

## APPENDIX Y

The Task Force on Best Financial Practices makes the following recommendations.

### Establishment of a Board of Governors' Audit Committee

The Board of Governors should form a permanent Audit Committee that would meet four times a year. The Audit Committee must contain at least one member with significant financial knowledge and experience. The Audit Committee would be responsible for the following.

- Developing and maintaining a system-wide code of ethics. The Audit Committee should ensure that each constituent institution annually reminds each employee of the code of ethics and provides continuing education to ensure adherence to ethical standards.
- Developing a charter to define roles and responsibilities.
- Reviewing the annual financial reports prepared by the State Auditor for each of the sixteen constituent institutions and affiliated entities of the University.
- At the beginning of the audit cycle, reviewing and approving a summary of the annual internal audit plans for the sixteen constituent institutions and providing guidance, through the Vice President for Finance, to campus internal auditors on specific issues that should be incorporated in their audit programs.
- Reviewing an annual summary of the work performed by the Audit Committees of the institutional Boards of Trustees, including a report of the work of the campus internal auditor which indicates any identified material reportable conditions and how they were addressed.
- Reviewing an annual report on University-associated entities.
- Reviewing an annual financial report for the entire University.
- Meeting with the State Auditor or a designated representative annually.
- Participating in training sessions to better understand aspects of University finances.

### Audit Committees of Boards of Trustees

The Task Force on Best Financial Practices recommends that the Board of Governors require that each campus Board of Trustees have an active Audit Committee, or alternatively a committee with the word “audit” in its title, that reports to the Board of Trustees and the Board of Governors annually on its activities. This Committee would be responsible for the following.

- Meeting with representatives of the State Auditor's office to review the institution's annual audit report and discuss corrective actions if needed.
- Reviewing audit reports of University-associated Entities.
- Receiving quarterly reports from the University's internal auditor.
- The internal auditor will report to the chancellor but will also have a reporting relationship to the chair of the Audit Committee to enable the auditor to freely discuss professional issues with the Committee chair.
- Developing a charter to define roles and responsibilities. One of the responsibilities is the assurance that the institution is performing self assessments of operating risks and evaluations of internal controls on a regular basis.

- Internal audit functions will be carried out in a way that meets professional standards.
- At the beginning of the audit cycle, reviewing and approving a summary of the annual internal audit plan for the campus. At the end of the cycle, reviewing a comparison of the plan advanced to the internal audits performed.
- Prepare and forward to the Board of Governors an annual summary of the work performed by the Audit Committee, including a report of the work of the campus internal auditor which indicates any identified material reportable conditions and how they were addressed.

It will be the responsibility of the Board of Governors to insure that trustee appointments on each campus include individuals who understand financial data and can serve on the Audit Committee.

#### University-associated Entities

An internal working group with representatives from six campuses and the Office of the President has, under the leadership of Vice President and General Counsel Leslie Winner, drafted a set of required elements that should exist in the relationships between the University and university-associated entities. The Task Force on Best Financial Practices endorses the work of this internal working group and recommends that the President issue regulations to ensure that the constituent institutions adhere to the required elements (Attachment A).

#### Background Checks for Senior Officers

The Task Force on Best Financial Practices believes that senior officers in the university should be offered positions contingent upon successful criminal background investigations. Campuses should adopt guidelines to prevent them from hiring senior officers whose background indicates that they cannot be relied on to maintain the fiscal integrity of the institution.

#### Personal Loans

The Task Force on Best Financial Practices believes that neither campuses nor university-associated entities should make personal loans to trustees or executive officers regardless of the funding source. Any loans to other employees should only be from funds restricted for that purpose by donors. Loans to employees should be monitored by the Chief Financial Officer of the campus even if the loan is from a University-Associated Entity.

**REQUIRED ELEMENTS OF UNIVERSITY-ASSOCIATED ENTITY RELATIONSHIP**  
Regulations 110205

The following requirements apply to any University Associated Entity.

**A. Definitions.** As used in these regulations:

1. An “Associated Entity” means any foundation, association, corporation, LLC, partnership or other non profit entity that was established by officers of the University, that is controlled by the University, that raises funds in the name of the University, that has a primary purpose of providing services or conducting activities in furtherance of the University’s mission pursuant to an agreement with the University, or that has a tax exempt status that is based on being a support organization for the University.
2. “Approving Institution” means a constituent institution of the University of North Carolina or the General Administration that approves an Associated Entity.
3. “General Administration” means the Office of the President and the affiliated programs of the University that are not centers or institutes of a constituent institution.
4. “Major Associated Entity” means an Associated Entity which has annual expenditures of \$100,000 or more.
5. “Minor Associated Entity” means an Associated Entity which has annual expenditures of less than \$100,000.
6. “Specified purpose entity” means an Associated Entity, or an approved subsidiary or LLC of an Associated Entity, that is established by the officers of the University or is controlled by the University, has as its sole purpose the constructing or managing facilities for the University, and does not engage in fundraising activities.
7. “State” means the State of North Carolina.
8. “University” means the University of North Carolina, including its constituent institutions.
9. When “president or chancellor” is used in these regulations, it means the chancellor if the approving institution is a constituent institution and it means the president if the approving institution is the General Administration.

**B. Creation of University-Approved Associated Entities**

1. Associated Entity Must be Approved—An Associated Entity must be approved in writing by the president, the chancellor, or the president or chancellor’s designee. An entity must be approved in order to receive University-provided services or to be able to use an institution’s or the University’s name or an institution’s or the University’s logo/trademark in fundraising. If an approved entity establishes a subsidiary entity or an LLC, then the subsidiary entity or LLC must be separately approved.
2. Abide by Relevant University Policies— In order to obtain approved status, the Associated Entity must formally agree to abide by the policies or regulations established by the University

and by the Approving Institution regarding the University's and the Approving Institution's relationship with related Associated Entities.

3. Periodic Review of Status– The Approving Institution may remove the approved status of any Associated Entity which fails to abide by the Approving Institution's or the University's policies or regulations which govern Associated Entities.

### **C. Organizational Requirements of an Associated Entity**

1. Purpose to Benefit University– The Associated Entity must be organized for the primary purpose of (i) supporting the University or one or more of its constituent institutions or programs, and/or (ii) conducting activities that are in furtherance of the mission of the University or of one or more of its constituent institutions or programs.

2. State Nonprofit Corporation– The Associated Entity must be organized on a nonprofit basis, and, if a corporation, be incorporated in North Carolina, and comply with the requirements of Chapter 55A of the North Carolina General Statutes. If a constituent institution proposes to establish or approve an associated entity on a for profit basis, it must receive approval from the Board of Governors before establishing the entity.

3. Tax Exempt Status– Except as provided in paragraph C.2., an Associated Entity must apply for, receive, and maintain both federal and State tax exempt status.

4. Dissolution of Associated Entity– The Associated Entity's articles of incorporation must include a clause which provides that, upon dissolution of the Associated Entity, all of its assets will revert to the University or the Approving Institution or another University approved Associated Entity unless otherwise designated by the donor of an asset.

5. University Representative(s) on Board–At least one Senior Academic or Administrative Officer of the Approving Institution or a designee of the president or the chancellor must sit as an ex-officio (either voting or non-voting) or regular member of the Associated Entity's governing board.

6. Audit Committee Required–

(a) A major Associated Entity's by-laws must provide for an audit committee which has no University employee as a member. The audit committee must receive the report of the independent CPA firm that conducts the Associated Entity's annual audit and relevant tax forms to be submitted by the Associated Entity.

(b) A minor Associated Entity's by-laws must provide for a committee which has these audit functions and which has a majority of members that are not University employees.

(c) No employee of the Associated Entity may serve on an audit committee or a committee with an audit function. If practical, each audit committee or committee with an audit function should have a financial expert as a member.

(d) A Specified Purpose Entity is not required to have an audit committee provided that it is subject to independent audit at the request of one or more designated trustees, sureties, insurers, certificate holders or bondholders.

## **D. Financial and Accounting Controls**

1. Sound Accounting and Business Principles– An Associated Entity must use sound fiscal and business principles, ensure that a sound internal control structure is in place, and follow generally accepted accounting procedures.
2. Annual CPA Audit– A major Associated Entity must be audited on an annual basis by an independent CPA firm. A minor Associated Entity must have an annual audit conducted either by the Approving Institution’s internal auditor, another University internal auditor, or an independent CPA firm. A CPA firm providing an audit for a major Associated Entity may not provide non-auditing services to the Associated Entity other than tax preparation services that are pre-approved by the audit committee.
  - a. An Associated Entity of a constituent institution must provide copies of the audit report, management letters, and responses to management letters to the chancellor of the Approving Institution, through the chancellor to the governing board of the Approving Institution and the president, and through the president to the Board of Governors.
  - b. An Associated Entity of the General Administration must provide copies of the audit report, management letters, and responses to management letters to the president, and through the president to the Board of Governors.
3. Annual Budgets– The Associated Entity must create an annual operations and capital budget.
4. Officer and Employee Compensation– All salary and non-salary compensation provided by the Associated Entity to its officers or employees must be approved by the Associated Entity’s governing board. The Associated Entity must comply with Board of Governors Policy §300.1.1 concerning the prohibition of payments to specified University employees. This requirement does not prohibit the Associated Entity from reimbursing its officers or employees for expenditures made on behalf of the Associated Entity.
5. Indemnification of University– The Approving Institution may require an Associated Entity to indemnify and hold the Approving Institution and the University harmless from any damages or liabilities that the Approving Institution or the University incurs as a result of the Associated Entity’s actions.
6. University- Associated Entity Monetary Transfers– All transfers of funds from the Associated Entity to the University or to the Approving Institution must be documented in writing or electronically in a form that has a retrievable transaction trail.
7. Whistle Blower Protection—An Associated Entity must have a confidential and anonymous mechanism to encourage employees to report any inappropriateness within the entity’s financial management and must prohibit punishment of or retaliation against any employee for reporting problems.
8. Chief Executive Officer-- The Chief Financial Officer of the Approving Institution may not be the chief executive officer of an Associated Entity.

9. Acquisition of debt—A Minor Associated Entity may not acquire debt in excess of \$100,000 that is not to be publicly traded without first notifying the president or the chancellor of the Approving Institution and then consulting with the Vice President for Finance of the University. A Major Associated Entity may not acquire debt in excess of \$500,000 that is not to be publicly traded without first notifying the president or the chancellor of the Approving Institution and then consulting with the Vice President for Finance of the University. In determining the level of scrutiny to give to the proposed transaction, the Vice President shall take into account the amount of the debt in relationship to the Associated Entity's assets and income and the extent of experience of the Associated Entity in entering into similar debt transactions. A Specified Purpose Entity that issues debt to construct facilities for the University must provide a financial or construction audit to the Vice President for Finance of the University at the Vice President's request or to the governing board of the Approving Institution at the request of the chair of the governing board.

10. Audit findings. Within 90 days of the issuance of the audit report with audit findings, the Associated Entity must demonstrate to the president or the chancellor of the Approving Institution and to the Vice President for Finance that satisfactory progress has been made to implement a corrective action plan. Failure of an Associated Entity to receive an unqualified audit opinion, to comply with the reporting requirements of this regulation, or to satisfactorily implement a corrective action plan in response to an audit finding may result in the Associated Entity's losing its approved status.

#### **E. Insurance and Bonding**

1. Bonding Required—Officers and employees of major Associated Entities who have check signing authority or who handle cash or negotiable instruments must be bonded in an amount determined to be reasonable by the Associated Entity's board. The Board of a minor Associated Entity should consider requiring bonding of appropriate employees.

2. Liability Insurance— The governing board of an Associated Entity must consider whether to obtain general liability and directors'/officers' insurance in an amount determined to be reasonable by the Associated Entity's board.

#### **F. Provision of Administrative and Other Services by University for Associated Entity**

1. Written Agreement Required— All services provided by the Approving Institution or the University for the Associated Entity (including use of University or constituent institution assets, facilities, and personnel) must be pursuant to a written agreement setting forth the terms under which such services will be provided.

2. Reimbursement of Costs— Any reimbursement to the Approving Institution or the University for services the Approving Institution or the University provides to the Associated Entity must be made pursuant to a written agreement between the University or the Approving Institution and the Associated Entity entered into before the service is provided.

3. Control of University Personnel– When University personnel provide services for the Associated Entity and there arises a conflict between the University and the Associated Entity, the University’s employee must comply with the policies, regulations and directives of the University.

#### **G. Acceptance of Gifts by Associated Entity**

1. Restricted Gifts That Require University Approval– An Associated Entity may not accept any restricted or conditional gifts that impose an obligation on the University or the State to expend resources in addition to the gift without first receiving the Approving Institution’s approval. In addition, an Associated Entity may not accept a gift which has any restriction that is unlawful.

2. Notification to Donors of Restricted Gift Policies– An Associated Entity must advise prospective donors of all restricted or conditional gifts to the Associated Entity if acceptance of the gift is conditioned upon the Approving Institution’s approval.

3. Coordination with University Development Office- In soliciting and accepting gifts in the name of the University, an Associated Entity must coordinate with the Approving Institution’s development office.

#### **H. Conflict of Interest and Ethics Policies**

1. Policies Required-The Associated Entity must have in place conflict of interest and ethics policies pertaining to relationships between the Approving Institution, the Associated Entity, members of the governing board of the Associated Entity and persons doing business with the Associated Entity and establishing required ethical standards for the members of the governing board and employees of the Associated Entity.

2. Transactions Between Associated Entity and its Employees-All transactions (other than reimbursements as provided in §D.5.) between the Associated Entity and an officer, director, or employee of the Associated Entity must be approved by the Associated Entity’s governing board.

3. Recusal from Business Decisions-No Associated Entity officer, director, or employee having a private business interest in an Associated Entity business transaction may be involved in the decision with respect to whether the Associated Entity should enter into such transaction.

4. Associated Entity Scholarships-No Associated Entity scholarship or fellowship award may be made to an officer, director, or employee of the Associated Entity or to a family member of such person unless the recipient of the award is determined by an independent awards committee.

#### **I. Reports required to be submitted by Associated Entity to University**

1. The Associated Entity must file annual reports with the president or chancellor of Approving Institution covering the following items:

- a. A list of all members of the Associated Entity’s board;

b. A copy of the publicly disclosed portion of the Associated Entity's Form 990, or other series 990 form.

c. A copy of the Associated Entity's CPA audit report and related management letters and responses to management letters

2. At the request of the chancellor, president, or the chair of governing board of the Approving Institution, for an articulated legitimate reason, the Associated Entity must meet with the requesting person, his or her designee, or the internal auditor of the Approving Institution and allow that person to inspect any of the following information that is related to the articulated reason:

a. A description of all monetary transfers from the Associated Entity to the Approving Institution or the University;

b. A description of all transactions entered into during the year between the Associated Entity and the Approving Institution or the University.

c. A copy of the Associated Entity's operating and capital expenditure budget for the year and a comparison of actual expenditures to budgeted expenditures.

d. A description of all real estate purchases, material capital leases, and investment/financing arrangements entered into during the year;

e. Copies of the minutes of all regular and special meetings of the Associated Entity's board;

f. The portions of the 990 forms that are not publicly disclosed and all other federal and state tax returns; and

g. Any other documents and records which are relevant to the articulated reason.

## **J. Miscellaneous Requirements**

1. Associated Entity Communications-An Associated Entity must conduct business in its own name and all correspondence, advertisements, and other communications by the Associated Entity must clearly indicate that the communication is from the Associated Entity, and not from the Approving Institution or the University.

2. Lobbying and Political Activities-An Associated Entity must comply with all provisions of the Internal Revenue Code and all State laws regarding lobbying and political activity.

3. Associated Entity Courses and Seminars-An Associated Entity may not offer any course or seminar in which the University's name is used without first obtaining the permission the institution or institutions whose name will be used.



4. Destruction of Documents—An Associated Entity must have a policy governing retention and destruction of documents including electronic files and which prohibits destruction of documents if an investigation into wrongdoing or litigation is anticipated or underway.

**K. Waiver**

If the application of any of the requirements of these regulations to a particular Associated Entity in specific circumstances is of limited benefit and is unduly burdensome, the President may waive that requirement as to that specific Associated Entity under circumstances that are set out in writing. The Associated Entity shall notify the Chancellor of the Approving Institution prior to making a request for a waiver under this section.

**L. Effective Date**

Every Associated Entity shall be in compliance with these regulations no later than July 1, 2006.