

Minutes of the September 7, 2007 Meeting  
of the Board of Governors' Audit Committee

The Audit Committee met in Conference Room A of the General Administration Building in Chapel Hill, North Carolina on Friday, September 7, 2007, at 8:30 a.m.

Members in attendance were Dr. Laura W. Buffaloe, Mr. Frank Daniels, Jr., Mr. G. Leroy Lail, Mr. Charles H. Mercer, Jr., Mr. William G. Smith, and Mr. David W. Young. Others attending the meeting were Vice Presidents Robyn Render and Leslie Winner; Associate Vice Presidents George Burnette, David King, and James Smith. In attendance from Appalachian State University was Chancellor Kenneth E. Peacock.

As designated by Board Chair Jim Phillips, Associate Vice President Burnette convened the meeting.

The first item of business was to elect Committee officers. On the motion of Mr. Young, seconded by Mr. Lail, Mr. Smith was elected Chair by unanimous consent. On the motion of Dr. Buffaloe, seconded by Mr. Young, Mr. Lail was elected Vice Chair by unanimous consent. On the motion of Mr. Mercer, seconded by Mr. Young, Dr. Buffaloe was elected Secretary by unanimous consent.

Chair Smith then welcomed everyone to the meeting and recommended approval of the minutes from the last meeting. On the motion of Mr. Lail, seconded by Mr. Young, the minutes of the May 10, 2007 meeting were approved.

Next, Chair Smith welcomed Associate Vice President David King as the new addition to the Finance Division and Audit Committee Staff. Mr. King came to UNC-GA from the North Carolina Office of the State Auditor. Chair Smith expressed a special thanks to Associate Vice President George Burnette for his work and support to the Committee, as well as other staff support from Leslie Winner, James Smith, and Angelisa King.

Mr. Burnette and Mr. King presented the next item, 2006 Financial Audit Report and 2007 Information Systems Audit Report released since the last meeting.

Questions were answered throughout the discussion.

1. Fayetteville State University: – (Information Systems Audit - Public Report): No Findings

Report URL:

<http://www.ncauditor.net/EPSSWeb/EDSreportdetail.asp?RepNum=ISA-2007-6088>

2. The University of North Carolina at Greensboro: – (Investigative Audit): Two Audit Findings

Report URL:

<http://www.ncauditor.net/EPSSWeb/EDSreportdetail.asp?RepNum=INV-2007-0319>

See attachment

3. North Carolina Central University: – (Financial Audit): No Audit Findings

Report URL:

<http://www.ncauditor.net/EPSWeb/Reports/Financial/FIN-2006-6090>

4. North Carolina A&T State University: – (Financial Audit): Three Audit Findings

Report URL:

<http://www.ncauditor.net/EPSWeb/Reports/Financial/FIN-2006-6070>

#### Matters Related to Financial Reporting or Federal Compliance Objectives

The following audit findings were identified during the current audit and describe conditions that represent significant deficiencies in internal control or noncompliance with laws, regulations, contracts, grant agreements or other matters.

##### 1. INSTANCES OF FRAUD/ABUSE

During the course of our audit, there were several allegations of fraud/abuse that were brought to our attention. These allegations were investigated by the University's internal auditors and/or a team of outside consultants hired by the University. Significant findings from those investigations include:

#### Office of Naval Research Grant

The program manager who administered the HBCU Future Engineering Faculty Fellowship Program funded by the Office of Naval Research was responsible for several improper business practices and expenditures. During the 2005-06 fiscal year, program expenditures for student stipends, travel, tuition and fees, and other payments increased significantly, the same year that the program manager's husband became a student participant in the program. The following items were noted:

- a. Stipends of over \$66,000 were paid to the program manager's husband during 2005-06. The highest yearly stipend payout prior to his entry in the program was less than \$23,000. In many cases, payments made to the program manager's husband exceeded those paid to other students. Stipend payments also exceeded the amount included in the grant proposal.
- b. The program manager hired and supervised her daughter as a student worker in violation of State nepotism policy.
- c. Unreasonable and unnecessary travel expenses were paid. The program manager spent 41 nights in hotels during 2005-06 at program expense, with an average cost of \$328.74 per night. She also approved travel expenses for her husband in excess of the \$1,500 student travel budget. Further, the program manager paid for her daughters, as well as other student workers not enrolled in the program, to attend out-of-State conferences. Finally, lodging and meals for a symposium held in the city where the University is located were paid. Expenditures for the symposium included payments for one room for the program manager and another room for her husband for three nights during the two-day symposium (other participants only stayed two nights). Restaurant/room service charges in the amount of \$369.68 were incurred by the program manager and her husband and paid for by the grant.
- d. Payments were made for tuition that exceeded actual tuition costs, and payments were made for books and supplies even though those costs were supposed to be covered by the base stipend.
- e. Payments were paid to students for reimbursement of personal computer and health insurance costs without requiring proof of purchase.

- f. Equipment purchased by grant funds could not be located. Missing items included computer equipment, a digital camcorder and a digital camera. In total, approximately \$500,000 of program expenditures were questioned by the consultants. The program manager was terminated from University employment in September 2006.

This finding is applicable to award number NOOO 14-0 1-1-0987 for the period July 1, 2001, through June 30, 2006, and contract number NOOO 14-0 1-C-040 1.

#### Natural Resources and Environmental Design Department

An administrative assistant in the Natural Resources and Environmental Design Department misused a total of eleven accounts related to Natural Resources and the School of Agriculture, resulting in a loss to the University of \$101,000. The loss involved unauthorized financial aid awards, stipends, student employment, purchases of goods and travel. The administrative assistant was terminated from University employment in February 2006 and later pled guilty to charges stemming from the misuse of funds.

The grant and award periods affected by this finding are: ACQ-4-33623-07 (7/26/2004-10/26/2007), 2004-33814-15095 (9/1/2004-8/31/2007), 2005-338820-16385 (9/1/2005-8/31/2008), NCX-207-5-06-130-1 (10/1/2005-9/30/2006), 2005-38820-16356 (9/15/2005-9/14/2008), ACQ-4-33623-07 (7/26/2004-7/25/2006), NCX-171-5-02-130-1 (10/1/2004-9/30/2005), U91619901-0 (8/1/2003-9/30/2005), 68-3A75-3-111 (9/30/2004-9/30/2005), 68-3A75-5-147 (10/18/2005-10/18/2007).

#### Information Technology and Telecommunications Division

The former Vice Chancellor for Information Technology and Telecommunications misappropriated \$87,000 in university funds during the period May 2004 through February 2006. The majority of the funds came from rebates on computer purchases that were directed to a discretionary account held by the North Carolina A&T Foundation. The Vice Chancellor approved purchases from the fund that appeared to have no business purpose. The Vice Chancellor is no longer employed by the University and has been charged by legal authorities in connection with this matter.

The former Vice Chancellor for Information Technology and Telecommunications also participated in awarding a contract that is questionable. The Purchasing Department bid committee initially ranked a vendor third, but after assistance from the Vice Chancellor in evaluating proposals, the vendor was ranked first. The vendor in question is the mother of the former Vice Chancellor's executive assistant. The \$93,100 contract was for training services and had explicit documentation requirements for the sessions. The vendor submitted invoices totaling \$94,100, which were approved for payment by the former Vice Chancellor. Not only was the contract overpaid by \$1,000, the vendor also did not submit required documentation to indicate that the requirements of the contract were completed.

**Recommendation:** The University should establish, communicate and reinforce proper ethical and behavioral standards for employees. Further, the University should reevaluate controls over expenditure activity and the delegation of authority at the department level and closely monitor controls to ensure that they are effective. No University accounts should be maintained by the Foundation.

**University's Response:** We concur with the recommendation. University and State policy prohibits the maintenance of University funds in any non-University account. This policy is communicated to campus annually.

- a. Office of Naval Research Grant: The Office of Naval Research (ONR) and the University have finalized grant amendments in writing, approving \$422,415 of the questioned program expenditures, including stipends, tuition, travel, insurance, and laptop computers. The University recognizes that control over expenditure activity is strengthened by obtaining written agency approvals or amendments before enacting transactions.

- b. The University terminated the program manager's employment and has initiated legal action to recover a major portion of the remaining questioned costs and missing equipment.
- c. Natural Resources and Environmental Design Department: The University has recovered a portion (\$75,851) of the loss from insurance proceeds and legal actions taken against the administrative assistant. The University anticipates some additional restitution from the former employee. The Purchasing Office conducts ongoing campus workshops stressing the proper use and control of the University procurement card, and they audit the monthly departmental procurement card reconciliations.
- d. Information Technology and Telecommunications Division: The University terminated the employment of the Vice Chancellor for Information Technology and Telecommunications and has initiated legal action to recover the misappropriated funds. The University has reinforced its existing ethical and behavioral standards and communicated those standards to the University community through numerous seminars. Additionally, the University and the Foundation have strengthened the policies for establishing accounts in the Foundation and for expenditures from those accounts. The existing policy of the University stipulates that no University funds are to be placed in any accounts outside of the University.

## 2. DEFICIENCIES IN GRANTS MANAGEMENT

In January 2007, a team of outside consultants hired by the University identified a number of problems in the management of federal grants, some of which had also been noted by internal auditors. The team's findings included:

- a. Since June 30, 2005, the University has not maintained documentation required by OMB Circular A-21 to support personnel charges to federal programs. As a result, the University has a potential liability for questioned costs associated with personnel charges to federal programs. The amount of potential questioned costs is not readily determinable.
- b. Of the approximately 500 grant fund accounts maintained by the University, 184 accounts have had no recorded activity since July 2005, indicating that the grants were closed. There were 69 inactive accounts with deficit cash balances totaling over \$395,000, which indicates that the budget for the grants was overspent using other funds. The other 115 grant accounts reflected a total cash balance of over \$716,000, which indicates excess federal revenues could have been received. However, the residual balances in these accounts could also be the result of accounting errors. A clearing account managed by the Contracts and Grants Office had a balance of over \$784,000 as of February 14, 2007. The account is used for the deposit of receipts that have not been identified to a particular program. These grant accounting deficiencies could also result in questioned costs in an amount that is not readily determinable.

**Recommendation:** The University should consult with federal grantor agencies to determine the corrective action to be taken. Also, the University should evaluate its accounting procedures for grant funds and make changes to ensure that receipts are properly applied and that over-expenditures are prevented.

### **University's Response:**

- a. A revised, more efficient time and effort reporting model was in the process of implementation at June 2005. Campus seminars had been conducted and programming was being initiated. However, resources were reprioritized with the implementation of the Banner Finance ERP and the time and effort project was not resumed until November 2006, when certification forms were distributed and informational seminars were conducted with project investigators by the Office of Contracts & Grants. Delinquent reports are now being collected (95% complete) and a policy has been developed that should ensure ongoing compliance.
- b. The University practice is to consult federal or sponsor grantor agencies for guidance with respect

to contentious issues or questionable expenditures. The specific grant deficiencies identified will be resolved by October 2007, with procedures put in place by September 2007 to prevent future occurrences. Following newly established procedures final resolution of grants will be completed in a more timely manner.

- c. The clearing account relates to University funds, predominately wired from outside sources that did not have proper documentation for immediate identification but are required to be deposited within 24 hours of receipt. Normally this account is reconciled monthly but the reconciliation was deferred during the Banner Finance ERP implementation. To date, over \$400,000 of the \$784,000 noted has been identified and properly credited. The remaining balance of approximately \$384,000 is being reviewed.

### 3. MISUSE OF VENDING RECEIPTS

The University inappropriately transferred \$380,000 of vending receipts to the Chancellor's Discretionary Fund maintained by the North Carolina A&T Foundation. These receipts were then primarily used for purposes that are inconsistent with those outlined in University of North Carolina System policy.

The University has a five-year campus vending contract that began in October 2003 that includes exclusive beverage service. The beverage vendor pays the University \$140,000 per year. During 2003 through 2005, \$380,000 of the vending receipts were transferred to the discretionary fund at the Foundation. In 2005, the former Chancellor signed a gift document indicating that the funds were solicited from the vendor for the Foundation; however, there is no mention of the Foundation in the vending contract. Internal auditors and a team of consultants hired by the University both concluded that the moneys should not have been transferred to the Foundation account.

We examined 89% of the expenditures from the Chancellor's Discretionary Fund during the 2006 fiscal year. Since, the majority of the receipts in the fund (85% in the 2006 fiscal year) came from the vending contract, we compared the expenditures to those allowed by University of North Carolina System policy related to vending receipts. The policy provides that vending moneys may be used for scholarships and direct student financial aid programs, debt service on self-liquidating facilities, and other specific student activities as authorized by the chancellor.

We concluded that 87% of the expenditures we examined were for unallowable purposes. Unallowable items included commission for art work, travel for the former Chancellor's wife to accompany him on University-related travel and payments for Foundation/ Alumni events.

The largest unallowable expenditure was the payment of \$150,000 to a faculty member exempt from the State Personnel Act for the purchase of an annuity. System policy requires all constituent institutions to have a policy concerning the granting of non-salary compensation for personnel exempt from the State Personnel Act other than the Chancellor. The policy shall either provide specified non-salary compensation to a defined category of employees uniformly or shall require approval by the board of trustees regarding non-salary compensation granted to an individual employee. The University was unable to produce a University policy regarding non-salary compensation or documentation to indicate the payment had been approved by the board of trustees.

**Recommendation:** The University should account for all of its activity in its own records and should not maintain any additional accounts within the Foundation. The University should adopt policies to ensure that it adheres to University of North Carolina System policy regarding the use of vending receipts and non-salary compensation for employees.

**University's Response:** University and State policy prohibit the maintenance of University funds in any non-University account. This policy is communicated to campus annually. We concur with the recommendation and are enforcing policies relating to vending receipts and non-salary compensation.

On the motion of Mr. Smith, seconded by Mr. Young, the Committee went into closed session to prevent the disclosure of information that was privileged or confidential pursuant to the law of this State or of the United States, or not considered a public record within the meaning of Chapter 132 of the General Statutes pursuant to G.S. §143-318.11(a)(1) and G.S. §147-64.6(d) which provides that the workpapers of the State Auditor are confidential.

#### CLOSED SESSION

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The Committee returned to open session.

Chair Smith reminded the committee that when the Audit Committee went into Closed Session to discuss investigative audits that only members of the Audit Committee would be in attendance. Also, discussion of any Closed Session information would not be permitted outside of the meeting.

There being no further business, the meeting was adjourned.

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Mr. William G. Smith  
Chair of the Audit Committee

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Dr. Laura W. Buffaloe  
Secretary of the Audit Committee