

**MINNESOTA STATE COLLEGES AND UNIVERSITIES
BOARD OF TRUSTEES
AUDIT COMMITTEE
MEETING MINUTES
November 15, 2011**

Audit Committee Members Present: Trustees James Van Houten, Chair; Philip Krinkie, Dan McElroy, David Paskach, and Michael Vekich.

Audit Committee Members Absent: none.

Others Present: Trustees Brett Anderson, Duane Benson, Cheryl Dickson, Jacob Englund, Alfredo Oliveira and Chancellor Rosenstone.

The Minnesota State Colleges and Universities Audit Committee held its meeting on November 15, 2011, at Wells Fargo Place, 4th Floor McCormick Room, 30 East 7th Street in St. Paul. Chair Van Houten called the meeting to order at 9:03 a.m. and reviewed the agenda.

Approval of the Audit Committee Meeting Minutes

Chair Van Houten reviewed the highlights of the October meeting minutes. He called for a motion to approve the October 18, 2011 audit committee meeting minutes. There was no dissent and the motion carried.

1. Review and Approve Release of Audited Financial Statements 2011 (Action Item)

Trustee Van Houten suggested, and the committee agreed, that the agenda be realigned to accommodate the external auditors who had come to present the audited financial statements.

Ms. Beth Buse, Executive Director of Internal Auditing began by explaining that audit committee members had received advance copies of all thirteen college and university financial statements, as well as the system wide audit and the revenue fund. She explained the contents of the six documents that were handed out to the committee. Those documents included the PowerPoint presentation, Required Communications from LarsonAllen, LLP, a one-page summary of the Net Operating Incomes and a one-page summary of the Composite Financial Index (CFI) for each college and university, a copy of the system wide financials, and a copy of the supplement to the financial statements.

Ms. Buse introduced Mr. Tom Koop, an audit partner with LarsonAllen, Mr. Craig Poppenhagen who was the partner in charge of the revenue fund and Ms. Brenda Scherer who was the audit manager for the college and university audits. She stated that the system had another good year in terms of the financial statements.

Mr. Koop reminded members that their audit responsibility was to express an opinion on fairness of presentation of the system wide financial statements for the year ended June 30, 2011. In support of the audit effort, internal controls were reviewed for material weaknesses or significant deficiencies. He stated that they were engaged 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 2012 when the process was completed.

Mr. Koop reviewed the audit scope and coverage of the sytemwide audit. He stated that it was a positive report with no material weakness or significant deficiency in internal controls and no compliance issues.

Ms. Scherer reviewed the process for the system wide financial statement audit. She stated that while there were no internal control issues to report, there were some observations and best practices that came out of the audit, and a formal letter was sent to management. Trustee Van Houten asked how many colleges would have received formal letters. Ms. Scherer responded that almost all of the colleges had one or two comments or best practice suggestions.

Mr. Koop informed the members that the audit opinion on the system wide financial statement, as well as on the revenue fund statement, was unqualified, which was the highest level that could be issued. He added that not only were there no internal control written findings, the auditor's procedures resulted in no auditor generated adjustments. He stated that was notable and a cause for celebration within the Minnesota State Colleges and Universities. Mr. Koop further stated that for the second year in a row, no significant deficiencies or material weaknesses were noted in the system wide audit or at any of the campus level audits.

Mr. Koop noted that the state shutdown caused delays in the flow of information which resulted in increased demands on system office staff, campus staff, as well as staff at the auditing firms. He complimented staff for remaining professional at all times even through that added stress. He further stated that the communications process that was established facilitated the work flow so that quality was maintained throughout the audit process.

Mr. Koop reviewed the three Levels of Financial Management as described by the Government Finance Officers Association's "Financial Management (FM) Tool."

Mr. Koop stated that the challenge going forward would be to maintain the results that had been delivered for the last two years as budget restraints and public scrutiny would demand even more continuous improvement in the future. 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.

Mr. Dougherty introduced the financial reporting team and Denise Kirkeby and Methody Popov. He thanked the staff at the system office and at the campuses for the hard work they did to get the system to the great audit results. He reviewed the highlights of the system wide financial performance for the committee.

Mr. Dougherty stated that the system's CFI in the fiscal year just ended was 2.91, essentially flat with the prior year performance. Mr. Dougherty noted that the CFI had been restated in fiscal year 2010. He added that the system's economic performance had

not changed, but that the Higher Learning Commission increased the emphasis on one of the four metrics requiring the need for a surplus condition was a deficit.

Trustee Van Houten stated that our current level of operating reserves might sound like a great deal of money, but it really is just a little more than one month of salaries for the system. Mr. Dougherty agreed and noted that the system had only been operating in a surplus for two years.

Mr. Dougherty reviewed the changes in net operating revenue in the previous fiscal year and the return on net assets. He reviewed the system's 2.91 CFI against Moody's credit rating. He explained that a poor CFI would increase the system's debt costs, or higher interest rates.

Mr. Dougherty compared the system's rating to other universities. He noted that the system was very comparable to the University of Minnesota.

Ms. Buse introduced Mr. Craig Popenhagen, the principal in charge of the Revenue Fund standalone 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.

Trustee McElroy asked if there were individual college or university revenue funds that were not operating as well as the whole. Mr. Popenhagen stated that there were and he mentioned Southwest Minnesota State University as one example. Ms. King explained the situation at the university and noted that the university has taken strong action to reduce their revenue fund related expenses and to launch new enrollment and program development strategies. Trustee McElroy asked if it would be possible to see the revenue fund numbers for individual campuses and Ms. King stated that they could provide that information.

Mr. Koop presented information on the financial statement audits that his firm conducted for Southwest Minnesota State University, Metropolitan State University, Minneapolis Community and Technical College, and Rochester Community and Technical College. 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.

Trustee Van Houten asked about the loss that occurred with the transfer of the parking lot property from Metropolitan State University back to Minneapolis Community and Technical College. Vice Chancellor King stated that this transaction was not in the performance results that for either the college or the university for fiscal 2011. She stated that it was a neutral transition that created some accounting consequences in the cost based asset accounting system that would have to be reviewed. She noted that the transaction would appear again in the fiscal year 2012 financial statements and she would be prepared at that point to explain how the transaction was booked.

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 Moorhead, Normandale Community College, Winona State University, Minnesota State University, Mankato, and St. Cloud 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.

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, and Minnesota State Community and Technical College. 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.

Trustee McElroy asked about the dramatic CFI reduction at Century College. Vice Chancellor King explained that the college had tremendous enrollment increases and they had done a lot of out of pocket construction financing to build classrooms and to buy computers. She added that it had been purposeful spending and that the college was finished with their build outs. Trustee Krinkie asked about the net operating loss at Anoka Technical College. Vice Chancellor King stated that she did not know the specifics about the non-audited colleges, but she thought it was likely a situation similar to Century College.

Chancellor Rosenstone stated that there was a balancing act that had to be done between the prudent management of resources and the management of risk and a greater expenditure of resources to accomplish good ends. He asked Mr. Koop, Vice Chancellor King, Mr. Dougherty and Ms. Buse to comment on how well the system was positioned with respect to that balance.

Mr. Koop stated that the system has a stable CFI which would allow the system to be more transformational. He added that in his opinion, the more sophisticated the financial management process was, the closer the system was able to operate to the edge, because it was in more control. Mr. Koop noted that the system did not have too much in reserves and added that with state shutdowns and dramatic changes in student demographics, the environment could change quickly. He stated that what the system had already accomplished was very solid and positive financially. He encouraged the system to continue moving slowly up the pyramid of financial reporting quality.

Vice Chancellor King stated that the system was facing a lot of downside risk with state appropriation exposure, tuition, inflation, downward pressure on system revenue, and the federal Pell Grant debate which could have a catastrophic impact for the system from a student affordability standpoint. She also noted that the state shutdown proved that the system had very few degrees of freedom from an operating environment standpoint. She stated that the Board of Trustees had been conservative and strongly supportive of improving system ratios, and she stated that she would like to continue to see the system wide number rise. She noted that the system wide number covered a lot of variability between the individual campuses.

Mr. Dougherty shared Vice Chancellor King's views and stated that he was even more committed and energized around the collaboration and cooperation that was happening in the system. He stated that he would like to see the system take more risk and move faster with the Campus Service Cooperative. Mr. Dougherty noted that there was innovation coming from around the system and he offered examples within the cooperative.

Ms. Buse agreed with what had been stated, but she added that there was a need to be competitive in the area of compensation and benefits. She noted that seventy percent of system expenditures were for compensation, which had only grown by one percent in the prior fiscal year. At the same time, the system saw a two percent enrollment growth. She cautioned that given what campuses have been doing to maintain costs over the last couple of years, it would be difficult to sustain growth into the future.

Chancellor Rosenstone acknowledged the need for caution to ensure that the system had the base for the transformative innovations that had been suggested, but also the base to protect the quality of academic programs in light of a long list of risks the system would be facing.

Vice Chancellor King stated that she was extremely grateful to the campuses for their hard work. She stated that this had been a particularly difficult year and noted that the SWIFT conversion had put a tremendous burden on the campuses. Vice Chancellor King stated that there had been outstanding cooperation and good spirits among staff given some very tough deadlines. She extended her congratulations to the presidents and the leadership teams on the campuses, who had been doing the tough day to day management, and paying attention to the internal control environment and the operating environment that enabled the system to produce financial statements without any material comments. She thanked the staff who worked extra hours to get the work done, and who took pride in the quality, accuracy, completeness and professionalism of their work.

Trustee Paskach stated that the reporting was really impressive work. He congratulated the staff and noted that it was clearly a high performing team of people. He asked how the system was able to get to this point. Vice Chancellor King stated that the centerpiece for these results was that they system had a great deal of continuity. She noted that there had been the same auditors and finance staff as well as largely the same Chief Financial Officers and that everyone had been invested in the continuous improvement curve. There had been good communication and shared best practices. She also complimented the audit committee for its commitment and the solid message of expectations.

Trustee Van Houten asked that the external auditor's positive comments be passed on to the appropriate staff. Chair Thiss stated that he had not expected that the high standard set last year would be exceeded, but through continuous improvement, the audit results this year were even more impressive. He stated that it was a marvelous accomplishment and congratulated everyone involved.

Trustee McElroy stated that it would be difficult next year to improve on the near perfect results this year. On the performance side, he added that he was really pleased to see that some of the smallest institutions had among the highest CFIs. He thought that was a testament to good management and to how important these institutions were to the system. He felt that was an important message to share with legislators.

Trustee Van Houten called for a motion to approve the release of the Audited Financial Statements for 2011. *Trustee Vekich made the motion, Trustee Paskach seconded.*

COMMITTEE ACTION:

The Audit Committee has reviewed the fiscal year 2011 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 2011 audited financial statements as submitted.

2. Proposed Amendment to Board Policy 1D.1 Office of Internal Auditing (Second Reading)

Ms. Buse noted that the proposed changes to Board Policy 1D.1 would mainly reflect changes in internal audit standards. She noted that some language had been removed regarding consulting services due to changes in services because of recent budget cuts. She stated that there had not been any changes since the first reading except to continue referencing the system office, rather than the “Office of the Chancellor.”

Trustee Van Houten called for a motion to approve the proposed amendment to Board Policy 1D.1 Office of Internal Auditing. *Trustee Vekich made the motion, Trustee Krinkie seconded.*

COMMITTEE ACTION

The Audit Committee recommends that the Board of Trustees adopt the following motion:

RECOMMENDED MOTION

The Board of Trustees approves the amendment to Policy 1D.1 Office of Internal Auditing.

3. Board Committee Goals (Information Item)

Ms. Buse suggested that the committee consider researching best practices of other audit committees as a goal for the year. She suggested that it might be a study of the audit approaches of other systems as well as the private industry. She noted that this type of study might be timed well as a succession planning tool given the significant audit committee rotation that would be coming in the next fiscal year.

Ms. Buse laid out the timing of the study. She stated that she could come back to the committee in January with a more specific plan as well as a start on the research. She reminded members that there would be a discussion in January about financial statement audits. She added that the committee could have the conclusion and final discussion in

June before the rotation of committee members occurred.

Trustee Paskach asked if the study could identify audit practices or best practices that would allow the audit committee to achieve the financial management level of enabling transformation. Ms. Buse stated that she was thinking the study might be more broad than only the financial piece. Trustee Van Houten stated that the committee goal could help the committee make decisions about the new audit plan and risk assessment. He noted that the committee would then have benchmarks which would give insights to leave behind for the next audit committee.

Trustee Van Houten asked President Szymanski and President Johns for their view of the project. President Szymanski thanked the committee for the work that it had done to provide assurance on campuses. She stated that she looks for ways to use the best practices that others have pioneered on her university, and she believed the project would be helpful from that prospective. President Johns stated that he thought looking at what other systems were doing would be very important for the system.

Vice Chancellor King reminded the committee that the audit committee would be having a discussion about the financial statement strategy for the next three to six years, which would require a decision by March to get the work underway. She wanted to make sure that the two projects would synchronize. Trustee Van Houten agreed, but stated that finding that the committee might not be working optimally, would be advantageous even if it were discovered after the plan was in place.

Ms. Buse stated that the research could be done in two phases. The research necessary to assist the committee with the decisions it needed to make about the financial statement process could be ready by January, and the broader conversation could take place in June.

Trustee Krinkie noted that it might be prudent for the audit committee to focus on any issues that might arise from the SWIFT conversion. Ms. King stated that she had had conversations about designing some special scope work for the fiscal year 2012 work, to go specifically to the conversion. She further stated that she had been in communication with the State Finance Commissioner about future adaptations for the accounting system. Ms. Buse agreed and stated that they could certainly consider the impacts of the SWIFT conversion as part of the audit risk assessment. She further noted that the Office of the Legislative Auditor had issued a user security report on the SWIFT implementation. She stated that she would keep in touch with the external auditors and what they need in preparation of the audit of fiscal 2012, as well as the internal plan.

The meeting adjourned at 11:00 a.m.