MESABI COMMUNITY COLLEGE
FINANCIAL AUDIT
FOR THE THREE YEARS ENDED JUNE 30, 1991

OCTOBER 1992

Financial Audit Division
Office of the Legislative Auditor
State of Minnesota

92-78

Centennial Office Building, Saint Paul, MN 55155 ● 612/296-4708

MESABI COMMUNITY COLLEGE

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Public Release Date: October 16, 1992 No. 92-78

OBJECTIVES:

- EVALUATE INTERNAL CONTROL STRUCTURE: Tuition and fees, federal revenues and cash management, employee payroll expenditures, and federal financial aid expenditures.
- TEST COMPLIANCE WITH CERTAIN FINANCE-RELATED LEGAL PROVISIONS.

CONCLUSIONS:

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

- Mesabi Community College is not controlling access to the student information system.
- Business office employees perform incompatible accounting functions.
- Mesabi Community College does not maintain adequate federal financial aid records.
- Mesabi Community College does not manage cash within its federal account properly.
- Contracts for joint instructional programs need improvement.
- Internal controls over recording Perkins Loan issuances are inadequate.

We found four areas where the college had not complied with finance-related legal provisions:

- Mesabi Community College has not complied with federal cash management regulations.
- Mesabi Community College is not charging late payment fees when required.
- Mesabi Community College is not complying with matching requirements for the Perkins Loan program.
- Mesabi Community College is not completing written consortium agreements.

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

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Dr. Geraldine Evans, Chancellor
Community College System

Members of the Community College Board

Dr. Philip J. Anderson, President
Arrowhead Community College Region

Mr. Richard Kohlhase, Provost
Mesabi Community College

Audit Scope

We have conducted a financial related audit of Mesabi Community College as of and 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 Mesabi Community College, as discussed in the Introduction. We have also made a study and evaluation of the internal control structure of Mesabi Community College in effect as of December 1991.

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 Mesabi Community College are free of material misstatements.

As part of our study and evaluation of the internal control structure, we performed tests of Mesabi Community College'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.

Federal Financial Aid

We performed tests on Mesabi Community College's federal financial aid programs 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 Community College System concerning federal financial aid during the audit period. They were dated April 26,1990, May 3, 1991, and April 29, 1992, and covered fiscal years 1989, 1990, and 1991, respectively.

All three systemwide management letters indicated that Mesabi Community College's satisfactory academic progress policy was inadequate. The fiscal year 1990 management letter contained two additional findings relating to Mesabi Community College. First, the college paid financial aid to an ineligible student. In addition, the college did not adequately document cost of attendance adjustments.

Management Responsibilities

The management of Mesabi Community College 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 in the following categories:

- tuition and fee receipts,
- federal receipts and cash management,
- employee payroll expenditures, and
- federal financial aid expenditures.

For all of the internal control structure categories listed above, 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.

Conclusions

Our study and evaluation disclosed the conditions discussed in findings 1 through 5, and 7 involving the internal control structure of Mesabi Community College. 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 the reportable conditions described in findings 1 and 2 are material weaknesses.

We also noted other matters involving the internal control structure and its operation that we reported to the management of Mesabi Community College in a meeting held on March 26, 1992.

The results of our tests indicate that, except for the issues discussed in findings 4, 6, 8, and 9, with respect to the items tested, Mesabi Community College complied, in all material respects, with the provisions referred to in the audit scope paragraphs. With respect to items not tested, except for the issues discussed in findings 3 and 9, nothing came to our attention that caused us to believe that Mesabi Community College had not complied, in all material respects, with those provisions.

This report is intended for the information of the Legislative Audit Commission and management of Mesabi Community College. This restriction is not intended to limit the distribution of this report, which was released as a public document on October 16, 1992.

We would like to thank the Mesabi Community College staff for their cooperation during this audit.

James R. Nobles
Legislative Auditor

John Asmussen, CPA
Deputy Legislative Auditor

End of Fieldwork: March 13, 1992

Report Signed On: October 8, 1992

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Audit Participation

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

John Asmussen, CPA	Deputy Legislative Auditor
Jeanine Leifeld, CPA	Audit Manager
Chris Buse, CPA	Auditor-in-Charge
Ron Mavetz, CPA	Auditor
Dan Quandt, CPA	Auditor

Exit Conference

The findings and recommendations in this report were discussed with the following officials of Mesabi Community College and the Arrowhead Community College Region at an exit conference on March 26, 1992:

Richard Kohlhase	Provost
Clint Coombe	Campus Services Director
Jon Smith	Financial Aid Director
Marlene Johnson	Accounting Clerk
Bill Maki	Administrative Services Director, Arrowhead Community College Region

Introduction

Mesabi Community College is part of the Arrowhead Community College Region. The region office consolidated the management of all community colleges in northeastern Minnesota. The college provost, Richard Kohlhase, reports to the president of the Arrowhead Community College Region.

Operations of Mesabi Community College are financed mainly by student tuition and fees and state appropriations from the General Fund. The college accounts for its instructional and operating activities on the statewide accounting system. Other activities, such as bookstore transactions and federal financial aid, are accounted for through manual records and local bank accounts. These local accounts are referred to as the All College Fund and are exempt from Department of Finance budgeting and accounting requirements. Community college board policies govern the use of the All College Fund.

According to Community College System records, Mesabi Community College collected and spent the following amounts during the audit period:

	Year Ended June 30		
	1991	1990	1989
Revenues:			
Tuition and Fees	$1,050,809	$1,076,868	$ 903,047
Federal	998,341*	987,234*	1,003,125*
Other	488,367	521,173	455,323
Total Revenues	$2,537,517	$2,585,275	$2,361,495
Expenditures:			
Employee Payroll	$3,231,592	$3,020,486	$2,612,198
Pell Grants	823,396*	793,255*	753,845*
Perkins Loans	21,236	26,319	18,200
Other	1,176,856	1,183,945	1,111,983
Total Expenditures	$5,253,080	$5,024,005	$4,496,226

* Includes federal financial aid activity for the Fond du Lac Community College Center.

Sources: Manager's Financial Reports for fiscal years 1989, 1990, and 1991. Community College System revenue spreadsheets for fiscal years 1989, 1990, and 1991. Mesabi Community College's statements of representation for fiscal years 1989, 1990, and 1991.

Current Findings and Recommendations

1. Mesabi Community College is not controlling access to the student information system.

The college's student information system access controls are weak for several reasons. The college uses the system to register students for classes, record tuition payments and deferments, and post grades. The college has authorized some employees to enter transactions which are unnecessary to carry out their jobs. In addition, business office employees are not keeping their user and cashier identification codes confidential. Finally, the college is not cancelling employee's access when they resign or change positions. These control weaknesses increase the risk of unauthorized users accessing the student information system.

Giving employees access to perform unnecessary accounting transactions breaks down the college's separation of duties. Currently, business office employees who collect receipts can also change tuition and fees assessments in the student information system. This ability makes it possible for them to conceal errors and irregularities. Four other employees also have the ability to change tuition and fee assessments, even though they only need to view information to complete their job responsibilities.

Controls are also weak because business office employees are not keeping their user and cashier identification codes confidential. Employees share identification codes to avoid logging on and off the system. They also permit student workers to use their access codes. The student information system allows users to access parts of the system through unique user and cashier identification codes. Sharing codes diminishes the accountability for transactions and the natural separation of duties provided by unique access codes.

Finally, the college is not promptly changing system access when employees resign or change positions. For example, in November 1990, a staff member moved from the registrar's office to the business office. However, the college did not cancel the employee's ability to perform registration transactions. Another former employee who left in June 1990 still has access to the student information system. Promptly changing identification codes decreases the risk of unauthorized users accessing the system.

Recommendation

- *Mesabi Community College should strengthen access controls over the student information system by:*
  - *limiting employee's access to only those functions necessary to perform their job responsibilities;*
  - *prohibiting employees from sharing access codes; and*
  - *changing employee's access codes when they resign or change positions.*

2. PRIOR FINDING NOT RESOLVED: Business office employees perform incompatible accounting functions.

Two employees in the college business office do not have distinct job responsibilities. Instead, they perform all receipt processing duties interchangeably. These employees collect receipts, operate the cash register, and post tuition payments to the student information system. At the end of each day they clear the cash register, count the cash, and prepare the daily cash report. One of these workers also reconciles the bank deposit to a computer report listing payments posted to student's accounts. No one else reviews the cash reports or reconciliations. Errors or irregularities could occur and remain undetected because these employees perform incompatible accounting duties and no independent person reviews their work.

Controls over collecting unpaid tuition and fees are also weak because of an inadequate separation of duties. One employee is responsible for pursuing delinquent student accounts. This same employee also collects receipts and operates the cash register. Internal controls are weak whenever one employee performs incompatible duties without independent oversight. To improve controls, a person independent of the daily receipt processing should review all balance due reports.

Recommendation

- *A person independent of receipt processing should prepare or review the daily cash reports, cash reconciliations, and balance due reports.*

3. PRIOR FINDING NOT RESOLVED: Mesabi Community College does not maintain adequate federal financial aid records.

Mesabi Community College does not have adequate accounting records to control its financial aid programs. The only accounting record the college prepares is a check register showing the combined cash balance for all federal programs. Employees are not posting or reconciling this check register promptly. At the time of our audit, the college was two months behind posting transactions to the check register. College employees had not reconciled the check register cash balance to the bank statement for over seven months. These recordkeeping weaknesses expose the college's federal programs to unnecessarily high financial risks.

The college does not prepare ledgers identifying federal awards and remaining balances in those awards. The college also has no records showing cash balances within individual programs. Without such records, the college could award aid that exceeds available funding or reject eligible students when funding is available. For example, the college Perkins Loan cash balance exceeded $35,000 throughout fiscal year 1989. However, the financial aid office only awarded loans totalling $16,450. The financial aid director told us that he did not know how much cash was in the college's Perkins Fund. On six occasions during fiscal year 1989, the college violated federal regulations by using cash from the Perkins Fund to pay expenditures of other programs. Records identifying cash balances within individual programs could prevent this from happening in the future.

Recommendations

- *Mesabi Community College should prepare control and subsidiary ledgers for its federal programs which identify all transactions.*
- *Mesabi Community College should post and reconcile its accounting records to the bank statement in a timely manner.*

4. Mesabi Community College does not manage cash within its federal account properly.

Mesabi Community College's procedures for estimating cash needs for its federal programs are inadequate. During some periods, the college had more cash in its federal account than was necessary. At other times, the college ran out of cash and had to borrow money and incur overdrafts. The United States Department of Education requires institutions to limit cash requests to amounts necessary to meet immediate program needs. The Department of Education considers cash balances exceeding three days needs to be excessive.

The college does not have precise procedures to estimate cash needs for its Pell Grant program. At the beginning of each quarter, the college requests Pell funds from the United States Treasury. The college does not consider its cash on hand or anticipated disbursements when making these requests. Instead, it bases request amounts on grants paid during prior quarters. This imprecise estimation technique is resulting in cash excesses and shortages. The college requested excessive cash in all three advances we tested. In one case, the college requested $235,000 even though it already had $72,636 in its federal account. It took the college 55 days to use this $307,636. The college also incurred overdrafts during seven months we tested. At one point, the college's federal account was overdrawn by more than $34,000. On nine occasions totalling $395,000, the college had to borrow money from its All College Fund and other institutions. The college must develop cash estimation procedures to avoid future cash shortages and comply with federal cash limitations.

Federal cash management requirements are changing. On March 23, 1992, the U.S. Department of Treasury proposed regulations to implement the federal Cash Management Act of 1990. These proposed rules provide states with several options to manage transfers of funds from the federal government for federal programs. Some options involve establishing check clearance patterns and/or incurring interest on federal fund balances. The Minnesota Department of Finance is currently working with state agencies to determine the specific funding techniques agencies will use and to negotiate a state/federal cash management agreement.

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Recommendation

- *Mesabi Community College should develop cash management procedures to make sure that cash balances in the college's federal account are adequate, but not excessive.*

5. Contracts for joint instructional programs need improvement.

Mesabi Community College is not enforcing the terms in its joint instructional agreements. The college entered into agreements with two area high schools for its Program for Advanced Opportunity. Under these agreements, high school students receive college credit for classes taken at the high schools. High school instructors teach these classes under the supervision of college faculty members. The Community College Board has authorized this type of program through board policy III.01.04. Mesabi Community College did not comply with the terms for one of the joint agreements. In that agreement, the college waived all tuition and fee charges. Despite this provision, the high school paid tuition and fees totalling $13,760. The agreement also stated that all instructional costs will be borne by the high school. However, the college returned the $13,760 to the high school to cover instructional costs.

Recommendation

- *Mesabi Community College should adhere to negotiated terms in its joint instructional agreements.*

6. Mesabi Community College is not charging late payment fees when required.

The college is not charging late payment fees to students who do not pay their tuition and fees promptly. Community College Board policies require colleges to charge registered students late fees if they do not pay their tuition by the first day of classes. Colleges also must charge late fees to students who register after the first day and do not pay on that day. Students can request a deferment of their tuition and fees to avoid paying these late fees. Thirty percent of the students we tested did not pay their tuition and fees by the first day of classes. The college did not charge these students late fees even though no one requested deferments.

Recommendation

- *Mesabi Community College should charge late payment fees when required.*

Mesabi Community College

7. PRIOR FINDING NOT RESOLVED: Internal controls over recording Perkins Loan issuances are inadequate.

Mesabi Community College's controls over Perkins Loans are weak in two respects. First, the college does not enter Perkins Loan information in the systemwide loan management system timely. Also, the college does not verify the accuracy of the information entered. Timely data entry reduces the risk of posting inaccurate information to the system. Comparing the information entered to the college's financial aid records helps detect loans missing from the system. The Community College System Office uses the information in the loan management system to bill borrowers and collect their repayments. Loans not posted to the loan management system might never be repaid.

Recommendations

- *Mesabi Community College should post information to the loan management system promptly.*
- *Mesabi Community College should reconcile information entered in the system to its financial aid records.*

8. PRIOR FINDING NOT RESOLVED: The college is not complying with matching requirements for the Perkins Loan program.

Mesabi Community College is not making its Perkins Loan program institutional match timely or accurately. Federal regulations require schools that receive federal funds for the Perkins Loan program to contribute a one ninth matching share. Regulations further require schools to deposit this institutional match at the same time or before they deposit the federal contribution. The college did not deposit its institutional match promptly in fiscal years 1989, 1990, or 1991. The college deposited its fiscal year 1991 match seven months after its federal capital contribution. This fiscal year 1991 institutional match was $268 less than the amount required by federal regulations.

Recommendations

- *Mesabi Community College should make its institutional match at the same time or before it deposits the federal capital contribution.*
- *Mesabi Community College should deposit $268 in its Perkins Loan Fund to remedy the fiscal year 1991 underpayment.*

Mesabi Community College

9. Mesabi Community College is not completing written consortium agreements.

Mesabi Community College is not preparing written consortium agreements for its federal financial aid recipients that are also attending other institutions. Federal regulations require colleges to complete consortium agreements with other institutions before paying combined enrollment status financial aid awards. Consortium agreements specify which institution is responsible for disbursing aid, thus preventing duplicate payments. Consortium agreements also identify the school that is responsible for monitoring student eligibility. The college financial aid office told us that they verbally consult with other schools when paying combined enrollment status awards.

Recommendation

- *Mesabi Community College should prepare written consortium agreements, when necessary.*

MCC Mesabi Community College
To Be The Best!

October 2, 1992

Ms. Jeanine Leifeld, CPA
Audit Manager
Office of the Legislative Auditor
Centennial Building
St. Paul, Minnesota 55155

Dear Ms. Leifeld:

Thank you for the audit report draft that was received at Mesabi Community College on September 21, 1992. I have conferred with the appropriate fiscal management and financial aid personnel, and our responses to your findings and recommendations follow:

Finding Number One: Mesabi Community College is not controlling access to the student information system.

College Response: The Community College System is working on a new program for user identification/access codes. When that program is in place, it will provide additional safeguards. Access codes of former employees and reassigned employees have been cancelled. The Director of College Services will review and update the users list on a monthly basis. Business office and records office personnel only have functions appropriate to their position descriptions. Employees have been directed not to share access codes.

Finding Number Two: Business office employees perform incompatible accounting functions.

College Response: The separation of duties is being achieved by having one business office employee operate the cash register, and the other business office employee be responsible for cash counting and reporting. Also, the Director of College Services is now reviewing and initialling daily cash reports, cash reconciliations and balance due reports.

Finding Number Three: Mesabi Community College does not maintain adequate federal financial aid records.

College Response: As of September, 1992, the Senior Account Clerk is using the control and subsidiary ledgers for the federal programs as required by The Blue Book. Posting and reconciliations are being done on a timely basis.

Finding Number Four: Mesabi Community College does not manage cash within its federal account properly.

College Response: The appropriate cash management procedures for federal funds have been implemented as directed by the Director of College Services. Funds are being drawn on actual expenditures.

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Finding Number Five: Contracts for joint instructional programs need improvement.

College Response: The Minnesota Community College System has adopted new policies and procedures to address the practice of offering college courses at cooperating high schools. Mesabi Community College is in strict compliance with the agreement and billing procedures for such cooperative relationships. The Dean of the College is responsible for compliance on agreement procedures, and the Director of College Services is responsible for processing the subsequent billing instruments.

Finding Number Six: Mesabi Community College is not charging late payment fees when required.

College Response: The Arrowhead Community College Region is in the process of seeking a change of policy on late fees.

Finding Number Seven: Internal controls on recording Perkins Loan issuances are inadequate.

College Response: Perkins Loan information will be entered in the system-wide loan management system on a timely basis. The Loan Collection Department will mail the Mesabi financial aid office a quarterly report indicating:

1. Perkins loan recipients names--enrolled students
2. Loan amount per student
3. Estimated graduation date

The information from this report will be reconciled against the student files and the check register from the Business Office. Student files and the Loan Management System will be updated as necessary. These procedures will insure prompt entry of students at the proper amounts.

Finding Number Eight: Mesabi Community College is not complying with matching requirements for the Perkins Loan program.

College Response: The $268 FY 1991 institutional match was deposited to the Perkins Loan Fund in FY 1992. The institutional matches will be made at the same time when the federal contribution is deposited.

Finding Number Nine: Mesabi Community College is not completing written consortium agreements.

College Response: Students are allowed to attend Mesabi Community College and Hibbing Community College concurrently--with financial aid being disbursed by one institution or the other. The Mesabi and Hibbing financial aid staff members communicate by telephone in such instances. A written information sheet is prepared for students and staff at both institutions. This information sheet identifies the methods used to:

1. Determine which institution is disbursing financial aid to the student.
2. Identify the method of tracking such students.

The Director of Financial Aid at Mesabi Community College will prepare a formal consortium agreement with Hibbing Community College during this fall quarter.

This concludes our response to the audit report for the three years ended June 30, 1991. As always, thank you for the positive comments and the candid recommendations shared during the exit conference of March 26, 1992.

Sincerely yours,

Richard N Kohlhase

Richard N. Kohlhase, Provost
Mesabi Community College

vs

cc: Dr. Geraldine Evans, Chancellor
Minnesota Community Colleges
Dr. Cynthia Heelan, President
Arrowhead Community College Region