STATE OF ILLINOIS

NORTHERN ILLINOIS UNIVERSITY

Report Required Under
Government Auditing Standards

For the Year Ended June 30, 2018

Performed as Special Assistant Auditors
for the Auditor General, State of Illinois

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NORTHERN ILLINOIS UNIVERSITY
***Government Auditing Standards* Report**

STATE OF ILLINOIS

NORTHERN ILLINOIS UNIVERSITY

UNIVERSITY OFFICIALS

Acting President (July 1, 2017 through September 19, 2018) President (from September 20, 2018)	Dr. Lisa C. Freeman
Acting Executive Vice President and Provost	Christopher McCord
Vice President for Administration and Finance and Chief Financial Officer (from January 8, 2018)	Sarah McGill
Associate Vice President for Finance and Budget, and Acting Chief Financial Officer (through January 7, 2018) Associate Vice President for Finance and Budget (January 8, 2018 through April 27, 2018)	Lawrence Pinkelton
Vice President for Research and Innovation Partnerships	Gerald Blazey
Acting Vice President and General Counsel	Gregory A. Brady
Vice President for Enrollment Management, Marketing and Communications	Sol Jensen
Vice President for Outreach, Engagement and Regional Development	Anne C. Kaplan
Vice President for University Advancement	Catherine Squires
Director of Internal Audit	Danielle Schultz

Financial Staff

Controller (through April 30, 2018) Acting Associate Vice President for Finance and Treasury (May 1, 2018 – July 31, 2018) Associate Vice President for Finance and Treasury (from August 1, 2018)	Shyree Sanan
Deputy Controller (through April 30, 2018) Acting Controller (May 1, 2018 through July 27, 2018)	Raul Garcia
Financial Reporting Manager (from May 1, 2018)	Kathy Marshall

NIU Office is located at:

300 Altgeld Hall

DeKalb, Illinois 60115

Summary

The audit of the financial statements of Northern Illinois University (the University) was performed by CliftonLarsonAllen LLP in accordance with *Government Auditing Standards*. This report is an integral part of that audit.

Based on their audit and the reports of other auditors, the auditors expressed an unmodified opinion on the University's basic financial statements.

Summary of Findings

The auditors identified certain deficiencies in the University's internal control over financial reporting that they considered to be a material weakness and a significant deficiency. The material weakness is described in the accompanying schedule on pages 5-8 of this report as item 2018-001, *Financial Reporting Process*. The significant deficiency is described in the accompanying schedule on pages 9-10 of this report as item 2018-002, *Untimely Cash Reconciliations*.

Exit Conference

The University waived an exit conference in correspondence dated February 8, 2019. Responses to the recommendations were provided by Shyree Sanan, Associate Vice President for Finance and Treasury, in correspondence dated February 8, 2019.

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Honorable Frank J. Mautino
Auditor General, State of Illinois
and
Board of Trustees
Northern Illinois University

As Special Assistant Auditors for the Auditor General, we have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities of Northern Illinois University and its aggregate discretely presented component units, a component unit of the State of Illinois, as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise Northern Illinois University's basic financial statements, and have issued our report thereon dated February 13, 2019.

Our report includes a reference to other auditors. Other auditors audited the financial statements of Northern Illinois University's discretely presented component units, as described in our report on Northern Illinois University's financial statements. This report does not include the results of the other auditors' testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors. The financial statements of the Northern Illinois University Foundation and the Northern Illinois University Alumni Association (discretely presented component units) were not audited in accordance with *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Northern Illinois University's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Northern Illinois University's internal control. Accordingly, we do not express an opinion on the effectiveness of Northern Illinois University's internal control.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. However, as described in the accompanying schedule, we have identified certain deficiencies in internal control that we consider to be a material weakness and a significant deficiency.

Honorable Frank J. Mautino
Auditor General, State of Illinois
And
Board of Trustees
Northern Illinois University

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency described in the accompanying schedule as item 2018-001 to be a material weakness.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying schedule as item 2018-002 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Northern Illinois University's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Northern Illinois University's Response to Findings

The University's responses to the findings identified in our audit are described in the accompanying schedule of findings. The University's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the responses.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of Northern Illinois University's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Northern Illinois University's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

SIGNED ORIGINAL ON FILE

CliftonLarsonAllen LLP

Oak Brook, Illinois
February 13, 2019

Finding 2018-001 Financial Reporting Process

Northern Illinois University's (the University) internal controls over financial reporting are not sufficient to prevent material misstatements.

During our audit of the significant balances comprising the University's financial statements, we noted the following:

I. Errors and Deficiencies Related to Capital Asset Recognition and Reporting

During testing over the University's balance of construction project expenditures capitalized as construction-in-progress as of June 30, 2018 (totaling $57,908,960 prior to any audit adjustments), we noted six projects, totaling $9,098,946, which were completed and placed in-service, but not appropriately transferred to a depreciable asset. It was determined that each of these projects were completed during the fiscal years ended June 30, 2013, 2014, or 2015.

The results of these errors in the University's financial records as of June 30, 2018 were as follows (amounts rounded to 000's):

- Overstatement of capital assets, construction-in-progress totaling $9,099,000
- Understatement of capital assets, buildings totaling $7,714,000
- Understatement of capital assets, land improvements totaling $1,223,000
- Overstatement of net position, unrestricted totaling $162,000
- Understatement of accumulated depreciation totaling $1,548,000
- Overstatement of net position, net investment in capital assets totaling $1,548,000

The University recorded an audit adjustment to correct this matter in the financial statements as of and for the year ended June 30, 2018.

The errors noted above also understated depreciation expense in prior year financial statements for the years ended June 30, 2013 through 2017. The result of these errors is an overstatement of opening net position as of July 1, 2017 totaling $1,102,000. The University did not record an audit adjustment to correct this matter in its fiscal year 2018 financial statements as it was not considered to be material to the users of the financial statements.

Accounting principles generally accepted in the United States of America require entities to begin depreciating capital assets when they are ready for their intended use and placed in service.

During the fiscal year 2018 audit, University officials made us aware of an asset impairment totaling $1,396,000, recognized in the University's financial statements for the fiscal year ending June 30, 2018. Although the University appropriately identified a residence hall (Lincoln Hall) in need of an impairment analysis, an impairment trigger occurred during fiscal year 2014, which should have prompted the University to perform an impairment test at that time.

An internal memo regarding the future use of Lincoln Hall was issued in August 2013 by University management stating that academic and academic-related services would be relocated to other campus facilities beginning with the 2013-2014 academic year because the Lincoln Hall facilities are dated and demand for housing is significantly less than other residential options.

The result of this error is a likely understatement of accumulated depreciation and an overstatement of net position in the University's fiscal year 2014 financial statements. The result of this error is a likely overstatement of opening net position as of July 1, 2017 totaling $1,396,000. The University did not record an audit adjustment to correct this matter in its fiscal year 2018 financial statements as it was not considered to be material to the users of the financial statements.

Governmental Accounting Standards Board (GASB) Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, paragraph 5, defines asset impairment as a significant, unexpected decline in the service utility of a capital asset. Governments generally hold capital assets because of the services the capital asset provide; consequently, capital asset impairments affect the service utility of the assets. Further, GASB Statement No. 42, paragraph 10, states a change in demand for the services of a capital asset associated with a change in the manner or expected duration of use of a capital asset should be tested for impairment.

Effective internal controls should include procedures to ensure timely identification and evaluation of impairment triggers.

II. Errors and Deficiencies Related to Inter-Entity Transactions

During testing over the University's implementation of GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pension (OPEB)*, specifically as to whether the Northern Illinois University Foundation (the Foundation), the Northern Illinois University Alumni Association (the Alumni Association), and the Northern Illinois Research Foundation (the Research Foundation) (collectively, the University Related Organizations, or UROs) should be allocated a portion of the University's share of its net OPEB liability, it was determined that the UROs, discretely presented component units of the University, were not preparing their financial statements under the appropriate financial reporting framework.

The UROs, non-profit corporations and separate legal entities from the University, do not meet the definition of a governmental entity under accounting principles generally accepted in the United States of America and should prepare their financial statements in accordance with financial reporting standards issued by the Financial Accounting Standards Board (FASB). Historically, the UROs have prepared their financial statements in accordance with financial reporting standards issued by GASB. The Foundation and the Alumni Association changed their financial reporting framework and prepared financial statements in accordance with financial reporting standards issued by FASB for the year ended June 30, 2018, for inclusion in the University's financial statements as discretely presented component units. The Research Foundation chose to continue presentation of their financial statements in accordance with financial reporting standards issued by GASB.

During the Foundation's process to convert its financial records to accommodate the change in its financial reporting framework, the Foundation identified 24 gift accounts with gift dates occurring from 1983 through 2018 totaling $3,347,000 previously considered to be resources owned by the Foundation and included in its net assets, which should have been reported as resources owned by the University and included in the University's net position. The Foundation recorded audit adjustments to recognize a liability for the resources owned by the University in the gift accounts mentioned above.

The results of this error in the University's financial records as of June 30, 2018 were as follows (amounts rounded to 000s):

- Understatement of due from component units totaling $3,347,000
- Understatement of net position (beginning balance) totaling $3,093,000
- Understatement of private gifts, grants, and contracts totaling $248,000
- Understatement of non-operating revenues totaling $115,000
- Understatement of operating expenses totaling $109,000

The University recorded an audit adjustment to correct this matter in the financial statements as of and for the year ended June 30, 2018.

Effective internal controls should include procedures to ensure gifts and other resources are allocated to the appropriate components of the financial reporting entity.

III. Errors and Deficiencies Related to Revenue Recognition

During testing over the University's process to estimate its allowance for doubtful student accounts and implementation of corrective actions related to a prior year finding, we noted the University has not fully implemented planned corrective actions over this area.

During the prior year audit, we noted the University's process to estimate its allowance for doubtful student accounts included assumptions over collection rates that had been used and unchanged since fiscal year 2009, and were not considered reasonable given the conditions noted during the prior year audit. An audit adjustment totaling $8.5 million was proposed and recorded for the fiscal year ended June 30, 2017.

The University's corrective action plan related to the prior year condition was to utilize the accounts receivable analysis developed during the prior year audit and to perform collections analysis to determine if an adjustment to its allowance for doubtful student accounts is necessary.

We noted that the University did update their overall estimate for its allowance for doubtful student accounts; specifically, the University updated percentages applied to its aging buckets (Current: 1%; 1-180 days past due: 45%; 181-364 days past due: 75%; 365+ days past due: 80%). We also noted the University did contract with a consultant to assist with analyzing collections. The University, however, was unable to complete its analysis over collection trends to support its current allowance estimate for doubtful student accounts for the preparation of its fiscal year 2018 financial statements. No audit adjustments were proposed in relation to the University's estimate for its allowance for doubtful student accounts reported in its statement of net position as of June 30, 2018.

Effective internal controls should include procedures to ensure estimates made during the preparation of the financial statements are supported by relevant and reliable assumptions.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires all State agencies to establish and maintain a system, or systems, of internal fiscal and administrative controls, to provide assurance that revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable statistical reports and to maintain accountability over the State's resources.

University officials stated the errors related to capital asset recognition and reporting were the result of insufficient communications between project managers and financial accounting personnel regarding the status of capital projects due to employee retirements and turnover. The errors related to inter-entity transactions were the result of insufficient oversight by employees during the gift agreement review process. The deficiency related to revenue recognition was the result of insufficient time and University resources, which did not allow the University to finalize its collections analysis prior to preparation of the fiscal year 2018 financial statements.

Inaccuracies in the recorded amounts of the University's financial statement balances delays completion of the audit process and delays the timely release of the University's financial reports to users. Also, insufficient and/or ineffective controls over financial reporting could lead to significant reporting inaccuracies in the financial statements. (Finding Code No. 2018-001, 2017-001, 2016-001, 2015-001, 2014-001, 2013-001, 12-1, 11-1)

Recommendation

We recommend the University continue to improve its controls over financial reporting to ensure amounts reported within the University's annual financial statements are accurate and presented in accordance with accounting principles generally accepted in the United States of America.

University Response

Accepted. Management has conducted a comprehensive review of each component of this finding and has taken corrective action to redesign related business practices and processes to continue improving its controls over financial reporting.

Finding 2018-002 Untimely Cash Reconciliations

Northern Illinois University's (the University) monthly reconciliations for cash accounts were not prepared and reviewed on a timely basis during the year ended June 30, 2018.

During our review of the design and implementation of the University's internal control procedures over the preparation and review of monthly cash account reconciliations, University officials stated the normal timeframe to prepare and review cash account reconciliations is 30 days after the monthly close of the general ledger, which normally takes place on the 9th day of a given month. The University's process includes preparation of two separate account reconciliations performed on a monthly basis: one reconciliation is prepared over the payroll cash deposit account (Payroll Reconciliation), and the other is prepared over all the remaining operating cash deposit accounts (Trust Reconciliation).

During testing, we noted cash reconciliations were being completed and reviewed between 1 to 3 months after the close of the monthly general ledger for the period of July through December 2017.

The Fiscal Control and Internal Auditing Act (30 ILCS 10/3001) requires the University to establish and maintain a system or systems of internal fiscal and administrative controls, which shall provide assurance that: (1) resources are utilized efficiently, effectively, and in compliance with applicable law; (2) obligations and cost are in compliance with applicable law; (3) funds, property, and other assets and resources are safeguarded against waste, loss, unauthorized use, and misappropriation; (4) revenues, expenditures, and transfers of assets, resources, or funds applicable to operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the State's resources; and (5) funds held outside the State Treasury are managed, used, and obtained in strict accordance with the terms of their enabling authorities and that no unauthorized funds exists. Effective internal controls include timely preparation and review of cash account reconciliations.

University officials stated that delays in the preparation and review of cash reconciliations were due to employee turnover and training of a new hire during the first half of the fiscal year.

Untimely preparation and review of cash account reconciliations could delay the detection and correction of inaccurate account balances in the University's accounting records and adversely affect the usefulness of financial reports utilized by University personnel in making management decisions. (Finding Code No. 2018-002, 2017-004)

Recommendation

We recommend the University establish and maintain to internal controls to ensure the timely preparation and review of all cash reconciliations.

University Response

Accepted. During the first half of fiscal year 2018, the University implemented corrective action by finalizing critical hires and providing staff training to level workloads. This action is expected to yield an enhancement to the quality and timeliness of the work product.

PRIOR YEAR FINDINGS NOT REPEATED – *GOVERNMENT AUDITING STANDARDS*
For the Year Ended June 30, 2018

A. Finding 2017-002 Inadequate Control over Reporting Restricted Accounts

Northern Illinois University (the University) did not ensure restrictions imposed through revenue bond covenants were properly reflected within the University's financial statements.

During the prior audit, we noted the University's system of internal controls over reporting restricted accounts were inadequate as the University's authoritative guidance was incorrect.

Disposition:
During the current year audit, we noted the University strengthened their internal controls over reporting restricted accounts in order to ensure adherence to accounting principles generally accepted in the United States of America. (Finding Code No. 2017-002)

B. Finding 2017-003 Noncompliance with Debt Covenants

Northern Illinois University (the University) did not comply with its revenue bond covenants.

During the prior audit, we noted the University violated its revenue bond covenants by transferring resources from restricted revenue bond accounts to its segregates accounts set-up for its public-private partnership.

Disposition:
During the current year audit, we noted the University strengthened their internal controls over restricted account transactions to ensure compliance with revenue bond covenants and there were no exceptions noted during our sample testing of restricted account disbursements. (Finding Code No. 2017-003)