

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM
(A Segment of the University of Illinois)

Report Required Under *Government Auditing Standards*

For the Year Ended June 30, 2009

Performed as Special Assistant
Auditors for the Auditor General,
State of Illinois

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM
(A Segment of the University of Illinois)

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The annual financial statements of the University of Illinois Auxiliary Facilities System for the year ended June 30, 2009 were issued under a separate cover.

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM
(A Segment of the University of Illinois)

Summary

For the Year Ended June 30, 2009

Government Auditing Report Summary

The audit of the financial statements of the University of Illinois Auxiliary Facilities System was performed by KPMG LLP in accordance with *Government Auditing Standards*. This report is an integral part of that audit.

Summary of Findings

The auditors identified certain deficiencies in internal control over financial reporting that they considered to be material weaknesses and other deficiencies that they considered to be significant deficiencies which are described in the accompanying schedule of findings and responses on pages 4 through 11 of this report.

Current Year Findings:

<u>Item No.</u>	<u>Page</u>	<u>Description</u>
AFS 09-01	4	Inadequate Controls over User Access to Information Systems
AFS 09-02	7	Inadequate Controls over University Procurement Card Transactions
AFS 09-03	10	Inadequate Year End Accounts Payable Process

Exit Conference

The findings and recommendations appearing in this report were discussed with University personnel at an exit conference on February 26, 2010. Attending were Walter Knorr, Douglas Beckmann, Patrick Patterson, Maxine Sandretto, Ginger Velazquez, William Devoney, Patrick O’Leary, Donald Moy, Michael Godsell and Phillip McCarthy from the University of Illinois; Thomas Kizziah from the Office of the Auditor General; and Catherine Baumann, Jacqueline Dippel, and Jeffrey Markert from KPMG LLP. Responses to the recommendations were provided by Patrick Patterson and Douglas Beckmann in a correspondence dated February 26, 2010.



KPMG LLP
303 East Wacker Drive
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**Independent Auditors' Report on Internal Control over Financial Reporting
and on Compliance and Other Matters Based on an Audit of Financial Statements
Performed in Accordance with *Government Auditing Standards***

The Honorable William G. Holland
Auditor General of the State of Illinois

and

The Board of Trustees
University of Illinois:

As Special Assistant Auditors for the Auditor General, we have audited the financial statements of the University of Illinois Auxiliary Facilities System (the System), a segment of the University of Illinois (the University), as of and for the year ended June 30, 2009, and have issued our report thereon dated February 26, 2010. Our report was modified to include an emphasis paragraph stating that the System did not present a management's discussion and analysis that U.S. generally accepted accounting principles requires to supplement, although not be a part of, the basic financial statements and that the System's financial statements only present the financial position, changes in financial position, and cash flows of the activities that are attributable to the transactions of the System for complying with the requirements of the indentures of the System's Revenue Bonds. We conducted our audit 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*, issued by the Comptroller General of the United States.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the System's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the System's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis.



A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies in the System's internal control over financial reporting described as finding number AFS 09-01 in the accompanying schedule of findings and responses to be a material weakness.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying schedule of findings and responses as finding numbers AFS 09-02 and AFS 09-03 to be significant deficiencies in internal control over financial reporting.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The University's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit the University's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Auditor General, the General Assembly, the Legislative Audit Commission, the Governor, University management, the Board of Trustees of the University, others within the University, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

February 26, 2010

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM

Schedule of Findings and Responses

For the Year Ended June 30, 2009

Finding AFS 09-01 – Inadequate Controls over User Access to Information Systems

The University has not established adequate internal controls over access to the information systems used in its financial reporting process.

The University operates an Enterprise Resource Planning (ERP) system to manage the activities of the University. Access is granted to users of the University's information systems based upon standardized user profiles designed by the Office of Business and Financial Services in connection with the Office of Administrative Information Technology Services. The University functions in a highly distributed operating environment with several thousand users having varying types of system access. The standardized user profiles are intended to assist the University in limiting access to the information systems based upon the assigned job functions of the specific users to which the profiles are assigned; however, the standardized user profiles currently used by the University are not designed to appropriately segregate conflicting duties and have resulted in an excessive number of users with access to perform transactions in unlimited dollar amounts or with the capability to modify system data. Specifically, we noted 2,258 users have access to create journal entries in unlimited dollar amounts without a supervisory review. We also noted 1,725 users with access to update employee pay rates within their assigned department and 112 individuals with access to update employee pay rates of all individuals across all departments of the University. Lastly, the University has not implemented procedures to monitor user access through periodic access reviews.

As a result of the internal control deficiencies identified above, we performed a detailed review of user access rights with the assistance of University management. This review identified several users with access rights that were inappropriate based on their roles and job functions presenting segregation of duties conflicts and the risk that erroneous or fraudulent transactions may be recorded in the general ledger. The exceptions identified during our review included the following:

- There are 10 users (out of 90 total users) with access to create and self approve restricted journal entries in unlimited dollar amounts whose access rights were not appropriate based upon review of each user's job functions.
- There are 23 users (out of 65 total users) with access to release financial holds whose access rights were not appropriate based upon review of each user's job functions.
- There are 21 users (out of a total of 121 users) with access to apply various payments whose access rights were not appropriate based upon review of each user's job functions.
- There are 91 users with access to the University's charts of accounts, 86 of which can also perform journal entries.
- There are five users (out of a total of 91 users) with access to update the chart of accounts whose access rights were not appropriate based upon review of each user's job functions.
- There are two users (out of a total of 44 users) with access to override three way matching whose access rights were not appropriate based upon review of each user's job functions.
- There are two super users in our sample of 40 super users with access rights for time approval that were not assigned to the appropriate organization based on their job function.

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM

Schedule of Findings and Responses

For the Year Ended June 30, 2009

- There are two users (out of a total of 38 users) with access to approve grants and contracts journal vouchers in unlimited dollar amounts whose access rights were not appropriate based upon review of each user's job functions.
- There are three terminated users (out of sample of 40 terminated users) with active accounts that were not removed in a timely manner.

The control deficiencies and exceptions discussed above relate to the operations of the University including the Auxiliary Facilities System.

The Fiscal Control and Internal Auditing Act (Illinois Compiled Statutes Chapter 30 Section 10/3001), requires the University to establish and maintain a system, or systems, of internal fiscal and administrative controls, which shall provide assurance that: (1) resources are utilized efficiently, effectively, and in compliance with applicable law; (2) obligations and costs are in compliance with applicable law; (3) funds, property, and other assets and resources are safeguarded against waste, loss, unauthorized use, and misappropriation; (4) revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources; and (5) funds held outside the State Treasury are managed, used, and obtained in strict accordance with the terms of their enabling authorities and that no unauthorized funds exist. The University's system of internal controls should include procedures to ensure access rights granted to University employees are appropriate and to monitor the appropriateness of access levels on a continuing basis. In addition, generally accepted information technology guidance endorses the development of well-designed and well-managed controls to protect computer systems and data. Effective computer security controls provide for safeguarding, securing, and controlling access to systems, properly segregating incompatible duties, and protecting against misappropriation.

In discussing these conditions with University personnel, they stated the access exceptions identified in the finding occurred as the result of untimely removal of user access for individuals changing job functions and the use of insufficiently designed user profiles in initially granting the user access. Additionally, University personnel believed that payroll edit reports and periodic financial reviews provided adequate compensating controls.

Failure to properly assign and monitor user access rights may result in erroneous or fraudulent transactions being recorded in the general ledger system. Without adequate security over access rights, there is a greater risk that unauthorized changes or additions to the University's financial systems could occur and not be detected in a timely manner. If access rights are not reviewed and updated based on job responsibilities on a regular basis, there is a greater risk that journal entries in unlimited dollar amounts, as well as cash disbursements, can be recorded by unauthorized individuals. (Finding Code AFS 09-01, 08-05)

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM

Schedule of Findings and Responses

For the Year Ended June 30, 2009

Recommendation:

We recommend the University review and modify the standard user profiles to ensure (1) the profiles assigned to users appropriately limit each user's access to the systems to which they require access based upon their assigned job responsibilities, (2) the authorization limits assigned to each user are appropriate, and (3) supervisory reviews of transactions are required as appropriate. The University should also implement formally documented review procedures to ensure the profile assigned to each user is compatible with the user's assigned job function and does not present a segregation of duties conflict prior to granting system access. Additionally, we recommend the University implement procedures to perform formal reviews of user access rights on a periodic basis to ensure that the access rights granted to each user are appropriate based on their job responsibilities and that the planned level of segregation of duties is achieved on a continuing basis.

University Response:

Accepted. The University's highly distributed operating environment involves several thousand system users, in hundreds of departments across the three campuses. These users are engaged in a variety of business and administrative functions necessary to perform the mission of the University. In connection with the implementation of the integrated information systems (Banner Systems) several years ago, certain system level controls and other processes were put in place to restrict accounts/funds accessible for users to post journal entries and also limit the ability of users to perform many other types of transactions. The University believes that many of these controls have been effective, but does agree that improvement to the user access control environment is needed and will be beneficial.

Since mid fiscal-year 2009, the University has been actively developing new policies and procedures to improve the controls over user access to information systems. Included in these improvements are new policies and procedures addressing controls over the set-up/maintenance of appropriate user access profiles and processes to be followed by unit security contacts (USCs). The improved USC controls include formally documented periodic reviews of user access, as well as training and other enhancements. The University's target date for implementation of these new policies/procedures is June 30, 2010. Staff has been increased and realigned in this area in preparation for implementation. The University plans to develop further user access control enhancements, and implement the new policies/procedures noted above, to address the recommendations in this finding.

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM

Schedule of Findings and Responses

For the Year Ended June 30, 2009

Finding AFS 09-02 – Inadequate Controls over University Procurement Card Transactions

The University has not established adequate internal controls over procurement card transactions.

The University operates a procurement card program which allows individuals throughout the University to make smaller purchases (defined as less than \$4,999) on a credit card which is directly reimbursed by the University on a monthly basis. The University's policies require individuals assigned a procurement card to sign an agreement stipulating they will use the card in accordance with University policy. This agreement is also required to be authorized by the individual's supervisor or the department head. The University's policies require transactions incurred on the procurement card to be approved in the University's procurement card system by the individual cardholder and an assigned reviewer. Although the University has established policies and procedures for issuing procurement cards, incurring and paying for expenditures with procurement cards, and reviewing and approving of procurement card transactions, we noted these policies and procedures were not properly designed to prevent erroneous charges from being paid by the University and were not followed consistently by University personnel.

Specifically, we noted the procurement card system is configured to automatically record transactions in the general ledger to pre-assigned accounts (auto-reconciled) if the cardholder and/or assigned reviewer have not approved the respective transactions within seven days. The configuration of the system is inconsistent with the University policy that requires both the cardholder and reviewer to approve all procurement card transactions. The University also has not implemented procedures to identify duplicate charges or to reconcile procurement card transactions with travel reimbursement forms. As a result, erroneous or duplicate charges may be paid and recorded by the University without any further detective controls to identify them. In our testwork over 40 procurement card transactions (totaling \$42,586), we identified the following exceptions:

- Two transactions (totaling \$91) were automatically reconciled by the system and as a result were not subject to supervisory approval procedures.
- Four transactions (totaling \$659) were reconciled and approved by the same individual.
- One transaction (totaling \$1,356) was made by an individual other than the card holder.
- Original supporting documentation could not be located for one P-Card transaction (totaling \$7).
- One transaction (totaling \$12) was for parking fees for which no University business purpose was documented.
- One transaction (totaling \$41) included a charge of \$2 for sales tax which is a prohibited charge because the University is tax-exempt.

In addition, the University was unable to locate approved Procurement Card Authorization/Agreement and Application forms for eight of 37 cardholders selected for testwork.

The control deficiencies and exceptions discussed above relate to the operations of the University including the Auxiliary Facilities System.

The University has approximately 5,700 active procurement cards and the procurement card expenditures paid during the year ended June 30, 2009 were \$108,100,000.

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The Fiscal Control and Internal Auditing Act (Illinois Compiled Statutes Chapter 30 Section 10/3001), requires the University to establish and maintain a system, or systems, of internal fiscal and administrative controls, which shall provide assurance that: (1) resources are utilized efficiently, effectively, and in compliance with applicable law; (2) obligations and costs are in compliance with applicable law; (3) funds, property, and other assets and resources are safeguarded against waste, loss, unauthorized use, and misappropriation; (4) revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources; and (5) funds held outside the State Treasury are managed, used, and obtained in strict accordance with the terms of their enabling authorities and that no unauthorized funds exist. The University's system of internal controls should include procedures to ensure procurement transactions are appropriately reviewed and approved to avoid erroneous or duplicate transactions from being paid and recorded.

In discussing these conditions with University personnel, they stated that the errors were the result of oversight and employees and their supervisors being unfamiliar with University policy.

Failure to properly review and approve procurement card transactions could result in erroneous or fraudulent transactions being recorded in the general ledger system. (Finding Code AFS 09-02, 08-03)

Recommendation:

We recommend the University revise its current process to require procurement card transactions be reviewed and approved by the card holder and an independent reviewer prior to recording the transactions in the general ledger. Such process modifications may include eliminating the auto-reconciliation function or establishing another mechanism to allow auto-reconciled transactions to be reviewed and approved prior to being recorded in the specific general ledger accounts. We also recommend the University implement procedures to identify duplicate transactions and to reconcile procurement card transactions to travel reimbursement forms.

University Response:

Accepted.

The University acknowledges there are inherent risks involved with a P-Card program and has devoted resources to ensure the University's program is established with a reasonable balance of control and efficiency. The P-Card system is critical to the University's initiatives to reduce administrative costs. It allows the efficient completion of small dollar business transactions, averaging approximately \$250 each, at minimal administrative overhead costs. The University recognizes that with 5,700 active procurement cards, erroneous charges can and do occur under current P-Card policies and procedures. The University employs careful oversight and review to ensure these errors are minimal, and it takes immediate action when errors are discovered. The University will continue to be proactive in improving controls over the P-Card system and will install system and/or process improvements to ensure all P-card transactions are reconciled. Due to the nature of P-card transaction activity, it may not be possible to achieve reconciliation prior to posting to the general ledger for all transactions.

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The eight cardholders for whom paper authorization forms could not be located are authorized cardholders who were issued cards prior to October 2005. Since this date, to ensure retention of this important documentation, units have been required to fax a copy of all signed authorization forms to the central Corporate Card Office before a card would be issued. In addition, all cardholders in the system as of the fall of 2007 were required to complete online training, testing, and re-certification prior to receiving renewal P-cards in February 2008. The University will ensure the Corporate Card Office has a copy of the paper authorization form on file for all current P-Card holders.

Current University procedures require units to establish appropriate internal controls to reconcile travel purchased using the P-Card to the traveler's *Employee Travel/Miscellaneous Reimbursement Form*. In addition to these existing controls, the University accepts the recommendation to implement additional, system controls to further eliminate the possibility of duplicate transaction and to reconcile P-Card transactions to travel reimbursement forms.

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM

Schedule of Findings and Responses

For the Year Ended June 30, 2009

Finding AFS 09-03 – Inadequate Year End Accounts Payable Process

The University has not established adequate internal controls over identifying and recording period end accounts payable for financial reporting purposes.

During our audit, we noted the University's year end accounts payable procedures include specifically reviewing cash disbursements made subsequent to year end through the fourth week in July to determine to which accounting period the expenditures pertain. Subsequent to the fourth week of July, further reviews are performed for certain expenditures by Health Services Facilities System to develop an accrual related to subsequent disbursements. No further formal procedures are performed over cash disbursements subsequent to the fourth week in July and the University does not perform procedures to estimate potential unrecorded liabilities.

In addition, we identified two subsequent disbursements (totaling \$18,325) which pertained to fiscal year 2009, but which were not properly accrued by the University and one disbursement (totaling \$204,156) which pertained to 2010, but which had been accrued in error. We also identified eight expenditures which pertained to fiscal year 2008 in our State Compliance testwork (totaling \$39,135) which were reported in fiscal year 2009.

The control deficiencies and exceptions discussed above relate to the operations of the University including the Auxiliary Facilities System.

Generally accepted accounting principles require expenditures to be reported in the period they are incurred. Additionally, the Fiscal Control and Internal Auditing Act (Illinois Compiled Statutes Chapter 30 Section 10/3001), requires the University to establish and maintain a system, or systems, of internal fiscal and administrative controls, which shall provide assurance that: (1) resources are utilized efficiently, effectively, and in compliance with applicable law; (2) obligations and costs are in compliance with applicable law; (3) funds, property, and other assets and resources are safeguarded against waste, loss, unauthorized use, and misappropriation; (4) revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources; and (5) funds held outside the State Treasury are managed, used, and obtained in strict accordance with the terms of their enabling authorities and that no unauthorized funds exist. The University's system of internal controls should include procedures to assess whether expenditures are reported in the appropriate period.

In discussing these conditions with University personnel, they stated that they believed their process was adequate.

Failure to analyze cash disbursements subsequent to year end may result in the misstatement of the University's financial position. (Finding Code AFS 09-03)

UNIVERSITY OF ILLINOIS AUXILIARY FACILITIES SYSTEM

Schedule of Findings and Responses

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Recommendation:

We recommend the University implement procedures to assess the completeness of its accounts payable at year end. Such procedures may include extending the timeframe for which the University evaluates cash disbursements subsequent to year end or developing procedures to estimate the accounts payable balance.

University Response:

Accepted. The University will develop improvements to procedures to address the recommendations noted in this finding.