University of North Texas System

Board of Regents

Schedule of Events for
Audit and Finance Committee Meeting

December 17, 2020

Real-Time Livestream Link: https://livestream.com/accounts/7090653/events/9427702

The University of North Texas System Board of Regents Audit and Finance Committee will meet on December 17, 2020, from 3:30 p.m. until approximately 5.00 p.m. according to the following agenda. It is necessary to conduct this special called meeting by videoconference with no in-person attendance due to the request by the Office of the Attorney General to allow for the advance of the public health goal of limiting face-to-face meetings (also called social distancing) to slow the spread of Coronavirus (COVID-19). The meeting will be livestreamed in real time for public attendance at the link listed in this posting.

The Audit and Finance Committee is posted as an individual meeting of a Board committee; however, any members of the Board may attend committee meetings. Because some Board members who are not committee members may attend committee meetings and thereby create a quorum of the full Board, the meeting of the Audit and Finance Committee is also being posted as a meeting of the full Board.

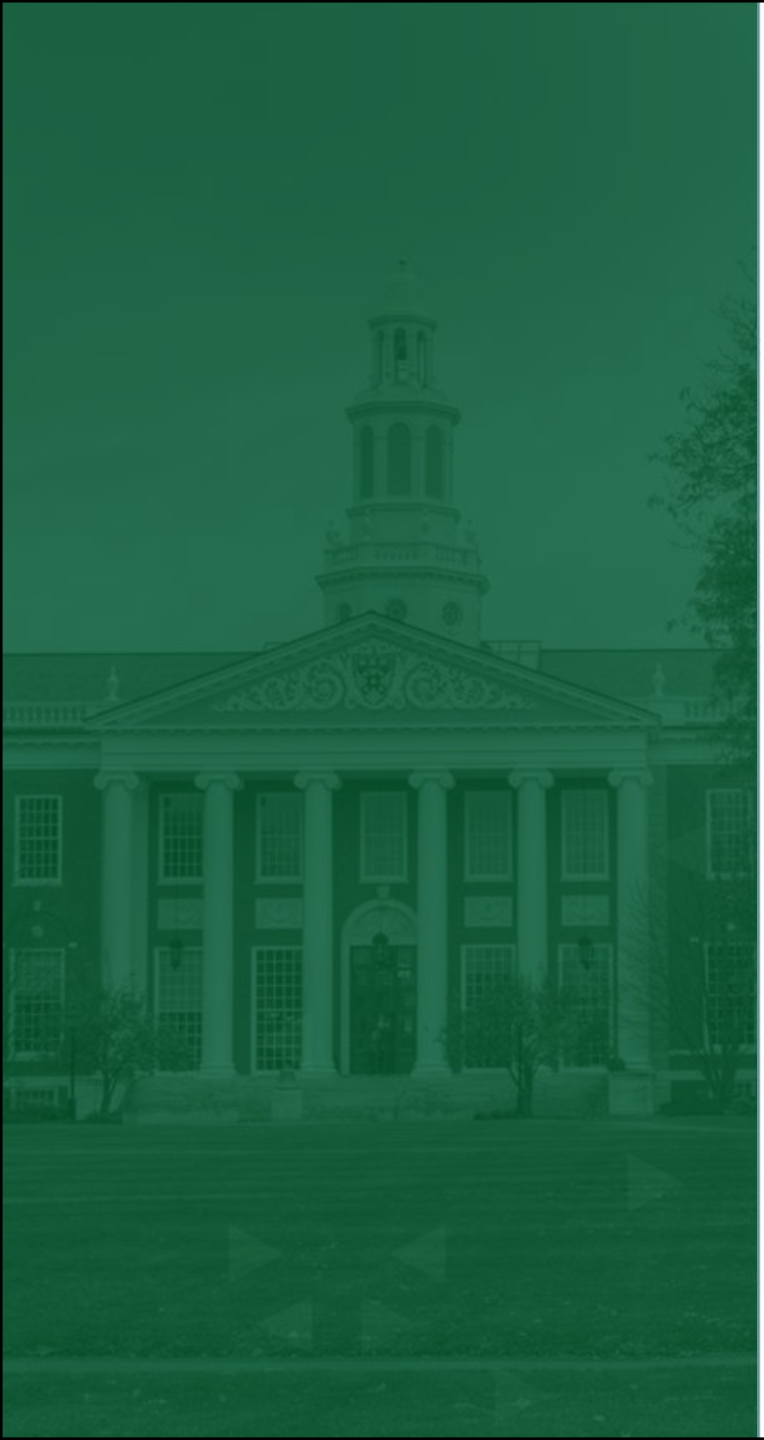
Please contact the Office of the Board Secretary with any questions at 214.752.5533.

3:30 p.m. **CONVENE AUDIT AND FINANCE COMMITTEE**

Action Item:

UNTS Acceptance of the Externally Audited UNT System FY20 Comprehensive Annual Financial Report

5:00 p.m. **ADJOURN AUDIT AND FINANCE COMMITTEE**



University of North Texas System

Results of the August 31, 2020 financial statement audit, internal control matters and other required communications

Sara E. Grenier, CPA
Partner
Fort Worth | 817.332.2301
sgrenier@bkd.com

Derek Pfeifer
Senior Manager
Fort Worth | 817.332.2301
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December 17, 2020

2020 Audit Results

	SYSTEM
Accomplished audit plan & timeline	✓
Good client assistance & responsiveness	✓
Unmodified “clean” opinion on financial statements	✓
Audit Journal Entries – None	✓
Passed Adjustments – 3 entries and one disclosure identified by BKD. 2 identified by management/prior auditors	✓
Significant deficiencies or material weaknesses in internal controls – One noted related to classification of net position	✓

AGENDA

- Summary of Our Audit Approach & Results
- Significant Estimates
- Reconciliation of Change in Net Position
- Required Communications
- Internal Control Over Financial Reporting
- Future Accounting Pronouncements

BKD

Summary of Audit Approach and Results

- Focus on areas of higher risk
- Objective – express an opinion on conformity of financial statements in accordance with GAAP
- Areas of emphasis:
  - Management override of controls
  - Revenue recognition
  - Valuation of investments
  - Classification of net position
  - Net pension and OPEB liabilities

Significant Estimates

- Allowance for doubtful accounts
- Valuation of investment securities
- Defined benefit pension assumptions
- Other postemployment benefit plan assumptions

Reconciliation of Change in Net Position

We proposed the following adjustments that were determined by management to be immaterial, both individually and in the aggregate, to the financial statements as whole.

	Before Misstatements	Misstatements	Subsequent to Misstatements	% Change
Current Assets	587,765,428		587,765,428	
Non-Current Assets & Deferred Outflows	2,248,317,200	(6,616,303)	2,241,700,897	-0.29%
Current Liabilities	(513,551,575)	5,955,639	(507,595,936)	-1.16%
Non-Current Liabilities & Deferred Inflows	(1,623,025,345)		(1,623,025,345)	
Current Ratio	1.145		1.158	1.14%
Total Assets & Deferred Outflows	2,836,082,628	(6,616,303)	2,829,466,325	-0.23%
Total Liabilities & Deferred Inflows	(2,136,576,920)	5,955,639	(2,130,621,281)	-0.28%
Total Net Position	(699,505,708)	660,664	(698,845,044)	-0.09%
Operating Revenues	(668,258,616)		(668,258,616)	
Operating Expenses	1,161,488,859	1,457,968	1,162,946,827	0.13%
Nonoperating (Revenues) Exp	(473,151,238)		(473,151,238)	
Change in Net Position	20,079,004	1,457,968	21,536,972	7.26%

Uncorrected disclosures:
Alternative investment reported as Level 1 investment in equities rather than Level 2 in fair value disclosure

BKD

Required Communications

Auditor’s Responsibility Under Auditing Standards Generally Accepted in the United States of America and the Standards Applicable to Financial Audits Contained in *Government Auditing Standards* Issued by the Comptroller General of the United States

BKD

Required Communications (continued)

- Significant Accounting Policies – Note 1
- Alternative Accounting Treatments – No matters are reportable
- Auditor's Judgments About the Quality of Accounting Policies – No matters are reportable
- Management Judgments & Accounting Estimates
- Financial Statement Disclosures
  - Investments and fair value
  - Defined benefit pension plan
  - Other postemployment benefit plans

BKD

Internal Control Over Financial Reporting

We considered the System's internal control over financial reporting as a basis for designing our audit procedures.

- Deficiency
- Significant deficiency
- Material weakness

BKD

Significant Deficiency

Adjustments were required for net position to be reported in accordance with generally accepted accounting principles between net investment in capital assets, restricted net position and unrestricted net position. We recommend management review procedures to ensure controls are in place related to the proper classification of net position.

Deficiencies

During the 2020 audit, management and BKD identified misstatements within capital assets

- Ending CIP and payables were overstated due to manual accruals
- 2020 additions were overstated for construction in 2019
- Property purchased in 2019 was misclassified

Other items communicated verbally

Future Accounting Pronouncements

- GASB Statement No. 87, *Leases*
  - Single model for lease accounting based on the principle that leases represent the financing of the right to use an underlying asset
  - Effective for the System's fiscal year 2022

UNT System Response to FY2020 External Audit Results

UNT System Board of Regents' Audit & Finance Committee

Paula Welch, AVC for Finance & System Controller

December 17, 2020

Agenda

- Overview of Findings
- Background – Historical Perspective
- Current Control Initiative
- Audit Deficiencies with Planned Remediation
- Questions

Overview of Findings

- UNT System is one of two university systems in Texas to attain an external financial audit.
  - Enables strong financial management and operational improvements.
- Recommend acceptance of the unmodified opinion; BKD performed a very comprehensive audit.
- Two Deficiencies:
  - Adjustments between Net Invested in Capital Assets, Restricted and Unrestricted Net Position. (Significant deficiency)
  - Capital Asset misstatements in construction accruals and asset classification.

Background

Controller Division created in FY2015.

Audit History

- FY2014
  - First UNT System external audit performed by Grant Thornton, LLP.
  - Primarily substantive testing. Control structure in development.
  - Audit report presented August 2015.
- FY2015 – 2018
  - Annual audits performed by Grant Thornton, LLP.
  - Transitioned from substantive testing to controls testing.
  - Substantially accelerated completion date. (FY2017 and FY2018 – February 6 months)
- FY2019
  - Audit performed by Grant Thornton, LLP
  - Controls based testing
  - Accelerated completion date to 12/19/2019
- FY2020
  - Audit performed by BKD, LLP
  - Controls based testing
  - Completion date 12/17/2020

Fiscal Year	Audit Firm	Report Date	BOR Meeting
2014	Grant Thornton, LLP	07/31/2015	08/2015
2015	Grant Thornton, LLP	08/19/2016	08/2016
2016	Grant Thornton, LLP	05/01/2017	05/2017
2017	Grant Thornton, LLP	02/22/2018	02/2018
2018	Grant Thornton, LLP	02/14/2019	02/2019
2019	Grant Thornton, LLP	12/19/2019	02/2020
2020	BKD, LLP	12/17/2020	02/2021

Internal Control Improvement Initiative - Reconciliations

Established May 2020 under the UNT System Controller

Population: GL Balance Sheet Account Reconciliations

- Phase I: Review and document current controls
- Phase II: Develop aging of accounts (in process)
- Phase III: Implement formal controls program
- Phase IV: Automate data reconciliation

Significant Deficiency – Net Position

Allocation of Net Position – Net Invested in Capital Assets (NICA) and Unrestricted

Net Investment in Capital Assets is the difference between the amount shown for capital assets, net of depreciation and outstanding debt incurred to finance those capital assets.

<u>NICA - $21 million</u>

- Unspent bond proceeds were not included in the NICA calculation.
  - NACUBO guidance recommends unspent bond proceeds should not be included in NICA calculation.
  - In FY2018, based on the NACUBO guidance, the Controller directed that unspent bond proceeds should not be included in the NICA calculation.
  - Prior auditors supported decision.
- Planned Remediation
  - Recalculate NICA for all 4 business units to include unspent bond proceeds where applicable.
  - Update template to include unspent bond proceeds.
  - Update process documentation and provide training on NICA calculation.

Significant Deficiency – Net Position (cont'd)

Allocation of Net Position Restricted and Unrestricted

Quasi-Endowments – $12.7 million

- Quasi-endowments were treated as restricted net position regardless of the source in prior years.
  - GASB 34 requires restriction based on the source of funds.
    - Restricted by donor/grantor (external) – Restricted Net Position
    - Restricted by management (internal) – Unrestricted Net Position
- Planned Remediation
  - Reclassify historical tax credits to unrestricted. ($10.9 million)
  - Reclassify one UNT quasi-endowment to unrestricted. ($1.8 million)
  - Review all endowments to validate classification and reclassify as necessary in FY2021.
  - Provide training on restricted v unrestricted net position classification.

Deficiency – Capital Assets

Construction in Progress (CIP) expense accrual overstated by $6 million

- Standard templates and processes were not followed for FY2020 year-end accruals.
  - Duplicate accruals – manual journal entries and automated invoice payment through Accounts Payable (AP).
  - AP close was later than prior years.
  - Review and reconciliation of year-end accrual was completed before FY2020 AP closed.
- Planned Remediation
  - Review and update training as needed and provide for new employee once hired.
  - Work with Procurement to establish FY2021 AP closing date and communicate before year-end.
  - Provide training for all Controller teams to ensure a basic understanding of capital asset and CIP accounting and strengthen expertise and review.
  - CIP process is included as part of the new Control Improvement Initiative to ensure controls are present and functioning as designed.

Deficiency – Capital Assets (cont'd)

Capital Assets Misclassified

- FY2020 Additions to Capital Assets were overstated related to construction that was completed in FY2019.
  - Discovered during testing and corrected prior to closing year-end.
- Misclassification of a building purchased in FY2018 as land.
  - Initial communication (email) was unclear as to asset type.
  - Depreciation expense was not recognized until FY2020.
- Planned Remediation
  - Develop and train new process for purchased land and buildings to ensure the asset type is clearly communicated and formally documented.
  - Provide training to campus property teams to ensure a clear understanding of asset capitalization classification and thresholds.

?

Questions

Board Briefing

Committee: Audit & Finance

Date Filed: December 9, 2020

Title: Acceptance of the Externally Audited UNT System FY20 Comprehensive Annual Financial Report

Background:

BKD will present results of the External Audit of the UNT System FY20 Comprehensive Annual Financial Report. The UNT System Audit and Finance Committee Charter, adopted May 14, 2020 established a responsibility for the Audit and Finance Committee to provide governance and oversight and annually review the external auditor's audit scope and approach, and to review, approve, and recommend to the Board of Regents the Comprehensive Annual Financial Report (CAFR) and Independent Auditor's Report.

Financial Analysis/History:

The Board of Regents directed management to obtain an external audit of the FY2020 Comprehensive Annual Financial Report.

Dan Tenney Digitally signed by Dan Tenney Date: 2020.12.11 14:20:31 -06'00'

Vice Chancellor for Finance

Legal Review:

This item has been reviewed by General Counsel.

Alan Stucky Digitally signed by Alan Stucky Date: 2020.12.11 13:38:22 -06'00'

Vice Chancellor/General Counsel

Schedule:

The External Audit Opinion of UNT System's FY20 Comprehensive Annual Financial Report will be included in the System's annual report upon approval.

Recommendation:

It is recommended that the Board of Regents accept the Externally Audited UNT System FY20 Comprehensive Annual Financial Report, and direct that the External Audit Opinion Letter be included in the System's Annual Report.

Recommended By:

Dan Tenney

Vice Chancellor

Lesa B. Roe Digitally signed by Lesa B. Roe Date: 2020.12.11 14:23:28 -06'00'

Chancellor

Attachments Filed Electronically:

- BKD report on the 2020 financial statement audit, internal control matters and other required communications.
- Findings Required to be Reported by Government Auditing Standards
- UNTS Response to FY20 Externally Audited CAFR

Board Order

Title: Acceptance of the Externally Audited UNT System FY20 Comprehensive Annual Financial Report

At an official meeting of the Board of Regents of the University of North Texas System properly posted and held on February 4-5, 2021, pursuant to a motion made by Regent and seconded by Regent , the Board approved the motion presented below:

Whereas, the UNT System Audit and Finance Committee Charter, adopted May 14, 2020 established a responsibility for the Audit and Finance Committee to provide governance and oversight and annually review the external auditor's audit scope and approach, and to review, approve, and recommend to the Board of Regents the Comprehensive Annual Financial Report (CAFR) and Independent Auditor's Report, and

Whereas, the external audit firm, BKD, LLP, conducted an audit of UNT System FY20 Comprehensive Annual Financial Statements, and provided an unmodified opinion, which is the best possible opinion, and

Whereas, the Board of Regents has reviewed the FY20 Comprehensive Annual Financial Report and the final audit opinion of the UNT System FY20 Comprehensive Annual Financial Report,

Now, Therefore, The Board of Regents authorizes and approves the following:

1. Acceptance of the Externally Audited UNT System FY20 Comprehensive Annual Financial Report

2. Inclusion of the Audit Opinion letter in the final UNT System FY20 Comprehensive Annual Financial Report

VOTE: ____ ayes ____ nays ____ abstentions

BOARD ACTION:

Attested By:

Approved By:

Rosemary R. Haggett, Secretary
Board of Regents

Laura Wright, Chair
Board of Regents

University of North Texas System

Report to the Board of Regents

December 17, 2020

Results of the 2020 financial statement audit, internal control matters and other required communications.

BKD
CPAs & Advisors

Contents

2020 Audit Results

Appendices

BKD
CPAs & Advisors

777 Main Street, Suite 2000 | Fort Worth, TX 76102-5332
817.332.2301 | Fax 817.338.4608 | bkd.com

December 17, 2020

Board of Regents
University of North Texas System
1112 Dallas Drive, Suite 4000
Denton, TX 76205

Dear Board of Regents:

We have completed our audit of the basic financial statements of the business-type activities and aggregate discretely presented component units of the University of North Texas System (collectively referred to as the "System"), as of and for the year ended August 31, 2020. This report includes communication required under auditing standards generally accepted in the United States of America as well as other matters.

Our audit plan represented an approach responsive to the assessment of risk of material misstatement in financial reporting for the System. Specifically, auditing standards require us to:

- Express an opinion on the August 31, 2020, financial statements and supplementary information of the System.
- Report on internal control over financial reporting and on compliance and other matters based on an audit of the financial statements performed in accordance with *Government Auditing Standards*.
- Issue communications required under auditing standards generally accepted in the United States of America to assist the Board in overseeing management's financial reporting and disclosure process.

This report also presents an overview of areas of audit emphasis, as well as future accounting standards and industry developments for the higher education and health care environment.

This communication is intended solely for the information and use of management, the Board of Governors and others within the System and is not intended to be, and should not be, used by anyone other than these specified parties.

Very truly yours,

Sara E Grenier

Sara E. Grenier
Partner

Summary of Our Audit Approach & Results

Our Approach

BKD's audit approach focuses on areas of higher risk—the unique characteristics of the System's operating environment, the design effectiveness of your internal controls and your financial statement amounts and disclosures. The objective is to express an opinion on the conformity of your financial statements, in all material respects, with accounting principles generally accepted in the United States of America.

Areas of Audit Emphasis

The principal areas of audit emphasis and results were as follows:

Risk Area	Results
• *Management override of controls* – The risk that management may override existing and functioning accounting controls is an inherent risk to the System.	➲ No matters are reportable.
• *Revenue recognition* – The risk that revenue is improperly categorized or recorded in the improper period. This risk includes timing of recognition of tuition and fee revenue and the consideration of the allowance for doubtful accounts.	➲ No matters are reportable.
• *Revenue recognition (Health Science Center)* – The risk that revenue is improperly categorized or recorded in the improper period. This risk includes consideration of the allowance for doubtful accounts, contractual allowances and consideration of amounts due to/from third-party payers	➲ No matters are reportable.
• *Valuation of investments* – The assumptions and methods used by treasury to value difficult-to-value investments, such as alternative investments.	➲ No matters are reportable.
• *Net position classification* – The risk that management has improperly classified ending net position.	➲ After adjustments, amounts and disclosures are appropriate
• *Net pension and OPEB liabilities* – the risk that the census data provided to the actuary was not correct or the disclosures were not complete	➲ No matters are reportable

Significant Estimates

The preparation of the financial statements requires considerable judgment because some assets, liabilities, revenues and expenses are “estimated” based on management’s assumptions about future outcomes. Estimates may be dependent on assumptions related to economic or environmental conditions, regulatory reform or changes in industry trends.

Some estimates are inherently more difficult to evaluate and highly susceptible to variation because the assumptions relating to future outcomes have a higher degree of uncertainty. To the extent future outcomes are different than expected, management’s estimates are adjusted in future periods, sometimes having a significant effect on subsequent period financial statements. The following are considered to be significant estimates for the System:

- **Allowance for Doubtful Accounts**– Management’s estimate for the allowance is based on historical collection, payer mix and anticipated trends.
- **Valuation of Investment Securities –** Management values investments at fair value as of the statement of net position date. Accounting standards define fair value as the price that would be received to sell a financial asset in an orderly transaction between market participants at the measurement date. Investments are valued using quoted market prices or third-party sources, including appraisers and valuation specialists, when available.
- **Defined Benefit Pension and Other Postemployment Benefit Plan Assumptions –** Assumptions are based on actuarial valuations based on age of participants, past history of the System and expected future return on investments.

Opinion

Unmodified, or “Clean,” Opinion Issued on Financial Statements

We have issued an unmodified opinion as to whether basic financial statements of the business-type activities and aggregate discretely presented component units of the University of North Texas System, as of and for the year August 31, 2020, are fairly presented, in all material respects.

Reconciliation of Change in Net Assets

We proposed the following adjustments that were determined by management to be immaterial, both individually and in the aggregate, to the financial statements as a whole. A schedule of these uncorrected misstatements is attached.

QUANTITATIVE ANALYSIS

	Before Misstatements	Misstatements	Subsequent to Misstatements	% Change
Current Assets	587,765,428		587,765,428	
Non-Current Assets & Deferred Outflows	2,248,317,200	(6,616,303)	2,241,700,897	-0.29%
Current Liabilities	(513,551,575)	5,955,639	(507,595,936)	-1.16%
Non-Current Liabilities & Deferred Inflows	(1,623,025,345)		(1,623,025,345)	
Current Ratio	1.145		1.158	1.14%
Total Assets & Deferred Outflows	2,836,082,628	(6,616,303)	2,829,466,325	-0.23%
Total Liabilities & Deferred Inflows	(2,136,576,920)	5,955,639	(2,130,621,281)	-0.28%
Total Net Position	(699,505,708)		(699,505,708)	
Operating Revenues	(668,258,616)		(668,258,616)	
Operating Expenses	1,161,488,859	1,457,968	1,162,946,827	0.13%
Nonoperating (Revenues) Exp	(473,151,238)		(473,151,238)	
Change in Net Position	20,079,004	1,145,968	21,536,972	7.26%

Required Communications

Generally accepted auditing standards require the auditor to provide to those charged with governance additional information regarding the scope and results of the audit that may assist you in overseeing management's financial reporting and disclosure process. Below, we summarize these required communications.

Auditor's Responsibility Under Auditing Standards Generally Accepted in the United States of America and the Standards Applicable to Financial Audits Contained in *Government Auditing Standards* Issued by the Comptroller General of the United States

An audit performed in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States is designed to obtain reasonable, rather than absolute, assurance about the financial statements. In performing auditing procedures, we establish scopes of audit tests in relation to the financial statements taken as a whole. Our engagement does not include a detailed audit of every transaction. Our engagement letter more specifically describes our responsibilities.

These standards require communication of significant matters related to the financial statement audit that are relevant to the responsibilities of those charged with governance in overseeing the financial reporting process. Such matters are communicated in the remainder of this communication or have previously been communicated during other phases of the audit. The standards do not require the auditor to design procedures for the purpose of identifying other matters to be communicated with those charged with governance.

An audit of the financial statements does not relieve management or those charged with governance of their responsibilities. Our engagement letter more specifically describes your responsibilities.

Area	Comments
Significant Accounting Policies Significant accounting policies are described in *Note 1* of the financial statements.	With respect to new accounting standards adopted during the year, unusual accounting policies or accounting methods used by the System for unusual transactions, we call to your attention the following: • GASB Statement No. 84, *Fiduciary Activities* was adopted during the fiscal year ended August 31, 2020

Area	Comments
Alternative Accounting Treatments We had discussions with management regarding alternative accounting treatments within accounting principles generally accepted in the United States of America for policies and practices for material items, including recognition, measurement and disclosure considerations related to the accounting for specific transactions as well as general accounting policies listed in the adjacent comments section.	• No matters are reportable
Management Judgments & Accounting Estimates Accounting estimates are an integral part of financial statement preparation by management, based on its judgments. Areas involving significant areas of such estimates for which we are prepared to discuss management's estimation process and our procedures for testing the reasonableness of those estimates are listed in the adjacent comments section.	• Refer to Significant Estimates section of this report
Financial Statement Disclosures The areas listed in the adjacent comments section involve particularly sensitive financial statement disclosures for which we are prepared to discuss the issues involved and related judgments made in formulating those disclosures.	• Investments and determination of fair values • Defined benefit pension plan • Post-employment benefits other than pensions
Audit Adjustments During the course of any audit, an auditor may propose adjustments to financial statement amounts. Management evaluates our proposals and records those adjustments that, in its judgment, are required to prevent the financial statements from being materially misstated. Some adjustments proposed were not recorded because their aggregate effect is not currently material; however, they involve areas in which adjustments in the future could be material, individually or in the aggregate.	Areas in which adjustments were proposed include: *Proposed Audit Adjustments Recorded* • No matters are reportable *Proposed Audit Adjustments Not Recorded* See attached summary of uncorrected misstatements we aggregated during the current engagement and pertaining to the latest period presented that were determined by management to be immaterial, both individually and in the aggregate, to the financial statements as a whole.

Area	Comments
Auditor's Judgments About the Quality of the System's Accounting Policies During the course of the audit, we made observations regarding the System's application of accounting principles listed in the adjacent comments section.	• No matters are reportable

Other Material Communications

Other material communications between management and us related to the audit include:

- Management representation letter (*attached*)

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements of the System as of and for the year ended August 31, 2020, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, we considered the System's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of System'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 significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies or material weaknesses have been identified. However, as discussed below, we identified a certain deficiency in internal control that we consider to be a significant deficiency.

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 of the System's financial statements on a timely basis. A deficiency in design exists when a control necessary to meet a control objective is missing or an existing control is not properly designed so that, even if the control operates as designed, a control objective would not be met. A deficiency in operation exists when a properly designed control does not operate as designed or when the person performing the control does not possess the necessary authority or competence to perform the control effectively.

Material Weakness – A deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the System's financial statements will not be prevented or detected and corrected on a timely basis.

Significant Deficiency – A deficiency, or 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 observed the following matters that we consider to be deficiencies or significant deficiencies.

Significant Deficiency

Adjustments were required for net position to be reported in accordance with generally accepted accounting principles between net investment in capital assets, restricted net position and unrestricted net position. We recommend management review procedures to ensure controls are in place related to the proper classification of net position.

Deficiencies

During the 2020 audit, management and BKD identified misstatements within capital assets as noted below:

- Ending construction in progress and accounts payable were overstated due to the manual accrual of retainage and invoices for work performed at year end
- 2020 additions were overstated related to construction that was completed in 2019
- Classification of some property in 2019 was misclassified between non-depreciable and depreciable, which also resulted in depreciation expense being understated in 2019 and 2020

Management should review these manual processes and see what additional controls could be put in place to ensure amounts are correct at the end of the year.

We also observed matters that we consider to be deficiencies that we communicated to management or orally.

This communication is intended solely for the information and use of management, the Board of Regents, the Finance and Audit Committee, others within the System and is not intended to be and should not be used by anyone other than these specified parties.

BKD, LLP

Fort Worth, Texas
December 17, 2020

Future Accounting Pronouncements

GASB Statement No. 87, *Leases*

In June 2017, GASB published Statement No. 87, *Leases*. This Statement was the result of a multi-year project to re-examine the accounting and financial reporting for leases. The new Statement establishes a single model for lease accounting based on the principle that leases represent the financing of the right to use an underlying asset. Specifically, GASB 87 includes the following accounting guidance for lessees and lessors:

Lessee Accounting: A lessee will recognize a liability measured at the present value of payments expected to be made for the lease term, and an intangible asset measured at the amount of the initial lease liability, plus any payments made to the lessor at or before the beginning of the lease and certain indirect costs. A lessee will reduce the liability as payments are made and recognize an outflow of resources for interest on the liability. The asset will be amortized by the lessee over the shorter of the lease term or the useful life of the asset.

The lease term used to measure the asset or liability is based on the period in which the lessee has the noncancelable right to use the underlying asset. The lease term also contemplates any lease extension or termination option that is reasonably certain of being exercised.

GASB 87 does not apply to leases for intangible assets, biological assets (i.e. timber and living plants and animals), service concession agreements or leases in which the underlying asset is financed with conduit debt that is reported by the lessor. Additionally, leases with a maximum possible term of 12 months or less are excluded.

GASB 87 is effective for fiscal years beginning after June 15, 2021. Early application is encouraged. It is anticipated that leases would be recognized using the facts and circumstances in effect at the beginning of the period of implementation.

December 17, 2020

BKD, LLP
Certified Public Accountants
777 Main Street, Suite 200
Fort Worth, Texas 76102

We are providing this letter in connection with your audit of the basic financial statements of the business-type activities and discretely presented component units of the University of North Texas System (System) as of and for the year ended August 31, 2020. We confirm that we are responsible for the fair presentation of the financial statements in conformity with accounting principles generally accepted in the United States of America. We are also responsible for adopting sound accounting policies, establishing and maintaining effective internal control over financial reporting, operations and compliance, and preventing and detecting fraud.

Certain representations in this letter are described as being limited to matters that are material. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement.

We confirm, to the best of our knowledge and belief, the following:

1. We have fulfilled our responsibilities, as set out in the terms of our engagement letter dated May 1, 2020, for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America.

2. We acknowledge our responsibility for the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

3. We acknowledge our responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud.

4. We have provided you with:

    (a) Access to all information of which we are aware that is relevant to the preparation and fair presentation of the financial statements such as records, documentation and other matters.

    (b) Additional information that you have requested from us for the purpose of the audit.

    (c) Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.

    (d) All minutes of meetings of the governing body held through the date of this letter.

(e) All significant contracts and grants.

5. All transactions have been recorded in the accounting records and are reflected in the financial statements.

6. We have informed you of all current risks of a material amount that are not adequately prevented or detected by entity procedures with respect to:

   (a) Misappropriation of assets.

   (b) Misrepresented or misstated assets, liabilities or net position.

7. We believe the effects of the uncorrected financial statement misstatements summarized in the attached schedule are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

8. We have no knowledge of any known or suspected:

   (a) Fraudulent financial reporting or misappropriation of assets involving management or employees who have significant roles in internal control.

   (b) Fraudulent financial reporting or misappropriation of assets involving others that could have a material effect on the financial statements.

9. We have no knowledge of any allegations of fraud or suspected fraud affecting the System received in communications from employees, customers, regulators, suppliers or others.

10. We have disclosed to you the identity of the entity's related parties and all the related party relationships and transactions of which we are aware. Related party relationships and transactions have been appropriately accounted for and disclosed in accordance with accounting principles generally accepted in the United States of America. We understand that the term <u>related party</u> refers to an affiliate; management, and members of their immediate families, component units; and any other party with which the entity may deal if it can significantly influence, or be influenced by, the management or operating policies of the other. The term <u>affiliate</u> refers to a party that directly or indirectly controls, or is controlled by, or is under common control with us.

11. Except as reflected in the financial statements, there are no:

    (a) Plans or intentions that may materially affect carrying values or classifications of assets and liabilities.

    (b) Material transactions omitted or improperly recorded in the financial statements.

    (c) Material gain/loss contingencies requiring accrual or disclosure, including those arising from environmental remediation obligations.

    (d) Events occurring subsequent to the statement of net position date through the date of this letter requiring adjustment or disclosure in the financial statements.

(e) Events occurring subsequent to the statement of net position date through the date of this letter requiring adjustment or disclosure in the financial statements.

(f) Agreements to purchase assets previously sold.

(g) Restrictions on cash balances or compensating balance agreements.

(h) Guarantees, whether written or oral, under which the System is contingently liable.

12. We have disclosed to you all known instances of noncompliance or suspected noncompliance with laws and regulations whose effects should be considered when preparing financial statements.

13. We have no reason to believe the System owes any penalties or payments under the Employer Shared Responsibility Provisions of the Patient Protection and Affordable Care Act nor have we received any correspondence from the IRS or other agencies indicating such payments may be due.

14. We have disclosed to you all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements. The effects of all known actual or possible litigation and claims have been accounted for and disclosed in accordance with accounting principles generally accepted in the United States of America.

15. Adequate provisions and allowances have been accrued for any material losses from:

(a) Uncollectible receivables.

(b) Reducing obsolete or excess inventories to estimated net realizable value.

(c) Sales commitments, including those unable to be fulfilled.

(d) Purchase commitments in excess of normal requirements or above prevailing market prices.

16. Except as disclosed in the financial statements, we have:

(a) Satisfactory title to all recorded assets, and they are not subject to any liens, pledges or other encumbrances.

(b) Complied with all aspects of contractual and grant agreements, for which noncompliance would materially affect the financial statements.

17. We have not been designated as a potentially responsible party (PRP or equivalent status) by the Environmental Protection Agency (EPA) or other cognizant regulatory agency with authority to enforce environmental laws and regulations.

18. We have notified you of any instances of noncompliance with applicable disclosure requirements of the SEC Rule 15c2-12 and applicable state laws.

19. With regard to deposit and investment activities:

    (a) All deposit, repurchase and reverse repurchase agreements and investment transactions have been made in accordance with legal and contractual requirements.

    (b) Disclosures of deposit and investment balances and risks in the financial statements are consistent with our understanding of the applicable laws regarding enforceability of any pledges of collateral.

    (c) We understand that your audit does not represent an opinion regarding the enforceability of any collateral pledges.

20. With respect to any nonattest services you have provided us during the year, including preparing a draft of the CPRIT financial statement and related notes and consulting for the adoption of GASB 87:

    (a) We have designated a qualified management-level individual to be responsible and accountable for overseeing the nonattest services.

    (b) We have established and monitored the performance of the nonattest services to ensure that they meet our objectives.

    (c) We have made any and all decisions involving management functions with respect to the nonattest services and accept full responsibility for such decisions.

    (d) We have evaluated the adequacy of the services performed and any findings that resulted.

21. We acknowledge that we are responsible for compliance with applicable laws, regulations and provisions of contracts and grant agreements.

22. We have identified and disclosed to you all laws, regulations and provisions of contracts and grant agreements that have a direct and material effect on the determination of amounts in our financial statements or other financial data significant to the audit objectives.

23. We have identified and disclosed to you any violations or possible violations of laws, regulations and provisions of contracts and grant agreements whose effects should be considered for recognition and/or disclosure in the financial statements or for your reporting on noncompliance.

24. We have taken or will take timely and appropriate steps to remedy any fraud, abuse, illegal acts or violations of provisions of contracts or grant agreements that you or other auditors report.

25. We have a process to track the status of audit findings and recommendations.

26. We have identified to you any previous financial audits, attestation engagements, performance audits or other studies related to the objectives of your audit and the corrective actions taken to address any significant findings and recommendations made in such audits, attestation engagements or other studies.

27. We have provided our views on any findings, conclusions and recommendations, as well as our planned corrective actions with respect thereto, to you for inclusion in the findings and recommendations referred to in your report on internal control over financial reporting and on compliance and other matters based on your audit of the financial statements performed in accordance with *Government Auditing Standards*.

28. The financial statements disclose all significant estimates and material concentrations known to us. Significant estimates are estimates at the statement of net position date which could change materially within the next year. Concentrations refer to volumes of business, revenues, available sources of supply, or markets for which events could occur which would significantly disrupt normal finances within the next year. Significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

29. The fair values of financial and nonfinancial assets and liabilities, if any, recognized in the financial statements or disclosed in the notes thereto are reasonable estimates based on the methods and assumptions used. The methods and significant assumptions used result in measurements of fair value appropriate for financial statement recognition and disclosure purposes and have been applied consistently from period to period, taking into account any changes in circumstances. The significant assumptions appropriately reflect market participant assumptions.

30. The supplementary information required by the Governmental Accounting Standards Board, consisting of management's discussion and analysis and pension and other postemployment benefit information, has been prepared and is measured and presented in conformity with the applicable GASB pronouncements, and we acknowledge our responsibility for the information. The information contained therein is based on all facts, decisions and conditions currently known to us and is measured using the same methods and assumptions as were used in the preparation of the financial statements. We believe the significant assumptions underlying the measurement and/or presentation of the information are reasonable and appropriate. There has been no change from the preceding period in the methods of measurement and presentation.

31. The System has recognized the amount of the institutional portion of the CARES Act Higher Education Emergency Relief Funds (HEERF) up to the amount of allowable expenditures made as we assert we have met the conditions and expect to meet the conditions of the remaining student portion of HEERF before the end of the period of performance.

32. We acknowledge the current economic volatility presents difficult circumstances and challenges for the higher-education industry. Higher education entities are facing declines in the fair values of investments and other assets, declines in the volume of business, constraints on liquidity and difficulty obtaining financing. We understand the values of the assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments to asset values, allowances for accounts and notes receivable, net realizable value of inventory, etc. that could negatively impact the System's ability to maintain sufficient liquidity. We acknowledge that you have no responsibility for future changes caused by the current economic environment and the resulting impact on the System's financial statements. Further, management and the Board are solely responsible for all aspects of managing the System, including questioning the quality and valuation of investments, inventory and other assets, reviewing allowances for uncollectible amounts and evaluating capital needs and liquidity plans.

Lesa B Roe | Daniel Tenney

Lesa Roe, UNT System Chancellor | Daniel Tenney, Vice Chancellor for Finance

UNIVERSITY OF NORTH TEXAS SYSTEM

ATTACHMENT

This analysis and the attached "Schedule of Uncorrected Misstatements (Adjustments Passed)" reflect the effects on the financial statements if the uncorrected misstatements identified were corrected.

QUANTITATIVE ANALYSIS

	Before Misstatements	Misstatements	Subsequent to Misstatements	% Change
Current Assets	587,765,428		587,765,428	
Non-Current Assets & Deferred Outflows	2,248,317,200	(6,616,303)	2,241,700,897	-0.29%
Current Liabilities	(513,551,575)	5,955,639	(507,595,936)	-1.16%
Non-Current Liabilities & Deferred Inflows	(1,623,025,345)		(1,623,025,345)	
Current Ratio	1.145		1.158	1.14%
Total Assets & Deferred Outflows	2,836,082,628	(6,616,303)	2,829,466,325	-0.23%
Total Liabilities & Deferred Inflows	(2,136,576,920)	5,955,639	(2,130,621,281)	-0.28%
Total Net Position	(699,505,708)	660,664	(698,845,044)	-0.09%
Operating Revenues	(668,258,616)		(668,258,616)	
Operating Expenses	1,161,488,859	1,457,968	1,162,946,827	0.13%
Nonoperating (Revenues) Exp	(473,151,238)		(473,151,238)	
Change in Net Position	20,079,004	1,457,968	21,536,972	7.26%

Misstatements within Notes to the Financial Statements

1 Alternative investment reported as Level 1 investment in equities rather thar

Client: UNIVERSITY OF NORTH TEXAS SYSTEM

Period Ending: August 31, 2020

Major Enterprise Fund

SCHEDULE OF UNCORRECTED MISSTATEMENTS (ADJUSTMENTS PASSED)

Description	Financial Statement Line Item	Factual (F), Judgmental (J) or Projected (P)	Assets & Deferred Outflows		Liabilities & Deferred Inflows		Operating Revenues	Operating Expenses	Nonoperating (Revenues) Exp	Net Position	Net Effect on Following Year	
			Current DR (CR)	*Noncurrent* DR (CR)	*Current* DR (CR)	*Noncurrent* DR (CR)	DR (CR)	DR (CR)	DR (CR)	DR (CR)	*Change in Net Position* DR (CR)	*Net Position* DR (CR)
Overaccrual of utility expesnes at 8/31/19		F	0	0	0	0	0	1,127,636	0	(1,127,636)	0	0
	Communication and utilities expense							1,127,636				
	Beginning net position									(1,127,636)	N/A	
Adjustment to reclassify realized/unrealized gains on DiMeo investment account		F	0	0	0	0	0	0	0	0	0	0
	Investment income								(1,072,439)		N/A	
	Net increase in fair value of investments								1,072,439			
To reclassify federal receivable from accounts receivable to federal receivables		F	0	0	0	0	0	0	0	0	0	0
	Accounts receivable		(4,568,230)								N/A	
	Federal receivable		4,568,230									
To correct the accrual of construction payables at August 31, 2020		F	0	(5,955,639)	5,955,639	0	0	0	0	0	0	0
	Capital assets - non-depreciable			(5,955,639)							N/A	
	Accounts payable				5,955,639							
To reclassify Inspire Park building cost and record accumulated depreciation		F	0	(660,664)	0	0	0	330,332	0	330,332	(660,664)	660,664
	Non-depreciable or non-amortizable			(7,649,794)								
	Depreciable or amortizable, net			6,989,130								
	Depreciation and amoritization							330,332			(660,664)	
	Net investment in capital assets									330,332		660,664
			0	0	0	0	0	0	0	0	0	0
Total passed adjustments			0	(6,616,303)	5,955,639	0	0	1,457,968	0	(797,304)	(660,664)	660,664

Impact on Change in Net Position	**1,457,968**
Impact on Net Position	**660,664**

SCHEDULE OF UNCORRECTED MISSTATEMENTS (NOTES TO THE FINANCIAL STATEMENTS)

	Uncorrected and/or Omitted Disclosure (Include Guidance Reference)	Misstatement Type	Quantitative Amount(s)	Relevant Financial Statement Line(s)
2	Alternative investment reported as Level 1 investment in equities rather than Level 2	Uncorrected	8,455,846	**No financial statement line items are effected by the uncorrected error to the footnote disclosure**

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

Independent Auditor's Report

Board of Regents
University of North Texas System
Denton, Texas

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the business-type activities and aggregate discretely presented component units of University of North Texas System (System) as of and for the year ended August 31, 2020, and the related notes to the financial statements, which collectively comprise the System's basic financial statements, and have issued our report thereon dated December 17, 2020, which contained a reference to the reports of other auditors and an emphasis of matter paragraph regarding comparative footnote information. The financial statements of University of North Texas Foundation, Inc. and University of North Texas Health Science Center Foundation, Inc. (Foundations), aggregate discretely presented component units included in the financial statements, were not audited in accordance with *Government Auditing Standards*, and accordingly, this report does not include reporting on internal control over financial reporting or instances of reportable noncompliance associated with the Foundations.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the System's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the System's internal control. Accordingly, we do not express an opinion on the effectiveness of System's internal control.

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 entity's financial statements will not be prevented, or detected and corrected, on a timely basis. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section 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 have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a certain deficiency in internal control, described in the accompanying schedule of findings and responses as item 2020-001, that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the System's 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 effect on the financial statements. 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*.

System's Response to Finding

The System's response to the finding identified in our audit is described in the accompanying schedule of findings and responses. The System's response was not subjected to the auditing procedures applied in the audit of the financial statements, and accordingly, we express no opinion on it.

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 result of that testing, and not to provide an opinion on the effectiveness of the entity'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 entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

BKD, LLP

Fort Worth, Texas
December 17, 2020

University of North Texas System

Schedule of Findings and Responses

Year Ended August 31, 2020

Findings Required to be Reported by *Government Auditing Standards*

Reference Number	Finding
2020-001	Criteria or specific requirement – Management is responsible for establishing and maintaining effective internal control over financial reporting and for the preparation of the financial statements in accordance with accounting principles generally accepted in the United States of America (GAAP).

Condition – The System's calculation of net investment in capital assets included debt associated with unspent bond proceeds and amounts that were board designated were improperly included in restricted net position.

Effect – Unrestricted and restricted expendable net position were overstated, and net investment in capital assets were understated.

Cause – Funds were originally set up as restricted in the general ledger and were not moved when it was determined that there was no donor or legal restriction. Additionally, guidance was followed to not include unspent bond proceeds in the net investment in capital asset calculation, but the related bond proceeds were incorrectly still included in the calculation.

Recommendation – Management should review procedures to ensure controls are in place related to the proper classification of net position.

Views of responsible officials and planned corrective actions – Net Investment in Capital Assets (NICA) reported for FY2020 has been adjusted to include unspent bond proceeds. The previous presentation was based on guidance from the National Association of College and University Business Officers (NACUBO) Financial, Accounting and Reporting Manual (FARM). We have updated our procedures and templates to include new guidance for unspent bond proceeds in future calculations. Updated procedures have been reviewed with staff responsible for this area. Going forward, NICA will be calculated quarterly using the new approach as a part of quarterly financial reporting.

Proceeds from the sale of historical tax credits and one quasi-endowment originally reported as Restricted Net Position have been reclassified and reported for FY2020 as Unrestricted Net Position. We will examine restricted quasi-endowments held at all institutions and validate related restrictions as external or internal. Any found to be governed by internal restrictions will be reclassified to Unrestricted Net Position in FY2021. Going forward, restrictions will be reviewed and documented for new quasi-endowments to ensure they are reported correctly. Staff will receive training on restricted v unrestricted net position classification as well.