

**MINUTES OF THE AUDIT AND COMPLIANCE SUBCOMMITTEE  
OF THE FINANCE COMMITTEE  
University of Kentucky Board of Trustees  
December 8, 3:00 pm  
327C Charles T. Wethington Building**

**Subcommittee Members Present**

Bill Britton (Chair), Angela Edwards, David Hawpe and Jim Stuckert

**Approval of Minutes**

The minutes of the September 5, 2014 Audit and Compliance Subcommittee (ACS) meeting were approved as presented.

**Reports and Discussion Items**

**BKD Results of FY 2014 Financial Statement Audit**

Ms. Mary McKinley, BKD Partner and Ms. Joanie Duckworth, BKD Supervisor reviewed the *Results of the 2014 Financial Statement Audit, Internal Control Matters and Other Required Communications*. The following items were highlighted:

BKD Management Letter (pages 2-7): BKD issued an unmodified (clean) opinion regarding the FY 2014 financial statements. There were no audit adjustments to the consolidated statements. BKD did have unrecorded passed adjustments that were reviewed with UK Management and Chair Britton. All agreed that the passed adjustments had no significant effect on the financial statements.

Audited Financial Statements: Per Footnote 1 (on page 26 of Tab 1), the University adopted GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* during FY 2014. As a result of the adoption, certain reclassifications have been made to FY 2013 financial statements to compare to FY 2014 financial statement presentation.

Single Audit Reports and Schedule of Expenditures of Federal Awards (A133 Report): The Summary of Auditor's Results is found on page 19 of Tab 3. Ms. McKinley reported that testing of Federal Awards (totaling \$445 million) was conducted on 3 major programs with the respective results: 1) Student Financial Aid Cluster (qualified opinion), 2) Research and Development Cluster (unmodified opinion), and 3) SNAP Cluster (unmodified opinion). Student Financial Aid compliance testing (verification) of 4,045 accounts was conducted using a sample size of 25 accounts. BKD found that three of the sample selections were not properly verified resulting in material non-compliance. Only one of the three had an incorrect amount of student financial aid awarded (\$2,583 was over-awarded to the student). Mr. Eric Monday, Executive Vice-President for Finance and Administration, noted that UK contracted with an external verification processor (KHEAA) used by other academic institutions. He reported that a defined action plan has been formulated by the Office of the Treasurer and Enrollment Management to address the BKD results; copies of the plan were distributed to members of the ACS. Ms. Ronda Beck, Controller, noted that the KHEAA contract has been reviewed and revised to strengthen the language regarding quality control. The action plan includes 100% validation of accounts verified by KHEAA for the 2014 Fall Semester. Ms. Susan Krauss, Treasurer, reported that there are several alternatives based on the results of the 100% validation: (1) Continue to outsource to KHEAA and add additional staff in-house to increase testing (2) Add additional staff and bring the entire process in-house (3) Consider another provider with a proven track record. Ms. McKinley asserted that other institutions deal with this same issue as it is a common error. She has seen no significant ramifications or fines in her experience. She noted that BKD will increase testing of Student Financial Aid next year.

Additional Discussion: Chair Britton asked Ms. McKinley to address the restatement of the separate audit report issued for the UK Department of Athletics (Athletics). Ms. McKinley reported that during the current year's audit, UK Management notified BKD that the pledge receivable amount for June 30, 2013 was incorrect. BKD determined that the error was material (\$9.7 million understatement of net pledge receivables) requiring the restatement of the Athletics' financial statements. The error was associated with the conversion process of changing the UK Athletics Association (a separate affiliate) to the UK Department of Athletics (a University department). This change was effective July 1, 2012. Mr. Monday reported that the Office of Development, Office of the Treasurer and Athletics have developed an action plan to address the handling and recording of Pledge Receivables moving forward. The action plan was distributed to the ACS members. He also noted that UK Internal Audit had recently performed an audit of Pledges. Mr. Joseph Reed, Senior Director of Internal Audit (UKIA), responded that going forward, UKIA will be performing a pledge audit on an annual basis that will involve the examination of input controls, data integrity and completeness of information. Ms. McKinley thanked the Office of the Treasurer for their work on this issue. Chair Britton thanked everyone for the good communication noting that he immediately received a call when the error was discovered.

### **UK Internal Audit Update**

Mr. Joe Reed, Senior Director of Internal Audit (UKIA) reported on the following items:

#### Internal Audit August 2014 QAR Draft Report

Mr. Reed reported that UKIA's responses have been placed in the Quality Assessment Review (QAR) draft report. Chair Britton noted that the ACS members and UK Administration need to formulate a response to the QAR recommendation on page 16 of the report to be discussed at the next meeting.

#### Fiscal Year 2015 Activity Update

Mr. Reed reviewed the FY 2015 Activity Update as of October 31, 2014. He noted that the first quadrant represents the FY 2015 UKIA Approved Work Plan. He highlighted that continuous audits and continuous auditing reviews were ongoing. UKIA will introduce a Grants continuous audit program in April of 2015. The Business/Operations & IT Audits with a status of red denotes that the audit has not been engaged. Mr. Reed reported that the second quadrant lists the FY 2015 UKIA Unplanned Reviews. He commented that Mining Engineering and Pledges audit reports have been issued. Comply Line Calls consists of UKIA review of certain calls received on the University hotline. Mr. Reed reviewed the third quadrant that lists the FY 2015 UKIA Audit Coverage by Enterprise Division, including the number of projects and project hours. He noted that it is UKIA's goal to be present in all Enterprise Divisions to provide adequate audit coverage across UK. The fourth quadrant lists the FY 2015 UKIA Metric Update. Mr. Reed reported that the UKIA productivity rate was 84%. Infrastructure hours comprised 10% of the total direct hours with most of this time spent on the QAR.

#### Fiscal Year 2014 Comply Line Update Summary

Mr. Reed reviewed the Summary, noting that the report out is normally in September. He reported that UKIA trends the Comply Line calls and considers the trends when formulating the Work Plan.

### **Action Items**

#### **ACSR 1 – Retain BKD, LLP for Audit of Financial Statements for Fiscal Year 2014-15**

Ms. Susan Krauss, Treasurer, recommended that the ACS approve retaining BKD for the audit for fiscal year 2015 and authorize Ms. Krauss to execute the engagement letter. It is expected that the BKD audit fees will be slightly higher than fiscal year 2014 (roughly \$366K); the fee terms will be negotiated and Ms. Krauss will bring the engagement letter before the ACS at the next meeting (February 19, 2015). She also noted that the FY 2015 audit is the final year of the contract with BKD. It will be rebid next year. Mr. Jim Stuckert moved to approve ACSR 1. Seconded by Mr. David Hawpe. Approved.

### **Other Business**

Chair Britton asked the members to consider for discussion at the February meeting whether the ACS should be a subcommittee of the Finance Committee or a true Committee reporting directly to the Board of Trustees. When asked, Ms. McKinley commented that in her experience, the Audit Committee is usually a direct report of the Board of Trustees. Mr. Bill Thro, UK Legal Counsel, will research this issue and report his findings at the February meeting. Chair Britton requested an update at the February meeting on the status of possible amendments to UK Governing and Administrative Regulations related to disciplinary actions.

There being no further business, the meeting was adjourned.

### **Next Meeting**

Monday, March 16, 2015

- BKD FY 2015 Engagement Letters
- Internal Audit FY 2015 Mid-year Activity Update
- ACS/UK Administration Response for UK Internal Audit QAR Report
- ACS Reporting Structure Discussion
- GR/AR Amendment Update

Respectfully submitted,

Catherine Miller