

# December 2019 Audit Committee Meeting

<b>Schedule</b>	Wednesday, December 4, 2019 12:00 PM — 12:40 PM CST
<b>Venue</b>	Wilder Student Union Ballroom, Lambuth Campus, Jackson, TN
<b>Organizer</b>	Jean Rakow

## Agenda

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# **1. Call to Order**



## **2. Roll Call and Declaration of Quorum**



### **3. Approval of Minutes - September 4, 2019**

For Approval

Presented by Carol Roberts

THE UNIVERSITY OF MEMPHIS  
BOARD OF TRUSTEES

MINUTES OF THE AUDIT COMMITTEE  
SEPTEMBER 4, 2019  
Memphis, TN

The Audit Committee of The University of Memphis Board of Trustees met at 9:45 a.m. CDT, on Wednesday, SEPTEMBER 4, 2019, on the University of Memphis' main campus in Memphis, TN.

**I. CALL TO ORDER**

Trustee Carol Roberts called the meeting to order.

**II. ROLL CALL AND DECLARATION OF QUORUM**

Melanie Murry, Legal Counsel and Board Secretary, called the roll and confirmed the following Audit Committee members were present, either in person:

Trustee Edwards\*  
Trustee Graf\*  
Trustee Johnson\*  
Trustee Roberts\*  
Trustee Springfield\*

Trustee North and Trustee Kemme were also present.

\*Voting members

Secretary Murry announced the presence of a quorum.

**III. APPROVAL OF MINUTES JUNE 5, 2019**

Trustee Roberts called for a motion to approve the June 5, 2019 Audit Committee meeting minutes that were included in the meeting materials. The motion was made by Trustee Graf and properly seconded. A voice vote was taken, and the motion was unanimously approved.

**IV. REVIEW OF THE AUDIT COMMITTEE CHARTER**

Trustee Roberts recognized Chief Audit Executive Vicki Deaton to discuss various items. The first item is acceptance of the review of the Audit Committee Charter. The review of the charter is required by the current charter which states, "review and assess the adequacy of the AC's charter...." The committee requested a change to the charter at the last meeting. The revision was made and members have the most recent version in their meeting materials. Trustee Roberts called for questions and/or discussion of the charter. There was no discussion. Trustee

Roberts then asked the General Counsel if a motion, second and roll call vote was necessary. Ms. Murry indicated that the vote was not necessary if there are no changes to the charter. No changes were requested.

**V. INTERNAL AUDIT QUALITY ASSESSMENT**

Ms. Deaton next discussed the Internal Audit Quality Assessment Validation Results. At the previous meeting the committee was provided with Internal Audit's self-assessment. Independent reviewers have visited campus and provided a validation of the self-assessment. The meeting materials contain a letter from the external reviewers indicating that they concurred with the self-assessment, that we are generally in compliance with the IIA's standards. Another assessment will be required in five years.

**VI. SUMMARY OF AUDIT REPORTS ISSUED**

Ms. Deaton reported on the audit reports issued for the quarter. These audits included: Cash Balances Audit (effective with no issues), the Inventory Observation Audit (effective with no issues) and the Lambuth Campus Financial and Compliance Audit (effective with opportunity for improvement). The Lambuth Campus Financial and Compliance Audit was very comprehensive and resulted in multiple issues; however, some were minor that were addressed with management and action plans were taken care of during the audit or are underway.

**VII. SUMMARY OF FRAUD, WASTE, ABUSE REPORTS RECEIVED**

Ms. Deaton reported on reports of fraud, waste and abuse to the Office of Internal Audit and Consulting. Of the five complaints that the office worked on since the prior meeting, one complaint required no further action, one was closed to a lack of evidence, one was referred to Human Resources and four are ongoing.

**VIII. EXTERNAL INSPECTION REPORT RECEIVED**

Ms. Deaton next reported on the External Audit or Inspection report received by the department. The report was issued by the Tennessee Department of Environment and Conservation, Division of Solid Waste Management. On June 18<sup>th</sup> and June 24<sup>th</sup>, the Division of Solid Waste Management came to campus to do an inspection of Chemistry facilities and found 10 violations. Previously, at the March meeting, the committee received a report related to the inspection of the Life Sciences Building and the Herzog Building where four violations were identified. All of the violations identified during the inspections related to items that were corrected right away and no penalties were assessed. Internal Audit requested management develop action plans to address these types of violations in the future. Representatives of the UofM assured the committee that there is work being done to take a proactive position to ensure compliance including the reorganization of a current position and establishment of a new compliance position within the institution. Trustee Roberts stated that the individuals on

the front line have to be the ones responsible for fulfilling their obligations. The people in the labs need to understand what they need to do and follow through, as appropriate.

#### **IX. FY 2019 INTERNAL AUDIT YEAR END REPORT**

Ms. Deaton presented a summary of the activities of the Division of Internal Audit for the FY 2019 as presented in the meeting materials. The presentation discussed audit functional areas, audit issues and investigations of fraud, waste, abuse or illegal activity. A suggestion was made the administrative functional area be broken down into administrative units.

#### **X. INFORMATION SECURITY PROGRAM**

Chair Roberts recognized CIO Robert Jackson to discuss information security program. Dr. Jackson provided a status update of activities the UofM engaged in to increase IT security: multi-factor authentication for all employees, IT security awareness training for all employees, hiring of an IT Security Communications Coordinator, monitoring of the email security gateway, improvement of the network firewall and a desktop security initiative. Dr. Jackson also discussed the extent of security threats on a daily basis. He stated that the UofM is experiencing relatively low level of attacks with the exception of a few spikes and the means that the UofM uses to eliminate the threats of viruses and spam email attacks. IT reported 12 security engagements related to unauthorized access, inappropriate usage, personally identifiable information and other issues. The next steps to strengthen IT Security Awareness includes: new employee on-boarding with in-depth training, annual refresher training for current employees, outreach efforts with the IT Security Communications Coordinator and the department is considering offering access training by students. Additionally, IT has scheduled core network/firewall upgrade during FY 2020, continues to leverage security information and event management (Splunk) and continue to review technology for blocking malicious web sites.

A question was asked about the time lapse between patch availability to implementation. Dr. Jackson stated that Microsoft distributes patches on the first Tuesday of every month and that the patch is installed on the test system on Wednesday and placed into production on the following weekend. There is some interruption of business when the systems need to be patched and there is always a tension between IT security and the need to do business. The more that we rely on external vendors to provide services, the more care needs to be taken to ensure system compatibility. Dr. Jackson stated that he believes that the UofM does a good job of patching as quickly as possible while working with various external entities. The University has implemented other strategies to provide higher levels of protection to the system during periods where patches have to be delayed. An example cited is the network firewall.

Another question was asked about whether the online programs are operated on a different server than operations and how do the two interact? The online system used for several years for academic programs is called Desire2Learn and is a hosted environment and does not pose additional risk to the system. Should the company experience a breach, they are required to notify the UofM of the issues. The UofM has rules and layered protections in place that

governing the interaction between the student data system and Desire2Learn. Desire2Learn has limited access to the student data system.

Does ITS have an ongoing review of vendors that are already on campus to ensure that they are keeping up with patches and other security measures? The UofM deals with this in two ways: 1) when a contract comes up for renewal the department ensures that they have appropriate language and content and 2) operationally when ITS is running into issues during testing. External vendors tend to be responsive to UofM concerns; however, some are not as aggressive as our security team would like them to be.

## XI. OFFICE OF INSTITUTIONAL EQUITY ANNUAL SUMMARY

Trustee Roberts recognized Kenneth Anderson to discuss the annual report of the Office for Institutional Equity. Mr. Anderson reviewed the key functions of the office, including: prevention and awareness programming, grievance and compliant procedure and training and policy enforcement. The office has developed a comprehensive primary prevention program that is research based to combat sexual assault and domestic violence affecting the UofM community. The grievance and complaint procedure is a central function of the office in terms of receiving reports of alleged misconduct or policy violation and responding appropriately. Responses begin with a consultation and depending on the decision of the involved party (complainant), the office moves to resolve the issue through informal resolution or formal investigation. Every October, the UofM is required to report to the Tennessee Human Rights Commission and the State auditing office with regard to prevention and enforcement activities of the past year.

The Title IX Prevention Center reached over 5,400 students focusing primarily on incoming freshman with online trainings, 1,300 plus students with 150 in-person trainings and 900 plus students through seven large scale events. The workshop training programs conducted with ACAD classes included helping students understand what a healthy relationship looks like as well as teaching skills and how to set boundaries, how to effectively communicate, how to give and withdraw consent and to receive that decision appropriately and some conflict resolution skills. The training also includes a component related to bystander intervention. Three of the large events were: Walk a Mile in Her Shoes (focusing on domestic violence), Take Back the Night (focusing on survivors) and the Healthy Relationships Fair (focusing on sexual assault awareness).

Last year was the first full year of implementation of a case management system that enables the staff to review cases and analyze data in ways that weren't previously available. There were 154 reports of Title IX sexual Misconduct. Previously, because the office was working with paper files, the office was not able to determine the number of complaints that went formal and the number that were investigations. The office received 226 total reports of which 69 resulted in formal complaints. (Details can be found in the meeting materials.)

Mr. Anderson also presented information on and off campus partners related to prevention efforts.

An annual report of the activities of the office will be available in October.

Trustee Johnson commended Mr. Anderson on the use of best practices and research-based criteria in this area.

Secretary Murry stated that Trustee Martin entered the room during the meeting.

**XII. ADDITIONAL COMMITTEE BUSINESS**

There was no additional Committee business.

**XIII. ADJOURNMENT**

The meeting adjourned at 9:47 a.m. CDT to Executive Session.

# **4. Summary of Audit Reports Issued**

Presentation  
Presented by Vicki Deaton

# The University of Memphis Board of Trustees

Presentation

For Information

**Date:** December 4, 2019

**Committee:** Audit Committee

**Presentation Title:** Summary of Audit Reports Issued

**Presented by:** Vicki D. Deaton, Chief Audit Executive

## **Synopsis:**

Three audit reports were issued this quarter. The Clery Act Compliance Audit report and the Animal Care Program Financial Audit report were issued with the opinion of Effective with the Opportunity for Improvement. The Audit of President's Expenses for the Period July 1, 2018 – June 30, 2019 report was issued with the opinion of Effective.

See the attached table for more information about the audit reports.

**Audit Reports Issued (12/4/2019 Audit Committee Meeting)**

Name of Audit	Date of Audit Report	Audit Engagement Report Opinion	Minor Issues - Addressed Verbally	Observation	Minor Issues	Moderate Issues	Major Issues	Issues Outstanding from Prior Audit
Clery Act Compliance Audit	10/14/2019	Effective with the Opportunity for Improvement	0	0	2	2	0	NA
Animal Care Program Financial Audit	11/11/2019	Effective with the Opportunity for Improvement	2	0	2	1	0	NA
Audit of President's Expenses for the Period July 1, 2018 - June 30, 2019	11/20/2019	Effective	0	2	0	0	0	NA



## **5. Summary of Fraud, Waste, Abuse Reports Received**

Presentation

Presented by Vicki Deaton

# The University of Memphis Board of Trustees

Presentation

For Information

**Date:** December 4, 2019

**Committee:** Audit Committee

**Presentation Title:** Summary of Fraud, Waste, or Abuse Reports Received

**Presented by:** Vicki D. Deaton, Chief Audit Executive

## **Synopsis:**

Four new reports of fraud, waste, or abuse, noncompliance with law, or conflict of interest were received by the Office of Internal Audit and Consulting since the last quarterly meeting. One of the new reports received was investigated and a memo was issued. One report that was received was referred to the Office of Institutional Equity, and the complaint has been closed by that office. Two reports received last quarter were resolved and investigation memos were issued. Two investigations by Internal Audit are in progress.

Attached is a summarized list of fraud, waste, or abuse reports received by the UofM Office of Internal Audit and Consulting, with additional information regarding the status of the investigations or referrals.

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# CONFIDENTIAL AUDIT INFORMATION

UofM Fraud, Waste, or Abuse Report Summary (12/4/2019 Audit Committee Meeting)								
Case Number	Date Received	Allegation Received by	Description of Allegation	Status	Investigation Outcome	\$ Loss	Date of Final Action by Internal Audit	Additional Explanation
19-013	5/2/2019	Verbal Conversation with CAE	Fundraising, Travel Per Diem, & Scholarship Improprieties	Memo Issued-Case Closed	No Evidence of Fundraising, Travel Per Diem, or Scholarship Improprieties	NA	11/12/2019	
19-016	6/19/2019	Email to Internal Audit	Conflict of Interest between Faculty & Vendor Providing Experiential Learning Credit	Memo Issued-Case Closed	A Conflict of Interest Existed Between 2 Part-Time Affiliate Faculty and a Vendor	NA	11/18/2019	The Faculty are no longer employed by the UofM and the vendor is not used.
20-001	8/22/2019	Internal Audit FWA Report	Allegation of Fraudulent Insurance Claim	Memo Issued-Case Closed	No Insurance Claim was Filed with the State of Tennessee Self-Insurance Policy	NA	10/1/2019	Asset repairs were completed and paid by the UofM and 2 contractors.
20-002	8/22/2019	Internal Audit FWA Report	Allegation that Faculty & Students were Discouraged from Reporting Complaints to OIE	Referred to OIE	Per OIE - Complaint Closed	NA	11/15/2019	
20-003	10/10/2019	Internal Audit FWA Report	Allegations Related to Use of FedEx Forum Suite	Internal Audit Investigation	ongoing	NA		
20-004	10/31/2019	Confidential Compliance Memo to Internal Audit	Allegation of Conflict of Interest	Internal Audit Investigation	ongoing	NA		



# **6. External Audit Report: University of Memphis Foundation 6/30/2019**

## **Report**

**Presented by Vicki Deaton**

# The University of Memphis Board of Trustees

Presentation

For Information

**Date:** December 4, 2019

**Committee:** Audit Committee

**Presentation Title:** External Audit Report - University of Memphis Foundation Financial Statements, June 30, 2019

**Presented by:** Vicki D. Deaton, Chief Audit Executive

## Synopsis:

The University is subject to external audits, program reviews, and similar activities by various agencies and other organizations. According to UofM Policy GE2016 Notification of External Audits and Reviews, it is the responsibility of the primary contact person for the program or activity being reviewed to notify Internal Audit of an external audit or review as early in the process as possible. After the audit or review is complete, the primary contact will usually receive notice of the results in writing. The primary contact (or designee) should forward a copy of the results to Internal Audit. The responsibility for Internal Audit under this policy includes reporting occurrences of external reviews and audits to the Audit Committee, Division of State Audit and others as the circumstances may dictate. Also, TCA 4-4-113 requires notification of federal award noncompliance or any deficiency related to compliance with federal statutes, regulations, or the terms and conditions of a federal award, to the Tennessee Comptroller of the Treasury and the Commissioner of Finance and Administration.

On October 31, 2019, the University of Memphis Foundation Financial Statements, June 30, 2019 were issued. The University of Memphis Foundation (Foundation) is considered a component unit of the University and is discretely presented in the University's financial statements. The Foundation's financial statements are presented for informational purposes.

The Foundation is a not-for-profit, tax-exempt corporation chartered in 1964 in the State of Tennessee. The Foundation accepts and manages private support to the University of Memphis (University).

The Foundation engaged an independent external CPA firm, Reynolds Bone & Griesbeck PLC, to perform an audit of the financial statements of the Foundation. The independent auditor's opinion stated that the financial statements present fairly, in all material respects, the financial position of the Foundation as of June 30, 2019, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

The auditors did not identify any deficiencies in internal control that would be considered material weaknesses during their limited consideration of internal control over financial reporting. There were no instances of noncompliance with certain provisions of laws, regulations, contracts, and grant agreements that were tested.

# The University of Memphis Foundation

FINANCIAL STATEMENTS

JUNE 30, 2019



REYNOLDS BONE & GRIESBECK PLC  
CERTIFIED PUBLIC ACCOUNTANTS & ADVISORS

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*The University of Memphis Foundation  
June 30, 2019*

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## **BOARD OF DIRECTORS AND FINANCIAL/ADMINISTRATIVE DIRECTORS**

*The University of Memphis Foundation*  
June 30, 2019

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### **Board of Directors**

George T. Johnson, President  
Harry L. Smith, Vice President  
Gary S. Shorb, Treasurer/Secretary  
Judith Edge  
Robert F. Fogelman  
Carolyn Hardy  
Fred Hodges  
Tanya L. Hart  
Thomas G. Kadien  
Raaj Kurapati  
James D. Lackie  
Jason Little  
David C. Perdue  
Dr. M. David Rudd  
Dr. Douglas Scarboro  
Fred Towler  
Monica Wharton  
James Wiertelak  
John Wilfong

### **Financial/Administrative Directors**

Byron Morgan, Managing Director  
Carolyn Stanley, Foundation Director



## INDEPENDENT AUDITOR'S REPORT

Board of Directors  
The University of Memphis Foundation  
Memphis, Tennessee

### **Report on the Financial Statements**

We have audited the accompanying financial statements of The University of Memphis Foundation (the Foundation) (a nonprofit organization), which comprise the statement of financial position as of June 30, 2019, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

#### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

#### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Foundation's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.



We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The University of Memphis Foundation as of June 30, 2019, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 2019, on our consideration of the Foundation's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the effectiveness of the Foundation's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Foundation's internal control over financial reporting and compliance.

*Reynolds, Bone & Griesbeck PLC*

October 31, 2019

## **STATEMENT OF FINANCIAL POSITION**

*The University of Memphis Foundation*  
June 30, 2019

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### **ASSETS**

Cash	\$ 591,801
Contributions receivable, net	18,504,231
Accrued interest, dividends, and other receivables	233,300
Investments, at fair value	133,103,818
Cash surrender value of life insurance	127,210
Total assets	<u>\$ 152,560,360</u>

### **LIABILITIES AND NET ASSETS**

Accounts payable, primarily to The University of Memphis	\$ 9,860,411
Gift annuity obligations	<u>148,487</u>
Total liabilities	10,008,898
Net assets	
Without donor restrictions	6,007,712
With donor restrictions	<u>136,543,750</u>
Total net assets	<u>142,551,462</u>
Total liabilities and net assets	<u>\$ 152,560,360</u>

## STATEMENT OF ACTIVITIES

*The University of Memphis Foundation  
Year Ended June 30, 2019*

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	Without Donor Restrictions	With Donor Restrictions	Total
Revenues, gains and other support:			
Contributions	\$ 325,122	\$ 26,181,394	\$ 26,506,516
Investment income	725,764	2,363,257	3,089,021
Net realized and unrealized gains on investments	108,901	1,058,809	1,167,710
Other income	-	7,442,356	7,442,356
Net assets released from restrictions	<u>33,030,833</u>	<u>(33,030,833)</u>	-
Total revenues, gains and other support	34,190,620	4,014,983	38,205,603
Operating expenses:			
University support and operational cost	22,668,132	-	22,668,132
Awards and scholarships	11,010,108	-	11,010,108
Management and general	722,987	-	722,987
Total expenses	<u>34,401,227</u>	<u>-</u>	<u>34,401,227</u>
Change in net assets from operating activities	<u>(210,607)</u>	<u>4,014,983</u>	<u>3,804,376</u>
Nonoperating activities:			
Interest expense	120,757	-	120,757
Bad debt expense	517,400	-	517,400
Change in net assets from nonoperating activities	<u>638,157</u>	<u>-</u>	<u>638,157</u>
Change in net assets	(848,764)	4,014,983	3,166,219
Net assets at beginning of year	<u>6,856,476</u>	<u>132,528,767</u>	<u>139,385,243</u>
Net assets at end of year	<u>\$ 6,007,712</u>	<u>\$ 136,543,750</u>	<u>\$ 142,551,462</u>

*See notes to financial statements.*

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## STATEMENT OF FUNCTIONAL EXPENSES

*The University of Memphis Foundation*  
Year Ended June 30, 2019

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	Program Services			Support Services	
	University Support and Operational Cost	Awards and Scholarships	Total	Management and General	Total Expenses
Salaries and benefits	\$ 867,825	\$ -	\$ 867,825	\$ 544,728	\$ 1,412,553
Moving expenses	2,000	-	2,000	-	2,000
Conferences and travel	349,821	-	349,821	481	350,302
Supplies	353,492	-	353,492	10,419	363,911
Postage	23,644	-	23,644	1,967	25,611
Printing	271,690	-	271,690	73	271,763
Telephone and communications	6,443	-	6,443	1,630	8,073
Maintenance and repairs	9,238	-	9,238	4,870	14,108
Audit services	-	-	-	24,215	24,215
Legal services	4,533	-	4,533	4,590	9,123
Annuity expenses	17,425	-	17,425	-	17,425
Professional services	1,866,829	-	1,866,829	7,914	1,874,743
Publicity/public relations	19,910	-	19,910	-	19,910
Rental fees	132,459	-	132,459	-	132,459
Insurance other	14,534	-	14,534	12,205	26,739
Other expenses	91,913	-	91,913	539	92,452
Dues and memberships subscriptions	161,332	-	161,332	533	161,865
Meals and entertainment	775,296	-	775,296	1,401	776,697
Tickets	22,065	-	22,065	-	22,065
Sponsorships and donations	116,258	-	116,258	1,166	117,424
Gifts and flowers	65,201	-	65,201	133	65,334
Fees	316,134	-	316,134	89,717	405,851
Honorariums	22,700	-	22,700	-	22,700
University support	3,326,718	-	3,326,718	-	3,326,718
USA grants special projects	4,062,498	-	4,062,498	15,493	4,077,991
USA chairs professorships	-	382,347	382,347	-	382,347
Awards	-	266,668	266,668	913	267,581
Furniture and equipment	167,831	-	167,831	-	167,831
Construction and renovation	9,460,292	-	9,460,292	-	9,460,292
USA capital improvements	140,051	-	140,051	-	140,051
Scholarships	-	10,209,584	10,209,584	-	10,209,584
Fellowships	-	39,360	39,360	-	39,360
Interns and graduate assistants	-	112,149	112,149	-	112,149
	<b>\$ 22,668,132</b>	<b>\$ 11,010,108</b>	<b>\$ 33,678,240</b>	<b>\$ 722,987</b>	<b>\$ 34,401,227</b>

*See notes to financial statements.*

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## STATEMENT OF CASH FLOWS

*The University of Memphis Foundation  
Year Ended June 30, 2019*

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Operating activities	
Change in net assets	\$ 3,166,219
Adjustments to reconcile the change in net assets to net cash used for operating activities	
Net realized and unrealized gain on investments	(1,167,710)
Provision for bad debts	517,400
Contributions restricted for endowment	(4,401,080)
Gifts of donated assets to the University of Memphis	882,517
Changes in operating assets and liabilities:	
Contributions receivable	(6,566,014)
Accrued interest, dividends, and other receivables	16,057
Accounts payable, primarily to the University of Memphis	226,550
Gift annuity obligations	6,155
Net cash used for operating activities	<u>(7,319,906)</u>
Investing activities	
Change in cash surrender value of life insurance	(22,212)
Proceeds from sale of investment	59,575,368
Purchases of investments	<u>(57,049,088)</u>
Net cash provided by investing activities	<u>2,504,068</u>
Financing activity - contributions restricted for endowment	<u>4,401,080</u>
Net change in cash	(414,758)
Cash at beginning of year	<u>1,006,559</u>
Cash at end of year	<u>\$ 591,801</u>

*See notes to financial statements.*

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation  
June 30, 2019*

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### **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### *Organization*

The University of Memphis Foundation (the Foundation) operates as a non-profit organization chartered in 1964 in the State of Tennessee. The Foundation accepts and manages private support to the University of Memphis (the University). Leading citizens of the Mid-South area comprise an independent Board of Directors.

#### *Use of Estimates*

Accounting principles generally accepted in the United States of America (U.S. GAAP) require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant financial statement estimates include those used in the valuation of certain investments, the allowance for uncollectible contributions, and the present value discount applied to contributions receivable. Management determines the estimate of the allowance for uncollectible contributions considering a number of factors, including historical experience and aging of accounts. See Notes 3 and 5 for discussions of the present value discounts and fair value measurements, respectively. Management believes that its estimates provided in the financial statements are reasonable. However, actual results could differ from those estimates.

#### *Financial Statements*

The Foundation prepares its financial statements on the accrual basis of accounting to focus on the Foundation as a whole by presenting balances and transactions according to the existence or absence of donor-imposed restrictions. This has been accomplished by classification of balances and transactions into two classes of net assets: net assets without donor restrictions and net assets with donor restrictions.

Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

Net assets without donor restrictions – Net assets not subject to donor-imposed restrictions and may be expended for any purpose in performing the primary objectives of the Foundation. The Foundation's board may designate assets without restrictions for specific operational purposes from time to time.

*Continued*

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation  
June 30, 2019*

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**Net assets with donor restrictions** – Net assets subject to donor-imposed restrictions. Some donor-imposed restrictions are temporary in nature such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resources was restricted has been fulfilled, or both.

Revenues are reported as increases in net assets without donor restrictions unless use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in net assets without donor restrictions. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in net assets without donor restrictions unless their use is restricted by explicit donor stipulation or by law. Expiration of net assets with donor restrictions (i.e., the donor-imposed stipulated purpose has been fulfilled or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets. During the year ended June 30, 2019, the Foundation released net assets with donor restrictions for scholarships, academic enrichment, capital improvements, and various other projects. See Note 6 for releases by purpose.

### *Endowment Fund*

The Foundation is subject to the Uniform Prudent Management of Institutional Funds Act (UPMIFA), which governs the state of Tennessee, the provisions of which apply to its endowment funds. Based on its interpretation of the provisions of UPMIFA, the Foundation is required to act prudently when making decisions to spend or accumulate donor-restricted endowment assets and in doing so to consider a number of factors including the duration and preservation of its donor-restricted endowment funds. Interest and dividend income from the endowment funds are recorded as income on net assets with or without restrictions depending on the donor stipulations. See Note 7 for required disclosures of endowment funds.

### *Statement of Cash Flows*

For purposes of the statement of cash flows, the Foundation recognizes all demand deposit accounts as cash. All money market funds are considered to be investments and no amounts are classified as cash equivalents.

### *Contributions Receivable, Net*

Contributions receivable consist of unconditional promises to give and are recorded when the pledge is received. Contributions receivable that are expected to be collected within the next year are recorded at their net realizable value. Contributions receivable expected to be collected in subsequent years have been discounted to the present value of their net realizable value.

*Continued*

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation*  
June 30, 2019

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Contributions receivable are stated at the amount management expects to collect from outstanding balances. Management monitors outstanding balances and provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based upon its assessments of the current status of individual accounts. Balances that are still outstanding after a reasonable period of time has elapsed are generally written off through a charge to the valuation allowance and a credit to the appropriate contribution receivable.

Conditional promises to give are not included as revenue until the conditions are substantially met. The Foundation had received conditional promises to give of \$10,266,778 at June 30, 2019. These potential contributions, if received, would generally be restricted for specific purposes stipulated by the donors.

### *Investments*

The Foundation's investments are stated at fair value. Fair value is the price that would be received to sell an asset in an ordinary transaction between market participants at the measurement date. See Note 5 for a discussion of fair value measurements.

Purchases and sales of investments are recorded on a trade-date basis. Interest income is recorded when earned and dividends are recorded on the ex-dividend date. Net realized and unrealized gains on investments include the Foundation's gains and losses on investments bought and sold as well as held during the year and are included in revenues, gains and other support on the statement of activities.

### *Income Taxes*

The Internal Revenue Service has ruled that the Foundation qualifies under Section 501(c)(3) of the Internal Revenue Code and is, therefore, not subject to federal income tax under present income tax laws. The Foundation's limited partnership investments generate unrelated business income or loss activity which is subject to federal income taxes. There was no unrelated business income tax expense for the year ended June 30, 2019.

In accordance with U.S. GAAP, if applicable, the Foundation recognizes interest expense and penalties related to uncertain tax positions as interest expense and penalties in operating expenses. No amounts have been recognized in operating expenses for 2019. The Foundation is subject to routine audits by taxing authorities; however, there are currently no audits for any tax periods in progress.

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation*  
June 30, 2019

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### *Administrative Fee*

In order to cover expenses of the Foundation's operations and provide funds for University support, an administrative fee of 2.0% was assessed on the carrying value of accounts invested in the endowment pool for the year ended June 30, 2019. The fee covers the cost of business office operations, provides support for University's fundraising activities, and assists with other needs of the University. Administrative fees earned were approximately \$1,905,000 for the year ended June 30, 2019.

### *Concentrations of Credit Risk*

Due to the nature of its business and the volume of revenue activity, the Foundation can accumulate, from time to time, bank balances in excess of the insurance provided by federal deposit insurance authorities. The risk of maintaining deposits in excess of amounts insured by federal deposit authorities is managed by maintaining such deposits in high quality financial institutions.

### *Functional Allocation of Expenses*

The costs of providing various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the program and support services benefited. The method of allocation for salaries and benefits was time and effort. All other expenses were allocated based on a full-time equivalent since they are incurred through invoices submitted by the University.

### *Adoption of Accounting Principle*

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Updated (ASU) No. 2016-14: *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The update addresses the complexity and understandability of net asset classification, deficiencies in information about liquidity and availability of resources, and the lack of consistency in the type of information provided about expenses and investment return. The Foundation has adjusted the presentation of these statements accordingly. The ASU has been applied retrospectively to all periods presented which increased net assets without donor restrictions by \$464,490 and decreased net assets with donor restrictions by \$464,490 resulting from the reclassifications of underwater endowment funds as required under ASU 2016-14.

In August 2018, the FASB issued ASU No. 2018-13, *Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement*, which modifies the disclosure requirements for fair value measurements by removing and modifying certain disclosures relating to transfers between levels in the fair value hierarchy, Level 3 investments, and investments that calculate net asset value (NAV). The new guidance is effective for reporting periods beginning after December 15, 2019. Early adoption is permitted. Effective July 1, 2018 the Foundation has early adopted ASU No. 2018-13, the effect of which was insignificant.

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation*  
June 30, 2019

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### *Recent Accounting Pronouncements*

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. It is intended to clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP. The new guidance is effective for reporting periods beginning after December 15, 2018. Early application is permitted for periods beginning after December 15, 2016. The Foundation has elected not to early implement ASU No. 2014-09 at this time. The effects of adopting ASU No. 2014-09 have not been determined.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326)*, which requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts and requires enhanced disclosures related to the significant estimates and judgments used in estimating credit losses on investments available for sale and purchased financial assets with credit deterioration. The new guidance is effective for reporting periods beginning after December 15, 2021. Early adoption of ASU No. 2016-13 is permitted for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The effects of adopting ASU No. 2016-13 have not been determined.

In June 2018, the FASB issued ASU No. 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, which clarifies the criteria for evaluating whether contributions are unconditional (and thus recognized immediately in income) or conditional (for which income recognition is deferred) and applies to all entities that receive or make contributions, including business entities. For transactions in which a non-public entity serves as a resource recipient, the entity should apply the amendments in ASU No. 2018-08 on contributions received to annual periods beginning after December 15, 2018. For transactions in which a non-public entity serves as a resource provider, the entity should apply the amendments in ASU No. 2018-08 on contributions made to annual periods beginning after December 15, 2019. Early adoption is permitted. The School has elected not to early adopt ASU No. 2018-08 at this time. The effects of adopting ASU No. 2018-08 have not been determined.

### *Subsequent Events*

Management has reviewed events occurring through October 31, 2019, the date the financial statements were available to be issued, and no subsequent events occurred requiring accrual or disclosure.

## **2. LIQUIDITY AND AVAILABILITY**

All assets of the Foundation are restricted for University support and expended for specific uses within the University. The budget allocation for Foundation operations for the year ended June 30, 2019 was \$650,790. Foundation operations are funded by the annual endowment administrative fee.

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation*  
June 30, 2019

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### **3. CONTRIBUTIONS RECEIVABLE, NET**

Contributions receivable, net at June 30, 2019 consist of the following:

Amounts due in:	
Less than one year	\$ 7,435,886
One to five years	12,036,725
More than five years	<u>635,823</u>
Gross promises to give	20,108,434
Less allowance for uncollectible pledges	(1,126,072)
Less unamortized present value discount	<u>(478,131)</u>
Contributions receivable, net	<u>\$ 18,504,231</u>

Contributions receivable beyond one year have been discounted to their net present value using imputed interest rates of 0.90% to 2.67% as of June 30, 2019.

### **4. INVESTMENTS**

Investments as of June 30, 2019 are summarized as follows:

	Cost	Fair Value
Money market funds	\$ 752,887	\$ 752,904
Public U.S. equity	3,000,000	3,135,921
Public global equity	1,350,000	2,220,445
Limited partnerships and LLCs	40,924,711	46,410,552
Mutual funds	49,268,310	48,381,474
U.S. government securities	5,697,585	5,720,454
Corporate bonds	<u>26,448,223</u>	<u>26,482,068</u>
	<u><u>\$ 127,441,716</u></u>	<u><u>\$ 133,103,818</u></u>

### **5. FAIR VALUE OF ASSETS AND LIABILITIES**

U.S. GAAP defines fair value and establishes a framework for measuring fair value. Fair value measurements apply to financial assets and liabilities, as well as non-financial assets and liabilities which are re-measured at least annually.

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation*  
June 30, 2019

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U.S. GAAP establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable market data, when available, and minimizes the use of unobservable inputs when determining fair value. Observable inputs reflect assumptions market participants would use in pricing an asset or liability based on market data obtained from independent sources. Unobservable inputs reflect the Foundation's assumptions about the assumptions market participants would use in pricing an asset or liability based on the best information available in the circumstances.

The Foundation groups its assets and liabilities measured at fair value in three levels based on the reliability of valuation inputs used to determine fair value. The proper level of fair value measurement is determined based on the lowest level of significant input. The levels are as follows:

- Level 1 valuations are based on quoted prices in active markets for identical assets or liabilities.
- Level 2 valuations are based on inputs other than quoted prices included in Level 1 that are observable for assets or liabilities, either directly or indirectly. These inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active (i.e. markets in which there are few transactions for the assets or liabilities, the prices are not current, or price quotes vary substantially either over time or among market makers), and modeling techniques based on inputs that are observable for the assets or liabilities.
- Level 3 valuations are based on modeling techniques using significant assumptions that are not observable in the market. The assumptions reflect the Foundation's own assumptions that market participants would use in pricing the assets or liabilities.

The availability of observable inputs varies from product to product and is affected by a variety of factors, including the type of product, whether the product is new and not yet established in the marketplace, and other characteristics particular to the transaction. To the extent valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised by the Foundation in determining fair value is greatest for instruments categorized in Level 3.

Financial assets and liabilities measured at fair value on a recurring basis include the following:

*Money market fund:* Valued at the daily closing price as reported by the fund. Money market funds held by the Foundation are open-ended mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily NAV and to transact at that price. The money market mutual funds held by the Foundation are deemed to be actively traded.

*Public U.S. and global equities:* Valued at the unadjusted quoted market price within active markets.

*Continued*

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## NOTES TO FINANCIAL STATEMENTS

*The University of Memphis Foundation*  
June 30, 2019

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**Mutual funds:** Valued at the daily closing price reported on the active market on which securities are traded.

**U.S. government securities and corporate bonds:** Valued at quoted prices from less active markets and/or quoted prices of securities with similar characteristics.

**Limited partnerships:** Valued using the NAV or capital balances as a practical expedient to determine the fair value.

Valuations provided by the general partners and investment managers are evaluated by management through accounting and financial reporting processes to review and monitor existence and valuation assertions. Management has instituted processes in the areas of initial due diligence, ongoing monitoring and financial reporting. Management also reviews interim financial information and reviews details of investment holdings to obtain an understanding of the underlying investments. Monitoring also includes obtaining and reviewing audited financial statements noting the type of opinion, basis of accounting, procedures pertaining to the valuation of alternative investments and comparison of audited valuation with the fund's valuation.

Information pertaining to investments measured at fair value on a recurring basis aggregated by valuation input level as of June 30, 2019 follows:

	Level 1	Level 2	Level 3	Total
Money market funds	\$ 752,904	\$ -	\$ -	\$ 752,904
Public U.S. equity	3,135,921	-	-	3,135,921
Public global equity	2,220,445	-	-	2,220,445
<b>Mutual funds</b>				
U.S. equity	10,226,953	-	-	10,226,953
Emerging markets equity	7,178,703	-	-	7,178,703
Real assets	2,172,108	-	-	2,172,108
Opportunistic	2,598,383	-	-	2,598,383
International equity	14,566,077	-	-	14,566,077
Fixed income	11,639,250	-	-	11,639,250
Total mutual funds	48,381,474	-	-	48,381,474
U.S. government securities	-	5,720,454	-	5,720,454
Corporate bond securities	-	26,482,068	-	26,482,068
<b>Limited partnerships measured at NAV</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>46,410,552</b>
<b>Total</b>	<b>\$ 54,490,744</b>	<b>\$ 32,202,522</b>	<b>\$ -</b>	<b>\$ 133,103,818</b>

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## NOTES TO FINANCIAL STATEMENTS

*The University of Memphis Foundation*  
June 30, 2019

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### Investments Measured Using Net Asset Value Per Share Practical Expedient or Capital Balances

The following table summarizes investments for which fair value is measured using the NAV per share practical expedient or capital balances as of June 30, 2019:

	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
Limited partnerships:				
Hedge strategies-hedged equity <sup>(a)</sup>	\$ 15,355,668	\$ -	Monthly/Quarterly/Annually	3-90 days
Private equity <sup>(b)</sup>	6,204,416	4,340,748	Upon Liquidation	N/A
Real assets <sup>(c)</sup>	7,786,416	3,043,562	Upon Liquidation	N/A
U.S. equity <sup>(d)</sup>	5,808,284	-	Quarterly	60-90 days
International equity <sup>(e)</sup>	7,425,665	-	Monthly/Quarterly	30-90 days
Emerging markets equity <sup>(f)</sup>	1,201,851	-	Monthly	30 days
Opportunistic <sup>(g)</sup>	2,628,252	-	Monthly	60-90 days

- (a) This category consists of a fund of funds that make long and short position equity investments.
- (b) This category consists of partnerships that invest primarily in U.S. based private companies. These investments cannot be voluntarily redeemed and are subject to sale based on market demand.
- (c) This category consists of investment partnerships and funds that invest primarily in U.S. and foreign commercial real estate and natural resources. Some investments in this category allow quarterly redemption, but distributions during periods of illiquidity are restricted by gate constraints.
- (d) This category generally consists of managers that invest primarily in equity securities of U.S. corporations. U.S. equity may include multiple styles (growth, value) and market capitalizations (small, mid, large). These investments will primarily be long-only.
- (e) This category will generally consist of managers that invest primarily in equity securities of corporations domiciled in foreign countries. International equity may include multiple styles (growth, value) and market capitalizations (small, mid, large). These investments will primarily be long-only.
- (f) This category will generally consist of managers that invest primarily in equity securities of corporations domiciled in emerging foreign countries. Emerging markets equity may include multiple styles (growth, value) and market capitalizations (small, mid, large). These investments will primarily consist of long-only investments and hedged equity investments (long and short).

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation*  
June 30, 2019

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- (g) This category may include any strategy that offers exceptional risk/reward opportunities. This category is designed to provide the investment committee with the flexibility to select investments for a relatively small part of an overall allocation, which may not fit into the other designed allocation categories.

### **6. NATURE AND AMOUNTS OF NET ASSETS WITH DONOR RESTRICTIONS**

Net assets with donor restrictions are restricted for the following purposes:

Subject to expenditure for a specified purpose:

Alumni relations	\$ 664,340
Awards	355,384
Centers, institutes, and labs	2,161,611
Contributions receivable, net	16,222,914
Departmental/academic enrichment	5,950,912
Gift annuities	37,628
Professorships/chairs/visiting scholars	290,059
Scholarships/fellowships	2,998,907
Special projects/lecture series/workshops	<u>8,011,295</u>
	36,693,050

Endowments:

Subject to expenditure for a specified purpose:

Alumni relations	166,764
Awards	660,038
Centers, institutes, and labs	1,199,234
Departmental/academic enrichment	2,304,175
Professorships/chairs/visiting scholars	4,015,213
Scholarships/fellowships	8,782,779
Special projects/lecture series/workshops	<u>2,143,873</u>
	19,272,076

*Continued*

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## NOTES TO FINANCIAL STATEMENTS

*The University of Memphis Foundation*  
June 30, 2019

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Perpetual in nature:	
Alumni relations	\$ 677,423
Awards	2,662,943
Centers, institutes, and labs	2,254,265
Contributions receivable, net	2,281,317
Departmental/academic enrichment	10,114,572
Professorships/chairs/visiting scholars	15,232,687
Scholarships/fellowships	35,389,728
Special projects/lecture series/workshops	<u>11,965,689</u>
	<u>80,578,624</u>
Total endowment	<u>99,850,700</u>
Total net assets with donor restrictions	<u>\$ 136,543,750</u>

Net assets with donor restrictions that are perpetual in nature originated with contributions received to establish perpetual endowments. The endowment gift is to be held in perpetuity with the capital appreciation and earnings thereon to be used to provide financial assistance to deserving scholars, salary supplements and awards to attract and retain outstanding faculty members, visiting artists and lecturers and to provide for various departmental and University needs.

Releases from donor restrictions for the year ended June 30, 2019 are as follows:

Subject to expenditure for a specified purpose:	
Alumni relations	\$ 427,700
Awards	114,434
Capital improvements	10,292,417
Centers, institutes, and labs	1,171,914
Contributions receivable, net	517,412
Departmental/academic enrichment	2,732,677
Gift annuities	18,045
Operations	10,221
Professorships/chairs/visiting scholars	71,225
Scholarships/fellowships	10,177,449
Special projects/lecture series/workshops	<u>4,632,409</u>
	<u>30,165,903</u>

*Continued*

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation*  
June 30, 2019

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### Endowments:

Subject to expenditure for a specified purpose:

Alumni relations	\$ 35,635
Awards	89,961
Centers, institutes, and labs	89,835
Departmental/academic enrichment	702,705
Professorships/chairs/visiting scholars	763,947
Scholarships/fellowships	1,042,507
Special projects/lecture series/workshops	<u>140,340</u>
	<u>2,864,930</u>
	<u><u>\$ 33,030,833</u></u>

## **7. ENDOWMENT FUNDS**

The Foundation's endowment accounts consist of donor-restricted endowment funds and include approximately 560 individual funds established for a variety of purposes. As required by U.S. GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Board of Directors of the Foundation has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as net assets with donor restrictions (a) the original value of gifts donated to the perpetual endowment funds and (b) the original value of subsequent gifts to the perpetual endowment funds. In accordance with UPMIFA, the Foundation considers the following factors in making a determination to appropriate or accumulate donor restricted endowment funds:

- The duration and preservation of the fund
- The purposes of the Foundation and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Foundation
- The investment policies of the Foundation

*Continued*

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## NOTES TO FINANCIAL STATEMENTS

*The University of Memphis Foundation*  
June 30, 2019

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*Endowment Net Asset Composition by Type of Fund as of June 30, 2019:*

	Without Donor Restrictions	With Donor Restrictions	Total
Donor-restricted endowment funds	\$ -	\$ 99,850,700	\$ 99,850,700
Board-designated endowment funds	<u>2,977,905</u>	-	<u>2,977,905</u>
	<u>\$ 2,977,905</u>	<u>\$ 99,850,700</u>	<u>\$ 102,828,605</u>

*Changes in Endowment Net Assets for the Year Ended June 30, 2019:*

	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets, beginning of year	\$ 3,191,044	\$ 96,666,152	\$ 99,857,196
Investment return:			
Investment income	6,946	263,330	270,276
Net change (realized and unrealized)	<u>29,118</u>	<u>1,058,809</u>	<u>1,087,927</u>
Total investment return	<u>36,064</u>	<u>1,322,139</u>	<u>1,358,203</u>
Contributions	-	4,478,136	4,478,136
Appropriation of endowment assets for expenditure	<u>(249,203)</u>	<u>(2,615,727)</u>	<u>(2,864,930)</u>
Endowment net assets, end of year	<u>\$ 2,977,905</u>	<u>\$ 99,850,700</u>	<u>\$ 102,828,605</u>

*Continued*

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation  
June 30, 2019*

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### *Underwater Endowments*

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the Foundation is required to retain in a fund of perpetual duration. In accordance with U.S. GAAP, deficiencies of this nature are reported in net assets with donor restrictions. These deficiencies resulted from unfavorable market fluctuations that occurred after the investment of net assets with donor restrictions contributions and/or continued appropriation for fees and expenditures. At June 30, 2019, deficiencies of this nature existed in 58 donor-restricted endowment funds, which together have an original gift value of \$13,608,607, a current fair value of \$12,806,243, and a deficiency of \$802,364.

### *Return Objectives and Risk Parameters*

The Foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment funds while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Foundation must hold in perpetuity or for a donor specified period as well as board-designated funds. Under this policy, as approved by the Board of Directors, the endowment assets are invested in a manner that is intended to produce consistent long-term growth of capital without undue exposure to risk.

### *Strategies Employed for Achieving Objectives*

To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that places an emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

### *Spending Policy and How the Investment Objectives Relate to Spending Policy*

The Foundation has a policy of budgeting for expenditure each year a percentage of its endowment funds' average fair value over the prior twelve quarters through the fiscal year-end one year preceding the fiscal year in which the expenditure is planned. This percentage was 4% for fiscal year 2019. In establishing this policy, the Foundation considered the long-term expected return on its endowment funds. Accordingly, over the long term, the Foundation expects the current spending policy to allow for endowment growth. This is consistent with the Foundation's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

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## **NOTES TO FINANCIAL STATEMENTS**

*The University of Memphis Foundation*  
June 30, 2019

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The Foundation has a policy that permits spending underwater endowment funds depending on the degree to which the fund is underwater, unless otherwise precluded by donor intent or relevant laws and regulations. The Board of Directors appropriated for expenditures \$51,068 from underwater endowment funds during the year ended June 30, 2019, which represents 3% of the 12 quarter moving average, not the 4% it generally draws from its endowment.

### **8. RELATED PARTY TRANSACTIONS**

The Foundation provided direct support to the University for general departmental expenditures, scholarships, and awards which totaled \$34,401,227 for the year ended June 30, 2019. The Foundation had accounts payable to the University in the amount of \$9,634,322 as of June 30, 2019.

#### *Interfund Advance*

The Foundation has agreed to advance up to \$10,976,899 to a Foundation fund as an interfund advance benefiting the athletic department of the University at a 4.00% annual interest rate for the purpose of providing financial support to allow the athletic department to undertake construction of a football practice facility in advance of receiving payment of donor funding commitments. The advance is to be repaid in full not later than June 30, 2025 and is secured by certain future collections of receivables and other collections related to certain Foundation funds benefitting the athletic department. Interfund advances totaling \$10,715,069 were outstanding as of June 30, 2019.

#### *Contributed Services*

Based upon an operating agreement between the University and Foundation, the University provides office space and donation collection and processing services for the Foundation. The University provided contributed services under the terms of the operating agreement in the amount of \$186,171 for the year ended June 30, 2019.

### **9. CONCENTRATIONS OF RISK**

Although the Foundation has a policy to maintain a diversified investment portfolio, its investments are subject to market and credit risks which may be affected by economic developments in a specific geographic region or industry.

Approximately 22% of the Foundation's contributions receivable balance at June 30, 2019 was due from one donor.



**INDEPENDENT AUDITOR'S 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***

Board of Directors  
The University of Memphis Foundation  
Memphis, Tennessee

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 University of Memphis Foundation (the Foundation) (a nonprofit organization), which comprise the statement of financial position as of June 30, 2019, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated October 31, 2019.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Foundation's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control. Accordingly, we do not express an opinion on the effectiveness of the Foundation'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 combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Foundation's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is 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.

Our consideration of the 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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.



## Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Foundation'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 determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

There were no prior year findings reported.

## 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 Foundation'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 Foundation's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Reynolds, Bone & Griswold PLC*

October 31, 2019

# **7. External Audit Report: University of Memphis Research Foundation 6/30/2019 Report**

**Presented by Vicki Deaton**

# The University of Memphis Board of Trustees

Presentation

For Information

**Date:** December 4, 2019

**Committee:** Audit Committee

**Presentation Title:** External Audit Report - University of Memphis Research Foundation Financial Statements, June 30, 2019

**Presented by:** Vicki D. Deaton, Chief Audit Executive

## Synopsis:

On September 30, 2019, the University of Memphis Research Foundation Financial Statements, June 30, 2019 were issued. The financial statements are presented for your information according to the responsibilities for Internal Audit under UofM Policy GE2016 Notification of External Audits and Reviews, which includes reporting occurrences of external reviews and audits to the Audit Committee, Division of State Audit and others as the circumstances may dictate.

From the Audit Report's Management Discussion and Analysis: The University of Memphis Research Foundation (UMRF) is a nonprofit corporation established on June 16, 2006, to develop and administer sponsored research and other sponsored projects conducted by the faculty and staff of the University. In addition, the UMRF may seek and hold patents and copyrights, negotiate and administer licenses, and collect and distribute royalties on behalf of the University. As of June 30, 2019, 41 patents had been assigned to the UMRF by the University. The UMRF's Board of Directors approves the annual operating budget for the UMRF's administrative expenses. Sponsored projects' budgets are passed through to the University. The UMRF utilizes University facilities and personnel to perform sponsored projects and for operating the UMRF. The University is reimbursed quarterly for expenses incurred on behalf of the UMRF. The UMRF is an affiliate of the University of Memphis.

The UMRF's financial report incorporates the financial statements and activities of the UMRF's wholly-owned subsidiary, UMRF Ventures, Inc. as a component unit. UMRF Ventures was incorporated in 2017 with the mission to create good paying, part-time jobs for UofM students in a professional on-campus environment, and to provide the students with financial resources, relevant job experience, and potential pathways to future full-time employment. At fiscal year-end, UMRF Ventures employed approximately 200 students with a monthly payroll approaching \$300,000. In April 2019 UMRF Ventures paid its first shareholder dividend to the UMRF in the amount of \$50,000.

The UMRF will continue to explore opportunities to support the advancement of research excellence and the expansion of research infrastructure at the University. The strategic focus will be on equity holdings in subsidiary ventures as the primary means for generating funds. The Foundation will proceed with further development of the UMRF Research Park. Phase Two will be the establishment of an applied research facility located on the Park Avenue Campus. Phase Three will focus on public-private partnerships to attract research enterprises and labs to the University District.

The UMRF engaged an independent external CPA firm, Fouts and Morgan, PC, to perform an audit of the financial statements of the business-type activity and discretely presented component unit of the UMRF. The independent auditor's opinion stated that the financial statements present fairly, in all material respects, the respective financial position of the business-type activity and the discretely presented component unit of the UMRF as of June 30, 2019, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

The auditors did not identify any deficiencies in internal control that would be considered material weaknesses during their limited consideration of internal control over financial reporting. Also, they did not identify any instances of noncompliance or other matters with certain provisions of laws, regulations, contracts and grant agreements.

**THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION  
FINANCIAL STATEMENTS  
JUNE 30, 2019**

# THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION

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JUNE 30, 2019

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**THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**  
**BOARD OF DIRECTORS AND MANAGEMENT OFFICIALS**  
**JUNE 30, 2019**

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**BOARD OF DIRECTORS**

David Scully	Secretary/Treasurer
Richard Bloomer	Director
Jan Bouten	Director
John Campbell	Director
Lakita Cavin	Director
Robert Jackson	Director
Raajkumar Kurapati	Director
Abby Parrill-Baker	Director
Brad Phillips	Director
Ted Townsend	Director
Scott Vogel	Director

**MANAGEMENT OFFICIALS**

Jasbir Dhaliwal	Executive Director
Angela Bunch	Accountant

## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors  
The University of Memphis Research Foundation  
Memphis, Tennessee

We have audited the accompanying financial statements of the business-type activities and discretely presented component unit of The University of Memphis Research Foundation as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Foundation's basic financial statements as listed in the table of contents.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

### Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

### Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the discretely presented component unit of The University of Memphis Research Foundation as of June 30, 2019, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

### Other Matters

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 - 9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated September 30, 2019, on our consideration of The University of Memphis Research Foundation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of The University of Memphis Research Foundation's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering The University of Memphis Research Foundation's internal control over financial reporting and compliance.

*Fouts & Morgan*

FOUTS & MORGAN  
Certified Public Accountants

Memphis, Tennessee  
September 30, 2019

# THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION

## MANAGEMENT'S DISCUSSION AND ANALYSIS PRIMARY GOVERNMENT

JUNE 30, 2019

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The following Management's Discussion and Analysis ("MD&A") provides an overview of the financial position and the results of operations of The University of Memphis Research Foundation (the "Foundation") for the year ended June 30, 2019. We encourage you to read this MD&A section in conjunction with the accompanying audited financial statements and notes to the financial statements.

### About the Financial Statements

As an affiliate unit of The University of Memphis (the "University"), the Foundation has implemented the governmental accounting standards for state and local governments and for public colleges and universities. Because the Foundation is not supported by governmental tax revenues, the Foundation presents its financial statements in a single column "business-type activity" format appropriate for college and university enterprise funds. Governmental accounting standards define business-type activities as those financed in whole or in part by fees charged to external parties for goods and services.

The financial statements incorporate the activities of the Foundation's wholly-owned subsidiary, UMRF Ventures, Inc., as a component unit.

In addition to this MD&A section, the financial statements consist of a statement of net position, a statement of revenues, expenses, and changes in net position, a statement of cash flows, and notes to the financial statements.

The statement of net position is the Foundation's balance sheet. It reflects the total assets, liabilities and net position of the Foundation as of June 30, 2019. Liabilities due within one year, and assets available to pay those liabilities, are classified as current. Other assets and liabilities are classified as noncurrent. Net position is grouped in the following categories:

- Restricted
- Unrestricted

The statement of revenues, expenses, and changes in net position details how net position has increased (or decreased) during the fiscal year ended June 30, 2019.

The statement of cash flows details how cash has increased (or decreased) during the fiscal year ended June 30, 2019. It classifies the sources and uses of Foundation cash into the following categories:

- Operating activities
- Investing activities
- Financing activities

Cash flows associated with the Foundation's unrestricted net assets primarily result from operating activities and investment income.

The notes to the financial statements provide additional details on the amounts reported in the financial statements.

### General

The Foundation is a nonprofit corporation established on June 16, 2006, to develop and administer sponsored research and other sponsored projects conducted by the faculty and staff of the University. In addition, the Foundation may seek and hold patents and copyrights, negotiate and administer licenses, and collect and distribute royalties on behalf of the University. As of June 30, 2019, forty-one (41) patents had been assigned to the Foundation by the University. The Foundation's Board of Directors approves the annual operating budget for the Foundation's administrative expenses. Budgets for sponsored projects are administered by the University. The Foundation utilizes University facilities and personnel to perform sponsored projects and for operating the Foundation. The Foundation reimburses the University quarterly for expenses incurred on behalf of the Foundation.

# THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION

## MANAGEMENT'S DISCUSSION AND ANALYSIS PRIMARY GOVERNMENT - Continued

JUNE 30, 2019

### Financial Highlights and Key Trends

During fiscal year 2019, the Foundation continued its management of sponsored projects processed through the Foundation. The Foundation also continued with an investment policy that considers risk tolerance, return objectives, and liquidity requirements.

In December 2018, the Foundation established the UMRF Research Park, launching the first of three phases by opening a facility in the heart of the University District. Phase One assembled an inaugural cohort of 17 citizen companies and collaborator members. Citizen companies reside in the facility and work with University students, faculty and staff to grow in the University District over the coming years. Collaborators also participate in the larger innovation community based in the facility.

A portion of the Foundation's operating expenses for the year ended June 30, 2019 was paid with funds from accumulated and current year interest income and contributions from The University of Memphis Foundation.

### Statement of Net Position

Current assets include cash, investments, and receivables expected to be collected in the coming year. Other assets include patents, notes receivable and equity interest in UMRF Ventures, Inc. Current liabilities include payables, deferred revenue expected to be recognized in the next fiscal year, and security deposits from UMRF Research Park residents. There were no long-term liabilities as of June 30, 2019. The amount of unrestricted net position is income after payment of operating expenses, while restricted net position is the amount of sponsored projects revenue being held for future expenditure.

At June 30, 2019, funds held by an investment broker on behalf of the Foundation totaled \$1,647,357. Of this amount, \$1,640,767 represents investments at fair value and \$6,590 represents deposits with banks affiliated with the broker.

A summary of the major components of the net position of the Foundation as of June 30, 2019 and 2018 is as follows:

	2019	2018
<b>Assets</b>		
Current assets	<u>\$ 1,879,788</u>	<u>\$ 1,898,561</u>
Other assets	<u>768,548</u>	<u>281,552</u>
<b>Total assets</b>	<u>\$ 2,648,336</u>	<u>\$ 2,180,113</u>
<b>Liabilities</b>		
	<u>\$ 741,570</u>	<u>\$ 503,378</u>
<b>Net position</b>		
Restricted for research	<u>\$ 231,551</u>	<u>\$ 364,066</u>
Unrestricted	<u>1,675,215</u>	<u>1,312,669</u>
<b>Total net position</b>	<u>\$ 1,906,766</u>	<u>\$ 1,676,735</u>

The increase in unrestricted net position is primarily due to the increase in the equity interest in UMRF Ventures, Inc. that resulted from a significant increase in its operating income.

The decrease in restricted net position is attributable to the expenditure in the current fiscal year of funds recorded as revenue in a prior fiscal year.

# THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION

## MANAGEMENT'S DISCUSSION AND ANALYSIS PRIMARY GOVERNMENT - Continued

JUNE 30, 2019

### Statement of Revenues, Expenses, and Changes in Net Position

A summary of the statement of revenues, expenses, and changes in net position for the years ended June 30, 2019 and 2018, is as follows:

	<u>2019</u>	<u>2018</u>
Operating revenues	\$ 364,551	\$ 2,814,318
Operating expenses	<u>(587,071)</u>	<u>(2,916,378)</u>
Operating loss	(222,520)	(102,060)
Nonoperating income (expense)		
Royalty income	14,265	42,916
Interest income	-	4,261
Net investment income	41,718	6,857
Increase (decrease) equity interest in subsidiary	<u>396,568</u>	<u>(135,885)</u>
Change in net position	<u>\$ 230,031</u>	<u>\$ (183,911)</u>

The significant decrease in operating revenues and expenses in fiscal 2019 compared to fiscal 2018 is largely attributable to fewer sponsored projects being completed in fiscal 2019.

The Foundation recognizes project revenue for grants upon receipt of cash or a pledge with no contingencies and recognizes expenses as incurred. The Foundation recognizes project revenue and expenses for contracts when projects are completed.

### Statement of Cash Flows

In fiscal 2019, cash inflows came from sponsored project revenue, contributions, UMRF Research Park revenue, and interest and royalty income. Personnel expenses of the Foundation were incurred by the University and reimbursed by The University of Memphis Foundation. Cash outflows for other operating activities were paid directly by the Foundation and were primarily for sponsored project expenses. All sponsored project expenses are incurred by the University and reimbursed by the Foundation. Cash outflows also included a \$225,000 loan to UMRF Ventures, Inc.

### Future

The Foundation will continue to explore opportunities to support the advancement of research excellence and the expansion of research infrastructure at the University. The strategic focus will be on equity holdings in subsidiary ventures as the primary means for generating funds.

The Foundation will proceed with further development of the UMRF Research Park. Phase Two will be the establishment of an applied research facility located on the Park Avenue Campus. Phase Three will focus on public-private partnerships to attract research enterprises and labs to the University District.

# **THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**

## **MANAGEMENT'S DISCUSSION AND ANALYSIS COMPONENT UNIT JUNE 30, 2019**

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UMRF Ventures, Inc. (the "Company") is a wholly-owned subsidiary of The University of Memphis Research Foundation (the "Foundation"). The following MD&A provides an overview of the financial position and the results of operations of the Company for the year ended June 30, 2019. We encourage you to read this MD&A section in conjunction with the accompanying audited financial statements and notes to the financial statements.

### **General**

The Company was incorporated in 2017 and started up its business on July 1, 2017 with the mission to create good-paying, part-time jobs for The University of Memphis' (the "University") students, in a professional on-campus environment, that provides the students with financial resources, relevant job experience, and potential pathways to future full-time employment.

### **Financial Highlights and Key Trends**

At the beginning of fiscal year 2019, the Company had in operation two Level 1 IT helpline call centers employing 80 students on the University's main campus and 25 students on the Lambuth campus, and an IT Command Center employing 40 graduate students on the main campus.

In January 2019, the Company started another venture, The Information Security Center, employing an additional 15 graduate students in support of FedEx's InfoSec group.

In May 2019, the Company opened its new South Campus facility. The Main Campus Level 1 Call Center was relocated there and expanded from 15 to 27 work stations. In addition, a new Level 2 call center was started with 10 work stations and an additional 25 student employees. The Company expended approximately \$382,000 for capital assets in connection with the move to this new facility.

As the Company exits year two, it is employing approximately 200 students and has a monthly payroll approaching \$300,000. The business has turned a profit, and in April 2019 paid its first shareholder dividend to the Foundation, in the amount of \$50,000.

### **Statement of Net Position**

Current assets include cash and receivables expected to be collected in the coming year. Long-term assets consist of property and equipment. Current liabilities include payables, accrued payroll, and deferred revenue expected to be recognized in the next fiscal year. Long-term liabilities include deferred revenue extending beyond one year, deferred taxes, and loans received from the Foundation and from the University. All net position is considered to be unrestricted as of June 30, 2019.

**THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
COMPONENT UNIT - Continued  
JUNE 30, 2019**

A summary of the major components of the net position of the Company as of June 30, 2019 and 2018 is as follows:

	<u>2019</u>	<u>2018</u>
<b>Assets</b>		
Current assets	\$ 880,140	\$ 482,903
Capital assets	372,025	11,858
Deferred income taxes	-	50,100
<b>Total assets</b>	<u>\$ 1,252,165</u>	<u>\$ 544,861</u>
<b>Liabilities</b>		
Current liabilities	\$ 275,491	\$ 365,980
Long-term liabilities	765,891	314,666
<b>Total liabilities</b>	<u>\$ 1,041,382</u>	<u>\$ 680,646</u>
<b>Net position</b>		
Common stock	\$ 100	\$ 100
Retained earnings	210,683	(135,885)
<b>Total net position</b>	<u>\$ 210,783</u>	<u>\$ (135,785)</u>

The increase in net position is due to a significant increase in operating income, principally driven by expansion of call center operations.

**Statement of Revenues, Expenses, and Changes in Net Position**

A summary of the statement of revenues, expenses and changes in net position for the years ended June 30, 2019 and 2018 is as follows:

	<u>2019</u>	<u>2018</u>
Operating revenues	\$ 3,667,690	\$ 921,862
Operating expenses	(3,217,523)	(1,107,847)
<b>Operating income (loss)</b>	<b>450,167</b>	<b>(185,985)</b>
Nonoperating income (expense)	(53,599)	-
Income tax benefit	-	50,100
<b>Change in net position before dividend</b>	<b>396,568</b>	<b>(135,885)</b>
Dividend	(50,000)	-
<b>Change in net position after dividend</b>	<b>\$ 346,568</b>	<b>\$ (135,885)</b>

The significant increase in operating revenues and expenses in fiscal 2019 compared to fiscal 2018 is primarily a result of the expansion in the number and size of the Company's call centers.

# **THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**

## **MANAGEMENT'S DISCUSSION AND ANALYSIS COMPONENT UNIT - Continued JUNE 30, 2019**

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The Lambuth Call Center became cash positive in July 2018, its third month of operation. The IT Command Center issued its first invoice to FedEx at the end of June 2018. The IT Command Center and the Information Security Center both operate as "cost plus mark-up" and are profitable and cash positive by design.

### **Statement of Cash Flows**

Fiscal 2019 cash inflows came from contract revenue and proceeds from a line of credit with a local bank and from loans from the Foundation and the University. Cash outflows were for operating expenses, full repayment of line of credit proceeds, and payment of a dividend to the Foundation.

### **Future**

The long-range vision for the Company is to operate a sustainably profitable enterprise, providing jobs and financial resources to over 500 students per year, and to dividend profits back to the Foundation.

**THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**

**STATEMENT OF NET POSITION**  
**JUNE 30, 2019**

	<b>ASSETS</b>	<b>Primary Government</b>	<b>Component Unit</b>
<b>Current Assets</b>			
Cash and cash equivalents	\$ 79,978	\$ 525,200	-
Investment securities	1,640,767	-	-
Accounts receivable	159,043	354,940	-
Total current assets	<u>1,879,788</u>	<u>880,140</u>	<u>880,140</u>
<b>Fixed Assets</b>			
Property and equipment	-	399,051	-
Allowance for depreciation	-	(27,026)	-
Net fixed assets	<u>-</u>	<u>372,025</u>	<u>372,025</u>
<b>Other Assets</b>			
Notes receivable	225,000	-	-
Equity interest in subsidiary	210,783	-	-
Patents, net of amortization	332,765	-	-
Total other assets	<u>768,548</u>	<u>-</u>	<u>-</u>
<b>Total Assets</b>	<u>\$ 2,648,336</u>	<u>\$ 1,252,165</u>	<u>\$ 1,252,165</u>
<b>LIABILITIES AND NET POSITION</b>			
<b>Current Liabilities</b>			
Current portion of related party debt	\$ -	\$ 62,500	-
Payable to The University of Memphis	234,910	11,667	-
Accounts payable	5,453	17,389	-
Deferred revenue	493,801	114,162	-
Accrued payroll and other liabilities	7,406	66,368	-
State taxes payable	-	3,405	-
Total current liabilities	<u>741,570</u>	<u>275,491</u>	<u>275,491</u>
<b>Long-term Liabilities</b>			
Related party debt - long term	-	662,500	-
Deferred federal and state income taxes	-	3,499	-
Deferred revenue	-	99,892	-
Total long-term liabilities	<u>-</u>	<u>765,891</u>	<u>765,891</u>
<b>Net Position</b>			
Restricted for research	231,551	-	-
Unrestricted	1,675,215	-	-
Common stock - proprietary component unit, \$.001 par value, 2,000,000 shares authorized, 100,000 issued and outstanding	-	100	-
Retained earnings - proprietary component unit	-	210,683	-
Total net position	<u>1,906,766</u>	<u>210,683</u>	<u>210,683</u>
<b>Total Liabilities and Net Position</b>	<u>\$ 2,648,336</u>	<u>\$ 1,252,165</u>	<u>\$ 1,252,165</u>

See accompanying notes to the financial statements.

**THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION  
FOR THE YEAR ENDED JUNE 30, 2019**

	<b>Primary Government</b>	<b>Component Unit</b>
<b>Operating Revenue</b>		
Contract revenue	\$ 142,488	\$ 3,667,690
Grants and contributions	72,856	-
Patent contributions	83,164	-
Income from Research Park	<u>66,043</u>	-
Total operating revenues	<u>364,551</u>	<u>3,667,690</u>
<b>Operating Expenses</b>		
Depreciation and amortization	26,020	21,809
General and administrative	-	27,476
Insurance	4,336	15,618
Interest	-	21,288
Network services	13,969	37,063
Office equipment	-	66,072
Other	1,262	10,528
Payroll taxes	-	223,315
Professional fees	53,700	85,006
Rent	4,475	123,733
Repairs and maintenance	-	34,582
Research projects	<u>466,386</u>	-
Salaries	<u>16,923</u>	<u>2,551,033</u>
Total operating expenses	<u>587,071</u>	<u>3,217,523</u>
<b>Operating Income (Loss)</b>	<u>(222,520)</u>	<u>450,167</u>
<b>Other Income</b>		
Royalty income	14,265	-
Net investment income	41,718	-
Increase in equity interest in subsidiary	<u>396,568</u>	-
Total other income	<u>452,551</u>	-
<b>Income before Income Taxes</b>	<u>230,031</u>	<u>450,167</u>
<b>Income Tax Expense</b>	<u>-</u>	<u>(53,599)</u>
<b>Change in Net Position</b>	<u>230,031</u>	<u>396,568</u>
<b>Net Position, Beginning of Year</b>	<u>1,676,735</u>	<u>(135,785)</u>
<b>Dividends Paid</b>	<u>-</u>	<u>(50,000)</u>
<b>Net Position, End of Year</b>	<u>\$ 1,906,766</u>	<u>\$ 210,783</u>

See accompanying notes to the financial statements.

**THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**

**STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED JUNE 30, 2019**

	<b>Primary Government</b>	<b>Component Unit</b>
<b>Cash flows from operating activities</b>		
Cash received from contract customers	\$ 606,888	\$ 3,220,077
Cash received from contributions	55,933	-
Cash received from Research Park	63,057	-
Cash payments to The University of Memphis	(662,432)	(168,970)
Cash payments to suppliers	(58,172)	(239,402)
Cash payments to employees	-	(2,752,585)
Cash paid for interest	-	(11,288)
Net cash provided by (used for) operating activities	<b>5,274</b>	<b>47,832</b>
<b>Cash flows from investing activities</b>		
Purchases of property and equipment	-	(381,976)
Purchases of investments	(1,634,717)	-
Investment maturities	888,000	-
Proceeds from the sale of investments	125,200	-
Income from royalties	14,265	-
Income from investments, net of fees	84,623	-
Loans to subsidiary	(225,000)	-
Net cash used for investing activities	<b>(747,629)</b>	<b>(381,976)</b>
<b>Cash flows from noncapital financing activities</b>		
Proceeds received from line of credit	-	124,977
Repayments made on line of credit	-	(225,589)
Proceeds received from related party debt	-	725,000
Dividends paid	-	(50,000)
Net cash provided by financing activities	<b>-</b>	<b>574,388</b>
Change in cash and cash equivalents	<b>(742,355)</b>	<b>240,244</b>
Cash and cash equivalents at beginning of year	<b>822,333</b>	<b>284,956</b>
Cash and cash equivalents at end of year	<b>\$ 79,978</b>	<b>\$ 525,200</b>

See accompanying notes to the financial statements.

**THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**

**STATEMENT OF CASH FLOWS - Continued  
FOR THE YEAR ENDED JUNE 30, 2019**

	<b>Primary Government</b>	<b>Component Unit</b>
<b>Reconciliation of operating income (loss) to net cash provided by (used for) operating activities</b>		
Operating income (loss)	\$ (222,520)	\$ 450,167
<b>Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities</b>		
Depreciation and amortization	26,020	21,809
Gain on sale of investments	-	-
Patent contributions	(83,164)	-
Patent impairment loss	5,932	-
<b>Changes in operating assets and liabilities</b>		
<b>(Increase) decrease in operating assets:</b>		
Accounts receivable	(94,971)	(156,993)
<b>Increase (decrease) in operating liabilities:</b>		
Accounts payable	5,453	(3,525)
Payable to The University of Memphis	(82,726)	1,826
Accrued payroll and other liabilities	7,406	21,763
State taxes payable	-	3,405
Deferred revenue	<u>443,844</u>	<u>(290,620)</u>
<b>Net cash provided by (used for) operating activities</b>	<b>\$ 5,274</b>	<b>\$ 47,832</b>

**See accompanying notes to the financial statements.**

# THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION

## NOTES TO FINANCIAL STATEMENTS JUNE 30, 2019

---

### PRIMARY GOVERNMENT

#### Note 1 - Summary of Significant Accounting Policies

##### *Organization and Activities*

The University of Memphis Research Foundation (the "Foundation") is a not-for-profit corporation created in June 2006 as an agent to promote the development, implementation, and coordination of sponsored research solely for the benefit of The University of Memphis (the "University") in the furtherance of the University's research objectives. Operations for the Foundation commenced on July 1, 2007.

##### *Financial Reporting Entity*

In determining the financial reporting entity, the Foundation complies with the provisions of GASB No. 14, *The Financial Reporting Entity*. Based on this standard, the Foundation's wholly-owned for-profit entity was determined to be a component unit. UMRF Ventures, Inc. is a legally separate entity for which the Foundation is considered to be financially accountable.

##### *Basis of Presentation*

The University is a public institution governed by an independent board of trustees under the FOCUS Act, which is a component unit of the State of Tennessee. Therefore, as an affiliate of, and created solely for the benefit of, the University, the financial statements of the Foundation have been prepared in accordance with accounting principles generally accepted in the United States of America for public colleges and universities, as prescribed by the Governmental Accounting Standards Board (GASB).

##### *Basis of Accounting*

For financial statement purposes, the Foundation is considered a special-purpose government engaged only in business-type activities. Accordingly, the financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

##### *Cash and Cash Equivalents*

For purposes of the statements of cash flows, all highly liquid investments purchased with initial maturities of three months or less are considered to be cash equivalents.

##### *Accounts Receivable*

Accounts receivable represent amounts due from grants and services rendered on contracts as of June 30, 2019. The Foundation records accounts receivable at their estimated net realizable value. An allowance for doubtful accounts is recorded based upon management's estimate of uncollectible accounts, determined by analysis of specific customer accounts. Past due balances and delinquent receivables are charged against the allowance when they are determined to be uncollectible by management. Management did not consider an allowance for doubtful accounts to be necessary as of June 30, 2019.

##### *Investment Securities*

The Foundation carries investments at fair value in the statement of net position. Investments are recorded on the trade-date basis. Realized and unrealized gains and losses are included in the net investment income in the statement of revenues, expenses, and changes in net position.

##### *Patents*

Certain patents related to research projects have been donated to the Foundation by the University. Donated patents are recorded as contributions at the estimated fair value on the date of donation, which approximates the cost incurred by the University.

## **NOTES CONTINUED**

### **Note 1 - Summary of Significant Accounting Policies - Continued**

#### ***Patents - Continued***

Patents are amortized over their useful lives, estimated at twenty years, using the straight-line method and are stated net of accumulated amortization.

It is the goal of the Foundation to license patents to companies with the expertise and capability to commercialize inventions covered by the patents. At least annually, or if a determination is made that there is no accessible market for a patent, an impairment assessment is performed and the carrying value of the patent may be adjusted. Any impairment loss determined by management is included in the statement of revenues, expenses and changes in net position in the year in which impairment is determined. Impairment loss determined during the year ended June 30, 2019 was \$5,932.

#### ***Equity Interest in Subsidiary***

In accordance with accounting principles issued by GASB, the Foundation's ownership of its wholly-owned for-profit subsidiary is accounted for using the equity method; whereby the recorded amount includes the purchase price of the stock plus the Foundation's share (100% in this case) of the subsidiary's profit or loss.

#### ***Net Position***

The Foundation's net position is classified as follows:

***Restricted for research*** - includes resources which the Foundation is legally or contractually obligated to spend on research in accordance with restrictions imposed by external third parties.

***Unrestricted*** - Unrestricted net position represents resources that do not meet the definition of restricted net position and may be used by the Foundation to meet expenses for any purpose. This classification includes any project residuals that are no longer restricted but have been designated for future research expenditures. There were \$452,964 of such residual funds available at June 30, 2019.

When both restricted and unrestricted resources are available, it is the Foundation's policy to use restricted resources first, then unrestricted resources as they are needed.

#### ***Revenue Recognition***

The Foundation's revenues are derived from grants, research contracts, and contributions which provide support for the Foundation. The Foundation recognizes revenue from research contracts once the project has been completed. The Foundation maintains records of any amounts that are remaining at the conclusion of a project by transferring the funds to a residual balance account in the name of the project's principal investigator and holds these funds for future projects to be approved by the Foundation. Deferred revenue consists of amounts billed on research contracts net of expenditures incurred to date.

Grants and contribution revenue are recognized when written documentation is received and all conditions have been satisfied for the Foundation to be eligible to receive the grant or contribution.

Revenues derived from grants, research contracts, and contributions are reported as operating revenues. Transactions that are investment-related are reported as non-operating income. Interest and royalties are recorded when earned and are reported as non-operating income.

#### ***Income Taxes***

The Internal Revenue Service has classified the Foundation as other than a private foundation, which is exempt from federal income taxes on its related purpose under Section 501(c)(3) of the United States Internal Revenue Code and is similarly exempt from state income taxes. Consequently, no federal or state income taxes have been provided for the primary government in these financial statements.

## **NOTES CONTINUED**

### **Note 1 - Summary of Significant Accounting Policies - Continued**

#### *Fair Value Measurements*

Accounting standards define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establish the framework for a fair value hierarchy. The fair value hierarchy gives the highest priority to observable inputs such as quoted prices in active markets for identical assets or liabilities (Level 1), the next highest priority to inputs (other than quoted prices within Level 1) such as quoted prices for similar assets or liabilities, quoted prices in inactive markets, or other inputs that can be corroborated by observable market data (Level 2), and the lowest priority to unobservable inputs (Level 3). Inputs are broadly defined as assumptions market participants would use in pricing an asset or liability.

#### *Use of Estimates*

Management uses estimates and assumptions in preparing financial statements in accordance with U.S. GAAP. Such estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and reported revenue and expenses. Accordingly, actual results could differ from estimates.

### **Note 2 - Deposits with Banking Institutions**

Deposits with financial institutions consist of demand deposits with local banks or with banks affiliated with the Foundation's investment broker.

Custodial credit risk is the risk that, in the event of bank failure, the Foundation's deposits may not be returned. The Foundation has implemented an investment policy to minimize custodial credit risk from banking institutions. As of June 30, 2019, the Foundation had no deposits in excess of federally insured limits.

Although the Foundation qualifies for reporting as a governmental entity under the GASB framework, management has determined that the Foundation does not meet the definition of a "public depositor." Accordingly, management does not believe that the Foundation's deposits are available to be collateralized by its banking institutions; therefore, the Foundation is exempt from Tennessee Code Annotated Section 9 requirements that all public deposits in excess of federally insured limits, if any, must be collateralized.

### **Note 3 - Investment Securities**

The objective of the Foundation's investment policy is to preserve capital with a secondary objective of earning the highest possible total return (capital appreciation and income return) consistent with prudent levels of risk. At a minimum, long-term rates of return should be equal to an amount sufficient to maintain the purchasing power of these assets plus a modest gain to help offset the expense of running the Foundation. The portfolio should be constructed using a total return approach with the majority of the funds invested to seek protection of principal over time. The assets are to be invested for the long term but with significant liquidity.

The Chair and Treasurer jointly, with active assistance and recommendations from the Foundation's Investment Consultant, shall have responsibility for establishing overall financial objectives, setting investment policy, and setting parameters for asset allocation. Domestic and international equities both large and small capitalization, fixed income, cash equivalent securities and alternative investments in the form of diversified fund of funds hedge funds have been determined to be acceptable vehicles for investment.

As of June 30, 2019, investment securities consisted of brokered certificates of deposit and publicly traded mutual funds with fair values totaling \$1,640,767.

Custodial credit risk is the risk that the Foundation's investments may not be returned. The Foundation does not have a policy for custodial credit risk for its investments; however, all investments are held in third-party safekeeping at an institution that is a member of the Securities Investor Protection Corporation (SIPC). SIPC covers custodial risk up to \$500,000 per investor.

Interest rate risk is the risk that changes in the interest rates may adversely affect an investment's fair value. As a means of maximizing interest income while minimizing fair value losses and maintaining adequate liquidity, the Foundation has adopted an investment policy to invest excess operating cash in brokered certificates of deposit.

## NOTES CONTINUED

### Note 4 - Fair Value Measurements

As of June 30, 2019, the following table presents the Foundation's financial assets measured at fair value on a recurring basis:

	Fair Value	Level 1	Level 2	Level 3
Brokered Certificates of Deposit	\$ 596,356	\$ -	\$ 596,356	\$ -
Mutual Funds	1,044,411	1,044,411	-	-
	<u>\$ 1,640,767</u>	<u>\$ 1,044,411</u>	<u>\$ 596,356</u>	<u>\$ -</u>

Brokered certificates of deposit are traded on a secondary market, which generally values these instruments by discounting the related cash flows based on current yields of similar instruments with comparable durations, as reported by the custodian.

Fair values for mutual funds are determined by reference to quoted market prices and other relevant information generated by market transactions.

The methods described above may produce fair value calculations that may not be indicative of net realizable value or reflective of future fair value. While the Foundation believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions could result in a different fair value measurement at the reporting date.

### Note 5 - Patents

As of June 30, 2019, patents consisted of the following:

	Patents, at <u>Contributed Value</u>	Accumulated <u>Amortization</u>	Patents, net
Balance, June 30, 2018	\$ 371,997	\$ (90,444)	\$ 281,553
Patents contributed by University of Memphis	83,164	-	83,164
Impairment loss	(9,303)	3,371	(5,932)
Amortization	-	(26,020)	(26,020)
Balance, June 30, 2019	<u>\$ 445,858</u>	<u>\$ (113,093)</u>	<u>\$ 332,765</u>

### Note 6 - Concentrations

The Foundation recorded approximately sixty-eight percent of total contract billings from one funding source during the year ended June 30, 2019.

## **NOTES CONTINUED**

### **Note 7 - Related Party Transactions**

Expenditures to the University represent amounts paid by the Foundation to reimburse the University for certain expenses including project management, business office operations and personnel support, incurred by the University on behalf of the Foundation.

Residual balance payments are paid annually to the University for costs incurred on projects that utilize excess funds from previously completed projects that are now available to be used in funding current projects. Such amounts are included in expenditures to the University in the accompanying statement of revenues, expenses, and changes in net position.

During the year ended June 30, 2019, the Foundation made cash transfers to the University in the amount of \$662,432. As of June 30, 2019, the Foundation had payables to the University totaling \$234,910.

The University allocates salary expense attributable to the Foundation totaling \$16,923 for the year ended June 30, 2019, and is reimbursed for these expenses directly by the University of Memphis Foundation, which is recorded in turn as contribution revenue by the Foundation. In addition, the Foundation received grant funding in the amount of \$48,000 to be used for government relations from the University of Memphis Foundation. The Foundation paid rent to the University for the use of office space in the amount of \$4,475 during 2019.

In September 2018, the Foundation loaned UMRF Ventures, Inc. \$225,000 for working capital support to expand its services. This loan bears interest at 5 percent per annum and is due September 20, 2020. The Foundation received interest relating to this loan totaling \$8,437 during the year ended June 30, 2019.

### **Note 8 - Component Unit**

The Foundation has one component unit, its wholly-owned for-profit subsidiary, UMRF Ventures, Inc. (the "Company"). The Company is managed by its own board of directors and management. The Foundation has determined that the Company meets the requirements of a discretely presented component unit under GASB 14. Significant disclosures related to the Company are included on pages 19 -21.

### **Note 9 - Subsequent Events**

Management has evaluated subsequent events through September 30, 2019, the date the financial statements were available to be issued.

## **NOTES CONTINUED**

### **COMPONENT UNIT**

Where applicable, UMRF Ventures, Inc. (the "Company") has adopted the same or substantially similar accounting policies as the Foundation. Accordingly, the disclosures presented herein represent only the policies and disclosures that are unique to the Company's operations.

#### **Note 1 - Summary of Significant Accounting Policies of Component Unit**

##### *Organization and Activities*

The Company is a for-profit entity, which is wholly-owned by the Foundation, that began operations on July 1, 2017 as part of an economic development initiative to provide real and transferable opportunities to students in the Memphis community through student-operated call centers. The Company believes that its call center model serves as a template for future opportunities that benefit students of the University.

##### *Accounts Receivable*

Accounts receivable represent amounts due for services rendered as of June 30, 2019. The Company records accounts receivable at their estimated net realizable value. An allowance for doubtful accounts is recorded based upon management's estimate of uncollectible accounts, determined by analysis of specific customer accounts. Past due balances and delinquent receivables are charged against the allowance when they are determined to be uncollectible by management. No allowance for doubtful accounts was considered necessary at June 30, 2019, and no accounts were written off during the year ended June 30, 2019.

##### *Property and Equipment*

Property, equipment, major renewals, and betterments are recorded at cost for individual items \$2,500 or greater and a useful life greater than one year. Expenditures for normal repair and maintenance are expensed to operations as they occur. Depreciation is provided through the straight-line method over the lease contract period of three years.

##### *Income Taxes*

The Company follows the asset and liability approach to financial accounting and reporting for income taxes. The Company's federal and state tax returns are prepared on the cash basis of accounting, and the difference between the financial statements and tax bases of assets and liabilities is determined annually. Deferred income tax assets and liabilities are computed for those differences that have future tax consequences using the currently enacted tax laws and rates that apply to the period in which they are expected to affect taxable income. Valuation allowances are established, if necessary, to reduce the deferred tax asset to the amount that will more likely than not be realized.

##### *Recently Issued Accounting Standard*

In June 2017, the Governmental Accounting Standards Board issued GASB Statement No. 87, Leases ("GASB No. 87"), effective for reporting periods beginning after December 15, 2019, with early adoption permitted. GASB No. 87 requires the recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows or outflows of resources based on the payment provisions of the contract. Management is still evaluating the effects of this standard on its financial statements but anticipates successfully implementing these provisions for its fiscal 2021 financial statements.

## NOTES CONTINUED

### Note 2 - Property and Equipment

As of June 30, 2019, property and equipment consisted of the following:

	<u>Balance</u> <u>June 30, 2018</u>	<u>Additions</u>	<u>Dispositions</u>	<u>Balance</u> <u>June 30, 2019</u>
Leasehold improvements	\$ 17,075	\$ 158,826	\$ -	\$ 175,901
Furniture & fixtures	- -	223,150	-	223,150
	<u>17,075</u>	<u>381,976</u>	<u>-</u>	<u>399,051</u>
Less Accumulated depreciation	(5,217)	(21,809)	-	(27,026)
Total Property and equipment	<u>\$ 11,858</u>	<u>\$ 360,167</u>	<u>\$ -</u>	<u>\$ 372,025</u>

### Note 3 - Line of Credit

At June 30, 2019, the Company had available a revolving line of credit of \$225,000 with a local bank which expires on March 26, 2020. Borrowings under this line of credit agreement bear interest at 2.55% per annum. Interest is payable monthly. The line is collateralized by a personal deposit account of a member of management. There were no borrowings outstanding under this line of credit at June 30, 2019.

### Note 4 - Related Party Debt

Note payable to The University of Memphis Research Foundation for working capital support, bearing interest at 5.0 percent. Interest only payments are due semiannually, with the entire principal due September 20, 2020.

\$ 225,000

Note payable to The University of Memphis, bearing interest at 4.0 percent, due in quarterly payments beginning January 1, 2020 and maturing on December 31, 2023.

500,000

Less: Current portion

725,000

Related party debt - long term

\$ 662,500

Principal payments due on related party debt for the next five years ending June 30 are as follows:

2020	\$ 62,500
2021	350,000
2022	125,000
2023	125,000
2024	<u>62,500</u>
	<u>\$ 725,000</u>

### Note 5 - Leases with Related Party

The Company leases rooms with workstations under various lease agreements with The University of Memphis, a related party, expiring through March 21, 2021. During 2019, the Company moved its operations into a facility on the University's South Campus and also rented space on the University's Lambuth Campus to house its expanding operations. For the year ended June 30, 2019, rent expense was \$123,733.

## **NOTES CONTINUED**

### **Note 5 - Leases with Related Party - Continued**

Minimum rental commitments under the leases are as follows:

2020	\$ 259,526
2021	<u>198,669</u>
	<u><u>\$ 458,195</u></u>

### **Note 6 - Other Related Party Transactions**

The Company pays the University monthly for rent and data usage. During the year ended June 30, 2019, the Company incurred expenses from the University totaling \$37,063 in data usage fees. As of June 30, 2019, the Company had \$11,667 due to the University for data fees and accrued interest.

### **Note 7 - Income Taxes**

The Company evaluates and accounts for uncertain tax positions in accordance with Accounting Standards Codification (ASC) 740-10 and has evaluated its tax positions taken for all open tax years. The Company has filed returns with the Internal Revenue Service and the Tennessee Department of Revenue and considers these to be its major tax jurisdictions. Currently, the 2018 and 2019 tax years are open and subject to examination. However, the Company is not currently under audit nor has the Company been contacted by these jurisdictions.

The Company has approximately \$180,000 of federal and state net operating loss ("NOL") carryforwards available to offset future taxable income.

As of June 30, 2019, the income tax liability consists of the following:

	<u>Federal</u>	<u>State</u>	<u>Total</u>
Excess tax depreciation	\$ 197,971	\$ 197,971	
Net operating loss carryforward	<u>(187,198)</u>	<u>(178,945)</u>	
Future taxable income	10,773	19,026	
Statutory rate	<u>21%</u>	<u>6.5%</u>	
Deferred tax liability	<u><u>\$ 2,262</u></u>	<u><u>\$ 1,237</u></u>	<u><u>\$ 3,499</u></u>

The income tax provision shown on the statement of revenues, expenses, and changes in net position differs from the amount that would result from applying statutory tax rates to income before provision for income taxes because of utilization of the prior year's net operating loss carryforward.

Based on the evaluation of the Company's tax positions, management believes all positions taken would more likely than not be upheld under examination. Therefore, no provision for the effects of uncertain tax positions has been recorded for the year ended June 30, 2019.

### **Note 8 - Concentrations**

The Company recorded approximately ninety-nine percent of total revenue and ninety-six percent of total receivables from FedEx during the year ended June 30, 2019.

The Company has two contracts with FedEx expiring in May 2021. Management expects to be able to renew the contracts on favorable terms.

Douglas A. Garner, CPA

J. Donald Short, CPA

Michael T. Odom, CPA, CVA

Randal L. Gregory, CPA

Gary D. Purdy, CPA, CA

Jimmie D. Fouts, CPA (1941-2008)

Don W. Morgan, CPA (1939-2005)

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**INDEPENDENT AUDITOR'S 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**

To the Board of Directors  
The University of Memphis Research Foundation  
Memphis, Tennessee

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 the discretely presented component unit of The University of Memphis Research Foundation, as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise The University of Memphis Research Foundation's basic financial statements, and have issued our report thereon dated September 30, 2019.

#### **Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered The University of Memphis Research Foundation's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of The University of Memphis Research Foundation's internal control. Accordingly, we do not express an opinion on the effectiveness of The University of Memphis Research Foundation'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.

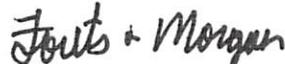
Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

#### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether The University of Memphis Research Foundation'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 determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

#### **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 Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



**FOUTS & MORGAN**  
Certified Public Accountants

Memphis, Tennessee  
September 30, 2019

**THE UNIVERSITY OF MEMPHIS RESEARCH FOUNDATION**

**SCHEDULE OF FINDINGS AND RESPONSES**  
**JUNE 30, 2019**

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Our audit disclosed no findings that are required to be reported herein under *Government Auditing Standards*.

# **8. External Audit Report: University of Memphis Auxiliary Services Foundation**

**6/30/2019**

Report

Presented by Vicki Deaton

# The University of Memphis Board of Trustees

Presentation

For Information

**Date:** December 4, 2019

**Committee:** Audit Committee

**Presentation Title:** External Audit Report - Auxiliary Services Foundation Financial Statements, June 30, 2019

**Presented by:** Vicki D. Deaton, Chief Audit Executive

## Synopsis:

On November 8, 2019, the Auxiliary Services Foundation Financial Statements, June 30, 2019, were issued. The financial statements are presented for your information according to the responsibilities for Internal Audit under UofM Policy GE2016 Notification of External Audits and Reviews, which includes reporting occurrences of external reviews and audits to the Audit Committee, Division of State Audit and others as the circumstances may dictate.

The Auxiliary Services Foundation (Foundation) engaged an independent external CPA firm, Fouts and Morgan, PC, to perform an audit of the financial statements of the Foundation. The independent auditor's opinion stated that the financial statements present fairly, in all material respects, the financial position of Auxiliary Services Foundation as of June 30, 2019, and the changes in its net assets and cash flows for the period April 15, 2019 through June 30, 2019 in accordance with accounting principles generally accepted in the United States of America.

The auditors did not identify any deficiencies in internal control that would be considered material weaknesses during their limited consideration of internal control over financial reporting. Also, they did not identify any instances of noncompliance or other matters with certain provisions of laws, regulations, contracts and grant agreements.

The Foundation is a not-for-profit corporation that commenced operations in April 2019 as an agent to operate auxiliary enterprises which directly benefit the University of Memphis (University). The Foundation accepts, administers, applies, and uses property acquired by gift, grant, devise, or bequest solely for the benefit of the University. The Foundation is currently managing two capital projects for the University – the Natatorium Facility Improvements Design services and the Indoor Football Practice Facility Phase 2 Construction.

Because the Foundation's resources can only be used by, or for the benefit of the University, the Foundation is considered a component unit of the University. The auditors noted that the Foundation's Board of Directors and management officials consulted with the University's auditors, the TN Comptroller of the Treasury's Division of State Audit, due to the component unit affiliation between the Foundation and the University. The TN Comptroller of the Treasury's Division of State Audit required an adjustment to the financial statements of the Foundation to remove the balances and activity arising from the transfer of the Herff Trust assets, pending the issuance of the Tennessee Attorney General's opinion on the allowability of the transfer.

**AUXILIARY SERVICES FOUNDATION  
FINANCIAL STATEMENTS**

**JUNE 30, 2019**

## AUXILIARY SERVICES FOUNDATION

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JUNE 30, 2019

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**AUXILIARY SERVICES FOUNDATION**  
**BOARD OF DIRECTORS AND MANAGEMENT OFFICIAL**  
**JUNE 30, 2019**

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**BOARD OF DIRECTORS**

Thomas G. Kadien	President
Richard A. Spell	Vice President
Fred A. Towler	Secretary
Raajkumar Kurapati	Treasurer
Dr. M. David Rudd	Director

**MANAGEMENT OFFICIAL**

Byron Morgan	Executive Director
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To the Board of Directors  
Auxiliary Services Foundation  
Memphis, Tennessee

## INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying financial statements of Auxiliary Services Foundation (a nonprofit organization) which comprise the statement of financial position as of June 30, 2019, and the related statements of activities and cash flows for the period April 15, 2019 through June 30, 2019, and the related notes to the financial statements.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

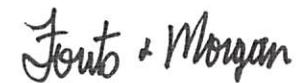
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Auxiliary Services Foundation as of June 30, 2019, and the changes in its net assets and cash flows for the period April 15, 2019 through June 30, 2019 in accordance with accounting principles generally accepted in the United States of America.

### **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2019, on our consideration of Auxiliary Services Foundation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Auxiliary Services Foundation's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Auxiliary Services Foundation's internal control over financial reporting and compliance.

The logo consists of the words "Fouts & Morgan" written in a cursive, handwritten-style font.

FOUTS & MORGAN  
Certified Public Accountants

Memphis, Tennessee  
November 8, 2019

**AUXILIARY SERVICES FOUNDATION**  
**STATEMENT OF FINANCIAL POSITION**  
**JUNE 30, 2019**

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**ASSETS**

**Current Assets**

Cash and cash equivalents	\$ 8,971,124
Due from affiliate	863
Total current assets	<u>8,971,987</u>

**Other Assets**

Cash value of life insurance	<u>302,590</u>
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**Total Assets**

\$ 9,274,577

**LIABILITIES AND NET ASSETS**

**Current Liabilities**

Accounts payable	\$ 606,185
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**Net Assets**

With donor restrictions	
Restricted for capital projects	\$ 8,365,802
Restricted for other University support	<u>302,590</u>
Net assets with donor restrictions	<u>8,668,392</u>

**Total Liabilities and Net Assets**

\$ 9,274,577

See accompanying notes to the financial statements.

**AUXILIARY SERVICES FOUNDATION**  
**STATEMENT OF ACTIVITIES**  
**FOR THE PERIOD APRIL 15, 2019 THROUGH JUNE 30, 2019**

	<b>Without Donor Restrictions</b>	<b>With Donor Restrictions</b>	<b>Totals</b>
<b>Support and Revenue</b>			
Transfers from affiliate organizations	\$ -	\$ 9,281,103	\$ 9,281,103
Investment income	- -	8,474	8,474
Total support and revenue	-	9,289,577	9,289,577
<b>Net Assets Released from Restrictions</b>	<b>621,185</b>	<b>(621,185)</b>	<b>-</b>
Total support and revenue and net assets released from restrictions	621,185	8,668,392	9,289,577
<b>Expenses</b>			
Program - University Support			
Natatorium architectural design	95,567	-	95,567
Football Phase II - construction costs	523,106	-	523,106
Total program expenses	618,673	-	618,673
Management and general			
Legal fees	2,512	-	2,512
Total Expenses	621,185	-	621,185
<b>Change in Net Assets</b>	<b>-</b>	<b>8,668,392</b>	<b>8,668,392</b>
Net Assets at April 15, 2019	-	-	-
Net Assets at June 30, 2019	<b>\$ -</b>	<b>\$ 8,668,392</b>	<b>\$ 8,668,392</b>

See accompanying notes to the financial statements.

**AUXILIARY SERVICES FOUNDATION**

**STATEMENT OF CASH FLOWS  
FOR THE PERIOD APRIL 15, 2019 THROUGH JUNE 30, 2019**

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**Cash Flows From Operating Activities**

Cash received from transfers from affiliate organizations \$ 8,971,124

Net increase in cash and cash equivalents 8,971,124

**Cash and cash equivalents at beginning of period** -

**Cash and cash equivalents at end of period** \$ 8,971,124

**Noncash Investing Transaction**

Life insurance policy transferred from affiliate organization \$ 302,590

See accompanying notes to the financial statements.

## AUXILIARY SERVICES FOUNDATION

### NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2019

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#### Note A - Summary of Significant Accounting Policies

##### Organization and Activities

Auxiliary Services Foundation (the "Foundation") is a not-for-profit corporation that commenced operations in April 2019 as an agent to operate auxiliary enterprises which directly benefit The University of Memphis ("University"); and accept, administer, apply, and use property acquired by gift, grant, devise, bequest, or otherwise solely for the benefit of The University. Because the Foundation's resources can only be used by, or for the benefit of The University, the Foundation is considered a component unit of the University.

##### Basis of Accounting

The financial statements have been prepared using the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

##### Cash and Cash Equivalents

For purposes of the statements of cash flows, all highly liquid investments purchased with initial maturities of three months or less are considered to be cash equivalents.

##### Net Assets

Net assets, revenues and support, gains, and losses are classified based on the existence or absence of donor or donor-imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

*Net Assets Without Donor Restrictions* - Net assets available for use in general operations and not subject to donor restrictions. The board of directors may designate net assets for certain purposes from net assets without donor restrictions, depending on future needs in accordance with the strategic plans for The University.

*Net Assets With Donor Restrictions* - Net assets subject to donor imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both.

*Restricted for capital projects* - includes resources received by the Foundation for specified capital expenditures which have been restricted by the donors when contributed to the original recipient organization.

*Restricted for other University support* - includes resources received by the Foundation to be used to support and fund the present and future needs of The University.

## **NOTES CONTINUED**

### **Note A - Summary of Significant Accounting Policies - Continued**

#### **Revenue Recognition**

The Foundation's revenues are derived from organizations affiliated with The University and contributions which provide support for the Foundation. Transfers from affiliate organizations are recognized as revenue when the determination to transfer the assets is made by the transferring organization. Contribution revenue is recognized when written documentation is received and all conditions have been satisfied for the Foundation to be eligible to receive the contribution.

#### **Income Taxes**

The Internal Revenue Service has classified the Foundation as other than a private foundation, which is exempt from federal income taxes on its related purpose under Section 501(c)(3) of the United States Internal Revenue Code and is similarly exempt from state income taxes. Consequently, no federal or state income taxes have been provided for the primary government in these financial statements.

#### **Fair Value Measurements**

Accounting standards define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establish the framework for a fair value hierarchy. The fair value hierarchy gives the highest priority to observable inputs such as quoted prices in active markets for identical assets or liabilities (Level 1), the next highest priority to inputs (other than quoted prices within Level 1) such as quoted prices for similar assets or liabilities, quoted prices in inactive markets, or other inputs that can be corroborated by observable market data (Level 2), and the lowest priority to unobservable inputs (Level 3). Inputs are broadly defined as assumptions market participants would use in pricing an asset or liability.

#### **Use of Estimates**

Management uses estimates and assumptions in preparing financial statements in accordance with U.S. GAAP. Such estimates and assumptions affect the reported amounts of assets and liabilities, and revenue and expenses. Accordingly, actual results could differ from estimates.

### **Note B - Deposits with Financial Institutions**

Deposits with financial institutions consist of demand deposits with local banks or with banks affiliated with the Foundation's investment broker.

Custodial credit risk is the risk that, in the event of the failure of a depository financial institution, the Foundation will not be able to recover deposits. The Foundation does not have a formal policy regarding custodial risk.

The Foundation had deposits held in financial institutions of \$8,721,124 which were in excess of FDIC coverage.

## **NOTES CONTINUED**

### **Note C - Related Party Transactions**

The Foundation received the following transfers from organizations affiliated to The University during the period ending June 30, 2019:

University of Memphis Foundation	\$ 8,558,091
University of Memphis Research Foundation	<u>723,012</u>
	<u><u>\$ 9,281,103</u></u>

Expenditures made by the Foundation are in support of The University and are presented by activity on the statement of activities.

### **Note D - Net Assets With Donor Restrictions**

Net assets are restricted for the following activities at June 30, 2019:

	<u>Capital Projects</u>	<u>Other University Support</u>	<u>Total Net Assets with Donor Restrictions</u>
Natatorium Facility Improvements	\$ 633,407	\$ -	\$ 633,407
Indoor Football Practice Facility Phase 2	7,732,395	-	7,732,395
University Support at the discretion of the Board of Directors	-	302,590	302,590
	<u><u>\$ 8,365,802</u></u>	<u><u>\$ 302,590</u></u>	<u><u>\$ 8,668,392</u></u>

### **Note E - Commitments**

The Foundation is currently managing two capital projects for The University and is under obligation for the following contracts for the design and construction of these projects:

	<u>Contract Amount</u>	<u>Expended through June 30, 2019</u>	<u>Commitment Remaining June 30, 2019</u>
Natatorium Facility Improvements			
Design services	\$ 140,995	\$ 95,567	\$ 45,428
Indoor Football Practice Facility Phase 2			
Construction	10,181,899	510,597	9,671,302
	<u><u>\$ 10,322,894</u></u>	<u><u>\$ 606,164</u></u>	<u><u>\$ 9,716,730</u></u>

## **NOTES CONTINUED**

### **Note F - Liquidity**

All the net assets of the Foundation are restricted for the support of The University. The cash held in a financial institution in the amount of \$8,971,124 is restricted specifically for the construction and design commitments noted above.

### **Note G - Subsequent Events**

Management has evaluated subsequent events through November 8, 2019, the date the financial statements were available to be issued.

**INDEPENDENT AUDITOR'S 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**

To the Board of Directors  
Auxiliary Services Foundation  
Memphis, Tennessee

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 Auxiliary Services Foundation (a nonprofit organization), which comprise the statement of financial position as of June 30, 2019, and the related statements of activities and cash flows for the period April 15 through June 30, 2019, and the related notes to the financial statements, and have issued our report thereon dated November 8, 2019.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered Auxiliary Services Foundation's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Auxiliary Services Foundation's internal control. Accordingly, we do not express an opinion on the effectiveness of Auxiliary Services Foundation'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.

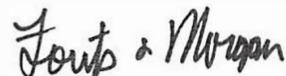
Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Auxiliary Services Foundation'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 determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **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 Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



FOUTS & MORGAN  
Certified Public Accountants

Memphis, Tennessee  
November 8, 2019

Board of Directors  
Auxiliary Services Foundation

Douglas A. Garner, CPA  
J. Donald Short, CPA  
Michael T. Odom, CPA, CVA  
Randal L. Gregory, CPA  
Gary D. Purdy, CPA, CA  
Jimmie D. Fouts, CPA (1941-2008)  
Don W. Morgan, CPA (1939-2005)

We have audited the financial statements of Auxiliary Services Foundation for the period April 15, through June 30, 2019, and we will issue our report thereon dated November 8, 2019. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated August 8, 2019. Professional standards also require that we communicate to you the following information related to our audit.

#### Significant Audit Matters

##### *Qualitative Aspects of Accounting Practices*

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by Auxiliary Services Foundation are described in Note A to the financial statements. Accounting policies prescribed by the Financial Accounting Standards Board (FASB) for nonprofit organizations were adopted in this first year of operations. We noted no transactions entered into by Auxiliary Services Foundation during the period for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The financial statements for the period did not include any significant estimates.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were the disclosures regarding the net assets with donor restrictions and the commitments for capital projects.

The financial statement disclosures are neutral, consistent, and clear.

##### *Difficulties Encountered in Performing the Audit*

We encountered no significant difficulties in dealing with management in performing and completing our audit. We were required to make several significant changes during the course of our engagement to comply with the presentation required by Tennessee Comptroller of the Treasury Local Government Audit Division (State Auditors).

##### *Corrected and Uncorrected Misstatements*

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. The attached schedule presents an uncorrected misstatement of the financial statements. Management has determined that its effect is immaterial to the financial statements taken as a whole. *Disagreements with Management*

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

##### *Management Representations*

We have requested certain representations from management that are included in the management representation letter dated November 8, 2019.

##### *Management Consultations with Other Independent Accountants*

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to Auxiliary Services Foundation's financial statements or a determination of the type of auditor's opinion that

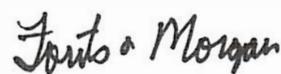
may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts.

It is our understanding that you have consulted with the State Auditors in connection with the audit of the University of Memphis and the presentation of Auxiliary Services Foundation as a component unit of The University. The State Auditors have determined that since Auxiliary Services Foundation is structured as a nonprofit organization, its financial statements should be presented under the FASB model for nonprofit organizations rather than under the Governmental Accounting Standards Board model for state and local governments. The State Auditors have also required an adjustment to the financial statements of the Foundation to remove the balances and activity arising from the transfer of the Herff Trust assets, pending the issuance of the Tennessee Attorney General's opinion on the allowability of the transfer.

#### *Other Audit Findings or Issues*

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management prior to retention as Auxiliary Services Foundation's auditors. In this case we also had several consultations with management after we were engaged as auditors and during the course of the engagement as a result of questions which arose from the State Auditors. These discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

This information is intended solely for the information and use of the Board of Directors and management of Auxiliary Services Foundation and is not intended to be, and should not be, used by anyone other than these specified parties.



FOUTS & MORGAN  
Certified Public Accountants

Memphis, Tennessee  
November 8, 2019

**9. External Audit Report: Herff Trust  
University of Memphis  
For Review  
Presented by Vicki Deaton**

# The University of Memphis Board of Trustees

Presentation

For Information

**Date:** December 4, 2019

**Committee:** Audit Committee

**Presentation Title:** External Audit Report – The Herff Trust Financial Statements, June 30, 2019

**Presented by:** Vicki D. Deaton, Chief Audit Executive

## Synopsis:

On November 15, 2019, the Herff Trust Financial Statements, June 30, 2019, were issued. The financial statements are presented per the responsibilities for Internal Audit under UoM Policy GE2016 Notification of External Audits and Reviews, which includes reporting occurrences of external reviews and audits to the Audit Committee, Division of State Audit and others as the circumstances may dictate.

In 1964, Herbert Herff and his wife donated the money to establish the Herff College of Engineering at the University of Memphis. In 1965, Herbert Herff and Gov. Frank Clement entered into an agreement for Mr. Herff to provide \$350,000 for the benefit of the University under the terms and provisions of the Last Will and Testament of Herbert Herff. When he died in 1966, Herbert Herff left the bulk of his estate in trust with the State of Tennessee for the benefit of the University. More than forty years later, the Trust continues to help sustain and expand University programs.

According to terms of the trust agreement, a Committee ("Trustees") would be established to "manage and control" the bequest. The funds of the trust were to be used for the benefit of the School of Law and School of Engineering at the University of Memphis (University), and such other uses as the committee may decide. The Trustees exercise financial oversight of Trust assets. An Investment Management Consultant advises the Trustees on investment selection and asset allocation. The business affairs of the Trust are managed by the University. The Trust has no employees. The Herbert Herff Trust was formed exclusively for the benefit of the University of Memphis. The Herff Trust is a component unit of the University of Memphis.

The Herff Trust engaged an independent external CPA firm, Fouts and Morgan, PC, to perform an audit of the financial statements of the Herff Trust. The independent auditor's opinion stated that the financial statements present fairly, in all material respects, the financial position of the Herff Trust as of June 30, 2019, and the changes in its financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

The auditors did not identify any deficiencies in internal control that would be considered material weaknesses during their limited consideration of internal control over financial reporting. Also, they did not identify any instances of noncompliance or other matters with certain provisions of laws, regulations, contracts and grant agreements.

**THE HERFF TRUST**  
**FINANCIAL STATEMENTS**  
**JUNE 30, 2019**

# THE HERFF TRUST

## CONTENTS JUNE 30, 2019

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Gary D. Purdy, CPA, CA

Jimmie D. Fouts, CPA (1941-2008)

Don W. Morgan, CPA (1939-2005)

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To the Board of Trustees  
The Herff Trust  
Memphis, Tennessee

## INDEPENDENT AUDITOR'S REPORT

We have audited the accompanying financial statements of The Herff Trust (a component unit of The University of Memphis) as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise The Herff Trust's basic financial statements as listed in the table of contents.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes 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.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Herff Trust as of June 30, 2019, and the changes in its financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

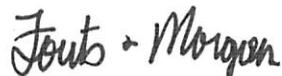
## **Other Matters**

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 and 4 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### **Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated November 15, 2019, on our consideration of The Herff Trust's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of The Herff Trust's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering The Herff Trust's internal control over financial reporting and compliance.

The logo consists of the company name "Fouts & Morgan" written in a cursive, handwritten-style font.

FOUTS & MORGAN  
Certified Public Accountants

Memphis, Tennessee  
November 15, 2019

**THE HERFF TRUST**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**JUNE 30, 2019**

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**Management Discussion and Analysis for the Herff Trust**

The following Management's Discussion and Analysis, or MD&A, provides an overview of the financial position and the results of operations of The Herff Trust (the "Trust") for the year ended June 30, 2019. We encourage you to read this MD&A section in conjunction with the accompanying audited financial statements and notes to the financial statements.

**About the Financial Statements**

As a component unit of The University of Memphis (the "University"), the Trust has implemented the governmental accounting standards for state and local governments and for public colleges and universities. Because the Foundation is not supported by governmental tax revenues, the Foundation presents its financial reports in a single column "business-type activity" format appropriate for college and university enterprise funds.

In addition to this MD&A section, the financial statements consist of a statement of net position, a statement of revenues, expenses, and changes in net position, a statement of cash flows, and notes to the financial statements.

The statement of net position is the Trust's balance sheet. It reflects the total assets, liabilities, and net position (similar to net equity) of the Trust as of June 30, 2019. Liabilities due within one year, and assets available to pay those liabilities, are classified as current. Other assets and liabilities are classified as non-current. Net position is to be used for University of Memphis support.

The statement of revenues, expenses, and changes in net position is similar to an income statement. It details how net position has increased during the year from July 1, 2018 to June 30, 2019.

The statement of cash flows details how cash has decreased during the year. It breaks out the sources and uses of Trust cash into operating and investing activities. Cash flows associated with the Trust's net assets result from investment income and related investment activities.

The notes to the financial statements provide additional details on the amounts reported in the financial statements.

**General**

In 1965 Herbert Herff and Gov. Frank Clement entered into an agreement for Mr Herff to provide \$350,000 for the benefit of the University under the terms and provisions of the Last Will and Testament of Herbert Herff. According to terms of the agreement a Committee ("Trustees") would be established to "manage and control" the bequest. The funds of the trust were to be used for benefit of the School of Law and School of Engineering at the University of Memphis, and such other uses as the committee may decide.

The Trustees exercise financial oversight of Trust assets. An Investment Management Consultant advises the Trustees on investment selection and asset allocation. The business affairs of the Trust are managed by the University. The Trust has no employees.

**THE HERFF TRUST**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS - Continued**  
**JUNE 30, 2019**

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**Statement of Net Position**

Current assets include cash and the current portion of a note receivable.

At June 30, 2019, funds held by an investment broker on behalf of the Trust totaled \$23,653,227. Of this amount, \$22,793,976 represents investments at fair value and \$859,251 represents deposits with banks affiliated with the broker.

A summary of the major components of the net position of the Foundation as of June 30, 2019 is as follows:

Current Assets	\$ 910,153
Other Assets	24,909,459
<b>Total Assets</b>	<b><u>\$ 25,819,612</u></b>
Liabilities	\$ -
Net Position Unrestricted	<u>\$ 25,819,612</u>

**Statement of Revenues, Expenses, and Changes in Net Assets**

A summary of the statement of revenue, expenses and changes in net position for the year July 1, 2018 to June 30, 2019 is as follows:

Net investment income	\$ 1,522,072
Student scholarships	(958,729)
<b>Change in net position</b>	<b><u>\$ 563,343</u></b>

**The Statement of Cash Flows**

In 2019, the cash receipts and expenses during the year primarily relate to investment activity - purchase, sale and investment income and expenses. Besides these, student scholarships paid to the University is the primary outflow.

**Future**

The Trust will continue to support the University to maintain and expand its programs, by prudently managing the investments of the Trust. All support will be in accordance with the original agreement with Mr Herff.

**THE HERFF TRUST**  
**STATEMENT OF NET POSITION**  
**JUNE 30, 2019**

---

**ASSETS**

**Current Assets**

Cash and cash equivalents	\$ 859,251
Note receivable - related party	50,902
Total current assets	<u>910,153</u>

**Other Assets**

Investments	\$ 24,453,694
Note receivable - related party	<u>455,765</u>
	<u>24,909,459</u>

**Total Assets**

**\$ 25,819,612**

**LIABILITIES AND NET POSITION**

**Liabilities**

**\$ -**

**Net Position**

Unrestricted	<u>25,819,612</u>
--------------	-------------------

**Total Liabilities and Net Position**

**\$ 25,819,612**

See accompanying notes to the financial statements.

# THE HERFF TRUST

## STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION FOR THE YEAR ENDED JUNE 30, 2019

---

**Revenue**

Investment income	\$ 1,654,087
Less: Investment expenses	(132,015)
Net investment income	<u>1,522,072</u>

**Expenses**

Student scholarships	<u>958,729</u>
----------------------	----------------

**Change in Net Position**

Net Position, Beginning of Year	<u>25,256,269</u>
Net Position, End of Year	<u>\$ 25,819,612</u>

See accompanying notes to the financial statements.

# THE HERFF TRUST

## STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2019

<b>Cash Flows From Operating Activities</b>		
Investment income received	\$	700,199
Investment fees		(132,015)
Cash paid for scholarships		<u>(958,729)</u>
Net cash used in operating activities		(390,545)
<b>Cash Flows From Investing Activities</b>		
Purchases of investments		(6,238,131)
Sales of investments		5,870,719
Investment maturities		364,000
Advances on note receivable - related party		<u>(500,000)</u>
Net cash used in investing activities		<u>(503,412)</u>
<b>Change in cash and cash equivalents</b>		(893,957)
<b>Cash and cash equivalents at beginning of year</b>		<u>1,753,208</u>
<b>Cash and cash equivalents at end of year</b>	\$	<u>859,251</u>
<b>Reconciliation of change in net position to net cash used in operating activities:</b>		
Change in net position	\$	563,343
Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities:		
Unrealized gain on investments		(960,555)
Increase in accrued interest included in note receivable		<u>6,667</u>
Net cash used in operating activities	\$	<u>(390,545)</u>

See accompanying notes to the financial statements.

# **THE HERFF TRUST**

## **NOTES TO THE FINANCIAL STATEMENTS JUNE 30, 2019**

---

### **Note A - Summary of Significant Accounting Policies**

#### **Organization and Activities**

The Herbert Herff Trust (the "Trust") was formed exclusively for the benefit of The University of Memphis. In 1964 Herbert Herff and his wife, Minnie G. Herff, donated the money to establish the Herff College of Engineering at the University of Memphis. When he died in 1966, Herbert Herff left the bulk of his estate in trust with the State of Tennessee for the benefit of the University. More than forty years later, the Trust continues to help sustain and expand University programs.

#### **Financial Reporting Entity**

In determining the financial reporting entity, the Trust complies with the provisions of the Governmental Accounting Standards Board (GASB) No. 14, *The Financial Reporting Entity*. Based on this standard, the Trust was determined to be a component unit of the University of Memphis ("The University"), as it was created solely for the purpose of providing benefits to The University.

#### **Basis of Presentation**

As a component unit of The University, the financial statements of the Trust have been prepared in accordance with accounting principles generally accepted in the United States of America for public colleges and universities, as prescribed by (GASB).

#### **Basis of Accounting**

For financial statement purposes, the Trust is considered a special-purpose government engaged only in business-type activities. Accordingly, the financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

#### **Cash and Cash Equivalents**

For purposes of the statements of cash flows, all highly liquid investments purchased with initial maturities of three months or less are considered to be cash equivalents.

#### **Investment Securities**

The Trust carries investments at fair value in the statement of net position. Investments are recorded on the trade-date basis. Realized and unrealized gains and losses as well as investment expenses are included in the net investment income in the statement of revenues, expenses and changes in net position.

## **NOTES CONTINUED**

### **Note A - Summary of Significant Accounting Policies - Continued**

#### **Fair Value Measurements**

Accounting standards define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date and establish the framework for a fair value hierarchy. The fair value hierarchy gives the highest priority to observable inputs such as quoted prices in active markets for identical assets or liabilities (Level 1); the next highest priority to inputs (other than quoted prices within Level 1) such as quoted prices for similar assets or liabilities, quoted prices in inactive markets, or other inputs that can be corroborated by observable market data (Level 2); and the lowest priority to unobservable inputs (Level 3). Inputs are broadly defined as assumptions market participants would use in pricing an asset or liability.

#### **Use of Estimates**

Management uses estimates and assumptions in preparing financial statements in accordance with U.S. GAAP. Such estimates and assumptions affect the reported amounts of assets and liabilities, and revenues and expenses. Accordingly, actual results could differ from estimates.

### **Note B - Deposits with Investment Broker**

Custodial credit risk is the risk that, in the event of institution failure, the Trust's deposits may not be returned. Balances held within cash accounts administered by its broker are covered by the Securities Investor Protection Corporation (SIPC) up to \$250,000 per account. None of these accounts exceeded the SIPC coverage as of June 30, 2019.

### **Note C - Investments**

One objective of the Trust's investment policy is to obtain a favorable absolute return with the preservation of purchasing power with some emphasis on long term growth. Another objective is to provide cash for distribution to The University in amounts approximating four to six percent of the portfolio's average market value.

The Board of Trustees shall have responsibility for establishing overall financial objectives, setting investment policy, setting parameters for asset allocation, and selecting an Investment Management Consultant. Domestic and international equities, both large and small capitalization, fixed income, cash equivalent securities and alternative investments in the form of diversified funds of funds, hedge funds, and limited partnership interests have been determined to be acceptable vehicles for investment.

Custodial credit risk is the risk that, in the event of the failure of the counterparty to a transaction, the Trust will not be able to recover the value of investment securities that are in the possession of an outside party. The Trust does not have a policy for custodial credit risk for its investments. The Trust utilizes an American multinational independent investment bank and financial services company for its custodial services and has no investment securities from a single issuer valued in excess of five percent of the total investment portfolio at June 30, 2019.

## NOTES CONTINUED

### Note C - Investments - Continued

Interest rate risk is the risk that changes in the interest rates may adversely affect the fair value of a debt instrument. The following table represents the relative maturity dates of the fixed income securities held by the Trust at June 30, 2019:

Maturity	Fair Value	Allocation Percentage
Less than one year	\$ 527,204	10.69%
One to three years	1,418,616	28.78%
Three to seven years	2,260,201	45.85%
Seven to fourteen years	623,082	12.64%
More than fourteen years	100,757	2.04%
Total	\$ 4,929,860	100.00%

Credit risk is the possibility of a loss resulting from an issuer's inability to repay debt or meet contractual interest obligations. Credit quality ratings of the Trust's investment in debt securities at June 30, 2019 based on Moody's, S&P, and Fitch rating agencies are as follows:

Security/Credit Rating	Fair Value	Allocation Percentage
U.S. Treasury	\$ 2,089,688	42.39%
Asset-backed securities	311,319	6.31%
AAA	87,065	1.77%
AA	267,607	5.43%
A	1,950,398	39.56%
BAA	223,783	4.54%
Total	\$ 4,929,860	100.00%

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. All of the investments in foreign securities are denominated in U.S. dollars.

## NOTES CONTINUED

### Note D - Fair Value Measurements

The following table presents the Trust's financial assets measured at fair value on a recurring basis at June 30, 2019:

	Fair Value	Level 1	Level 2	Level 3
Money market fund	\$ 600,000	\$ 600,000	\$ -	\$ -
Domestic equities	6,544,199	6,544,199	-	-
Foreign equities	4,424,427	4,424,427	-	-
U.S. Treasury notes	2,089,687	-	2,089,687	-
Corporate bonds	2,528,854	-	2,528,854	-
Asset-backed securities	311,319	-	311,319	-
Mutual funds	3,986,063	3,986,063	-	-
Real estate investment trusts	317,220	-	-	317,220
Alternative investments	1,992,208	-	-	1,992,208
Limited partnership	1,659,718	-	-	1,659,718
	<b>\$ 24,453,695</b>	<b>\$ 15,554,689</b>	<b>\$ 4,929,860</b>	<b>\$ 3,969,146</b>

*Money market mutual fund:* Valued at the daily closing prices as reported by the fund. The money market mutual fund held by the Trust is an open-ended mutual fund that is registered with the Securities and Exchange Commission (SEC). This fund is required to publish its daily NAV and to transact at that price. The money market mutual fund held by the Trust is deemed to be actively traded.

*Domestic and foreign equities:* Valued at the unadjusted quoted market price within active markets.

*U.S. Treasury notes, corporate bonds and asset-backed securities:* Valued at quotes from less active markets and/or quoted prices of securities with similar characteristics.

*Mutual funds:* Valued at the daily closing price reported on the active market on which securities are traded.

*Real estate investment trusts:* Values are obtained from independent valuation services or information made public by the issuer. Investments are not listed on a securities exchange, do not have readily liquid markets or ascertainable prices, and generally must be held to termination to maximize returns.

*Alternative investments:* Held directly with the issuer, and valuation is derived from information provided by an external source.

*Limited partnership:* Valued using the capital balance as a practical expedient to determine the fair value.

## **NOTES CONTINUED**

### **Note D - Fair Value Measurements - Continued**

The following is a reconciliation of the beginning and ending balances of assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended June 30, 2019:

	<b>Real Estate Investment Trusts</b>	<b>Alternative Investments</b>	<b>Limited Partnership</b>
Balance, June 30, 2018	\$ 382,554	\$ 1,870,860	\$ 1,714,082
Unrealized gain (loss)	(65,334)	121,348	80,523
Capital distributions	-	-	(134,887)
 Balance, June 30, 2019	 <u>\$ 317,220</u>	 <u>\$ 1,992,208</u>	 <u>\$ 1,659,718</u>

### **Note E - Related Party Transactions**

The Trust was involved in the following transactions with organizations affiliated with The University during the period ending June 30, 2019:

Scholarships disbursed for the benefit of University of Memphis students	\$ 958,729
Loan receivable from UMRF Ventures, Inc.	\$ 506,667

### **Note F - Net Position**

All of the Trust's net position is to be used for the benefit of The University. The Board of Trustees expects to expend approximately four to six percent of the investments' average market values over the previous three years in support of The University for student scholarships on an annual basis. Other University support is determined at the discretion of the Board of Trustees.

### **Note G - Subsequent Events**

Management has evaluated subsequent events through November 15, 2019, the date the financial statements were available to be issued.

**INDEPENDENT AUDITOR'S 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**

To the Board of Trustees  
The Herff Trust  
Memphis, Tennessee

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 Herff Trust (a component unit of The University of Memphis), which comprise the statement of net position as of June 30, 2019, and the related statements of revenues, expenses and changes in net position and cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise The Herff Trust's basic financial statements, and have issued our report thereon dated November 15, 2019.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the The Herff Trust's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of The Herff Trust's internal control. Accordingly, we do not express an opinion on the effectiveness of The Herff Trust'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.

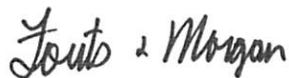
Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether The Herff Trust'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 determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **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 Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



FOUTS & MORGAN  
Certified Public Accountants

Memphis, Tennessee  
November 15, 2019

**THE HERFF TRUST**

**SCHEDULE OF FINDINGS AND RECOMMENDATIONS**

**JUNE 30, 2019**

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Our audit disclosed no findings that are required to be reported herein under *Government Auditing Standards*.



# **10. Information Security Update**

Presentation  
Presented by Robert Jackson

# The University of Memphis Board of Trustees

Recommendation

Presentation

**Date:** December 4, 2019

**Committee:** Audit Committee

**Topic:** Information Security Update

**Presented by:** Robert Jackson, Chief Information Officer

This is an update of the information security program for the University of Memphis.

# *Information Security Program Update*

## *Audit Committee*

Dr. Robert Jackson  
Chief Information Officer

December 4, 2019  
Wilder Student Union  
UofM Lambuth

December 2019 Audit Committee Meeting

10. Information Security Update



DECEMBER 2019 Page 110 of 129

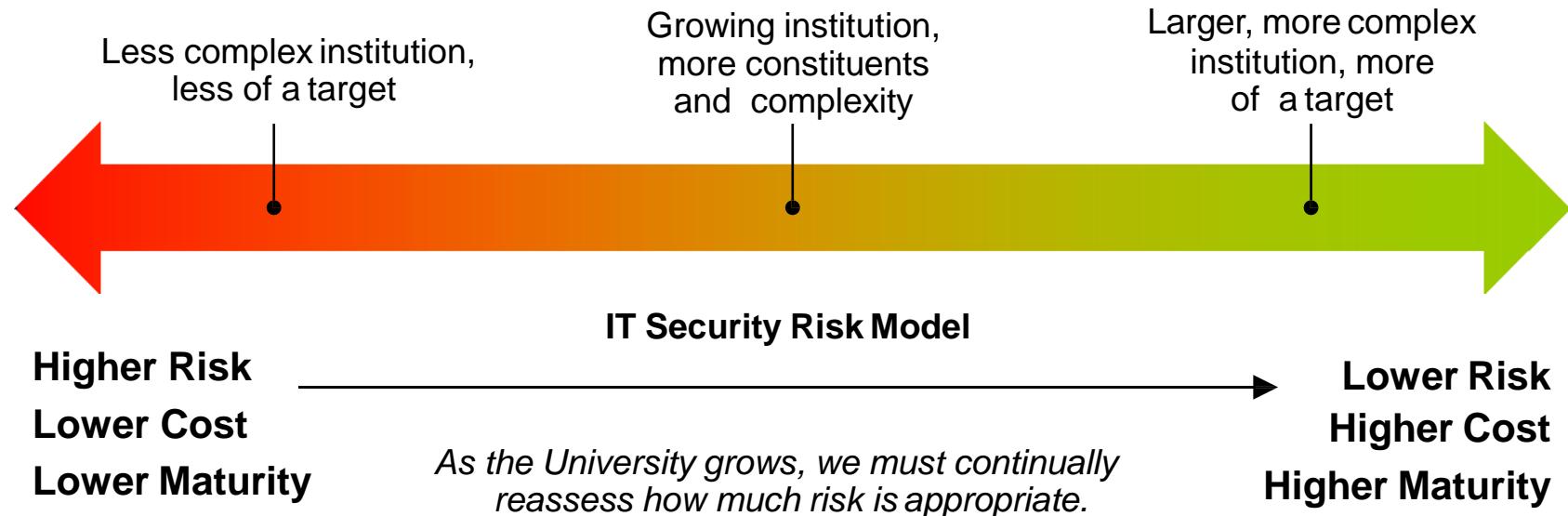
# Defining Appropriate IT Security Risk



THE UNIVERSITY OF  
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Board of  
Trustees

There is no such thing as "perfect protection"



*Our goal is to build a sustainable information security program that balances the need to protect against the need to conduct University business.*

- IT Security Awareness Training
  - New hires within 30 days of on-boarding
  - Existing employees Nov 2019 – Feb 2020
- Desktop security initiative complete (central administration)
  - Administrative privileges revoked by default
  - Encryption enabled
- ITS Technology pilot for blocking malicious web sites
  - URL filtering – the border firewall blocks access to known malicious sites by browsers, IoT devices, malicious software, etc.
  - URL re-writing – URL's embedded within emails are re-written so that when a user clicks the link, the site/content is reviewed for malicious content before the web page is displayed

# FY2020 Q1 IT Security Engagements



Board of  
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Category	Escalation Level						Total
	1 - Very Minor	2 - Minor	3 - Low	4 - Moderate	5 - High	6 - Very High	
Denial of Service							0
Malicious Code							0
Unauthorized Access			5				5
Inappropriate Usage	3						3
Personally Identifiable Information							0
Other							0
Total	3	5	0	0	0	0	8

## Outcomes included:

- No Action Required (3)
- Issue Remediated (5)

Note: Most unauthorized access items are the result of spam/phishing attempts. These numbers will increase as we improve user education and reporting processes. Piloting process that identified

70 potential phishing attacks during this period.

# A Layered System of Security Controls

## Foundation Controls

- Perimeter (network security):
  - Firewalls
  - Intrusion prevention
- Access controls:
  - User provisioning (role-based)
  - **Access management (two-factor)**
- Vulnerability management:
  - Scanning
  - Patching
- IT Policies
- Organization:
  - Staff (delineation of duties)
  - Skills (certifications)
- Compliance:
  - Audit
  - Requirements management
  - E-Discovery

## Good Controls

- Detection:
  - Log analysis (SIEM)
  - Email threat detection
  - End-point alerts
  - Data loss prevention
  - User reported
- Incident response plan
- Risk assessment:
  - Technology risks
  - Facility risks
  - Personnel risks
- Governance:
  - Governance committees
  - Change management
  - Strategic Planning
- End-point protection:
  - Data disposal guidelines
  - Encryption guidelines
  - **Privileged access controls**

## Advanced/Nice to Have

- Business alignment:
  - Student, HR, & Finance processes
  - Research standards
- Ethical hacking
- IT Security awareness:
  - Annual Required Training
  - Program Expansion
- Risk management:
  - Enterprise risk
  - Accountability
  - Scenario / table-top exercises
- Previous improvements
- Planned improvements

- Technology for blocking malicious web sites – Spring 2020
- Disabling outdated email protocols (POP/IMAP) – January 2020
  - Prepares UofM for protecting email via multi-factor authentication
- FY2020 Network Core / Firewall upgrade – Spring 2020
- Review new endpoint protection tools – Spring/Summer 2020
- Enhance processes for proactively identifying and reporting potential security issues
- Expansion of desktop security initiative to academic departments

Text



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# Thank you



# **11. ITS Network Upgrade**

Presentation

Presented by Robert Jackson

# The University of Memphis Board of Trustees

Recommendation

Presentation

**Date:** December 4, 2019

**Committee:** Audit Committee

**Topic:** ITS Network Upgrade

**Presented by:** Robert Jackson, Chief Information Officer

Presentation provides an overview of the 2020 Core Network Upgrade Project. The project seeks to improve the UofM network experience by 1) supporting business continuity through reliability and security, 2) enhancing the ability to support emerging technology needs and challenges, 3) building capacity for future growth and 4) replacing critical equipment that is approaching end-of-support.

# *2020 Core Network Upgrade Project*

*Governance and Finance Committee*

Dr. Robert Jackson  
Chief Information Officer

December 4, 2019  
Wilder Student Union

UofM Lambuth

December 2019 Audit Committee Meeting

11. ITS Network Upgrade



DECEMBER 2019 Page 119 of 129



The University network is upgraded as needed to ensure our students, faculty, staff, and guests receive the best experience.

This network upgrade will improve the UofM network experience by:

- Supporting business continuity through reliability and security
- Enhancing our ability to support emerging technology needs and challenges
- Building capacity for future growth

And,

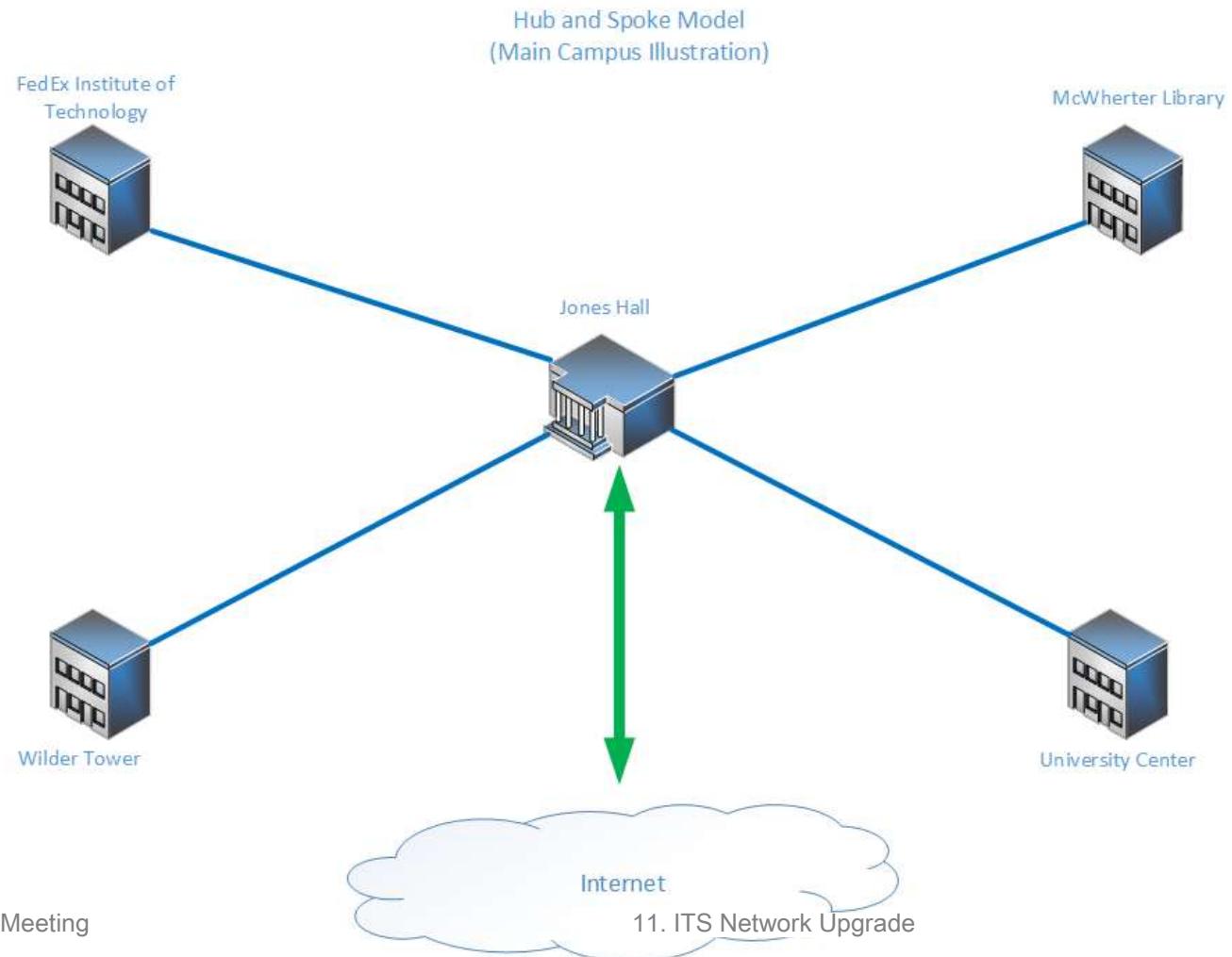
- Replacing critical equipment that is approaching end-of-support

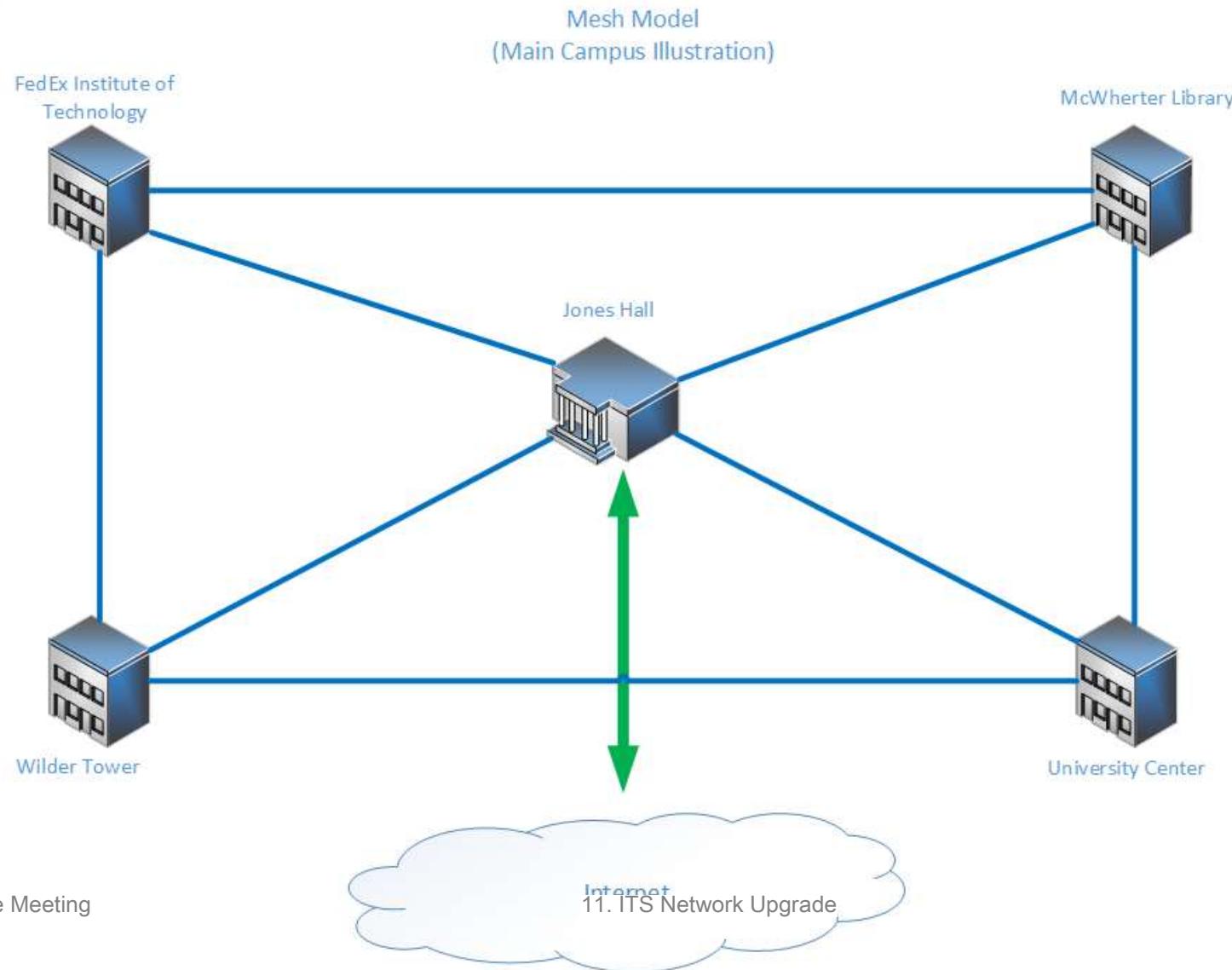
## Performance, Redundancy, Lower Cost

- Upgraded VPN security
- Enhanced scalability of the network that can support future Internet bandwidth demands (up to 100gbs)
- Decentralizes the network core to create a mesh network thereby minimizing dependency on a single building and improving campus network redundancy
- Creates infrastructure that supports secondary ingress/egress Internet connectivity thereby adding fault tolerance (e.g., fiber cuts)

And,

- **Improves network resiliency critical for leveraging modern cloud-based services at lower costs than traditional hub and spoke model, and provides network scalability to support future R1 growth.**





- Cisco - world-renowned in the network market and was named by Gartner as a leader in the 2018 Magic Quadrant for WAN Edge Infrastructure. UofM has a long-standing relationship with Cisco and continues to use their equipment for critical services.
- Palo Alto Networks - recognized by Gartner as the leader in the 2019 Magic Quadrant for Network Firewalls. UofM has benefited from Palo Alto's dependable platform and security offerings.

Description	Amount	Funding Source
<b>Year 1 equipment, subscriptions, and maintenance</b>	\$2,164,590.55	R&R budget
<b>Year 2 maintenance and subscriptions</b>	\$73,584.00	Operating budget
<b>Year 3 maintenance and subscriptions</b>	\$73,584.00	Operating budget
<b>Year 4 maintenance and subscriptions</b>	\$73,584.00	Operating budget
<b>Year 5 maintenance and subscriptions</b>	\$73,584.00	Operating budget
<b>Year 6 maintenance and subscriptions</b>	\$277,708.00	Operating budget
<b>Year 7 maintenance and subscriptions</b>	\$277,708.00	Operating budget
<b>Total project cost</b>	\$3,014,342.55	



- Spring 2019 – Identify potential improvements
- Summer 2019 – Finalize proposed network design and begin vendor reviews
- Fall 2019 – Identify best solution and begin procurement process
- Spring 2020 – Implementation



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Board of  
Trustees

# Thank you



## **12. Additional Business**



## 13. Adjournment