

## **MINUTES OF THE AUGUST 1, 2013, AUDIT AND REVIEW COMMITTEE MEETING**

The Audit and Review Committee (“the Committee”) of the Board of Regents conducted a teleconference meeting on August 1, 2013. Participating were Committee Chair John McCarter and Committee members Barbara Barrett, Shirley Ann Jackson, Representative Sam Johnson, and Robert Kogod. Committee member Senator Jack Reed and Special Advisor to the Committee Herb Schulken were unable to participate.

Participating staff included Secretary G. Wayne Clough (by telephone); Chief of Staff to the Secretary Patricia Bartlett; Inspector General Scott Dahl; Office of the Regents Senior Writer-Editor Barbara Feininger (recorder); Under Secretary for Finance and Administration and Chief Financial Officer Albert Horvath; Deputy Under Secretary for Finance and Administration John K. Lapiana; Assistant to Senator Reed Moira Lenehan-Razzuri; General Counsel Judith Leonard; and Associate General Counsel Marsha Shaines.

### **CALL TO ORDER**

Mr. McCarter called the meeting to order at 2:02 p.m.

### **APPROVAL OF THE MINUTES OF THE JANUARY 24, 2013, COMMITTEE MEETING AND THE NOTES OF THE APRIL 18, 2013, COMMITTEE MEETING**

Mr. McCarter directed the participants’ attention to the records of the January 24 and April 18, 2013, Committee meetings. An amendment was proposed regarding the participants in the April 18 meeting. There being no further comments, the January meeting minutes and the April meeting notes were approved as amended.

### **REVIEW AND AFFIRMATION OF FISCAL YEAR 2012 IRS FORM 990 SUBMISSION**

Under Secretary Albert Horvath introduced the discussion of the Smithsonian’s draft fiscal year (FY) 2012 IRS Form 990 return by noting that it must be filed by August 15, 2013. Mr. Horvath said he would discuss the comprehensive review process for the development of the draft return, as well as provide a high-level summary of the important issues in the return.

The draft IRS Form 990, he said, was prepared by the Office of Finance and Accounting (OFA). A detailed review of the draft was made by multiple parties and questions comprised most of the feedback received during the review process. The draft return was made available to the Board of Regents on June 14, 2013. Other reviewers included the OFA director; KPMG, the Smithsonian’s external auditors; Mr. Horvath; a sub-committee of the Audit and Review Committee, including Mr. Schulken; the Office of the General Counsel (OGC); the Secretary; and Bertrand Harding, an external tax attorney who specializes in non-profit tax issues. The review by Mr. Harding was a new step in the review process. In response to a question from Mr. Kogod, Mr. Horvath affirmed that Mr. Harding found the draft return to be complete and reflective of best practices.

Mr. Horvath then reviewed specific parts of the draft Form 990. All of the financial information, he said, had been reconciled to the Smithsonian's other audited financial statements for the same period. Consistent with filings since FY 2008, the form includes all Federal and Trust revenues, expenses, assets, and liabilities. Filing requirements are consistent with those in prior years, and no major changes were made to the required disclosures made by the IRS.

The Under Secretary directed the Committee's attention to some of the Smithsonian's responses to questions regarding organizational governance and compliance with Federal regulations. Part VI, Section A and related sections in the Schedule O form reflect the diversion of assets that resulted from the theft of parking revenues at the Udvar-Hazy Center. Part VII and the related Schedule J, which disclose compensation information for certain employees, was prepared by OFA with input from the Office of Human Resources. Data in this section is drawn from different reporting periods: the tax return covers fiscal year 2012 and the compensation data relates to calendar year 2011.

Part IX, the Statement of Functional Expenses, breaks out overall expenses incurred for program service, management expenses, general expenses, and fundraising expenses. Whereas prior years' expenses were submitted as one collective sum, this year's expenses were itemized. In addition, facility-related expenses were allocated on the basis of building square footage rather than total expense. This practice predominates among large, complex non-profits, and resulted in a decrease in the percentage of such expenses that are assigned to management administration and a more accurate representation of the operations the Smithsonian's expenses support. KPMG, added Mr. Horvath, supports this methodology.

Schedule C, Political Campaign and Lobbying Activities, also was reviewed. The Smithsonian noted that less than \$7,500 had been spent in lobbying activities in pursuit of a specific grant to support capital improvements and educational programs for Cooper-Hewitt, National Design Museum. Schedule F, Statement of Activities Outside the United States, included expenditures in support of program activities at the Smithsonian Tropical Research Institute. Any foreign investment amounts, said Mr. Horvath, are obtained from the Office of Investments. Schedule J, Compensation Information, did not include any material changes to the Smithsonian's disclosures in FY 2012. Thirty-four individuals were listed. Mr. Horvath noted that this relatively high number of reported individuals reflects the number of people who held interim or acting roles during this reporting period; many individuals will not be included in future filings.

In response to a question from Dr. Jackson, Mr. Horvath said that a complex algorithm is used to determine the number of hours Regents devote to Board activities. The information, he said, is benchmarked against comparable institutions. Noting that different Board positions demand different commitments of time, Mr. McCarter said that adjustments should be made to reflect such differences. Mr. Horvath said the form's notation of Dr. Jackson's hours would be amended to be consistent with those of Mr. McCarter.

Mr. McCarter noted that the Committee's responsibility is to review and then approve the draft FY 2012 IRS Form 990 return. He asked if there were questions from the Committee.

Ambassador Barrett asked which sections typically attract attention. Hr. Horvath responded that salaries consistently draw scrutiny, adding that the return carefully reflects aggregated compensation figures. Expansive and transparent disclosures of other information demonstrate the Smithsonian's commitment to its mission and policies. A third item that may attract attention, said Mr. Horvath, would be information related to the theft of parking fees at the Udvar-Hazy Center. Ambassador Barrett also asked if Mr. Horvath could, to the best of his knowledge, attest to the accuracy of the return. He confirmed that he could.

There being no further comments, the Committee approved the fiscal year 2012 IRS Form 990 for the Smithsonian. Dr. Jackson clarified that it is a function of the Committee to affirm, not approve, the return, and that it is the responsibility of the Financial Officer and the Secretary to attest to its accuracy. Mr. Horvath agreed, and said that the purpose of the Committee's action is to document to the IRS that the return was provided to and reviewed with the Committee. Accordingly, the motion was amended as follows:

**VOTED** that the Audit and Review Committee affirms the Smithsonian's proposed submission of its fiscal year 2012 Form 990 to the Internal Revenue Service.

## **ANNUAL FINANCIAL DISCLOSURE AND CONFLICT OF INTEREST REVIEW**

General Counsel Judith Leonard reported on the annual financial disclosure and conflict of interest review conducted by the OGC. The Board of Regents and senior executives are included in the review. She reported that the OGC did not identify any significant or new reportable conflicts of interest, or circumstances that could create the appearance of a conflict.

Two Regents disclosed financial interests in vendors doing business with the Smithsonian; the 2012 review also included these disclosures. The Regents have been advised to recuse themselves should an issue involving these vendors be presented to the Board for action.

There are currently 83 senior executives who are required to file an annual report on all non-profit board memberships and paid outside activities. The OGC, said Ms. Leonard, determined that there were no reportable issues, and that additional action is unnecessary at this time.

## **INSPECTOR GENERAL UPDATE**

Mr. McCarter noted that President Obama nominated Smithsonian Inspector General Scott Dahl to be the next inspector general of the U.S. Department of Labor. On behalf of the Committee, he thanked Mr. Dahl for his contributions to the Smithsonian and to the Audit and Review Committee. He cited Mr. Dahl's efforts to improve the Smithsonian's management of its collections and investigation of the Udvar-Hazy parking thefts as examples of Mr. Dahl's professional leadership, and asked General Counsel Judith Leonard to draft a resolution expressing the appreciation of the Committee to Mr. Dahl. The following motion was later approved by the Committee:

**VOTED** that the Audit and Review Committee of the Board of Regents thanks Scott Dahl for his service as Inspector General of the Smithsonian Institution and commends his professionalism in carrying out his responsibilities.

Mr. Dahl thanked Mr. McCarter and the Committee for their support. He expressed his intention, pending confirmation of his appointment by Congress, to continue to work closely with the Committee both to maintain the pace of the projects under way and to support the search process for his successor. He then updated the Committee on the activities of the Office of the Inspector General (OIG).

***Development of Fiscal Year 2014 Audit Plan.*** The development of the FY 2014 audit plan is being informed by input solicited from Smithsonian leadership. The audit will examine ways to improve the efficiency and effectiveness of priority activities, as well as identify activities that pose the highest risk to achieving Smithsonian priorities. The views of the Regents, said Mr. Dahl, also will be solicited.

***Congressional Testimony on Collections Stewardship.*** The meeting materials included Mr. Dahl's July 17, 2013, testimony before the Committee on House Administration. The Secretary and Deputy Secretary for Collections and Interdisciplinary Support Scott Miller also testified at the panel hearing. Mr. Dahl reported that members of the House Committee expressed satisfaction with the Smithsonian's pan-institutional collections stewardship efforts.

***Information Security Program Audit.*** A brief of the audit of the Smithsonian's information security program was provided in the meeting materials. The Smithsonian complies with the Federal Information Security Management Act of 2002 (FISMA), which requires organizations to adopt a risk-based, life-cycle approach to improving information security. The issues identified in the audit, said Mr. Dahl, are not unique to the Smithsonian. Mr. Horvath and Chief Information Officer Deron Burba are working with the OIG to address identified weaknesses, including the timely testing and installation of security patches.

***Udvar-Hazy Center Update.*** Mr. Dahl reported that a former PMI parking lot supervisor was sentenced for conspiring to steal parking fees from the museum. In addition to a 40-month prison term, the sentence included a restitution order of approximately \$1.4 million. The criminal investigation continues. The OIG and the Office of the General Counsel are working with the Department of Justice Civil Division to recover funds, including penalties, from PMI. Mr. McCarter noted that the likelihood of financial recovery from individuals is limited. Ms. Leonard added that additional discovery of criminal activity delays progress on civil recovery efforts.

## **EXECUTIVE SESSION**

The Committee then conducted an executive session. The meeting was adjourned at approximately 2:40 p.m.

Respectfully submitted,  
John McCarter, Chair