UNIVERSITY OF MINNESOTA
BOARD OF REGENTS
Audit Committee
Wednesday, May 7, 2008
2:00 - 3:30 p.m.
600 McNamara Alumni Center, East Committee Room

Committee Members
Linda Cohen, Chair
Clyde Allen, Vice Chair
Dallas Bohnsack
John Frobenius
Venora Hung
Dean Johnson

Student Representatives
Meghan Keil
Nathan Swanson

A G E N D A

1. Impact of EFS Implementation & New Accounting Pronouncements on the University's Internal Control Environment - M. Volna/D. Seck (p. 2)
2. External Audit Plan - D. Seck/C. McElroy (pp. 3-24)
3. Internal Audit Update - G. Klatt (pp. 25-55)
4. Information Items - G. Klatt (pp. 56-59)
Audit Committee

May 7, 2008

Agenda Item: Impact of EFS Implementation & New Accounting Pronouncements on the University's Internal Control Environment

☐ review  ☐ review/action  ☐ action  ☒ discussion

Presenters: Associate Vice President Michael Volna
Associate Controller, Denise Seck

Purpose:

☐ policy  ☐ background/context  ☒ oversight  ☐ strategic positioning

This discussion is intended to provide the Audit Committee with an overview of the impact of the Enterprise Financial System (EFS) implementation and several new auditing standards on the University's Internal Control Environment.

Outline of Key Points/Policy Issues:

The presentation will cover the critical changes to policies, procedures, and system designs impacting internal controls as a result of the implementation of the Enterprise Financial System. The presentation will also address the significant increase in the documentation of internal controls as required by Statements on Auditing Standards No. 104 – No. 111.

Background Information:

The Audit Committee has previously received updates on the EFS project through previous Semi-annual Controller's Reports, and has received summary information on Statements on Auditing Standards No. 104 – No. 111 in the November 2007, and current Semi-Annual Controller's Report.
Audit Committee  May 7, 2008

Agenda Item:  External Audit Plan

☐ review  ☒ review/action  ☐ action  ☐ discussion

Presenters:  Associate Controller, Denise Seck
            Chas McElroy, Principal, LarsonAllen

Purpose:

☐ policy  ☐ background/context  ☒ oversight  ☐ strategic positioning

To provide an overview of the audit plan to be used by LarsonAllen in performing the University's annual audits for the year-ended June 30, 2008, as required by Audit Committee Charter.

Outline of Key Points/Policy Issues:

The external audit plan presents the approach, objectives, and scope to be used for the University's financial audits and compliance audits. LarsonAllen's work plan and timeline will be reviewed with the Audit Committee.

Background Information:

This report is prepared annually and presented to the Board of Regents Audit Committee in conformance with Board of Regents Policy: Board Operations and Agenda Guidelines.
Audit Approach for the
UNIVERSITY
OF
MINNESOTA

For the Year Ending
June 30, 2008

Submitted by:

LarsonAllen

Minneapolis, Minnesota

DONALD J. LOBERG, CPA
Principal, Nonprofit and Government Group
612/397-3064

CRAIG W. POPENHAGEN, CPA
Principal, Nonprofit and Government Group
612/397-3087

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Minneapolis, Minnesota 55402-1436

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I. CLIENT SERVICE TEAM

Board of Regents of The University of Minnesota

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- Nancy Kaplan: Senior Manager, Information Systems
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- Barry Hanson: Chartered Accountant RUMINCO Ltd.
  - Phone: 441/295-1393
  - Email: bhanson@zobec.bm

Contact Information:

<table>
<thead>
<tr>
<th>Name</th>
<th>Title &amp; E-mail</th>
<th>Office Phone</th>
<th>Cell Phone</th>
<th>Fax</th>
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<tbody>
<tr>
<td>Don Loberg</td>
<td>Lead Client Service Principal <a href="mailto:dloberg@larsonallen.com">dloberg@larsonallen.com</a></td>
<td>612/397-3064</td>
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<tr>
<td>Barry Hanson</td>
<td>RUMINCO-Chartered Accountant <a href="mailto:bhanson@zobec.bm">bhanson@zobec.bm</a></td>
<td>441/295-1393</td>
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<td>441/292-1244</td>
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II. SCOPE OF SERVICES

Our services to the University of Minnesota (the University) for the fiscal year ending June 30, 2008, will include the following:

<table>
<thead>
<tr>
<th>Reports to be issued:</th>
<th>U of M</th>
<th>Rumimco</th>
<th>OHE</th>
<th>NCAA</th>
<th>Student Activities</th>
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<td>Report on Basic Financial Statements, Including In-Relation to Opinion for By-Campuses Statements (1)</td>
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<td>Report on Internal Control Over Compliance with Major Program Requirements (3)</td>
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<td>Report on Statement of Activities of the University’s Department of Concerts and Lectures (5)</td>
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<td>Report on Agreed-Upon Procedures (6)</td>
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| Management Letter (7)                                                              |       | X       |     |      |                    |
| Required Communications Letter (8)                                                 |       |         | X   |      |                    |

1. We will express an opinion on the fair presentation of the University’s consolidated financial statements taken as a whole. We will not provide an audit opinion on management’s discussion and analysis nor any introductory material to the consolidated financial statements for the University.

The discretely presented component units that are included in the University’s consolidated financial statements are audited by other audit firms. Our opinion on the financial statements of the discretely presented component units will be based solely on the report of such other audit firms.

The financial statement audit will also include an “in-relation-to” report on the financial statements by campus.

Bermuda regulations state that only an accounting firm domiciled in Bermuda may audit and provide an opinion on entities located in Bermuda. Therefore, the firm of Barry Hanson, a Chartered Accountant licensed in Bermuda, will express an opinion on the fair presentation of RUMINCO Ltd.’s financial statements taken as a whole. Barry Hanson, Chartered Accountant, is a subcontractor to LarsonAllen.

2. We will report to the University’s management and Audit Committee any material instances of noncompliance with laws and regulations and material weaknesses or significant deficiencies in internal controls over financial reporting that we detect during our audit.
II. SCOPE OF SERVICES

3. We will issue a report on the University’s compliance with federal grant programs, such as federal Student Financial Aid and federally-sponsored research programs, that are selected by us for testing under OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. We will also report on the University’s internal controls over compliance with such requirements.

Our report will communicate any significant deficiencies found during our audit of the University. A significant deficiency shall be defined as a single control deficiency, or a combination of control deficiencies, that adversely affects the entity’s ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of an entity’s financial statements that is more than inconsequential will not be prevented and detected.

A significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected will be disclosed as a “material weakness”.

The report on compliance will also include an “in-relation-to” report on the schedule of expenditures of federal awards.

Additionally, we will prepare the data collection form to be submitted to the Federal Audit Clearinghouse as part of the University’s annual reporting package.

4. We will issue a report on University management’s assertions on compliance over state-funded student financial aid programs in accordance with the Minnesota Office of Higher Education’s (OHE) 2007-08 Audit Guide.

5. We will express an opinion on the fair presentation of the statement of activities of the Department of Concerts and Lectures (Northrop Auditorium). This audit is required primarily for purposes of Northrop Auditorium’s annual application for grant funding from the Minnesota State Arts Board.

6. We will issue a report on agreed-upon procedures performed for the University’s Office of Investments and Banking, the National Collegiate Athletic Association, and Student Organizations.

7. We will issue a Management Letter containing other observations and recommendations, including responses from University management.

8. We will provide a letter to the Audit Committee concerning certain communications required by Statement on Auditing Standards No. 114, The Auditor’s Communication with Those Charged with Governance.

9. We will also summarize the results of our audits in a Powerpoint presentation to the Board of Regents.
## II. SCOPE OF SERVICES

### Work Plan Summary

For our audit of fiscal year 2008, we plan to perform a significant amount of audit procedures at interim dates in May and June and will begin our final fieldwork in September. We will meet with University officials to design the exact audit schedule, including the pre-audit planning meetings.

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III. SIGNIFICANT AUDIT AREAS

Some of the areas where we will focus our attention are as follows:

**New Auditing Standards** – The American Institute of Certified Public Accountants has issued ten new auditing standards during 2005/2006 which will affect the audit of the year ending June 30, 2008. In general, the new auditing standards are a result of an initiative to converge the auditing requirements for non-SEC organizations with those of the Public Company Oversight Board (i.e. SEC companies) and those of the international auditing standards boards.

These new auditing standards require a more rigorous assessment of risks related to financial reporting and a significantly enhanced linking of perceived risk areas to the auditing procedures performed. Under the new standards, auditors will be required not only to test the effectiveness of internal controls over all aspects of financial reporting, but also to fully understand the internal controls of the Institution. This will require the Institution to fully document and evaluate the design of internal controls. This documentation will allow the auditors to perform the necessary sample testing or “walkthroughs” of internal controls for all audits.

To assure the University of Minnesota would have the necessary information required by the new standards, LarsonAllen performed a half day training for the University and its component units. The training included understanding how to prepare both the risk assessment and internal control documentation required by the standards. In addition to the training we performed, we have been an available resource to management if a need would occur.

We anticipate that we will continue to be able to obtain service auditors reports (i.e. SAS 70 reports) to evaluate the effectiveness and design of controls at outsourced service providers such as investment asset managers and student loan servicer’s like ECSI and Campus Partners. However, we will also need to document the design and test the effectiveness of the University’s oversight of such outsourced service providers.

**A-133 Compliance Audit** – The University’s A-133 compliance audit will be a significant audit area given the magnitude of the University’s annual federal grant expenditures. We will audit the federally-sponsored research and Student Financial Aid clusters of programs each year in order to obtain appropriate A-133 audit coverage. Due to the decentralized administration of the University’s several federal and state grant programs, we will perform the A-133 compliance audits for the federal student awards cluster on-site at the Twin Cities, Duluth, Crookston and Morris campuses on a rotational basis.

We will also review the preliminary schedule of expenditures prepared by the University’s Sponsored Financial Reporting personnel to assess whether testing of additional federal programs will be necessary.

**Revenue Recognition and Presentation** – Under GASB Statement No. 34/35, we will evaluate the University’s revenue recognition procedures, particularly when determining the amount of summer session revenue and sponsored projects revenue earned vs. deferred. We will also evaluate the University’s procedures for calculating and presenting the scholarship allowance. While the above work is similar to the previous fiscal year’s audit plan, we will increase our internal control testing and reduce our substantive testing during the 2008 audit.
III. SIGNIFICANT AUDIT AREAS

Payroll Expense – As with all higher education clients, payroll comprises a significant amount of overall operating expense. Our audit procedures will include testing of internal controls over the processing of payroll and predictive tests on payroll accruals and payroll expense based on such factors as changes in full-time equivalents and pay rate increases over the prior year.

Alternative Investments – The valuation of alternative investments represents a significant estimate for the University, and we will assess whether the University’s procedures for estimating the values of alternative investments produce reasonable results. Therefore, we will perform “lookback” procedures regarding valuation of alternative investments by comparing the recorded values of selected investments as of June 30, 2007, to revised values that encompass information available through June 30, 2008 and thereafter. We will mail confirmation letters to the respective asset managers to verify the existence of the holdings of alternative investments and request other detailed information from the asset managers for each holding. While the above work is similar to the previous fiscal year’s audit plan, we will increase our internal control testing and reduce our substantive testing in 2008.

We will also evaluate the University’s internal controls, processes, and procedures for any commitments that the University has made during fiscal year 2008 to increase their holdings of alternative investments.

Enterprise Financial and Grants Management Systems Replacement Project (EFGMS) – We will audit the activity of the University’s EFGMS Replacement and other hardware / software implementation projects focusing particularly on the capitalized costs of these projects, as well as the design and effectiveness of internal controls for any elements of EFGMS or other hardware / software changes that were “go-live” during fiscal 2008. We plan to perform much of the auditing procedures during our interim work in summer 2008.

Fixed Assets as it Relates to Accounts Payable – In the previous year’s financial statement audit we noted property and equipment which were not properly recorded within the fiscal year 2007 financial statements. As part of this year’s audit we will evaluate the design of the controls to assure the proper recognition of property and equipment, and to substantively test for proper recognition.

Cash Reconciliations – During our fiscal year 2007 financial statement audit we noted a lack of support in the reconciling items within the operating accounts reconciliation. We will substantially test the bank reconciliation to assure the proper support is provided for the items within the reconciliations.
Bonds and Notes Payable – The University has significant amounts of general obligation bonds payable for which we will mail letters of confirmation. We will also evaluate and test the University’s process for monitoring compliance with covenants, if any, and the amount of arbitrage rebate liability recorded.

Other Post-Employment Benefits – The GASB issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which applies to state and local government employers that provide postemployment benefits other than pensions (OPEB) to employees. The statement provides guidance on the accounting and reporting by employers for the costs and obligations of postemployment healthcare and other non-pension benefits provided to employees as part of their compensation for services. In addition, for the OPEB plans in which the employer participates, the statement requires certain disclosures, including disclosures regarding the employer’s funding policy and the actuarial process and assumptions. GASB Statement No. 45 is effective for the University’s fiscal year ending June 30, 2008.

Pension Disclosures – The GASB issued Statement No. 50, *Pension Disclosures-an amendment of GASB Statements No. 25 and No. 27*. This Statement more closely aligns the financial reporting requirements for pensions with those for other postemployment benefits (OPEB) and, in doing so, enhances information disclosed in notes to financial statements or presented as required supplementary information (RSI) by pension plans and by employers that provide pension benefits. The reporting changes required by this Statement amend applicable note disclosure and RSI requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* to conform with requirements of Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The provisions of the new standard are effective for the University’s fiscal year ending June 30, 2008.

Estimates – Auditing standards require us to rotate procedures for testing of significant estimates. In the current year, we plan to perform a test on accounts payable to ascertain recognition of expense in the proper fiscal year. We will perform a test on the allowance for uncollectible receivables to ascertain whether receivable are recorded at net realizable value.

Financial Reporting – The new auditing standards require us to attain an understanding of the internal controls and test such controls in regards to the financial reporting process, including the by-campus reporting.

Given the implementation of SAS No. 112 in the previous year, we will perform auditing procedures to ascertain that the financial statements drafted by University management contain all significant disclosures and that the disclosures are accurate. We will also audit the disclosure checklist to assure that all required disclosures are included in the consolidated financial statements.

RUMINCO Ltd. – The audit of RUMINCO will be subcontracted to Barry Hanson, an independent chartered accountant in Bermuda. Our Minneapolis audit team will assist Barry Hanson by auditing a sample of insurance claims processed by third-party claims administrators in Minnesota. We will also review the work performed by the Bermuda audit firm.
III. SIGNIFICANT AUDIT AREAS

Internal Controls – In addition to the areas noted in previous sections, we will test internal controls for a sample of the following types of transactions:

- Expenses / cash disbursements based on transactions recorded in CUFS
- Payroll based on transactions recorded in Peoplesoft and interfaced to CUFS
- Cash receipts based on transactions recorded in CUFS
- Student Financial Aid based on transactions recorded in Peoplesoft and interfaced to CUFS
- Sponsored Research based on transactions recorded in JD Edwards and interfaced to CUFS

Our procedures for internal controls will include testing whether selected transactions were recorded in a manner consistent with the following significant assertions of the University’s management:

- Transactions were recorded consistently with the University’s chart of accounts
- Transactions were supported by appropriate documentation
- Transactions were recorded in the appropriate fiscal year
- Transactions were in accordance with University policies
- Transactions were recorded within the appropriate campus
III. SIGNIFICANT AUDIT AREAS

Information Systems Audit Procedures – The University has a complex and robust information processing environment. As a result, the automated procedures for processing information are an important aspect of the University’s internal controls. We therefore involve information systems specialists to test automated controls.

We identified the following key information systems during our previous audits of the University:

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<thead>
<tr>
<th>Category</th>
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<td>Financial</td>
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<td>EGMS / EGMSi</td>
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<td>Document Management</td>
<td>DocuWare Document Imaging</td>
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LarsonAllen’s information systems auditors will update our risk assessment of the University’s information technology environment and continue a rotational plan commenced with our audit of fiscal year 2006 to audit key information systems.

Component Units – The inclusion of the financial statements of several discretely-presented component units makes coordination with their respective auditors imperative to assure that their respective audits of the components units are completed by the deadlines established for issuance of the University’s consolidated financial statements. We will also request independence representations from the auditors of the component units, as required by generally accepted auditing standards.

Other Items of Interest – During our audit, other items of interest will include resolution of previous year’s management letter comments.
The following is a description of the general approach that we follow for all audits.

**Audit Philosophy**
We perform efficient, effective audits and we use the audit to gain a better understanding of our client's organization. We believe that auditing should be viewed as a contributing factor to better business and administrative practices. Recommendations or suggestions for improvement in systems and procedures, and comments on business problems will be offered to you.

To the extent possible, we will involve your personnel as a means of controlling efficiency and as a basis for broadening the usefulness of information produced. With this involvement, recommendations are more comprehensive, better understood, and more frequently implemented. This approach makes your audit a worthwhile and positive experience.

**Risk Focus**

**Audit Approach**
Our firm follows a risk based approach similar to the COSO framework in which we build our audit test plan. We build our test plan by identifying the risks concerning the University and the material accounts and transactions inherent in the year end financial statements as well as compliance with federal and state regulations.

**Planning**
Planning for the audit will include three distinct objectives including understanding the processes, assessing risk and development of materiality. Through meeting the three objectives we will build a comprehensive audit plan which should reduce the risk of misstatement in the financial statements to a level of low.

**Understanding of Processes**
One of the planning objectives in building our audit plan is to understand any changes made to the University of Minnesota’s policies and procedures. The ultimate goal is to reach a conclusion on the critical processes in meeting compliance requirements and building the financial statements to be audited. LarsonAllen will perform inquiries of the associated University of Minnesota personnel; obtain policies and internal control documentation to map processes of areas critical to providing auditable financial statements and meeting the federal and state regulations necessary to give an opinion on compliance; and test the internal controls relative to areas with perceived high risk of material misstatement of the financial statements.

Under our approach, significant internal control cycles include cash and investments, revenues, general ledger journal entries, payroll, accounts payable, single audit, and purchasing.
IV. THE LARSON ALLEN APPROACH

Risks Assessment and Materiality
During the planning stages and throughout the audit, we also identify the external and internal pressures and risks influencing the University’s day to day operations and future goals.

We utilize a multi-faceted approach to identify significant audit risk areas. Some of the inputs to our risk identification process include:

♦ Principal-led fraud risk discussion with the audit team, as required by Statement on Auditing Standards No. 99
♦ Meetings with management
♦ Meetings with the Audit Committee
♦ Reading minutes of meetings
♦ Use of our specialized college and university audit professionals
♦ Industry-specific training provided by both in-house specialists and outside professional organizations
♦ Communications from the Minnesota Office of Higher Education, Offices of Inspectors General or other oversight agencies
♦ Level of University management controls – whether these controls are centralized in the Twin Cities or decentralized and performed at Crookston, Morris, and Duluth

Another objective of planning is to establish materiality, generally calculated as a percentage of assets or revenues. The goal of establishing materiality is to assign a qualitative and quantitative boundary for the transactions and accounts in producing the audited financial statements, taken as a whole. We also establish qualitative and quantitative boundaries for compliance issues during the planning stages.

The concept of materiality focuses our attention on areas that are significant to the financial statements. In this manner we utilize a “top-down” risk assessment that provides us with the basis for determining the most effective audit-testing plan. In our assessment, we consider quantitative materiality factors such as:

♦ Materiality of individual operations
♦ Degree of risk of loss or error – e.g., complex transactions

We also consider qualitative materiality factors such as:

♦ Inherent complexities of operations
♦ Inherent risks related to control risks associated with account balances and transactions
♦ Status of changes in financial systems
♦ Nature and degree of centralization of key functions
♦ Industry, economic, political and regulatory environment
♦ Public scrutiny and effect on operations
♦ Needs and concerns of management
IV. THE LARSON ALLEN APPROACH

Re-evaluation of our understanding of the processes, the risk assessment and materiality will be ongoing during the audit.

Testing Internal Controls
The scope of our tests of controls is driven by our combined assessment of inherent risk and control risk, which we determine during the planning phase.

We challenge the combined risk assessment for each significant financial statement assertion related to each significant account balance, which was identified based on the concept of materiality.

This combined risk assessment then is used to balance our testing of internal controls (control risk) with the nature, timing, and extent of substantive audit procedures (detection risk).

Generally, testing internal controls, provided they are effectively designed, is the most effective and efficient audit strategy.

Our utilization of sampling in auditing generally centers on compliance and controls testing, rather than substantive testing of account balances. We use a series of quality control materials in all our audit engagements. These forms guide our staff through a logical process of assessing inherent risk, control risk, and combined audit risk, followed by an assessment of appropriate sample size for testing areas.

We are usually able to obtain assurance on multiple levels when sampling transactions for testing compliance. For example we may also incorporate elements for testing of internal controls and substantive testing into our compliance testing. In this manner we obtain “dual-purpose” or “triple-purpose” testing for internal controls, compliance, and substantive assurance with one sample, resulting in a very efficient transaction testing phase.

Substantive Testing
While reliance upon testing of effectively designed controls reduces the amount of substantive testing that is required, it does not eliminate the need for substantive testing. Therefore, substantive testing will be performed on account balances. Again, the results of our tests of controls influences the nature, timing, and extent of substantive audit procedures, which may include the “dual-” or “triple-purpose” tests as described above, other detailed sampling of account balances or classes of transactions particularly related to balance sheet accounts, or predictive analytical tests related particularly to revenues and expenses.
IV. THE LARSON ALLEN APPROACH

Substantive Testing (continued)
With audit risks identified, our control emphasis reduces duplicative verification efforts and the associated time and cost. Based on our understanding of management and the internal control structure, we evaluate the effectiveness and then use that evaluation in our substantive testing of operating results in place of item-by-item verification. Conversely, when controls in a particular area are found insufficient, we direct our substantive audit testing to that area and recommend to management appropriate countermeasures either during the audit or as part of our management letter at the end of the audit, depending on the circumstances.

Analytical Review
In accordance with generally accepted auditing standards (SAS No. 56, Analytical Procedures), analytical review will be utilized in the planning process to identify significant account balances for audit fieldwork and during the final review stage of the audit. Specific procedures would include comparison of actual results to prior years and to adopted budget (as amended), including known fluctuation in funding levels, contributions, student enrollment, rates for tuition, fees, etc. and a reasonableness test for return on investments. Other substantive procedures may be supplemented by analytical procedures, depending on our audit risk assessment process.

Information Technology Audit Strategy
The scope of our information technology audit is “driven” by the financial reporting process, whereby we focus on the information systems that are critical to the financial reporting process.

We will update our understanding of key financial controls and business processes within each financial reporting cycle (revenues, expenditures, payroll, etc.), identifying any changes to the key business applications that support those key controls and processes.

Once we have updated our understanding of key controls, business applications, and critical infrastructure, we will request information and meet with the appropriate individuals and proceed with testing the following areas:

♦ Control environment
♦ Information systems general controls, including:
  ▪ Organization and management controls
  ▪ System security administration
  ▪ Access controls
  ▪ Network security
  ▪ Operations controls
  ▪ Physical security
  ▪ Data center environment controls
  ▪ Backup and recovery
♦ System development controls (system development life cycle)
♦ Separation of duties (development, operations, change management)
♦ Change management
IV. THE LARSONALLEN APPROACH

Information Technology Audit Strategy (continued)

- Application controls, including:
  - Input controls (data validation)
  - Processing controls
  - Output controls
  - Interfaces
  - Security features (user account profile management)

Test procedures for each control domain will include the following as applicable:

- Inquiry / observation
- Inspection of key documents
- Review / observation of information system configuration settings

Information Technology Audit Focus

We will focus on understanding the overall technical environment within the University of Minnesota for “mission critical” application software systems that are categorized as follows:

- IBM Main frame
- Implemented PeopleSoft modules
- Centralized servers (Within Central IT)
- Decentralized servers
- Web-based applications

Certain portions of the IBM mainframe systems documentation may involve the use of a subcontractor.

Our Information Technology audit procedures will also enhance single audit testing under OMB Circular A-133 since the processing of federal grant transactions is performed on many of the same systems as the University of Minnesota’s general financial accounting.

Reliance on Other Auditors

We are aware of other auditors being involved for the audits of several discretely presented component units which are included in the University’s financial report, and we will refer to the other auditors’ opinions within our opinion on the consolidated financial statements of the University. We will require that the other auditors sign a representation letter as required by professional standards. If we believe the other auditors have performed substandard work, we reserve the right to modify our opinion for such.
IV. THE LARSONALLEN APPROACH

Communications to the Audit Committee, Board of Regents and University Management

During the Audit
During the audit process we will participate in weekly meetings, including audit in-charges of LarsonAllen and the University of Minnesota and/or other entities to assure all parties are aware of how the audit process is going.

Fraud-Risk Discussions
The engagement principals and managers will engage in discussions with management, the Audit Committee, and members of the Board of Regents to obtain an understanding of potential risks of fraud within University of Minnesota and its several entities. These discussions are required by Statement on Auditing Standards No. 99, Consideration of Fraud in a Financial Statement Audit, issued by the American Institute of Certified Public Accountants, and will be held during the planning phase of our audit.

Communication of Internal Control Related Matters
Statement on Auditing Standards (SAS) No. 112, Communicating Internal Control Related Matters Identified in an Audit, applies in all audits for years ending after December 15, 2006, and requires the auditor to communicate significant deficiencies in internal control to the audit committee or to individuals with a level of authority and responsibility equivalent to an audit committee in organizations that do not have one, (e.g. the legislative body). For purposes of SAS No. 112, the following definitions apply:

Deficiency 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 misstatements on a timely basis. Deficiencies, as defined, are the least severe in nature, and may therefore be communicated verbally to management.

Significant Deficiency A single control deficiency, or a combination of control deficiencies, that adversely affects the entity’s ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of an entity’s financial statements that is more than inconsequential will not be prevented and detected. Significant deficiencies are required to be communicated in writing to management and to the Board of Regents.

Material Weakness A significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected. Material weaknesses, as defined, are the most severe in nature and, like significant deficiencies, must be communicated in writing to management and to the Board of Regents.

The auditor is required by SAS No. 112 and Government Auditing Standards (the Yellow Book) to separately identify and communicate in writing any significant deficiencies and material weaknesses. We will discuss, immediately upon discovery, any instances of material accounting or internal control weaknesses or suspected fraud, defalcations, collusion or manipulation, and request instructions as to how to proceed with the audits.
IV. THE LARSONALLEN APPROACH

Communication of Internal Control Related Matters (continued)

Management Letter At the conclusion of our audit, we can, at your option, communicate our recommendations and suggestions for strengthening your accounting procedures, internal controls and possible business improvements by way of a Management letter. One of the reasons our clients retain LarsonAllen as their auditor, we believe, is because of the ideas and recommendations we can offer to improve the organization’s operating effectiveness and efficiency, giving our clients the opportunity to utilize best practices in operating your organization. Communication of other comments to management is optional under SAS No. 112.

Required Audit Communication (SAS 114)
We will inform the University Board (and/or Audit Committee) of each of the following:

♦ The auditor's responsibility under generally accepted auditing standards and OMB Circular A-133.
♦ Significant accounting policies.
♦ Management judgments and accounting estimates.
♦ Significant audit adjustments and waived adjustments, if any.
♦ Our responsibility for reading other unaudited information in documents such as bond offerings, etc., which contain audited financial statements.
♦ Disagreements with management, if any.
♦ Management consultation with other accountants.
♦ Major issues discussed with management prior to retention.
♦ Difficulties encountered in performing the audit, if any.

Irregularities and Illegal Acts
We understand that we are required to make an immediate, written report on all irregularities and illegal acts or indications of illegal acts of which we become aware. It is our firm’s policy to report alleged irregularities or illegal acts to the level of management having immediate oversight of the department or employee(s) suspected of committing the act. Professional standards also require us to report such matters directly to the University Board, depending upon the materiality of an identified act.

Non Audit Period
After the audit is completed and until the subsequent year’s audit has commenced, we will be active in attending the audit committee meetings as requested by the audit committee. Our lead engagement principals will also meet with the Audit Committee Chairperson on a quarterly basis to assure the optimal client service and audit product quality.

We will also meet with management of the University of Minnesota to assure the optimal client service and audit product quality. We find that the meetings with representatives of the Board of Regents and management allows the client representatives a chance to ask questions of current and possible future transactions and activities that might affect the audited financial statements. We also believe the discussions allow us as auditors to provide Board of Regents and management allows the client representatives a chance to ask
IV. THE LARSONALLEN APPROACH

Non Audit Period (continued)
questions of current and possible future transactions and activities that might affect the audited financial statements. We also believe the discussions allow us as auditors to provide insights to management and the Board of Regents, allowing us to compile inherent risks that might not be transparent if the meetings and discussions were not held.
V. FACTORS AFFECTING FUTURE AUDITS

New Campus – We will continue monitoring the position of the Minnesota Office of Higher Education regarding their interpretation of whether the Rochester, Minnesota, learning center will be viewed as a separate campus of the University. Based on discussion with the University’s financial aid management team and with the Minnesota Office of Higher Education in the spring of 2008, the Rochester learning center is not viewed as a separate campus for the fiscal year ending June 30, 2008. However, this interpretation may change in future years and therefore may require us to perform on-site auditing for purposes of complying with OHE’s requirements for state-funded student financial assistance programs. We may also need to do additional on-site testing for the federal student awards for the OMB Circular A-133 compliance audit.

New Accounting Standards
The GASB issued Statement No. 49, Accounting and Financial Reporting for Pollution Remediation Obligations. The statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations. The statement excludes pollution prevention or control obligations with respect to current operations, and future pollution remediation activities that are required upon retirement of an asset. The statement provides that, once any of the defined obligating events has occurred, the University would be required to estimate the expected pollution remediation outlays and determine whether such outlays should be accrued as a liability or, if appropriate, capitalized when goods and services are acquired. As proposed, the provisions of the new standard would be effective for the University’s fiscal year ending June 30, 2009.

The GASB issued Statement No. 51, Accounting and Financial Reporting for Intangible Assets. This Statement requires that all intangible assets, including easements, water rights, timber rights, patents, trademarks, and computer software, be classified as capital assets. Accordingly, existing authoritative guidance related to the accounting and financial reporting for capital assets should be applied to these intangible assets, as applicable. This Statement also establishes guidance specific to intangible assets related to amortization and provides guidance on determining the useful life of intangible assets when the length of their life is limited by contractual or legal provisions. If there are no factors that limit the useful life of an intangible asset, the Statement provides that the intangible asset be considered to have an indefinite useful life. Intangible assets with indefinite useful lives should not be amortized unless their useful life is subsequently determined to no longer be indefinite due to a change in circumstances. The requirements of this Statement will be effective for the University’s fiscal year ending June 30, 2010. The provisions of this Statement generally are required to be applied retroactively back to and including the University’s fiscal year ended June 30, 1981.
The GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*. This Statement establishes consistent standards for the reporting of land and other real estate held as investments by essentially similar entities. It requires endowments to report their land and other real estate investments at fair value. This statement also requires that changes in fair value of such investments be reported as investment income. This statement also requires the disclosure of the methods and significant assumptions used to determine fair value, and other information that they currently present for other investments reported at fair value.

In 2007, the GASB issued a draft of a pending new accounting standard, *Accounting and Financial Reporting for Derivative Instruments*. A key provision in this proposed Statement and a major change from current practice is that most derivative instruments covered in the scope of this proposed Statement would be reported at fair value in the University's statement of net assets. Derivative instruments associated with a hedgeable item that are effective in reducing a exposure to an identified financial risk would be considered hedging derivative instruments. Effectiveness would be determined by considering whether the changes in cash flows or fair values of the potential hedging derivative instrument substantially offset the changes in cash flows or fair values of the hedgeable item. In these instances, the changes in fair values of the hedging derivative instrument would be recognized as either deferred inflows or deferred outflows in the University's statement of net assets. Much of this proposed Statement describes and illustrates the methods of evaluating effectiveness. The disclosures of GASB Technical Bulletin No. 2003-1, *Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets*, have been incorporated into this proposal for hedging derivative instruments. Disclosures for investment derivative instruments would be modified to be more consistent with the disclosures of other investments. The Board also proposes including a summary of derivative instrument activity during the period as a note disclosure. The requirements of this proposed Statement would be effective for financial statements for the University’s fiscal year ending June 30, 2010.

The issuance by the AICPA of Auditing Standards No. 104 to 111, and 114, (previously discussed in this document) are illustrative of the convergence of private industry auditing standards with several of the auditing standards issued by the Public Company Accounting and Oversight Board, which oversees SEC registrants. Several accounting and auditing standard-setting bodies are discussing future changes that may lead to a further convergence of international, domestic, SEC and private industry accounting and auditing principles.
Audit Committee

May 7, 2008

Agenda Item: Internal Audit Update

☐ review  ☐ review/action  ☐ action  ☑ discussion

Presenters: Associate Vice President Gail Klatt

Purpose:

☐ policy  ☐ background/context  ☑ oversight  ☐ strategic positioning

To update the Audit Committee on Internal Audit activities, results, and observations. The report also includes the status of outstanding “essential” recommendations.

Outline of Key Points/Policy Issues:

• This past quarter, 22% of the outstanding recommendations rated as “essential” were implemented by University departments. This percentage is lower than the previous quarter, and is less than our expected rate of 40%. An updated control evaluation chart is included for each audit to show progress made on the “essential” items. Four units fully implemented all their remaining “essential” recommendations.

• Six audit reports containing 21 recommendations rated as “essential” were issued in the last three months.

Background Information:

This report is prepared on a quarterly basis and is presented to the Audit Committee in conformance with Board Operations and Agenda Guidelines.
This report includes:
- Audit Observations/Information/Status of Critical Measures
- Status of “Essential” Recommendations & Bar Charts Showing Progress Made
- Audit Activity Report
- Audit Reports Issued Since February 1, 2008

Details for any of the items in this report are available on request. Individual reports were sent to the President, Provost, Vice Presidents, and Chancellors about these internal audit issues.

**Audit Observations/Information**

**Status of Critical Measures**

As part of our on-going efforts to provide the Audit Committee with critical information in as concise a format as possible, we have developed the following three charts to present a “snapshot” status report on work performed by the Office of Internal Audit.

The first chart, “Essential Recommendation Implementation”, provides our overall assessment of the success University departments had during the last quarter in implementing our essential recommendations. Readings in the yellow or red indicate implementation percentages less than, or significantly less than, our expected University-wide rate of 40%. Detailed information on this topic, both institution-wide and for each individual unit, is contained in the next section of this Update Report.

The second chart, entitled “Progress Towards Annual Audit Plan Completion”, is our assessment of how we are progressing towards completion of the FY 2008 Annual Audit Plan. Readings less than green could be influenced by a variety of factors (i.e. insufficient staff resources; increased time spent on non-scheduled audits or investigations).

The final chart, “Time Spent on Investigative Activities”, provides a status report on the amount of time consumed by investigative activities. Our annual plan provided an estimated budget for this type of work, and the chart will indicate if we expect that budget to be sufficient. Continued readings in the yellow or red may result in seeking Audit Committee approval for modifying the Annual Audit Plan.
Work to be Performed for the Office of the Legislative Auditor

We have been asked by the Office of the Legislative Auditor to assist them with a state-wide review they are performing on the use of general obligation bond funding authorized by the 2006 legislative session. They have identified four University projects to be included in this review, and we have agreed to perform the controls assessment and testing required for those projects. Our results will be reported to them for inclusion in their overall report. This work will be included in our planned audit of the University Plant Fund.
Status of "Essential" Recommendations as of April 25, 2008

<table>
<thead>
<tr>
<th>Report Date</th>
<th>Audit</th>
<th># of Essential Recommendations in the Report</th>
<th># of Essential Recommendations Remaining From Prior Quarter</th>
<th>Current Quarter Results</th>
<th>Overall Progress Towards Implementation</th>
<th>Any Individual Issues With &lt; Satisfactory Progress?</th>
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<tbody>
<tr>
<td>Aug-04</td>
<td>UMD Health Service</td>
<td>10</td>
<td>3</td>
<td>3</td>
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<tr>
<td>Jan-05</td>
<td>A Review of Education Abroad Programs</td>
<td>4</td>
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<td>1</td>
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<td>Jan-05</td>
<td>University of Minnesota - Crookston</td>
<td>11</td>
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<td>1</td>
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<td>Apr-05</td>
<td>Carlson School of Management</td>
<td>4</td>
<td>2</td>
<td>2</td>
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<td>May-05</td>
<td>UMD School of Fine Arts</td>
<td>10</td>
<td>2</td>
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<td></td>
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<tr>
<td>Jul-05</td>
<td>Intercollegiate Athletics</td>
<td>12</td>
<td>2</td>
<td>2</td>
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<td></td>
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<td>Sep-05</td>
<td>Facilities Management Maintenance Operations</td>
<td>10</td>
<td>2</td>
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<td>Dec-05</td>
<td>Disaster Recovery</td>
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<td>Jul-06</td>
<td>Medical School Duluth</td>
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<td>eResearch Systems</td>
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<td>Capital Planning &amp; Project Management</td>
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<td>Law School</td>
<td>5</td>
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<td>Nov-06</td>
<td>OVPR-Central Units Supporting Research</td>
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<td>3</td>
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<td>Jan-07</td>
<td>UMD-College of Liberal Arts</td>
<td>9</td>
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<td>1</td>
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<td>Jan-07</td>
<td>University Libraries</td>
<td>5</td>
<td>2</td>
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<td>Jan-07</td>
<td>Department of Neurology</td>
<td>5</td>
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<tr>
<td>Apr-07</td>
<td>University Stores</td>
<td>3</td>
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<td>2</td>
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<td>May-07</td>
<td>Ticketing System - Phase 1 Review</td>
<td>4</td>
<td>3</td>
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<td>May-07</td>
<td>Central Authentication Services</td>
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<td>Jun-07</td>
<td>Epidemiology &amp; Community Health</td>
<td>11</td>
<td>7</td>
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<td>Jun-07</td>
<td>School of Physics &amp; Astronomy</td>
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<td>4</td>
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<td>Jun-07</td>
<td>stem Cell Institute</td>
<td>4</td>
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<td>1</td>
<td>Completed</td>
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<td>Department of Psychology</td>
<td>10</td>
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<td>3</td>
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<td>Aug-07</td>
<td>General Clinical Research Center</td>
<td>12</td>
<td>10</td>
<td>4</td>
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<td></td>
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<tr>
<td>Aug-07</td>
<td>UM - Morris Campus</td>
<td>2</td>
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<td>Sep-07</td>
<td>University Press</td>
<td>8</td>
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<td>Oct-07</td>
<td>UMD Intercollegiate Athletics</td>
<td>9</td>
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<td>Oct-07</td>
<td>Department of Recreational Sports</td>
<td>6</td>
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<td>Oct-07</td>
<td>Veterinary Medical Center</td>
<td>4</td>
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<td>Nov-07</td>
<td>Department of Central Security</td>
<td>8</td>
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<td>Dec-07</td>
<td>Central Computing Operations System Administration</td>
<td>1</td>
<td>1</td>
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<td>Jan-08</td>
<td>Department of Computer Science and Engineering</td>
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<td>Jan-08</td>
<td>University of Minnesota Cancer Center</td>
<td>4</td>
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<td>1</td>
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<td>Jan-08</td>
<td>Office of the Vice President for Equity and Diversity</td>
<td>9</td>
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<td>4</td>
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<td>Jan-08</td>
<td>Weisman Art Museum</td>
<td>8</td>
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<td>Jan-08</td>
<td>Active Directory Administration Managed by OIT</td>
<td>9</td>
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<td>Jan-08</td>
<td>College of Biological Sciences</td>
<td>9</td>
<td>9</td>
<td>2</td>
<td>Satisfactory</td>
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<td>Jan-08</td>
<td>Natural Resources Research Institute</td>
<td>7</td>
<td>7</td>
<td>1</td>
<td>Satisfactory</td>
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Total: 255 157 35 90 32

(a) Lack of computer programming resources has slowed progress on this issue. Expected system implementation will now be by Fall 2008.

* The following bar charts provide details on progress made towards implementation

**"Essential" Recommendation Implementation Trends**

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<tr>
<td># of Essential Recommendations Receiving Follow-up</td>
<td>157</td>
<td>102</td>
<td>86</td>
<td>96</td>
<td>91</td>
<td>114</td>
<td>108</td>
<td>112</td>
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<tr>
<td># of Recommendations Considered Fully Implemented</td>
<td>35</td>
<td>31</td>
<td>32</td>
<td>29</td>
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<td>46</td>
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<td>Implementation Percentage</td>
<td>22%</td>
<td>30%</td>
<td>37%</td>
<td>30%</td>
<td>53%</td>
<td>40%</td>
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<td>Audit/Report Date</td>
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<td>A Review of Education</td>
<td>P</td>
<td>E. Thomas Sullivan, Meredith</td>
<td>The University should roll-out to all colleges and departments a uniform process for the assessment</td>
<td>Management reports they are now on the following timeline:</td>
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<td>Abroad Programs</td>
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<td>McQuaid</td>
<td>of program costs associated with study abroad programs. This process should ensure all study abroad</td>
<td>Technical design documentation is currently in progress. Development will be in place in the DEV and/or testing</td>
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<td>Jan-05</td>
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<td>program charges are billed to the student’s University financial account.</td>
<td>environments in the near future. Testing by university departments identified as users of this module will be done over</td>
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<td>summer in the appropriate testing environments in preparation for a move to Production for Fall 2008 posting and billing</td>
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<td>processes.</td>
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<td>University of Minnesota -</td>
<td>P</td>
<td>Charles Casey, Robert Jones</td>
<td>For standard keys issued UMC needs to implement a process to ensure keys are returned as students or</td>
<td>The UMC Vice Chancellor indicates that a new facilities director has now been hired. They hope to complete the key</td>
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<td>Crookston</td>
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<td>staff leave campus. The return of keys should be a requirement before issuing final paychecks,</td>
<td>process in the next quarter.</td>
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<td>Jan-05</td>
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<td>transcripts etc. Also the use of an appropriate key deposit can facilitate their return.</td>
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<td>Enterprise Imaging System</td>
<td>P</td>
<td>Amie Dardis, Dan Wagner</td>
<td>Management and OIT Data Security should continue to work with the vendor to address security</td>
<td>During the testing of the Login Monitoring Process the Imaging team and Data Security found that it could have a significant impact on ImageNow system performance. It was decided further testing was necessary to minimize any performance issues. Due to the EFS project and staff availability, it was decided to not address this until after the EFS implementation in July. OIT is actively investigating the use of M Key for user access to ImageNow. Our Unix group has tested system configuration changes needed for going forward with M Key in our development and test environments, and planning is underway to make these changes in the production system.</td>
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<td>Apr-05</td>
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<td>concerns identified. User authentication and intrusion monitoring processes should be</td>
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<td>enhanced to address security concerns noted in this review.</td>
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<td>OIT Data Security should continue to work with the vendor about the problem with deleted IDs in the</td>
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<td>application. The application should be modified to allow userIDs to be deleted without</td>
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<td>affecting audit trails. The application should also be modified so application users do not have to</td>
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<td>have accounts established within the operating system.</td>
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<td>As management works with the vendor to correct these problems, management should continue its</td>
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<td>efforts to get upgrades in a more timely manner.</td>
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<td>UMD School of Fine Arts Jun-05</td>
<td>P</td>
<td>Jack Bowman</td>
<td>SFA administration needs to establish an environment in which ethical behavior and compliance with policy and procedure are emphasized. This emphasis should be communicated to employees in writing; it should be reinforced through the provision of adequate training to ensure employees fully understand policies and procedures; and it should be exemplified through management's actions.</td>
<td>The dean has been working with the director of UMD Human Resources and a consultant from UMTC in an effort to improve the work environment within SFA. These efforts are on-going.</td>
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<td>P</td>
<td>Vince Magnuson</td>
<td>SFA administration should utilize the knowledge, skills, and talents of faculty and staff to help identify SFA priorities and to formulate effective methods for accomplishing those priorities. The department should work with Human Resources to develop a system for promoting employee involvement and input. This could include the use of periodic surveys, suggestion boxes, or open discussions.</td>
<td>The dean has been working with the director of UMD Human Resources and a consultant from UMTC in an effort to improve the work environment within SFA. These efforts are on-going.</td>
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<td>Intercolligate Athletics Aug-05</td>
<td>P</td>
<td>Joel Maturi</td>
<td>The Athletic Ticket Office should ensure that employees are adequately trained in Paciolan and cross trained in areas that affect their current duties, and potentially back-up duties.</td>
<td>Athletics continues to make progress in the cross-training of the ticket office staff in regards to AudienceView. The progress is slow to date as we have yet to make it through a full year with the new system. AudienceView staff is currently implementing the entire &quot;renewal process&quot; for all sports for the first time through. The OIT AudienceView staff is fully operational and they should be able to help us improve our cross-training. They are also in the process of hiring a new ticket manager, who will have no experience with this system. It is a work in progress, but we are expecting to be about 70% up to speed by September 1, 2008.</td>
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<td>30</td>
<td>P</td>
<td>Joel Maturi</td>
<td>Athletics should implement the following:</td>
<td>In the past three months, Athletics has migrated all general file sharing services to Active Directory, which will allow us to leverage OIT's vetted disaster recovery and business continuity preparations.</td>
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<td>• Develop a formal system administrator procedure manual,</td>
<td>Additionally, we are currently in the process of transitioning our internal web server to an OIT-hosted server, which will similarly allow us to leverage their disaster recovery and business continuity preparations.</td>
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<td>• Define and post emergency shut down procedures in the data center,</td>
<td>Remaining services include our photo archive, and a database/application server running proprietary software for a disparate, small user base (&lt;10 people). Currently, the disaster recovery plan for these services has</td>
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<td>• Establish a formal disaster recovery and business continuity plan,</td>
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<td>• Identify critical recovery times and back-up locations for servers, with documented agreements for space use,</td>
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<td>• Maintain an up-to-date off-site list of equipment, applications, data files, and procedures needed to recover the network,</td>
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<td>• Contract for the securing of equipment via quick purchase or a recovery insurance policy, and</td>
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<td>• Test recovery procedures on a periodic basis.</td>
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<td>not been completed or tested.  Our goal is to have as many of these services physically hosted and backed up by OIT by the end of August 2008.</td>
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<td>Facilities Management Maintenance Operations Sep-05</td>
<td>P</td>
<td>Mike Berthelsen</td>
<td>FM should develop a procedures manual to ensure that necessary activities are conducted for payroll and are processed timely and accurately by more than one payroll staff. There also should be cross-training in the FM payroll unit.</td>
<td>The FM Finance Director indicates that some progress has been made. An assistant director has been hired with oversight and backup responsibilities for payroll. Some cross training has started. The key payroll contact continues to be heavily involved with the EFS project, and the documenting of processes is not yet completed.</td>
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<td>CCO Disaster Recovery Dec-05</td>
<td>P</td>
<td>Steve Cawley</td>
<td>OIT should continue its efforts in implementing/updating disaster recovery plans for all of the key central administration systems. Management should assure OIT plans will address all key central administration systems including applications CCO does not support and/or has recently been assigned support responsibilities. Steps should be taken to assure a disaster recovery plan is in place that can address both minor and major events (i.e., the corruption of data files and the loss of the data center where servers reside). The disaster recovery plans should include: •Expectations in the event of a disaster, •Roles and responsibilities, •Resources needed to recover the system including reports to validate a successful recovery, •Procedures for activation of the plan and escalation processes, •Priorities for system restoration, •Contact information of implementation team members, •Test plans for ensuring the system is functioning as intended and the integrity of data was not compromised, and •Time interval for regular testing of the disaster recovery plan. In addition, management should ensure that the disaster recovery team is trained in their responsibilities in the event of an emergency or disaster and are aware of manual or alternate processing procedures that are to be used when processing is delayed for an extended period of time.</td>
<td>Progress has been made in creating a disaster recovery plan process and is being tested by the Active Directory support team. Upon completion of plan revisions from the pilot, a plan for AudienceView (the University ticketing system) will be done. A timeline will also be prepared for completing plans for all OIT supported systems.</td>
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# of Items: 2

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Total: 9
The bar charts shown below are presented to provide pictorial displays of the progress units are making on implementing audit recommendations rated as "essential". The bar chart included in the original report is shown in the left column, along with updated bar charts showing the previous quarter and the current status of the "essential" recommendations only (those bars that have red segments). The chart in the center column displays the status as of February 2008, while the chart on the right represents the current status. Charts are not presented for investigations. Charts for those units having implemented all "essential" recommendations during the current quarter are shown at the end of this report.
eResearch Systems (September 2006)

Law School (November 2006)

Adequate Control  Significant Control Level  Critical Control Level  Potential Over-Control
University Libraries (January 2007)

Department of Neurology (January 2007)
UMD Intercollegiate Athletics (October 2007)

Department of Recreational Sports (October 2007)
Weisman Art Museum (January 2008)

Active Directory Administration Managed By OIT (January 2008)
Units with Charts that Fully Implemented their "Essential" Recommendations During the Past Quarter

Original Report Evaluation

Previous Quarter Evaluation

Current Quarter Evaluation

UMD Health Service (August 2004)

Carlson School of Management (May 2005)
Audit Activity Report

Scheduled Audits

- Completed audits of: M Key two-factor authentication, University of Minnesota Bookstores, Capital Planning & Project Management Unifier Project Management System, UMD Swenson College of Science & Engineering, an EFS Pre-Implementation Review, and Athletic Facilities. Details are shown on the following charts.

- Began/continued audits of: the College of Food, Agricultural, and Natural Resource Sciences, Molecular and Cellular Therapeutics, the College of Education and Human Development, UMD Kirby Student Center, UMD Police, the Department of Obstetrics and Gynecology, the Department of Mechanical Engineering, UMD Housing & Residence Life, a University-wide purchasing review, the University Plant Fund, and a review of the AudienceView ticketing system for Athletics.

Non-Scheduled Audits

- Continued an audit of the Minnesota Population Center. This audit was requested by the Vice President for Research due to a change in reporting structure.

Investigations

- Performed investigative work on 13 issues in accordance with the University Policy on Reporting and Addressing Concerns of Misconduct.

Special Projects

- Provided consulting services related to: HIPAA compliance, data security, the Enterprise Financial System implementation, computer disposal, the new credential system project, and University payroll exception testing.

Other Audit Activities

- Participated in the following:
  - HRMS PeopleSoft Steering Committee
  - Training Advisory Committee
  - Fairview Health Systems Audit Committee
  - University of Minnesota Foundation Audit Committee
  - Enterprise Financial System Executive Steering Committee
  - Research Compliance Committee
  - Executive Administrative Committee
  - Executive Compliance Oversight Committee
  - Subcommittee C of the International Working Group
  - Institutional Conflict of Interest Committee
  - NCAA Self-Study Committee
  - NCAA Committee for Review of Academic Support for Student Athletes
  - Search Committee for Associate Director of Purchasing Services
  - Search Committee for Institutional Compliance Officer
  - Search Committee for Recruitment Manager
  - Search Committee for Director of Research Integrity and Oversight
  - Committee for Defining a Strategy for Research Compliance
Audit Reports Issued Since February 2008

M Key Two-Factor Authentication

Control Environment
Monitoring
Information & Communication
Risk Assessment
System Design & Functionality
System Configuration
Change Control
Disaster Recovery
Systems Interoperability
Strategic Planning

Report # 819  Issue Date Apr-08
# of Essential Recs. 2  Total # of Recs. 4
Overall Assessment Good Adequacy of MAP Satisfactory

This audit reviewed the implementation of the new and more robust user authentication system called "M Key" which requires users to have two-factors (i.e., a pin and a token) to access many of our systems. This authentication method is being rolled to our most sensitive systems first such as PeopleSoft HR/Student and EFS. The M Key implementation is well designed and configured and constitutes a material improvement in information security.

University of Minnesota Bookstores

Control Environment
Monitoring
Information & Communication
Risk Assessment
Information Systems
Revenues
Inventory
Disbursements
Payroll

Report # 820  Issue Date Apr-08
# of Essential Recs. 5  Total # of Recs. 10
Overall Assessment Good Adequacy of MAP Satisfactory

Based on the results of our review, the Bookstores has established an effective system of controls that addresses most of its major risks. In addition, the results of an employee survey indicated that employees share a very positive view of management and support staff.

We did, however, note several issues resulting in "essential" recommendations, where further improvements are warranted to minimize existing operational, compliance and financial risks. Recommendations rated as "essential" were made for several information systems issues, specifically:

• improving system security processes, to ensure servers and workstations are configured in a consistent manner and in compliance with OIT standards;
• strengthening the monitoring of system and application activity logs and implementing a more robust intrusion detection system;
• enhancing program change control procedures used for the Ratex application;
• improving controls over access rights to Bookstore systems; and
• ensuring Bookstore systems are modified to achieve full compliance with PCI standards.
Our audit included an analysis of operational, financial, and compliance risks and related controls in place in the UMD Swenson College of Science and Engineering. While in general the controls in SCSE are working effectively, the main opportunities to further enhance controls were in the areas of information system security, disaster recovery, laboratory safety and hazardous materials, and sponsored projects effort reporting. SCSE management has developed plans to address all the issues in the report.

CPPM - Unifier Project Management System

Capital Planning and Project Management (CPPM), a unit within University Services, is responsible for the planning, design, and construction of capital improvement projects for the University of Minnesota. To assist them in effectively carrying out this mission CPPM has purchased and implemented the Unifier Project Management System.

The most critical issues in the report relate to the risks that are present because CPPM has outsourced the responsibilities for hosting and operating the Unifier application without documenting how the vendor complies with University/OIT information system standards and how they will mitigate the associated risks. CPPM Management has developed plans to work with the Unifier vendor to address these risks and enhance these controls.
### EFS Pre-Implementation Review

This audit reviewed components of the Enterprise Financial System’s implementation and project management in its current pre-rollout status. The EFS project is using a disciplined system development and testing approach that is positioning the University for a successful system cutover. The project team and the Controller’s Office have been working with staff across the organization to identify the ramifications of a conversion process which will occur over multiple weeks and require some financial processing to be temporarily curtailed or delayed. Strategies have been developed to minimize the impact on University operations during the cutover period. The preliminary plans prepared by Accounting Services and the Controller’s Office to address the impact of the cutover appear comprehensive, logical, and robust.

### Athletic Facilities

The Athletic Facilities Department, who reports to the Department of Intercollegiate Athletics, manages the athletic facilities on the University Twin Cities campus. This includes all stadiums, arenas, Baseline Tennis Center, Les Bolstad Golf Course, and the Bierman complex. These facilities are maintained both for use by the University community and, when appropriate, for rental to the general public. Our review showed this to be a generally well managed unit. Three of the four essential recommendations are in the area of compliance with state and federal regulations. Specific recommendations were developed addressing: collecting and remitting the correct amount of sales tax on items sold, reporting Unrelated Business Income Tax, and providing annual safety training required by “Employee Right-To-Know” regulations. Other recommendations were aimed at improving controls or efficiencies in the areas of: payroll, credit card processing, cash receipts, inventory, and disbursements.
Audit Committee  
May 7, 2008

Agenda Item: Information Items

☐ review  ☐ review/action  ☐ action  ☒ discussion

Presenters: Associate Vice President Gail Klatt

Purpose:

☐ policy  ☐ background/context  ☒ oversight  ☐ strategic positioning

To provide the Audit Committee with the Semi-Annual Controller’s Report.

Outline of Key Points/Policy Issues:

Semi-Annual Controller’s Report

This report presents a summary of activities completed by the Controller’s Office in the last six months that enhance financial accounting and reporting, strengthen internal controls, reduce financial or compliance risks to the University, and improve efficiencies and services.

Background Information:

The Controller’s Report is prepared semi-annually and presented to the Regents Audit Committee in conformance with Board of Regents Policy: Board Operations and Agenda Guidelines.
UNIVERSITY OF MINNESOTA
BOARD OF REGENTS AUDIT COMMITTEE

SEMI-ANNUAL CONTROLLER’S REPORT
May 7, 2008

This report presents a summary of activities completed by the Controller’s Office in the last six months that have improved financial reporting, enhanced internal controls, reduced financial risks, improved services to the University community, or created efficiencies in financial operations.

I. Accounting and Financial Reporting Matters

The Controller’s Office is currently planning for the adoption of three new accounting and reporting standards issued by the Governmental Accounting Standards Board (GASB), and eight new Statements on Auditing Standards (SAS’s) that will impact the University’s external audit for fiscal 2008. Three additional standards are being evaluated for implementation in subsequent fiscal years. These standards and the related implementation dates are as follows:

Effective June 30, 2008
- GASB Statement 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions
- GASB Statement 48, Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues
- GASB Statement 50, Pension Disclosures – an amendment of GASB Statements No. 25 and No. 27
- SAS No. 104 – SAS No. 111

Effective June 30, 2009
- GASB Statement 49, Accounting and Financial Reporting for Pollution Remediation Obligations
- GASB 52, Land and Other Real Estate Held as Investments by Endowments

Effective June 30, 2010
- GASB 51, Accounting and Financial Reporting for Intangible Assets

The following is a brief summary of these new standards.

Accounting and Reporting Standards

GASB Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions – This Statement addresses how public entities (state and local governments, public universities, etc.) should account for and report their costs and obligations related to postemployment healthcare and other non-pension benefits. Collectively, these benefits are commonly referred to as “other postemployment benefits” or OPEB. GASB Statement No. 45 generally requires that public entity employers account for and report the annual cost of OPEB, and the outstanding obligations and commitments related to OPEB, in essentially the same manner as they
currently do for pensions. The provisions of GASB Statement 45 may be applied prospectively and do not require governments to fund their OPEB plans. This statement will be effective for fiscal 2008 reporting.

GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues* – Public entities sometimes exchange an interest in their expected cash flows from collecting specific receivables or specific future revenues for immediate cash payments – generally, a single lump sum. This statement establishes criteria that public entities will use to ascertain whether the proceeds received should be reported as revenue or as a liability.

GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations* - The statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. The statement excludes pollution prevention or control obligations with respect to current operations, and future pollution remediation activities that are required upon retirement of an asset. The statement provides that, once any of the defined obligating events has occurred, the University would be required to estimate the expected pollution remediation outlays and determine whether such outlays should be accrued as a liability or, if appropriate, capitalized when goods and services are acquired. This statement will be effective for the University’s fiscal year ending June 30, 2009.

GASB Statement No. 50, *Pension Disclosures—an amendment of GASB Statements No. 25 and No. 27* – The statement aligns financial reporting requirements for pension and with those for OPEB and, in doing so, enhances information disclosed in notes to financial statements or presented as required supplementary information by pension plans and by employers that provide pension benefits. This statement is effective for the fiscal year ending June 30, 2008.

Statement No. 51, *Accounting and Financial Reporting for Intangible Assets* – This statement addresses the recognition of intangible assets, including easements, water rights, timber rights, patents, trademarks, and computer software. Additionally, it establishes a specified-conditions approach to recognizing intangible assets that are internally generated. GASB Statement No. 51 provides guidance on determining the useful life of intangible assets when contractual or legal provisions limit the length of their life. This statement is effective for the fiscal year ending June 30, 2010, and the provisions of this statement are generally required to be applied retroactively for fiscal years ending after June 30, 1980.

Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments* – Accounting Standards previously required permanent and term endowments, including permanent funds, to report land and other real estate held as investments at their historical cost. This statement establishes consistent standards for the reporting of land and other real estate as investment by essentially similar entities. It requires endowments to report their land and other real estate investments at fair value. Public entities also are required to report the changes in fair value as investment income and to disclose the methods and
significant assumptions employed to determine fair value, and other information that they currently present for other investments reported at fair value. This statement is effective for fiscal year ending June 30, 2009.

Auditing Standards

Risk Assessment Standards: SAS No. 104—SAS No. 111—
In March 2006, the AICPA ASB issued eight Statements on Auditing Standards (SASs) that provide extensive guidance concerning the auditor’s assessment of the risks of material misstatement in a financial statement audit, and the design and performance of audit procedures whose nature, timing, and extent are responsive to the assessed risks. Additionally, the SASs establish standards and provide guidance on planning and supervision, the nature of audit evidence, and evaluating whether the audit evidence obtained affords a reasonable basis for an opinion regarding the financial statements under audit. These statements in general apply to the external auditors and will impact the University most heavily in the documentation of internal controls. SAS No. 104—SAS No. 111 are effective for the University’s financial statement audit for fiscal year ending June 30, 2008.

II. Internal Control, Compliance, and Service and Efficiency Improvements

The Enterprise Financial System project continues to be the primary operational focus of the entire Controller’s Office. Nevertheless, the following compliance and improvements and cost-savings have been recently implemented.

Internal Service Organizations
As reported to the Board of Regents Audit Committee at its February 2008 meeting, the Controller’s Office has initiated substantive changes to policies and procedures for internal service organizations (ISOs). ISOs are internal sales activities conducted between University departments, and are subject to federal rules governing costing and charging practices. Within the Controller’s Office, we have combined the Internal Sales and External Sales offices to better serve the University community, and to create synergies between the two units. They share the same vision to develop and enforce policies and procedures that educate the University Community on sales to internal and external customers regarding legal requirements, prudent business practices, and appropriate rate development. The Internal Sales Office published a revised Internal Sales policy and procedures. The Internal Sales Office also completed two on-line training courses that are ready to be rolled out to departments, with a third course to follow in May.

Shipping and Freight Management Contract
Purchasing Services has entered into a shipping and freight management contract with a third party vendor. The goal of the contract is to reduce the shipping and freight costs on the goods that the University purchases from external vendors. An evaluation of University purchasing and shipping patterns, and the related freight costs, concluded that the University could save, on average, between 40% and 50% on shipping and freight costs. A competitive process was conducted last year and a contract was recently awarded. Purchasing Services will begin a pilot program on May 1, 2008 with the intent
to roll out the program University-wide about a year later. Based on industry benchmarks and projections, the University’s goal is to realize savings of several million dollars per year on shipping and freight costs when the contract is fully rolled out to the entire University.

III. Enterprise Financial System Replacement Project

The University purchased the PeopleSoft Enterprise Financial System software in September 2003. The University has pursued a two-phase approach to implementation. Phase 1, a preparatory and exploratory phase, ran from January 2004 through July 2005. Phase 2, the implementation phase, began August 2005 and concludes in July 2008 when the new system goes live.

The implementation project continues to be on track to go-live in July 2008. Testing began in mid-November. The project has successfully completed two full test passes, which involved executing several thousand test scripts to identify defects. This has included testing of the integration of existing enterprise systems, such as the student and human resource systems. Test defects have decreased dramatically.

End user training began the last week of March 2008. Approximately 2,800 users must be trained in the three months prior to go-live. There will be approximately 63 training courses designed to prepare the financial user community for the new system. 37 organizational design and change management committees were formed – one for every college, administrative unit, and coordinate campus. The committees were comprised of staff from those colleges and departments, and their role was to identify the changes needed at the local departments to make the new processes and the new system work effectively. These committees have begun implementing the needed organizational changes in the colleges and administrative units.

The Controller’s Office completed its own organizational design activities, which resulted in some changes to the central units in the Controller’s Office. We are also working on revising all financial policies and procedures, so they conform to the new system. Finally, each of our departments has been converting financial data, such as vendor data (for purchasing and accounts payable) and sponsored data (for sponsored projects), from the existing systems into the new system.

At the May 2008 Board of Regents meetings, the Audit Committee will receive a presentation highlighting the new system’s impact on the institution’s financial internal controls, and the Finance and Operations Committee will be updated on the status of the implementation project.