

**FISMA**

**CALIFORNIA STATE UNIVERSITY  
OFFICE OF THE CHANCELLOR**

**Audit Report 09-09  
March 25, 2010**

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## **ABBREVIATIONS**

CMS	Common Management Systems
CO	Office of the Chancellor
CST	Calstate TEACH
CSU	California State University
EHDB	Employment History Database
EO	Executive Order
FISMA	Financial Integrity and State Manager's Accountability Act
GC	Government Code
HR	Human Resources
ID	Identification
IP	International Programs
PIMS	Personnel/Payroll Information Management System
PS	PeopleSoft
SAM	State Administrative Manual

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## EXECUTIVE SUMMARY

The California Legislature passed the Financial Integrity and State Manager's Accountability Act (FISMA) of 1983, Government Code (GC) Sections 13400 through 13407. This act requires state agencies to establish and maintain a system of internal accounting and administrative control. To ensure that the requirements of this act are fully complied with, state entities with internal audit units are to complete biennial internal control audits (covering accounting and fiscal compliance practices) in accordance with the *International Standards for the Professional Practice of Internal Auditing* (Institute of Internal Auditors) as required by GC Section 1236. The Office of the University Auditor of the California State University (CSU) is currently responsible for conducting such audits within the CSU.

Office of the Chancellor (CO) management is responsible for establishing and maintaining adequate internal control. This responsibility, in accordance with GC Sections 13402 et seq., includes documenting internal control, communicating requirements to employees, and assuring that internal control is 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 control 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.
- ▶ Established controls are not only effective but also promote operational efficiency.
- ▶ Financial operations are conducted in accordance with policies and procedures established in the State Administrative Manual, Education Code, Title 5, and Trustee policy.

We visited the CO from October 12, 2009, through November 6, 2009, and made a study and evaluation of the accounting and administrative control in effect as of November 6, 2009. This report represents our biennial review.

Our study and evaluation revealed certain conditions that, in our opinion, could result in errors and irregularities if not corrected. Specifically, the CO did not maintain adequate internal control over the following areas: cash receipts, accounts receivable, cash disbursements, and payroll. These conditions, along with other weaknesses, are described in the executive summary and body of this report.

In our opinion, except for the effect of the weaknesses described above, the CO accounting and administrative control in effect as of November 6, 2009, taken as a whole, was sufficient to meet the objectives stated above.

As a result of changing conditions and the degree of compliance with procedures, the effectiveness of controls changes over time. Specific limitations that may hinder the effectiveness of an otherwise adequate system of controls include, but are not limited to, resource constraints, faulty judgments,

unintentional errors, circumvention by collusion, and management overrides. Establishing controls that would prevent all these limitations would not be cost-effective; moreover, an audit may not always detect these limitations.

The following summary provides management with an overview of conditions requiring 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 [7]**

The CO did not maintain an inventory control system for parking permits sold to CO employees, nor did it reconcile parking permits sold to cash receipts.

### **ACCOUNTS RECEIVABLE [7]**

Administration of third-party accounts receivable for CalState TEACH and International Programs needed improvement. Accounts receivable reconciliations for the months of July, August, and September 2009 were not signed and dated by the preparer and a reviewer.

### **CASH DISBURSEMENTS [10]**

The CO could not provide evidence of its efforts to periodically request local banks to search for unauthorized bank accounts that use the CO name, address, and/or federal identification number.

### **PAYROLL [10]**

Duties and responsibilities related to certain payroll functions were not properly segregated.

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## INTRODUCTION

### **STATEMENT OF INTERNAL CONTROLS**

Internal accounting and related operational controls established by the State of California, the California State University Board of Trustees, and the Office of the Chancellor (CO) 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. The ultimate responsibility for good internal control rests with management.

Internal control, in the broad sense, includes controls that 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 recordkeeping and accounting reports from those concerned with operations or asset custody, physical controls over assets, personnel of a quality commensurate with responsibilities, and an effective system of internal review.

#### 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.

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.

Experience indicates that the existence of certain danger signals will usually be indicative of a poorly maintained or vulnerable control system. These symptoms may apply to the organization as a whole or to individual units or activities, and generally include any of the following danger signals:

- ▶ Policy and procedural or operational manuals are either not currently maintained or are non-existent.
- ▶ Lines of organizational authority and responsibility are not clearly articulated or are non-existent.
- ▶ Financial and operational reporting is not timely and is not used as an effective management tool.

- ▶ Line supervisors ignore or do not adequately monitor control compliance.
- ▶ No procedures are established to assure that controls in all areas of operation are evaluated on a reasonable and timely basis.
- ▶ Internal control weaknesses detected are not acted upon in a timely manner.
- ▶ Controls and/or control evaluations have little relationship to organizational exposure to risk of loss or resources.

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.

### **PURPOSE**

The principal audit objectives were to assess the adequacy of the systems of internal accounting and administrative control and to determine whether financial operations were conducted in accordance with policies and procedures established in the State Administrative Manual, Education Code, Title 5, and directives of the Board of Trustees and the CO. Specifically, we sought assurances that:

- ▶ Legal and regulatory requirements are complied with.
- ▶ 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, systems output, or accounting entries are reviewed and approved.
- ▶ Management does not intentionally override internal controls to the detriment of 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 recordkeeping, inappropriate accounting, fraudulent financial reporting, financial loss, and exposure.

## **SCOPE AND METHODOLOGY**

Our study and evaluation were conducted in accordance with the *International Standards for the Professional Practice of Internal Auditing* issued by the Institute of Internal Auditors, and included the audit tests we considered necessary in determining that accounting and administrative controls are in place and operative. The management review emphasized, but was not limited to, compliance with state and federal laws, Board of Trustee policies, and CO policies, letters, and directives. For those audit tests that required annualized data, fiscal year 2008/09 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 February 1, 2008, to September 30, 2009. Our primary focus was on internal controls.

A preliminary survey of the campus was used to identify risks. Risk was defined as the probability that an event or action would adversely affect the campus. Our assessment of risk was based upon a systematic process using management's feedback and 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.

Based upon this assessment of risks, we specifically included within the scope of our review the following:

- ▶ Procedures for receipting and storing cash, segregation of duties involving cash receipting, and recording of cash receipts.
- ▶ Administration and reconciliation of bank accounts.
- ▶ Establishment of receivables and adequate segregation of duties regarding billing and payment of receivables.
- ▶ Adequate segregation of duties regarding authorization and payment of cash disbursements and appropriate controls over campus vendors.
- ▶ Approval of purchases and reconciliation of expenditures to State Controller's balances.
- ▶ Authorization and proper classification of personnel/payroll transactions.
- ▶ Posting of the property ledger and monthly reconciliation of the property to the general ledger.
- ▶ Access restrictions to accounting systems.
- ▶ Accounting of trust funds.

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INTRODUCTION

We have not performed any auditing procedures beyond November 6, 2009. Accordingly, our comments are based on our knowledge as of that date. Since the purpose of our comments is to suggest areas for improvement, comments on favorable matters are not addressed.

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## **OBSERVATIONS, RECOMMENDATIONS, AND MANAGEMENT RESPONSES**

### **CASH RECEIPTS**

The Office of the Chancellor (CO) did not maintain an inventory control system for parking permits sold to CO employees, nor did it reconcile parking permits sold to cash receipts.

State Administrative Manual (SAM) §7920 states that each agency is responsible for completing any reconciliation necessary to safeguard assets and ensure reliable financial data.

SAM §20050 states that the elements of a satisfactory system of internal accounting and administrative controls shall include a system of authorization and recordkeeping procedures adequate to provide effective accounting control over assets, liabilities, revenues, and expenditures.

The manager of emergency management, safety, and compliance stated that most employee parking permits were paid via payroll deduction. She also stated that additional controls in this area were not considered necessary, as payments by cash or check were minimal and only received from new or temporary employees.

Inadequate control over parking permit inventories and cash receipts increases exposure to loss from inappropriate acts.

#### **Recommendation 1**

We recommend that the CO perform an inventory of parking permits and reconcile the parking permits to cash receipts.

#### **Management Response**

We concur with the recommendation. An inventory was completed October 14, 2009, and all employee parking permits and temporary parking permits were accounted for. Written procedures were prepared and implemented in connection with the identification of cash receipts, the recording of permit numbers, and the tracking of the inventory of permits. Staff with responsibility for receiving cash and issuing permits has been fully trained on these procedures.

### **ACCOUNTS RECEIVABLE**

#### **COLLECTIONS AND WRITE-OFF**

Administration of third-party accounts receivable for CalState TEACH (CST) and International Programs (IP) needed improvement.

We found that:

- ▶ A sequence of three collection letters in 30-day intervals were not sent for 7 of 11 CST receivables that were 360 days past due as of June 30, 2009. Additionally, there was no documented evidence of collection correspondences (i.e., e-mails, phone call log) on file to support supplemental collection efforts, nor were the accounts considered for further administrative action or write-off.
- ▶ IP collection procedures did not include provisions for write-off of uncollectible receivables. As of June 30, 2009, the receivables totaled \$15,725 and had past-due dates ranging from the 1987/88 to 2007/08 academic years.

State University Administrative Manual §3822 requires each campus to establish procedures that provide for prompt follow-up of accounts receivable. These procedures should include the preparation and issuance of follow-up letters and/or calls and the utilization of the offset claim procedures for accounts greater than \$10.

Executive Order (EO) 616, *Discharge of Accountability*, dated April 19, 1994, states that campuses will be obligated to comply with the collection efforts outlined in SAM §8776.6, which includes procedures that ensure prompt follow-up on receivables. EO 616 also delegates authority to the campus for local adjustments of up to \$1,000 when the campus determines that a receivable is uncollectible or that the amount does not justify the collection costs.

SAM §8776.6 provides procedures and guidelines regarding adequate collection efforts and follow-up on receivables. These procedures include sending a sequence of three collection letters at 30-day intervals with progressively stronger tones. The procedures also establish specific requirements for filing applications for discharge from accountability with the State Controller's Office.

SAM §8776.7 includes procedures to be employed in the collection of amounts due from employees. These procedures include notifying the employee of the receivable in writing and documenting any response by the employee, including his/her agreement to repay the state.

The general accounting manager stated that the CO policies and procedures were not specific in relation to CST because of the uniqueness of the program. She also stated that students are billed in arrears and payment plans are approved by the department. She added that there has not been a formal process for communicating write-offs between IP and CO Accounting.

## **Recommendation 2**

We recommend that the CO:

- a. Establish and implement policies and procedures to collect CST delinquent accounts receivable, including the use of collection letters, documenting evidence of collection correspondence, and consideration of administrative action or write-off.

- b. Include write-off provisions in IP collection procedures, analyze delinquent accounts receivable to determine which receivables are uncollectible, and write off receivables as warranted.

### **Management Response**

We concur with the recommendations as set forth in (a) and (b). The CO has revised and implemented its policies and procedures for CST and IP accounts receivable. As a result, all receivables are now part of the documented standard processing and review for aging, collections, and write-offs. Formal write-off procedures are included within the revised policies and procedures.

### **RECONCILIATIONS**

Accounts receivable reconciliations for the months of July, August, and September 2009 were not signed and dated by the preparer and a reviewer.

SAM §7901 states, in part, that the accuracy of an agency's accounting records may be proved partially by making certain reconciliations and verifications.

SAM §7908 states that all reconciliations will show the preparer's name, reviewer's name, date prepared, and date reviewed.

The general accounting manager stated that the CO reconciles the general ledger receivables quarterly, which are signed and dated by the preparer and the reviewer. She was not aware that individual fund reconciliations must also be signed and dated by both preparer and reviewer.

Inadequate control over accounts receivable reconciliations increases the risk of errors in reported financial position.

### **Recommendation 3**

We recommend that the CO ensure that reconciliations are signed and dated by the preparer and a reviewer.

### **Campus Response**

We concur with the recommendation. We have developed and implemented procedures for accounts receivable reconciliations that will ensure they are performed on a timely basis with the appropriate signatures.

## **CASH DISBURSEMENTS**

The CO could not provide evidence of its efforts to periodically request local banks to search for unauthorized bank accounts that use the CO name, address, and/or federal identification (ID) number.

SAM §20050 states that the elements of a satisfactory system of internal accounting and administrative controls, include limiting access to state assets to authorized personnel who require these assets in the performance of their assigned duties.

The director of cash management operations stated that there is no specific SAM requirement that the CO conduct a local bank search for unauthorized accounts.

The lack of a process to periodically search for unauthorized bank accounts increases the risk of the CO being associated with improper bank accounts.

### **Recommendation 4**

We recommend that the CO establish procedures to periodically request local banks to search for unauthorized bank accounts that use the CO name, address, and federal ID number and maintain documentation of such efforts.

### **Management Response**

We will establish the recommended procedures and complete by October 22, 2010.

## **PAYROLL**

Duties and responsibilities related to certain payroll functions were not properly segregated.

We found that payroll personnel could access and update both personnel records in PeopleSoft (PS) and payroll records in the Personnel/Payroll Information Management System (PIMS).

California State University Directive HR/EHDB 2007-01, *KPMG Recommendation Concerning Payroll-Related Segregation of Duties*, dated May 7, 2007, states that payroll employees should not be the same individuals who modify employee master files.

SAM §20050 states, in part, that the elements of a satisfactory system of internal accounting and administrative controls include a plan of organization that provides segregation of duties appropriate for proper safeguarding of state assets.

The associate director of human resource services stated that best practice requires a backup for PS data entry to ensure that salary updates are timely. She stated further that best practice also requires

controls to ensure human resources managers approve documents generated by PS before they are sent to payroll and entered into the payroll system. She also stated that systemwide policy does not mandate different individuals key data into PS and PIMS, nor does it mandate separation of these two functions.

Inadequate segregation of duties related to certain payroll functions increases the risk of irregularities.

#### **Recommendation 5**

We recommend that the CO remove update capabilities to either PS or PIMS for the affected employees, or implement compensating controls.

#### **Management Response**

We agree with the recommendation and have already taken steps to mitigate the risk. However, we believe that complete resolution of this finding requires an automated solution. The auditors are concerned that the same person at the CO may enter compensation data into PeopleSoft and also into PIMS (the State Controller's Office computer system). The ultimate goal is to implement a technological solution in which these two duties would be combined, and a single person would enter the data into *both* PeopleSoft and PIMS as one transaction. This would eliminate "double-keying" of the same data, which is redundant and time consuming. The double entry is the result of the inability of the CSU Common Management Systems (CMS) to interface with the old legacy system at the State Controller's Office. Timing of this solution is dependent on the State Controller's Office implementing a new payroll system, originally anticipated to be operational for the CSU in June 2009. At that time, the data will be input only once.

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## APPENDIX A: PERSONNEL CONTACTED

<u>Name</u>	<u>Title</u>
Benjamin F. Quillian	Executive Vice Chancellor and Chief Financial Officer
Amy Ahearn	Financial Information Systems Administrator
Arti Annaswamy	Research Assistant
George Ashkar	Interim Assistant Vice Chancellor/Controller, Financial Services (At time of review)
Lillian Audet	Revenue Management Program Accounting Supervisor
Sue Bell-Ramirez	Manager, Emergency Management, Safety, and Compliance
Robert Boyhan	Director of Operations
Sean Boylan	Director, Cash Management Operations
Sue Chen	Assistant Trust Fund Accountant
Jolene Colman	International Programs Secretary
Kelly Cox	Enterprise Accounting Manager
Joyce Cury	Student Fund Coordinator, International Programs
Tracy Daniels	Administrative Support Coordinator
Austin Davis	Assistant Cash Management Officer
Bruce Gibson	Senior Director, Systemwide Equal Employment Opportunity and Chancellor's Office Human Resources
Jean Gill	Interim Assistant Controller
Ellyce Gordon	Property Clerk
Kristy Hawman	Associate Director of Human Resource Services
Sedong John	Associate Director, Systemwide Financial Reporting
Alice Kim	Enterprise Accounting Supervisor
Thoa Le	Budget Director
Roberta McNeil	Manager, Financial Systems Internal Control and Compliance
Caron Oberg	Senior Communications Manager
Sharon Okashima	Assistant Director of Finance, International Programs
Sylvia Olivas	General Accounting Manager
Sherry Pickering	General Accounting Manager
Terri Porter	Bank Reconciliation Accountant
Oliver Ravela	Banking Analyst
Lauri Reilly	Accounts Payable Manager
Rodney Rideau	Director of Budget
Pat Ritchie	Payroll and Data Manager
Jason Stanton	Program Coordinator, CalState TEACH Program
Joselyn Zamora	Human Resources Assistant
Colleen Zenger	Financial Manager
Erica Zuniga	Human Resources Generalist



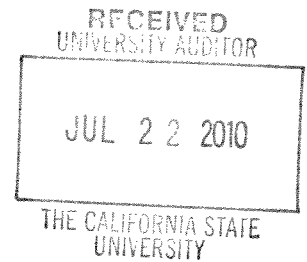
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Executive Vice Chancellor/  
Chief Financial Officer

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**Date:** July 22, 2010  
**To:** Larry Mandel  
University Auditor  
**From:** Benjamin F. Quillian *B.F.*  
Executive Vice Chancellor & Chief Financial Officer  
**Subject:** Management Response to Recommendations for Audit Report 09-09,  
FISMA at the Office of the Chancellor



Enclosed are the management responses to the audit recommendations pertaining to Audit Report 09-09. All actions required to implement or complete these audit recommendations have been taken and approved. We believe our corrective actions described will be sufficient to restore appropriate controls and comply with the recommendations of this audit.

Should you have any questions, please feel free to contact George V. Ashkar.

BFQ:GV:gs

Attachment

c: George V. Ashkar  
Gail Brooks

**CSU Campuses**  
Bakersfield  
Channel Islands  
Chico  
Dominguez Hills  
East Bay

Fresno  
Fullerton  
Humboldt  
Long Beach  
Los Angeles  
Maritime Academy

Monterey Bay  
Northridge  
Pomona  
Sacramento  
San Bernardino  
San Diego

San Francisco  
San José  
San Luis Obispo  
San Marcos  
Sonoma  
Stanislaus

**FISMA****CALIFORNIA STATE UNIVERSITY  
OFFICE OF THE CHANCELLOR****Audit Report 09-09****CASH RECEIPTS****Recommendation 1**

We recommend that the CO perform an inventory of parking permits and reconcile the parking permits to cash receipts.

**Management Response**

We concur with the recommendation. An inventory was completed October 14, 2009 and all employee parking permits and temporary parking permits were accounted for. Written procedures were prepared and implemented in connection with the identification of cash receipts, the recording of permit numbers and the tracking of the inventory of permits. Staff with responsibility for receiving cash and issuing permits has been fully trained on these procedures.

**ACCOUNTS RECEIVABLE****COLLECTIONS AND WRITE-OFF****Recommendation 2**

We recommend that the CO:

- a. Establish and implement policies and procedures to collect CST delinquent accounts receivable, including the use of collection letters, documenting evidence of collection correspondence, and consideration of administrative action or write-off.
- b. Include write-off provisions in IP collection procedures, analyze delinquent accounts receivable to determine which receivables are uncollectible, and write off receivables as warranted.

**Management Response**

We concur with the recommendations as set forth in (a) and (b). The Chancellor's Office has revised and implemented its policies and procedures for CST and IP accounts receivable. As a result, all receivables are now part of the documented standard processing and review for aging, collections and write-offs. Formal write-off procedures are included within the revised policies and procedures.

## RECONCILIATIONS

### Recommendation 3

We recommend that the CO ensure that reconciliations are signed and dated by the preparer and a reviewer.

### Management Response

We concur with the recommendation. We have developed and implemented procedures for accounts receivable reconciliations that will ensure they are performed on a timely basis with the appropriate signatures.

## CASH DISBURSEMENTS

### Recommendation 4

We recommend that the CO establish procedures to periodically request local banks to search for unauthorized bank accounts that use the CO name, address, and federal ID number and maintain documentation of such efforts.

### Management Response

We will establish the recommended procedures and complete by October 22, 2010.

## PAYROLL

### Recommendation 5

We recommend that the CO remove update capabilities to either PS or PIMS for the affected employees, or implement compensating controls.

### Management Response

We agree with the recommendation and have already taken steps to mitigate the risk. However, we believe that complete resolution of this finding requires an automated solution. The auditors are concerned that the same person at the CO may enter compensation data into PeopleSoft and also into PIMS (the State Controllers Office computer system). The ultimate goal is to implement a technological solution in which these two duties would be combined, and a single person would enter the data into *both* PeopleSoft and PIMS as one transaction. This would eliminate “double-keying” of the same data, which is redundant and time consuming. The double entry is the result of the inability of the CSU Common Management System (CMS) to interface with the old legacy system at the State Controller’s Office. Timing of this solution is dependent on the State Controller’s Office implementing a new payroll system, originally anticipated to be operational for the CSU in June 2009. At that time, the data will be input only once.

THE CALIFORNIA STATE UNIVERSITY  
OFFICE OF THE CHANCELLOR

BAKERSFIELD

CHANNEL ISLANDS

August 12, 2010

CHICO

**MEMORANDUM**

DOMINGUEZ HILLS

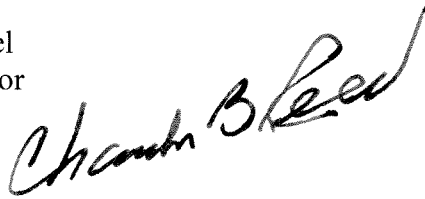
EAST BAY

TO: Mr. Larry Mandel  
University Auditor

FRESNO

FULLERTON

FROM: Charles B. Reed  
Chancellor



HUMBOLDT

SUBJECT: Draft Final Report 09-09 on *FISMA*, Office of the Chancellor

LONG BEACH

LOS ANGELES

In response to your memorandum of August 12, 2010, I accept the response as submitted with the draft final report on *FISMA*, Office of the Chancellor.

MARITIME ACADEMY

MONTEREY BAY

NORTHRIDGE

CBR/amd

POMONA

SACRAMENTO

SAN BERNARDINO

SAN DIEGO

SAN FRANCISCO

SAN JOSÉ

SAN LUIS OBISPO

SAN MARCOS

SONOMA

STANISLAUS