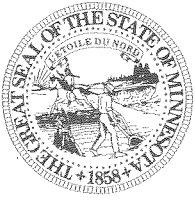


**UNIVERSITY OF MINNESOTA
LEGAL COMPLIANCE AUDIT
FOR THE THREE YEARS ENDING JUNE 30, 1986**

AUGUST 1987

Financial Audit Division
Office of the Legislative Auditor
State of Minnesota



STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

VETERANS SERVICE BUILDING, ST. PAUL, MN 55155 • 612/296-4708

JAMES R. NOBLES, LEGISLATIVE AUDITOR

Representative Phillip J. Riveness, Chairman
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Kenneth H. Keller, President
University of Minnesota

Audit Scope

We have completed a legal compliance audit of various activities at the University of Minnesota funded in whole or in part by the State of Minnesota for the three years ending June 30, 1986. Section I provides a brief description of the University's activities and finances. Our audit was made in accordance with generally accepted auditing standards and the standards for financial and compliance audits contained in the U.S. General Accounting Office Standards for Audit of Governmental Organizations, Programs, Activities, and Functions, and accordingly, included such audit procedures as we considered necessary in the circumstances. Field work was completed on May 27, 1987.

The objective of the audit was to verify compliance with finance-related legal provisions, including:

- Article XI, Section 9 of the Constitution of the State of Minnesota;
- Minn. Stat. Chapters 135A, 137, and 158; and
- 1983 and 1985 appropriation laws applicable to the University of Minnesota.

Management Responsibilities

The management of the University of Minnesota is responsible for the University's compliance with laws and regulations. In connection with our audit, we selected and tested transactions and records from the programs administered by the University of Minnesota. The purpose of our testing of transactions was to obtain reasonable assurance that the University of Minnesota had, in all material respects, administered its programs in compliance with applicable laws and regulations.

Audit Techniques

In the course of our audit, we employed a variety of audit techniques. These included, but were not limited to, auditor observation, interviews with agency staff, and the examination of documentation supporting a number of transactions. Judgemental sampling techniques were used to select specific samples of transactions for testing.

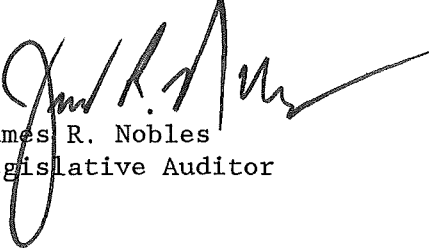
Representative Phillip J. Riveness, Chairman
Members of the Legislative Audit Commission
Mr. Kenneth H. Keller, President
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Conclusions

In our opinion, except for the issues addressed in Section II, the University of Minnesota, for the period July 1, 1983 to June 30, 1986, administered its programs, in all material respects, in accordance with finance-related legal provisions governing state appropriated funds.

Section II of this report contains the recommendations we developed during this audit. They are presented to assist the University in improving accounting procedures and controls. We will be monitoring and reviewing the University of Minnesota's progress on implementing these recommendations. A summary of the progress made on all audit recommendations discussed in our last audit report covering the three years ending June 30, 1979 is shown in Section III entitled "Status of Prior Audit Recommendations and Progress Toward Implementation."

We would like to thank the University's staff for their cooperation during this audit.



James R. Nobles
Legislative Auditor



John Asmussen, CPA
Deputy Legislative Auditor

July 22, 1987

UNIVERSITY OF MINNESOTA

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AUDIT PARTICIPATION

The following staff from the Office of the Legislative Auditor prepared this report:

| | |
|--------------------------|----------------------------|
| John Asmussen, CPA | Deputy Legislative Auditor |
| Claudia Gudvangen, CPA | Audit Manager |
| Jack Hirschfeld, CPA | Auditor-in-Charge |
| Steve Pyan | Staff Auditor |
| Michael E. Anderson, CPA | Staff Auditor |
| Kim Bergstrom | Intern |
| Diane Jaquet | Intern |

EXIT CONFERENCE

The findings and recommendations in this report were discussed with the following staff of the University of Minnesota on July 16, 1987:

| | |
|---------------------|--|
| Carol Campbell | Controller and Treasurer |
| Brian Obermeier | Director, Accounting Records and Services |
| Carole Friedrichson | Assistant Director, Accounting Records and Services |
| Katherine Cram | Director, Purchasing and Materials Management |

UNIVERSITY OF MINNESOTA

I. INTRODUCTION

The University of Minnesota was founded in February 1851 under Chapter III of the Territorial Laws enacted by the Legislative Assembly. It began as a preparatory school seven years before the new territory of Minnesota became a State. Twenty-five and one-third acres were purchased in 1854, and the first campus building was completed in 1858. The University has grown to become one of the largest universities in the country, with an enrollment of 56,443 for the Fall quarter of 1986.

The Board of Regents is the governing body of the University. Their chief responsibilities include the election of the chancellor, enactment of rules, regulations, and policies governing the University, control of University expenditures, and approval of major personnel changes. Six vice presidents are responsible for administering the University. Their individual areas of responsibility include Academic Affairs, Agriculture, Forestry and Home Economics, Finance and Operations, General Counsel, Health Sciences, Institutional Relations, and Student Affairs. The coordinate campuses at Crookston, Duluth, Morris and Waseca are each administered by a provost, who reports to the president. Kenneth H. Keller has served as president of the University since March 1985.

Operations of the University are financed primarily by state appropriations, student tuition and fees, federal grants and contracts, private gifts, grants and contracts, investment income, and sales and services of auxiliary enterprise operations, hospitals, and their educational activities. State appropriations for the fiscal years 1984, 1985, and 1986 are summarized as follows:

| <u>Appropriations</u> | <u>For the Years Ended June 30:</u> | | |
|---|-------------------------------------|---------------|---------------|
| | <u>1984</u> | <u>1985</u> | <u>1986</u> |
| General Operations and Maintenance | \$247,291,600 | \$253,232,700 | \$284,576,900 |
| Special Purpose | \$ 49,253,400 | \$ 55,614,000 | \$ 63,635,900 |
| Buildings (amounts expended during year) | \$ 16,562,000 | \$ 35,044,400 | \$ 41,256,800 |
| Legislative Commission on Minnesota Resources | \$ 1,835,000 | \$ 1,826,000 | \$ 2,749,000 |

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II. CURRENT FINDINGS AND RECOMMENDATIONS

Procedures for measuring compliance with Set Aside requirements should be revised.

In 1975 the Minnesota Legislature established the state Set Aside Program requiring the Commissioner of Administration to designate and set aside for small business a percentage of anticipated state procurement contracts. This program was established to encourage and foster the ability of small businesses and those owned by socially and economically disadvantaged persons to do business with the state. Laws of 1979, Chapter 86 required the University to establish a similar Set Aside Program. In October 1979 the University Board of Regents adopted a resolution directing the Vice President for Finance to establish a Set Aside Program in accordance with the statutory provisions.

Minn. Stat. Section 137.31, Subd. 1 requires that the, "Regents of the University of Minnesota shall designate and set aside for awarding to small businesses approximately 20 percent of the value of procurement contracts which are to be awarded during that fiscal year and which are to be paid in total or in part from funds appropriated to the university by the legislature." The amounts awarded under the University Set Aside Program in fiscal years 1985 and 1986 were less than 20 percent of procurement contracts. The table below shows the total procurement amounts, the amounts required for the Set Aside Program, and the actual amounts awarded under the program.

UNIVERSITY OF MINNESOTA SET ASIDE PROGRAM EXPENDITURES Fiscal Years 1985 and 1986

| <u>Year</u> | <u>Amount of Procurement Contracts</u> | <u>Amount Re- quired for Set Aside Program</u> | <u>Amount Actu- ally Awarded Under Set Aside Program</u> | <u>Deficit Amount for Set Aside Program</u> | <u>Set Aside Expenditures as a % of Procurement Expenditure</u> |
|-------------|--|--|--|---|---|
| 1986 | \$115,796,000 | \$23,159,000 | \$21,900,000 | \$1,259,000 | 18.9% |
| 1985 | <u>103,255,000</u> | <u>20,651,000</u> | <u>17,200,000</u> | <u>3,451,000</u> | <u>16.6%</u> |
| TOTAL | <u>\$219,051,000</u> | <u>\$43,810,000</u> | <u>\$39,100,000</u> | <u>\$4,710,000</u> | <u>17.8%</u> |

The deficit amounts for the Set Aside Program for fiscal years 1985 and 1986 were the result of inappropriate procedures used to determine the estimated amount of contracts designated for the program. The estimated amount of contracts designated for the Set Aside Program for fiscal years 1984-1986 was based on the total of the prior year's expenditures provided annually by the University's Accounting Records and Services Department.

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Minn. Stat. Section 137.31, Subd. 1 requires the Set Aside amount to be based on the value of contracts awarded during the current year. The use of prior year's expenditures rather than current year expenditures as the basis for the Set Aside Program resulted in an under allocation totaling \$4.7 million for fiscal years 1985 and 1986. While the statutory provision only requires an approximate level of Set Aside contracts, University procedures for monitoring this requirement should make use of the most appropriate data available. The Accounting Records and Services Department has agreed to begin providing current year expenditure information to the Set Aside coordinator. This will allow the coordinator to more closely comply with statutory requirements by allowing more frequent adjustments to the amount of contract expenditures designated for the Set Aside Program.

Minn Stat. Section 137.31 also provides that an annual report be submitted by the University to the Legislature. Minn. Stat. Section 137.31, Subd. 6 lists the required information to be included in the report. The fiscal year 1986 report included most of the required information. However, it did not include:

- the number of procurement contracts awarded to small businesses owned and operated by economically or socially disadvantaged persons; or
- the estimated total dollar value of contracts designated for the Set Aside Program but were not awarded to a small business, the lowest bid on each of these awards, and the price at which these contracts were awarded pursuant to regular procurement procedures.

This information should be included in the report so the Legislature can evaluate the progress being made on the Set Aside Program.

RECOMMENDATIONS:

1. The University of Minnesota should use current year expenditures in determining the amount of contracts designated for the Set Aside Program.
2. The annual reports to the Legislature should include all information required by applicable statutes.

The University of Minnesota is not including all donated equipment on property accounting records.

During fiscal years 1984 and 1985, the University received \$122,849,000 in state appropriations to fund 26 research and development programs and 15 capital projects. The appropriation riders for five of these projects required the University to obtain matching funds from non-state sources prior to receiving state funds. The University department receiving the state appropriations is responsible for obtaining this non-state match. When the match has been obtained, the University Controller requests the House Appropriations and Senate Finance Committees to release the state funds.

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Some University departments received donated equipment as part of the non-state match. When equipment is received, the department is required to notify property accounting so that the donated equipment can be properly recorded. However, some departments were not always notifying property accounting. Eight of twelve equipment items used to fulfill the matching requirements, with a value of \$726,000, were not recorded on property accounting records. Failure to record these items on the property accounting records causes the value of the fixed assets to be understated and the property records relating to the non-state match to be incomplete.

The University is currently establishing a new gift receiving program to be in operation by April 1, 1988. This program includes a new data management computer system and the assignment of a development officer to each department. The development officers would be appropriate individuals to be assigned the task of notifying property accounting of donated equipment because this coincides with their other responsibilities of obtaining and recording gifts and donations.

RECOMMENDATIONS:

3. The University of Minnesota should add the \$726,000 of donated equipment to the property accounting records.
4. The University should develop a process to ensure that all donated equipment is properly recorded. One option would be to assign the development officer the responsibility of notifying property accounting of all equipment obtained through donations.

UNIVERSITY OF MINNESOTA

III. STATUS OF PRIOR AUDIT RECOMMENDATIONS
AND
PROGRESS TOWARD IMPLEMENTATION

The University has not complied with state statutes which require unexpended appropriations of completed building projects to be returned to the state Debt Service Fund. \$260,205 should be returned from appropriation years 1963-1973. In addition, 21 transfers totaling \$452,949 were made between appropriation years without proper authority.

1. A written policy should be established for the annual review of building appropriation projects. This policy should include criteria for determining when a project is complete and for appropriate disposition of account balances in accordance with Minn. Stat. Section 16A.63 and applicable appropriation laws.

RECOMMENDATION SUBSTANTIALLY IMPLEMENTED. The University has not formally developed a written policy for reviewing building appropriation projects. However, in December 1982 the Department of Finance developed Statewide Accounting Procedure 06:03:20 requiring the University to annually certify building appropriation drawdown balances. During this certification process all building project balances are reviewed. In addition, project balances are also reviewed when preparing the legislative budget request.

2. The University should revise their practices to conform with the policy on journal vouchers dated November 11, 1974. Detailed documentation to support journal vouchers should be maintained such as listings of original invoices supporting amounts transferred.

RECOMMENDATION IMPLEMENTED. We reviewed journal vouchers relating to building projects for fiscal years 1984 to 1986, and determined that the journal vouchers contained adequate descriptions. Detailed documentation supporting the journal vouchers are maintained by the Accounting Records and Services Department.

3. The University should refund \$260,205 in balances for completed projects to the state's Debt Service Fund.

RECOMMENDATION IMPLEMENTED. The University refunded \$90,000 to the Debt Service Fund on September 13, 1982. The remaining amount of \$170,204 was transferred to other building projects in accordance with the provisions of the appropriation laws.

4. Building projects for which appropriations have been made since 1973 should be reviewed by University staff for completion and for appropriate disposition of balances. Balances which are not eligible for transfer within the same appropriation should be returned to the state's Debt Service Fund.

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RECOMMENDATION IMPLEMENTED. A review of building project balances was completed in September 1982. Any balances were refunded to the state's Debt Service Fund or transferred to other building projects. See response to Recommendation #3 above.

The method used by the University to calculate periodic receipt of state appropriation results in loss of investment income to the state's General Fund.

5. The University should work with the Department of Finance to analyze the relative percentages of income deriving from state appropriations and tuition and fees, and outside income from sales and services, for the purpose of certifying cash balances pursuant to Minn. Stat. Section 137.025.

RECOMMENDATION IMPLEMENTED. The Accounting Records and Services Department has completed an analysis of the relative percentages of income for fiscal years 1982 through 1985. An analysis of income for fiscal year 1987 will be completed after year end. These analyses are provided to the Department of Finance and are used in certifying cash balances pursuant to Minn. Stat. Section 137.025.

University investment policies for the Permanent University Fund are not in accordance with statutory requirements.

6. The University should develop investment policies for the Permanent University Fund which comply with Minn. Stat. Section 137.022 and Sections 11A.18 and 11A.24.

RECOMMENDATION SUBSTANTIALLY IMPLEMENTED. The University developed investment policies for long term investments of the Permanent University Fund that comply with Minn. Stat. Section 137.022 and Section 11A.18 and 11A.24. The University's short-term investment policies still provide for investment of securities of foreign countries. However, no evidence was found of any investments not in compliance with Minnesota Statutes.

7. In accordance with Minn. Stat. Section 11A.24, the University should compute all percentage limitations on the basis of the book value or original cost of the fund.

RECOMMENDATION WITHDRAWN. Minn. Stat. Section 11A.24 no longer requires the University to compute all percentage limitations on the lower or book value or original cost of the fund.

Students who enlist in the military services during a University term do not receive full tuition refunds.

8. The University's policy for tuition refunds to students voluntarily entering the military service should be changed to allow full refunds of tuition in compliance with Minn. Stat. Section 137.10.

UNIVERSITY OF MINNESOTA

RECOMMENDATION IMPLEMENTED. The University's policy complies with Minn. Stat. Section 137.10 and allows for tuition refunds to all students ordered to active duty.

Tuition is not waived by the University for children of persons who died while in military service. Such waiver is required by Minn. Stat. Section 197.75, Subd. 1.

9. The University should comply with the provisions of Minn. Stat. Section 197.75, Subd. 1 by waiving tuition for children of persons who died in military service.

RECOMMENDATION WITHDRAWN. The University stated that the legislation adopted in 1944, Chapter 663 does not specify the University in the relevant provisions and has never been deemed applicable to the University of Minnesota.

University of Minnesota
Responses to Recommendations of OLA
Fiscal Years 1984, 1985 and 1986

RECOMMENDATION #1

The University of Minnesota should use current year expenditures in determining the amount of contracts designated for the Set Aside Program.

RESPONSE

The legislation requires us to identify the amount to be awarded to small and small socially and economically disadvantaged businesses "prior to the beginning of each fiscal year". However, we agree that actual results of Set Aside Program should make use of the most appropriate data available, which is current fiscal year actual expenditures.

Beginning with the last fiscal year ended June 30, 1987, our annual report to the Legislature will measure our results against the actual expenditures for the same period. Beginning July 1, 1987, all internal Program reports will also be revised to measure actual Set Aside Program results against actual expenditures for the same period.

RECOMMENDATION #2

The annual reports to the Legislature should include all information required by applicable statutes.

RESPONSE

To fully comply with the legislation, we will add the following information to the annual Set Aside Program report to the Legislature beginning with fiscal 1987.

Number of procurement contracts awarded to small businesses owned and operated by economically or socially disadvantaged persons.

Number of requisitions "set aside" for small and economically disadvantaged (SED) firms that were not awarded to such firms; the lowest bid amount on these awards; and the price at which these awards were made to non-SED vendors.

Katherine Cram, Director, Purchasing and Materials Management, has overall responsibility for implementation of Recommendations 1 and 2.

RECOMMENDATION #3

The University of Minnesota should add the \$726,000 of donated equipment to the property accounting records.

RESPONSE

Four of the eight donated equipment items valued at approximately \$588,000 have been recorded. The remaining four items will not be recorded for the following reasons:

IBM Microscope and Digital Voltmeters - These consisted of several pieces of equipment each with a value less than \$500. The University's property accounting policy provides for capitalization of individual items in excess of \$500 only.

Toro Die Caster and Control Data Datatron Testing - These items, which were acquired in 1983, have been disposed of.

Recommendation #4

The University should develop a process to ensure that all donated equipment is recorded.

RESPONSE

We agree that additional control needs to be implemented to ensure the timely recording of donated equipment. This has been a problem in the past due to untimely reporting by University departments to Property Accounting.

Accounting Records and Services is responsible for preparing the draw request for State funds based upon information from University departments that the match has been made. Effective immediately, Accounting Records and Services will notify Property Accounting when the draw request is received. This will serve as notice to Property Accounting that the donated equipment exists. Property Accounting will then contact the respective department in order to obtain the necessary information to record the transaction.

Brian Obermeier, Director, Accounting Records and Services, has overall responsibility for implementation of Recommendations 3 and 4.



UNIVERSITY OF MINNESOTA

Office of the Controller and Treasurer

Vice President for Finance and Operations
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Minneapolis, Minnesota 55455
(612) 625-4555

July 22, 1987

Ms. Claudia Gudvangen
Audit Manager
Office of the Legislative Auditor
Veterans Service Building
St. Paul, MN 55155

Dear Ms. Gudvangen:

Enclosed are our responses to your recommendations which resulted from your legal compliance audit of the University of Minnesota for fiscal years 1984, 1985 and 1986.

Very truly yours,

A handwritten signature in cursive script that reads "Carol N. Campbell".

Carol N. Campbell
Controller and Treasurer

CNC/lis