



A REPORT  
TO THE  
ARIZONA LEGISLATURE

Financial Audit Division

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Report on Internal Control and Compliance

# Northern Arizona University

Year Ended June 30, 2013

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**Debra K. Davenport**  
Auditor General

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Northern Arizona University  
Report on Internal Control and Compliance  
Year Ended June 30, 2013

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**DEBRA K. DAVENPORT, CPA**  
AUDITOR GENERAL

**STATE OF ARIZONA**  
OFFICE OF THE  
**AUDITOR GENERAL**

**MELANIE M. CHESNEY**  
DEPUTY AUDITOR GENERAL

**Independent Auditors' Report on Internal Control over Financial Reporting and on  
Compliance and Other Matters Based on an Audit of Basic Financial Statements  
Performed in Accordance with *Government Auditing Standards***

Members of the Arizona State Legislature

The Arizona Board of Regents

We have audited the financial statements of the business-type activities and discretely presented component unit of the Northern Arizona University as of and for the year ended June 30, 2013, which collectively comprise the University's basic financial statements and have issued our report thereon dated October 28, 2013. Our report includes a reference to other auditors who audited the financial statements of the discretely presented component unit, as described in our report on the University's financial statements. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. However, the financial statements of the discretely presented component unit were not audited in accordance with *Government Auditing Standards*, and accordingly, this report does not include reporting on internal control over financial reporting or compliance associated with the discretely presented component unit.

### **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 opinions on the basic 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 and Recommendations, we identified certain deficiencies in internal control that we consider to be a material weakness and significant deficiency.

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 University's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency described in the accompanying Schedule of Findings and Recommendations as item 2013-01 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 deficiencies described in the accompanying Schedule of Findings and Recommendations as item 2013-02 to be a significant deficiency.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the University's basic 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 Arizona University's Responses to Findings**

Northern Arizona University's responses to the findings identified in our audit are presented on pages 5 through 6. 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 them.

### **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 of 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.

Debbie Davenport  
Auditor General

October 28, 2013

Northern Arizona University  
Schedule of Findings and Recommendations  
Year Ended June 30, 2013

Financial Statement Findings

**2013-01**

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**The University should strengthen its policies and procedures over access controls and change management for its financial accounting system**

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Criteria: Effective system access controls help prevent and detect unauthorized use, damage, loss, or modification of programs and data, including sensitive and confidential information. In addition, no one employee should have the ability to record, review, and approve transactions within the system. Further, effective change controls should ensure that program changes and changes to data are valid, meet user needs, are reviewed and approved independently, and are implemented accurately.

Condition and context: The University did not have adequate policies and procedures in place to ensure user access roles within its financial accounting system were compatible with their job responsibilities. Specifically, the University assigned multiple personnel responsibility for approving access to different modules within its system. However, there was no additional review performed to ensure employees were not assigned any incompatible roles and responsibilities within the system. In addition, the University assigned multiple employees the ability to review and approve their own journal entries within the financial accounting system. Further, the Change Management Team was able to perform system updates or database changes using a universal login identification and these changes were not monitored.

Effect: There is an increased risk that users could gain inappropriate access with the ability to manipulate or intentionally misuse financial information or record unauthorized or inaccurate changes. In addition, transactions could have been inaccurately recorded in the system.

Cause: The University implemented a new financial system at the beginning of the fiscal year and did not develop policies and procedures for reviewing system access controls for incompatible duties or for monitoring changes made to the system.

Recommendation: The University should develop and implement policies and procedures for both reviewing system access controls to prevent incompatible duties from being assigned to an employee and monitoring changes made to the system. Specifically, the University should review its existing employees' system access to ensure that employees' access is proper based on their job description and correct any incompatible duties identified. In addition, the University should develop a system for monitoring changes made by the Change Management Team to ensure all system and program changes are authorized, reviewed, tested, and approved prior to being implemented. Further, each team member should have a separate login to make changes to the system.

Northern Arizona University  
Schedule of Findings and Recommendations  
Year Ended June 30, 2013

**2013-02**

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**The University should follow its policies and procedures when preparing financial statements**

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Criteria: The University should follow its policies and procedure to ensure its financial statements are prepared in accordance with U.S. generally accepted accounting principles. Accurate financial statements provide valuable information to those charged with governance, management, and other financial statement users, to make important decisions about the University's financial operations.

Condition and context: The University did not follow its policies and procedures to conduct a thorough review of its financial statements to ensure proper report presentation. Specifically, the University incorrectly reported approximately \$9 million in capital leases and capital assets on its Statement of Cash Flows for a capital lease and did not properly disclose approximately \$37 million in noncash transactions for its defeasance of bonds. Also, the University overstated accounts receivable and understated expenses, each by approximately \$5 million because information was not correctly set up in its new financial accounting system.

Effect: The University's financial statements were not initially prepared in accordance with U.S. Generally accepted accounting principles. The University made recommended audit adjustments to the financial statements for all significant errors and misclassifications.

Cause: In an effort to help ensure the financial statements were issued in a timely manner and because of implementation delays with a new financial accounting system, the University's review time was reduced, which increased the risk of compilation errors.

Recommendation: To help ensure the accuracy of the University's financial statements, the University should strengthen its existing internal control policies and procedures by requiring a thorough review of the financial statements by someone who is independent of the person preparing the financial statements and knowledgeable of the University operations and reporting requirements.

# UNIVERSITY RESPONSE



# NORTHERN ARIZONA UNIVERSITY

COMPTROLLER'S OFFICE

November 26, 2013

Debra K. Davenport, CPA  
Auditor General  
2910 N. 44<sup>th</sup> Street, Suite 410  
Phoenix, AZ 85018

Dear Ms. Davenport,

The University has reviewed the schedule of findings and recommendations associated with the annual audit of the University's Annual Financial reports for the year ended June 30, 2013. We concur with the audit findings and will implement procedures to strengthen access controls and to ensure proper review of the University financial statements.

I have attached the University's response and action plan to the recommended changes as well as the anticipated implementation date.

If you have any questions please do not hesitate to contact me at 928 523-6054.

Cordially,

Robert G. Norton  
Associate Vice President and Comptroller



# NORTHERN ARIZONA UNIVERSITY

## COMPTROLLER'S OFFICE

13-01

*The University has reviewed the audit finding and recommendation associated with the annual audit of the University's Annual Financial Report for the year ended June 30, 2013. We concur with the audit finding and recommendation. The implementation of the University's new financial system presented many challenges, and we recognized the risks associated with our implementation decisions. We have since taken steps to mitigate the risks. Prior to the Auditor General's review, an internal security review was completed in April, 2013 which identified issues consistent with the audit findings and resulted in the removal of incompatible security roles and responsibilities from certain users. In addition, workflow approval was implemented in May, 2013 to limit the ability to self-approve journals within the central accounting office. In addition to these actions, we will take the following steps to further address the audit findings:*

- We will implement a 2<sup>nd</sup> level security access review to help ensure that system access is consistent with user job responsibilities and incompatible security access is not granted across system modules.*
- We will develop monitoring tools to help identify system access vulnerabilities and use the information to take corrective actions.*
- NAU Information Technology Services recognizes the accountability issue associated with the use of a shared user ID in our change management procedures for modifications to our PeopleSoft systems. We will immediately begin investigating our options for providing a more granular level of accountability within the constraints of the Oracle/PeopleSoft application product as well as possible monitoring controls.*

*Completion of the above corrective action steps will be by May 1, 2014.*

13-02

*The University has reviewed the audit finding and recommendation associated with the annual audit of the University's Annual Financial Report for the year ended June 30, 2013. We concur with the audit finding and recommendation. The University will take the following corrective actions:*

- The University will improve the financial statement review process to ensure accounting standards and applicable NAU policies and procedures are followed, and that transactions are recorded and reported correctly. We will also consider the need to implement additional review procedures and checklists, shift staff responsibilities and or add staffing resources to help ensure timely and accurate financial reporting.*
- The University made recommended audit adjustments to the financial statements for all significant errors and misclassifications and the final financial statements were revised in time to report the accurate numbers for financial statement production.*
- While the findings represent certain financial reporting risks, we believe that with the corrective actions taken our annual financial report accurately reflects the University's financial position. In addition, we believe the risks were not the result of nor did not lead to any loss of assets through malfeasance or theft.*

