OLA

OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial Audit Division Report

Lake Superior College

July 1, 2002, through June 30, 2005

June 20, 2006 **06-17**

Financial Audit Division

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- Support Good Financial Management.

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OFFICE OF THE LEGISLATIVE AUDITOR

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Dr. James H. McCormick, Chancellor
Minnesota State Colleges and Universities

Member of the Minnesota State Colleges and Universities Board of Trustees

Dr. Kathleen Nelson, President
Lake Superior College

We have audited Lake Superior College for the period July 1, 2002, through June 30, 2005. Out audit scope included: control environment, financial management, tuition and customized training receipts, employees' payroll, auxiliary enterprise activities, and administrative expenditures. We highlight the audit objectives and conclusions in the individual chapters of this report.

Lake Superior College did not establish adequate controls to prevent or detect fraud or accounting errors and to ensure compliance with state statutes and Minnesota State Colleges and Universities' policies. The college had not established a strong control environment. The former vice president of finance and administration, terminated in November 2005 for gross misconduct, did not effectively manage the financial operations of the college. In addition, he submitted duplicate claims and incurred ineligible expenses totaling $14,666; the college has recovered $12,425 of this amount. Many of the 26 findings in this report result from the ineffective control environment and the misconduct of the former vice president of finance and administration.

As required by *Minnesota Statutes* 2005, 3.975, we have referred this report to the offices of the Attorney General and the St. Louis County Attorney. The Attorney General has the responsibility to recover state funds that were used inappropriately, and the county attorney will be asked to determine whether criminal proceedings are warranted against the college's former vice president of finance and administration.

This report is intended for the information of the Legislative Audit Commission, the management of Lake Superior College, and the members of the Minnesota State Colleges and Universities' Board of Trustees. This restriction is not intended to limit the distribution of this report, which was released as a public document on June 20, 2006.

/s/ James R. Nobles	*/s/ Cecile M. Ferkul*
James R. Nobles Legislative Auditor	Cecile M. Ferkul, CPA, CISA Deputy Legislative Auditor

End of Fieldwork: March 17, 2006

Report Signed On: June 16, 2006

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Audit Participation

The following members of the Office of the Legislative Auditor prepared this report:

Cecile Ferkul, CPA, CISA	Deputy Legislative Auditor
David Poliseno, CPA, CISA, CFE	Audit Manager
Jack Hirschfeld, CPA	Auditor-in-Charge
Marla Conroy, CPA, CISA	Director of Investigations
Ellen Sibley, CPA, CFE	Auditor
Tesfaye Negash	Auditor
Tim Rekow	Auditor

Exit Conference

We discussed the results of the audit with representatives of the Office of the Chancellor and Lake Superior College at an exit conference on June 2, 2006:

Office of the Chancellor:	
Laura King	Vice Chancellor – Chief Financial Officer
Tim Stoddard	Associate Vice Chancellor – Financial Reporting
John Asmusssen	Executive Director – Internal Auditing
Margaret Jenniges	Financial Reporting Director
Denise Kirkeby	Financial Reporting Supervisor
Kim McLaughlin	Regional Audit Coordinator
Marie Peterson	Campus Assistance
Lake Superior College:	
Kathleen Nelson	President
Mark Winson	Vice President of Finance and Administration

Report Summary

Overall Conclusion:

Lake Superior College did not establish adequate controls to prevent or detect fraud or accounting errors and to ensure compliance with state statutes and Minnesota State Colleges and Universities' (MnSCU) policies.

Key Findings:

- The former vice president of finance and administration, terminated in November 2005 for gross misconduct, inappropriately submitted duplicate claims and incurred ineligible expenses (Finding 1, page 7).
- Lake Superior College did not establish an effective control environment (Finding 2, page 9).
- The college did not effectively delegate authority for key financial decisions (Finding 3, page 11).
- The college did not adequately manage its budgeting process (Finding 5, page 15).
- The college did not monitor its outstanding student accounts receivable (Finding 13, page 22).
- The college did not obtain bids or have contracts for certain services (Finding 19, page 31).

The report contained 26 findings related to internal control and legal compliance. Lake Superior College resolved four of the seven prior audit findings.

Audit Scope:

Audit Period:
July 1, 2002, to June 30, 2005

Programs Audited:
- Control Environment
- Financial Management
- Tuition
- Payroll
- Auxiliary Enterprise Activities
- Administrative Expenditures

Agency Background:

Lake Superior College resulted from a 1995 merger of Duluth's community and technical colleges. It is one of 32 colleges that make up the Minnesota State Colleges and Universities system. The college served about 8,500 students in fiscal year 2005, representing a full-time equivalent of over 3,400 students. Lake Superior College offers more than 90 technical majors and courses from 27 academic disciplines. Dr. Kathleen Nelson is the college president.

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Chapter 1. Introduction

The Minnesota State Colleges and Universities (MnSCU) system contracts with the Office of the Legislative Auditor to provide selected internal control and compliance audits of the Office of the Chancellor and individual colleges and universities that comprise MnSCU. This additional audit work complements the annual financial statement audits of the MnSCU system and certain individual colleges and universities conducted by certified public accounting firms. Together with MnSCU management, we used various criteria to determine the specific financial activities included in the scope of our work and the MnSCU entities we audited. Those criteria include the size and type of each entity's financial operations, length of time since the last audit, whether the college had been subject to financial statement audit coverage, changes in organizational structure and key personnel, and available audit resources. Our contract with MnSCU incorporated a schedule for the audit of selected colleges, and Lake Superior College was scheduled for an audit in fiscal year 2006.

In June 2005, the Office of the Legislative Auditor received an anonymous complaint about questionable charges on a credit card issued to Lake Superior College's vice president of finance and administration. We referred this complaint to MnSCU's Office of Internal Auditing, who after consultation with the college president, conducted an investigation. Their investigation, completed in August 2005, resulted in the vice president of finance and administration's immediate three-month suspension. The president blocked this employee's physical access to the college's facilities and his security access to the college's computer systems. In response to additional concerns identified by the internal auditors, we conducted a preliminary assessment to determine whether a more in-depth audit was necessary. The purpose of our preliminary assessment was to determine whether there was sufficient evidence to substantiate the additional allegations, and to help plan the audit scope for this audit. The president terminated the vice president of finance and administration for gross misconduct in November 2005. In accordance with the Personnel Plan for MnSCU Administrators, the college determined that the former vice president of finance and administration was not eligible for severance pay. The determination of gross misconduct and disallowance of severance pay were appealed by the former vice president of finance and administration. A hearing was pending as of May 31, 2006. The college offset the former employee's accrued vacation leave for repayment of $12,425 of the amount owed. The college intends to take action needed to recover the remaining amounts incorrectly received by the former employee. As of May 31, 2006, no criminal or civil charges had been filed against him. The Office of the Legislative Auditor has referred this report to the offices of the Attorney General and St. Louis County Attorney for possible legal action to consider whether the matter warrants further legal action against the former employee.

The president reviewed all duties and responsibilities of the former vice president of finance and administration and implemented new procedures to provide better oversight and accountability. The president appointed an interim vice president of finance and administration and hired a permanent replacement in December 2005.

Lake Superior College

Throughout the investigation and audit, the president cooperated fully with the MnSCU Office of Internal Auditing and the Office of the Legislative Auditor.

Agency Overview

Lake Superior College is the product of a merger in 1995 of Duluth's community and technical colleges. It is one of 32 colleges and universities that make up the MnSCU system, which began operations on July 1, 1995. Dr. Kathleen Nelson is the college president.

Lake Superior College offers more than 90 technical majors and courses from 27 academic disciplines. The larger programs include Associate in Arts transfer program, practical nursing, fire technology and administration, and electronics. Some of the more unique programs include Online Associate in Arts, professional pilot, fire technology and administration, respiratory care, and paralegal. During fiscal year 2005, the college served about 8,500 students, representing a full-time equivalent of over 3,400 students. The college has experienced enrollment increases the past three years. Lake Superior College funds its operation from three major sources: state appropriations allocated by the Office of the Chancellor, tuition and fee receipts, and federal revenue.

Audit Approach

We conducted our audit in accordance with *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of the college's internal controls relevant to the audit objectives. We used the guidance contained in *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission, as our criteria to evaluate college controls. The standards also require that we plan the audit to provide reasonable assurance that the college complied with financial-related legal provisions that are significant to the audit. In determining the college's compliance with legal provisions, we considered requirements of laws, regulations, contracts, and grant agreements.

To meet the audit objectives, we gained an understanding of MnSCU's and Lake Superior College's financial policies and procedures. We considered the risk of errors in the accounting records and noncompliance with relevant legal provisions. We analyzed accounting data to identify unusual trends or significant changes in financial operations. We examined documents supporting the college's internal controls and compliance with laws, regulations, contracts, and grant provisions. We also reviewed management responsibilities and specific accounting transactions approved by the former vice president of finance and administration.

Chapter 2. Control Environment

Chapter Conclusions

In November 2005, the Lake Superior College president terminated the former vice president of finance and administration for gross misconduct because he did not effectively manage the financial operations of the college. The college inappropriately reimbursement him for $14,666 of ineligible expenses or duplicate claims, as discussed in Finding 1.

The college did not establish or implement a control environment and internal controls sufficient to prevent or detect fraud, ensure compliance with rules and regulations and to assure employees met its management objectives. The college had the following deficiencies in its control environment:

- ***Lake Superior College did not establish an appropriate control environment (Finding 2).***
- ***The college did not establish an effective process for delegating authority (Finding 3).***
- ***The college did not have a process to implement its conflicts of interest policy (Finding 4).***

These control environment weaknesses lead to many of the findings reported in the remainder of this audit report.

Audit Objective

Our audit objective was to answer the following question:

- Did the college establish a control environment and internal controls sufficient to prevent fraud, ensure compliance with rules and regulations, detect and prevent accounting errors, and assure employees meet its management objectives?

Background

The Committee of Sponsoring Organizations' (COSO) framework prepared by the Treadway Commission[1] provides a common definition of internal control and the general standards for

[1] The Treadway Commission (formally known as the National Commission on Fraudulent Financial Reporting) and its Committee of Sponsoring Organizations (COSO) were established in the mid-1980s by the major national associations of accountants. One of their primary tasks was to identify the components of "internal control" that organizations should have in place to prevent inappropriate financial activity.

maintenance of effective internal controls. National auditing standards refer to the COSO Internal Control-Integrated Framework as a guide for evaluating entity internal controls. Entity internal controls are a major responsibility of managing an organization. The internal controls comprise the plan, method, and procedures an entity uses to meet its mission, goals, and objectives. Internal controls also serve as the primary method for safeguarding assets and preventing and detecting errors and fraud.

An essential component of an effective internal control system is the establishment of an appropriate control environment. The control environment sets the tone for the organization and lays the foundation for all components of internal control. An appropriate control environment reflects the integrity, values, and competence of the entity's employees, the operating style of employees, assignment of authority and responsibility, and the direction provided by management. However, an inherent limitation of any control environment is the risk that management may override controls.

Termination of the Former Vice President of Finance and Administration

In November 2005, the president terminated the former vice president of finance and administration for gross misconduct because he did not properly manage the financial operations of the college. His responsibilities included maintaining proper internal controls, preparing and monitoring the college financial budget, and providing supervisory leadership to ensure that employees effectively performed assigned job duties and complied with legal provisions and MnSCU policies and procedures. He overrode some of the controls and did not ensure staff were properly trained or supervised to complete their assigned duties. For example, employees responsible to process procurement transactions did not appear to understand bidding, sole source, and contract requirements. Many of these transactions were completed without supporting documentation. A significant number of findings in this audit report are the result of deficiencies in these areas.

The MnSCU Office of Internal Auditing's investigation into the financial activities of the former vice president of finance and administration identified weaknesses in internal controls over processing credit card payments and expense reports. They told us about other concerns over vendor contracts, missing equipment and financial records, and the former vice president of finance and administration's use of false credentials.[2]

We identified similar issues that involved the former vice president of finance and administration contained in the following findings:

- He inappropriately overcharged the college $14,666 (Finding 1).
- He did not disclose a conflict of interest (Finding 4).
- He did not properly manage the college's financial budget (Finding 5).

[2] In March 2004, the vice president of finance and administration was suspended for 15 days for falsifying his credentials.

- He did not maximize investment earnings in the college's local bank account (Finding 12).

- He did not follow proper bidding procedures (Findings 19 and 20).

- He did not prepare annual financial statements for the auxiliary enterprise activities (Finding 25).

An important feature of an appropriate control environment is the monitoring or oversight of personnel at all levels of management. A college president must carefully assign authority and delegate responsibility to the proper personnel to achieve the college's goals and objectives. However, that delegation does not relieve the president of the responsibility to implement effective procedures to monitor results. In addition, the MnSCU Board of Trustees' procedure for the delegation of authority requires a monitoring and audit system of the proper exercise of authority. As further discussed in Finding 2, the president assigned responsibility for financial management of the college to the former vice president of finance and administration, but did not ensure that he established effective internal controls.

Current Findings and Recommendations

1. The college inappropriately reimbursed the former vice president of finance and administration for $14,666 of ineligible expenses or duplicate claims.

Lake Superior College and MnSCU Internal Auditing conducted an investigation of the former vice president of finance and administration and developed a listing of duplicate claims, ineligible expenses, and unauthorized transactions totaling $14,666. The list disclosed numerous alleged improprieties including:

- The former vice president of finance and administration improperly submitted reimbursement claims for duplicate charges. In some cases, the former vice president of finance and administration submitted the same expense on different expense reports. Sometimes, he charged the expense on his college-issued credit card and also requested reimbursement for the same expense on an expense report. The college did not detect the duplicate payments and overpaid the former vice president of finance and administration.

- The former vice president of finance and administration incurred ineligible costs and charged them to the college. Some of these costs included hosting retirement parties, purchasing an expensive camera for a retiring employee, and meals for which reimbursement was not permitted.

- The former vice president of finance and administration used a personal frequent flyer voucher to obtain an airline ticket for college business and then requested reimbursement for the value of the airline ticket.

- The former vice president of finance and administration submitted numerous reimbursement claims without adequate documentation to support the legitimacy of the expense. For example, he requested reimbursement for meals at local restaurants without documentation to show that these expenses met circumstances under which they are allowable. To be reimbursed, the employee needs to provide sufficient documentation to support the charges.

- The former vice president of finance and administration circumvented the intent of the reimbursement for improper travel cost by processing an inappropriate payment. In 2003, we reported that the college needed to obtain repayment of $1,716 in travel costs the college had inappropriately paid for a faculty member's spouse and a dependent child. The college reviewed the costs we had questioned and obtained reimbursement for $1,534 from the faculty member in March 2004. However, two weeks later, the former vice president of finance and administration disbursed a check for $1,600 to the faculty member's spouse. No documentation supported this transaction; it may have been meant to offset the reimbursement by the faculty member. The former vice president of finance and administration processed the $1,600 payment after business office staff refused to process it.

- The college incurred $465 in late fees and interest charges on the former vice president of finance and administration's credit card because he did not submit the credit card statements in a timely manner.

- In the summer of 2005, the former vice president of finance and administration inappropriately provided bid information to a company during a sealed bid process. The request for proposal specifically stated, "Responses to this RFP will not be open for public review until Lake Superior College decides to pursue a contract and that contract is awarded." After receiving the proposals, the vice president of finance and administration told a vendor by e-mail that the company was the "high bidder" by a specific dollar amount. The college threw out the first bids and requested second bids. Based on the information provided by the former vice president of finance and administration, the company with which he had communicated lowered its bid offer. For other reasons, the college decided not to award the contract.

- Also, we found four undeposited checks totaling $808 dollars in his office; some of the checks dated back to 1992. These checks should have been routed to the cashier's office for depositing and not held by the former vice president of finance and administration. *Minnesota Statutes* 2005, 16A.275 requires that all monies over $250 must be deposited daily. Due to the length of time that the college held these checks, it is unlikely that the checks would be honored by a bank.

The former vice president of finance and administration misused his authority to get these duplicate and ineligible expenses reimbursed. He supervised the business office staff that processed these claims, and he approved the charges and directed the staff to process the payments. In addition, he did not submit his expense reports to the president for approval. The college policy allowed vice presidents to approve each other's expense reports and other charges. Rather than have the president approve his expense reports and risk questions about his reimbursement requests, the former vice president of finance and administration obtained another vice president's authorization. Had the president approved all of his expense reports, she would have been in a position to question some of the charges.

The president terminated the vice president of finance and administration for gross misconduct in November 2005. In accordance with the Personnel Plan for MnSCU Administrators, the college determined that the former vice president of finance and administration was not eligible for severance pay. The determination of gross misconduct and disallowance of severance pay were appealed by the former vice president of finance and administration. A hearing was pending as of May 31, 2006. The college offset the former employee's accrued vacation leave for repayment of $12,425 of the amount owed. The college intends to take action needed to recover the remaining amounts incorrectly received by the former employee. As of May 31, 2006, no criminal or civil charges had been filed against him.

Recommendations

- *The college should finalize its action against the former vice president of finance and administration for duplicate claims and ineligible expenses he charged the college.*
- *The college should ensure that employees are reimbursed only for allowable expenses based on appropriate supporting documents.*
- *The college should comply with sealed bid requirements and not reveal nonpublic information that could influence the outcome of the bidding process.*
- *All receipts should be routed to the cashier's office for timely deposit.*
- *The college should contact the check makers and determine if replacement checks could be issued.*

2. Lake Superior College did not establish an appropriate control environment.

The college did not establish a control environment that ensured management and other employees appropriately carried out their responsibilities. An important aspect of establishing a control environment is to provide oversight of the performance of all managers with delegated responsibilities. The president assigned responsibility for financial management of the college to the former vice president of finance and administration, but she did not ensure that he established effective internal controls. The president should have gained a sufficient understanding of internal controls and statutory, policy, and procedural requirements to ensure that he carried out his responsibilities and managed the business office effectively. The lack of an appropriate control environment resulted in the following serious internal control weaknesses:

- A lack of controls to prevent or detect fraud and ensure compliance with board policies and procedures (discussed in Chapter 2);

- Inadequate financial management of the college, including poor budgetary controls, cash management, and overall financial management procedures (discussed in Chapter 3);
- Inadequate tuition and customized training internal controls and registration procedures (discussed in Chapter 4);
- Inadequate procurement procedures and internal controls (discussed in Chapter 6); and
- Inadequate financial management of the college's enterprise activities (discussed in Chapter 7).

The president is ultimately responsible for any management deficiencies. She must take steps to ensure that basic, effective internal controls exist for essential functions. She should have better monitored the financial activities of the former vice president of finance and administration. Had the president adequately understood the internal control structure and the significant legal compliance requirements, these weaknesses might have been identified and addressed.

Another aspect of a sound control environment is the establishment of good communication throughout the organization. Employees stated that the former vice president for finance and administration intimidated them and made it difficult for them to question his decisions. His intimidation may have disrupted the effectiveness of communications regarding college business activities. Employees need to know that they have alternative channels for voicing complaints, and they will be protected from retaliation when doing so.

The president acted promptly to improve the college's control environment after the allegations about the former vice president of finance and administration surfaced. She assumed responsibility for many administrative functions. She also assigned certain responsibilities to other staff and developed new policies and procedures to address certain deficiencies. She encouraged staff to bring concerns to her regarding their responsibilities. Progress has been made to establish an appropriate control environment, but more work needs to be completed to ensure that assets are adequately safeguarded and that errors and fraud are prevented or detected.

Recommendations

- *The college needs to establish an internal control structure that will prevent material errors and irregularities and ensure compliance to system policies and procedures.*

- *The current vice president of finance and administration needs to periodically review and verify that internal controls are operating as designed, and that the college is complying with MnSCU policies and procedures.*

- *The president should strengthen the college's control environment by monitoring the performance of key college employees to ensure that they perform their job duties and responsibilities.*

- *The college should ensure that all employees have a way to communicate their questions and concerns.*

3. The president did not effectively delegate authority for key financial decisions.

System Delegation of Authority, Procedure 1A.2.2, allows college presidents to delegate to their respective subordinates specific authority for certain actions. It further states that the delegations of authority should only be used in limited situations, including where the person receiving the delegation has the expertise to use the delegation appropriately and knowledgeably, and where there is a method in place to ensure proper exercise of the delegations of authority including a monitoring and audit system. The procedure provides that delegation of authorities should be appropriate to the individual's level of responsibility and should be as specific as possible with dollar limits indicated.

The college did not have adequate procedures to ensure that the delegation of authorities was properly administered. Some problems with the delegation of authority process included:

- Individuals approved contracts and other purchases without being delegated that authority. For instance, in December 2004, one employee approved a $26,000 contract, and in March 2005, another employee approved a $130,000 contract. Neither employee had been delegated the authority to approve contracts.

- The college did not specifically identify actions that required a delegation of authority or those individuals whose responsibilities included those actions. The college needs to identify the employees and the responsibilities and expertise that require a delegation of authority.

- The college did not have delegations with specific dollar limits. Dollar limits would reduce the risk that improper contracts and activities would be approved.

- The college did not monitor or audit the appropriateness of delegations of authority.

- Finally, the business office did not have copies of the delegations of authority to ensure that college employees only authorized the transactions they had been formally delegated.

Without completing these procedures, the college cannot ensure that the delegation of authority process is operating as intended, and that the college maintains fiscal integrity.

Recommendations

- *The college should monitor its delegation of authority process to ensure that employees with the delegations have the proper expertise, necessity, and responsibility for the delegations.*

- *The college should include specific dollar limits in its delegations of authority.*

- *The business office should have copies of all delegations to ensure that employees have been delegated the authority to approve the transaction.*

4. The college did not have a procedure to implement its conflicts of interest policy.

Lake Superior College did not ensure that employees complied with MnSCU's conflict of interest requirements. MnSCU identified its expectations in part 11 of the purchasing procedure, which states that state employees are covered by *Minnesota Statutes* 2005, 43A.38 and 43A.39. These statutes cover such topics as acceptance of gifts, conflicts of interest, and use of confidential information. MnSCU's policy further incorporates *Minnesota Statutes* 2005, 15.43, which limits employees' contact with suppliers or others who may directly or indirectly influence a purchasing decision. This statute also addresses financial interest and the acceptance of gifts. The college established a fraud policy that prohibited conflicts of interest. . However, the college did not have a mechanism to help employees identify and disclose potential conflicts of interest.

The former vice president of finance and administration did not notify the president about a conflict of interest resulting from a personal relationship between himself and a vendor. The vice president of finance and administration was a long-time friend of the vendor and routinely vacationed at the vendor's condominium in Florida and received tickets to professional sporting events. The former vice president of finance and administration should have advised the president about this relationship and sought appropriate remedies.

Recommendations

- *The college needs to develop, communicate, and implement a conflict of interest procedure for its employees.*

- *The college should ensure employees who directly or indirectly influence purchasing decisions and contracts are aware of and comply with Minnesota Statute 2005, 15.43.*

Chapter 3. Financial Management

Chapter Conclusions

Lake Superior College operated within available resources. The college had an appropriate relationship with its foundation. However, many of the college's financial processes need improvement, as disclosed below:

- ***The college did not properly manage its financial budget (Finding 5).***
- ***The college improperly encumbered funds budgeted for fiscal year 2005 for costs it intended to incur in fiscal year 2006 (Finding 6).***
- ***The college did not encumber funds before incurring obligations, as required by statute and MnSCU policy (Finding 7).***
- ***The college did not appropriately limit computer access to its business systems (Finding 8).***
- ***The college did not separate certain key, incompatible financial duties for various functions (Finding 9).***
- ***The college did not comply with MnSCU's special expense and the president's expense procedures (Findings 10 and 11).***
- ***The college did not maximize investment earnings in its local bank account (Finding 12).***

As a result of these weaknesses and the other weaknesses reported in the other chapters, Lake Superior College did not always reasonably and prudently manage its financial activities.

Audit Objectives

Our review of Lake Superior College's financial management structure focused on the following questions:

- Did the college's internal controls provide reasonable assurance that financial activities were properly recorded in the accounting systems?

Lake Superior College

- Did the college's internal controls provide reasonable assurance that it operated within available financial resources in compliance with applicable legal provisions and management's authorization?

- Did the college's internal controls provide reasonable assurance that local bank financial activities were adequately safeguarded, accurately recorded in the accounting records, and in compliance with applicable legal provisions and management's authorization?

- Did the college's internal controls provide reasonable assurance that it had an appropriate operating relationship with related organizations?

- Did the college's internal controls provide reasonable assurance that its budget process and overall financial management activities were reasonable?

- Did Lake Superior College's management reasonably and prudently manage the financial activities of the college?

Background

Lake Superior College used the MnSCU accounting system to record its financial activity and to initiate transactions. MnSCU accounting interfaces with the state's accounting system, the Minnesota Accounting and Procurement System, to generate warrants from the state treasury. The Office of the Chancellor requires that all campuses use the MnSCU accounting system to account for money.

Budgetary Controls

MnSCU receives a significant amount of its funding for operations from General Fund appropriations. The Board of Trustees, acting through the Office of the Chancellor, is responsible for the allocation to individual colleges, including Lake Superior College. The allocation is formula based and is related to enrollment, past appropriations, and other factors. In addition, Lake Superior College, like other colleges, retains the tuition and other receipts its collects to arrive at its total authorized spending level. The college maintained a seven percent reserve amount in compliance with MnSCU policy.

The former vice president of finance and administration was responsible for managing the college budget. He allocated funding to the various cost centers and was responsible for monitoring the revenues and expenditures of the college. The college assigned a cost center number to each college activity or department and used those cost centers to monitor the budget. Cost center managers were responsible for reviewing and managing their individual budgets.

Foundation

Lake Superior College is affiliated with Lake Superior College Foundation. The foundation has its own directors, articles of incorporation, and bylaws. The foundation maintains its own financial records and accounts, which are audited every three years by a CPA firm. The foundation has a written agreement with the college to provide staffing and other administrative support in exchange for student scholarships and grants that benefit the educational mission of the college.

Financial Management

The president of the college relied on the former vice president of finance and administration to manage the college's financial activity. The vice president of finance and administration's responsibilities included providing supervision to staff, ensuring that internal controls were in place to prevent or detect errors or fraud, and to ensure compliance with rules and regulations.

Current Findings and Recommendations

5. The college did not adequately manage its financial budget process.

The college did not properly manage its budgeting function. MnSCU Policy 5.9, Biennial and Operating Budget Planning and Administration, states that the board of trustees will approve the operating budget for all colleges. It is the colleges' responsibility to prepare budgets consistent with board policies and systems procedures. Lake Superior College completed its annual budget, as required by system policy. However, once established, the college did not efficiently and effectively monitor its budget function. The college did not establish a satisfactory internal budget process. Some of the problems included:

- The college did not load all of the budgets into the cost centers. Many cost centers were not initially funded for the complete year. As a result, cost center managers had to routinely request funding increases during the year. This left the funding decisions to one person -- the vice president of finance and administration. Because some cost center managers did not know what their approved budgets were for the year, they did not know if they always received their full budgeted amounts. Further, the college did not have an audit trail to document these funding adjustments. It appears that the former vice president of finance and administration would either arbitrarily move funding among the cost centers without informing the cost center managers, or retain a large amount of the budget in the reserve account and allocate it as needed.

- The cost center managers did not adequately review budgetary reports. These reports provided the budget status of the costs centers, including available funding. The college directed each cost center manager to routinely obtain and review these reports. However, many managers said they did not understand these reports and did not request assistance. In addition, the college did not provide sufficient instruction to the cost center managers.

The college did not have an effective process for rolling encumbrances forward at the end of the year. The college did not roll encumbrances forward at the end of fiscal year 2004, requiring a large number of manual entries to bring the funding forward to fiscal year 2005. To compensate for the complaints related to the prior year, the same individual brought forward all of the 2005 encumbrances into fiscal year 2006. The cost centers did not review these encumbrances beforehand, allowing many invalid encumbrances to be carried forward.

The annual budget has to properly be allocated to the cost centers based upon an approved college budget. Adjustments will continually need to be made, but should be done under the review of the management team.

Recommendations

- *The college needs to ensure that the budgets are properly loaded to each cost center.*
- *Cost center managers need to be better informed about the budget process, including how to use various budget reports.*
- *The college needs to ensure that the budgets include accurate encumbrance information. Adjustments and other activities, such as rollovers between fiscal years, need to be properly completed to ensure appropriate cost center funding.*

6. In fiscal year 2006, the college inappropriately encumbered fiscal year 2005 funds for purchases made in fiscal year 2006.

The college inappropriately encumbered approximately $125,000 in July of fiscal year 2006 against the fiscal year 2005 budget. The college encumbered the fiscal year 2005 funds to be used for purchases of supplies and services for fiscal year 2006. By shifting some costs to the prior fiscal year, spending for the current fiscal year increased. The college should establish encumbrances in the year that the obligation exists.

Recommendation

- *The college should establish encumbrances out of the proper budget year*.

7. The college did not always encumber funds before incurring obligations.

The college did not always encumber funds before incurring an obligation in violation of MnSCU Procedure 5.14.5. Part 5 of that procedure states that,

> Funds must be encumbered prior to making an obligation through an authorized employee certifying that the accounting system shows sufficient allotment or encumbrance balance in the fund, allotment, or appropriation to meet it. An expenditure or obligation authorized or incurred prior to encumbering funds is illegal and ineligible for payment until made valid and is in violation of *Minnesota Statutes*, 16A.15, subd. 3.

In an effort to monitor these violations, Lake Superior College developed a form to identify and track each occurrence. On September 1, 2005, the college president required all employees to complete the form for each instance when an expenditure or obligation is authorized before the availability of funds in the accounting system is verified. College staff completed the form for 88 such violations between September 2005 and January 2006. This large number of violations indicates that employees did not routinely verify that adequate funding existed in their accounts before incurring an obligation. The college needs to review the reasons for the extensive number of violations and reduce the necessity for the letters.

Recommendations

- *Lake Superior College needs to comply with MnSCU purchasing procedures and ensure that funds are available before incurring obligations.*

- *The college should review any instances when a violation occurs and take appropriate action to ensure future compliance with this statutory provision*

8. The college did not adequately limit computer access to certain business systems.

Lake Superior College did not adequately restrict access to some of its computerized business systems, including MnSCU accounting, SCUPPS Human Resources, and the accounts receivable module in the Integrated Student Information System (ISRS). Our review of the security access to college computerized business systems disclosed the following weaknesses:

- Six employees, including two system office staff, had incompatible access to the SCUPPS profile and the SEMA4 profile (HR_20H and HR_80 H). This access allowed these employees to schedule pay disbursements and add, change, or delete human resources information. The problem existed because MnSCU includes payroll disbursement updates in the HR80 screen. As a result, the payroll clerk entering mass time entry into SEMA4 also has access to process human resources transactions in SCUPPS. MnSCU has established a focus group to consider changing the security profile. The focus group’s goal is to define a profile that limits human resources staff to updating SCUPPS modules and limits payroll staff to updating SEMA4.

- The college did not restrict access to its accounts receivable module in ISRS. A customer service specialist in the bookstore has access to update employee waivers. An account clerk has access to the department head module allowing the employee to adjust tuition and tax rates. Neither of these employees needs this access to perform their duties. In addition, four cashiers had access that lacked proper segregation of incompatible duties. They could collect and record receipts and also process waivers and make corrections to the accounts receivable module.

- The college did not restrict access to its purchasing control system. Seven employees had purchasing head access, allowing them to authorize purchases and to update the accounting system. Four of these employees did not need this access to perform their job duties.

- The cashiers in the business office did not always use unique user identification numbers (ID) when processing tuition receipts into ISRS. The college used one cash drawer;

cashiers log in at each session. However, student workers did not have their own user ID numbers and used one of the cashiers' numbers. Each day's activity was reflected in the cash drawer. Daily receipts sometimes totaled as much as $327,000. The college reconciled the cash drawer to the business system, but the college could not identify which individual processed each transaction.

Recommendations

- *The college should limit employee system access to the access needed for them to perform their job responsibilities. The college should assign duties and access to eliminate any incompatible access. If the college is unable to eliminate incompatible access, it must develop detection controls to provide a periodic and independent review of the employees' work.*

- *Lake Superior College's cashiers should use, not share, user ID numbers so that the college can identify individuals responsible for any overages or shortages.*

9. The college did not separate certain key, incompatible financial duties over various functions.

The college did not separate key financial duties in the business office:

- When a business office employee resigned in December 2005, the college assigned that employee's duties to another business office employee without considering the impact on internal controls. As a result, one employee was responsible for collecting receipts, recording the receipts on the accounting system, and reconciling the recorded receipts to the monthly bank statement. These duties are incompatible because they may allow discrepancies to exist between the recorded receipts and actual deposits, whether intentional or due to error, without those discrepancies being detected and corrected. If the college is not able to assign these incompatible duties to different employees, it should implement mitigating controls, such as reviews of the reconciliations by the employee's supervisor, that would allow for detection and correction of any errors or irregularities should they occur.

- The employee responsible for purchasing of goods also performed the 2005 physical inventory. These duties are incompatible because they would allow the employee to attest to the existence of goods purchased with college funds but inappropriately taken off the campus by him for personal use.

Recommendation

- *The college should identify incompatible duties and either segregate those duties or establish mitigating controls to ensure that errors or irregularities will be detected in a timely manner.*

10. The college did not comply with MnSCU's special expense procedure.

The college recorded unallowable purchases as special expenses. Also, the college did not follow MnSCU procedures for special expenses or document authorization for the transactions with a special expense form. MnSCU Procedure 5.20.1 defines special expenses as, "extraordinary expenses incurred in connection with work-related responsibilities or official functions not generally supported with public funds of MnSCU…" The procedure lists 11 categories of covered expenses, where the benefits of the employee's attendance or participation will accrue primarily to the state. However, the college recorded as special expenses various purchases not covered by the special expense procedure, such as an employee flower fund, gifts, Grandma's Marathon entry fees, and pizza orders for Student Senate meetings. Recorded special expense transactions also identified a large number of food purchases that may not comply with the special expense criteria; a determination could not be made due to a lack of documentation.

The procedure also requires that, "Except in emergency situations, approval is required before any special expense is incurred and before commitments involving special expenses are made." The procedure also recommends processing the special expenses as follows:

- Determining whether the expense is appropriate to pay as a special expense;
- Preparing a requisition form and special expense form; and
- Having an authorized employee sign the invoice and submit it to the business office for payment.

The college did not use a special expense form during our audit scope. Therefore, there was no evidence to support that the expenses were properly approved in advance. In addition to documenting the proper authorization of the special expense, the form would allow the college to compare the actual expense to the approved special expense request to verify that the amount and purpose of the costs were accurate and legitimate.

Recommendation

- *The college should comply with MnSCU's special expense procedure by developing a form that is timely submitted for approval and comparing the special expense form to the subsequent payment.*

11. Lake Superior College did not comply with MnSCU's presidential expense allowance.

Lake Superior College employees improperly charged expenditures to the presidential expense allowance. Supervisors and faculty were using the presidential expense allowance account for expense reimbursements without the president's knowledge. We tested 15 presidential expense allowance charges and noted that the president did not authorize 13 of the 15 payments. MnSCU System Procedure 5.20.1, Presidential Expense Allowances, states that, "… are expense accounts which permit the payment of expenses related to the duties and responsibilities of the chancellor and the presidents for which no other reimbursement is provided. All expenditures must have a public purpose and must provide benefit to MnSCU or one of its colleges or universities."

Lake Superior College

MnSCU policy sets the annual dollar limit for Lake Superior College at $5,000 and requires all expenditures to have the president's approval.

College employees also used the presidential expense allowance account to obtain reimbursement for costs, which should have been reimbursed through normal employee reimbursement requests. For 15 charges sampled, 14 were unallowable expenses. The presidential expense allowance procedure states that the presidential expense allowance account may be used only for meals and related expenses when conducting college business or memberships to certain organizations for which no other reimbursement is provided. The 14 charges in the sample did not comply with the requirements.

The president became aware of these improper expenditures and sent a memo instructing faculty on the policy requirements of the presidential expense allowance. The college also reversed charges totaling $3,769 in expense reimbursement for fiscal year 2005 and transferred these costs to other cost centers. In August 2005, the president created a Department Head Expense Expenditure Information form to be completed for each reimbursement. This form will provide an explanation of the expenditure and the president's approval.

Recommendation

- *All presidential expense allowance expenditures should be submitted for reimbursement on the appropriate form, contain all documentation to assure that the account was used for allowable activities, and must be approved by the president.*

12. The college did not maximize its investment earnings for funds in its local bank account.

Lake Superior College did not properly invest available cash in its local account. The college had an average of about $876,000 in its local checking account for the five months ending February 2006. This amount accumulated from cash from the bookstore, parking permits, student life, and health services accounts. This is an excessive balance to be carried in the checking account and could be invested in more profitable accounts.

The college did not actively monitor its bank accounts. A bank representative stated that the college had minimal contact with the bank over the past couple of years

Recommendations

- *The college should analyze its cash needs and establish a cash management strategy to maximize its investment earnings.*

- *The college should review its banking needs with the local bank on a periodic basis.*

Chapter 4. Tuition and Fees

Chapter Conclusions

Lake Superior College accurately recorded tuition and fee revenues in the accounting records. Generally, the college complied with applicable legal provisions and management's authorization. However, we identified the following areas of concern:

- ***The college did not monitor its accounts receivable or send past due receivables to the Minnesota Collection Enterprise in a timely manner (Finding 13).***
- ***The college did not properly approve certain student tuition payment plans (Finding 14).***
- ***The college has not effectively established or controlled tuition waivers (Finding 15).***
- ***The college did not register some customized training students in a timely manner (Finding 16).***
- ***The college did not properly approve or retain customized training contracts (Finding 17).***
- ***The college did not deposit receipts in a timely manner (Finding 18).***

Audit Objectives

Our review of Lake Superior College's tuition and fees focused on the following questions:

- Did the college's internal controls provide reasonable assurance that all tuition and fees were collected and safeguarded, properly reported in the accounting records, and in accordance with applicable legal provisions and management's authorizations?
- For the items tested, did the college comply, in all material respects, with the significant finance-related legal provisions concerning tuition and fees?

Lake Superior College

Background

Lake Superior College collected approximately $34 million in tuition and fees during the three-year period ending June 30, 2005. The college offered credit-based courses leading to a diploma, certificate, or an Associate of Arts degree. In addition to its regular programs, the college provided noncredit programs consisting of customized training and continuing education. The college developed customized training courses to meet the educational needs of a specific business or industry and offered continuing education courses to the general public. Based on available space, the college also allowed Minnesota high school juniors and seniors to enroll in college courses through the post-secondary enrollment option.

In fiscal year 2005, the college charged Minnesota residents $100.50 per semester credit and non-residents $201. Fees amounted to approximately $15 per credit. The college used the MnSCU Integrated Student Records System (ISRS) accounts receivable module to register, bill, and collect tuition. The business office collected tuition and fees and deposited the receipts in the local bank account. Table 4-1 shows the amounts collected for tuition, fees, and customized training programs for fiscal years 2003 through 2005.

Table 4-1
Tuition and Fee Revenues
Fiscal Years 2003 through 2005

Revenue Source	2003	2004	2005
Tuition (Note 1)	$6,949,768	$ 8,557,850	$ 9,981,509
Fees	2,161,866	2,274,039	2,362,558
Customized Training	630,844	698,248	679,949
Total	$9,742,478	$11,530,137	$13,024,016

Note 1: Tuition amount is net of tuition refunds.

Source: MnSCU Accounting System.

Current Findings and Recommendations

13. Lake Superior College did not adequately monitor its accounts receivable balance.

Lake Superior College did not monitor the accounts receivable balance or refer past due receivables to the Minnesota Collection Enterprise (MCE) in a timely manner. The college's accounts receivable balance increased from approximately $703,000 in 2002 to $1,300,000 in 2005. Tuition and enrollment increases could not sufficiently explain these significant increases over the three years. The college should analyze significant changes to determine any reasons for major fluctuations.

Lake Superior College did not refer uncollectible accounts to the Minnesota Collection Enterprise in a timely manner. MnSCU Procedure 7.6.2 states that, "accounts receivables which the institution is unsuccessful in collecting and are 121 days past due, must be referred to MCE for collection." Lake Superior College's policy varies from MnSCU's policy and sends collection letters to students with overdue balances after 120 days and allows another 20 days for their response before sending them to MCE.

In addition, the college failed to submit overdue accounts receivable to MCE according to MnSCU's collection procedure. For example, for fall semester 2005, accounts receivable balances should have been referred to MCE by January 19, 2006. However, the college did not refer overdue accounts receivable to MCE until March 23, 2006, two months after the required date. During fiscal years 2003 to 2005, Lake Superior College was consistently about six week late in referring uncollectible accounts receivables to MCE. The college should change its collection procedures to ensure that it complies with MnSCU's requirements.

Finally, Lake Superior College did not adequately document its decision to not pursue collection on a $1,329 accounts receivables balance for a student deployed in the military. Tuition payments are due the day before classes start. Receivables from students who do not pay their debt are sent to MCE for collection. However, the college makes an exception to this rule for students who have been militarily deployed. The college puts a hold on the collection of these receivables. In this instance, the college did not obtain documentation, such as a deployment order or a similar document, to verify the status of the student. Without supporting documentation, the college cannot be sure the student is actually deployed.

Recommendations

- *Lake Superior College should monitor the balance of its receivables and determine the cause for any significant changes.*

- *The college should refer its uncollected accounts receivables to MCE in accordance with MnSCU policy.*

- *The college should obtain documentation to support decisions to not pursue collection of student receivables.*

14. Lake Superior College's cashiers did not obtain the required authorization prior to establishing certain tuition payment plans.

The college permitted students who are unable to pay their tuitions at the time of registration to set up payment plans. The college's tuition payment policy required students to complete and sign a deferred payment agreement. The college's policy required an initial payment of one-third, followed by two consecutive monthly payments of one-third each. If the student did not comply with the payment plan, the college referred the account to the Minnesota Collection Enterprise. The college's policies allowed cashiers to establish other payment plans with the authorization of the vice president of finance and administration. However, cashiers routinely established other payment plan arrangements without proper authorization. In August 2005, the president reaffirmed the policy, which requires the vice president of finance and administration's approval of other types of payment plans. However, we did find one nonstandard payment plan issued in November 2005 that was not properly authorized.

In addition, we found the following problems with the payment plans:

- Three of twelve payment plans tested were not signed by the student.

- Four of twelve payment plans tested were not paid in accordance with the plan's requirements.

- The college did not refer past due accounts to the Minnesota Collection Enterprise when the students did not adhere to the payment plans.

To ensure that the college collects all money it is due from the students, it needs to establish and follow a sound collection policy involving student payment plans.

Recommendations

- *The college should ensure that its cashiers receive authorization from the vice president of finance and administration for nonstandard payment plans.*

- *Lake Superior College should obtain student signatures at the time the payment plans are created.*

- *The college should closely monitor student payment plans and, if students do not promptly adhere to those payment plans, forward the receivables to the Minnesota Collection Enterprise.*

15. The college has not effectively established or controlled tuition waivers.

The college has not established a formal tuition waiver policy and has improperly waived tuition charges. Tuition waivers eliminate all or a part of a student's tuition and fees. In 2005, the college waived tuition totaling approximately $253,000. The accounting system identified the largest amounts waived as being related to significant personal circumstances that made it difficult or impossible for a student to complete the course and to tuition waivers for college staff and their dependents.

Lake Superior College did not have a formal tuition waiver plan. MnSCU Board Policy 5.12 states that, "Each college or university shall define the terms under which any authorized waiver will be granted. The college or university must document the reason for all waivers." Our audit of tuition waivers disclosed the following concerns:

- In January 2006, the college waived tuition for a student who failed to drop his fall 2005 class on time. MnSCU's waiver policy did not recognize the failure to drop a class as a legitimate reason to process a tuition waiver.

- In fiscal year 2004, the college inappropriately used tuition waivers to adjust the accounting records for a billing error. For at least eight attendees of a customized training course, the college erroneously charged $300 per credit instead of the correct amount of $325 per credit. Instead of billing the employer for the $25 difference per student, the college waived this amount.

- In fiscal year 2004, the college inappropriately used tuition waivers to adjust the accounting records for errors in the tuition it charged students from Wisconsin. Wisconsin students who took more than 16 credits should have been charged a maximum (bundled) rate rather than a per credit rate. The college's accountant did not use the module in the Integrated Student Record System (ISRS) that would have assessed the correct tuition rate. Instead, the accountant used tuition waivers to make the corrections and process refunds for any overpayments.

Recommendations

- *Lake Superior College should design, implement, and apply a tuition waiver policy that ensures consistency and accountability.*

- *The college should not use tuition waivers to correct college errors.*

16. PRIOR AUDIT FINDING NOT RESOLVED: The college did not properly register some customized training students.

The college did not register some students before the completion of its civil tech customized training course, and the Emergency Response Training Center did not use ISRS to register any students in 2004. In our prior audit report of Lake Superior College, we reported that customized training at Lake Superior College did not register students for classes in a timely manner. Customized training students were often registered several months after the beginning of classes. We found the same concerns during fiscal years 2003 through 2005. The college did not register four out of the ten customized training students we tested before the start of class. The delay in registering students ranged from two months to one year after the start of the class.

The Emergency Response Training Center, a division of Customized Training, did not use ISRS to record student registrations amounting to about $280,000 in fiscal year 2004. According to MnSCU Procedure 7.6.2, "The receivable must be entered into [ISRS] at the time the amount is first established or within a reasonable period afterwards." By failing to register Emergency Response Training Center students in ISRS, there is no record of the receivables in the accounting system.

Recommendation

- *The college should register all students in ISRS in a timely manner.*

17. Lake Superior College did not properly execute customized training contracts.

Lake Superior College did not always execute customized training contracts prior to the start of the class and did not maintain copies of all the contracts. Lake Superior College signed a $12,000 customized training contract six weeks after the service period specified in the contract. The college also signed other contracts up to two months after the start of the class. Customized training contracts stipulate the services to be provided, the time period, and the payment terms. Contracts should be signed by all parties before any services are provided.

Additionally, the college could not locate 4 of the 15 contracts we tested. The college should maintain copies of the contracts to document the legal understanding of both parties.

Recommendations

- *The college should sign contracts before the beginning dates of classes.*
- *The college should maintain copies of all contracts.*

18. The college did not deposit tuition, customized training, and food service receipts in a timely manner.

The college did not deposit some receipts in a timely manner. MnSCU Policy 7.5 requires that, "All monies received by the college shall be deposited daily, unless receipts are less than $250, in which event deposits may be deferred until they total such sum." For 3 of 15 deposits tested, the college did not comply with this policy. The late deposits mainly related to customized training receipts. For example, the college deposited customized training tuition receipts totaling $455 two weeks after they were received.

Additionally, the college did not promptly deposit receipts for 3 of 10 food service deposits tested. The late deposits averaged $1,000 and ranged from two days to one week late.

Recommendation

- *The college should deposit daily receipts exceeding $250 in a timely manner.*

Chapter 5. Employee Payroll

Chapter Conclusions

Lake Superior College's internal controls provided reasonable assurance that it properly authorized and accurately reported employee payroll expenditures in the accounting records, and that payments complied with applicable legal provisions and management's authorizations. However, the college did not restrict access to its human resources and payroll computer systems, discussed in Finding 8, Chapter 3.

For the items tested, the college complied with material finance-related legal provisions and applicable compensation plans.

Audit Objectives

Our review of Lake Superior College's employee payroll expenditures focused on the following objectives:

- Did the college's internal controls provide reasonable assurance that it accurately recorded payroll expenditures in the accounting records, and that it complied with applicable legal provisions and management's authorization?

- For the items tested, did the college comply with material finance-related legal provisions governing payroll?

Background

Employee payroll represents Lake Superior College's largest expenditure and averaged $18.4 million annually during our audit period. During fiscal year 2005, Lake Superior College employed about 590 employees consisting of about 100 full-time faculty, 300 part-time faculty, and 190 full and part-time supervisory and support staff. During 2005, Lake Superior College employees belonged to the following compensation plans:

- Administrative Plan
- American Federation of State, County, and Municipal Employees
- Commissioner's Plan
- Minnesota Nurses Federation
- Minnesota Association of Professional Employees
- Middle Management Association
- Minnesota State College and University Faculty

Lake Superior College

Lake Superior College processes biweekly payroll transactions on the state's payroll system. The state's payroll system interfaces with the State Colleges and Universities Payroll and Personnel System (SCUPPS), which provides employment history, pay rates, and bargaining contract details for all college employees. The human resources section enters all personnel changes and new employee records onto SCUPPS.

Chapter 6. Administrative Expenditures

Chapter Conclusions

Lake Superior College's internal controls did not provide reasonable assurance that administrative expenditures were accurately reported in the accounting records, adequately safeguarded, and in compliance with applicable legal provisions and management's authorization. Our audit of administrative expenditures disclosed the following weaknesses:

- ***The college did not solicit bids or prepare contracts for some purchases (Finding 19).***
- ***The college did not adequately maintain documentation for some of its bids and purchases (Finding 20).***
- ***The college did not properly record certain transactions in its accounting system (Finding 21).***
- ***The college used unauthorized credit cards to make some purchases (Finding 22).***
- ***The college has not conducted a complete fixed asset inventory (Finding 23).***

Audit Objectives

Our audit of administrative expenditures focused on the following questions:

- Did the college's internal controls provide reasonable assurance that administrative expenditures were accurately reported in the accounting records, adequately safeguarded, and in compliance with applicable legal provisions and management's authorization?
- For the items tested, did the college comply, in all material respects, with the significant finance-related legal provisions concerning administrative expenditures?

Background

Lake Superior College's faculty and staff incur various operating and administrative expenditures to facilitate the educational mission of the college. Our audit focused on expenditures for purchased and consultant services, supplies, and equipment. Our audit also reviewed expenditures for presidential expense allowance and employee travel expenses. Table 6-1 shows a breakdown of each of these expenditures by fiscal year.

Table 6-1
Selected Administrative Expenditures
Budget Fiscal Years 2003 to 2005

Description	2003	2004	2005	9999 (Note 1)
Supplies	$3,757,359	$3,010,271	$3,275,480	$ 51,681
Purchased Services	1,509,695	2,158,096	1,987,100	92,357
Equipment Purchases	658,202	493,726	98,568	
Consultant/Contract Services	437,283	573,252	693,075	674,630
Employee Travel Expense	228,784	335,705	302,307	
Presidential Expense Allowance	1,090	1,511	1,289	

Note 1: Budget fiscal year 9999 represents appropriations that extend over a period greater than one year.

Source: MnSCU Accounting as of December 31, 2005.

Purchased and Consultant Services, Supplies, and Equipment

To purchase goods or services, college departments submitted a purchase requisition to the purchasing agent of the college. MnSCU policy established dollar thresholds that required specific procurement action on the part of the purchasing agent, including bid solicitation. The purchasing agent should assure the availability of funds in the appropriate cost center by initiating a system encumbrance in the MnSCU Purchase Controls System. Using the Purchase Control System, the purchasing agent generated a purchase order and sent it to the vendor. After the college received the goods or services, the business office matched the invoice to the purchase order and the receiving documentation. The business office then processed the payments on the MnSCU accounting system.

Presidential Expense Allowance

Presidential expense allowances, formally called department head expenses, permits the payment of certain expenses related to the duties and responsibilities of the president for which no other reimbursement is provided. The expense allowance is for the reimbursement of meals and related expenses for entertaining allowable business persons. The account can also be used to reimburse dues for college memberships in a private professional organization or individual membership in a professional organization. MnSCU procedure outlines the policies related to the presidential expense allowance account and establishes the annual expense account limit of $5,000. MnSCU also provides a department head expense expenditure information form to accompany any expenditure reimbursements. As explained in Finding 12, Chapter 3, Lake Superior College's employees improperly charged expenditures to the presidential expense allowance.

Employee Travel Expenses

Employee travel expenses generally were reimbursed to the employees through their bi-weekly paycheck. The employee expense process begins at the college when the employee completes a purchase order for the estimated amount of their local or out-state trip, their supervisor authorizes it, and the business office staff encumber the necessary funds. The employee then completes the employee expense report for the costs, such as trip miles, meals, personal telephone use, parking, and other reimbursable costs allowed by the employees bargaining unit. A supervisor must endorse and authorize the expense report. All required documentation for reimbursable costs must be included with the expense report. After the college processed the employee expense report, the employee received the reimbursed amount on their paycheck.

Current Findings and Recommendations

19. PRIOR FINDING NOT RESOLVED: The college did not solicit bids or prepare contracts for certain purchases.

Lake Superior College did not routinely solicit bids as part of its procurement process. Of the 28 samples requiring bids during fiscal year 2003 through 2005, 20 did not have evidence of any bids. MnSCU Procedure 5.14.5 stipulates the bidding requirements necessary to make certain purchases. The procedure establishes various dollar thresholds that require the number of bids and the process that must be followed. By not following the bidding requirements, the college may not receive the best price for the goods or services provided.

The college did not solicit bids for its food service operations. The college paid one vendor $24,781 in fiscal year 2003 and $29,452 in fiscal year 2004. In fiscal year 2005, this vendor became the main food service vendor, and payments increased to $55,904. Based on these amounts, the college should have obtained sealed bids. Also, it did not have a written contract with this vendor. The college should have written contracts detailing the prices and terms of the service and to ensure that all parties agree to the contract’s terms and provisions.

Also, the college did not develop written contracts for some purchased services, consultant, or professional/technical services. Of the 28 administrative expenditures tested, 17 did not have contracts between the college and the vendors as required by MnSCU Procedure 5.14.5, part 3. That procedure requires that all purchases must be prepared on contract forms approved by the system office to assure that they include all state required contract language. For example, the college used a purchase order instead of a written contract for a parking lot resurfacing project totaling $68,780. Although obtaining a service using only a purchase order may be appropriate in certain circumstances, such as when emergency services are needed, generally, the college should initiate formal contracts that clearly define the rights and duties of each party. By not preparing written contracts, there is no assurance that all of the required provisions are understood by both parties, and it is more difficult to enforce compliance with contract terms.

In addition, the college allowed work to be performed before it had a fully executed contract, in violation of MnSCU Procedure 5.14.2. One of the sampled consultant/contract services was performed before the contract was executed. Three payments totaling $3,570 were made from a purchase order before the contract was signed by the delegated authority.

Recommendations

- *Lake Superior College should follow MnSCU's bidding requirements when making purchases.*

- *Lake Superior College should use formal written contracts for required purchases.*

- *Lake Superior College should ensure that contracts are authorized and fully executed before a service is performed.*

20. The college did not maintain supporting documentation for certain supplies and equipment transactions.

The college did not always maintain supporting documentation for the decisions and/or transactions it made concerning supplies and equipment purchases. Our review of supplies and equipment purchases disclosed the following documentation weaknesses:

- Lake Superior College did not maintain bid documentation for four out of five sample items requiring bids. The total cost of these four items was $112,571.

- The college allowed departments to obtain their own bids or quotes. However, departments did not always submit the required documentation to the purchasing agent, as required by college policy.

- The college did not document the justification for using sole source vendors. Two sample items, totaling $46,310, were for goods the college stated could only be provided by a sole source vendor. Without documentation of the sole source determination, we were unable to determine if the college appropriately determined the vendor and the price of goods.

Recommendations

- *The college should retain sufficient documentation to support its bid process.*

- *The college should maintain adequate documentation to support its decision to use sole source providers.*

21. The college did not properly record certain expenditure transactions in the MnSCU accounting system.

The college recorded certain disbursement transactions using incorrect object codes and occurrence dates. We found that transactions recorded as supplies were not always supply purchases. For example, the college miscoded a payment totaling $68,780 for parking lot resurfacing to the supplies account. Other types of incorrectly coded transactions as supplies included travel, memberships, rent, flowers, food, and consortium payments to school districts.

In addition, the college did not record the correct occurrence dates on the accounting system and could not always provide sufficient documentation to support the recorded occurrence date for supplies and equipment transactions. The occurrence date is intended to capture the date the college received the goods and is used to identify the college's liabilities for financial reporting purposes. In 10 of 20 transactions tested, we could not determine the correct occurrence date. The college used the invoice date or the date it received the invoice for these transactions. This occurred because the business office did not always have packing slips or other documents supporting the date the goods were received. Properly recording the occurrence date is necessary to produce meaningful financial information for management as well as for reliable financial reporting.

Recommendations

- *The college should record transactions using the proper subobject codes and the correct occurrence dates.*

- *The college should require that packing slips or other forms of receiving evidence be submitted to the business office to document the date the college received the goods.*

22. The college did not comply with MnSCU credit card procedures.

The college did not comply with MnSCU procedures for the use of credit cards. According to MnSCU Procedure 7.3.3, the college may establish a credit card in the name of the college with a financial institution provider for official college use only. However, we found that the college also used vendor-issued charge cards to purchase goods. In addition, the college allowed someone not employed by the college to charge on one of the accounts. The college closed some of the charge card accounts, but as of March 2006, it still had eight noninstitution issued cards.

The college allowed employees to incur certain travel-related expenses, such as meals, on the college's credit cards. MnSCU Procedure 7.3.3 prohibits the use of credit cards for these types of expenses.

Also, as discussed in Finding 1, Chapter 2, the former vice president of finance and administration used the college's credit card for some costs and submitted the same claims on his expense reports. Because the college did not reconcile the credit card charges to the expense report, the college paid the credit card company and the employee for the same costs.

Recommendations

- *The college should not use vendor-issued charge cards.*

- *The college should only use the credit cards for allowable purchases.*

- *The college needs to reconcile credit card statements to the employee expense reports.*

23. The college has not conducted a complete inventory of its fixed assets.

The college has not conducted a complete inventory of its fixed assets. MnSCU Procedure 7.3.6 states that, "A physical inventory of all assets with an acquisition cost or value of $10,000 or greater shall be completed on an annual basis. A physical inventory of all other assets maintained in the equipment/capital asset module shall be completed on a cycle of no less than three (3) years." The college performed a physical inventory in fiscal year 2003. However, the college did not reconcile the results of that inventory with the fixed asset inventory balance in the MnSCU accounting system. The college conducted another physical inventory in March 2005 and identified approximately 900 discrepancies between the items counted and those on the inventory records. In April 2005, the college again attempted to conduct an inventory but did not complete it. The fixed asset records have not been adjusted.

Also, the college did not maintain a separation of duties over fixed assets. The same employee responsible for purchasing fixed assets performed the inventory verification. Without an independent review of inventory results, there is a risk that theft or errors could occur and not be detected. Someone independent of the purchasing function should complete the physical inventory.

Recommendations

- *The college should complete a physical inventory of its fixed assets and update the accounting records.*

- *Someone independent of the purchasing function should conduct the physical inventory.*

Chapter 7. Auxiliary Enterprise Activities

Chapter Conclusions

Lake Superior College's internal controls provided reasonable assurance that bookstore and food service revenues were properly collected, adequately safeguarded, and that it complied with applicable legal provisions and management's authorization. The college did not document voided or return transactions, as discussed in Finding 24. Finally, the college could not locate deposit records, as discussed in Finding 26.

For the items tested, except for the issues discussed below, Lake Superior College complied, in all material respects, with the significant finance-related legal provisions concerning enterprise activities. The college did not prepare annual financial statements for the enterprise activities, as discussed in Finding 25. In addition, the college did not solicit bids or prepare contracts for its food service operations, as discussed in Chapter 6, Finding 19.

Audit Objectives

Our audit of auxiliary enterprise activities focused on the following questions:

- Did the college's internal controls provide reasonable assurance that the bookstore and food service revenue collection were safeguarded, accurately recorded in the accounting records, and in compliance with applicable legal provisions and management's authorization?

- Did the college comply, in all material respects, with the significant finance-related legal provisions concerning bookstore and food service deposits?

Background

Lake Superior College's bookstore, food service operations, and parking fees are the main revenue activities within the college's Enterprise Fund. The revenues for fiscal years 2003-2005 are shown in Table 7-1. Parking fees were reviewed as part of our audit of tuition and fees, which was discussed in Chapter 3. Bookstore and food service activities had separate managers, but received administrative support from the college's business and human resources offices. The vice president of finance and administration is responsible for the financial oversight of the enterprises. The college is required by MnSCU procedure to maintain a multi-year business/ finance plan for its enterprise activities. Enterprise expenditures were tested as part of payroll and administrative expenditures and are included in chapters 5 and 6, respectively.

Table 7-1
Selected Enterprise Activities
Fiscal Years 2003 to 2005

Revenue Source	2003	2004	2005
Bookstore	$1,494,148	$1,701,228	$1,678,640
Food Service	211,062	209,248	261,384
Parking Fees	136,644	140,657	129,254
	$1,837,820	$2,047,036	$1,970,503

Source: MnSCU Accounting Records as of December 31, 2005.

Bookstore

The Lake Superior College bookstore sells textbooks and a wide variety of school and personal supplies. Revenues exceeded expenditures in each of the three fiscal years for a total cumulative gain of about $450,000. Students have the option of paying with cash, check, credit card, or charges to financial aid. The bookstore manager supervises two full-time employees as well as two to five student workers, depending on seasonal needs. Bookstore employees perform a physical inventory count at the end of each fiscal year, and the business office adjusts the bookstore inventory in MnSCU accounting to reflect actual inventory on hand.

Food Service

The Lake Superior College cafeteria provides meals, snacks, and beverages to college students, staff, and visitors. The cafeteria also offers catering services for college functions and other academic events. The food service enterprise sustained losses in all three fiscal years, resulting in a cumulative loss of nearly $163,000. Food services employ five employees, including two student workers. At the end of the day, the manager closes out the cash register and forwards the receipts to the business office for deposit. The college also earns food service revenues through an agreement with a local nonprofit organization for the rental of vending machines.

Current Findings and Recommendations

24. The college did not properly document voided or sales return transactions in the bookstore and food service operations.

The college's bookstore and food service activities supervisors did not consistently review and approve voided or sales return transactions. The college bookstore cashiers did not monitor or obtain approval for voids or return transactions. Student workers generally operated the cash register, and the bookstore manager reconciled the day's activity. The bookstore policy requires cashiers to fill out specific forms to document voided or return transactions. However, in 14 out of 19 daily bookstore deposits tested, the bookstore did not document some or all of the voided or return transactions.

Food services employees generally maintained a log of voided transactions and updated the log as voids occurred. A supervisor was responsible for approving each voided transaction. However, when food service employees were busy, a log was not maintained, and the voids were not documented and approved. A person independent of the register operator should review voided transactions. The lack of documentation and proper authorization increases the risk that amounts recorded as voids or returns are inaccurate or inappropriate.

The business office did not reconcile the food service void logs to the to the daily deposit reports. A reconciliation of the receipts that includes voids is necessary to substantiate the deposit amount. In fiscal year 2006, the food service purchased a new cash register that records each void and includes the voids in the recap of the day's receipts. The supervisor still needs to verify the propriety of each voided transaction.

Recommendation

- *Each void should be reviewed, verified, and approved by a supervisor.*

25. Lake Superior College did not comply with certain MnSCU procedures regarding reporting requirements for its bookstore and food service operations.

Lake Superior College did not prepare multi-year business plans or comprehensive annual financial statements for its enterprise activities during our audit period. MnSCU Procedure 7.3.2, part 5, requires colleges to prepare financial statements in accordance with generally accepted accounting principles for any auxiliary enterprise with an annual activity level in excess of $50,000. The business plan and annual financial statements are an essential process in ensuring that the college effectively and efficiently manages its auxiliary functions. Preparing financial statements would provide the college with complete and accurate financial information necessary in measuring the financial performance of the enterprise activities.

Recommendations

- *The college should prepare financial statements for its auxiliary enterprise activities in accordance with MnSCU procedures.*

- *The college should maintain a written multi-year finance/business plan for its auxiliary enterprise activities.*

26. The college could not locate all deposit records.

The college could not locate bookstore deposit records for 3 of the 19 days selected for testing. Two of those dates were in the months of July and August 2003. Both sample items were in the same box, and the college could not locate the entire box. The missing records prevented us from verifying that those receipts were properly collected, recorded, and deposited. *Minnesota Statutes* 2005, 15.17 requires officers and agencies of the state to preserve all records necessary to maintain a full and accurate knowledge of their official activities. To document the financial activity of the college, Lake Superior College needs to retain essential supporting documentation.

Recommendation

- *The college should maintain all accounting records in compliance with MnSCU's record retention policy.*

Status of Prior Audit Issues
As of March 17, 2006

Legislative Audit Report 03-51, issued in September 2003, covered the three fiscal years ending June 30, 2002. The audit scope included financial management, tuition and fees, employee payroll, administrative expenditures, and auxiliary enterprise revenues. The report contained seven audit findings. The department implemented four of the seven findings. Although the college collected repayment for the travel fees questioned, the former vice president of finance and administration offset the repayment by processing an unauthorized payment back to the faculty member. The college included the unauthorized payment amount in its claim against the former vice president of finance and administration, as discussed in Finding 1. The college did not resolve the issue related to timely registering students in customized training courses, as discussed in Finding 16. Finally, the college did not resolve the issue of preparing written contracts for consultants or contact services purchases. This issue is discussed in Finding 19.

State of Minnesota Audit Follow-Up Process

The Department of Finance, on behalf of the Governor, maintains a quarterly process for following up on issues cited in financial audit reports issued by the Legislative Auditor. However, Finance has delegated this responsibility for audits of Minnesota State Colleges and Universities (MnSCU) to the MnSCU Office of Internal Auditing. MnSCU's Office of Internal Auditing process consists of quarterly activity reports documenting the status of audit findings. The follow-up process continues until the Office of Internal Auditing is satisfied that the issues have been resolved. The process covers all colleges and universities within the MnSCU system.

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Lake Superior College

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Office of the President

James R. Nobles
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Office of the Legislative Auditor
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June 9, 2006

Re: Official Response to the Office of Legislative Auditor's Findings for Lake Superior College

This letter serves as Lake Superior College's official response to the Office of the Legislative Auditor's findings for the audit conducted for fiscal years 2003, 2004, and 2005. The audit was conducted during fiscal year 2006 and encompassed both the standard three-year audit conducted of Minnesota State Colleges and Universities' institutions and a more indepth audit of business functions following the termination of the college's Chief Finance Officer (CFO) in August of 2005. I want to thank the Office of the Legislative Auditor's investigative team of Marla Conroy and David Polisino and the audit team of Jack Hirschfield, Ellen Sibley, Tesfaye Negash, Tim Rekow and David Polisino for undertaking a very extensive audit to assist Lake Superior College in identifying those issues, business practices and policies needing review, revision, or creation in order to strengthen the business affairs and the internal controls of the institution. All members of these teams conducted themselves professionally, with an understanding of the institutional sensitivities surrounding the August termination of the CFO, and with respect for the college president's and college administrators' determination to correct all inappropriate, poorly designed, or missing policies and practices at the institution. I would also like to thank members of the Minnesota State Colleges and Universities' finance division and the system's Department of Internal Auditing for their support and assistance during the investigations leading up to this audit and during the audit period. They have been invaluable to the work of our college and to the assistance of our personnel.

Lake Superior College is a financially healthy institution. It charges the second lowest tuition of the system's colleges, maintains the maximum allowed reserve of 7%, is the system's most instructionally cost efficient college whose program mix includes technical education, and has a healthy total financial balance. Still, in the midst of such financial good health, we have clearly not had the fiscal controls in place that we have needed to ensure continued good health and to adequately safeguard our fiscal resources.

During the past ten months and in the few months just prior to the termination of the former Vice President of Finance and Administration, Lake Superior College reorganized the staffing within the Finance and Administration unit of the college to ensure greater professional oversight of all business functions and proper assistance to the college's Chief Finance Officer and President.

- A new Vice President of Finance and Administration was hired in January, 2006.
- The former Business Office Manager was reclassified to an accountant's position, removing supervisory responsibilities from her position. She terminated her work at the college during the fall term, 2005.
- A new accountant's position was created to assist the college's Business Office, and a new employee began her work in this position in March, 2006.
- A new Business Office Manager was recently hired and began his work at the college on May 15, 2006.
- A new clerical support position was created to assist the managers of the physical plant and food service and to assist all employees with travel arrangements. This individual began her work in this position in January, 2006.
- The Physical Plant Supervisor was reassigned and a new Physical Plant Director was hired in FY05 to assume greater oversight of issues relating to physical plant work, including the management functions of contracts, work with external contractors, and the monitoring of expenses relating to the physical plant operations.
- A new evening Physical Plant Supervisor was hired during FY06 to assist the Physical Plant Director with direct supervision of evening staff, allowing the Director more time to adequately complete his management responsibilities relating to general physical plant oversight.
- An audit was conducted of a position within the bookstore, creating a Bookstore Manager's position. This position was reallocated to a current employee during FY06. The creation of this management position will assist the Vice President of Finance and Administration with the creation of policies, the supervision of staff, and the management of business functions relating to the bookstore operations.

The college has also developed and implemented policies and procedures, where such were missing. These will be referenced throughout this response. Lake Superior College has conducted staff development or has provided training opportunities for business office staff and other employees regarding many of the findings cited in this report. I have worked with the new Chief Finance Officer to review and revise business office processes to ensure proper management and oversight and to abide by generally-accepted accounting practices. These procedural changes will also be noted in this response. Additionally, Lake Superior College has reviewed and revised processes within the Academic Affairs Office and, specifically, within the Department of Workforce and Community Development to ensure appropriate, timely, and accurate business transactions. Finally, I have analyzed personal fiscal reimbursements required of the former Vice President of Finance and Administration and have withheld accumulated annual leave payout to cover these charges. Additionally, a letter has been sent to the former Vice President to recover reimbursement beyond that covered by the annual leave payout.

Lake Superior College clearly understands that it has not had adequate policies and procedures in place to manage some of the college's business activities. Since I became aware of the issues addressed in this audit report in August of 2005 and in the ensuing months, I have garnered all of the institution's administrators' and managers' commitments to reviewing, revising, and implementing policy and structural changes to ensure good practice in business management and institutional operations. The college's personnel changes and its heightened awareness of critical business policies and procedures position it well to meet the educational and fiscal challenges in its future. I take full responsibility to ensure that all audit issues are addressed; that policies and procedures to affect strong internal controls are designed, implemented, and monitored; and that individual administrators and managers are held accountable for their roles in these activities.

I respectfully submit this letter and the attached response to the current findings as the institution's formal response to this audit.

Sincerely,

/s/ Kathleen L. Nelson

Kathleen L. Nelson, Ed.D.
President
Lake Superior College

Current Findings and Actions:

Finding #1: The college inappropriately reimbursed the former Vice President of Finance and Administration for $14,666 of ineligible expenses or duplicate claims.

- **Response and Action:** We agree with this finding. The President immediately placed the former Vice President of Finance and Administration on leave and removed his access to building and computer services as she learned about the Office of Internal Auditing's preliminary findings in early August of 2005. On August 20 she placed him on unpaid leave pending completion of a special OLA investigation in September. Upon review of those findings the President terminated him for gross misconduct on November 15, 2005. The findings of this report clearly support that action.

  The President has personally reviewed all findings of ineligible expenses and duplicate claims against the former Vice President of Finance and Administration as determined by the OLA and the Office of Internal Auditing. Since the former vice president was terminated for gross misconduct and there was no severance pay against which to charge these debts, all expenses were tallied and charged against the outstanding monetary value of the former vice president's annual leave. A letter was sent in late May to request payment of the remaining funds owed to the college. No response has yet been received from the former vice president.

  When the President learned of the former vice president's improper communication with a bidder, she immediately halted action relating to this contract (security services). The college maintained its security services for another year. The contract will be rebid in early FY07 and will be appropriately bid. All personnel associated with bidding practices have been instructed as to proper bidding protocols.

  The college has strengthened its reimbursement processes to ensure that all allowable expenses have appropriate documentation, that reimbursement requests are handled in a timely manner, and that personal reimbursement requests are cross-referenced to credit card statements for those administrators who have authorized credit card use.

  All managers and individuals accepting money on behalf of the college have been instructed that those receipts must be deposited within 24 hours of receipt. The new business office (occupancy in August, 2007) will have a night depository available to assist individuals with such deposits.

  All checks found in the former vice president's desk which were uncashed were reviewed by the former Business Office Manager who contacted the checks' makers to check current validity. None of the checks was able to be cashed. The value of these checks has been added to the reimbursement expected of the former vice president.

- **Person Responsible:** President and Vice President of Finance and Administration
- **Time Line for Completion:** Completed pending response from the former vice president and his payment of the remaining charges.

Finding #2: Lake Superior College did not establish an appropriate control environment.

Response and Action: We agree with this finding. Clearly, the findings of this audit and the investigations of the MnSCU Department of Internal Auditing and the Office of the Legislative Auditor demonstrated deterioration in internal control and compliance with MnSCU and state policies and procedures. The college's President will assume responsibility for ensuring that such findings are resolved and that, in the future, a strong system of internal control is established at the institution. In cooperation with the new Vice President of Finance and Administration, MnSCU's finance division, and the Office of Internal Auditing, the President will create a systematic, periodic review of all major fiscal and business control functions at the college. The college will also work with the administrators and managers as well as all employees to ensure they know of alternative channels for addressing their concerns or issues.

- **Person Responsible:** President and Vice President of Finance and Administration
- **Time Line for Completion:** Review plan developed by September, 2006.

Finding #3: The president did not effectively delegate authority for key financial decisions.

- **Response and Action:** We agree with this finding. Delegation of authority letters were completed and filed with the Office of the Chancellor as required by policy. These delegation letters did not, however, list specific dollar amounts. The letters of delegation for FY07 will be completed with more specifics and with dollar limitations. The President has reviewed all delegations with her Cabinet and has established more detailed lists of authority delegation. We agree that the former Vice President of Finance and Administration did not make such delegation authority known to members of the Business Office nor did he monitor the execution of such delegations within the business office. The current Vice President of Finance and Administration will create a monitoring system within the Business Office to check on appropriate use of delegation by the college's administrators and managers and will report the results of this review semi-annually to the President.

- **Person Responsible:** President and Vice President of Finance and Administration
- **Time Line for Completion:** Letters of delegation to be completed by July 1, 2006. First review and report due January 1, 2007.

Finding #4: The college did not have a procedure to implement its conflicts of interest policy.

- **Response and Action:** We agree with this finding. While administrators and managers knew about and discussed conflict of interest and potential impact upon their responsibilities and the college's administrators had training related to this issue, there was no formal form stating the applicable state statutes and MnSCU policy. However, employees who had conflicts of interest did indeed share that information with supervisors. We agree that the former Vice President of Finance and Administration did not disclose a conflict of interest with the college's President. The current Vice President of Finance and Administration and the Director of Human Resources created a form reflective of statute and policy for review by the President's Cabinet. The Cabinet approved the form in April, and all administrators and managers with purchasing authority have completed the form and have been instructed about the need to inform their supervisors if new potential conflicts surface. All employees have been informed about the state statutes and MnSCU policy and have been informed about what to do should such a conflict surface.

- **Person Responsible:** Vice President of Finance and Administration and Director of Human Resources
- **Time Line for Completion: C**ompleted.

Finding #5: The college did not adequately manage its financial budget process.

- **Response and Action:** We agree with this finding. While the college does have in place a clearly-defined decentralized budgeting process, we agree that the former Vice President of Finance and Administration did not ensure that all budget cost centers were loaded and available for use by cost center managers. Business Office staff are currently developing a system of providing appropriate, understandable and timely reports for cost center managers and will provide training on accessing and understanding these reports to allow cost center managers to accurately review the status of encumbrances and financial transactions taking place in the cost center. While training was provided to all managers who requested assistance with understanding budget reports, there was not systematic, required training.

  Individuals responsible for the inappropriate rollover of budgets taking place between fiscal years 05 and 06 have been clearly instructed by the current Vice President of Finance and Administration and the new Business Officer Manager as to appropriate procedures for recording accurate encumbrance information.

- **Person Responsible:** Vice President of Finance and Administration and the Business Office Manager
- **Time Line for Completion:** Budget process is established and is on-going. Monitoring reports system will be in-place by September 1, 2006. Training has begun and will continue.

Finding #6: In fiscal year 2006, the college inappropriately encumbered fiscal year 2005 funds for purchases made in fiscal year 2006.

- **Response and Action:** We agree with this finding. Encumbrances will not be made against a prior fiscal year. The Business Office Accountant is tasked with reviewing all encumbrances and verifying that they are in the appropriate fiscal year.

- **Person Responsible:** Vice President of Finance and Administration, Business Office Manager and Business Office Accountant.
- **Time Line for Completion:** Completed.

Finding #7: The college did not always encumber funds before incurring obligations.

- **Response and Action:** We agree with this finding. Since September, 2005, the accounts payable clerk has reviewed every requested payment for compliance with MnSCU policy 5.14.5 before processing for payment. When a violation of this policy is identified, the accounts payable clerk generates a "16A" form that must be completed by the originator of the expense, reviewed by the appropriate Vice President and approved by the Vice President of Finance and Administration. The payment is not made until the appropriate encumbrance is in place. Through this process, staff has determined that the primary reasons for expenses being incurred without the appropriate encumbrance are: employees being given authority to make purchases without appropriate training, lack of a timely and accurate system of providing current encumbered balances on purchase orders to cost center managers and those with purchasing authority in that cost center and a cumbersome system of providing additional budget authority throughout the fiscal year reflecting personal property and other fees collected in certain cost centers.

  To eliminate violation of statute, the following actions will be taken; the amount of anticipated personal property and other fees will be included in the initial budget of the appropriate cost center with adjustments made during the year for over/under in actual collections that will be reviewed and approved by the appropriate Vice President; the Business Office Manager will develop and implement a timely and accurate report system to allow cost center managers to monitor their own encumbrances; employees will not be given authority to make purchases without appropriate training; and the Business Office Manager will review all "16A" violations to determine remedial action which may include suspension of authority to make purchases of those individuals that cause a violation.

- **Person Responsible:** Vice President of Finance and Administration, Business Office Manager
- **Time Line for Completion:** September 1, 2006.

Finding #8: The college did not adequately limit computer access to certain business systems.

- **Response and Action:** We agree with this finding. With regard to the incompatible access in SCUPPS and the SEMA4 profile, we comply with the findings of the MnSCU established focus group on the appropriate security profile for this access. We will review the current access authority of all employees and identify incompatibilities and modify the access as appropriate. Each person serving as a cashier in the business office will use a unique cash drawer and employees will not share their user ID. Any new access authority request will be reviewed by the Business Office Manager for appropriateness and compatibility before being authorized.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** September 1, 2006.

Finding #9: The college did not separate certain key, incompatible financial duties over various functions.

- **Response and Action:** We agree with this finding. With the termination of the former Vice President of Finance and Administration and the resignation of the accountant, day-to-day duties of the Business Office had to be adjusted among the remaining six business office employees resulting in the temporary incompatibility of duties. The college has replaced the accountant position as of March 2006 and the new position of Business Office Manager was filled on May 15, 2006. The Business Office Manager will review the duties of all Business Office personnel, identify incompatibilities and provide the Vice President of Finance and Administration with a recommendation of duties by employee that provides segregation of duties in accordance with GAAP.

- **Person Responsible:** Vice President of Finance and Administration, Business Office Manager
- **Time Line for Completion:** September 1, 2006.

Finding #10: The college did not comply with MnSCU's special expense procedure.

- **Response and Action:** We agree with this finding. Effective September 22, 2005, a "Special Expense Request" procedure and form which are compliant with MnSCU Prodedure 5.20. 1 was put in place by the college's president.

- **Person Responsible:** President
- **Time Line for Completion:** Completed.

Finding #11: Lake Superior College did not comply with MnSCU's presidential expense allowance.

- **Response and Action:** We agree with this finding. The former Vice President of Finance and Administration did not alert business office staff and other employees as to the appropriate use of the presidential expense account object code. When the President learned about this finding, she sent a memo to the Business Office staff that, effective

August 26, 2005, they were to stop using the Department Head Expense object code for individuals other than the President. A form for authorization of the use of the account, approved only by the President was created and has been in use since August 26, 2005.

- **Person Responsible:** President
- **Time Line for Completion:** Completed.

Finding #12: The college did not maximize its investment earnings for funds in its local bank account.

- **Response and Action:** We agree with this finding. We are in the process of soliciting proposals from banks to provide local banking services for the college. One of the desired services is monthly customer analysis reports and quarterly face-to-face meetings with bank managers to analyze expenses and investment performance. We are currently working with our current banking partner to reduce expenses and increase interest earnings until we have a new relationship in place.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** New banking agreement in place by October 1, 2006.

Finding #13: Lake Superior College did not adequately monitor its accounts receivable balance.

- **Response and Action:** We agree with this finding. The Business Office Manager will review receivables on a monthly basis and provide an analysis of significant changes to the Vice President of Finance and Administration. The college has discontinued the policy of allowing an additional 20 days past the initial 120 days and will submit all accounts older than 120 days to MCE on the 121st day. A procedure will be established defining the required documentation to accompany the decision to not pursue collection.

- **Person Responsible:** Vice President of Finance and Administration, Business Office Manager
- **Time Line for Completion:** July 1, 2006.

Finding #14: Lake Superior College's cashiers did not obtain the required authorization prior to establishing certain tuition payment plans.

- **Response and Action:** We agree with this finding. The college is moving out of the practice of locally providing payment plans. Effective June 15, 2006, the college will be using FACTS Management Company for student payment plans which will greatly reduce the college's involvement in payment plans. Recognizing that there will occasionally arise a situation that is not conducive to using FACTS, the college is developing a policy and procedure for providing a local student payment plan that will be administered by the Vice President of Finance and Administration. This procedure will stipulate the conditions under which the college will enter into a payment plan, the terms of such plans and resolution of defaults.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** August 1, 2006.

Finding #15: The college has not effectively established or controlled tuition waivers.

- **Response and Action:** We agree with this finding. Some of the incidents described in this section of the report are reflective of coding errors. The college's new accountant has reviewed the coding and is aware of the correct codes to use in order to make adjustments to various types of billing errors. LSC will commit to writing, its tuition waiver policy and the process to be used to complete such waivers. The policy will include the student's right to appeal the policy.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** August 1, 2006.

Finding #16: PRIOR AUDIT FINDING NOT RESOLVED: The college did not properly register some customized training students.

- **Response and Action:** We agree with this finding. LSC has made administrative changes in the registration process for students enrolled through the ERTC and other customized training programs. The Vice President of Academic Affairs and the Dean of Workforce and Community Development will monitor the registration process to ensure that such errors do not continue.

- **Person Responsible:** Vice President of Academic Affairs and Dean of Workforce and Community Development
- **Time Line for Completion:** Completed.

Finding #17: Lake Superior College did not properly execute customized training contracts.

- **Response and Action:** We agree with this finding. The Vice President of Academic Affairs and the Dean of Workforce and Community Development have designed a system whereby there will be careful monitoring of all contract signing within this division. All contracts will be signed prior to the start of classes. The original of all signed contracts will be housed in the college's Business Office. A copy of each contract will be maintained in the office of the Dean of Workforce and Community Development.

- **Person Responsible:** Vice President of Academic Affairs and Dean of Workforce and Community Development
- **Time Line for Completion:** Completed.

Finding #18: The college did not deposit tuition, customized training, and food service receipts in a timely manner.

- **Response and Action:** We agree with this finding. The newly added Business Office Manager will be tasked with assuring that deposits of daily receipts in excess of $250 will be made daily. The Vice President of Finance and Administration will review compliance on a monthly basis.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** Completed.

Finding #19: PRIOR AUDIT FINDING NOT RESOLVED: The college did not solicit bids or prepare contracts for certain purchases.

Response and Action: We partially agree with this finding. We believe the MnSCU Office of Internal Auditing has evidence that the prior finding was resolved and appropriate processes implemented. However, either deteriorating controls or the inability of the college to locate documents accounts for the present finding. The Vice President of Finance and Administration will review the requirements of MnSCU Procedure 5.14.5 and MN Statute 471.345 with all Business Office staff, budget unit leaders and managers. The Vice President of Finance and Administration will review compliance on a monthly basis.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** July 1, 2006.

Finding #20: The college did not maintain supporting documentation for certain supplies and equipment transactions.

- **Response and Action:** We agree with this finding. The college will implement policy and procedure specifying the documentation required to be retained for purchases made by contract, whether competitively bid or sole source.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** July 1, 2006.

Finding #21: The college did not properly record certain expenditure transactions in the MnSCU accounting system.

- **Response and Action:** We agree with this finding. The college will implement written procedures to assist staff in determining appropriate coding and occurrence date on all transactions.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** July 1, 2006.

Finding #22: The college did not comply with MnSCU credit card procedures.

- **Response and Action:** We agree with this finding. The college will close all noninstitution-issued accounts and will comply with MnSCU Procedure 7.3.3. In August, 2005, administrators with authorization to use state credit cards (the President and her direct reports) created a system of cross-referencing reimbursement requests with state credit card statements. This cross-referencing is done by the President's Executive Assistant prior to final approval of the reimbursement forms.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** June 15, 2006.

Finding #23: The college has not conducted a complete inventory of its fixed assets.

- **Response and Action:** We agree with this finding. The Vice President of Finance and Administration and the Business Office Manager will review the procedures used in the previous inventories and determine the most appropriate method of resolving past issues and discrepancies, which may include hiring an outside entity to perform a complete inventory.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** August 1, 2006.

Finding #24 The college did not properly document voided or sales return transactions in the bookstore and food service operations.

- **Response and Action:** We agree with this finding. The college has instituted procedures to ensure that all voids are reviewed, verified and approved by the appropriate operation manager. Student workers in the bookstore are no longer allowed to void transactions and must have a regular employee complete any voided transaction.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** Completed.

Finding #25: Lake Superior College did not comply with certain MnSCU procedures regarding reporting requirements for its bookstore and food service operations.

- **Response and Action:** We agree with this finding. The college will prepare separate financial statements at the close of FY 06 and prepare multi-year finance/business plans for the three enterprise activities.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** September 1, 2006.

Finding #26: The college could not locate all deposit records.

- **Response and Action:** We agree with this finding. At the time of the suspension of the former Vice President of Finance and Administration, the college moved as many records as possible to an offsite, secure location. It is suspected that the box containing the missing deposit records was mis-labeled and, therefore, not retrieved from the secure warehouse. The college has recently approved a master document retention schedule which is now in place. Secure centralized storage for records is part of the business office space within the new addition that will be completed in August 2007.

- **Person Responsible:** Vice President of Finance and Administration
- **Time Line for Completion:** Completed.