

AUXILIARY ORGANIZATIONS

**CALIFORNIA POLYTECHNIC STATE UNIVERSITY,
SAN LUIS OBISPO**

**Report Number 02-50
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Members, Committee on Audit

Shailesh J. Mehta, Chair
Roberta Achtenberg, Vice Chair
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Frederick W. Pierce, IV Daniel Weinstein

Staff

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**BOARD OF TRUSTEES
THE CALIFORNIA STATE UNIVERSITY**

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ABBREVIATIONS

ASI	Associated Students, Incorporated of California Polytechnic State University at San Luis Obispo
CSU	California State University
EO	Executive Order
Foundation	California Polytechnic State University Foundation
Housing	Cal Poly Housing Corporation
IRC	Internal Revenue Code
IRS	Internal Revenue Service
UBI	Unrelated Business Income

INTRODUCTION

PURPOSE

The principal audit objectives were to determine compliance with the Education Code, Title 5, and directives of the Board of Trustees and the Office of the Chancellor and to assess the adequacy of controls and systems. Specifically, we sought assurances that legal and regulatory requirements are complied with regarding the:

- ▶ Formation of the auxiliary.
- ▶ Functions the auxiliary performs on the campus.
- ▶ Creation and operation of the auxiliary's board of directors.
- ▶ Establishment of policies and procedures based upon sound business practices.
- ▶ Observance of mandates to maintain an "arms-length" in business transactions between the auxiliary and the campus.
- ▶ Campus oversight of auxiliary operations.

In addition, we reviewed internal controls to assure that:

- ▶ Accounting data is provided in an accurate, timely, complete, or otherwise reliable manner.
- ▶ Assets are adequately safeguarded from loss, damage, or misappropriation.
- ▶ Duties are appropriately segregated consistent with appropriate control objectives.
- ▶ Transactions, accounting entries, or systems output is reviewed and approved.
- ▶ Management does not intentionally override internal controls to the detriment of the overall internal control objectives.
- ▶ Accounting and fiscal tasks, such as reconciliations, are prepared properly and completed timely.
- ▶ Deficiencies in internal controls previously identified were corrected satisfactorily and timely.
- ▶ Management seeks to prevent or detect erroneous record keeping, inappropriate accounting, fraudulent financial reporting, financial loss, and exposure.

SCOPE AND METHODOLOGY

Our management review emphasized, but was not limited to, compliance with state and federal laws and regulations, Board of Trustee policies, and Office of the Chancellor policies, letters, and directives as they relate to California State University (CSU) auxiliaries. For those audit tests that required annualized data, fiscal years 1999-2000, 2000-2001 and 2001-2002 were the primary periods reviewed. In certain instances, we were concerned with representations of the most current data—in such cases, the test period was extended to February 2003. Our primary focus was on internal compliance and controls.

Specifically, for the period reviewed, we examined compliance of the campus and each auxiliary with the Education Code and Title 5 as they relate to the operation of CSU auxiliary organizations. Individual codes and regulations included within the scope of our review were identified through an assessment of risk. Similarly, internal controls were included within our scope based upon risk. Therefore, the scope of our review varied from auxiliary to auxiliary.

A preliminary survey of CSU auxiliaries at each campus was used to identify risks. Risk was defined as the probability that an event or action would adversely affect the auxiliary and/or the campus.

Our assessment of risk was based upon a systematic process, using professional judgments on probable adverse conditions and/or events that became the basis for development of our final scope. We sought to assign higher review priorities to activities with higher risks. As a result, not all risks identified were included within the scope of our review.

The scope of our review, regarding internal compliance considerations, focused on areas which were identified during our preliminary assessment of risks related to the CSU and its requirements to exercise oversight of auxiliaries. (See Appendix B.)

The scope of our internal control review focused on separation of duties, safeguarding of assets, and reliability and integrity of information. Within these, we considered areas of risk identified during a preliminary survey of the campus' auxiliary operations in addition to risks related to the CSU and its oversight of auxiliaries. (See Appendix B.)

We have not performed reviews or analyses beyond the date of our report. Accordingly, our comments are based on our knowledge as of that date and should be read with that understanding. Since the purpose of our comments is to suggest areas for improvement, comments on favorable matters are not discussed.

BACKGROUND

Education Code §89900 states, in part, that the operation of auxiliary organizations shall be conducted in conformity with regulations established by the Trustees.

Education Code §89904 states, in part, that the Trustees of the California State University and the governing boards of the various auxiliary organizations shall:

- ▶ Institute a standard systemwide accounting and reporting system for businesslike management of the operation of such auxiliary organizations.
- ▶ Implement financial standards which will assure the fiscal viability of such various auxiliary organizations. Such standards shall include proper provision for professional management, adequate working capital, adequate reserve funds for current operations and capital replacements, and adequate provisions for new business requirements.
- ▶ Institute procedures to assure that transactions of the auxiliary organizations are within the educational mission of the state colleges.
- ▶ Develop policies for the appropriation of funds derived from indirect cost payments.

Executive Order No. 698, superseding Executive Order No. 682, was issued on March 3, 1999. In that directive, the president of each campus was instructed, in part, as follows:

Section 2. *Authority and Responsibility of the Campus President.* Title 5, Section 42402 establishes the authority of campus presidents to require auxiliary organizations to operate in conformity with policy of the Board of Trustees and the campus. The president is required to review auxiliary programs and budgets and to require discontinuance of activities not in conformity with policies of the Board of Trustees and campus.

The following Trustee policy supplements the existing policy of Section 42402 and provides an additional mechanism for the president to administer his or her responsibilities concerning auxiliary organizations. Action taken by the Trustees' Committee on Audit at the January 1999 meeting of the Board requires an internal compliance/internal control review to be performed by the University Auditor.

The Office of the University Auditor will perform an internal compliance/internal control review of auxiliary organizations. The review will be used to determine compliance with law, including statutes in the Education Code and rules and regulations of Title 5, and compliance with policy of the Board of Trustees and of the campus, including appropriate separation of duties, safeguarding of assets and reliability and integrity of information. This review of each auxiliary organization shall be completed on a triennial basis pursuant to procedures established by the chancellor.

This report represents our triennial review.

OPINION

We visited the California Polytechnic State University, San Luis Obispo campus from February 3, 2003, through March 14, 2003, and reviewed the internal compliance and internal control structures in effect at that time. Our study and evaluation were conducted in accordance with the *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 that accounting and administrative controls are in place and operative.

The campus and management at each auxiliary are responsible for establishing and maintaining adequate internal controls. This responsibility includes documenting internal controls, communicating requirements to employees, and assuring that internal controls are functioning as prescribed. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures.

The objectives of accounting and administrative controls are to provide management with reasonable, but not absolute, assurance that:

- ▶ Assets are safeguarded against loss from unauthorized use or disposition.
- ▶ Transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of reliable financial statements.
- ▶ Financial operations are conducted in accordance with policies and procedures established in the State Administrative Manual, Education Code, Title 5, and Trustee policy as applicable.

Our audit disclosed conditions which, in our opinion, would result in significant errors and irregularities if not corrected. These conditions, along with other weaknesses, are described in the executive summary and in the body of the report.

As a result of changing conditions and the degree of compliance with procedures, the effectiveness of controls change 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 to prevent these limitations would not be cost-effective; moreover, an audit may not always detect these limitations. (See Appendix C.)

EXECUTIVE SUMMARY

The purpose of this section is to provide management with an overview of conditions requiring their 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

LEGAL AND REGULATORY COMPLIANCE [10]

DISSOLUTION OF AUXILIARY [10]

The Cal Poly Housing Corporation (Housing) articles of incorporation did not specify that the net assets of the dissolved auxiliary must be distributed to a successor approved by the campus president and the California State University (CSU) Trustees. The inclusion of a dissolution clause in accordance with Title 5 reduces the risk of net assets not being properly distributed in the event the corporation is dissolved.

LEASING OF FACILITIES [10]

Certain lease agreements between the Foundation and the campus were not updated in a timely manner, and failed to reflect current leasing arrangements. Appropriately executing and updating lease agreements in a timely manner reduce the risk of misunderstandings regarding the terms of the arrangements.

WRITTEN AGREEMENTS [11]

Certain Foundation operating arrangements with the campus were not properly supported by written agreements. Maintaining current, written agreements reduces the risk of misunderstandings and miscommunication regarding rights and responsibilities.

TRUSTS AND OTHER LIABILITIES [12]

The campus did not exercise sufficient control over funds held in trust by its auxiliary organizations. Sufficient control over trust accounts reduces the risk of inappropriate expenditures and misunderstandings about account operations.

CALIFORNIA POLYTECHNIC STATE UNIVERSITY FOUNDATION

LEGAL AND REGULATORY COMPLIANCE [14]

AUXILIARY FUNCTIONS [14]

The California Polytechnic State University Foundation (Foundation) held funds on behalf of, and provided fiscal and operational services for, various unaffiliated organizations. Performing only authorized functions reduces the risk that the auxiliary will participate in transactions inconsistent with Title 5 and reduces the CSU's exposure to unwarranted liability.

WRITTEN AGREEMENTS [15]

Certain Foundation loan arrangements with the campus were not properly supported by written agreements. Maintaining current, written agreements reduces the risk of misunderstandings and miscommunication regarding rights and responsibilities.

RESERVES [15]

The Foundation's reserve policy required revision. Sufficient reserve planning and analysis reduce the auxiliary's risk to fund future needs.

SEGREGATION OF DUTIES [16]

Duties and responsibilities over payroll were not adequately segregated at the Foundation. Adequate segregation of duties reduces the risk that errors and irregularities will not be detected in a timely manner.

CASH RECEIPTS AND HANDLING [17]

Certain controls over Foundation cash receipts processing were inadequate. Sufficient controls over cash receipts processing reduce the risk of a loss or misappropriation of funds.

FEES, REVENUES, AND RECEIVABLES [18]

ACCOUNTS RECEIVABLE [18]

Certain controls over Foundation accounts receivable were inadequate. Sufficient controls over accounts receivable reduce the risk of loss, errors, and irregularities.

UNRELATED BUSINESS INCOME [19]

The Foundation had not recently analyzed its revenues for unrelated business income (UBI). Properly analyzing, documenting, and reporting UBI reduce the auxiliary's exposure to potential penalties and actions by the Internal Revenue Service (IRS).

PURCHASING AND ACCOUNTS PAYABLE [20]

Certain Foundation cash disbursements were not supported by sufficient and appropriate documentation and evidence of appropriate authorization. Sufficient supporting documentation and appropriate authorization reduce the risk of errors, irregularities, and misappropriation of funds.

PERSONNEL AND PAYROLL [21]

Certain controls over Foundation payroll administration and processing were inadequate. Adequate controls over payroll administration and processing reduce the risk of errors, irregularities, and misappropriation of funds.

FIXED ASSETS [22]

Certain controls over Foundation fixed assets were inadequate. Adequate controls over fixed assets reduce the risk that property may be lost or stolen.

TRUSTS AND OTHER LIABILITIES [23]

DEPOSIT AGREEMENTS [23]

Funds held and administered by the Foundation on behalf of campus departments were not supported by a written agreement. Maintaining a written agreement reduces the risk of misunderstandings and miscommunication regarding rights and responsibilities.

RESTRICTED FUNDS [24]

Certain controls over Foundation restricted endowments and gifts were deficient. Sufficient controls over restricted funds reduce the risk of a loss or misappropriation of funds and reduce the risk that the auxiliary will enter into transactions inconsistent with the educational mission of the campus.

AUXILIARY PROGRAMS [25]

Foundation contracts for the solicitation of federal funds for sponsored programs were incomplete. Maintaining complete, written agreements reduces the risk of misunderstandings and miscommunication regarding rights and responsibilities and may reduce legal liability.

INFORMATION TECHNOLOGY [26]

The Foundation had not developed a sufficiently detailed, written information technology disaster recovery plan and corresponding business continuation procedures. A detailed, written disaster recovery plan and corresponding business continuation procedures reduce the risk that the auxiliary may not be able to restore data processing operations within a reasonable time frame.

ASSOCIATED STUDENTS, INCORPORATED OF CALIFORNIA POLYTECHNIC STATE UNIVERSITY AT SAN LUIS OBISPO

LEGAL AND REGULATORY COMPLIANCE [28]

LEASING OF FACILITIES [28]

Certain Associated Students, Incorporated of California Polytechnic State University at San Luis Obispo (ASI) lease arrangements with the campus were not properly supported by written agreements. Appropriately executing and updating lease agreements in a timely manner reduce the risk of misunderstandings regarding the terms of the arrangements.

WRITTEN AGREEMENTS [29]

A written agreement had not been established between ASI and the campus concerning ASI's administration of an instructionally related activity. Maintaining a written agreement reduces the risk of misunderstandings and miscommunication regarding rights and responsibilities.

SEGREGATION OF DUTIES [30]

Duties and responsibilities over cash receipts were not adequately segregated at ASI. Adequate segregation of duties reduces the risk that errors and irregularities will not be detected in a timely manner.

CASH RECEIPTS AND HANDLING [31]

GAME ROOM TOKENS [31]

Controls over ASI game room tokens were deficient. Sufficient controls over tokens reduce the risk of loss or misappropriation of funds.

SAFE COMBINATIONS [32]

ASI did not maintain a record of when safe combinations were last changed. Periodically changing the safe combinations reduces the risk of errors, irregularities, and misappropriations.

FEES, REVENUES, AND RECEIVABLES [32]

ACCOUNTS RECEIVABLE [32]

The ASI recreation center had not established a means for reconciling memberships designated to be paid through payroll deductions with the actual cash receipts. Sufficient controls over accounts receivable reduce the risk of loss, errors, and irregularities.

UNRELATED BUSINESS INCOME [33]

ASI had not tracked, analyzed, or reported UBI. Properly analyzing, documenting, and reporting UBI reduce the auxiliary's exposure to potential penalties and actions by the IRS.

SALES COMMISSION AUDITS [34]

ASI did not exercise its contractual right to verify the Foundation's records of gross sales receipts, upon which ASI commissions were based. Verifying contractor gross sales receipts reduces the risk of underpayment of earned commission revenue.

PURCHASING AND ACCOUNTS PAYABLE [35]

SUPPORTING DOCUMENTATION [35]

Certain ASI cash disbursements were not supported by sufficient and appropriate documentation and evidence of appropriate authorization. Sufficient supporting documentation and appropriate authorization reduce the risk of errors, irregularities, and misappropriation of funds.

UNCLAIMED MONIES [36]

ASI had not developed policies and procedures to escheat unclaimed monies to the state. Meeting the requirements of unclaimed property law could reduce the auxiliary's exposure to potential penalties and fines.

TRUSTS AND OTHER LIABILITIES [37]

Funds held and administered by ASI on behalf of student clubs and other programs were not supported by written agreements. Maintaining written agreements reduces the risk of misunderstandings and miscommunication regarding rights and responsibilities.

OBSERVATIONS, RECOMMENDATIONS, AND CAMPUS RESPONSES

CAMPUS

LEGAL AND REGULATORY COMPLIANCE

DISSOLUTION OF AUXILIARY

The Cal Poly Housing Corporation (Housing) articles of incorporation did not specify that the net assets of the dissolved auxiliary must be distributed to a successor approved by the campus president and the California State University (CSU) Trustees.

Title 5 §42600(b) states that upon dissolution of the organization, net assets, other than trust funds, shall be distributed to a successor approved by the president of the campus and by the Board of Trustees.

The California Polytechnic State University Foundation (Foundation) administrative projects manager indicated that Housing management believed its attorney's review of the articles of incorporation would ensure its compliance with Title 5.

Failure to include a dissolution clause in accordance with Title 5 could result in net assets not being properly distributed in the event the corporation is dissolved.

Recommendation 1

We recommend that Housing amend its articles of incorporation to include a dissolution clause in accordance with Title 5.

Campus Response

We concur. An amendment to the articles of incorporation was submitted to the Housing Corporation board of directors at their meeting on August 15, 2003. The board adopted the changes to the articles as presented. The amended articles of incorporation have been submitted to the president for his approval.

Anticipated date of completion: September 30, 2003

LEASING OF FACILITIES

Certain lease agreements between the Foundation and the campus were not updated in a timely manner, and failed to reflect current leasing arrangements.

We found that the property listing in the license agreement between the Foundation and the campus:

- ▶ Had not been updated annually as required by the license agreement.

- ▶ Did not include the poultry unit as a licensed facility.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that facility lease arrangements be properly supported by current, written agreements.

The vice president of administration and finance indicated that the process of updating agreements is an ongoing process where exceptions as noted will occur.

Failure to appropriately execute and update lease agreements in a timely manner increases the risk of misunderstandings regarding the terms of the arrangements.

Recommendation 2

We recommend that the campus take appropriate measures to ensure that lease agreements with the Foundation:

- a. Are updated in a timely manner.
- b. Reflect current leasing arrangements.

Campus Response

We concur with the narrower finding concerning the Aid to Instruction Facilities and Property License Agreement between Trustees and California Polytechnic State University Foundation. The property listing exhibit required to be updated annually by the license agreement has been completed, and now also includes the poultry unit as a licensed facility. In response to the general recommendation, the campus maintains an electronic database in its effort to ensure agreements with the Foundation are updated timely to reflect current leasing arrangements.

Anticipated date of completion: Completed

WRITTEN AGREEMENTS

Certain Foundation operating arrangements with the campus were not properly supported by written agreements.

We found that although the Foundation continued to provide residence hall food services, the written agreement between the Foundation and the campus for those services had expired.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound

business practices. Sound business practice mandates that business arrangements be supported by current, written agreements.

The vice president of administration and finance indicated that the update to the agreement was in process at the time of the audit.

The absence of written agreements increases the risk of misunderstandings and miscommunication regarding rights and responsibilities.

Recommendation 3

We recommend that the campus take appropriate action to ensure that the written agreements between the Foundation and the campus are executed timely.

Campus Response

We concur. This recommendation was made with respect to the narrower finding that “although the Foundation continued to provide residence hall food services, the written agreement between the Foundation and the campus for those services had expired.”

A Food Service Supplemental Operating Agreement effective June 30, 2001, was in effect at the time of the audit that authorizes the Foundation “to provide and operate food services, including establishing, operating and maintaining student residence dining facilities.” The campus had not provided the Foundation with an executed copy of this agreement at the time of the audit. The campus subsequently provided the Foundation with a copy of this agreement.

Anticipated date of completion: Completed

TRUSTS AND OTHER LIABILITIES

The campus did not exercise sufficient control over funds held in trust by its auxiliary organizations.

We found that:

- ▶ Certain revenue derived from sponsored program indirect costs were deposited in Foundation trust accounts rather than being remitted to the General Fund, even though the cost of state facilities was included in the calculation of the federal indirect cost rate.
- ▶ The Foundation held funds in trust accounts for certain non-campus, non-profit corporations and organizations.

Title 5 §42401, §42402, §42500 and Education Code §89900 establish a responsibility to operate in accordance with sound business practices in the interest of the campus. Education Code §89721 and various chancellor's office mandates establish standards for such operations and related funds management.

The CSU *Investment Manual for California State University Trust Funds*, AD 97-08, indicates that all CSU trust fund money, pending disbursement for its intended purpose, will be managed in custodial accounts in the name of the CSU system.

Title 5 §42500(a) indicates various functions that may be performed by an auxiliary organization. Title 5 §42500(e) indicates that an auxiliary organization shall not engage in a function not listed in subdivision (a) of this section unless an appropriate amendment is made to subdivision (a) by the Board of Trustees, adding said function to the list of approved functions of auxiliary organizations, or unless such function is essential to satisfy the corporation laws of the State of California.

The vice president of administration and finance stated that the sponsored programs function and related transactions are administered by the Foundation in accordance with the auxiliary operating agreements. He further stated that any allocation of costs between the university and its auxiliary organizations is documented with the annual campus cost allocation plan (as per Executive Order No. 753). In addition, the vice president of administration and finance stated that the funds held for certain non-campus, non-profit corporations and organizations were not held in the state university trust fund but were held by the Foundation in non-state accounts.

Insufficient control over trust accounts increases the risk of inappropriate expenditures and misunderstandings about account operations.

Recommendation 4

We recommend that the campus increase its oversight of auxiliary management, specifically in the area of funds held in trust accounts.

Campus Response

The university will review funds held in trust accounts by the Foundation in relation to the functions that are assignable to auxiliary organizations as per Title 5 §42500(a).

Anticipated date of completion: December 31, 2003

CALIFORNIA POLYTECHNIC STATE UNIVERSITY FOUNDATION

LEGAL AND REGULATORY COMPLIANCE

AUXILIARY FUNCTIONS

The California Polytechnic State University Foundation (Foundation) held funds on behalf of, and provided fiscal and operational services for, various unaffiliated organizations.

Title 5 §42500(a) indicates various functions that may be performed by an auxiliary organization. Title 5 §42500(e) indicates that an auxiliary organization shall not engage in a function not listed in subdivision (a) of this section unless an appropriate amendment is made to subdivision (a) by the Board of Trustees, adding said function to the list of approved functions of auxiliary organizations, or unless such function is essential to satisfy the corporation laws of the State of California.

The Foundation executive director indicated that fiscal services contracts were entered into at the request of, and authorization by, the campus. He further indicated that, in certain instances, contracts were established based on former affiliation with the campus and Foundation.

Performing unauthorized functions increases the risk that the auxiliary will participate in transactions inconsistent with Title 5 and subjects the CSU to unwarranted liability.

Recommendation 5

We recommend that the Foundation:

- a. Perform only those functions listed in Title 5 or seek approval for variances from the Office of the Chancellor.
- b. Divest itself of those funds held for unaffiliated organizations.

Campus Response

We concur with this recommendation. The Internet Education Equal Access Foundation agency account has been closed as of June 30, 2003, and the balance of the account transferred to the CSU Trustees, based upon the request of the new service provider. In regards to Atascadero State Hospital, we will seek approval of the CSU to continue providing this service through the existing contract date of December 31, 2006.

Anticipated date of completion: October 31, 2003

WRITTEN AGREEMENTS

Certain Foundation loan arrangements with the campus were not properly supported by written agreements.

We found that the Foundation loaned funds to a campus program; however, the terms and conditions of the arrangement were not contained in a signed agreement.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that business arrangements be supported by current, written agreements.

The Foundation chief financial officer indicated that a written loan agreement was not considered necessary, as the loan terms had been identified in a board resolution.

The absence of written agreements increases the risk of misunderstandings and miscommunication regarding rights and responsibilities.

Recommendation 6

We recommend that the Foundation take appropriate action to ensure that the terms and conditions of the arrangement are contained in signed agreements.

Campus Response

We concur with this recommendation. On March 14, 2003, the Foundation board adopted Policy #123, which authorizes Foundation funds to be invested in loans to departments with either board or investment committee approval. A template form to be used in future agreements is being developed.

Anticipated date of completion: September 30, 2003

RESERVES

The Foundation's reserve policy required revision.

Such a policy should address or consider the following areas:

- ▶ Minimum reserve requirements.
- ▶ The inclusion of reserves in the budget submitted to the campus president.
- ▶ Board review of reserve levels.
- ▶ Reserves for working capital and capital replacement.
- ▶ The methodology used for the calculation of reserves.

Education Code §89904(b), §89904.5, and §89905 indicate that reserve planning is necessary.

The Foundation chief financial officer indicated that reserve calculation information was documented in the Foundation's year-end closing procedures, but the information had not been formalized in a policy statement.

Insufficient reserve planning and analysis increase the auxiliary's risk to fund future needs.

Recommendation 7

We recommend that the Foundation coordinate with the campus to update its formal policy for the allocation of surplus funds/reserves.

Campus Response

We concur with this recommendation. We will work with outside auditors and management staff to develop a more refined policy and submit this policy to our board for approval.

Anticipated date of completion: June 30, 2004

SEGREGATION OF DUTIES

Duties and responsibilities over payroll were not adequately segregated at the Foundation.

We found that:

- ▶ Payroll technicians and supervisors approved certain employees' time records in the absence of the employees' supervisors.
- ▶ A payroll technician processed payroll and assigned identifications within the payroll system.

Executive Order (EO) No. 698, *Board of Trustees Policy for the CSU Auxiliary Organizations*, dated March 3, 1999, states that the review of auxiliary organizations will be used to determine appropriate separation of duties, safeguarding of assets, and reliability and integrity of information.

The Foundation chief financial officer indicated that payroll personnel occasionally approved employees' timecards in order to meet payroll processing deadlines.

Inadequate segregation of duties increases the risk that errors and irregularities will not be detected in a timely manner.

Recommendation 8

We recommend that the Foundation segregate payroll duties or institute mitigating controls approved by the campus.

Campus Response

We concur with this recommendation. We have instituted procedures where payroll personnel are not allowed to sign off time clock entries in the absence of a departmental supervisor. A secondary level of supervision will be assigned within the department and will be given access to sign off on employees' time in the absence of their immediate supervisor. We will also analyze duties and the segregation between human resources and payroll functions as we work to implement our new HRMS system.

Anticipated date of completion: March 31, 2004

CASH RECEIPTS AND HANDLING

Certain controls over Foundation cash receipts processing were inadequate.

We found that:

- ▶ Personnel and funds were not adequately safeguarded while in-transit to/from the cashier's office.
- ▶ The Foundation did not maintain a current record of outlying safe locations, individuals with knowledge of the safe combinations, and when such combinations were last changed.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that sufficient internal controls be maintained over cash receipts processing.

The Foundation administrative projects manager indicated that management believed safeguards for personnel with cash in-transit were adequate. She further indicated that issues related to safe locations and combinations were due to oversight.

Inadequate controls over cash receipts processing increase the risk of a loss or misappropriation of funds.

Recommendation 9

We recommend that the Foundation:

- a. Implement procedures to adequately safeguard personnel and funds while in-transit.
- b. Maintain records of safe locations, safe combination changes, and individuals who have access to the safe.

Campus Response

We concur with this recommendation. Additional notice will be sent to transporting departments to provide dual custody while transporting funds. A log has been developed to track safe combination changes and individuals having access.

Anticipated date of completion: September 30, 2003

FEES, REVENUES, AND RECEIVABLES

ACCOUNTS RECEIVABLE

Certain controls over Foundation accounts receivable were inadequate.

We found that:

- ▶ The poultry unit did not maintain numerical control over delivery invoices.
- ▶ Approximately one-third of poultry unit accounts receivable (nearly \$40,000) was greater than 30 days past due.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates adequate internal controls over accounts receivable.

The campus professor of animal science indicated that a better billing system had not been established due to time constraints. He further indicated that the outstanding receivables resulted from the customers' confusion over the invoicing procedures.

Insufficient controls over accounts receivable increase the risk of loss, errors, and irregularities.

Recommendation 10

We recommend that the Foundation:

- a. Numerically or sequentially control or otherwise account for all invoices.
- b. Implement procedures to achieve a more timely collection of overdue accounts receivable.

Campus Response

We concur with this recommendation. Procedures will be distributed to billing departments which specify the numerical control of billing or charge documents and tracking to insure completeness of the billing process. The invoicing practice has been improved by creating a one-to-one billing relationship between departmental charge tags and Foundation invoices. Hopefully, this will reduce confusion on the customer's part and improve the collection time of receivables.

Anticipated date of completion: December 31, 2003

UNRELATED BUSINESS INCOME

The Foundation had not recently analyzed its revenues for unrelated business income (UBI).

We found that revenues generated from certain poultry unit egg sales and revenues resulting from services provided to unaffiliated organizations were not included in the Foundation's UBI analysis.

Internal Revenue Code (IRC) §512 through §514 defines an unrelated trade or business of an exempt organization as any trade or business, the conduct of which is not substantially related to the exercise or performance of its tax-exempt purpose. UBI in excess of \$1,000 must be reported to the Internal Revenue Service (IRS), whether or not a tax liability is incurred. In addition, the organization's tax-exempt status may be jeopardized if too large a proportion of its revenue is derived from UBI.

The Foundation executive director indicated that management had not considered certain poultry unit egg sales UBI, because students were directly involved in the operations. He further indicated that the service contracts with unaffiliated organizations were entered into based on the organizations' former affiliation to the campus and Foundation and that the UBI analysis was not updated to reflect the change in affiliation due to oversight.

Failure to properly analyze, document, and report UBI increases the auxiliary's exposure to potential penalties and actions by the IRS.

Recommendation 11

We recommend that the Foundation analyze its operations for UBI and appropriately track and report it.

Campus Response

We concur with this recommendation and will work with our auditors to more appropriately identify UBI.

Anticipated date of completion: May 31, 2004

PURCHASING AND ACCOUNTS PAYABLE

Certain Foundation cash disbursements were not supported by sufficient and appropriate documentation and evidence of appropriate authorization.

Our review of 100 cash disbursements disclosed the following:

Process Controls

- ▶ In 23 instances, faxed and photocopied invoices were processed without sufficient documentation to clearly demonstrate such were sent by the vendor for billing purposes.
- ▶ In 20 instances, the approval signature did not match the signature specimen on file.

Processing Exceptions

- ▶ In 25 instances, documentation to support the expenditure was not on file.
- ▶ In four instances, disbursements were coded to an incorrect expense account.
- ▶ In three instances, a signature specimen was not on file for the fund from which a disbursement was made.
- ▶ In two instances, the contract in support of the disbursement was unsigned.
- ▶ In two instances, IRS Form 1099 was not appropriately issued.
- ▶ In one instance, there was no one-up authorization for the disbursement.
- ▶ In one instance, there was no authorization for the disbursement.
- ▶ In one instance, receipts were not compiled to support credit card payments.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that all cash disbursements be fully supported and properly authorized.

The Foundation executive director indicated that the process controls and processing exceptions noted were due to an oversight and that every attempt is made to follow stated policies and procedures.

Insufficient supporting documentation and lack of appropriate authorization increase the risk of errors, irregularities, and misappropriation of funds.

Recommendation 12

We recommend that the Foundation ensure that cash disbursements are supported by sufficient and appropriate documentation and evidence of appropriate authorization.

Campus Response

We concur with this recommendation. We will implement procedures to identify faxed and photocopied invoices as coming from the vendor. We will also implement additional procedures to ensure that all signature authorization forms reflect all valid signatures for applicable accounts.

Anticipated date of completion: November 30, 2003

PERSONNEL AND PAYROLL

Certain controls over Foundation payroll administration and processing were inadequate.

We found that:

- ▶ A signature specimen was not consistently on file for certain supervisors approving timesheets.
- ▶ The payroll technicians did not consistently verify unrecognized supervisors' signatures.
- ▶ Rubber signature stamps were used to approve certain timecards in conflict with Foundation policy.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates adequate controls over payroll administration and processing.

The Foundation accounting manager indicated that the processing issues noted were due to management oversight.

The lack of adequate controls over payroll administration and processing increases the risk of errors, irregularities, and misappropriation of funds.

Recommendation 13

We recommend that the Foundation:

- a. Consistently obtain facsimile signatures for all supervisors approving timesheets.

- b. Implement procedures to ensure payroll technicians verify supervisors' signatures.
- c. Enforce its policy prohibiting the use of signature stamps for approvals without mitigating controls.

Campus Response

We concur with this recommendation. Signature authorization forms will be updated and unrecognized signatures researched. A procedure for the authorized use of signature stamps is in use and has recently been adopted by Associated Students as well. Signatures will be verified as time permits within the legal payment deadlines. We are hopeful that the process can be improved with the implementation of our new HRMS system.

Anticipated date of completion: March 31, 2004

FIXED ASSETS

Certain controls over Foundation fixed assets were inadequate.

We found that:

- ▶ Annual physical inventories were not performed by all Foundation departments.
- ▶ Physical inventories were not performed by independent personnel.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates strong controls over fixed assets.

The Foundation administrative projects manager indicated that annual physical inventories had not been performed by independent personnel due to resource constraints.

Inadequate controls over fixed assets increase the risk that property may be lost or stolen.

Recommendation 14

We recommend that the Foundation:

- a. Ensure its periodic physical inventory of fixed assets includes all Foundation departments.
- b. Utilize independent personnel to perform physical inventories.

Campus Response

We concur with this recommendation. Periodic physical inventories of fixed assets have been an issue due to staff resource availability. In many instances, the complexity of identifying particular assets has also been an issue. We will work at developing procedures for a more thorough inventory process within continued resource constraints.

Anticipated date of completion: January 31, 2004

TRUSTS AND OTHER LIABILITIES

DEPOSIT AGREEMENTS

Funds held and administered by the Foundation on behalf of campus departments were not supported by a written agreement.

Such agreements should address or consider the following areas:

- ▶ Purpose of the account.
- ▶ Source of funds.
- ▶ Reporting requirements.
- ▶ Time constraints.
- ▶ Instructions for closing the account.
- ▶ Disposition of unexpended balance.
- ▶ Administrative fees.
- ▶ Interest allocation.
- ▶ Applicable restrictions.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that funds held and administered on behalf of others be properly supported by written agreements.

The Foundation administrative projects manager indicated that current procedure is to obtain a "Request for New Account Form" to establish new accounts, but due to the age of certain accounts, the form might not be on file.

The absence of a written agreement increases the risk of misunderstandings and miscommunication regarding rights and responsibilities.

Recommendation 15

We recommend that the Foundation establish a written agreement for the administration and maintenance of funds held on behalf of campus departments.

Campus Response

We concur with this recommendation. A “Request for New Account” form is in use for establishing new campus programs accounts. It incorporates some of the details specified for the agreements. We have made an attempt to update all accounts that were previously missing this documentation. We will modify our form to include additional areas as specified in the audit.

Anticipated date of completion: February 29, 2004

RESTRICTED FUNDS

Certain controls over Foundation restricted endowments and gifts were deficient.

Our review of 26 endowment and gift files disclosed the following:

Establishment of Accounts

- ▶ In two instances, the donor document establishing the endowment was not on file.
- ▶ In three instances, the endowments or gifts were inappropriately accepted, as the CSU system could not satisfy the established purpose. Because there were no qualifying CSU recipients, payouts were therefore provided to non-CSU entities.
- ▶ In nine cases, proof of all cash receipts was not on file. There were no corpus reconciliation requirements for endowments between cash receipts, the expected corpus contributions, and the established corpus value.

Contract Compliance

- ▶ Detailed procedures for the monitoring of endowment and gift contracts were not in place.

Disposition of Inactive Accounts

- ▶ The campus loan repayment account connected with an endowment had accumulated a significant balance because the loan requirements were difficult for students to achieve.
- ▶ There were no procedures in place to follow-up on non-responses from account holders concerning the distribution of endowment or gift proceeds.

Title 5 §42401 and §42402 indicate that campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates the establishment of a system of controls to ensure the reasonable management of restricted funds.

The Foundation's executive director stated that the documentation issues related to aged endowments and that the files for more recently established endowments were more adequately documented.

Inadequate controls over restricted funds increase the risk of a loss or misappropriation of funds and increase the risk that the auxiliary will enter into transactions inconsistent with the educational mission of the campus.

Recommendation 16

We recommend that the Foundation:

- a. Ensure clear documentary evidence is maintained in support of the establishment of endowment accounts.
- b. Establish more detailed procedures for the monitoring of endowment and gift contracts.
- c. Establish procedures to identify and resolve issues pertaining to inactive endowment and gift accounts.

Campus Response

We concur with this recommendation. We will implement a checklist to insure that appropriate documentation is obtained when establishing endowments. We will also implement a process for following up on inactive accounts.

Anticipated date of completion: January 31, 2004

AUXILIARY PROGRAMS

Foundation contracts for the solicitation of federal funds for sponsored programs were incomplete.

We found that:

- ▶ Certain lobbying contracts did not specifically prohibit activities disallowed by Title 5.
- ▶ The contracts did not adequately define the scope of work.

Title 5 §42403 prohibits auxiliaries from expending funds on certain political activities.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that contracts detail the scope of work to be performed and restrictions applicable to the contract.

The Foundation executive director indicated that the contract used was industry standard and that he was unaware of the need to include language to define and prohibit certain activities.

The absence of a complete, written agreement increases the risk of misunderstandings and miscommunication regarding rights and responsibilities and may increase legal liability.

Recommendation 17

We recommend that the Foundation revise its contracts with lobbyists to ensure:

- a. Political activities disallowed by Title 5 are specifically prohibited.
- b. The contracts include essential contractual provisions, including details of the scope of work to be performed.

Campus Response

We concur with this recommendation. A new contract was executed May 13, 2003, and was updated with language indicating that the vendor will comply with all California and federal laws and regulations.

Anticipated date of completion: Complete

INFORMATION TECHNOLOGY

The Foundation had not developed a sufficiently detailed, written information technology disaster recovery plan and corresponding business continuation procedures.

A written disaster recovery plan for data processing services did not exist to ensure timely recovery of service. Written plans were needed for the financial accounting, bookstore inventory, and food services inventory systems. Contracts for equipment replacement were in place for most systems, and backup tapes were taken off-site to help ensure the recoverability of the systems, but the recovery steps were not documented in writing.

EO No. 696, *Implementation of the California State University Emergency Preparedness Program*, dated January 29, 1999, states, in part, that each campus president is delegated the responsibility for

the implementation of a multihazard emergency program on campus and shall ensure that management activities including, but not limited to, maintenance and regular updating of the institutional multihazard emergency plan and determination, acquisition, and maintenance of facilities, equipment, and related supplies required for emergency preparedness are accomplished.

The Foundation management information systems director indicated that development of a written disaster recovery plan was postponed due to significant changes being made to the critical financial systems during the current system conversion.

Without a detailed, written disaster recovery plan and corresponding business continuation procedures, the auxiliary may not be able to restore data processing operations within a reasonable time frame.

Recommendation 18

We recommend that the Foundation document a sufficiently detailed, written disaster recovery plan and corresponding business continuation procedures.

Campus Response

We concur with this recommendation. Although documented business continuation procedures have been developed for the various accounting functions, a system disaster recovery plan was put on hold until our completed implementation of our new financial system.

Anticipated date of completion: June 30, 2004

**ASSOCIATED STUDENTS, INCORPORATED OF
CALIFORNIA POLYTECHNIC STATE UNIVERSITY AT SAN LUIS OBISPO**

LEGAL AND REGULATORY COMPLIANCE

LEASING OF FACILITIES

Certain Associated Students, Incorporated of California Polytechnic State University at San Luis Obispo (ASI) lease arrangements with the campus were not properly supported by written agreements.

We found that:

- ▶ ASI had not executed a lease agreement with the campus for the sports complex, although the intentions of both parties to do so were contained in a memo (this agreement was subsequently executed during the audit fieldwork).
- ▶ The agreement between ASI and the campus pertaining to the land on which the children's center resides did not include a specific reference to the land.
- ▶ ASI had no written agreement with the campus for the land used by the ASI lighted marquee outside of the student market.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that lease arrangements be properly supported by written agreements.

The ASI executive director indicated that the written agreement deficiencies occurred under previous leadership and the current leadership did not have knowledge of why those particular deficiencies existed.

Failure to appropriately execute and update lease agreements in a timely manner increases the risk of misunderstandings regarding the terms of the arrangements.

Recommendation 19

We recommend that ASI establish or revise written agreements with the campus for:

- a. The children's center, specifically with respect to land.
- b. The land used by the ASI lighted marquee outside of the student market.

Campus Response

- a. We concur with the recommendation. An Exhibit "A," consisting of a campus map showing the location of the children's center and a building facility floor plan, has been attached to the Children's Center Lease Agreement.

Anticipated date of completion: Complete

- b. We concur with the recommendation. ASI followed the permit process and was issued a written permit in order to erect the lighted marquee at issue. Because ASI followed the campus process authorizing the location and use of the marquee, the campus did not feel a separate license agreement was necessary. The campus will review the campus building permit process and make a determination as to the legal necessity for a license.

Anticipated date of completion: December 31, 2003

WRITTEN AGREEMENTS

A written agreement had not been established between ASI and the campus concerning ASI's administration of an instructionally related activity.

The current year agreement concerning the rose float project had not been completed, although the project had begun operations.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that business arrangements be supported by written agreements.

The ASI executive director indicated that a contract was not executed in a timely manner due to delays in processing between ASI and the campus.

The absence of a written agreement increases the risk of misunderstandings and miscommunication regarding rights and responsibilities.

Recommendation 20

We recommend that ASI establish a written agreement with the campus concerning the administration of the project described above.

Campus Response

We concur with the recommendation. Each year ASI and the campus execute a written agreement outlining the scope and requirements concerning the management of the project. At the time of the audit, the agreement had not been finalized. This agreement has been subsequently prepared and executed by ASI and the campus.

Anticipated date of completion: Complete

SEGREGATION OF DUTIES

Duties and responsibilities over cash receipts were not adequately segregated at ASI.

We found that:

- ▶ The university union services technician maintained custody of the two keys required to open the game room change safe, purchased additional change, and balanced the safe.
- ▶ The university union services technician's safe balancing documentation was not reviewed by her supervisor or the ASI business office.
- ▶ The university union services technician's token machine readings and cash withdrawals were not witnessed.

EO No. 698, *Board of Trustees Policy for the CSU Auxiliary Organizations*, dated March 3, 1999, states that the review of auxiliary organizations will be used to determine appropriate separation of duties, safeguarding of assets, and reliability and integrity of information.

The ASI executive director indicated that deficient safe and token machine controls were due to area management's assessment that no material risk existed.

Inadequate segregation of duties increases the risk that errors and irregularities will not be detected in a timely manner.

Recommendation 21

We recommend that ASI segregate cash receipt duties or institute mitigating controls approved by the campus.

Campus Response

We concur with the recommendation. ASI will implement internal controls to mitigate the risk associated with the game room change safe access and reconciliation processes.

Anticipated date of completion: November 30, 2003

CASH RECEIPTS AND HANDLING

GAME ROOM TOKENS

Controls over ASI game room tokens were deficient.

We found that:

- ▶ There were no inventory or reconciliation procedures established related to tokens.
- ▶ Tokens were not adequately safeguarded. Certain tokens were maintained in an unlocked bag at the cashier's desk.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates strong controls over items with a ready cash value.

The ASI executive director indicated that deficient accounting controls over game room tokens were due to area management's assessment that no material risk existed.

Inadequate controls over tokens increase the risk of loss or misappropriation of funds.

Recommendation 22

We recommend that ASI:

- a. Implement inventory and reconciliation procedures to adequately account for game room tokens.
- b. Store tokens in an appropriately restricted area.

Campus Response

We concur with this recommendation. Beginning in August 2003, ASI has contracted out for the provision of all coin/token operated electronic games. The external contractor has been licensed to utilize floor space in the games area and is paying a monthly rental. Additionally, the contractor purchased all of ASI's coin/token operated games equipment and is solely responsible for their maintenance and operation. Therefore, any and all issues related to safeguarding tokens and cash withdrawals from games have been eliminated.

Anticipated date of completion: Complete

SAFE COMBINATIONS

ASI did not maintain a record of when safe combinations were last changed.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that frequent changes to safe combinations be performed.

The ASI executive director indicated that the combinations had not been changed due to infrequent staff turnover.

Failure to periodically change the safe combinations increases the risk of errors, irregularities, and misappropriations.

Recommendation 23

We recommend that ASI change its safe combinations on a periodic basis and when there is a turnover in personnel with safe access, as well as maintain a log of when the combinations were changed.

Campus Response

We concur with the recommendation. ASI will implement a program of periodic changes to safe combinations and begin maintaining a detailed log of any changes made.

Anticipated date of completion: November 30, 2003

FEES, REVENUES, AND RECEIVABLES

ACCOUNTS RECEIVABLE

The ASI recreation center had not established a means for reconciling memberships designated to be paid through payroll deductions with the actual cash receipts.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates strong controls over accounts receivable.

The ASI director of business services stated that establishing the means for developing a payroll deduction membership reconciliation procedure had been attempted, but had not been successful due to the lack of automated membership system reports and access to campus payroll reports.

Insufficient controls over accounts receivable increase the risk of loss, errors, and irregularities.

Recommendation 24

We recommend that ASI establish a system for reconciling recreation memberships sold through payroll deductions with cash receipts.

Campus Response

We concur with the recommendation. ASI will work with the university payroll office to develop a reconciliation of recreation center memberships sold through payroll deduction to cash receipts from payroll deduction.

Anticipated date of completion: November 30, 2003

UNRELATED BUSINESS INCOME

ASI had not tracked, analyzed, or reported UBI.

We found that ASI had no means in place to track potential UBI. ASI neither filed an IRS Form 990T nor identified UBI from these arrangements.

IRC §512 through §514 defines an unrelated trade or business of an exempt organization as any trade of business, the conduct of which is not substantially related to the exercise or performance of its tax-exempt purpose. UBI in excess of \$1,000 needs to be reported to the IRS whether or not a tax liability is incurred. In addition, an organization's tax-exempt status could be at risk if too large a portion of its revenue is derived from UBI.

The ASI executive director indicated that this potential tax reporting liability had never been brought to their attention by the independent accounting firm who prepares their annual tax returns.

Failure to properly analyze, document, and report UBI increases the auxiliary's exposure to potential penalties and actions by the IRS.

Recommendation 25

We recommend that ASI analyze its operations for UBI and appropriately track and report it, if appropriate.

Campus Response

We concur with the recommendation. ASI will work with its external auditors on a plan to accurately identify and track UBI. If it is determined that UBI exists, then ASI will appropriately report it to the proper authority.

Anticipated date of completion: March 31, 2004

SALES COMMISSION AUDITS

ASI did not exercise its contractual right to verify the Foundation's records of gross sales receipts, upon which ASI commissions were based.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates strong controls over commission-based payments.

The ASI executive director indicated that current Foundation reports were considered to be sufficient for purposes of collecting commissions.

Failure to verify contractor gross sales receipts could result in the underpayment of earned commission revenue.

Recommendation 26

We recommend that ASI obtain the Foundation's records of gross sales receipts and verify the accuracy of the commission revenues remitted to ASI.

Campus Response

We concur with the recommendation. ASI will examine Foundation records on an annual basis to verify gross sales amounts.

Anticipated date of completion: July 31, 2004

PURCHASING AND ACCOUNTS PAYABLE

SUPPORTING DOCUMENTATION

Certain ASI cash disbursements were not supported by sufficient and appropriate documentation and evidence of appropriate authorization.

Our review of 60 cash disbursements disclosed the following:

Process Controls

- ▶ In eight instances, payments were processed without proof of receipt of goods or services.
- ▶ In four instances, faxed, photocopied, undated, or unnumbered invoices were processed, without sufficient documentation to clearly demonstrate such were sent by the vendor for billing purposes.

Processing Exceptions

- ▶ In 14 instances, the business reason for the purchase was unclear.
- ▶ In six instances, the requisition was unsigned or the approval signature did not match the signature specimen on file.
- ▶ In three instances, check request forms were not completed, and the unit approver's identity was not clear.
- ▶ In two instances, the funding source for significant expenditures was not identified in the requisition.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that all cash disbursements be fully supported and properly authorized.

The ASI executive director indicated that the current system of documentation for disbursement approvals was adequate and the above are just exceptions.

Insufficient supporting documentation and lack of appropriate authorization increase the risk of errors, irregularities, and misappropriation of funds.

Recommendation 27

We recommend that ASI ensure that cash disbursements are supported by sufficient and appropriate documentation and evidence of appropriate authorization.

Campus Response

We concur with the recommendation. ASI has implemented (prior to the audit) and continues to maintain a strong system of internal controls that requires several levels of authorizations and approvals. During the course of the audit, there were a few items that were identified as exceptions to documented procedures. ASI is confident that existing controls are appropriate and sufficient to assure that all cash disbursements are appropriately documented and authorized. However, to assure compliance with internal controls and mitigate future exceptions, management will re-double efforts on educating staff on proper procedures. This will be accomplished through ongoing review and training related to the ASI policy manual.

Anticipated date of completion: November 30, 2003

UNCLAIMED MONIES

ASI had not developed policies and procedures to escheat unclaimed monies to the state.

Unclaimed checks totaled approximately \$12,000, and certain checks dated back four years.

Code of Civil Procedure, Chapter 7, *Unclaimed Property Law*, Article 2 §1510 and §1511 indicate that property held by a business association escheats to the state, subject to various requirements and limitations.

The ASI executive director indicated that the examination of unclaimed checks for their disposition is always ongoing, but that currently, staff was behind in processing due to other priorities.

Failure to meet the requirements of unclaimed property law could increase the auxiliary's exposure to potential penalties and fines.

Recommendation 28

We recommend that ASI, in conjunction with the campus, develop operating procedures that implement the requirements of the Code of Civil Procedure with respect to unclaimed property.

Campus Response

We concur with the recommendation. ASI will work in conjunction with the campus to develop appropriate procedures to handle unclaimed monies.

Anticipated date of completion: March 31, 2004

TRUSTS AND OTHER LIABILITIES

Funds held and administered by ASI on behalf of student clubs and other programs were not supported by written agreements.

Such agreements should address or consider the following areas:

- ▶ Purpose of the account.
- ▶ Source of funds.
- ▶ Reporting requirements.
- ▶ Time constraints.
- ▶ Instructions for closing the account.
- ▶ Disposition of unexpended balance.
- ▶ Administrative fees.
- ▶ Interest allocation.
- ▶ Applicable restrictions.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that funds held and administered on behalf of others be properly supported by written agreements.

The ASI executive director indicated that the importance of incorporating the terms and conditions of the arrangement contained in the club and team manuals into the signature authorization form signed by officers of club entities with funds on deposit was not recognized.

The absence of written agreements increases the risk of misunderstandings and miscommunication regarding rights and responsibilities.

Recommendation 29

We recommend that ASI establish a written agreement for the administration and maintenance of funds held on behalf of student clubs and other programs.

Campus Response

We concur with the recommendation. ASI will execute agreements with the clubs outlining the services to be provided to the clubs and clearly articulate ASI's responsibility with respect to the clubs' funds.

Anticipated date of completion: March 31, 2004

APPENDIX A: PERSONNEL CONTACTED

Name

Title

CAMPUS

Warren J. Baker	President
Kevin Bright	Accountant, College of Agriculture
Scott Cooke	Assistant Director, Financial Reporting
Nana Farkye	Professor/Creamery Manager
Leslie Ferreira	Department Head, Dairy Sciences
Lawrence R. Kelley	Vice President, Administration and Finance
Gary Ketcham	Administrator II, Farm Operations
Mark Shelton	Associate Dean, College of Agriculture
Robert J. Spiller	Professor, Animal Science
Vicki Stover	Associate Vice President, Administration and Finance

CALIFORNIA POLYTECHNIC STATE UNIVERSITY FOUNDATION

Robert Ambach	Associate Executive Director
Jodi Block	Payroll Clerk
Karen Brown	Accounting Manager
Frank Cawley	Bookstore Director
Lori Cordova	Senior Investment Analyst
Alan Cushman	Associate Director, Campus Dining
Steve Eckgren	Loss Prevention Coordinator
Tammy Farrell	Financial Accounting Coordinator, Bookstore
Maurie Higgenbotham	Accounts Payable Supervisor
Jill Keezer	Sponsored Programs Director
Diana Kinunen	Administrative Projects Manager
Starr Lee	Legal Counsel
Frank Mumford	Executive Director
Lisa Nunes	Campus Program Analyst
Nancy Osorio	Customer Service Supervisor, Campus Dining
Nancy Owen	Customer Service Supervisor
Nanci Palmer	Account Clerk I
Monica Potter	Cashier
Lisa Rockwell-Harpster	Trust Administrator
Holly Sletteland	Director, Management Information Systems
Linda Teeple	Accounts Payable Clerk
Dale Texter	Chief Financial Officer
April Thomas	Cashier
Debbie Tuson	Payroll Clerk
Mariann Van Pelt	Accounting Manager
Ron Weaver	Investment Administrator

**ASSOCIATED STUDENTS, INCORPORATED OF
CALIFORNIA POLYTECHNIC STATE UNIVERSITY AT SAN LUIS OBISPO**

Carmen Alicea	University Union Services Technician
Dawn Annoni	Human Resource Technician
Michelle Broom	Public Relations/Marketing Coordinator
Dwayne A. Brummet	Director, Business Services
Cecilia Chen	Cashier/Payroll Assistant
Judie Hagstrom	Assistant to the Executive Director
Tonya Iverson	Director, Children's Programs
Rick Johnson	Executive Director
Marcy Maloney	Director
Kim Rynhard	Administrative Assistant
Jan Stiles	Accountant

SCOPE

INTERNAL COMPLIANCE SCOPE

As discussed in the body of our report, we evaluated each organization's compliance with the Education Code and Title 5 as related to the operation of CSU auxiliary organizations.

Within the scope of our review, we included the following internal compliance considerations, which were identified during our preliminary assessment of risks related to the CSU and its oversight of auxiliaries in determining whether:

- ▶ The auxiliary performed only those functions determined by the CSU Trustees to be appropriate for auxiliary organizations.
- ▶ The auxiliary performed only those functions authorized under a written agreement executed with the chancellor.
- ▶ The auxiliary board of directors established provisions in either the articles of incorporation or constitution stating that, upon dissolution, net assets other than trust funds will be distributed to a successor approved by the campus president (or designee) and the CSU Trustees.
- ▶ The auxiliary board of directors adopted a constitution and, if the auxiliary is not incorporated, has filed a copy of the constitution with the chancellor (or designee).
- ▶ All leasing of campus facilities by the auxiliary was effected under provisions of Education Code §89046 or other laws governing the leasing of state facilities and whether it appropriately paid rent on space in tax-supported buildings on campus utilized by federally sponsored projects, unless the projects were excluded from space reimbursement requirements.
- ▶ All contracts or other business arrangements involving real property were entered into with prior approval of the campus president (or designee) and prior notification and consultation with the CSU chancellor (or designee).
- ▶ The auxiliary board of directors met statutory requirements in size and composition.
- ▶ Statutory requirements applicable to public meetings were adhered to as applicable to the auxiliary.
- ▶ The auxiliary board of directors held business meetings at least once a quarter.

- ▶ The auxiliary was established by constitution, statute, bylaws, or resolution and whether there were provisions for election of officers and board members.
- ▶ Sufficient operating procedures had been established by the auxiliary to allow the campus president (or designee) to ascertain the propriety of all expenditures and the integrity of financial reporting and whether all expenditures were made in accordance with policies of the CSU Trustees.
- ▶ The auxiliary had all expenditures and fund appropriations approved by its board and whether it had fund appropriations for use outside of normal business operations of the auxiliary approved by an officer designated by the CSU Trustees.
- ▶ The auxiliary provided full-time employee salaries, working conditions, and benefits comparable to those provided by the CSU.
- ▶ The auxiliary operated commercial services on a self-supporting basis.
- ▶ The auxiliary submitted its programs and budgets for review in a timely manner as specified by the president (or designee).
- ▶ The auxiliary maintained a reasonable provision for reserves and used surplus funds from commercial operations for purposes consistent with regulations of the CSU Trustees.
- ▶ The auxiliary used indirect cost reimbursements in accordance with statutory requirements.
- ▶ The auxiliary gave loans, scholarships, stipends, and grants-in-aid to currently admitted students only.
- ▶ The auxiliary accepted grants, contracts, bequests, trusts, or gifts, to be used only for purposes consistent with the policies of the CSU Trustees.
- ▶ The auxiliary forwarded records of student financial assistance to the campus financial aid office on a timely basis.
- ▶ Expenditures for public relations or other purposes which would serve to augment state appropriations for operation of the campus were approved by the governing body of the auxiliary organization and that this policy was filed with the chancellor (or designee).
- ▶ The auxiliary had taken measures to protect the campus from all possible liability associated with the operation of commercial services.
- ▶ The auxiliary obtained indemnity bonds for officers and employees handling funds as statutorily mandated.

- ▶ Conflict-of-interest statutes and regulations had been complied with, including, but not limited to, the prohibition of financial conflicts of interest or personal pecuniary gains in transactions with governing board members.
- ▶ The auxiliary adopted a nondiscrimination and affirmative action in employment policy approved by the chancellor (or designee).
- ▶ The student body organization auxiliary deposited in trust with the chief financial officer of the campus all student body organization fees or other funds and money under the programmatic control of the student body organizations, except for those collected from and used in or for major commercial services and agency funds.
- ▶ The student body organization auxiliary sufficiently enabled the chief fiscal officer of the campus to comply with legislative mandates by recommending the most appropriate institution or medium for investment of unexpended funds.
- ▶ The student body organization auxiliary submitted appropriate claim schedules to the chief fiscal officer of the campus after review and approval by an officer of the student body organization.

INTERNAL CONTROL SCOPE

As to the scope of our internal control review, our focus was on the separation of duties, safeguarding of assets, and reliability and integrity of information. The areas included were identified through a preliminary survey and risk assessment of the operation of each auxiliary on the campus. Risks were defined as the probability that an event or action may adversely affect the auxiliary and/or the campus.

We generally considered that duties were adequately segregated when no individual performed more than one of the following duties: (1) receiving and depositing remittances; (2) authorizing disbursements; (3) preparing checks; (4) operating a check-signing machine; (5) comparing signed checks with authorizations and supporting documents; (6) reconciling bank accounts and posting to the general ledger or any subsidiary ledger affected by cash transactions; and (7) initiating or preparing invoices.

Within our general internal control focus, we considered and reviewed, as deemed appropriate based upon our assessment of risk, the following:

- ▶ Procedures for receipting and storing cash, segregation of duties involving cash receipting, and recording of cash receipts.
- ▶ Establishment of receivables and adequate segregation of duties regarding billing for and payment of receivables.
- ▶ Approval of purchases, receiving procedures, and reconciliation of expenditures to general ledger balances.

- ▶ Use of petty cash funds, periodic cash counts, and reconciliation of bank accounts.
- ▶ Authorization of personnel/payroll transactions.
- ▶ Posting of the property ledger, regular reconciliation of the property to the general ledger, and physical inventories.
- ▶ Access restrictions to automated accounting systems and proper documentation of the systems.
- ▶ Procedures for initiating, overseeing, and accounting for investments.
- ▶ Establishment of trust funds, separate accounting, adequate agreements, and annual budgets.

As discussed, the areas actually included within the scope of our review were identified through a preliminary survey and risk assessment of each auxiliary's operation. They were included within the scope of our review because they were deemed to address the risks associated with each auxiliary's operation on the campus. Risk was defined as the probability that an event or action may adversely affect the auxiliary and/or the campus.

STATEMENT OF INTERNAL CONTROLS

A. INTRODUCTION

Internal accounting and related operational controls established by the State of California, the CSU Board of Trustees, and the Office of the Chancellor are evaluated by the university auditor, in compliance with professional standards for the conduct of internal audits, to determine if an adequate system of internal control exists and is effective for the purposes intended. Any deficiencies observed are brought to the attention of appropriate management for corrective action.

B. INTERNAL CONTROL DEFINITION

Internal control, in the broad sense, includes controls which may be characterized as either accounting or operational as follows:

1. Internal Accounting Controls

Internal accounting controls comprise the plan of organization and all methods and procedures that are concerned mainly with, and relate directly to, the safeguarding of assets and the reliability of financial records. They generally include such controls as the systems of authorization and approval, separation of duties concerned with record keeping and accounting reports from those concerned with operations or asset custody, physical controls over assets, and personnel of a quality commensurate with responsibilities.

2. Operational Controls

Operational controls comprise the plan of organization and all methods and procedures that are concerned mainly with operational efficiency and adherence to managerial policies and usually relate only indirectly to the financial records.

C. INTERNAL CONTROL OBJECTIVES

The objective of internal accounting and related operational control is to provide reasonable, but not absolute, assurance as to the safeguarding of assets against loss from unauthorized use or disposition, and the reliability of financial records for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that the cost of a system of internal accounting and operational control should not exceed the benefits derived and also recognizes that the evaluation of these factors necessarily requires estimates and judgment by management.

D. INTERNAL CONTROL SYSTEMS LIMITATIONS

There are inherent limitations that should be recognized in considering the potential effectiveness of any system of internal accounting and related operational control. In the performance of most control procedures, errors can result from misunderstanding of instruction, mistakes of judgment, carelessness, or other personal factors. Control procedures whose effectiveness depends upon segregation of duties can be circumvented by collusion. Similarly, control procedures can be circumvented intentionally by management with respect to the executing and recording of transactions. Moreover, projection of any evaluation of internal accounting and operational control to future periods is subject to the risk that the procedures may become inadequate because of changes in conditions and that the degree of compliance with the procedures may deteriorate. It is with these understandings that internal audit reports are presented to management for review and use.

CAL POLY

California Polytechnic State University
San Luis Obispo, CA 93407

Administration & Finance Division
(805) 756-2171 • Fax (805) 756-7560

September 19, 2003

RECEIVED
UNIVERSITY AUDITOR

SEP 19 2003

THE CALIFORNIA STATE
UNIVERSITY

Mr. Larry Mandel
University Auditor
Office of the University Auditor
The California State University
401 Golden Shore
Long Beach, CA 90802-4275

Subject: Audit Report Number 02-50, *Auxiliary Organizations* at California Polytechnic State University, San Luis Obispo

Dear Larry:

As requested in your letter of August 19th, attached is the campus response to recommendations of Audit Report Number 02-50, *Auxiliary Organizations*. It is anticipated that documentation supporting audit findings that are specified as complete will be forwarded to you within the next few weeks.

If you have questions regarding this document, please contact Vicki Stover, Associate Vice President for Administration, at 805-756-2171 or VStover@calpoly.edu.

Sincerely



Lawrence Kelley
Vice President for Administration & Finance

cc: R. Ramirez
F. Mumford
R. Johnson

w/o attachments
W. Baker
V. Stover

AUXILIARY ORGANIZATIONS
CALIFORNIA POLYTECHNIC STATE UNIVERSITY,
SAN LUIS OBISPO
REPORT NO. 02-50

CAMPUS

LEGAL AND REGULATORY COMPLIANCE

DISSOLUTION OF AUXILIARY

Recommendation 1

We recommend that Housing amend its articles of incorporation to include a dissolution clause in accordance with Title 5.

Campus Response

We concur. An amendment to the articles of incorporation was submitted to the Housing Corporation Board of Directors at their meeting on August 15, 2003. The Board adopted the changes to the articles as presented. The amended articles of incorporation have been submitted to the President for his approval.

Anticipated date of completion: September 30, 2003

LEASING OF FACILITIES

Recommendation 2

We recommend that the campus take appropriate measures to ensure that lease agreements with the Foundation:

- a. Are updated in a timely manner.
- b. Reflect current leasing arrangements.

Campus Response

This recommendation was made with respect to the auditor's narrower finding that the property listing in the license agreement between the Foundation and the campus:

- Had not been updated annually as required by the license agreement.
- Did not include the poultry unit as a licensed facility.

We concur with the narrower finding concerning the Aid to Instruction Facilities and Property License Agreement between Trustees and California Polytechnic State University Foundation. The property listing exhibit required to be updated annually by the License Agreement has been completed, and now also includes the Poultry Unit as a licensed facility. In response to the general recommendation, the campus maintains an electronic database in its effort to ensure agreements with the Foundation are updated timely to reflect current leasing arrangements.

Anticipated date of completion: Completed.

WRITTEN AGREEMENTS

Recommendation 3

We recommend that the campus take appropriate action to ensure that the written agreements between the Foundation and the campus are executed timely.

Campus Response

We concur. This recommendation was made with respect to the narrower finding that “although the Foundation continued to provide residence hall food services, the written agreement between the Foundation and the campus for those services had expired.”

A Food Service Supplemental Operating Agreement effective June 30, 2001, was in effect at the time of the audit that authorizes the Foundation “to provide and operate food services, including establishing, operating and maintaining student residence dining facilities.” The campus had not provided the Foundation with an executed copy of this agreement at the time of the audit. The campus subsequently provided the Foundation with a copy of this agreement.

Anticipated date of completion: Completed.

TRUSTS AND OTHER LIABILITIES

Recommendation 4

We recommend that the campus increase its oversight of auxiliary management, specifically in the area of funds held in trust accounts.

Campus Response

The university will review funds held in trust accounts by the Foundation in relation to the functions that are assignable to auxiliary organizations as per Title 5 §42500(a).

Anticipated date of completion: December 31, 2003

CALIFORNIA POLYTECHNIC STATE UNIVERSITY FOUNDATION

LEGAL AND REGULATORY COMPLIANCE

AUXILIARY FUNCTIONS

Recommendation 5

We recommend that the Foundation:

- a. Perform only those functions listed in Title 5 or seek approval for variances from the Office of the Chancellor.
- b. Divest itself of those funds held for unaffiliated organizations.

Campus Response

We concur with this recommendation. The Internet Education Equal Access Foundation agency account has been closed as of June 30, 2003, and the balance of the account transferred to the CSU Trustees, based upon the request of the new service provider. In regards to Atascadero State Hospital, we will seek approval of the CSU to continue providing this service through the existing contract date of December 31, 2006.

Anticipated date of completion: October 31, 2003

WRITTEN AGREEMENTS

Recommendation 6

We recommend that the Foundation take appropriate action to ensure that the terms and conditions of the arrangement are contained in signed agreements.

Campus Response

We concur with this recommendation. On March 14, 2003, the Foundation Board adopted Policy #123 which authorizes Foundation funds to be invested in loans to departments with either Board or Investment Committee approval. A template form to be used in future agreements is being developed.

Anticipated date of completion: September 30, 2003

RESERVES

Recommendation 7

We recommend that the Foundation coordinate with the campus to update its formal policy for the allocation of surplus funds/reserves.

Campus Response

We concur with this recommendation. We will work with outside auditors and management staff to develop a more refined policy and submit this policy to our board for approval.

Anticipated date of completion: June 30, 2004

SEGREGATION OF DUTIES

Recommendation 8

We recommend that the Foundation segregate payroll duties or institute mitigating controls approved by the campus.

Campus Response

We concur with this recommendation. We have instituted procedures where payroll personnel are not allowed to sign off time clock entries in the absence of a departmental supervisor. A secondary level of supervision will be assigned within the department and will be given access to sign off on employees' time in the absence of their immediate supervisor. We will also analyze duties and the segregation between Human Resources and Payroll functions as we work to implement our new HRMS system.

Anticipated date of completion: March 31, 2004

CASH RECEIPTS AND HANDLING

Recommendation 9

We recommend that the Foundation:

- a. Implement procedures to adequately safeguard personnel and funds while in-transit.
- b. Maintain records of safe locations, safe combination changes, and individuals who have access to the safe.

Campus Response

We concur with this recommendation. Additional notice will be sent to transporting departments to provide dual custody while transporting funds. A log has been developed to track safe combination changes and individuals having access.

Anticipated date of completion: September 30, 2003

FEES, REVENUES, AND RECEIVABLES

ACCOUNTS RECEIVABLE

Recommendation 10

We recommend that the Foundation:

- a. Numerically or sequentially control or otherwise account for all invoices.
- b. Implement procedures to achieve a more timely collection of overdue accounts receivable.

Campus Response

We concur with this recommendation. Procedures will be distributed to billing departments which specify the numerical control of billing or charge documents and tracking to insure completeness of the billing process. The invoicing practice has been improved by creating a one-to-one billing relationship between departmental charge tags and Foundation invoices. Hopefully this will reduce confusion on the customer's part and improve the collection time of receivables.

Anticipated date of completion: December 31, 2003

UNRELATED BUSINESS INCOME

Recommendation 11

We recommend that the Foundation analyze its operations for UBI and appropriately track and report it.

Campus Response

We concur with this recommendation and will work with our auditors to more appropriately identify UBI.

Anticipated date of completion: May 31, 2004

PURCHASING AND ACCOUNTS PAYABLE

Recommendation 12

We recommend that the Foundation ensure that cash disbursements are supported by sufficient and appropriate documentation and evidence of appropriate authorization.

Campus Response

We concur with this recommendation. We will implement procedures to identify faxed and photocopied invoices as coming from the vendor. We will also implement additional procedures to ensure that all signature authorization forms reflect all valid signatures for applicable accounts.

Anticipated date of completion: November 30, 2003

PERSONNEL AND PAYROLL

Recommendation 13

We recommend that the Foundation:

- a. Consistently obtain facsimile signatures for all supervisors approving timesheets.
- b. Implement procedures to ensure payroll technicians verify supervisors' signatures.
- c. Enforce its policy prohibiting the use of signature stamps for approvals without mitigating controls.

Campus Response

We concur with this recommendation. Signature authorization forms will be updated and unrecognized signatures researched. A procedure for the authorized use of signature stamps is in use and has recently been adopted by Associated Students as well. Signatures will be verified as time permits within the legal payment deadlines. We are hopeful that the process can be improved with the implementation of our new HRMS system.

Anticipated date of completion: March 31, 2004

FIXED ASSETS

Recommendation 14

We recommend that the Foundation:

- a. Ensure its periodic physical inventory of fixed assets includes all Foundation departments.
- b. Utilize independent personnel to perform physical inventories.

Campus Response

We concur with this recommendation. Periodic physical inventories of fixed assets have been an issue due to staff resource availability. In many instances, the complexity of identifying particular assets has also been an issue. We will work at developing procedures for a more thorough inventory process within continued resource constraints.

Anticipated date of completion: January 31, 2004

TRUSTS AND OTHER LIABILITIES

DEPOSIT AGREEMENTS

Recommendation 15

We recommend that the Foundation establish a written agreement for the administration and maintenance of funds held on behalf of campus departments.

Campus Response

We concur with this recommendation. A "Request for New Account" form is in use for establishing new campus programs accounts. It incorporates some of the details specified for the agreements. We have made an attempt to update all accounts that were previously missing this documentation. We will modify our form to include additional areas as specified in the audit.

Anticipated date of completion: February 29, 2004

RESTRICTED FUNDS

Recommendation 16

We recommend that the Foundation:

- a. Ensure clear documentary evidence is maintained in support of the establishment of endowment accounts.
- b. Establish more detailed procedures for the monitoring of endowment and gift contracts.

- c. Establish procedures to identify and resolve issues pertaining to inactive endowment and gift accounts.

Campus Response

We concur with this recommendation. We will implement a checklist to insure that appropriate documentation is obtained when establishing endowments. We will also implement a process for following up on inactive accounts.

Anticipated date of completion: January 31, 2004

AUXILIARY PROGRAMS

Recommendation 17

We recommend that the Foundation revise its contracts with lobbyists to ensure:

- a. Political activities disallowed by Title 5 are specifically prohibited.
- b. The contracts include essential contractual provisions, including details of the scope of work to be performed.

Campus Response

We concur with this recommendation. A new contract was executed May 13, 2003, and was updated with language indicating that the vendor will comply with all California and Federal laws and regulations.

Anticipated date of completion: Complete

INFORMATION TECHNOLOGY

Recommendation 18

We recommend that the Foundation document a sufficiently detailed, written disaster recovery plan and corresponding business continuation procedures.

Campus Response

We concur with this recommendation. Although documented business continuation procedures have been developed for the various accounting functions, a system disaster recovery plan was put on hold until our completed implementation of our new financial system.

Anticipated date of completion: June 30, 2004

ASSOCIATED STUDENTS, INCORPORATED OF
CALIFORNIA POLYTECHNIC STATE UNIVERSITY AT SAN LUIS OBISPO

LEGAL AND REGULATORY COMPLIANCE

LEASING OF FACILITIES

Recommendation 19

We recommend that ASI establish or revise written agreements with the campus for:

- a. The children's center, specifically with respect to land.
- b. The land used by the ASI lighted marquee outside of the student market

Campus Response

We concur with the recommendation. An Exhibit "A," consisting of a campus map showing the location of the Children's Center and a building facility floor plan, has been attached to the Children's Center Lease Agreement.

Anticipated date of completion: Complete

- b. We concur with the recommendation. ASI followed the permit process and was issued a written permit in order to erect the lighted marquee at issue. Because ASI followed the campus process authorizing the location and use of the marquee, the campus did not feel a separate license agreement was necessary. The campus will review the campus building permit process and make a determination as to the legal necessity for a license.

Anticipated date of completion: December 31, 2003

WRITTEN AGREEMENTS

Recommendation 20

We recommend that ASI establish a written agreement with the campus concerning the administration of the project described above.

Campus Response

We concur with the recommendation. Each year ASI and campus execute a written agreement outlining the scope and requirements concerning the management of the project. At the time of the audit, the agreement had not been finalized. This agreement has been subsequently prepared and executed by ASI and the campus.

Anticipated date of completion: Complete

SEGREGATION OF DUTIES

Recommendation 21

We recommend that ASI segregate cash receipt duties or institute mitigating controls approved by the campus.

Campus Response

We concur with the recommendation. ASI will implement internal controls to mitigate the risk associated with the game room change safe access and reconciliation processes.

Anticipated date of completion: November 30, 2003

CASH RECEIPTS AND HANDLING

GAME ROOM TOKENS

Recommendation 22

We recommend that ASI:

- a. Implement inventory and reconciliation procedures to adequately account for game room tokens.
- b. Store tokens in an appropriately restricted area.

Campus Response

We concur with this recommendation. Beginning in August 2003, ASI has contracted out for the provision of all coin/token operated electronic games. The external contractor has been licensed to utilize floor space in the games area and is paying a monthly rental. Additionally, the contractor purchased all of ASI's coin/token operated games equipment and is solely responsible for their maintenance and operation. Therefore, any and all issues related to safeguarding tokens and cash withdrawals from games have been eliminated.

Anticipated date of completion: Complete

SAFE COMBINATIONS

Recommendation 23

We recommend that ASI change its safe combinations on a periodic basis and when there is a turnover in personnel with safe access, as well as maintain a log of when the combinations were changed.

Campus Response

We concur with the recommendation. ASI will implement a program of periodic changes to safe combinations and begin maintaining a detailed log of any changes made.

Anticipated date of completion: November 30, 2003

FEES, REVENUES, AND RECEIVABLES

ACCOUNTS RECEIVABLE

Recommendation 24

We recommend that ASI establish a system for reconciling recreation memberships sold through payroll deductions with cash receipts.

Campus Response

We concur with the recommendation. ASI will work with the University payroll office to develop a reconciliation of recreation center memberships sold through payroll deduction to cash receipts from payroll deduction.

Anticipated date of completion: November 30, 2003

UNRELATED BUSINESS INCOME

Recommendation 25

We recommend that ASI analyze its operations for UBI and appropriately track and report it, if appropriate.

Campus Response

We concur with the recommendation. ASI will work with its external auditors on a plan to accurately identify and track UBI. If it is determined that UBI exists, then ASI will appropriately report it to the proper authority.

Anticipated date of completion: March 31, 2004

SALES COMMISSION AUDITS

Recommendation 26

We recommend that ASI obtain the Foundation's records of gross sales receipts and verify the accuracy of the commission revenues remitted to ASI.

Campus Response

We concur with the recommendation. ASI will examine Foundation records on an annual basis to verify gross sales amounts.

Anticipated date of completion: July 31, 2004

PURCHASING AND ACCOUNTS PAYABLE

SUPPORTING DOCUMENTATION

Recommendation 27

We recommend that ASI ensure that cash disbursements are supported by sufficient and appropriate documentation and evidence of appropriate authorization.

Campus Response

We concur with the recommendation. ASI has implemented (prior to the audit) and continues to maintain a strong system of internal controls that requires several levels of authorizations and approvals. During the course of the audit, there were a few items that were identified as exceptions to documented procedures. ASI is confident that existing controls are appropriate and sufficient to assure that all cash disbursements are appropriately documented and authorized. However, to assure compliance with internal controls and mitigate future exceptions, management will re-double efforts on educating staff on proper procedures. This will be accomplished through on-going review and training related to the ASI policy manual.

Anticipated date of completion: November 30, 2003

UNCLAIMED MONIES

Recommendation 28

We recommend that ASI, in conjunction with the campus, develop operating procedures that implement the requirements of the Code of Civil Procedures with respect to unclaimed property.

Campus Response

We concur with the recommendation. ASI will work in conjunction with the campus to develop appropriate procedures to handle unclaimed monies.

Anticipated date of completion: March 31, 2004

TRUSTS AND OTHER LIABILITIES

Recommendation 29

We recommend that ASI establish a written agreement for the administration and maintenance of funds held on behalf of student clubs and other programs.

Campus Response

We concur with the recommendation. ASI will execute agreements with the clubs outlining the services to be provided to the clubs and clearly articulate ASI's responsibility with respect to the clubs funds.

Anticipated date of completion: March 31, 2004



THE CALIFORNIA STATE UNIVERSITY

 OFFICE OF THE CHANCELLOR

BAKERSFIELD November 3, 2003

CHANNEL ISLANDS

CHICO

MEMORANDUM

DOMINGUEZ HILLS

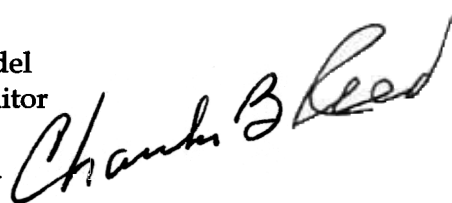
FRESNO

TO: Mr. Larry Mandel
University Auditor

FULLERTON

HAYWARD

FROM: Charles B. Reed
Chancellor



HUMBOLDT

SUBJECT: Draft Final Report Number 02-50 on *Auxiliary Organizations*,
California Polytechnic State University, San Luis Obispo

LONG BEACH

LOS ANGELES

MARITIME ACADEMY

In response to your memorandum of November 3, 2003, I accept the response as submitted with the draft final report on *Auxiliary Organizations*, California Polytechnic State University, San Luis Obispo.

MONTEREY BAY

NORTHRIDGE

POMONA

CBR/amd

SACRAMENTO

Enclosure

SAN BERNARDINO

cc: Dr. Warren J. Baker, President
Mr. Lawrence R. Kelley, Vice President for Administration and Finance

SAN DIEGO

SAN FRANCISCO

SAN JOSE

SAN LUIS OBISPO

SAN MARCOS

SONOMA

STANISLAUS