

Contact: Patrice Sayre

MINUTES OF APRIL 30, 2008
AUDIT/COMPLIANCE AND INVESTMENT COMMITTEE
BOARD OF REGENTS, STATE OF IOWA
MAUCKER UNION, OLD CENTRAL BALLROOM, ROOMS A AND B
UNIVERSITY OF NORTHERN IOWA
CEDAR FALLS, IOWA

Committee Members

Jack Evans, Chair
Bonnie Campbell
Jenny Connolly

Robert Downer
Michael Gartner
Ruth Harkin

Craig Lang
David Miles
Rose Vasquez

Staff Members

Andrea Anania, Andy Baumert, Patrice Sayre, Todd Stewart

Regent Institutions

SUI Cynthia Bartels, Doug True, Terry Johnson
ISU Stephanie Fox, Joan Piscitello, Warren Madden
UNI Tom Schellhardt, Gary Shontz

Others

Mike Dudkowski, Wilshire Associates Incorporated
Andrew Nielsen, Deputy Auditor of State
David Vaudt, Auditor of State

The corresponding docket memorandum for each agenda item, an integral component of the minutes, is available on the Board of Regents web site: www2.state.ia.us/regents. Copies of these memoranda can also be obtained from the Board Office by calling 515-281-3934.

Chair Evans called the meeting to order at 1:00 p.m.

External Audit Overview

Auditor of State David Vaudt discussed the Auditor of State's (AOS) responsibilities concerning the Regents institutions. He:

- ◆ Reviewed General Accounting Standards Board Statements (GASB) 45, 48, 49, 51, 52;
- ◆ Discussed audit scopes, saying that the AOS's Office uses a risk-based approach, coordinates work with Internal Audit Director Todd Stewart, reviews internal controls, reviews and tests controls for federal financial assistance, and performs single audit compliance procedures;
- ◆ Reported that the AOS prepares separate audited financial statements for each university, adding that the AOS reports any significant findings and reviews internal control letters and reports of recommendations with the Committee;
- ◆ Said that additional audits are performed on: (1) activities subject to the Single Audit Act (such as federal financial assistance); (2) special schools and the Board Office (limited scopes on the schools and office); and (3) internal control and compliance;
- ◆ Said that approximately 25% of the AOS's time is spent on federally-mandated audit areas (Single Audit);
- ◆ Reviewed the timeline of audit work; and
- ◆ Discussed historical and projected audit hours and fees. He noted that total hours decreased by 10.1% from 2003 to 2008 and that the average hourly rate for 2008 is \$69.25.

Chair Evans asked if anything applicable in the public sector, such as Sarbanes Oxley, has a similar impact on the Regents institutions. Auditor Vaudt replied that there is nothing imminent at this time and that his office monitors what appears at the national level through national associations.

Internal Audit Overview and Reports

OVERVIEW OF THE INTERNAL AUDIT FUNCTION

Internal Audit Director Todd Stewart gave an overview of the internal audit function. He reported that: (1) the first internal auditor was employed by SUI in 1956; (2) the internal audit function operated separately at each university until 2004 when he was hired to manage the work and promote consistency and standardization; (3) he reports directly to this Committee and to the Board Office, while the auditors he manages remain employees of their respective universities; and (4) an audit charter was adopted by the Board of Regents in 2007 that covers all internal auditors.

Internal Director Stewart reviewed the staffing, mission, and goals of internal audit. He said that some of the challenges he faces are hiring, retention and training; productivity; maintaining senior leadership trust; and peer reviews. He also discussed all of the work that is put into preparing the annual internal audit plan.

Regent Harkin stated she has read that a number of states have adopted Sarbanes Oxley (SOX) for non-profit state facilities and asked how nimble the internal audit function would be if that were to happen in Iowa. Internal Audit Director Stewart replied that many SOX guidelines are already in place, such as an ethics hotline and an audit committee with financial expertise.

SUI Controller Terry Johnson talked about SOX Section 404 on internal controls and Internal Audit Director Stewart talked about SOX Section 802 on criminal penalties for altering or manipulating documents.

President Miles asked if prioritizing risk is standard practice and if there are things that always fall to the bottom and never get audited. Director Stewart said that with over 300 departments across universities, only a few can be audited each year. The plan tries to review smaller audit areas, not just high risk ones.

INTERNAL AUDIT REPORTS

President Miles noted that the majority of the audits presented this month are rated high for materiality / criticality. Discussion followed about the audit dashboard.

Internal Audit Director Todd Stewart discussed the reports presented this month. With respect to the UIHC Access Control Security Report, President Miles requested that Vice President Doug True address the University's response to the mechanical key control section which indicated that the security risk could not be corrected due to an unsuccessful capital request.

Vice President True concluded this discussion stating that many audit findings apply to other areas and departments and that these universal findings should be shared more widely through councils and committees existing at each university.

OTHER AUDITS OVERVIEW

Chief Business Officer Patrice Sayre reviewed other audits that are performed by external auditors and presented to the Board, as well as affiliated organization reports that are reviewed by staff but are not presented to the Board unless significant findings are reported.

OPERATING PORTFOLIOS

Each university presented their operating portfolios, discussing the mix of funds:

- ◆ SUI – Vice President for Finance and Operations Doug True spoke about best practices, working with Wilshire, and an internal advisory group that analyzes the best use of funds – diversification, lowered risk, and increased returns. Vice President True hopes to bring results and recommendations to the Committee in the future.
- ◆ ISU – Vice President for Business and Finance Warren Madden clarified that foundation funds are not managed by the University. He added that a few affiliated organizations with small endowment funds are managed by ISU, such as the ISU Research Foundation, because the University can do it more efficiently and cost effectively.

Treasurer Joan Piscitello reviewed portfolio management and noted that, since 9/11, there has been greater diversity in where funds are placed. In response to questions from Regent Lang and Chair Evans, Ms. Piscitello clarified that short-term cash flow is kept at a zero balance by entirely investing it daily and that mortgage funds have had a lower income return than if they would have been invested in treasuries.

- ◆ UNI – Vice President for Administration and Finance Tom Schellhardt reported that UNI endowment funds of approximately \$10 million are pooled with SUI funds. Before turning detailed discussion of the portfolio over to Gary Shontz, Vice President Schellhardt listed the accomplishments of Mr. Shontz, including the fact that, for the last sixteen years, UNI has received a financial reporting award under his expertise.

Controller, Secretary, and Treasurer Gary Shontz spoke to the cyclical nature of UNI's cash flow, noting that operating assets are the smallest in mid-August.

LONG-TERM (INCLUDING ENDOWMENT) PORTFOLIOS

Mike Dudkowski from Wilshire Associates, investment advisor to the Board and to the Regent institutions, gave an overview of the long-term endowment pool. He reported that Wilshire's role is to assist and provide education and information to this Committee. Particular focus is on the asset allocation mix; Wilshire believes that is the most important decision that will be considered by this Committee. The next step is to educate and study and recommend changes in the asset allocation – perhaps increasing real assets and determining if hedge funds have a role in the universities endowment funds, and if so, to what extent.

Regent Vasquez asked if these key considerations match that of peer institutions. Mr. Dudkowski responded that the Regents are not driven by peer performance, but by what we believe to be the objectives of this portfolio; that we have lower exposure as compared to peers.

Regent Campbell probed the topic of hedge funds further asking if other universities and Iowa Public Employees Retirement System (IPERS) invest in them. Mr. Dudkowski answered that generically, saying that others do invest in them and that they can be helpful in achieving goals, but that making direct investments in them is challenging as they are staff time intensive and not usually transparent.

Chair Evans clarified that a review of asset allocation is part of the contract services that Wilshire provides. He suggested that Wilshire and university professionals discuss asset allocation and bring a recommendation on change in allocation to the Committee.

President Miles asked that this group also determine what an appropriate peer group would be for comparative purposes, including foundations.

The suggestion for Wilshire and university professionals to discuss asset allocation and recommendations was changed to a direction to do so for approval at the May 1, 2008, Board meeting.

Mr. Dudkowski finished the Wilshire presentation reviewing portfolio performance.

The Committee was not able to discuss in depth the final agenda topics - roles of the institutions and the Investment Advisor, hiring/reviewing the Investment Advisor & Fund Managers, and changes to investment law. Chief Business Office Patrice Sayre briefly spoke to the annual evaluation and the need to set up this process soon.

Chair Evans asked university personnel to work with Wilshire to develop a calendar for pertinent topics covered today and fund manager evaluations.

- The Committee recommended that the Board:
 - ◆ Receive the original and follow-up internal audit reports; and
 - ◆ Direct university personnel to work with Wilshire Associates and review the Regents asset allocation and provide any recommendations to the Committee.

Chair Evans thanked everyone for good discussion and adjourned the meeting at 3:00 p.m.