

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

Agenda Item Summary Sheet

Committee: Audit Committee

Date of Meeting: October 18, 2011

Agenda Item: Review Annual Internal Auditing Report for FY2012, Including Status of Unresolved Findings.

Proposed
Policy Change

Approvals
Required by
Policy

Other
Approvals

Monitoring

Information

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

Board Policy 1D requires an annual report from the Office of Internal Auditing.

Scheduled Presenter(s):

Beth Buse, Executive Director, Office of Internal Auditing

Outline of Key Points/Policy Issues:

- Internal Audit activities were consistent with the audit plan for fiscal year 2011.
- An update on the resolution of outstanding audit findings for fiscal year 2011 is incorporated into the annual report.

Background Information:

- The audit plan approved by the Board of Trustees in September 2010 provided the foundation for the internal auditing activities carried out in fiscal year 2011.

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

BOARD INFORMATION

REVIEW ANNUAL INTERNAL AUDITING REPORT FOR FY2011,
INCLUDING STATUS OF UNRESOLVED FINDINGS

The annual report for fiscal year 2011 is attached.

Date Presented to the Board of Trustee: October 18, 2011



Minnesota
STATE COLLEGES
& UNIVERSITIES

Internal Auditing Annual Report Fiscal Year 2011

Office of Internal Auditing
Reference Number 2011-10-004

October 6, 2011

October 6, 2011

Members of the Board of Trustees

I am pleased to submit the annual report on the Office of Internal Auditing for fiscal year 2011 as required by Board Policy 1D.1 part 8.

Fiscal year 2011 was a year of transition, new Executive and Deputy Directors were hired and the office was restructured to improve information technology audit capabilities. The office has talented and dedicated professional staff members who take great pride in their work. The office complies fully with the professional practices of internal auditing.

I wish to reiterate my commitment to managing an office that provides you with credible, professional services. Organizationally, the Office of Internal Auditing is structured to ensure its independence by reporting directly to the Audit Committee. Personally, I take great care to avoid assignments or relationships that would compromise my independence. Accordingly, I pledge to you that I continue to remain independent and objective pursuant to the professional practices of internal auditing in my role as Executive Director of the office.

Thank you for your confidence and support in our work.

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Summary

The audit plan approved by the Board of Trustees in September 2010 provided the foundation for the internal auditing activities carried out in fiscal year 2011. Some noteworthy activities included:

- **Staffing changes** – hiring of Executive and Deputy Directors. In addition, the office was restructured to improve information technology audit capabilities.
- **Follow-up** - colleges and universities made significant progress in resolving outstanding audit findings during fiscal year 2011.

The Office of the Chancellor made significant progress on findings cited by the Legislative Auditor in its February 2010 program evaluation report, *MnSCU System Office*

- **External Audits** - LarsonAllen, the principal auditor for the system, and two other audit firms gave unqualified (clean) financial statement audit opinions for the system and 13 colleges and universities. Notably, no material weaknesses or significant deficiencies were reported.
- **Inquiries and Investigation** - Internal Auditing saw an increase in the number of fraud incidents reported this year as compared to prior years. Fortunately, there were no significant losses.
- **Audit Planning** - completed an initial audit risk assessment for use in prioritizing audit resources that focused on enterprise, financial, and information technology risks.

*Beth Buse, Executive Director,
had lead responsibilities for this report.*

I. Assurance Services

The Office of Internal Auditing spent the majority of its time working on assurance services which, depending on the scope of the audit, may focus on the quality and reliability of information, legal and policy compliance, and operational efficiency and effectiveness. The following assurance service projects were conducted during fiscal year 2011.

Audited Financial Statements

Audits of fiscal year 2010 financial statements marked the tenth year that the Minnesota State Colleges and Universities contracted for an external audit of its financial statements. The system transitioned to a new principal external audit firm (LarsonAllen). LarsonAllen provided an unqualified (clean) opinion on the system-wide financial statements in November 2010.

At the system-wide level, the external auditor also did not cite any “material weaknesses” or “significant deficiencies.” in internal controls. The auditing literature considers a “material weakness” to be the most serious type of problem associated with an internal control structure, so the absence of “material weaknesses” is a positive indicator. Less serious, but noteworthy internal control considerations are referred to as “significant deficiencies.”

In addition, audited financial statements were developed for 13 of the largest institutions: the seven state universities and six two-year colleges. The financial statements for all 13 institutions received unqualified audit opinions from the CPA firms that the board appointed for the audits. Notably, all 13 institutions had no “material weaknesses” or “significant deficiencies.” in internal controls. This is a significant accomplishment and the first time this has occurred. Normandale Community College should be commended for this accomplishment since it was a first time audit for the college.

The Financial Reporting Unit of the Office of the Chancellor, college and university finance staff, and the Office of Internal Auditing have worked hard to deliver the audited financial statements. Internal Auditing spent 26 percent of its applied hours on assisting with financial statement audits in fiscal year 2011. This level of support provides benefits to the firms by utilizing the expertise of Internal Auditing’s knowledge of the Minnesota State Colleges and Universities system and its business systems.

Financial Internal Control and Compliance Audits

In the past, the Audit Committee and other stakeholders relied on internal control and compliance audits provided through a contract with the Office of the Legislative Auditor to conduct rotating audits of colleges without annual financial statement audits. By mutual agreement, the contractual arrangement with the Legislative Auditor ended after the fiscal year 2010 audits.

Fiscal year 2011 was a year of transition for Internal Auditing and no specific internal control and compliance audits were conducted. Many conversations took place with the Audit Committee and senior leadership on determining the appropriate level of audit coverage for the future of financial internal control and compliance audits.

Follow-up on Prior Audit Findings

The Board of Trustees and Chancellor expect timely resolution of audit findings. Internal Auditing maintains a database for tracking audit findings. Internal Auditing monitors the status of audit findings through resolution. Presidents are provided a mid-year and end-of-year follow-up report. Beginning in 2011, the status report format was revised in order to provide a tool which allows presidents to more quickly identify areas needing their immediate attention. This change resulted in positive feedback. The following table summarizes fiscal year 2011 activity:

**College and University
Audit Finding Activity Summary – As of June 30, 2011**

Unresolved as of July 1, 2010	108
Additions – Fiscal Year 2011	231
Resolved – Fiscal Year 2011	(297)
Unresolved as of June 30, 2011	42

Status of Unresolved Findings

Satisfactory Progress	37
Unsatisfactory Progress	5

Colleges and universities made significant progress on resolving outstanding audit findings during fiscal year 2011. As of June 30, 2011, there were only 42 unresolved audit findings, of those only five were given unsatisfactory progress. The findings in unsatisfactory progress are classified as ‘important’, additional information is shown below.

**College and University
Audit Findings with Unsatisfactory Progress – As of June 30, 2011**

Type	Findings	Days Since Issuance	Days Past Target Completion
User Security - Incompatible Access	2	652	180
Bank Reconciliation	1	244	0
Capital Asset Management	2	620	297

In addition to monitoring progress on college and university outstanding audit findings, Internal Audit also monitored progress on the findings cited by the Legislative Auditor in its February 2010 program evaluation report, *MnSCU System Office*. The program evaluation focused on questions regarding the size and performance of the central administrative office of the Minnesota State Colleges and Universities. Progress was tracked with monthly updates to the Audit Committee. In November 2010, a letter was sent from Chair Thiss and Chancellor McCormick to Senator Ann Rest, along with an enclosure that highlighted that the majority of the recommendations were implemented or in progress to be implemented.

Other Internal Auditing Assurances

The Office of Internal Auditing also provides other assurance services as requested by the board, Chancellor, or presidents. Some recurring projects include:

- Facilitating transition reviews of colleges and universities when there is a change of presidents.
- Limited testing for finance legal compliance of expenses incurred by the Chancellor and Board of Trustees.

II. 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 reported potential fraud incidents to the Legislative Auditor, as required by state law.

Overall, Internal Auditing saw an increase in the number of fraud incidents reported this year as compared to prior years. Although there were no material losses to the organization, it is important to note that policy 1.C.2 requires an inquiry to determine whether evidence of fraudulent or other dishonest acts is substantiated and merits a fraud investigation or other remedy. Where warranted, a fraud investigation must be completed. As a result of the increase in the number of reported incidents, a significant amount of college and university staff time as well as Internal Auditing staff time was dedicated to completing inquiries and investigations. A summary of the types of incidents commonly reported to Internal Auditing were:

- **Theft of equipment or vandalism:** commonly includes the theft of laptop and desktop computers and other information technology equipment such as overhead projectors. College and university campuses commonly see vandalism to their buildings and other property. In most cases, colleges and universities report these incidents to local law enforcement.
- **Financial aid fraud:** in the past few years we have seen a substantial increase in student financial aid fraud primarily at the two year institutions. My office works closely with the Inspector General's Office of the U.S. Department of Education on these incidents.
- **Bank account incidents:** these types of incidents commonly include fraudulent checks being drawn on an account or attempts to gain unauthorized electronic access to an account.

Internal Auditing assisted with other inquiries and investigations primarily centering on allegations of employee misconduct or misuse of property.

III. Professional Advice

Internal Auditing also makes itself available to offer professional advice on topics within its expertise. During fiscal year 2011, Internal Auditing fielded numerous questions dealing with various topics. Common questions pertained to compliance with board policies, system procedures, and best practices.

Internal Auditing representatives also sit on various system task forces and committees, including: Security Steering Committee, Finance User Group, Financial Aid Directors, Chief Information Officers, and Students First working groups.

IV. Planning

In August 2010, the Audit Committee approved the following committee goal for the year:

Complete a thorough evaluation of the audit approach for the Minnesota State Colleges and Universities. The evaluation should:

- *Be based on a risk assessment and include a plan for obtaining internal control and compliance audit coverage given that the contractual relationship with the Office of the Legislative Auditor has ended.*
- *Consider the value and role of obtaining annual financial statement audits for individual colleges and universities.*
- *Determine a strategy for an information technology audit approach.*

Internal Auditing completed a three-staged audit risk assessment during fiscal year 2011 that identified enterprise strategic, fiscal, and information technology risk factors. The results of the risk assessments were discussed with the Audit Committee in May and June. In addition, the results were taken into consideration in building the proposed audit plan for fiscal year 2012.

V. Analysis of Staff Hours

For 2011, Internal Auditing underwent a transition in staffing. The office restructured in order to improve information technology audit capabilities. The majority of professional staff, regional audit coordinators, are located on college or university campuses throughout the system. The audit coordinators serve multiple colleges or universities located in their regions.

Table 1 provides a summary of how internal auditing staff resources were used during fiscal years 2009 through 2011.

**Table 1: Percentage of Internal Auditing Technical Service Staff¹ Hours
Fiscal Years 2009, 2010 and 2011**

Service	Fiscal Year 2011	Fiscal Year 2010	Fiscal Year 2009
Follow-up on Prior Audit Findings	34%	28%	21%
Audited Financial Statements	27%	23%	16%
Internal Control and Compliance Audits	3%	14%	3%
Fraud Inquiry and Investigation Support	17%	11%	12%
System-wide Audits	0%	9%	22%
Professional Advice	7%	8%	7%
Planning	6%	0	0
Other Internal Auditing Assurances	6%	7%	6%
Consulting Services	0	0	13%

The Future

In October 2011, the Board of Trustees will be asked to approve an audit plan for fiscal year 2012 that takes into consideration the results of audit risk assessments and available audit resources. Audit plans and other information on Internal Auditing are available at the office website, www.internalauditing.mnscu.edu.

¹ Excludes executive and deputy director hours.