



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

Report Required under *Government Auditing Standards*

Year ended June 30, 2013

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)

Table of Contents

	Page(s)
Summary	1
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 <i>Government Auditing Standards</i>	2-3
Schedule of Findings and Responses	4-8

The annual financial statements of the University of Illinois Auxiliary Facilities System for the year ended June 30, 2013 were issued under a separate cover.

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

Summary

Year ended June 30, 2013

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 significant deficiencies, which are described in the accompanying schedule of findings and responses on pages 4 through 8 of this report.

Schedule of Findings and Responses

Current Year Findings:

<u>Item No.</u>	<u>Page</u>	<u>Description</u>
AFS 2013-001	4	Inadequate Year-End Expense Accruals, and Revenue and Expense Deferrals Process
AFS 2013-002	7	Inadequate Controls over University Procurement Card Transactions

Exit Conference

A formal exit conference was waived by the University in a letter dated December 7, 2013. Responses to the recommendations were provided by the University's Office of Business and Financial Services in a correspondence dated December 9, 2013.



KPMG LLP
Aon Center
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Chicago, IL 60601-6436

**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 of the State of Illinois, we have audited, in accordance with the 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, the financial statements of the University of Illinois Auxiliary Facilities System (the System), a segment of the University of Illinois (the University), which comprise the statement of net position as of June 30, 2013, and the related statements of revenue, expenses, and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon date December 20, 2013. Our report includes references stating that the System did not present a management's discussion and analysis that accounting principles generally accepted in the United States of America require 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.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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. Accordingly, we do not express an opinion on the effectiveness of the System's internal control.

A deficiency in internal control 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, 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. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit, we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in



the accompanying schedule of findings and responses as finding numbers AFS 2013-001 and AFS 2013-002, which we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's financial statements are free from 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 Findings

The System's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. The System's responses were not subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on the responses.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the System's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the System's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Chicago, Illinois
December 20, 2013

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

Schedule of Findings and Responses

Year ended June 30, 2013

Finding AFS 2013-001 – Inadequate Year-End Expense Accruals, and Revenue and Expense Deferrals Process

The University has not established adequate internal controls over accurately identifying and recording period-end accounts payable and deferred expense and revenue 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 end of 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 process to identify expense deferrals includes a review of all cash disbursements by University Payables. University Payables identifies cash disbursements for invoices that cover multiple fiscal years and reports them to University Accounting and Financial Reporting (UAFR). UAFR will then post year-end adjustments to defer the appropriate expenses. The University's year-end deferred revenue procedures require units to identify and report any known deferred revenue transactions to UAFR.

In relation to our testwork over Educational Activities and Auxiliary Enterprises revenue transactions, we reviewed 164 revenue transactions recorded during the fiscal year (totaling \$5,737,468). Additionally, we separately reviewed 31 internal journal voucher revenue transactions recorded during the fiscal year (totaling \$70,704,670 debits and \$38,727,786 credits). In relation to our testwork over expense transactions, we reviewed 189 cash disbursement transactions recorded during the fiscal year (totaling \$158,100,167) and 70 cash disbursements subsequent to year-end (totaling \$86,780,967). Additionally, we separately reviewed 72 internal journal voucher expense transactions recorded during the fiscal year (totaling \$129,667,697 debits and \$293,900,157 credits).

During our review of these transactions, we noted the following items were not recorded in the proper accounting period:

Educational Activities and Auxiliary Enterprises revenue transaction:

- One Auxiliary Enterprises revenue transaction for summer intern housing (totaling \$93) that was recognized as revenue in fiscal year 2013, which should have been reported as deferred revenue at the end of fiscal year 2013 and recognized as revenue in fiscal year 2014;

Supplies and Services expense transactions:

- One Supplies and Services internal journal voucher expense transaction (totaling \$6,278) that was recognized as expense and accrued for in fiscal year 2013, which should have been recognized as expense in fiscal year 2014;

(Continued)

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

Schedule of Findings and Responses

Year ended June 30, 2013

- Two Supplies and Services expense transactions (totaling \$393,695) that included \$387,544 that were recognized as expense in fiscal year 2013, which should have been recognized as expense and accrued for in fiscal year 2012;
- Two Supplies and Services expense transactions (totaling \$3,747,837) that were recognized as expense in fiscal year 2013, which included \$1,768,266 that should have been deferred at fiscal year-end 2013 and recognized as expense in fiscal year 2014;
- One Supplies and Services expense transaction (totaling \$1,200) that was recognized as expense in fiscal year 2012, which should have been recognized as expense in fiscal year 2013; and
- One Supplies and Services expense transaction (totaling \$103,101) that was appropriately recognized as expense for fiscal year 2013, which should have been recognized as an accounts payable and a capitalized advertising cost for fiscal year 2012.

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 expenses and revenues are reported in the appropriate period.

The units associated with the exceptions did not adequately understand/follow the procedures to record the transactions in the proper period. While the University believes it has processes in place to prevent material misstatements in the financial statements, the highly decentralized business environment with hundreds of units and large volumes of transactions does present challenges to catching all errors.

Failure to accurately analyze revenue and expense transactions at year-end and subsequent to year-end may result in the misstatement of the University's financial statements. (Finding Code No. AFS 2013-001, AFS 12-01, AFS 11-01, AFS 10-03, and AFS 09-03)

Recommendation:

We recommend the University review its current process to assess the completeness and existence of its revenue and expense transactions at year-end and consider changes necessary to ensure all period-end accounts payable, and deferred revenues and expenses are accurately identified and recorded.

(Continued)

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

Schedule of Findings and Responses

Year ended June 30, 2013

University Response:

Accepted. The University has already implemented significant process enhancements in this area. Through analysis of the exceptions identified in this audit, the University will work to develop and implement corrective actions to further improve the year-end processes in this area.

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

Schedule of Findings and Responses

Year ended June 30, 2013

Finding AFS 2013-002 – 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 that allows individuals throughout the University to make smaller purchases (defined as less than \$4,999) on a credit card, which is directly paid 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 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.

During our testwork over 40 procurement card transactions totaling \$98,097, we noted the following:

- One transaction (totaling \$2,938) was recorded in the incorrect fiscal year;
- Two transactions (totaling \$2,964) were for charges prohibited by the University's procurement card policies; and
- One transaction (totaling \$71) included a charge of \$6 for sales tax which is a prohibited charge because the University is tax-exempt.

The University has approximately 5,461 active procurement cards, and the procurement card expenditures paid for the year ended June 30, 2013 totaled \$65,039,944.

The Fiscal Control and Internal Auditing Act (30 ILCS 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 effectively, and in compliance with applicable law; (2) obligations and cost 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 preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources; and (5) fund 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.

The bulleted exceptions noted in this finding were a result of human error.

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 No. AFS 2013-002, AFS 12-02, AFS 11-03, AFS 10-02, AFS 09-02, and AFS 08-03)

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

Schedule of Findings and Responses

Year ended June 30, 2013

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.

University Response:

The University recognizes that with over 5,000 active purchasing 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.