

2009 and Audit Report Released Since Last Meeting By the North Carolina Office of the State Auditor:

1. Elizabeth City State University: - (2009 Financial): Three Audit Findings
Released Date: 10/27/2010

Report URL

<http://www.ncauditor.net/EPSWeb/Reports/Financial/FIN-2009-6086.pdf>

Matters Related to Financial Reporting

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. Elements of findings number one and two were also reported in the prior year.

1. DEFICIENCIES IN FINANCIAL REPORTING

The financial statements and related notes prepared by Elizabeth City State University contained significant misstatements that were corrected as a result of our audit. These misstatements indicate that the University's internal control over financial reporting was not effective, and without our corrections, the financial statements could have been misleading to readers. The misstatements noted during our audit included:

- a. The University misclassified \$9.6 million as noncapital grant revenues from federal student financial aid, when in fact the grants were not for federal student financial aid.
- b. Scholarships and fellowships expense was understated by over \$3.7 million because some grants that had not been recognized by the University were included in the University's scholarship discount calculation. An adjustment was required to increase the expense and noncapital grant revenues by \$3.7 million.
- c. The University did not properly classify net assets on the Statement of Net Assets. Adjustments were required to reclassify \$2.6 million between expendable net assets restricted for scholarships and fellowships, nonexpendable net assets restricted for scholarships and fellowships, and unrestricted net assets. Also a reclassification of over \$1 million was required between unrestricted net assets and net assets invested in capital assets.
- d. The University did not properly classify cash on the Statement of Net Assets. An adjustment was required to reclassify \$2 million to current restricted cash primarily due to misclassifying restricted cash amounts as noncurrent when posting an adjustment to the 2008 beginning cash balance.
- e. The University did not properly record debt maintenance reserve transfers, resulting in a \$1.8 million misclassification between revenues and expenses. The University discovered the error after the

statements were submitted for audit. Adjustments were required to reduce the interest and fees on debt expense by \$1.8 million, reduce other operating revenues by over \$1 million, and adjust nonoperating revenues and expenses by over \$800,000.

- f. The student accounts receivable balance was overstated by over \$949,000 because the University recognized receivables and unearned revenues for summer school charges that were not earned as of the fiscal year-end.
- g. Revenues from capital grants and expenses for supplies and materials were overstated by \$346,000 due to the University posting an entry twice.
- h. The University understated intergovernmental accounts receivable, revenues from federal contracts and grants, and restricted expendable net assets for scholarships and fellowships in the amount of \$370,000 due to the University improperly reversing a prior year accrual balance twice.

Findings related to deficiencies in financial reporting were reported in two prior audits.

Recommendation: The University should place greater emphasis on the year-end financial reporting process and implement effective internal control procedures to ensure the completeness and accuracy of the financial statements.

University's Response: The University acknowledges that its financial statements contained classification errors. Subsequent to this finding staff has taken key steps to improve internal control over financial reporting. In 2010, staff made use of additional functionality in the Banner financial management system, which further automated the accrual processing and reporting functions. This enhanced automation should lead to streamlined year-end processes, a reduction in recording errors and provide additional time for staff to review financial statements for accuracy prior to their production. During 2011, Business and Finance set up journal entry approval queues. This established a defined process for management review and approval of all journal entries and supporting documentation prior to posting entries to the general ledger. Business and Finance is also planning to establish a distinct and adequately resourced financial reporting and general ledger maintenance section within the division. Their expanded focus will include more intense review and analysis of daily, monthly and other periodic financial transactions and reports. Finally, we are continuing to aggressively recruit to fill key vacancies in Business and Finance.

2. DEFICIENCIES IN BANK RECONCILIATION AND CHECK DISBURSEMENT PROCEDURES

The University has not adequately reconciled its bank accounts on a monthly basis. As a result, there is an increased risk that errors will occur and not be detected in a timely manner. In addition, the University did not submit unclaimed outstanding checks to the State's escheat fund or to the federal government as required.

At June 30, 2009, the University had three bank accounts with unexplained reconciling differences between the bank balance and the accounting records. We noted the following deficiencies:

- Two of the bank accounts were reconciled together and had total unresolved reconciling items of \$23,071, which included outstanding checks that have been on the reconciliation since June 2006.
- One bank reconciliation had offsetting unresolved differences that overstated the accounting records by over \$167,000. This overstatement consisted of cumulative reconciling differences that overstated the accounting records by approximately \$716,000 and understated the records by approximately \$549,000. Several reconciling items on the June 2009 reconciliation had been identified as differences on the June 2007 reconciliation. Further, the reconciliation included outstanding checks dated prior to July 2006.
- The University has not submitted any unclaimed outstanding checks to the State's escheat fund since fiscal year 2005. North Carolina General Statute 116B requires that abandoned property, such as outstanding checks, be delivered to the Department of State Treasurer by November 1 of each year and should include property abandoned during the twelve months preceding July 1 of that year.
- After year end, a consultant provided the University a \$938,000 cash adjustment to the accounting records to reconcile with the cash in the bank. This adjustment included the \$167,000 of unresolved reconciliation differences noted above and corrections for errors made by the University when posting adjustments from the 2008 audit.

The deficiencies described above indicate that the University has not implemented effective controls over the bank reconciliation process to ensure outstanding items are properly researched and resolved, nor have they implemented effective controls to ensure outstanding checks are submitted to the escheat fund timely.

In addition, we noted that as of January 28, 2010, the University was holding in its vault outstanding checks totaling over \$194,000 that had been written to students prior to June 30, 2009. The majority of these checks were held by the University until March 29, 2010, when the checks were voided and subsequently reissued.

In regards to federal student financial aid funds, institutions are allowed to hold checks for up to 21 days after the student is notified that the check is available. If the student does not pick up the check within the 21 days, the institution must immediately mail the check to the student or parent, initiate an electronic payment to the student or parent, or return the funds to the federal government. If the institution attempts to disburse funds to the student but the check is not cashed, the institution must return the funds to the federal government no later than 240 days after the date the school issued the check.

As of June 30, 2009, approximately \$58,000 of the checks in the vault had been outstanding for more than 240 days. We examined 13 of these checks, totaling approximately \$20,000, and determined that eight of the checks included

federal student financial aid funds totaling approximately \$10,000. As of March 29, 2010 when the checks were voided, the entire \$194,000 had been outstanding for more than 240 days.

Deficiencies related to the reconciliation of the bank accounts were reported in the prior two audits.

Recommendation: The University should enhance internal control to ensure the bank statements are properly reconciled to the accounting records each month. Adequate reconciliation procedures include promptly investigating and resolving outstanding items. In addition, the University should implement procedures to ensure that unclaimed outstanding checks are submitted to the State's escheat fund or the federal government as required.

University's Response: The University currently reconciles its bank accounts on a monthly basis; however, previously identified reconciling items were not resolved in a timely manner. The University has since developed solid reconciliation procedures which promptly address and resolve current outstanding items. In addition, we have established a procedure that places specific limits on the number of days that unclaimed outstanding checks and refunds are held if they are not picked up on their distribution date.

3. INAPPROPRIATE INFORMATION SYSTEM ACCESS

The University administered information system access rights inconsistent with adequate internal controls. Improper access to computer systems can result in both intentional and unintentional security breaches that place the confidentiality and integrity of information at risk.

The following deficiencies were noted:

- The administrative account for the critical network devices was shared between multiple members of the Network Services division. We also noted inappropriate access to the Banner Security features that allow multiple users to share security account access. Sharing accounts does not allow for proper accountability of the individual performing system activities.
- An external contractor had access to the production database where daily operating transactions post and there was no monitoring by the University of the contractor's activity.
- The University does not have proper procedures in place to inform system administrators to remove or suspend access rights for individuals who are on extended leave. We noted two employees out on short-term disability leave who had access to the Banner accounting system during their leave of absence. The University did not properly lock the users' access in a timely manner.

Findings related to system access deficiencies were reported in the prior two audits.

Recommendation: The University should limit system access rights to ensure that employees and third parties are assigned access privileges that are appropriate for the necessary job requirements.

University's Response: We concur with the recommendation. The University immediately took corrective actions by revoking the inappropriate system access for shared accounts, an external contractor and employees on extended leave. On October 11, 2010, the University's Administrative Council amended its Network Security Policy (policy #700.2.2), adding specific provisions for terminating the access of employees on extended leave. Additionally, the University will continue to limit access privileges to employees and external contractors as appropriate to their task requirements.