



CANCER PREVENTION AND RESEARCH INSTITUTE OF TEXAS

CHARTER OF THE AUDIT SUBCOMMITTEE FOR THE CANCER PREVENTION AND RESEARCH INSTITUTE OF TEXAS

BACKGROUND

The Oversight Committee of the Cancer Prevention and Research Institute of Texas (“CPRIT” or “Institute”) established an Audit Subcommittee (the “Subcommittee”) on June 18, 2010. This Charter, adopted by the Oversight Committee on November 22, 2013, and amended August 17, 2016, supersedes any other documents relating to the Audit Subcommittee.

PURPOSE

The primary purpose of the Subcommittee is to assist the Oversight Committee in fulfilling its responsibilities for monitoring the audit, financial and compliance functions of the Institute to assure the transparency and integrity of Institute’s operations and use of taxpayer funds. Specifically, the Subcommittee is to assist the Oversight Committee by monitoring the following activities and making recommendations to the Oversight Committee regarding:

- The Institute’s annual operating budget and strategic plan, including variances in the operating budget of more than five percent (5%) or \$25,000;
- The integrity of the financial reporting process, the system of internal controls, the audit process and policies, and the process for monitoring compliance with laws and regulations;
- The performance of the Institute’s independent auditors;
- Internal audit functions performed by the CPRIT finance office and grant management staff;
- Audits of the Institute performed by the Texas State Auditor’s Office;
- The Institute’s enterprise risk management;
- The Institute’s compliance program; including the Institute’s adherence to state law, and administrative and regulatory requirements and internal polices for monitoring the performance of cancer research and prevention grants awarded by

the Institute;

- Certain financial decisions of the Institute, including the employment of senior staff (Chief Scientific Officer, Chief Prevention Officer, Chief Product Development Officer, Chief Operating Officer, Chief Compliance Officer, and General Counsel) and related compensation, approval of certain non-grant contracts and variances of more than ten percent (10%) in any announced grant award.

The Subcommittee will take all appropriate actions to set the overall tone at the Institute for quality financial reporting, sound risk practices, and ethical behavior. The Subcommittee is responsible for maintaining free and open communication as well as effective working relationships among the Subcommittee members, Institute staff responsible for the grant review and administration, the Chief Compliance Officer, independent external auditors, the CPRIT finance office, the Texas State Auditor's Office, and senior management of the Institute.

SCOPE

This Audit Subcommittee Charter sets forth the Subcommittee's monitoring responsibilities with respect to the Institute and its use of state funds, including the awarding of grant funds for cancer research and prevention. As such, the role and purpose of the Subcommittee includes monitoring the functions and processes of the Institute and the funds issued on behalf of the State of Texas for cancer research and prevention grant awards.

COMPOSITION

The Subcommittee shall be composed of at least three members of the Oversight Committee; such members to be appointed from time to time by a majority vote of the Oversight Committee at a meeting at which a quorum is present and approved by the Oversight Committee. The Oversight Committee shall designate a Chairperson of the Subcommittee from among its members. Members of the Subcommittee must meet the independence and, to the extent possible, the financial literacy requirements as defined below. To perform their role effectively, each Subcommittee member will need to develop and maintain his or her skills and knowledge, including an understanding of the Subcommittee's responsibilities and of the Institute's activities, operations and risks. A member of the Subcommittee will serve until his or her successor is duly appointed and qualified unless the member resigns or is removed from the Subcommittee. The Oversight Committee may replace any member of the Subcommittee by a majority vote of the Oversight Committee.

INDEPENDENCE REQUIREMENTS

The Oversight Committee shall determine that all members of the Subcommittee are independent. A person is “independent” who has no relationship with the Institute which would interfere with the exercise of independence from management. In addition, Subcommittee members would not be “independent” if during the three years prior to their appointment or at any time during their service on the Subcommittee they accepted, directly or indirectly, any consulting, advisory, or other compensatory fee from the Institute apart from travel and expense reimbursements they may receive as members of the Oversight Committee and its Committees.

FINANCIAL LITERACY

The Oversight Committee, based on its business judgment, shall determine that each member of the Subcommittee is financially literate.

FINANCIAL MANAGEMENT EXPERTISE

To the extent possible, the Oversight Committee, based on its business judgment, shall determine that at least one member of the Subcommittee is a “financial expert.” A financial expert possesses the following attributes:

- An understanding of generally accepted accounting principles (GAAP) and financial statements;
- An ability to assess the application of GAAP in connection with accounting for estimates, accruals and reserves;
- An understanding of audit committee functions;
- Experience preparing, auditing, analyzing or evaluating financial statements, or experience actively supervising persons engaged in such activities; and
- An understanding of internal controls and procedures for financial reporting as specifically related to Texas state agencies.

MEETINGS AND QUORUM

The Subcommittee shall meet as often as the Chairperson of the Subcommittee deems appropriate, but at least quarterly, to perform its duties and responsibilities under the Bylaws. The Subcommittee shall keep regular minutes of its meetings and cause such minutes to be recorded in books kept for that purpose in the principal office of the Institute, and report the

same to the Oversight Committee at its next regular meeting.

If a member of the Subcommittee is absent from any meeting, or disqualified from voting at that meeting, then the remaining member or members present at the meeting and not disqualified from voting, whether or not such member or members constitute a quorum, may, by a unanimous vote, appoint another member of the Oversight Committee to act at the meeting in the place of any such absent or disqualified member. Unless the Oversight Committee provides otherwise, at all meetings of the Subcommittee, a majority of the then authorized members of the Subcommittee will constitute a quorum, and the vote of a majority of the members of the Subcommittee present at any meeting at which there is a quorum will be the act of the Subcommittee.

Unless the Oversight Committee provides otherwise, the Subcommittee may make, alter, and repeal rules and procedures for the conduct of its business. In the absence of such rules and procedures, the Subcommittee shall conduct its business in the same manner as the Oversight Committee conducts its business, except that meetings of the Subcommittee are not required to be conducted pursuant to the Open Meetings Act.

FUNCTIONS, DUTIES AND RESPONSIBILITIES

Review Financial Statements for Quality Considerations

The Subcommittee has the following duties and responsibilities with respect to the financial statements of the Institute and the grant award funds managed on behalf of the State of Texas:

- Review the annual audited financial statements with management and the independent auditor, including significant issues regarding adequacy of internal controls and accounting principles and practices;
- Review an analysis prepared by management and the independent auditor of significant financial reporting issues and judgments made in connection with the preparation of the financial statements;
- Discuss with the independent auditor the matters required to be communicated by AU 380, *The Auditor's Communication with Those Charged with Governance*, as amended, relating to an audit of financial statements;
- Discuss with the independent auditor any fraud of which the independent auditor becomes aware that involves senior staff and/or which causes a material misstatement of the financial statements; and

- Receive and review periodic reports from the independent auditor regarding the auditor's independence and discuss such reports with the auditor.

Monitor Management's Handling of Internal Controls

The Subcommittee has the following duties and responsibilities with respect to its monitoring of the integrity of the financial reporting process and internal controls of the Institute and the grant award funds managed on behalf of the State of Texas:

- Review with the independent auditor all significant deficiencies and material weaknesses identified during the audit as required by AU 325, *Communicating Internal Control related Matters Identified in an Audit*, as amended.
- Review with the independent auditor any problems or difficulties the auditor may have encountered during its audit and any management letter provided by the auditor and the Institute's response to that letter, such review to include:
 - any restrictions on the scope of activities or access to required information; and
 - any changes required in the planned scope of the audit;
- Obtain reports from management, the independent auditor, the Chief Compliance Officer and CPRIT finance office and grant accountants with respect to the Institute's policies and procedures regarding compliance with applicable laws, regulations and grant policies;
- When considered necessary, meet with the independent auditor and the senior personnel of the CPRIT finance office and grant accountants without management participation;
- Meet periodically with management to review the major financial risk exposures and the steps management has taken to monitor and control such exposures;
- Review significant changes to internal controls and accounting principles and practices as suggested by the independent auditor, internal auditors or management;
- Review the significant reports to management prepared by the State Auditor's Office and the Comptroller of Public Accounts and management's responses; and

- Review with the Institute’s legal counsel legal matters that may have a material impact on the financial statements, the Institute’s compliance policies and any material reports or inquiries received from regulators or governmental agencies.

Manage the Relationship with the External Auditors

The external auditors for the Institute are selected by and report to the Oversight Committee. The Oversight Committee directs the external auditors to have dual reporting responsibilities to the Oversight Committee and to the Subcommittee. The Subcommittee may approve additional audit and non-audit services provided by the external auditor related to the Institute and grant award funds as long as the work does not impair auditor independence.

The Subcommittee has the following specific duties and responsibilities with respect to the Institute’s independent auditors:

- Recommend to the Oversight Committee the appointment of the independent auditor, which firm is ultimately accountable to the Subcommittee and the Oversight Committee.
- Approve the fee arrangement of the independent auditor;
- After interviewing members of the Institute's staff, evaluate together with the Oversight Committee the performance of the independent auditor and, if so determined by the Subcommittee, recommend that the Oversight Committee replace the independent auditor; and
- If determined by the Subcommittee to be necessary or advisable, recommend that the Oversight Committee take appropriate action to satisfy itself of the independence of the auditor.

Auditor Independence

In connection with the selection of external auditors, the Subcommittee shall determine that:

- The public accounting firm engaged to perform the annual audit does not provide non-audit services contemporaneously with the audit;
- The lead audit partner and reviewing partner rotate off of the audit every 3 years, unless the Subcommittee adopts a resolution affirmatively determining that such

rotation is not required; and

- The Institute's Chief Executive Officer, Grant Accountant, Finance Officer, or person in an equivalent position shall not have been employed by the public accounting firm during the one year period preceding the audit.

Work with the Internal Audit Function

The Institute uses a third-party auditor to perform internal audit functions hereunder with respect to the Institute and grant award funds. The third-party auditor reports directly to the Subcommittee. The Subcommittee has the following duties and responsibilities with respect to internal audit:

- Review the independence, qualifications, activities, resources and structure of the internal audit function;
- Review significant findings and recommendations made by the internal auditor and management's response and proposed implementation plan;
- Review the proposed internal audit plan for the coming year to determine that it addresses key areas of risk and that there is appropriate coordination with the external auditor;
- Review completed internal audits and the status of management's implementation of related recommendations;
- Receive a progress report on the internal audit plan with explanations for any deviations from the original plan; and
- Review procedures for the receipt, retention and treatment of complaints about accounting, internal accounting controls or auditing matters.

Oversee Regulatory Compliance

The Subcommittee is responsible for overseeing the effectiveness of the system for assuring Institute compliance with laws and regulations, particularly with the award of cancer research and prevention grant funds; as such, the Subcommittee has the following duties and responsibilities:

- Review the effectiveness of the system for monitoring compliance with laws and

regulations and the results of management's investigation and follow-up of any fraudulent acts or non-compliance;

- Obtain regular updates from management, the Chief Compliance Officer, and the Institute's legal counsel regarding compliance matters that may have a material impact on the Institute's financial statements, grant awards or compliance policies;
- Obtain regular updates from management and the Chief Compliance Officer regarding their consideration of all regulatory compliance matters in connection with the preparation of the financial statements;
- Review the findings of any examinations by regulatory agencies, including the Texas State Auditor's Office;
- Review agency operational activities related to state diversity-related requirements, e.g. Historically Underutilized Business (HUB) requirements and personnel practices.

Oversee the Institute's Enterprise Risk Management

Without limiting any of the foregoing, the Subcommittee, along with management and other personnel, as directed by the Oversight Committee, is responsible for the Institute's enterprise risk management. Enterprise risk management assists management in achieving the Institute's performance goals and prevents loss of resources, helps ensure effective reporting and compliance with laws and regulations, and helps avoid damage to the Institute's reputation and associated consequences. Enterprise risk management enables management to deal effectively with uncertainty and associated risk and opportunity, enhancing the capacity to build value. The Subcommittee has the following responsibilities related to enterprise risk management:

- Evaluate the overall effectiveness of the Institute's achievement of its objectives, as set forth in four categories:
 - 1) Strategic – high-level goals, aligned with and supporting its mission;
 - 2) Operations – effective and efficient use of its resources;
 - 3) Reporting – reliability and timeliness of reporting; and
 - 4) Compliance with applicable laws and regulations and with Oversight Committee policies such as the Code of Conduct and Ethics and

Delegation of Authority.

- Evaluate whether management is setting the appropriate tone at the top by communicating the importance of enterprise risk; and
- Inquire of management, the Chief Compliance Officer, and the independent external auditor about significant enterprise risks or exposures to the Institute and how these are being managed.

Review the Overall Duties and Responsibilities of the Chief Compliance Officer

The Chief Compliance Officer will report functionally to the Subcommittee and administratively to the CPRIT Chief Executive Officer. The Chief Compliance Officer will report compliance activities of the Institute to the Chief Executive Officer and directly to the Subcommittee at its regular meetings and to the chair between meetings. The Chief Executive Officer will direct day-to-day responsibilities of the Chief Compliance Officer with oversight by the Subcommittee.

Other Duties

The Subcommittee has the following additional duties and responsibilities:

- Review and make recommendations to the Oversight Committee regarding:
 - 1) The Chief Executive Officer's recommendations for senior staff hires or dismissals and related compensation;
 - 2) Variances in the operating budget of the Institute of more than 5% or \$25,000;
 - 3) Non-grant contracts exceeding \$100,000;
 - 4) Variance of more than ten percent (10%) in any announced grant award; and
 - 5) The adequacy of this Audit Subcommittee Charter periodically and any proposed changes.
- Make regular reports (at least twice each calendar year) to the Oversight Committee regarding the Subcommittee's activities and such other reports as may be requested by the Oversight Committee;

- Perform such additional special functions, duties or responsibilities as may from time to time be designated by the Oversight Committee; and
- Evaluate the Subcommittee's own performance, both of individual members and collectively, on a regular basis.

POWERS AND LIMITATIONS

The Subcommittee shall have the authority to retain special legal, accounting or other consultants to advise the Subcommittee, subject to state laws and regulations regarding retention of professional services. The Subcommittee may request any employee of the Institute, consultant, or independent auditor to attend any meeting of the Subcommittee or to meet with any members of, or consultants to, the Subcommittee.