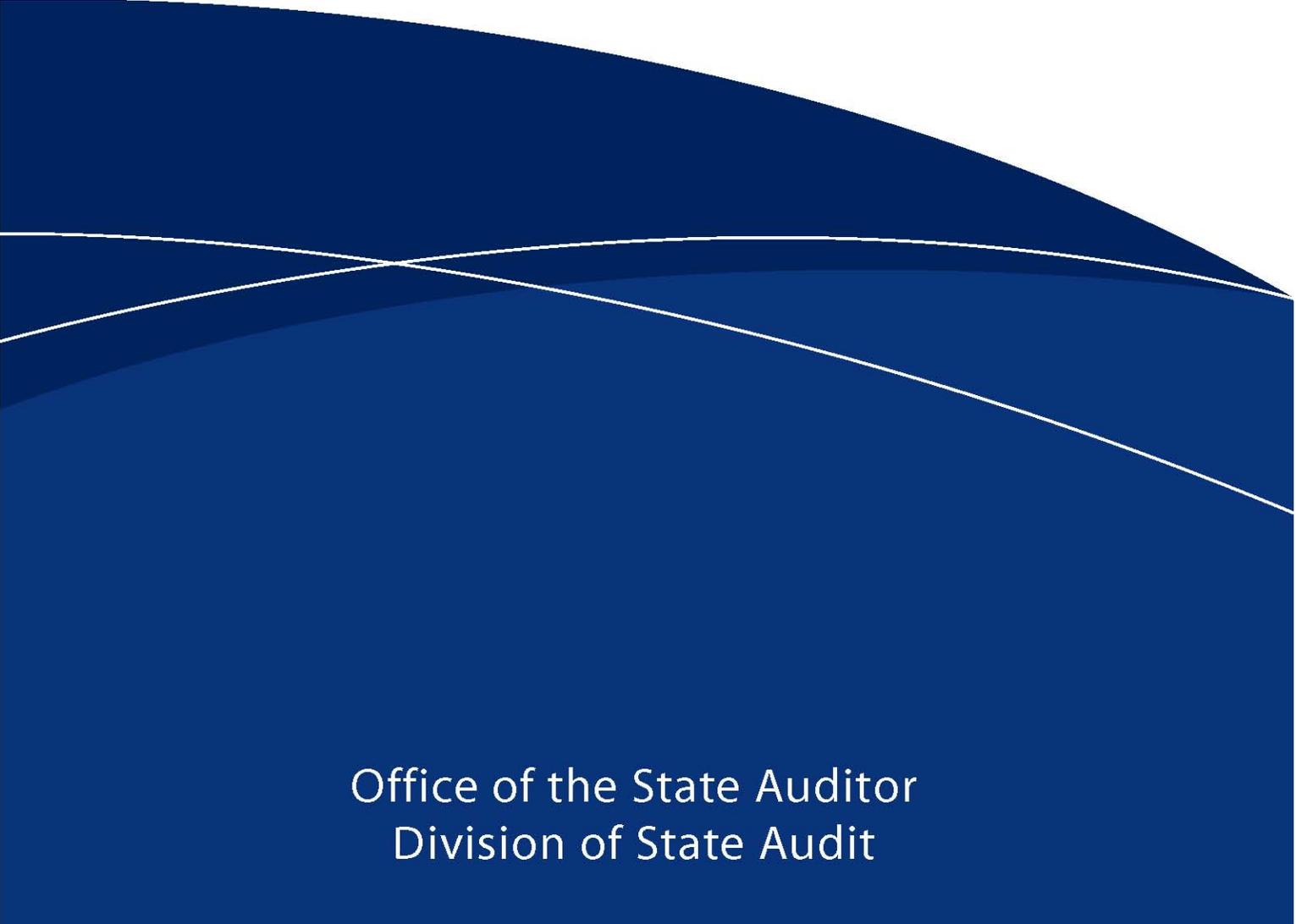


# NORTH DAKOTA UNIVERSITY SYSTEM

## **Governance Communication Including the Report on Internal Control, Compliance, and Other Matters**

For the Year Ended  
June 30, 2015

ROBERT R. PETERSON  
STATE AUDITOR



Office of the State Auditor  
Division of State Audit

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STATE OF NORTH DAKOTA  
**OFFICE OF THE STATE AUDITOR**  
FARGO BRANCH OFFICE  
1655 43<sup>rd</sup> STREET SOUTH, SUITE 203  
FARGO, NORTH DAKOTA 58103

## ***Transmittal Letter***

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December 2, 2015

Honorable Jack Dalrymple, Governor  
Members of the North Dakota Legislative Assembly  
State Board of Higher Education

I am pleased to submit our report on internal control and compliance for the North Dakota University System. This report relates to the audit of the North Dakota University System's financial statements for the year ended June 30, 2015. This report on internal control and compliance has been completed in accordance with *Government Auditing Standards*, as issued by the Comptroller General of the United States.

Also enclosed you will find our audit findings, governance communication, passed audit adjustments, and management letter. These communications are required by generally accepted auditing standards.

The audit manager for this audit was Robyn Hoffmann, CPA. Inquiries or comments relating to this audit may be directed to Ms. Hoffmann by calling (701) 239-7291. I wish to express our appreciation to the North Dakota University System for the courtesy, cooperation, and assistance they provided to us during the audit.

Respectfully submitted,

A handwritten signature in cursive script that reads "Bob Peterson".

Robert R. Peterson  
State Auditor

## ***Executive Summary***

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### **RESPONSES TO THE LAFRC AUDIT QUESTIONS**

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state institutions:

**1. What type of opinion was issued on the financial statements?**

Unmodified on Business-Type Activities and Qualified on the Aggregate Discretely Presented Component Units.

**2. Was there compliance with statutes, laws, rules, and regulations under which the agency was created and is functioning?**

No. For additional commentary see the schedule of Findings, Recommendations, and University System Responses, Finding 15-1 on page 7.

**3. Was internal control adequate and functioning effectively?**

No. We noted the following five internal control matters which need to be addressed and corrected:

- SBHE & NDUS – Legislative Approval for Local Fund Expenses (Finding 15-1)
- SBHE & NDUS – Fraud Risk (Prior Recommendations Not Implemented #1)
- SBHE & NDUS – Governance and Internal Controls of Foundation Audits (Prior Recommendations Not Implemented #2)
- WSC – Reconciling (Prior Recommendations Not Implemented #3)
- MISU –Background Checks (Prior Recommendations Not Implemented #4)

For additional commentary see the Findings, Recommendations, and University System Responses on page 7 and Prior Recommendations Not Implemented starting on page 8.

**4. Were there any indications of lack of efficiency in financial operations and management of the agency?**

No.

**5. Has action been taken on findings and recommendations included in the prior audit?**

No. Four (three pre-fiscal year 2014 and one fiscal year 2014) prior recommendations were not implemented as follows:

- NDUS management has not conducted a comprehensive fraud and control risk assessment by each institution [2008, 2009, 2010, 2011, 2012, 2013 and 2014 audits]
- NDUS management had not obtained GAAP-compliant financial statements or an annual GAAP audit for all component units in compliance with SBHE Policy 340.2. [2013 and 2014 audits]
- WSC did not perform monthly bank reconciliations and understated their general ledger for cash accounts. [2011, 2012, 2013, and 2014 audits]
- MISU did not complete employee criminal history background checks for four out of seven employees before their start date. [2014 audit]

**6. Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.**

Yes. We made the following 6 informal recommendations to which management responded and agreed to implement. For additional commentary and management responses, see the Management Letter starting on page 17.

1. VCSU – Inadequate Monthly Investment Reconciliation
2. MISU, VCSU, & WSC – Improper Recording of Institutional Endowments/Investments
3. MISU – Commingling of Cash between Institution and Foundation
4. NDSU & UND – Expenses Not Recorded in Proper Fiscal Year
5. BSC – Pledge Revenues Note
6. BSC, VCSU, & WSC – PeopleSoft Asset Management System Utilization

## **LAFRC AUDIT COMMUNICATIONS**

**1. Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.**

The NDUS changed accounting policies related to pensions by adopting Statement No. 68, *Accounting and Financial Reporting for Pensions*. There were no management conflicts of interest or significant unusual transactions noted. The NDUS's commitments and contingent liabilities are reported on pages 56 and 72 of the fiscal year 2015 NDUS Annual Financial Report.

**2. Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.**

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements:

- Fair value of investments (Note 2)
- Useful lives of capital assets (Note 5)
- Scholarship allowance: \$64,323,230
- Allowance for uncollectible receivables:
  - Accounts: \$6,061,785
  - Loans and notes: \$8,020,966

We evaluated the key factors and assumptions used to develop these estimates and determined that they are reasonable in relation to the financial statements taken as a whole.

**3. Identify any significant audit adjustments.**

The Passed Audit Adjustments schedule on page 16 summarizes uncorrected misstatements of the financial statements. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

- 4. Identify any disagreements with management, whether or not resolved to the auditor's satisfaction relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.**

We are pleased to report that no significant disagreements arose during the course of our audit.

- 5. Identify any serious difficulties encountered in performing the audit.**

None.

- 6. Identify any major issues discussed with management prior to retention.**

This is not applicable for audits conducted by the Office of the State Auditor.

- 7. Identify any management consultations with other accountants about auditing and accounting matters.**

None.

- 8. Identify any high-risk information technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six audit report questions to be addressed by the auditors are directly related to the operations of an information technology system.**

ConnectND Finance, Human Resource Management System (HRMS), and Campus Solutions are the most high-risk information technology systems critical to the North Dakota University System. None of the exceptions noted were directly related to the operation of an information technology system.

***Report on Internal Control Over Financial Reporting and on Compliance  
and Other Matters Based on an Audit of Financial Statements Performed  
in Accordance with Government Auditing Standards***

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**Independent Auditor's Report**

Honorable Jack Dalrymple, Governor

Members of the Legislative Assembly

State Board of Higher Education

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the business-type activities and the aggregate discretely presented component units of the North Dakota University System as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the North Dakota University System's basic financial statements, and have issued our report thereon dated December 2, 2015. Our report was qualified because management did not include the financial data for one of the reporting entity's discretely presented component units. Our report includes a reference to other auditors who audited the financial statements of the discretely presented component units, as described in our report on the North Dakota University System's financial statements. The financial statements of the discretely presented component units were not audited in accordance with *Government Auditing Standards*.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the North Dakota University System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the North Dakota University's internal control. Accordingly, we do not express an opinion on the effectiveness of the North Dakota University System's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of *Findings, Recommendations, and University System Responses* and schedule of *Prior Recommendations Not Implemented and University System Responses*, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable

possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies numbered 1 and 2 in the accompanying schedule of *Prior Findings Not Implemented and University System Responses* to be material weaknesses.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies numbered Finding 15-1 in the accompanying schedule of *Findings, Recommendations, and University System Responses* and 3 and 4 in the accompanying schedule of *Prior Findings Not Implemented and University System Responses* to be significant deficiencies.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the North Dakota University System's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which is described in the accompanying schedule of *Findings, Recommendations, and University System Responses* as Finding 15-1.

### **North Dakota University System's Response to Findings**

The North Dakota University System's response to the findings identified in our audit are described in the accompanying schedule of *Findings, Recommendations, and University System Responses* and schedule of *Prior Findings Not Implemented and University System Responses*. The North Dakota University System's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

### **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Robert R. Peterson  
State Auditor

Fargo, North Dakota

December 2, 2015

## **Findings, Recommendations, and University System Responses**

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### **SBHE & NDUS – LEGISLATIVE APPROVAL FOR LOCAL FUND EXPENSES (Finding 15-1)**

#### **Condition:**

We noted several institutions with construction/renovation projects that did not obtain legislative or budget section approval. All of the projects were funded with transfers from other funds and under current accounting practices it is often difficult to determine the funding source.

NDCC 54-27-12 states that the SBHE may not construct or renovate any public building or structure in excess of any appropriation made by the legislative assembly for such purpose. NDCC 15-55-10 states that no building or other campus improvement may be constructed at a cost exceeding the amount fixed by the legislature.

#### **Effect:**

There is potential noncompliance with state law or legislative intent.

Significant capital projects which will require future operating and maintenance costs funded in whole or part by public funds are not being subjected to legislative approval.

#### **Cause:**

NDUS does not believe legislative approval is required for building construction, improvements, or maintenance funded with local funds.

#### **Criteria:**

NDCC 54-27-12 and NDCC 15-55-10.

Internal controls require an audit trail that would provide adequate support for sources of funding for construction/renovation projects.

#### **Recommendation:**

We recommend the SBHE and NDUS improve capital projects, improvements, and renovations funded by local funds by:

- Complying with NDCC Section 54-27-12 and 15-55-10 and obtain appropriate legislative approval for construction or renovation of any public building;
- Ensuring proper controls exist to specifically identify the actual sources of moneys used in local funded projects; and
- Taking appropriate action to modify or clarify state law with the Legislative Assembly to make it clear when approval is or is not required for local funded projects.

#### **University System Response/Planned Corrective Actions:**

*Partially disagree. The NDUS will review accounting procedures to determine what changes could be made to further specify funding sources by June 30, 2016. However, after consulting with legal counsel, the NDUS believes it is in compliance with all statutes related to local-funded capital construction projects, improvements or maintenance. Additionally, the 64th Legislative Assembly considered legislation that would have required legislative approval for all capital improvement projects over \$385,000. That legislation was not passed.*

#### **Auditor Concluding Remarks:**

*We stand behind our recommendation that the SBHE and NDUS take appropriate action to modify or clarify state law to make it clear when legislative approval is required for capital projects, improvements, and renovations which utilize local fund moneys.*

## **Prior Recommendations Not Implemented and University System Responses**

Prior recommendations not implemented and client responses, item #5 of the Special Comments Requested by the Legislative Audit and Fiscal Review Committee.

### **1. SBHE & NDUS – FRAUD RISK**

Condition:

During the 2008 and subsequent audits, we recommended the SBHE require a comprehensive fraud and control risk assessment by each institution and that they establish appropriate internal controls to detect, deter, and avoid potential fraudulent activity and risk relevant to the preparation of financial statements.

Current Status:

During fiscal year 2015, a comprehensive fraud and control risk assessment was not completed.

Effect:

The lack of adequate risk assessments at any level can create significant areas of risk of material misstatements in the general ledger and in the financial statements.

Cause:

A compliance plan was presented to the Audit Committee, however, it was not formally approved and NDUS is now looking to revise it with the transfer of the legal staff to the Attorney General's Office.

Criteria:

COSO (Committee on Sponsoring Organizations of the Treadway Commission) outlines five essential components of an effective internal control system. Risk assessment which involves the identification and analysis by management of relevant risks to achieving predetermined objectives is one of these five essential components.

Recommendation:

We recommend the North Dakota University System require a comprehensive fraud and control risk assessment by each institution.

University System Response/Planned Corrective Actions:

Agree. The 2015 Legislative Assembly transferred the NDUS legal staff to the Office of the Attorney General and the internal audit staff to the State Auditor's Office. As a result, NDUS restructured the internal audit function. A Director of Audit Services will be hired in early 2016 and report directly to the SBHE Audit Committee. The director will coordinate and compile a periodic system-wide risk assessment.

## 2. SBHE & NDUS – GOVERNANCE AND INTERNAL CONTROLS OF FOUNDATION AUDITS

### Condition:

During the 2013 and subsequent audits, we recommended the NDUS, as part of its governance responsibility, direct the impacted foundations to improve operations and reporting to obtain GAAP compliant financial statements as required by SBHE Policy 340.2 and review all institution affiliated organizations operating agreements annually.

### Current Status:

We noted during our review of the foundation audit reports:

- The DSU Foundation was unable to receive an audit opinion due to inadequate financial records which lead to litigation, being forced into receivership, and ultimately in the process of being dissolved; and
- There were 15 out of the 31 institution affiliated organizations operating agreements that were not reviewed by the NDUS for fiscal year 2015 and of these 15 organizations, 5 did not have an operating agreement.

### Effect:

There is noncompliance with SBHE policy 340.2, a qualified opinion on the NDUS discretely presented component unit financial statements, bond rating, and reputational issues which could affect future funding.

Additionally, NDUS institutions could become financially liable for costs associated with foundations in financial distress that are being dissolved.

### Cause:

There is inadequate oversight by the NDUS to ensure the affiliated organizations comply with the applicable SBHE policies.

### Criteria:

SBHE policy 340.2, section 3, in-part states, a foundation is a private legal entity separate from the institution and must be governed accordingly to protect the foundation's private, independent status. However, because the State Board of Higher Education is responsible for ensuring the integrity and reputation of the University System, it must be assured of the manner in which any affiliated foundation will operate.

SBHE policy 340.2, section 3e, in-part states, a requirement to provide the institution with GAAP-compliant financial statements and an annual GAAP audit of the foundation, or a draft of an audited financial statement submitted for but pending foundation board approval by September 15 each year for:

- all entities considered component units of the NDUS under GASB 39; and
- all other related organizations that are not component units, whose total assets exceed \$1 million and total program expenses exceed \$100,000, for the previous fiscal year-end.

SBHE policy 340.2, section 4, states that agreements shall be reviewed annually, and updated as necessary. A copy of each agreement shall be filed with the NDUS General Counsel.

### Recommendation:

We recommend the NDUS:

- Ensure DSU Foundation provides GAAP compliant financial statements;
- Review all institution affiliated organizations operating agreements annually to ensure compliance with SBHE policies, that updates are made to the agreement in a timely manner, and that the agreement is filed with the proper personnel.

University System Response/Planned Corrective Actions:

Agree. Proposed revisions to Policy 340.2 are in the final stages of development and will be presented to the SBHE in early 2016.

### 3. WSC - RECONCILING

Condition:

During fiscal year 2011 and subsequent audits, we noted a lack of cash bank reconciliations at WSC.

Current Status:

WSC did not perform monthly bank reconciliations and understated their general ledger cash accounts \$87,022 as of June 30, 2015.

Effect:

If cash is not reconciled fully every month, errors or misappropriations may occur and not be detected in a timely manner. Further, the general ledger and ultimately the financial statements are misstated and depending on the severity of the misstatements, the result could be a modified financial statement opinion.

Cause:

In our opinion, in the past several years WSC has not made cash reconciliations a high priority.

Criteria:

Proper internal control reduces the risk of asset loss and helps ensure the reliability of the financial statements. To adequately safeguard cash and ensure the reliability of the financial statements, reconciliations of bank balances to the general ledger are imperative.

Recommendation:

We recommend that WSC reconcile cash bank and general ledger balances to a zero difference on a monthly basis and isolate and investigate all differences fully so that the appropriate general ledger adjustments can be made in a timely manner.

University System Response/Planned Corrective Actions:

Agree. *Monthly reconciliations are essential and are considered a high priority. Since 2014, WSC has hired temporary employees, part-time consultants and entered into a shared service arrangement with another institution to help reconcile cash that had not been reconciled since July 2010. The shared service arrangement was cancelled June 30, 2015 due to lack of funding. Fiscal years 2011 through 2014 have been reconciled within an immaterial amount. WSC will establish a monthly reconciliation process and complete monthly reconciliations for Fiscal Year 2016 and Fiscal Year 2015 by fall of 2016.*

#### 4. MISU – BACKGROUND CHECKS

Condition:

During our testing of background investigations, we noted that MASU, MISU, NDSU, UND, and WSC failed to require background checks for student workers given access to PeopleSoft HRMS, Financials, and Campus Connection allowing them to view other student's names, ID numbers, addresses, etc.

Current Status:

MISU did not complete employee criminal history background checks for four out of seven employees before their start date. Two of these employees were hired after the SBHE procedure was changed on July 1, 2015.

Effect:

There is noncompliance with the SBHE procedure and an unnecessary risk to the NDUS of hiring of persons who have civil or criminal histories for sensitive jobs.

Cause:

The procedure changed on July 1, 2015 and MISU has not fully complied with the new procedure.

Criteria:

State Board of Higher Education Procedure, 602.3 Job Applicant/Employee Criminal History Background Checks part 4 CHRC and SOR checks are required for new hires for the following positions:

1. All benefited positions; and
2. Non-benefited positions, including volunteers who:
  - a) have access to confidential or proprietary information;
  - b) have master keys;
  - c) have access to cash, credit, debit, or other financial transactions;
  - d) are resident hall and/or apartment managers, directors, or assistants;
  - e) are child care employees and other employees who have unsupervised contact with minor children;
  - f) are responsible for, or with access to, controlled substances and other drugs, explosives or potentially dangerous chemicals and other substances; and
  - g) are instructional faculty and staff, including graduate teaching assistants, and are counselors and coaches.

Recommendation:

We recommend that MISU complete background investigations for all employees including student workers before access is given to PeopleSoft.

University System Response/Planned Corrective Actions:

Agree. MISU will implement a monitoring process to ensure that background checks have been completed for all new employees listed in SBHE procedure 602.3. The new process will be implemented beginning January 1, 2016.



STATE OF NORTH DAKOTA  
**OFFICE OF THE STATE AUDITOR**  
FARGO BRANCH OFFICE  
1655 43<sup>RD</sup> STREET SOUTH, SUITE 203  
FARGO, NORTH DAKOTA 58103

## ***Governance Communication***

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December 2, 2015

State Board of Higher Education

Legislative Audit and Fiscal Review Committee

We have audited the financial statements of the business-type activities and the aggregate discretely presented component units of the North Dakota University System for the year ended June 30, 2015, and have issued our report thereon dated December 2, 2015. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated May 26, 2015. Professional standards also require that we communicate to you the following information related to our audit.

### **Significant Audit Findings**

#### **Qualitative Aspects of Accounting Practices**

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the North Dakota University System are described in Note 1 to the financial statements. As described in Note 1 to the financial statements, the North Dakota University System changed accounting policies related to measuring and recognizing pension liabilities and expense as well as deferred outflows and deferred inflows of resources related to pensions by adopting Statement of Governmental Accounting Standards (GASB Statement) Nos. 68 and 71, *Accounting and Financial Reporting for Pensions* and *Pension Transition for Contributions Made Subsequent to the Measurement Date*, respectively, in fiscal year 2015. The statements required retroactive adoption and resulted in a restatement of prior period net position of \$72.4 million. Accordingly, the cumulative effect of the accounting change as of the beginning of the year is reported in the Statement of Revenues, Expenses, and Changes in Net Position. We noted no transactions entered into by the NDUS during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements:

- Fair values of investments (Note 2)
- Useful lives of capital assets (Note 5)
- Scholarship allowance: \$64,323,230
- Allowance for uncollectible receivables:
  - Accounts \$6,061,785
  - Loans and notes \$8,020,966

We evaluated the key factors and assumptions used to develop these estimate in determining that they are reasonable in relation to the financial statements taken as a whole.

The disclosures in the financial statements are neutral, consistent, and clear. Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were:

- The disclosure of Component Unit Transactions in Note 16 to the NDUS fiscal year 2015 financial statements.
- The disclosure of Subsequent Events in Note 24 to the NDUS fiscal year 2015 financial statements.

### **Difficulties Encountered in Performing the Audit**

We encountered no significant difficulties in dealing with management in performing and completing our audit.

### **Corrected and Uncorrected Misstatements**

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

The Passed Audit Adjustments schedule on page 16 summarizes uncorrected misstatements of the financial statements. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

There were no Posted Audit Adjustments.

### **Disagreements with Management**

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor’s report. We are pleased to report that no such disagreements arose during the course of our audit.

### **Management Representations**

We have requested certain representations from management that are included in the management representation letter dated November 30, 2015.

### **Management Consultations with Other Independent Accountants**

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a “second opinion” on certain situations. If a consultation involves application of an accounting principle to the governmental unit’s financial statements or a determination of the type of auditor’s opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the

consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

### **Other Audit Findings or Issues**

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the governmental unit's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

We issued a qualified opinion on the aggregate discretely presented component units for fiscal year 2015 because the financial data for Dickinson State University Foundation were not included with the aggregate discretely presented component units in the North Dakota University System's financial statements. This is addressed in Prior Recommendations Not Implemented #2 – SBHE/NDUS – Governance and Internal Controls of Foundation Audits on page 9.

### **Other Matters**

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information, except the Deficit Net Position Balances > \$100,000 and the Financial Information for Revenue Producing Buildings, to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

This information is intended solely for the use of North Dakota State Board of Higher Education, the Legislative and Fiscal Review Committee, and management of the North Dakota University System and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,



Robyn Hoffmann, CPA  
Audit Manager, Division of State Audit

December 2, 2015

## Audit Adjustments

### PASSED AUDIT ADJUSTMENTS

DESCRIPTION		DR	CR	EXPLANATION/DISPOSITION
<b>1. SNP</b>				
<b>NDSU</b>	Unrestricted net position	349,785		To correct compensated absences
	Compensated absences - current		25,534	
	Compensated absences - noncurrent		324,251	
	<b>SRECNP</b>			
	Salaries and wages	349,785		
	Net increase/decrease		349,785	
<b>2. SNP</b>				
<b>MISU</b>	Endowment investments	1,360,508		To record the Wuttke endowment
	Nonexpendable scholarships and fellowships		1,360,508	
<b>3. SNP</b>				
<b>MISU</b>	Capital assets - construction in progress	502,604		To reclassify capitalized equipment as construction in progress
	Capital assets - equipment		502,604	
<b>4. SCF</b>				
<b>NDUS</b>	Insurance proceeds	717,118		To reclassify elimination entry
	Other nonoperating revenues		717,118	
<b>5. SRECNP - CU</b>				
<b>BSCF</b>	Change in split-interest agreement	2,604		To reclassify change in split interest agreements and supporting services
	Support and revenue - change in split-interest agreement		2,604	
<b>NDSUDF</b>	Support and revenue - change in split-interest agreement	515,463		Change in split-interest agreement
	Change in split-interest agreement		515,463	
<b>UND Alumni</b>	Support and revenue - change in split-interest agreement	2,876,352	2,876,352	Change in split-interest agreement
<b>MISUDF</b>	Support and revenue - change in split-interest agreement	35,477		Expenses - supporting services - other
	Expenses - supporting services - other		35,477	

SNP – Statement of net position

SRECNP – Statement of revenues, expenses and changes in net position

SCF – Statement of cash flows

## *Management Letter*

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December 2, 2015

Ms. Robin Putnam  
Director of Financial Reporting  
North Dakota University System  
600 East Boulevard Avenue, 10<sup>th</sup> Floor  
Bismarck, ND 58505-0230

Dear Ms. Putnam:

The Office of the State Auditor has completed its financial audit of the North Dakota University System for the year ended June 30, 2015. As part of our examination, we gained an understanding of the internal control over financial reporting and tested compliance with laws and regulations to the extent we considered necessary. We have issued our report on internal control over financial reporting and compliance and other matters dated December 2, 2015.

Our audit procedures are designed primarily to enable us to report on the internal control over financial reporting and compliance with laws and regulations as they relate to the financial statements and may not bring to light all deficiencies in internal control or noncompliance with laws and regulations that may exist. We aim, however, to use our knowledge gained during our work to make comments and suggestions, which we hope will be useful to you.

In connection with the audit, we noted certain conditions that we did not consider reportable within the context of your audit report. These matters, which do not have a material effect on the financial statements, involve control deficiencies and/or instances of noncompliance with laws and regulations. The recommendations presented below are intended to improve or correct control deficiencies and noncompliance with laws and regulations. During future audit engagements, we will review the status of these recommendations to ensure that procedures have been initiated to address these recommendations. If no action has been taken, we will consider the appropriate course of action. Action could consist of inclusion in future audit reports.

I would encourage you to contact our Fargo office if you have any questions about the implementation of recommendations included in your audit report or this letter.

Sincerely,



Robyn Hoffmann, CPA  
Audit Manager, Division of State Audit

## 1. VCSU – Inadequate Monthly Investment Reconciliation

### Condition:

VCSU did not reconcile to zero their general ledger investment balances to the bank balance. There was a \$1,446 difference between bank to general ledger.

### Effect:

If investments are not reconciled fully every month, errors or misappropriations may occur and not be detected in a timely manner.

### Cause:

VCSU received incorrect information from the VCSU Foundation which did not agree to the bank balances.

### Criteria:

Proper internal control reduces the risk of asset loss and helps ensure the reliability of the financial statements. To adequately safeguard investments and ensure the reliability of the financial statements, reconciliations of bank balances to the general ledger are important.

### Recommendation:

We recommend that VCSU reconcile investments so that the bank and general ledger balance agree on a monthly basis, and isolate and investigate all differences fully.

### University System Response/Planned Corrective Actions:

Agree. VCSU receives the investments held with the foundation on a quarterly basis and will reconcile to the general ledger beginning in FY 2016. All other investments are currently balanced monthly.

## 2. MISU, VCSU, & WSC - Improper Recording of Institution Endowments/Investments

### Condition:

MISU, VCSU, and WSC have failed to hold, document donor intent, or record donations, gifts, and endowments that were donated directly to the institutions on their financial statements. Instead, the institutions are giving or potentially giving, where no documentation of donor intent exists or is retained, these dollars to the foundations.

### Effect:

By failing to record and document donor intent for endowments, it causes or may cause the Statement of Net Position to be understated and could result in the violation of NDCC and ND State Constitution.

### Cause:

There is a lack of compliance and unfamiliarity with NDCC, SBHE Policy, and ND State Constitution.

### Criteria:

A basic concept of governmental financial reporting is to assist in fulfilling government's duty to be publicly accountable and demonstrating compliance with legal and contractual requirements.

SBHE Policy 810 (6) - Donations or gift funds and endowment funds shall be invested according to the intent of the donor, if such intent is expressed in a gift instrument and provided such intent is consistent with applicable laws. Absent terms expressing donor intent in a gift instrument, NDUS institution officers initially shall deposit the funds in institution accounts at the Bank of North Dakota as required by law.

NDCC 15-10-12 – states in part that the state board of higher education may, subject to the limitations of section 15-10-12.1, receive donations, gifts, grants, and bequests offered or tendered to or for the benefit of any institution of higher education under its control or subject to its administration, and all moneys coming into the hands of the board as donations, gifts, grants, and bequests must be used for the specific purpose for which they are donated or given.

NDCC 59-21-05 - states in part that the donor can consent to a change in the restrictions, or can be modified by the court upon application by the institution.

North Dakota Constitution Article X section 18 - states in part that the state nor any political subdivision thereof shall otherwise loan or give its credit or make donations to or in aid of any individual, association or corporation except for reasonable support of the poor.

Recommendation:

We recommend that MISU, VCSU, and WSC record and retain adequate donor documentation for all donations, gifts, and endowments given to the institutions, and recorded on their financial statements.

University System Response/Planned Corrective Actions:

*MiSU: Agree. MiSU will record the endowments currently held by the MiSU Development Foundation originally given to university on the MISU financial statements by June 30, 2016.*

*VCSU: Agree. VCSU will have all donor documentation reviews completed by December 31<sup>st</sup>, 2015 to ensure donations are held on the correct financial statement.*

*WSC: Agree. WSC met with the foundation to review endowed funds. The database will be updated by June 30, 2016 to include information showing verification of donor intent.*

### **3. MISU - Commingling of Cash Between Institution and Foundation**

Condition:

MISU is allowing a legally separate component unit, the Beaver Boosters, to share their campus bank accounts. The commingling of cash in the same bank accounts, by this separate legal entity, places the cash and possibly the separate status of the entity at risk.

Effect:

A combined bank account with the foundation increases the risk of misappropriating cash as well as possible liability for foundation bad debts and expenses.

Cause:

MISU performs accounting duties for the Beaver Boosters and keep the same bank accounts for ease of depositing.

Criteria:

Funds that are owned and controlled by a related Foundation or Alumni Association should be recorded in bank accounts under the Foundation or Alumni Association's Employer Identification Number (EIN).

SBHE Policy 340.2 (3) states: A foundation is a private legal entity separate from the institution and must be governed accordingly to protect the foundation's private, independent status.

Recommendation:

We recommend MISU keep separate bank accounts from the Beaver Boosters.

University System Response/Planned Corrective Actions:

*Agree. A separate bank account was opened for Beaver Boosters. As of November 2015, MiSU transferred the entity's cash balance to the new bank account.*

### **4. NDSU & UND – Expenses Not Recorded in Proper Fiscal Year**

Condition:

We noted 7 out of 24 expenses were posted to fiscal year 2016, when they should have been posted to fiscal year 2015. At NDSU and UND, these expenses totaled \$3,853,930.

Effect:

Expenses and payables are understated in fiscal year 2015, thus misstating the financial statements.

Cause:

All items at NDSU that were not recorded in the proper fiscal year were processed through FAMIS. FAMIS transactions had a much earlier cut-off date than other items processed through regular entry.

The one item at UND was a grant related expenditure with the close of mid-July and the item in question did not come into the central office until late August.

Criteria:

GAAP requires the recognition of an expense and liability when incurred.

Recommendation:

We recommend that NDSU and UND implement procedures to ensure that all expenses, especially those where the departmental reporting cut-off may be earlier than the campus cut-off, are recorded in the proper fiscal year.

University System Response/Planned Corrective Actions:

*NDSU: Agree. NDSU believes this issue is isolated to a single department. The Accounting Office will work with the applicable department to ensure expenses are recorded in the proper fiscal year.*

*UND: Agree. The Grants and Contracts Office utilizes a project year, not fiscal year, which has caused difficulties receiving invoices in a timely manner. UND will increase communication with the Grants & Contracts Office and educate principal investigators on the importance of fiscal year-end. UND also will communicate with vendors to require June invoices be sent to UND by July 10th every year.*

## **5. BSC – Pledged Revenues Note**

Condition:

In the Pledged Revenues note in the financial statements, BSC only included the principal payment in the Pledged Revenue Required for Future Principal and Interest on Existing Bonds. It should also include the interest payments on the bonds outstanding, which totaled \$2.9 million.

Effect:

The notes to the financial statements are misstated, therefore incorrect information is included which could potentially mislead financial statement users.

Cause:

BSC did not include the amount on the template used to prepare the notes to the financial statements.

Criteria:

GASB 48 Section 21.a states the following should be included in the disclosure; "Identification of the specific revenue pledged and the approximate amount of the pledge. Generally, the approximate amount of the pledge would be equal to the remaining principal and interest requirements of the secured debt."

Recommendation:

We recommend that BSC include both remaining principal & interest payments due on the bonds in the Pledged Revenue Required for Future Principal and Interest on Existing Bonds to ensure the Notes to the Financial Statements are correct.

University System Response/Planned Corrective Actions:

*Agree. BSC will review the requirements of this note disclosure and ensure compliance beginning with FY16.*

## 6. BSC, VCSU, & WSC – PeopleSoft Asset Management System Utilization

### Condition:

BSC, VCSU, and WSC are not fully utilizing the PeopleSoft Asset Management (AM) module for keeping track of various asset classes. BSC did not include land, VCSU did not include land improvements/infrastructure and WSC did not update land improvements/infrastructure, buildings, and equipment.

### Effect:

This results in a lack of consistency and efficiency and serves to diminish internal controls by increasing the likelihood of human error impacting the financial statements.

### Cause:

Prior to fiscal year 2015, there had been no established policies and procedures for tracking capital assets to ensure effective and efficient capital asset records. Land, buildings, improvements, and infrastructure had always been tracked using off-system records so institutional personnel have continued to track them as they have in the past. The movement to utilizing PeopleSoft Asset Management is fairly new, and is still a work in progress.

### Criteria:

PeopleSoft Asset Management has the ability to track buildings, land, and improvements but the system is not being used to its full potential.

### Recommendation:

We recommend BSC, VCSU, and WSC fully utilize the PeopleSoft Asset Management system for all asset classes.

### University System Response/Planned Corrective Actions:

*BSC: Agree. Land was mistakenly excluded from the asset management upload when buildings and infrastructure were added to asset management. Land will be added to Asset Management in FY16.*

*VCSU: Agree. VCSU will have all infrastructure added to the PeopleSoft Asset Management system by the end of Fiscal Year 2016.*

*WSC: Agree. WSC will fully utilize the PeopleSoft Asset Management module to track all asset classes by the end of FY16.*

You may obtain reports by contacting the  
Division of State Audit  
at the following address:

Office of the State Auditor  
600 East Boulevard Avenue – Department 117  
Bismarck, ND 58505-0060  
(701) 328-2241

Reports are also available on the internet at:  
[www.nd.gov/auditor/](http://www.nd.gov/auditor/)