

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

Report Required under *Government Auditing Standards*

Year ended June 30, 2011

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, 2011 were issued under a separate cover.	

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Summary

Year ended June 30, 2011

(1) 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.

(2) Summary of Findings

The auditors identified a certain deficiency in internal control over financial reporting that they considered to be a material weakness 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 10 of this report.

Schedule of Findings and Responses		
Current year findings		
Item no.	Page	Description
AFS 11-01	4	Inadequate year end receivable and payable accruals process
AFS 11-02	6	Inadequate controls over user access to information systems
AFS 11-03	9	Inadequate controls over University procurement card transactions

(3) Exit Conference

A formal exit conference was waived by the University in a letter dated December 5, 2011. Responses to the recommendations were provided by Patrick Patterson, Maxine Sandretto and Michael Bass in a correspondence dated December 2, 2011.



KPMG LLP
303 East Wacker Drive
Chicago, IL 60601-5212

**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, 2011, and have issued our report thereon dated December 16, 2011. 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

Management of the System is responsible for establishing and maintaining effective 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 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 a certain deficiency in internal control over financial reporting that we consider to be a material weakness 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 deficiency in the System's internal control over financial reporting described as finding number AFS 11-01 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 11-02 and AFS 11-03 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 System's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit the System's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Illinois Auditor General, the Illinois General Assembly, the Illinois Legislative Audit Commission, the Illinois Governor, University management, the Board of Trustees of the University of Illinois, 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

Chicago, Illinois
December 16, 2011

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Schedule of Findings and Responses

Year ended June 30, 2011

Finding AFS 11-01 – Inadequate Year End Receivable and Payable Accruals Process

The University has not established adequate internal controls over accurately identifying and recording period end accounts payable and accounts receivable transactions 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 October to determine to which accounting period the related expense transactions pertained. We further noted the University's year end accounts payable procedures also include calculating and recording an estimate of unrecorded liabilities largely based on historical disbursement activity. In addition, the University performs reviews over cash disbursements subsequent to year end to track and monitor the actual level of unrecorded liabilities. The actual level of unrecorded liabilities is then compared to the estimate originally recorded for financial reporting purposes. The University's year end accounts receivable procedures require units to identify and report any accounts receivable. In relation to our testwork on revenue transactions, we reviewed 124 revenue transactions recorded during the fiscal year (totaling \$14,545,678) and 27 cash receipt transactions recorded subsequent to year end (totaling \$1,274,941). In relation to our testwork on expense transactions, we reviewed 205 expense transactions recorded during the fiscal year (totaling \$51,343,490) and 63 cash disbursements subsequent to year end (totaling \$39,192,830). During our review of these transactions we noted the following items were not recorded to the proper accounting period:

- Six educational activities revenue transactions for third party pharmacy billings (totaling \$370,897) which pertained to fiscal year 2010 but were recognized as revenue in fiscal year 2011.
- Three educational activities revenue transactions for drug information services billings (totaling \$52,356) which pertained to fiscal year 2011 but was recognized as revenue in fiscal year 2012.
- Two rental and lease revenue transactions (totaling \$813) which pertained to fiscal years 2010 and 2012 but were recognized as revenue in fiscal year 2011.
- One rental and lease revenue transaction (totaling \$1,016) which pertained to fiscal year 2012 but was recognized as revenue in fiscal year 2011.
- One rental and lease revenue transaction (totaling \$401) which pertained to fiscal year 2011 but was recognized as revenue in fiscal year 2010.
- Two educational activities revenue transactions for an accelerated corporate MBA cohort program (totaling \$955,642) which pertained to fiscal years 2009 and 2010 but were recognized as revenue in fiscal year 2011.
- One employee benefits expense transaction (totaling \$92,718) which pertained to fiscal year 2010 but was recognized as expense in fiscal year 2011.
- One supplies and services expense transaction (totaling \$34,553) which pertained to fiscal year 2011 but was recognized as expense in fiscal year 2012.
- Two travel expense employee reimbursements (totaling \$5,120) which pertained to fiscal year 2010 but were recognized as expense in fiscal year 2011.

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- One scholarships and fellowships expense transaction (totaling \$1,250) which pertained to fiscal year 2010 but was recognized as expense in fiscal year 2011.
- Two supplies and services expense transactions (totaling \$44,020) which pertained to fiscal year 2010 but were recognized as expense in fiscal year 2011.

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

Generally accepted accounting principles require transactions 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 accurately assess whether expenditures and revenues are reported in the appropriate period.

In discussing these conditions with University personnel, they stated that the units associated with the exceptions did not adequately understand/follow the procedures required to record the transactions in the proper period.

Failure to accurately analyze cash disbursements and receipts subsequent to year end may result in the misstatement of the University's financial statements. (Finding Code AFS 11-01, AFS 10-03, AFS 09-03)

Recommendation:

We recommend the University review its current process to assess the completeness of its revenue and expense accruals at year end and consider changes necessary to ensure all period end accounts payable and accounts receivables are accurately identified and recorded.

University Response:

Accepted. The University will review existing procedures in these areas and take corrective action to address the recommendation in this finding.

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Finding AFS 11-02 – 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, in addition to operating and supporting information systems for purchasing and human resource. The University functions in a highly distributed operating environment with several thousand users having varying types of system access. Access is granted to users of the University's information systems based on standardized user access profiles. 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. The University has implemented a process to review standardized user profiles, train unit security contacts, and perform an annual access review for the Banner ERP system. However, the annual access reviews are not consistently and formally documented to provide evidence supporting the results of each user review. Further, the University has not performed a periodic access review of the human resources supporting information system.

In addition to the internal control deficiencies identified above, during our review of user access rights we 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. We identified the following exceptions regarding improper authorization or inappropriate access rights based upon review of each user's job function:

- There are 161 terminated users (out of 418 total terminated users) with active accounts that were not removed in a timely manner.
- There were 43 users (out of 99 total users) with inappropriate access to update accrued leave or sick time in Banner. None of these 43 users appeared to have performed inappropriate transactions.
- There were 8 users (out of 44 total users) with inappropriate access to release financial holds from a student account in Banner.
- There were 3 users (out of 84 total users) with inappropriate access to update employee pay rates in Banner.
- There was one user (out of 21 total users) with inappropriate access to update tuition rates and fees and student rate codes in Banner.
- There was one user (out of 45 total users) with inappropriate access to apply and unapply payments on student accounts in Banner.
- There was one user (out of 14 total users) with inappropriate access to update the vendor master file in Banner.
- There were two users (out of 17 total users) with inappropriate administrative access to the human resources supporting information system.
- There was one generic user account (out of 4,481 total user accounts) with inappropriate access to the purchasing information system.

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- There were two new user accounts (out of a sample of 30 new user accounts) that were not properly authorized.

Further, we noted reviews of terminated employees with access to the information systems are not being performed effectively. Beginning in August 2010, the University's information technology department began implementing procedures to perform terminated employee access reviews on a daily basis. However, this procedure alone was not sufficient to provide timely removal of access of terminated employees. In addition, there are no procedures in place to monitor user access rights for employees who transfer positions and change job functions.

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, and unauthorized use; (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 document monitoring procedures of 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 that they agreed with the exceptions noted in this finding. They further noted that work had been underway to address many of the weakness noted.

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 transactions can be recorded by unauthorized individuals. (Finding Code AFS 11-02, AFS 10-01, AFS 09-01, AFS 08-05)

Recommendation:

We recommend the University implement procedures to formally document the reviews of user access rights, and maintain documentation of the results of those reviews, 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. Additionally, we recommend the University implement procedures to monitor user access

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rights for employees who transfer positions and change job functions and implement procedures to ensure reviews of user access rights for terminated employees are effectively performed.

University Response:

Accepted. The University's decentralized operating environment involves several thousand 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. The University does have processes in place to limit the ability of users to perform transactions, but does agree that improvement to the user access control environment is needed and will be beneficial. The University has been working steadily to improve information systems access controls over the past year and will take the necessary corrective action going forward to address the recommendation in this finding.

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Finding AFS 11-03 – 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 authorized employees throughout the University to make smaller qualified purchases (defined as less than \$4,999) on a charge card which is directly reimbursed by the University on a monthly basis. The University's policies require employees assigned a procurement card to complete training on policies and procedures, pass a test, and sign an agreement stipulating they will use the card in accordance with University policy. This agreement is also required to be authorized by the employee'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 the University 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. We also identified the following exceptions in our testwork over 40 procurement card transactions (totaling \$146,809):

- One transaction (totaling \$2,557) was for charges prohibited by the University's procurement card policies.
- Two transactions (totaling \$12,680) were each paid in two installments, circumventing the card holders' approved single transaction limit of \$4,999.
- Two transactions (totaling \$19,364) exceeded the single transaction limit of \$4,999.
- Two transactions (totaling \$2,664) were not reviewed and approved by an assigned reviewer.

The University has approximately 5,100 active procurement cards and the procurement card expenditures paid for the year ended June 30, 2011 totaled \$98,042,483.

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 procurement card transactions are in accordance with University policies and procedures and supporting documentation for each transaction is maintained.

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In discussing these conditions with University personnel, they stated the University is still in the process of implementing its new Travel and Expense Management System, which will provide controls, in addition to those already in place, to further eliminate the possibility of duplicate transactions with regard to travel reimbursements. The bulleted exceptions noted in this finding are a result of human error; specifically, the failure of certain employees to comply with University policy that is clearly stated and disseminated to all through required training.

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 11-03, AFS 10-02, AFS 09-02, and AFS 08-03)

Recommendation:

We recommend the University review its current process for reviewing and approving procurement card transactions and consider any changes necessary to ensure charges are made in accordance with University policies and procedures and supporting documentation for each transaction is maintained. 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 recognizes that with approximately 5,100 active procurement cards, erroneous charges can and do occur. 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 continue to provide training and review of policies and requirements for all cardholders. The University anticipates completing implementation of its new Travel and Expense Management System, which will provide additional controls related to employee travel reimbursements, by the end of fiscal year 2012.