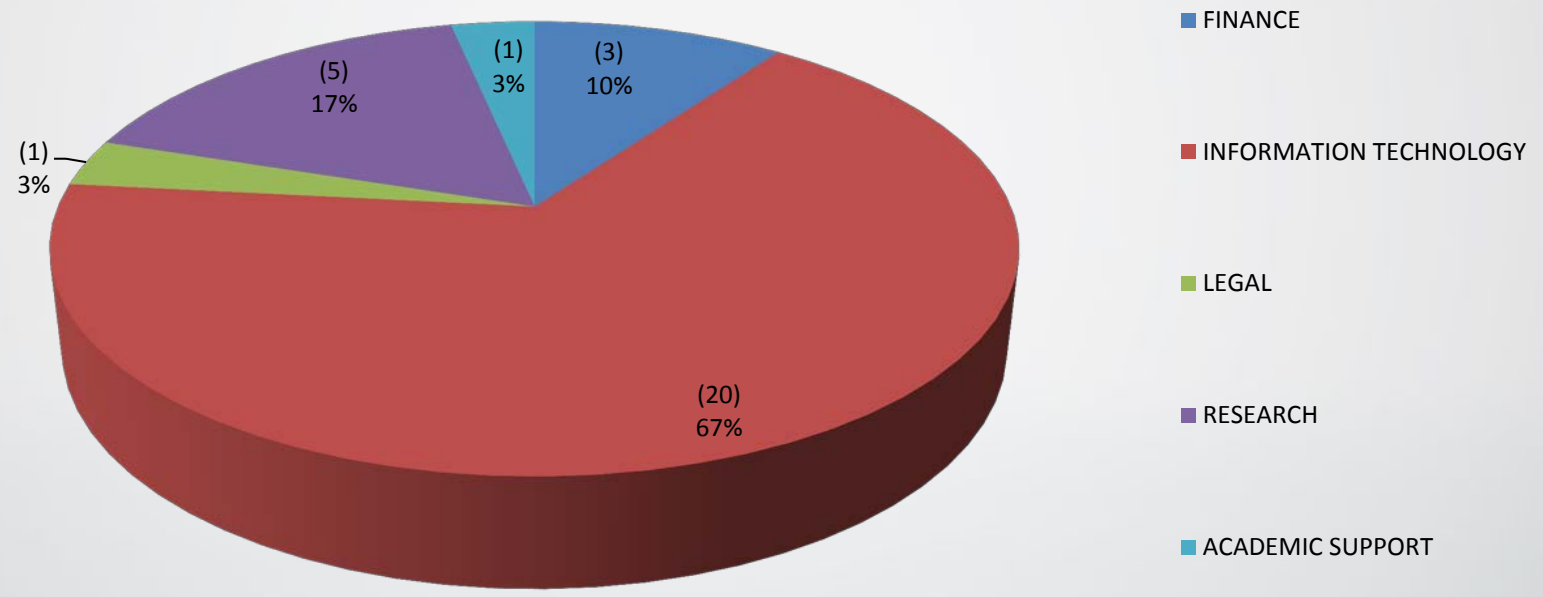


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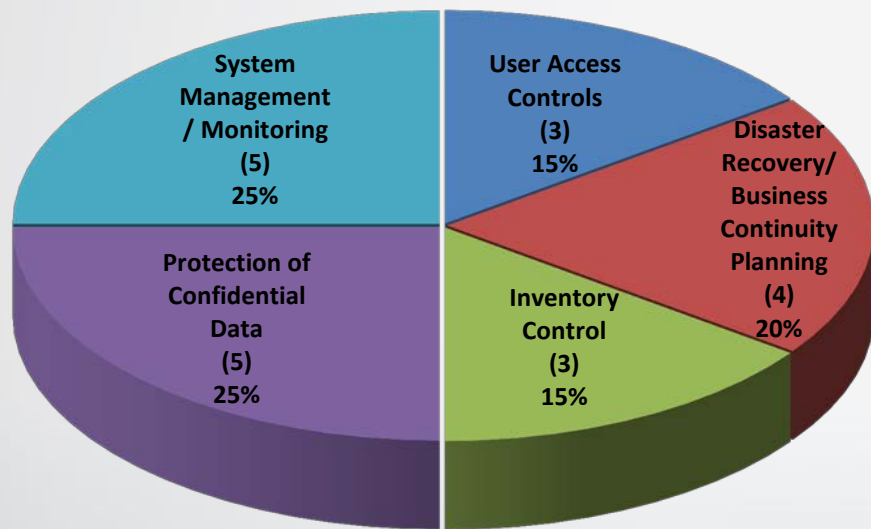
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Priority Findings by Organizational Area



48

IT Related Priority Findings

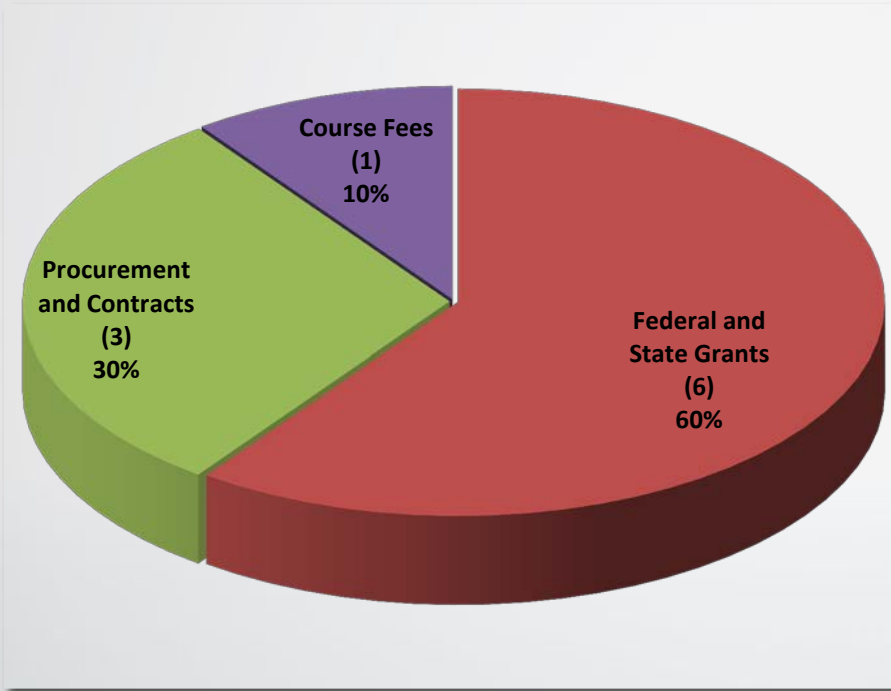


The 20 IT related Priority Findings fall under five themes:

- *System Management and Monitoring* (5): Change management, system configuration standards, timely patch management, and network and system monitoring weaknesses were noted.
- *Protection of Confidential Data* (5): Some confidential data was not identified so that protection and monitoring procedures could be applied, and improvements were needed to ensure encryption is applied when required (no specific breach incidents were cited in these audits).
- *Disaster Recovery and Business Continuity Planning* (4): Plans were outdated or not tested.
- *User Access Controls* (3): Highly-privileged access beyond the minimum needed was noted, along with opportunities to improve controls over management of system-level service accounts (used by database or operating systems rather than individuals). Technical limitations prevented full compliance with password management policies.
- *Hardware Inventory Controls* (3): Hardware devices were not inventoried, limiting the ability to enforce required controls, such as encryption and software licensing.



Non-IT Related Priority Findings

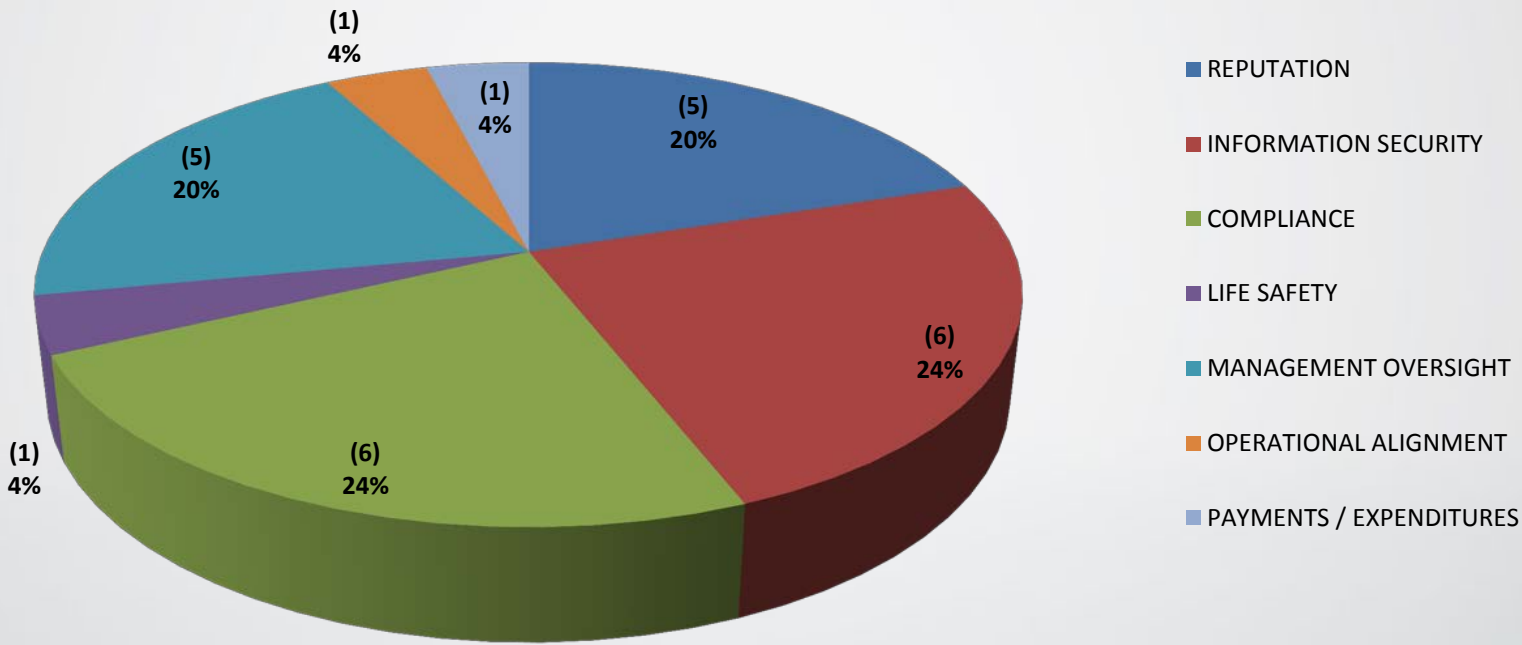


The 10 Non-IT related Priority Findings fall under three themes:

- *Federal and State Funds* (6): Errors in calculation of Title IV returns and withdrawals; untimely return of funds; inconsistent access controls over user accounts; erroneous calculation of drawdowns; lack of monitoring controls over effort reporting and other required financial reports.
- *Procurement and Contracts* (3): Conflict of interest not recognized/managed; sole source procurement without adequate justification; inability to readily identify and track documents with Business Associate Agreements.
- *Course Fees* (1): Certain student fees assessed without appropriate approvals.



Priority Findings Risk Factors



51



Other Findings Not Ranked Priority

- Will begin consistently ranking at all institutions
- High, Medium, or Low – all assessed and monitored by the institutional audit committees
- Tagged with organizational areas, like Priority Findings, to assist in identifying trends by institution and Systemwide



4. **U. T. System: Report on the Fiscal Year 2014 Annual Financial Report, including the report on the U. T. System Annual Financial Report Audit, and audits of U. T. M. D. Anderson Cancer Center, U. T. Southwestern Medical Center, U. T. Medical Branch - Galveston, and U. T. Health Science Center - Tyler financial statements and for funds managed by The University of Texas Investment Management Company (UTIMCO)**

REPORT

See Item 1 on [Page 56](#) of the Finance and Planning Committee.