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University of South Carolina
BOARD OF TRUSTEES

Audit and Compliance Committee

August 18, 2017

The Audit and Compliance Committee of the University of South Carolina met at 9:00 a.m. on Friday, August 18, 2017, in the Alumni Center's C. Edward Floyd Boardroom.

Members present were: Dr. C. Dorn Smith III, Chairman; Mr. Chuck Allen; Mr. J. Egerton Burroughs; Mr. Thomas C. Cofield; Mr. Mack I. Whittle Jr.; Mr. Charles H. Williams; and Mr. John C. von Lehe Jr., Board Chairman. Mr. Tommy Preston Jr. was absent.

Other Board members present were: Mr. A. C. "Bubba" Fennell III; Dr. C. Edward Floyd; Mr. William C. Hubbard; Mr. Toney J. Lister; Mr. Miles Loadholt; Mr. Hubert F. Mobley; Ms. Leah B. Moody; Ms. Molly M. Spearman; Mr. Eugene P. Warr Jr.; and Mr. Thad H. Westbrook.

Also present were: Faculty Senate Chairman Marco Valtorta and USC Columbia Student Government President Ross Lordo.

Others present were: President Harris Pastides; Secretary J. Cantey Heath Jr.; General Counsel Walter "Terry" H. Parham; Provost Joan T. A. Gabel; Chief Operating Officer Edward L. Walton; Chief Financial Officer Leslie Brunelli; Vice President for Student Affairs Dennis A. Pruitt; Vice President for Human Resources Chris Byrd; Vice President for Information Technology Doug Foster; Vice President for Facilities and Transportation Derrick Huggins; Vice President for System Planning Mary Anne Fitzpatrick; Chief Communications Officer Wes Hickman; Executive Director of Audit & Advisory Services Pam Doran; Palmetto College Chancellor Susan Elkins; USC Beaufort Chancellor Al Panu; USC Upstate Chancellor Brendan Kelly; Athletics Director Ray Tanner; University Treasurer Pat Lardner; College of Arts and Sciences Dean Lacy Ford; College of Pharmacy Dean Stephen J. Cutler; Associate Vice President & Chief of Police Chris L. Wuchenich; Executive Director of Economic Engagement William D. "Bill" Kirkland; Deputy Provost Helen Doerpinghaus; Audit & Advisory Services Assistant Director Glenn Murray; Audit & Advisory Services IT Audit Manager Roscoe Patterson; Chief Diversity Officer John H. Dozier; Community Relations, Law Enforcement and Safety, Captain Eric Grabski; Associate Director of Public Relations, Office of Communications and Public Affairs, Jeff Stensland; Executive Director of My Carolina Alumni Association Jack W. Claypoole; USC Aiken Executive Vice Chancellor for

Academic Affairs Jeff Priest; Fluor Corporation Chairman and Chief Executive Officer David T. Seaton who serves as a strategic advisor to the Board; Brian D'Amico and Tom McNeish, with Elliott Davis Decosimo; University Technology Services Production Manager Matt Warthen; and Board staff members Debra Allen and Terri Saxon.

I. Call to Order

Chairman Smith called the meeting to order, welcomed those in attendance including the University's strategic advisor Mr. David Seaton, and asked everyone at the table to introduce themselves.

Mr. Hickman introduced Avery Wilks with *The State*.

Chairman Smith stated the agenda had been posted and the press notified as required by the Freedom of Information Act; the agenda and supporting materials had been circulated to the committee members; and a quorum was present to conduct business.

II. Elliott Davis Decosimo – Budget Comparison Project Update

Chairman Smith called on Mr. Brian D'Amico from Elliott Davis Decosimo (EDD). First, Mr. Tom McNeish discussed key points of the project. He said the objectives of the two illustrative reports are to convert the University's budget to a Generally Accepted Accounting Principles (GAAP) based budget and to generate reporting on a responsibility unit-level. The allocation methodologies used to develop the reports include numerous approaches that require the use of estimates and assumptions; implementation of the budget model will require disseminating to major stakeholders, and it should include education and acceptance.

Mr. D'Amico discussed the significant reclassifications and adjustments required to generate a GAAP budgetary comparison: student fees for debt service, reclassification of scholarship allowance and of indirect cost recovery, athletic ticket bond fees for debt service, GASB 68 – Pension Liability, depreciation, interest on debt service, state capital appropriations, capital grants and gifts. The estimated GAAP adjustments change in the University's net position is \$16,974,878.

Mr. D'Amico stated revenues and expenses related to specific revenue generating units were recorded in USC Columbia administrative units, and these amounts have been directly allocated to their revenue generating units. Significant direct allocations include: graduate scholarships and abatements; interest expense for athletics, parking, the Darla Moore School of Business, and the Law School; bond fees for athletics; reversal of institutional administration charges to auxiliaries and campuses; moving activity in the administration unit CL061 (Institute for Families in Society) to Social Work; state capital appropriation and capital gifts and grants awarded for specific unit projects; reversal of indirect cost recovery allocated to

revenue generating and administrative units; and capital purchases made by revenue generating units, but reversed out of administrative units.

Significant allocation revenue drivers include student tuition, fees and scholarship allowance.

Undergraduate is allocated in two ways: 70% based on undergraduate credit hours; 30% based on undergraduate headcount by major. Graduate programs have significantly different rates and are allocated 100% based on University Tuition Analysis Report (TAR).

Other significant revenue drivers include State grants and contracts, and state appropriations in which undergraduate resident (in-state) credit hours are used. Non-operating federal grants and contracts are based on undergraduate credit hours.

Significant expense drivers include salaries and wages, fringe benefits, services and supplies. These drivers are combined for each administrative unit and allocated using the same driver, that is determined based on the unit's function. Examples of drivers include: total credit hours, total Full Time Equivalent (FTE) for students and employees, and square footage.

Another significant expense driver is depreciation. Direct depreciation is allocated based on actual current year depreciation expense for the academic and auxiliary unit's buildings and land improvements. Indirect depreciation for administrative buildings and all equipment was allocated using a combination of drivers: 80% based on total FTE and 20% based on square footage.

The utilities expense of \$18 million was allocated based on square footage.

At the beginning of the presentation, Mr. D'Amico provided the Trustees a draft alternative budget summary document to view, and collected it after the meeting.

Mr. D'Amico responded to Trustees' questions and Ms. Brunelli clarified responses as needed.

Chairman Smith stated the update was received as information. He asked EDD to prepare a more detailed budget comparison of Athletics and the Darla Moore School of Business. Mr. Burroughs asked for University Administration to be the third focus. Mr. D'Amico said he would present his findings at the Committee's meeting on March 16, 2018; as he was scheduled to present the FY financial statements at the meeting on October 12, 2017.

III. IT Governance and Initiatives

Chairman Smith called on Mr. Foster, who discussed aligning information technology (IT) supply versus demand. To do so, he and his staff considered the following five questions:

- Are we investing in the right things?
- Are we optimizing our IT capacity?
- What value do we derive?

- How are IT investment decisions made?
- What is the “right” level of IT investment?

Mr. Foster said he divided the IT investment portfolio into three tiers: 80% support, 15% optimization, and 5% strategic. The IT challenge is to increase strategic investments while maintaining support. He discussed the complexity of higher education IT governance and initiatives, in which investment choices affect support services.

Mr. Foster discussed the creation of an IT governance model to include three tiers: to advise, research and propose; to review, approve and prioritize; and an executive steering committee to solve conflicts, prioritize and approve complex projects.

Mr. Foster reported on current IT projects: PeopleSoft HR/Payroll implementation; multi-factor authentication; Microsoft Cloud email (faculty/staff); high performance computing; redesigning the IBM partnership; and IT Division reorganization.

Trustee Fennell asked if the University’s IT disaster recovery plan efforts, as noted in a recent internal audit, were on track for completion by December 2017. Mr. Foster responded yes and said he and his staff were exploring options to address disaster recovery issues.

Chairman Smith asked for an update on the PeopleSoft implementation final phase timeline. Mr. Foster said the HR/Payroll component implementation is expected by January 2019, with the Time and Attendance implementation six-months thereafter. Chairman Smith asked Mr. Foster if he anticipated “Banner going away,” once the PeopleSoft implementation is complete. Mr. Foster responded that if the Board was making the software decision today, they might make a different choice. He said the issue at hand is that with so much institutional investment (seven-ten years) in the project, it would be very challenging to unwind it.

Chairman Smith asked Mr. Foster for his thoughts on the University’s hybrid relationship with IBM. Mr. Foster said he did not think “a total outsourcing in big bites made sense.”

Chairman Smith asked Mr. Foster to comment on how the University compared to their peers in cyber security. Mr. Foster noted the University’s IT complexity didn’t help, but that he and his staff were working to simplify it. The good news, he said, was that the University’s security program is the best he has seen and is highly confident in the staff.

Chairman Smith stated the report was received as information.

IV. Internal Audits/Reviews

A. Clery Act Reporting Audit Report

Ms. Doran said in 1990, Congress enacted the Crime Awareness and Campus Security Act, which in 1998, was renamed the Jeanne Clery Disclosure of Campus Security Policy and Crime Statistics Act. The Act requires colleges and universities participating in federal financial aid to report crime statistics and security information. In 2013, the Violence Against Women Reauthorization Act; added dating violence, domestic violence, sexual assault and stalking to the reportable standards.

The Department of Education's Office for Civil Rights enforces the Clery Act. Components of the Act include: daily crime log; collection and classification of crime statistics; annual security and fire safety report; annually reported crime statistics to the U. S. Department of Education; warnings and emergency notifications; missing student notifications; and fire safety information and educational programs for students and staff; and institutional disciplinary action procedures.

In April 2017, the Department of Education announced increased Clery Act fines to \$54,789 per violation. The largest fine imposed to date is \$2.4 million.

Ms. Doran reported that Audit & Advisory Services (AAS) determined the University was properly managing compliance with the Clery Act within the audit scope. One recommendation regarding the reportable geographic area was noted. AAS recommended Law Enforcement, and they agreed, annually obtain a list of University owned and leased property from Facilities.

Chief Wuchenich responded to Mr. Lordo's questions about the Clery Act campus/off-campus definitions.

Chairman Smith stated the report was received as information.

B. Tracking Report

Ms. Doran said the Tracking Report summary table showed there were 33 outstanding recommendations when the committee met in June 2017, with six of those recommendations implemented, 14 not yet due and 13 deferred. Details of the deferred recommendations, she said, were provided in the report.

V. Audit & Advisory Services

A. Institute of Internal Auditors (IIA) Standards Overview

Ms. Doran said the IIA International Standards for the Professional Practice of Internal Auditing (Standards) require internal audit activities to develop and maintain a Quality Assurance and Improvement Program covering all aspects of the activity. The three program components are:

- Ongoing Monitoring: includes day-to-day supervision, review and measurement of AAS's activity, and conducting client surveys.
- Periodic Assessments: includes a self-assessment activity; and a leadership survey during University Risk Assessment.
- External Assessments: to be conducted once every five years by a qualified external assessor or assessment team. Ms. Doran noted AAS has planned for one in 2018, and that it will be the University's first.

Discussion ensued regarding the selection of the peer group to perform the external assessment. Chairman Smith said he would discuss the selection of the external assessment team and the cost with Ms. Doran, then bring a recommendation to the committee for their consideration.

Ms. Doran reported that in preparation of an external assessment in 2018, AAS staff performed a self-assessment, including the review of the function's compliance with the Standards to determine where additional attention is warranted. She discussed the two major categories of the Standards:

Attribute Standards: address the attributes of organizations and individuals performing internal auditing (e.g. organizational independence, individual objectivity, proficiency, and due professional care).

- Standard 1000 – Purpose, Authority and Responsibility
- Standard 1100 – Independence and Objectivity
- Standard 1200 – Proficiency and Due Professional Care
- Standard 1300 – Quality Assurance and Improvement Program

Performance Standards: describe the activities performed by internal auditing and provide quality criteria against which the performance of these services can be measured.

- Standard 2000 – Managing the Internal Audit Activity
- Standard 2100 – Nature of Work
- Standard 2200 – Engagement Planning
- Standard 2300 – Performing the Engagement
- Standard 2400 – Communicating Results
- Standard 2500 – Monitoring Progress
- Standard 2600 – Communicating the Acceptance of Risks

Ms. Doran reported that the External Assessment will report one of three conclusions:

Generally Conforms – Internal audit function has a charter, policies and processes, and the execution and results of these are judged to be in conformance with the Standards.

Partially Conforms – Deficiencies in practice are judged to deviate from the Standards, but these deficiencies did not preclude the function from performing its activities.

Does Not Conform – Deficiencies in practice are judged to be so significant that they seriously impair/preclude the function from performing adequately in all or in significant areas of its responsibilities.

B. Quality Assurance Self-Assessment Report

The overall conclusion of AAS's self-assessment was Generally Conforms (the highest rating for a Quality Assurance Review). Ms. Doran shared some of the assessment comments.

The following assessment recommendations were made:

- Update and strengthen the Charter (Policy BTRU 1.06, Audit & Advisory Services)
- Establish ongoing self-assessment activities and metrics
- Complete an external assessment
- Formalize and document the risk assessment performed in years 2 and 3, of the 3-Year Audit Plan

C. Annual Report

Chairman Smith called on Ms. Doran who said the Annual Report summarizes the items the Standards require her to communicate to the committee. The mission of AAS, which reports directly to the Audit and Compliance Committee of the Board of Trustees, she said, is to enhance and protect organizational value by providing risk-based and objective assurance, advice, and insight. To do so, AAS follows the mandatory guidance of the International Professional Practices Framework (IPPF) provided by Institute of Internal Auditors, which includes: Core Principles for the Professional Practice of Internal Auditing; Definition of Internal Auditing; Code of Ethics, and International Standards for the Professional Practice of Internal Auditing (Standards). AAS's charter is documented in University Policy BTRU 1.06 Audit & Advisory Services and its values include: integrity, objectivity, confidentiality, competency, and insightfulness.

Ms. Doran reported AAS's FY 16-17 Goals were accomplished with 79% of AAS's effort focused on providing assurance and advisory services in performing audits, investigations, advisory reviews and internal control training. Those goals are:

- Raise awareness of stewardship responsibilities and lead internal control practices.
- Provide assurance that the University's high priority risk areas, within AAS' purview, are appropriately managed by performing assurance audits prioritized in the Audit Plan.
- Establish a high quality and value-added internal audit service organization.

Risk based audits, from the Audit Plan approved by the committee, represented 63% of this effort; followed by 12% audit support; 9% advisory activities; 9% professional development; 6% investigations; and 1% training the University community.

Ms. Doran reviewed the FY 2016-17 list of completed and in-progress audits, and the audit topics proposed for the following three fiscal years. Most notable for FY 17-18, will be efforts to raise awareness of ethics, governance, risk management and internal controls; increase AAS committee participation; and

start an AAS newsletter to communicate best practices, internal controls, and stewardship. In addition, Ms. Doran said AAS would focus on completing and implementing the staff Conflict of Interest Disclosure Process and Code of Conduct. Just as important, she noted, was the need to place greater emphasis on employee satisfaction to recruit and retain high performing personnel.

Ms. Doran reported on the personnel qualifications of her team that included, six audit staff and an administrative coordinator. All seven AAS staff have bachelor's degrees and two have master's degrees, in addition to various certifications.

Trustee Fennell expressed congratulations to Ms. Doran for having represented the University well as President of the Association of College and University Auditors.

Chairman Smith stated the Annual Report was provided on the Board Portal and received as information.

VI. Audit and Compliance Committee Matrix Review

Ms. Doran informed the committee an updated matrix had been provided on the Board Portal. She said the committee had completed all business items listed for FY 2016-17.

Trustee Fennell and others asked Ms. Doran if she had the resources needed to continue her successful efforts. Discussion ensued and Chairman Smith said he is in contact with Ms. Doran and will inform the committee of needs as they arise.

Chairman Smith thanked Ms. Doran for her informative presentation.

Chairman Smith said there was a personnel matter, the annual performance evaluation of the Executive Director of Audit and Advisory Services (AAS) appropriate for discussion in Executive Session. He called for a motion to enter Executive Session. Mr. Whittle so moved and Mr. Williams seconded the motion. The vote was taken and the motion passed.

Chairman Smith invited President Pastides, Secretary Heath, and Mr. Byrd to remain.

EXECUTIVE SESSION

RETURN TO OPEN SESSION

VII. Executive Director of Audit and Advisory Services Annual Performance Evaluation

Chairman Smith called for a motion to recommend the full Board increase Ms. Doran's salary by 5%. Mr. Williams so moved and Mr. Allen seconded the motion. The vote was taken and the motion carried.

VIII. Other Matters

Chairman Smith called for any other matters to come before the committee. There were none.

IX. Adjournment

As there were no other matters to come before the committee, Chairman Smith called for the meeting to adjourn at 10:40 a.m.

Respectfully submitted,

J. Cantey Heath, Jr.
Secretary