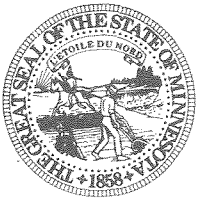


**STATE UNIVERSITY SYSTEM  
SOUTHWEST STATE UNIVERSITY  
FINANCIAL AND COMPLIANCE AUDIT  
FOR THE THREE YEARS ENDED JUNE 30, 1987**

**JULY 1988**





STATE OF MINNESOTA

**OFFICE OF THE LEGISLATIVE AUDITOR**

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

JAMES R. NOBLES, LEGISLATIVE AUDITOR

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Representative Phillip J. Riveness, Chairman  
Legislative Audit Commission

Members of the Legislative Audit Commission

Dr. Robert Carothers, Chancellor  
State University System

Members of the State University Board

Dr. Douglas Treadway, President  
Southwest State University

**Audit Scope**

We have completed a financial and compliance audit of Southwest State University (SSU) for the three years ended June 30, 1987, except for those programs and activities further described in the Scope Limitations section of this letter. 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 March 4, 1988.

We have issued separate management letters to the State University System, dated March 24, 1988 and March 26, 1987, which include the audit of major federal programs administered by SSU for the fiscal years ended June 30, 1987 and 1986.

The objectives of this audit were to:

- study and evaluate certain Southwest State University internal accounting control systems, including a review of tuition receipts, payroll, disbursements through the statewide accounting system including the Job Skills Partnership and Science and Technology Resource Center grants, imprest cash, federal student financial aid, and receipts and disbursements from the University Activity Fund;
- verify that financial transactions were made in accordance with applicable laws, regulations, and policies, including Minn. Stat. Chapter 136, State University Board policies and procedures, and other finance-related laws and regulations;
- evaluate the recording and reporting of financial transactions on the statewide accounting system and the university's internal accounting system; and
- determine the status of prior audit recommendations.

Representative Phillip J. Riveness, Chairman  
Members of the Legislative Audit Commission  
Dr. Robert Carothers, Chancellor  
Members of the State University Board  
Dr. Douglas Treadway, President  
Southwest State University  
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Southwest State University is affiliated with a separate nonprofit foundation. The university and the foundation have entered into a written agreement specifying their relationship. Pursuant to the agreement, SSU personnel are responsible for providing various administrative services for the foundation. The foundation maintains an independent Board of Directors who oversee foundation activities and are responsible for policy-making decisions. The foundation is audited by a private CPA firm. We did not audit the foundation. We did, however, review the relationship with the foundation and performed limited testing of the administrative services provided by university personnel to the foundation. We satisfied ourselves that the foundation is sufficiently autonomous from the university and that the administrative services provided by the university are subject to adequate controls.

#### Management Responsibilities

The management of SSU is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgements by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system of internal control are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorizations and recorded properly.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions, or that the degree of compliance with the procedures may deteriorate.

The management of SSU is also 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 SSU. The purpose of our testing of transactions was to obtain reasonable assurances that SSU had, in all material respects, administered their programs in compliance with applicable laws and regulations.

#### Scope Limitations

The Revenue Fund is audited each year by a private CPA firm for the limited purpose of expressing an opinion on the financial statements of the fund. We have not placed any reliance on the work done by other auditors on the Revenue Fund in connection with this audit. Although our audit did include a review of internal controls and the performance of substantive tests for certain material components of the State University Revenue Fund activities administered by SSU for the three years ended June 30, 1987, our limited scope precludes us from rendering audit opinions on these activities.

Representative Phillip J. Riveness, Chairman  
Members of the Legislative Audit Commission  
Dr. Robert Carothers, Chancellor  
Members of the State University Board  
Dr. Douglas Treadway, President  
Southwest State University  
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We did not audit major federal programs at SSU for the fiscal year ended June 30, 1985. Those programs were audited by a private CPA firm for that year. We did not review the work done by other auditors on the federal programs and have placed no reliance on their work.

### Conclusions

In our opinion, except for those issues raised in Section II, finding #1, and subject to the effects, if any, of the federal programs and Revenue Fund activities which we did not audit as described in the Scope Limitations section of this letter, the SSU system of internal controls in effect as of December 31, 1987, taken as a whole, was sufficient to provide management with reasonable, but not absolute assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions relating to those systems are executed in accordance with management's authorization.

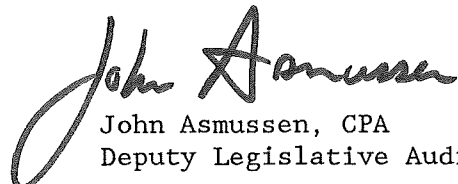
In our opinion, except for the issue raised in Section II, finding #2, and subject to the effects, if any, of the federal programs and Revenue Fund activities which we did not audit as described in the Scope Limitations section of this letter, for the three years ended June 30, 1987, SSU administered its programs in compliance, in all material respects, with applicable finance-related laws and regulations.

In our opinion, and subject to the effects, if any, of the federal programs and Revenue Fund activities which we did not audit as described in the Scope Limitations section of this letter, for the three years ended June 30, 1987, SSU properly recorded, in all material respects, its financial transactions on the statewide accounting system, or the university accounting system as appropriate.

The recommendations included in this report are presented to assist the university in resolving the audit findings and in improving accounting procedures and controls. We will be monitoring and reviewing SSU's progress on resolving these findings. A summary of the progress made on audit recommendations discussed in our last audit report covering the year ended June 30, 1984, dated August 26, 1985, is shown in Section III entitled "Status of Prior Audit Recommendations and Progress Toward Implementation."

We would like to thank the SSU staff for their cooperation during this audit.

  
James R. Nobles  
Legislative Auditor

  
John Asmussen, CPA  
Deputy Legislative Auditor

July 12, 1988



# SOUTHWEST STATE UNIVERSITY

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## AUDIT PARTICIPATION

The following members of the Office of the Legislative Auditor participated in this audit:

John Asmussen, CPA	Deputy Legislative Auditor
Jim Riebe, CPA	Audit Manager
Michael Hassing	Auditor-in-Charge
Ellen Merlin, CPA	Staff Auditor
Colleen Skillings	Staff Auditor

## EXIT CONFERENCE

The findings and recommendations in this report were discussed with the following staff of Southwest State University on March 4, 1988:

Douglas Treadway	President
Lynn Cupkie	Vice President - Student Affairs
William Marshall	Vice President - Administration
Dennis Bakke	Director - Business Services
James Babcock	Director - Science & Technology Resource Center
Sharon Peterson	Financial Aids Assistant





# SOUTHWEST STATE UNIVERSITY

## I. INTRODUCTION

Southwest State University (SSU) is one of Minnesota's seven state universities governed by the State University Board (SUB). Board members are appointed by the Governor and subject to confirmation by the state senate. Appointed by the Board, Dr. Douglas Treadway serves as the president of the university.

SSU offers academic programs in both the liberal arts and in technical fields, as well as varied social, cultural, and recreational opportunities. These courses are funded primarily through student tuition and fees. In addition, SSU receives state appropriations from the General Fund. Educational operations of the university are generally accounted for through the statewide accounting system. Other activities including federal financial aid programs, dormitory, and student union accounts are handled through a local bank and are recorded on the state university accounting system. These other activities are governed by the SUB and accounted for in the Revenue Fund and University Activity Funds.

SSU collected the following current fund receipts and made the following expenditures during the audit period. These amounts were taken from the university's annual reports.

	<u>Fiscal Year</u> <u>1984-85</u>	<u>Fiscal Year</u> <u>1985-86</u>	<u>Fiscal Year</u> <u>1986-87</u>
Current Receipts:			
Tuition and fees	\$ 2,321,317	\$ 2,531,551	\$ 2,890,984
State appropriation	7,838,186	8,544,972	9,022,564
Federal grants and awards	1,356,515	1,606,681	1,660,728
Sales and services of auxiliary enterprises	2,564,580	2,544,242	2,925,470
Other resources	<u>949,884</u>	<u>1,326,233</u>	<u>1,738,129</u>
Total Receipts	<u>\$15,030,482</u>	<u>\$16,553,679</u>	<u>\$18,237,875</u>
Expenditures:			
Instruction	\$ 4,904,144	\$ 5,231,995	\$ 5,260,540
Other educational costs	1,126,287	1,383,082	1,541,415
Financial aids	1,715,156	1,950,114	2,265,445
Student support services	1,415,262	1,396,903	1,288,896
Institutional support services	1,626,294	1,755,168	1,800,314
Plant operations	1,410,499	1,481,370	1,553,534
Auxiliary enterprise expenditures	2,428,799	2,433,165	2,780,002
Other operating expenses	<u>650,641</u>	<u>699,433</u>	<u>903,612</u>
Total Expenditures	<u>\$15,277,082</u>	<u>\$16,331,230</u>	<u>\$17,393,758</u>

From 1985 to 1987, the period covered by this audit, enrollment at SSU has increased 13 percent, from 1,758 to 1,987 full-time students.

## SOUTHWEST STATE UNIVERSITY

### II. CURRENT FINDINGS AND RECOMMENDATIONS

1. Financial controls of the Science & Technology Resource Center are inadequate to ensure that expenditures are appropriate.

The Science & Technology Resource Center (STRC) was established in 1985 to encourage economic development in southwestern Minnesota. The STRC utilizes the resources of Southwest State University (SSU) and other regional post-secondary educational institutions to provide entrepreneurs with technical advice in research and development, as well as assistance in marketing and securing capital. The Minnesota Legislature appropriated \$600,300 and \$524,700 to the STRC for each of the first two years of this program. During these years, approximately \$172,000 has been disbursed on behalf of grantees. Additionally, \$412,000 and \$289,000 have been spent on administrative and instructional costs.

While some direction is provided by an advisory committee and the president of SSU, applications for assistance are approved by the STRC director. When the STRC program was originated, the members of the advisory committee completed project evaluations to be used in determining which projects would be accepted. However, that practice has been discontinued. Since then the STRC project evaluation and selection process has become too informal. The project applications should be formally discussed by the advisory committee members or another board of university personnel and recommendations made which indicate the ranking of projects to be approved. SSU may want to resume the completion of project evaluations by advisory committee members to formalize evaluation criteria and the selection process. Also, committee decisions should be recorded in minutes of committee meetings.

The director also has sole responsibility for authorizing project expenditures. Under strong accounting controls, authorization and disbursement functions would be separate. Without such separation, there is not adequate assurance that all project expenditures are reasonable, or that errors and irregularities will be detected in the normal course of business. Better separation of duties might include more active participation by the advisory committee or the business office in reviewing project expenditures.

Once STRC projects have been approved, there should also exist an adequate system to monitor the status of these projects. The STRC has not established initial budgets for projects and has not developed a system to compare actual and estimated costs to prevent potential cost overruns; neither have they required the submission of periodic financial reports and evaluations to ensure that all contractual obligations have been met. STRC staff may also want to exercise the right to review grantee records that support the financial information submitted by grant recipients. Regarding the lack of final reports or evaluations, support outlining the benefits received from a \$10,000 contract negotiated in 1987 could not be located during our audit. The consulting contract was for exploring potential economic opportunities in the Far East from which other projects

## SOUTHWEST STATE UNIVERSITY

might be developed locally. Without a final report or evaluation, payment may have been made inappropriately, before the contractual services were completed.

Without an established system of control over the approval and disbursement functions, there can be virtually no assurance that all program expenditures are appropriate.

### RECOMMENDATIONS

- A formal process should be established for reviewing and approving applications for STRC funds.
- Administrative and financial controls should be established to ensure the propriety of project expenditures.

2. There is no mechanism to address potential conflicts of interest involving university employees, particularly STRC staff.

Minn. Stat. Section 43A.38, Subd. 5(a) and (b) states that the use of an employee's position to secure advantages for the employee which are different from those available to the general public, or the acceptance of a contractual relationship that will affect the employee's independence of judgment in the exercise of official duties, constitutes a conflict of interest. The statute provides that if the potential for a conflict of interest exists, it is the employee's duty to avoid the situation. Furthermore, if a conflict of interest does exist, the matter shall be assigned to another employee who does not have a conflict of interest. Finally, if it is not possible to reassign the matter to another employee, interested persons should be notified of the conflict and the employee may proceed with the assignment.

The director of the STRC ultimately makes the final decisions on which projects receive financial assistance. However, he often relies on technical and administrative advice from STRC staff to reach his conclusions. Therefore, it is important to ensure that conflict of interest procedures are followed so that staff do not receive an unfair advantage over other applicants. To date, STRC staff members have applied for assistance in developing four projects from which they could potentially profit. One of the projects was rejected and the following three projects were approved without regard to the requirements of Minn. Stat. Section 43A.38:

Based on a suggestion from a past STRC director, a technical staff member applied for project assistance in November 1985 to develop frozen or freshly packaged food entrees. The project did not appear to have enough potential and was rejected. Later, after the technician had been promoted to assistant director of the STRC, the new director gave approval for renewed development of the project. Although the project has not received any material funding to date, there are plans to continue developing the project once better research facilities are available at SSU.

## SOUTHWEST STATE UNIVERSITY

A project featuring packaged science experiments for instructional purposes was developed by two faculty members of Southwest State University. These faculty members were later hired as technicians by the STRC. The application was approved after evaluation by the advisory committee. To date no monetary assistance has been provided. However, under the director's approval, the technicians have spent STRC time developing the project.

A secretary of the STRC donated private property for use in a wildflower project. Her involvement in the project was never officially approved nor was a contract signed. In fact, we were concerned that the staff member became involved in this project because of a breach of confidentiality by the STRC over client information. In this case, information from another project for the manufacture of perfume from wildflowers was used in a manner that potentially will benefit this employee. Even though only \$500 has been spent on the project, because the STRC has a responsibility to avoid any questionable use of client data, they should determine what action must be taken to resolve this issue, including possibly recovering the initial investment or receiving potential royalties from any profits derived.

As discussed in the last example, university staff need to maintain the confidentiality of client data. In the STRC Project Disclosure and Agreement, an attempt has been made to disclaim the confidential relationship with contracting entrepreneurs. However, according to Minn. Stat. Section 13.37, Subd. 1(b), data collected on projects at the STRC is nonpublic since independent economic value, actual or potential, may be derived from the information not being generally available to other persons. Therefore, the STRC has a responsibility to protect project information from use for any purpose other than that stated by the entrepreneur without his or her express permission.

### RECOMMENDATION

- The STRC should develop policies to address potential conflicts of interest and the safeguarding of project information.

SOUTHWEST STATE UNIVERSITY

III. STATUS OF PRIOR AUDIT RECOMMENDATIONS  
AND  
PROGRESS TOWARD IMPLEMENTATION

Southwest State University (SSU) needs to more closely monitor outstanding overdue accounts receivable.

1. To improve control over overdue accounts receivable, SSU should:
  - comply with SUB policies concerning minimum collection efforts on all accounts receivable; and
  - consider writing off eligible overdue accounts receivable when appropriate.

RECOMMENDATION IMPLEMENTED. Southwest State University has taken appropriate action to collect overdue accounts receivable and currently follows established guidelines for writing off eligible overdue accounts.

Internal controls over ticket receipts need improvement.

2. SSU should improve internal controls over ticket receipts by:
  - reconciling tickets sold with cash receipts for each theater ticket sales location. Each individual reconciliation should be approved by the ticket manager;
  - maintaining printers' certifications of tickets printed and accounting for the complete sequence of ticket numbers on each roll; and
  - maintaining a minimum inventory of ticket rolls.

RECOMMENDATION IMPLEMENTED. SSU has developed procedures, dated November 10, 1987, to monitor ticket inventory and distribution. These procedures require the reconciliation of cash receipts to tickets sold by location for each event.



July 12, 1988

James R. Nobles, Legislative Auditor  
Office of the Legislative Auditor  
1st Floor Veterans Service Building  
20 W. 12th Street  
St. Paul, MN 55155

Dear Mr. Nobles:

We have received the Audit findings and recommendation for the Audit covering the three year period ending June 30, 1987. The following are our responses:

Finding #1: Financial controls of the Science and Technology Resource Center are inadequate to ensure that expenditures are appropriate.

Response: We concur with the recommendation to implement a procedure to ensure that projects and budgets are reviewed, evaluated and approved by the Vice President for Marketing and Development prior to start of project. In addition, ad hoc committees will be formed consisting of members from the Advisory Committee to review projects involving expenditures over \$10,000. Approved budgets will be established in a separate project account so that they can be monitored. This will be implemented by August 1, 1988. The person responsible will be the Director of the Science and Technology Resource Center.

Finding #2: There is no mechanism to address potential conflicts of interest involving University employees, particularly Science and Technology Resource Center staff.

Response: We concur with the recommendation and a policy statement and procedure will be written by the Director of the Science and Technology Resource Center and approved by the President by September 1, 1988.

Because of concerns indicated in the audit report, I feel that it is important to clarify the facts regarding the "wildflower project".

In meeting with the STRC mandate to relieve economic stress through new product development, three avenues of investigation were pursuant:

1. Technical feasibility of producing perfume from wildflowers.
2. Market feasibility of wildflowers.
3. Test plot to determine durability of varieties of wildflowers.

The information generated by this research will be used in the following manner:

1. Information concerning the growing and marketing of wildflowers will be made available to any parties interested in wildflowers as a crop. This is not proprietary information and the investigation of growing and marketing of wildflowers was not investigated by the request of one client.
2. Any information generated concerning the use of wildflowers as a base for perfume will be provided only to the client requesting that information unless the client gives permission for it to be released to others.

The audit report raises two issues regarding the wildflower project:

1. Breach of confidentiality.
2. Potential benefit of staff member.

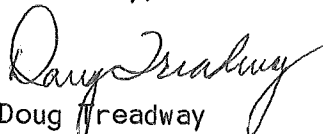
First, we are not aware of a breach of client confidentiality since information regarding the manufacture of perfume from wildflowers was not released to anyone except the client requesting the information.

Second, there was never intended to be any economic benefit accruing to the staff member who offered to donate the land for the test site. The offer of land use was accepted since it was at no cost to the State of Minnesota. It was a goodwill offer by a conscientious employee. In addition, there does not seem to be an opportunity for any economic benefit to occur, since the quantities of the many varieties grown in the small plot are insufficient to harvest for profit. We will continue to monitor the test plot for the remainder of the growing season and the plot will be returned to crop land in the spring of 1989, ensuring that no economic benefit will accrue to the employee.

Because of concerns about potential conflict of interest raised, I am revoking all previous decisions to provide assistance for projects submitted by staff members employed by the STRC. This action is intended to eliminate any appearance of potential conflict of interest that may exist.

Thank you for the opportunity to respond to these audit findings. If you have any questions concerning this matter, let me know.

Sincerely,



Doug Treadway  
President

/ljp

cc: James Babcock, Director, STRC  
Robert Johnson, Vice President for Marketing & Development  
William Marshall, Vice President for Administration