

MINUTES OF THE JANUARY 19, 2011, AUDIT AND REVIEW COMMITTEE MEETING

On January 19, 2011, the Regents' Audit and Review Committee ("the Committee") met in the Regents' Room of the Smithsonian Castle. Participating were Committee Chair John McCarter and Committee members Shirley Ann Jackson* and Sam Johnson*; member Robert Kogod was unable to participate. Also participating were Assistant to Congressman Johnson David Heil* and Committee Advisor Herb Schulken. Participating staff included Chief of Staff to the Secretary Patricia Bartlett; Acting Chief Financial Officer (CFO) Bruce Dauer; Assistant Inspector General for Audits Daniel Devlin; Chief of Staff to the Regents John K. Lapiana; General Counsel Judith Leonard; Under Secretary for Finance and Administration Alison McNally; Director of Government Relations Nell Payne; Inspector General (IG) Sprightley Ryan; and Comptroller Andrew Zino. Also in attendance were Joanna Biegler, Ellen Harrison, and Wendy Lewis, who represented the Institution's external auditors, KPMG LLP. Minutes were taken by Special Assistant to the CFO Susan Block.

Committee Chair John McCarter called the meeting to order at 2:00 p.m. He informed the Committee that the March 2, 2011, meeting has been moved to April 8, 2011.

Status of KPMG Fiscal Year 2010 Financial Statement Audit

KPMG LLP Senior Partner Ellen Harrison reported that the audit of the "closing package" special-purpose financial statements for the Federal funds was completed in accordance with Department of Treasury and Office of Management and Budget (OMB) requirements. It was completed on time and submitted on November 15, 2010. An unqualified opinion was issued with no material weaknesses noted.

The audit of the Smithsonian-wide financial statements is ongoing. Ms. Harrison informed the Committee that management had informed KPMG in early December 2010 about delays related to the financial reporting of the Endowment because of the extended absence of the employee responsible for furnishing that information. She stated that the schedules had been due to KPMG on December 13, 2010, and were not received until January 14, 2011. She informed the Committee that, even though these schedules were late, there were other areas of the audit that could go forward while KPMG awaited that portion. Ms. Harrison informed the Committee that the audit will now be completed on March 4, 2011.

The Chair observed that this delay is unacceptable, potentially embarrassing to the Institution, and must be corrected so that it does not recur. He added that the delay points out the weakness of having a single individual responsible for any one portion of the audit. He expressed the Committee's displeasure, adding that he had never encountered such a delay in his experience.

Committee Advisor Herb Schulken noted that other deliverables were still due. Comptroller Andrew Zino clarified that the only outstanding deliverable was the second draft of the financial statements, which will be delivered to KPMG on January 21, 2011. Mr. Schulken asked if any further delays were anticipated and Ms. Harrison and Comptroller Zino responded that they did

* *participated by teleconference*

not expect any further slippage. Comptroller Zino informed the Committee that KPMG now has the schedule of the employee associated with the slippage and that the individual will be available to answer any questions that may arise from KPMG.

Ms. Lewis fulfilled the required communications to the Committee on the audit of the Federal closing package. She stated that communications with management have been very good during this audit and that no major issues arose during the course of the audit. There were a few audit differences in the areas of property and equipment, construction accruals, conditional asset retirement obligations, and imputed costs. She reported that these differences were not recorded in the financial statements as they were determined by management to be immaterial, and noted that KPMG agreed with that assessment. She informed the Committee that the management representation letter will be furnished to them at a later date. No material weaknesses have been noted to date.

Because Committee member Jackson needed to leave the meeting early, the Chair suspended the meeting at 2:25 p.m. to conduct executive sessions with KPMG, the Inspector General, and the Under Secretary for Finance and Administration.

Following the conclusion of the executive sessions, the meeting resumed at 3:00 p.m.

Status of Internal Control Improvement Project

Comptroller Zino updated the Committee on the status of the internal control improvement project. He reported that three of the five high-risk internal control areas—personal property management, capital projects, and charitable contributions—remain on track but that the remaining two—procurement, contracting, and leasing and purchase card use and use of funds—have been delayed. The improvement of risk controls concerning the use of funds, including the pan-Institutional review of the handbook that will accompany that directive, is taking longer than planned and the anticipated completion date is now the second quarter of fiscal year 2011. The improvement of procurement risk controls is slightly more problematic.

Although seven contracting policy manuals were to be completed by the end of calendar 2010, only three were completed and issued. The remaining four have been developed and are currently being reviewed. Dr. Jackson asked about the reasons for these delays and Acting CFO Dauer responded that changes in priorities, not obstacles, had impacted the schedule. The importance of releasing these manuals was reemphasized and staff agreed that the manuals will be completed as expeditiously as possible. Regardless, the deadline to achieve full compliance for both the use of funds and the contracting internal control areas has not slipped.

The Chair stated that the Committee was not satisfied with the progress being made. Under Secretary McNally was asked to submit a status report to the Committee by February 15, 2011. The report will detail actions being taken to recover the schedule more quickly.

Comptroller Zino also reported modest slippage in some of the moderate risk areas.

Inspector General's Update

The Chair asked IG Ryan if she had anything to bring to the attention of the Committee besides the issues that were discussed in executive session. She stated that her office would be undergoing a peer review by the Inspector General of the Federal Deposit Insurance Corporation and that the results of the review would be reported to the Committee.

Acting Chief Financial Officer's Issues Update

Acting CFO Dauer informed the Committee that the A-133 audit planning for fiscal year 2010 has begun and should be completed on time in June 2011. With regard to the financial system implementation, he said that the interface with the Smithsonian's payroll provider, the National Finance Center, has been completed. The project costing module is in the final stages of being deployed and the grants module, which will be a significant improvement in the way grants are reported, is also on schedule to be completed during the second quarter of fiscal year 2011. Acting CFO Dauer indicated that the cash management module, which had been delayed to incorporate the new advancement information system in its design, should now become more of a priority. He noted that he will discuss the schedule for this module implementation with the Chief Information Officer.

Mr. Dauer reported that the national campaign's strategy and plan is being discussed with the Advancement Committee and that the campaign's financing strategy is being discussed with the Finance Committee. Both strategies will be discussed with the full Board of Regents on January 31, 2011. He provided a brief outline of the financing strategy to the Committee.

Acting CFO Dauer then gave the Committee an update on the Federal budget. He informed the Committee that since the fiscal year 2011 appropriation has not been passed, the Institution will operate under a Continuing Resolution until March 4, 2011. He reported that the House is considering a proposal to reduce Federal spending levels to fiscal year 2008 levels. For the Smithsonian this would represent a \$93 million drop below its fiscal year 2010 Federal budget. He informed the Committee that budget negotiations with OMB on the fiscal year 2012 budget were recently completed. The Institution received a \$125 million increase to fund the construction of the National Museum of African American History and Culture. The balance of the budget, however, is \$4 million below the fiscal year 2010 level.

With regard to the fiscal year 2010 tax return, extensions have been filed for both the Form 990 and 990-T. Comptroller Zino informed the Committee that he had conducted the annual meeting with the KPMG tax team on tax return issues and other tax matters. He reported that the Institution will not pay any unrelated business income tax because the return indicates a small overall net loss of \$39,911. He stated that, with the Committee's permission, the same process used last year would be followed wherein he and Committee Advisor Schulken would conduct a detailed review of the 990, after which any potential issues would be brought first to the attention of the Chair and then to a meeting with the full Committee in August 2011. The Chair thanked Mr. Schulken for his willingness to perform this duty.

Acting CFO Dauer informed the Committee that Federal reporting changes promulgated by OMB and the Treasury under the Governmentwide Treasury Account Symbol Adjusted Trial Balance System will require significant resources from both the Office of the Comptroller and the Office of the Chief Information Officer and will be a major focus over the next 12–24 months. The Internal Revenue Service has informed the Institution that it will be conducting an audit of 2009 tax forms 941, 1042, and 1099-M. An entrance conference was held on January 13, 2011, during which the Institution was advised to anticipate this audit every five years. Also, the National Aeronautics and Space Administration Inspector General’s office has notified the Institution of their intent to perform a quality control review of the fiscal year 2009 A-133 audit. Acting CFO Dauer informed the Committee that KPMG was asked to supply tax services to Smithsonian Enterprises (SE) in connection with the Smithsonian Networks agreement. The Chair requested that the Committee receive a cost estimate for these services, a copy of the statement of work, and a proposed motion to approve SE’s use of KPMG.

Senior Executive Travel

The Committee is updated on senior executive travel twice a year. Mr. Schulken asked Comptroller Zino to explain the finding that there were eight instances wherein a traveler was overpaid. Mr. Zino responded that the traveler was either paid too much per diem or that the documents were not supplied that supported the requested reimbursement amounts. Mr. Schulken requested more information on the misuse of travel cards. Comptroller Zino responded that he would get the requested information from the Office of Contracting and Personal Property Management, which is responsible for the oversight and management of travel cards. With regard to the finding that there were 15 instances of missing receipts, the Chair asked if those requests for reimbursement were disallowed. The Comptroller responded that it is not Smithsonian policy to disallow payment for lack of receipts. The Chair responded that he thought that the policy statement should be changed to disallow payment if receipts are not furnished. The Under Secretary for Finance and Administration said that the policy would be reviewed and that she would report the review’s findings to the Committee.

The Chair stated that he endorses the Committee meeting schedule and believes that it supports the participation of Committee members. Committee members agreed with the Chair’s assessment.

Since there was not a quorum, the Chair asked that the minutes of the Committee’s September 7, 2010, meeting be approved by e-mail or fax ballot. [The minutes were subsequently approved.]

The meeting was adjourned at 3:20 p.m.

Respectfully submitted,
John McCarter, Chair