

FISMA

HUMBOLDT STATE UNIVERSITY

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ABBREVIATIONS

CSU	California State University
HSU	Humboldt State University
IT	Information Technology
FISMA	Financial Integrity and State Manager's Accountability Act
FRS	Financial Reporting System
SCO	State Controller's Office
SDM	System Development Methodology
SAM	State Administrative Manual
SUAM	State University Administrative Manual

INTRODUCTION

PURPOSE

The principal audit objective was to assess the adequacy of controls and systems that assure that:

- ▶ cash receipts are processed in accordance with laws, regulations and management policies;
- ▶ receivables are promptly recognized and balances are periodically evaluated;
- ▶ purchases are made in accordance with laws, regulations and management policies;
- ▶ revolving fund disbursements are authorized and processed in accordance with laws, regulations, and management policies;
- ▶ cash disbursements are properly authorized and made in accordance with established procedures and adequate segregation of duties exists;
- ▶ payroll/personnel criteria for hiring employees, establishing compensation rates and authorizing disbursements are controlled and access to personnel and payroll records and processing areas is restricted;
- ▶ purchase and disposition of fixed assets are controlled and recording of assets are made promptly in the subsidiary records;
- ▶ physical computer controls are in place and functioning;
- ▶ investments are adequately controlled and securities are safeguarded; and
- ▶ trust funds are established in accordance with SUAM guidelines.

SCOPE AND METHODOLOGY

The management review emphasized, but was not limited to, compliance with state and federal laws, Board of Trustee policies, and Office of the Chancellor policies, letters, and directives. For those audit tests that required annualized data, fiscal year 1998-99 was the primary period reviewed. In certain instances, we were concerned with representations of the most current data—in such cases, the test period was July to December 1998. Our primary focus was on internal controls. Specifically, we reviewed and tested:

- ▶ 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 over the establishment of billing for and payment of receivables;
- ▶ approval of purchases, receiving procedures and reconciliation of expenditures to State Controller's balances;
- ▶ limitations on the size and types of revolving fund disbursements;
- ▶ use of petty cash funds, periodic cash counts, and reconciliation of bank accounts;
- ▶ authorization of personnel/payroll transactions and accumulation of leave credits in compliance with state policies;
- ▶ posting of the property ledger, monthly 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, evaluating, and accounting for investments; and
- ▶ establishment of trust funds, separate accounting, adequate agreements, and annual budget.

We have not performed any auditing procedures 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

In 1983, the California Legislature passed the Financial Integrity and State Manager's Accountability Act of 1983 (FISMA). This act required that state agencies establish and maintain a system of internal accounting and administrative control. To ensure that the requirements are fully complied with, the head of each agency is required to prepare and submit a report on the adequacy of the system of internal accounting and administrative control following the end of each odd-numbered fiscal year. The Office of the University Auditor of the CSU is currently responsible for conducting the audits of internal accounting and administrative control within the CSU. This report represents our biennial review.

OPINION

We visited the CSU Humboldt from January 25, 1999, through February 12, 1999 and audited the internal control structure in effect at that time.

In accordance with the Government Code Section 13402, et seq., state agency heads are responsible for establishing and maintaining systems of internal accounting control. The broad objectives of control systems for state agencies are to provide management with reasonable, but not absolute, assurance that:

- ▶ assets are safeguarded from unauthorized use or disposition; and
- ▶ transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial reports in accordance with the State Administrative Manual.

Because of inherent limitations in control systems, errors or irregularities may occur and not be detected. In addition, projection of any evaluation of systems to future periods is subject to risk, inasmuch as procedures may become inadequate as a result of changes in conditions, or the degree of compliance with the procedures may deteriorate. (See Appendix B, *Statement of Internal Controls*.)

Our audit disclosed certain conditions which, in our opinion, if not corrected, could result in errors and irregularities. Areas needing improvement are found in the Executive Summary.

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.

CASH RECEIPTS [6]

Cash controls at the student health center were inadequate. Adequately controlling cash collections and deposits reduces exposure to loss as a result of inappropriate acts.

ACCOUNTS RECEIVABLE [7]

Employee payroll receivables were not collected/discharged in a timely manner. Ensuring the timely follow-up and collection of payroll receivables increases working capital and decreases the potential for loss of revenue from uncollectable accounts.

PAYROLL/PERSONNEL [8]

Pre-authorization of overtime procedures was inadequate. Obtaining pre-authorization for overtime reduces the risk of unnecessary overtime payments.

FIXED ASSETS [9]

Property disposition procedures and records were inadequate. Obtaining prior written approval by the property survey board increases accountability over property disposals.

FISCAL INFORMATION TECHNOLOGY [10]

INFORMATION SECURITY [10]

The automatic logoff feature for user inactivity of the financial reporting system (FRS) application was not operational. The implementation of automatic logoff procedures decreases the risk of inappropriate access to confidential data by unauthorized individuals.

APPLICATION CHANGE PROCEDURES [11]

The campus had not established adequate segregation of duties over application change procedures. Proper segregation of duties over the application change process decreases the risk of unauthorized system changes and errors.

SYSTEM DEVELOPMENT METHODOLOGY [12]

The campus system development methodology (SDM) was not formally documented. Formally documenting the SDM decreases the risk of application implementation errors.

OBSERVATIONS, RECOMMENDATIONS, AND CAMPUS RESPONSES

CASH RECEIPTS

Cash controls at the student health center were inadequate.

We found that:

- ▶ two employees worked from the same cash drawer with no intervening close-out; and,
- ▶ the system used to receipt cash did not provide an audit trail to identify the individual completing a transaction.

SAM §20003 states, in part, that there should be an established system of authorization and record keeping procedures adequate to provide effective accounting control over assets, liabilities, revenues, and expenditures.

According to the health center's associate director, implementation of the new computer system (Med Pro) changed the cash operations from one cash drawer to two. She also pointed out that Med Pro does not distinguish between individuals performing transactions.

Inadequate internal controls over cash receipts increase exposure to loss from inappropriate acts.

Recommendation 1

We recommend that the campus ensure that appropriate cash controls over cash drawers are implemented at the student health center.

Campus Response

We concur.

MedPro, the vendor for the software application used by the Student Health Center, will provide a new cash reconciliation report later this summer which will identify the individual who processes the transaction. This new report will be put in use when the Student Health Center reopens in August. Staff will be instructed to log out when changing cashiers.

The vendor is developing further reporting enhancements to the application which are scheduled to be released later this fall. Effective January 1, 2000, the application software will have the capability of providing separate cash reconciliation reports for each cashier/cash drawer.

ACCOUNTS RECEIVABLE

Employee payroll receivables were not collected/discharged in a timely manner.

We noted that:

- ▶ Three of six employee payroll receivable files reviewed did not contain any documentation regarding follow-up activity.
- ▶ Relief from accountability and local write-off options were not being utilized for 4 of the 6 delinquent payroll accounts receivable reviewed.
- ▶ Tax offset procedures were not utilized for 4 of the 6 delinquent payroll accounts receivable reviewed.

SAM §8776.6 provides specific criteria for collecting outstanding amounts owed the university including the sending of three follow-up letters at thirty-day intervals after the initial billing and the use of tax offset.

SAM §8776.7 also established procedures for the collection of outstanding accounts receivable. If all reasonable collection efforts do not result in payment, the campus may request relief from accountability of uncollectable amounts from the State Board of Control.

Executive Order No. 616 delegates to the campuses the authority to write-off debts of \$1,000 or less, which are either uncollectable or the amount(s) involved do not justify the cost of collection.

The payroll supervisor stated that it was her understanding that delinquent accounts once forwarded to financial aid accounting for submission to FTB for tax offset, remained on file until collected. She also stated that the documentation supporting follow-up action on the 3 files referenced above had been accidentally purged.

Not ensuring timely follow-up and collection of payroll receivables increases the potential for loss of revenue from uncollectable accounts and decreases working capital.

Recommendation 2

We recommend that the campus:

- a. establish procedures to timely manage and follow up on outstanding employee payroll receivables; and,

- b. strengthen procedures to ensure the timely local write-off and relief from accountability procedures for accounts deemed uncollectable.

Campus Response

We concur.

Procedures have been established in accordance with State Administrative Manual requirements for the timely follow-up on outstanding employee payroll receivables. A time schedule was developed and adopted for local write-off and for requesting relief from accountability for payroll accounts receivable/salary advances deemed uncollectable. The campus has taken action to write-off and request relief from accountability for all uncollectable payroll accounts receivables. Copies of supporting documentation for the requests were either provided during audit field work or forwarded under separate cover on February 17, 1999.

PAYROLL/PERSONNEL

Pre-authorization of overtime procedures was inadequate.

There was no documentation to support the pre-authorization of overtime worked for any of the 10 1998-99 overtime payments selected for review.

SAM §8540 requires that, as a general practice, compensation for overtime, either by cash payment or time off, should be based upon prior written approval signed by a designated supervisor.

The payroll supervisor indicated that the payroll department did not monitor this activity and it was left up to the departments to ensure that pre-authorizations were obtained prior to overtime work, if practical.

Not obtaining pre-authorization for overtime increases the risk of unnecessary overtime payments.

Recommendation 3

We recommend that the campus improve procedures to ensure that all overtime work is pre-authorized and properly approved. When it is not practical to do so, we recommend that an explanation of exceptions be completed on form (Std. 682), *Authorization for Extra Hours*.

Campus Response

We concur.

Campus departments will be notified and advised that all overtime work must be preauthorized in writing in advance of the work being performed. In cases where this is impractical due to emergency situations, approval will be retroactive. All supporting documentation will be retained by the employing campus department. This recommendation will be implemented by July 1, 1999. In keeping with current practice, the Payroll Department will not process any requests for overtime, either compensable by cash or time off, without receipt of properly executed and approved Overtime and Call Back Hours Reports.

FIXED ASSETS

Property disposition procedures and records were inadequate.

We found that:

- ▶ sixteen of twenty items in our review did not include the date of physical property disposition.
- ▶ three of twenty items in our review were disposed prior to approval by the property survey board.

SAM §20003 requires a system of authorization and record keeping procedures adequate to provide effective accounting control over assets.

SAM §3520.2 requires each agency to have a duly appointed property survey board. It is the responsibility of the board to determine that the best interest of the state is served in disposing of state property. At least two members of the property survey board must approve all property survey reports and transfer of location of equipment.

The property clerk indicated that he consistently contacts members of the property survey board by telephone to obtain approval when disposal of property is necessary prior to the next scheduled property survey board meeting. No documentation is maintained to evidence such approvals.

Failure to obtain written approval of the property survey board reduces accountability over property dispositions.

Recommendation 4

We recommend that the campus:

- a. dispose of property only after the property survey board has approved of such disposition in writing and;
- b. ensure that property records are updated to reflect all actions regarding disposal.

Campus Response

We concur.

In cases where it is necessary to dispose of University property prior to the next scheduled Property Survey Board meeting, the property clerk will solicit approval from the board members via a newly created form which identifies the item and requested disposition. Written approval of at least three board members will be required prior to disposal of any property. The date the property is physically disposed of will be entered into the University's property inventory system. Both of these recommendations have been implemented.

FISCAL IT

INFORMATION SECURITY

There was no automatic logoff feature for user inactivity in the campus financial reporting system (FRS) application.

SAM §20003 requires, in part, that there be a plan that limits access to State agency assets to authorized personnel who require these assets in the performance of their assigned duties.

To ensure that access is limited to authorized users, applications should automatically log off users after a period of inactivity.

The system administrator indicated that, according to digital technical support, there is no logoff feature available in the VMS operating system. The systems analyst stated that according to BMS technical support, there has not been any auto-logoff feature available in their FRS application. Reliance for maintaining security has been placed on proper user training and appropriate access control.

Without the automatic logoff feature, unauthorized personnel could gain access to CSU systems and confidential data.

Recommendation 5

We recommend that the campus install/develop an automatic logoff feature in the FRS system to ensure that appropriate security is maintained in the event of user inactivity.

Campus Response

We concur.

At our initiation, the Chancellors Office made an automatic logoff feature available in the Compaq DIGITAL OpenVMS version of the FRS application on May 7, 1999. We will install the feature by July 31, 1999.

APPLICATION CHANGE PROCEDURES

The campus had not established adequate segregation of duties over application change procedures.

Employees are allowed to move applications from the testing environment into the production environment, which does not provide for an adequate separation of duties.

SAM §8080.1 indicates that a key element in a system of internal audit is separation of duties. Employees should not be allowed to move their own developments and changes from test to production environment.

The system analyst indicated that programmers have installed their own changes because there are not enough other appropriately qualified personnel to perform this task in the small fiscal IT environment. Reliance for detecting improper alteration of data has been placed on reporting and balancing controls.

Without adequate separation of duties, there is an increased risk of unauthorized system changes and errors.

Recommendation 6

We recommend that the campus review their change control procedures to ensure that appropriate compensating controls are implemented for application installation and changes to the production environment.

Campus Response

We concur.

We will review our change control procedures and formalize them in a document by October 31, 1999. We are currently using the Accounting Report Control model (Option #1 in the list proposed by Richard Teal, IT Auditor, in an email of May 12, 1999).

SYSTEM DEVELOPMENT METHODOLOGY

The campus system development methodology (SDM) was not formally documented.

A documented SDM provides guidelines in developing controlled application systems that will produce consistent results and satisfy user requirements. The documentation defines the phases, activities, responsibilities, and end products needed to bring discipline and consistency during a system development process.

The system analyst indicated that a documented SDM has not been produced because in the small environment of fiscal IT, the methodology has been informal and understood rather than formally articulated and written down. Face-to-face communication has been relied on in place of formal signoffs.

Not documenting system development methodology procedures increases the cost of development, the risk of overruns, and confusion between users and programmers.

Recommendation 7

We recommend that the campus document the SDM and include the specific phases, tasks, and definitions that are needed to develop an adequate application.

Campus Response

We concur.

We will document a system development methodology by December 31, 1999.

APPENDIX A: PERSONNEL CONTACTED

<u>Name</u>	<u>Title</u>
Alistair McCrone	President
Teri Bronder-Lewis	Information Specialist, Enrollment Management
Don Christensen	Vice President, Development & Administrative Services
Debbie Coles	Assignments Coordinator
Patti Clinton	Accounting Officer
Nick DeRuyter	System Administrator, Information Technology
Tami Evans	Clerical Assistant, Enrollment Management
Sandra Fedder	Payroll Supervisor
Dick Giacolini	Director, Contracts, Procurement and Risk Management
Katherine Granfield	System Analyst, Fiscal Affairs
Doris Gunther	Accounting and Accounts Payable Supervisor
Kathleen Heil	Director, Graphics and Distribution Services
Diana Hensen	Clerical Assistant, Health Center
Conine Higgins	Cashiering Supervisor
Vicki Kauffman	Secretary, Enrollment Management
Lori Kerrigan	Manager, Financial Aid Accounting
Ann Kimbrow	Associate Director, Health Center
Rita Limmer	Senior Housing Cashier
Zena Lundberg	Supervisor, Financial Aid Accounting
Paul Meyer	Property Clerk
Lynda Moore	Director, Personnel
Carolyn Mueller	Executive Assistant to the President
Sandi O'Dell	Clerical Assistant, Health Center
Dave Simpson	Associate Director, Information Technology
Lee Anne Smith	Cashier
Donna Sorensen	Director, Fiscal Affairs
John Westmoreland	Supervisor, Distribution Services

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.