
**Arrowhead Community College Region and
Northeast Service Unit**

Financial Audit

For the Period July 1, 1995, through June 30, 1998

September 1999

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**Financial Audit Division
Office of the Legislative Auditor
State of Minnesota**

99-50

SUMMARY

State of Minnesota

Office of the Legislative Auditor

1st Floor Centennial Building

658 Cedar Street • St. Paul, MN 55155

(651)296-1727 • FAX (651)296-4712

TDD Relay: 1-800-627-3529

email: auditor@state.mn.us

URL: <http://www.auditor.leg.state.mn.us>

Arrowhead Community College Region and Northeast Service Unit

Financial Audit

For the Period July 1, 1995, through June 30, 1998

Public Release Date: September 16, 1999

No. 99-50

Agency Background

The Minnesota State Community College Board established the Arrowhead Community College Region in 1981. Arrowhead received state appropriations and provided administrative and other support services to the colleges of northeast Minnesota through 1997. The Northeast Service Unit (NESU) was created in fiscal year 1998 to provide support services to six colleges. The funding structure changed in 1998 to a fee for service operation. The colleges were charged for the costs of support services provided by NESU. The presidents of the participating colleges established a council to provide administrative oversight of NESU activities. The NESU director, Ms. Sally Thompson, reports to the council of presidents. NESU provided the following services in 1998: institutional research, library services, payroll, accounts payable, purchasing, and federal grant management. In fiscal year 1999, the council of presidents decided to eliminate certain services including purchasing, accounts payable, and payroll functions. The colleges will either perform these services themselves or contract with other colleges.

Audit Scope and Conclusions

Our audit scope included the Arrowhead Community College Region employee payroll and other administrative expenditures for the years ended June 30, 1996 and 1997. We also reviewed the Northeast Service Unit employee payroll, other administrative expenditures, and the charges to the participating colleges and related fees collected for the year ended June 30, 1998.

We concluded that the Northeast Service Unit properly charged the participating colleges and collected the related revenues in fiscal year 1998. However, NESU did not properly record loan receivable balances on MnSCU accounting. We found that the Arrowhead Community College Region and NESU properly recorded payroll and other administrative expenditures on the accounting system and complied with laws and regulations for the items tested.

In its written response, the Northeast Service Unit agreed with the finding and, effective immediately, all loan transactions will be accounted for within the MnSCU accounting system using the appropriate receivable object codes.



STATE OF MINNESOTA
OFFICE OF THE LEGISLATIVE AUDITOR
JAMES R. NOBLES, LEGISLATIVE AUDITOR

Representative Dan McElroy, Chair
Legislative Audit Commission

Members of the Legislative Audit Commission

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Minnesota State Colleges and Universities

Members of the Minnesota State Colleges and Universities Board of Trustees

Dr. Kathy Nelson, Chair
Council of Presidents

Ms. Sally Thompson, Director
Northeast Service Unit

We have audited the Arrowhead Community College Region and the Northeast Service Unit for the period July 1, 1995, through June 30, 1998, as further explained in Chapter 1. Our audit scope included service revenue, employee payroll, and other administrative expenditures. We discuss these areas more fully in the individual chapters of this report.

We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards* as issued by the Comptroller General of the United States. These standards require that we obtain an understanding of management controls relevant to the audit. The standards also require that we design the audit to provide reasonable assurance that the Arrowhead Community College Region and Northeast Service Unit complied with provisions of laws, regulations, contracts, and grants that are significant to the audit. Management is responsible for establishing and maintaining the internal control structure and for compliance with applicable laws, regulations, contracts, and grants.

This report is intended for the information of the Legislative Audit Commission and the management of the Northeast Service Unit. This restriction is not intended to limit the distribution of this report, which was released as a public document on September 16, 1999.

James R. Nobles
Legislative Auditor

Claudia J. Gudvangen, CPA
Deputy Legislative Auditor

End of Fieldwork: July 2, 1999

Report Signed On: September 13, 1999

Arrowhead Community College Region and Northeast Service Unit

Table of Contents

	Page
Chapter 1. Introduction	1
Chapter 2. Revenues	3
Chapter 3. Payroll and Other Administrative Expenditures	5
Northeast Service Unit's Response	7

Audit Participation

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

Claudia Gudvangen, CPA	Deputy Legislative Auditor
Renee Redmer, LPA	Audit Manager
Connie Stein	Auditor-in-Charge

Exit Conference

The following staff from Northeast Service Unit and the MnSCU system office participated in the exit conference held on August 24, 1999:

MnSCU System Office:

Laura King	Vice Chancellor, Chief Financial Officer
Rosalie Greeman	Associate Vice Chancellor, Financial Reporting
John Asmussen	Executive Director of Internal Auditing
Kim McLaughlin	Regional Audit Coordinator, Northeast Region
Dr. Kathy Nelson	President, Lake Superior College
Sally Thompson	Director, Northeast Service Unit

Chapter 1. Introduction

The Minnesota State Community College Board established the Arrowhead Community College Region in 1981. The region office consolidated certain management functions for community colleges in northeastern Minnesota. The office provided the following services: accounts payable, human resources, purchasing, centralized maintenance supervision, and grant management. Minnesota State Colleges and Universities (MnSCU) began operations on July 1, 1995, when state universities, community colleges, and technical colleges throughout the state merged under one governance structure. MnSCU consolidated many colleges in the northeast and, as a result, the Board of Trustees recommended that executive positions in the Arrowhead office be discontinued in 1998. However, the board recommended that MnSCU continue to provide support services to the northeast colleges.

The Northeast Service Unit (NESU) was created in 1998, and the support services staff transferred to NESU from the Arrowhead regional office. The current director is Ms. Sally Thompson. The director reports to the council of presidents, which consists of the presidents from the following participating colleges: Hibbing Community College, Itasca Community College, Laurentian Community and Technical College, Rainy River Community College, Fond du Lac Tribal and Community College, and Lake Superior College. NESU provided the following services in fiscal year 1998: institutional research, library services, payroll, accounts payable, purchasing, and federal grant management. In fiscal year 1999, the council of presidents decided to eliminate the purchasing, accounts payable, and payroll functions as a NESU provided service. The colleges will either perform these services themselves or contract with other colleges.

Arrowhead Community College Region and Northeast Service Unit

Table 1-1 provides a summary of NESU's sources and uses of funds in fiscal year 1998.

**Table 1-1
Northeast Service Unit
Sources and Uses of Funds
Fiscal Year 1998**

	<u>General Fund</u>	<u>Special Revenue Fund</u>
Beginning Balance (2)	\$ 478,322	\$ 1,818
Sources:		
Service Income	\$ 351,048	\$ 0
Special Projects	60,000	
NEAT Grant (3)	106,795	0
Federal Grants	0	282,517
Transfers	83,184	0
Other Income	19,081	0
Subtotal	<u>\$ 835,108</u>	<u>\$282,517</u>
Total Resources	<u>\$1,098,430</u>	<u>\$284,335</u>
Uses:		
Payroll	\$ 475,875	\$135,263
Memberships	2,385	0
Purchased Services	63,517	1,825
Supplies/Equipment	20,853	17,797
Travel	10,642	6,572
Other	14,497	110,919
Total Expenditures	<u>\$ 587,770</u>	<u>\$272,375</u>
Ending Fund Balance	<u>\$ 510,660</u>	<u>\$ 11,960</u>

Note (1): Table 1-1 is presented on the budgetary basis of accounting. The basis does not include long-term assets and liabilities. The compensated absence liability is \$58,921 at June 30, 1998.

Note (2): The General Fund beginning and ending fund balances include monies designated as available for loans to participating colleges. The operating and maintenance loan fund and the repair and betterment loan fund were established at \$250,000 and \$200,000, respectively. At June 30, 1998, outstanding loans totaled \$60,000.

Note (3): NEAT is the NorthEast Alliance for Telecommunications.

Note (4): In addition to the financial activity shown above, the Arrowhead Community College Region transferred approximately \$214,000, on an equal basis, to the five colleges that were originally a part of the region.

Source: MnSCU accounting system.

Chapter 2. Revenues

Chapter Conclusions

The Northeast Service Unit designed and implemented internal controls to provide reasonable assurance that service income revenue was collected, accurately reported in the accounting records, and in compliance with certain material finance-related legal provisions. However, NESU did not properly record loans receivable in the accounting system.

During fiscal years 1996 and 1997, the Arrowhead regional office received state appropriation allocations of \$1,146,000 and \$1,502,000, respectively. In fiscal year 1998, NESU began charging the participating colleges for the support services provided. The director developed an operating budget and allocated costs to colleges based on the services used and estimated student enrollment data. NESU billed the colleges 75 percent of budgeted costs at the beginning of the fiscal year. After the final enrollment data was known, NESU calculated the final bill. Table 2-1 shows the fees charged and received from the participating colleges.

Table 2-1
Fees Received from Colleges
Fiscal Year 1998

<u>Colleges</u>	<u>Fees</u>
Laurentian	\$111,378
Hibbing	105,952
Itasca	58,463
Fond du Lac	27,500
Rainy River	27,072
Lake Superior	<u>20,683</u>
Total	<u>\$351,048</u>

Source: MnSCU accounting system.

Audit Objectives and Methodology

We focused on the following objectives during our review of revenue:

- Did NESU design and implement internal controls to provide reasonable assurance that service income revenues were collected, accurately reported in the accounting records, and in compliance with certain material finance-related legal provisions?
- Did NESU properly charge the colleges for services rendered?

Arrowhead Community College Region and Northeast Service Unit

To address these objectives, we interviewed NESU staff to gain an understanding of the receipt process and the basis used to establish service fees. We also performed analytical procedures to determine and evaluate changes in revenues during the audit period.

Conclusions

The Northeast Service Unit designed and implemented internal controls to provide reasonable assurance that service income revenue was collected, accurately reported in the accounting records, and in compliance with certain material finance-related legal provisions. However, NESU did not properly record loans receivable in the accounting system.

1. NESU did not properly report loans receivable on MnSCU accounting.

NESU did not properly record loan transactions on MnSCU accounting and did not report the receivables for financial reporting purposes. The council of presidents established two loan funds, an operating and maintenance loan fund and a repair and betterment loan fund. Participating colleges can borrow from both loan funds. The operating and maintenance loan fund is to help address budget issues arising due to low enrollment, early retirements, sabbatical replacements, and other unforeseen circumstances. The authorized level for this loan fund is \$250,000. The repair and betterment loan fund is to be used for repair and betterment of capital facilities. The authorized level for this loan fund is \$200,000.

Since July 1, 1995, Arrowhead and NESU have authorized \$270,000 in loans to participating colleges. Outstanding loans at June 30, 1999, totaled \$250,000. NESU manually tracks the outstanding balances; however, it did not record the loan receivable balance on MnSCU accounting. Instead, loan payments were shown as an expenditure and reduction of fund balance, and repayments were recorded as revenue. The improper reporting of loan transactions on the MnSCU accounting system understates the Northeast Service Unit's General Fund balance. MnSCU accounting is used for financial statement preparation and budget decisions.

Recommendation

- *NESU should record loans receivable on the MnSCU accounting system to ensure the completeness of its reported financial activity.*

Chapter 3. Payroll and Other Administrative Expenditures

Chapter Conclusions

Arrowhead Community College Region and Northeast Service Unit designed and implemented internal controls to provide reasonable assurance that payroll and administrative expenditures were accurately reported in the accounting records and in compliance with applicable legal provisions and management's authorization. For the items tested, Arrowhead and NESU complied, in all material respects, with the significant finance-related legal provisions concerning payroll and other administrative expenditures.

NESU expended approximately \$1.4 million during fiscal year 1998 for administrative expenditures. Payroll was the largest administrative expenditure category totaling approximately \$611,000. Other administrative expenditure categories include memberships, purchased services, supplies, and equipment.

Northeast Service Unit had approximately ten employees during fiscal year 1998. NESU employees belong to various compensation plans, including the American Federation of State, County, and Municipal Employees (AFSCME), the Minnesota Association of Professional Employees (MAPE), the Excluded Administrators' Plan, and the Commissioner's Plan.

During fiscal year 1996, the colleges used the state's personnel/payroll system (PPS) and the State Colleges and Universities Personnel/Payroll System (SCUPPS) to process payroll information. SCUPPS stored pay rate information and bargaining agreement history. PPS contained pay rate and deduction information to determine the payments to employees. In October 1996, the college began processing its payroll information in the state's SEMA4 payroll system while continuing to use SCUPPS for personnel information. The human resources section enters all new employee data and makes changes to employees' records directly in SCUPPS.

Audit Objectives and Methodology

We focused our review of payroll and other administrative expenditures on the following objectives:

- Did NESU design and implement internal controls to provide reasonable assurance that payroll and other administrative expenditures were accurately reported in the accounting records and in compliance with applicable legal provisions and management's authorization?
- For the items tested, did NESU comply, in all material respects, with significant finance-related legal provisions concerning payroll and other administrative expenditures?

Arrowhead Community College Region and Northeast Service Unit

We interviewed the NESU staff to gain an understanding of the payroll and other administrative expenditure procedures. We performed analytical procedures for administrative expenditures to evaluate any trends in specific account classes throughout the audit period. We also reviewed a sample of expenditure transactions to determine if the items were properly authorized, processed, and recorded and in compliance with material finance-related legal provisions.

Conclusion

Arrowhead Community College Region and Northeast Service Unit designed and implemented internal controls to provide reasonable assurance that payroll and administrative expenditures were accurately reported in the accounting records and in compliance with applicable legal provisions and management's authorization. For the items tested, Arrowhead and NESU complied, in all material respects, with the significant finance-related legal provisions concerning payroll and other administrative expenditures

NORTHEAST SERVICE UNIT

1001 Chestnut St. W.
Virginia, MN 55792
Phone (218) 749-9620
Fax (218) 749-9619

August 30, 1999

Mr. James R. Nobles
Legislative Auditor
100 Centennial Office Building
658 Cedar Street
St. Paul, MN 55155

Dear Mr. Nobles:

Thank you for the opportunity to respond to the recently completed audit report for the Northeast Service Unit for the period July 1, 1995 through June 30, 1998. During the audit period there were many changes taking place among the colleges in northeast Minnesota, including our evolution from a regional governance/service office to a regional service office. We were pleased to have had a good audit, with only one important finding. Following is our response to the audit finding:

1. NESU did not properly report loans receivable on MnSCU accounting.

We concur with the auditor's finding and effective immediately all loan transactions will be accounted for within the MnSCU accounting system using the appropriate receivable object codes.

Person responsible: Sally Thompson
NESU Director

Implementation Date: Immediately

Please feel free to contact me if you have any questions regarding the response.

Sincerely,

Sally Thompson, Director
Northeast Service Unit