

**Sarbanes-Oxley Workgroup Report**  
**Recommendations Regarding Implementation of Sarbanes-Oxley and NACUBO Best Practices**  
**Prepared for the Vice President of Finance for the North Carolina System**

Section	Sarbanes-Oxley Act Of 2002	NACUBO Best Practices Recommendations	Implement As-Is or already implemented Implement w/Modification Do not Implement or Not applicable	SOX Workgroup Comments & Recommendations
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Title I	Public Company Accounting Oversight Board (PCAOB)			
101-109	Describes public company accounting oversight board duties.	Not applicable.		Not applicable.
Title II	Auditor Independence			
201	Public accounting firms are prohibited from performing these non-audit services to financial statement audit clients: 1. Bookkeeping or other services related to the accounting records or financial statements; 2. Financial system design and implementation; 3. Appraisal or valuation services, fairness opinions, or contribution-in-kind reports; 4. Actuarial services; 5. Internal auditing outsourcing services; 6. Management or human resource functions;	Institutions should prohibit their independent auditors from providing the non-audit services prohibited by the Act unless extenuating circumstances exist, and the audit committee approves the work in advance.		Not applicable.  Comment: Auditor independence is not an issue for the universities since the State Auditor (as required by statute) performs the annual financial audits. The State Auditor does not perform non-audit services for profit. Should a university use an independent auditor for selected operations and these operations are material, then that university should comply with the NACUBO Best Practices regarding non-audit services.

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	7. Broker or dealer, investment adviser, or investment banking services; 8. Legal services and expert services unrelated to the audit; 9. Any other service the Accounting Oversight Board determines, by regulation, is impermissible.  A registered public accounting firm may engage in any other service, including tax services for an audit client, <i>but only if the Audit Committee approves the activity in advance.</i>			
202	The audit committee must pre-approve all services provided by the auditor.	Institutions should require pre-approval by the audit committee for all prohibited, non-audit services performed by the independent auditor.		Not applicable.  Comment: This is not an issue since the State Auditor does not perform non-audit services for-profit.
203	The lead (or coordinating) audit partner and the reviewing audit partner of the public accounting firm must rotate off the audit every five years.	Institutions should require a rotation of the lead partner every seven years with a timeout of two years.		Not applicable.  Comment: The State Auditor should determine the appropriate rotation.

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204	<p>The public accounting firm must report to the audit committee:</p> <ol style="list-style-type: none"> <li>1. All critical accounting policies and practices used by the client that have been discussed with management;</li> <li>2. All alternative treatments of financial information, ramifications of such use, and the treatment preferred by the public accounting firm;</li> <li>3. Other material written communication between the public accounting firm and management, such as the management letter or schedule of unadjusted differences.</li> </ol>	<p>Audit Committee oversight is critical to ensure the independence of the audit decisions.</p> <p>The audit engagement letter should be addressed to the audit committee rather than internal management.</p>		<p><b>Recommendation:</b> The Audit Committee of the Boards of Trustees should request the concurrence of the State Auditor's Office for reporting directly to the Committees items 1 and 2, and item 3 with respect to the schedule of unadjusted differences.</p> <p><b>Comment:</b> Currently, the engagement letters <u>are</u> addressed to the chancellors with copies sent to the CFOs, the controllers, and the chairs of the Audit Committees. The management letters <u>are</u> addressed to the chancellors and copies are sent to the CFOs and the Office of the President.</p>
205	Conforming amendments to the SEC Act of 1934.	Not applicable.		Not applicable.
206	The public accounting firm cannot have employed the CEO, controller, CFO, chief accounting officer, or any person in an equivalent position, during the one-year	Institutions should carefully consider the benefits of employing a CFO or controller who has worked for the auditing firm		<p>Will not recommend implementation.</p> <p><b>Comment:</b> In North Carolina, the State Auditor has no history of hiring</p>

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	period preceding the audit.	within the last year and consider how the position may relate to the institution's external audit. To forego the one-year waiting period, institutions should document the benefits and risks and seek board approval.		chancellors, CFOs or others involved with the audit of the universities. However, universities frequently hire State Auditor's staff due to their knowledge and experience within the system. A one-year waiting period could place an unnecessary burden on the universities and is not recommended.
207	The GAO will do a study on the potential effects of mandatory rotation of public accounting firms.	The current emphasis is on rotation of audit partners (section 203) rather than rotation of firms. The audit committee should annually evaluate the performance of the external auditor. In addition, the committee should consider periodically recompeting the selection of the external audit firm.		Not applicable.  Comment: Firm rotation is not an option since the State Auditor (as required by statute) performs the annual financial audits. Use of independent auditors is limited to selected operations within the universities, and if these operations are material, NACUBO Best Practices should be considered.
208-209	SEC final authority for Section 10A of the Securities Act of 1934 and considerations by appropriate State regulatory authorities.	Not applicable.		Not applicable.

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Title III Corporate Responsibility				
301	Public Company Audit Committees	Institutions that do not have an audit committee should assign the audit function to another committee of the board of trustees, for example, the finance committee, or to the board as a whole. Institutions that assign audit committee functions to another committee should add “audit” to the committee title, for example, “Finance and Audit” Committee.		Not applicable.  Recommendation: Each Board of Trustees should have an active committee of the Board that serves as an audit committee. The name “Audit” should be included in the official name of the committee.
301	(1) The Commission may prohibit the listing of securities of any firm found not to be in compliance with paragraphs 2-6 of this section.	(1) Not applicable		Not applicable.
301	(2) The audit committee shall be directly responsible for the appointment, compensation, and oversight of the work of any registered public accounting firm employed by its company and the public	(2) Audit committee involvement is critical in the selection of auditors and the performance of the audit.		Comment: The State Auditor has statutory responsibility for performing the universities’ annual financial audits. The audit committees would have no authority with respect to the State Auditor.

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	accounting firm shall report directly to the audit committee.			<p>Recommendation: Audit Committees of the Boards of Trustees should meet with representatives of the State Auditor's staff at least annually to review and discuss the financial reports, related audit activities and necessary corrective actions.</p>
301	(3) Each member of the audit committee shall be a member of the Board of Directors and shall otherwise be independent. Independent is defined as not receiving, other than for service on the Board of Directors, any consulting advisory, or other compensatory fee from the company, and not being an affiliated person of the company.	(3) Independence of audit committee members is important. Management representatives should not be voting members of the committee.		<p>Not applicable.</p> <p>Comment: All Audit Committee members would be trustees who are independent of the universities.</p>
301	(4) The audit committee shall establish procedures for: (a) The receipt, retention, and treatment of complaints received by the company regarding accounting, internal controls and auditing matters.	(4) A good practice would be the establishment of confidential complaint mechanisms for employees: for example, a hot line, anonymous e-mail/voicemail, secure complaint boxes, or		<p>Not applicable.</p> <p>Comment: Sarbanes-Oxley only addresses complaint mechanisms for accounting, internal controls and auditing matters related to financial reporting.</p>

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	(b) The confidential, anonymous submission by employees of questionable accounting or auditing matters.	extending existing employee grievance processes or communication channels to the institution's internal auditors. The audit committee should review the nature and disposition of reported matters.		Currently, the State Auditor's Office has a hot-line for reporting any improprieties within state government.
301	(5) The Audit Committee shall have the authority to engage independent counsel or other advisors, as necessary to carry out its duties.	(5) The audit committee should have all necessary authority contained in its charter.		<b>Recommendation:</b> The Audit Committees of the Boards of Trustees should develop charters that define their roles and responsibilities. Trustees have access to the Attorney General's office for legal advice.
301	(6) Each company shall provide appropriate funding as determined by the Audit Committee for payment to the public accounting firm and any advisors employed by the Audit Committee under paragraph 5 above.	(6) The charter should also specify that appropriate funding be available for the audit committee.		Not applicable.  Comment: The State Auditor bills the individual universities for audit services based on hours required to complete the audit of federal funds only.
302	The CEO and CFO shall certify along with the annual audit report that:	The provisions of the Act extend the current audit representation letter responsibilities. If		Comment: The CEOs and CFOs currently provide certifications to the State Auditor similar to those required by

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	<p>(1) They have reviewed the report;</p> <p>(2) Based on their knowledge, the report does not contain any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made not misleading;</p> <p>(3) Based on their knowledge, the financial statements present in all material respects the financial condition and results of operations;</p> <p>(4) They are responsible for establishing and maintaining internal controls, ensuring that material information relating to the company and its consolidated subsidiaries is made known to officers and others within those entities; have evaluated the effectiveness of internal controls within 90 days prior to the report; and have presented their conclusions about the effectiveness of their internal controls based on their</p>	<p>institutions publicly disclose financial statements, they should consider these assertions. However, be warned that assertion 4 includes new and complex affirmations on the adequacy of internal controls over both financial reporting and financial disclosures.</p> <p>The degree of centralization of financial operations is an important consideration for higher education. Business units' responsibility for financial reporting should be clearly defined, including policies for those activities. Institutions that are decentralized should consider implementing "sub-certification" requirements from financial</p>		Section 302.



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	<p>evaluation as of that date;</p> <p>(5) They have disclosed to the auditors and the audit committee all significant deficiencies and material weaknesses in the internal controls that could adversely affect the company's ability to record, process, summarize and report financial data;</p> <p>(6) They have indicated in the report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of their evaluation, including any corrective actions.</p> <p>Reincorporating outside of the United States does not lessen the requirements of Section 302.</p>	<p>leaders responsible for the financial results of units, departments or schools. The sub-certification provides assurance on the underlying numbers and controls.</p> <p>Institutions should start documenting their financial reporting process; and identifying and evaluating the adequacy of controls over financial reporting and other financial disclosures.</p> <p>The audit committee should consider periodic inquires of financial executives on the adequacy of controls.</p>		
303	It is unlawful for any officer or director of a company to take an action to fraudulently	This should be addressed in the institution's code of conduct/code		Recommendation: Include the following statement in a system-wide code of ethics

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	influence, coerce, manipulate, or mislead an auditor engaged in the performance of an audit for the purpose of rendering the financial statements materially misleading.	of ethics.		for all employees, “No employee, trustee or agent may take any action to fraudulently influence, coerce, manipulate, or mislead an auditor engaged in the performance of an audit for the purpose of rendering the financial statements materially misleading.”
304	If an accounting restatement is necessary due to misconduct, the CEO and CFO shall reimburse the company for any bonus or other incentive or equity-based compensation received by that person during the 12-month period following the issuance of the financial statements, as well as reimburse the company for any profits realized from the sale of securities of the company during that same 12-month period.	Not applicable.  However, the audit committee may want to review compensation arrangements for the CEO and CFO. Incentives related to financial results should be disclosed to the audit committee.		No further action required.  Comment: CEO (chancellor) compensation is approved by the Board of Governors. No senior executives have incentive arrangements related to financial results.
305	The SEC may issue an order to prohibit, conditionally or unconditionally, permanently or temporarily, any person who has violated section 10(b) of the 1934	Not applicable.  However, institutions should consider any SEC action in		Recommendation: An offer of employment for all senior officer positions should be made contingent on the outcome of a background

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	Act from acting as an officer or director of a company if the SEC has found that such person is unfit.	connection with hiring officers and nominating trustees; and ensure that employment contracts of senior officers allow removal for financial impropriety.		investigation. Appropriate legal review of this process must be performed so as to eliminate potential breach of employment.
306-308	Concerns sales of stock, fair funds for investors and attorneys practicing before the SEC.	Not applicable.		Not applicable.
<b>Title IV</b>	<b>Enhanced Financial Disclosures</b>			
401	SEC shall study off-balance sheet disclosures to determine their extent and whether GAAP results reflect the economics of such transactions.	Higher education should follow current and appropriate accounting standard guidance (i.e. FASB, GASB).		No action required.  Comment: Universities already follow GASB.
402	In general, it shall be unlawful for a company to extend personal loans to any director or executive officer.	The audit committee should be aware of and review policies on personal loans and understand that housing assistance included as part of compensation is not a personal loan.		Recommendation: The UNC system should adopt policies that prohibit universities or foundations from making personal loans to trustees or executive officers irregardless of the funding source. Additionally, any other loans to employees should only be from funds restricted for that purpose by donors. Loans to employees should be monitored

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				by the Controller's Office regardless of the source.
403	Directors, officers, and 10%+ owners must report designated equity security transactions by the end of the second business day following the day the transaction was executed.	The audit committee should be aware of and review policies on ownership interest in related ventures or start-ups. Existing conflict of interest policies can be leveraged and should be reviewed with the audit committee.		Not applicable.  Comment: Conflict of Interest policies already exist for trustees and senior administrative officers.
404	Each annual report shall contain an internal control report, which:  (1) States the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting; and  (2) Contains an assessment, as of the end of the fiscal year, of the effectiveness of the internal control structure and procedures of the company for financial reporting.	Identifying, designing, and maintaining controls and procedures that safeguard assets and minimize risk is sound business practice. A good business practice would be to start planning how an internal control assessment might be conducted. A few institutions have started doing risk assessments and documenting key financial processes. The audit committee should consider independence		Not applicable.  Comment: The resources and effort required to provide a positive assertion on internal control could be substantial, and may be ill-advised given limited university resources.

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	<p>The public accounting firm shall attest to the report on the internal control assessment made by management.</p>	<p>issues if contemplating using the external auditor for this review function. For reference, institutions can obtain a copy of the Committee of Sponsoring Organizations (COSO) model of an internal control framework. The COSO model is considered the most widely accepted model for controls.</p> <p>Institutions with internal audit departments should consider using them to periodically report on internal controls to the audit committee in addition to reporting to management. These activities should be coordinated with the risk assessment and internal control initiatives described above.</p> <p>The results of the internal control</p>		

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		<p>assessment should be tested to ensure compliance. A positive assertion on controls would require a large sustained effort and would require the external auditor to perform an attestation on internal controls, which would be expensive and time consuming. NACUBO does not recommend external auditor attestation or audit of internal controls. An alternative would be for management to provide the assertions and testing without the external audit attestation.</p> <p>NACUBO encourages institutions to take this topic seriously and start planning how an internal control assessment might be conducted. NACUBO will monitor the actions of institutions</p>		

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		and communicate discoveries. At this point, NACUBO and the APC are not aware of any institutions that have committed to this positive assertion on controls.		
405	Sections 401, 402, and 404 do not apply to any investment company registered under Section 8 of the Investment Company Act of 1940.	Not applicable.		Not applicable.
406	Requires each company to disclose whether it has adopted a code of ethics for its senior financial officers and the contents of the code of ethics.	A best practice is the adoption of a code of ethics for senior financial officers. Subsequently, the audit committee should review the adequacy of the code and periodically review how compliance is assured.		Recommendation: The UNC system should adopt a code of ethics for all employees of the university system. This program should be augmented by periodic workshops on ethical conduct for employees to gain an appreciation and understanding of their responsibility in this area.
407	Companies are required to disclose whether at least one member of the audit committee is a “financial expert”.  The final rule also provides a definition of	A best practice would be the inclusion of at least one financial expert on the audit committee. Institutions should consider the following in defining financial		Recommendation: The Board of Governors should discuss options for insuring trustee appointments that include individuals who understand financial data.

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	<p>a financial expert. In the final rule, recognition was given that an audit committee financial expert can acquire the requisite attributes of an expert in many different ways and that experience, in addition to education, is an important consideration.</p>	<p>expertise:</p> <ul style="list-style-type: none"> <li>familiarity with estimates, accruals, and reserves relevant to higher education</li> <li>longevity and experience with a given institution can be considered “other relevant experience.”</li> </ul> <p>Colleges and universities should also consider rotating the financial expert and begin planning for the process and cost of recruiting, training, and retaining financial expertise.</p> <p>The recruitment and retention of a financial expert by public institutions might be limited when alumni or elected officials appoint the board.</p>		<p>If a Board of Trustees is successful in gaining such an appointment, that individual should be expected to be a continuing member of the Audit Committee during his or her term on the Board, unless and until another person with comparable qualifications is appointed.</p>



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408-409	Addresses enhanced and real time disclosures by issuers of securities.	Not applicable.		Not applicable.
<b>Title V</b>	<b>Analyst Conflicts of Interest</b>			
501	Treatment of security analysts by registered securities associations and national security exchanges.	Not applicable.		Not applicable.
<b>Title VI</b>	<b>Commission Resources and Authority</b>			
601-604	Appearance and practice before the SEC, funding, federal court authority and qualifications of brokers and dealers.	Not applicable.		Not applicable.
<b>Title VII</b>	<b>Studies and Reports</b>			
701-705	Concerns studies regarding accounting firms, credit rating agencies, violators, violations, investment banks, financial advisors, and enforcement of securities laws.	Not applicable.		Not applicable.
<b>Title VIII</b>	<b>Corporate and Criminal Fraud Accountability</b>			
801-807	Discusses securities fraud, penalties, statute of limitations, sentencing, and employee protection.	Not applicable.  However regarding section 802, a good practice would be to ensure		Do not implement.  Comment: University records retention schedules for audit-related documents are

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		that documents and records sent or received in connection with the audit are retained for seven years.		designed to meet Federal and/or North Carolina's statutory requirements. No changes are advocated.
<b>Title IX</b>	<b>White Collar Crime Penalty Enhancements</b>			
901-906	This section advances criminal penalties for fraudulent acts and the US Department of Justice jurisdiction of financial statement certification. The certification requirement under section 906 is separate from the requirement under section 302.	Not applicable.		Not applicable.
<b>Title X</b>	<b>Corporate Tax Returns</b>			
1001	The chief executive officer, per the "sense of the senate," should sign the federal income tax return of a corporation.	Institutions should review the level of authority of signers on the various tax returns; a senior financial manager with financial accountability for the information presented on the tax return should sign the return.		Recommendation: The chief business officer of each university should designate, for each tax return, the senior financial manager(s) with financial accountability for information on the tax return who should sign the return.
<b>Title XI</b>	<b>Corporate Fraud Accountability</b>			
1101-1104	Discusses fines, consequences, and sentencing for individuals and issuers	Not applicable.		Not applicable.

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1105	Gives the SEC the authority to prohibit anyone convicted of securities fraud from being an officer or director of any publicly traded company.	Institutions should consider securities fraud convictions relevant in background checks for new employees.		<p>Recommendation:  As part of evaluating candidates for senior officer*** positions, the universities should consider the ramifications of hiring a candidate with a any type of fraud conviction before extending an offer of employment.</p> <p>***The term “senior officer” will need to be defined for consistency in system-wide application.</p>
1106-1107	Addresses criminal penalties under the SEC Act of 1934 and penalties for retaliation against informants.	Not applicable.		Not applicable.