

**UNIVERSITY OF VIRGINIA
BOARD OF VISITORS**

**Meeting of the Audit, Compliance,
and Risk Committee**

December 6, 2018

AUDIT, COMPLIANCE, AND RISK COMMITTEE

Thursday, December 6, 2018

4:00 – 5:00 p.m.

Board Room, The Rotunda

Committee Members:

Babur B. Lateef, M.D., Chair
Robert M. Blue
Mark T. Bowles
L.D. Britt, M.D.
James B. Murray Jr.
C. Evans Poston Jr.
Frank M. Conner III, Ex-off
Adelaide Wilcox King, Faculty Consulting Member

AGENDA

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I. REMARKS BY THE COMMITTEE CHAIR (Dr. Lateef)	1
II. COMMITTEE DISCUSSION	
A. Auditor of Public Accounts Audit and Management Report for FY 2017-2018 (Ms. Melody Bianchetto to introduce Mr. Eric Sandridge; Mr. Sandridge to report)	2
• Action Item: Auditor of Public Accounts' Findings for FY 2017-2018	
B. Construction Management: Financial Controls and Project Monitoring (Ms. Saint to introduce Mr. Donald Sundgren; Mr. Sundgren to report)	3
C. Enterprise Risk Management Program Report on FY 2019 Goals (Ms. Saint to introduce Mr. James Matteo; Mr. Matteo to report)	11
III. WRITTEN REPORTS	
• Office of Audit and Compliance: Summary of Current Activities	12
IV. CLOSED SESSION	
Discussion and consideration of the performance of specific administrative personnel; discussion of information technology security-related matters; and discussion of proprietary, business-related information pertaining to Medical Center operations as provided for in Section 2.2-3711(A)(1), (19) and (22) of the <u>Code of Virginia</u>	

**UNIVERSITY OF VIRGINIA
BOARD OF VISITORS AGENDA ITEM SUMMARY**

BOARD MEETING: December 6, 2018

COMMITTEE: Audit, Compliance, and Risk

AGENDA ITEM: I. Remarks by the Committee Chair

ACTION REQUIRED: None

BACKGROUND: Dr. Babur Lateef, the Committee Chair, will open the meeting and provide an overview of the agenda.

**UNIVERSITY OF VIRGINIA
BOARD OF VISITORS AGENDA ITEM SUMMARY**

BOARD MEETING: December 6, 2018

COMMITTEE: Audit, Compliance, and Risk

AGENDA ITEM: II.A Auditor of Public Accounts Audit and Management Report for FY 2017-2018

BACKGROUND: The Auditor of Public Accounts (APA) of the Commonwealth conducts an annual audit of the University and the Medical Center and reports findings to the Board. Ms. Bianchetto will introduce Mr. Eric M. Sandridge, Director of Higher Education Programs for the Virginia Auditor of Public Accounts, who will report on the fiscal year 2017-2018 audit.

DISCUSSION: Mr. Sandridge will present the required communications on the auditor's opinion, scope of internal control work, compliance testing, fraud and illegal acts, significant accounting policies, alternative accounting treatments, accounting estimates, significant audit adjustments (if any), and disagreements with management (if any).

ACTION REQUIRED: Approval by the Audit, Compliance, and Risk Committee and by the Board of Visitors

AUDITOR OF PUBLIC ACCOUNTS' FINDINGS FOR FY 2017-2018

RESOLVED, the Auditor of Public Accounts' Findings for FY 2017-2018, are approved as recommended by the Audit, Compliance, and Risk Committee.

**UNIVERSITY OF VIRGINIA
BOARD OF VISITORS AGENDA ITEM SUMMARY**

BOARD MEETING: December 6, 2018

COMMITTEE: Audit, Compliance, and Risk

AGENDA ITEM: II.B. Construction Management: Financial Controls and Project Monitoring

ACTION REQUIRED: None

BACKGROUND: UVA’s Audit Department engaged ResX, PC (ResX) to perform an interim audit of the University’s Hospital Expansion Project (HEP). The audit report was issued on June 4, 2018.

The HEP comprises expansion of the Emergency Department and the surgical services suite on the second level, development of a six-story inpatient tower, and expansion of ancillary spaces on the lower level. New construction is approximately 425,000 square feet and renovation is approximately 95,000 square feet. The work will encompass new drop off and entries into the Emergency Department for ambulance and ambulatory patients. The Board of Visitors approved this project, with an estimated cost of \$322 to \$394 million, in March 2015.

Mr. Donald Sundgren, Associate Vice President and Chief Facilities Officer, will discuss improvements to be implemented based on audit recommendations and review Facilities Management’s processes for overseeing the University’s construction portfolio.

The following table is an excerpt from the report, summarizing priority audit findings (4 P2 findings) and process improvement recommendations:

**Summary Recommendations and Management's Corrective Action Plans
Refer to ResX Report for Details of Each Observation and Recommendation**

Note: Corrective action plans are not required for process improvement recommendations

ResX issue #	Priority Rating	Observation	Recommendation	Management's Corrective Action Plan	Responsible Person & Expected Completion Date
Audit Topic: Mark-Ups					
III.1 Page 4	P2	<p>Contracts signed with Skanska allowed it to bill \$336,354 more in mark-up than Skanska would have billed if it were required to adhere to the rates it bid in its Pricing Proposal</p> <p>Refer to detailed analysis highlighting calculations supporting \$336,354 in mark-up overcharges in Attachment #2.</p>	<p>Mark-ups agreed to in the Pricing Proposal should be incorporated into all of the CM's contracts. If multiple contracts are used to complete a project, mark-ups should be tracked on a consolidated schedule to ensure compliance with the overall agreed upon mark-up percentages.</p> <p>See report page 8 for more detail on a related process improvement recommendation.</p>	<p>The mark-ups cover CM services and include a variety of cost elements. Those in the pricing proposal for the initial contract applied to that contracted scope of work. While on many projects those mark-ups would apply to the full project, this project had numerous contracts awarded over a period of years and the mark-ups for each of those contracts were negotiated separately for the various scopes of work. We will do a comparative analysis of the mark-ups for our records.</p>	<p>George Southwell/ Jeff Moore</p> <p>9/30/18</p>
Audit Topic: Change Order Approval Process					

ResX issue #	Priority Rating	Observation	Recommendation	Management's Corrective Action Plan	Responsible Person & Expected Completion Date
III.2.A Page 4	P2	Skanska's CO No. 12 with Bell BCI Company (Bell) stated a Payment and Performance Bond was needed based on the contract value of \$46,146,897 unable to be bonded through Subguard.	<ol style="list-style-type: none"> 1. UVA should determine to what extent Bell was not covered by CM's Subguard insurance and issue a deductive CO to the CM for the amount of any shortfall (potentially \$622,938 or 1.35% of contract value) 2. UVA Facilities Management, in consultation with UVA Risk Management, should study the use of bonds on the Project and whether coverage provided by these bonds overlap with coverages available under Skanska's Subguard insurance. 	<p>Bell was covered by the Subguard program for the initial portions of the work. For subsequent contracts Bell obtained a separate Performance and Payment Bond. UVA was charged the Subguard rate but was not charged for the cost of the separate Payment and Performance Bond. As a follow-up we will do a cost comparison of the two programs for the work that was bonded separately.</p> <p>Our analysis showed that the coverages do not overlap. We would be glad to review with UVA Risk Management.</p>	George Southwell/ Jeff Moore 9/30/18
III.2.B Page 5	P2	Change order prices were not consistently approved before work was underway	<ol style="list-style-type: none"> 1. Ensure change orders are approved timely. Document the negotiation process so that the CO file or electronic directory includes the initial proposal and management's 	There was a negotiated fixed price for each of the change orders prior to commencement	Jeff Moore 12/31/18

ResX issue #	Priority Rating	Observation	Recommendation	Management's Corrective Action Plan	Responsible Person & Expected Completion Date
		<p>or completed for 6 COs tested (67% of all CO dollars).</p> <p>During testing, we did not find evidence of negotiation with subcontractors prior to work commencing.</p>	<p>response and proposed modifications to the proposal. There should be some proof of "negotiation" in the file to inform the approval process.</p> <p>2. If work commences before CO approval, ensure HECOM requirements are followed by either tracking cost of work in the field and obtaining reimbursement on a cost basis or establishing a negotiated fixed price prior to commencing the work.</p> <p>3. Field activities (e.g. labor hours, equipment usage, or material usage) related to any CO started before the CO price is approved should be tracked to that actual costs can be estimated. In this manner, the CO price can be set at cost plus the CM's contractual mark-ups.</p>	<p>of the work, however in some cases the multi-layer approval process had not been completed. We will emphasize that the approvals are to be in place prior to commencement of the work unless, at the judgment of the team, there is a compelling reason for the work to move forward prior to formal approval. We will also review our approval process to see if there are opportunities to reduce the time typically required for approvals.</p>	
Audit Topic: Design Assist Subcontractors					
III.4 Page 6	P2	The subcontractors invited to simultaneously bid both design assist work and the subsequent construction work eventually	1. If the final construction documents for Design Assist Subs' (D-A Subs) scope of work results in a material increase in the D-A Subs' price as compared to the original bid, consider rebidding the work, if possible.	We maintain the option of re-bidding the D-A Subs scope of work at any time prior to the execution of the construction contract, as we	Jeff Moore 9/30/18

ResX issue #	Priority Rating	Observation	Recommendation	Management's Corrective Action Plan	Responsible Person & Expected Completion Date
		<p>negotiated contracts that were higher than their original bids.</p> <p>For example, Bell Mechanical's bid of \$39.5 million (as memorialized in the MON) increased by \$7.2 million once the design was complete. This increase was incorporated into Bell's various subcontracts. The increase was not processed as a change order because the change in scope occurred during pre-construction and before the final contracts were executed.</p>	<p>2. If re-bidding in the open market is not feasible: a) engage an engineering/estimating firm to perform a 3rd party review of the proposed additional scope and price, with a documented letter of recommendation from the reviewer. b) retain the right to conduct a close-out audit of the D-A Sub.</p>	<p>have done on some of our projects. In this case the cost increase was a result of recognized scope increases and the pricing was reviewed and reconciled with a 3rd party estimating firm.</p> <p>We will review the D-A Subs language in our RFP documents to be sure there is clarity regarding our process and options.</p> <p>Our existing audit clause gives us audit rights for the D-A Subs.</p>	

Process Improvement Recommendations: Management Response Not Required

Audit Topic: Subguard Insurance Mark-Up			
ResX issue #	Priority Rating	Observation	Recommendation
III.3 Page 5	PI	Skanska was permitted to use its in-house captive self-insurance program, for which UVA has no audit rights, to cover subcontractor default risk. The rate charged, 1.35% of total subcontractor cost, generally exceeds normal market rates from recognized sources (e.g. Zurich Insurance) which charges rates from 0.75% to 1.25% of the enrolled subcontractor costs.	Given the potential for savings available in the market for Subguard products, UVA should consider allowing 3 rd parties to compete with a CM's captive insurer.
Audit Topic: eBuilder System			
III.5 Page 6	PI	The eBuilder system does not contain all the Project's records because it was implemented after the project was underway. Consequently, early project documentation, including bid related documents) was not routinely entered into the system.	Ensure all project documents are uploaded into eBuilder to ensure completeness of file and enable audit or management review
Audit Topic: Price Proposal			
III.6 Page	PI	Skanska inserted a series of end notes in its Price Proposal that added new terms to UVA's Price Proposal form. Skanska's end notes were overruled by language in the RFP, and the contracts signed stipulated the order of document precedence. Allowing the CM to insert end notes underscores the importance of including audit rights language in the contract documents that is at a higher level of precedence than the Price Proposal.	Continue to ensure audit rights are inserted in contract documents with the highest order of precedence. Limit or eliminate contracting parties' ability to insert end notes in Price Proposals that could change contract terms.
Process Improvements and Recommendations: Fixed Price Contract Controls			
IV.1 Pages 6-9	PI	If fixed price contracts are to be used, then control of the bidding process, is critical to ensuring project costs are minimized.	CM should bid all rates at cost (labor, Subguard, CCIP, builder's risk) except for their CM fee, which should be the only rate within which the CM is allowed to cover overhead and profit. Rates bid at cost should be auditable and if found to contain profit, should be

			adjusted through execution of a retroactive deductive CO.
	PI	See overall observation on fixed price contract controls on page 4.	Subguard mark-up should only be applied to subcontractors with contracts valued in excess of \$500k that are enrolled in the Subguard program. The CM's contract should specify the amount allowed as a deductible on the Subguard policy.
	PI	See overall observation on fixed price contract controls on page 4.	UVA should have the right to audit any financial representation made by the CM in its pricing proposal and all costs incurred during the course of the contract, including subcontractor costs, even if the contract is a fixed price.
	PI	See overall observation on fixed price contract controls on page 4.	If subcontractors are engaged to provide design assist services, this should either be communicated in the scope description provided in UVA's request for proposals (RFP) for architectural/engineering (A/E) and in the RFP for CM services. If these RFPs do not stipulate the use of DA-Subs, UVA should consider negotiating a deduct from the A/E's contract price and/or from the CM's price, if any of the design assist services are expected to reduce the scope of work of the A/E or CM during pre-construction.
Process Improvement Recommendations: Contracts, Other			
	PI	Certain items were not observed to be included in contract documents reviewed (HECOM, CO-7, HECO-7, and HECO-9CM)	<p>Consider modifying future CM contracts by adding these items on the HECO-9CM contract form signed by the parties.</p> <p>Audit rights: UVA should have the right to audit the accounting records underlying any cost based representation made in the CM's price proposal and the accounting records of the CM's subcontractors related to any cost based representation made during the bidding process.</p> <p>UVA should state in its audit clause that it has the right to audit any subcontractor's books and records related to its cost of work.</p>

	PI	Additional items to consider adding to HECO-9CM (Construction Manager at Risk with Design Phase Services UVA contract template)	CM In-House Insurance Programs: CM should not be allowed to use an in-house captive insurance program unless it can demonstrate it is properly underwritten. Rates charged by an in-house captive should not exceed market.
	PI		Contingency: CM should issue a change order when removing funds from the contingency account. The change order should be approved by UVA. All unused contingency money should be returned to UVA.
	PI		CO Pricing: As noted elsewhere in the report, field activities related any CO started before the CO price is approved should be tracked by the CM. The eventual price of the CO should be set based on the actual field cost plus a mark-ups established in the contract.

Priority Rating Definitions

Individual findings are evaluated with the context of the area under review. Audit findings are classified into categories as defined below. The Audit Department assigns each of the findings in this report to one of these categories to assist management in the prioritization and implementation of audit recommendations.

Ratings for Internal Audit Testing Results		
1	Priority 1	A Priority 1 item signifies a control and/or process deficiency of sufficiently high risk that it provides minimal or no assurance that institutional objectives will be achieved. Management must take immediate corrective action to mitigate Priority 1 deficiencies.
2	Priority 2	A Priority 2 item signifies a control and/ or process deficiency that hinders the effectiveness and efficiency of operations, potentially impeding the attainment of institutional objectives. Management must take timely corrective action to mitigate Priority 2 deficiencies.
PI	Process Improvement	A process improvement item signifies an opportunity to achieve additional control and/or process efficiencies.

**UNIVERSITY OF VIRGINIA
BOARD OF VISITORS AGENDA ITEM SUMMARY**

<u>BOARD MEETING:</u>	December 6, 2018
<u>COMMITTEE:</u>	Audit, Compliance, and Risk
<u>AGENDA ITEM:</u>	II.C. Enterprise Risk Management Program Report on FY 2019 Goals
<u>ACTION REQUIRED:</u>	None

BACKGROUND: The Enterprise Risk Management (ERM) Charter (amended and approved in September 2017) states that the program’s mission is to:

[S]trengthen the University’s ability to achieve its mission and strategic objectives. This is done by effectively managing key risks and seizing opportunities related to the achievement of our strategic objectives. In this context, risk encompasses both negative events (downside risk) and opportunities (upside risk). An effective ERM program helps the University effectively deploy its resources in pursuit of its objectives.

In keeping with the ERM mission, FY 2018 program goal accomplishments included:

- Enhancing communication and discussion among executives and board members related to key risk management
- Strengthening risk management efforts through better understanding and use of risk appetite and key risk indicators
- Updating the ERM charter
- Better aligning and integrating ERM efforts with University planning and audit cycles

DISCUSSION: Mr. James Matteo, Associate Vice President and Treasurer, will report on the ERM program and on the following FY 2019 goals:

1. Working to further on-board Wise into the ERM program
2. Building a key-risk interaction map
3. Moving ERM data into the Governance Risk Compliance (GRC) system being implemented by Audit
4. Revising the annual ERM cycle and governance structure

**UNIVERSITY OF VIRGINIA
BOARD OF VISITORS AGENDA ITEM SUMMARY**

BOARD MEETING: December 6, 2018

COMMITTEE: Audit, Compliance, and Risk

AGENDA ITEM: III. Office of Audit and Compliance: Summary of Current Activities

ACTION REQUIRED: None

BACKGROUND: The Office of Audit & Compliance Status Report outlines activities since the September 2018 Board of Visitors meeting including: audits completed and in flight; a summary of Priority 1 and Priority 2 audit findings reported; status of management action plans due within the period; and activities of the Institutional Compliance function.

Audit Projects Completed and In Flight Since September 2018 Board of Visitors Meeting:

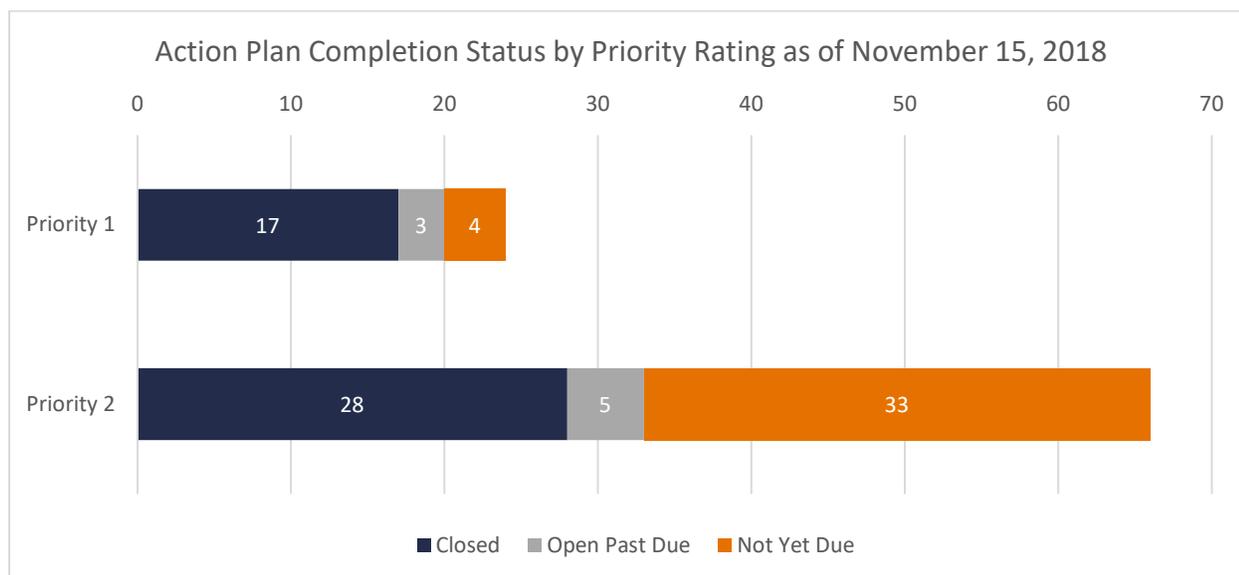
Project Status	Audit Subject	UVA Division
Completed	Network Security: Intrusion Prevention and Detection, Firewalls	Academic
Completed	Distributed IT Systems Management	Academic
Completed	UVa College at Wise Risk Assessment	College at Wise
In progress	Title IX Complaint Management (Phase 2 of Minors Protections Audit) conducted under direction of Counsel	Pan-University
In progress	NIST 800-171 (Controlled Unclassified Information) Ivy Environment	Pan-University
In progress	Sub-Recipient Monitoring	Pan-University
In progress	COSO Internal Controls: Payroll	Pan-University
In progress	Presidential Turnover Audit	Pan-University
In progress	Workday Data Analysis for Effort Reporting	Pan-University
In progress	Patient Cash Receipts and Refunds	Health System
In progress	Charge Capture: Neurology	Health System
In progress	Distributed IT Systems Management - Medical Center	Health System
In progress	Clinical Trial Billing	Health System
In progress	Ivy Mountain Musculoskeletal Center Construction Audit	Academic
In progress	UVA Wise Budget Process	Academic

Summary of Prioritized Audit Findings Reported Sept 2018 to Date:				
Audit Subject	Responsible Unit	P1	P2	PI
Executive VP Travel and Entertainment	Executive VP/COO		3	
UVA Network Security	Information Technology Services		12	6
Total rated findings reported for the period			15	6

For Priority Rating Definitions see page 10 above

Status of Management’s Action Plans for Priority 1 and Priority 2 Findings

IIA Standard 2500: Monitoring Progress requires the chief audit executive to establish and maintain a system to monitor the disposition of results communicated to management. The chart below displays the status of management’s action plans through November 15, 2018.



Details of Open Past Due Action Plans

Audit	Past Due Action Item	Priority Rating	Action Plan Owner
Travel & Expense Management	Administrative System Changes: Awaiting testing documentation to confirm resolution of segregation of duties issue.(Due 9/30/18)	P1	Korby Griffith, PSDS Finance Manager
Travel & Expense Management	Email and Vacation Delegated Approvals: Awaiting testing documentation to confirm resolution	P1	Korby Griffith, PSDS Finance Manager, and Lisa Atkins, ITC EA

Audit	Past Due Action Item	Priority Rating	Action Plan Owner
	of segregation of duties issue. (Due 9/30/18)		Business Systems Analyst
Travel & Expense Management	Escalation of Policy Violations: SOP in process of development. (Due 9/30/18)	P1	Raegan Harouff, PSDS Travel, Expense & Card Programs Manager
Travel & Expense Management	Monitoring for Split Transactions: SOP in process of development. (Due 9/30/18)	P2	Korby Griffith, PSDS Finance Manager
Travel & Expense Management	Expense Processing Delays: Training program developed and operationalized; escalation procedures in development. (Due 9/30/18)	P2	Korby Griffith, PSDS Finance Manager
Construction-Hospital Expansion	Analyze Markup Terms in Comparative Contracts: In process. (Due 9/30/18)	P2	George Southwell, Health System Director; Jeff Moore, Construction Services and Contracts Administration Director
Construction-Hospital Expansion	Compare Costs of Performance Bond Options: In process. (Due 9/30/18)	P2	George Southwell, Health System Director; Jeff Moore, Construction Services and Contracts Administration Director
Construction-Hospital Expansion	Review RFP Language for Design-Assist Subcontractors: In process. (Due 9/30/18)	P2	Jeff Moore, Construction Services and Contracts Administration Director

Procurement and Supplier Diversity Services (PSDS) is accepting the risk of the following action plan, which was classified with a Priority 2 rating in the audit report. The Audit Department is closing the action plan. (Action plan originally due 9/30/18)

Data Inconsistencies between Systems: Because ExpenseUVA does not support transaction controls, transactions are blocked during the interface to the Integrated System (IS) and require manual correction by ITS/PSDS. These changes are not reflected in ExpenseUVA, introducing inconsistencies between the two systems. Because Expense UVA is not as accurate and complete as the IS, reports run in ExpenseUVA still have the potential to introduce decision making risks. In light of the way the systems are used, PSDS assesses the decision making risk as low and believes the reporting risk is acceptable.

Institutional Compliance Activities:

1. Participated in Gartner’s Ignition Diagnostics program to conduct a thorough assessment of the university’s compliance program, using industry best practices and a questionnaire completed by institutional compliance as well as the members of the

compliance network, in order to develop future strategic objectives for the compliance program. Results are being evaluated and will be shared with the Board of Visitors at its next meeting.

2. Explored additional uses for the Medical Center's IntegriLink compliance incident management system for potential use by institutional compliance and the academic division. Partnered with the Medical Center on a joint contract with NAVEX to develop a web form through which anonymous reports could be made to the university.
3. Continued to conduct best practices research and participate in professional development programs to confirm that the university has appropriate compliance practices in place. Attended the November, 2018 meeting of the University Compliance Leadership Group to analyze best practices with the compliance officers from 20 other top-tier universities. Mr. Gary Nimax moderated a session about the impact of the #metoo movement on higher education.
4. Partnered with the University of Richmond to identify compliance contacts at other Virginia universities to develop relationships, address state-specific requirements, and expand peer network. The first meeting of the group was held in November 2018.