

**MINNESOTA STATE COLLEGES AND UNIVERSITIES  
BOARD OF TRUSTEES**

**Agenda Item Summary Sheet**

**Committee:** Audit Committee

**Date of Meeting:** January 21, 2009

**Agenda Item:** Review External Audit Plan and Select Colleges Subject to Annual Financial Statement Audits

- Proposed Policy Change       Approvals Required by Policy       Other Approvals       Monitoring
- Information

**Cite policy requirement, or explain why item is on the Board agenda:**

According to Board Policy 1A2, Part 5, Subpart E, the Audit Committee oversees the work of external auditors. The audit contracts for six individual college and university audits have expired, so the committee needs to reconsider whether to continue with the existing strategic plan for external auditing services or make adjustments.

**Scheduled Presenter(s):**

John Asmussen, Executive Director, Office of Internal Auditing  
Laura King, Vice Chancellor - CFO

**Outline of Key Points/Policy Issues:**

- The contract with the principal auditor, Kern DeWenter Viere, requires that MnSCU contract for individual financial statement audits of colleges and universities so that at least 60% of the system-wide financial activity is covered by individual college and university audits.
- Board Policy 1A.2, Part 5, Subpart E. states that “An independent audit firm may not be appointed to a particular engagement for more than six consecutive years.” All six institutions have had the same auditing firm for six consecutive years, consequently these firms will not be eligible to bid on the same institutions again for this contracting cycle.

**Background Information:**

- The strategic external auditing plan was approved by the Audit Committee in January 2005.
- MnSCU has contracted with the Legislative Auditor for supplemental audit coverage for over ten years.

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MINNESOTA STATE COLLEGES AND UNIVERSITIES**

<b>BOARD INFORMATION</b>
REVIEW EXTERNAL AUDIT PLAN AND SELECT COLLEGES SUBJECT TO ANNUAL FINANCIAL STATEMENT AUDITS

In January 2005, the Board of Trustees approved the Strategic Plan for External Audit Services (a copy of the plan is available at <http://www.internalauditing.mnscu.edu/committee/2005/january/plan-to-contract-cpa-firms-2005.pdf>). The plan provided for a combination of contracting with CPA firms to conduct annual financial statements of the larger colleges and universities and contracting with the Legislative Auditor to audit the smaller colleges on a three-year cycle.

The plan provided that the annual audit of the system-level financial statements would be augmented with the stand-alone audits of twelve colleges and universities. This group of stand-alone audits was intended to account for approximately 60% of system-wide financial activity and, thus, improve the cost-effectiveness of the system-level audit.

For the past three years, the twelve colleges and universities shown in Table 1 have received stand-alone audits of their financial statements. It shows that contracts that expired in FY 2008 are needed in order to account for about 60% of system financial activity.

**Table 1: Stand-alone College or University Financial Statement Audits  
As of Fiscal Year 2008**

Contract Cycle / Audited Entity	% System Assets	% System Operating Expenses
<b><u>Contracts that Expired in FY 2008</u></b>		
Century College	2.87%	3.72%
Hennepin Technical College	1.40%	2.70%
Metropolitan State University	3.08%	3.28%
Minneapolis Community & Technical College	4.91%	3.69%
Rochester Community & Technical College	3.62%	2.83%
Southwest Minnesota State University	4.05%	2.69%
<b><u>Contracts Expiring in FY 2010</u></b>		
Bemidji State University	4.02%	4.35%
Minnesota State Community & Technical College	1.91%	2.91%
MSU, Mankato	11.41%	10.29%
MSU Moorhead	5.92%	5.36%
St. Cloud State University	10.19%	10.86%
Winona State University	10.02%	6.93%
<b>Total Audit Coverage – Standalone Audits</b>	<b>63.41%</b>	<b>59.61%</b>

Note: Percentages are based on fiscal year 2008 audited financial statements.

Some trustees have asked whether it would be prudent to add to or change the colleges and universities subject to stand-alone financial statement audits. Table 2 shows the other colleges that comprise more than 2% of either system assets or system operating expenses.

**Table 2: Next Largest Colleges Not Subject to Financial Statement Audits  
As of Fiscal Year 2008**

<b>College</b>	<b>% System Assets</b>	<b>% System Operating Expenses</b>
Northeast Higher Education District	3.00%	3.70%
Normandale Community College	2.70%	3.34%
Anoka Ramsey Community College	2.55%	2.59%
North Hennepin Community College	2.37%	2.32%
St. Cloud Technical College	2.27%	1.89%
St. Paul College	2.01%	2.38%
Lake Superior College	1.89%	2.13%
Ridgewater College	1.62%	2.28%
Northland Community & Technical College	1.52%	2.04%

Note: Percentages are based on MnSCU Supplement to the Annual Financial Report - Fiscal year 2008.

There are clear benefits to having more colleges subject to annual audits. The rigor of an annual financial statement audit results in a deeper understanding of a college's finances and provides important assurances to the president, Chancellor, Board of Trustees and other important college stakeholders. At the same time, there are some significant costs associated with adding new colleges to the financial statement audit schedule. The learning curve is steep and would require extra resources. The average cost estimate for a stand alone audit in 2005 (see January 2005 report cited earlier) was about \$51,000. That cost estimate would be significantly higher under current conditions because of the extra work required by the series of Auditing Standards (#104-111) that become effective in fiscal year 2008. These new auditing standards require additional effort for documenting internal controls as part of a financial statement audit.

Weighing the costs and benefits of expanding these stand-alone financial statement audits, the Vice Chancellor for Finance and the Executive Director of Internal Auditing recommend that colleges and universities listed in Table 1 continue to have annual audits and that the process be started for the possible additional of one more college, Normandale Community College, to the annual audit cycle. It is recommended that Normandale Community College be considered for a full financial statement audit beginning in fiscal year 2010. The college should spend fiscal year 2009 documenting major internal control structures and have staff members complete the training needed to prepare financial statements. Proposals for adding Normandale Community College to the annual audit schedule in fiscal year 2010 could be solicited as part of the upcoming Request for Proposals. Accordingly, the Audit Committee would create the option of adding it to the schedule, yet withhold a final decision until next year.

Several factors support adding Normandale Community College to the annual audit schedule:

- It is the largest college currently excluded from the annual audit schedule. In terms of operating expenses, it is larger than four of the colleges and one university presently subject to annual audits.
- The college has financial staff capable of producing financial statements. When the external audit plan was approved in January 2005, the Normandale business office was not ready for such an effort.
- Normandale Community College is a better candidate than the Northeast Higher Education District. The district is comprised of five colleges which have distinct internal control structures, thus, making it a much more difficult and costly institution to audit.
- The addition of one more college provides additional opportunity so that at least 60% of system assets and operating expenses will be audited as part of the annual schedule.

With the current budget uncertainties, though, the Audit Committee can wait to make a final decision on adding the college to the audit schedule until 2010.

Legislative Auditor contract

The strategic plan for external auditing services also provided for contracting with the Legislative Auditor to obtain additional internal control assurances. MnSCU has contracted with the Legislative Auditor for audit services since 1996. To complement the audit coverage achieved with the CPA firms, the focus of the Legislative Audit coverage has been on the colleges not subject to annual financial statement audits. As a result, these colleges and the Office of the Chancellor have been on a three-year schedule for audits conducted by the Legislative Auditor. Table 3 shows the eight colleges that the Legislative Auditor tentatively plans to audit in fiscal year 2009.

**Table 3: Tentative Legislative Audits Scheduled For Fiscal Year 2009**

<b>College</b>	<b>% System Assets</b>	<b>% System Operating Expenses</b>
Saint Paul College	2.01%	2.38%
North Hennepin Community College	2.37%	2.32%
Lake Superior College	1.89%	2.13%
Northland Community & Technical College	1.52%	2.04%
South Central College	0.74%	1.86%
Dakota County Technical College	1.43%	1.73%
Alexandria Technical College	1.13%	1.55%
Anoka Technical College	1.09%	1.09%

Note: Percentages are based on MnSCU Supplement to the Annual Financial Report - Fiscal year 2008

Because of budget difficulties, the Legislative Auditor is having difficulty with maintaining its three-year audit cycle for MnSCU colleges. In order to preserve this schedule for fiscal year 2009, the Office of Internal Auditing will enter into a service level agreement to assist the Legislative Auditor with conducting fieldwork on these eight colleges. Further discussions are needed to identify longer term solutions for maintaining the audit cycle for these colleges.

Finally, the Legislative Auditor still does not have the staffing resources to reinstate periodic information technology (IT) audits. As recently as fiscal year 2007, the Legislative Auditor conducted periodic IT audits that affected MnSCU (the state payroll system). It issued the most recent audit of a MnSCU IT area in September 2005 (wireless technology). Due to a staffing shortage within its IT audit unit, the Legislative Auditor had to discontinue these audits in 2007. As a result, MnSCU expanded the scope of its contract with the principal auditor to include additional coverage of information technology systems in fiscal year 2007. This level of IT audit coverage, though, is very minimal for an organization as large and complex as MnSCU. Therefore, further consideration is needed about the appropriate level of IT audit coverage. Internal Auditing will continue to monitor this issue and work with the Vice Chancellor for Information Technology to ensure adequate IT audit services are maintained.

#### **RECOMMENDED COMMITTEE ACTION:**

*The Audit Committee has reviewed the external audit plan and selected the colleges and universities subject to annual financial statement audits for Fiscal Years 2009-2011 and financial audits conducted by the Legislative Auditor during fiscal year 2009. The committee recommends that the Board of Trustees adopt the following motion:*

#### **RECOMMENDED MOTION:**

*Based on the review and recommendation of the Audit Committee, the Board of Trustees approves the Executive Director of Internal Auditing and Vice Chancellor for Finance issuing a Request for Proposals to solicit bids from certified public accounting firms interesting in conducting annual financial statement audits of the following colleges and universities:*

- *For fiscal years 2009 to 2011: Century College, Hennepin Technical College, Metropolitan State University, Minneapolis Community & Technical College, Rochester Community & Technical College, and Southwest Minnesota State University.*
- *Contract option for fiscal years 2010 and 2011: Normandale Community College.*

*Furthermore, based on the review and recommendation of the Audit Committee, the Board of Trustees approves the Executive Director of Internal Auditing and Vice Chancellor for Finance making arrangements with the Legislative Auditor to conduct periodic financial audits of colleges not subject to annual financial statement audits.*

*Date Presented to the Board of Trustees: January 21, 2009*