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University of South Carolina
BOARD OF TRUSTEES

Audit and Compliance Committee

March 16, 2012

The Audit and Compliance Committee of the University of South Carolina met on Friday, March 16, 2012, at 9:00 a.m. in the 1600 Hampton Street Board Room.

Members present were: Mr. J. Egerton Burroughs, Chairman; Mr. Chuck Allen; Mr. W. Lee Bussell, Sr.; Mr. Hubert F. Mobley; Dr. C. Dorn Smith, III; Mr. Thad H. Westbrook; Mr. Eugene P. Warr, Jr., Board Vice Chairman; and Mr. Miles Loadholt, Board Chairman. Members absent were: Mr. Mack I. Whittle, Jr.; and Mr. Charles H. Williams.

Other Board members present were: Mr. Herbert C. Adams; Mr. Thomas C. Cofield; Mr. William W. Jones, Jr.; Ms. Leah B. Moody; and Mr. John C. von Lehe, Jr.

Others present were: President Harris Pastides; Secretary Amy E. Stone; Vice President for Academic Affairs and Provost Michael D. Amiridis; Chief Financial Officer Edward L. Walton; Vice President for Student Affairs and Vice Provost for Academic Support Dennis A. Pruitt; Vice President for Human Resources Chris Byrd; Vice President for Information Technology and Chief Information Officer William F. Hogue; Vice President for Communications Luanne Lawrence; General Counsel Walter (Terry) H. Parham; Senior Vice Provost and Director of USC System Planning Christine W. Curtis; Vice Provost and Dean of Undergraduate Studies Helen Doerpinghaus; Vice Provost and Dean of Graduate Studies Lacy Ford; Dean of the College of Arts and Sciences Mary Anne Fitzpatrick; Executive Assistant to the President for Equal Opportunity Programs Bobby Gist; Associate Vice President for Finance and Budget Director Leslie Brunelli; Associate Vice President for Business and Finance and Medical Business Affairs Jeffrey L. Perkins; University Treasurer Susan D. Hanna; Associate Dean for Academic Affairs in the College of Education Zach Kelehear; USC Upstate Senior Vice Chancellor for Academic Affairs Marsha Dowell; USC Beaufort Department Chair for Early Childhood Education Nancy L. Gallenstein; USC Upstate Chair of Department of Informatics Ron D. Fulbright; Director of the Department of Internal Audit Phil Iapalucci; Director of State Relations Trey Walker; Department of Athletics Chief Financial Officer Jeff Tallant; Associate Vice President for Environmental Health and Safety and Risk Management Thomas Syfert; Director of Capital Budgets and Financing Charles FitzSimons; Controller Patrick Lardner;

Director of Financial Reporting Mary Peak; Professor in the Department of Psychology, College of Arts and Sciences, and Chair of the Faculty Senate Sandra J. Kelly; Special Assistant to the President J. Cantey Heath, Jr.; Director of Governmental and Community Relations and legislative Liaison Shirley D. Mills; Director of News and Internal Communications, Division of Communications Wesley T. Hickman; Student Government Association President Kenny Tracy; Tom McNeish and Brian D'Amico with the outside audit firm Elliott Davis, LLC; Reporters with the Gamecock Cassie Cope and Thad Moore; University Technology Services Production Manager Justin Johnson; Board staff members Terri Saxon and Vera Stone; and members of the media.

Chairman Burroughs called the meeting to order, welcomed those in attendance and asked them to introduce themselves. Mr. Hickman introduced members of the media who were in attendance.

Chairman Burroughs stated that the agenda had been posted and the press had been notified as required by the Freedom of Information Act; the agenda and materials had been e-mailed to the Committee members; and a quorum was present to conduct business.

Chairman Burroughs called for a motion to enter Executive Session to receive legal advice on a personnel matter. Mr. Westbrook moved to enter Executive Session and Mr. Warr seconded the motion. The Board and Mr. Walton were asked to remain. At the conclusion of the Executive Session, Chairman Burroughs declared a return to Open Session.

Since there were no other matters appropriate for discussion in Executive Session, Chairman Burroughs declared the meeting returned to Open Session.

Return to Open Session

Chairman Burroughs called on Mr. Walton who introduced Mr. Tom McNeish from Elliott Davis and Company to talk about external audits reported on by his firm. Mr. McNeish related back to the goals and topics that occurred during the Audit Retreat. He discussed the University's progress on some of the objectives. He reported that the University was moving forward and was looking at development areas in the financial reporting and controls over transactions and communications.

I. External Audits:

A. FY11 Management Letter: While the Management Letter pointed out possible deficiencies or weaknesses, it should be viewed as a diagnostic tool. With an institution the size of the University of South Carolina, there would always be areas for improvement. The auditing of the University's financial statements gives the firm insight or leverage into the many processes and the implementation of the internal controls. The firm can comment on this process and part of that would be required communication. If a significant deficiency or material weakness was identified, government auditing standards require notification to the University by Elliott Davis. Those were typically going to be, in a severity context, the items that would need to be shored up and fixed. Part of what would be seen as we are going through and evaluating what was being done on the internal controls was management's response to any given finding. In addition to that, the firm's requirement would be to follow up on what could have been a finding in the previous year and see what progress has been made; specifically what has been done to address the findings from the prior year. Discussions would be held with the relative members of the administration to see if progress was being made. For any audit firm, if there was not a sense of urgency, or if a desire to address those issues was not seen, then it becomes, in terms of severity, a red flag and indicates management's philosophy or the tone at the top, starting with the Trustees - is it where the University should be in that internal controls in the processes are being addressed and areas in question are being evaluated.

The good news is that there are two internal control letters – one for the University as a whole and the campuses, and another one specifically for Parking Services. With maybe one exception, improvements were found on all the findings that were noted last year. The one finding exception is a work in progress and it is being addressed. The first good news point is that based on when some of the issues identified were revisited, the administration is going back, walking us through what is being done to address those issues. Going back to the Management Letter, there are basically five buckets that the findings fall into:

- (1) Segregation of duties – If there is a disbursement that occurred, the person who initiated that is different from the person who ultimately approves it.
- (2) Controls in place that are occurring – There is an old adage that auditors live by “If you didn’t document it, you didn’t do it.” Items should indicate that processes are in place and that you documented that you did it.
- (3) Adhering strictly to University policy – Make sure the policy in place, or if it is a part of State procurement policy, is strictly adhered to.
- (4) System shortcoming – If detailed transactions as of June 30, which is year end, need to be reviewed, make sure the system is capable of running that detail to where date is not purged.
- (5) Communication, specifically among departments – Make sure all transactions are reported correctly and communicated through the proper channels.

The Management Letter is divided into two sections. Section I identifies findings for the year ended June 30, 2011. Section II identifies findings ended June 30, 2010. The findings in Section II were followed up on and all were responded to by Management and a status update is included to indicate the issue is being addressed. With the exception of one item, Elliott Davis was satisfied that the administration was addressing the issues.

B. FY11 Circular A-133: This is a very important part of the reporting for the University. This particular report is required under the Federal Single Audit Act. Considering the volume and amount of Federal Grant money the University receives and expends, the Single Audit Act requires that Elliott Davis tests the major programs. Elliott Davis is required to look specifically at those grant requirements to make sure the University is in compliance; that are the most significant for any given year in terms of dollars. The risk or liability there is that any one of the agencies that grants funds to the University has the latitude to perform their own oversight audit. The two largest types of grants that the University has are Research and Development, and Student Financial Aid. Elliott Davis performs an entirely separate audit on these and provides an opinion as to whether or not the University is in compliance with the major programs. Last year, there were two findings related specifically to the Recovery Act money. Many entities received funding through the Recovery Act. This was new. While some of these programs had the same objectives, there was a large volume of dollars that was circulated and there were different requirements that had to be maintained. The two findings were specific to

Recovery Act money. To put in perspective, that even though these are compliance issues that we want to make sure we adhere to, they were new and both findings were being handled with the sense of urgency and correction necessary.

C. FY11 Department of Athletics Financial Report: This audit is performed because there are two identified users, three if the Gamecock Club membership is included, who are very interested in the Athletics Department's financial statements. One of these users will be Bond Underwriters or Bond holders for revenue bonds that are issued proceeds supporting the Athletics Department. Secondly, there will be an NCAA compliance requirement that requires certain reporting be kicked up to NCAA so they are able to perform their monitoring function of the University from a financial standpoint in relation to the Athletics Department. Finally, a large part of what is included in the financial statements will relate to Gamecock Club endowments or contributed funds and that will be a group that also will be interested in fiduciary responsibility of those dollars in the financial performance of Athletics as a department within the University. What we are doing or what the administration is doing when they provide these financial reports to audit is to carve out specific accounts and funds from the University's overall general ledger. We are lifting that out of what is co-mingled in the University financial statements and breaking those out so there is a separate picture of the balance sheet and revenue and expenses of the Athletics Department. Most significant in the financial statements, since Athletics is a department of the University, is the net transfer of approximately \$12.4 million from Athletics to the General fund of the University.

A discussion ensued on how to arrange the financial report so all parties involved can understand and readily find data and comparisons in an easier read. It was pointed out that this has been a goal of the committee to make sure the information is available to each committee and each Trustee in a form that is meaningful and understandable to ensure the right decisions are made. Mr. McNeish advised he will follow up on a comparative presentation for the supplemental schedule for the revenue/expenditures and also on what can be advanced on incorporating debt and related assets.

D. FY11 Innovista Garages Financial Report and Management Letter: This audit is performed for the users of a joint venture between the University and the City of Columbia, and also to some extent, Richland County, where a capital facilities corporation was formed to essentially monitor and report on the two garage facilities. Since there is bank funding for this, an audit will be called for by the credit provider. The audit will be used initially to make a credit decision and then the audited financial statement will be used on an ongoing basis to monitor the health of what is at risk in terms of lending

money. Mr. Walton commented that initially these garages were totally off the balance sheet and recognized that it was improper. They were put on the balance sheet and a plan was established that will have these garages solvent in seven years.

E. Individual Campus Financial Reports: The internal control letter that was prepared by Elliott Davis was campuswide and any findings for the campuses are included in the first management letter discussed.

II. Internal Audits:

A. Graduate School: Mr. Iapalucci discussed the new format for the audit reports. The report began with a background section which will demonstrate that the Audit Department was well versed in the operations audited. Another section contained observations and recommendations from the Audit and Advisory Services. The last section provided exhibits and attachments that would provide reference information on the audited operation. The second document that was included with the report was an Executive Summary, or a dashboard. This document allowed Mr. Iapalucci to communicate with management what he thought in terms of the control environment, in a simplified way.

B. Tracking Report: Mr. Iapalucci distributed the Tracking Report to committee members. Considerable progress had been made on the two items reflected. This report did not include the two items from today's report, as these would be reported on the next tracking document. There was good progress but there would always be a tracking report with a couple of items.

As requested by Chairman Burroughs, Mr. Iapalucci distributed the results of the fall survey in which the Audit and Compliance Committee evaluated themselves. The results were very positive. Another survey would be conducted in the fall of 2012.

III. Review Board and President Expenditures:

These reports were accepted as information.

IV. Review Environmental Risk Management Report:

Mr. Walton introduced Mr. Tom Syfert, Associate Vice President for Health and Safety, who briefed the Committee on the overall mission of the Environmental Health and Safety (EHS) Department, which is to provide health, safety and loss control services to the University. He reviewed the main EHS programs; the compliance programs; the research safety program; projects outside of the office, such as the Rocky Branch Creek; and grants, specifically bio-diesel. He updated the committee on past accomplishments and future plans for the department.

V. Annual Review of the Committee Charter:

Mr. Walton stated that the Committee's current Charter and Matrix needed to be addressed. The Charter that the Committee operated under this year needed to be adjusted, approved and forwarded to the Board of Trustees for adoption. Mr. Walton stated that he would like the Charter reviewed between now and the next meeting. It would then be taken up for adoption. Any questions, edits, corrections and comments would be taken and incorporated into the Charter, so that the version to be presented at the next meeting would be the version to be approved.

VI. Other Matters:

There were no other matters to be brought before the Committee.

VII. Adjournment:

Since there were no other matters to come before the Committee, Chairman Burroughs called for the meeting to adjourn at 12:30 pm.

Respectfully submitted,

Amy E. Stone