

**SPECIAL INVESTIGATION**  
**SAN FRANCISCO STATE UNIVERSITY**

**Report Number 99-91**  
**January 12, 2000**

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**OFFICE OF THE  
UNIVERSITY AUDITOR**

January 12, 2000

Report #9991

Dr. Charles Reed  
Chancellor  
The California State University  
Long Beach, CA 90802


Dear Dr. Reed:

Pursuant to a request from your office on September 9, 1999, the Office of the University Auditor has conducted an investigation of possible misappropriation of assets at San Francisco State University (SFSU). Our investigation was predicated upon allegations of inappropriate contracting with the San Francisco Performing Arts Library and Museum (PALM) by SFSU.

Our examination was conducted in accordance with generally accepted investigative techniques, which included, but were not limited to, examination of books and records, voluntary interviews with appropriate SFSU and PALM personnel, and other such evidence-gathering procedures as necessary under the circumstances.

Included within the report, along with our conclusion as to whether there was a misappropriation of assets, are specific recommendations which we believe would benefit the campus if it were to again contract with PALM or a similar entity.

Sincerely,

  
Larry Mandel  
University Auditor

LM:cw

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# **CONTENTS**

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## **EXECUTIVE SUMMARY**

Executive Summary.....	1
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## **INTRODUCTION**

Allegations.....	2
Background.....	3
Scope and Method of Investigation.....	3

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## **RESULTS OF INVESTIGATION**

Results of Investigation.....	4
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## **RECOMMENDATIONS**

Recommendations.....	6
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## **APPENDICES**

Appendix A	Chancellor's Acknowledgement of Campus Response
Appendix B	Campus Response

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## **EXECUTIVE SUMMARY**

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### **ALLEGATIONS**

- San Francisco State University (SFSU) had agreed to provide the San Francisco Performing Arts Library and Museum (PALM) \$100,000 per year for a period of three years without receiving adequate consideration in return (a gift of public funds.)
- A pecuniary gain may have been received by the campus president's spouse through her membership on the board of PALM.

### **INVESTIGATION RESULTS – ALLEGATIONS**

- A gift of public funds did not result from the agreement with PALM; the agreement, however, did not clearly describe specific benefits received by the university.
- No pecuniary gain to the spouse of the university president resulted from the agreement with the PALM.

### **INVESTIGATION RESULTS – ANCILLARY FINDINGS**

- Both the campus' agreement with PALM and its operation under it were inadequate. In the body of the agreement, an insufficient description of the consideration received is provided, while oversight by the SFSU Foundation over its outstationed PALM employees was deficient.

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## **INTRODUCTION**

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### **ALLEGATIONS**

A member of the California State Assembly apprised the CSU Chancellor's Office of complaints from a constituent regarding the administration of San Francisco State University (SFSU). On September 7, 1999, the Chancellor requested a preliminary review of the allegations presented to the assemblyman.

A meeting with the complainant took place on September 16, 1999. At that meeting, nine general concerns were voiced, the majority of which were subjective and could not be supported by specific facts which might predicate an investigation (i.e. general comments that weak accounting controls existed for one campus program, while specific control failures which might justify an investigation were not provided). We did, however, determine that the facts and circumstances related to two items warranted further investigation. The campus president invited further investigation and offered full support from campus and foundation management and staff.

Allegations were made by the complainant that: (1) the president of SFSU agreed to provide \$100,000 per year for three years to the San Francisco Performing Arts Library and Museum (PALM) without receiving adequate consideration in return (a gift of public funds); and (2) the president's spouse, a board member of the PALM, may have received pecuniary gain as a result of the agreement with the PALM.

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## **INTRODUCTION**

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### **BACKGROUND**

In its web page, the PALM indicates that it “preserves and makes accessible materials about the performing arts...” through “...its unique collection (which) contains more than two million items, including books, periodicals, photographs, programs, playbills, newspaper clippings, audio and video tapes, costume and set designs, and other artifacts.” PALM states that its “research facility is open to the public without charge” and that it is “an independent nonprofit organization that relies on a variety of funding sources, including memberships, and corporate, foundation and individual gifts.”

Campus officials indicated that SFSU’s affiliation with PALM offers resources for research, internships, and other educationally related opportunities as well as establishing an association with a recognized organization (PALM). It was further indicated that this affiliation “could open doors for the University” within the downtown cultural establishment of San Francisco, including a physical presence near city hall and San Francisco’s opera and symphony.

In July 1997, a contract between SFSU and PALM was executed. This agreement stated that SFSU “shall provide funding of \$100,000 for salaries per year for a three year period to PALM to assist in defraying personnel support costs.” This agreement states that the support shall be provided through the University's fiscal agent, the SFSU Foundation, Inc., and be in the form whereby employees of PALM are placed on the Foundation’s payroll.

Among the various open ended contract provisions was an agreement to negotiate a separate agreement with the campus with respect to custody of the collection. The agreement noted, “It is the intent of the parties that, subject to their entering into a written agreement establishing a permanent relationship between them on or before the expiration of the term of this Agreement, the ownership of the Permanent Collection then owned by PALM shall be transferred to SFSU. . .” It also states, “. . .and provides further that, in such event, PALM shall use its best efforts to facilitate SFSU becoming custodian or trustee as the case may be.”

The affiliation between SFSU and PALM was done publicly. It has been included in various press releases, in PALM’s letterhead, and on the sign outside the PALM library as required by the agreement. PALM’s relationship with SFSU has been footnoted in PALM financial statements and included in SFSU budget documents. The PALM project appeared as a separate budget line item within the campus’ budget which, according to campus officials, was approved by the campus’ budget committee in an open meeting with both faculty and staff members present.

### **SCOPE AND METHOD OF INVESTIGATION**

To investigate the allegations, we reviewed agreements related to the SFSU and PALM affiliation. To better understand the operations under the agreements, we also reviewed related SFSU, Foundation and PALM policies and procedures. The review included an examination of financial and non-financial records and documents as available. Additionally, we interviewed SFSU, Foundation and PALM employees with regard to SFSU and PALM’s affiliation.

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## **RESULTS OF INVESTIGATION**

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### **NO GIFT OF PUBLIC FUNDS**

It was alleged that a gift of public funds resulted from the SFSU and PALM agreement.

We found that, based upon a study of PALM, SFSU, and SFSU Foundation records and interviews with management responsible for those records, the agreement between PALM and SFSU appears to present a lack of sufficient consideration received by the campus. Without sufficient consideration, a gift of public funds would result.

Specifically, a review by our office and that of general counsel for the CSU indicated that consideration received by the campus, as expressed in the SFSU and PALM agreement, was inadequate. The terms of the contract require state funds of \$100,000 per year for three years, to be expended by SFSU for services resembling those offered by PALM to the public without charge. In return, the contract contains the promise, by PALM, to discuss the transfer of the PALM's collection to SFSU (to be set out in a separate contract for separate consideration if an agreement is reached), participation on PALM's board, a say in PALM's selection of its new location in downtown San Francisco, and a sign indicating a relationship between the campus and PALM. In total, we believe that the consideration described within the agreement did not appear to be adequate, acknowledging that a strict quantification of costs and benefits would be very difficult.

However, upon further investigation, we found that it was the PALM's policy to grant SFSU students and faculty the privileges of paid members of the library. Such privileges include the ability to check out materials from the collection, discounts on copying and photographic usage, use of the facilities, etc. These privileges are not offered to non-members.

We further found that it was the intent of the parties to establish specific academic offerings limited to SFSU students and faculty through the workgroups process described within the agreement. However, these workgroups were never formed.

These ancillary offerings, limited to SFSU students and faculty, along with consideration expressly stated within the agreement, appear to indicate sufficient consideration. Again, it is not possible for us to precisely quantify the benefits received under the agreement.

### **NO PECUNIARY GAIN**

It was alleged that a pecuniary gain may have been received by the campus president's spouse through her membership on the board of PALM.

We found that, even though the president's spouse has been a volunteer board member for PALM since 1993, evidence of a direct benefit derived from the relationship between PALM and SFSU was neither presented nor discovered. This conclusion was based upon a study of PALM, SFSU, and SFSU Foundation records and interviews with management responsible for compiling these records.

## **INADEQUATE OPERATION UNDER THE AGREEMENT**

We found that both the agreement and the campus' operation under it were inadequate, including insufficiently described consideration within the body of the agreement and insufficient oversight by the SFSU Foundation over its outstationed PALM employees.

First, as noted above, the agreement did not adequately describe consideration to be received by SFSU. Such agreements must expressly state such consideration and demonstrate sufficient consideration in their writing in both substance and form.

Further, we found that state funds were claimed under an agreement between SFSU and its Foundation which represented the Foundation as a mere fiscal agent for the agreement between SFSU and PALM. The agreement indicates that the Foundation will provide payroll and other administrative services only. As noted below, the Foundation became the employer of record of the PALM director and two PALM staff.

Next, we found that, as a result of the agreement, a significant liability was accepted by SFSU and its Foundation when it made the PALM director and two staff members employees and provide them with medical and retirement benefits. Significant liability accrues to the Foundation when its employee acts as the director of an independent corporation that does not operate solely for the benefit of the campus. We found that the Foundation did not exercise sufficient oversight of these employees; all parties viewed the Foundation as a provider of payroll services rather than as an employer. In effect, the Foundation accepted responsibility for administrating a large art collection.

Finally, the liability accepted by the campus was further increased when the Foundation later entered into an agreement with PALM, allowing PALM to place its funds within the Foundation's investment pool. Such an offering would appear to be inappropriate and viewed as being out of compliance with functions allowable under Title 5 §42500 Functions of Auxiliary Organizations.

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## **RECOMMENDATIONS**

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Our investigation was administrative in nature. Conclusions drawn were made within that context. Recommendations that would mitigate the recurrence of similar findings in the future are presented below along with a recommendation to effect specific corrective actions:

### **1. Review of SFSU and PALM Affiliation**

We recommend a comprehensive review of:

- a. the affiliation between SFSU and PALM to support a redrafting of existing agreements to clearly express the benefits to the university in connection with the relationship with PALM;
- b. the risk/benefit of assuming responsibility for operating an independent corporation which does not operate solely for the benefit of SFSU; and
- c. the sufficiency of consideration currently articulated within agreements.

### **Campus Response:**

We concur. A campus review is currently underway of the contractual arrangement with the Performing Arts Library and Museum (PALM). The review will be completed by May 1, 2000. This review was begun in anticipation of the contractual term of the agreement expiring in June 2000 with the intent of determining whether the affiliate relationship with PALM should continue. Particular emphasis is being focused on analyzing the programmatic and community benefit of continuing the relationship along with exploring improved means of quantifying those benefits.

While we do not dispute the findings noting that little was accomplished in the past two and a half years with respect to program development, we feel it necessary to point out that during the initial year of the agreement there was a change of ownership of the premises occupied by PALM in a rented facility in San Francisco's civic center. For this reason both PALM staff and those working with PALM on the University staff directed all of their energies to finding an alternative location for PALM. Senior management of the University worked closely with PALM in identifying and securing space in the prestigious Veteran's Building adjacent to the San Francisco Opera House and opposite City Hall in San Francisco's Civic Center. This activity occurred over most of the period covered by the agreement. In addition, securing this valuable space involved significant interaction between PALM's leadership and staff, and the President of the University, and Vice President for University Advancement and the Vice President for Business and Finance. The new location in the Veterans Building was much sought after by other civic groups and there was intense competition for space in this facility. Obtaining it for PALM involved extensive interaction with civic officials and community constituencies. We assert that this effort was of such complexity and required so much of PALM's resources that the issue of programmatic development had to be set aside until the space issue could be resolved. Thus, while we concede little was done with regard to joint programming, we suggest that there were extenuating circumstances which need to be acknowledged.

With regard to quantification of benefits during the term of the agreement, we wish to note here that one of the benefits can be quantified. PALM grants the privileges and cost savings of paid members to SFSU students and faculty. Since PALM membership is \$15.00, this benefit alone potentially exceeds the University support provided by a substantial amount.

## **2. Termination of PALM Deposit Agreement**

We recommend that the SFSU Foundation divest itself of PALM's endowments.

### ***Campus Response:***

We concur with the recommendation. We wish once again to restate the original intent of the agreement which was to be the first step in making PALM an affiliate of the University and ultimately achieving a transition of PALM into a program, institute or collection of the University. The endowment funds of PALM were deposited into the SFSU Foundation to strengthen the affiliate relationship between the campus and PALM in anticipation of achieving the original objective of the agreement. We concede that the acceptance of the deposit was premature, since transition issues remain unresolved.

For this reason, and in full compliance with the audit recommendation, the Foundation has taken steps to divest itself of PALM's endowment immediately. The PALM Board Chairman and new Executive Director were informed that the funds are being returned to PALM, and a courier will deliver a check February 4 to the PALM offices for the full amount invested.



# THE CALIFORNIA STATE UNIVERSITY

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CHARLES B. REED  
 CHANCELLOR

February 7, 2000

## MEMORANDUM

TO: Larry Mandel  
 University Auditor

FROM: Charles B. Reed *Charles B. Reed*  
 Chancellor

SUBJECT: Draft Final Report Number 99-91 on *Special Investigation*,  
 San Francisco State University

In response to your memorandum of February 7, 2000, I accept the response as submitted with the draft final report on *Special Investigation*, San Francisco State University.

CBR/cw

Enclosure

cc: Dr. Robert A. Corrigan, President



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Office of the President

1600 Holloway Avenue  
San Francisco, California 94132

Tel: 415/338-1381

January 28, 2000

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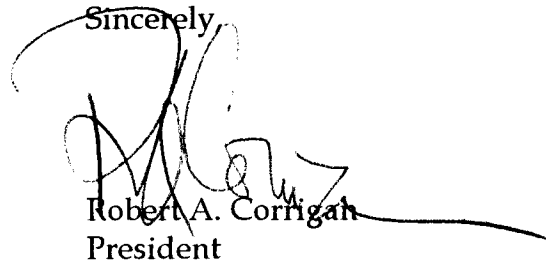
Mr. Larry Mandel  
University Auditor  
The California State University  
401 Golden Shore  
Long Beach, California 90802-4275

Dear Mr. Mandel:

We have carefully reviewed Office of University Auditor Special Investigation Report #99-91 on PALM at San Francisco State University. Our responses to the two recommendations are attached.

Questions regarding the responses may be directed to Don Scoble, Vice President for Business and Finance, at 415/338-1323, or Jim Van Ness, Internal Auditor, at 415/338-7183. We appreciate the professional manner in which this special investigation was handled.

Sincerely,



Robert A. Corrigan  
President

JVN/lmf

cc: Don W. Scoble, Vice President, Business and Finance  
Jim Collier, Vice President, University Advancement  
Larry Ware, Director of Administration, SFSU Foundation, Inc.  
Jim Van Ness, Internal Auditor

San Francisco State University Response to  
 University Auditor Special Investigation Report Number 99-91 on  
 Performing Arts Library and Museum (PALM)

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**Recommendation 1: Review of SFSU and PALM Affiliation**

*We recommend a comprehensive review of:*

- a. the affiliation between SFSU and PALM to support a redrafting of existing agreements to clearly express the benefits to the university in connection with the relationship with PALM;*
- b. the risk/benefit of assuming responsibility for operating an independent corporation which does not operate solely for the benefit of SFSU; and*
- c. the sufficiency of consideration currently articulated within agreements.*

**Campus Response**

We concur. A campus review is currently underway of the contractual arrangement with the Performing Arts Library and Museum (PALM). The review will be completed by May 1, 2000. This review was begun in anticipation of the contractual term of the agreement expiring in June 2000 with the intent of determining whether the affiliate relationship with PALM should continue. Particular emphasis is being focused on analyzing the programmatic and community benefit of continuing the relationship along with exploring improved means of quantifying those benefits.

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San Francisco State University Response to  
University Auditor Special Investigation Report Number 99-91 on  
Performing Arts Library and Museum (PALM)

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**Recommendation 2: Termination of PALM Deposit Agreement**

*We recommend that the SFSU Foundation divest itself of PALM's endowments.*

**Campus Response**

We concur with the recommendation. We wish once again to restate the original intent of the agreement which was to be the first step in making PALM an affiliate of the University and ultimately achieving a transition of PALM into a program, institute or collection of the University. The endowment funds of PALM were deposited into the SFSU Foundation to strengthen the affiliate relationship between the campus and PALM in anticipation of achieving the original objective of the agreement. We concede that the acceptance of the deposit was premature, since transition issues remain unresolved.

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