



OFFICE OF THE LEGISLATIVE AUDITOR
STATE OF MINNESOTA

Financial-Related Audit

Minnesota State Academies
July 1, 1996, through June 30, 2000



Financial Audit Division

The Office of the Legislative Auditor (OLA) is a professional, nonpartisan office in the legislative branch of Minnesota State government. Its principal responsibility is to audit and evaluate the agencies and programs of state government (the State Auditor audits local governments).

OLA's Financial Audit Division annually audits the state's financial statements and, on a rotating schedule, audits agencies in the executive and judicial branches of state government, three metropolitan agencies, and several "semi-state" organizations. The division also investigates allegations that state resources have been used inappropriately.

The division has a staff of approximately fifty auditors, most of whom are CPAs. The division conducts audits in accordance with standards established by the American Institute of Certified Public Accountants and the Comptroller General of the United States.

Consistent with OLA's mission, the Financial Audit Division works to:

- Promote Accountability,
- Strengthen Legislative Oversight, and
- Support Good Financial Management.

Through its Program Evaluation Division, OLA conducts several evaluations each year and one best practices review.

OLA is under the direction of the Legislative Auditor, who is appointed for a six-year term by the Legislative Audit Commission (LAC). The LAC is a bipartisan commission of Representatives and Senators. It annually selects topics for the Program Evaluation Division, but is generally not involved in scheduling financial audits.

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OFFICE OF THE LEGISLATIVE AUDITOR
State of Minnesota • James Nobles, Legislative Auditor

Senator Ann H. Rest, Chair
Legislative Audit Commission

Members of the Legislative Commission

Ms. Linda Mitchell, Superintendent
Minnesota State Academy for the Deaf

Ms. Elaine Sveen, Superintendent
Minnesota State Academy for the Blind

Board of Minnesota State Academies

We have audited the financial activities of the Minnesota State Academies for the four years ended June 30, 2000. Our audit scope included payroll, administrative expenditures, tax-sheltered annuities, resident accounts, and tuition revenues. The audit objectives and conclusions are highlighted in the individual chapters of this report.

We conducted our audit in accordance with *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 the Minnesota State Academies complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management of the Minnesota State Academies 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 and the management of the Minnesota State Academies. This restriction is not intended to limit the distribution of this report, which was released as a public document on August 2, 2001.

/s/ James R. Nobles

James R. Nobles
Legislative Auditor

/s/ Claudia J. Gudvangen

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: June 8, 2001

Report Signed On: July 30, 2001

Minnesota State Academies

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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
Renee Redmer, LPA	Audit Manager
Sonya Johnson, CPA	Auditor-in-Charge
Dave Massaglia	Auditor
Kathy Fisher	Auditor

Exit Conference

We discussed the audit report conclusions with the following representatives of the Minnesota State Academies at the exit conference held on July 23, 2001:

Elaine Sveen	Superintendent, Minnesota State Academy for the Blind
Linda Mitchell	Superintendent, Minnesota State Academy for the Deaf
Tom Schoenbauer	Accounting Supervisor Senior

Report Summary

Overall Conclusion:

In general, the Minnesota State Academies safeguarded its assets and accurately recorded receipts and expenditures in the state's accounting and payroll systems. However, we noted the following internal control and compliance areas where the academies need improvement.

Key Findings:

- The Minnesota State Academies did not transfer the correct amount of basic education revenue to the General Fund. During the audit period, the academies retained \$167,221 more tuition revenue than provided for in the statutory formula. (Finding 1, page 6)
- The academies did not adequately segregate duties over student tuition revenue. One individual was responsible for billing school districts for tuition and also receiving the collections. (Finding 2, page 7)
- The academies need to improve controls over resident accounts by forwarding the signed student allowance sheets to the business office to support resident withdrawals from their accounts. (Finding 3, page 10)
- The academies input incorrect record dates for certain professional/technical services, supplies, and equipment transactions in the statewide accounting system. (Finding 4, page 13)

Agency Background:

The Minnesota State Academies consists of the Minnesota State Academy for the Deaf (MSAD) and the Minnesota State Academy for the Blind (MSAB). The academies provide educational services to meet the needs of deaf/hard of hearing and blind/visually impaired students. These services include both the public school core curriculum and any required disability-specific curriculum.

Financial Audits address internal control weaknesses and noncompliance issues found during our audits of state departments and agencies. The scope of our audit work at the Minnesota State Academies included payroll, other administrative expenditures, resident accounts, and tuition revenues for the period from July 1, 1996, through June 30, 2000.

Minnesota State Academies

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Chapter 1. Introduction

The Minnesota State Academies consists of the Minnesota State Academy for the Deaf (MSAD) and the Minnesota State Academy for the Blind (MSAB). The residential academies provide educational services to meet the needs of deaf/hard of hearing and blind/visually impaired students. These services include both the public school core curriculum and any required disability-specific curriculum.

The State Board of Education directed the operations of the academies until December 1999. The Governor appointed a new, seven-member board in the spring of 2000. The Board of Minnesota State Academies currently provides governance for the academies and delegates responsibility for the day-to-day administration of the academies to the chief administrator of each school. Currently, Linda Mitchell is the MSAD superintendent and Elaine Sveen is the MSAB superintendent.

The agency receives state appropriations and student tuition to fund the general operations of the academies. Table 1-1 provides a summary of the academies' financial activities for the four fiscal years ended June 30, 2000.

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Table 1-1
Sources and Uses of Funds
Fiscal Years Ended June 30, 1997, 1998, 1999, and 2000

	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>
Sources:				
State Appropriations	\$ 8,526,000	\$ 9,449,000	\$ 9,486,000	\$10,039,000
Less: Cancellations	<u>4,972</u>	<u>0</u>	<u>9,135</u>	<u>0</u>
Net Appropriations	<u>\$ 8,521,028</u>	<u>\$ 9,449,000</u>	<u>\$ 9,476,865</u>	<u>\$10,039,000</u>
Dedicated Receipts ⁽¹⁾	1,154,570	1,493,013	1,912,579	1,693,696
Balance Forward In	<u>625,614</u>	<u>395,656</u>	<u>704,958</u>	<u>844,652</u>
Total Sources	<u><u>\$10,301,212</u></u>	<u><u>\$11,337,669</u></u>	<u><u>\$12,094,402</u></u>	<u><u>\$12,577,348</u></u>
Uses:				
Payroll	\$ 8,049,788	\$ 8,156,065	\$ 8,650,240	\$ 9,048,519
Utilities and Maintenance	325,972	324,691	321,940	341,711
Consultant Services	414,032	378,811	447,507	403,014
Supplies ⁽²⁾	382,084	402,999	628,821	378,821
Equipment ⁽²⁾	81,024	433,316	446,235	131,902
Annuities and Pensions ⁽³⁾	196,247	283,008	224,272	220,052
Resident Accounts	55,259	47,291	52,434	57,009
Other	240,950	564,657	435,381	459,824
Transfer Out	160,200	41,873	42,920	0
Balance Forward Out	<u>395,656</u>	<u>704,958</u>	<u>844,652</u>	<u>1,536,496</u>
Total Uses	<u><u>\$10,301,212</u></u>	<u><u>\$11,337,669</u></u>	<u><u>\$12,094,402</u></u>	<u><u>\$12,577,348</u></u>

- (1) Dedicated receipts include tuition revenue available for operations, resident accounts, payroll deductions for tax sheltered annuity payments, and other miscellaneous receipts.
- (2) Increase in supplies and equipment expenditures in fiscal years 1998 and 1999 are due to an upgrade in the academies' computer technology.
- (3) The academies processed payments of employee payroll deductions to various vendors for the tax sheltered annuity program.

Source: Minnesota Accounting and Procurement System.

Chapter 2. Tuition Revenue

Chapter Conclusions

The Minnesota State Academies' internal controls provided reasonable assurance that tuition revenue was accurately billed, timely deposited, and properly recorded in the state's accounting system. However, the academies did not transfer the correct amount of basic education revenue to the General Fund according to state law. In addition, the academies did not adequately segregate duties over certain receipt functions.

The Minnesota State Academies (MSA) serve various school districts by providing instructional services to approximately 200 students. The school districts pay the costs incurred by those students to attend the academies. The academies collect various types of tuition revenue from the school districts, including basic education revenue, compensatory education revenue, and management aides revenue. With the exception of basic education revenue, the institution retains the revenues generated to fund general operations of the academies. State law establishes the method for allocating resident tuition to the General Fund and to the academies' general operating account.

For basic revenue, MSA bills the individual school districts for the number of days that each student attends the academies. For compensatory education revenue, which began in fiscal year 1998, the Department of Children, Families & Learning calculates the amount due from districts for special education students. Management aide revenue provides reimbursement for the staff that provides special care or services to approximately 30-40 students. Beginning in fiscal year 2000, the state funded 68 percent of the aides' gross salary. The school districts paid the remaining 32 percent of the salaries, plus all fringe benefits. Table 2-1 summarizes the revenues by type for the fiscal year ended June 30, 2000.

Table 2-1
Student Tuition Revenue by Source
Fiscal Year Ended June 30, 2000

	<u>Total</u>	<u>Returned to General Fund⁽¹⁾</u>	<u>Retained for MSA's Operations</u>
Basic Education ⁽¹⁾	\$ 772,213	\$614,875	\$ 157,338
Compensatory Education	289,035	N/A	289,035
Management Aides	649,032	N/A	649,032
Total	<u>\$1,710,280</u>	<u>\$614,875</u>	<u>\$1,095,405</u>

(1) See Finding 1 regarding the calculation of basic education revenue transferred to the General Fund.

Source: Minnesota Accounting and Procurement System.

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Audit Objectives and Methodology

We focused our review of revenues on the following objectives:

- Did the MSA's internal controls provide reasonable assurance that tuition revenues were accurately billed, properly collected, timely deposited, and accurately reported in the accounting records?
- Did the MSA's revenue collections comply with applicable legal provisions?

To address these objectives, we interviewed office staff to gain an understanding of the controls in place over the processing and recording of receipts. We also performed analytical procedures and tested a sample of transactions.

Conclusions

The Minnesota State Academies' internal controls provided reasonable assurance that tuition revenue was accurately billed, timely deposited, and properly recorded in the state's accounting system. However, the academies did not transfer the correct amount of basic education revenue to the General Fund according to state law. In addition, the academies did not adequately segregate duties over certain receipt functions.

1. The Minnesota State Academies did not transfer the correct amount of basic education revenue to the General Fund.

The MSA did not properly allocate basic education tuition revenue collected for resident students between the General Fund and the academies' operating account. State statutes establish the formula for distribution of tuition collections to the General Fund and to the academies' general operating account. The amount allocated is based on the grade level of students. The statutes provide two different allocation formulas, one for kindergarten and elementary students and one for secondary students.

Minn. Stat. Section 125A.65, Subd. 8 provides that :

On May 1 of each year, the board of the academies shall count the actual number of Minnesota resident kindergarten and elementary students and the actual number of Minnesota resident secondary students enrolled and receiving education services. The board of the academies shall deposit in the state treasury an amount equal to all tuition received less:

- 1) the total number of students on May 1 less 175, times the ratio of the number of kindergarten and elementary students, times the general education formula allowance; plus

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- 2) the total number of students on May 1 less 175, times the ratio of the number of secondary students on May 1 to the number of students on May 1, times 1.3, times the general education formula allowance.

Currently, MSA serves preschool, kindergarten, elementary, and secondary students. Over the timeframe of our audit, the academies calculated that the agency should retain \$595,279 of the basic education revenue for resident students. The academies incorrectly applied the basic education revenue formula to all student groups. MSA also included preschool students in the calculation of the amount of funding it could retain, even though these students are not defined in the statutory formula. These errors resulted in a loss of \$167,221 to the General Fund for the audit period.

Recommendations

- *MSA should follow the current statutory language to calculate the amounts allocated between the General Fund and the academies' operating account. In addition, the MSA should consider seeking a revision of Minn. Stat. Section 125A.65 to include preschool students in the allocation computation.*
- *MSA should work with the Department of Finance to resolve the \$167,221 not properly transferred to the General Fund.*

2. PRIOR FINDING NOT RESOLVED: The academies did not adequately segregate duties over certain tuition receipt functions.

The Minnesota State Academies did not have an adequate segregation of duties in the area of tuition billings and collections of incoming receipts. One person was responsible for generating invoices from the Minnesota Accounting and Procurement System and receiving the incoming payments before forwarding them to the person who prepares the deposit. These functions are typically incompatible and increase the risk of errors or irregularities occurring and not being detected.

Recommendation

- *MSA should segregate duties over tuition receipts by having separate individuals performing the functions of billing and receiving payments.*

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Chapter 3. Resident Accounts

Chapter Conclusions

The Minnesota State Academies' internal controls provided reasonable assurance that student account collections and disbursements were adequately safeguarded, accurately reported in the accounting records, and in compliance with applicable legal provisions and management's authorization. However, the academies need to improve controls over signed allowance sheets.

Students enrolled at the Minnesota State Academy for the Deaf (MSAD) and the Minnesota State Academy for the Blind (MSAB) may deposit personal funds with the academies' business office and receive those funds either through a set weekly allowance or as needed. Personal checks and cash either come through the mail or are brought to the campus by the student. The MSAB sends checks received at its location via intercampus mail to the MSAD business office. Resident program staff delivers any cash directly to the business office upon receipt. The business office maintains individual account records for each student. All revenue and disbursement activity is recorded in the Minnesota Accounting and Procurement System. The accounting supervisor performs monthly reconciliations between the Minnesota Accounting and Procurement System and the individual student records.

The academies maintain an imprest cash account for daily cash requests and a checking account for larger withdrawals. The academies periodically request reimbursement of the imprest cash account. For the fiscal year ended June 30, 2000, resident account receipts totaled \$24,868 and expenditures totaled \$22,729.

Audit Objective and Methodology

We focused our review of student accounts on the following objective:

- Did the Minnesota State Academies' internal controls provide reasonable assurance that all student account collections and disbursements were adequately safeguarded, accurately reported in the accounting records, and in compliance with applicable legal provisions and management's authorization?

To address these objectives, we interviewed office staff to gain an understanding of the controls in place over student collections, student disbursements, and the recording of the receipts and expenditures in the accounting records. We performed analytical procedures, detailed transaction testing, and verified the completeness and accuracy of reconciliations.

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Conclusions

The Minnesota State Academies' internal controls provided reasonable assurance that student account collections and disbursements were adequately safeguarded, accurately reported in the accounting records, and in compliance with applicable legal provisions and management's authorization. However, the academies need to improve controls over signed allowance sheets.

3. The Minnesota State Academies need to improve controls over student allowance sheets.

The resident program staff at the academies collect the students' weekly allowance from business office staff to distribute to the students. The program staff sign allowance sheets documenting the receipt of these allowances. According to the academies' policy, the student is also required to sign the allowance sheets. The program staff are to return the allowance sheets to the business office. During the audit period, the staff was not consistently returning all of the signed allowance sheets to the business office. Inadequate documentation increases the risk that these allowances could be lost, stolen, or not properly accounted for.

Recommendation

- *The Minnesota State Academies should ensure that all signed student allowance sheets are returned as outlined in the academies' policy.*

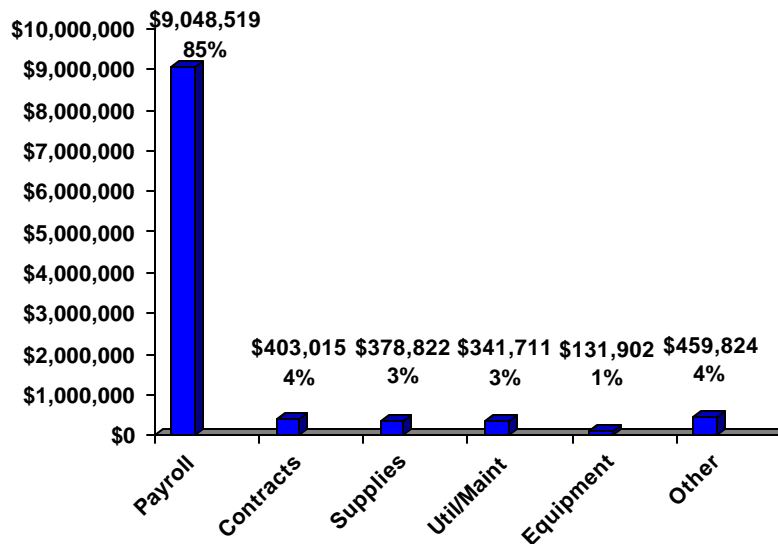
Chapter 4. Payroll and Other Administrative Expenditures

Chapter Conclusions

The Minnesota State Academies' internal controls provided reasonable assurance that payroll and other administrative expenditures were accurately reported in the accounting records and in compliance with applicable bargaining unit agreements, applicable legal provisions, and management's authorization. However, the academies did not input the correct record date in the Minnesota Accounting and Procurement System for some transactions.

Payroll was the Minnesota State Academies' largest expenditure. In addition to payroll, the agency incurred other administrative costs for contracts, supplies, utilities/maintenance, and equipment. Figure 4-1 shows the amount of expenditures by type for the fiscal year ended June 30, 2000.

Figure 4-1
Minnesota State Academies
Expenditures by Type
Fiscal Year Ended June 30, 2000



Note: In addition, the MSA disbursed \$220,052 to vendors for the tax shelter annuity program.

Source: Minnesota Accounting and Procurement System.

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Payroll

Payroll was the academies' largest expenditure, totaling \$9 million in fiscal year 2000. The Minnesota State Academies employs approximately 200 employees. A senior account clerk inputs the biweekly payroll into the state's payroll system (SEMA4). The human resources director handles the personnel functions for the academies.

Contracts

In fiscal year 2000, the academies expended \$403,015 for contract services. The majority of the expenditures were for the contract with the Faribault school district. Students from the academies attended classes in the local school district and interacted with district students. This contract pays for the cost of the students to attend classes in the school district.

Supplies and Equipment

The academies incurred \$378,822 in expenditures for supplies and \$131,902 for equipment expenditures in fiscal year 2000. The largest expenditures consisted of food purchases from a state contract vendor and miscellaneous computer and other supplies and equipment purchases.

Utilities/Maintenance

The academies' utility/building maintenance expenditures of \$341,711 in fiscal year 2000 consisted primarily of expenditures related to utility billings, payments to the Department of Corrections for steam heat provided to the academies' buildings and security services.

Annuities

Expenditures of \$220,052 in fiscal year 2000 were for payments made to various vendors selected by participants in the tax sheltered annuity program. This plan is a long-term retirement plan which employees of public institutions can participate through payroll deduction. The academies' employees elect to have a certain amount deducted from their payroll checks and invested with various vendors. The academies remit the payroll deductions to the vendors that the participants have selected.

Audit Objectives and Methodology

Our audit of payroll and other administrative expenditures focused on the following objectives:

- Did the Minnesota State Academies' internal controls provide reasonable assurance that payroll and other administrative expenditures were accurately reported in the accounting records and in compliance with applicable bargaining unit agreements, applicable legal provisions, and management's authorization?

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- For the items tested, did the office comply, in all material respects, with significant finance-related legal provisions concerning payroll and other administrative expenditures?

To answer these questions, we obtained an understanding of the internal control structure over payroll and other administrative expenditures. We analyzed employee compensation and tested hours worked and payrate increases to ensure compliance with the terms of the applicable bargaining unit agreements. We performed detailed transaction testing and determined whether payments were properly documented, authorized by management, and in compliance with applicable state policies and procedures. We reviewed selected interagency agreements and tested tax sheltered annuity payments.

Conclusions

The Minnesota State Academies' internal controls provided reasonable assurance that payroll and other administrative expenditures were accurately reported in the accounting records, in compliance with applicable bargaining unit agreements, applicable legal provisions, and management's authorization. However, the academies did not input the correct record date in the Minnesota Accounting and Procurement System for some transactions.

4. The Minnesota State Academies did not record the correct record dates in the Minnesota Accounting and Procurement System for some transactions.

The academies did not record the correct record dates for some supplies, equipment, and professional/technical services expenditures. The accounting system record date identifies when the goods or services were received and is used to establish dates that liabilities are incurred for financial reporting purposes. The date of record used by MSA was the date the invoice was paid, not the date that the goods or services were received. Fourteen of twenty sample items tested, totaling \$735,904, had incorrect record dates in the accounting system. Incorrect record dates may cause the financial statement amounts for year-end accrued liabilities to be misstated.

Recommendation

- *The Minnesota State Academies should ensure that the record date recorded in the accounting system is the date that the goods or services were received.*

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Status of Prior Audit Issues As of June 12, 2001

Most Recent Audit

Legislative Audit Report 96-38, issued in September 1996, covered the five fiscal years ended June 30, 1996. The scope of this audit included tuition, federal grants, payroll, professional/technical services, and resident accounts. There were four written issues related to revenues, the academies' operations, and resident accounts. All of the findings were implemented with the exception of the lack of segregation of duties over receipt billing and collection functions, which we have repeated in this report.

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. The process consists of an exchange of written correspondence that documents the status of audit findings. The follow-up process continues until Finance is satisfied that the issues have been resolved. It covers entities headed by gubernatorial appointees, including most state agencies, boards, commissions, and Minnesota state colleges and universities. It is not applied to audits of the University of Minnesota, any quasi-state organizations, such as metropolitan agencies or the State Agricultural Society, the state constitutional officers, or the judicial branch.

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July 27, 2001

Mr. James Nobles, Legislative Auditor
Office of the Legislative Auditor
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658 Cedar Street
St. Paul, Mn. 55155

Dear Mr. Nobles:

Enclosed are our responses regarding the recent audit conducted at the Minnesota State Academy for the Deaf and the Minnesota State Academy for the Blind. The audit report, the findings and recommendations were discussed with agency administrators in an exit conference on July 23, 2001.

The agency has already implemented three of the recommendations and intends to act on the final recommendation as well.

We would like to thank the Office of the Legislative Auditor for the manner in which the audit was conducted. We appreciated working with your audit team.

Sincerely,

/s/ Linda Mitchell

Linda Mitchell
MSAD Superintendent

/s/ Elaine Sveen

Elaine Sveen
MSAB Superintendent

enclosure

Minnesota State Academies

Recommendation # 1:

MSA should follow the current statutory language to calculate the amounts allocated between the General Fund and the academies' operating account. In addition, the MSA should consider seeking a revision of Minn. Stat. Section 125A.65 to include preschool students in the allocation computation.

MSA should work with the Department of Finance to resolve the \$167,221 not properly transferred to the General Fund.

Response to # 1:

MSA will pursue statutory changes to reflect current practice. Until such time statutory changes are finalized, MSA will follow current law.

MSA will work with the Department of Finance to resolve the \$167,221 not properly transferred to the General Fund.

Recommendation # 2:

MSA should segregate duties over tuition receipts by having separate individuals performing the functions of billing and receiving payments.

Response to # 2:

The above recommendation was implemented during the audit visit, with the Account Clerk Senior being responsible for the processing of all billings, and the Personnel Aide responsible for the receipt and deposit of all monies collected.

Recommendation # 3:

The Minnesota State Academies should ensure that all signed student allowance sheets are returned as outlined in the academies' policy.

Response to # 3:

The Central Services Administrative Specialist Principal will be responsible for the collection of all signed student allowance sheets. This is effective with the beginning of the upcoming school year.

Recommendation # 4:

The Minnesota State Academies should ensure that the record date recorded in the accounting system is the date that the goods or services were received.

Response to # 4:

This recommendation was also implemented during the audit visit. The Account Clerk Senior was instructed in properly coding the record date for all goods or services received.