

MnSCU Office of Internal Auditing Annual Report Fiscal Year 2006

Submitted to the MnSCU Board of Trustees on March 21, 2007, as required by Board Policy 1.D. Part 8.

During fiscal year 2006, the Office of Internal Auditing continued to help the Minnesota State Colleges and Universities build a strong foundation for integrity and reliable information.

Assurance Services Requested by Board of Trustees

The Office of Internal Auditing spent the majority of its time working on assurance services which focus on improving the quality and reliability of information. The following assurance services were conducted at the request of the Board of Trustees.

Audited Financial Statements

Fiscal year 2006 marked the sixth year that the Minnesota State Colleges and Universities contracted for an external audit of its financial statements. The external audit firm of Kern, DeWenter, Viere & Company provided an unqualified (clean) opinion on the system-wide financial statements. The Financial Reporting Unit of the Office of the Chancellor and the Office of Internal Auditing both worked very hard to deliver the audited financial statements.

In addition, audited financial statements were developed for twelve of the largest institutions: the seven state universities and five two-year colleges. The financial statements for all twelve institutions received unqualified audit opinions from the CPA firms that the board appointed for the audits. These audits follow direction and scope for audited institutional financial statements set forth in the strategic external auditing plan adopted by the Board of Trustees in January 2005.

Internal Control & Fiscal Compliance Issues

The annual financial statement audit program ensures that the most significant internal control cycles are reviewed for universities and five of the largest colleges each year. In addition, the principal auditor for the system-wide financial statements reviews internal controls at about one-third of the remaining colleges each year.

Since 1996, MnSCU has had a contract with the Office of the Legislative Auditor (OLA) to obtain periodic finance-related audits of each college and university. In fiscal year 2004, the OLA audit coverage was adapted to complement the institutional financial

statement audits conducted by CPA firms. Basically, the colleges not subject to an annual financial statement audit are to be audited by the OLA on a three year rotating schedule. In fiscal year 2006, the OLA audits covered eight colleges. The Legislative Auditor released a special report on Lake Superior College in June 2006 and a combined report on the other seven colleges in October 2006. The situation at Lake Superior College was quite unique and involved misconduct by a former Vice President for Finance and Administration. As a result, the college was cited for several significant financial control weaknesses. The other seven colleges were cited for relatively few audit findings.

The Office of Internal Auditing monitors unresolved audit findings and works with colleges and universities responsible for corrective actions. Any findings that remain unresolved at the end of the fiscal year are reported to the Chancellor as part of the presidential performance evaluation process.

Fraud Awareness Report

At the request of the Audit Committee, Internal Auditing conducted a system-wide study to assess employee awareness of responsibility for reporting evidence of fraudulent or other dishonest acts. The report, issued in June 2006, found extensive variability both in efforts to build awareness and in reporting practices. A task force of the Leadership Council has nearly completed work on a system-wide employee code of conduct that will ensure greater consistency across the system in employee awareness about these matters.

Requested Assurance & Consulting Services

The Board of Trustees, as demonstrated in policy 1.D., intends to share internal auditing services with the Office of the Chancellor and college and university presidents. Accordingly, Internal Auditing has made its services available to the chancellor or a college or university president upon request.

Although some requested services are for traditional assurance audits, many requests are for consulting services. Internal Auditing will accept consulting engagements as long as no conflict is created with its auditing role. The office supplements its traditional audit skills with the services of an organizational improvement professional for consulting projects.

During fiscal year 2006, Internal Auditing conducted several consulting or assurance services which had been requested.

- At the request of the Vice Chancellor - CFO, Internal Auditing completed on a major system-wide study of capital construction administration. The final report was presented to the audit committee in June 2006.

- At the request of the Vice Chancellor for Human Resources, Internal Auditing completed an audit of State University faculty supplemental compensation. The final report was presented to the Vice Chancellor in August 2006.
- Internal Auditing worked with colleges and universities to address issues related to potential non-compliance with federal student financial aid programs. Some issues arose as the result of program reviews conducted by the U.S. Department of Education; other issues were identified as part of the annual external audit of federal financial assistance programs.
- Internal Auditing also provided consulting services at the institutional level, including projects focused on business practice improvement and administration of employee climate surveys.
- Other kinds of recurring services provided by Internal Auditing include projects that:
 - Tested spending by the Chancellor and Board of Trustees.
 - Coordinated completion of four presidential transition reviews at colleges and universities hiring new presidents.
 - Assisted the Board of Trustees with compilation of the performance evaluation of the Chancellor.

Fraud Inquiry and Investigation Support

Internal Auditing assists with conducting fraud inquiries and investigations. When evidence of fraud is identified it must be dealt with appropriately. The results of most fraud inquiries and investigations were reported to affected presidents or the chancellor for action. Board policy requires that only significant violations of board policy or law, be communicated to the Board of Trustees. The Executive Director of Internal Auditing advised the Chair of the Audit Committee about fraud investigations and informed other trustees about incidents as warranted.

Also, during fiscal year 2006, Internal Auditing continued to assist institutions with implementing Board Policy 1.C.2 on Fraud and Other Dishonest Acts. Presidents have identified key contacts on campus for the implementation of the board's policy. Internal Auditing has worked with these contacts to process evidence of potential fraud or dishonest acts and to improve awareness of the policy at the institutions.

Internal Auditing received reports on 78 incidents of potential fraud or dishonest acts during fiscal year 2006. The vast majority of these incidents related to theft of public property. These matters were reported to local law enforcement officials for

investigation. Internal Auditing assisted with investigations of only a few remaining incidents, primarily centering on allegations of employee misconduct or misuse of property.

Professional Advice

Internal Auditing also makes itself available to offer professional advice on topics within its expertise. During fiscal year 2006, Internal Auditing fielded 178 questions dealing with various topics. Common questions pertained to compliance with board policies and best practices. Internal Auditing representatives also sit on various MnSCU task forces and committees, including: Business Practice Alignment Committee, Security Steering Committee, Finance User Group, Staff and Leadership Development Committee and Financial Aid Directors.

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 regions.

The office has had the same size and structure since shortly after it was created in 1997. Its centralized structure and auditing approach allows the office to retain a modest complement of audit staff. Table 1 compares the MnSCU Office of Internal Auditing to 21 other internal audit offices in large, public higher education systems.

Table 1: Internal Auditing Staff Size Compared to Other Higher Education Systems

Metric	MnSCU Office of Internal Auditing	Median Comparative	
		Measure	System
Number of Auditors	10	16	Mississippi State Institutions of Higher Learning
System Expenses per Auditor	\$125 million	\$146 million	University of Minnesota
System Assets per Auditor	\$182 million	\$193 million	Nevada System of Higher Education
System Employees per Auditor	1,600	1,071	University of California
Students per Auditor	17,800	5,952	The University System of Georgia

Source: 2006 Survey Conducted by the Association of College and University Auditors.

Each year the Board of Trustees approves an audit plan for the ensuing fiscal year. In June 2005, the board approved a plan that estimated use of staff time. Table 2 shows how actual use of staff time compares to the audit plan for technical services.

**Table 2: Percentage of Internal Auditing Technical Service Staff Hours
July 1, 2005 to June 30, 2006**

Activity	Percentage of Staff Hours	
	Audit Plan	Actual
Technical Services		
Assurance Services	64%	74%
Inquiry/Investigations Support	8%	7%
Consulting Services	12%	10%
Professional Advice	11%	6%
Planning & Development	5%	3%
Percentage of Total Applied Hours	100%	100%

Finally, it should be noted that Internal Auditing has committed the equivalent of two full-time positions to supporting the work of external auditors (shown as assurance services). This level of support provides two benefits: cost savings to make the external audit contracts affordable and strengthened external audit coverage by use of Internal Auditing's knowledge of the Minnesota State Colleges and Universities system and its business systems.

The Future

In June 2006, the Board of Trustees approved the Audit Plan for Fiscal Year 2007. That plan and other information on Internal Auditing's projects are available at the Office website, www.internalauditing.mnscu.edu.