This page intentionally left blank.
Members of the Board of Trustees

I am pleased to submit the annual report on the Office of Internal Auditing for fiscal year 2015 as required by Board Policy 1D.1 part 8.

This report summarizes the activities accomplished and facilitated by Internal Auditing over the past year. I am proud of the work that the office has accomplished in the past year. The office conducts audits in conformance with International Standards for the Professional Practice of Internal Auditing.

I wish to reiterate my commitment to help manage 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. All internal audit staff, including myself, take great care to avoid assignments or relationships that would compromise our independence. I pledge to you that I will continue to remain independent and objective in my role as Deputy Director of the office.

Thank you for your continued support.

Eric Wion, CPA, CISA, CISSP
Deputy Director

Contents
2 Overview and Assurance Services
7 Fraud Inquiry & Investigation Support
8 Advisory Services
8 Planning
8 Staffing
10 The Future
11 Appendix A – Annual Required Communication

Summary
The audit plan approved by the Board of Trustees in June 2014 provided the foundation for the internal auditing activities carried out over the past year. Some noteworthy activities included:

- **Internal Control and Compliance Audits**
  - Grant Management
  - Minneapolis Community and Technical College
  - Dakota County Technical College
  - Clery Act

- **Special Review**
  - Metropolitan State University Personnel and Payroll

- **Information Technology Audit:**
  - CAP Servers

- **External Audits**
  - Financial Statements - CliftonLarsonAllen gave unmodified (clean) financial statement audit opinions for the system, revenue fund, and four universities for fiscal year 2014.
  - Student Financial Aid – the system contracts with CliftonLarsonAllen to complete required audit work on federal financial aid. The Minnesota Office of Higher Education completes compliance audits of state aid programs.

- **Follow-up:** Colleges and universities and the system office continued to make progress in resolving outstanding audit findings.

- **Inquiries and Investigation:** Internal Auditing continues to spend a significant amount of time in conducting fraud inquiries and investigations. Fortunately, there were no significant losses.
Office overview

The Office of Internal Auditing (OIA) is an independent and objective assurance and advisory function designed to add value and improve MnSCU operations. OIA assists the organization in accomplishing its objectives by bringing a systematic and disciplined approach to evaluate and improve the effectiveness of the organization’s governance, risk management, and control processes. Internal auditing also focuses on raising awareness of risks and controls, providing advice to management in developing internal control solutions, and monitoring the implementation of management’s corrective actions to mitigate risks and strengthen controls.

Audit Projects

OIA spent the majority of its time working on assurance services, which depending on the scope of the audit, may focus on internal controls, the quality and reliability of information, legal compliance, and operational efficiency and effectiveness. The following assurance service projects were conducted during fiscal year 2015.

Financial Internal Control and Compliance Audits

The following audits were completed and discussed with the Audit Committee:

- **Grant Management:** In March 2015, Internal Auditing released an internal control and compliance audit report on grants management.

  Colleges, universities, and the system office apply for and receive a variety of grants, including state, federal, and private grants. In fiscal year 2014 grant revenues, excluding student financial aid, totaled nearly $95 million. Grant requirements vary by the type of grant received. Specifically, federal grant compliance requirements are more uniform, numerous and complex, state grants have some uniform compliance requirements, and private grants requirements are based on the individual grantor. Most institutions did not have dedicated resources (grant office or grant accountant) focused on the management of grants.

  The report contained five findings:

  - There was minimal guidance addressing grant management practices.
  - Some institutions did not have procedures to ensure they complied with time and effort requirements for federal grants.
  - Some institutions did not have procedures to ensure they complied with federal conflict of interest requirements.
  - Some grant agreements were not reviewed by general counsel prior to contract execution and two grants exceeding $3 million were not approved by the Board.
  - Delegations of authority were not always in place for those that applied for and signed grant agreements.

  **Considerations for System Leaders**

  College, university, and system office leaders should consider alternative models for managing grants.
• **Minneapolis Community and Technical College:** In April 2015, Internal Auditing released an internal control and compliance audit of Minneapolis Community and Technical College.

The audit scope included receipts (tuition, fees, parking and bookstore), employee business expenses, purchases, disbursements, equipment inventory, personnel and payroll expenses, and bookstore inventory balances.

Our audit concluded that the college generally had adequate internal controls and for items tested, generally complied with MnSCU policies and finance-related legal provisions. The report contained seven findings.

- The college had errors that resulted in three faculty members being overpaid and other errors that did not impact pay.
- The college needs to improve its processes over staff and faculty leave.
- The college did not have some controls to ensure receipts were safeguarded in the business office, bookstore, and parking ramp operation.
- The college did not have a process to review waivers for accuracy.
- The college did not adequately manage its asset inventory records.
- The college did not obtain proper approval for two purchases that exceeded $100,000.
- Computer access was not removed timely for two employees who left the college.

• **Dakota County Technical College:** In September 2015, Internal Auditing released an internal control and compliance audit of Dakota County Technical College.

The audit scope included receipts (tuition, fees, parking and bookstore), employee business expenses, purchases, disbursements, equipment inventory, personnel and payroll expenses, and key financial reconciliations.

Our audit concluded that except for bookstore operations, the college generally had adequate internal controls and for items tested, generally complied with MnSCU policies and finance-related legal provisions. The report contained seven findings.

- The bookstore had significant internal control deficiencies and the college lacked adequate oversight of its bookstore operations. A fraud was discovered during the audit that resulted in the theft of some bookstore receipts.
- The college had payroll-related errors including some that affected some employee’s pay.
- The college had errors that resulted in some inaccurate employee leave balances.
- The college did not adequately manage its equipment inventory records.
- The college used backdated drops rather than waiver transactions to waive tuition and fees for some students.
- The college did not routinely perform and document controls to mitigate the risks with several employees having incompatible ISRS access. In addition, system access was not always removed timely when it was no longer needed.
- The business office’s cashiering area lacked some physical controls and customized training receipts collected at the college’s Eagan location were not sent to the business office and deposited timely.
Operational or Compliance Audits

**Clery Act:** In September 2015, Internal Auditing released an internal control and compliance audit of the Clery Act.

Participation in federal student financial aid programs requires colleges and universities to comply with the Clery Act, a federal law that requires colleges and universities to disclose information about crime on and around their campuses.

The audit concluded that: colleges and universities were aware of Clery Act requirements, fully understood the importance of complying with the requirements, and had procedures in place to collect and report crime data. The report contained six findings:

- Six institutions did not properly identify Clery geography for campus and non-campus sites and 10 institutions may not have obtained crime data from some law enforcement agencies.
- Some institutions did not provide training to new campus security authorities (CSAs) or refresher training to remind CSAs of their responsibilities and one institution did not properly identify all CSAs.
- Five institutions did not properly maintain and allow access to crime or fire logs.
- Four institutions did not address new requirements related to Violence Against Women Reauthorization Act (VAWA) legislation.
- Nine annual security reports were missing required policy statements or other required information.
- Seven institutions did not provide sufficient notification about the availability of the report to students and employees.

**Considerations for System Leaders**

College, university, and system leaders should consider how the Clery Act support team can help institutions address audit findings and assist with compliance.
Special Reviews

Metropolitan State University Personnel and Payroll: In January 2015, Internal Auditing released a special review of pay issues that occurred at Metropolitan State University.

In early September 2013, the Inter Faculty Organization (IFO) informed Minnesota State College and University leadership and the Board of Trustees that serious problems existed in the accuracy and timeliness of pay to faculty at Metropolitan State University for summer and fall 2013 terms. Shortly after system leaders were informed of the issues, a number of critical newspaper articles were published on the pay issues. In response to the concerns, an external review team composed of human resource professionals conducted a line-by-line review of faculty payroll-related transactions for fiscal years 2012, 2013 and 2014 (to date), including sick leave accrual, insurance premiums, and pension contributions. In addition, the chancellor and board leadership requested Internal Audit conduct a review of the issues at Metropolitan State University and the work completed by the external review team.

The results of the special review found that:

- The university sustained significant turnover and the system lacked formalized strategies and resources to provide sufficient oversight to respond to it.
- The process for paying faculty is overly complex and system office and college and university leaders need to look for opportunities to simplify.
- Unique practices at Metropolitan contributed to pay errors.
- Metropolitan’s paper-based process for authorizing faculty pay needs improvement.
- Three areas of the external review team had not been completed; leave accrual review, insurance premiums, and pension coding.
- Internal audits testing approach found some additional pay errors.

Long-Term Considerations for System Leaders

- The system office should evaluate moving to one personnel and payroll system.
- System office and university leaders should look for opportunities to clarify and simplify provisions with the IFO Agreement.
- System office and university leaders should evaluate whether Metropolitan’s unique provisions with the IFO Agreement are still relevant given changes occurring within higher education and Charting the Future efforts.

Information Technology Audits

CAP Servers: In March 2015, Internal Auditing released an information technology audit of MnSCU CAP (Consolidated Access Point) servers. Each college, university, and the system office own and manage at least one CAP server that is allowed to connect to and query data in MnSCU’s enterprise database management system that houses ISRS data. ISRS Data is frequently copied and stored on individual college and university servers.

This audit focused primarily on internal controls that help to protect the confidentiality, integrity, and availability of these environments and data.
The report contained five findings and recommendations to improve security controls in current CAP environments. The report also discussed factors that system office, college, and university leaders should consider as they perform long term strategic IT planning.

**External Information Technology Security Assessment:** Internal Auditing contracted for four short information technology security assessments. The results of these assessments are being used to help guide the development of a security plan for the system.

**External Audit Activity**

Board policy requires internal auditing to coordinate all audit-related activities within MnSCU. The following audits were conducted by external auditors.

- **Systemwide, Revenue Fund, and College and University Financial Statements:** Audits of fiscal year 2014 financial statements marked the fourteenth year that MnSCU contracted for an external audit of its financial statements. The external audit firm of CliftonLarsonAllen provided an unqualified (clean) opinion on the systemwide, revenue fund, and four individual state universities’ financial statements in November 2014.\(^1\)

  CliftonLarsonAllen 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.”

- **Federal Student Financial Aid:** Federal law requires an annual audit of major federal programs. The Office of the Legislative Auditor identifies major federal programs for the State of Minnesota, including MnSCU. It identified student federal financial aid as the only major federal program for MnSCU in fiscal year 2014. CliftonLarsonAllen completed the audit work as part of its responsibilities as principal auditor for MnSCU. The audit concluded that MnSCU complied, in all material respects, with the compliance requirements over student financial aid. The report did include five minor compliance findings with questioned costs of $11,000.

  The results of CliftonLarsonAllen’s work were incorporated into the State of Minnesota’s Single Audit report that was released in March 2015.

- **State Student Financial Aid:** The Minnesota Office of Higher Education conducts regular program reviews of state paid financial aid administered by MnSCU colleges and universities. The results of fiscal year 2014 audits are similar to past year results and contained minor technical findings that are typically the result of manual calculation errors or incomplete information for determining program eligibility.

---

\(^1\) Bemidji State University, Metro State University, St. Cloud State University, and Winona State University each obtained an audit opinion of their standalone financial statements.
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 and monitors the status of both internal and external audit findings through resolution. OIA provides presidents an annual follow-up report that identifies outstanding audit findings and whether the college or university is making satisfactory progress in resolving each one. Colleges and universities continued to make significant progress on resolving outstanding audit findings during fiscal year 2014. As of June 30, 2014, there were 60 unresolved audit findings, all of which were in satisfactory progress.

Fraud Inquiry and Investigation Support

Internal Auditing assists colleges and universities with conducting fraud inquiries and investigations. The results of most fraud inquiries and investigations were reported to affected presidents 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.

Internal Auditing continues to spend more time on fraud incidents 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**: includes the theft of laptops, iPads, iPhones, and other information technology equipment. In most cases, colleges and universities report these incidents to local law enforcement.

- **Financial aid fraud**: Two-year colleges, primarily in the metro area, continue to deal with student financial aid fraud cases. Internal Auditing works closely with the Inspector General 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.

---

2 The Office of Internal Auditing concluded that colleges and universities were on track to resolving the findings timely.
Internal Auditing assisted with other inquiries and investigations primarily centering on allegations of employee misconduct or misuse of property. Internal Auditing reports internal control issues and recommendations to presidents and other administrators when noted and follows up on identified issues.

Advisory Services

The Institute of Internal Auditing allows internal auditors to provide advice and guidance to management through consulting or advisory services. These services can be invaluable to management when transforming an area to help ensure that appropriate risks and controls are built in up front rather than waiting until an assurance service engagement. In providing these services, it is important to note that management is responsible for decisions or actions that are taken because of the advice or guidance provided.

Specific areas that Internal Auditing was engaged in advisory services included:

- **Professional advice** - Internal Auditing makes itself available to answer questions on various topics. Common questions pertained to resolving audit findings, compliance with board policies, system procedures, and best practices.

- **Task forces and other committees** - Internal Auditing representatives also sit on various system task forces and committees, including: IT Risk Management Committee, IT Guidelines Committee, Finance User Group, and Financial Aid Directors.

- **Campus Services Cooperative** – Internal Auditing was actively engaged in activities that took place during the fiscal year.

Planning

Internal Auditing completed an audit risk assessment that included strategic and operational risks. While the risk assessment took into account risks across the organization in most functional areas, we completed a more intensive focus on financial and information technology risks. The results of the risk assessments were discussed with the Audit Committee in June 2015. In addition, the results were taken into consideration in building the audit plan for fiscal year 2016.

Staffing

Figure 1 contains the organization chart for the Office of Internal Auditing as of November 1, 2015. The chart notes employees that are not located in St. Paul.
Figure 1 – Organizational Chart

Minnesota State Colleges and Universities
Office of Internal Auditing

- Board of Trustees
  Through Audit Committee Chair
- Vacant Executive Director
- Vacant Internal Audit Investigator
- Eric Wion
  Deputy Director
- Darla Senn
  Office Manager
- Mohammad Fadialla
  IT Audit Manager
- Melissa Primus
  Audit Project Manager
  (Waite Park)
- Craig Fautsch
  West Metro Regional
  (Minneapolis)
- Carolyn Gabel
  Northwest Regional
  (Moorhead)
- Marita Hickman
  East Metro Regional
- Kim McLaughlin
  Northeast Regional
  (Hibbing)
- Indra Mohabir
  SW/Central Regional
  (Waite Park)
Internal auditing staff have on average 20 years of auditing experience. They hold the following professional certifications:

- Certified Public Accountants – 5 employees
- Certified Internal Auditors – 1 employee
- Certified Fraud Examiners – 2 employees
- Certified Information System Auditors – 3 employees
- Certified Information System Security Professional – 1 employee
- Certified Information Privacy Professional – 1 employee

Table 2 provides a summary of how staff resources were used during fiscal years 2013, 2014 and 2015.

**Table 2: Percentage of Internal Auditing Staff Hours**
**Fiscal Years 2013, 2014 and 2015**

<table>
<thead>
<tr>
<th>Audit Services and Time Categories</th>
<th>Fiscal Year 2015</th>
<th>Fiscal Year 2014</th>
<th>Fiscal Year 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal Control and Compliance Audits</td>
<td>44%</td>
<td>19%</td>
<td>22%</td>
</tr>
<tr>
<td>Information Technology Audits</td>
<td>6%</td>
<td>11%</td>
<td>6%</td>
</tr>
<tr>
<td>Support on Financial Statement Audits</td>
<td>-</td>
<td>5%</td>
<td>7%</td>
</tr>
<tr>
<td>Follow-up on Prior Audit Findings</td>
<td>5%</td>
<td>7%</td>
<td>8%</td>
</tr>
<tr>
<td>Investigations and Special Reviews</td>
<td>11%</td>
<td>21%</td>
<td>14%</td>
</tr>
<tr>
<td>General Planning</td>
<td>3%</td>
<td>3%</td>
<td>2%</td>
</tr>
<tr>
<td>Professional Advice</td>
<td>2%</td>
<td>4%</td>
<td>5%</td>
</tr>
<tr>
<td>Administrative</td>
<td>9%</td>
<td>10%</td>
<td>20%</td>
</tr>
<tr>
<td>Employee Benefits (Holidays, Vacation, Sick Leave)</td>
<td>20%</td>
<td>20%</td>
<td>16%</td>
</tr>
</tbody>
</table>

Note: Time excludes executive and deputy director’s time

**The Future**

In June 2015, the Board of Trustees approved an audit plan for fiscal year 2016 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](http://www.internalauditing.mnscu.edu)
## Appendix A – Annual Required Communication Checklist with the Audit Committee

<table>
<thead>
<tr>
<th>Standard</th>
<th>Communication Requirement</th>
<th>Annual Communication Documentation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1000</td>
<td>The Chief Audit Executive (CAE) must periodically review the Internal Audit Charter and present it to senior management and the Audit Committee for approval.</td>
<td>The OIA Audit Charter was amended and presented to the Chancellor and the Audit Committee for review and approval at the May 20, 2015 (first reading), and June 16, 2015 (second reading), Audit Committee Meeting.</td>
</tr>
<tr>
<td>1010</td>
<td>The CAE should discuss the Definition of Internal Auditing, the Code of Ethics, and the IIA Standards with Senior Management and the Finance and Audit Committee.</td>
<td>The Definition of Internal Auditing, the Code of Ethics, and the Standards were discussed with the Chancellor and the Audit Committee in conjunction with the OIA Audit Charter review at the May 20, 2015, Audit Committee Meeting.</td>
</tr>
<tr>
<td>1110</td>
<td>The CAE must confirm to the Finance and Audit Committee, at least annually, the organizational independence of the internal auditing activity.</td>
<td>The Deputy Director confirmed the organizational independence of the internal audit activity as of October 24, 2015.</td>
</tr>
<tr>
<td>1111</td>
<td>The CAE must communicate and interact directly with the Finance and Audit Committee.</td>
<td>As the CAE, I confirm that an appropriate level of communication and interaction has taken place between me and the Audit Committee.</td>
</tr>
<tr>
<td>1312</td>
<td>The chief audit executive must discuss with the Finance and Audit Committee the form and frequency of external assessment as well as the qualifications and independence of the external assessor or assessment team, including any potential conflicts of interest.</td>
<td>Discussions were held at the October 10, 2013, Audit Committee Meeting related to the need for and the frequency of the periodic external assessments, the form of the external assessment, and the qualification and independence of the external assessor.</td>
</tr>
<tr>
<td>1320</td>
<td>The CAE must communicate the results of the quality assurance and improvement program to senior management and the Finance and Audit Committee. The results of external and periodic internal assessments are communicated upon completion of such assessments and the results of ongoing monitoring are communicated at least annually. The results include the reviewer’s or review team’s assessment with respect to the degree of conformance.</td>
<td>The results of the external quality assessment performed by Basil Woller and Associates, LLC was communicated to Executive Management and the Audit Committee on March 25, 2013.</td>
</tr>
<tr>
<td>2020</td>
<td>The CAE must communicate the internal audit activity’s plans and resource requirements, including significant interim changes, to senior management and the Finance and Audit Committee for review and approval. The CAE must also communicate the impact of resource limitations.</td>
<td>Communication of status of internal audit plans and resource requirements was reported on at least a quarterly basis to the Audit Committee. There were no material impacts associated with resource limitations.</td>
</tr>
<tr>
<td>2060</td>
<td>The CAE must report periodically to senior management and the Finance and Audit Committee on the internal audit activity’s purpose, authority, responsibility, and performance relative to its plan. Reporting must also include significant risk exposures and control issues, including fraud risks, governance issues, and other matters needed or requested by senior management and the Audit Committee.</td>
<td>Communication of OIA’s purpose, authority, and responsibility was reported to the Audit Committee on October 21, 2014. On a periodic basis, the CAE also reports significant risk exposures and control issues, including fraud risks, governance issues, and other matters at the request of the Audit Committee.</td>
</tr>
</tbody>
</table>