

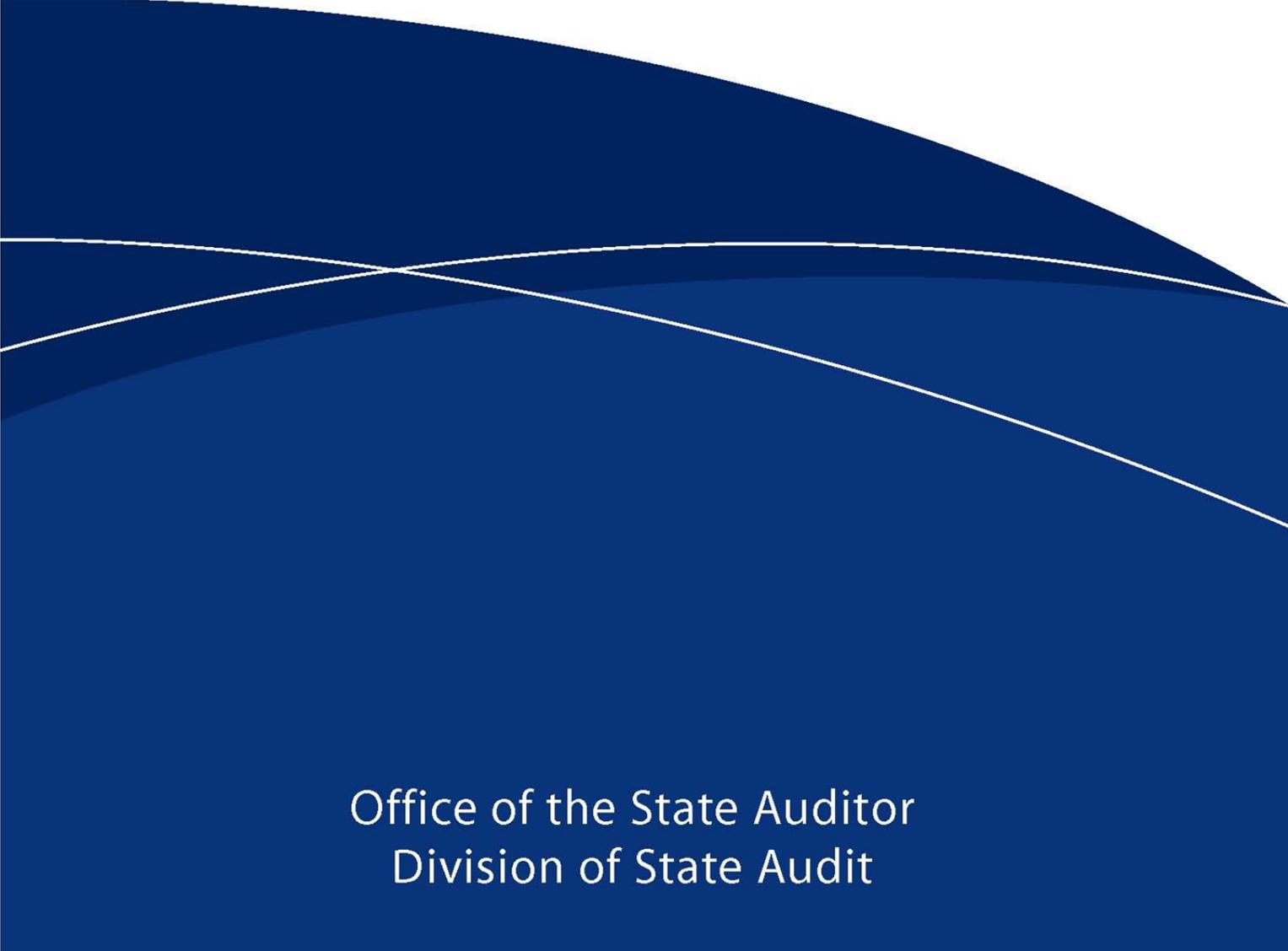
LAKE REGION STATE
COLLEGE

DEVILS LAKE, NORTH DAKOTA

Audit Report

For the Biennium
June 30, 2011

ROBERT R. PETERSON
STATE AUDITOR



Office of the State Auditor
Division of State Audit

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Transmittal Letter

May 29, 2012

The Honorable Jack Dalrymple, Governor
Members of the North Dakota Legislative Assembly
North Dakota State Board of Higher Education
Dr. Mike Bower, President, Lake Region State College

We are pleased to submit this audit of Lake Region State College for the biennium ended June 30, 2011. This audit resulted from the statutory responsibility of the State Auditor to audit or review each state agency once every two years. The same statute gives the State Auditor the responsibility to determine the contents of these audits.

In determining the contents of the audits of state agencies, the primary consideration was to determine how we could best serve the citizens of the state of North Dakota. Naturally we determined financial accountability should play an important part of these audits. Additionally, operational accountability is addressed whenever possible to increase efficiency and effectiveness of state government.

The in-charge auditor for this audit was Robyn Hoffmann, CPA. John Grettum, CPA, was the audit manager. Inquiries or comments relating to this audit may be directed to the audit manager by calling (701) 239-7289. We wish to express our appreciation to President Bower and his staff for the courtesy, cooperation, and assistance they provided to us during this audit.

Respectfully submitted,

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

Robert R. Peterson
State Auditor

Executive Summary

Introduction

Lake Region State College is a student-centered, open access, comprehensive community college within the North Dakota University System. The College provides quality academic education, vocational/technical training, workforce training, educational outreach opportunities, and life-long learning.

The Legislative Audit and Fiscal Review Committee (LAFRC) requests that certain items be addressed by auditors performing audits of state agencies. Those items and the Office of the State Auditor's responses are noted below.

Responses to LAFRC Audit Questions

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

The financial statements for Lake Region State College were obtained from the Annual Financial Report of the North Dakota University System; however, the related note disclosures are not included in accordance with generally accepted accounting standards, so an opinion is not applicable. An unqualified opinion was issued on the annual financial report of the North Dakota University System.

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

Other than our finding addressing "noncompliance with procurement laws" (page 17), Lake Region State College was in compliance with those significant statutes, laws, rules, and regulations under which it was created and is functioning that we subjected to testing.

3. Was internal control adequate and functioning effectively?

Other than our finding addressing "purchase cards" (page 14), we determined internal control was adequate.

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 prior audit reports?

Yes.

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

No.

LAFRC Audit Communications

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

As of June 30, 2011, Lake Region State College began reporting the receipt and disbursement of student financial aid on the Statement of Cash Flows as Direct Lending Receipts and Direct Lending Disbursements. Prior to June 30, 2011, these amounts were included net on the Statement of Cash Flows as Agency Fund Cash Increases/Decreases. We noted no reportable management conflicts or interests, no contingent liabilities were identified or any significant unusual transactions.

- 8. 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.*

The most significant accounting estimates used by Lake Region State College include the useful lives of capital assets and allowance for uncollectible receivables. Estimated useful lives are used to compute depreciation on capital assets and are based on industry standards and guidelines. Management's estimate of the allowance for uncollectible receivables is based on aging categories. We evaluated the key factors and assumptions used to develop the allowances in determining that it is reasonable in relation to the financial statements taken as a whole.

- 9. Identify any significant audit adjustments.*

None.

- 10. 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.*

None.

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

None.

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

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

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

None.

14. 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 Student Administration are high-risk information technology systems critical to Lake Region State College. No exceptions related to the operations of the information technology system were noted.

Audit Objectives, Scope, and Methodology

Audit Objectives

The objectives of this audit of Lake Region State College for the biennium ended June 30, 2011 were to provide reliable, audited financial statements and to answer the following questions:

1. What are the highest risk areas of Lake Region State College's operations and is internal control adequate in these areas?
2. What are the significant and high-risk areas of legislative intent applicable to Lake Region State College and are they in compliance with these laws?
3. Are there areas of Lake Region State College's operations where we can help to improve efficiency or effectiveness?

Audit Scope

This audit of Lake Region State College is for the biennium ended June 30, 2011. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Lake Region State College has operations in the following locations. Each location was included in the audit scope:

- Main campus in Devils Lake
- Grand Forks Air Force Base campus

Audit Methodology

To meet the objectives outlined above, we:

- Prepared condensed financial statements from the fiscal years 2011 and 2010 annual audited financial reports of the North Dakota University System and developed a discussion and analysis of the financial statements.
- Performed detailed analytical procedures including computer-assisted auditing techniques. These procedures were used to identify high-risk transactions and potential problem areas for additional testing.
- Tested internal control and compliance with laws and regulations which included selecting representative samples to determine if controls were operating effectively and to determine if laws were being followed consistently. Non-statistical sampling was used and the results were projected to the population. Where applicable, populations were stratified to ensure that particular groups within a population were adequately represented in the sample, and to improve efficiency by gaining greater control on the composition of the sample.
- Interviewed appropriate agency personnel.
- Queried the ConnectND (PeopleSoft) system. Significant evidence was obtained from ConnectND.
- Observed Lake Region State College's processes and procedures.

In aggregate there were no significant limitations or uncertainties related to our overall assessment of the sufficiency and appropriateness of audit evidence.

Discussion and Analysis

The accompanying financial statements have been prepared to present Lake Region State College's revenues and expenses on the legal (budget) basis. The accompanying financial statements are not intended to be presented in accordance with generally accepted accounting principles (GAAP).

For the biennium ended June 30, 2011, operations of Lake Region State College were primarily supported by appropriations from the state's general fund (30%), student tuition and fees (27%), federal grants and contracts (17%), and auxiliary enterprises (11%).

Financial Summary

Revenues consisted primarily of state appropriations, student tuition and fees, auxiliary enterprises, federal grants and contracts, as well as state and local grants and contracts, sales and services of educational departments and gifts. Other revenues during the audited period included state appropriations – capital assets and nongovernmental grants and contracts. Revenues remained fairly constant between fiscal years 2011 and 2010, except student tuition and fees, federal grants and contracts, and state and local grants and contracts.

- Student tuition and fees increased \$355,000 primarily due to credit hour production increasing by 2,424 credits for fall, spring, and summer. This is due to an increase in the number of non-degree (specifically dual credit and collaborative) students enrolled in degree credit courses.
- Federal grants and contracts increased by \$425,000 primarily due to a federal grant received from the American Recovery and Reinvestment Act for Health Information Technology.
- State and local grants and contracts decreased by \$655,000 in fiscal year 2011 primarily due to grants received in fiscal year 2010 for workforce training, center of excellence, and workforce enhancement grant for purchase of equipment for start-up of the wind technician program.

Total expenses for Lake Region State College were \$13.9 million for the year ended June 30, 2011 as compared to \$12.3 million for the prior year. The increase in total expenses for the audited period reflects primarily an increase in salaries and wages due to an annual salary increase of 5.24%, health insurance increase and temporary salary increase due to an increase in online courses and courses at the Grand Forks Air Force Base. Salaries and wages account for 64% of the total expenses. All other expenses remained fairly constant.

Analysis of Significant Changes in Operations

In fiscal year 2010, Lake Region State College was approved to:

- Charge all Minnesota students the resident rate for tuition.

In fiscal year 2011, Lake Region State College was approved to:

- Offer an A.A.S. in Fitness Trainer Technician both traditionally and at a distance.

Analysis of Significant Variances - Budgeted and Actual Expenses

Lake Region State College did not have any significant variances for the general fund expenses as reflected on the statement of appropriations.

Financial Statements

Statement of Net Assets

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
ASSETS		
Cash and cash equivalents	\$ 3,978,902	\$ 3,732,369
Investments	105,000	105,000
Accounts receivable, net	575,911	606,672
Grants & contracts receivables, net	538,027	509,844
Inventories	296,325	316,097
Notes receivable, net	384,063	397,383
Other assets	19,645	22,121
Capital assets, net	3,560,550	3,774,625
Total assets	<u>\$ 9,458,423</u>	<u>\$ 9,464,111</u>
LIABILITIES		
Accounts payable	\$ 208,521	\$ 281,756
Accrued payroll	440,371	365,096
Deferred revenue	449,450	443,603
Deposits	313,995	258,668
Due to others	1,383,900	1,519,001
Total liabilities	<u>\$ 2,796,237</u>	<u>\$ 2,868,124</u>
NET ASSETS		
Invested in capital assets, net of related debt	\$ 2,576,976	\$ 2,625,632
Restricted for:		
Expendable:		
Research	57,782	218,918
Loans	410,903	426,376
Debt service	55,419	63,427
Unrestricted	3,561,106	3,261,634
Total net assets	<u>\$ 6,662,186</u>	<u>\$ 6,595,987</u>

Statement of Revenues, Expenses, and Changes in Net Assets

	June 30, 2011	June 30, 2010
OPERATING REVENUES		
Student tuition and fees	\$ 3,757,789	\$ 3,400,828
Federal grants and contracts	987,370	600,757
State and local grants and contracts	472,114	1,128,649
Nongovernmental grants and contracts	58,655	2,433
Sales and services of educational departments	798,072	512,947
Auxiliary enterprises	1,527,734	1,410,979
Other	8,553	8,221
Total operating revenues	\$ 7,610,287	\$ 7,064,814
OPERATING EXPENSES		
Salaries and wages	\$ 8,902,174	\$ 7,848,496
Operating expenses	3,000,428	2,490,024
Data processing	247,329	226,318
Depreciation	483,022	473,452
Scholarships and fellowships	543,626	605,140
Cost of sales and services	629,503	552,558
Total operating expenses	\$ 13,806,082	\$ 12,195,988
Operating loss	\$ (6,195,795)	\$ (5,131,174)
NONOPERATING REVENUES (EXPENSES)		
State appropriations	\$ 4,130,972	\$ 3,886,650
Federal grants and contracts	1,470,821	1,433,502
Gifts	614,133	431,734
Investments income	14,082	16,940
Interest on capital asset-related debt	(50,114)	(57,285)
Loss on capital assets		(5,304)
Other nonoperating revenues	17,683	11,782
Net nonoperating revenues	\$ 6,197,577	\$ 5,718,019
Income before capital grants, gifts, and transfers	\$ 1,782	\$ 586,845
State appropriations-capital assets	64,418	73,051
Total other revenue	\$ 64,418	\$ 73,051
NET ASSETS		
Net Assets-beginning of the year	\$ 6,595,987	\$ 5,936,091
Net Assets-end of the year	\$ 6,662,187	\$ 6,595,987

Statement of Cash Flows

	June 30, 2011	June 30, 2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Student tuition and fees	\$ 3,746,005	\$ 3,579,764
Grants and contracts	1,489,956	1,630,321
Payments to suppliers	(3,919,283)	(3,242,030)
Payments to employees	(8,796,580)	(7,763,505)
Payments for scholarships and fellowships	(543,626)	(605,140)
Loans issued to students	(66,600)	(50,608)
Collection of loans to students	55,839	55,143
Auxiliary enterprise charges	1,531,363	1,405,033
Sales and service of educational departments	847,816	490,412
Cash received (paid) on deposits	21,616	(6,512)
Other receipts	28,711	13,346
Net cash used by operating activities	\$ (5,604,783)	\$ (4,493,776)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	\$ 4,130,972	\$ 3,906,650
Grants and gifts received for other than capital purposes	2,084,954	1,865,236
Direct Lending Receipts	2,453,686	
Direct Lending Disbursements	(2,453,686)	
Agency fund cash increase (decrease)	41,275	(77,958)
Net cash flows provided by noncapital financing activities	\$ 6,257,201	\$ 5,693,928
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Capital appropriations	\$ 64,418	\$ 73,051
Capital grants and gifts paid	(12)	(83)
Proceeds from sale of capital assets		11,000
Purchases of capital assets	(268,839)	(529,526)
Principal paid on capital debt and lease	(165,420)	(161,310)
Interest paid on capital debt and lease	(50,114)	(57,285)
Net cash used by capital and related financing activities	\$ (419,967)	\$ (664,153)
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest on investments	\$ 14,082.00	\$ 16,940.00
Net cash provided by investing activities	14,082	16,940
Net increase in cash	\$ 246,533	\$ 552,939
CASH - BEGINNING OF YEAR	3,732,369	3,179,430
CASH - END OF YEAR	\$ 3,978,902	\$ 3,732,369

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**RECONCILIATION OF NET OPERATING REVENUES TO
NET CASH USED BY OPERATING ACTIVITIES**

	<u>June 30, 2011</u>	<u>June 30, 2010</u>
Operating loss	\$ (6,195,795)	\$ (5,131,174)
Adjustments to reconcile net loss to net cash provided (used) by operating activities		
Depreciation expense	483,022	473,452
Other nonoperating revenues	17,682	11,784
Change in assets and liabilities		
Accounts receivable adjusted for interest receivable	21,801	(56,801)
Grant & contract receivables	(28,183)	(101,518)
Inventories	19,772	(64,919)
Notes receivable	13,320	33,011
Other assets	2,476	(6,659)
Accounts payable and accrued liabilities adjusted for interest payable	(71,936)	51,947
Accrued payroll	75,275	50,728
Compensated absences	30,319	34,263
Deferred revenue	5,847	218,622
Deposits	21,617	(6,512)
Net cash used by operating activities	<u>\$ (5,604,783)</u>	<u>\$ (4,493,776)</u>

Statement of Appropriations

For The Biennium Ended June 30, 2011

Expenses by line item:	Original		Final		Unexpended
	<u>Appropriation</u>	<u>Adjustments</u>	<u>Appropriation</u>	<u>Expenses</u>	<u>Appropriation</u>
Operating Expenses	\$ 7,956,210	\$ 61,412	\$ 8,017,622	\$ 8,017,622	
Capital Assets	2,653,582		2,653,582	43,662	\$ 2,609,920
Deferred Maintenance	93,807		93,807	93,807	
Federal Stimulus Funds - 2009	2,609,920		2,609,920		2,609,920
Totals	\$ 13,313,519	\$ 61,412	\$ 13,374,931	\$ 8,155,091	\$ 5,219,840
Expenses by source:					
General fund	\$ 10,703,599	\$ 61,412	\$ 10,765,011	\$ 8,155,091	\$ 2,609,920
Federal fund	2,609,920		2,609,920		2,609,920
Totals	\$ 13,313,519	\$ 61,412	\$ 13,374,931	\$ 8,155,091	\$ 5,219,840

Appropriation Adjustments:

The \$61,412 adjustment to operating expenses was a transfer from the NDUS for security and emergency preparedness pursuant to 09 SB 2003, section 13.

Internal Control

In our audit for the biennium ended June 30, 2011, we identified the following areas of Lake Region State College's internal control as being the highest risk:

Internal Controls Subjected to Testing:

- Controls surrounding the processing of revenues.
- Controls surrounding the processing of expenses.
- Controls effecting the safeguarding of assets.
- Controls relating to compliance with legislative intent.
- Controls surrounding the ConnectND (PeopleSoft) system.

The criteria used to evaluate internal control is published in the publication *Internal Control – Integrated Framework* from the Committee of Sponsoring Organizations (COSO) of the Treadway Commission.

We gained an understanding of internal control surrounding these areas and concluded as to the adequacy of their design. We also tested the operating effectiveness of those controls we considered necessary based on our assessment of audit risk. We concluded that internal control was not adequate noting a certain matter involving internal control and its operation that we consider to be a significant deficiency.

Auditors are required to report deficiencies in internal control that are significant within the context of the objectives of the audit. 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 (1) misstatements in financial or performance information, (2) violations of laws and regulations, or (3) impairments of effectiveness or efficiency of operations, on a timely basis. Considering both qualitative and quantitative factors, we identified the following significant deficiency in internal control.

Purchase Cards (Finding 11-1)

During our test of purchase cards we noted the following:

- Many cardholders are not reconciling their monthly JP Morgan statements to their Purchasing Card Record form. They are submitting their Purchasing Card Record form to the Accounts Payable Associate. The Accounts Payable Associate then compares the Purchasing Card Record to the agency-wide statement. Therefore, the responsibility of reconciling each department's purchase card expenditures rests on Accounts Payable and not the individual cardholder.

Lake Region State College's purchase card policy manual states that each cardholder is responsible for reconciling the cardholder statement with the Purchasing Card Record form and original receipts.

Recommendation:

We recommend that Lake Region State College:

- Comply with established policies by ensuring that each cardholder reconcile the cardholder statement with the Purchasing Card Record form and original receipts, forward the signed completed Purchasing Card Record form, JP Morgan statement, and original receipts to the designated supervisor for approval, which then is forwarded to the Accounts Payable Associate in the Business Office for final review and approval, and
- Revoke cards of cardholders who refuse to reconcile cardholder statements with the Purchasing Card Record.

Lake Region State College Response:

Lake Region State College agrees. We will attempt to have all cardholders reconcile their own statements before the Accounts Payable Associate reconciles the statement as a whole. If cardholders refuse to reconcile their statements, we will revoke their cards. We will share this information with the cardholders.

Compliance With Legislative Intent

In our audit for the biennium June 30, 2011, we identified and tested Lake Region State College's compliance with legislative intent for the following areas we determined to be significant and of higher risk of noncompliance:

- Reported to the appropriations committee of the sixty-second legislative assembly on the use of one-time funding (09 SB2003, chapter 31, section 7).
- Proper use/approval of clearing account and petty cash/till funds (NDCC 54-06-08.1, Article X, Section 12, part 1 of the North Dakota Constitution, Attorney General's letter dated September 11, 1987).
- BND used as credit card processing depository (NDCC 54-06-08.2).
- Gifts used in compliance with the wishes of the donor (Article IX, Section 1 of the ND Constitution, NDCC section 1-08-02, and NDCC section 15-10-12).
- Fixed asset requirements including record keeping, surplus property, and lease analysis requirements (NDCC 44-04-07, 54-27-21, 54-27-21.1, 54-44-04.6).
- Expenses including proper voucher approvals (NDCC 44-08-05.1, Article X, Section 12, subpart 2 of North Dakota Constitution) and being within budgeted amounts (NDCC 54-44.1-09, Attorney General Opinion dated January 6, 1977).
- Travel-related expenses are made in accordance with state statute (NDCC 44-08-04, 44-08-04.1, 04.2, 04.3, 04.4, 04.5, and 54-06-09).
- Purchasing including bidding (NDCC 54-44.4-01, 05, 06, 54-44.7-02).
- Conflict of Interest (NDCC 12.1-13-03, 48-01.2-08, 48-02-12).
- Carryover of unexpended appropriations (NDCC 54-44.1-11).
- Adequate blanket bond coverage (NDCC 26.1-21-08).
- Unclaimed property laws (NDCC 47-30.1-02.1, 47-30.1-03.1).
- Nepotism (NDCC 44-04-09).
- Bond Revenues and Reserves (NDCC 15-55-03, 15-55-06).
- Misapplication of entrusted property (NDCC 12.1-23-07).

The criteria used to evaluate legislative intent are the laws as published in the *North Dakota Century Code* and the *North Dakota Session Laws*.

Government Auditing Standards requires auditors to report all instances of fraud and illegal acts unless they are inconsequential within the context of the audit objectives. Further, auditors are required to report significant violations of provisions of contracts or grant agreements, and significant abuse that has occurred or is likely to have occurred.

The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards*. The finding is described below. Other than this finding, we concluded there was compliance with the legislative intent identified above.

Noncompliance With Procurement Policies and Laws (Finding 11-2)

Lake Region State College does not consistently follow Board and Century Code established procurement guidelines. SBHE Policy 308.1 (effective date of June 17, 2010) states employees “responsible for spending or approving expenditure of NDUS funds or incurring any reimbursable expenses must comply with all applicable laws and policies and use good judgment on behalf of the NDUS to ensure that good value is received for every expenditure.”

Per our review of large dollar operating expenses and equipment purchases at LRSC we noted:

- Four Mobile EMS Workstations were purchased in the amount of \$121,995. These workstations were not bid out because according to LRSC, there were no other training station manufacturers making the particular product. Therefore, this was a sole source purchase but a sole source request and proper documentation was not submitted.
- Electrical services from Bergstrom Electric for ten Training Station Switch Gears were purchased in the amount of \$53,500. The electrical services for the switch gears were not bid out because it was believed that Bergstrom Electric is the normal electrical contractor for the college.

NDCC 54-44.4-01 states that it is state policy to provide comprehensive purchasing services based upon sound procurement practices and principles wherein, through full competition with fair and equal opportunity to all qualified persons and firms to sell to the state, each state agency and institution shall obtain its necessary supplies and equipment at competitive cost, consistent with quality, time, and performance requirements.

NDCC 54-44.4-05 states that purchasing contracts must be awarded to the lowest responsible bidder considering conformity with specifications, terms of delivery and quality and serviceability.

State Board of Higher Education Policy 803.1 part 6 states sole source products or services do not require competitive bids if approval is granted. Purchase of an item or service under this exception is permitted only with the written approval of the purchasing officer or other official delegated that authority based upon documentation of the unique characteristics of the product or service, and unavailability of similar products or services of equal value, utility and merit

Recommendation:

We recommend that purchases are

1. Bid in compliance with NDCC 54-44.4-05 and
2. Sole source purchase requests and documentation are submitted in accordance with SBHE Policy 803.1 part 6.

Lake Region State College Response:

Lake Region State College agrees: More care will be taken to ensure that purchases are bid in compliance with NDCCC 54-44.4-05 and sole source purchase requests and documentation are submitted in accordance with SBHE Policy 803.1 part 6. We will attempt to educate individual departments on the policies.

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