

**SOUTH DAKOTA BOARD OF REGENTS**

**Planning and Resource Development**

**AGENDA ITEM: 5 – J**

**DATE: August 10, 2017**

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**SUBJECT: Creation of Audit Committee and Approval of Audit Committee Charter**

Upon request by the Board at the June 2017 meeting, additional language was added to the draft Audit Committee Charter to clarify the responsibilities of management and the Audit Committee. The proposed revisions were discussed at the July 2017 COPS meeting with the recommendation that it move forward for Board approval. Attachment I shows the changes to the Charter highlighted in yellow.

At the June 2017 Board meeting, proposed language was discussed that would create the Audit Committee as a Special Committee of the Board. However, Board members indicated that the Audit Committee should be created and added to the By-Laws as a Standing Committee. The creation of the Audit Committee as a Standing Committee will require additional revisions to Article III of the Board's By-Laws, which addresses Standing Committees. Those additional revisions are being introduced, along with other revisions to other parts of the By-Laws, as part of another Board Agenda Item under consideration for a first reading (see Board Item 5-H).

Rather than delaying the creation of the Audit Committee until the second reading of the comprehensive revisions to the By-Laws are approved, this Board item seeks to create the Audit Committee as a Special Committee of the Board. This Board item also seeks to approve the Audit Committee Charter. If the Board approves the motion, the newly created Audit Committee would be able to operate immediately consistent with the Audit Committee Charter.

As part of the comprehensive review of the By-Laws, the Audit Committee will eventually be codified in the By-Laws as a Standing Committee of the Board.

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**DRAFT MOTION 20170810\_5-J:** I move to approve (1) the creation of the Audit Committee as a Special Committee of the Board, and (2) the Audit Committee Charter.

## **AUDIT COMMITTEE CHARTER**

### **Purpose, Responsibility and Authority of the Audit Committee**

The Audit Committee (“Committee”) shall assist the Board of Regents in its financial oversight responsibilities. The Committee is a permanent standing advisory committee of the Board. The Committee will advise and assist the Board and other standing committees on matters relating to financial reporting and financial controls and procedures. The Committee shall be responsible for communication with and among the independent external auditing firm, Department of Legislative Audit (DLA), institution management, the internal audit staff and the Board. The Committee will not assist in the preparation of or assess the institutions’ budgets or perform other management functions. The Committee shall make policy recommendations to the Board to improve financial oversight. Approval of adoption or changes to policies are exclusively under the responsibility of the Board.

### **Composition**

The Committee members shall be appointed by the Board President and shall consist of 5 members. Three members of the Committee shall be current Board members and 2 shall be non-board members who are permanent residents of the state of South Dakota. All members shall have voting rights. No employee of an institution under the governance of the Board shall serve on the Committee.

The Committee chairperson shall be a member of the Board and appointed by the Board President. Appointments shall be for a three-year term. Terms will be staggered. Committee members may be reappointed.

Committee members shall have (1) knowledge of the primary activities of the institutions; (2) the ability to read and understand nonprofit financial statements, including a statement of financial position, statement of activities and changes in net assets, statement of cash flows and key performance indicators; and (3) the ability to understand key operational and financial risks, and related controls and control processes. The committee shall have access to counsel and other advisers at the committee’s sole discretion.

At least one member should be literate in nonprofit financial reporting and control, including an understanding of GAAP, experience in preparing, auditing analyzing or evaluating financial statements, ability to assess the general application of such principles in the accounting for estimates, accruals and reserves, an understanding of risk assessment and internal controls concepts, an understanding of the roles of internal and external audit, and an understanding of audit scope methodology and process, knowledge of tax and regulatory requirements, and should have past or current employment experience in finance or accounting, or other comparable experience or background.

### **Meetings of the Committee**

The committee shall meet at least bi-annually and at additional times when necessary. The Committee chairperson shall prepare and/or approve an agenda in advance of each meeting. A

majority of the members of the Committee shall constitute a quorum for the purpose of making recommendations to the Board. The Committee shall maintain minutes or other records of meetings and activities of the Committee. The Committee shall, through its chairperson, report regularly to the Board following the meetings of the Committee.

## **Responsibilities of the Committee**

### **RISKS and CONTROLS**

The Committee will review and assess the institution's operating and financial risk management process, including the adequacy of the overall control environment and controls in selected areas representing significant risk. The Committee will review the plans to minimize or respond to those risks and assure that management is setting the appropriate tone in communicating the importance of internal controls and establishing policies and procedures to mitigate risk. The Committee will identify best practices and develop and recommend governance principles applicable to the institution.

### **FINANCIAL REPORTING**

The Committee will review with management and the external auditors the results of the annual audit and related footnotes, including any difficulties or disputes with management. The Committee will review and assess the key financial statement issues and risks, their effect or potential effect on reported financial information, the processes used by management to address such matters, related auditors' view and the basis for audit conclusions. The Committee will review the management letter and monitor the institution's compliance with its recommendations. The Committee will be provided by financial management timely analysis of significant current financial reporting issues and practices.

### **AUDIT FUNCTIONS**

Institution's management shall be responsible for the accurate preparation, presentation and integrity of the financial statements and for establishing and maintaining appropriate accounting and financial reporting policies. The Committee shall receive information regarding all audits performed.

### **OVERSIGHT of INTERNAL AUDIT FUNCTION**

The charter for the internal audit function shall be approved by the Committee. Internal auditors shall have sufficient access to employees, property, and records of the institutions to complete the internal audit plan approved by the Committee. The Committee shall review any internal audit reports with the internal auditors and institution management and act upon those reports presented. The internal audit report shall include significant findings, management's responses and all other such information as may be beneficial for the use of the Committee. The Committee shall review and approve the annual internal audit plan based on a comprehensive internal audit risk assessment. Before hiring any new internal audit manager, the institution president shall confer with the Committee Chair. The Committee shall approve the termination of any institutional internal auditor.

The Committee shall ascertain that management has the appropriate structure and staffing to carry out its internal audit responsibilities effectively. The audit committee shall monitor the work of the internal auditors and monitor management's progress in responding to the findings.

#### OVERSIGHT of REPORTING and COMPLIANCE

**The Committee shall be responsible for reviewing and updating the Audit Committee charter.**

The Committee shall review with Institution management, as it deems necessary, the institution's financial policies and procedures and the results of any review of these areas by the internal auditor or the external auditing firm. The Committee shall inquire of Institution management, the auditing firm and internal auditors about significant risks and uncertainties facing the institutions.

The Committee shall review with the general counsel legal and regulatory matters that, in the opinion of management, may have a material impact on the financial statements and compliance with federal, state, and local laws and regulations.

The Committee shall review with Institution management and the auditing firm the auditing firm's reports on the Institution's financial statements, compliance audits and all related reports, information and auditing results.

The Committee shall accept assignments from the Board in financial oversight of the Board's activities as directed by the Board.

The Committee shall review control deficiencies and remediation plans with institution management and the auditing firm or internal audit as deemed necessary by the Committee. Any unresolved deficiencies or disputes shall be brought to the attention of the Board.

The Committee is responsible for understanding:

- The clarity and completeness of financial statements and other financial and compliance disclosures.
- Management's selection and application of significant account principles.
- Critical accounting policies.
- Significant or unusual transactions or events.
- Significant accounting judgments and estimates.

All Committee members shall have an understanding of the financial affairs and the ability to exercise independent judgment. Understanding of the institution's financial position will require looking at such diverse information as applications and admissions data, results of fund-raising efforts, financial-aid policies, and any revenue streams resulting from research and indirect cost recovery. Appropriate orientation for new Committee members will be provided by the Board office and institutions' financial staff under the direction of the Committee chair.