

# **BOARD OF REGENTS**

## **EASTERN MICHIGAN UNIVERSITY**

SECTION: 2

DATE:

March 21, 2006

### **RECOMMENDATION**

#### **REPORT: INTERNAL AUDIT**

##### **ACTION REQUESTED**

It is recommended that the Internal Auditor's activity report for the period February through March 2006 be received and placed on file.

##### **STAFF SUMMARY**

The reports for the internal audit review of the University Relations department and internal audit review of information systems general and application controls of the Information and Communications Technology division have been issued. The reports include findings and corresponding recommendations to improve controls. The recommendations have been discussed with the appropriate personnel. Management agrees with the recommendations and is proceeding with actions to implement the recommendations. Rehmann Robson is satisfied that management's responses will satisfy the intent of the recommendations.

Also attached is the report for the Conflict of Interest review in accordance with University Policies 3.1.6.1, 3.1.6.2, and 3.1.6.3. Any potential conflicts were to be documented on the disclosure statement by the individual. Five disclosures were submitted. Rehmann Robson evaluated the five disclosure statements and consulting with University general legal counsel, Rehmann Robson concluded that there does not appear to be any substantial or material conflict of interest based on the information disclosed.

Also attached is the report prepared by University management on the status of audit recommendations made from the Physical Plant – Design/Build Contractor audit. As noted in the report, management has agreed with the internal auditor's recommendations and all of the recommendations have been fully implemented.

An updated internal audit activity schedule for the period ending September 30, 2006 is included with the report.

##### **FISCAL IMPLICATIONS**

The projected expenditures for Rehmann Robson are within approved budget limitations.

##### **ADMINISTRATIVE RECOMMENDATION**

The proposed Board action has been reviewed and is recommended for Board Approval.

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University Executive Officer

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Date



# REHMANN ROBSON

*Certified Public Accountants*

*A member of THE REHMANN GROUP*

*An Independent Member of Baker Tilly International*

**Date:** February 16, 2006

**To:** Mr. Joseph E. Antonini  
Board of Regents

**From:** Rehmann Robson

**Re: AUDIT REPORT  
UNIVERSITY RELATIONS**

Attached is the report for the internal audit review of the University Relations Department. Responses from the Interim Director of Finance and Treasurer to the Board of Regents have been incorporated in the report.

There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention of overriding controls. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to the prevention or detection of errors. Furthermore, because of changes in conditions, the effectiveness of internal control may vary over time. Any questions, comments, or concerns that you may have relative to this report can be directed to Kirk Balcom at (517) 841-4876.

Your cooperation with this request and assistance and support provided during this audit is appreciated.

Attachment

cc: Board of Regents  
Dr. John A. Fallon, III  
Mr. Steven Holda  
Mr. Daniel Cooper

**Internal Audit Report**  
**University Relations**  
**February 16, 2006**

Rehmann Robson has completed an audit of the former University Relations Division. The purpose of the audit was to determine whether University Relations internal controls are designed effectively and operating effectively. We used the Committee of Sponsoring Organizations (COSO) internal control framework to evaluate the controls. COSO is a voluntary private-sector organization dedicated to improving the quality of financial reporting through business ethics, effective internal controls and corporate governance. The COSO framework defines five internal control components that we used as a basis of our evaluation:

- Control Environment
- Risk Assessment
- Information and Communication
- Control Activities
- Monitoring

We sample tested payroll, procurement credit card purchases, business expense reimbursements, contracted services, and journal entries processed for funding allocations.

In our opinion, internal controls were generally designed and operating effectively.

University Relations was comprised of five major business units including University Relations which performs community and government relations work; Charter Schools Office, which serves as fiscal agent for the charter schools, reviews and recommends new charters and new school board members to the Board of Regents, and provides oversight and evaluation of all charter schools, including monitoring of fiscal matters, educational objectives, state and federal compliance and school board training; WEMU-FM Radio which broadcasts 24 hours every day and participates in the educational and public purposes of the University; Institute for Community and Regional Development (ICARD) which promotes public service, civic engagement and community outreach on behalf of the University through applied research and training activities; and Convocation Center which is responsible for the daily operations of the Convocation Center, a 9,500-seat multi-purpose facility used for University commencement, athletics, and rentals. It is also responsible for Pease Auditorium, a 1,500-seat performing arts theater, and Ticket Operations, located at the Convocation Center, Pease Auditorium, and Quirk Theater that also includes telephone and Internet ticket selling capabilities.

The University Relations Division had numerous financial funds. The major funds and their expenditures year-ended June 30, 2005 included University Relations General Funds (\$2.7 million), WEMU-FM Radio General Funds (\$601,000), Charter Schools Designated Funds (\$762,000), WEMU-FM Radio Designated Funds (\$586,000), ICARD Designated Funds (\$274,000), Convocation Center Designated Funds (\$1.1 million), WEMU-FM Radio Expendable Restricted Funds (\$193,000), and ICARD Restricted Funds (\$560,000).

We found that University Relations was being managed in a reasonable manner consistent with University Policies and Procedures. We do note, however, that the ICARD Designated Funds balance deficit should not have been allowed, and either the program should have been curtailed to operate within the revenue available, or the General Fund support should have been increased to allow operations to continue without creating a deficit fund balance.

We have also noted a few recommendations to strengthen University-wide internal controls that came to our attention in the course of the audit. We sincerely appreciate the excellent cooperation and assistance extended to us by University Relations management and employees and the Controller's area during the internal audit. Those recommendations are as follows:

1. Effective practices for controlling employee use of P-Cards should include ensuring that all activity is reviewed and approved by the cardholders' supervisor, documenting the business purpose for each expense, and retaining original receipts for all purchases made. The University is in the process of establishing guidelines for what is a legitimate business purchase and implementing an online review and approval process for monthly P-Card activity.
2. The Banner System is capable of including budgets. Without budget information entered in Banner there is no centralized control of budget shortfalls. While we recognize that business units do use their own internal budget processes, centralized control and roll up reporting of budgets to the Vice Presidential level or above is more accurate and more efficient through Banner. Explanations of budget variances can then be acted upon in a timely manner. The University is in the process of implementing budgets on Designated Fund accounts.
3. Designated funds have a specific purpose with expected revenues and expenses. Occasionally external risk factors such as the state economy and state appropriations can lower actual revenues obtained or increase expenses incurred. A specific risk assessment, along with action plans for each designated fund, that address the financial impact of those external risks is not prepared. The University should perform a risk assessment for each designated fund, over a University established dollar threshold, at the funds origin and have it updated annually. Action plans that will be implemented to stop deficits should also be included. Vice President or above approval of the risk assessment should be obtained. Management will emphasize to all University departments that contingency plans should be developed to respond to unexpected decreases in their revenue streams.

Our finding, risk analysis, recommendation and management's response relating to the audit of the University Relations Division is listed below.

### ***Finding***

ICARD sustained another annual combined operating deficit, for their 11 Designated Funds, bringing their deficit fund balance total to (\$568,478) after \$150,000 was transferred from the fund balances of University Relations, WEMU and the Convocation Center in fiscal year 2005 through journal entries. The journal entries received business unit approval. Two of the journal entries totaling \$100,000 were reversed in 2006 and the funds returned to WEMU and the Convocation Center for their internal reserves. The remaining \$50,000 which was transferred from University Relations General Fund surplus for 2005 was not reversed.

The Convocation Center has a surplus of \$223,194 for its four designated funds. The Convocation Center sustained an annual operating deficit for two of their four designated funds bringing the deficit fund balance for these two funds to (\$61,282) after \$106,000 was transferred from the fund balances of the other two Convocation Center designated funds with a surplus of \$201,114 and \$83,362 after the transfers. The journal entries received business unit approval.

### ***Risk***

There is substantial risk that University General Fund revenues (State appropriation, Tuition and fees) are being allocated to designated funds that were not intended to receive the funding.

### ***Recommendation***

We recommend that a Vice President or above, Budget Director, and Controller each approve deficit funding journal entries.

### ***Management's Response***

Management agrees. We will recommend that future deficit funding journal entries require approval by both the Divisional Vice President and the Vice President of Business and Finance. In case the Division of Business and Finance desires to make a deficit funding journal entry, the Vice President of Business and Finance and the President must approve the entry.

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# REHMANN ROBSON

*Certified Public Accountants*

*A member of THE REHMANN GROUP*

*An Independent Member of Baker Tilly International*

**Date:** March 2, 2006

**To:** Mr. Joseph E. Antonini  
Board of Regents

**From:** Rehmann Robson

**Re: AUDIT REPORT  
INFORMATION COMMUNICATIONS AND TECHNOLOGY**

Attached is the report for the internal audit review of information systems general and application controls of the Information Communications and Technology Division. Responses from Information Communications and Technology have been incorporated in the report.

There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention of overriding controls. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to the prevention or detection of errors. Furthermore, because of changes in conditions, the effectiveness of internal control may vary over time. Any questions, comments, or concerns that you may have relative to this report can be directed to Kirk Balcom at (517) 841-4876.

Attachment

cc: Board of Regents  
Dr. John A. Fallon, III  
Dr. Donald A. Loppnow  
Dr. Connie J. Schaffer  
Mr. Steven Holda  
Mr. Daniel Cooper

**Internal Audit Report**  
**Information Communications and Technology**  
**March 2, 2006**

Rehmann Robson has completed an audit of information systems general controls and application controls of the Information Communications and Technology (ICT) Division. General controls are pervasive control activities that help ensure the integrity of the computing environment including policies and procedures, risk assessment, program change, computer operations, and access to programs and data. Application controls are control activities that are embedded in business processes that help ensure completeness, accuracy, validity, authorization, and segregation of duties of transactions processed.

The purpose of the audit was to determine whether information systems general and application controls are designed effectively and operating effectively. We used the Control Objectives for Information and related Technology (COBIT) framework to evaluate controls design. COBIT is a worldwide-recognized framework that helps management understand and manage risks associated with information technology.

In our opinion, general and application controls are designed and operating effectively.

The information systems are run on numerous Unix, Linux, or Windows servers. The key business applications including General Ledger, Purchasing, Accounts Payable, Human Resources, Payroll, Student Management, Accounts Receivable, and Financial Aid are processed by SCT Banner. Two key outsourced services include an on-line billing and payment system and a financial aid refund processing system.

A few recommendations to strengthen general and application controls are discussed below in order of significance, along with ICT management's responses to those recommendations. We sincerely appreciated the excellent cooperation and assistance extended to us by the ICT management team during the internal audit.

**Finding 1**

A formal information technology (IT) risk assessment has not been performed and documented. An IT risk assessment consists of identifying all IT related risk elements for the University, analyzing current control activities which may mitigate risks, and understanding the resulting residual, or unmitigated, IT risks.

***Risk***

Without an appropriate IT risk assessment, University and ICT management may not have a full understanding of the overall IT risk exposure, or the IT internal control environment and its effectiveness. In addition, the IT risk assessment can provide key input when designing the ICT strategic plan.



### ***Recommendation***

Perform an initial IT risk assessment and establish an ongoing process to update the risk assessment on an annual basis. This risk assessment should also be reviewed and approved annually by the Board.

### ***Management's Response***

Agree. A Risk Assessment will be prepared as part of the University's Business Continuity Plan. A Request for Proposal (RFP) has been prepared for the Business Continuity Plan (BCP) and includes an ICT Risk Assessment. The RFP has been reviewed with Purchasing and Controller's Office. Purchasing is in the process of soliciting bids for the BCP.

### ***Finding 2***

End-user access to University computer systems, including the network and Banner, is not being reviewed on a periodic basis.

### ***Risk***

End-user access to computer systems can be very dynamic due to new hires, terminations, job changes and system upgrades. These changes may result in unauthorized or inappropriate access. Periodically reviewing access helps ensure that each end-users' access is properly authorized and appropriate for their job function.

### ***Recommendation***

Formal end-user access templates should be created by system owners, and with ICT oversight, that detail the specific access required for each job function. The templates should be the basis for authorizing access. The templates should also specifically identify conflicting Banner functions that must be separated in order to ensure appropriate segregation of duties. Then, using these templates as the baseline, at least an annual review of end-user access should be coordinated by ICT.

### ***Management's Response***

Three projects have been initiated to address Finding #2. The projects are: Implement Security Audit System, Implement Workflow for Security Processes, and Implement a Security Tracking System. A functional security team is already established. This team will review security access yearly. Additionally, this team will document banner forms that should never be assigned to the same person.



### **Finding 3**

ICT has made significant progress toward establishing a comprehensive set of formal IT policies and procedures, and communicating them across the University through the ICT intranet. However, several critical policies and procedures have not been completed including:

- A comprehensive security plan and program
- User access administration
- Security event logging and review
- Program change management
- End user computing
- Job scheduling and process monitoring

### ***Risk***

Formal policies and procedures serve as the basis for communicating workflows, key activities, goals and expectations for each functional area. In addition, documented procedures ensure that knowledge of how processes and functions are performed is retained when key employees terminate or transfer to new roles.

### ***Recommendation***

Formal written policies and procedures related to the areas identified above should be created and communicated to appropriate personnel.

### ***Management's Response***

ICT has an active team continuously addressing policy and procedure needs that affect the institutions operations. The auditors' identified policies and procedures are a current focus of the team.

### **Finding 4**

The data center housing critical University computing infrastructure is located in a secured room with three methods of access. The computer room doors can be accessed via metal key locks, numeric combination locks and card key. The metal key locks and numeric combination locks do not provide the ability to monitor access to the computer room.

### ***Risk***

Without the ability to monitor computer room access, ICT management may be unable to detect unauthorized access and modification to critical computing infrastructure.

### ***Recommendation***

Expand the card key access system to all computer room doors and have card key access the main access method. Use metal keys only for emergency situations such as power outages and eliminate combination locks for accessing the computer room.

### ***Management's Response***

Agree. The auditor's recommendation will be implemented as a part of the campus-wide security project.

### **Finding 5**

The ability to recover critical University data from the daily backups is currently not being verified through periodic testing of the data restoration process.

#### ***Risk***

The University may not have the ability to timely restore critical data in the event of a system failure.

#### ***Recommendation***

Establish a formal policy and procedure to perform tests of data restores on a periodic basis.

#### ***Management's Response***

A part of the Business Continuity Plan is the identification of required testing for the recovery process. This includes periodic testing of the data restoration process. ICT will create a formal policy and necessary procedures defining this testing of data restores.

### **Finding 6**

The on-line billing and payment system has been outsourced to a third party service provider without obtaining an independent evaluation of the service providers internal control environment.

#### ***Risk***

Confidential student financial information may be inappropriately disseminated or altered if the third party service provider has not implemented an effective system of internal controls.

#### ***Recommendation***

Obtain a SAS 70 or other independent evaluation of the internal control environment for all third party service providers used by the University.

#### ***Management's Response***

Agree. A SAS 70 will be obtained from the University's provider.

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# REHMANN ROBSON

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**Date:** February 21, 2006  
**To:** Mr. Joseph E. Antonini  
Board of Regents  
**From:** Rehmann Robson  
**Re:** **AUDIT REPORT**  
**CONFLICT OF INTEREST**

We have completed our Conflict of Interest review in accordance with University Policies 3.1.7, Conflict of Interest: University Employees, 3.1.6.1, Reporting Relationships, 3.1.6.2, Supplemental Employment – Non-Bargained for Employees, and 3.1.6.3, Use of Facilities by Private Research and Consulting. Our objective was to evaluate adherence to the policies based on disclosures received. The scope of our review included 173 Administrative and Professionals (AP) and six Professional Technicals (PT) who are not covered under the existing policy, but who function as purchasing agents or construction supervisors who influence purchasing and contracting. The Assistant Vice President and Controller met with Human Resources and the PT union leadership and received permission to have the PTs fill out the conflict of interest disclosure.

We distributed a copy of the conflict of interest policies and a disclosure statement to each individual and requested they return the disclosure statement with their signature acknowledging their understanding and adherence to the policy. Any potential conflicts were to be documented on the disclosure statement by the individual. Five returned disclosure statements with disclosures.

We independently evaluated the five disclosure statements and consulted with University general legal counsel. We concluded that there does not appear to be any substantial or material conflicts of interest based on the information disclosed.

There are inherent limitations in the effectiveness of any system of internal control, including the possibility of human error and the circumvention of overriding controls. Accordingly, even an effective internal control system can provide only reasonable assurance with respect to the prevention or detection of errors. Furthermore, because of changes in conditions, the effectiveness of internal control may vary over time. Any questions, comments, or concerns that you may have relative to this report can be directed to Kirk Balcom at (517) 841-4876.

cc: Board of Regents  
Dr. John A. Fallon, III  
Mr. Steven Holda  
Mr. Daniel Cooper

**Eastern Michigan University Internal Audit Schedule**  
**Rehmann Robson**

For Period Ending September 30, 2006

<u>Internal Audit</u>	<u>Completed or Start Date</u>	<u>Budget Hours</u>	<u>Actual Hours</u>
Physical Plant - Construction	Completed Oct 2005	100	98
Conflict of Interest	Completed Feb 2006	32	23.5
Information Systems - General Controls and Application Controls Review	Completed Mar 2006	120	113.5
Dining Services	Postponed	120	0
Financial Aid	Feb 2006	60	74.5
Payroll	Apr 2006	120	0
Benefit Administration	May 2006	120	0
Equipment Inventory	Jun 2006	40	0
Catering and Conferences	Jun 2006	60	0
Tuition and Fees	Jul 2006	120	0
Regulatory/Compliance	Aug 2006	100	0
Vending Operations	Aug 2006	24	0
Sarbanes-Oxley	Ongoing	184	26.5
Planning, Risk Analysis, and Administration	Ongoing	100	21.3
Special Projects			
- Audit Design Build Contractor Related to Construction Audit	Completed Dec 2005	40	32
- University Relations Audit	Completed Feb 2006	60	136.5
Contingencies	Oct 2005	100	0
<b>Total Hours</b>		<u><u>1,500</u></u>	<u><u>525.8</u></u>
<b>Contracted Rate Per Hour</b>		<b>\$80</b>	<b>\$80</b>
<b>Total Fees</b>		<u><u>\$120,000</u></u>	<u><u>\$42,064</u></u>

# STATUS OF AUDIT RECOMMENDATIONS

March 21, 2006

**Physical Plant – Design/Build Contractor**

Prepared by  
Vice President for Business and Finance Office

## INTERNAL AUDIT RECOMMENDATION STATUS

**AUDIT PERFORMED:** PHYSICAL PLANT – DESIGN/BUILD CONTRACTOR

**DATE COMPLETED:** DECEMBER 20, 2005

### 1. Recommendation:

We recommend that the design build contractor provide actual salaries of the project accountants and cost engineers. Any overcharges would have inflated the general conditions portion of the GMP. Therefore, the effect of these overcharges on the calculation of the general conditions portion of the GMP should be reflected as a reduction to the GMP, via a change order, so that 100 percent of the overcharge accrues to the University.

#### Management's Response:

Management requested the audit to determine if any overcharges existed in the General requirements and general conditions and to assure future charges are compliant. We agree that any verified overcharges should be returned to the University via a change order.

#### Implementation Status:

EMU has requested the accounting rate breakdown from the design/build contractor, which in turn has supplied EMU with inadequate information. EMU has since requested this information again. Until this information is adequately provided, EMU will not approve this portion of the monthly invoices. Further developments of this recommendation will be addressed at future board meetings.

Verification Date: February 16, 2006

### 2. Recommendation:

Obtain actual salaries and time worked each month and recomputed the invoice.

#### Management's Response:

Management agrees with the finding that this verification is necessary. For all future invoices EMU will request to receive the details by month for each invoice for actual cost verification. A spreadsheet has been developed to allow for clear review and comparison. In accordance to the part 2 Agreement, the contractor is expected to work overtime, multiple shifts or take any other action necessary in order to meet the Master Project Schedule and achieve Substantial Completion of the work within the contract time. Except as otherwise provided for in the Agreement, the cost of such action will be borne solely by the contractor and will not entitle the contractor to an increase in the contract price unless due to University's fault. If the University reasonably believes the work is not progressing fast enough to insure completion within the contract time, the contractor will be required to work such additional shifts and overtime, if in the reasonable opinion of the University it is necessary to complete the work on the required date without extra cost to the University. Verification will be completed to assure contract compliance is in place.

Implementation Status:

The design/build contractor has supplied EMU with the appropriate breakdown of hours worked and salary amounts. These numbers are accurately verified against the monthly invoices.

Verification Date: February 16, 2006

Audit recommendations verified by:

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Todd Ohmer

Interim Assistant to the VP for Business and Finance