



BOARD OF REGENTS

SUMMARY OF ITEM FOR ACTION,
INFORMATION OR **DISCUSSION**

TOPIC: SB & Company, LLC. – Communication of Audit Strategy and Approach for the FYE 2014 Independent Audit of Financial Statements

COMMITTEE: Audit Committee

DATE OF COMMITTEE MEETING: June 11, 2014

SUMMARY:

Materials attached.

FISCAL IMPACT: none

CHANCELLOR'S RECOMMENDATION:

COMMITTEE ACTION: None

DATE:

BOARD ACTION: None.

DATE:

SUBMITTED BY: David Mosca



SB & COMPANY, LLC



COMMUNICATIONS WITH THOSE
CHARGED WITH GOVERNANCE

AUDIT STRATEGY AND APPROACH

FOR THE YEAR ENDED JUNE 30, 2014

JUNE 11, 2014

EXPERIENCE



QUALITY



CLIENT SERVICE



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Executive Summary



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Scope of services/timing/deliverables

- Continue our institutions rotations approach
- Timing similar to last year
- Same deliverables as last year

Audit institutions

- Bowie State University
- Frostburg State University
- University of Maryland, College Park
- University of Baltimore
- Will perform an analytical scope at Coppin State University because still in process of changes; Will perform a follow-up on prior year's issues

Significant current year areas of emphasis

- Migration from FRS to Quali Financial System at UMCP
- Accounting for cost of implementation of Quali Financial System
- ACC Receivable and revenue recognition for Big 10 contract
- Status of ACC Litigation and potential liability
- UMUC operations (decline in revenue and cost containment / reduction effect)
- Overseas activity at UMAB and reporting entity requirements
- Finance function at Coppin
- Collectability of receivables
- Preparation for adoption of GASB No. 68



Scope of Services



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- Audit of the June 30, 2014, financial statements
- OMB Circular A-133 Single Audit testing and findings to be included in the State of Maryland Single Audit Report
- Recommendations and observations noted during the audit process and status of prior year recommendations
- Campus enrollment agreed-upon procedures reports
- Agreed-upon procedures for bond issuances and review of official statements
- Year-round advice and consultation



Engagement Timing



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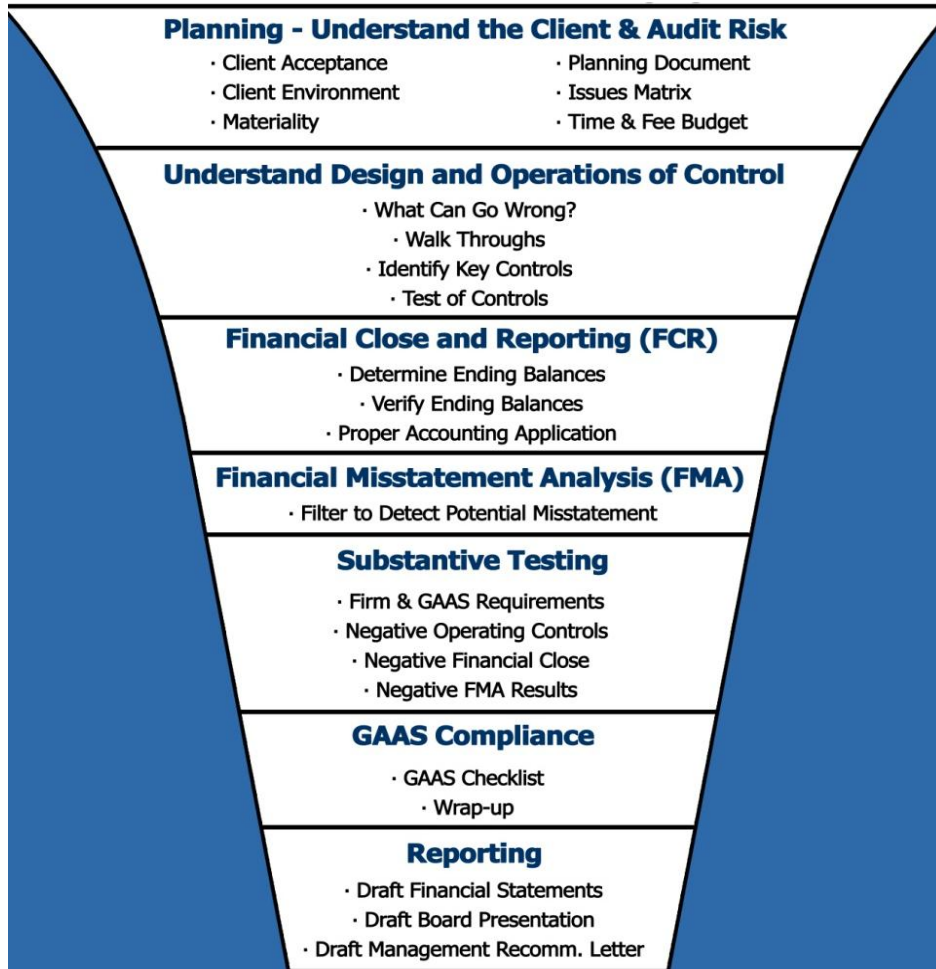
April 2014	Planning meeting with system headquarters
May 2014	Meeting with internal auditor (IA) on the scope of their assistance for 2014 audit
May – June 2014	Preliminary field work, includes single audit walkthrough and IT environment review of testing
June – August 2014	IA perform MHEC enrollment audits
August 2014	Meet with IA to discuss preliminary results
September– October 2014	Final field work
October 2014	Exit conference with institutions regarding findings and recommendations
November 2014	Meet with Audit Committee to review Financial Statement draft and observations
December 2014	Audit and Finance Committee presentation



SBC Risk-Based Audit Approach



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Focus During this Stage

- Identifying internal, external, and financial statements risks
- Develop audit plans
- Evaluate your controls and processes
- Test your key controls
- Evaluate your processes to report correct amounts
- Evaluate reporting policies
- Review financial statements for misstatements
- Verify selected account balances
- Obtain third-party verification
- Professional standards requirements
- Obtain representation
- Evaluate results of audit procedures
- Communicate results and prepare reports to issue

Working with Internal Audit



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Process	Assistance Provided
Planning	<ul style="list-style-type: none">• Communication on risks and issues by institution• Review of IA audit plan• Review of IA reports issued
Risk Assessment	<ul style="list-style-type: none">• Discussion on overall risk of the system• Sharing of internal risk assessment
Internal Controls	<ul style="list-style-type: none">• Collaboration on testing key processes• Assistance on MHEC agreed upon procedures on enrollment data• Sharing of reports issued by IA and reliance on areas tested by IA
Preliminary Fieldwork	<ul style="list-style-type: none">• IA staff helps with testing during site visits• Discussion as issues arise during audit
Final Fieldwork	<ul style="list-style-type: none">• IA staff helps with testing during site visits• IA staff present at institution exit interviews

Understanding of the Entity and its Environment External Factors Effecting the University



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- Providing a safe environment / campus security
- Performance based funding
- Tuition policy
- Admission and acceptance rate
- Enrollment management and graduation rates
- Limited growth in college spending
- Declining enrollment
- Disaster preparedness
- Additional needs for capital spending
- Competition from internet-based institutions
- Decentralized revenue sources and controls over that revenue
- Pressures for alternative funding of instruction and private and public partnerships
- Private and public partnerships governance
- Potential increase in uncollectible student receivables
- Technology enhancements and investments
- Need to be more energy efficient to save costs
- IRS concern with tax compliance
- Succession and talent management planning
- New accounting and reporting for pension and OPEB liability
- Rising pension and OPEB contributions
- Green expenditures and expectations
- Autonomy of departments
- Endowment spending and management
- Athletic departments spending and compliance
- Recruiting skilled employees and faculty
- Changes in bond ratios outlook
- Federal policy expanding the rights of undocumented youth
- Student loans outstanding
- Technology security and cyber security
- Reduction in programs offered
- Funding for education
- Effect of rise in interest rates
- Increased debt outstanding
- Consolidation of back office operations and outsourcing



Understanding of the Entity and its Environment External Factors Effecting the University



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(continued)

Accounting and Audit Pronouncements

Number	Statement	Effective Date
GASB 68	Accounting and Financial Reporting for Pensions -- An amendment of GASB Statement No. 27	June 30, 2015
GASB 70	Accounting and Financial Reporting for Nonexchange Financial Guarantees	June 30, 2014
GASB 71	Pension Transition for Contributions Made Subsequent to the Measurement Date (an amendment of GASB Statement No. 68)	June 30, 2015



Specific Risks by Institution



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University-wide

- Public and Private partnership monitoring
- Investment valuation and valuing alternative investments
- Pension liability
- OPEB liability
- Collectability of receivables
- Cash receipts outside of finance office
- Legislative audit findings
- IT security

Coppin State University

- Finance function
- Growth of campus and increased costs

UM, Baltimore

- Accountability of overseas activity (audit)
- Continued clean-up of unbilled receivables
- Limited controls over grant overspending
- P-card monitoring
- Physician Practice Accounting

UM, College Park

- Revenue recognition for Big 10 contract
- Migration from FRS to Quali Financial System
- Accounting for ACC receivable/liability

UM, Baltimore County

- Grant accounting system
- Fixed asset accounting

UM, University College

- Decreased enrollment due to sequestration
- Cost containment/reduction
- Software cost accounting

Bowie State University

- Follow up on legislative audit IT findings

Frostburg State University

- Follow up on legislative audit IT findings



Assessment of Control Environment



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Area	Points to Consider	Our Assessment
Control Environment	<ul style="list-style-type: none"> • Key executive integrity, ethical, and behavior • Control consciousness and operating style • Commitment to competence • Exercise oversee responsibility • Organizational structure, responsibility, and authority • Enforce accountability • HR policies and procedures 	
Risk Assessment	<ul style="list-style-type: none"> • Define objectives and risk tolerances • Identify, analyze, and respond to risk • Assess fraud risk • Identify, analyze, and respond to change • Mechanisms to anticipate, identify and react to significant events • Processes and procedures to identify changes in GAAP, business practices, and internal control. 	
Control Activities	<ul style="list-style-type: none"> • Design control activities • Design activities for the information system • Implement control activities • Existence of necessary policies and procedures • Clear financial objectives with active monitoring • Logical segregation of duties • Periodic comparisons of book-to-actual and physical count-to-books • Adequate safeguards of documents, records, and assets • Access controls in place 	



Assessment of Control Environment



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Area	Points to Consider	Our Assessment
Information & Communication	<ul style="list-style-type: none"> • Use quality information • Communicate internally • Communicate externally • Adequate performance reports produced from information systems • Information systems are connected with business strategy • Commitment of HR and finance to develop, test, and monitor IT systems and programs • Business continuity and disaster plan for IT • Established communication channels for employees to fulfill responsibilities • Adequate communication across organization 	
Monitoring	<ul style="list-style-type: none"> • Perform monitoring activities • Remediate deficiencies • Periodic evaluations of internal controls • Implementation of improvement recommendations • Internal Audit 	



Evaluation of Key Processes



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Process	Function	Design	Operation
Treasury	<ul style="list-style-type: none"> • Cash Management • Investment Accounting • Reconciliation 		
Estimation	<ul style="list-style-type: none"> • Methodology • Information • Calculation 		
Financial Reporting	<ul style="list-style-type: none"> • Accounting Principles and Disclosure • Closing the Books • Consolidation • General Ledger and Journal Entry Processing • Verification and Review of Results 		
Expenditures	<ul style="list-style-type: none"> • Vendor Maintenance • Purchasing • Receiving • Accounts Payable and Cash Disbursement 		
Payroll	<ul style="list-style-type: none"> • Hiring • Attendance Reporting • Payroll Accounting and Processing • Payroll Disbursements • Separation 		
Revenue	<ul style="list-style-type: none"> • Billing • Cash Receipts 		
Fixed Assets	<ul style="list-style-type: none"> • Physical Custody • Asset Accounting • Depreciation 		
Compliance	<ul style="list-style-type: none"> • Assess Internal and External Risk • Regulatory Compliance • Monitor Compliance • Compliance 		
Information Technology	<ul style="list-style-type: none"> • Computer Operations • Segregation of Duties and Management Oversight • Information Security and Transaction Authorization • Program Integrity and Change Management 		
Grant Compliance	<ul style="list-style-type: none"> • Acceptance • Grant oversight • Compliance • Reporting • Monitoring • Accounting • Billing and collection • Grant close out 		



Scope and Location of Testing



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University	Scope of Work				
	Audit	Review	Analytical	Single Audit	IT Review
University of Maryland, College Park	X			X	X
University of Maryland at Baltimore		X			
University of Maryland, Baltimore County		X		X	
Towson University			X		
University of Maryland, University College		X			
Coppin State University			X *		
University of Maryland, Eastern Shore			X		
University of Baltimore	X				X
Bowie State University	X			X	X
Salisbury University		X			
Frostburg State University	X			X	X
University of Maryland Center for Environmental Science			X		
Headquarters (cash, debt, and investments)	X				
Five-year rotation of Level of Testing at Each Institution					

* Coppin State University will be an analytical school with substantive testing and follow up on prior year issues.





Audit Coverage

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Level	Understand Control Environment	Understand Effectiveness of the Design of Controls	Testing Effectiveness of Key Controls	Understand Financial Close Process	Financial Misstatement Analysis	Substantive Testing	Evaluate General IT Controls	Evaluate Applications IT Controls
Audit	X	X	X	X	X	X	X	X
Review	X	X		X	X	X *		
Analytical				X	X			

* Certain substantive testing for high risk/problem areas





IT Review Coverage

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General IT Controls

➤ Computer Operations

- Password policies/Audit logs
- Server Operating System Configurations
- Server Operating System software versions
- Physical Security and Environmental controls over data center
- Database system configuration
- Database software versions
- Timely implementation of security patches for servers and desktops in Finance and Infrastructure
- Anti-virus software, keeping current on virus definitions
- Disaster recovery testing

➤ Segregation of Duties and Management Oversight

- Review of permissions to datasets that maintain or change source and object code (as applicable)
- Periodic dataset review process (as applicable)
- Implementation of security policy
- Governance (policies in place to address emerging concerns for example cyber threats)
- Oversight and enforcement of policies

➤ Information Security and Transaction Authorization

- Logical separation of financial systems (VLANS)
- Firewall rules which manage traffic to/from financial systems.
- Network Monitoring (IT and Finance areas only)
- Network security scanning (IT and Finance areas only)/remediation of identified concerns

➤ Program Integrity and Change Management

- Change management process and monitoring
- Problem management





IT Review Coverage

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Applications IT Controls for the following processes

- Cash receipts
- General ledger / financial reporting
- Cash disbursement / purchase cards / expense reimbursement / accounts payable
- Procurement / vendor management
- Inventory
- Fixed assets / construction in process
- Payroll / time reporting / human resources
- Student tuition billing / financial aid / accounts receivable
- Auxiliary services billing / accounts receivable
- Grant and contract billing / unbilled accounts / accounts receivable
- Student registration / enrollment



Testing Coverage



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Key Accounts	June 30, 2013 Balance	Percentage Coverage		
		Audit Schools	Review Schools	Analytical Schools
Cash and cash equivalents	\$1,871,781,518	47%	26%	27%
Accounts receivable, net	268,855,816	41%	39%	20%
Notes receivable, net	66,295,623	28%	47%	26%
Inventories	10,271,714	32%	18%	51%
Endowment investments	192,920,622	57%	41%	2%
Capital assets, net	5,273,348,180	48%	31%	21%
Accounts payable and accrued liabilities	310,619,251	43%	32%	26%
Revenue bonds	1,108,158,762	44%	32%	24%
Deferred revenue	177,345,393	39%	31%	30%
Deferred service concession arrangement receipts	380,711,678	52%	34%	14%
Unrestricted net assets	1,442,111,011	47%	25%	27%
Invested in capital assets	3,733,261,041	48%	31%	21%
Tuition and fees, net	1,187,769,356	38%	23%	39%
Federal grants and contracts	691,994,706	55%	42%	3%
Sales and services of educational departments	287,007,719	9%	87%	4%
Residential facilities	149,800,185	50%	34%	16%
Dining facilities	107,529,267	53%	28%	19%
Intercollegiate athletics	91,248,018	64%	20%	16%
Bookstore	26,179,415	0%	51%	49%
Parking facilities	38,875,667	40%	38%	22%
Other auxiliary enterprises revenues	137,775,593	44%	29%	28%
Other operating revenues	61,658,055	60%	23%	17%
Operating expenses	4,293,338,895	44%	37%	20%



Responsibility for Mitigating Fraud



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Management

- ⦿ CFO/Controller: controls to deter and detect fraud
- ⦿ General Counsel/Compliance: monitoring

Audit Committee

- ⦿ Evaluate management identification of fraud risk
- ⦿ Evaluate implementation of fraud controls
- ⦿ Reinforce “tone at the top”
- ⦿ Conduct special investigations

External Auditor

- ⦿ Evaluate management programs and controls to deter and detect fraud for identified risks
- ⦿ Reasonable assurance that financial statements are free of material misstatement due to fraudulent financial reporting or misappropriation of assets
- ⦿ Compliance with fraud standard (SAS 99)
 - Conversations with finance and operations personnel
 - Disaggregated analytics
 - Surprise audit procedures
 - Journal entry testing



How to Better Serve You



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- **Expectations of us**
- **Communications with you**
- **Communications you want us to have with management**
- **Other things we could do to better serve you**
- **Knowledge we should deliver**
- **Other**





Questions?

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Engagement Team



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