

**MINNESOTA STATE COLLEGES AND UNIVERSITIES
BOARD OF TRUSTEES
AUDIT COMMITTEE
MEETING MINUTES
November 17, 2010**

Audit Committee Members Present: Trustees James Van Houten, Chair; Philip Krinkie, Dan McElroy, Alfredo Oliveira, and Thomas Renier.

Audit Committee Members Absent: Trustee Michael Vekich.

Other Board Members Present: Trustees Jacob Englund, Christopher Frederick, David Paskach, Louise Sundin, and Scott Thiss.

Others Present: Beth Buse, Laura King, Gail Olson, and President Pat Johns.

The Minnesota State Colleges and Universities Audit Committee held its meeting on November 17, 2010, at Wells Fargo Place, 4th Floor Board Room, 30 East 7th Street in St. Paul. Chair Van Houten called the meeting to order at 9:50 a.m. and reviewed the agenda.

Approval of the Audit Committee Meeting Minutes

Chair Van Houten called for a motion to approve the September 14, 2010 audit committee meeting minutes. There was no dissent and the motion carried.

1. Review and Approve Release of the Audited Financial Statements (Action Item)

Ms. Beth Buse, Executive Director of Internal Auditing began by introducing Mr. Eric Wion as the new Deputy Director of Internal Auditing. Ms. Laura King, Chief Financial Officer, introduced Mr. Colin Dougherty as the new Associate Vice Chancellor for Finance, and members of his finance team. Trustee Van Houten welcomed everyone.

Ms. Buse explained that Audit Committee members had received advance copies of all thirteen college and university financial statements, as well as the systemwide audit and the revenue fund. She explained the contents of the five documents that were handed out to the committee. Those documents included a copy of the systemwide financials, the supplement to the financial statements, fifteen coversheets that summarized the results of each audit, the required communications letter from LarsonAllen, and a copy of the presentation. She added that there was also a single page document related to the Office of the Legislative Auditor's evaluation of the system office.

Ms. Buse introduced Mr. Tom Koop, an audit partner with LarsonAllen. Mr. Koop introduced Ms. Brenda Scherer who was the audit manager for the college and university audits. Mr. Koop reminded members that their audit responsibility was to express an opinion on the overall systemwide financial statements for the year ended June 30, 2010 and to express an opinion on compliance with federal compliance parameters regarding the American Recovery and Reinvestment Act (ARRA) and the student financial aid programs. He noted that that opinion would be discussed early in 2011 when the process

was completed. In support of the audit effort, internal controls were reviewed for material weaknesses or significant deficiencies. He also noted that the internal controls over information technology were reviewed to support the systemwide audit and that a report had been issued to management containing housekeeping details. He added that it had been a positive report with no material weakness or significant deficiency in internal controls.

Mr. Koop informed the members that the audit opinion on the systemwide financial statement, as well as on the revenue fund statement, was unqualified, which was the highest level that could be issued. He added that there were no internal control written findings, and that it was notable and a cause for celebration within the Minnesota State Colleges and Universities.

Ms. Scherer stated that there was a \$9 million materiality threshold systemwide. She stated that they were issuing a clean unqualified opinion; there were no significant deficiencies or material weaknesses in the systemwide audit. She noted that the two prior year significant deficiencies related to access controls and bank reconciliations had both been tested and they had been cleared for the current fiscal year. She thanked the staff for all their hard work. Trustee Van Houten stated that the clean audit results represented a big achievement for the colleges and universities. Ms. Scherer continued by reviewing the required communications.

Mr. Koop stated that over the years, the colleges and universities had taken more ownership of financial statement process and it was clear that they understood them. They have responded to internal control audit findings and those have all been cleared. He stated that the challenge going forward would be to maintain those results, and he added that ensuring continuous training, retrained and reassessing the process would continue to be important. Mr. Koop stated that in difficult economic times, providing stable service levels, strong leadership, and enabling technology would be key to maintaining a strong financial process.

Trustee Renier asked if the strong audit results could be attributed to the investments the system had made in technology. Mr. Koop stated that there had been good leadership in responding to prior audit results by the investments that had been made in the technology effort, but he was not able to quantify which investments were responsible for the current results. He added that in general he thought those investments had contributed in a positive way.

Trustee Van Houten reminded members that the Office of Legislative Auditor had suggested that reassessing the system approach to risk management would be worth reviewing. He noted that the audit process and the positive results did not mean necessarily that the risk assessment approach was good enough. He asked if the system had adequately assessed the risk in assigning staff work. Mr. Koop stated that recent changes in the audit standards which required the organization to formally document the risks at each college and university and within the system and identify internal controls had pushed the system to do more risk assessment.

Trustee Van Houten asked if the match of staff work and budget to oversee accounting activities seemed to be in line with the risks that were in place. Mr. Koop agreed. Ms.

King agreed that the internal control documentation process that the colleges and universities went through had been very useful in explicitly examining and documenting processes and identifying areas of risk. But she did not conclude from that that the colleges and universities were staffed correctly with the right skills covering the right risk points. She stated that the system was thinly staffed in this area and that it was a continuous challenge to ensure that the right staff was in the right place, covering the right risk profiles. Trustee Van Houten thanked her for the clarification and agreed it was an important point.

Trustee Krinkie stated that the positive audit results were due primarily to those people who had handled the millions of transactions. He commended them and stated that it had taken collaborative efforts as well as meticulous work to ensure that the audit had come out clean. He stated that those people should be recognized by a letter from Chair Thiss and the Chancellor for their work.

Mr. Dougherty echoed Trustee Krinkie's compliments to the collaborative effort across the system, that not only contributed to the strong audit results, but also to the strong financial performance. He reviewed the highlights of the financial statements for the committee.

Mr. Dougherty stated that the system's composite financial index in the fiscal year just ended was 3.21 which was a healthy improvement over the prior year of 1.62. He reminded members that the Higher Education Learning Commission starts to pay attention to individual institution level when they fall into the 0-1 range. He noted that the net operating revenue was a key component driving the favorable results of the composite financial index. Mr. Dougherty explained the four key components of the composite financial index.

Trustee Van Houten commented that the composite financial index provided benchmarks that gave insight on how the system has performed versus other systems. He added that they were a set of criteria that were somewhat different than what was used in the private sector, so it was particularly helpful for the committee to see those numbers and understand them. Mr. Dougherty commented that three was a respectable number based on the analytical framework that had been developed through KPMG, Bearing Point and others.

Ms. King noted that if the system were to seek a credit analysis for a system issued debt offering, this rating would suggest that the system would be viewed by the rating agency as a Triple A credit. She stated that as the committee thought about the system's financial condition, the composite financial index provided a way to understand how the system was keeping up with the national trends and the national macroeconomic forces that were moving through higher education. Trustee Van Houten agreed that was helpful. Ms. King noted that Moody's indicated that the system revenue fund was even stronger than the system as a whole.

Trustee Van Houten noted that the standard deviation for the system could be wide and it could be that although the number looked strong at the system level, at certain individual institutions, a challenge would be much more difficult to protect with the reserves. Ms. King agreed.

Trustee McElroy stated that historically there had been larger enrollment growth in slower economies and slower enrollment growth in growing economies. He added that there had been a slow decline in the overall numbers of high school graduations that started after the 2009 class and according to the state demographer, that decline would likely continue for 10 years. He asked how comfortable the system was that it would continue to see the enrollment increases that had contributed to the increased performance in the last three years. He stated that he was concerned that a two percent growth was not sustainable overtime. Mr. Dougherty stated that for the most part, the colleges and universities had managed the fine performance and control of expenses in fiscal year 2010 with the use of adjuncts and resources that gave them more flexibility in a very dynamic enrollment environment.

Trustee McElroy agreed the growth was dynamic, but noted that some of the increase in financial aid was due to a significant increase in federal PELL grant, in both funding and maximums, and that it was not certain that that would continue over time. He noted that growth was good news, but he added that the system needed to exercise caution. Trustee McElroy further noted that if the colleges and universities were to continue to be successful in increasing retention and completion rates, that would have the effect of increasing enrollments, as students stayed longer and completed programs. He added that he was excited about the financial results, and particularly excited about the strong performance of the audit. But he added that the purpose of the system was at least partially measured by completion, graduation and retention, and those were not as strong as the financial results.

Ms. King stated that they had identified the financial aid trends as one of the areas for additional analytical work before the January meeting, and they could add to that a more extensive understanding of what was happening around the enrollment forecasting.

Ms. King thanked the college and university financial staff and the presidents for their hard work. She noted that she was very pleased with the level of adoption of this effort by the campuses, and their commitment to it and their growing sophisticated use of the information. She thanked LarsonAllen for a very strong first year and added that it gave value to the Board's position that lead auditors be rotated periodically to bring new questions and new perspective. She thanked Normandale Community College and President Opatz. She added that it was not easy work but that the college had done a terrific job, and produced an unqualified opinion their first year out, which was a material accomplishment. She thanked the financial reporting staff and the Office of Internal Auditing for all their efforts. She extended her appreciation to Darrel Huish and Carolyn Parnell and their staff. She noted that they had received a message from the Chancellor and from the Chair of the Board that cleaning up the technology issues was a priority, and they staffed it hard until those problems were resolved. Finally, she congratulated the college and university leadership for the positive audit results. She stated that it provided a strong foundation to have the discussion this committee wanted to have in January about the audit strategy for the future.

Chair Thiss commented that he had seen a steady progression toward the use of data to support progress rather than quantitative comments and he complemented the staff. He added that the Chancellor had clearly driven the message of continuous improvement all

the way down through the system, and Chair Thiss acknowledged his efforts.

Trustee Dickson stated that while it may not be appropriate for the system to issue a press release about the wonderful audit results, she encouraged the auditors to spread the word when they could about the hard work and wonderful results happening within the system.

Trustee Krinkie suggested that the Government Relations staff should share the audit results with legislators. He noted that twenty-five percent of the legislators would be arriving in January as first term members. He noted that those legislators would be making decisions in the future and would need to know that the system's fiduciary responsibility had been fulfilled and that outstanding work had been done.

Mr. Koop introduced Mr. Craig Popenhagen, the principal in charge of the Revenue Fund stand alone audit. Mr. Popenhagen stated that an unqualified opinion had been issued on the Revenue Fund financial statements. They were fairly stated in accordance with accounting principles. No significant deficiencies or material weaknesses had been identified in internal controls. He stated that the control environment was very strong.

Mr. Koop presented information on the financial statement audits that his firm conducted for Metropolitan State University, Minneapolis Community and Technical College, Rochester Community and Technical College and Southwest Minnesota State University. Some of the key points shared by Mr. Koop were as follows:

- Unqualified Opinions issued for all audits.
- No internal control, compliance, material weakness or significant deficiencies.

Mr. Koop noted that in the prior year there had been a material weakness at Rochester Community & Technical College with regards to accounts payable cut off. The college had a very intense response to ensure that finding had been addressed. He stated that there were internal control findings in the current year.

Chair Thiss asked if the Board should be concerned about the three years of operating losses at Rochester Community & Technical College. Ms. King stated that there had been some large onetime events working through their books because of an asbestos expense project and that her office had been working with the college.

Mr. Koop noted that there were no findings at Southwest Minnesota State University. The university had improved its bottom line from a significant \$3.1 million loss last year to a \$1.3 loss in the current year, but they were still in the red.

Trustee Van Houten welcomed Mr. Steve Wischmann, partner with the firm of Kern, DeWenter and Viere. Mr. Wischmann presented information on the financial statement audits that his firm conducted for Hennepin Technical College, Minnesota State University, Mankato, Minnesota State University Moorhead, Normandale Community College and Winona State University. Some of the key points shared by Mr. Wischmann were as follows:

- Unqualified Opinions issued for all audits.
- No internal control, compliance, material weakness or significant deficiencies.

Mr. Wischmann stated that this was the first year audit of Normandale Community College. He stated that his firm had reviewed the balance sheet for the college last year to obtain assurance on the beginning balances. He stated that there can be a large learning curve with first year audits, but he stated that the college had done a fantastic job of dedicating the resources they needed to ensure an efficient and effective campus audit. He thanked them for all their hard work.

Trustee Van Houten welcomed Mr. Darrel DeKam, partner with the firm of Baker Tilly Virchow Krause. Mr. DeKam presented information on the financial statement audits that his firm conducted for Bemidji State University, Century College, Minnesota State Community and Technical College and St. Cloud State University. Some of the key points shared by Mr. DeKam were as follows:

- Unqualified Opinions issued for all audits.
- No internal control, compliance, material weakness or significant deficiencies.

Mr. DeKam noted that in prior years there have been some challenges with regards to credit cards and journal entries at Bemidji State University. He stated that the issues had been cleared and that there were no internal control findings in the current year.

Mr. DeKam noted that there had been one significant deficiency with regards to materiality of journal entries at Century College in the prior year, but that finding had not reoccurred in the current year.

Mr. DeKam stated that a tornado had come through the northern part of the state just before the end of the year. He stated that the firm had been concerned that Minnesota State Community and Technical College's ability to provide all of the information that was required for the audit work would be impacted. Mr. DeKam stated that they were particularly pleased that the audit was able to proceed as scheduled. He noted that there were some unusual audit entries in order to ensure that the impact of the tornado was appropriately recorded, but the audit went very smoothly.

Trustee Van Houten called for a motion to approve the Release of the Audited Financial Statements. *Trustee Krinkie made the motion, Trustee Renier seconded. The Audit Committee recommends that the Board of Trustees approve the following motion:*

COMMITTEE ACTION:

The Audit Committee has reviewed the fiscal year 2010 audited financial statements and discussed them with representatives of management and the external auditing firms. 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 release of the fiscal year 2010 audited financial statements as submitted.

2. Follow-up to OLA Evaluation of the System Office (Information Item)

Ms. Buse referred to the one page summary of the recommendations from the Office of the Legislative Auditor. She stated that members would be discussing the summary in the upcoming study session of the Board and that the summary would likely be attached to the letter that Chair Thiss and Chancellor McCormick would be sending to the Legislative Audit Commission.

Ms. Buse stated that members had heard discussion in each committee of the Board on the actions taken by individual committees and staff in following up on the recommendations from the report. The one page status summary was based on those discussions. Ms. Buse highlighted the discussion in the Academic and Student Affairs Committee related to online education and the cost effectiveness. She noted that particular recommendation was incorporated in the summary of office organization and that the status of that particular recommendation was in progress.

Trustee Van Houten thanked her for her report and stated that it would be helpful in the next session.

3. Progress on Committee Goals (Information Item)

Trustee Van Houten stated that in January the committee would need to consider whether to hire audit firms for six audits. He noted that the committee would also need to start serious work on the risk assessment plan, which would include discussion on the number of audits that should take place.

Ms. Buse stated that the information from the audit plan that was presented in September was also included in this month's packet materials. The timeline related to the committee's goal indicated that the committee would receive more information related to a risk assessment approach in November, but Ms. Buse stated that there had not been enough time in the last couple of months to put together a report that was worthy of the committee's consideration. She stated that she would present that information to the committee in January. She noted that the six college and university audits that would be discussed in January were the largest six college and university audits related to the financial statement audits. Trustee Van Houten noted that the only issue that had a specific deadline for January was the hiring of the audit firms.

Trustee Van Houten thanked the committee members for their work of reading through the fifteen individual audits, and he thanked the staff for putting together a set of reports and summaries that were clean and uncomplicated. He noted that it was clear that the organization took its financial responsibility seriously and that the Audit Committee took its work seriously as well.

The meeting adjourned at 11:18 a.m.

Respectfully submitted,
Darla Senn, Recorder