

**MINNESOTA STATE COLLEGES AND UNIVERSITIES  
BOARD OF TRUSTEES  
AUDIT COMMITTEE  
MEETING MINUTES  
August 19, 2010**

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

**Audit Committee Members Absent:** none.

**Other Board Members Present:** Trustees Christopher Frederick, and Scott Thiss.

**Others Present:** Beth Buse, Laura King, and Gail Olson.

The Minnesota State Colleges and Universities Audit Committee held its meeting on August 19, 2010, at Wells Fargo Place, 4<sup>th</sup> Floor Board Room, 30 East 7<sup>th</sup> Street in St. Paul. Chair Van Houten called the meeting to order at 8:03 a.m. and reviewed the agenda.

**Approval of the Audit Committee Meeting Minutes**

*Chair Van Houten called for a motion to approve the July 20, 2010 Audit Committee meeting minutes. Trustee Renier made the motion, Trustee McElroy seconded the motion. There was no dissent and the motion carried.*

1. Discuss Optional Approaches for Future Audit Coverage (Information Item)

Ms. Beth Buse, Executive Director of Internal Auditing, began by explaining that during fiscal year 2011, the Audit Committee would need to take action on future audit coverage. Significant decisions would need to be made in the area of internal control and compliance audits, college and university financial statement audits, and information technology audits.

Trustee Van Houten noted that a recent audit brought attention to the area of how information technology audits were conducted. He stated that there had not been any specific issues raised, but that the system had a clear responsibility to make improvements in how information technology audits were conducted.

Ms. Laura King, Vice Chancellor for Finance/Chief Financial Officer, urged the committee to think about the question of future audit coverage in the context of the system's entire financial management assurance program. She noted that audit coverage was one component of a strategy that was designed to give the Board financial management assurance.

Ms. Buse provided the committee with a summary of the services provided by the Office of Internal Auditing as well as a summary of audits conducted by external audit resources.

Ms. King stated that the Minnesota State Colleges and Universities external contract for the system-wide financial statement audit provided a service to the State of Minnesota for its statewide consolidated financial statement. She added that if the system were to discontinue conducting this audit, the State of Minnesota would have to replace that audit coverage and the cost burden would shift to the state. Ms. King further added that there was a cascading relationship between the thirteen individual audits, the system-wide audit and the state's consolidated financial statements. She pointed out that a change to any of those components would have implications for the rest of the entity. Ms. King explained that the Office of the Legislative Auditor's burden to perform the state consolidated financial statement review remained an unchanging burden. As their budgets have gone down, they have had fewer auditors available to provide service, which is why the Office of the Legislative Auditor did not have the resources available to continue auditing the smaller colleges. The State has an obligation to prepare financial statements and to have them audited. She noted that if the system were to stop conducting the system-wide audit, it would create a problem for the state, which the state would expect the system to help solve.

Trustee Thiss asked if there was an appreciation for the fact that the system spent a million dollars every year to conduct audits that benefited the State of Minnesota. Ms. King affirmed that the state was aware of the investment made by the system and stated that they had consciously worked, over the past ten years, to develop a relationship with the Office of the Legislative Auditor in a way that was cost beneficial to both organizations.

Trustee Thiss noted that the Legislative Auditor had questioned why the system conducted college and university financial statement audits, when the system did not have investors in the same way as private businesses. Ms. King stated that there were a variety of reasons for conducting financial statement audits. She noted that the principal auditor provided services that fulfilled an obligation to the state's consolidated financial statements. The thirteen financial statement audits helped to install a financial assurance environment on the campuses. They helped to inculcate skills in campus financial management staff for GAAP reporting and structured financial reporting. Some of the larger state universities have funders, and the availability of audited financial statements was an expectation in the funding community. Ms. King further noted that because the system-wide financial audit is a materially correct exercise, institution level audits gave the Board a deeper assurance around the largest institutions.

Trustee Van Houten stated that the financial statement audits were important for the purchase of state bonds as well. He noted that the bond rating was influenced by the financial performance reported out by the external auditors. Ms. King agreed and stated that the statewide audited financial statements were very important for all bond sales.

Trustee Krinkie asked if there was money budgeted in fiscal year 2011 for the contract with the Office of the Legislative Auditor. Ms. Buse explained that the contract with the Office of the Legislative Auditor had ended and that the money which had been set aside in the past for that contract would be a part of the budget discussion on the September Audit Committee agenda. There would need to be decisions made about internal control

and compliance coverage going forward. She noted that the Office of the Legislative Auditor had challenged in their recent audit of St. Cloud State University that there needed to be deeper coverage of internal controls and compliance than just a financial statement audit. Ms. Buse stated that she would come back in September with some options for the committee to consider in making decisions about future internal control and compliance coverage.

Trustee Van Houten noted that in the past the Office of the Legislative Auditor had paid for half of the audit coverage they provided and the Minnesota State Colleges and Universities had paid for the other half of the audit coverage. Ms. Buse agreed and stated that in fiscal year 2009, the Office of the Legislative Auditor provided over 6,000 hours of audit time. Fiscal year 2010 was a transition year where they provided 3,000 hours and the system paid for all of those hours.

Trustee McElroy stated that cost of the services provided by the Office of the Legislative Auditor had been significantly below market value for the same number of hours. He noted that although it would be a challenge to replace those services for the same cost, certified audits were not the only option available.

Ms. Buse stated that the Audit Committee could choose to expand the internal control and compliance audit approach by conducting a three-year rotation of audits on all institutions rather than just the un-audited institutions. She stated that the current audit approach might also be revised to review specific control cycles each year, such as a review of credit and purchasing cards across the system at all colleges and universities.

Ms. Buse reviewed the audit resource options. She stated that, depending on the scope of the audit approach, the committee could choose to add internal audit staff, reallocate audit staff, use outside firms, or use of other types of resources, such as hiring interns or accounting faculty for sabbatical work.

Trustee Vekich asked if there had been a risk assessment done of each of the institutions

Ms. King agreed that an assessment would be a valuable tool. She stated that the financial reporting staff was far ahead of state government and most public entities in documenting control cycles. She added that those documentation cycles were the first step in a risk assessment. Ms. King stated that that Office of Internal Auditing had done a system risk assessment a number of years ago, but that assessment had not been repeated. She stated that the system had developed sophisticated financial management monitoring methods and the Finance Committee had discussed financial management indicators, which were a measure of process compliance as well as financial condition.

Trustee Van Houten asked for a comparison of how the audits conducted by the Office of the Legislative Auditor versus those audits done by the external auditing firms. Ms. Buse explained that the Office of the Legislative Auditor had done internal control and compliance audits but that they did not necessarily have a materiality threshold compared to a financial statement audit. She noted that control cycle documentation related to material financial statement cycles and that the Office of the Legislative Auditor used

different standards in determining the areas of their focus. They used a more detailed analysis and testing approach.

Trustee Van Houten stated that by auditing the largest institutions in depth every year and auditing the smaller colleges for internal control and compliance every three years, there would be insights into issues that might exist throughout the system. He noted that the financial reporting staff put together training programs for all institutions based on the results of a few audits where systemic issues were discovered. He added that a fair amount of resources had gone into that institutional effort. Trustee Van Houten noted that conducting fewer audits could mean that patterns of errors might be missed and that opportunities to educate other campuses would be missed.

Trustee McElroy stated that the committee would have to consider whether to retain independent auditors or to add internal resources to conduct internal control and compliance audits. He noted that another option would be to conduct financial statement audits at the smaller colleges. Trustee McElroy further noted that some of the smaller colleges had fairly significant budgets. Trustee Van Houten added that some of the errors identified in the external audits had taken place more frequently at the smaller college because they had smaller staffs overseeing financial operations and student aid.

Trustee Vekich stated that when the recommendations about whether to use external or internal audit resources were brought before the committee, it would be important to have an understanding of the costs. He added there was a permanent cost to adding headcount as compared to external audits.

Ms. King stated that when the original audit approach was developed, there had been an intentional split strategy to use external auditors to do financial statements for the institutions that as a group represented sixty percent of the total revenue. It was decided to contract with the Office of the Legislative Auditor to conduct internal control and compliance work at the smaller colleges. Ms. King noted that in combination there would be satisfaction on the financial statement level where there was material risk and there would also be a stream of information about the environment that could be used from year to year to build up the skills and capacity of all of the colleges and universities.

Trustee Van Houten noted that the Office of the Legislative Auditor had been critical of the system's oversight particularly on some of the technology issues. He suggested that reducing the system level costs by reducing the number of audits might appear to be even less system oversight. He stated that it was important that the committee's decision did not appear to reduce the financial control oversight of the system.

Ms. King commented that Office of the Legislative Auditor's report had given high marks for the financial management environment. She noted that there was satisfaction with the Board's posture on financial management, praise for Board's commitment to the audit environment, and high marks from the campuses about the relationship between the campus financial management community and the system office. Trustee Van Houten thanked her for that reminder.

Trustee Vekich reiterated his desire to see a risk assessment prior to any decision to continue or expand on the current audit approach. Ms. Buse assured the committee that the internal auditing standards required that a risk assessment be part of any audit approach and in building an audit plan. She stated that she would discuss a risk assessment with the committee in more detail in the future.

Trustee Van Houten asked if there had been a resolution with the Office of the Legislative Auditor regarding the minimum levels of internal control and compliance audit coverage. Ms. King stated that a resolution had not been reached but that both parties had benefited from an exchange of views. She noted that there may not be an agreement in the end. Trustee Van Houten pointed out that there had been a lot of discussion and thinking that had taking place within the finance department and the Office of Internal Auditing as a result of the discussion with the Office of the Legislative Auditor,

Trustee Van Houten stated that the Audit Committee had a very complicated set of issues to debate and review in the coming months. As the committee begins the busy season of financial statement reviews, Trustee Van Houten reiterated that he felt it was important for the members to have an understanding of what had gone on before, and what the committee would be trying to replace or reproduce.

Trustee Krinkie asked if the Office of the Legislative Auditor would still be conducting audits of the colleges and universities, despite the lack of a contract with the Minnesota State Colleges and Universities. Ms. Buse confirmed that the Office of the Legislative Auditor had the authority and discretion to audit any part of state government. But she noted at this time, she was not aware of any planned new audits by the Office of the Legislative Auditor.

Trustee Van Houten noted that further program evaluations would be conducted at the direction of the Legislative Audit Commission. Ms. Buse agreed and stated that the Government Relations staff would know when there were further discussions by the commission about additional studies or audits. She noted that if the Office of the Legislative Auditor planned to conduct additional financial and compliance audits, the system would receive a notification letter in advance of when they planned to conduct the audit work

## **2. Selection of Committee Priorities (Action Item)**

Trustee Van Houten explained that expectation was that the committee would select goals from the list of committee priorities that had be printed in the Board packet or some other priority that would be brought up by the committee. He further noted that it would be important for the committee to define a timeframe for each goal as well. Trustee Thiss added that the object for the committee should be to choose an issue that was strategic and was reflective of the committee's priority for the year.

Ms. Buse reviewed the Audit Committee issues and goals that had been previously identified. She noted that the first four items all related to clearing past audit findings. As part of its normal work plan, the Office of Internal Auditing would be following up on audit findings and working to clear past findings. She further noted that Chancellor McCormick had given specific emphasis in his work plan that all outstanding auditing findings be resolved prior to arrival of a new Chancellor. Trustee Van Houten agreed and added that the issue of credit card policy recommendations might be one that could be referred to the Finance Committee for discussion of an appropriate credit card policy, but the Audit Committee might have an oversight role.

Ms. King agreed that many of the issues were in the process of being resolved. She stated that the Office of Internal Auditing would be following-up on the outstanding audit findings. She assured the committee that the commitment from the Chancellor's Office to resolve the Office of the Legislative Auditor findings was in place and reliable. There had been a lot of management time spent on the ISRS security issue and there would be more attention during the new audit season. She agreed that the credit card policy discussion should be referred to the Finance Committee, but added that she would want to return to the Audit Committee with an update.

Trustee Van Houten suggested that if the first four items were currently being reviewed by staff already, then the committee might focus on the final two potential goal areas.

Ms. Buse stated that the Audit Committee would need to discuss an internal controls and compliance approach going forward and make decisions about the thirteen college and university financial statement audits. She added that the system has had limited coverage related to information technology auditing and it would be important to develop that strategic approach in order to give the appropriate independent assurance to the Board.

Ms. King stated that the Audit Committee would be having discussions over the next ninety days about how to proceed with the thirteen certified audits. She further added that the committee could bring good value in helping work through the Information Technology audit strategy.

Trustee Van Houten asked if an analysis in terms of a strategic approach to risk assessment and internal controls, as Trustee Vekich had suggested, would be appropriate to addressing the thirteen audits and the Information Technology audit.

Trustee Renier stated that a worthwhile goal for the committee would be to do a thorough and complete evaluation of the audit approach, including the strategic Information Technology approach, the use of external auditors, the relationship with the Office of the Legislative Auditor and risk assessment. He stated that the objective would be to look at the whole approach which would take into account the system's responsibility, the public's expectations, and current budget constraints.

Ms. Buse agreed that an overall assessment of the audit approach would encompass the decisions that needed to be made about the thirteen financial statement audits and the Information Technology audit as well as the internal controls and compliance aspect.

Trustee Van Houten agreed and asked if the Information Technology strategic audit approach might need to be resolved in a different way, as part of another project. Ms. Buse stated that the system was not in compliance with the auditing standards as they related to Information Technology audit because of the changes that had taken place in the past several years related to that coverage. She stated that it would be necessary to include Information Technology as part of the conversation.

Trustee Thiss stated that he thought the Audit Committee goal was a kind of strategic risk assessment and then to develop a process for future years. He stated that the first year might be a transition year, and then there would be a process in place going forward. He noted that there were a lot of subset topics that needed to be addressed.

Trustee Renier stated that he would like to see staff come back in subsequent meetings to present a plan and timetable for the overall assessment of the audit approach. He noted that some of the issues needed to be resolved sooner than others.

Trustee Vekich suggested that staff come back with a framework as to how they would approach the assessment so that everyone would have a clear understanding of the audit approach with clear expectations, and some understanding of the best practices around the issues.

Ms. King suggested that because there were issues that needed to move more quickly than others, it might be helpful to return to the committee in September with a beginning scoping document that outlines the components of a risk assessment, the evaluation method and the proposed timetable. She noted that there were some decisions that would have to be made in January, but she added that Board Chair recognized that this was a year long committee work plan.

Ms. King stated that a matrix could be built that outlined the elements of a risk assessment that would include financial aid administration, property and casualty liability insurance, student conduct, and other issues that would speak to the organization's vulnerabilities.

Trustee Van Houten stated that the Office of Internal Auditing would like to participate in the system level budgeting strategies but that it would be impossible to draw budget assumptions until the committee had worked through some of the audit strategy issues.

*Trustee Vekich made the motion, Trustee Renier seconded. The Audit Committee recommends the following motion:*

*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.*

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- *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.*
3. Discussion of Office of Internal Auditing Issues and Priorities for Next Budget (Information Item)

Ms. Buse noted that the committee had discussed this agenda topic as part of the previous agenda discussion.

4. Status of the Office of the Legislative Auditor's Program Evaluation Findings (Information Item)

Ms. Buse presented the updated status report on the progress toward addressing issues cited in the February 2010 Office of the Legislative Auditor report. She noted that some progress had been made during the month but she suggested that the committee focus its discussion on the two areas that were still listed as red and would require additional work.

Trustee Thiss asked if all cabinet members had received the status report and if there was work taking place on the yellow items. Ms. Buse assured the committee that Cabinet members had received the status report. She stated that issues shown as green were already complete, those that were yellow were in progress and on track.

Trustee Van Houten stated that the Chancellor's expectation was that everything on the list would be substantially completed or have a specific plan in place by December in preparation for when the Legislative Audit Commission would meet next calendar year.

Trustee Frederick noted that there were a number of issues which had changed to green over the last month and he complimented that effort, but he also noted that two issues were still red from the previous month.

Ms. King stated that the efficiency and effectiveness project had been started, but that it was not yet in a position to put a resource estimate on it, and so the internal process to seek resources had not yet begun. She noted that there had been a presentation at the Finance Committee in March and April. There had been ongoing workgroup discussions with campus administrators and system office administrators. Ms. King stated that the efficiency and effectiveness project would be at least as expensive as the Students First Initiative, and at least as resource intensive. She stated that she hoped to have an understanding of the strategy by January. Ms. King stated that there had been some work done regarding the contracts issue, but more work needed to be done to move that project along.

Trustee Thiss asked if the deliverable for the efficiency and effectiveness project was a strategy or a plan. Ms. King stated that the Board had approved the strategy back in April. She stated that the eventual deliverable in the project would be a year to two years away because it would require technology, re-engineering, and campus practice changes.



Ms. Buse stated that she planned to bring another updated status report to the Board in September. Trustee Van Houten reminded members that the Audit Committee's responsibility to the Office of the Legislative Auditor was to provide oversight to ensure that the issues were addressed. He added that Vice Chair Hightower would be instrumental in coordinating the effort and would need to be kept informed of the progress.

Trustee Van Houten reviewed the committee work schedule for the next several months. He noted that at the September meeting, the committee would review the results of the five smaller college audits done by Office of the Legislative Auditor. Ms. Buse explained that members would receive an advanced copy of that audit the day before the committee meeting and that representatives from the Office of the Legislative Auditor would present the material and highlight items that were of Board significance.

Trustee Van Houten added that there would also be a sixth campus audit that had been done by the Office of Internal Auditing. Ms. Buse explained that St. Cloud Technical and Community College would have been up for an audit under the three-year rotation but because of the limited resources within in the Office of the Legislative Auditor they were not able to do that audit. She stated that results of that audit would be available in September as well. Trustee Van Houten noted that the work done by the Office of Internal Auditing on the St. Cloud Technical and Community College would provide good insight into the time commitment and implications into replacing the internal control and compliance services that had been provided by the Office of the Legislative Auditor. Ms. Buse agreed and stated that the staff had approached the audit in that manner to understand the kind of efficiencies that could be added using the same audit approach.

Trustee Van Houten stated that an audit plan would also be presented to the committee in September. Ms. Buse stated that approval of an annual audit plan was a requirement under internal audit standards as well as in Board policy.

Trustee Van Houten stated that about a week or a week and a half before the November Audit Committee meeting the thirteen audits by the external auditors would be distributed to the committee members. He stated that in the past the committee had divided the reports up so that each committee member was responsible for reviewing half of the reports. The system level audit would be delivered to all committee members for review. He noted that if members had time, they could read all of the individual audit reports as well. But he noted that by dividing the report among the members, they ensured a deeper level of committee study and exposure and to each of the reports. Trustee Van Houten stated that there would be a fair amount of reading and preparation for the November meeting. He further noted that there would also be a status report of prior audit findings. Trustee Van Houten noted that there would not be much time for committee members to review the Office of the Legislative Auditor report in September. He asked if time should be allotted for committee discussion and questions at the November meeting. Ms. King stated that the Office of Internal Auditing would prepare an evaluation of the findings in the report, so the committee would have an instrument to assist them to quickly review significant findings, administrative findings, those findings that might

have system wide implications. She stated that members should be able to review that document at the September meeting.

5. Roles and Responsibilities of the Audit Committee (Information Item)

Ms. Buse reviewed the Board policies the related to the Audit Committee or to the Office of Internal Auditing. She explained that the Executive Director of Internal Auditing reported directly to the Board of Trustees through the Audit Committee, with an administrative relationship to the Chancellor. She further explained that the committee had the responsibility for overseeing the process of selecting external auditors.

Trustee Van Houten asked how the need to approve the recommendation to contract with external auditors fit into the strategic goal to review the audit approach over the coming year.

Ms. Buse stated the contracts that needed review in January were for the largest institutions and that the committee would need to decide whether to contract with an external audit firm for the fiscal year 2011 college and university audits which would occur next summer and fall. She stated that she would come back to the committee in January with an approach that would allow the committee to consider moving forward on this component of the audit plan framework.

Trustee Van Houten noted that the Audit Committee was not scheduled to meet between November and January. He further noted if the committee would need to move quickly on a recommendation to proceed with the contract process for fiscal year 2011 external audit coverage, members might need to consider the need for a special meeting in December.

Ms. Buse stated that she would develop a framework for the committee goal that was approved in the earlier agenda item. She added that she would build steps within the audit plan for the committee to discuss in September and that would determine the structure for the January meeting. Trustee Van Houten agreed and stated that the committee may have to agree that certain aspects of the proposed audit plan might have to be phased in more slowly. Ms. Buse agreed and stated that there may need to be a transition year because the implications of not auditing the largest institutions would have implications on the system wide audit contract. She stated that she would document those implications and that the impact would affect other things that would have to occur.

Ms. Buse finished her review of the Board policies that relate to the audit function. She noted that the Audit Committee review and discuss the results of each audit engagement with the independent auditor and management prior to recommending that the Board release the audited financial statements. She reviewed the responsibilities of the Office of Internal Auditing in conducting and working with colleges and university presidents and the Chancellor on fraud investigations. She noted that it was time for the required five-year review of Policy 1D.1 Office of Internal Auditing, and that there were some proposed amendments that the committee would need consider in the next calendar year.

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Finally, Ms. Buse noted that there was a checklist in the Board packet for the committee to review and consider as they prepared to review the draft financial statements in November. She noted that Vice Chancellor King's staff would also prepare a one-page highlight for each report to summarize the information in the draft financial statements.

Trustee Van Houten thanked Ms. Buse for her presentation. He noted that the Audit Committee had a very busy schedule for the next several months. He reminded members that they should plan to approach the financial statements by reading the highlights and footnotes first. He encouraged committee members to contact Ms. Beth Buse or Ms. Laura King with any questions as they began their review.

The meeting adjourned at 9:47 a.m.

Respectfully submitted,  
Darla Senn, Recorder