

Minnesota
STATE COLLEGES
& UNIVERSITIES

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Date: August 6, 2004

To: Chancellor McCormick

From: John Asmussen
Executive Director of Internal Auditing

Cc: Catherine McGlinch, Executive Director of Development
Linda Baer, Senior Vice Chancellor
Laura King, Vice Chancellor – CFO
Linda Kohl, Associate Vice Chancellor
Gail Olson, General Counsel
Christopher Halling, System Director for Student Financial Aid

Re: Alliss Grant Program

You asked me to review the Alliss Grant Program that is administered by the Office of the Chancellor. Our review focused on activities conducted by the Office of the Chancellor related to accounting and grant reporting to the donor organization. We examined financial activity from fiscal year 1999 through 2004 (as of August 6, 2004).

Methodology

For this review, we conducted the following activities:

- Reviewed grant award letters and other related information maintained by the Public Affairs Division. Background information on the grant program was prepared by the Public Affairs Division and is attached to this report.
- Traced financial data to the ISRS system and reviewed financial schedules with the Finance Division.
- Compared annual financial activity with grant stipulations to ensure compliance.
- Discussed preliminary findings and recommendations with representatives from the Public Affairs Division (Linda Kohl, Peg Boots, and Joyce Petsch). Our discussion resulted in Peg Boots meeting with a representative of the Allis Foundation to discuss the potential issues identified in this review. She sent two letters to the foundation (copies are attached to this report) to clarify understandings about certain aspects of the program.
- Discussed final recommendations with Catherine McGlinch and Joyce Petsch. Ms. McGlinch has developed a corrective action plan that is attached to this report.

We did not test whether our institutions are providing Alliss grants to only eligible recipients. The Office of the Chancellor, however, pulls data on Alliss grant recipients directly from the ISRS system and does not rely on institutions to self report. Also, the Public Affairs Division provides guidance to institutions on awarding these grants. Those activities diminish, but do not eliminate, the risk of awarding grants to ineligible students.

Conclusions

The Office of the Chancellor administers two distinct Alliss grant programs: one for state university students and the other for community college students. The grant requirements for the two programs are very different, so we cite separate conclusions for each program.

State University Program

For the six fiscal years from 1999 to 2004, a total of \$4.6 million in Alliss grant funds and related interest earnings were disbursed to the seven state universities. The Office of the Chancellor has administered this program in compliance with the requirements of the donor.

The State University program, as shown in Appendix I, has a significant carryover amount at the end of each fiscal year. This carryover occurs, however, because grant funds received from the donor are not available for expenditure until the next fiscal year. We found that the program consistently disbursed at least 97% of available funding to the state universities for student grants. Any residual funding that carried forward was due to unspent interest income earned during the year.

Community College Program

For the six fiscal years from 1999 to 2004, community college students have been awarded \$3.1 million as a result of the Alliss grant program. The system contributed \$1.8 million of its own funds to the \$1.3 million of Alliss funding spent during that five-year period.

The Office of the Chancellor has created three separate cost centers for managing the program: (1) the grant proceeds are deposited into an Alliss Grant account entitled "CC Book Reimbursement Account", (2) the system commitment has been recorded in an account entitled "CC Matching State Appropriation", and (3) investment earnings accrued on unspent grant proceeds have been recorded in an account entitled "CC Alliss Investment Account". Appendix II shows the financial activity in the three cost centers. The Appendix also combines these three accounts in a community college summary.

1. The Office of the Chancellor inadvertently accumulated a significant carryover balance in accounts related to the Community College Alliss Grant program

As shown in the Table 1, the Office of the Chancellor accumulated over \$900,000 in accounts related to the Community College Alliss grant program by fiscal year 2001. This accumulation occurred because the grant funds were not actively managed. A simple, passive method was used to distribute program costs between grant funds and supplemental funding that the system pledged from state appropriations¹ – book charges were paid from the grant funds and tuition costs were paid from the state appropriation. This

¹ The community college program, unlike the state university program, commits system funding to augment the Alliss donation each year. The supplemental system funding comes from state appropriations.

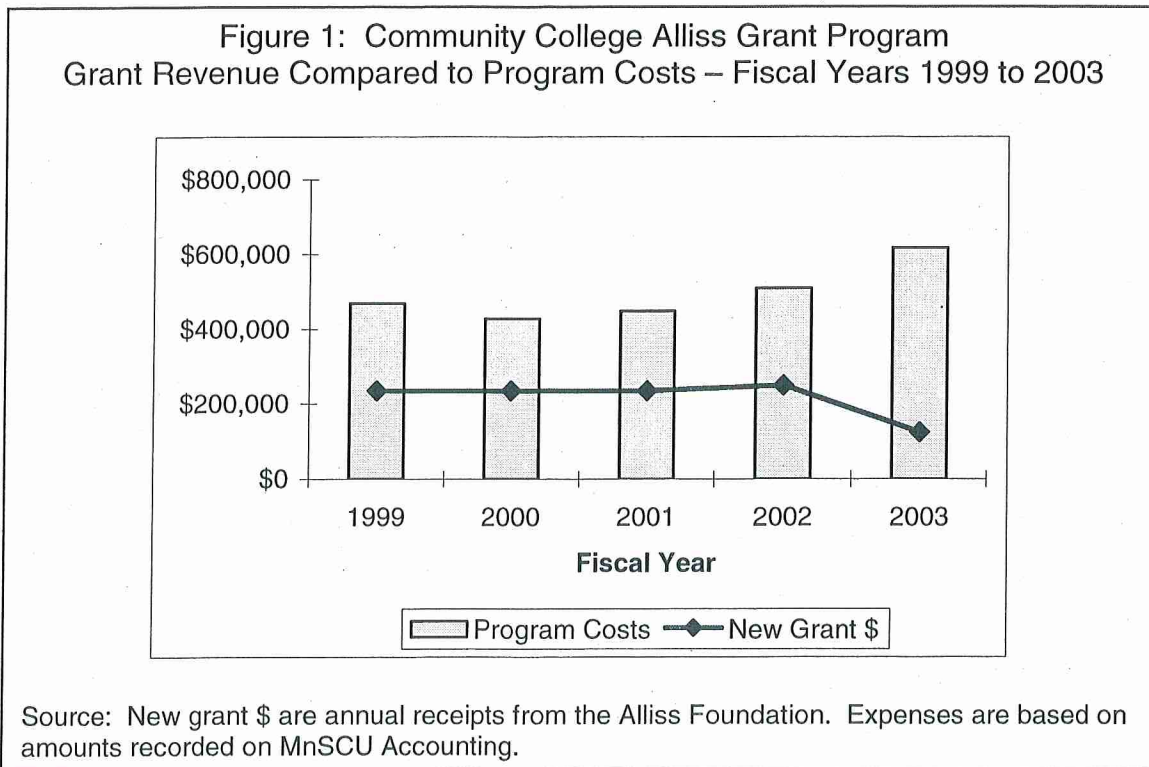
method, though, resulted in a disproportionate share of program costs being charged to the state appropriation. Unused grant funds were invested and further accumulated.

Table 1: Distribution of Alliss Program Costs Compared to Funding Sources
Fiscal Years 1999 to 2004

Fiscal Year	Amount Pledged from the State Appropriation	Grant Amount Received	Total Program Costs: Tuition & Book Charges	Year End Carryover: Grant & Investment Accounts
1999	700,000	235,000	469,535	539,989
2000	500,000	235,000	427,839	722,522
2001	500,000	235,000	448,161	924,665
2002	500,000	250,000	508,741	902,421
2003	500,000	125,000	616,568	429,280
2004 (as of 8/6)	500,000	125,000	609,494	388,884

The Alliss grant applications submitted by the Office of the Chancellor have consistently stated that the grant funds could be used *“to purchase books, with any remaining amounts being applied to tuition.”* Through fiscal year 2001, however, only book purchases were charged against the grant funds and only tuition fees were charged against the state appropriation. Because the book purchases were substantially less than the new grant funds awarded each year, the balance in the grant account grew significantly. Unused funds in the state appropriations account did not carryover at year end, however, and were returned to the Office of the Chancellor fund balance.

Because the total program costs easily surpassed the amount of new Alliss grant funds each year (see Figure 1), the accumulated balance in the grant account was almost inexplicable.



It created the appearance that new monies were being sought while a large, unspent balance continued to accumulate. When the Public Affairs Division assumed responsibility for managing the program, it

became concerned about the accumulated grant balance. After consulting with the Vice Chancellor – CFO in fiscal year 2002, it was decided that both tuition and books would be charged against the grant account and nothing charged to the state appropriation fiscal year 2003. Accordingly the amount carrying over to fiscal year 2004 was reduced to \$429,280 (\$255,771 in the grant account and \$173,509 of accumulated investment earnings).

In fiscal year 2004, as of August 6, 2004, the grant account continued to show a healthy balance of \$212,416 and the state appropriation account had been spent down to \$8,860. The Office of the Chancellor could consider transferring additional tuition charges against the grant account in fiscal year 2004 to further diminish the balance that has accumulated in the grant account.

The accumulated interest balance of \$176,468 (as of August 6, 2004) poses a different problem. Neither the Alliss Grant application nor the award letter addressed how any related investment income was to be spent. By 2001, \$165,000 had accumulated in the investment earnings account. The former system Development Director Peggy Boots told us that she had an understanding with the Alliss foundation representatives that the investment earnings could be used to promote the Alliss Grant program. As a result, \$3,894 was spent in fiscal year 2001 on printing the “Believe It” brochures for marketing the program. In fiscal year 2002, about \$42,000 of the accumulated investment earnings were spent on a consulting contract with Market Models, Inc. The contract was intended to generate reliable alumni lists for system institutions and had only a remote connection to the Alliss grant program. This effort was connected to the Alliss program by attributing it as the funding source and encouraging it as an educational opportunity for qualified recipients. Only a small amount of the accumulated investment earnings have been spent past two years, so that balance has grown to \$176,468.

In an attempt to clarify how the accumulated investment earnings may be spent, former system Development Director Peggy Boots met with the executive director of the Alliss foundation, Joth Blodgett, in March 2004. She submitted a letter dated, March 24, 2004, to Mr. Blodgett that recapped their discussion. Regarding the interest earnings, she wrote:

We were in agreement that the interest earned on the community college grant funds is to be used for marketing the community college Alliss Foundation program and issues consistent with the program. We both agreed to check our past grants to see exactly when that commitment was originally made. Joth, one thought for future discussion: as the program becomes more and more popular, could we consider using interest funds not needed for marketing to cover regular grants?

The system development office is attempting to schedule a follow-up meeting with Mr. Joth to reach a final determination on the use of the investment earnings.

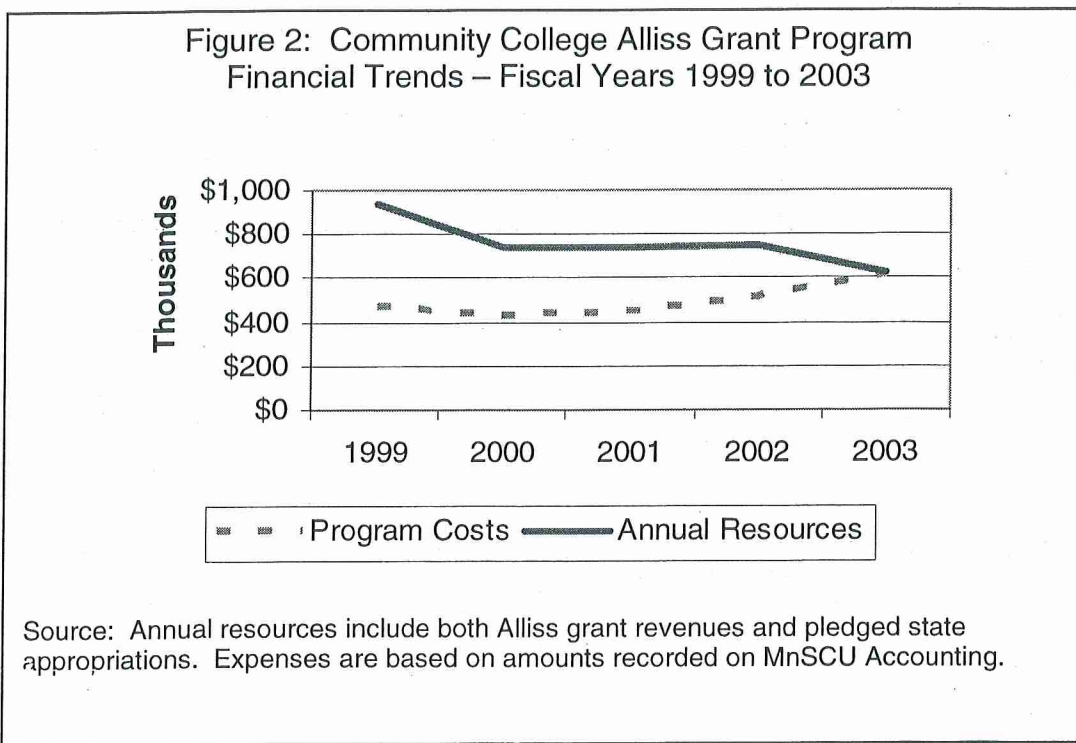
Recommendation

- *The Office of the Chancellor should consider using the balance remaining in the Alliss grant account to pay for the recipients' books and tuition fees before using state appropriations.*
- *The Executive Director of Development should consult with the Vice Chancellor – CFO on whether to record an adjusting to expense additional tuition payments against the grant account rather than the state appropriation in fiscal year 2004.*
- *Reach a clear understanding with the Alliss Foundation on the allowable use of the investment income earned on the unused grant funds.*

2. **The growth in the Alliss grant program is rapidly approaching the limit of available resources for the program. The system may exceed available resources without detection and has no plan on how to respond if demand exceeds resources.**

The accumulated grant funds discussed in Finding 1 are masking the system's ability to monitor whether the demand for system resources exceeds the amount pledged. While the accumulated grant funds were being spent down in fiscal year 2003, the Finance Division did not record the \$500,000 system commitment as a matching state appropriation. In fiscal year 2004, the system has only recorded \$450,000 of state appropriations committed to this program, despite pledging \$500,000 to the foundation².

In recent years, the combination of increased marketing efforts and higher tuition rates has increased the Alliss grant program costs significantly in recent years. At the same time, the Alliss foundation cut its donation in half. Thus, as shown in Figure 2, the program expenditures nearly equalled the annual amount pledged for the program in fiscal year 2003. In fiscal year 2004, the program costs are approaching the annual amount pledged.



The Office of the Chancellor should reconsider whether it wishes to continue to pledge significant funding to a program that garners a shrinking amount of grant funds and is narrowly constructed to benefit only community college students. The Alliss foundation will not permit funds to be used for technical college programs and no system funds are required to match the Alliss contribution for state university students. Committing \$500,000 of system funds in order to collect \$125,000 of grant funds needs to be reevaluated. Also, the \$500,000 pledge was made when applying for \$250,000 of grant funds. When the system only received \$125,000 in grant funds, it did not approach the Alliss foundation about reducing the system pledge.

² This reduction was consistent with the 10% budget cut imposed on all Office of the Chancellor accounts in fiscal year 2003. However, the Office of the Chancellor did not have unilateral authority to reduce its commitment without gaining agreement from the donor.

Reducing the system's financial commitment to the program must be considered carefully, however. The marketing efforts have created a demand that relies on that level of funding. The community colleges also expect to be reimbursed for all Alliss scholarships that they award. So, any change in that practice must be communicated to the colleges well in advance.

Recommendations

- *State appropriations pledged to support the Alliss program should be recorded fully on the accounting system and used as a budgetary control.*
- *A contingency plan should be adopted so that appropriate action may be taken if demand for Alliss grants exceeds available resources. Either community colleges need to receive an early warning that Alliss funds may be exhausted or to additional resources must be designated to fund any shortage.*
- *The value of committing \$500,000 in system funding to receive \$125,000 in grant funds should be reevaluated.*

APPENDIX I
Alliss Grant Program - State Universities
Fiscal Year 1999 - 2004

	Fiscal Year					
	1999	2000	2001	2002	2003	2004 (as of 8/6)
STATE UNIVERSITY ACCOUNT						
Balance Forward In Revenues	609,838.72	677,945.52	781,360.14	864,066.11	880,947.29	740,055.57
Investment Income	27,257.14	33,854.62	38,051.26	23,588.24	15,046.16	7,774.93
Total Available Resources	637,095.86	711,800.14	819,411.40	887,654.35	895,993.45	747,830.50
Expenses						
Allocation to State Universities	(620,590.34)	(689,440.00)	(797,345.29)	(867,990.06)	(887,158.88)	(743,639.36)
Balance Forward Out						
Unrestricted Year-end Balance	16,505.52	22,360.14	22,066.11	19,664.29	8,834.57	4,191.14
Alliss Grant Received for Next FY	661,440.00	759,000.00	842,000.00	861,283.00	731,221.00	725,056.00
Net Assets	677,945.52	781,360.14	864,066.11	880,947.29	740,055.57	729,247.14
% of Available \$ Spent	97%	97%	97%	98%	99%	99%

APPENDIX II
Alliss Grant Program - Community Colleges
Fiscal Years 1999 - 2003

	Fiscal Year					
	1999	2000	2001	2002	2003	2004 (as of 8/6)
CC Book Reimbursement Account						
Balance Forward In						
CC program	330,795.61	462,816.64	605,239.61	759,072.85	747,338.70	255,771.08
Revenues						
Alliss Grant for Current FY	235,000.00	235,000.00	235,000.00	250,000.00	125,000.00	125,000.00
Total Available Resources	565,795.61	697,816.64	840,239.61	1,009,072.85	872,338.70	380,771.08
Expenses						
Book Reimbursements	(102,978.97)	(92,577.03)	(81,166.76)	(106,512.81)	(116,553.20)	(168,354.71)
Tuition Reimbursements				(155,221.34)	(500,014.42)	
Balance Forward Out						
Unrestricted Year-end Balance	462,816.64	605,239.61	759,072.85	747,338.70	255,771.08	212,416.37
Alliss Grant Received for Next FY	-	-	-	-	-	-
Net Assets	462,816.64	605,239.61	759,072.85	747,338.70	255,771.08	212,416.37
CC Alliss Investment Account						
Balance Forward In						
CC Investment Account	48,487.96	76,172.51	117,282.64	165,592.00	155,082.38	173,509.04
Revenues						
Investment Income	27,684.55	41,110.13	52,203.36	31,593.51	18,426.66	5,073.27
Total Available Resources	76,172.51	117,282.64	169,486.00	197,185.51	173,509.04	178,582.31
Expenses						
Misc. Expenses	-	-	(3,894.00)	(42,103.13)	-	(2,114.00)
Balance Forward Out	76,172.51	117,282.64	165,592.00	155,082.38	173,509.04	176,468.31
CC Matching State Appropriation						
Balance Forward In	-	-	-	-	-	-
Revenues						
State Approp Committed	700,000.00	500,000.00	500,000.00	500,000.00	500,000.00	500,000.00
Total Available Resources	700,000.00	500,000.00	500,000.00	500,000.00	500,000.00	500,000.00
Expenses						
CC Tuition Reimbursements	(366,555.61)	(335,262.24)	(366,994.52)	(247,006.62)	-	(441,139.32)
Less: Cancelled Appropriation	(333,444.39)	(164,737.76)	(133,005.48)	(252,993.38)	(500,000.00)	(50,000.00)
Balance Forward Out	-	-	-	-	-	8,860.68
Combined CC Accounts						
Balances Forward In	379,283.57	538,989.15	722,522.25	924,664.85	902,421.08	429,280.12
Revenues						
Alliss Grants - Current Year	235,000.00	235,000.00	235,000.00	250,000.00	125,000.00	125,000.00
Investment Income	27,684.55	41,110.13	52,203.36	31,593.51	18,426.66	5,073.27
State Appropriations Pledged	700,000.00	500,000.00	500,000.00	500,000.00	500,000.00	500,000.00
State Appropriation Cancelled	(333,444.39)	(164,737.76)	(133,005.48)	(252,993.38)	(500,000.00)	(50,000.00)
Total Available Resources	1,008,523.73	1,150,361.52	1,376,720.13	1,453,264.98	1,045,847.74	1,009,353.39
Expenses						
Book Reimbursements - CC	(102,978.97)	(92,577.03)	(81,166.76)	(106,512.81)	(116,553.20)	(168,354.71)
Tuition - CC	(366,555.61)	(335,262.24)	(366,994.52)	(402,227.96)	(500,014.42)	(441,139.32)
Misc	-	-	(3,894.00)	(42,103.13)	-	(2,114.00)
Balance Forward Out						
Unrestricted Year-end Balance	538,989.15	722,522.25	924,664.85	902,421.08	429,280.12	397,745.36
Alliss Grant Received for Next FY	-	-	-	-	-	-
Net Assets	538,989.15	722,522.25	924,664.85	902,421.08	429,280.12	397,745.36

(1) I cannot find the \$255,771.08 carryover amount recorded on ISRS.

(2) Although a \$500,000 pledge was committed to Alliss for fiscal year 2004, the amount was reduced by 10% for across-the-board budget cutbacks. The propriety of this reduction is questionable because it was not agreed to by the Alliss Foundation.

(3) Approximately \$162,000 of tuition reimbursements have not been paid yet in fiscal year 2004.

Memorandum

Date: June 2, 2004

To: John Asmussen

From: Catherine McGlinch

Re: Allis Grant Program

CC: Joyce Petsch

John,

Thanks so much for your efforts to discern the current situation with the Alliss Grant Program, specifically with the issues that have developed within the Community College Program. I appreciate the recommendations you have made to keep the program strong and in compliance with the gift agreement and our internal operations.

Based on your recommendations, I'll undertake the following action steps to rectify the areas within my control:

- 1) Initiate conversation with Laura King and her staff to clarify interpretation of usage of funds and next steps of how to use remaining funds.
- 2) Initiate a conversation with Chris Halling as a means to talk with financial aid officers from throughout the system in preparing for making a recommendation to the Alliss Foundation for
 - a. possibly re-defining the program
 - b. discussing ways to best place a cap on campuses as funds may otherwise be exhausted for the program
 - c. begin to create an awareness that funds for this program are limited and declining.
- 3) Initiate a conversation with Joth Blodgett at the Alliss Foundation to accomplish several things
 - a. Reach a clear understanding of the allowable use of investment income earned on the unused grant funds
 - b. Discuss the value of the system continuing to commit nearly \$500,000 when the Alliss match has decreased to \$125,000
 - c. Discuss how the program might be re-defined to reach a more strategic target population of students.