MINUTES

BOARD OF REGENTS’ COMMITTEE ON INDEPENDENT AUDIT MEETING

DECEMBER 9, 2015

I. CALL TO ORDER

Committee Vice Chair Ben Kudo, called the meeting to order at 9:37 a.m. on Wednesday, December 9, 2015, at the University of Hawai‘i at Mānoa, 2465 Campus Road, Executive Dining Room, Honolulu, Hawai‘i 96822.

Committee members in attendance: Committee Vice Chair Ben Kudo; Regent Wayne Higaki; Regent Michael McEnerney; Regent Jeffrey Portnoy.

Excused (1): Committee Chair Stanford Yuen.

Others in attendance: Board Chair Randy Moore; Board Vice Chair Jan Sullivan; Regent Simeon Acoba; Regent Lee Putnam; Regent Michelle Tagorda; Regent Ernie Wilson (ex officio committee members); President David Lassner; Vice President for Academic Affairs Risa Dickson; Vice President for Legal Affairs and University General Counsel Carrie Okinaga; Vice President for Information Technology and Chief Information Officer Garret Yoshimi; Vice President for Budget & Finance/Chief Financial Officer Kalbert Young; UH Mānoa (UHM) Chancellor Robert Bley-Vroman; Executive Administrator and Secretary of the Board of Regents Cynthia Quinn; and others as noted.

II. APPROVAL OF MINUTES OF THE NOVEMBER 5, 2015 MEETING

Regent Higaki moved and Regent McEnerney seconded the motion to approve the minutes of the November 5, 2015 meeting, which was unanimously approved.

III. PUBLIC COMMENT PERIOD

Executive Administrator and Secretary of the Board Cynthia Quinn announced that the Board Office received no written testimony, and no individuals signed up to testify.

IV. AGENDA ITEMS

A. For Action:

1. Review and Acceptance of Officer of Internal Audit Report on the UH Mānoa Athletic Department’s Acquisition, Maintenance, and Distribution of Equipment and Apparel

Committee Vice Chair Kudo noted the auditor’s report at the last meeting did not include the athletic department’s response, which was distributed to the committee members with the materials. Regent McEnerney indicated the current audit report was responded to and accepted by the athletic department, the suggested remedies were
accepted, a timetable and program to meet those has been submitted. He moved that the committee accept the internal audit report, accept the response, and requested that both the athletic department and the internal auditor report back to the committee in May 2016 with a status report on the outcomes and address any goals that may have not been met. Regent Portnoy seconded the motion, and the motion carried by unanimous vote.

2. Review and Acceptance of the University of Hawai‘i Audited Consolidated Financial Statements for the Fiscal Year Ended June 30, 2015

External Auditor Cory Kubota of Accuity LLP explained that the UH Consolidated Financial Statements for the years ended June 30, 2015 and 2014 are in draft because although Accuity is complete with the audit procedures for the university’s accounts and transactions, information is pending from Employee Retirement System (ERS) of the State of Hawai‘i. The ERS produces a separate annual financial and audited financial statements, and provides all state agencies their proportionate share of the state’s pension obligation on their balance sheets, as required under new GASB 68 and 71 standards. The ERS retained KPMG to conduct the audit, and release is pending final approval from their national office. Once that information is available, it is estimated a few days will be required by the State of Hawai‘i to process and analyze that information and then distribute it to all state agencies. The particular information Accuity is waiting on from the ERS pertains to the invested assets in ERS that need to be disaggregated and allocated based on which employers contributed what and when, and then allocating the related investment earnings on those contributions made. Accuity does not believe that any of the numbers in the university financial statements will change, but could not be definitive without the benefit of the final KPMG audit reports. The university has reviewed and vetted the preliminary allocation reflected in the draft of the pension obligation of approximately $1.1 billion dollars as of July 1, 2014, and the methodology for the allocations. The deadline for the university to submit the report to the federal government is the first quarter of calendar year 2016.

The committee discussed the charge the Board of Regents to the committee to approve the audit of the University of Hawai‘i, and whether the draft statements meet the charge; materiality of the footnotes, the timeframe required for the university to submit this audit to the state, calling another special meeting if the final report from Accuity is received before the end of the year, and providing the committee with a redlined copy to the changes. The committee concurred to defer the item and further discussions on the remaining items in the consolidated financial statements to the special meeting. Regent McEnerney moved to approve deferral of the item, subject to rescheduling a special meeting before the end of the year. Board Chair Moore seconded the motion, and the motion carried by unanimous vote.

3. Review and Acceptance of the University of Hawai‘i at Mānoa Intercollegiate Athletics Audit Reports for the Fiscal Year Ended June 30, 2015

Mr. Kubota indicated the documents distributed to the committee members contained the draft Financial Statements and supplementary information; the Report on Agreed-Upon Procedures, which is required by the National Collegiate Athletic Association (NCAA); and the Internal Control and Business Issues Report, which is a management
letter with Accuity observations during the 2015 audit. Mr. Kubota then presented a PowerPoint slides on the Required Auditor Communications specific to the Athletics Department. He explained that Accuity is engaged to perform an independent audit of the Athletic Department’s separate financial statement. The Athletic Department is a division with the University of Hawai‘i at Mānoa campus of the UH System, and not a separate legal entity. Accuity is prepared to issue a clean, unmodified opinion on the June 30, 2015 and 2014 financial statements. The department’s financial statements are unique because they incorporate booster accounts under the custody of University of Hawai‘i Foundation (UHF), a separate governing board, and a separate Audit Committee procures its own external auditor. As the group auditor for the University of Hawai‘i, Accuity issues instructions to the UHF’s auditors for specific procedures to support the University of Hawai‘i audit. There are communications between the auditors throughout the audit process on significant accounting matters, but there has yet to be an instance where Accuity disagreed with the final conclusions. The report contained the actual communication requirement under Generally Accepted Auditing Standards (GAAS), Accuity’s response, and adjustments proposed by Accuity that management did record into the 2015 financial statements.

Questions raised included the role and scope of review of the UHF financials, the different booster organizations, clarity of in-kind support offset by institutional support, the difference between a management report and quarterly and annual financial statements, how the university internally accounts for things different than what is externally reported, and how the information of this report is not used for any decisionmaking.

Mr. Kubota reported that Accuity is prepared to issue clean, unmodified opinion on the Athletic Department’s financial statements. Accuity has held many discussions with management, and it is not anticipated there will be a significant turnaround in Fiscal Year 2016. Management is working on plans from a cost savings standpoint and AD Matlin presented his five year goals to raise the top line for the department. The department is run very lean administratively, to be very cost conscientious. AD Matlin concurred that he had reviewed the audit, held meetings with Accuity, were in agreement with the audit, and had already acted on some of the issues that were raised.

Accuity noted that the Management’s Discussion and Analysis section provided a good summary of the department's difficult Fiscal Year 2015, resulting, on a combined basis with those accounts maintained by UHF, a decrease change in net position of $4.6 million, or in a commercial sense a net loss for the year. He pointed out that in current liabilities, the cash overdraft due to university and other units as of June 30, 2015 was approximately $1.9 million. This represents the department’s borrowing of funds from other units within UHM to finance its operations.

The committee noted a typographical error on the bottom of page 22, “The Athletics Department’s policy is not o reflect…” should read “is not to reflect…” Mr. Kubota further explained the common practice not to monetize in-kind contributions so as not to skew or mislead in terms of the dollar value of in-kind gifts the department receives. Moreover, typically the agreements are structured as an exchange type of transaction, and not an outright contribution. The department has elected not to gross up the financial statements for those amounts.
Questions regarding internal controls at booster organizations, specifically ‘Ahahui Koa Ānuenue (AKA), were raised. Accuity explained that prior to May 2015 the department did not provide regular oversight over cash disbursements in accounts maintained and managed by AKA. AKA now holds cash on its own outside of UHF in its own bank account and uses those funds to operate, with full time personnel and administrative costs associated with running the organization. During the majority of Fiscal Year 2015, there was no oversight by the department, which Accuity considered to be a significant issue because it is an indicator of institutional control issue. When management was informed of this, immediate corrective action was taken and a review and approval process was implemented by the department’s fiscal department and athletic director. A retroactive review of all activity was also done during the fiscal year and no inappropriate usage of funds was identified. While the NCAA requires the AUP to be done annually, it is not required to be submitted to the NCAA, but must be made available upon request by the NCAA. Every few years the NCAA does an inspection of the department, and the AUP will be one of the documents requested in connection with the inspection. The AUP must be performed by an external auditor, which in some states could be performed by a state auditor, but an Internal Audit Department is not acceptable to the NCAA. Of note, it was reported that due to timing, as of June 30, 2015 the remaining amount of AKA’s commitment that still needed to be remitted over to the department was $13,000.

Sick leave reported was clarified that it was a non-vesting benefit, not an actual liability of the department, and traded in for pension credit upon retirement. The pension credit is factored into the ERS actuarial calculation of the net pension obligation, and not actual cash that would be paid out upon termination. GASB 68 and 71 are not being rolled over into this particular statement, and if it were, there would be an additional expense reflecting the cost of this conversion of the accrued sick pay and benefits based on the actuated assumptions on how much of that would eventually roll over into a retirement. It was noted that although doing so amplifies the deficit, it is university policy to reflect it at the system and not department level, similar to other post-employment benefits or post retirement medical.

Regent Acoba left the meeting at 10:30 a.m.

Accuity noted there were three comments in the Internal Control and Business Issues Report for Fiscal Year 2015: Comment No. 15-01 related to AKA oversight (Material Weakness); Comment 15-02 related to H-Zone (Material Weakness); and Comment No. 15-03 related to fiscal deficit. Accuity follows up on comments during the successive year’s audit or earlier, depending on the severity of the issue. The issues for Comment No. 15-01 have been resolved. The issues for Comment 15-02 are ongoing, and reported by Tiffany Kuraoka, Assistant Athletic Director for Business Operations, as a matter now resolved once downloads from the point of sale (POS) system were inputted into Excel, and proper training on inventory records and processes are done. Any associated cost was diminimus. AD Matlin added that ongoing monitoring with H-Zone management continues to timely address issues, note improvements, and focus on areas needing addressing. Mr. Kubota added that management vets any fix or change to a policy or
procedure with Accuity prior to implementation, and Accuity will concur or recommend revisions. The actual validation of the H-Zone items is expected by the next audit.

Board Chair Moore moved that the University of Hawai‘i at Mānoa Intercollegiate Athletics Audit Reports for the Fiscal Year Ended June 30, 2015 be accepted. Regent Portnoy seconded the motion, which carried upon unanimous vote.

V. ADJOURNMENT

There being no further business, on the motion of Regent Higaki and second by Chair Moore and with unanimous approval, the meeting was adjourned at 10:50 a.m.

Respectfully Submitted,

/S/

Cynthia Quinn
Executive Administrator and
Secretary of the Board of Regents