

FISMA

California Maritime Academy

Report Number 98-08

December 15, 1998

Members, Committee on Audit

Stanley T. Wang, Chair
Ali C. Razi, Vice Chair
William D. Campbell Ronald L. Cedillos
Harold Goldwhite Eric C. Mitchell
Joan Otomo-Corgel Ralph R. Pesqueira
Frederick W. Pierce, IV

Staff

University Auditor: Larry Mandel
Senior Director: Norman Buettner
Staff Auditor: Stacey Adams

BOARD OF TRUSTEES

THE CALIFORNIA STATE UNIVERSITY

CONTENTS

INTRODUCTION

Purpose.....	1
Scope and Methodology.....	1
Background	3
Opinion.....	3
Executive Summary.....	4

OBSERVATIONS, RECOMMENDATIONS, AND CAMPUS RESPONSES

Cash Receipts.....	6
Segregation of Duties.....	6
Safeguarding of Receipts	6
Restrictive Endorsements	8
Purchasing	8
Receiving	8
Procurement Cards.....	9
Fixed Assets.....	10
Fiscal IT.....	11
Computer Room Security and Information Management.....	11
Data Security Configuration	12
Disaster Recovery Plan.....	13
Offsite Backup	14

APPENDICES

APPENDIX A:	Personnel Contacted
APPENDIX B:	Statement of Internal Controls
APPENDIX C:	Campus Response
APPENDIX D:	Chancellor's Acceptance

ABBREVIATIONS

A/P	Accounts Payable
B of A	Bank of America
CIRS	Customized Information Retrieval System
CO	Chancellor's Office
CPU	Central Processing Unit
CSEA	California State Employees Association
CSU	California State University
CMA	California Maritime Academy
CME	Continuing Maritime Education
FAS	Financial Accounting System
FRS	Financial Reporting System
FISMA	Financial Integrity and State Manager's Accountability Act
G/LGeneral Led
IT	Information Technology
LAN	Local Area Network
MPR	Monthly Purchase Report
PO	Purchase Order
PSR	Property Survey Report
PTF	Payroll Transaction Form
RACF	Resource Access Control Facility
SCO	State Controller's Office
SDM	System Development Methodology
SO	Service Order
SAM	State Administrative Manual
SRR	Stock Received Report
SUAM	State University Administrative Manual
TEC	Travel Expense Claim
UPS	Uninterruptible Power Supply

INTRODUCTION

PURPOSE

The principal audit objective was to assess the adequacy of controls and systems to ensure 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/ payroll records and processing areas are restricted;
- ▶ purchase and disposition of fixed assets are controlled and assets are promptly recorded 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 1997-98 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 through September 1998. Our primary focus was on internal controls, and 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 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 make recommendations in areas requiring 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 state agencies to 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 responsible for conducting such audits within the CSU. This report represents our biennial review.

OPINION

We visited the CMA campus from August 17, 1998, through October 9, 1998, 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 and administrative 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 remain undetected. 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. Specifically, the campus does not maintain adequate internal control over the following areas: cash receipts, purchasing and fiscal information technology.

EXECUTIVE SUMMARY

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

CASH RECEIPTS [6]

SEGREGATION OF DUTIES [6]

There was inadequate segregation of duties within the cashier's office. This is a repeat finding from our prior FISMA audit. Proper segregation of duties reduces the risk that state monies will be misappropriated.

SAFEGUARDING OF RECEIPTS [6]

Checks received in the admissions office were not adequately safeguarded prior to their deposit with the cashier's office. Safeguarding negotiable instruments reduces the risk that funds will be lost or stolen.

RESTRICTIVE ENDORSEMENTS [8]

Checks received at housing and residential life, admissions, and the galley were not restrictively endorsed by the end of each day. The timely endorsement of checks and money orders decreases the potential risk of misuse if lost or stolen.

PURCHASING [8]

RECEIVING [8]

Purchased goods are oftentimes receipted by the ordering department rather than the receiving department. This is a repeat finding from our prior FISMA audit. Proper delivery and receipt procedures ensure that all goods purchased and paid for are actually received and in satisfactory condition.

PROCUREMENT CARDS [9]

Procedures for approving payment of procurement card transactions were not being followed. Adherence to campus controls regarding procurement card purchases reduces the risk of unauthorized card purchases.

FIXED ASSETS [10]

Procedures regarding both tagging and recording of property items were unsatisfactory. Tagging and properly recording acquisitions reduces the potential for property to be lost or stolen and ensures that property inventory records are accurate.

FISCAL IT [11]

COMPUTER ROOM AND DATA SECURITY [11]

Computer room security and Data Security was inadequate. Ensuring that the computer room is secure and data security reports are periodically reviewed reduces the risk of theft, damage, and unauthorized access to the computers.

DATA SECURITY CONFIGURATION [12]

The setup configuration for passwords in the system security software is inadequate. Adequate configuration setup reduces the risk that unauthorized personnel will gain access to CSU systems and confidential data.

DISASTER RECOVERY PLAN [13]

A disaster recovery plan has not been developed for the information technology environment. A disaster recovery plan identifies critical applications that must be recovered in an emergency.

OFFSITE BACKUP [14]

Backup data for the local area network (LAN) was not stored offsite. Offsite storage reduces the risk that data will be lost during a disaster.

OBSERVATIONS, RECOMMENDATIONS, AND CAMPUS RESPONSES

CASH RECEIPTS

SEGREGATION OF DUTIES

There was inadequate segregation of duties within the cashier's office. This is a repeat finding from our prior FISMA audit.

After receiving cash through the mail and over the counter, the cashier prepared deposits and student invoices.

SAM § 8080 states "No one person shall perform more than one of the following seven types of duties: (1) Receiving and depositing remittances...(7) Initiating or preparing invoices."

The accounting manager stated that because of the small size of the campus, many employees must perform multiple duties.

Inadequate segregation of duties increases the risk that state monies will be misappropriated.

Recommendation 1

We recommend that the campus adequately segregate duties within the cashier's office.

Campus Response

We concur with the recommendation as it applies to SAM 8080. However, the size of our staff does not allow us to have complete segregation of duties as stated in SAM 8080. We attempt to mitigate our risk from this issue by performing reconciliations between our accounts receivable records residing in our accounting office and the cashier records. In the specific case cited, the cashier assists in the preparation of student invoices. Invoices are pre-numbered and copies transferred to our accounting department.

As cash is received, there are reconciliations between the accounts receivable ledger (and subsequent collection procedures) kept in the accounting office to those records kept in the cashier's office. Receipt numbers are sequentially assigned by our computer system and are reviewed for completeness by the accounting office.

SAFEGUARDING OF RECEIPTS

Checks received in the admissions office were not adequately safeguarded prior to their deposit with the cashier's office.

For example:

- ▶ Checks and money orders were placed in an envelope and held in the admissions counselor's office. Although the office is locked after hours and when she is away for extended periods, personnel and visitors have access to this office during working hours.
- ▶ Transfer receipts were not used when checks were sent to the cashier.
- ▶ Checks were not properly accounted for prior to deposit.

SAM § 8021 states:

". . . A separate series of transfer receipts will be used to localize accountability for cash or negotiable instruments to a specific employee from the time of its receipt to its deposit."

SAM § 8032.1 states:

" . . . Agencies that do not have a safe, vault, or money chest that is adequate to safeguard cash will accumulate collections until they amount to \$250 in cash or \$10,000 in cash, checks, money orders, and warrants . . . whichever occurs first."

The admissions counselor stated that she was not aware of the requirement to use transfer receipts when submitting funds to the cashier for deposit.

Failure to properly secure cash receipts and non-use of transfer receipts increases the risk for loss or misuse of funds.

Recommendation 2

We recommend that the campus:

- a. implement procedures for adequately safeguarding checks received in the admissions office
- b. utilize transfer receipts when transmitting funds from the admissions office to the cashier.

Campus Response

We concur with the recommendation. We have already discussed this issue on campus and have issued campus policy relating to the acceptance of checks and the safeguarding of assets. The policy requires that any department accepting and holding checks restrictively endorse the checks and store them in a secure area until transfer to the cashier's office.

For those departments referenced in the audit, we have already issued endorsement stamps and reviewed their cash handling procedures. These procedures have already been implemented.

RESTRICTIVE ENDORSEMENTS

Checks received at housing and residential life, admissions, and the galley were not restrictively endorsed by the end of each day.

Some units were holding deposits as long as one week, thereby exposing the unendorsed checks to further risk of misappropriation.

For example:

- ▶ Funds received at housing and residential life were deposited weekly.
- ▶ Funds received at the admissions office are deposited weekly, unless a large volume of checks is received in one day.

SAM § 8023 states that “all checks, money orders, and warrants received for deposit will be restrictively endorsed for deposit as soon as practicable after receipt, but no later than the end of the working day.”

The director of food service, the assistant director of housing and residential life, and the admissions counselor all stated that it has not been their practice to endorse negotiable instruments.

When checks and money orders are not endorsed timely, there is an increased potential for misuse of lost or stolen negotiable instruments.

Recommendation 3

We recommend that the campus implement procedures to ensure that all negotiable instruments are restrictively endorsed by the end of each working day.

Campus Response

See Safeguarding of Receipts above.

PURCHASING

RECEIVING

Purchased goods are oftentimes receipted by the ordering department rather than the receiving department. This is a repeat finding from our prior FISMA audit.

Only the receiving coordinator and the receiving assistant have access to Stock Received Reports (SRR), which must be completed and forwarded to Accounting for vendor payments. When end users receive the goods, they do not contact the receiving department to have an SRR completed.

SAM § 8422.20 states that “The Agency’s receiving department will prepare Stock Received Reports...”

The receiving coordinator and receiving assistant expressed concern about completing Stock Received Reports for goods that were not delivered to central receiving, as they must rely on the end users’ assertions regarding the condition and quality of goods received. The director of finance and information technology stated that staff was inadvertently not following both campus and SAM policy.

When purchases are not delivered directly to central receiving, verification that orders are complete and in satisfactory condition is compromised.

Recommendation 4

We recommend that the campus implement procedures to ensure that purchased items are delivered directly to central receiving.

Campus Response

We concur with this recommendation. It is CMA's policy that our receiving department receipts all purchased goods. We have made improvement from the time of the recommendation on our last FISMA audit; however, we do have room for improvement.

We will send a memo to departments stating their responsibility to send purchased goods through receiving for proper receipting. This memo will be issued by March 31, 1999.

PROCUREMENT CARDS

Procedures for approving payment of procurement card transactions were not being followed.

For example:

- ▶ Four statement reconciliations were not initialed by either the cardholder or approving official.
- ▶ Nine statement reconciliations were not dated by either the cardholder or the approving official.
- ▶ One Monthly Purchase Report lacked the approving official’s signature.

The California Maritime Academy Credit Card Procurement Handbook states that the cardholder will initial and date the bank statement next to the total amount, at the top right on page one. The Handbook also states that the approving official will initial and date the cardholder bank statement next to the total amount at the top right of page one and sign and date the cardholder’s Monthly Purchase Report.

The accounting manager stated that initialing and dating the bank statement is a duplicate effort, as the cardholder and the approving official must sign the Monthly Purchase Report. The director of finance and information technology feels that the handbook should be modified to reflect this.

The risk of unauthorized procurement card purchases is increased when control procedures contained in the Procurement Card Handbook policies are not adhered to.

Recommendation 5

We recommend that the campus strengthen credit card purchase procedures.

Campus Response

We concur with this recommendation. The procurement card has been in a pilot process (2 departments) for a period of three months. Our policies and procedures relating to the procurement card are well documented, however, we agree that compliance with the policies and procedures could be improved.

We audit our procurement card process on a quarterly basis and will emphasize the need for compliance with policies and procedures, especially as they relate to the payment approval process. After each of these audits, we will provide additional training, focusing on deficiencies uncovered in the audit. This has been integrated into our plans for implementation of the procurement card.

FIXED ASSETS

Procedures regarding both tagging and recording property items were unsatisfactory.

For example:

- ▶ Four of ten equipment items tested had not been tagged upon inspection.
- ▶ Two of the ten items tested could not be located on the inventory listing. These items also accounted for two of the four items noted above that were not tagged
- ▶ Serial number and model number information was inaccurately listed on the campus inventory for two of the ten items tested.

SAM § 8651 requires all state property to be tagged after acquisition. To maintain a comprehensive listing of all campus property, items should be added to the inventory listing upon acquisition.

The purchasing manager stated that the two items not included on the inventory listing were mere oversights. Additionally, the two items with inaccurate information in the inventory listing were due to a return of those two items that were not processed properly.

When property is not tagged and entered on the property inventory, property records are understated and there is an increased potential that property will be lost or stolen.

Recommendation 6

We recommend that the campus strengthen procedures to ensure that all property acquisitions are tagged and entered accurately and timely on the campus inventory listing.

Campus Response

We concur with this recommendation. Current CMA procedures address most of the compliance issues noted in the audit. However, we agree that compliance with these procedures could be improved.

We will review our current policies and procedures to see if there are areas that could be improved. We will send a memo to the receiving department reminding them of the importance of tagging and updating our fixed asset records. We have already had meetings and will provide additional training to the receiving staff to stress the importance of following procedures. This will be completed by June 30, 1999.

FISCAL IT

COMPUTER ROOM AND DATA SECURITY

Computer room security and Data Security was inadequate.

The computer room has limited protection from break-ins and environmental hazards. We found that the windows to the computer room could easily be broken, which would allow access to the room to be made from the outside. In addition, there were no fire extinguishers, and a raised floor had not been installed to protect wiring or prevent water damage.

There was no periodic review of data security configuration and reports.

A secure computer room should include raised floors, fire and smoke detectors, sealed walls and floors, and automatic fire suppression. Additionally, a periodic review of data security reports helps to detect whether unauthorized users have access to sensitive information.

The director of finance and information technology stated that, due to the small size of the campus and a limited number of personnel having access to the computer room and data, a secure computer room and review of data security reports has not been a high priority.

Inadequate computer room security could allow computers to be stolen or damaged by fire or water. Additionally, failure to periodically review security reports could lead to unauthorized personnel having access to sensitive data.

Recommendation 7

We recommend that management improve the security environment of the computer room and periodically review data security reports.

Campus Response

We concur with this recommendation. Over the past three years, CMA has made great strides in its use of technology. The information technology infrastructure has not been developed as quickly as we would like. The computer room was designed as an office space located next to our campus computer lab, rather than as a computer operations room. Creating the computer area alluded to in the recommendation would take a monetary allocation that is currently not available to CMA.

We have installed fire extinguishers and are planning to address the problem with the computer room windows. Our completion date will be dictated by the available of funding for a new computer room.

DATA SECURITY CONFIGURATION

The setup configuration for passwords in the system security software was inadequate.

We found that:

- ▶ there was no password character length requirement in the resource access control facility (RACF);
- ▶ password failures were allowed for up to 15 attempts; and,
- ▶ passwords were not periodically changed in Windows NT.

Passwords should be changed periodically, restricted to an acceptable number of unsuccessful attempts and require at least six to eight characters.

The director of finance and information technology stated that, due to the small number of persons with access to the CMA system, the impact of new technology to circumnavigate data security systems had not been periodically reviewed.

Inadequate system security software could allow unauthorized users to guess passwords, thereby giving them access to campus systems and confidential data.

Recommendation 8

We recommend that the campus:

- a. improve the data security configuration on password requirements to six or eight characters in RACF;
- b. reduce the number of password attempts to three before sign on is revoked in RACF; and

- c. determine and implement a periodic password change in Windows NT.

Campus Response

We concur with this recommendation. We do have policies relating to data and computer security, however, we have not formalized procedures relating to the monitoring and control of passwords on campus.

We have performed a general risk analysis against the data currently residing on our network computers and have determined that we have limited risk relating to the information residing on our network. We do plan to improve our security structure and reporting as it relates to information residing on our network in the next fiscal year. We will formalize procedures relating to the monitoring and control of passwords by September 30, 1999.

Our Financial Resource System is maintained by the Chancellor's Office. We had been under the impression that security reports and configuration were being reviewed at the Fresno data center (CMA currently pays \$60,000 for license and \$50,000 for direct support of this system). We will review the responsibility of security with the Chancellor's Office and provide for the review of reports and the data security configuration on a periodic basis. We will implement these procedures by June 30 1999.

DISASTER RECOVERY PLAN

A disaster recovery plan had not been developed for the campus information technology environment.

Effective risk management requires the development and implementation of a disaster recovery plan.

The director of finance and information technology stated that technology at CMA had not previously reached a level of sophistication to require disaster recovery planning.

Without a disaster recovery plan, the campus cannot ensure continuity of computing operations for support of critical applications, maximize the use of remaining resources, or achieve an orderly migration toward the resumption of all computing services.

Recommendation 9

We recommend that the campus develop a disaster recovery plan for its information technology environment.

Campus Response

We concur with this recommendation.

We have performed a general risk analysis against the data currently residing on our network computers and have determined that we have limited risk relating to the information residing on our network. We are targeting December 31, 1999 to the drafting of an information technology disaster recovery plan.

OFFSITE BACKUP

Backup data for the local area network (LAN) was not stored offsite.

We found that the applicable backup data was stored in a file cabinet within the room containing the LAN.

Backup media should be sent periodically to a site that is not located within the same vicinity and subject to a concurrent disaster.

The director of finance and information technology stated that due to costs, a local file cabinet was selected as the storage site.

In the event of a disaster, the campus could lose critical data that could effect operating capacity and efficiency.

Recommendation 10

The campus should research the cost of either sending its backup information to a storage facility outside the Bay area or send information via electronic transfer. Either alternative should be implemented accordingly.

Campus Response

Currently, we do not store our back-ups at an off-site storage facility. This is due to the limited data that currently resides on our computer network. We do store our back-ups in a fireproof safe in the computer room. For an interim step, we will explore moving this safe to another part of campus.

During the next year, we will study our computer needs and develop a computer disaster recover plan that will be integrated into the campus emergency plan. We will target December 31, 1999 for the formalization of the plan.

APPENDIX A: PERSONNEL CONTACTED

<u>Name</u>	<u>Title</u>
Jerry Aspland	President
Janice Beitler	Accountant II
Pat Beitler	Admissions Counselor
Marjo Crowley	Director, Human Resources
Victor Culatta	Director, Housing and Residential Life
Vineeta Dhillon	Purchasing Assistant
Pamela Elbeck	Accounting Technician
Edward Gerry	Receiving Coordinator
Brian Goldman	Network Analyst
Gale Gomez	Cashier
Eric Heuer	Director, Food Services
Emile Jackson	Secretary, Housing and Residential Life
Jill Johns	Business Manager
Susan Johnson	Accounts Payable Lead
Donna Lichty	Buyer
Sylvester Morris	Director, Public Safety
Les Ojeda	Receiving Assistant
Roger Ono	Director, Finance and Information Technology
Mary Pierce	Purchasing Manager
Richard Ratkey	Accountant I
Christy Redford	Accounting Manager
Cheri Sims	Payroll Technician II
Peg Solveson	Assistant Director, Housing and Residential Life
Monna Throop	Assistant Manager, Food Services
Ken Toet	Controller, CMA Foundation

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.