

APPROVED BY THE
COMMITTEE

AUG 31 2011

Michele M. Thompson
SECRETARY OF THE BOARD

MEETING OF THE AUDIT, BUDGET, FINANCE, AND FACILITIES COMMITTEE
OF THE BOARD OF TRUSTEES OF THE UNIVERSITY OF ILLINOIS

July 11, 2011

This meeting of the Audit, Budget, Finance, and Facilities Committee was held on Monday, July 11, 2011, beginning at 1:00 p.m. via videoconference in Room 1030, National Center for Supercomputing Applications, 1205 West Clark Street, Urbana; Room 414, Administrative Office Building, 1737 West Polk Street, Chicago; and the Hatmaker Room, Room 550, Public Affairs Center, One University Plaza, Springfield. Trustee Oliver, acting as chair of the committee in Trustee McMillan's absence, convened the meeting and asked the clerk to call the roll. The following committee members were present: Mr. James D. Montgomery, Mr. Lawrence Oliver, and Ms. Pamela B. Strobel.

Also present were President Michael J. Hogan; Mr. Walter K. Knorr, vice president/chief financial officer and comptroller; Dr. Robert A. Easter, interim vice president, University of Illinois and chancellor of the Urbana campus; Dr. Avijit Ghosh, special assistant to the president; Mr. Thomas P. Hardy, executive director for University relations; Mr. Thomas R. Bearrows, University counsel; Mr. Lester H. McKeever, Jr., treasurer; and Dr. Michele M. Thompson, secretary.

Attached is a listing of other staff members in attendance at this meeting, as well as some members of the media.

Mr. Oliver welcomed everyone to the meeting and stated that the first item on the agenda was to approve the minutes from the meeting that was held on May 31, 2011. On motion of Mr. Montgomery, and seconded by Ms. Strobel, the minutes were approved unanimously.

**REVIEW OF RECOMMENDED BOARD ITEMS FOR THE MEETING OF THE BOARD
OF TRUSTEES OF THE UNIVERSITY OF ILLINOIS ON JULY 21, 2011**

Purchase Recommendations

Next, Mr. Oliver asked Dr. Heather Haberaecker, executive assistant vice president for business and finance, to review the purchase recommendations (materials on file with the clerk) that will be on the agenda at the meeting of the Board of Trustees on July 21, 2011. Dr. Haberaecker discussed two purchase recommendations totaling \$5.2 million at Urbana and provided information about each. She stated that the recommended purchase for mercury deposition analytical services for the Prairie Research Institute and Illinois Water Survey is grant funded, and she also provided details regarding the recommended purchase of subscriptions to electronic journals at the University Library for \$1.7 million. She responded to questions from committee members, and a brief discussion regarding each purchase followed. Dr. Haberaecker stated that discussions related to purchases of electronic journals that could be used at all three campuses is ongoing, and explained that currently, each campus library purchases its own electronic journals or obtains a discount by purchasing them through a consortium.

There was no opposition to any of these recommendations being advanced to the Board as a whole.

REPORTS TO THE COMMITTEE

Investment Update

Mr. Oliver introduced Mr. Brady O'Connell and Ms. Angela Cantillon, both from Hewitt EnnisKnupp, Inc., and asked them to provide an investment update. Mr. O'Connell referred to the third slide in the presentation (materials on file with the clerk) and provided an update on capital markets, stating that it has been a volatile but positive year. He advised focusing on long term rates of return with quarterly monitoring, and stated that the investment market has been strong in 2011. Ms. Cantillon reviewed the allocation of investments and reported that seven managers are responsible for the operating pool assets, with 71 percent invested in low risk money market mutual funds, and she discussed causes for volatility within the operating pool assets. She then presented the operating pool performance and reported that it has outperformed its benchmark over the quarter and the one year period. She stated that its underperformance during the five and ten year period was due to challenging markets in 2007 and 2008, and she reported that an average of \$23.8 million of income has been the average generated per year over the last ten years. She and Mr. O'Connell provided additional information about benchmark indices, and Mr. Douglas E. Beckmann, senior associate vice president for business and finance, stated that greater liquidity is needed at this time because of State finances and cash flow issues.

Dr. Peter J. Newman, assistant vice president for treasury operations, discussed continuous monitoring and analysis of operating pool balances and investments, and referred to recent changes in the policy dictating the ranges of asset allocation, which he said provide greater flexibility. He also emphasized diversification among fund providers, and Ms. Strobel inquired about the possibility of using a product that would provide greater investment returns while meeting the need for liquidity. Dr. Newman referred to a request for proposal that has been

issued to qualify additional managers and strategies to increase income and reduce risk. He also emphasized the need to maintain cash for payroll or bills, adding that a line of credit cannot be used for payroll purposes.

Ms. Cantillon then presented a report on the endowment pool market value and asset allocation as of May 31, 2011, noting that this is an interim policy allocation. She did not recommend any action at this time. She presented the endowment pool performance as of March 31, 2011, and stated that it has outperformed its policy benchmark during the quarter and one year period and underperformed over longer term periods. She discussed challenges with equity managers, and then presented charts depicting the current asset allocation policy and the asset allocation policy that was approved by the Board in January 2011. She reviewed the reasons for suggesting these changes and stated that this will result in a modestly higher rate of return with lower risk. Next, she reviewed the implementation schedule for these recommendations, and committee members discussed the schedule, whether the timing could be expedited, and difficulties with the procurement process. With no additional questions or comments, Mr. Oliver thanked Mr. O'Connell and Ms. Cantillon for their presentation.

Long Term Debt Update

Next, Mr. Oliver asked Mr. Knorr to provide a presentation on long term debt (materials on file with the clerk). Mr. Knorr provided information regarding the University's current long term outstanding debt of slightly more than \$1.6 billion, and stated that this is composed primarily of auxiliary facilities debt. He reported that other areas of debt have resulted from certificates of participation, health facilities, construction of the south campus at Chicago, and an energy service contract that was issued for the College of Veterinary Medicine at Urbana. He then discussed bonds that were issued the previous week, which were approved by the Board in June,

and stated that the majority of the funding from these will be used to fund the construction of Ikenberry Commons at Urbana. He reported that \$14.0 million was used to refund outstanding debt and achieve a lower interest rate. Mr. Knorr then discussed the University's credit rating and said Moody's and Standard and Poor's most recent ratings maintained their previous ratings of the University with a negative outlook. He thanked his colleagues at the University for working with the credit rating agencies, and he provided some additional information about the process of working with the agencies throughout the year.

Internal Audit Plan for Fiscal Years 2012-2013

Mr. Oliver then asked Ms. Julie A. Zemaitis, executive director of University Audits, to present the internal audit plan for fiscal years 2012 and 2013. Ms. Zemaitis began her presentation (materials on file with the clerk) by stating that the creation of a two year plan is required by State Statute and that this plan has been approved by President Hogan and reviewed by Mr. McKeever, treasurer, and Trustee McMillan, chair of the Audit, Budget, Finance, and Facilities Committee. She emphasized that this plan is risk-based and is designed to enable responsiveness. She presented a slide depicting some elements of the plan and the development process, and she provided a list of risk categories in the audit development plan. She discussed high level focus areas and presented a chart depicting the concentration of planned hours, and then showed the distribution of high impact planned hours in several areas. Next, she presented the distribution of planned hours by campus and area compared to fiscal year 2011, and stated that the fluctuation in hours spent on healthcare is due to changes in staffing, noting that the two remaining healthcare auditor positions that are open on her staff should be filled in time for audits to be conducted in fiscal year 2013. She then referred to the last slide in her presentation, which she said provides a performance metric that analyzes audit universe coverage, and

described methods for analyzing this coverage. She reviewed audit coverage for the past five years and planned coverage for the next two years in various areas of the University and noted that these percentages reflect a presence in each area, rather than a full audit.

Committee members briefly discussed the presentation, and Ms. Zemaitis provided additional information regarding the allocation of high impact hours and creating the audit plan. Mr. McKeever stated that he is proud of the progress that has been made in the area of internal audits, and said the assessment of risk areas is very sophisticated.

External Audit Scope – Fiscal Year 2011

Mr. Oliver then asked Mr. Beckmann to introduce the next presenters. Mr. Beckmann introduced Ms. Maxine Sandretto, assistant vice president for business and finance, who he said oversees the external audit that is provided by auditors hired by the Illinois Auditor General; Mr. Patrick Patterson, controller and assistant vice president for business and finance, who he said is responsible for financial aspects of the audit; and Ms. Jackie Dippel and Ms. Cathy Baumann, both from the firm KPMG, and hired by the Auditor General. He then asked Mr. Patterson to begin the presentation on the external audit (materials on file with the clerk).

Mr. Patterson stated that the University receives external financial and compliance audits annually, and explained that these are conducted by KPMG as special assistant to the Office of the Auditor General. He introduced Ms. Jackie Dippel and Ms. Cathy Baumann, both representatives from KPMG, to provide information about these audits. Ms. Dippel stated that this is the third year that KPMG has performed these audits, and she reviewed the audit scope and deliverables for the fiscal year that ended on June 30, 2011. She provided a list of members of the engagement team involved in the audit, described objectives and responsibilities, and presented four phases of audit methodology. She also discussed the reliance on reports from

other external auditors for University Related Organizations, and she told the committee that the engagement team will also include the use of a firm as a subcontractor. She presented preliminary risk assessments and the planned audit approach for each, reported on the OMB Circular A-133 Federal single audit, and provided information regarding State compliance attestation and supplemental financial information. She then discussed engagement timing, listed new accounting pronouncements, and provided information about KPMG's Audit Committee Institute, which she said is a resource for Board members, committee members, and administration. Mr. Patterson referred to the audit timeline, and he described University efforts to support KPMG and the Office of the Auditor General throughout the audit process. Mr. Oliver thanked Mr. Patterson, Ms. Dippel, and Ms. Baumann for the presentation.

Preliminary Budget Request

Next, Mr. Oliver asked Dr. W. Randall Kangas, associate vice president for planning and budgeting, to provide a presentation (materials on file with the clerk) regarding the fiscal year 2013 preliminary budget request. Dr. Kangas reviewed current key issues and stated that this draft addresses the University's competitive position, facilities stewardship, and unavoidable costs. He described the timeline and cycle for this process and explained that a budget request is required by State Statute and helps identify University priorities. He referred to campus capital priority requests, emphasized the need for repair and renovation, and said a combined priority list will be available at a later date. Dr. Kangas provided additional information regarding the capital budget and the status of capital funding from fiscal year 2010, and noted that there was no capital budget in fiscal years 2011 or 2012.

Legislative, State Budget, and Finance Update

Mr. Knorr stated that the governor signed the appropriations bill on June 30, 2011, that includes a 1.15 percent reduction to the University's current (fiscal year 2011) appropriation. He said that as of June 30, 2011, the State had not paid \$313.0 million of its appropriation to the University from fiscal year 2011, and said it may be paid by the end of the calendar year. He reported that the State may be able to advance some funds from the fiscal year 2012 appropriation through the Educational Assistance Fund, although he indicated this is not certain. He also stated that the State failed to provide for the transfer of funds for the State surveys (Prairie Institute), totaling approximately \$16.0 million, and stated that he is unsure why the transfer did not occur.

OLD BUSINESS

There was no business presented under this aegis.

NEW BUSINESS

There was no business presented under this aegis.

MEETING ADJOURNED

Mr. Oliver requested a motion to adjourn the meeting. On motion of Mr. Montgomery, seconded by Ms. Strobel, the meeting adjourned at 2:30 p.m.

Respectfully submitted,



Michele M. Thompson

Clerk



Edward L. McMillan

Chair



Eileen B. Cable

Assistant Clerk

**AUDIT, BUDGET, FINANCE, AND FACILITIES COMMITTEE
STAFF AND PUBLIC ATTENDANCE, MEETING OF JULY 11, 2011**

Urbana Campus Site

Mike Bass, Senior Associate Vice President for Capital Programs and Real Estate Services
Cathy Baumann, Partner, KPMG
Doug Beckmann, Senior Associate Vice President for Business and Finance
Jackie Dippel, Partner, KPMG
Dean Hagan, Director of University Investments
Randy Kangas, Associate Vice President for Planning and Budgeting
Janier Koss, Staff, Board of Trustees Office
Jo Menacher, Associate Director, Planning and Budgeting
Peter Newman, Assistant Vice President, Treasury Operations
Pat Patterson, Controller and Assistant Vice President, Business and Financial Services
Sean Powers, WILL Radio
Menah Pratt-Clarke, Associate Chancellor, Urbana-Champaign Campus
Scott Rice, Senior Associate University Counsel
Maxine Sandretto, Assistant Vice President for Business and Finance, Urbana-Champaign Campus
Larry Schook, Interim Vice President for Research
Joseph Vitosky, Assistant Vice President, Capital Programs and Real Estate Services
Julie Zemaitis, Executive Director of University Audits

Chicago Campus Site

Jerry L. Bauman, Interim Vice Chancellor for Academic Affairs and Provost, Chicago Campus
Mark Donovan, Vice Chancellor for Administrative Services, Chicago Campus
Heather Haberaecker, Executive Assistant Vice President for Business and Finance, Chicago Campus
Angela Cantillon, Associate, Hewitt EnnisKnupp, Inc.
Brady O'Connell, Principal, Hewitt EnnisKnupp, Inc.

Springfield Campus Site

Aaron Shures, Associate Provost, Director of Business and Financial Analysis, Springfield Campus

8/2/11