North Dakota State Board of Higher Education
Audit Committee
Meeting Notice and Agenda
Friday, May 23, 2014

The State Board of Higher Education Audit Committee will meet via conference call originating from Bismarck State College, Horizon Building, conference room, 1815 Schafer St., Bismarck, ND 58501 on Friday, May 23, 2014 at 8:30 a.m. CST.

Call to Order

1. Opening Comments – Chair Neset
2. Approval of Agenda
3. State Auditor’s Office – Mr. John Grettum
4. Non-financial Reporting – Mr. John Grettum
5. Review Policy 302.2 – Chair Neset
6. IT Security – Dr. Lisa Feldner
7. Compliance – Ms. Kirsten Franzen
8. Proposed 2014-15 audit budget – Mr. Tim Carlson
9. Proposed 2015-17 biennial budget – Mr. Tim Carlson
10. Internal Audit Charter 802.8 – Mr. Tim Carlson
11. Future Meetings

Contact Kristie Hetzler (701) 328-2966 or Kristie.hetzler@ndus.edu prior to the scheduled meeting date if auxiliary aids or services are needed.
Defining Internal Control

Internal control is defined as follows:

Internal control is a process, effected by an entity’s board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting, and compliance.

This definition reflects certain fundamental concepts. Internal control is:

- **Geared to the achievement of objectives** in one or more categories—operations, reporting, and compliance
- **A process** consisting of ongoing tasks and activities—a means to an end, not an end in itself
- **Effectuated by people**—not merely about policy and procedure manuals, systems, and forms, but about people and the actions they take at every level of an organization to affect internal control
- **Able to provide reasonable assurance**—but not absolute assurance, to an entity’s senior management and board of directors
- **Adaptable to the entity structure**—flexible in application for the entire entity or for a particular subsidiary, division, operating unit, or business process

This definition is intentionally broad. It captures important concepts that are fundamental to how organizations design, implement, and conduct internal control, providing a basis for application across organizations that operate in different entity structures, industries, and geographic regions.

Objectives

The Framework provides for three categories of objectives, which allow organizations to focus on differing aspects of internal control:

- **Operations Objectives**—These pertain to effectiveness and efficiency of the entity’s operations, including operational and financial performance goals, and safeguarding assets against loss.
- **Reporting Objectives**—These pertain to internal and external financial and non-financial reporting and may encompass reliability, timeliness, transparency, or other terms as set forth by regulators, recognized standard setters, or the entity’s policies.
- **Compliance Objectives**—These pertain to adherence to laws and regulations to which the entity is subject.
Members of Audit Committee  
State Board of Higher Education  
North Dakota University System  

May 23, 2014

Dear Audit Committee:

We are pleased to have this opportunity to meet with you on May 23, 2014 to present our 2014 Audit and Communications Plan for the North Dakota University System (NDUS) fiscal year 2014 financial audit. Discussion of our 2014 plan with you ensures our audit team members understand your concerns and we agree on mutual needs and expectations to provide the highest level of service quality. Our plan has been developed to provide the NDUS with an efficient, high quality audit, which addresses the key risks and issues impacting the organization. Our plan also takes into account our responsibility to provide the Audit Committee and NDUS's management the Office of the State Auditor's insight on technical accounting and industry matters that may be of interest to you.

We look forward to meeting with you to present our audit plan, address your questions and discuss any other matters of interest to you.

Please feel free to contact me at 701-239-7289 with any questions you may have.

Very truly yours,

John Grettum, CPA  
Audit Manager
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Executive Summary

The North Dakota University system and its stakeholders expect us to deliver a high quality audit and this is our goal again this year. The Office of the State Auditor provides audits that are independent, objective, nonpartisan assessments of the stewardship and performance of government policies, programs or operations. Our mission is to provide innovative audit services designed to improve governmental operations and provide accountability for the benefit of the citizens of North Dakota.

What's New for 2014

From new accounting standards to audit planning here are some of the highlights:

- We revised due dates on our audit request letter that was sent to all campuses to correspond more accurately to when we needed the information for the audit in order to balance out the work load for the campus personnel and provide timely information to the ND Office of Management and Budget.
- The following are new accounting standards in place during fiscal year 2014:
  - Governmental Accounting Standards Board (GASB) Statement 65 – Items Previously Reported as Assets and Liabilities, amends or supersedes the accounting and financial reporting guidance for certain items previously required to be reported as assets or liabilities. This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities.
  - GASB Statement 66 – Technical Corrections – 2012 – an amendment of GASB Statements No. 10 and No. 62. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, and No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.
  - GASB Statement 67 – Financial Reporting for Pension Plans – an amendment of GASB Statement No. 25. The objective of this Statement is to improve financial reporting by state and local governmental pension plans. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency.
  - GASB Statement 70 – Accounting and Financial Reporting for Nonexchange Financial Guarantees. The objective of this Statement is to improve accounting and financial reporting by state and local governments that extend and receive nonexchange financial guarantees.

We anticipated minimum effect of these new accounting standards on the NDUS audit.
Looking Forward

We will continue adapt our audit to changing facts and circumstances. Below we highlight some of the changes that will impact your audit from 2015 and beyond:

• The following are new accounting standards that will require implementation in 2015 and beyond:
  o GASB Statement 68 – Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency.
  o GASB Statement 71 – Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB No. 68. The objective of Statement No. 71 is to improve accounting and financial reporting by addressing an issue in Statement No. 68, Accounting and Financial Reporting for Pensions, concerning transition provisions related to certain pension contributions made to defined benefit pension plans prior to implementation of that statement. This statement amends paragraph 137 of Statement No. 68 which limited recognition of pension-related deferred outflows of resources and deferred inflows of resources at the transition to circumstances in which it is practical to determine the amounts of all deferred outflows of resources and deferred inflows of resources related to pensions.

We anticipated GASB Statement 68 to a have major impact on the NDUS financial statements and we are unsure as to the actual audit impact at this time. At least some of the audit impact will depend on the audit work performed by the auditor of the plans.

Our Audit Objectives

As the NDUS’s auditor, we are responsible for reporting on numerous financial statements. In performing our audit for 2014, our primary objectives are as follows:

• Perform an audit of the North Dakota University System financial statements in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards (GAS), issued by the Comptroller General of the United States. The financial statements are comprised of the business-type activities and the aggregate discretely presented component units, including the related notes to the financial statements of the
NDUS. In connection with our audit, we will obtain reasonable rather than absolute assurance about whether the financial statements are free of material misstatement, whether caused by error, fraud, misappropriation of assets or violations of laws or governmental regulations.

- Communicate in writing to management and the Audit Committee all material weaknesses and significant deficiencies identified during the audit. In addition, we will include a management letter communication in writing to management and the Audit Committee all deficiencies in internal control, of consequence, over financial reporting identified during the audits.
- Complete other communications required under professional standards to the Audit Committee on a timely basis.

In meeting these objectives, we will do the following:
- Consult with management on a timely basis regarding accounting and financial reporting issues and ensure all matters of significance are reviewed and discussed with the NDUS Director of Financial Reporting and relevant campus personnel.
- Coordinate efforts with management to ensure that all significant financial statement components are subject to sufficient audit coverage.
- Evaluate changes in the NDUS's risk profile and internal controls to determine the nature, timing and extent of our testing of controls and substantive tests.
- Provide relevant expertise to facilitate the resolution of important issues.
- Report the results of our work to management and the Audit Committee including constructive observations relating to the NDUS's financial processes and controls.

We note that the campus foundations have separate audits of their financial statements and auditor's reporting on those foundations is directed to the individual foundation audit committees. Accordingly, this Audit and Communications Plan is not focused on the specifics of the campus foundations.

**Our Audit Approach and Risk Assessment**

Our audit strategy is based on:
- The use of a top-down, risk-based approach to planning and conducting an audit; and
- The application of well-reasoned professional judgment

These principles allow us to develop and execute our audit strategy in an effective and efficient manner.

**Significant Risks**

The designation of significant risks which is required by the professional auditing standards ensures that we place appropriate emphasis and testing on those areas most likely to cause a material financial reporting misstatement. Accordingly, as part of our audit planning, we identify certain audit areas as subject to significant risk of material financial reporting misstatement in the financial statements based on our knowledge of the NDUS. Such audit areas are subject to inherent or specific risks and complexities, critical accounting policies and/or significant judgments and estimates, as further described in the NDUS's consolidated financial statements, and are key considerations as we develop our current year audit approach. For the fiscal year
2014, we have not determined the significant risks yet, but based on our past experience we noted the following areas of concern in prior audits:

- **Management override of controls** – This is an area of presumed significant risk on all audit engagements. We perform testing on the appropriateness of journal entries and other adjustments, significant accounting estimates, and significant and/or unusual transactions to address this risk.
- **Turnover in financial staff at several campuses** – This is an area that may pose problems with accounting consistency and propriety.
- **Lack of comprehensive fraud and control risk assessment** – There is an indication of lack of monitoring of fraud and internal control risk system-wide.

### Areas of Audit Emphasis

In addition to the significant risk identified above, in past audits we have identified the areas below that were not considered significant risks but are areas of focus during the audit due to materiality of the balance or complexity/judgment involved in the accounting. Such audit areas are subject to material accounting policies and/or judgments and are considerations as we develop our current year audit approach. They include the following:

- Determination of which entities are to be included as component units under GASB reporting guidelines due to their significance and the nature of the NDUS's relationship with the entities.
- Treatment of related party transactions with the NDUS, as applicable to the separately-issued financial statements of the foundations.
- Presentation and disclosure of the financial statements.
- Cash and Investments
- Grants and contracts receivable
- Capital assets and depreciation expense
- Accounts payable and accrued payroll
- Bonds, notes and capital leases payable
- Proper classification of net position accounts
- Student tuition and fees
- Federal and nongovernmental grants and contracts
- Sales and services of educational departments
- Auxiliary enterprises
- Salaries and wages
- Operating expenses
- Scholarship and fellowship expenses
- Cost of sales and services expenses
- State appropriations
Audit Team

<table>
<thead>
<tr>
<th>Name</th>
<th>Position</th>
<th>Phone Number</th>
<th>Email Address</th>
</tr>
</thead>
<tbody>
<tr>
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</tr>
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Audit Timeline

We have developed the following reporting timeline that facilitates NDUS meeting the deadlines set by the Office of Management and Budget (OMB) in order for NDUS’s financial statements to be a part of the State of North Dakota’s Comprehensive Annual Financial Report (CAFR).

<table>
<thead>
<tr>
<th>Key Procedures Performed</th>
<th>Timing of Procedure</th>
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</thead>
<tbody>
<tr>
<td>Send out audit request letter</td>
<td>May 1, 2014</td>
</tr>
<tr>
<td>Send out engagement letter</td>
<td>May 12, 2014</td>
</tr>
<tr>
<td>Assess key audit risks and materiality</td>
<td>May – June 2014</td>
</tr>
<tr>
<td>Complete understanding of controls and complete preliminary audit plans of accounts</td>
<td>June – July 2014</td>
</tr>
<tr>
<td>Interim testing</td>
<td>June – August 2014</td>
</tr>
<tr>
<td>Complete audit programs</td>
<td>August – mid November 2014</td>
</tr>
<tr>
<td>Present any potential audit adjustments to NDUS</td>
<td>Mid November 2014</td>
</tr>
<tr>
<td>Present any draft recommendations</td>
<td>Mid December 2014</td>
</tr>
<tr>
<td>Office of State Auditor Final Report - Governance Communication Including the Report on Internal Control, Compliance, and Other Matters Issued</td>
<td>No later than 60 days after the opinion date</td>
</tr>
</tbody>
</table>

Mutual Understanding of Responsibilities

Office of the State Auditor’s Responsibilities

Our responsibility is to express an opinion, based on our audit, on the NDUS’s basic financial statements which includes the business-type activities, the aggregate discretely presented component units of the NDUS and the related notes to the financial statements. We conduct our audit in accordance with audit standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Government Audit Standards (GAS), issued by the Comptroller General of the United States. Those standards required that the auditor obtain reasonable rather than absolute assurance about whether the financial statements are free of material misstatement, whether caused by error, fraud, misappropriation
of assets or violations of laws or governmental regulations. Accordingly, a material misstatement may remain undetected. An audit is not designed to detect error or fraud that is immaterial to the financial statements. An audit includes obtaining an understanding of internal control sufficient to plan the audit and to determine the nature, timing and extent of audit procedures to be performed. An audit is not designed to provide assurance on internal control or to identify all significant deficiencies. However, as your auditor, we are responsible for ensuring that the Audit Committee is aware of any significant deficiencies or material weaknesses that come to our attention.

Our responsibility with respect to other information in documents containing audited financial statements is to read such information and consider whether the information or the manner of its presentation is materially consistent with the information appearing in the basic financial statements.

Our responsibility with respect to the Audit Committee communications is to convey those matters that have come to our attention as a result of the performance of our audit.

Our audit does not relieve management of its responsibilities with regard to the financial statements.

Management’s Responsibilities
As part of the audit process, management is responsible for the following:

- Preparing the NDUS’s financial statements in accordance with generally accepted accounting policies.
- Establishing and maintaining effective internal control over financial reporting.
- Identifying and ensuring that the University complies with the laws and regulations applicable to its activities.
- Making all financial records and related information available to the Office of the State Auditor.
- Providing the Office of the State Auditor with a letter confirming certain representations made during the audits.
- Adjusting the financial statements to correct material misstatements and affirming to the Office of the State Auditor in the representation letter that the effects of any uncorrected misstatements aggregated by the Office of the State Auditor during the current engagement pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Audit Committee’s Responsibilities
As part of the audit process, the Audit Committee is responsible for the following:

- Overseeing the reliability of financial reporting including the effectiveness of internal control over financial reporting.
- Reviewing and discussing the annual financial statements for the NDUS and determining whether they are complete and consistent with operational and other information known to the Audit Committee members.
- Understanding significant risks and exposures and management’s response to minimize those risks.
- Understanding the audit scope.
Communications and Planned Interactions

Our Communications Plan with Management

We communicate with management both in writing and verbally continuously throughout the audit. Examples of our ongoing communications include:

- Issues identification and resolution
- Internal Audit planning and coordination, as applicable
- Meetings with management at various campuses
- Planning discussions
- Discussions of draft audit recommendations
- Review of draft financial statements
- Monthly audit status updates

Our Communications Plan with the Audit Committee

Our communications with the Audit Committee are designed to comply with the standards established by the American Institute of Certified Public Accountants.

Our formal communications may occur via periodic meetings with the Audit Committee at various stages during the audit. We will also send our monthly audit status updates via email to keep the Audit Committee aware of any significant issues that have occurred during the audit. In addition, we will present the results of our audits upon completion. We generally communicate our significant findings at the conclusion of the audit. However, some matters could be communicated sooner, particularly if significant difficulties are encountered during the audit where assistance is needed to overcome the difficulties or if the difficulties may lead to a modified opinion.

In addition, we are also available, at any time, to respond to the Audit Committee members' questions.

Our Interaction with Internal Audit

Although our objectives and responsibilities are necessarily different from those of Internal Audit, the efforts of both our organizations may be complementary and provide a combined program of balanced audit coverage for the NDUS.

We consider Internal Audit to be a potentially effective and important element in the NDUS's overall internal control environment. We complete certain procedures when relying on their work, as follows:

- Reviewing on a timely basis Internal Audit reports and management responses.
- Understanding the Internal Audit plan, including the nature, timing and extent of work.
- Considering the impact of Internal Audit findings on our audit.

Materiality and Independence

Materiality

We consider both quantitative and qualitative factors in our assessment of materiality. We identify and assess the risk of material misstatement at:

- The overall financial statement level; and
In relation to classes of transaction, account balances and disclosures.

We use different materiality levels for our audit of the various financial statements including the consolidated statements and the discretely presented component units.

**Independence**

As auditors of the NDUS, we are subject to the standards set forth in the Government Auditing Standards (GAS) to ensure our independence. Our quality control processes include confirmation of independence by professional staff and training and are established to ensure our continuing independence.

**Perspectives on Fraud Risk**

We have a responsibility to plan and perform our audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error, fraud, misappropriation of assets or violations of laws or governmental regulations. In order to fulfill that responsibility, as part of our audit, we are required to gain an understanding of the risk of material misstatement due to fraud at the NDUS and perform certain procedures to respond to the fraud risk identified.

The oversight responsibilities of senior management and the Audit Committee and the auditor’s responsibilities related to fraud are outlined below:

<table>
<thead>
<tr>
<th>Management Responsibilities</th>
<th>Audit Committee Considerations</th>
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</thead>
<tbody>
<tr>
<td>• Design and implement programs and controls to prevent, deter and detect fraud (antifraud programs)</td>
<td>• Evaluate management’s identification of fraud risks, implementation of antifraud measures, and creation of appropriate “tone at the top”</td>
</tr>
<tr>
<td>• Ensure that the NDUS’s culture and environment promote honesty and ethical behavior</td>
<td>• Ensure that senior management implements appropriate fraud deterrence and prevention measures to better protect employees and stakeholders</td>
</tr>
<tr>
<td>• Perform a risk assessment that specifically includes the risk of fraud addressing incentives and pressures, opportunities, and attitudes and rationalization</td>
<td>• Investigate any alleged or suspected wrongdoing brought to its attention</td>
</tr>
<tr>
<td>• Assess management override of controls and communicate with the Audit Committee</td>
<td>• Challenge management in the areas of non-routine, related party and inter-institution transactions</td>
</tr>
</tbody>
</table>
| Office of the State Auditor's Role | • Plan and perform the audit to provide reasonable assurance that the financial statements are free of material misstatement, whether caused by fraud, error, misappropriation of assets or violations of laws or governmental regulations  
• Evaluate whether the NDUS's programs and controls that address identified risks of material misstatement due to fraud have been suitably designed and placed in operation  
• Evaluate management's process for assessing effectiveness of antifraud programs and controls  
• Evaluate fraud of any magnitude on the part of senior management and the impact on the control environment |

| Office of the State Auditor’s Procedures | In order to fulfill our responsibilities related to fraud, we plan to perform the following procedures:  
• Inquires of the management, the Chair of the Audit Committee, Internal Audit and others related to knowledge of fraud or suspected fraud, the fraud risk assessment process and how fraud risks are addressed by the NDUS  
• Analytical procedures  
• Incorporate an element of unpredictability in the selection of the nature, timing and extent of audit procedures to be performed annually  
• Identify and select journal entries and other adjustments for testing  
• Evaluate estimates and assumptions used by management that could have a material impact on the financial statements  
• Review Internal Audit reports and remain alert for matters that are indicators of fraud |
DSU still struggles with reporting student enrollment, audit finds

DICKINSON, N.D. – Two years after a performance audit highlighted issues with inflated enrollment at Dickinson State University, improvements are still needed on how the school reports its student enrollment, a report recently released by the North Dakota state auditor shows.

By: Nadya Faulx, Forum News Service

DICKINSON, N.D. – Two years after a performance audit highlighted issues with inflated enrollment at Dickinson State University, improvements are still needed on how the school reports its student enrollment, a report recently released by the North Dakota state auditor shows.

The operational audit, covering June 2011 to June 2013, found that DSU does not have proper controls for either student enrollment reporting or for determining student residency.

Regarding student enrollment, the report states: “Dickinson State University has not considered it necessary to adequately review the student enrollment reporting process and develop proper policies and procedures.”

The school had no procedures to document student admissions and enrollment, nor an independent review of enrollment numbers that are reported to the State Board of Higher Education and the Integrated Postsecondary Education Data System. The audit offered recommendations to limit the school’s risk of reporting an inaccurate picture of its student body, which, as of this spring, stood at 1,404 enrolled students – one of the university’s lowest enrollments in years.

An audit conducted in 2011 found that DSU artificially inflated enrollment numbers by counting people who attend workshops as enrolled students. The university’s president at the time, Richard McCallum, was terminated as a result of the findings.

Marie Moe, executive director of enrollment services and communication, said that since the audit was completed in spring 2013, the school has looked at the audit’s recommendations “in order to implement the process so that we are limiting error.

“We are constantly looking at the processes that are in place,” she said.

DSU, in its response to the auditor’s recommendations to strengthen its controls, agreed “that it is important to review (the) student enrollment reporting process.”

The university said it implemented new controls last fall “to ensure that enrollment statistics reported to state and federal agencies were correct” through a two-step process that involves checks at the departments and an independent review by the Office of Institutional Research.

“We have documented the process and mapped out what that’s going to look like” as the new processes are used going forward, Moe said.

The audit also found issues with student residency requirements.
In-state tuition for North Dakota residents was $5,718 for the 2012-13 academic year, while out-of-state students paid $7,980.

The report states that “proper controls have not been established for student residency determinations” or changes in residency status.

DSU responded in agreement to the audit’s findings. It wrote in the report that it has developed processes for initially determining residency that follow the North Dakota University System’s requirements developed in 2013.

The audit was completed a year ago. The university “has ample time to get things straight (and) hopefully make those improvements” before the next audit in two years, audit manager John Grettum said.

He said the report’s auditors “were pleased with the responses” they received from the university, and that they will “also be validating these responses” with the next audit to ensure the school follows through with addressing its issues with enrollment and residency reporting procedures.

Though DSU has room for improvement, it’s not alone. Auditors found similar problems throughout the university system, Grettum said.
NORTH DAKOTA STATE BOARD OF HIGHER EDUCATION
POLICY MANUAL

SUBJECT: GOVERNANCE AND ORGANIZATION    EFFECTIVE: February 27, 2014

Section: 302.2 Audit Committee

1. PURPOSE
   To assist the State Board of Higher Education (Board) in fulfilling its oversight responsibilities for the financial reporting process, the system of internal control, the audit process, and the North Dakota University System's (NDUS) process for monitoring compliance with laws, policies, regulations and the code of conduct.

2. AUTHORITY
   The Audit Committee has authority to conduct or authorize investigations into any matters within its scope of responsibility. It is empowered to:

   a. Appoint, compensate, and oversee the work of any registered public accounting firm employed by the organization.
   b. Resolve any disagreements between management and the auditor regarding financial reporting.
   c. Pre-approve all auditing and non-audit services.
   d. Retain independent counsel and request appointment of legal counsel by the attorney general as a special assistant attorney general, accountants, or others to advise the committee or assist in the conduct of an investigation.
   e. Seek any information it requires from employees (all of whom are directed to cooperate with the committee's requests) or external parties.
   f. Meet with officers, external auditors, or outside counsel, as necessary.

3. COMPOSITION
   The Audit Committee will consist of three voting members of the Board. The Board president will appoint committee members and the committee chair and may also appoint additional SBHE faculty and staff advisors, as ex-officio non-voting members. Each committee member will be both independent and financially literate.

4. MEETINGS
   The committee will meet at least four times a year, with authority to convene additional meetings, as circumstances require. All committee members are expected to attend each meeting, in person or via teleconference or video-conference. The committee will invite members of management, auditors or others to attend meetings and provide pertinent information, as necessary. It may hold executive sessions in
compliance with law. In compliance with law, meeting agendas will be prepared, and provided in advance to members, along with appropriate briefing materials. In compliance with law, minutes will be prepared.

5. RESPONSIBILITIES
The committee will carry out the following responsibilities:

a. Financial Statements:

i. Review significant accounting and reporting issues, including complex or unusual transactions and highly judgmental areas, and recent professional and regulatory pronouncements, and understand their impact on the financial statements.

ii. Review with management and the external auditors the results of the audit, including any difficulties encountered.

iii. Review the annual financial statements, and consider whether they are complete, consistent with information known to committee members, and reflect appropriate accounting principles.

iv. Review other sections of the annual report and related regulatory filings before release and consider the accuracy and completeness of the information.

v. Review with management and the external auditors all matters required to be communicated to the committee under generally accepted auditing Standards.

vi. Understand how management develops interim financial information, and the nature and extent of internal and external auditor involvement.

vii. Review interim financial reports with management and the external auditors and consider whether they are complete and consistent with the information known to committee members.

b. Internal Control:

i. Consider the effectiveness of the university system's internal control system, including information technology security and control.

ii. Understand the scope of internal and external auditors' review of internal control over financial reporting, and obtain reports on significant findings and recommendations, together with management's responses.

c. Internal Audit:

i. Approve an internal audit charter.
ii. Ensure there are no unjustified restrictions or limitations, and review and concur in the appointment, replacement, or dismissal of the chief auditor.

iii. Approve the annual audit plan and all major changes to the plan. Review the internal audit activity's performance relative to its plan.

iv. Review with the chief auditor the internal audit budget, resource plan, activities, and organizational structure of the internal audit function.

v. At least once per year, review the performance of the chief auditor and recommend the annual compensation and salary adjustment.

vi. Review the effectiveness of the internal audit function, including conformance with The Institute of Internal Auditors' the Definition of Internal Auditing, Code of Ethics and the International Standards for Professional Practice of Internal Auditing.

vii. On a regular basis, meet with the chief auditor to discuss relevant matters.

d. External Audit:

i. Review the external auditors' proposed audit scope and approach, including coordination of audit effort with internal audit.

ii. Review the performance of the external auditors.

iii. On an 'as-needed' basis, meet with the external auditors to discuss relevant matters.

e. Compliance:

i. Review the effectiveness of the system for monitoring compliance with laws and regulations and the results of management's investigation and follow-up (including disciplinary action) of any instances of noncompliance.

ii. Review the findings of any examinations by regulatory agencies, and any auditor observations.

iii. Review the process for communicating the code of conduct to Board members and university system personnel, and for monitoring compliance therewith.

iv. Obtain regular updates from management and Board and university system legal counsel regarding compliance matters.

f. Reporting Responsibilities:

i. Regularly report to the Board about committee activities, issues, and related recommendations.
ii. Provide an open avenue of communication between internal audit, the external auditors, and the Board.

iii. Review any other reports the company issues that relate to committee responsibilities.

**g. Other Responsibilities:**

i. Perform other activities related to this policy as requested by the Board.

ii. Institute and oversee special investigations as needed.

iii. Review and assess the adequacy of the committee policy annually, requesting Board approval for proposed changes, and ensure appropriate disclosure as may be required by law, policy or regulation.

iv. Confirm annually that all responsibilities outlined in this policy have been carried out.

v. Evaluate the committee's and individual members' performance on a regular basis.

**HISTORY:** New Policy, SBHE Minutes, February 27, 2014.
NORTH DAKOTA STATE BOARD OF HIGHER EDUCATION
POLICY MANUAL

SUBJECT: MISCELLANEOUS  EFFECTIVE: January 31, 2003

Section: 1901.2 Computing Facilities

All employees, students and other users of North Dakota University System computing and networking resources shall comply with applicable laws, policies and procedures. The chancellor shall adopt procedures establishing rules governing access to and use of computing and networking resources.

REFERENCE: NDUS Procedure 1901.2

1. Every NDUS employee who uses data as part of the employee’s job (whether entering, extracting, analyzing or reporting data) is responsible for the quality of the data and using it as described in the data element dictionary.

2. The NDUS System Information Technology Services is responsible for managing the Data Element Dictionary in consultation with NDUS institutions. The data elements include fields (dimensions) used in computer systems and calculations (facts) made with that data from which institution and university system reports are drawn. By standardizing the data going into the systems, and standardizing calculation formulas, reporting will be more reliable and comparable between campuses.

REFERENCE:

The Case for Compliance Programs: The Legal and Policy Mandates

NACUA CLE Program
November 2011

Program Speakers:
John Hansen, Center for Business Ethics, Bentley University
Christopher Myers, Holland & Knight LLP
Bart Schwartz, SolutionPoint International, Inc

Robert Roach, Moderator, New York University
Introduction:
The Case for Compliance

The ultimate mission of every college and university is to create and communicate human creativity and knowledge through research, teaching, and free expression of artistic endeavors. Honesty and integrity are necessary hallmarks of all that we do in higher education.

For knowledge to be advanced and the free exchange of ideas to be undertaken successfully, truthfulness, individual accountability, and ethical behavior are necessary companions; anything less compromises our commitment to academic excellence and merit as prevailing values.

Just as this is true in our academic enterprise, so must it be true in our other activities: our co-curricular activities, our operations, and our administration of our institutions of higher education—the entire range of activities that make up university life and external interactions. While different activities—be they academic, financial, administrative, operational, or other—may be governed by the application of different specifics, they must all be bound by a common high standard of ethical and honest behavior.

University\(^1\) faculties have published the results of significant research on how organizations can create and maintain ethical environments and a commitment to compliance with the law. Higher education has “talked the talk.” Our institutional mission to create and communicate human creativity and knowledge and advance the free expression of ideas likewise calls upon our academic and administrative leaders to “walk the walk” by building effective ethics compliance programs.

In the paper below, we set forth “the Case for Compliance” based on three principles:

A. The Legal Case for Compliance: Universities should have ethics and compliance programs to ensure they fulfill their U.S. and international legal and regulatory obligations.

B. The Value Case for Compliance: Ethics and compliance programs enhance the university’s community culture.

C. The Business Case for Compliance: Academic, business and administrative processes benefit from ethics and compliance programs.

\(^{1}\) For easy and consistency, in this article we will refer to an institution of higher education, whether it is a community college, four year college or a university, as a “university.”
A. The Legal Case for Compliance:

*Universities should have ethics and compliance programs to ensure they fulfill their U.S. and international legal and regulatory obligations.*

Attorneys practicing higher education law often discuss the question, “Is it necessary for a university to have a compliance program”? The simple answer is “yes.” Universities operate in an environment governed by a vast and constantly changing array of federal, state and local regulations. The sheer number of these laws, their complexity and the gravity of violating many of these regulations necessitates a comprehensive and effectively maintained compliance program.²

The risks for a university operating without an effective compliance program are great than ever. For example, recent amendments to the federal False Claims Act (FCA) significantly increase risk for universities. These amendments now:

- Trace federal funds through grants and subcontracts;³
- Expand reverse false claims;⁴
- Cover failure to return overpayments;⁵
- Expand whistleblower protections.⁶

Given the increased complexity of the regulatory landscape and increased economic risks resulting from non-compliance, Universities should consider the Federal Sentencing Guidelines for Organizations and other statutory provisions discussed below.

1. The U.S. Federal Sentencing Guidelines for Organizations

a. A Short History of Compliance

1986 - Defense Industry Initiative on Ethics and Conduct

The Defense Industry Initiative (DII) is generally considered the beginning of formal organizational ethics and compliance programs. During the 1980s, allegations of fraud and government mismanagement resulted in a Presidential Blue Ribbon Commission on Defense Management (called referred to as the “Packard Commission”).

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² See Holland & Knight, Corporate Compliance Answer Book, Chapter 32 Institutions of Higher Education, p 1113-1116 (Practicing Law Institute 2011)
⁵ 31 U.S.C. § 3729(b)(3).
The Commission found that public confidence in the defense industry had been eroded by reports of waste, fraud and abuse within both the industry and the Defense Department. The Commission concluded that the defense acquisition process, the defense business environment, and confidence in the defense industry could be improved by placing greater emphasis on corporate self-governance. Subsequently, several leading defense contractors voluntarily joined together to establish the DII, which had three main purposes:

- To nurture and promote a culture of ethical conduct within every company in the defense industry;
- To promote self-governance as a means of confirming management's commitment to abide by ethical standards – even when they exceed legal requirements – and of discovering and correcting instances when conduct falls below these standards; and
- To share best practices in dealing with ethics and business conduct issues, which included the development of formal Codes of Ethics and mandatory ethics training for employees, internal "hotlines" and other reporting mechanisms, with a promise of no retaliation.

However, the 1980's were rife with corporate corruption scandals that extended well beyond the defense industry. (Anyone remember Ivan Bosky, Michael Milken and "Junk Bonds"?) These scandals lead to additional programs designed to encourage greater corporate self government.


The Federal Sentencing Guidelines were created by the U.S. Congress in 1984 to provide certainty and fairness in sentencing and to avoid unwarranted sentencing disparities. The Federal Sentencing Guidelines also sought to maintain sufficient flexibility to permit individualized sentencing when warranted through use of mitigating or aggravating factors. Congress also created the United States Sentencing Commission which was delegated the responsibility for periodically reviewing and amending the Guidelines.

In response to corporate corruption scandals, the U.S. Federal Sentencing Commission submitted to Congress in 1991 amendments to the Federal Sentencing Guidelines that established a set of standards to govern the sentences federal judges impose on organizations convicted of federal crimes. The intent of the new organizational sentencing guidelines was to "prevent and deter organizational wrongdoing" by providing credit to organizations with "an effective program to prevent and detect violations of law."7 These amendments were also designed to encourage greater self governance efforts. Under these Guidelines, the hallmark of an effective ethics and compliance program was "due diligence in seeking to prevent and detect criminal conduct."8

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8 Id.
c. The 2004 Amendments to the Federal Sentencing Guidelines for Organizations

The Enron and WorldCom scandals of 2001 and 2002 caused a period of reflection on the effectiveness of corporate self governance and compliance efforts. In 2004, the Federal Sentencing Guidelines were amended to require more than simple legal compliance to prevent and detect criminal conduct. The guidelines were amended to reflect the growing consensus among policy makers\(^9\) that in order to have an effective compliance program, an organization must establish and maintain an organizational culture that "encourages ethical conduct and a commitment to compliance with the law."\(^{10}\)

The 2004 Amendments also added an "eighth" element of an effective compliance program. The new Guidelines provided that, "In implementing [an effective compliance program], the organization shall \textit{periodically assess the risk of criminal conduct} and shall take appropriate steps to design, implement, or modify each requirement [for an effective compliance program] to \textit{reduce the risk of criminal conduct} identified through this process."\(^{11}\)

d. The 2010 Amendments to the Federal Sentencing Guidelines for Organizations

In 2010, the Federal Sentencing Guidelines were again amended to include the following provisions:

- **Reporting Requirements:** High level personally must have regular and direct access to the Board or appropriate committee (e.g. Audit Committee) to report at least annually on the compliance and ethics program. If criminal conduct is detected high level compliance personnel must have prompt access to the Board.\(^{12}\)

- **Response to Criminal Conduct.** If criminal conduct is detected an organization must consider: restitution or other reparations to victims; self-disclosure and cooperation with the government; and amendments to its compliance program to ensure further criminal conduct does not occur.\(^{13}\)

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\(^9\) Section 805(a)(2)(5) of the Sarbanes-Oxley Act directed the Federal Sentencing Commission to review and amend, as appropriate, the Federal Sentencing Guidelines and related policy statements to ensure that the guidelines that apply to organizations "are sufficient to deter and punish organizational criminal misconduct."

\(^{10}\) U.S. Federal Sentencing Guidelines §8B2.1(a)(2)

\(^{11}\) U.S. Federal Sentencing Guidelines §8B2.1(a)(2)


As amended, the U.S. Federal Sentencing Guidelines for Organizations provide the following elements for an effective compliance program:

**e. Federal Sentencing Guidelines for Organizations: Elements of an Effective Ethics and Compliance Program**

In order to be effective, an organization's ethics and compliance program must include:

1. High level company personnel who exercise effective oversight. Individual(s) with day-to-day responsibility must have the authority to report directly to the Board or an appropriate subcommittee: (a) at least annually regarding the effectiveness of the program, and (b) promptly if criminal conduct is discovered.

2. Written policies and procedures/Code of Ethical Conduct.

3. Compliance and ethics training and education.

4. Lines of communication, including anonymous reporting lines and a policy of non-retaliation.

5. Standards enforced through well-publicized disciplinary guidelines.

6. Internal compliance monitoring.

7. Response to detected offenses and corrective action plans. If criminal conduct is detected, the organization restitution or other reparations must be made, if appropriate; the criminal conduct should be reported and the organization should cooperate with government officials; the compliance program accessed and amended to ensure further criminal conduct does not occur; and

8. Periodic risk assessments


**i. General applicability**

The Federal Sentencing Guidelines for Organizations apply when the convicted defendant is an organization. According the Federal Sentencing Guidelines Manual, Commentary 8A.1.1
"Organization" means "a person other than an individual." 18 U.S.C. § 18. The term includes corporations, partnerships, associations, joint-stock companies, unions, trusts, pension funds, unincorporated organizations, governments and political subdivisions thereof, and non-profit organizations. (Emphasis added)

ii. Fiduciary Responsibility

1996 - In re Caremark International Inc. Derivative Litigation,

In Caremark, the Delaware Chancery Court was asked to review a proposed settlement of litigation against the company's directors. The company engaged in illegal payments in violation of the federal anti-referral payments law. The suit alleged that the company's directors' breached their fiduciary responsibility to the shareholders through a lack of proper oversight.

The Caremark court stated, in effect, that a board of directors has a fiduciary responsibility to assure that the company has an effective compliance program following the Federal Sentencing Guidelines. According to the court,

Any rational person attempting in good faith to meet an organizational governance responsibility would be bound to take into account [the Federal Sentencing Guidelines] ... and the opportunity for reduced sanctions....

The Caremark decision was upheld by the Delaware Supreme Court in Stone v Ritter, 911 A.2d 362 (Del.Sup. 2006).

iii. Other Federal and State Regulations

In recent years, other federal laws and guidelines have been amended or promulgated that require recipients of federal funds to have effective ethics and compliance programs, including the Federal Acquisition Contracting Regulations (FAR); the Deficit Reduction Act (Medicaid); and the Health and Human Services Office of Inspector General (HHS OIG) Guidelines.

States have also mandated compliance programs. For example, organizations in New York that receive Medicaid funding must have compliance programs that comply with specific regulatory requirements.

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14 698 A.2d 959 (Del Ch. 1996).
17 http://oig.hhs.gov/compliance/compliance-guidance/index.asp
18 18 NYCRR Part 521.
iv. International Laws and Standards

More than ever, Universities are actively developing international operations, including overseas campuses. Thus, they must also be cognizant of international compliance requirements. For example:

- **OECD Compliance Guidelines:** In February 2010 the Organization for Economic Cooperation and Development (OECD) adopted a “Good Practice Guidance” framework that was addressed to companies for establishing and ensuring the effectiveness of internal controls, ethics, and compliance programs for preventing and detecting the bribery of foreign public officials in their international business transactions. The Guidance recognizes that to be effective, such compliance programs should be interconnected with a company’s overall compliance framework. ¹⁹

- **U.K. Bribery Act 2010:** The Bribery Act creates the following offences: Active bribery: promising or giving a financial or other advantage; Passive bribery: agreeing to receive or accepting a financial or other advantage; Bribery of foreign public officials; The failure of commercial organisations to prevent bribery by an associated person (corporate offense). ²⁰ The Act’s provisions are more aggressive that the U.S. Foreign Corrupt Practices Act in that they cover commercial bribery and do not provide an exception for small “facilitating payments” to foreign officials. ²¹


a. COSO Background and Summary:

While the Federal Sentencing Guidelines for Organizations were being developed, a group of leading public accounting organizations called the Committee of Sponsoring Organizations (COSO) joined together to address perceived deficiencies in financial accounting practices. COSO’s report *Internal Control – Integrated Framework* sets forth a methodology for helping assure ethical and legally compliant accounting and financial reporting practices. ²² The COSO report sets forth a comprehensive risk

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²¹ Other countries have similar corporate ethics and compliance guidelines. See e.g. King II Corporate Governance Principles of South Africa. [https://www.saica.co.za/TechnicalInformation/LegalAndGovernance/King/tabid/626/language/en-ZA/Default.aspx](https://www.saica.co.za/TechnicalInformation/LegalAndGovernance/King/tabid/626/language/en-ZA/Default.aspx)
²² [http://www.coso.org/guidance.htm](http://www.coso.org/guidance.htm)
assessment methodology and a process for establishing a system of internal controls designed to achieve: effectiveness and efficiency of operations; reliability of financial reporting, and compliance with applicable laws and regulations.\textsuperscript{23} The COSO standards further advise:

- Integrity and ethical values of the people who create, administer and monitor internal controls ... are essential elements of the control environment.”
- The ethical “tone at the top” is critical to effective internal controls.
- Audit committees should help assure that “ethical values be communicated” and “explicit guidance ... be given” to an entity’s staff.

b. COSO Internal Control Framework

The following illustrates and explains the COSO framework:

- Each section of the pyramid is critical to a successful integrated compliance program
- Monitoring = assessing compliance controls through on-going activities and evaluations, with modifications made as appropriate.
- Control Activities = compliance policies and procedures.
- Information and Communication = clear message from top management to all personnel that control responsibilities must be taken seriously and embrace their own role in the internal control system. Ready means for personnel to communicate information upstream.
- Risk Assessment = The identification and analysis of risks relevant to achieving NYU’s objectives, including financial, operational, reputational, legal and regulatory.
- Control Environment = The environment in which personnel operate, including the people, their individual attributes, and expectations for integrity, ethical values and competence — and create the environment in which they operate.

c. COSO Applicability to Universities

The COSO Internal Control Framework is applied to Universities by:

- OMB Circulars A-133\textsuperscript{24} and Compliance Supplement\textsuperscript{25}
- AU 110 and SAS 78 Auditing Standards\textsuperscript{26}
- PCAOB 5 Auditing Standards\textsuperscript{27}

\textsuperscript{23} Id.
\textsuperscript{24} http://www.whitehouse.gov/sites/default/files/omb/circulars/a133/a133.pdf
\textsuperscript{25} http://www.whitehouse.gov/omb/circulars/a133_compliance_supplement_2011
\textsuperscript{26} http://www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AU-00110.pdf
\textsuperscript{27} http:// pcaobus.org/Standards/Auditing/Pages/Auditing_Standard_5.aspx

Despite the efforts in the 1990's to encourage compliance and good self governance, corporate corruption scandals continued to unfold, including the Enron and WorldCom corporate scandals. As a result of these scandals, Public Law 107–204 (the Sarbanes-Oxley Act or "SOX") was passed.

SOX Section 406 requires that as part of "internal controls" public companies must adopt and publish a Code of Ethics which promotes:

- Honest and ethical conduct;
- Avoiding conflicts of interest;
- Full, fair, accurate, timely and understandable disclosures;
- Compliance with government laws, rules and regulations;
- Internal reporting of violations of the code, and
- Accountability for adherence to the code.

While most of the provisions of SOX are limited to public companies, the National Association of College and Business Officers (NACUBO) have analyzed SOX and recommended that Universities follow certain provisions, including SOX Section 406, as best practices.28

Additionally, recent amendments to SOX have made its whistleblower protections applicable to all organizations.29 Any employee who files a complaint, gives testimony, provides information or otherwise assists in an SEC, Congressional or law enforcement investigation is protected. Under SOX, an employee whistleblower may not be harmed or discriminated against in the terms and conditions of employment because of any lawful act done as a whistleblower. 30

B. The Values Case for Compliance:

1. Effective Ethics and Compliance Programs Can Enhance A Values-Based Community Culture in Higher Education

In higher education, the process of building an effective compliance program starts with a handicap – the name. Look in Black's Law Dictionary, for example, and you will see "compliance" defined as, "Submission, obedience, conformance." Clearly, an

28 See e.g. NACUBO and PriceWaterhouseCoopers Sarbanes Summit: Taking the Right Path, and NACUBO Checklist for Higher Education (NACUBO recommendations regarding Sarbanes-Oxley Act of 2002).
29 SOX §§806, 1107.
30 Id.
ethics and compliance program based primarily on mandated submission and obedience will not be well received on most American campuses.

Nowadays, instead of submission and obedience we need to think of compliance programs as a reflection of an organizational culture that is defined by norms or beliefs shared by the university community. This culture is shaped by the organization’s leadership and is often expressed in terms of shared values and guiding principles. In turn, these values and principles are reinforced by systems and procedures implemented throughout the organization. Together, these values, guiding principles, systems and procedures form a University’s compliance program.

The concept of compliance as “shared values” driven by organizational leadership was described by Lynn Sharpe Paine, in Managing for Organizational Integrity, Harvard Business Review (March-April 1994). According to Paine, it is the responsibility of an organization’s leadership to:

Define and give life to an organization’s guiding values, to create an environment that supports ethically sound behavior, and to instill a sense of shared accountability among employees . . . The need to obey the law is viewed as a positive aspect of organizational life, rather than an unwelcomed constraint imposed by external authorities.

Thus, a university ethics and compliance program should reflect the shared values of the university community and its leadership. These values should embrace a desire to fulfill the university’s academic mission with integrity and include a commitment to establishing systems and procedures designed to ensure that the university’s legal, regulatory and ethical responsibilities are fulfilled.

A “shared values” compliance program may be summarized by the following philosophy, processes and expected results:

- **Philosophy**

  The organization clearly communicates, not just by word, but by deed, high ethical values that are shared by employees.

- **Process**

  As social beings we are guided by values and ideals that are often shared with our peers. With shared values compliance, the community engages in self governance according to chosen standards that:
  - Reflect organizational values & standards;
  - Are management driven (i.e. they are not driven by lawyers, but guided by lawyers who advise managers on their legal obligations) and integrated by management (not lawyers) into organizational systems, and
  - Provide guidance that enables responsible conduct.
• **Expected Results**

If members of the community are socially motivated to follow the rules, they will do so because they share organizational beliefs. Thus, their behavior is more strongly voluntary – they defer rather than simply comply. Surveillance and sanctioning are less necessary and people are more likely to follow rules “when no one is watching.”

2. **All Members of the University Community Can Enhance A Values-Based Ethics and Compliance Program**

While ethics and compliance programs must have the visible support of university leadership to succeed, there are statistically validated processes that encourage values-based ethics and compliance programs; cost little to implement, and at the same time, promote a more satisfied and effective workforce.

One process such process is to adopt *procedural justice* in management and organizational decision making. The concept of applied procedural justice is described in Tyler, Dienhart, Thomas, *The Ethical Commitment to Compliance: Building Value-based Cultures That Encourage Ethical Conduct and a Commitment to Compliance*, California Management Review (February 2008):

Procedural justice is important because it shapes the extent to which it is possible to build a values-based ethical culture....Not only do procedurally just cultures promote compliance, they also increase the probability that employees will become committed to their organizations’ values and go beyond their job description to help their organization succeed. In particular, employees will voluntarily follow the rules.

There are four key procedural justice ideas: Voice, Neutrality, Respect, and Trust. The concept of Voice is simple – people want to have an opportunity to tell their side of the story in their own words. Thus, managers should listen to people. Give them a chance to explain their side of the story. Once people have done so, they are very willing to defer to decisions even if the decisions are adverse.

Managers must be neutral decision makers. People bring their problems to authorities when they view them as neutral, principled, decision makers who make decisions based on rules and values, not personal opinions and apply rules consistent with values across people and over situations.

Authorities are representatives of the organization. People draw a message about their status in an organization from the way they are treated by these authorities. Respect communicates high status and value. Disrespect suggests that you are marginal and unimportant.

12
Managers must earn the trust of their employees. Studies constantly show that the central attribute influencing evaluations about organizational judgments are about the character of the decision makers – are they sincere and caring; are they listening to and considering people’s views; are they trying to do what is right for everyone involved; and are they acting in the interests of the parties, not out of personal prejudice?

3. Suggested Readings on Values-Based Ethics and Compliance Programs

- Weaver, Trevino, *Compliance and Values Oriented Ethics Programs: Influences on Employees’ Attitudes and Behavior*, Business Ethics Quarterly (April 1999)
- Leading Corporate Integrity: *Defining the Role of the Chief Ethics & Compliance Officer (CECO)*, Ethics Resource Center (2008)
- Tyler, Dienhart, Thomas, *The Ethical Commitment to Compliance: Building Value-based Cultures That Encourage Ethical Conduct and a Commitment to Compliance*, California Management Review (February 2008)
- Roach, Davis, *Establishing a Culture of Ethics and Integrity in Government*, Ethikos (September-October 2007).

C. The Business Case for Compliance:

*Academic, business and administrative processes benefit from ethics and compliance programs*

Effective compliance programs can serve as both a sword and a shield for Universities. As a shield, a compliance program can help protect universities from fines and penalties, false claims act/qui tam claims, reputational loss, operational loss and disruption, and agency and court imposed compliance programs.\(^{31}\)

As a sword, effective compliance programs can increase the effective of business processes. Independent research studies, published university research findings and corporate surveys have established that organizations with effective compliance

\(^{31}\) See generally Holland & Knight, Corporate Compliance Answer Book, Chapter 32 Institutions of Higher Education (Practicing Law Institute 2011) for a historical discussion of Universities who suffered from fines, damages and other losses resulting in part for insufficient compliance controls.
programs have lowered cost of capital and credit; higher levels of growth and profitability; better access to talent and information sharing among employees, and enhanced reputation.
### Internal Audit Budget Plan - Remainder of FY14 and FY15 - Draft

| Campus Assessment | FY14 | | FY15 | | | | | Projected FY14 and FY15 Budget |
|-------------------|------|---|------|---|------|---|---|---|---|
|                   | (1)  | (2) | (3)  | (4) | (5)  | (6) | (7) | (8) | (9) |
| Tim Carlson       | $135,000.00 | $94,173.00 | $7,850.00 | $102,023.00 | $139,050.00 | $172,625.00 | $15,700.00 | $188,325.00 |
| Vacant position   | $        | $     | $     | $     | $80,000.00 | $108,517.00 | $15,700.00 | $124,217.00 |
| TeamMate audit software | $13,000.00 | $13,000.00 | | | | $7,200.00 | $7,200.00 | $319,742.00 | $434,765.00 |
| NDUS Office Budget | | | | | | | | | |
| New position      | | | | | $70,000.00 | $96,436.00 | $15,700.00 | $112,136.00 |
| New position      | | | | | $70,000.00 | $96,436.00 | $15,700.00 | $112,136.00 |
|                   | | | | | $224,272.00 | $224,272.00 | | |
| Transfer Funds    | $385,982.00 | | | | $385,982.00 | | | $771,964.00 |
| TOTAL             | | | | | $1,431,001.00 | | | | |

1/ assumes legislatively appropriated 3% salary increase for positions in place prior to 7/1/14

![7 FTE's](image)
### Summary - Estimated Total Cost (and State Increase) to Fund 2015-17 Internal Audit Positions and Eliminate Campus Assessments

<table>
<thead>
<tr>
<th>Assumes 4% Annual Salary Increases</th>
<th>Assumes 3% Annual Salary Increases</th>
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<tbody>
<tr>
<td></td>
<td>2015-17</td>
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<tr>
<td></td>
<td>FY16</td>
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<tr>
<td>Est cost of 7 FTE funded in FY15:</td>
<td></td>
</tr>
<tr>
<td>Salaries &amp; FB (7 FTE; 5 filled, 1 vacant, 1 new)</td>
<td>$875,897</td>
</tr>
<tr>
<td>Operating:</td>
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<tr>
<td>$15,700 per FTE</td>
<td>109,900</td>
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<tr>
<td>TeamMate audit software mtnce &amp; hosting (8 @ $1,250/yr, included Hetzler)</td>
<td>10,000</td>
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<tr>
<td>Total Estimated Expenses</td>
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<tr>
<td>Less:</td>
<td></td>
</tr>
<tr>
<td>State funding - UND/NDSU Transfer</td>
<td>($771,964)</td>
</tr>
<tr>
<td>Add'l funding - $200,000 FY15 from NDUS Office</td>
<td>($200,000)</td>
</tr>
</tbody>
</table>

| 15-17 State increase to fund 7 FTE, assuming no campus assessments & $200,000 (from NDUS Office) in base | $1,054,034 | ✓ |

| Est cost of 3 additional FTE and consultant proposed to be funded 01/01/15: |         |         |          |         |         |          |
| Salaries & FB (3 New FTE) | $305,396 | $315,958 | $621,364 | $302,855 | $310,707 | $613,562 |
| Operating: |         |         |          |         |         |          |
| $15,700 per FTE | 47,100 | 47,100 | $94,200 | 47,100 | 47,100 | $94,200 |
| TeamMate audit license (one-time 3@$1,400) | 4,200 | - | $4,200 | - | - | $0 |
| TeamMate audit software mtnce & hosting (3 @ $1,250/yr) | 3,750 | 3,750 | $7,500 | 3,750 | 3,750 | $7,500 |
| Consultant | 70,000 | 70,000 | $140,000 | 70,000 | 70,000 | $140,000 |

| 15-17 Add'l state increase to fund add'l 3 FTE & consultant | 430,446 | 436,818 | $867,264 | ✓ | 423,705 | 431,557 | $855,262 |

| 15-17 Total increase to fund 10 FTE & consultant | $1,921,297 | $1,894,284 |

C:\Users\timothy.p.carlson\AppData\Local\Microsoft\Windows\Temporary Internet Files\Content.Outlook\WP3W7SG\[Audit Budget Est at $200000 to Tim.xlsx\Summary-No Campus Assess
NORTH DAKOTA STATE BOARD OF HIGHER EDUCATION POLICY MANUAL

SUBJECT: FINANCIAL AFFAIRS  

Section: 802.8 Internal Audit Charter  

EFFECTIVE: March 27, 2014

1. INTRODUCTION:  
Internal Auditing is an independent and objective assurance and consulting activity that is guided by a philosophy of adding value to improve the operations of the North Dakota University System (NDUS). It assists NDUS in accomplishing its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of the organization's governance, risk management and internal control.

2. ROLE:  
The internal audit activity is established by the State Board of Higher Education (Board). The internal audit activity’s responsibilities are defined by the Board and the Audit Committee as part of their oversight role.

3. PROFESSIONALISM:  
a. The internal audit activity will govern itself by adherence to The Institute of Internal Auditors' mandatory guidance including the Definition of Internal Auditing, the Code of Ethics, and the International Standards for the Professional Practice of Internal Auditing (Standards). This mandatory guidance constitutes principles of the fundamental requirements for the professional practice of internal auditing and for evaluating the effectiveness of the internal audit activity’s performance.

b. The Institute of Internal Auditors' Practice Advisories, Practice Guides, and Position Papers will also be adhered to as applicable to guide operations. In addition, the internal audit activity will adhere to relevant Board policies and procedures and the internal audit activity's standard operating procedures manual.

4. AUTHORITY:  
The internal audit activity, with strict accountability for confidentiality and safeguarding records and information, is authorized full, free, and unrestricted access to any and all NDUS (and affiliated organizations) records, physical properties, and personnel pertinent to carrying out any engagement. All NDUS (and affiliated organizations) employees are requested to assist the internal audit activity in fulfilling its roles and responsibilities. The internal audit activity will also have free and unrestricted access to the Board and Audit Committee.

5. ORGANIZATION:  
The Chief Auditor (CAE) will report functionally to the Board and administratively (i.e. day to day operations) to the Chancellor.
a. The Board and Audit Committee will:
   i. Approve the internal audit charter.
   ii. Approve the risk based internal audit plan.
   iii. Approve the internal audit budget and resource plan.
   iv. Receive communications from the CAE on the internal audit activity’s performance relative to its plan and other matters.
   v. Make decisions regarding the appointment and removal of the CAE.
   vi. Recommend and approve the remuneration of the CAE.
   vii. Make appropriate inquiries of management and the CAE to determine whether there is inappropriate scope or resource limitations.

b. The CAE will communicate and interact directly with the Board and Audit Committee, including in executive sessions and between Board meetings as appropriate.

6. INDEPENDENCE AND OBJECTIVITY:
   a. The internal audit activity will remain free from interference by any element in the organization, including matters of audit selection, scope, procedures, frequency, timing, or report content to permit maintenance of a necessary independent and objective mental attitude.

   b. Internal auditors will have no direct operational responsibility or authority over any of the activities audited. Accordingly, they will not implement internal controls, develop procedures, install systems, prepare records, or engage in any other activity that may impair internal auditor’s judgment.

   c. Internal auditors will exhibit the highest level of professional objectivity in gathering, evaluating, and communicating information about the activity or process being examined. Internal auditors will make a balanced assessment of all the relevant circumstances and not be unduly influenced by their own interests or by others in forming judgments.

   d. The CAE will confirm to the Board, at least annually, the organizational independence of the internal audit activity.

7. RESPONSIBILITY:
The scope of internal auditing encompasses, but is not limited to, the examination and evaluation of the adequacy and effectiveness of the organization's governance, risk management, and internal controls as well as the quality of performance in carrying out assigned responsibilities to achieve the organization’s stated goals and objectives. This includes:
   a. Evaluating risk exposure relating to achievement of the organization’s strategic objectives.
b. Evaluating the reliability and integrity of information and the means used to identify measure, classify, and report such information.

c. Evaluating the systems established to ensure compliance with those policies, plans, procedures, laws, and regulations which could have a significant impact on the organization.

d. Evaluating the means of safeguarding assets and, as appropriate, verifying the existence of such assets.

e. Evaluating the effectiveness and efficiency with which resources are employed.

f. Evaluating operations or programs to ascertain whether results are consistent with established objectives and goals and whether the operations or programs are being carried out as planned.

g. Monitoring and evaluating governance processes.

h. Monitoring and evaluating the effectiveness of the organization's risk management processes.

i. Evaluating the quality of performance of external auditors and the degree of coordination with internal audit.

j. Performing consulting and advisory services related to governance, risk management and internal control as appropriate for the organization.

k. Reporting periodically on the internal audit activity’s purpose, authority, responsibility, and performance relative to its plan.

l. Reporting significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by the Board.

m. Evaluating specific operations at the request of the Board or Chancellor, or institution presidents, as appropriate.

8. INTERNAL AUDIT PLAN:

a. At least annually, the CAE will submit to the Chancellor, institution presidents, and the Board an internal audit plan for review and approval. The internal audit plan will consist of a work schedule as well as budget and resource requirements for the next fiscal year. The CAE will communicate the impact of resource limitations and significant interim changes to the Chancellor, institution presidents, the Board, and Audit Committee.

b. The internal audit plan will be developed based on a prioritization of the audit universe using a risk-based methodology, including input of the Chancellor, institution presidents, and the Board. The CAE will review and adjust the plan, as
necessary, in response to changes in the organization’s business, risks, operations, programs, systems, and controls. Any significant deviation from the approved internal audit plan will be communicated to the Chancellor, institution presidents, the Board, and Audit Committee through periodic activity reports.

9. REPORTING AND MONITORING:
   a. A written report will be prepared and issued by the CAE or designee following the conclusion of each internal audit engagement and will be provided to the Chancellor and appropriate institution president(s).

   b. Internal audit results will also be communicated to the Board and Audit Committee.

   c. The internal audit report may include management’s response and corrective action taken or to be taken in regard to the specific findings and recommendations. Management's response, whether included within the original audit report or provided thereafter (i.e. within thirty days) by management of the audited area should include a timetable for anticipated completion of action to be taken and an explanation for any corrective action that will not be implemented.

   d. The internal audit activity will be responsible for appropriate follow-up on engagement findings and recommendations. All significant findings will remain in an open issues file until cleared.

   e. The CAE will periodically report to the Chancellor, institution presidents, the Board, and Audit Committee on the internal audit activity’s purpose, authority, and responsibility, as well as performance relative to its plan. Reporting will also include significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by the Chancellor, institution presidents, the Board, and Audit Committee.

10. QUALITY ASSURANCE AND IMPROVEMENT PROGRAM:
    The internal audit activity will maintain a quality assurance and improvement program that covers all aspects of the internal audit activity. The program will include an evaluation of the internal audit activity’s conformance with the Definition of Internal Auditing and the Standards and an evaluation of whether internal auditors apply the Code of Ethics. The program also assesses the efficiency and effectiveness of the internal audit activity and identifies opportunities for improvement.
    The CAE will communicate to the Chancellor, institution presidents, the Board, and Audit Committee on the internal audit activity’s quality assurance and improvement program, including results of ongoing internal assessments and external assessments conducted at least every five years.

History:
Amended. SBHE Minutes, September 26, 2012.
Amended. SBHE Minutes, March 27, 2014.