

MnSCU Office of Internal Auditing

Annual Report

Fiscal Year 2000

Submitted to the MnSCU Board of Trustees on October 18, 2000, as required by Board Policy 1.D. Part 8.

On July 1, 1995, the MnSCU Board of Trustees assumed governance responsibilities for a newly formed network of Minnesota public colleges and universities. The colleges and universities had come from three different systems, each with its own culture, systems, priorities, and business practices. As the board faced the challenge of overseeing this mega-merger of public higher educational institutions, it struggled to obtain the information it needed for decision making. Information systems were not reliable and external audits showed that college and university business practices were vulnerable to significant financial and operational problems.

In 1996, the board decided to explore establishing an internal auditing function to assist it with oversight and accountability. The board brought in an expert advisor and received testimony from public accounting firms and others with internal auditing expertise. It solicited information from other higher educational institutions on their experiences with internal auditing functions. In early calendar year 1997, the MnSCU Board of Trustees commissioned a national search for its first Executive Director of Internal Auditing.

On November 3, 1997, the MnSCU Board of Trustees hired Mr. John Asmussen as its first Executive Director of Internal Auditing. Mr. Asmussen had over twenty years of auditing experience with the State of Minnesota. The board directed Mr. Asmussen to establish a state-of-the-art internal auditing function that would serve as a decision-making resource to the board, the chancellor, and college and university presidents.

The end of fiscal year 2000 marked the fifth anniversary for the MnSCU system. Internal Auditing has existed for roughly half that time. Much has been accomplished. A solid financial and operational foundation is being formed for the system. Information systems have become more stable and are able to produce data that is more reliable and uniform across campuses. The organization is beginning to pursue new opportunities in training incumbent workers and developing electronic education sites. Many people throughout the system have made this progress possible. Internal Auditing has attempted to stay in tune with system-wide priorities and to contribute to these successes when possible.

Internal Auditing activities during fiscal year 2000 ranged from system-wide studies to coordinating work with external auditors to completing special request work for MnSCU presidents. Also, significant effort was made to develop a consulting practice to

complement the traditional assurance and investigative services offered by Internal Auditing.

System-wide Studies

In June 2000, Internal Auditing issued a major system-wide study entitled, “Incumbent Workforce Training Programs”. This report was the first topic where Internal Auditing had the opportunity to work closely with MnSCU Academic Affairs on a system-wide study. It proved to be a very effective working relationship. Major findings and conclusions contained in the report included:

- The report recognized that MnSCU colleges and universities, particularly the two-year colleges, have developed the capacity to deliver timely, relevant training opportunities to Minnesota’s incumbent workforce. Yet, it pointed out that MnSCU has a unique opportunity to leverage its cumulative resources to address the training needs of Minnesota employers. The report urged MnSCU to seek creative ways to maintain institutional autonomy, while blending college and universities into a unified entity that can compete effectively in the corporate environment.
- The report found that financial matters pertaining to incumbent workforce training programs needed much attention. The methods for distributing and achieving accountability for system-level funding needed improvement. Market pricing practices required extensive study. Also, financial reporting measures were needed to generate meaningful, consistent financial information on the programs.
- The report recommended that system-wide opportunities to improve program operations be explored. It identified areas where operational efficiencies were possible. Furthermore, it identified best practices that would allow colleges and universities to improve their own operations.

Internal auditing also completed most fieldwork on a system-wide study of network security. This study is examining practices for securing access and use of information technology resources at each of the 35 MnSCU colleges and universities. A final report is expected to be released in late calendar year 2000.

Finally, in June 2000, the Audit Committee approved a major study of the Post-secondary Enrollment Options program. This program allows high school juniors and seniors to earn college credits. Once again, Internal Auditing will receive expert assistance from Academic Affairs in conducting this study.

Progress on Prior System-wide Studies

In its first year and a half of existence, Internal Auditing had issued three other system-wide studies on topics that had significant implications. Internal Auditing continued to report on progress that MnSCU made toward resolving issues identified in those studies.

- **Y2K** (the Year 2000 computing problem) posed an ominous threat to most organizations as the calendar marched toward the end of the 1900's. Internal Auditing had issued its first system-wide study on this topic in June 1998. It revealed that MnSCU was ill prepared for some of the potential problems associated with the Y2K challenge. The Audit Committee requested Internal Auditing to provide it with monthly progress reports to show how the System Office and MnSCU colleges and universities were protecting the organization against potential problems. Although progress was slow at first, momentum grew throughout calendar year 1999 and sufficient steps were taken to provide the organization with reasonable assurance that it would avoid any major consequences. The hard work paid off and the organization made a smooth transition into the new millennium.
- **The Student Information System (ISRS)** was the topic of a major internal auditing study issued in January 1999. The study revealed significant problems with the MnSCU system development methodology, resulting in major risks for the new student system. The Audit Committee requested periodic reports from Internal Auditing as the new student system was implemented throughout calendar year 1999. The system implementation proved to be rocky at times, but ultimately all MnSCU colleges and universities converted to the new system for the Fall 1999 semester. Also, during fiscal year 2000, the Board of Trustees approved a new information technology (IT) strategic plan and governance structure. While some IT matters remain to be resolved, the environment has experienced significant stability in the past year. Internal Auditing will continue to monitor areas that still need improvement, such as system security, project management, and implementation of the governance structure.
- **Reliability of MnSCU Financial Data** was addressed in an internal auditing study issued in May 1999. The study found that while the organization had successfully consolidated financial systems, the current systems were complicated and not well understood by users. As a result, the reliability of financial data was questionable. The problem with financial data reliability was embodied in the realization that almost two-thirds of MnSCU colleges and universities were unable to reconcile their cash balances to their bank statements. The Audit Committee asked for periodic reports on the status of bank reconciliations. The board's plan to obtain audited financial statements would not be possible unless colleges and universities could reconcile to their bank statements. Monthly reports from Internal Auditing showed steady progress toward completing satisfactory bank reconciliations. The problem with bank reconciliations has now essentially been resolved and is not expected to be a barrier to the board's financial reporting plan.

Coordination with External Audits

Since shortly after its inception, MnSCU has had a contract with the Office of the Legislative Auditor (OLA) to obtain periodic financial audits of each college and university. This contract results in about one-third of the colleges and universities being audited each year. By the end of fiscal year 1999, the OLA had audited all 36 colleges and universities. The audits showed numerous and significant problems with financial management and business practices. Since the merger, over 700 audit findings have been issued on MnSCU institutions. Internal Auditing created a system and a policy to monitor external audit findings. It produces quarterly follow-up reports to the Audit Committee to show progress toward implementing corrective action. Generally, colleges and universities have been responsive and implemented timely corrective actions. Some issues have proven more difficult to resolve and have required changes to MnSCU financial policies.

During fiscal year 2000, the OLA completed its second financial audit of 13 MnSCU colleges and universities. Most of those colleges and universities had received their first audit in fiscal year 1996, the first year after the merger. Comparing the results of those first audits to the most recent audit results demonstrates the progress that has been made in financial management and business practices. The first round of audits produced 159 audit findings. The second round produced 117 findings (a decline of 26%). Perhaps more importantly, the number of critical findings (those presenting an immediate risk to an institution) dropped from 74 to 26 (a decline of 65%).

An analysis that compares critical audit findings cited in the first round of OLA audits with critical findings cited in the second round produces further insights into how the organization has progressed in the past three years. Table 1 compares these critical findings by areas cited. There are some noteworthy trends shown in the table.

- Separation of duties issues were a very serious problem in the first round of audits and have virtually disappeared in the second round. Improvements in this area may be attributed to a greater understanding of the importance of assigning financial duties properly.
- Serious problems with revenue and cash controls and reconciliations have also diminished greatly. Many of these problems have been resolved due to the implementation and increased understanding of new financial systems.
- The only category that showed a significant increase in number of findings is system security. In essence, the challenge of separating the physical duties of employees has now moved inside the computer. Increased computerization has accentuated the need for colleges and universities to exercise great care in assigning security clearances to employees. This is clearly an area that needs additional education and awareness in order to improve.

**Table 1: Comparison of OLA Critical Audit Findings
1996 (1) Audits Compared to 1999 Audits**

Finding Area	No. 1996 Findings	No. 1999 Findings
Separation of Duties	20	2
Revenue & Cash Controls	14	3
Reconciliations	13	4
Financial Management	8	2
System Security	5	9
Payroll	4	1
Purchasing	2	2
Inventory	2	2
Other Areas	6	1
Totals	74	26

(1) 1996 Audits contains 1 audit of FY 1998.

The only other external auditor, besides the Legislative Auditor, used by MnSCU is the CPA firm that audits the Revenue Fund. In fiscal year 2000, the firm completed its second audit (on a three year contract) of the Revenue Fund financial statements. The audit resulted in an unqualified (clean) audit opinion and revealed no major concerns with internal controls or legal compliance.

Consulting Services

Since being created, the Office of Internal Auditing has aspired to create a consulting practice to complement its work on assurance services. The internal auditing profession is redefining itself to add consulting services as a standard component of the internal audit function. In June 1999, Internal Auditing hired Ms. Julie Smendzuik-O'Brien to develop its consulting practice. During fiscal year 2000, Internal Auditing consulting services were sought and used by the Board of Trustees, System Office, and several colleges and universities. Examples of consulting engagements include the administration of employee surveys, facilitation of business process improvement efforts, implementation of the quality improvement efforts, and team building exercises. Internal Auditing has also assisted the Board of Trustees with its improvement efforts.

Policy Development

While policy development is not a primary responsibility of Internal Auditing, audit reports often identify matters that must be addressed through the enactment or amendment of board policies. During fiscal year 2000, Internal Auditing assisted with the following board policies and actions.

- **The Board Plan on Audited Financial Statements** was approved in June 1999. The committee also took the lead in establishing a plan for obtaining audited financial statements. In July 1999, the Board of Trustees accepted a plan to obtain a system-wide audited balance sheet for fiscal year 2000 and complete system-wide financial statements for fiscal year 2001. For fiscal year 2002, the plan calls for audited financial statements for each MnSCU college and university.
- **MnSCU Financial Policies** underwent a substantial rewrite and were approved by the Board of Trustees in June 2000. MnSCU Finance took the lead on this rewrite. Internal Auditing assisted, particularly with matters that had been the subject of prior audit reports.
- A new **Internal Auditing Policy** was developed to replace the previous audit charter and to incorporate language that was more representative of recent changes in internal auditing standards and practices developed by the Office of Internal Auditing. The Board of Trustees approved the new policy in July 2000.
- A **Policy Against Fraudulent and Other Dishonest Behavior** is being developed jointly by Internal Auditing, MnSCU General Counsel, and MnSCU Human Resources. It received a first reading in September 2000 and is expected to be approved by the end of the calendar year.

Special Requests

By board policy, Internal Auditing is a service that the Board of Trustees shares with the Chancellor and presidents. The Chancellor and several presidents have taken advantage of internal auditing services and requested assistance with several projects. Internal Auditing has assisted with conducting fraud inquiries and investigations on a few occasions. It has also provided special assurance services upon request. The results of special requests are usually communicated only to the president or chancellor, depending upon the nature of the request. Significant violations of board policy or law, however, must be communicated to the Audit Committee, if discovered while conducting a special request.

Educational Efforts

Internal Auditing also makes itself available to offer professional advice on topics within its expertise. During fiscal year 2000, it fielded a variety of questions dealing with topics such as compliance with finance-related policies or laws, best practices, and assignment of financial duties. Internal Auditing representatives also sit on various MnSCU task forces and committees.

Analysis of Staff Hours

Internal Auditing has a staff complement of ten professional auditors and consultants and one administrative assistant. The majority of its professional staff, regional audit coordinators, are located on college or university campuses throughout the system. The audit coordinators serve 5-7 colleges or universities located in their region.

Fiscal year 2000 was the third year of existence for the MnSCU Office of Internal Auditing. The Internal Auditing budget has remained unchanged since its inception, but fiscal year 2000 was the first time that Internal Auditing was fully staffed. Table 2 shows the distribution of staff hours by year since the office was created 2 ½ years ago.

Table 2: Internal Auditing Staff Hours – FY 1998 to 2000

Fiscal Year	Staff Hours			
	Technical	Planning	Admin	Total
1998	2,403	631	1,038	4,072
1999	9,365	2,451	3,012	14,828
2000	11,734	1,454	3,606	16,794

Each year the Board of Trustees approves an audit plan for the ensuing fiscal year. In June 1999, the board approved a plan that estimated 16,000 hours of staff time. Table 3 shows how actual staff hours applied compares to the audit plan.

**Table 3: Internal Auditing Staff Hours
July 1, 1999 to June 30, 2000**

Activity	Staff Hours		
	Audit Plan	Actual	% of Actual
Technical Products & Services			
Topics Selected by Audit Committee	5,600	5,905	35%
Quality Management Self-Assessments	2,800	1,249	7%
Consultative & Advisory Services	1,800	1,771	11%
Follow-up on Prior Findings	2,400	2,809	17%
Subtotal – Technical	12,600	11,734	70%
Planning & Development Activities	1,600	1,454	9%
Administrative Activities	1,800	3,606	21%
Hours – 7/1/99 to 6/30/2000	16,000	16,794	100%

Total staff hours generated in fiscal year 2000 were about 5% higher than anticipated. Minimal staff turnover accounted for the greater number of hours. Most categories of services were close to the audit plan estimates, with the exception of the quality management self-assessment projects. Development of these projects was slowed due to the late hiring of the Organizational Improvement Coordinator. More time in administrative activities resulted from the need to continue developing internal office policies and processes, the steep learning curve associated with learning new systems and preparing for new study topics, and the investment of time in developing a consulting practice.

The Future

In June 2000, the Board of Trustees approved the Audit Plan for Fiscal Year 2001. It and continual updates on Internal Auditing projects are available at the office website, www.internalauditing.mnscu.edu.