

**MANKATO STATE UNIVERSITY
FINANCIAL AUDIT
FOR THE THREE YEARS ENDED JUNE 30, 1991**

AUGUST 1992

Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

SUMMARY

State of Minnesota

Office of the Legislative Auditor

Centennial Office Building • St. Paul, MN 55155

612/296-4708

MANKATO STATE UNIVERSITY

FINANCIAL AUDIT FOR THE THREE YEARS ENDED JUNE 30, 1991

Public Release Date: August 28, 1992

No. 92-55

OBJECTIVES:

- EVALUATE INTERNAL CONTROL STRUCTURE: Tuition and fee revenues, student and employee payroll, administrative expenditures, computer store revenues and expenditures, and federal financial aid (for fiscal year 1992).
- TEST COMPLIANCE WITH CERTAIN FINANCE-RELATED LEGAL PROVISIONS.

CONCLUSIONS:

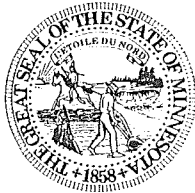
We found three areas where the internal control structure needed improvement:

- Mankato State University does not have adequate control over supplemental fees.
- Some university departments do not complete receiving reports for computer equipment.
- Several employees have inappropriate access to a computer program.

We found two areas where the university had not complied with finance-related legal provisions:

- An employee inappropriately received overtime.
- Mankato State University did not properly bid out two contracts.

Contact the Financial Audit Division for additional information.
(612) 296-1730



STATE OF MINNESOTA

OFFICE OF THE LEGISLATIVE AUDITOR

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

JAMES R. NOBLES, LEGISLATIVE AUDITOR

Representative Ann Rest, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

Dr. Terrence J. MacTaggart, Chancellor
State University Board

Members of the State University Board

Dr. John B. Davis, Interim President
Mankato State University

Audit Scope

We have conducted a financial related audit of selected financial activities of Mankato State University for the three years ended June 30, 1991. Our audit was limited to only that portion of the State of Minnesota financial activities attributable to the transactions of Mankato State University, as discussed in the Introduction. We have also made a study and evaluation of the internal control structure of Mankato State University in effect at January 1992.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial activities attributable to the transactions of Mankato State University are free of material misstatements.

As part of our study and evaluation of the internal control structure, we performed tests of Mankato State University's compliance with certain provisions of laws, regulations, contracts, and grants. However, our objective was not to provide an opinion on overall compliance with such provisions.

Testing of Federal Financial Aid

Testing of Mankato State University's federal financial aid programs is done in conjunction with our Statewide Audits of the State of Minnesota's annual financial statements and federal programs. We issued three separate management letters to the State University System concerning federal financial aid during the audit period. They were dated May 3, 1990, April 8, 1991, and April 16, 1992, and covered fiscal years 1989, 1990, and 1991, respectively. The fiscal year 1989 management letter contained one finding related to Mankato State University. The

university did not assess late charges on delinquent Perkins loan accounts. The fiscal year 1990 and 1991 management letters did not contain any findings relating to Mankato State University.

Management Responsibilities

The management of Mankato State University is responsible for establishing and maintaining an internal control structure. This responsibility includes compliance with applicable laws, regulations, contracts, and grants. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that:

- assets are safeguarded against loss from unauthorized use or disposition;
- transactions are executed in accordance with applicable legal and regulatory provisions, as well as management's authorization; and
- transactions are recorded properly on the statewide accounting system in accordance with Department of Finance policies and procedures.

Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

Internal Control Structure

For purposes of this report, we have classified the significant internal control structure policies and procedures into various categories. For all of the internal control structure categories listed below, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk.

- tuition revenues;
- administrative expenditures;
- employee payroll;
- student payroll;
- federal financial aid revenues;
- federal Pell and SEOG grant expenditures;
- Perkins loan expenditures and repayments;
- computer store revenues; and
- computer store expenditures.

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We also identified the Revenue fund as another significant internal control structure category. However, we did not assess control risk for this category. The Chancellor's Office, under the guidance of the Minnesota State University board administers the State University System's Revenue Fund. The Revenue Fund was established for the purpose of operating self-supporting residence halls, food services, and student union programs. The State University System's Revenue Fund is audited annually by a CPA firm.

Conclusions

Our study and evaluation disclosed the conditions discussed in findings 1 to 5 involving the internal control structure of Mankato State University. We consider these conditions to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the entity's ability to record, process, summarize, and report financial data.

A material weakness is a reportable condition in which the design or operation of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial activities being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We believe none of the reportable conditions described above is a material weakness.

We also noted other matters involving the internal control structure and its operation that we reported to the management of Mankato State University at the exit conference held on April 9, 1992.

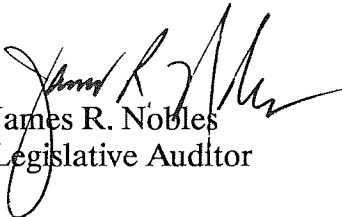
The results of our tests indicate that, except for the issues discussed in findings 1 and 3, with respect to the items tested, Mankato State University complied, in all material respects, with the provisions referred to in the audit scope paragraphs. With respect to items not tested, nothing came to our attention that caused us to believe that Mankato State University had not complied, in all material respects, with those provisions.

Pursuant to Minn. Stat. Section 3.975, finding 1 shall be referred to the Attorney General. The Attorney General has the responsibility to ensure the recovery of state funds and in fulfilling that role may negotiate the propriety of individual claims.

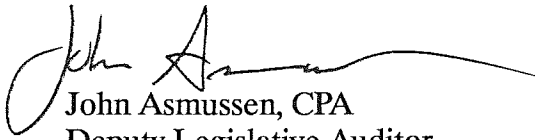
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This report is intended for the information of the Legislative Audit Commission and management of Mankato State University. This restriction is not intended to limit the distribution of this report, which was released as a public document on August 28, 1992.

We thank the Mankato State University staff for their cooperation during this audit.



James R. Nobles
Legislative Auditor



John Asmussen, CPA
Deputy Legislative Auditor

End of Fieldwork: April 10, 1992

Report Signed On: August 21, 1992

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Audit Participation

The following members of the Legislative Auditor prepared this report:

John Asmussen, CPA	Deputy Legislative Auditor
Tom Donahue, CPA	Audit Manager
Alan Finlayson, CPA	Auditor-in-Charge
Sonya Hill, CPA	Auditor
Mark Johnson	Auditor

Exit Conference

The findings and recommendations in this report were discussed with the following staff of Mankato State University on April 9, 1992:

Dr. John B. Davis	Interim President
H. Dean Trauger	Vice President for Fiscal Affairs
Laverna Alm	Comptroller
Joan Rigdon	Director of Accounting
Garnet Cafourek	Director of Accounts Receivable

Introduction

Mankato State University is under the management and control of the Minnesota State University Board. The board appoints a president for each university. Dr. Margaret Preska served as president of Mankato State University until February 1, 1992. Dr. John B. Davis is the interim president while the board begins its search for a new president.

Operations of the university are financed mainly by student tuition and fees, and state appropriations from the General Fund. Financial activities of the university are accounted for on the statewide accounting system (SWA). Other activities are accounted for only on the university's accounting system. These programs include student financial aid, self supporting enterprises, and student activity accounts. Funds for these activities are maintained in a local bank account. The State University Board has established policies to govern these accounts.

The following is a summary of the financial activity for Mankato State University for the three years ended June 30, 1991:

Revenue:	
Tuition and Fees	\$ 64,351,773
Federal Financial Aid	22,082,937
Perkins Loan Repayments	3,220,542
Computer Store	3,494,139
Other	<u>49,480,851</u>
Total	<u>\$142,630,242</u>
Expenditures:	
Employee Payroll	\$155,855,929
Pell and SEOG Grants	20,457,004
Perkins Loans	3,010,270
Administrative Expenditures	32,571,761
Student Payroll	10,707,707
Computer Store	2,816,730
Other	<u>34,035,518</u>
Total	<u>\$259,454,918</u>

Sources: Statewide Accounting Manager's Financial Reports for fiscal years 1991, 1990, and 1989, as of the closing date. Mankato State University Financial Reports and accounting system balances for fiscal years 1991, 1990, and 1989.

Current Findings and Recommendations

1. An employee inappropriately received overtime.

Robert Herickhoff, Dean of the School of Physics, Engineering and Technology, inappropriately claimed and received \$12,000 of overtime for working on a grant. The overtime payments occurred between August and December, 1990. Dr. Herickhoff is an unclassified manager who is not covered by a collective bargaining unit. The State University Board establishes the compensation terms for this classification. Under board policy, employees cannot receive overtime except "in emergency situations where managerial employees are asked to assume unusual extra duties...".

We do not believe an emergency situation existed in this instance. Dr. Herickhoff requested the overtime upon the resignation of a staff member who was working on the grant. Dr. Herickhoff stated that he had to perform additional tasks to complete the grant. These duties consisted of writing status reports and attending meetings. The assistant vice president for Academic Affairs approved the overtime. However, he stated that he was not aware of the board policy. The board policy only allows for overtime in "exceptional situations." We do not believe that completing status reports and attending meetings meets the requirements of the policy.

The grantor, Minnesota Advanced Manufacturing Technology Center, Inc. (MAMTC) claims that the grant ended before the occurrence of the overtime. MAMTC has refused to reimburse the university for approximately \$21,000 in costs, incurred after August 1990. The grant was for the planning of a manufacturing center in Mankato. The grant term was to end the earlier of December 31, 1990 or completion of the final report and plan. The university issued its plan in June 1990. Dr. Herickhoff continued to work on the project and charge his payroll to the grant through December 1990.

Recommendation

- *Mankato State University should seek repayment of \$12,000 from Dr. Herickhoff.*

2. Mankato State University does not have adequate control over supplemental fees.

The university does not ensure that supplemental fees are collected and recorded or that outstanding receivables are adequately pursued. In addition, the university does not report supplemental fees to the State University Board Office.

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Currently, individual university departments are responsible for ensuring the collection of supplemental fees. However, the Business Affairs Office does not have records of the amounts charged to each student. We noted that the Home Economics Department has collected cash for its supplemental fees. This situation increases the risk that cash receipts may be lost or stolen and not be detected.

University Board policy 5.4, subdivision 2(b) provides that "Each university may charge special fees to recover costs for course supplies beyond those necessary for normal instruction. Subdivision 2(c) requires that "each university shall submit a complete listing of all supplemental course fees to the Chancellor for transmittal to the State University Board at its annual meeting."

The Business Affairs Office is in the best position to ensure that adequate control over supplemental fees is maintained. It has established controls already in place to ensure the proper depositing of receipts and adequate follow up of uncollected amounts. The Business Affairs Office would then be in a position where it could report on supplemental fees to the State University Board Office.

Recommendation

- *Mankato State University should improve controls over supplemental fees by*
 - *having the Business Affairs Office record, collect, and monitor the charges, and*
 - *reporting the fees to the board office.*

3. Mankato State University did not properly bid two contracts.

The university did not follow state bidding requirements for two contracts. Several problems existed with a \$49,472 contract for construction of a road. In another instance, the length of a contract exceeded statutory limits. Minn. Stat. Section 16B.07 establishes the procedures for competitive bidding.

In the first instance, Mankato State University did not advertise the contract, or obtain sealed bids. Instead, the university used a private engineering firm to solicit bids. Staff stated that the engineering firm verbally contacted three companies, but only one expressed an interest in the project. As a result, that company received the contract.

According to Minn. Stat. Section 16B.07, subd. 3, "If the amount of an expenditure is estimated to exceed \$15,000, sealed bids or requests for proposals must be solicited by public notice...in a newspaper or trade journal." In addition, "All original bids and all documents pertaining to the award of a contract must be retained and made part of a permanent file or record." In our view, the use of a private engineering company, or the process it followed, did not satisfy this requirement.

Mankato State University

The university and the State University Board stated that the project was an emergency. Minn. Stat. Section 16B.08, subd. 6, does provide an exception to the competitive bid requirements outlined in Section 16B.07, subd. 3. Subd. 6 specifies that “in emergencies, the Commissioner (of Administration) may without calling for bids, contract directly for the repair, rehabilitation...” It also defines an emergency as “an unforeseen occurrence or combination of circumstances which calls for immediate action in the public interest.” Although there was a sense of urgency to the situation that gave rise to the contract, it was not an emergency as defined above. Additionally, if it was an emergency, the Commissioner of Administration should have provided the authorization.

In the second instance, Mankato State University entered into a 10 year contract with a vendor to provide gas cylinders. Minn. Stat. Section 16B.07, subd. 2, limits the terms of standard price contracts to five years, including all extensions. At the end of the contract, the state must solicit bids for the service.

The university needs to follow the bidding process to ensure that the state receives the lowest cost for the desired level of service. This process also demonstrates that the state purchases without bias.

Recommendation

- *Mankato State University should follow state bidding requirements for all contracts.*

4. University departments do not consistently complete receiving reports for computer equipment.

Some university departments do not complete receiving reports for computer equipment. For 6 of 13 items tested, no receiving reports were on file. The central receiving department counts most goods when delivered and prepares a receiving report. However, it does not count or prepare receiving reports for computer equipment because of its technical nature. Therefore, individual departments receiving the computer equipment must verify the quantity and condition of the equipment received. In addition, departments receiving computer equipment should complete and sign a receiving report and forward a copy to the Business Affairs Office.

Recommendation

- *University departments should complete and sign receiving reports for computer equipment and forward copies to the Business Affairs Office.*

Mankato State University

5. Several employees have inappropriate access to a computer program.

Several Business Affairs Office employees have inappropriate authority to run an accounts receivable program. The program could be run to eliminate charges, other than tuition, and go undetected. One of the individuals is the lead cashier. The cash handling function should be kept separate from the accounting function. There are also six individuals in the Computer Services department that have authority to run this program. These employees do not need access to the program as part of their job. If they need to modify the program, the security administrator can give them temporary access.

Recommendation

- *Mankato State University should further restrict access to the accounts receivable program.*

Mankato

STATE UNIVERSITY

OFFICE OF THE VICE PRESIDENT FOR FISCAL AFFAIRS
MSU BOX 60
389-6621

August 7, 1992

Thomas Donahue, Audit Manager
Office of the Legislative Auditor
1st Floor, Centennial Office Building
658 Cedar Street
St. Paul, MN 55155

Dear Tom,

President Davis has asked me to handle Mankato State University's response to your report which summarizes the results of the audit work at Mankato State for the three years ended June 30, 1991.

We very much appreciate the fine work that the Office of the Legislative Auditor did for us during the recent financial audit of Mankato State University. The auditors assigned to the audit were very thorough in their work and handled their responsibilities in a very professional manner. Their work is invaluable to us since our staff handles a \$100 million a year operation, but we do not have an internal auditor(s) to review internal controls, or make compliance checks.

Mankato State's response to the five audit findings and recommendations is enclosed. We agree with all of them. If you have any questions regarding our response to the audit findings and recommendations, please contact me at (507)389-5010.

Sincerely.



H. Dean Trauger
Vice President for Fiscal Affairs

Enc.

xc: John B. Davis
Ed McMahon

HDT/ks

Mankato State University
Office of Legislative Auditor
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1. An employee inappropriately received overtime.

Recommendation: Mankato State University should seek repayment of \$12,000 from Dr. Herickhoff.

We concur with the finding and the recommendation. The Board's policy regarding excluded compensation has been available to all excluded employees, but we will send a copy of the pay policy to all excluded employees so that they have all details regarding the excluded pay plan. This was a situation where a payroll document was processed through the pay system without appropriate review for the type of transaction being processed. We have taken steps to safeguard against such a reoccurrence.

2. Mankato State University does not have adequate control over supplemental fees.

Recommendation: Mankato State University should improve controls over supplemental fees by having the Business Affairs Office record, collect and monitor the charges and reporting the fees to the Board Office.

We concur with the finding and the recommendation. It has been a University policy that no course fees could be assessed unless the department asked for and received permission to charge the fee from their Dean, the Academic Affairs Office and the Fiscal Affairs Office.

The Business Office had established some self-supporting accounts in our local bank account to handle the purchasing of supplies for students' course work in larger more economical amounts (such as gold or silver for jewelry classes). The students were to deposit their share of costs directly to the Cashiers Office so quantity purchases could be made by the instructor or designee. We did not require and should have required that the charge be put on the Accounts Receivable System under the individual student's name. In reviewing this matter, we find that the instructors were in some cases collecting the money directly from the students.

We also found that there were supplemental fees being charged and collected in some classes where approval had not been obtained. Fee information had been listed in the Quarterly Class Schedules, but it was assumed that these fees were to be paid directly to third party entities (Bowling Alley - purchase of arrows for archery, etc.). Most of them were this type of fee.

We are presently working on a communication that will be sent to all departments reiterating that no student supplemental fees may be assessed without the approval of the Academic Affairs and Fiscal Affairs Vice President offices. No fees will be collected in the classroom or departments. We will make adjustments to our billing system so that all charges associated with a specific class will be charged automatically and entered to the Accounts Receivable System at the time regular tuition billings are generated for students.

A list of the approved fees will be submitted annually to the State University Board Office.

3. Mankato State University did not properly bid two contracts.

Recommendation: Mankato State University should follow State bidding requirements for all contracts.

We concur with the finding and the recommendation. However, we have comments regarding the two situations cited.

(1) We agree with the comments regarding the bidding on the road construction project. Lester Gieneart, Asst. Vice President for Facilities Planning, worked with Bolton and Menk, Inc. on the project and he has summarized what occurred.

During the planning and design of Andreas Observatory, we reviewed the function of the Observatory and the designs with the City of Mankato and the Department of Administration's Building Code Department. Initially their assessment of the structure and function was of an experimental and research nature and, thus, authorized us to design a structure and access with minimal fire access and Section 504 accessibility compliance: the determination of an experimental status for the Observatory was completely supported by the astronomy faculty as the lights of vehicles on an access road could seriously disrupt their observations and instructional programs. Based on these approvals by the City and the State, we proceeded to design and construct the Observatory.

Once the Observatory was completed, the Department of Administration's Building Code Department informed us that full Section 504 compliance was required. The City of Mankato also changed their position and stated that because of the accessibility by the public, ambulant and physical challenged and emergency response access road was required before they would issue a Certificate of Occupancy. Having handled the design and construction of the Observatory in accordance with directives provided by our regulatory agencies, we were now faced with the embarrassing prospect of not being able to use the completed Observatory.

We, therefore, quickly moved forward with the design of an access road to meet the demands of these regulatory agencies.

It was late in the construction season and we expedited the project on an emergency basis working with Bolton and Menk, Inc. Bolton and Menk did the engineering work and handled the project bidding. Unfortunately, authorization to handle the project as an emergency was not obtained from the Commissioner of Administration.

Since this project, closer working relationships have been established with Mankato State's Purchasing Office to ensure strict compliance with applicable Minnesota Statutes.

(2) We agree that the University needs to follow the bid process to ensure that the State receives the lowest cost for the desired level of service. The ten year contract with Gopher Welding was entered into for several reasons, but two of the more important ones were:

1. Gopher Welding being the current State contract vendor (M-9966) agreed to give the University special pricing discounts by entering into the long term lease. In actuality, all demurrage charges would be removed over the course of the lease and the total savings in terms of demurrage would be about \$25,000. Since the lease agreement provides for a cancellation clause and a refund schedule set up in the event of cancellation, the University may consider rescinding the lease if Gopher Welding does not continue as a State contract vendor in subsequent years.

2. All University departments who use gas cylinders on campus collectively agreed to set up the lease for the benefit of their departments and for the University in general. The lease agreement was pursued with Gopher Welding as it was deemed to be in the very best interest of the University and the State of Minnesota. The benefits not only included cost savings from demurrage charges, but also some related savings in labor costs by not having the burdens associated with accounting for the cylinders at the department level and in the Business Affairs Office.

Mankato State University was unaware of the 10 year contract restriction at the time the decision was made to enter into this long term agreement. However, we feel the contract should be continued because Gopher Welding is the only vendor in the Mankato area that stocks many of the specialty gases that are required by our University departments. Since most

of the gases are needed quickly for various needs, i.e. research projects, special events, etc., it simply is not feasible to order the gases from vendors located in outlying communities. Consequently, most of the gases will be procured from Gopher Welding one way or the other. Thus, the University and the State should take advantage of the cost savings and the "effort free" opportunity inherent in the long term lease.

4. University departments do not consistently complete receiving reports for computer equipment.

Recommendation: University departments should complete and sign receiving reports for computer equipment and forward copies to the Business Affairs Office.

We concur with the finding and the recommendation. Normally all equipment and supply purchases must go through the Receiving Department where receiving reports are completed and forwarded to Accounts Payable. Due to the technical nature of the equipment, the MicroComputer Store delivers directly to the buying department so purchases do not go through the Receiving Department.

The following procedure has been implemented for the MicroComputer Store: At the time of delivery to the department, the department verifies the order was received and signs the receiving form and will forward the receiving form to the Business Office. Payments will not be processed without an invoice and receiving form.

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5. Several employees have inappropriate access to a computer program.

Recommendation: Mankato State University should further restrict access to the Accounts Receivable program.

We concur with the finding and the recommendation. The lead cashier will no longer have access to the Accounts Receivable program which allows for direct input of charge credits to the system. The six individuals in the Computer Services Department will also be denied access on a permanent basis. Access will be allowed on a temporary basis by the Computer Services security administrator when authorized by the Comptroller to do requested work on applicable systems.