University of Maine System
Board of Trustees
at the University Maine System, Rudman Board Room
May 17, 2013

Audit Committee

Present at USM: Committee Members: Kurt Adams, Chair; and Mark Gardner. System Staff: Tracy Elliott. Other Participants: Renee Bishop – BerryDunn, and Sarah Belliveau - BerryDunn.

Present at UMS: Committee Members: Norman Fournier. System Staff: Janis Manning, Darla Reynolds Kelley Wiltbank, and Rebecca Wyke. Guests: Janet Waldron - UM, Amanda Butterfield – BerryDunn and Sue Randall – UM.

Present by Phone: Committee Members: Samuel Collins.

Committee Members Absent: Michelle Hood and Marjorie Medd

Trustee Adams called the meeting to order and thanked everyone for participating.

OMB Circular A-133 Audit Fiscal Year 2012.

Ms. Renee Bishop, Ms. Amanda Butterfield and Ms. Sarah Belliveau from Berry Dunn McNeil & Park, outlined the highlights of the FY2012 audit. The UMS Federal expenditures were $317 million for FY2012, of which $216 million was for student financial assistance. The total federal expenditures decreased by $19 million from the prior fiscal year, but included a $1 million increase in student financial assistance. The $19 million decrease from FY2011 to FY2012 related to American Recovery and Reinvestment Act (ARRA) funding and is primarily the result of a $6.5 million decline in the ARRA State Fiscal Stabilization Fund and the FY2011 expenditures of $10.3 million for a one-time ARRA National Institute of Standards and Technology Construction grant received by UMaine. The external auditors issued a favorable (unqualified) opinion on compliance. They identified no material weaknesses or significant deficiencies in internal controls, no instances of noncompliance, and no findings or questioned costs.


Risk Based Audit Approach

The audit approach for FY2013 will emphasize assessing risk by financial statement assertion in order to focus the audit work towards areas that are more sensitive and/or have the greatest risk of material misstatement. Investigative and analytical auditing procedures will be used to help gain an understanding of policies, procedures and responsibility reporting/accountability. An understanding of significant internal control systems, documenting the systems (from interviews and observations) and walking through certain transactions within each system will be used to ascertain if the understanding and documentation are accurate. After an evaluation of internal controls, the external auditors will identify the major areas of strength and areas for opportunities within the internal control systems and design the audit procedures accordingly. Heavy emphasis will be placed on analytical procedures such as industry comparisons and budget variance analysis, as well as the analysis of relationships between the expected and actual results.

Significant Audit Areas

The following will initially be assessed as significant areas of focus for the 2013 audit:

• Cash
• Investments, including deposits with bond trustees
• Accounts receivable and revenue *(primarily related to collectability and revenue recognition)*
• Grants receivable and related revenue
• Capital assets *(primarily related to capital projects started or finished in 2013)*
• Accounts payable and accrued expenses
• Payroll expense and related accrued liabilities, including pension and other retirement benefit obligations
• Indebtedness
• Federal financial assistance programs (OMB Circular A-133)

It is anticipated that the time needed to complete the audit will be approximately 950 hours for the financial statement audit and 370 hours for the A-133 audit.

**Significant Accounting Estimates and Judgments Made by Management**

Accounting estimates, based upon management's judgments, are an integral part of an entity's financial statements. Those judgments are normally based on knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ markedly from management's current judgments and therefore will be evaluated during the course of the audit. Based on the preliminary planning, it is anticipated those estimates to be as follows:

• Liabilities for self-insured plans, pension and other retirement benefit obligations
• Allowances for uncollectible receivables
• Valuation of investments
• Cost allocations and depreciation expense

**Federal Compliance Audit in Accordance with OMB Circular A-133**

The following federal award programs will be tested for compliance under OMB Circular A-133:

• U.S. Department of Education - Student Financial Aid Cluster
• U.S. Department of Agriculture - Cooperative Extension Services

Type B programs (those with greater than $300,000 but less than $3,000,000 in federal expenditures) will also be evaluated to determine whether they are high or low-risk. If it is determined there are high-risk Type B programs, the external auditors will be required to audit the program as a major program, and consequently perform additional testing. The number of high-risk Type B programs to be tested will not exceed the number of low-risk Type A programs. The timing of audits was also discussed.

**Timing of Audit**

Planning and interim work has already started and will continue until July 2013. Financial Statement audit field work will take place in September and October. The A-133 Audit will include audits at UMaine, USM and UMPI.

**New Accounting or Auditing Standards and Other Professional Guidance**

The auditors discussed new or pending standards highlighting the following in particular:

• *Governmental Accounting Standards Board (GASB) Statement No. 63 (GASB 63) – Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resource, and Net Position*
GASB 63 is intended to improve financial reporting by providing users of state and local government financial reports with information about how past transactions will continue to impact a governmental entity's financial statements in the future. GASB 63 provides a new statement of net position format to report all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position (which is the net residual amount of the other elements). GASB 63 requires that deferred outflows of resources and deferred inflows of resources be reported separately from assets and liabilities. The provisions of GASB 63 are effective for the UMS in FY2013.

- **GASB Statement No. 65 (GASB 65) - Items Previously Reported as Assets and Liabilities**
  GASB 65 provides guidance on determining which balances currently reported as assets and liabilities should instead be reported as deferred outflows of resources or deferred inflows of resources. Based on those definitions, GASB 65 reclassifies certain items currently being reported as assets and liabilities (such as assets and liabilities from refunding of debt) as deferred outflows of resources and deferred inflows of resources. In addition, GASB 65 will require that certain items currently being reported as assets and liabilities (such as debt issuance costs) be instead expensed in the period incurred. GASB 65 is effective for periods beginning after December 15, 2012, and will be applied on a retroactive basis. This would be effective for the UMS in FY2014, unless the standard was adopted early by the System.

- **GASS Statement No. 68 (GASB 68) - Accounting and Financial Reporting for Pensions**
  GASB 68 mandates new measurement and reporting requirements for governmental employers that provide defined benefit pension plans to their employees. The statement is intended to highlight the promise governments make to their employees regarding pension benefits.

GASB 68 is designed to recognize pension liabilities that reflect the entire unfunded portion of pension obligations regardless of when the government intends to fund the obligations. In addition, the statement requires future pension obligations to be discounted to present value using a single discount rate that reflects both of the following:

- The long-term expected rate of return on pension plan investments that are expected to be used to finance the payment of benefits, to the extent the pension plan's fiduciary net position is projected to be sufficient to make projected benefit payments and pension plan assets are expected to be invested using a strategy to achieve that return.
- A yield or index rate for 20-year, tax-exempt general obligation municipal bonds with an average rating of AA/Aa or higher (or equivalent quality on another rating scale), to the extent that those conditions are not met.

Current standards require the discount rate to only reflect the long-term investment expected rate of return, which for the UMS is currently 7.25%. Because pension investments generally yield greater returns than long-term borrowing rates, the discounted net present value of pension obligations will be larger under the new statement to the extent the projected fiduciary net position will not be sufficient to cover all the projected benefit payments.
GASB 68 is effective for periods beginning after June 15, 2014 (the System's 2015 year-end), although early application is encouraged. To the extent practical, accounting changes made to comply with this statement should be reported as adjustments of prior periods and financial statements presented for the affected periods should be restated.

Ms. Elliott reported that the University will have an actuarial valuation of the Defined Benefit plan performed for fiscal year 2013 and will then be able to determine any impacts this GASB may have on the financial statements. The University had a funded ratio of 96.8% as of the most recent valuation (July 1, 2011). Future negative investment performance could result in additional financial statement impacts given these new requirements.

Other GASB Statements Issued or in Effect in FY2013
There were new GASB statements issued this year that initially do not appear to have a significant impact on the System's financial statements including

- GASB Statement No. 69 - Government Combinations and Disposals of Government Operations
- GASB Statement No. 60 - Accounting and Financial Reporting for Service Concession Arrangements
- GASB Statement No. 61 - The Financial Reporting Entity: Omnibus an amendment of GASB Statements No. 14 and No. 34

Internal Audit Update.
Ms. Janet Waldron, Vice President for Finance and Administration at UMaine, provided an overview of the UMaine Department of Athletics for the following reports:

- Agreed-Upon Procedures in Accordance with National Collegiate Athletic Association Bylaw 3.2.4.16.1 for the year ended June 30, 2012 performed by O’Connor & Drew.

Athletics reported nearly $19 million in revenue with a reported annual surplus of $193 thousand. Several recommendations were made to improve internal controls and compliance and management has or will take corrective action.

The Audit Committee members stated that they were not comfortable with Management’s response to the issues raised in the report and expressed disappointment that this recurring issue has not been resolved. The Committee requested additional information on the UMaine vacation time accrual issue and requested that a permanent resolution be reported back to the Committee.

Adjournment.

Ellen Doughty for
J. Kelley Wiltbank, Clerk of the Board