

Item: <u>AF: I-2b</u>

# **AUDIT AND FINANCE COMMITTEE**

Wednesday, October 20, 2010

SUBJECT: REVIEW OF AUDITS: FAU 09/10-4 AUDIT OF BANK ACCOUNT RECONCILIATIONS FOR THE PERIOD OCTOBER 1 THROUGH DECEMBER 31, 2009.

#### PROPOSED COMMITTEE ACTION

Information Only.

#### **BACKGROUND INFORMATION**

Key objectives of this audit were to determine whether:

- All bank accounts were being reconciled on a monthly basis;
- Internal controls over the reconciliation process were adequate and effective;
- The bank account reconciliations were properly documented, prepared by independent personnel, and completed in a timely and accurate manner; and,
- Reconciling items were identified and cleared timely.

Two recommendations were made to address conflicting duties and write-off of unidentified reconciling items.

#### IMPLEMENTATION PLAN/DATE

Management has agreed to implement the audit recommendations no later than October 31, 2010.

#### FISCAL IMPLICATIONS

Not Applicable.

**Supporting Documentation:** Audit Report FAU 09/10-4

Presented by: Mr. Morley Barnett, Inspector General Phone: 561-297-3682

Report No. FAU 09/10-4 Report Issue Date: June 25, 2010

# FLORIDA ATLANTIC UNIVERSITY

# Office of Inspector General

Audit Report: Bank Account Reconciliations For the Period October 1 through December 31, 2009

#### **Use of Report**

We are employed by Florida Atlantic University. This report is intended solely for the internal use of the State University System and is not intended to be used for any other purpose. This restriction is not intended to limit the distribution of this report, which is a matter of public record.

# REPORT ON THE AUDIT OF

## BANK ACCOUNT RECONCILIATIONS

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#### MEMORANDUM

TO:

Dr. Mary Jane Saunders

President

FROM:

Morley Barnett

Inspector General

DATE:

June 25, 2010

SUBJ:

AUDIT OF BANK ACCOUNT RECONCILIATIONS

In accordance with the University's Internal Audit Plan for fiscal year 2009-10, we have conducted an audit of the bank account reconciliation function at Florida Atlantic University. The report contained herein presents our scope and objectives and provides comments and conclusions resulting from procedures performed.

We have made three recommendations to address our findings. Management has already taken appropriate corrective action to effectively implement one of the recommendations. The responses of the auditee to the other two recommendations have been incorporated into the report. In accordance with our established procedures, follow-up will be performed subsequent to the issuance of this report to determine effective implementation of these two recommendations by management.

Please call me if you have any questions.

cc:

University Provost Senior Vice Presidents Vice Presidents

Auditee

FAU BOT Audit and Finance Committee Inspector General, Florida Board of Governors

Florida Auditor General

#### **EXECUTIVE SUMMARY**

In accordance with the University's Internal Audit Plan for fiscal year 2009-10, we have conducted an audit of the bank account reconciliation function at Florida Atlantic University for the quarter ended December 31, 2009.

Our audit objectives were to determine whether:

- All bank accounts were being reconciled on a monthly basis;
- Internal controls over the reconciliation process were adequate and effective;
- The bank account reconciliations were properly documented, prepared by independent personnel, and completed in a timely and accurate manner; and,
- Reconciling items were identified and cleared timely.

Audit procedures included, but were not limited to, the evaluation of internal controls as those controls relate to the accomplishment of the foregoing audit objectives, as well as the performance of compliance testing on samples of bank account reconciliations and reconciling items in order to determine whether control procedures were operating effectively.

Based on our observations and tests performed, we are of the opinion that the university's bank account reconciliation operations were being conducted in general compliance with all applicable laws, rules and regulations, university policies and procedures, and sound business practices. However, we identified opportunities for improvement in the following areas:

- Proper segregation of conflicting duties;
- Write-off of unidentified reconciling differences (Reserve bank account); and,
- Timely preparation of monthly account reconciliations (Federal Perkins Loan bank account).

The details of these findings, as well as the suggestions for corrective action, where applicable, can be found in the Comments and Recommendations section of this report.

June 25, 2010

Dr. Mary Jane Saunders President Florida Atlantic University Boca Raton, Florida

Dear President Saunders:

#### SCOPE AND OBJECTIVES

In accordance with the University's Internal Audit Plan for fiscal year 2009-10, we have conducted an audit of the bank account reconciliation function at Florida Atlantic University for the period October 1 through December 31, 2009.

Our audit objectives were to determine whether:

- All bank accounts were being reconciled on a monthly basis;
- Internal controls over the reconciliation process were adequate and effective;
- The bank account reconciliations were properly documented, prepared by independent personnel, and completed in a timely and accurate manner; and,
- Reconciling items were identified and cleared timely.

Audit procedures included, but were not limited to, the evaluation of internal controls as those controls relate to the accomplishment of the foregoing audit objectives, as well as the performance of compliance testing on samples of bank account reconciliations and reconciling items in order to determine whether control procedures were operating effectively.

We obtained an understanding of the activities associated with the bank account reconciliation function by reviewing written policies and procedures, interviewing key personnel, observing actual practices, and analyzing key internal controls. Our assessment of compliance with established policies and procedures was based on reviews of pertinent supporting documentation for samples of bank account reconciling items. Populations, sample sizes, and selection methods were determined based on our evaluation of internal controls and assessment of audit risk, the availability of pertinent University records, and other factors including auditor judgment.

We conducted our audit in accordance with the Institute of Internal Auditors' International Standards for the Professional Practice of Internal Auditing.

#### **BACKGROUND**

All cash needed to meet the operational requirements of the university is currently held in local bank accounts, with any excess cash being invested in the university's Special Purpose Investment Accounts (SPIAs) at the State Treasury. The university is currently responsible for the reconciliation of eight local bank accounts maintained at Bank of America. Six of the eight accounts are owned by FAU, while the FAU Research Corporation and the FAU Finance Corporation (direct support organizations) each own one account respectively. During the course of the audit, a ninth local bank account – the Athletic Petty Cash – was closed because of inactivity.

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The Controller's Office is responsible for the periodic reconciliation of all the abovementioned eight local bank accounts. The *Cash Management* unit of the Controller's Office is responsible for the monthly reconciliation of the Main Depository, Reserve, Accounts Payable, Research Corporation, Payroll, Student Refund, and FAU Finance Corporation bank accounts. The *General Accounting* unit of the Controller's Office is responsible for the monthly reconciliation of the Federal Perkins Loan Fund bank account. As of 12/31/09, the combined cash balances of all eight local bank accounts amounted to \$3,913,945.27 as follows:

	Corresponding Banner GL Cash-in-Bank	
Bank Account Name	<u>Account</u>	Bank Account Balance
		<u>(12/31/09)</u>
Main Depository Account	11200 (Cash-in-Bank – Bank Fund)	\$425,732.71
Reserve Account	11226 (Cash-in-Bank – Reserve Account)	\$3,360,195.48
Accounts Payable	11205 (Cash-in-Bank – Accounts Payable)	\$0.00
Payroll Account	11210 (Cash-in-Bank – Payroll)	\$0.00
Student Refund Account	11220 (Cash-in-Bank – Student Refunds	\$0.00
	Fund)	
Research Corporation	11215 (Cash-in-Bank – Research Corp)	\$0.00
Federal Perkins Loan Fund	11225 (Cash-in-Bank – Perkins Loan Fund)	\$128,017.08
FAU Finance Corporation	11230 (FAU Finance Corporation)	\$0.00

Total \$3,913,945.27

Under the university's current banking arrangement, all monies paid to the university for student tuition & fees, meal plans, housing fees, parking fees, miscellaneous revenues, appropriations from the State, and so on, are initially posted to the Main Depository bank account. On a daily basis, monies are wired from the Main Depository account to the Reserve account to fund newly-issued obligations of the university for employee payroll, vendor payments, student refunds, and student financial aid disbursements. These checks and electronic funds transfers (EFTs) are drawn daily, as applicable, against the Accounts Payable, Research Corporation, Payroll, and Student Refund bank accounts, and on an ongoing basis, these items will be presented for payment against the aforementioned bank accounts which have been established as *zero balance accounts* (ZBAs). As such, any debits (representing checks/EFTs presented for payment) to these four accounts on a given day will be offset at the end of the day by automated clearinghouse (ACH) credit transfers from the Reserve bank account. As a result, the aforementioned four bank accounts will always have *zero balances* at the end of each day.

The Federal Perkins Loan Fund bank account is used to receive daily ACH payments from the third party loan servicer to which borrowers repay Perkins loans received from the university. Currently, the FAU Finance Corporation bank account has a zero balance and is not being used. Future plans call for this account to be used to process housing revenues and expenditures for the Innovation Village

student housing complex when it becomes operational.

To minimize the risk of unauthorized check disbursements, the Controller's Office (via Information Resource Management) submits an electronic file of newly-issued checks to Bank of America on a daily basis. Only those checks listed on this daily positive pay file are authorized to be paid by the bank, with any exceptions being subject to the approval of authorized personnel of the Controller's Office. Currently, all of the local bank accounts are participants in the positive pay system.

#### COMMENTS AND RECOMMENDATIONS

#### **Current Findings and Recommendations**

#### Inadequate Segregation of Conflicting Duties

Our review of current (4/6/10) *User Entitlement Reports* for Cash Management employees with online access to FAU's bank accounts at Bank of America (BOA), indicated the following inadequate segregation of duties for personnel involved (as preparers/reviewers/back-up preparers) in the reconciliation of one or more local bank accounts:

- The Assistant Controller had the capability to independently initiate, approve, and release non-repetitive wire transfers from the FAU Finance Corporation bank account (currently has a zero balance); and, independently initiate, approve, and release positive pay decisions for the Payroll bank account; and,
- An Accountant had the capability to independently initiate and approve positive pay decisions for the Payroll bank account; and, independently initiate, approve, and release issues (of items) for the Payroll bank account. In addition, the Accountant (under another authorized BOA Direct userID) had the capability to independently initiate, modify, and approve positive pay decisions for seven local bank accounts, along with the capability to release positive pay decisions for five of the seven accounts. Another Accountant had the capability to independently initiate, approve, and release issues (of items) for seven local bank accounts.

The current level of access afforded the abovementioned individuals did not provide assurance that a minimum of two Cash Management employees would be involved (on the BOA Direct system) in all online banking transactions involving non-repetitive outgoing wire transfers, decisions to pay or return positive pay exception items, or the electronic issuance of items against local bank accounts. To the extent that the aforementioned employees were involved in the bank account reconciliation process, they had the potential to conceal unauthorized online banking transactions which they themselves may have independently initiated, approved, and released.

#### Recommendation No. 1

We recommend management takes appropriate action to adjust the online banking capabilities of the abovementioned employees of Cash Management such that all non-repetitive wire transfers, positive pay actions, or electronic issuances of payment items initiated by one employee – on the Bank of America Direct system – are unable to be processed without the (online) approval of another employee. In addition, management should implement procedures

to independently monitor user access changes made by the university's administrator of the BOA Direct system, and/or ensure that BOA user entitlements reports for applicable university employees are periodically requested and reviewed by an independent manager to ensure proper segregation of user capabilities.

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#### **Management's Response**

#### **Action Plan:**

The university will require that two staff members be available for positive pay decisions to assure segregation of duties. Entitlement reports showing the online banking capabilities of the Cash Management Department have been provided to the Assistant Vice President for Financial Affairs and University Controller and will be reviewed quarterly.

#### **Implementation Date:**

October 31, 2010

### **Responsible Auditee:**

Stacey Semmel, Assistant Vice President and University Controller

#### Write-Off of Unidentified Reconciling Items

Effective internal control procedures require designated university personnel to prepare and approve monthly reconciliations of bank account balances to the corresponding General Ledger (GL) cash balances to provide assurance that recorded money collections and disbursements are in agreement with bank records, and to permit the timely detection and correction of any unrecorded, erroneous, or unauthorized transactions.

During the course of compliance testing of the monthly reconciliations of the local bank accounts as of December 31, 2009, we were unable to determine the validity of two of twelve reconciling items judgmentally selected for review from the Reserve bank account reconciliation. One item for \$1,288.70 initially appeared on the November 2009 reconciliation, and the second item for \$5,000.00 initially appeared on the December 2009 reconciliation. As of the March 2010 reconciliation of the Reserve bank account, both items remained unidentified and unexplained by management.

On 4/30/10, Cash Management elected to write-off the combined total of both of the abovementioned items - \$6,288.70 – as a monetary loss to the GL expenditure control account of the Student Fee Trust Fund on Banner Finance. Upon further inquiry, we determined that management did not have an approved written policy and procedure addressing the write-off of stale-dated unidentified reconciling differences on the account reconciliations.

#### Recommendation No. 2

Given the materiality of the write-off cited above, we recommend that management develops and implements a written policy and procedure for the write-off of unidentified reconciling items. The guidance should include, at a minimum, a definition of when an unidentified item is considered stale; an evaluation of the sufficiency of the efforts to identify and clear the item; management approvals required for write-off; and, the requisite documentation of the write-off decision.

#### Management's Response\_

#### **Action Plan:**

While the university feels that the amount written-off is not considered material given the total withdrawal and credit activity of the year (approximately six thousandths of one percent - .006%), a policy will be developed to outline approval processes for material amounts.

#### **Implementation Date:**

September 1, 2010

#### **Responsible Auditee:**

Stacey Semmel, Assistant Vice President and University Controller

#### **Corrective Action Already Taken**

#### *Untimely Completion of Federal Perkins Loan Fund Account Reconciliations*

The Federal Perkins Loan Fund bank account is used as a clearing account for ACH payments received daily from a third party loan servicer to which borrowers repay Perkins loans received from the university. During the course of the fall 2009 semester, the General Accounting unit of the Controller's Office assumed the responsibility for performing monthly reconciliations pertaining to the Federal Perkins Loan Fund – a function previously performed by the Student Financial Services unit of the Controller's Office. The position responsible for performing the reconciliations was vacant from October 2009 until it was filled in May 2010.

Existing written procedures and best practice currently require three types of monthly reconciliations to ensure that all Perkins loan payments received are properly recorded, applied, and accounted for on the university financial records:

- Reconciliation of the Perkins Loan Fund Cash-in-Bank GL account balance to the Federal Perkins Loan Fund bank account balance;
- Reconciliation of the Federal Perkins Loan Fund bank account balance to the loan servicer's cash-on-hand monthly report; and,

• Reconciliation of the beginning of the month balance to the end of month balance for the Perkins Loan04 Fund Claim-on-Cash GL account.

Based on discussions with management, and a review of the available Perkins Loan Fund monthly reconciliation records for the 2009/10 fiscal year-to-date, we noted that – *through the end of April 2010* – the monthly reconciliations were not being prepared in a consistently timely manner as follows:

- The latest month for which all three types of monthly reconciliations were completed and signed-off was August 2009;
- Although reconciliations of the Federal Perkins Loan Fund bank account balance to the loan servicer's cash-on-hand report, and reconciliations of the beginning of the month balance to the end of month balance for the Perkins Loan04 Fund Claim-on-Cash GL account were prepared for the months of October 2009 through December 2009, they had not been signed-off and dated by the preparer and an approver, and, as such, we could not ascertain when these reconciliations were originally completed; and,
- There was no documented evidence that reconciliations of any type were prepared during the months of January, February, and March 2010.

According to management, during the period of time in which the responsible position was vacant, a formal reconciliation was not completed, but on a monthly basis Cash Management reviewed the bank statements in addition to the Assistant Controller reviewing the loan servicer's activity. Additionally, the loan servicer's statements were compared to the bank statement. Management believes compensating controls existed as the source of all bank credit activity that flows through this account is managed by the loan servicer.

During the course of the audit, management took appropriate corrective action to ensure the completion of the tardy reconciliations, and, as of 6/8/10, all the requisite reconciliations for the months of September 2009 through May 2010 had been completed and signed-off, with the April and May 2010 reconciliations being completed in a timely manner. To the extent that we were able to verify that this corrective action had been taken prior to the completion of the audit, no further action or response from management is deemed necessary.

#### **Prior Audit Recommendations**

Our examination generally includes a follow-up on findings and recommendations of prior internal audits, where the subjects of such findings are applicable to the scope of the current audit being performed.

Within the past three years, our office has not conducted any audits related to the bank account reconciliation function. Accordingly, a follow-up on prior audit findings is not applicable.

#### **CONCLUSION**

Based on the results of the testwork performed, we are of the opinion that the university's bank account reconciliation operations were being conducted in general compliance with all applicable laws, rules and regulations, policies and procedures, and sound business practices. Notwithstanding this assessment, we have made recommendations to strengthen the existing control environment pertaining to the bank account reconciliation process which we believe are cost-beneficial to implement.

We wish to thank the staff of the Controller's Office for their cooperation and assistance which contributed to the successful completion of this audit.

Morley Barnett, CPA, CFE

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Inspector General

Audit Performed By: Mike Hewett, CIA, CGAP, CBA, CFSA

Allaire Vroman