

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

Agenda Item Summary Sheet

Committee: Audit Committee

Date of Meeting: January 18, 2011

Agenda Item: Audit Risk Assessment Methodology Discussion

Proposed Policy Change Approvals Required by Policy Other Approvals Monitoring

Information

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

As part of the Fiscal Year 2011 Audit Plan, the Office of Internal Auditing proposed conducting a risk assessment.

Scheduled Presenter(s):

Beth Buse, Executive Director, Office of Internal Auditing

Outline of Key Points/Policy Issues:

- Overview of system risk management practices.
- Coordination with Finance division, Information Technology division, and Office of General Counsel.
- Proposed methodology for determining risk factors for development of fiscal year 2012 audit plan.

Background Information:

- As part of the Audit Plan for Fiscal Year 2011, presented to the Audit Committee in September 2010, the Office of Internal Auditing proposed an Audit Approach Evaluation which included determining a risk assessment methodology.
- Professional internal auditing standards require that the audit plan be based on a risk assessment to ensure that audit resources are focused on the most critical and value-added projects.

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BOARD INFORMATION

AUDIT RISK ASSESSMENT METHODOLOGY DISCUSSION

Professional internal auditing standards require; the chief audit executive (CAE) to establish risk-based plans to determine the priorities of the internal audit activity, consistent with the organizations goals.¹ Guidance on this standard states that the CAE should prepare the audit plan based on the audit universe, input from senior management and the board, and an assessment of risk and exposures affecting the organization.

When a formal process or Enterprise Risk Management (ERM²) program exists, internal audit is able to leverage the results to limit additional risk assessment. However, a mature process does not exist within the Minnesota State College and University system.

Overview of Risk Management in the Minnesota State College and University System

Every day system leaders and managers make risk based decisions in the day to day activities that are common on college and university campuses:

- Should we expand the number of employees that have purchasing cards?
- When it is snowing, how often should we remove the snow from walkways?
- Should we allow student workers to file student and parent tax forms in financial aid files?
- How many employees should have access to make student grade changes?

The board's current expectations regarding risk management are contained in Board Policy 5.16 – Risk Management and Insurance:

Part 2. Responsibilities: The chancellor for the office of the chancellor and the presidents for the colleges and universities are responsible for effectively managing risks in order to conserve and manage the assets of the office of the chancellor, colleges and universities and minimize the adverse impacts of risks or losses.

The Office of the Internal Auditor, the General Counsel's office and the Finance Division have participated in a structured approach to risk assessment and mitigation that includes:

¹ Institute of Internal Auditors, International Standards for the Professional Practice of Internal Auditing 2010 - Planning.

² The Committee of Sponsoring Organizations (COSO) of the Treadway Commission defines ERM as a "...process, effected by an entity's board of directors, management, and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives."

- Regular and repeated training programs available to the campuses concerning systems, policies, procedures and guidelines
- Cascading monitoring and reporting protocols that culminate in Board Audit and Finance and Facilities Committee oversight
- Regular review of policy and procedures for refreshment and identification of new or emerging best practices and risks.

The Finance division also requires all colleges and universities to document and assess risk on their key financial internal control cycles. Internal controls are expected to provide reasonable, but not absolute assurances about their effectiveness.

The system is in the beginning phases of developing a more formalized risk assessment strategy. A risk assessment strategy is a key management tool for protecting an organization. A formal risk assessment and management strategy is a process-driven tool that enables senior management to visualize, assess, and manage significant risks that may adversely impact the attainment of key organizational objectives; ideally, it is integrated with the strategic planning process.

While this process will likely take several years until it is fully implemented, as the systemwide risk assessment program is formalized and matures, the Office of Internal Auditing will be able to leverage the results in future annual risk assessments. However, in the near-term, the Office of Internal Auditing will coordinate with the Finance Division and Office of General Counsel to conduct initial risk assessment meetings. Coordination of initial meetings should help reduce duplication of effort and eliminate confusion related to the dual-purpose of collecting the information.

Research on Higher Education Internal Audit Risk Assessment Processes

The Office of Internal Auditing conducted research on internal audit risk assessment best practices and methodologies to provide insight in determining a methodology for supporting the Audit Committee's goal of reevaluating the audit approach for the system. We reviewed materials and held conversations with internal audit employees from many higher education systems and institutions to determine the processes used for their annual audit risk assessment. In the end, we determined that there are a variety of methods used in conducting risk assessments for building annual audit plans. A number of factors come into play in determining a risk assessment process including: the maturity of an enterprise risk management program, available audit resources, complexity of the organization, and auditor professional judgment.

Proposed Audit Risk Assessment Methodology

We recommend a three-staged approach to conduct our audit risk assessment as depicted and described below. In stage one, systemwide meetings to identify risk factors would be conducted jointly with the Finance Division, Office of General Counsel and the Office of Internal Auditing. The remaining two stages would be facilitated by the Office of Internal Auditing.



- **Systemwide Risk Factors**

Representatives of the Finance division, Office of Internal Audit, and Office of General Counsel will meet with senior leadership and others to discuss risk factors.

Regional meetings will take place in February 2011 in conjunction with Vice Chancellor King's Trends and Highlights sessions with the leadership at 25 colleges that do not have an annual financial statement audit. In March, meetings will be held with a sampling of leadership from the 13 largest colleges and universities.

Other meetings will include representatives from Board of Trustees, Chancellor and his executive leadership, external auditors, and other focused groups to be determined (may include, for example, groups of chief financial officers, financial aid directors, and registrars).

- **Fiscal-Focused Risk Factors**

Internal Audit will assess individual college and university fiscal internal controls based on several factors that may include: financial activity, transaction volume, prior audit findings, exception reporting, staff size and turn-over, and systems security access. We will begin to build and use data analysis techniques to identify potential vulnerabilities.

- **Information Technology Risk Factors**

Internal Audit will develop an initial methodology for conducting an information technology audit risk assessment. The first two stages may include information technology components as they relate to key activities.

Date Presented to the Board of Trustees: January 18, 2011