LOTTERY FUNDS

HUMBOLDT STATE UNIVERSITY

Audit Report 14-22
May 6, 2014

Members, Committee on Audit

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ABBREVIATIONS

Act                The California State Lottery Act of 1984
BOT                Board of Trustees
CO                 Chancellor’s Office
CSU                California State University
EO                 Executive Order
FY                 Fiscal Year
GC                 Government Code
LF                 Lottery Funds
OAAS               Office of Audit and Advisory Services
EXECUTIVE SUMMARY

As a result of a systemwide risk assessment conducted by the Office of Audit and Advisory Services (OAAS) during the last quarter of 2013, the Board of Trustees, at its January 2014 meeting, directed that Lottery Funds (LF) be reviewed. The OAAS has never reviewed lottery funds as a stand-alone audit.

We visited the Humboldt State University campus from March 17, 2014, through April 18, 2014, and audited the procedures in effect at that time.

In our opinion, except for the effect of the weaknesses described below, the fiscal, operational, and administrative controls for LF activities as of April 18, 2014, taken as a whole, were sufficient to meet the objectives stated in the “Purpose” section of this report. An area of concern is campus program expenditures.

As a result of changing conditions and the degree of compliance with procedures, the effectiveness of controls changes over time. Specific limitations that may hinder the effectiveness of an otherwise adequate system of controls include, but are not limited to, resource constraints, faulty judgments, unintentional errors, circumvention by collusion, and management overrides. Establishing controls that would prevent all these limitations would not be cost-effective; moreover, an audit may not always detect these limitations.

The following summary provides management with an overview of conditions requiring attention. Areas of review not mentioned in this section were found to be satisfactory. Numbers in brackets [ ] refer to page numbers in the report.

CAMPUS PROGRAM EXPENDITURES [6]

Campus administration of lottery fund expenditures needed improvement. Specifically, lottery funds were used to pay for faculty overload performed during the academic instructional period and for a faculty honorarium. In addition, lottery funds were used to pay for non-instructional hospitality expenses that did not contribute to the education of students, and for a travel expense in a program that disallowed this type of expenditure. Also, proper approvals had not been obtained prior to the commencement of work for the special consultant request form used to compensate faculty for work performed on lottery-funded projects. Further, expenditures were not always approved by an individual authorized by the campus’ delegation of signature authority form, and delegation of signature authority forms for lottery trust funds were not always executed by an individual who had been delegated authority from the campus president or president’s designee.
INTRODUCTION

BACKGROUND

The California State Lottery Act (Act) of 1984 directed the lottery administration to provide supplemental funding for the state’s public schools and colleges. The Act states that all lottery funds allocated to public education must be considered supplemental to other funds allotted to public education, and that no educational program shall receive less financial support from the state because it receives lottery proceeds.

Most of the lottery funds allocated to public education are given to K-12 and community college districts. In fiscal year (FY) 2012/13, K-12 education received 81 percent of the lottery fund allocation for public education. Community college districts received 13 percent, and the California State University (CSU) received less than four percent.

The CSU’s allotment, based on units of full-time-equivalent student enrollment, is given directly to the Board of Trustees (BOT). Since the passage of the Act in 1984, the CSU has received nearly $1 billion in lottery funds. The annual amount has generally increased each year, and the CSU allocation for FY 2012/13 was $43.9 million. Some of the funds are retained by the chancellor’s office (CO) for use in systemwide programs, but the majority are distributed to the individual campuses for use in enhancing instruction. More than $30 million was allocated to campuses in FY 2012/13.

The Act has been codified in Government Code §8880. In addition to outlining terms for the administration of lottery games, the legislation addresses the Act’s intent to ensure that lottery funds are considered supplemental to state education funding. It also mandates that lottery funds be managed separately from state appropriations and deposited in and expended from the California State Lottery Education Fund. Further, it emphasizes the intent that lottery fund allocations to educational institutions are to be used exclusively for the education of students and specifically prohibits the use of the funds for the acquisition of real property, construction of facilities, financing of research, or any other non-instructional purpose.

The CO Budget Office provides the following written guidance for campus lottery fund allocations:

- **Lottery Budgeting and Allocation Process** outlines the principles of the Act, including the provisions stating that the funds are supplemental to state appropriations and are intended to be used for instructional purposes. It also provides guidelines for both appropriate and prohibited expenditures; states that lottery funds are to be administered separately from state-appropriated funds; and outlines campus and systemwide reporting requirements for the annual report to the BOT, governor and Legislature. Sections discuss in detail the proper use of lottery funds in campus-based programs and in systemwide programs administered by the CO.

- **General Guidelines for Expenditures**, dated September 3, 2008, provides more detailed guidelines regarding appropriate lottery fund expenditures, including specific discussion about the use of lottery funds for faculty compensation. The guidelines prohibit using lottery funds to pay faculty for classroom instruction, to fund faculty overloads, or to increase the compensation rate for any staff, but do allow lottery funds to be used for faculty development, in certain circumstances.


- **Carry-Forward Fund Policy**, dated August 28, 2007, states, in part, that lottery fund allocations should be spent in the year they are allotted, and that excess funds may be subject to de-allocation by the CO. It further states that campuses may carry forward no more than 80 percent of the fiscal year allocation, and that campuses with carry-forward balances will be required to provide to the CO, as part of the financial reporting package, an annual supplemental report addressing the balance.

- **Process for Reporting Expenditure Plan for Amounts that Exceed Carry-Forward Policy**, dated April 21, 2008, provides campuses with more specific instructions on the treatment and reporting of lottery fund carry-forward balances.

The CSU also has policies for the fiscal management of funding sources, including lottery funds. Executive Order (EO) 1000, *Delegation of Fiscal Authority and Responsibility*, dated July 1, 2007, provides the authority and responsibility for effective oversight of all state funds held by the campuses and all funds held in a fiduciary capacity. Lottery funds are one of the many funding sources for CSU campuses and are, as such, subject to the budget and accounting requirements as outlined in the EO.
PURPOSE

Our overall audit objective was to ascertain the effectiveness of existing policies and procedures related to lottery funds and to determine the adequacy of controls that ensure compliance with relevant governmental regulations, Trustee policy, Office of the Chancellor directives, and campus procedures.

Within the overall audit objective, specific goals included determining whether:

- Administration of the lottery fund program is well-defined and includes clear lines of organizational authority and responsibility and documented delegations of authority.
- Policies and procedures related to lottery funds are current, comprehensive, and effectively distributed.
- The campus is providing accurate and timely lottery fund expenditure information to the CO for annual BOT and state reporting.
- The allocation process for lottery funds is well-documented and includes appropriate review and approval.
- The campus is appropriately budgeting and accounting for lottery fund allocations.
- The campus is properly administering and maintaining appropriate reserves of lottery fund allocations.
- The campus is complying with programmatic restrictions for funds received for specific CO lottery fund programs.
- Lottery funds expended in campus-based programs are in compliance with state and CSU requirements and restrictions.
SCOPE AND METHODOLOGY

The proposed scope of the audit as presented in Audit Agenda Item 4 of the January 28 and 29, 2014, meeting of the Committee on Audit stated that Lottery Funds includes activities for the budgeting, receipt, accounting, and expenditures of lottery fund proceeds allocated to the campuses. Proposed audit scope could include, but was not limited to, review of campus lottery fund allocation and expenditure policies and procedures to ensure compliance with CSU and state requirements; review of internal campus processes for monitoring, reviewing, and approving campus discretionary allocations to specific programs; and examination of specific programs receiving lottery funding to confirm the expenditures are in conformance with state and CSU restrictions.

Our study and evaluation were conducted in accordance with the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors and included the audit tests we considered necessary in determining whether fiscal, operational, and administrative controls are in place and operative. This review emphasized, but was not limited to, compliance with federal and state regulations and guidance, Board of Trustee policies, and Office of the Chancellor and campus policies, letters, and directives. The audit focused on procedures in effect from July 1, 2011, through April 18, 2014.

We focused primarily on the internal administrative, compliance, and operational controls over Lottery Funds activities. Specifically, we reviewed and tested:

- Administration of lottery fund allocations, including defined responsibilities and current policies and procedures.
- Processes to identify appropriate programs or areas for receipt of campus lottery fund allocations.
- Budgeting and accounting processes.
- Administration and reporting of carry-forward balances.
- Use of lottery fund allocations for administrative expenses.
- Expenditures from lottery fund allocations.
OBSERVATIONS, RECOMMENDATIONS, AND CAMPUS RESPONSES

CAMPUS PROGRAM EXPENDITURES

Campus administration of lottery fund expenditures needed improvement.

We reviewed 50 lottery fund expenditures and found that:

- In two instances, lottery funds were used to pay for faculty overload performed during the academic instructional period.
- In one instance, lottery funds were used to pay for a faculty honorarium.
- In one instance, conference travel expenses were paid through the teacher recruitment program lottery account.
- In two instances, lottery funds were used to pay for non-instructional hospitality expenses that did not contribute to the education of students.
- In three instances, proper approvals had not been obtained prior to the commencement of work for the special consultant request form used to compensate faculty for work performed on lottery-funded projects.
- In ten instances, lottery fund expenditures had not been approved by an individual authorized by the campus’ delegation of signature authority form.
- Delegation of signature authority forms for lottery trust funds were not always executed by an individual who had been delegated authority from the campus president or president’s designee.

The General Guidelines for Expenditures, dated September 3, 2008, state that lottery funds may not be used to finance faculty overloads. It further states that lottery funds may not be used to finance increases in the rate of compensation paid to existing staff; thus, stipends and honoraria are not permissible.

Coded memorandum Academic Affairs 2006-07, Teacher Recruitment Project Focus on Math and Science Teachers, dated March 14, 2006, states that conference attendance cannot be funded through the teacher recruitment project budget.

Government Code (GC) §8880.5 (m) states that all funds allocated from the California State Lottery Education Fund shall be used exclusively for the education of students, and no funds shall be spent for acquisition of real property, construction of facilities, financing of research, or any other non-instructional purpose.

The Humboldt State University Special Consultant Request Form and Procedures states that the appropriate approvals must be obtained prior to the work being performed.
Executive Order 1000, *Delegation of Fiscal Authority and Delegation*, dated July 1, 2007, delegates authority to campus presidents to manage funds and approve certain fiscal transactions.

Integrated California State University Administrative Manual §3103.01, *Disbursements – General*, effective January 1, 2014, states that it is the policy of the California State University (CSU) that funds disbursed are properly authorized, supported by a documented business purpose, substantiated by applicable receipts, and correctly processed for payment. It further states that the campus chief financial officer or his/her delegate is responsible for implementing this policy on behalf of the president, and may delegate in writing to additional staff members, in part or in whole and with appropriate limitations, authority to disburse or expense from campus authorized funds.

GC §13402 and §13403 state that management is responsible for establishing and maintaining a system of internal administrative controls, which includes documenting the system, communicating system requirements to employees, and assuring that the system is functioning as prescribed and is modified, as appropriate, for changes in conditions. It further states that administrative controls are the methods through which reasonable assurance can be given that measures adopted by state agency heads to safeguard assets and promote operational efficiency are being followed.

The associate vice president of business services stated that the campus’ lottery fund administrators were aware of the CSU budget office general guidelines for lottery fund expenditures. She further stated that the administration of lottery-funded expenditures did not always comply with campus procedures or systemwide policies and guidelines due to administrative oversight. She also stated that for many years the campus used electronic delegations of fiscal authority in the PeopleSoft module and recently transitioned back to hard-copy signature forms. She stated that due to oversight, during this transition, delegation of signature authority forms were not always executed by an individual with delegation from the president or president’s designee, and in some instances delegations were not always completed and kept on file for individuals approving expenditures.

Inadequate administration of lottery funds and absence of proper delegations of signature authority over expenditures increases the risk of unauthorized and unallowable purchases and subjects the campus to possible regulatory scrutiny.

**Recommendation 1**

We recommend that the campus:

a. Discontinue the practice of using lottery funds to pay for faculty overload performed during the academic instructional period.

b. Discontinue the practice of using lottery funds to pay faculty honoraria.

c. Discontinue the practice of paying for conference travel expenses through the teacher recruitment program lottery account.

d. Require that all lottery-funded expenditures be used for instructional purposes that contribute to the education of students.
e. Obtain proper approvals on special consultant request forms prior to the commencement of work.

f. Obtain approvals for lottery fund expenditures from individuals authorized by the campus’ delegation of signature authority.

g. Require that all delegation of signature authority forms for lottery trust funds be executed by an individual who has been delegated authority from the campus president or president’s designee.

Campus Response

We concur. The campus will create a procedure that describes lottery funds are to be used for instructional purposes that contribute to the education of students, and identifies typical allowable expenses, as well as typical unallowable expenses. In addition, language will be added to the “Special Consultant Request Instructions” sheet that states that approval to use a Special Consultant must be obtained prior to the commencement of work, using the Special Consultant Request Form, and that the form must be approved by an individual authorized by the campus’ delegation of signature authority. The campus will also develop and document a delegation of authority process that identifies proper delegation of authority from the campus president or president’s designee.

Completion date: September 5, 2014
## APPENDIX A: PERSONNEL CONTACTED

<table>
<thead>
<tr>
<th>Name</th>
<th>Title</th>
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</thead>
<tbody>
<tr>
<td>Rollin C. Richmond</td>
<td>President (At time of review)</td>
</tr>
<tr>
<td>Patricia Ambrosini</td>
<td>Payroll Officer</td>
</tr>
<tr>
<td>Sandra Berry</td>
<td>Administrative Support Assistant, College of Professional Studies</td>
</tr>
<tr>
<td>Amber Blakeslee</td>
<td>Budget Analyst, University Budget Office</td>
</tr>
<tr>
<td>Jena’ Burges</td>
<td>Vice Provost and Dean of Undergraduate and Graduate Studies, Academic Programs</td>
</tr>
<tr>
<td>Terri Fisher</td>
<td>Graduate Coordinator, Academic Programs</td>
</tr>
<tr>
<td>Denise Gentry</td>
<td>Administrative Support Assistant, Contracts and Procurement</td>
</tr>
<tr>
<td>Denice Helwig</td>
<td>Chief of Staff, President’s Office</td>
</tr>
<tr>
<td>Chris Hopper</td>
<td>Department Chair, Kinesiology and Recreation Administration</td>
</tr>
<tr>
<td>Cindy Hori</td>
<td>Accounting Supervisor, General Accounting</td>
</tr>
<tr>
<td>Su Karl</td>
<td>Director, Learning Center</td>
</tr>
<tr>
<td>Volga Koval</td>
<td>Director of Academic Resources, Academic Affairs</td>
</tr>
<tr>
<td>John Lee</td>
<td>Dean, College of Professional Studies</td>
</tr>
<tr>
<td>Joyce Lopes</td>
<td>Vice President, Administrative Affairs</td>
</tr>
<tr>
<td>Carol Lorentzen</td>
<td>Associate Vice President, Business Services</td>
</tr>
<tr>
<td>Lupe Lovio</td>
<td>Administrative Support, Early Opportunity Program</td>
</tr>
<tr>
<td>Peggy Metzger</td>
<td>Director, Financial Aid</td>
</tr>
<tr>
<td>Kevin O’Brien</td>
<td>Director, Student Disability Resource Center</td>
</tr>
<tr>
<td>Dan Saveliff</td>
<td>Director, Early Opportunity Program</td>
</tr>
</tbody>
</table>
June 26, 2014

Larry Mandel  
Vice Chancellor and Chief Audit Officer 
The California State University 
401 Golden Shore 
Long Beach, CA 90802

Dear Mr. Mandel:

Please find enclosed Humboldt State University’s response to Audit Report 14-22 Lottery Funds.

Please review the information and let us know if there are any questions or if we can provide additional information. We appreciate the effort you and your staff have made to indicate areas where our procedures could be strengthened.

Please direct questions regarding the response to Carol Lorentzen, Associate Vice President, Business Services, at 707-826-5728 or carol.lorentzen@humboldt.edu.

Sincerely,

Joyce Lopes  
Vice President for Administrative Affairs

Cc: Rollin C. Richmond, President (with enclosures)  
Carol Lorentzen, Associate Vice President for Business Services (with enclosures)
LOTTERY FUNDS
HUMBOLDT STATE UNIVERSITY
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CAMPUS PROGRAM EXPENDITURES

Recommendation 1

We recommend that the campus:

a. Discontinue the practice of using lottery funds to pay for faculty overload performed during the academic instructional period.

b. Discontinue the practice of using lottery funds to pay faculty honoraria.

c. Discontinue the practice of paying for conference travel expenses through the teacher recruitment program lottery account.

d. Require that all lottery-funded expenditures be used for instructional purposes that contribute to the education of students.

e. Obtain proper approvals on special consultant request forms prior to the commencement of work.

f. Obtain approvals for lottery fund expenditures from individuals authorized by the campus' delegation of signature authority.

g. Require that all delegation of signature authority forms for lottery trust funds be executed by an individual who has been delegated authority from the campus president or president's designee.

Campus Response

We concur. The campus will respond to the recommendations above as follows:

• (a), (b), (c), and (d) – Create a procedure that (1) describes lottery funds are to be used for instructional purposes that contribute to the education of students, and (2) identifies typical allowable expenses, as well as typical unallowable expenses.

• (e) – Add language to the “Special Consultant Request Instructions” sheet that states that approval to use a Special Consultant must be obtained prior to the commencement of work, using the Special Consultant Request Form and that the form must be approved by an individual authorized by the campus' delegation of signature authority.
• (f) and (g) – Develop and document a delegation of authority process that identifies proper
degression of authority from the campus president or president’s designee.

Completion Date: September 5, 2014
July 23, 2014

MEMORANDUM

TO: Mr. Larry Mandel
   Vice Chancellor and Chief Audit Officer

FROM: Timothy P. White
      Chancellor

SUBJECT: Draft Final Report 14-22 on Lottery Funds,
         Humboldt State University

In response to your memorandum of July 23, 2014, I accept the response as
submitted with the draft final report on Lottery Funds, Humboldt State
University.

TPW/amd