Southwest State University

Financial Audit
For the Period July 1, 1995 through June 30, 1998

August 1999

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Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

99-43

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SUMMARY

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Southwest State University

Financial Audit
For the Period July 1, 1995, through June 30, 1998

Public Release Date: August 19, 1999 No. 99-43

Background

Southwest State University was authorized by the 1963 Minnesota Legislature as the state's only four-year liberal arts and technical university. In 1967 the university opened its doors. Southwest State University is part of the Minnesota State Colleges and Universities (MnSCU) system, which began operations on July 1, 1995. Southwest State University has approximately 3,200 students and is located in Marshall, Minnesota. Dr. Douglas Sweetland is the university's president.

Audit Scope and Conclusions

Our audit scope included a review of the university's financial management, tuition and fees, room and board revenues, employee and student payroll, selected expenditure areas, and miscellaneous revenues for the period July 1, 1995, through June 30, 1998. We also reviewed the college's internal controls over compliance with federal student financial aid for fiscal year 1999.

We found that the university designed and implemented internal controls to provide reasonable assurance that financial activities were properly recorded. The university operated within its financial resources and had an appropriate relationship with its related foundation. Generally, the university provided reasonable assurance that money in local bank accounts was adequately safeguarded. However, in two months, local bank account balances were not properly collateralized. The university designed internal controls to provide reasonable assurance that it managed student financial aid programs in compliance with legal requirements.

Generally, the university designed and implemented controls to provide accurate recording of revenues, payroll, and other expenditures. We identified some weaknesses in internal controls over tuition and fee adjustments, entry fees, and administrative expenditures. We also noted that the university's access privileges to computerized accounting and payroll business systems were not adequately restricted.

In its response, Southwest State University generally agreed with the audit findings and is taking corrective action to resolve the issues.

STATE OF MINNESOTA
OFFICE OF THE LEGISLATIVE AUDITOR
JAMES R. NOBLES, LEGISLATIVE AUDITOR

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Mr. Morrie Anderson, Chancellor
Minnesota State Colleges and Universities

Members of the Minnesota State Colleges and Universities Board of Trustees

Dr. Douglas Sweetland, President
Southwest State University

We have audited Southwest State University for the period July 1, 1995, through June 30, 1998, as further explained in Chapter 1. Our audit scope included tuition and fees, employee and student payroll, selected administrative expenditures, and other miscellaneous revenue. We also reviewed the college's internal controls over compliance with federal student financial aid for fiscal year 1999.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, as issued by the Comptroller General of the United States. Those standards require that we obtain an understanding of management controls relevant to the audit. The standards require that we design the audit to provide reasonable assurance that Southwest State University complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the college is responsible for establishing and maintaining the internal control structure and complying with applicable laws, regulations, contracts, and grants.

This report is intended for the information of the Legislative Audit Commission, the management of Southwest State University, 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 August 19, 1999.

James R. Nobles	Claudia J. Gudvangen, CPA
Legislative Auditor	Deputy Legislative Auditor

End of Fieldwork: June 18, 1999

Report Signed On: August 16, 1999

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Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Jeanine Leifeld, CPA, CISA	Audit Manager
Sonya Johnson, CPA	Auditor-in-Charge
Terry Hanson	Auditor
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Exit Conference

We discussed the findings and recommendations with the following representatives of Southwest State University and the MnSCU system office at the exit conference held on July 30, 1999:

Southwest State University:	
Doug Sweetland	President
Doug Fraunfelder	Associate Vice President for Finance and Human Resources
Debra Kerkaert	Business Manager
MnSCU System Office:	
Laura King	Vice Chancellor, Chief Financial Officer
Rosalie Greeman	Associate Vice Chancellor, Financial Reporting
Beth Hammer Buse	Deputy Director, Office of Internal Audit
Marilyn Hansmann	Internal Audit Coordinator

Chapter 1. Introduction

Southwest State University was authorized by the 1963 Minnesota Legislature as the state's only four-year liberal arts and technical university. In 1967 the university opened its doors. Southwest State University is part of the Minnesota State Colleges and Universities (MnSCU) system, which began operations on July 1, 1995. The campus is located 150 miles southwest of the Twin Cities in Marshall, Minnesota. Dr. Douglas Sweetland is the university's president.

Southwest State University has approximately 3,200 students with a majority of them coming from the southwest region of Minnesota. The university offers 43 baccalaureate majors, 4 associate degree majors, and 38 minors. In addition, it offers two master degree programs and six certifications. Students can enter a four-year bachelor's degree program (Bachelor of Science, Bachelor of Arts, or Bachelor of Applied Technology), a two-year associate degree (associate in science) program, or one of 16 pre-professional programs. The university's largest program areas are business and education at both the graduate and undergraduate level.

The university finances its operations primarily from state appropriations and student tuition and fees. MnSCU receives the majority of its funding for operations from General Fund appropriations. The MnSCU system office allocates funds to Southwest State University and other MnSCU campuses based upon an allocation formula. Southwest State University, like other institutions, retains tuition and other dedicated revenues to obtain total resources available for operations. Table 1-1 provides a summary of the university's sources and uses of funds reported in the General Fund, Special Revenue Funds, and Enterprise Funds for the fiscal year ended June 30, 1998.

Table 1-1
Southwest State University
Sources and Uses of Funds
Fiscal Year Ended June 30, 1998

	General Fund	Special Revenue Fund	Enterprise Funds
Beginning Balance	$1,314,583	$83,752	$2,384,704
Sources			
State Appropriation Allocation	$13,305,117	0	0
Tuition, Fees, Room and Board (1)	6,292,968	353,306	2,808,075
Rents and Sales	205,787	365,814	545,877
Federal Grants	0	1,875,074	0
State Grants (2)	578,399	790	0
Private Grants	40,377	49,254	12,898
Other	663,549	134,602	1,049,018
Total Sources	$21,086,197	$2,778,840	$4,415,868
Uses			
Employee Payroll	$15,330,166	$409,191	$789,767
Student Payroll	297,678	177,365	202,341
Purchased Services	653,235	119,771	1,239,502
Contracts/Consultants	1,516,660	153,943	142,075
Utilities	542,230	0	198,118
Supplies and Equipment	941,679	146,092	335,065
Financial Aid	81,760	1,302,206	82
Other	921,354	266,300	177,609
Transfers Out	409,124	106,194	146,778
Total Uses	$20,693,886	$2,681,062	$3,231,337
Fund Balance at June 30, 1998	$ 1,706,894	$ 181,530	$3,569,235

(1) Amount shown is net of refunds.

(2) Includes a grant totaling $519,274 from the Minnesota Higher Education Services Office to finance a telecommunications network among a cooperative of specific institutions in southwestern and west central Minnesota.

Note: The table is for informational purposes and only presents selected funds of the university. It is not intended to be a complete financial analysis of all university activities. The financial information is presented on the budgetary basis of accounting. This basis does not include long-term assets and liabilities. Examples of financial activities not included in the table are tuition receivables not collected at the close of the books and compensated absence liabilities, totaling $2,014,984 as of June 30, 1998. The university indicated that its General Fund reserve at June 30, 1998, was $406,564.

Source: Auditor prepared from MnSCU acco unting data.

Chapter 2. Financial Management

Chapter Conclusions

Southwest State University designed and implemented internal controls to provide reasonable assurance that financial activities were properly recorded on the MnSCU and MAPS accounting systems. However, we noted that the university did not adequately restrict computer access in several areas. The university operated within its financial resources and had an appropriate relationship with its related foundation. Generally, the university provided reasonable assurance that money in local bank accounts was adequately safeguarded. However, in two months, local bank account balances were not properly collateralized.

On July 1, 1995, the consolidated Minnesota State Colleges and Universities System (MnSCU) began operations. At that time, a new computerized accounting system, MnSCU accounting, as well as the State Colleges and Universities Personnel/Payroll System (SCUPPS) were implemented. MnSCU required all campuses to use the MnSCU accounting system to account for money maintained within the state treasury and local bank accounts maintained outside the state treasury. Southwest State University administered certain funds, including financial aid, in a local bank account. A different account served as the state depository for transfer of funds into the state treasury.

The State of Minnesota also implemented computerized financial and personnel/payroll systems in 1995. The state's accounting system (MAPS) is the primary accounting system for funds appropriated to state agencies. The university used the MnSCU accounting system to initiate transactions that involved appropriated funds. Through a system interface, the MnSCU accounting system updates these transactions into MAPS, which generates state treasury warrants for state-appropriated expenses. Similarly, the State Employee Management System (SEMA4) is used to generate payroll warrants initiated in the university's SCUPPS subsystem.

Southwest State University is affiliated with the Southwest State University Foundation, a non-profit organization. The foundation has its own board of directors and bylaws. The university provided administrative support to the foundation during the audit period. Foundation financial statements are subject to an external audit by an independent CPA firm. As of June 30, 1998, the foundation had an ending fund balance of $5.4 million.

Audit Objectives and Methodology

Our review of Southwest State University's overall financial management focused on the following objectives:

Southwest State University

- Did the university design and implement internal controls to provide reasonable assurance that financial activities were properly recorded on the MAPS and MnSCU accounting systems?

- Did the university design and implement internal controls to provide reasonable assurance that it operated within available financial resources?

- Did the university design and implement internal controls to provide reasonable assurance that monies in local bank accounts were adequately safeguarded, accurately reported in the accounting records, and in compliance with applicable legal provisions and management's authorization?

- Did the university have an appropriate operating relationship with its related foundation?

To answer these questions, we interviewed college staff to gain an understanding of how the MnSCU accounting system is used for the programs in our audit scope. We also gained an understanding of management controls, including budgeting, budget monitoring, and reconciliations in place over state treasury and local bank account activities. We reviewed local bank activity to determine compliance with material finance-related legal provisions, such as collateral sufficiency. Finally, we reviewed security privileges to determine whether the university had adequately restricted access to its computerized business systems.

Conclusions

Southwest State University designed and implemented internal controls to provide reasonable assurance that financial activities were properly recorded on the MnSCU and MAPS accounting systems. However, we noted that the university did not adequately restrict computer access in several areas. The university operated within its financial resources. The business office staff and individual departments reviewed monthly budgetary summary and detail transaction reports in order to monitor and manage budgets. Generally, the university provided reasonable assurance that money in local bank accounts was adequately safeguarded. However, in two months, local bank account balances were not properly collateralized. The university maintained an appropriate relationship with its related foundation.

1. Southwest State University did not maintain sufficient collateral for its local bank account during two months in 1999.

The university did not maintain adequate collateral on its local bank account funds for 15 days during January and February 1999. Due to a problem with the university's computer system at the beginning of spring semester, the university was unable to produce certain edit reports used by the school for key balancing and reconciliations. As a result, the institution did not process local bank account checks during that time, causing unusually high balances in the account.

In order for its money to be properly protected, the university should ensure that the bank provides sufficient collateral at all times. Government entities should establish collateral on their accounts equal to at least ten percent more than the amount on deposit plus accrued interest at the close of the business day. Because of this incident, the bank increased the college's collateral level in March 1999.

Recommendation

- *Southwest State University should ensure that it maintains collateral sufficient for balances in its local bank account.*

2. Southwest State University did not adequately restrict certain computer security access privileges.

Southwest State University did not adequately administer and control access to specific computerized systems, including payroll, accounts receivable, and procurement. The university has the ultimate responsibility to ensure that employee access is necessary based upon job responsibilities. Our review of computer security access disclosed the following:

- Three institution computer services personnel had clearances to perform business office functions, including purchasing, disbursing, and cashiering. These clearances were not necessary in order to perform their job duties.

- Six business office staff had incompatible clearances in relation to the duties they performed. For example, several employees had the ability to both make purchases and payments in the accounting system. These clearances increase the risk that inappropriate transactions could be initiated and go undetected.

- One personnel employee had access to both payroll functions in SEMA4 and human resource functions in SCUPPS. Access to both personnel and payroll could permit the employee to make unauthorized personnel changes and use those transactions to initiate unauthorized payroll transactions.

- Two employees had payroll clearances that were more powerful than necessary to complete their job responsibilities. They had full payroll access, even though their only responsibility was to process employee business expense claims.

- Two former business office employees, including the previous business manager, still had access to some system functions.

- Several MnSCU system office employees had the ability to update Southwest State University accounting system data. It was not known whether these system office staff have job responsibilities requiring them to update system transactions for the university.

The university did not appear to have a process in place to monitor the computer security clearances of its users on an ongoing basis. The university should monitor computer security clearances to ensure that users only have the access necessary to perform their duties.

Recommendation

- *Southwest State University should periodically monitor computer security clearances to ensure that:*

  -- *users only have the required clearances to perform their jobs,*

  -- *employees who no longer work at the university have their access deleted, and*

  -- *users with incompatible access privileges have those privileges modified.*

Chapter 3. Tuition, Fees, and Room and Board Revenue

Chapter Conclusions

Generally, Southwest State University designed and implemented internal controls to provide reasonable assurance that tuition, fees, and room and board revenue were adequately safeguarded, accurately recorded in the accounting records, and in compliance with legal provisions. However, we noted that the university did not perform an independent review of administrative adjustments made to fee revenues. Southwest State University complied, in all material respects, with significant finance-related legal provisions concerning tuition, fees, and room and board revenue for the items tested.

Southwest State University collected approximately $20.5 million in tuition and fees during fiscal years 1996 through 1998. Resident tuition rates were $49.05, $78.00, and $80.35 per credit plus fees for the 1995-96, 1996-97, and 1997-98 school years, respectively. In school year 1996-97, the university converted from quarters to semesters. Tuition, fees, and room and board revenue for the three fiscal years 1996, 1997, and 1998 are shown in Table 3-1.

Table 3-1
Tuition and Fee Revenue
Fiscal Years 1996, 1997, and 1998

Revenue Source:	1996	1997	1998
Tuition	$5,239,388	$5,573,429	$6,330,233
Fees	1,053,419	1,112,093	1,139,523
Room and Board	2,251,389	2,287,471	2,400,331
Less Refunds	(40,823)	(185,523)	(357,406)
Net Total	$8,503,373	$8,787,470	$9,512,681

Note: This table includes approximately $58,000 of Agency Fund activity that is not included in Table 1-1.

Source: Fiscal years 1996, 1997, and 1998 tuition and fee data from the MnSCU accounting system.

The university collects tuition and fees from all students attending courses at the university. In addition, the university collects room and board fees from students who elect to stay on campus or purchase meal plans. Students register for courses at the registration offices through the registration system. Students also have the option of selecting housing and meal plans through the housing system located at the housing office. Both the registration and housing systems feed data into the accounts receivable system. The accounts receivable system tracks and maintains the student's registration, housing, and account information. The university uses the accounts receivable system to collect payments from students and track outstanding balances.

Audit Objectives and Methodology

Our review of Southwest State University's tuition and fee revenues focused on the following questions:

- Did the university design and implement internal controls to provide reasonable assurance that revenue collections were adequately safeguarded, accurately reported in the accounting records, and in compliance with applicable legal provisions and management's authorization?

- For the items tested, did the university comply, in all material respects, with the significant finance related legal provisions concerning tuition?

To answer these questions, we reviewed the controls over tuition and fee billing, collection, and deposit. We also tested, on a sample basis, transactions to determine if the university accurately recorded transactions on the MnSCU accounting system. In addition, we reconciled the credits awarded on the registration system to the tuition revenue recorded on the MnSCU accounting system.

Conclusion

The university generally designed and implemented internal controls to provide reasonable assurance that tuition, fees, and room and board revenues were adequately safeguarded, accurately reported in the accounting records, and in compliance with legal provisions and management's authorization. For the items tested, the university complied, in all material respects, with significant finance related legal provisions concerning tuition. However, as explained in the finding below, we noted a weakness in the internal control structure over tuition with regards to adjustments.

3. The university did not adequately control adjustments made to tuition, fees, and room and board receipts.

The university did not have adequate controls over adjustments cashiers made to accounts receivable records. The cashiers collected tuition, fees, and room and board receipts. They also entered the receipts into the billing system, prepared deposits, gave out refunds, and made adjustments to the student account receivable records. This set of responsibilities allowed the cashiers to have complete control over collecting receipts and recording those receipts into the accounting system A separate person reconciled the accounting records to the bank statements. However, there was no independent review of any adjustments the cashiers made to the accounting records while initially recording incoming receipts. The lack of an independent review increases the risk of errors or irregularities occurring and going undetected.

Recommendation

- *Southwest State University should perform an independent review of accounting record adjustments made to tuition, fee, and room and board receipts.*

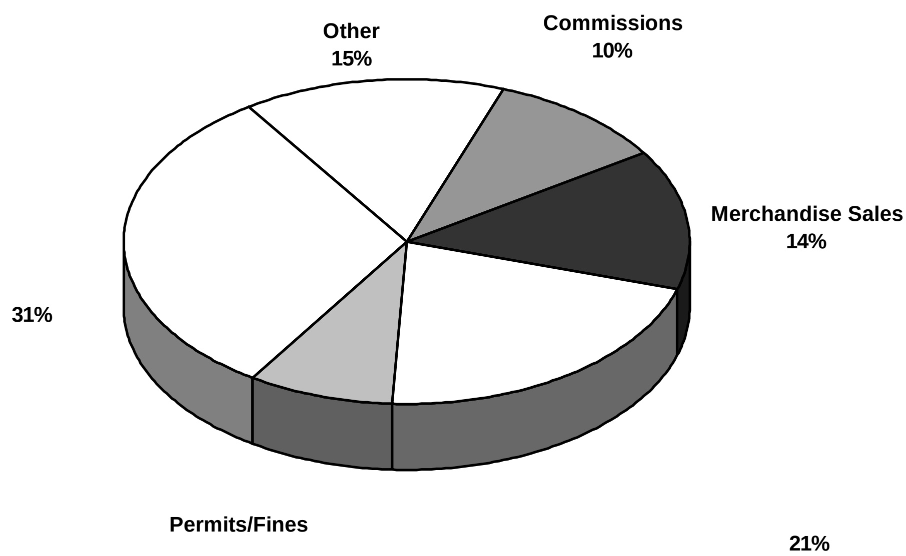
Chapter 4. Rent and Sales Revenue

Chapter Conclusions

Southwest State University designed and implemented internal controls to provide reasonable assurance that rent and sales revenue was adequately safeguarded, accurately recorded in the accounting records, and in compliance with applicable legal provisions. However, we found that the university needs to improve internal controls over certain sports camp fees. We also found that the institution coded some revenues to the wrong fiscal year. For the items tested, Southwest State University complied, in all material respects, with significant finance-related legal provisions concerning rent and sales revenue.

Southwest State University collects rent and sales revenues from contractual agreements, parking, sale of merchandise, and other campus activities. The university collected approximately $1.1 million of these revenues during fiscal year 1998. The sources of rent and sales revenues for fiscal year 1998 is shown in Figure 4-1.

Figure 4-1
Sources of Rent and Sales Revenues
Fiscal Year 1998



Source: Fiscal year 1998 rent and sales data from MnSCU accounting system.

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Audit Objectives and Methodology

Our review of Southwest State University's rent and sales revenues focused on the following questions:

- Did the university design and implement internal controls to provide reasonable assurance that rent and sales collections were adequately safeguarded, accurately reported in the accounting records, and in compliance with applicable legal provisions?

- For the items tested, did the university comply, in all material respects, with the significant finance-related legal provisions concerning rent and sales revenues?

To answer these questions, we reviewed the controls over revenue billing, collection, and depositing. We also tested, on a sample basis, transactions to determine if the university accurately recorded transactions on the MnSCU accounting system. In addition, we performed analytical procedures on multiple sources of revenues.

Conclusion

The university designed and implemented internal controls to provide reasonable assurance that rent and sales revenues were adequately safeguarded, accurately reported in the accounting records, and in compliance with legal provisions. For the items tested, the university complied, in all material respects, with significant finance related legal provisions concerning rent and sales revenue. However, we noted certain weaknesses in the internal control structure over rent and sales revenue as discussed in the findings presented below.

4. The university had inadequate controls over certain sports camp fees.

The university did not adequately segregate duties over the collection, recording, and depositing of entry fees. The university collects entry fees for various sport camps coached by university coaches. The university's main camps are football, volleyball, and basketball. Each camp had a slightly different process for recording, collecting, and depositing receipts. However, in all instances, one person was responsible for recording the receipts and had access to the funds prior to deposit. The receipts were not collected at the business office. In addition, the university did not perform reconciliations of revenue collected to the number of people attending camp. Lack of segregation of duties and lack of a reconciliation to independent source documentation increased the risk of errors and irregularities occurring and going undetected in the ordinary course of business.

Recommendations

- *The university should segregate sports camp fee collection and recording duties.*

- *The university should perform a reconciliation between entry fee receipts and the number of individuals attending the camps.*

5. The university miscoded some rent and sales revenues.

The university coded revenues totaling $71,800 to incorrect fiscal years. The university coded various lease, housing, bookstore, and food service revenues to the wrong fiscal years by using incorrect occurrence dates in the accounting system. In some cases, the university used the date of receipt as the occurrence date, rather than the date in which the university earned the revenue. For example, revenue received in July 1997 for June 1996 services was coded to fiscal year 1997 instead of fiscal year 1996. Because of this incorrect coding, MnSCU did not properly reflect the year's total revenues on the system's financial statements.

Recommendation

- *The university should code revenues to the fiscal year in which they were earned.*

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Chapter 5. Employee and Student Payroll

Chapter Conclusions

Southwest State University designed and implemented internal controls that provided reasonable assurance that employee and student payroll transactions were properly authorized and accurately reported in the accounting records. The university complied with statutory provisions and bargaining unit agreements for employee payroll. However, as noted in Finding 2, the university did not adequately restrict certain incompatible clearances to the human resources and payroll systems.

Payroll represents the largest expenditure for Southwest State University. The university had employee payroll expenditures of $48,280,862 for fiscal years 1996 through 1998. The university also paid $2,238,953 in student payroll expenditures during the same time period.

Audit Objectives and Methodology

We focused our review of payroll expenditures on specific audit objectives related to the following questions:

- Did the university design and implement internal controls to provide reasonable assurance that employee and student payroll expenditures were properly authorized and accurately reported in the accounting records?

- Did the university's payroll expenditures comply with applicable statutory provisions and related bargaining agreements?

To answer these questions, we obtained an understanding of the internal control structure over the payroll and personnel processes. We interviewed university employees to gain an understanding of the personnel and payroll accounting systems used by the university and observed procedures used to process and reconcile payroll transactions. We reviewed the security clearances for payroll and human resource personnel. We performed various analytical and detail tests of employee and student payroll transactions to support our conclusions.

Employee Payroll Processing

Southwest State University employed approximately 120 full-time and 75 part-time faculty during fiscal year 1998. The university also employed about 194 staff and administrators. The following organizations represent the university's employees:

- The Inter Faculty Organization (IFO)
- The Minnesota State University Association of Administrative and Service Faculty (MSUAASF)
- The American Federation of State, County and Municipal Employees (AFSCME)
- The Middle Management Association (MMA)
- The Minnesota Association of Professional Employees (MAPE)

In fiscal year 1996, the university used the state's personnel/payroll system (PPS) and the State Colleges and Universities Personnel/Payroll System (SCUPPS) to process payroll information. The university used SCUPPS to store pay rate information and bargaining agreement history, and to monitor and evaluate compensation paid to employees. The institution also used SCUPPS to identify the different types of classification assignment codes pertaining to faculty appointments. PPS contained pay rate information and calculated the employee payroll amount. PPS also handled leave accruals for classified and unclassified employees. The university converted to the State Employee Management System (SEMA4) human resource/payroll system in early fiscal year 1997.

The university maintained separate human resource and payroll offices to handle personnel and payroll transactions. Human resource staff input personnel transactions into SCUPPS. The payroll section recorded employee payroll data into SEMA4.

Student Payroll

The university employed students to perform various job duties throughout the campus. The university participated in both the federal and state work-study programs, allocating funding to students based on financial need. The university also paid certain students from institutional funds. The university's financial aid office entered appointment and tax information into the student payroll system. Students completed bi-weekly timesheets that their supervisors approved. The business office entered the timesheets into the student payroll system which generated the payroll checks. Students subsequently picked up their payroll checks at the business office.

Conclusions

Southwest State University designed and implemented internal controls that provided reasonable assurance that employee and student payroll transactions were properly authorized and accurately reported in the accounting records. The university complied with statutory provisions and bargaining unit agreements for employee payroll. However, as noted in Finding 2 in Chapter 2, the university assigned certain users incompatible clearances to payroll and personnel transactions.

Chapter 6. Selected Administrative Expenditures

Chapter Conclusions

Southwest State University designed and implemented internal controls to provide reasonable assurance that selected administrative expenditures were accurately recorded in the accounting records and in compliance with applicable legal provisions and management's authorization. However, as noted in Finding 2, the university did not adequately restrict certain incompatible clearances to the accounting system. Also, the university also did not complete an inventory count and properly record fixed assets on the MnSCU accounting system. Finally, the university failed to properly encumber funds in the MnSCU accounting system for some library expenditures.

We audited selected Southwest State University administrative expenditures, including supplies, equipment, purchased services, consultant services, and utilities. Table 6-1 provides a breakdown of the audited areas for the three fiscal years included in our scope.

Table 6-1
Southwest State University
Selected Administrative Expenditures
Fiscal Years 1996 - 1998

	1996	1997	1998
Purchased Services	$2,737,758	$2,001,141	$2,112,853
Consultant / Contract Services	1,483,136	1,641,585	1,860,140
Supplies and Materials	1,073,284	1,452,141	1,117,832
Utilities	721,111	741,644	740,348
Equipment	406,809	1,300,792	313,974
Total	$6,422,098	$7,137,303	$6,145,147

Note: This table includes certain Agency Fund activity that is not included in Table 1-1.

Source: MnSCU accounting system for fiscal years 1996, 1997, and 1998.

A centralized purchasing department within the university is responsible for procuring goods and services, following MnSCU guidelines. Administrative and academic departments initiate purchase requests by creating an internal requisition form and forwarding it to the business office. According to MnSCU guidelines, the purchasing department obtains two or more written quotations for purchases from $1,001 to $25,000. Purchases in excess of $25,000 require a sealed bid. The business office receives evidence of receipt of goods and approves invoices. The accounts payable clerks matches invoices to the open purchase orders and receiving evidence before processing payments.

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Southwest State University defines equipment as all machinery, vehicles, instruments, apparatuses, furniture, and other articles that meet all of the following requirements:

- a unit cost of $2,000 or more,
- a useful life of more than one year, and
- retains its identity for inventory purposes.

The university identifies and tags new equipment with a State of Minnesota identification sticker. New equipment should be recorded and tracked on MnSCU's fixed asset system. MnSCU policy requires institutions to record fixed assets valued at over $2,000. Fixed assets valued between $500 and $1,999 are recorded at the university's discretion.

Audit Objectives and Methodology

The primary objectives of our review of supplies, equipment, purchased and consultant services, and utilities expenditures were as follows:

- Did Southwest State University design and implement internal controls to provide reasonable assurance that assets acquired were adequately safeguarded, expenditures were for goods and services actually received, and transactions were accurately recorded in the accounting system?

- Did the university comply with applicable legal provisions governing procurement and disbursements?

To meet these objectives, we interviewed university employees to gain an understanding of the internal controls over the procurement and disbursement processes for services, supplies, and equipment. We performed analytical reviews and tested transactions to determine if the university properly procured, disbursed, and recorded selected administrative expenditures in the accounting system. Finally, we reviewed the university's process to record and track its fixed assets.

Conclusions

Southwest State University designed and implemented internal controls to provide reasonable assurance that audited expenditures were accurately reported in the accounting records and in compliance with management's authorization. However, we noted in Chapter 2, Finding 2, that the university did not adequately restrict certain incompatible clearances to the accounting system. We also found that the university did not properly record its fixed assets on the MnSCU fixed asset system or complete an inventory count. In addition, the university failed to comply with applicable MnSCU procurement policies for certain library purchases.

6. Southwest State University did not properly account for fixed assets on the MnSCU accounting system.

Southwest State University did not complete a physical inventory of its fixed assets, nor did it record fixed assets on the MnSCU fixed asset system in a timely manner. As of the time of our audit, the university had not recorded all new and existing assets onto the fixed asset module. The person in charge of entering fixed assets was unable to keep up with new equipment purchases. MnSCU policies require institutions to develop procedures to record all fixed assets over $2,000 on the MnSCU fixed asset module. Periodic physical inventory counts and accurate records are necessary in order to properly account for and safeguard inventory.

Recommendation

- *Southwest State University should conduct a physical inventory count and record all fixed assets in the MnSCU fixed asset system.*

7. Southwest State University did not encumber funds in the MnSCU accounting system prior to making certain library purchases.

Southwest State University did not encumber funds on the MnSCU accounting system prior to incurring library related expenditures totaling $78,000. The library created a purchase order and encumbered funds on PALS (Project for Automated Library Systems). However, PALS does not interface with MnSCU accounting so funds were not encumbered in MnSCU accounting prior to the obligation being incurred. MnSCU policy 5.5.2, Part 5, and Minn. Stat. Section. 16A.15, Subd. 3, requires funds to be encumbered prior to authorizing or incurring an obligation or expenditure. By not encumbering funds prior to incurring an obligation, the university is violating MnSCU policy and could be subject to a potentially large unanticipated obligation.

Recommendation

- *Southwest State University should develop procedures to ensure funds are encumbered on the MnSCU accounting system prior to incurring obligations.*

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Chapter 7. Student Financial Aid

Chapter Conclusions

Southwest State University designed and implemented internal controls to provide reasonable assurance that it managed its financial aid programs in compliance with applicable legal requirements. The university properly recorded financial aid transactions in the MnSCU accounting system. For the items tested, the institution complied with federal cash management and reporting requirements. However, we noted an instance of noncompliance with a specific federal notification requirement related to the Perkins Loan Program.

Southwest State University participates in a variety of federal financial aid programs and some state administered grant programs. Table 7-1 summarizes federal program expenditures for fiscal year 1998:

Table 7-1
Southwest State University
Federal Financial Aid Expenditures
Fiscal Year Ended June 30, 1998

CFDA Number	Program	Total Expenditures
84.032	Federal Family Education Loan (FFEL)	$4,842,056
84.063	Federal Pell Grant	1,169,394
84.038	Federal Perkins Loan	181,371
84.007	Federal Supplemental Education Opportunity Grant (FSEOG)	141,667
84.033	Federal Work Study (FWS)	113,803

Sources: Fiscal year 1998 Federal Operations Report and Application to Participate (FISAP) and auditor prepared FFEL amounts worksheet.

The federal Pell grant is considered the first source of assistance to eligible students. The federal government bases eligibility for the grant on the cost of education, the family's ability to pay, and the student's enrollment level. Pell grant funding is not limited to funds available at an institution. The maximum Pell grant for the 1998-99 award year was $3,000 per student.

The Federal Family Education Loan (FFEL) program includes Subsidized and Unsubsidized Stafford loans and PLUS loans. The student applies for a loan from a private lender. The school certifies the promissory note for qualifying students. The federal government pays the interest to the private lender on Subsidized Stafford Loans while the student is in school and during certain deferment periods. For Unsubsidized Stafford Loans, the interest accrues from the date of origination and is the responsibility of the borrower. For PLUS loans, the borrower is responsible for the interest that accrues on the loan while the student is in school and during certain deferment periods. The maximum FFEL program amount for a given student is determined by the borrower's grade level and the amount previously borrowed. For PLUS loans, the amount of the loan cannot exceed the student's estimated cost of attendance minus other aid awarded during the period of enrollment.

The Federal Perkins Loan Program provides low-interest loans to needy students. The university acts as a lender, using both federal funds and a state match for capital contribution. The university performs loan collection duties including corresponding with students entering repayment status, receiving loan repayments, and pursuing delinquent loans. The university collected $192,133 in Perkins principal and interest repayments during the 1997-1998 academic school year.

The Federal Work-Study (FWS) Program and Federal Supplemental Educational Opportunity Grant (FSEOG) are additional sources of federal financial aid. The federal government share must not exceed 75 percent of the total expenditures in the FSEOG and FWS Programs. The state contributes the remaining 25 percent of the program funding.

Southwest State University also participates in the Minnesota State Grant Program funded by the Minnesota Higher Education Services Office. The university packages Minnesota state grants along with federal financial aid. The Minnesota Higher Education Services Office remits funding to the university for the grants. During fiscal year 1998, the university disbursed state grants totaling $912,757.

Audit Objectives and Methodology

The primary objectives of our audit were to answer the following questions:

- Did Southwest State University design and implement internal controls to provide reasonable assurance that it is managing federal student financial aid programs in compliance with applicable legal requirements and accurately recorded in the accounting system?

- Did Southwest State University comply with federal regulations governing cash management and federal reporting?

To answer these questions, we interviewed employees from the university financial aid and business offices to gain an understanding and perform testing of the internal controls over the eligibility, packaging, awarding, and disbursing of financial aid funds. We also evaluated controls and tested compliance with federal requirements governing federal cash management and reporting requirements.

Conclusions

Southwest State University designed and implemented internal controls to provide reasonable assurance that it managed federal student financial aid programs in compliance with applicable legal requirements and accurately recorded financial aid activity in the accounting system. The university also complied with federal regulations governing cash management and federal reporting. However, we noted an instance of noncompliance with a federal regulation governing the Perkins Loan Program, as discussed in the finding below.

8. Southwest State University did not notify Perkins Loan borrowers the required number of times during grace periods.

The university did not comply with federal regulations regarding the number of grace period contacts for Perkins borrowers. Federal regulation 674.42 (b)(2)(i) requires that the institution contact the borrower three times after the commencement of the grace period to remind them about the requirements of their loan.

When a student graduates, withdraws, or ceases to attend an institution less than half-time, the grace period begins. The university runs a report in an attempt to capture these students and determine if any of these students has received a Perkins loan. These students are given exit and other specific information, reminding them of their obligation to the university. The student has a nine month grace period before they are required to begin repayment of their loan. The university's notices are generated automatically. However, the system only generates two notices during the grace period, instead of the required three as outlined in federal regulations.

Recommendation

- *Southwest State University should ensure they notify Perkins recipients three times during the grace period required by federal regulations.*

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Status of Prior Audit Issues
As of June 25, 1999

Most Recent Audits

Legislative Audit Report 99-19, issued in March 1999, covered MnSCU activities material to the state's general-purpose financial statements for the year ended June 30, 1998. The audit included coverage of federal financial aid programs administered by the State of Minnesota in fiscal year 1998. This report did not include any findings related specifically to Southwest State University.

Legislative Audit Report 98-16, issued in March 1998, covered material MnSCU financial activities and federal financial aid programs administered by the State of Minnesota in fiscal year 1997. This report did not include any findings related specifically to Southwest State University.

Legislative Audit Report 97-29, issued in March 1997, covered material MnSCU financial activities and federal financial aid programs administered by the State of Minnesota in fiscal year 1996. This report did not include any findings related specifically to Southwest State University.

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 aid reports issued by the Legislative Auditor. However, Finance has delegated this responsibility for audits of the 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 the 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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OFFICE OF THE PRESIDENT

Southwest State University
Marshall, Minnesota 56258

August 11, 1999

James Nobles
Legislative Auditor
Office of the Legislative Auditor
1st Floor South, Centennial Building
658 Cedar Street
St. Paul, MN 55155

Dear Mr. Nobles:

Following are our responses to the findings in the audit of fiscal years 1996 through 1998 for Southwest State University.

FINDING 1:
SOUTHWEST STATE UNIVERSITY DID NOT MAINTAIN SUFFICIENT COLLATERAL FOR ITS LOCAL BANK ACCOUNT DURING TWO MONTHS IN 1999.

SHORT RESPONSE:
Agree. The institution has established adequate controls and will institute even further controls to assure that a reoccurrence of this type is not possible.

FULL RESPONSE:
A computer software error caused the local bank account to not be sufficiently collateralized during the fifteen days cited. Subsequently, the software was rewritten by Southwest State University's computer programming staff. Southwest State University's bank has now placed this account on a list for daily review that will assist us in assuring maintenance of adequate collateral. In the near future, Southwest State University plans to institute "PC Banking" that will allow us to review cash balances on a daily basis, among other things. Finally, with collateral now set at $2.7 million (face value $4.25 million) it is very unlikely that balances will exceed the collateral amount in the foreseeable future.

PERSON RESPONSIBLE FOR RESOLUTION: Business Manager
DATE OF PROJECTED COMPLETION: Done

FINDING 2:
SOUTHWEST STATE UNIVERSITY DID NOT ADEQUATELY RESTRICT CERTAIN COMPUTER SECURITY ACCESS PRIVILEGES.

Telephone (507) 537-7021 • FAX (507) 537-7154
www.southwest.msus.edu

SHORT RESPONSE:
Agree. The institution will modify computer security access privileges or establish compensating controls in those cases where minor risks may exist. In addition, a quarterly review of security access will be completed by the Security Officer and Business Manager.

FULL RESPONSE:
Computer access security is a complex issue. When installing the large number of systems that institutions, such as those in MnSCU, have been faced with, it is not unusual for errors to occur. Some of these errors are the result of misunderstandings or lack of clarity. Some happen because systems must be put in place quickly, security is established to “get the job done” and, then, changes are overlooked when the task is completed. Others require modifications in business practices. Still others are those that, while internal control suggests one process, another process is more practical for the institution because of issues such as staffing levels. In these cases, compensating controls are typically instituted to mitigate the effect of the access incompatibility.

In the case of Computer Services personnel who have access, it is our understanding that system security does not allow access to the replicated database without access to the production system. This is being researched but, if true, while we agree that such access is not desirable, it is necessary for us to continue. Our computer services personnel assist other campus staff in developing reports from the replicated database until such time as the staff receive training to develop reports by themselves.

In the case of six Business Office staff who has incompatible clearances, we agree, but plan to institute compensating controls for one individual who supervises both the purchasing and accounts payable functions.

In the case of the employee in the Human Resources Office who has access to both payroll and personnel, we will eliminate access to payroll functions.

In the case of the payroll clearances for employees who have more powerful access than necessary, we agree. This was probably the result of our misunderstanding of the type of security needed.

In the case of two former employees who continued to have access to some system functions, one, our Cashier, was an error and should have been deleted. The other, the previous Business Manager, was purposely not deleted. Both employees were employed by another state agency. The Business Manager was employed by another MnSCU institution. In both cases, it was the intent that they would return to Southwest State University to provide training for new employees. The Cashier did return and security was requested to be deleted. Because of human error, the request was not accomplished. Since the Business Manager was employed by another MnSCU institution and the determination that she would not be needed for training was made at the time of the field work being performed by the Office of Legislative Audit, we do not feel this is a material internal control weakness.

We agree that MnSCU System Office employees should only have query access to our systems.

PERSON RESPONSIBLE FOR RESOLUTION: Business Manager/Security Officer
DATE OF PROJECTED COMPLETION: 9/1/99

FINDING 3:
THE UNIVERSITY DID NOT ADEQUATELY CONTROL ADJUSTMENTS MADE TO TUTITION, FEES, AND ROOM AND BOARD RECEIPTS.

SHORT RESPONSE:
Agree. A procedure has been put in place to provide adequate review.

FULL RESPONSE:
Budgetary concerns caused Southwest State University to eliminate two positions in the accounts receivable/cash receipts functions. One of these positions previously performed the type of review discussed. We agree that this review is a good internal control and, with the addition of staffing, have reinstituted a procedure to perform this review.

PERSON RESPONSIBLE FOR RESOLUTION: Business Manager
DATE OF PROJECTED COMPLETION: Done

FINDING 4:
THE UNIVERSITY HAD INADEQUATE CONTROLS OVER CERTAIN SPORTS CAMP FEES.

SHORT RESPONSE:
Agree. A procedure has been put in place to provide appropriate separation of duties and reconciliation.

FULL RESPONSE:
Sport camp fees will be sent to the Cashier, funds will be deposited, and the registration form will then be delivered to the Athletics Department. A reconciliation, between registration forms received and cash receipted, will be performed.

PERSON RESPONSIBLE FOR RESOLUTION: Business Manager/Athletics Business Manager
DATE OF PROJECTED COMPLETION: Done

FINDING 5:
THE UNIVERSITY MISCODED SOME RENT AND SALES REVENUES.

SHORT RESPONSE:
Agree. A closer review of transactions, especially near the end or beginning of a fiscal year, will be performed.

FULL RESPONSE:
In the system Southwest State University used prior to implementation of the MnSCU system, coding of receipts to the appropriate fiscal year was done by review of batch transactions, after

the fact. With the implementation of the MnSCU system, fiscal year coding is done at the time of original entry that should act to lessen coding errors.

PERSON RESPONSIBLE FOR RESOLUTION: Business Manager
DATE OF PROJECTED COMPLETION: Done

FINDING 6:
SOUTHWEST STATE UNIVERSITY DID NOT PROPERLY ACCOUNT FOR FIXED ASSETS ON THE MnSCU ACCOUNTING SYSTEM.

SHORT RESPONSE:
Agree. Southwest State University will devote more effort to this function to provide more timely entry and a periodic physical inventory.

FULL RESPONSE:

We agree that improvements should be made. In truth, this is a function that has been neglected for the past few years. In prior years, entry was more timely and a cycle was established allowing for a complete inventory every three or four years. With the addition of staff, this will be implemented again as we agree it is an important internal control feature.

Again, because of budgetary concerns, staffing was reduced and not all tasks were able to be performed. In addition, several new systems were installed during this time that limited staff availability.

Because we are located in a rural, relatively crime free area, we felt our exposure to risk was less than it may be in other locations. We attempted to compensate by providing annual lists of equipment inventory to departments for their review. Admittedly, this control is much weaker than a centralized physical inventory.

Our plan is to dedicate more staff time to entry of inventory. Additionally, we will perform a physical inventory of a proportion of our equipment, each year, so a complete inventory is accomplished every three to four years.

PERSON RESPONSIBLE FOR RESOLUTION: Supervisor, Purchasing & Payables
DATE OF PROJECTED COMPLETION: 6/30/00

FINDING 7:
SOUTHWEST STATE UNIVERSITY DID NOT ENCUMBER FUNDS IN THE MnSCU ACCOUNTING SYSTEM PRIOR TO MAKING CERTAIN LIBRARY PURCHASES.

SHORT RESPONSE:
Partially agree. While library materials are not encumbered in the MnSCU accounting system, they are encumbered in the PALS (Project for Automated Library Systems). We feel that we are meeting the spirit of the law and policy and that adequate compensating controls exist to mitigate exposure to risk. Further, MnSCU systems priorities indicate future development of a direct interface between PALS and the accounting system that will address this concern.

FULL RESPONSE:
We recognize that the MnSCU accounting system represents our official books of entry and that encumbrances should flow through this system. However, to accomplish this it would be necessary for dual entry and reconciliation between the two systems. We feel this would represent an unwise utilization of resources for minimal enhancement of our internal controls. We feel features in PALS and other compensating controls provide adequate internal controls to limit risk.

PALS currently replicates the budget provided in the MnSCU accounting system. Encumbrances and purchases orders have been delegated to the Library staff for library holdings. Expenditures are made from the MnSCU accounting system. A monthly review of account balances is performed and, if a large deficit would appear in the library account, Business Office staff would investigate. Additionally, SSU has a carryover policy that allows departments to carryover positive and negative balances in their operating budgets. This, then, acts to provide controls over departmental spending. Finally, there is sufficient budget in Southwest State University's total carryover amount to "cover" quite a large departmental overdraft, if it would occur.

Again, we agree that encumbrances for library materials should be entered into the MnSCU accounting system but feel prudent use of resources dictates that we maintain our current system.

PERSON RESPONSIBLE FOR RESOLUTION: Supervisor, Purchasing & Payables/Director of Library/ MnSCU Systems Development
DATE OF PROJECTED COMPLETION: 6/30/01

FINDING 8:
SOUTHWEST STATE UNIVERSITY DID NOT NOTIFY PERKINS LOAN BORROWERS THE REQUIRED NUMBER OF TIMES DURING GRACE PERIODS.

SHORT RESPONSE:
Agree. A software error caused the required, three notifications to drop to two for a period of time. SSU is now using the MnSCU-LMS (Loan Management System). The likelihood of a similar occurrence is minimal.

FULL RESPONSE:
A modification to Southwest State University's software caused an error in the notification function of the software.

SSU is now using the MnSCU LMS (Loan Management System). The likelihood of a similar occurrence is minimal.

PERSON RESPONSIBLE FOR RESOLUTION: Business Manager
DATE OF PROJECTED COMPLETION: Done

Thank you for this opportunity to respond to the findings in our recent audit. I also wish to express my gratitude to your staff who performed a very thorough and professional audit. It was a pleasure working with them.

If you have any further questions or comments, please feel free to contact me.

Sincerely,

Doug Sweetland
President

CC: Jeanine Leifeld - Audit Manager, Office of the Legislative Auditor
Laura King – MnSCU Vice Chancellor, Chief Financial Officer
Rosalie Greeman - MnSCU Associate Vice Chancellor
John Asmussen - MnSCU Executive Director of Internal Auditing
Andrew Boss – Chair, MnSCU Audit Committee
Michael Vekich – Chair, MnSCU Board of Trustees
Doug L. Fraunfelder – SSU Associate VP for Finance & Human Resources
Deb Kerkaert – SSU Business Manager