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University of South Carolina
BOARD OF TRUSTEES

Audit and Compliance Committee

October 11, 2019

The Audit and Compliance Committee of the University of South Carolina Board of Trustees met at 2:35 p.m. on Friday, October 11, 2019, in the C. Edward Floyd Boardroom at the Pastides Alumni Center.

Members present were: Ms. Rose Buyck Newton, Chair; Mr. Chuck Allen; Mr. Robert F. Dozier Jr.; Dr. C. Dorn Smith III; Mr. Thad H. Westbrook; Mr. Mack I. Whittle Jr.; Mr. Charles H. Williams; Mr. John C. von Lehe Jr., Board Chairman; and Mr. Hubert F. Mobley, Board Vice Chairman. Mr. J. Egerton Burroughs was absent.

Other Board members present were: Mr. C. Dan Adams; Mr. William C. Hubbard; Mr. Richard A. Jones Jr.; Mr. Toney J. Lister; Mr. Miles Loadholt; Ms. Leah B. Moody; Ms. Molly M. Spearman; and Mr. Eugene P. Warr Jr.; with Mr. A.C. "Bubba" Fennell III joining by telephone.

Also present were Strategic Advisor David Seaton, USC Columbia Faculty Senate Chairman Mark Cooper and USC Columbia Student Government President Luke Rankin.

Others present were: President Robert L. Caslen Jr.; Secretary J. Cantey Heath Jr.; General Counsel Walter "Terry" H. Parham; Interim Executive Vice President for Academic Affairs and Provost Tayloe Harding; Senior Vice President for Administration and Chief Operating Officer Edward L. Walton; Vice President for Student Affairs and Vice Provost for Academic Support Dennis A. Pruitt; Vice President for Human Resources Caroline Agardy; Vice President for Information Technology and Chief Information Officer Doug Foster; Athletics Director Ray Tanner; Vice President for Research Prakash Nagarkatti; Interim Chief Communications Officer and Director of Public Relations Jeff Stensland; Interim Chief Development Officer Will Elliott; Senior Advisor to the President for Advancement Paula Harper Bethea; Palmetto College Chancellor Susan Elkins; USC Aiken Chancellor Sandra Jordan; College of Arts and Sciences Dean Lacy Ford; University Architect and Associate Vice President of Facilities Planning, Design and Construction Derek Gruner; University Controller Mandy Kibler; University Budget Director Joe Sobieralski; University Treasurer Pat Lardner; Associate Vice President for Administration and Finance

and Medical Business Affairs Jeffrey L. Perkins III; Associate Vice President for Finance Kelly Epting; Vice Provost and Dean of Undergraduate Studies Sandra Kelly; Executive Director for the Office of Economic Engagement William D. “Bill” Kirkland; Chief Audit Executive Pam Doran; Executive Director for Strategic Initiatives Jack Claypoole; University Director of Institutional Effectiveness and Accreditation Donald Miles; Director of Audit & Advisory Services Glenn Murray; Audit Manager, Audit & Advisory Services, Kim Dwiggin; Assistant Controller Lindsay Anastasio; Director of Financial Reporting Sandy Smith; Office of Equal Opportunity Programs Director Clifford Scott; Office of Research Compliance Director Thomas Coggins; Assistant to the President for System Affairs Eddie King; Associate Director, Distributed Learning, Trena Houp; Palmetto College Faculty Senate Chair Christine Sixta Rinehart; Accreditation Manager, USC Beaufort Department of Education, Rachel Burns; Maggie Metcalf, guest of Trustee von Lehe; Trustee Emeritus M. Wayne Staton; Elliott Davis shareholders Brian D’Amico and Howie Houston; Elliott Davis Senior Manager Brittany Long; Association of Governing Boards consultants Rick Legon and Ellen Chaffe; Vice President of Gibson Consulting Carolyn Cooper; University Technology Services Production Manager Matt Warthen; and Board staff members Debra Allen and Terri Saxon.

I. Call to Order

Chair Newton called the meeting to order, welcomed those in attendance and asked all at the table to introduce themselves. Secretary Heath confirmed Trustee participation by telephone. Chair Newton 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.

Chair Newton called on Mr. Stensland, who introduced Mike Fitts with the *Post and Courier*, and Meghan Crum with *The Daily Gamecock*.

II. External Audits

Chair Newton called on Mr. Howie Houston from Elliott Davis to present results of the External Audit.

A. Comprehensive Annual Financial Report for the Year Ended June 30, 2019

B. System Audit Management Letter and Findings Fiscal Year 2018-2019

Mr. Houston congratulated the Controller’s Office for issuing the Comprehensive Annual Financial Report (CAFR) in record time as a result of process improvement efforts related to

financial reporting. He reported that as part of the audit of the CAFR, an unmodified opinion was issued. There were no corrected adjustments during the audit and only one uncorrected misstatement. There were no significant disagreements with management, no difficulties in executing audits, no changes in significant judgments or estimates, and no significant changes in accounting policies. Mr. Houston advised that higher education institutions, particularly in South Carolina, recently experienced two significant comprehensive standards that pushed a proportionate share of the state's retirement liability and the post-employment liability to the institutions' financial statements, and he noted that these standards were dealt with in previous years.

Mr. Houston briefed the committee on the reconciliation issue that resulted in an uncorrected misstatement. There was a comprehensive implementation of the PeopleSoft fixed asset system and process improvements. The capital assets within PeopleSoft were not in agreement with the general ledger, resulting in an approximate \$2.1 million addition to capital assets in the general ledger. Management recognized the error and corrected it in the current year; the reconciliation had not been completed in prior years. A policy of monthly reconciliation and review has been implemented to promptly identify and correct discrepancies.

In response to Trustee Whittle's question about the pension liability, Mr. Houston said the employer and employee contributions were increased in response to the inherent issues across the country. Information and estimates pushed down to the university's level are based on the prior year's actuarial results. When reports are issued in the spring, the University Chief Audit Executive and Controller assess those reports as quickly as possible to identify areas impacted this year and begin to address them. The pension is a cost share plan and there is no direct ability to change how those plans are governed or managed, the investment returns, or any other assumptions as they operate. In the short term, the liability has worsened, and it is likely that over time there will be more increases in employer and employee contributions to address those liability issues long term.

Trustee Whittle said the University owns a significant number of valuable collectible items and antiques and he asked if an inventory on those items is maintained. USC Controller, Mandy Kibler, responded that Inventory Control was moved under the Controller's Office two years ago and a complete inventory was conducted last year through the PeopleSoft system with all items receiving new tags. Items moving between departments require a transfer and that is managed through the PeopleSoft system. She further noted that insurance is maintained on each item.

Mr. Houston reported that the University's 2019 CAFR received a certificate of excellence from the Government Finance Officers Association.

C. Darla Moore School of Business Professional MBA Program, Fiscal Year 2018-2019 Compliance Report

Mr. Houston said the State of North Carolina requires any higher education institution doing business in North Carolina to provide evidence of a guaranty tuition bond equivalent to the amount of tuition paid by the State's residents. This requirement is necessary for the Moore School Professional Master of Business Administration Program. Elliott Davis affirmed that the bond was sufficient and there were no observations or findings.

D. Open Projects

1. System Uniform Guidance Audit Fiscal Year 2018-2019

Mr. Houston said he would present the comprehensive update of the Federal Awards and Uniform Guidance audits at the next board meeting.

2. NCAA Agreed Upon Procedures Engagements

The NCAA requires some agreed upon procedures for both USC Columbia and USC Upstate. This is not an audit, but rather a process for ensuring that the University meets their compliance requirements related to the financial information that is provided to the NCAA. The review is scheduled for later in the month.

In closing, Mr. Houston noted there is a new standard related to leased assets that do not qualify as a capital or financing lease. Historically, those leased assets have been disclosed on the financial statements, he explained. The essence of the new standard is to take those operating leases that the University is contractually committed to within the next two years and put them on the balance sheet as a liability so that there is greater transparency. This also applies to lessor leases.

Chair Newton thanked Mr. Houston and noted these reports and the supporting documentation provided in the meeting materials are received as information. She also congratulated Ms. Kibler and her team for all they have accomplished.

III. Internal Audits/Reviews

Chair Newton called on Ms. Doran to present.

A. IT Infrastructure – WiFi Audit

Ms. Doran called on Mr. Patterson, who said the University's Division of Information Technology (DoIT) manages approximately 6,000 wireless infrastructure devices and

equipment, which includes 4,113 wireless access points within administrative buildings and housing facilities across the Columbia campus. A multi-year project was undertaken in 2015 to replace outdated wireless equipment and improve the wireless experience; however, the final phase of the project was not completed due to funding limitations.

Mr. Patterson said Audit & Advisory Services (AAS) conducted an audit and determined the current Wi-Fi infrastructure does not meet the overall demands of the growing student population as well as faculty and staff. AAS assessed the required service level for upgrading the wireless network and funding required to support the infrastructure. Security threats were monitored and authentication requirements for accessing all wireless networks, including the guest network, were evaluated. Appropriate use of the University's wireless assets was also assessed. AAS determined there were no authentication requirements for access to the guest network. DoIT remedied that issue and users now must provide log-in credentials to access the guest network. AAS recommended DoIT work with stakeholders to identify a long-term strategy and a sustainable funding model to address outdated wireless network technology, coverage gaps, and connectivity holes.

Dr. Cooper said he served on the Faculty Senate's IT Committee several years ago, and it made these same observations and recommendations. He asked why three years later, after additional study and DoIT coming to the same conclusion, action has not been taken. Mr. Patterson responded that the Faculty Senate's report, as well as student survey responses were leveraged and a driving factor behind AAS' recommendation. Mr. Foster advised the issue had primarily been related to design and that a design was now in place and an investment proposal had been put forward. In response to Trustee von Lehe's question about the estimated project completion time, Mr. Foster responded DoIT was working on an investment plan to start January 1, 2020 and is expected to be complete within 18 months.

B. Research Accounting Audit – Report III

Ms. Doran presented the third and final Research Accounting Audit Report, which primarily focuses on the relationship between the South Carolina Research Foundation (SCRF) and the University. She noted the SCRF was established in 1997 as a separate 501c(3) support organization to promote research. There are three major components: Health Sciences South Carolina (HSSC), the Institute of Medicine and Public Health (IMPH), and research grants awarded to the SCRF that are 100% subcontracted back to the University to conduct the work. The federal draw systems being used to reimburse the University for research expenses are drawn down for both the University and the SCRF by

University personnel. The review was conducted because as those draws occurred there was some comingling of funds and those funds had to be reconciled and sorted.

Ms. Doran said the scope of the review looked at the Affiliation Agreement between the SCRF and the University, the SCRF Bylaws and structure of the foundation, and compliance with grant policies and procedures. The reconciliations of the federal draw systems were also reviewed to ensure that the adjustments being made were appropriate and that the draws made through the draw system were appropriate. The Higher Education Research Development (HERD) survey was also reviewed.

AAS determined the University/SCRF relationship, originally more structured had evolved over time and was currently not operating as a typical sub-recipient/prime relationship with a formal sub-recipient agreement to outline roles and responsibilities, billing and payment terms. Also, University employees perform administrative functions for the SCRF for which the University is not being reimbursed. The audit revealed several internal controls would need to be strengthened to continue administration in the way it is designed.

AAS determined the real benefit of the University's relationship with SCRF is the ability to be awarded grants that can only be awarded to a 501c(3) organization. In weighing whether the benefits of the relationship outweigh the administrative costs with adequate internal controls, an alternative was identified whereby relationships with existing foundations that have established procedures can be leveraged. Management will conduct an assessment and report back to the Board by March of 2020, as to whether keeping SCRF in place makes sense from a cost benefit perspective. Ms. Doran said if it is determined the cost exceeds the benefits, then a process for dissolving the SCRF and transferring existing research grants to an already established University Foundation would be determined.

Ms. Doran reviewed the Higher Education Research and Development (HERD) survey results. This voluntary survey is administered by the National Science Foundation for institutions that have \$150,000 or more in federal, state, or institution-funded research. An audit was undertaken because the financial information being reported was not prepared using the University's financial "system of record," which led to misclassifications, errors, and unsupported amounts reported on the survey. AAS recommended the Controller's Office take over that reporting process and that the financial information reported use the University's financial "system of record" going forward. One of the unsupported amounts was an estimate of institutionally funded research. This research is non-sponsored faculty research; however, it is not being separately tracked in a research account, which is one of the criteria of the HERD

survey. Management is looking at a way to track those unsupported costs so that USC can include that research activity in the HERD survey financial information. If able to track the unsupported costs, the adjustment for last year's report would be much smaller. However, if unable to track those costs, that amount would have to be revised.

Trustee von Lehe asked which Trustee served on the SCRF Board and Trustee Westbrook responded he was appointed and would attend his first meeting the next week. Trustee von Lehe asked Mr. Walton to share his thoughts about the SCRF. Mr. Walton said more review was needed before making a recommendation to dissolve the SCRF. Trustee Mobley asked Mr. Walton to consider if there were untapped opportunities in the SCRF. Ms. Doran said she would follow up after the March 2020 evaluation of the SCRF.

C. Succession Planning Audit

Ms. Doran called on Mr. Murray, who said Policy HR 2.00 – Succession Planning and Post-Retirement Employment initiated in fiscal year 2017-18, required succession planning be developed by March 31, 2018. AAS sought to determine if there was documentation and communication of succession planning requirements and if templates, resources, and guidance were available to the University's business units to develop and maintain succession plans. The process for developing a succession plan is identifying key executives and pivotal positions and conducting skills gap analyses to determine whether potential candidates are being developed. A sampling of 12 business units throughout the University system determined Human Resources has done a great job in developing resources and providing guidance to the business units. However, of the 12 units audited, one third did not have fully developed formal succession plans.

AAS recommended the University HR 2.00 policy be strengthened to provide greater clarity as to what is a key, pivotal position and who the business units should be identifying for inclusion in succession planning. AAS also recommended Human Resources reinforce awareness of the policy and requirements for developing succession plans as well as develop a monitoring process to determine which University units have succession plans. Mr. Murray noted Human Resources has strengthened the policy's two-year review requirement to include review when there are substantial changes.

D. Tracking Report

Ms. Doran reviewed the Audit Tracking Reporting noting there are 31 outstanding audit recommendations, 17 of which are not yet due and 14 have been extended. Four audit

recommendations have been extended beyond two years; however, they are close to being implemented. Since the issue of faculty conflict of interest reporting is still not resolved, the audit team continues to work very closely with the chair of the Faculty Senate to develop a process that allows for appropriate review of disclosed conflicts and encourages responses from those required to disclose.

In response to Trustee Whittle's question about the status of this process, Ms. Doran advised a process should be in place in time for the January 2020 disclosures and management plans. He asked Ms. Doran to report back to the Committee on the number of outstanding conflict of interest disclosures.

Trustee Moody asked for clarification as to whether the faculty were "encouraged" or "required" to comply with the University's conflict of interest reporting policy. Ms. Doran confirmed the faculty were required to report potential conflicts of interest. Dr. Cooper shared efforts to get faculty to comply with the policy including working with the Provost's Office.

In response to Trustee von Lehe's question, Ms. Doran said approximately 20% of faculty and 20% of staff have not yet complied with the University's Conflict of Interest policy. Following discussion, Ms. Doran indicated a compliance report would be provided to the Board in March 2020. It would include information as to the process developed to ensure compliance.

Chair Newton thanked Ms. Doran and noted that these reports and the supporting documentation provided in the meeting materials are received as information.

IV. Deferred Maintenance Financial Update

Chair Newton called on Mr. Gruner, who provided background information as to the external standards set by the Commission on Higher Education (CHE); in addition to other regulatory standards. The CHE mandates that every three years, the University survey all Education or General (E&G) buildings on campus based on 89 different categories to evaluate the building maintenance needs and to determine the value of the outstanding maintenance versus replacement value. The next CHE standards survey will be in 2020.

Mr. Gruner said capital renewal and maintenance deferral decisions are often based on alignment with institutional priorities, strategic plans, availability of swing space, and inadequacy of available funding. Life, health, and safety items are the areas prioritized first with building envelope, utility-related systems, accessibility, and interior finishes following. Projects that meet the criteria for capital renewal and maintenance are placed in a five-year plan only if a funding source has been identified. Mr. Gruner noted the most effective and reliable funding sources for addressing USC Columbia's capital renewal and

maintenance over the past few years have been Institutional Capital Project Funds (ICPF) and the E&G Maintenance Reserve, which is generated from a student fee. He advised that \$14 million for deferred maintenance was included in this year's state budget request as a matching element to the \$14 million in funding received by the ICPF. Mr. Gruner underscored the fact that maintenance project requests in excess of \$250,000 require board approval and projects in excess of \$1 million not only come to this board but are also subject to review by the CHE, the Joint Bond Review Committee (JBRC) and State Fiscal Accountability Authority (SFAA) for phase I and phase II approval.

Mr. Jeff Perkins gave an overview of the capital renewal and deferred maintenance authorization process flow and noted on average, between \$20 and \$22 million is spent per year for deferred maintenance, excluding utilities and direct labor costs. He said there is a movement across the country whereby institutions are financing funding sources up front and monetizing existing assets. He also reviewed the capital and maintenance appropriations for FY19 and FY20 and addressed questions from the board.

Mr. Gruner and Mr. Perkins reviewed the status of recent comprehensive capital projects previously approved by the board. Four of the capital projects are in the planning stage, five in the design stage, and three in the construction stage. Mr. Gruner noted future capital renewal challenges involve 1.75 million square feet of significant E&G academic space constructed between 1965 and 1976 on the Columbia campus. Areas in most need of comprehensive capital renewal include the Humanities Classroom Building, Coker Life Sciences, 300 Main Street, the Welsh Humanities Building, the Blatt PE Center, and the Swearingen Engineering Center. Mr. Perkins said most of the University's utility systems are quite old and the high voltage electrical system is well past its prime. Mr. Gruner and Mr. Perkins recommended the condition and capacity of the utility infrastructure be surveyed as part of a Master Utility Plan.

In response to Trustee Jones' question, Mr. Gruner referred to the 2017 CHE building inspection report that reflected a total aggregate amount of deferred maintenance on the Columbia campus of \$302 million.

Chair Newton noted these reports and the supporting documentation provided in the meeting materials are received as information.

V. Policy Reviews

– BTRU 1.06, *Audit & Advisory Services Policy*

Based on her review, Ms. Doran proposed minor grammatical changes to the policy.

No action was required.

VI. Audit and Compliance Committee

A. Education – Financial System Fund Types Overview

Since there are new Trustees, Chair Newton said she requested this overview and called on Controller Mandy Kibler. Ms. Kibler noted a fund is a set of accounts that are segregated to identify the transactions associated with a specific activity conducted by the University. There are two different types of funds: restricted and unrestricted. Unrestricted funds are funds received that have no restrictions as to use. They are typically used for general operating purposes such as tuition and fees, state appropriations, auxiliary revenue, and sales and service revenues. There are two types of restricted funds: expendable and nonexpendable. Expendable restricted funds are funds received with a restriction that will be satisfied generally within a two-year period. The restrictions relate to a specific purpose or program and are in the form of grants, contracts, or gifts. Nonexpendable restricted funds are received with a donor-imposed restriction that states the donation must be maintained permanently but may, however, permit use or expenditures for part or all the income derived from the asset. These funds are typically endowments, scholarships, or debt service.

Ms. Kibler provided an overview of the sources, support, and restrictions of the General Operating Fund (A Funds); Auxiliary Funds; Student Activity Fund; Sales and Service Fund; Designated Fund; Grants and Contract Fund; Scholarship and Loan Funds; Endowment Funds; Bond and Interest Funds; and Capital and Maintenance Fund.

Chair Newton thanked Ms. Kibler and advised the report would be received as information.

B. Matrix Review

Chair Newton said the Matrix on the board portal, reflects the committee items for this meeting have been completed. She noted the Conflicts of Interest policy will be reviewed at the March 2020 meeting.

C. Self-Assessment

Chair Newton advised that the Audit and Compliance Committee Self-Assessment form being distributed should be completed and returned by end of the day.

VII. Other Matters

Chair Newton called for any other matters to come before the committee. There were none.

VIII. Adjournment

Chair Newton declared the meeting adjourned at 4:16 p.m.

Respectfully submitted,

J. Cantey Heath, Jr.
Secretary