Common Issues & Risks
For Audit Committee Focus

Presentation to: Audit Committee

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“The Audit Committee serves as the institution’s first line of defense when considering financial reporting, internal control, compliance, and risk management.”

-AGB Effective Committee Series
Financial Risks – Functional Areas

Control Environment
- Integrity & Ethical Values
- Risk Management
- Commitment to excellence
- System Policies & Procedures

Financial Management
- Financial Health Indicators
- Banking & Cash controls
- Regulatory compliance
- Budgeting & Allocation Standards
- User Security – Financial Systems
- Grant Management

Revenues
- Tuition & Fees
- Accounts receivable
- Service revenue
- Grants & Contracts
- Foundations
- Customized Training
- IP Licensing

Expenditure
- Employee payroll
- Accounts payable
- Procurement
- Purchase cards
- Capital projects
- Financial Aid
- Student payroll

Other
- Auxiliary
- Athletics & Students
- Capital Assets
- Activity Fund
- Document Imaging
- Revenue Fund
### Institution Financial Risks: Metrics

<table>
<thead>
<tr>
<th>Metric Category</th>
<th>Factors Measured</th>
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<tbody>
<tr>
<td>Financial Condition</td>
<td>• Operating gains or the size of losses</td>
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<tr>
<td>(Points = 300)</td>
<td>• Composite Financial Index (CFI)</td>
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<td>• Overall materiality of financial transactions</td>
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<td>Audit</td>
<td>• Time since last internal control and compliance audit and the volume of findings</td>
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<td>(Points = 350)</td>
<td>• Whether the institution has an annual financial statement audit; volume of findings from the last audit</td>
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<td>• Number of outstanding unsatisfactory audit findings</td>
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<tr>
<td>Business Operations</td>
<td>• Change or loss in key personnel, knowledge, or skill</td>
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<td>(Points = 275)</td>
<td>• Diversity or complexity of operations</td>
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<td></td>
<td>• Number of incomplete security access rights</td>
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<tr>
<td>Other</td>
<td>• Use of professional judgment to make or adjust for a significant financial risks at a specific institution</td>
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<tr>
<td>(Points = 100)</td>
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Total points = 1025
Broad Themes

- The key component to manage global risk is taking a holistic view (i.e. a total picture of risk correlations and aggregations) to connect the risk dots.

- What are the known unknowns?
1) Financial Statements, Adequacy of Internal Controls, Compliance, and Strategic Risks

1.1. Challenges/ vulnerabilities (could be possible game changers)

Revenue Trends (5 years)

- Steps we are taking to address declining enrollment, flat GF budget revenue?
- Grants... will we see growth? How? Where?
- Endowment/ Gifts... will we see growth? How?
Costs Trends (5 years)

Plot the following samples:

- Expenditures per 100 headcount of students.
- Cost associated with raising $1.
- Number of staff FTEs per 100 headcount of students.
- Facilities expenditures per 2,000 gross square feet.
- Research expenditures per researcher FTE.
1.2. New accounting standards:
• What are the new GASB requirements for FY15? How will new GASB requirements impact the university?

1.3. Compliance:
• Is the university in compliance with federal and state laws and regulations (including FERPA, PCI, Red Flag, OSHA, Form 990T tax returns, A-133, NCAA, financial statements audits, granting agency audits, HIPPA)?

1.4. Component units:
• Which of the university’s component units (Nanook Innovation Corporation, Seawolf Holdings) have benefited from significant activity?
1.5. Enterprise risk management

- What risks are associated specifically with *Shaping Alaska’s Future*?
- Has our risk tolerance changed? How much more/less financial risk is the university willing to take? Identify risks that we are clearly unwilling to take.
- Do our perceived risks and our risk tolerance limits reflect the real UA operating environment?
- Have we clearly identified leadership’s decision-making responsibilities with regard to risk?
- Can the UA System satisfactorily seek out conflicts of interest among campuses?
• What risks are impacted or created by accepting new academic or business models, new student loan programs, federal funding, grants, accreditation, and meeting unfunded federal mandates?
2) Education Trust of Alaska and the University Pension Funds

- Trusts must be in compliance with the Internal Revenue Code and regulatory requirements.
- Investments managed, not set on autopilot.
- Assessing potential investment liabilities is a continuous process of oversight by experts.
3) Land Grant & Inflation Proofing Funds

- Can the investment portfolio return support continued levels of scholarship spending in a persistent down market?
- Is the process for setting the spending rate appropriate?
4) Operating Funds

- Needs continuous review.
- Does setting appropriate risk in the portfolio follow BOR policy?
- Can “adequate liquidity” actually be too conservative?
5) Cyber Security. Potential risk to university finances, reputation, are huge. Cyber attacks against universities are occurring daily across the U.S.

- What is our cyber risk?
- Cyber threats and risks to the university’s highest value assets originate from where?
- Should we use something like a cyber security scoreboard to assess principal cyber risk areas/ incidents/ trending, etc.?
- Is cyber-risk mitigation sensitive to cost of mitigation? Are we maxing our capability to afford?
Cyber Security
Complex, Expensive, Not Well Understood

- Intergovernmental agreements and cooperation
- Contractual service agreements and federations
- Indemnification
- Regulatory/administrative law
- Criminal law
- Legal remedies may also institute protective measures

1. Measures for protection
   - Real-time data availability
   - Data retention and auditing
   - Identity Management
   - Encryption/VNPs
   - Resilient infrastructure
   - Routing & resource constraints

2. Measures for threat detection
   - Provide data for analysis
   - Vulnerability notices
   - Patch development
   - Blacklists & whitelists
   - Threat analysis
   - Provide basis for actions

3. Measures for remediation
   - Vulnerability notices
   - Restrict resources
   - State & integrity
   - Blacklists & whitelists
   - Reputation sanctions
   - Investigation & measure initiation

4. Legal Remedies
   - Legal remedies may also institute protective measures

Legal remedies may also institute protective measures

= information exchange for analysis
= information exchange for actions

Public Interest Report 2012
Goodman-Lukasik-Rutkowski Model
http://fas.org/pubs/pir

September 19, 2014
A Few Examples of Breaches in Higher Education

• University of Maryland Data breach (February 2014)
  • Over 300,000 student and employee records dating as far back as 1998.
  • Cost is unknown - as per industry experts cost is couple of million.

• Indiana University (February 2014)
  • 140,000 student records exposed for 11 months because of an employee error.
  • Known costs: $75K for call centers, $6k on mailings, & 700 hours of staff time.

• Maricopa County Community College District (April 2013)
  • 2.4 M student, employee and vendor records going as far back as 30 years.
  • Approx. $10 M in notification, credit monitoring, and remediation. $2.5 M in legal fees. $7 M in hardware update. Class action suites & settlements.

• North Dakota University (March 2014)
  • Over 290,000 student and employee records.
  • Known costs include $200,000 on identity theft protection.
6) **External Auditor**

- Compares university’s financial health to last year.
- Audit opinion “unqualified?”
- Looks for internal-control issues.
- Assesses management’s accounting estimates.
- Looks for any management issues.
7) **Internal Audits**

- Powerful tool for management oversight.
- Provides trends.
- Cycle-time to get reports out must be reasonable.
- Must track major findings and closure rates.
- How well does our team search for evidence of fraud?
8) Title IX: Sexual Misconduct

- Bottom line: Has to stop.
- 55 higher education institutions are currently under review by the U.S. Department of Education Office of Civil Rights*.
- Potentially large unfunded mandates.
- Potentially large liability, fines.
- Bottom line: Take this very seriously!

*Two separate offices within DOE handle campus sexual assault investigations (OCR handles Title IX & Federal Student Aid office oversees investigations under the Clery Act.)