

**STATE OF ILLINOIS
NORTHERN ILLINOIS UNIVERSITY**

Report Required Under
Government Auditing Standards
For the Year Ended June 30, 2014
Performed as Special Assistant Auditors
for the Auditor General, State of Illinois

State of Illinois
Northern Illinois University
Report Required Under *Government Auditing Standards*
For the Year Ended June 30, 2014

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**State of Illinois
Northern Illinois University**

Agency Officials

Douglas D. Baker	President
Lisa C. Freeman	Executive Vice President and Provost
Anne C. Kaplan	Vice President, Outreach, Engagement, and Regional Development
Brett Coryell	Vice President, Information Technology
Lesley Rigg	Vice President, Research and Innovation Partnerships
Sean T. Frazier	Associate Vice President and Director, Intercollegiate Athletics
Eric A. Weldy	Vice President, Student Affairs and Enrollment Management
Raymond W. Alden III	Vice President, International Affairs
Michael P. Malone	Vice President, University Advancement
Harlan Teller	Interim Vice President, Marketing and Communications
Jerry D. Blakemore	Vice President and General Counsel
Danielle Schultz	Director of Internal Audit

Financial Staff

Nancy D. Sutenfield	Interim Chief Financial Officer
Linda J. Blair	Acting Controller

NIU Office is located at:

300 Altgeld Hall
DeKalb, Illinois 60115

**State of Illinois
Northern Illinois University**

Government Auditing Standards Report

Financial Statement Report

Summary

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

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

Summary of Findings

The auditors identified a matter involving the University's internal control over financial reporting that they considered to be a material weakness. This material weakness is 2014-001, Financial Reporting Process. The auditors did not identify any matters involving the University's internal control over financial reporting that they considered to be a significant deficiency.

Exit Conference

The University waived an exit conference in correspondence dated January 16, 2015. Responses to the recommendations were provided by Douglas D. Baker in correspondence dated January 20, 2015.



**Independent Auditor's 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 William G. Holland
Auditor General
State of Illinois and

Robert T. Boey, Honorable Chair of the
Compliance, Audit, Risk Management, and Legal Affairs Committee

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 (University) and its aggregate discretely presented component units, collectively a component unit of the State of Illinois, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the University's basic financial statements, and have issued our report thereon dated January 21, 2015. Our report includes a reference to other auditors who audited the financial statements of the discretely presented component units as described in our report on the 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.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the 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 the University's internal control. Accordingly, we do not express an opinion on the effectiveness of the University's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph 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 were not identified. However, as described in the accompanying schedule of findings, we identified a certain deficiency in internal control that we consider to be a material weakness.

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. 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 of findings as item 2014-001 to be a material weakness, we did not note any significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the 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 response to the finding identified in our audit is described in the accompanying schedule of findings. The University's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

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 results of that testing, and not to provide an opinion on the effectiveness of the 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 the University's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

McGladrey LLP

Schaumburg, Illinois
January 21, 2015

State of Illinois
Northern Illinois University
Current Findings – Government Auditing Standards
For the Year Ended June 30, 2014

Schedule of Findings

Finding 2014-001 Financial Reporting Process

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

During our review of the draft financial statements provided by the University, several errors were identified. Some of the more significant items were as follows:

- The University recorded a year-end interest accrual entry for the Series 2010B Student Housing Revenue Bonds, the Northern View Capital Lease, and the New Residence Hall Capital Lease twice. This improperly increased interest expense by \$2,203,000 and Build America Bond subsidy revenue by \$870,000.
- The University classified a \$1,141,000 premium on the 2014 Certificates of Participation issuance as unearned revenue rather than as part of certificate of participation debt as required by generally accepted accounting principles (GAAP).
- The University classified \$6,910,000 of escrow funds for the phase 11 performance contract as construction in progress, rather than as long-term restricted cash as required by GAAP.
- The University classified \$4,000,000 of investments held for over a year in its 2010B bond pool as current cash equivalents instead of long-term restricted investments as required by GAAP.
- During the fiscal year 2013 closing process, the University expensed \$4,231,000 of construction in progress rather than including it as part of capital assets in accordance with GAAP. To correct the impact this had on net position, during fiscal year 2014 the amount was added to capital assets and expenses were reduced by a matching amount.
- As part of its closing process, the University removed all billed fall 2014 tuition and fee revenue from unearned revenue and accounts receivable. This revenue was unearned as of June 30, 2014 and as of that date the University had no legal claim to receive any payments. However, \$1,140,000 of the billed charges had been prepaid by students and should have remained on the University's Statement of Net Position under GAAP.
- The University did not properly eliminate a transfer of resources between University departments. This transfer increased the amount of revenue and expenses reported by the University by \$1,400,000.

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Current Findings – Government Auditing Standards
For the Year Ended June 30, 2014

Schedule of Findings (Continued)

Finding 2014-001 Financial Reporting Process (Continued)

- The University included a capital lease in the operating lease footnote which increased the amount of future lease payments disclosed by \$490,000.
- The University did not include the employer portion of Medicare taxes in its accrual calculation for compensated absences in accordance with GAAP. This understated the balance of compensated absences by \$259,000.
- The University did not accrue for \$93,000 of incurred but unpaid interest expense on the 2014 Certificates of Participation in accordance with GAAP. This caused interest expense and accrued payables to be understated by \$93,300.
- The University calculated the amount of accrued compensated absences for salaried employees as of June 30, 2014 using May 30, 2014 data. Once the correct data was obtained, it was determined that accrued compensated absences were understated by \$53,000.

Financial Accounting Standards Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*, states that “the discount or premium should be reported in the balance sheet as a direct deduction from or addition to the face amount of the note [...] the face amount should also be disclosed in the financial statements or in the notes to the statements.”

Governmental Accounting Standards Board Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, states that “cash and claims to cash that are restricted as to withdrawal or use for other than current operations, that are designated for disbursement in the acquisition or construction of noncurrent assets, or that are segregated for the liquidation of long-term” are excluded from classification as current assets.

Governmental Accounting Standards Board Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities that Use Proprietary Fund Accounting*, states that “Cash equivalents are defined as short-term, highly liquid investments.” The investments must have original maturities of less than 3 months or purchased with 3 months or less until maturity.

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Schedule of Findings (Continued)

Finding 2014-001 Financial Reporting Process (Continued)

Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, as amended by Governmental Accounting Standards Board Statement No. 37, *Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments: Omnibus - an Amendment of GASB Statements No. 21 and No. 34*, states that, “capital assets should be reported at historical cost. The cost of a capital asset should include ancillary charges necessary to place the asset into its intended location and condition for use. Ancillary charges include costs that are directly attributable to asset acquisition — such as freight and transportation charges, site preparation costs, and professional fees.”

National Council on Governmental Accounting Statement No. 1, *Governmental Accounting and Financial Reporting Principles*, states that “revenues may be collected in advance of the fiscal year to which they apply. Such prepayments should be recorded as unearned revenue and recognized as revenue of the period to which they apply.”

Governmental Accounting Standards Board Statement No. 16, *Accounting for Compensated Absences*, requires that “An additional amount should be accrued as a liability for salary-related payments associated with the payment of compensated absences, using the rates in effect at the balance sheet date. The salary-related payments subject to this accrual are those items for which an employer is liable to make a payment *directly and incrementally associated with payments made for compensated absences on termination*. Such salary-related payments include the employer's share of social security and Medicare taxes.”

Further, 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, which shall 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 financial and statistical reports and to maintain accountability over the State’s resources.

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Schedule of Findings (Continued)

Finding 2014-001 Financial Reporting Process (Continued)

According to University management, the financial reporting errors are due to employee turnover of key personnel who prepared the draft financial statements in prior years and did not leave documentation of the preparation process.

Submitting incomplete and inaccurate draft financial statements 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 Nos. 2014-001, 2013-001, 2012-001, 2011-001)

Recommendation

We recommend the University improve controls over financial reporting to ensure accurate presentation and disclosure of the University's annual financial statements.

University Response

The University concurs with the auditor's comments and the following actions are in the process of being undertaken to improve controls over the financial reporting process.

The Controller's Office will document the policies and procedures for the year-end close process and financial reporting by April 30, 2015. These policies and procedures will be consolidated into one manual that will be available to the Controller's Office staff both in hard copy and on the Controller's Office network shared drive. Revisions to the manual will be made as needed to ensure the manual is current at all times. The Controller's Office staff will undergo refresher training and review of new accounting guidance prior to the beginning of the year-end audit processes each year.

Roles and responsibilities of individual members of the Controller's Office staff will be documented to ensure completeness of the year-end financial reporting process and eliminate duplication of effort. The year-end checklist will be expanded to include additional procedures, source of information and listing of the responsible staff member.

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Schedule of Findings (Continued)

Finding 2014-001 Financial Reporting Process (Continued)

University Response (Continued)

A year-end close calendar will be created and posted on the Controller's Office website and communicated across University Departments.

After each audit cycle is complete, there will be an audit debriefing to assess which processes and/or procedures need to be changed in order to improve internal controls over the financial reporting process in preparation for the next cycle.