

# Northeast Texas Community College

## Table of Contents

<b>Key Points of Report Executive Summary</b> .....	1
---	---

Section 1:

<b>Management Override by the Former President and Inaction by the Board of Trustees Has Resulted in Fiscal Mismanagement of College Assets</b> .....	5
---	---

Section 2:

<b>Questionable Business Decisions, Inaction by the Business Office, and Poor Cash Management Have Placed a Significant Financial Strain on the College</b> .....	6
---	---

Questionable Business Transactions Compounded the Financial Strain on the College .....	6
--	---

Business Officers Failed to Take Action on Important Fiscal Matters .....	8
--	---

Poor Cash Management Resulted in a Backlog of Unpaid Bills .....	10
---	----

Section 3:

<b>Significant Internal Control Problems Exist in the Financial Operations of Northeast Texas Community College</b> .....	13
---	----

Northeast Texas Community College Bookstore Lacks Fundamental Financial Reports .....	14
--	----

Food Service Department Lacks Fundamental Financial Information to Track Revenue and Expenditures .....	15
--	----

Value of the College's Fixed Assets May Not Be Accurate Because No Physical Inventory Has Been Conducted Since 1990, and Assets Donated to the College Are Not Tagged or Recorded in the Fixed Asset Records .....	16
---	----

Accounts Payable Clerk Performs Incompatible	
--	--

# Table of Contents, concluded

Functions and Lacks Essential Automated Processes .....	17
Accounts Receivable Billings Are Not Timely, and the Accounts Receivable Clerk Performs Incompatible Clerical Functions .....	18
Payroll Clerk Performs Incompatible Functions .....	19
Northeast Texas Community College Information System Fails to Provide Essential Information on a Timely Basis .....	20
Section 4:	
<b>Accounting for the Foundation’s Scholarship and Endowment Funds Is Inadequate, and There Has Been Little Oversight by the Foundation’s Board .....</b>	<b>21</b>
Fundamental Accounting for the Foundation Has Been Neglected .....	21
Oversight of Foundation Activities by the Foundation’s Board Has Been Almost Non-Existent .....	22
Section 5:	
<b>The Legality of Certain Business Office Transactions Is Questionable .....</b>	<b>23</b>
Beginning in 1992, the College Bookstore Was Used as a Channel to Fund College Operations through Fictitious Grants Billing .....	23
Business Office Officials Inappropriately Reported Federal Grant Monies as Local Matching Funds to Obtain Additional Revenue .....	23
College Funds Were Used to Pay Debts of the Athletics Booster Club .....	24
<b>Management’s Responses .....</b>	<b>25</b>
<b>Appendix</b>	
Objective, Scope, and Methodology .....	40

# Key Points Of Report

## An Audit Report on Management Controls at Northeast Texas Community College

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February 1996

### Overall Conclusion

Inaction by the Board of Trustees, management override by the former administration, and poor internal controls have resulted in operational and financial mismanagement at Northeast Texas Community College. Improvements are needed in all areas of financial operations as well as information management. The new president has initiated improvements in financial and management controls and in communication with the Board of Trustees, faculty, and staff. However, serious financial problems and internal control weaknesses remain.

### Key Facts and Findings

- Management override by the previous administration and inaction by the Board of Trustees resulted in mismanagement of college assets. Excessive and inappropriate expenditures went unchallenged until the Texas Rangers were called in to investigate.
- Northeast Texas Community College has been unable to pay its bills on a timely basis and has incurred thousands of dollars in insufficient funds charges. The College has extended payment on its long-term debt, costing the College millions in interest expense and jeopardizing the future growth of the College.
- Accounting for the Foundation's scholarship and endowment funds is inadequate, and there has been little oversight by the Foundation's board. The College's accounting system is not able to compile scholarship fund account balances, which has resulted in overawarding of student scholarships and the liquidation of some scholarship balances.

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*This management control audit was conducted in accordance with Government Code, § 321.0133.*

## Executive Summary

Management override by the former administration, inaction by the Board of Trustees, and poor internal controls have resulted in operational and financial mismanagement at Northeast Texas Community College. Improvements are needed in all areas of financial operations as well as information management. The new president has initiated improvements in financial and management controls and in communication with the Board of Trustees, faculty, and staff; however, serious financial problems and internal control weaknesses remain. In spite of its financial problems, Northeast Texas Community College is providing quality education to the local community and has received the Excellence in Higher Education Award for 1995 for its Community in Schools program.

### **Management Override by the Former President and Inaction by the Board of Trustees Has Resulted in Fiscal Mismanagement of College Assets**

The former president of Northeast Texas Community College disregarded established policies and procedures which contributed to his indictment and the indictment of three members of his staff. Some of these acts were committed openly, such as a personal vacation at college expense and purchases of personal items from the bookstore and cafeteria without payment. Other acts were concealed by falsifying documents and reports to the Board of Trustees such as political contributions, payments for renovation of box seats at Texas Ranger baseball games, and construction work at the former president's personal residence performed by college maintenance staff on college time. In addition, to pay for construction of a baseball field for the College, the former president bartered college assets valued at more than \$120,000 to a

private construction company without approval of the Board of Trustees..

Although the Board of Trustees were informed by the Texas Rangers about the president's trip to Las Vegas, his fishing trips to Missouri, and his extravagant spending on credit cards, no action was taken nor was there any internal investigation. The board members placed too much reliance on the integrity and business experience of the former president and fiscal managers of the College. Finally, the Texas Rangers responded to repeated calls and letters from external sources to conduct an investigation.

### **Questionable Business Decisions, Inaction by the Business Office, and Poor Cash Management Have Placed a Significant Financial Strain on the College**

The Board of Trustees, with the advice of college financial officers, approved increasing long-term bond debt, increasing funding for athletics, and awarding pay raises to all employees even though available tax revenue was declining, and the College was unable to pay its bills on time.

The poor financial condition of the College was exacerbated by inadequate fund reserves, the failure of the Business Office to submit timely billings, and failure to monitor the cash balances of the operating funds. As a result, more than \$10,000 in bank penalties were incurred for writing checks without sufficient bank funds.

## Executive Summary

### **Significant Internal Control Problems Exist in the Financial Operations of Northeast Texas Community College**

We reviewed the internal control policies and procedures related to financial operations and noted more than 20 significant internal control weaknesses. Weaknesses include but are not limited to: failure to provide profit and loss statements for food service and bookstore operations, failure to safeguard assets, failure to provide essential accounting and reporting on a timely basis, and failure to obtain appropriate approval for large expenditures.

A review of food service transactions revealed that the department lost approximately \$40,000 for fiscal year 1994-1995. Although the bookstore is profitable, the exact amount of profit has not been determined. Profits are partially attributable to a 20 percent markup of supplies and equipment purchased through the bookstore for academic departments.

Internal controls over fixed assets are inadequate due to the failure to conduct a physical inventory and the failure to tag and record all donated assets. A physical inventory has been recommended by the auditing firm of Thomas and Thomas in the last three audit reports. Each time the response has been that an inventory would be taken. However, to date, this has not happened.

### **Accounting for the Foundation's Scholarship and Endowment Funds Is Inadequate, and There Has Been Little Oversight by the Foundation's Board**

Although the assets of the Northeast Texas Community College Foundation are significant, accounting for the transactions and

balances involving these assets is neglected. The Foundation's assets were valued at more than \$230,000 as of August 31, 1995, based on unaudited data. Foundation financial transactions are recorded in the College's accounting system, but this system is not capable of compiling financial statements and account balances for each scholarship fund.

An audited annual financial report has not been submitted for the Foundation since fiscal year 1990. An external audit of the Foundation covering fiscal years 1991 through 1994 was released in December 1995. The fiscal year 1995 audit was completed in January 1996.

The Foundation's Board has not met since May 6, 1993. There are only three other documented meetings of the Foundation's Board since its inception in 1984: January 14, 1985; June 21, 1989; and February 24, 1992.

### **The Legality of Certain Business Office Transactions Is Questionable**

In addition to the bookstore operations, we noted other college business transactions which are questionable. One instance is in the grants billing operations. The public accounting firm of Thomas and Thomas recently determined that federal grant funds were erroneously reported as local matching funds to the U.S. Department of Defense. This error in reporting resulted in excess billings of \$20,871.61.

Another questionable transaction involved the payment of booster club obligations with college funds. Two payments, in August 1994 and March 1995, totaling \$42,484 were made to Guaranty National Bank to meet the obligation of a note signed by a booster club president. Since the booster club is not part of

## Executive Summary

the College, and no college official signed the note, there was no obligation on the part of the College to pay this amount.

Also, the legality of bookstore charges to federal grants in 1992 and 1993 for supplies which were not delivered is questionable.

### **Summary of Management's Responses**

Northeast Texas Community College management generally agrees with the findings and recommendations included in this report except for findings regarding long-term debt and sufficiency of information provided to the Board of Trustees. College management chose not to respond to the adequacy of board oversight. The complete management response follows the body of the report.

In addition, college management will prepare a detailed corrective action plan which will be submitted to the Texas Higher Education Coordinating Board for review.

### **Summary of Audit Objectives and Scope**

The objective of this audit was to determine the strength of internal controls over financial administration and included a review of the overall financial condition as well as college governance.

The scope of the audit included the review of the financial administration process, including annual financial reporting and budgeting, the external audit function, and the governance of financial administration by the Board of Trustees.

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Section 1:

## **Management Override by the Former President and Inaction by the Board of Trustees Has Resulted in Fiscal Mismanagement of College Assets**

The former president of Northeast Texas Community College disregarded established policies and procedures and treated the College as his private bank, travel agency, restaurant, and shopping center.

According to witnesses, the former president of Northeast Texas Community College withdrew large sums of money through petty cash for personal use, took personal vacations at taxpayer expense, treated his family to free meals in the cafeteria, took items from the bookstore without payment, and committed numerous other breaches of college policy. Some of these acts were committed openly. Other acts were concealed by falsifying documents and reports to the Board of Trustees.

Although the Board of Trustees was informed by the Texas Rangers during their investigation about fishing trips and extravagant spending, no action was taken nor was there any internal investigation. The former president also bartered college assets valued at more than \$120,000 to a construction company for construction work on school facilities, including a baseball field. The Board of Trustees had not approved this transaction. Finally, the Texas Rangers responded to repeated calls and letters from external sources to conduct an investigation. As a result of this investigation, a Titus County grand jury handed down indictments on the Northeast Texas Community College president, the vice president of administrative services, the controller, and the dean of plant services. Included in the charges were:

- theft
- misapplication of fiduciary property
- tampering with governmental records

The former president pleaded “no contest” to the charges of theft by a public servant and misapplication of fiduciary property. The dean of plant services pleaded no contest to misapplication of fiduciary property. The charges of tampering with governmental records were dropped against the vice president of administrative services and the controller. In addition, the State Board of Public Accountancy initiated an investigation of the controller for falsifying expenditure reports to the Board of Trustees. The former president resigned in March 1995. The vice president of administrative services and the controller resigned in December 1995.

The management philosophy of a majority of the Board of Trustees has been, “hire a good president and stay out of the way.” The seven members of the Board of Trustees are among the leaders in their communities. The present Board of Trustees consists of a bank president, a retired chief executive officer and certified public accountant, a practicing certified public accountant, a civic leader and dentist, an engineer, a senior vice president of a regional health care system, and a retiree from Lone Star Steel Company. The board members are highly respected in their professions and their



communities who placed too much reliance on the integrity and business experience of the former president and fiscal managers of the College.

Recommendations:

We recommend that the Board of Trustees receive additional training regarding their responsibilities and that the Board, with assistance from college staff, develop and implement a plan to address the financial problems and internal control weaknesses of the College.

We also recommend that the Texas Higher Education Coordinating Board request from the College a financial and operational plan addressing the State Auditor's recommendations. We further recommend that the Coordinating Board monitor this plan for timely compliance.

Section 2:

## **Questionable Business Decisions, Inaction by the Business Office, and Poor Cash Management Have Placed a Significant Financial Strain on the College**

Northeast Texas Community College has been unable to pay its bills on time during six months of fiscal year 1995 and has incurred more than \$10,000 of insufficient fund penalty charges. In addition, the College's debt repayment schedule had to be extended because the College had exceeded its ability to make the required payments. This debt extension will result in additional interest payments of more than \$3 million. The poor financial condition of the College is partially due to questionable business decisions, inaction by college business officers, and poor cash management.

Section 2-A:

### **Questionable Business Transactions Compounded the Financial Strain on the College**

Questionable management decisions noted during our audit include:

- significantly increasing debt while revenue was declining
- providing \$318,630 annually to fund athletics, which generated only \$10,000 annually in revenue from sports activities
- giving significant pay raises when the College could not pay its bills on time
- continuing to incur banking penalties for writing checks with insufficient funds

**Long-term debt was increasing while tax revenue was declining.** Although tax revenue has been decreasing since the founding of the College, debt has continued to grow. The taxable assessed value of property located within the Northeast Texas Community College service area has decreased from \$2,545,207,704 in 1985 to

\$2,077,278,003 in 1995. Based on a \$.10 tax rate per \$100 valuation, this drop equates to a reduction in potential tax revenue of \$467,930 per year.

Although tax resources have dwindled, long-term debt of the College has continued to grow. Some of the debt increase was to fund a theater and art complex, additional classrooms and classroom renovation, computer hardware and software, and instruction. Some of this debt was also used to fund dormitories and athletics and to extend payments of existing debt. As of August 31, 1994, the long-term debt of the College dependent upon tax revenue included the following:

• 1986 Series Limited Tax Obligation Bonds and Compound Interest Bonds	\$5,430,415
• 1991 Series Limited Tax General Obligation Bonds	\$2,175,000
• 1994 Public Property Finance Contractual Obligations	\$ 210,000

In addition, the following long-term debt not dependent upon tax revenue for repayment was outstanding as of August 31, 1994:

• 1990 Series Tuition and Building Use Fee Revenue Bonds	\$1,605,000
• 1992 Series Housing Revenue Bonds	\$ 785,000
• 1994 Series Dormitory	\$ 550,000

The annual operating budget for fiscal year 1996 includes \$1,370,246 of interest and sinking expense to pay the interest and principal of the existing debt for the year. Of this amount, \$945,118 will be paid from local taxes. This represents 45 percent of the total amount estimated to be collected from taxes for the year. Based on 1994 financial data, Northeast Texas Community College was ranked last out of 50 junior and community colleges in the State in the ratio "Expendable Fund Balances to Plant Debt." This ratio indicates the relative liquidity of the institution. It is a fundamental indicator of financial strength. It reflects the availability of sufficient cash, or assets that will convert to cash in the normal course of business, to meet all obligations as they become due.

**Northeast Texas Community College spends more than \$318,000 per year on athletics and does not follow recommended procedures for reporting the expenditures.** The fiscal year 1996 operating budget includes a total of \$318,630 for expenditures and only \$10,000 for revenues from the following activities:

	<u>Expenditures</u>	<u>Revenues</u>
Intercollegiate Athletics		\$73,380
Rodeo Team	\$81,250	\$10,000
Baseball	\$91,500	
Softball	\$63,500	
Golf	\$ 9,000	

Included in these *athletic* costs are \$160,750 for scholarships. In comparison, there is only \$10,211 of *academic* scholarships funded from local sources. Funding for academic scholarships is primarily from private donations while funding for athletic

scholarships is from student activity fees and auxiliary operations which includes bookstore and food service operations.

These athletic costs are included in the annual operating budget as “Organizational Activities Related to Instruction.” The Texas Higher Education Coordinating Board recommends that these costs be included in Auxiliary Funds along with operations of the bookstore, food service department, housing, and the post office. By commingling athletics with instructional expenditures, the actual amount of student activity fees allocated to athletics is not disclosed. If athletics were reported in Auxiliary Funds, it would be necessary to transfer funds to athletics from other sources such as student activity funds, cafeteria operations, and bookstore operations. This would allow for identification of the resources expended on athletics and highlight the financial drain that athletics places on the College.

**Pay raises were awarded even though the College was unable to pay its bills on time.** Although the College has not been able to pay its bills on time for any month during 1994-1995, pay raises were awarded to administrators and faculty. The former president of the College received a substantial pay raise in the preceding year. During the investigation by the Texas Rangers in September 1994, several employees were given raises by the president. In January 1995, all employees received a pay raise.

**Business officers routinely wrote checks without sufficient bank funds** During the period from September 1, 1994, through August 31, 1995, more than \$8,900 of insufficient fund penalty charges were assessed against Northeast Texas Community College for writing checks on the operating checking account with insufficient funds. This was reported to the Board of Trustees in September 1995. The next month, more than \$900 was assessed in insufficient fund penalty charges on the same account.

Section 2-B:

### **Business Officers Failed to Take Action on Important Fiscal Matters**

In addition to questionable decisions, the Business Office failed to take action on the following:

- failure to complete the 1994 Annual Financial Report until 13 months after the end of the fiscal year
- failure to file budget documents with the county clerks as required by board policy
- failure to complete the transfer of stock donated to the College in 1992 valued at \$65,000
- failure to comply with repeated audit recommendations to conduct a physical inventory of college fixed assets

- failure to establish a line of credit within a reasonable time after it was approved by the Board of Trustees

**Business officers failed to file the annual financial report in a timely manner**

The annual financial report for the fiscal year ended August 31, 1994, was not completed until September 28, 1995. The Texas Higher Education Coordinating Board requests submission by January 1 after the end of the fiscal year. The Coordinating Board, the State Auditor's Office, and the College's auditing firm of Thomas and Thomas made numerous inquiries about the report without adequate response from college officials. According to Coordinating Board officials, the submission by Northeast Texas Community College was the most delinquent of all 50 community and junior colleges. The college business officer failed to notify the newly appointed interim president of the delinquency. However, as soon as he became aware of the situation, he took action to resolve the delinquency.

**College officials failed to file budget documents with the required counties**

The Morris County Clerk's Office reports that no budget has been filed since 1989. Camp County reports that no budget report has ever been filed.

In each annual operating budget adopted by Northeast Texas Community College is a statement that, in compliance with the statutes of the State of Texas, copies of the budget are to be filed with the County Clerks of Camp, Morris, and Titus Counties; the Texas Higher Education Coordinating Board; and the Texas Education Agency. The president of the Board of Trustees is responsible for filing these documents.

**Business officers failed to complete transfer and sale of donated stock certificates.**

Funds that should be available for scholarships are not available due to inaction by college administrators. One of the current board members donated stock valued at \$65,000 to the College Foundation in 1992. He directed that this stock be sold and the proceeds be used to fund scholarships for students from Pittsburg, Texas. Not only has this stock not been sold, the stock has not even been transferred to the College Foundation for sale. The vice president of administrative services stated that this has not occurred because the Foundation's Board must meet in order to adopt a resolution to hire a stock broker to handle the transaction. The last time this board met was in 1993.

**Recurring audit recommendations were never implemented** A physical inventory of fixed assets has not been performed although such an inventory was repeatedly recommended by the College's external auditor, Thomas and Thomas. Consequently, there is no assurance that assets listed on the college books are in fact present. College administrators have responded that an inventory will be conducted, but no inventory has ever been performed. Consequently, there is a risk that college assets are not protected and that accounting records are not accurate. (Specific weaknesses related to fixed asset accounting are discussed in Section 3 of this report.)

**Business officers failed to follow up on the implementation of a line of credit**

More than \$200,000 of delinquent accounts payable remained at the end of September 1995 even though a line of credit for \$300,000 was approved by the Board of Trustees

during the September 1995 board meeting. By the end of October, the line of credit was still not established, and checks had to be held for lack of funds.

Section 2-C:

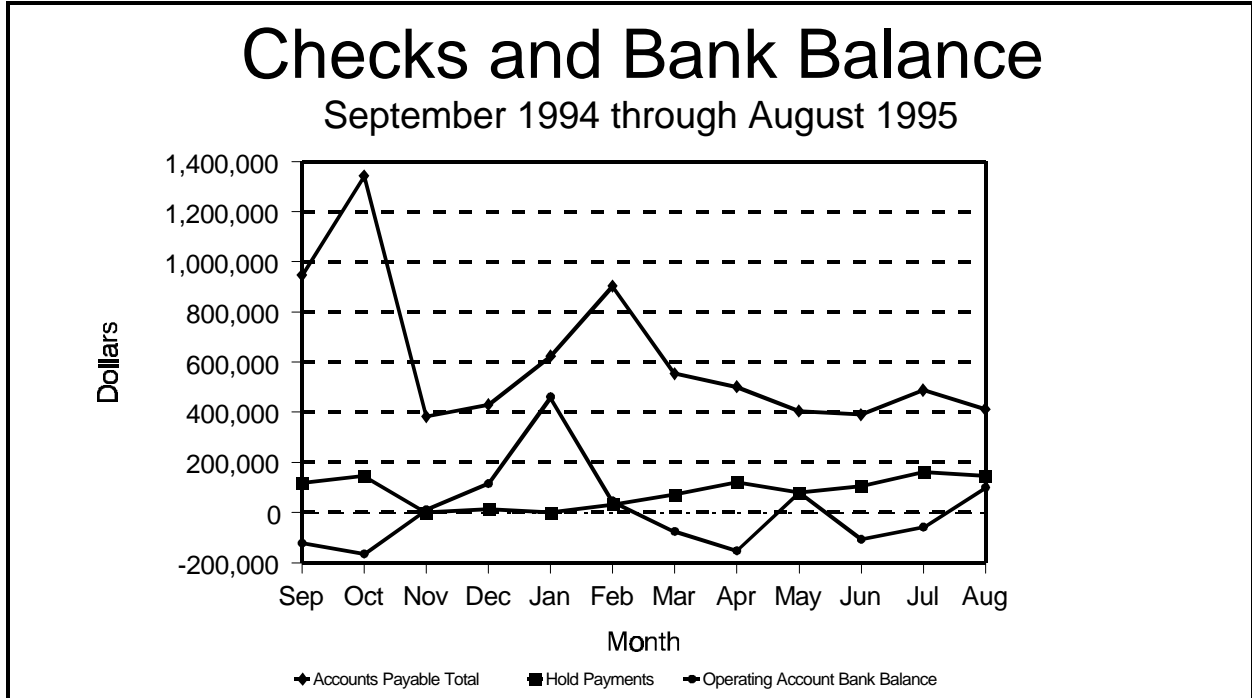
### **Poor Cash Management Resulted in a Backlog of Unpaid Bills**

Northeast Texas Community College has been unable to pay its bills on time due to a lack of adequate fund balances, lack of cash forecasting, failure to provide timely billing, and unauthorized expenditures. Additionally, there were more than \$10,000 in insufficient fund charges in the last 13 months. This represents more than 550 checks written without sufficient funds in the bank.

Figure 1 indicates the total accounts payable due, the amount of accounts payable checks held for lack of funds (hold payments) on the last check processing of the month, and the end of month operating account bank balance. As this figure depicts, the value of the hold payments is growing, and the operating account bank balance was negative for 6 of the 12 months. This is due, in part, to the inability of the College Business Office to accurately forecast cash needs and availability.

Northeast Texas Community College business officers rely on the local bank to tell them when the operating checking account is overdrawn. This occurred routinely, and more than 550 checks were returned for insufficient funds in the last 13 months. Each time an overdraft situation occurs, the College is charged \$18 by the bank.

Figure 1



Although business officers have known of the poor financial condition of the College, this information has not been provided to the Board of Trustees. Each month, the financial information provided by the Business Office for board meetings has given the impression that all is well financially. The accounts payable ageing, which is supposed to reflect how old the past due bills are, has shown that there are no overdue invoices. For example, the accounts payable ageing provided for the October board meeting listed no invoices as being past due. In reality, more than \$200,000 in invoices were past due.

Board members were also never told about the \$10,000 for bank charges to cover insufficient fund checks for the period from September 1994 through September 1995. If the board members had been given accurate, timely, and relevant financial information, the current cash problems could have been adequately addressed.

As a result of the cash shortage, the Business Office has delayed paying some vendors. The October 12, 1995, Cash Requirements and Check Preparation Report listed more than \$246,000 of invoices which were due but were not being paid. Although some of these invoices may have been held for legitimate reasons such as billing disputes, the majority of these past due bills were held for lack of funds. A local manufacturer is owed more than \$28,000 for work done in May, June, and July of 1992.

One of the reasons for the current cash shortage is the failure to bill federal and state agencies as well as local businesses on a timely basis. For example:

- The college billing clerk reports that the College is more than 30 days late billing the State for more than \$50,000.

- Bills to local merchants for advertising in the college newspaper (in the spring of 1995) still have not been prepared.
- Sign revenue for advertising on the baseball outfield signs has not been collected for the past two seasons. Annual sign revenue is estimated at \$17,500 per year.
- Admission to baseball games has not been charged during the past two years because access to the stadium is not controlled.

In addition to failure to bill in a timely manner, inaction on the part of administrators has resulted in loss of revenue to the College. For example:

- Surplus land owned by the College Foundation could have been sold for \$50,000 if college officials had acted within a reasonable time.
- Stock donated more than two years ago still has not been transferred to the College. As a result, the College is losing dividends and funding for targeted scholarships.

Conversely, the College did pay \$42,484 to a local bank on a note which was not an obligation of the College. This note was for a loan which paid part of the baseball field construction costs. Payment was used authorized by the vice president of administrative services and approved by the controller to pay for a note of a booster club because the club did not have the money. This was done without Board of Trustees' knowledge or approval.

#### Recommendations:

Although board members should not be involved in the day-to-day operations of the College, they are responsible for oversight of the College. Board members should require feedback from college administrators to ensure board policies are being implemented and enforced. We recommend that the Board of Trustees do the following:

- Ensure the annual financial report is submitted in a timely manner.
- Ensure budget documents are filed with county clerks as required.
- Scrutinize any addition of long-term debt.
- Determine if the level of expenditures on athletics is consistent with the mission and financial condition of the College.
- Approve pay raises in a meeting of the whole board.
- Enact a policy prohibiting bartering of assets without board approval.
- Ensure that previous annual financial report audit recommendations are implemented.
- Require monthly financial information which includes fund balance and cash forecast information.

In addition, we recommend the following:

- Develop and utilize a cash needs and resources forecast on a monthly basis that can be updated weekly so that weekly accounts payable processing will not result in overdraft bank charges.
- Develop a financial contingency plan to address unexpected expenditures and decreased revenues. This plan should include increasing available fund balances so that bank financing or a line of credit will not be necessary.
- Provide timely, accurate, and relevant financial information to the Board of Trustees, including:
  - accurate accounts payable ageing
  - financial balance sheet as well revenue and expenditure information
  - fund balance information
  - any unanticipated or budgeted expenditures such as bank charges
- Aggressively pursue other financial resources such as sales of surplus assets and unrestricted donated properties.
- Submit timely billings to federal and state agencies and collect monies owed to the College for advertising in the college newspaper and for baseball field signs.
- Construct a fence around the baseball field and charge admission as well as concession sales if the potential revenue would offset the additional cost.
- Collect payments made on behalf of the booster club, and strictly prohibit the payment of any item that is not a legal obligation of the College.

Section 3:

### **Significant Internal Control Problems Exist in the Financial Operations of Northeast Texas Community College**

Improvements are needed in all areas reviewed, but the lack of internal controls over bookstore and food service operations as well as fixed assets requires immediate attention. We reviewed the internal control policies and procedures of the following fiscal operations:

- bookstore
- food service
- fixed assets
- accounts payable
- personnel
- accounts receivable
  
- payroll



- information systems

Section 3-A:

### **Northeast Texas Community College Bookstore Lacks Fundamental Financial Reports**

The Northeast Texas Community College bookstore lacks routine financial statements to measure profit. In addition, bookstore profits are partially generated by charging academic departments a 20 percent markup for supplies, materials, and equipment.

According to the Northeast Texas Community College fiscal year 1996 budget, bookstore operations should result in a profit. However, there is no accounting process to determine the profit and losses for bookstore operations. Although the bookstore is profitable, the exact amount of profit is not determined. Revenue and expenditure data is collected, but no financial statement is prepared to compute periodic profit or loss. Consequently, there is no analysis provided to determine the efficiency of operations nor any comparative data to evaluate each expenditure category. A profit and loss statement should be a fundamental internal control over financial operations.

Part of the profits from bookstore operations is generated from academic department purchases of supplies, materials, and equipment from or through the bookstore. Departments are encouraged to purchase supplies and equipment from the bookstore rather than directly from outside vendors. Departments are charged 20 percent over cost for the items, and purchases of items funded by state and federal grants are marked up 40 percent over cost. While it is recognized that the bookstore should recover its cost plus cover its operating expenses, no analysis has been conducted to determine if 20 percent is appropriate.

In addition to financial reporting and cost allocation concerns, we noted several violations of internal controls, including:

- The safe combination was not changed after an employee with knowledge of the combination terminated employment.
- The door lock was also not changed after resignation of an employee with a key.
- Four persons have keys to the bookstore.
- Fixed asset items ordered through the bookstore and entered on Inventory Control Report forms are not entered into the fixed asset record keeping system.

#### Recommendations:

We recommend the following:

- The college bookstore should change its 20 percent markup to academic departments to an amount equal to its cost plus an overhead rate to cover operations.
- The door locks and safe combination should be changed.

Section 3-B:

### **Food Service Department Lacks Fundamental Financial Information to Track Revenue and Expenditures**

Our review of food service revenue and expenditures revealed that food service operations had a loss of approximately \$40,000 for the year ended August 31, 1994. Income statement information is not usually prepared for food services. Therefore, there is no way for college administrators to know if the operations are profitable, nor is there any way of knowing how much commission is owed to the food service manager since part of his salary is based on profits from food service operations.

The food service operation is budgeted to make a modest profit of \$12,665 for fiscal year 1996. The food service manager does not have an employment contract; however, he believes that his salary is based, in part, on the profits from food service sales. The food service manager reports that he has not been paid this portion of his salary for the fall of 1994, nor for the spring of 1995. When he did receive commission on profits in prior years, no employee taxes were deducted. The payments were treated as contract employee wages not subject to payroll deductions. The food service manager is a full-time college employee. Although the food service manager wrote a letter to the new president, no action has been taken regarding commission arrearage. The food service manager has no method to calculate earnings and profits because he receives only expenditure information from the Business Office.

#### **Recommendation:**

We recommend that food service revenues and expenditures be reviewed and prices adjusted as necessary to eliminate operating losses. We also recommend that monthly income statement information be provided by the Business Office.

Section 3-C:

### **Value of the College's Fixed Assets May Not Be Accurate Because No Physical Inventory Has Been Conducted Since**

## **1990, and Assets Donated to the College Are Not Tagged or Recorded in the Fixed Asset Records**

The value of the fixed assets at Northeast Texas Community College was \$18,343,432 as of August 31, 1994. Furniture, fixtures, and vehicles comprised \$2,876,392 of this amount. These values are based on purchases made by the College since inception. Also, the College's computer system has not been programmed to delete items from the inventory which are no longer present such as vehicles which have been traded in. For example, in a test of the accounting records for college vehicles, we noted the following:

- The value of the vehicles per the computer records was \$178,079, but the amount listed in the annual financial report was \$143,572.
- Three vehicles which had been traded in were still on the College's records.
- One dump truck purchased and present at the campus was not recorded.
- One pick-up truck which had burned in a fire was still on the books while another truck which had been purchased at the same time was not recorded.

A physical inventory has been recommended by the auditing firm of Thomas and Thomas in the last three audit reports. Each time, the response has been that an inventory would be taken; however, to date, this has not happened.

### Recommendations:

We recommend the following:

- Conduct a physical inventory of equipment and vehicles.
- Give a tag number to and record all fixed assets, whether purchased or donated, in the fixed asset ledger.
- Program the accounting software to allow removal of assets from the inventory and to record the reason for disposal.
- Reconcile the fixed asset ledger to the annual financial report.

Section 3-D:

## **Accounts Payable Clerk Performs Incompatible Functions and Lacks Essential Automated Processes**

The accounts payable department is the center of the College's accounting operations. The accounts payable clerk processes purchase orders, receives invoices, prints and mails checks, takes phone calls from vendors who have not been paid, maintains vendor files, makes bank deposits, prepares monthly reports, and occasionally assists other departments. The accounts payable clerk has an unmanageable workload not only because of the volume of activity, but also because of the manual operations she performs which could be automated.

For example, in order to process the weekly accounts payable check run, the clerk manually prepares a check request for each vendor listing the following items:

- vendor identification number
- invoice number
- payee name
- invoice date
- date
- purchase order number
- total vendor amount
- account number

This manual operation takes between 16 and 20 hours per week and could be converted to a simple automated printout. Other manual operations include:

- separating and sorting checks
- signature stamping of each check one at a time
- stuffing checks in envelopes

Many tasks could be automated, thus saving an estimated 30 hours per week, eliminating the accounts payable backlog, and preventing unnecessary overtime. In addition to these time-consuming manual tasks, the accounts payable clerk uses her private automobile to take deposits to the bank daily without security.

Also, the accounts payable clerk performs incompatible functions. The combined functions of purchase order processing, invoice processing, and check printing and mailing are internal control weaknesses which creates a risk of fictitious vendor payments. Since invoices are not defaced or marked "paid," the possibility exists for duplicate payments.

There is no backup for the accounts payable clerk although this position is critical to the operation of the Business Office. If the clerk is absent for annual or sick leave, the work builds up, and overtime is required upon return. Also, if the clerk were to terminate employment, there would be no immediate replacement.

Recommendations:

We recommend that the Business Office:

- Discontinue the practice of manually preparing check requests.

- Automate, when practical, the functions of check printing, signing, separating, sorting, and stuffing.
- Provide a method for defacing invoices or stamping “paid” on each invoice.
- Separate the accounting functions of invoice preparation and check printing and mailing.
- Provide other means of making banking deposits such as using the College’s security officer.
- Provide cross training to provide a backup to the accounts payable clerk.

Section 3-E:

**Accounts Receivable Billings Are Not Timely, and the Accounts Receivable Clerk Performs Incompatible Clerical Functions**

As of November 2, 1995, billings for Job Training and Partnership Act (JTPA) and Texas Rehabilitation Commission expenditures were one month delinquent. The amount of this arrearage in billings is approximately \$53,000. Accounts receivable billing is not timely because the billings have to be approved by the controller who often does not have time to immediately process the forms.

The incompatible accounts receivable clerical functions of physical and accounting control provide an opportunity for misappropriation of funds with the ability to conceal the action through accounting entries. Although mail is opened by another employee, the accounts receivable clerk logs the checks, restrictively endorses the checks, and maintains the accounts receivable records.

Recommendation:

We recommend that the billing process not require controller approval in order to expedite this process. We also recommend that the functions of logging and restrictively endorsing checks be transferred to another person.

Section 3-F:

**Payroll Clerk Performs Incompatible Functions**

The payroll clerk performs incompatible functions of processing, printing, and delivering checks as well as maintenance of payroll accounting records.

The payroll clerk individually stamps a signature on each payroll check with a manual check signing machine. Approximately 250 checks are individually machine signed each month. Then, the checks are manually signed by an authorized person.

There are no written procedures for payroll operations. However, the director of personnel is familiar with the process and could fill in if necessary.

The payroll clerk also performs personnel functions such as maintenance of personnel files. A review of personnel files revealed that the contents of these files are inconsistent. Figure 2 represents a list of required items in personnel files and the frequency of appearance.

Figure 2

Required Item	Frequency of Appearance in Files
Applications	Sometimes
Transcripts	Rarely
Terms of Employment	Rarely
Contracts	Never
Salary Adjustments	Sometimes
Job Descriptions	Rarely
Evaluations	Almost Never No evaluations have been performed since 1989.

In spite of these deficiencies, there is no ongoing effort to include missing items in personnel folders.

Recommendations:

We recommend the following:

- Include required missing items in the personnel folders.
- Printing and distributing checks should be performed by someone other than the payroll clerk.
- Develop policies and procedures for the payroll and personnel function, including a list of what should and should not be included in the personnel files.

Section 3-G:

**Northeast Texas Community College Information System Fails to Provide Essential Information on a Timely Basis**

Northeast Texas Community College employs a full-time director of computer services, pays a service company \$18,000 annually for software maintenance, and pays \$6,000 per year for hardware maintenance. In addition, a new computer system was purchased in 1993 at a cost of more than \$200,000. This system was designed to be a complete financial and student services software system. In spite of these expenditures, essential information is not available to users on a timely basis, if at all. For example:

- Scholarship account balances are not available except by manual calculations.
- Cash flow forecasts are prepared manually.
- There is no income statement information for food services department and bookstore operations.
- Academic departments complain about a lack of timely budget information.
- The bookstore and food service operations are not tied into the computer.
- There is no Local Area Network (LAN) for interdepartmental communication.
- The fixed asset system software has not been programmed to provide for deletion of assets.
- Departments are not able to query the information system or prepare ad hoc reports.
- The purchasing system is not automated for departmental users.
- Until October 1995, the business software was not capable of preparing an accurate aged accounts payable report.

As a result of this lack of timely information, departments have created their own unique accounting and information systems. The controller writes his own programs rather than request programming assistance from the director of computer operations. Also, since information concerning Foundation account balances is not readily available, the perception among some staff and external donors is that these funds are misappropriated. As a consequence, donations have dwindled.

Recommendation:

In order to restore confidence in the Business Office and to provide timely, accurate information to the Board of Trustees, we recommend that a user needs survey be conducted and that the director of computer operations be actively involved in programming and procuring college hardware and software systems.

Section 4:

**Accounting for the Foundation's Scholarship and Endowment Funds Is Inadequate, and There Has Been Little Oversight by the Foundation's Board**

Section 4-A:

**Fundamental Accounting for the Foundation Has Been Neglected**

Although the assets of the Northeast Texas Community College Foundation are significant, accounting for the transactions and balances involving these assets is neglected. According to unaudited Business Office records, Foundation assets were valued at more than \$220,000 as of August 31, 1995. These balances may not be accurate because although Foundation financial transactions are recorded in the College's accounting system, this system is not capable of compiling financial statements and account balances for individual scholarship funds. Consequently, 13 of 34 scholarship funds were so overawarded that they had deficit balances as of November 1, 1995.

The Foundation's endowment and scholarship fund balances and investment balances are updated infrequently. As of November 1, 1995, endowment fund balances were updated through August 31, 1993, on a spreadsheet which is separate from the mainframe accounting system. The last two scholarship fund balance reports were prepared on spreadsheets in May 1994 and March 1995.

An audited annual financial report has not been submitted for the Foundation since fiscal year 1990. An audit of the Foundation covering fiscal years 1991 through 1994 is in progress and was released in December 1995. The fiscal year 1995 audit was completed in January 1996.

Another example of the inadequacies of Foundation accounting is the failure of the Business Office to draw funds from the Foundation to pay for awarded scholarships. When Foundation scholarships are provided to students, their tuition is reduced by the amount of the scholarships, but no transfer of cash occurs. An accounting entry is made to recognize the amount due from the Foundation, but funds are not forwarded to the College.

The amount due the College has accumulated over years, and payments to the operating fund to cover the balance owed have been infrequent. As a result, the balance owed to the College is usually significant. In June 1994, the amount owed the College by the Foundation was more than \$113,000. When funds were finally transferred, all the money was erroneously taken from one scholarship fund instead of allocating the withdrawals from the proper funds. As a result, that fund was overdrawn by \$45,068.

Another example of inadequate accounting of Foundation balances is the failure to reconcile Foundation bank accounts. Foundation bank account reconciliations were not made in a timely manner until June 1995. As a result, numerous correcting entries and transfers occurred when performing the June 1995 bank reconciliation. Formal reconciliations of the money market account for endowment investments are still not prepared.

Section 4-B:

### **Oversight of Foundation Activities by the Foundation's Board Has Been Almost Non-Existent**



The Foundation's Board has been inactive since its last meeting on May 6, 1993. There are only three other documented meetings of the Foundation's Board since its inception in 1984: January 14, 1985; June 21, 1989; and February 24, 1992. The current chair of the Board of Directors for the Foundation is not certain who the other board members are. The College's auditing firm is attempting to determine the members of the Board in order to complete the annual financial report for the Foundation.

As a result of the lack of monitoring and updating scholarship and endowment balances, the Business Office has been unable to provide reliable and current information on a timely basis to users such as donors, faculty, and Foundation staff. These users are unable to get this information within a reasonable time, even after making repeated requests to Business Office personnel. It is particularly difficult for users to obtain a written report or accounting of endowment or scholarship activity. As a result, scholarships are sometimes overawarded, and, in some cases, funds available are not utilized.

Recommendations:

In order to provide for the safeguarding of Foundation assets as well as to ensure accurate and timely reporting of transactions, we recommend the following:

- Implement system controls which automatically update endowment and scholarship fund balances at least monthly. This could be performed in conjunction with the monthly closing of the accounting records. This would also help prevent the overawarding of scholarships.
- Report endowment and scholarship activity and balances to faculty, the Financial Aid Office, and Foundation staff at least monthly. Consideration should also be given to providing annual statements of endowment and scholarship activity and balances to donors.
- Regularly monitor endowment and scholarship balances and implement controls to prevent the overawarding of scholarships.
- Fund scholarships and pay the corresponding tuition when scholarships are provided to students.
- Conduct regular meetings of the Foundation's Board and document and maintain meeting minutes. In addition, assign sufficient personnel resources to properly administer and manage the Foundation's funds.
- Promptly correct errors in the Foundation's accounting records.
- Prepare formal monthly reconciliations of the money market account for endowment investments.

## **The Legality of Certain Business Office Transactions Is Questionable**

During our audit of the internal controls of Northeast Texas Community College, we noted some activities which were potentially illegal. The actions involve bookstore operations, grants billing procedures, and the payment of non-college debt with college funds.

Section 5-A:

### **Beginning in 1992, the College Bookstore Was Used as a Channel to Fund College Operations through Fictitious Grants Billing**

A highly questionable credit scheme involving the bookstore which began in 1992 continued to fund college operating costs until July 1995. Federal and state grants with unexpended funds which were about to expire during 1992 and 1993 were charged for supplies for the balance of the grant. The supplies were apparently not delivered. Instead, an entry was made in a "credit book" maintained in the bookstore which listed the grant, account number, credit amount, and date of the credit. The fictitious charges were reported to the federal or state granting agency as having been expended. In subsequent years, purchases were made from the bookstore and charged to these credits. The subsequent purchases were not used for grant purposes, but rather to supply other departments. In July 1995, the credit scheme was abandoned, not because it was questionable or unethical, but because the credit book was lost.

Section 5-B:

### **Business Office Officials Inappropriately Reported Federal Grant Monies as Local Matching Funds to Obtain Additional Revenue**

Local matching funds are expenditures from local sources which are matched with federal funds. According to the College's external auditors, federal Housing and Urban Development funds were erroneously recorded as local matching funds in an expenditure report to the U.S. Department of Defense grant administrator. This erroneous billing resulted in excess reimbursement to the College of approximately \$20,000 in fiscal year 1994.

Section 5-C:

### **College Funds Were Used to Pay Debts of the Athletics Booster Club**

In August 1994 and again in March 1995, individual payments of \$21,242 were made to Guaranty National Bank to meet the obligation of a note signed by a booster club president. Although the note was partial payment of the construction of the College's baseball field, the booster club is not part of the College, and no college official signed the note. Therefore, there is no obligation on the part of the College to pay this amount. The vice president of administrative services authorized the payment, and the

controller approved the payment. The Board of Trustees was not notified of the payment by the Business Office until it was discovered by the auditing firm.

Recommendation:

Although we do not believe that referral for prosecution is warranted for the above actions, we recommend that the College contact the relevant grantor agencies to determine if restitution is required.

**Management's Response**

Management's Response to An Audit Report on

**Management Controls at  
Northeast Texas Community College**

**President's Office  
Charles B. Florio, Ph.D.**

**January 1996**



# NORTHEAST TEXAS COMMUNITY COLLEGE

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*Office of the President*

## **Preface**

Thank you very much for giving the management of Northeast Texas Community College the opportunity to respond to the draft of An Audit Report on Management Controls at Northeast Texas Community College. Our objective of the response is to have an accurate, complete, objective, and fair report and response. We are sure the personnel of the Office of the State Auditor share these objectives.

Management means the members of the College's Deans' Council who are the president, interim vice president for instructional services, interim vice president for administrative services, vice president for student services, dean of continuing education, dean of adult and developmental education, dean of admissions and registrar, dean of plant services, public information officer, and assistant to the president. Please note that the former vice president for administrative services also contributed to management's response.

We appreciate the State Auditor's acknowledgement in the first paragraph of the executive summary that since the departure of the former president some improvements have been initiated in financial and management controls. These improvements, among others, include:

1. Elimination of the petty cash fund.
2. Elimination of excessive discounts for administrators at the College bookstore.
3. Completion by December 30, 1995, of the backlog of College and College Foundation audit reports.
4. Resumption of College Foundation Board of Directors meetings. One meeting was held December 21, 1995, and another is scheduled for January 24, 1996. The former meeting was to effect the acceptance of a \$65,000 gift and the sale of surplus land.
5. Development of a truly ageing accounts payable monthly report, first presented to the Board of Trustees at its October, 1995, meeting.
6. Development of a cash flow forecast monthly report, first presented to the Board of Trustees at its November, 1995, meeting.

7. Establishment on November 3, 1995, of a \$300,000 line-of-credit with the College's depository bank.
8. Elimination on October 30, 1995, of incurring non-sufficient fund charges to the operating checking account.
9. Adoption by the Board of Trustees at its December, 1995, meeting of a revised Fiscal 1996 College Budget, which provides for a more realistic projection of College revenues.
10. Billed contracted baseball field boxseat holders and outfield sign holders for their 1996 payments. To date the baseball booster club has collected approximately \$7,000.
11. Built an Americans with Disabilities Act specified walkway to the baseball field for access to the disabled and other patrons.
12. Scheduled construction in February of a fence around the baseball field which will control access and permit the College to charge for admission.
13. Developed a new democratically driven budget preparation process which should produce more realistic budgets in the future.
14. Employed in August, 1995, an additional accountant who has a successful career as an auditor, accounting manager, controller, and administrator. She is a CPA.
15. Employed in December, 1995, a highly experienced recently retired chief fiscal officer from Midland College who will serve in an interim capacity as chief fiscal officer.
16. Filed revised Fiscal 1996 College Budget with the three counties in the district and College library.

Also, we sincerely appreciate the State Auditor noting the improvement in communication concerning the board of trustees, faculty, and staff.

Section 1:

**Management override by the former president and inadequate supervision by the Board of Trustees has resulted in fiscal mismanagement of College assets.**

Management acknowledges the State Auditor's report concerning the former president, which is a matter of public record. The management chooses not to respond to the statement that .... "inadequate supervision by the Board of Trustees has resulted in fiscal mismanagement of College assets" as it feels it is inappropriate for management to characterize the Board of Trustees.

The management of NTCC accepts the three suggestions made by the State Auditor, that is, we will suggest appropriate training for our Board of Trustees, and prepare and implement a financial and operational performance action plan addressing the State Auditor's findings and conclusions and his recommendations based on same. We accept the Texas Higher Education Coordinating Board's monitoring of this plan for timely compliance.

Section 2:

**Questionable business decisions, inaction by the business office, and poor cash management have placed a financial strain on the College.**

**Questionable business decisions**

***Increased Debt***

In regard to the statement that the College's tax revenue has been decreasing since the founding of the College, debt has continued to grow, there are other factors which should be considered. According to Table 1, derived from the College's annual financial statements in 1986 and 1994, the College's operating revenues have increased approximately 72.42 percent during its first nine full years of operations. Thus, total revenue is increasing.

Table 2 shows a decline in tax base value of approximately \$450 million, a decrease of 18%. During the same time frame, cumulative inflation totals more than 40%. The effect of a tax cap, declining tax base, and cumulative inflation means that the College receives 60% less in taxes than in 1985. The Board of Trustees, through very thoughtful bond refundings, has decreased the negative impact of these combined forces.

Table 3 displays the College's general obligation debt schedule with changes from bond refundings. The table shows an increase in general obligation debt of 29%, less than half the decrease in tax revenues. Since state law does not allow expenditure of state appropriations on the construction of buildings, or for their maintenance and operations, local taxes are used for interest and sinking payments and physical plant operations as well as for instructional programs.

In regard to the statement that *tax resources have dwindled, long term debt of the College has continued to grow*, the soundness of bond issues is, of course, determined by their revenue source. The revenue bonds listed do not use taxes as a revenue source. The sources of revenue for these issues have not dwindled, and, in fact, have actually increased as documented in Table 1. Obviously, some debt is tax based and some debt is revenue based. Although the tax base resource has decreased, the revenue base resources have increased.

***Athletic funding and reporting***

This information is essentially correct and management agrees with these findings.

The College agrees that the athletic costs should be included in the auxiliary area and will so budget and report in the future. The College will also solicit athletic scholarship funds as it does academic scholarship funds. There are no funds which were donated for athletic scholarships. Currently, athletic scholarships cost the College approximately \$90,000 annually. Most of this amount is funded from bookstore profits and the remainder from student services fees. Their respective contributions will be determined in the future. Please note that the current athletes (96) generate approximately \$175,000 per year in contact hour reimbursement, according to a study prepared by the director of institutional effectiveness (research).

***Pay Raises***

Management agrees with these findings.

***Writing checks without sufficient funds***

Management agrees with this finding. Incurring insufficient fund penalty charges is obviously irresponsible. Writing checks without sufficient funds was discontinued in October when the interim president learned of this activity.

***Inaction by the Business Office***

***Failure to file the annual financial report timely***

Management agrees with these findings. (Please see item 3, page 1.)

***Failure to file budget documents with the required counties.***

Management agrees with this finding. (Please see item 16, page 2.)

***Failure to complete transfer and sale of donated stock certificates.***

Management agrees with this finding. (Please see item 4, page 1.)

***Failure to implement audit recommendations.***

Management agrees with this finding. (Please see item 17 of Proposed Improvements to the Financial Management Control of NTCC - Appendix A.)

***Failure to follow up on the implementation of a line of credit.***

Management agrees with this finding. (Please see item 7, page 1.)



## **Poor Cash Management**

***Northeast Texas Community College has been unable to pay its bills on time due to a lack of cash forecasting, failure to provide timely billing, and unauthorized expenditures.***

Management essentially agrees with this finding. However, it wishes to note that if there had been adequate cash forecasting, timely billing of receivables, no unauthorized expenditures, and a line of credit or revenue anticipated notes, the College would have been able to pay its bills in a timely manner. The point that management desires to emphasize is that the College had the ability to meet its financial obligations. Knowledge of this fact is important in terms of retaining and recruiting high quality faculty, maintaining the confidence of bond holders, and maintaining institutional viability in the minds of students and prospective students and their parents. Management is concerned with these factors if the public "perceives" rightly or wrongly that the College is unable to pay its bills. NTCC is an important entity to the people in rural Northeast Texas.

***Although business officers have known of the poor financial condition of the College, this information has not been provided to the Board of Trustees. Each month the financial information provided by the business office for board meetings has given the impression that all is well financially.***

Board minutes will show that the former Vice President for Administrative Services told the board that some cost-reimbursement grants are among the most significant reasons for cash flow problems, that he continually updated the board concerning the declining tax base, and that he advised the board not to approve a salary increase in January, 1995, because the only source would be the funds budgeted to go to fund balance. Board minutes will also show that he presented past audits showing a negative fund balance in current unrestricted funds. Financial reports submitted to the board will show that he has presented negative general ledger operating cash balances every time they occurred. However, he should have provided other relevant and significant financial information to assist the trustees. Also, the former president still recommended expenditures in spite of the above information. In essence, all essential financial information was not disclosed to the trustees.

***The accounts payable ageing which is supposed to reflect how old the past due bills are, has shown that there are no overdue invoices.***

Management agrees with this finding. However, please note that the former controller developed a true accounts payable ageing report when requested in September, 1995, and he presented it to the Board of Trustees at its October, 1995, meeting.

***If the board members had been given accurate, timely, and relevant financial information the current cash problems could have been adequately addressed.***

Please see the above section on monthly financial information.

***The College billing clerk reports that the College is more than 30 days late billing the state for more than \$50,000.***

Management is unsure of this finding and will investigate.

***Bills to local merchants for advertising in the College newspaper for the spring of 1995 still have not been prepared.***

Management agrees with this finding. Billing will be done on a timely basis.

***Ticket sales for baseball .....***

Management agrees with this finding. The College will change admission to baseball games in the future.

***Recommendation: Aggressively pursue other financial resources such as sales of idle assets and unrestricted donated properties.***

Management agrees to implement the recommendations made by the State Auditor regarding the improvement of cash management by the business office.

Section 3:

**Significant internal control problems exist in all areas audited at Northeast Texas Community College.**

***Bookstore Operations***

Management agrees with these findings and it will consider the State Auditor's two recommendations regarding the bookstore. Never the less, management pledges to charge the same markup for academic departments and grant departments.

***Food Service***

Management agrees with these findings and will implement the State Auditor's recommendation.

***Fixed Assets***

***The value of the College's fixed assets may not be accurate because no physical inventory has ever been taken.***

Management agrees with this finding. Please note that the College will conduct an inventory this coming Spring as recommended by the State Auditor and the College's independent auditor.

The College agrees to implement the four (4) recommendations in regard to fixed assets.

***Accounts Payable***

***The accounts payable clerk .... maintains vendor files, makes bank deposits, prepares monthly reports, and occasionally assists other departments.***

Please note that the accounts payable clerk does not make the bank deposits any longer.

***Provide a method for defacing invoices...***

A review of accounts payable procedures and computer system design will be conducted to determine needed changes. Additional training will emphasize adherence to established procedures for purchasing, receiving, and invoice payment.

***Provide other means for making bank deposits...***

This has already been done. (Please see above.)

***Discontinue the practice of manually preparing check requests. Automate when practical...***

The Board of Trustees adopted policies at its December 21, 1995, meeting that implement these two recommendations.

***Accounts Receivable***

Management agrees with these findings and will implement the state Auditor's two recommendations in regard to accounts receivable.

***Personnel/Payroll***

Management recognizes that significant improvement is needed concerning personnel records. We accept the State Auditor's three recommendations in regard to Personnel/Payroll. We will also review personnel policies to determine needed revisions and additions for proper personnel administration.

***Information Management***

***In spite of these expenditures, essential information is not available to users on a timely basis, if at all. For example:***

Management essentially agrees with these findings.

***As a result of this lack of timely information, departments have created their own unique accounting and information systems.***

Departments had already created their own unique accounting and information systems before the College purchased its current software. Many departmental personnel develop records to provide additional management control, because the departments have their own records with which to reconcile the G/L detail. Thus, creation of these systems is not necessarily because of lack of timely information.

Management will conduct a user needs survey concerning the information system as recommended by the State Auditor.

Section 4:

**Accounting for the Foundation's scholarship and endowment funds is inadequate and there has been little oversight by the Foundation board.**

Management essentially agrees with these findings and accepts the State Auditor's seven recommendations.

The Foundation Board of Directors was recently mailed by Thomas and Thomas two formal financial reports of the Foundation for years 1991 through 1994 and the year 1995.

Management will implement the State Auditor's seven recommendations regarding the safeguarding of Foundation assets as well as to insure accurate and timely reporting of transactions.

Section 5:

**The legality of certain business office transactions is questionable.**

***Bookstore Operations***

Project directors will be trained in the requirements for grant expenditures and will be informed that responsibility for adhering to grant expenditure regulations will be part of their job responsibilities. In addition, the Business Office will monitor expenditures to further insure compliance with grant regulations. The various agencies involved in making inappropriate reimbursements will be contacted and an effort made to negotiate settlement of any overpayment, either by repayment or adjustment.

***Grants Billing (Matching Funds)***

As stated above regarding Bookstore credits, grant project directors will be trained in grant regulations and notified that compliance with those regulations will be one of their job responsibilities. The Department of Defense will be contacted and a negotiated settlement made with the agency for repayment or adjustment.

***Payment of Non-College Debt with College Funds.***

The College will not make any future payments on the Eagle Booster Club note. In addition, outfield advertisers have been billed and some \$7,000.00 has been received. All advertisers will continue to be billed on a timely basis. All advertising revenue as well as other revenue generated by baseball games will be deposited in the Booster Club bank account. As funds are collected, the first priority on those funds will be to pay future note payments. If any funds are in excess of note payment obligations, the College will request repayment of the receivable at the College. To improve income from box seat and admission ticket sales, a fence around the field is being planned for installation this year.

## Appendix A

### **Proposed Improvements to the Financial Management Controls of Northeast Texas Community College**

The management of Northeast Texas Community College makes the following pledges to the Office of the State Auditor in regard to how it will do business in the future:

1. The College will conduct internal investigations of any future alleged wrongdoing based on known witnesses and substantiated claims.
2. The College Foundation will hold at least semi-annual meetings to conduct its business.
3. The College will actively solicit private donations for athletic scholarships in addition to academic scholarship.
4. The College will over the next three years significantly reduce the percentage of athletic scholarships funded from institutional funds.
5. The College will budget athletic expenditures with auxiliary enterprises.
6. The College will adopt an administrative policy that no one is to expend funds not budgeted without the express written approval of the president.
7. The College will notify all financial institutions in its taxing district that the bid specifications to be the College's depository bank in the future will include automatic transfer of funds from operating savings accounts to the operating checking account.
8. The College will resume billing holders of baseball box seats.
9. The College has resumed billing of businesses and industries who have contracted for outfield signs. To date, over \$7,000 has been collected. The president of the Eagle Booster Club and the head baseball coach are very actively seeking payment of these pledges at this time.
10. The College baseball booster club opened a bank account for in which to deposit outfield sign revenue. Payments to pay off the note which partially funded the building of the baseball field will be made from this account in the future.
11. The College will prepare and file all of its required financial reports in a timely manner.

12. The College will continue to prepare a cash flow forecast report on a monthly basis for the Board of Trustees and for use in financial planning and management.
13. The College will prepare quarterly profit and loss statements for auxiliary enterprises, e.g., bookstore, food service.
14. The College will develop and implement policies concerning personnel documents and administration.
15. The College will file budget and audit reports in the three district court houses and in the College library in a timely manner.
16. The College will accept all Foundation gifts of negotiable instruments in a timely manner and convert them to useable form in a reasonable and prudent manner.
17. The College will conduct an inventory of its equipment prior to June 1 and will maintain an accurate and up-to-date inventory.
18. The Security personnel of the College will continue to transport all deposits to the depository bank.
19. Grant project directors will be trained in the requirements for grant expenditures and will be informed that responsibility for adhering to grant expenditure regulations will be part of their job responsibilities. Their job descriptions will be revised accordingly. In addition, the Business Office will monitor expenditures to further insure compliance with grant regulations.

**Appendix B**

**Proposed Plan to  
Increase Financial Reserves  
of  
Northeast Texas Community College**

The following plan is proposed to increase the college's financial reserves by more than \$100,000 before the end of this fiscal year.

1. Increase in student fees and tuition by approximately 10% effective Summer, 1996, which should yield approximately \$160,000 for fiscal year 1997.
2. Decrease current budget (except personnel) by 1%, which should yield approximately \$35,000.
3. Appropriate excess departmental budget balances in May -- \$25,000.
4. Sell surplus Foundation property and College equipment -- \$45,000 and \$5,000 respectively.

Also, the College will budget \$125,000 in reserves each year until capital and interest reach \$1,000,000.

Table 1

Northeast Texas Community College  
Analysis of Changes in Revenues

<u>Revenue Source</u>	<u>1985-86</u>	<u>1993-94</u>	<u>% Change</u>
State Funds	2,342,125	3,151,761	34.57%
Federal Funds	185,381	49,020	-73.58%
Tuition and Fees	329,918	1,885,936	471.64%
Local Taxes	896,280	1,259,751	40.55%
Other Income	129,264	348,498	169.60%
* Auxiliary Income	N/A	N/A	
	<u>3,882,968</u>	<u>6,694,966</u>	72.42%

Source: Northeast Texas Community College Financial Statements, 1986 and 1984

\* Auxiliary Income offset by Auxiliary Expenditure commitments.



Table 2

Northeast Texas Community College  
Tax Base/Revenue Analysis

Fiscal Year Ended 8/31	Taxable Assessed Valuation	Tax Split		Tax Generation		
		Local Maintenance	Interest & Sinking	Local Maintenance	Interest & Sinking	Total Taxes
1985	2,545,207,704	0.063	0.037	1,603,481	941,727	2,545,208
1986	2,456,376,000	0.064	0.036	1,572,081	884,295	2,456,376
1987	2,342,096,000	0.042	0.058	983,680	1,358,416	2,342,096
1988	2,258,346,446	0.045	0.055	1,016,256	1,242,091	2,258,346
1989	2,306,983,780	0.046	0.054	1,061,213	1,245,771	2,306,984
1990	2,267,419,970	0.049	0.051	1,111,036	1,156,384	2,267,420
1991	2,159,740,740	0.0442	0.0558	954,605	1,205,135	2,159,741
1992	2,207,606,000	0.057	0.043	1,258,335	949,271	2,207,606
1993	2,186,438,000	0.0575	0.0425	1,257,202	929,236	2,186,438
1994	2,182,002,356	0.0576	0.0424	1,256,833	925,169	2,182,002
1995	2,080,659,583	0.0633	0.0367	1,317,058	763,602	2,080,660
1996	2,077,278,003	0.0548	0.0452	1,138,348	938,930	2,077,278

Table 3  
 NORTHEAST TEXAS COMMUNITY COLLEGE  
 GENERAL OBLIGATION DEBT SERVICE RECAP  
 AUGUST 1994

YEAR ENDED 8/31	1984 ORIGINAL ISSUE	1986 REFUNDING	1991 REFUNDING	1994 REFUNDING
1985	1,049,540 *			
1986	1,356,875 *			
1987	1,344,375	738,757 *		
1988	1,375,875	1,194,190 *		
1989	1,374,875	1,192,615 *		
1990	1,367,875	1,190,615 *		
1991	1,354,875	1,228,255 *		
1992	1,359,375	1,412,980	899,420 *	
1993	1,363,275	1,413,430	899,858 *	
1994	1,342,925	1,416,350	895,938 *	
1995	1,363,675	1,425,700	897,837	897,837 *
1996	1,372,963	1,400,000	1,544,638	994,638 * **
1997	1,370,675	1,400,000	1,544,637	994,637 * **
1998	1,356,800	1,450,000	1,594,638	994,638 * **
1999	1,473,500	1,450,000	1,594,637	994,637 * **
2000		1,500,000	1,644,638	994,638 * **
2001		1,500,000	1,644,637	994,637 * **
2002			824,638	1,069,638 * **
2003			824,417	1,064,417 * **
2004			821,205	1,071,205 * **
2005				1,070,000 * **
2006				1,070,000 * **
2007				1,070,000 * **
2008				1,070,000 * **
2009				1,070,000 * **
Original Payout	20,227,478		* Updated Payout	26,066,985
			** Payments Outstanding	14,523,085

## **Objective, Scope, and Methodology**

### **Objective**

Our audit objective was to determine the financial stability of Northeast Texas Community College and to review the internal controls over operations. This audit evaluated the control systems in place as of October 31, 1995.

The evaluation focused on answering the following questions:

- Does the Board of Trustees of the College provide adequate oversight and monitoring of fiscal operations?
- Does Northeast Texas Community College have the financial resources to meet its current and long-term obligations?
- Are internal controls over fiscal and administrative operations sufficient to protect the College's assets and provide for efficient operations?
- Are assets of the College Foundation adequately monitored, recorded, and reported?

### **Scope**

The scope of this audit included consideration of College's policy management, information management, and resource management.

Evaluation of policy management included a review of:

- strategic planning for financial operations and information management
- the role of the Board of Trustees in monitoring and supervising fiscal operations
- policies and procedures necessary to provide internal controls over fixed assets, accounts payable, accounts receivable, purchasing, and human resources

Consideration of the College's information system included an evaluation of the accuracy and completeness of fiscal information provided to the Board of Trustees and to the College president.

Consideration of resource management included a review of:

- human resources - the processes, policies, and procedures to ensure that employees have the skills, knowledge, and training to perform their jobs and that their performance is adequately monitored, evaluated, and reported
- cash - balances are monitored and reported to management

- fixed assets - assets are economically purchased or constructed, economically used, and protected against waste and abuse

## **Methodology**

The audit methodology consisted of collecting information, performing audit tests and procedures, analyzing the information, and evaluating the information against pre-established criteria.

Information collected to accomplish our objectives included the following:

- Interviews with the College's Board of Trustees, administration, and staff
- Documentary evidence such as:
  - various management reports
  - audited financial reports
  - Junior College Data Base
  - Titus County court records
  - transcripts of Texas Ranger interviews
  - bank statements
  - vendor invoices
- Agency-generated data on accounts payable and bank balances

Procedures and tests conducted:

- Statistical analysis of annual financial report
- Process flowcharting and review
- Comparison of cash forecasts to historical records

Fieldwork was conducted from September 17, 1995, through November 25, 1995. The audit was conducted in accordance with applicable professional standards, including:

- Generally Accepted Government Auditing Standards
- Generally Accepted Auditing Standards

There were no significant instances of noncompliance with these standards.

The audit work was performed by the following members of the State Auditor's staff:

- Aubrey Smart, CPA (Project Manager)
- Chuck Dunlap, CPA
- Bernie Gilmore, CPA (Audit Manager)
- Deborah Kerr, Ph.D. (Director)

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