



VIRGINIA STATE UNIVERSITY

REPORT ON AUDIT FOR THE YEAR ENDED JUNE 30, 2014

Auditor of Public Accounts
Martha S. Mavredes, CPA

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AUDIT SUMMARY

Our audit of Virginia State University for the year ended June 30, 2014, found:

- the financial statements are presented fairly, in all material respects;
- internal control findings requiring management's attention; and
- instances of noncompliance or other matters required to be reported under Government Auditing Standards.

We have audited the basic financial statements of Virginia State University as of and for the year ended June 30, 2014, and issued our report thereon, dated April 27, 2015. Our report, included in the University's Annual Report is available at the Auditor of Public Accounts' website at www.apa.virginia.gov and at the University's website at www.vsu.edu.

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INTERNAL CONTROL AND COMPLIANCE FINDINGS AND RECOMMENDATIONS

Improve Financial Management

Our audit found several areas where the University should improve its financial management processes that support decision-making.

First, in fiscal year 2014 the University set its room and board rates using enrollment estimates that did not reflect actual trends, resulting in lower per student rates than needed to accumulate sufficient revenues to pay for the University's planned expenses. Using unrealistic enrollment estimates without full disclosure to management affects the University's budget quality and forces leadership to make reactionary choices under pressure rather than contemplating them during the budget development and rate setting process. We recommend the University implement changes that will require reasonable budget estimates based on actual data trends and expenses that balance with a realistic forecasted income.

Second, as of fiscal year 2014, the University's auxiliary funds maintenance reserve balance is \$2.1 million and the University places \$180,000 annually from its room and board revenues into the fund. Auxiliary facilities include buildings such as residence halls and are required to be self-supporting meaning the room and board paid by students should cover their operating costs including repairs and maintenance. We found no analysis to show that this annual contribution is sufficient to accumulate reserves to an adequate level to pay for future building maintenance of these auxiliary facilities, which is estimated at \$5.2 million in deferred maintenance plus an additional \$8.5 million in new maintenance through fiscal year 2020. We recommend that the University perform an analysis of its auxiliary funds maintenance reserve requirements and develop a plan to ensure they accumulate adequate reserves for auxiliary buildings, and include those amounts in their budget.

Third, a 2012 feasibility study of the University's multi-purpose center, which is currently under construction, shows that its operating revenues will not cover its operating expenses and the University will need to increase student fees to compensate for its operating deficit and fund a maintenance reserve. We recommend that for future projects, management share all financial analysis with the Board of Visitors for their examination and discussion. The financial analysis should include pro forma financial statements under worst case, best case, and most likely case scenarios. Management should also consider the implications of projects on rate increases passed on to students and assess the trade-offs of pursuing the project over other initiatives.

Finally, the University does not budget for local fund expenses like they do for education and general expenses. As of fiscal year 2014, local funds carried an approximate \$1.3 million deficit that is not readily evident on the financial statements due to the blending effect of all the funds. We recommend the University budget for all funds, including local funds, to provide control that they operate within their means.

Improve Procurement and Contract Management Processes

We found instances where the University's contract procurement and management processes did not comply with best practices and/or the Department of General Services' Agency Procurement and Surplus Property Manual (Procurement Manual), as described below.

Sole Source Awards

The University awarded 56 sole source contracts in fiscal year 2014, all of which were less than \$100,000, and could have been procured using the small purchase procedures. However, the University chose to designate them as sole source contracts, yet the Procurement Manual has specific requirements that the University did not consistently follow. There was no sole source justification for 18 percent of the contracts, no determination as to the price reasonableness for 93 percent of the contracts, no evidence of negotiation for 29 percent of the contracts, and the award was not posted timely for 67 percent of the contracts.

Emergency Awards

Of the eight emergency contracts awarded during fiscal year 2014, three did not meet the definition of an emergency as provided in the Procurement Manual. In addition, the University did not consistently document the rationale for choosing a specific vendor, evidence that they considered competition, or a determination that the vendor's price was reasonable.

Food Service Vendor

This procurement involved a new food service contract and although the procurement process appeared reasonable, the University received only one response to its solicitation. Several vendors attended the pre-proposal conference and discussed the intended contract with University personnel; however, the current food service vendor was the only one that officially responded to the solicitation. In the case of a single response to a solicitation, the Procurement Manual section 3.1 k requires the University to investigate why other vendors did not respond and prepare a written determination that the price of the one responding vendor is fair and reasonable and why the sole vendor's proposal was not rejected and re-solicited. In addition, the Procurement Manual section 4.10 requires a written price reasonableness determination. The Procurement Director indicated that she discussed this sole solicitation with General Services and they approved the award to the vendor; however, written analysis was not evident in the procurement file.

Beyond the procurement procedure for this contract, we are also concerned about the procedure's financial implication. The previous food service contract required the University to sell 2,400 meal plans each semester and the new contract calls for a minimum of 2,800 meal plans each semester at an annual cost of \$7.9 million and provides for a increasing per meal price scale when actual plans sold are less than 2,800 but greater than 2,550 plans. The minimum cost of the plan is \$7.6 million annually and represents the least amount the University will pay the vendor.

The food service contract provides a \$250,000 signing bonus, which the University plans to use to award scholarships as a means of enticing students to live on campus and purchase meal plans. The scholarship will be available on a first come, first serve basis to all non-freshman students, including those who already planned to live on campus. While the plan will likely yield some increase in students choosing to live on campus, the University has no analysis to show how many students will possibly move back to campus and whether it will be sufficient to increase sales to the goal of 2,800.

In addition, there is no analysis of the financial impact after the signing bonus money is exhausted in the first year of the contract. Given the University's declining enrollment and the challenges associated with retaining students on-campus versus living in the surrounding community, we are concerned that this new contract may place a financial burden on the University at a time when they cannot afford it.

Vendor Consultant

This Memorandum of Understanding (memorandum) for approximately \$135,000 with a vendor consultant is in violation of all procurement standards the University is required to follow, including exceeding their delegated purchasing authority of \$100,000. The Virginia Public Procurement Act requires all procurements for professional services be obtained by competitive negotiation. A memorandum of understanding is not a recognized or acceptable form of procurement in the Commonwealth. In addition, the current memorandum cost is \$143,000 with no document authorizing an increase beyond the original memorandum amount. No specific performance metrics are evident in the memorandum and the deliverable is a list of activities performed each month with no quantitative requirements. Contract administration is assigned to the Provost who approves the vendor's invoices but does not document the specific activities performed and whether they met the University's expectations.

Enrollment Services Contract

The University procured an enrollment services contract totaling \$725,775, which does not have clear deliverables. The University followed the proper procurement process and the Provost was assigned as the contract administrator; however, we found the Provost was unaware that this contract was under his purview. Consequently, he has not performed any contract administration or analyzed whether applications or enrollments have increased.

We recommend the University improve its procurement and contract management practices to include ensuring they comply with state rules and regulations, and perform cost/benefit analysis before entering into contracts.

Improve IT Procurement Process

The University outsourced the primary management and security functions for the IT operations of the Banner system to the service provider, at a monthly cost of approximately \$40,000,

using an existing master services agreement that does not include hosting services. The University believed the general category of IT services described in the agreement was sufficient to also encompass outsourcing. We believe, however, that they should have followed the Sole Source IT Procurement process defined in the Commonwealth's IT Procurement Manual.

The Sole Source IT Procurement process requirement for sole source procurements that have an estimated total amount exceeding the agency's delegated purchase authority (\$100,000 in the case of the University) is that the Sole Source Justification Form be completed. The Procurement Manual also requires:

- The agency head or designee must sign the Sole Source Justification Form and submit it to the Virginia Information Technologies Agency (VITA) for review and approval prior to the entity taking any additional contractual action.
- Any procurement that exceeds \$100,000 in costs for the entire life cycle of the procurement must have approval from the Commonwealth's Chief Information Officer prior to the beginning of the procurement.
- VITA must conduct the procurement unless specifically delegated to the institution.
- The University is also required follow the eGov Hosting Process for this type of host service, which includes completing the VITA Hosting Request form and submitting it to VITA for review and approval.

The service provider's agreement does not include a provision that they comply with the Commonwealth's Information Security Standard (Security Standard) nor has the University cross-walked the standards the service provider follows to the Security Standard to ensure they are adequately comparable. The current outsourcing agreement does not require that the service provider have an annual Service Organization Control (SOC) report for their operations as well as for the operations of any companies to which they may have outsourced components of the services they provide to the University, such as hosting. If the University followed the IT Procurement Manual process described above, VITA's review would have likely observed the lack of provisions in the contract related to compliance with the Security Standard and SOC reporting and ensured they were added to the terms and conditions of the contract.

We recommend the University follow the IT Procurement Manual when it is more appropriate to do so. Furthermore, we recommend the University complete the sole source and eGov hosting processes for its service provider contract and obtain the proper approvals from the Commonwealth's Chief Information Officer.

Ensure Foundations Reimburse for University Employee Time

During fiscal year 2014 all foundations used University employees to perform work on their behalf, but only the VSU Foundation reimbursed the University for some of that time. Although the

reimbursement covers the time spent by a University accountant who maintains the Foundation's financial records, the reimbursement was insufficient to pay for any other employee's time.

During the fiscal year 2013 audit we found instances where several University employees worked nearly exclusively for Foundations, but the University was never reimbursed. In March 2014 we verbally asked the University to seek reimbursement for prior unrecovered salary expenses and to obtain an agreement with each Foundation to deal with the matter moving forward. The University has drafted agreements, but they have not been finalized and each Foundation refuses to pay prior amounts because they have no legal responsibility to do so, leaving the University left with a liability to repay the state. In addition, although no agreements have been established, some employees continue to perform work for the Foundations while being paid by the University.

We also found instances of three University employees whose salaries are paid from Title III Federal funds that are also working on behalf of the Foundation. The estimated amount of salaries and fringe benefits misdirected to the Foundations is estimated at \$68,030 in fiscal year 2014. The Code of Federal Regulations (CFR) section 608.10(b)(1) classifies unallowable activities under Title III as those that are not included in the grantee's approved application, and the University's application does not provide for University employees to work on Foundation activities. The University should repay these questioned costs to the Title III program, Catalog of Federal Domestic Assistance No. 84.031.

We are concerned about the financial burden from the practice of providing staff for the Foundations. Therefore, we recommend the University require the Foundations to hire their own staff unless they agree to reimburse the University for the time actually worked by University employees, a practice that is common at peer institutions. In addition, we are concerned that the University has no process to accurately account for employees actual hours worked on behalf of the Foundation. The current Kronos timekeeping system, implemented in 2012, is only used for hourly wage employees. However, the system is a total human resources package, which includes the ability to manage time and attendance for both wage and salaried employees, perform leave calculations, and track time charged to grants and specific projects for level of effort reporting. Requiring salaried employees to track their time by project would be the perfect solution to track how much time University employees spend on Foundation work. It would provide a detailed and accurate accounting to allow the University to bill each Foundation and recoup these monies spent. Finally, we recommend that the University not use employees paid with Title III Federal funds to support the Foundation without first obtaining the approval of the grantor agency; and that they obtain a \$68,030 reimbursement from the Foundation for this amount, or repay Title III from local funds.

Improve Controls over Physical Inventory

The University did not complete a physical inventory of its capital assets in fiscal year 2014 and it has been two years since a complete inventory was performed, in violation of General Service's regulations. The University hired and paid a vendor approximately \$27,000 to perform the inventory of both capital and controllable assets during the year, but they did not complete the work as provided in the scope of the contract; their draft inventory results indicated they could not locate

almost 5,000 items. The University stated that they finished the inventory, but no documentation was provided and; therefore, we recommend the University complete a physical inventory.

Our observation of capital assets discovered a spectrometer costing \$227,000 in the Chemistry Department that was purchased more than seven years ago, but still in its original packaging. Purchasing capital assets that are not placed into service within a reasonable amount of time may result in outlay of funds that could be used for other purposes. We recommend that the University monitor asset utilization to ensure unnecessary purchases do not occur.

Finally, during the fiscal year 2013 audit, we recommended the University update its policies to address removal of research equipment from University grounds. The current policy does not address removal of equipment, but instead alludes to misconduct by a research participant and there is no definition of what constitutes misconduct. We recommend the University specifically address the procedures that employees should follow when requesting the removal of research equipment.

Improve Policy over the Proper Use of Travel Cards

The University needs to review its travel card policy and revise it accordingly to clearly explain what constitutes inappropriate use. Further, they need to articulate the consequences of not following the policy, including termination. Finally, the University should ensure the revised policy does not conflict with the Travel Card Agreement signed by employees upon receiving a card. A well-defined travel card policy will provide clarification to employees and describe the specific actions that supervisors should follow when inappropriate use instances are found, including the timely reporting of the potential fraud as required by Code of Virginia Section 30-138.

Improve User Access Review Process

The University's current annual user access review process is ineffective in identifying all users who have access to screens in Banner that perform critical business functions. The current review process involves having business managers certify that their employees need access to their assigned security classes, but it does not include a review of the Banner screens underlying those classes. This process is flawed because the responsible business manager is unaware of which screens are part of the employees class and the listing does not include employees from other departments that have access to the Banner screens under that manager's responsibility. As a consequence, our review found users assigned to two classes with access to critical screens that were created for test purposes when the system was installed in 2006 and this access was never deleted.

Specifically, we found 27 employees who had access to Banner's main security screen, giving them the ability to add, delete, and modify security for all University employees. Access to this screen should be limited to only a few trusted individuals due to the risk associated with granting inappropriate access. We also found 14 employees who had access to the Banner table that stores approved tuition, fee, room, and board rates. Access to this screen should be limited to only a few trusted employees in the Bursar's office because unauthorized changes to this table can affect the amounts charged to student accounts.

We recommend the University improve its user access review process to provide information to business managers about all users and classes that have access to screens under their responsibility. We further recommend the University work to automate the review process using the Banner GUVUACC table, shifting the focus to users and their access to Banner screens rather than their assignment to specific classes. Automating the review process can also help the University to quickly and easily identify users who have accidentally been granted access to multiple business processes, such as the ability to record and approve a journal entry, and make appropriate corrections.



Martha S. Mavredes, CPA
Auditor of Public Accounts

Commonwealth of Virginia

Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

April 27, 2015

The Honorable Terence R. McAuliffe
Governor of Virginia

The Honorable John C. Watkins
Chairman, Joint Legislative Audit
and Review Commission

Board of Visitors
Virginia State University

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS

We have audited, in accordance with the 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 Virginia State University as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the University's basic financial statements and have issued our report thereon dated April 27, 2015. Our report includes a reference to other auditors. We did not consider internal controls over financial reporting or test compliance with certain provisions of laws, regulations, contracts, and grant agreements for the financial statements of the component units of the University, which were audited by other auditors in accordance with auditing standards generally accepted in the United States of America, but not in accordance with Government Auditing Standards.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the University's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances 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 University's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the University's internal control over financial reporting.

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 over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control over financial reporting that we may consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control over financial reporting entitled "Improve Financial Management," "Improve Procurement and Contract Management Processes," "Improve IT Procurement Process," "Ensure Foundations Reimburse for University Employee Time," "Improve Controls over Physical Inventory," "Improve Policy over the Proper Use of Travel Cards," and "Improve User Access Review Process," which are described in the section titled "Internal Control and Compliance Findings and Recommendations," that we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the University's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the section titled "Internal Control and Compliance Findings and Recommendations" in the findings entitled "Improve Procurement and Contract Management Processes," "Improve IT Procurement Process," "Ensure Foundations Reimburse for University Employee Time," and "Improve Controls over Physical Inventory."

The University's Response to Findings

We discussed this report with management at an exit conference held on June 2, 2015. The University's response to the findings identified in our audit is described in the accompanying section titled "University Response." The University'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.

Status of Prior Findings

The University has not taken adequate corrective action with respect to the previously reported finding “Improve Controls over Physical Inventory.” Accordingly, we included this finding in the section entitled “Internal Control and Compliance Findings and Recommendations.”

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion 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 Audit Standards in considering the entity’s internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

AUDITOR OF PUBLIC ACCOUNTS

KKH/alh



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June 4, 2015

Ms. Martha Mavredes
Auditor of Public Accounts
P.O. Box 1295
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Dear Ms. Mavredes:

Virginia State University (VSU) has reviewed the Auditor of Public Accounts' (APA) Report on Internal Control over Financial Reporting and on Compliance and Other Matters for the fiscal year ended June 30, 2014. The University appreciates the opportunity to respond to the findings and recommendations. In accordance with Government Auditing Standards, VSU provides the following responses for inclusion in the report:

AUDIT FINDING AND RECOMMENDATIONS

Improve Financial Management

For FY2014, the University set its room and board rates using the most current data available; adjusting for economic downturns, enrollment fluctuations, and cost drivers beyond our control such as market forces within the off-campus housing market. The University made a business decision to base its FY2014 budget on a more conservative enrollment estimate based on existing trend data. The University has a sound process that supports budget development and execution. The process includes input from the University's senior administration and formal approval by the Board of Visitors. Prior to presenting information to the Board of Visitors, numerous meetings, discussions, and work sessions are conducted with the President's Vice Presidents Council.

As it relates to the auxiliary funds maintenance reserve, the auxiliary space portfolio at VSU has changed significantly due to an aggressive construction program that has taken failing properties offline and replaced them with new facilities. Going forward, the university intends to perform an analysis of its auxiliary funds maintenance reserve requirements and develop a plan to ensure they accumulate adequate reserves.

Currently, the University is in negotiations for a facility operator who has submitted an operating pro-forma. Current negotiations suggest that revenues are consistent with prior analysis but expenses are significantly lower. The educational and general contribution to the operating costs due to public service, classroom and institutional support components of the

building program has not been determined. It is important to note that increases in student fees in the FY16 budget are not specifically attributable to the Multipurpose Center.

Improve Procurement and Contract Management Processes

The University's Purchasing Department Contract Administration procedures are as outlined in its regulation manual issued by the Department of General Services, Purchases and Supply, Agency Procurement and Surplus Property Manual. The University has Contract Manager duties that provides oversight to the administrators and contractors. Formal and informal training is conducted on a regular basis. The contract files consist of two types of documents – the contract award and the working papers. The contract award contains the actual contract and the working papers are included in the supporting documentation file. This best practice was recommended by a central agency and implemented at VSU.

The files in the purchasing office can substantiate that a sole source award was the appropriate method of procurement for all Sole Source procurement-to include: the justification, price reasonableness, evidence of negotiation, and timely posting. Most of the sole source awards were for software licenses renewals for academic instruction that would have prevented the outlined classroom instruction. The University internal procedures are in accordance with the provisions of the Agency Procurement and Surplus Property Manual. The files in the Purchasing Office and substantiate that all emergency awards were conducted in accordance with prescribed procedures.

As it relates to the solicitations issued for food service, academic consultant and enrollment services, the university followed the proper procurement procedures. The above solicitations were competed/awarded in FY15 and FY16. For the food services contract, the University received three (3) responses to the solicitation but only one of the three, issued a proposal. Two of the responses were official letters documenting the reason for withdrawing their firm from the solicitation process. These documents are filed in the Working Paper file. VSU solicited input from the Department of Purchases & Supply on moving forward with one response. Both VSU and DP&S found no reason to re-solicit the RFP. Also, the new food services contract was negotiated in FY2015, with an effective date in FY2016. As such, this contract file was still being assembled during the APA's audit of FY2014. Economically speaking, the goals for the food services contract are realistic and attainable. There has only been one year in the last decade where the University's board sales approached the base sales' threshold. The University analyzed the data, is cognizant of the root causes, and implemented the appropriate operational changes.

Improve IT Procurement Process

The University completed the eGov hosting form per discussion with the APA. VITA rejected the form stating that the eGOV hosting form is for public facing websites that are hosted using one of three external service providers under a VITA contract. VITA Supply Chain Management (SCM) delegated the Banner procurement to Virginia Commonwealth University. VSU is not the contract administrator for the Banner contract and would not be in a position to amend the contract to the requirement for the Banner agreement to recognize the Commonwealth IT Security Standard (Sec 501-09). However, the university and APA audits VSU's security compliance per the Commonwealth's IT security standard. The university will comply with VITA's IT procurement regulations for Tier 1 higher education institutions.

Improve Controls over Physical Inventory

An inventory of all University-owned capital fixed assets was conducted and all necessary documents to support this activity were provided to the audit team. In the future, the university will communicate with the auditor to ensure the supporting documentation meets their specifications.

Improve Policy over the Proper Use of Travel Cards

The university agrees that a review of travel card procedures is necessary and that the university will revise its travel card policy.

Improve User Access Review Process

The university is continuing its efforts to improve IT security across all IT systems. VSU has been proactively reviewing Banner Security: (1) Ellucian Consultant performed report and issued report in July 2014, (2) VSU Applications Security Administrator met with Banner Security Managers to discuss security review and matrixes, (3) one-on-one sessions were setup with Banner Security Managers and Ellucian Functional Consultants to discuss security matrixes, least privileges, and best practices, (4) monthly meeting between Applications Security Administrator and Banner Security Managers to review access request forms, security matrixes, and respond to questions, and (5) Applications Specialist worked with Invoice Processing on Accounts Payable employee and supervisor roles.

Virginia State University is committed to addressing these audit findings and recommendations. We would like to thank you and your staff for your continued collaboration and support and look forward to our FY2014 audit.

Sincerely,



Kevin Davenport
Vice President for Administration and Finance

cc: Dr. Pamela V. Hammond, Interim President
Mr. Hubert D. Harris, VSU Chief of Staff
Mr. David A Von Moll, State Comptroller
The Honorable Anne Holton, Secretary of Education
Mr. Daniel Timberlake, Director of Planning and Budget

APA COMMENTS TO UNIVERSITY RESPONSE

Below is our response to certain aspects of the University's response that requires additional clarification.

The University's response suggests that documentation was available that we did not consider; however, all documentation that was provided to us during the audit was taken into account in developing our findings and recommendations. In addition, the University's response to the finding entitled "Improve IT Procurement Process" suggests that we audit for compliance with the Commonwealth's IT security standard. While our work related to the University may include some tests for compliance, we do not have authority or responsibility to audit the service vendor for compliance. As such, we continue to recommend the University obtain an annual SOC report.

UNIVERSITY OFFICIALS

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ADMINISTRATIVE OFFICIALS As of June 30, 2014

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