

AUXILIARY ORGANIZATIONS
SAN DIEGO STATE UNIVERSTIY

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CONTENTS

Executive Summary.....	1
Introduction	6
Background.....	6
Purpose	7
Scope and Methodology	7

OBSERVATIONS, RECOMMENDATIONS, AND CAMPUS RESPONSES

CAMPUS

Operating and Administrative Agreements	10
Campus Oversight and Control	11
Auxiliary Programs	12

SAN DIEGO STATE UNIVERSITY FOUNDATION

Corporate Governance.....	14
Operational Compliance.....	14
Segregation of Duties	15
Purchasing and Accounts Payable.....	16
Construction Policies and Procedures	16
Vendor Selection	17

THE CAMPANILE FOUNDATION

Corporate Governance.....	19
Dissolution Clause.....	19
Board Composition.....	19
Public Meetings	20

AZTEC SHOPS, LTD.

Operating and Administrative Agreements	21
Corporate Governance.....	21
Fiscal Compliance	22

CONTENTS

Operational Compliance23

Property and Equipment23

Loss Prevention24

ASSOCIATED STUDENTS, SAN DIEGO STATE UNIVERSITY

Operating and Administrative Agreements25

Corporate Governance25

Operational Compliance26

Property and Equipment27

APPENDICES

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

ABBREVIATIONS

AS	Associated Students, San Diego State University
CCRP	College Community Redevelopment Project
CFO	Chief Financial Officer
CSU	California State University
EO	Executive Order
Foundation	San Diego State University Foundation
RFIN	Resolution of the Committee on Finance
Shops	Aztec Shops, Ltd.

EXECUTIVE SUMMARY

In July 1981, the Board of Trustee policy concerning auxiliary organizations was adopted in the Resolution of the Committee on Finance (RFIN) 7-81-4. Executive Order 698, *Board of Trustees Policy for the California State University Auxiliary Organizations*, dated March 3, 1999, required that the Office of the University Auditor conduct internal compliance/internal control reviews of auxiliary organizations, and the Board of Trustees instructed that such reviews be conducted on a triennial basis pursuant to procedures established by the chancellor.

San Diego State University management is responsible for establishing and maintaining an adequate system of internal compliance/internal control and assuring that each of its auxiliary organizations similarly establishes such a system. This responsibility, in accordance with California Code of Regulations, Title 5, Section 42402 et seq. and Executive Order 698, *Board of Trustees Policy for the California State University Auxiliary Organizations et seq.*, includes requiring the documentation of internal control, communicating requirements to employees, and assuring that its system of internal compliance/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 a system of internal compliance/internal control are to provide management with reasonable, but not absolute, assurance that:

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

We visited the San Diego State University campus and its auxiliary organizations from March 29, 2004, through May 14, 2004, and made a study and evaluation of the system of internal compliance/internal control in effect for the period July 2001 to May 2004. This report represents our triennial review.

Our study and evaluation at the *San Diego State University Foundation* did not reveal any significant internal control problems or weaknesses that would be considered pervasive in their effects on the accounting and administrative controls. However, we did identify other reportable weaknesses that are described in the executive summary and in the body of the report. In our opinion, the accounting and administrative control in effect as of May 2004, taken as a whole, was sufficient to meet the objectives stated above.

Our study and evaluation at *The Campanile Foundation* did not reveal any significant internal control problems or weaknesses that would be considered pervasive in their effects on the accounting and administrative controls. However, we did identify other reportable weaknesses that are described in the executive summary and in the body of the report. In our opinion, the accounting and administrative control in effect as of May 2004, taken as a whole, was sufficient to meet the objectives stated above.

Our study and evaluation at *Aztec Shops, Ltd.* did not reveal any significant internal control problems or weaknesses that would be considered pervasive in their effects on the accounting and administrative controls. However, we did identify other reportable weaknesses that are described in the executive summary and in the body of the report. In our opinion, the accounting and administrative control in effect as of May 2004, taken as a whole, was sufficient to meet the objectives stated above.

Our study and evaluation at *Associated Students, San Diego State University* did not reveal any significant internal control problems or weaknesses that would be considered pervasive in their effects on the accounting and administrative controls. However, we did identify other reportable weaknesses that are described in the executive summary and in the body of the report. In our opinion, the accounting and administrative control in effect as of May 2004, 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 change over time. Specific limitations that may hinder the effectiveness of an otherwise adequate system of controls include, but are not limited to, resource constraints, faulty judgments, unintentional errors, circumvention by collusion, and management overrides. Establishing controls 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.

CAMPUS

OPERATING AND ADMINISTRATIVE AGREEMENTS [10]

Specific written agreements had not been established between the campus and the San Diego State University Foundation regarding campus supervision of certain auxiliary employees.

CAMPUS OVERSIGHT AND CONTROL [11]

The campus had not established specific procedures regarding fiscal oversight and control over campus centers, institutes, and similar organizations and programs whose funds were held in operating accounts maintained by the Foundation.

AUXILIARY PROGRAMS [12]

Royalty arrangements between academic departments and the Aztec Shops, Ltd. were not in compliance with current campus administrative and academic/professional responsibility policies regarding instructional materials publishing and related reimbursements due the campus.

SAN DIEGO STATE UNIVERSITY FOUNDATION

CORPORATE GOVERNANCE [14]

The San Diego State University Foundation (Foundation) Articles of Incorporation did not specify that the net assets of the dissolved auxiliary must be distributed to a successor approved by the campus president and the CSU Trustees.

OPERATIONAL COMPLIANCE [14]

The Foundation had not included within its written personnel policies and procedures standards for evidencing its analysis of the comparability of salaries, working conditions, and benefits for its full-time employees in relation to those provided campus employees performing substantially similar services.

SEGREGATION DUTIES [15]

Duties and responsibilities over certain accounting functions for personnel and payroll were not appropriately segregated at the Foundation.

PURCHASING AND ACCOUNTS PAYABLE [16]

The Foundation's procurement policies and procedures did not specifically address construction project administration. Construction policies and procedures should address, among other things, project and contract prebid, bid, and award processes, including the bid proposal package, bid documentation, prequalification of bidders, withdrawal of bids, bid rejection, bid acceptance, and award of contract. Additionally, the policies and procedures should address project oversight, including progress schedule and contract cost breakdown, contractor's payment requests, and safety compliance, as well as contract change order procedures, including normal change orders, change order proposal procedures, contract change orders, emergency change orders, disputed work issues, and requests for time extensions. Also, policies and procedures should address contract compliance and monitoring, including final inspections, project completion reports, and work performed under local jurisdictions and reconciliation of contract time. In addition, the Foundation did not formally document the basis for awarding contracts for construction manager services for specific projects within the College Community Redevelopment Project.

THE CAMPANILE FOUNDATION

CORPORATE GOVERNANCE [19]

The Campanile Foundation did not establish by resolution the time, date, and location for holding regular and annual board meetings, and its current governing board did not include a student representative. In addition, The Campanile Foundation Articles of Incorporation did not specify that

the net assets of the dissolved auxiliary must be distributed to a successor approved by the campus president and the CSU Trustees.

AZTEC SHOPS, LTD.

OPERATING AND ADMINISTRATIVE AGREEMENTS [21]

The Aztec Shops, Ltd. (Shops) performed functions inconsistent with CSU policy, specifically, the operation of dining services at two community colleges.

CORPORATE GOVERNANCE [21]

The Shops board adopted changes in the number of required members from ten to twelve without reflecting this change in its current bylaws.

FISCAL COMPLIANCE [22]

The Shops written reserve policy had not been updated to reflect current practice on the allocation of surplus funds/reserves.

OPERATIONAL COMPLIANCE [23]

The Shops current non-discrimination policy did not address discrimination based on pregnancy.

PROPERTY AND EQUIPMENT [23]

The Shops fixed asset inventory listing had not been reconciled to the general ledger on a timely basis. Adjustments resulting from the August 2003 inventory had not been reflected in the general ledger and fixed asset inventory listing as of May 2004.

LOSS PREVENTION [24]

The Shops did not maintain documentation of loss prevention audits and similar analysis of operations for management's review.

ASSOCIATED STUDENTS, SAN DIEGO STATE UNIVERSITY

OPERATING AND ADMINISTRATIVE AGREEMENTS [25]

Business arrangements between the Associated Students, San Diego State University (AS) and a local community service non-profit corporation were not supported by appropriate and current written agreements. Specifically, the AS continued to provide and receive programmatic services under an expired agreement. Additionally, the indemnity clause within a master agreement between the AS

and the non-profit corporation did not sufficiently indemnify the state, the campus, or the CSU Trustees.

CORPORATE GOVERNANCE [25]

The AS Articles of Incorporation did not specify that the net assets of the dissolved auxiliary must be distributed to a successor approved by the campus president and the CSU Trustees.

OPERATIONAL COMPLIANCE [26]

The AS was not in compliance with its conflict-of-interest policy, as conflicts of interest were not reported to the vice president of business and financial affairs, and all board members did not sign conflict-of-interest statements. In addition, signed statements for all board members were not retained for fiscal years 2001/02 and 2002/03, as a retention policy had not been established.

PROPERTY AND EQUIPMENT [27]

The AS did not conduct an independent physical inventory of fixed assets for fiscal year ended June 30, 2003. In addition, inventories conducted in prior years were completed by property custodians rather than by independent personnel.

INTRODUCTION

BACKGROUND

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

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

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

The Board of Trustee policy concerning auxiliary organizations was originally adopted in July 1981 in the Resolution of the Committee on Finance (RFIN) 7-81-4. Executive Order 698, *Board of Trustees Policy for the California State University Auxiliary Organizations*, dated March 3, 1999, represents policy of the Trustees addressing CSU auxiliary organization activity and governing the internal management of the system. CSU auxiliary organizations are required to comply with Board of Trustee policy (California Code of Regulations, Title 5, Section 42402 and Education Code, Section 89900).

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

PURPOSE

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

- ▶ Legal and regulatory requirements are complied with.
- ▶ Accounting data is provided in an accurate, timely, complete, or otherwise reliable manner.
- ▶ Assets are adequately safeguarded from loss, damage, or misappropriation.
- ▶ Duties are appropriately segregated consistent with appropriate control objectives.
- ▶ Transactions, accounting entries, or systems output is reviewed and approved.
- ▶ Management does not intentionally override internal controls to the detriment of 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 *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 Office of the Chancellor policies, letters, and directives. For those audit tests that required annualized data, fiscal years 2000/01, 2001/02, and 2002/2003 were the primary periods reviewed. In certain instances, we were concerned with representations of the most current data—in such cases, the test period was July 2003 to May 2004. Our primary focus was on internal compliance/internal control.

Specifically, we reviewed and tested:

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

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

INTRODUCTION

A preliminary survey of CSU auxiliaries at each campus was used to identify risks. Risk was defined as the probability that an event or action would adversely affect the auxiliary and/or the campus. Our assessment of risk was based upon a systematic process, using professional judgments on probable adverse conditions and/or events that became the basis for development of our final scope. We sought to assign higher review priorities to activities with higher risks. As a result, not all risks identified were included within the scope of our review.

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

San Diego State University Foundation

- ▶ Operating and Administrative Agreements
- ▶ Facilities Agreements
- ▶ Corporate Governance
- ▶ Fiscal Compliance
- ▶ Operational Compliance
- ▶ Program Compliance
- ▶ Campus Oversight and Control
- ▶ Segregation of Duties
- ▶ Cash Receipts and Handling
- ▶ Investments
- ▶ Fees, Revenues, and Receivables
- ▶ Purchasing and Accounts Payable
- ▶ Personnel and Payroll
- ▶ Campus Programs
- ▶ Auxiliary Programs – Contracts and Grants
- ▶ Information Technology

The Campanile Foundation

- ▶ Operating and Administrative Agreements
- ▶ Facilities Agreements
- ▶ Corporate Governance
- ▶ Fiscal Compliance
- ▶ Operational Compliance
- ▶ Program Compliance
- ▶ Campus Oversight and Control
- ▶ Segregation of Duties
- ▶ Investments

Aztec Shops, Ltd.

- ▶ Operating and Administrative Agreements
- ▶ Facilities Agreements
- ▶ Corporate Governance
- ▶ Fiscal Compliance
- ▶ Operational Compliance
- ▶ Program Compliance

INTRODUCTION

- ▶ Campus Oversight and Control
- ▶ Segregation of Duties
- ▶ Cash Receipts and Handling
- ▶ Fees, Revenues, and Receivables
- ▶ Purchasing and Accounts Payable
- ▶ Personnel and Payroll
- ▶ Property and Equipment
- ▶ Trusts and other Liabilities
- ▶ Information Technology
- ▶ Commercial Operations

Associated Students, San Diego State University

- ▶ Operating and Administrative Agreements
- ▶ Facilities Agreements
- ▶ Corporate Governance
- ▶ Fiscal Compliance
- ▶ Operational Compliance
- ▶ Program Compliance
- ▶ Campus Oversight and Control
- ▶ Segregation of Duties
- ▶ Cash Receipts and Handling
- ▶ Petty Cash and Change Funds
- ▶ Investments
- ▶ Fees, Revenues, and Receivables
- ▶ Purchasing and Accounts Payables
- ▶ Personnel and Payroll
- ▶ Property and Equipment
- ▶ Auxiliary Programs
- ▶ Information Technology

We have not performed any auditing procedures beyond May 14, 2004. 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.

OBSERVATIONS, RECOMMENDATIONS, AND CAMPUS RESPONSES

CAMPUS

OPERATING AND ADMINISTRATIVE AGREEMENTS

Specific written agreements had not been established between the campus and the San Diego State University Foundation (Foundation) regarding campus supervision of auxiliary employees.

Section 4.11 of the *California State University (CSU) Policy Manual for Contracting and Procurement* indicates that contracts should include terms and conditions necessary to convey a clear understanding of each party's expected role, its obligations, and the parameters in which the activities must be carried out under the contract.

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

The associate vice president of business enterprise stated that current practices had been long standing and duties and responsibilities were clearly understood by all involved parties.

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

Recommendation 1

We recommend that the campus establish specific written agreements with the Foundation that clearly define the responsibilities of each of the respective organizations regarding campus supervision of auxiliary employees.

Campus Response

We concur. The campus will establish specific written agreements with the Foundation that clearly define the responsibilities regarding campus supervision of auxiliary employees. This will be completed by April 30, 2005.

CAMPUS OVERSIGHT AND CONTROL

The campus had not established specific procedures regarding fiscal oversight and control over campus centers, institutes, and similar organizations and programs whose funds were held in operating accounts maintained by the Foundation.

We noted that:

- ▶ Procedures relating to the establishment of campus centers, institutes, and similar organizations and programs did not require a specific financial review and analysis by campus fiscal administration.
- ▶ Procedures were not established to ensure that all of these organizations and programs were included among approved centers, institutes, and similar organizations reported to the chancellor's office.
- ▶ Agreement between responsible campus departments had not been documented clarifying the evaluation and oversight risks associated with campus centers, institutes, and similar organizations and programs.
- ▶ Responsibility for evaluating and overseeing risks associated with campus centers, institutes, and similar organizations and programs required clarification.
- ▶ Funds generated by state organizations and programs were held as Foundation funds regardless of the fact that many of the costs associated with the operation of these organizations and programs were funded by the state.

Executive Order (EO) 751, *Centers, Institutes and Similar Organizations on Campuses of the California State University*, dated July 5, 2000, states that each CSU campus is to have explicit policies and procedures for establishing, operating, monitoring, reviewing, and discontinuing centers, institutes, and similar entities.

EO 715, *California State University Risk Management Policy*, dated October 27, 1999, states that each president shall develop campus risk management policies and procedures.

EO 849, *CSU Insurance Requirements*, dated February 5, 2003, states that student placement agreements must be in writing and shall specify minimum insurance requirements applicable to the contracting parties and appropriate hold harmless provisions based upon the needs of the contracting parties.

The associate vice president of financial management stated that the campus understood that additional fiscal oversight was necessary; however, conflicting requirements prevented implementation.

Insufficiently documented agreements and procedures increase the risk of misunderstandings and miscommunication regarding rights and responsibilities.

Recommendation 2

We recommend that the campus:

- a. Institute procedures requiring a specific financial review and analysis by campus fiscal administration during the establishment of campus centers, institutes, and similar organizations and programs.
- b. Establish procedures to ensure that all of these organizations and programs were included among approved centers, institutes, and similar organizations reported to the chancellor's office.
- c. Document agreement between responsible campus departments regarding the evaluation and oversight risks associated with campus centers, institutes, and similar organizations and programs.
- d. Clarify responsibility for evaluating and overseeing risks associated with campus centers, institutes, and similar organizations and programs.
- e. Ensure that funds generated by state organizations and programs are maintained and administered as in state accounts.

Campus Response

We concur. The campus will strengthen its procedures regarding centers, institutes, and similar organizations and programs. Revised procedures will require an appropriate level of financial review and analysis by campus fiscal administration. As part of the review, funds generated by specific programs will be evaluated and administered in the appropriate accounts. In addition, procedures will include an evaluation and oversight of risks which will include adequate documentation. Annually, all centers and institutes will be reported to the chancellor's office. Revised procedures will be completed by April 30, 2005.

AUXILIARY PROGRAMS

Royalty arrangements between academic departments and the Aztec Shops, Ltd. (Shops) were not in compliance with current campus administrative and academic/professional responsibility policies regarding instructional materials publishing and related reimbursements due the campus.

We found that Shops paid fees to departments for the reproduction and sale of course materials. Students were required to purchase the materials at the bookstore, which tracked sales and remitted payments to the departments based on a percentage of the sale price. This percentage was based on industry standard for author royalty payments for research and writing expenses. However, the department did not submit documentation to support these expenses. Furthermore, these fees were not reimbursed to the General Fund; instead, they were inappropriately credited to a Shops accounts receivable account for use in the bookstore or transferred to a trust account at the Foundation.

The San Diego State Senate Policy 1.0, *Royalties from Instructional Materials*, states that it is a conflict of interest and a violation of professional ethics for a faculty member, academic department, or school to accept payment of royalties or commissions for assigned course materials.

The Shops controller stated her belief that the fees paid to academic departments were not royalties but were reimbursements for costs of production incurred by the campus department for preparation of the course materials. The campus stores director stated that the fee percentage was based on industry standard for authors.

Non-compliance with administrative and academic/professional responsibility policies increases the risk of misunderstandings regarding rights and authorities over published materials, including reimbursement to the General Fund.

Recommendation 3

We recommend that the campus review the current royalty arrangements between academic departments and the Shops and take appropriate action to ensure compliance to administrative and academic/professional responsibility policies regarding instructional materials publishing and related/required reimbursements to the General Fund.

Campus Response

We concur. The campus will review the current arrangements between academic departments and Aztec Shops regarding the publishing of instructional materials and take appropriate action to ensure compliance with administrative and academic/professional policies. This review will be completed by April 30, 2005.

SAN DIEGO STATE UNIVERSITY FOUNDATION

CORPORATE GOVERNANCE

The San Diego State University Foundation (Foundation) Articles of Incorporation did not specify that the net assets of the dissolved auxiliary must be distributed to a successor approved by the campus president and the CSU Trustees.

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

The Foundation chief financial officer (CFO) stated her belief that the dissolution clause currently in place was in compliance with the regulatory requirements in existence at the time of the last amendment to the Articles of Incorporation.

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

Recommendation 4

We recommend that the Foundation redraft its corporate dissolution clause in accordance with Title 5 and appropriately reflect this change in its Articles of Incorporation.

Campus Response

We concur. The Foundation will redraft its corporate dissolution clause in accordance with Title 5. Board approval for the change will be completed by March 15, 2005.

OPERATIONAL COMPLIANCE

The Foundation had not included within its written personnel policies and procedures standards for evidencing its analysis of the comparability of salaries, working conditions, and benefits for its full-time employees in relation to those provided campus employees performing substantially similar services.

Title 5 §42405 states that the governing board of each auxiliary organization shall provide salaries, working conditions, and benefits for its full-time employees that are comparable to those provided campus employees performing substantially similar services. For those full-time employees who perform services that are not substantially similar to the services performed by campus employees, the salaries established shall be at least equal to the salaries prevailing in other educational institutions in the area or commercial operations of like nature.

The Foundation CFO stated her belief that while the Foundation performs such reviews periodically in the normal course of business and maintains the documentation during the evaluation process, such documentation was not necessarily retained after the evaluation process.

Failure to evidence the comparative analysis of positions increases the risk that the auxiliary may be expending inappropriate amounts on salaries and benefits for employees who perform substantially similar services as employees for the campus.

Recommendation 5

We recommend that the Foundation include within its written personnel policies and procedures standards for evidencing its analysis of the comparability of salaries, working conditions, and benefits for its full-time employees in relation to those provided campus employees performing substantially similar services.

Campus Response

We concur. The Foundation will revise its procedures to provide evidence of its analysis of salaries, working conditions, and benefits for its full-time employees in relation to those provided campus employees performing substantially similar services. Procedures will be revised by March 31, 2005.

SEGREGATION OF DUTIES

Duties and responsibilities over certain accounting functions for personnel and payroll were not appropriately segregated at the Foundation.

We found that certain employees:

- ▶ Changed employee addresses in the payroll system.
- ▶ Entered time and processed payroll in the payroll system.
- ▶ Distributed payroll checks via mail to Foundation employees.

EO 698, *Board of Trustees Policy for The California State University Auxiliary Organizations*, dated March 3, 1999, states that the review of auxiliary organizations will be used to determine appropriate separation of duties, safeguarding of assets, and reliability and integrity of information.

The Foundation director of financial management stated that the Foundation payroll department was entirely segregated from the human resources department. Therefore, payroll staff could not set up a new employee, or change pay status or pay amount. She also stated that the main responsibility of the payroll department is to process time reports and prepare the check run. In addition, she stated that various post-check run reviews were in place to ensure the accuracy of payroll.

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

Recommendation 6

We recommend that the Foundation properly segregate accounting functions for personnel and payroll or institute mitigating procedures approved by the campus CFO.

Campus Response

We concur. The Foundation will request that its mitigating procedures are approved and documented by the vice president for business and financial affairs by March 15, 2005.

PURCHASING AND ACCOUNTS PAYABLE

CONSTRUCTION POLICIES AND PROCEDURES

The Foundation's procurement policies and procedures did not specifically address construction project administration.

Such policies and procedures should address, among other things:

- ▶ The project and contract prebid, bid, and award processes, including the bid proposal package, bid documentation, prequalification of bidders, withdrawal of bids, bid rejection, bid acceptance, and award of contract.
- ▶ Project oversight, including progress schedule and contract cost breakdown, contractor's payment requests, and safety compliance.
- ▶ Contract change order procedures, including normal change orders, change order proposal procedures, contract change orders, emergency change orders, disputed work issues, and requests for time extensions.
- ▶ Contract compliance and monitoring, including final inspections, project completion reports, and work performed under local jurisdictions and reconciliation of contract time.

The *Compilation of Policies and Procedures for California State University Auxiliary Organizations* sets sound business practice guidelines for auxiliary organizations operating within the CSU system. Section §8.9.5, *Procurement*, states that the auxiliary should establish a written system that provides for purchases and service contracts to be made within governing board policies, source restrictions, funds availability, and other applicable requirements. The compilation further states that a written system should be established that ensures that purchases and service contracts coding, classification, recording, and competitive bidding requirements are applied in a consistent manner.

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

business practices. Sound business practice mandates specific written policies and procedures over the vendor selection and administration process for major capital projects.

The Foundation CFO stated her belief that the Foundation had existing purchasing policies and procedures that address the construction requirements. She further stated that although these policies and procedures were sufficient for the current level of construction activity, they would be enhanced as the Foundation embarks on larger, more complex construction activities.

Failure to fully develop written policies and procedures weakens internal controls, increases the risk that misunderstandings will occur, and may subject the auxiliary and the CSU to liability.

Recommendation 7

We recommend that the Foundation develop procurement policies and procedures specific to its major capital construction projects to address, among other things:

- a. The project and contract prebid, bid, and award processes, including the bid proposal package, bid documentation, prequalification of bidders, withdrawal of bids, bid rejection, bid acceptance, and award of contract.
- b. Project oversight, including progress schedule and contract cost breakdown, contractor's payment requests, and safety compliance.
- c. Contract change order procedures, including normal change orders, change order proposal procedures, contract change orders, emergency change orders, disputed work issues, and requests for time extensions.
- d. Contract compliance and monitoring, including final inspections, project completion reports, and work performed under local jurisdictions and reconciliation of contract time.

Campus Response

We concur. The Foundation will develop procurement policies and procedures specific to its major capital construction projects to address the project and contract prebid, bid, and award process, project oversight, contract change order procedures, and contract compliance and monitoring. Procedures will be documented by April 15, 2005.

VENDOR SELECTION

The Foundation did not formally document the basis for awarding contracts for construction manager services for specific projects within the College Community Redevelopment Project (CCRP).

We found that the overall CCRP project management services consultant (master project manager) also received contracts to provide project manager services for specific projects. The agreement with the master project manager states that, "the parties anticipate that it will be appointed a specific project manager for multiple projects, the Foundation shall have no obligation to do so, and each

party acknowledges and agrees that the Foundation shall at all times be free to solicit and/or appoint third-party developers to do entire projects or certain elements thereof.” Notwithstanding the foregoing, the Foundation agreed that, “in determining whether to appoint the master project manager as specific project manager or to seek a third-party developer, the Foundation would remain mindful that the master project manager entered into the agreement in anticipation of receiving such appointment to multiple projects, and will not base its decision primarily on avoiding payment of incentive compensation to the master project manager.”

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that the basis for appointing construction project management should be formally documented.

The Foundation chief operating officer stated that it was the intent of the Foundation from the outset to appoint the CCRP master project manager as the specific project manager for all CCRP projects. However, he further stated that the management contract was written to provide it with the option, should special circumstances arise, to select a different project manager for a specific project. The Foundation chief operating officer also stated that the special circumstances could be a situation where an outside investor is brought in and demands a different management arrangement. Finally, he stated that the management contract was implemented as intended and no special circumstances as described above have arisen.

Insufficient supporting documentation increases the risk that misunderstandings and miscommunication regarding rights and responsibilities could occur and exposes the campus and the CSU Trustees to potential liability.

Recommendation 8

We recommend that the Foundation, in the future, refrain from awarding all construction management services contracts to the same company that is to provide services as the master project manager.

Campus Response

We concur. For future construction projects, the Foundation will refrain from awarding construction management services contracts to the same company that will provide services as the master project manager.

THE CAMPANILE FOUNDATION

CORPORATE GOVERNANCE

DISSOLUTION CLAUSE

The Campanile Foundation Articles of Incorporation did not specify that the net assets of the dissolved auxiliary must be distributed to a successor approved by the campus president and the CSU Trustees.

The existing clause states that the successor would be approved by The Campanile Foundation's board of directors.

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

The Campanile Foundation chief financial and information officer of university advancement stated that the dissolution clause had been in place since the auxiliary was formed. He further stated his belief that the variance was immaterial and did not justify the cost to amend the Articles of Incorporation.

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

Recommendation 9

We recommend that The Campanile Foundation redraft its corporate dissolution clause in accordance with Title 5 and appropriately reflect this change in its Articles of Incorporation.

Campus Response

We concur. The Campanile Foundation will redraft its corporate dissolution clause in accordance with Title 5. Board approval for the change will be completed by April 1, 2005.

BOARD COMPOSITION

The Campanile Foundation's board did not include a student representative.

Title 5 §42602 (a)(b)(c) and Education Code §89903 specifically require student participation on auxiliary organization boards. In addition, this is also a requirement of the Foundation's bylaws.

The Campanile Foundation chief financial and information officer of university advancement stated that Associated Students, San Diego State University (AS) had not nominated a candidate to fill the vacant student representative seat.

Failure to maintain mandated board composition violates statutory requirements and increases the risk that all views will not be adequately represented.

Recommendation 10

We recommend that The Campanile Foundation coordinate with the AS to ensure that student board representation is maintained in accordance with Title 5 and CSU policy.

Campus Response

We concur. Student board representation has been coordinated with the AS to ensure compliance with Title 5 and CSU policy.

PUBLIC MEETINGS

The Campanile Foundation did not establish by resolution the time, date, and location for holding regular and annual board meetings as required by its bylaws.

Education Code §89921 states that each governing board shall establish by resolution, bylaws, or whatever rule is required for the conduct of business by that body, the time and locations for holding regular meetings.

Section 4.17 of The Campanile Foundation bylaws state that the board and any standing committee shall annually establish by resolution the time, date, and location for annual and regular board meetings.

The Campanile Foundation chief financial and information officer of university advancement stated that due to limitations in the availability of certain board members, meetings were not set by board resolution, but rather by notification at the annual meeting each year.

Non-compliance with regulations for public meetings increases the risk of misunderstandings and may increase legal liability.

Recommendation 11

We recommend that The Campanile Foundation comply with requirements to set meeting schedules by resolution as established within its bylaws or amend its bylaws in accordance with practice and in compliance with Education Code §89921.

Campus Response

We concur. The Campanile Foundation board will by "resolution" establish in advance the schedule for regular board and annual meetings at its annual meeting held each November.

AZTEC SHOPS, LTD.

OPERATING AND ADMINISTRATIVE AGREEMENTS

The Aztec Shops, Ltd. (Shops) performed functions inconsistent with CSU policy, specifically, the operation of dining services at two community colleges.

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

The Shops controller stated her belief that operating dining services for other educational institutions would be an authorized function since the Shops was authorized to operate dining services as part of its operating agreement with the CSU.

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

Recommendation 12

We recommend that the Shops perform only those functions listed in Title 5 or obtain approval for variances from the Office of the Chancellor.

Campus Response

The campus was unaware of an existing policy for approval of variances as suggested by the auditor. The campus will notify the Office of the Chancellor of the activities performed by Shops and will outline the bases for these activities.

CORPORATE GOVERNANCE

The Shops board adopted changes in the number of required members from ten to twelve without reflecting this change in its current bylaws.

Corporations Code §5151 (a) states, in part, that the bylaws shall set forth the number of directors of the corporation.

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

The Shops controller stated that the bylaws had not been updated due to the health situation of its attorney.

Operating under inappropriately authorized bylaws increases the risk of misunderstandings regarding rights and responsibilities.

Recommendation 13

We recommend that the Shops revise its bylaws to include recent changes adopted by its board.

Campus Response

We concur. Shops will revise its bylaws by April 30, 2005, to include recent changes adopted by its board.

FISCAL COMPLIANCE

The Shops written reserve policy had not been updated to reflect current practice on the allocation of surplus funds/reserves.

The *Compilation of Policies and Procedures for California State University Auxiliary Organizations* sets sound business practice guidelines for auxiliary organizations operating within the CSU system. Section §8.9.9, *Reserves and Net Assets*, states that the auxiliary should adopt written governing board policies that describe appropriate reserve requirements and provide for compliance with donor and other third-party legal obligations.

The Shops controller stated that she was aware that the reserve policy did not reflect current practice and that the Shops was in the process of determining the methodology to account for reserves.

The absence of a current, written reserve policy increases the risk of misunderstandings and miscommunication regarding reserves maintained.

Recommendation 14

We recommend that the Shops update its written reserve policy to reflect current practice on the allocation of surplus funds/reserves.

Campus Response

We concur. Shops will update its written reserve policy by March 31, 2005.

OPERATIONAL COMPLIANCE

The Shops current non-discrimination policy did not address discrimination based on pregnancy.

EO 883, *Systemwide Guidelines for Nondiscrimination and Affirmative Action Programs in Employment*, dated October 31, 2003, prohibits discrimination on the basis of race, color, religion, national origin, sex, sexual orientation, marital status, pregnancy, age, disability, medical condition, and covered veterans' status.

The Shops controller stated that legal counsel advised management that gender included pregnancy.

An inadequate non-discrimination policy increases the auxiliary's risk of non-compliance with state and federal laws and may result in regulatory actions.

Recommendation 15

We recommend that the Shops revise its non-discrimination policy to include discrimination based on pregnancy.

Campus Response

We concur. Shops non-discrimination policy has been revised.

PROPERTY AND EQUIPMENT

The Shops fixed asset inventory listing had not been reconciled to the general ledger on a timely basis.

We found that the adjustments resulting from the August 2003 inventory had not been reflected in the general ledger and fixed asset inventory listing as of May 2004.

The *Compilation of Policies and Procedures for California State University Auxiliary Organizations* sets sound business practice guidelines for auxiliary organizations operating within the CSU system. Section §8.9.7, *Property and Equipment*, states that the auxiliary should reconcile physical inventories to the general ledger on a timely basis with review by management.

The Shops controller stated that management intended to perform the reconciliation at year end.

Failure to reconcile physical inventories to the general ledger timely increases the risk that property may be lost or stolen.

Recommendation 16

We recommend that the Shops reconcile its fixed asset inventory listing to the general ledger on a timely basis.

Campus Response

We concur. Shops will reconcile its fixed asset inventory to the general ledger on a timely basis.

LOSS PREVENTION

The Shops did not maintain documentation of loss prevention audits and similar analysis of operations for management's review.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that audits and similar analysis of operations should be documented for management review.

The Shops controller stated that hard copies of these audits were not retained due to problems with the loss prevention computer.

Failure to maintain adequate documentation detailing audits and similar analysis of operations performed increases the risk of errors, irregularities, and misappropriation of funds.

Recommendation 17

We recommend that the Shops maintain documentation of loss prevention audits and similar analysis of operations for management's review.

Campus Response

We concur. As of October 1, 2004, Shops has maintained documents for loss prevention audits and analysis of operations for management's review.

ASSOCIATED STUDENTS, SAN DIEGO STATE UNIVERSITY

OPERATING AND ADMINISTRATIVE AGREEMENTS

Business arrangements between the Associated Students, San Diego State University (AS) and a local community service non-profit corporation were not supported by appropriate and current, written agreements.

We found that the AS continued to provide and receive programmatic services under an expired agreement. Additionally, the indemnity clause within a master agreement between the AS and the non-profit corporation did not sufficiently indemnify the state, the campus, or the CSU Trustees.

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

The AS associate director stated her belief that the master agreement eliminated the need for the programmatic agreement. She further stated that the failure to include required indemnification clauses was due to oversight.

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

Recommendation 18

We recommend that the AS ensure that business arrangements with a local community service non-profit corporation are properly supported by appropriate and current, written agreements.

Campus Response

We concur. Business arrangements between AS and a local community service non-profit corporation will be properly supported by written agreements.

CORPORATE GOVERNANCE

The AS Articles of Incorporation did not specify that the net assets of the dissolved auxiliary must be distributed to a successor approved by the campus president and the CSU Trustees.

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

The AS associate director stated her belief that the current dissolution clause was sufficient since it had been in place for a number of years.

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

Recommendation 19

We recommend that the AS redraft its corporate dissolution clause in accordance with Title 5 and appropriately reflect this change in its Articles of Incorporation.

Campus Response

We concur. AS will redraft its corporate dissolution clause in accordance with Title 5. Board approval for the change will be completed by April 30, 2005.

OPERATIONAL COMPLIANCE

In certain instances, the AS was not in compliance with its conflict-of-interest policy.

Specifically, we found that:

- ▶ The executive director did not report conflicts of interest to the vice president of business and financial affairs at the end of each calendar year.
- ▶ Non-voting board members did not sign a statement to evidence that they had read, understood, and would abide by the conflict-of-interest policy.

In addition, we found that signed statements were not on file for fiscal years 2001/02 and 2002/03, as it was not the policy of the AS to retain prior year conflict-of-interest statements.

AS conflict-of-interest policy required that the executive director report at the end of each calendar year to the vice president of business and financial affairs that there were no conflicts of interest for that year. Further, the AS conflict-of-interest policy required that all board members sign a statement to evidence that they had read, understood, and would abide by the policy.

Education Code §89906 states that no member of the governing board of an auxiliary organization shall be financially interested in any contract or other transaction entered into by the board of which he is a member, and any contract or transaction entered into in violation of this section is void.

Title 5 §42401, §42402, §42500 and Education Code §89900 establish a responsibility to operate in accordance with sound business practices in the interest of the campus. Sound business practice mandates establishing conflict-of-interest policies and procedures to implement Education Code §89906-89909, including provisions to appropriately retain documentation evidencing the implementation of those policies and procedures.

The AS associate director stated that the vice president of business and financial affairs was not notified regarding conflict of interest due to oversight. She also stated that non-voting board members did not sign the conflict-of-interest statements as it was her belief that only voting board members were required to sign statements. She further stated that signed statements were not retained for fiscal years 2001/02 and 2002/03 due to a lack of a record retention policy for conflict-of-interest documents.

Failure to comply with conflict-of-interest code policies and procedures for auxiliary boards and retain documentation evidencing compliance increases liability for acts contrary to the code.

Recommendation 20

We recommend that the AS ensure compliance with conflict-of-interest policies and procedures by:

- a. Reporting conflicts of interest to the vice president of business and financial affairs at the end of each calendar year.
- b. Requiring all board members sign a statement to evidence that they had read, understood, and would abide by the conflict-of-interest policy or clarifying policies by indicating that only voting board members are required to file statements.
- c. Developing a policy requiring the AS to retain prior year conflict-of-interest statements to evidence the implementation of conflict-of-interest policies and procedures.

Campus Response

We concur. AS has complied with its conflict-of-interest policies and procedures by:

- a. Reporting to the vice president for business and financial affairs at the end of each calendar year.
- b. Requiring all voting board members to sign statements.
- c. Retaining prior year statements.

PROPERTY AND EQUIPMENT

The AS did not conduct an independent physical inventory of fixed assets for fiscal year ended June 30, 2003. In addition, inventories conducted in prior years were completed by property custodians rather than by independent personnel.

The *Compilation of Policies and Procedures for California State University Auxiliary Organizations* sets sound business practice guidelines for auxiliary organizations operating within the CSU system. Section §8.9.7, *Property and Equipment, Conducting Physical Inventories*, states, in part, that the auxiliary should ensure physical inspection of property and equipment.

Title 5 §42401 and §42402 indicate that the campus president shall require that auxiliary organizations operate in conformity with policy of the Board of Trustees and the campus. One of the objectives of the auxiliary organizations is to provide fiscal procedures and management systems that allow effective coordination of the auxiliary activities with the campus in accordance with sound business practices. Sound business practice mandates that physical inventories of property and equipment be performed by someone other than the custodian.

The AS associate director stated that independent physical inventories of fixed assets were performed on an annual basis; however, one was not conducted for fiscal year ended June 30, 2003, due to oversight.

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

Recommendation 21

We recommend that the AS conduct a physical inventory of fixed assets annually and that it be performed by independent personnel.

Campus Response

We concur. AS will conduct an inventory of fixed assets, in a three-year cycle, performed by independent personnel. A full count of items over \$5,000 will be completed by April 30, 2005.

APPENDIX A: PERSONNEL CONTACTED

Name

Title

CAMPUS

Stephen L. Weber	President
Allan Bailey	Chief Financial and Information Officer, University Advancement
Edward Bulinski	Director, Budget and Planning
Valerie Carter	Audit and Tax Manager
Ellene Gibbs	Director, Business Information Management
Elizabeth A. Klonoff	Professor, Psychology and Co-Director, Clinical Training
Kenneth Perry	Associate Vice President, Financial Management
Sally Roush	Vice President, Business and Financial Affairs
Richard Schulte	Professor, Psychology and Co-Director, Clinical Training
Howard Toole	Professor, Accounting
Joseph Vasquez	Associate Vice President, Business Enterprise
Robert Wilbur	Associate Dean, Academic Affairs

SAN DIEGO STATE UNIVERSITY FOUNDATION

Steve Bloom	Chief Operating Officer
Bob Brown	Risk Manager
Denise Carroll	Purchasing Manager
Melinda Coil	Director, Financial Management
Michele Goetz	Director, Sponsored Research Administration
Patty Kastner	Accounting Manager
Leslie Levinson	Chief Financial Officer
Dianne Lovell	Associate Director, Human Resources
Shirley McGary	Payroll Manager and Alien Tax Coordinator
Nancy Monaghan	Accounts Payable Manager
Freya E. Sladek	Chief Executive Officer
Anthony Wallace	Accounts Payable Clerk
Carol Zito	Administrative Assistant

THE CAMPANILE FOUNDATION

Allan Bailey	Chief Financial and Information Officer, University Advancement
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AZTEC SHOPS, LTD.

Denise Allen	Assistant Sales Audit Supervisor
Rick Barber	Associate Director, Dining Services
Debbie Burchianti	Associate Director
Robyn Clarke	Associate Director, Campus Stores
Sandi Craig	General Ledger Technician
Michelle Duarte	Sales Audit Assistant
Liz Eller	Bookstore Manager
Gayle Fernandez	Executive Assistant
Sue Ann Finn	Human Resources Director
Imelda Hernandez Villa	Sales Audit Working Assistant Supervisor

APPENDIX A

Jahan Jamshidi	Management Information Systems Director
Dory Lee	Sales Audit Assistant Supervisor
Sylvia Mangubat	Campus Stores Director
Gary Mansfield	Associate Director, Distribution and E-Commerce
Larry Marmon	Chief Executive Officer
Donna Martens	Accounting Technician
Jan Mask	Director, Course Materials and Montezuma Publishing
Lois McCoy	Sales Audit Manager
Leah Messenger	Payroll Manager
Marnee Morris	Administrative Assistant
H.E. Reichert	Auditor and Contract Specialists
Veronica Sandoval	Sales Audit Working Assistant Supervisor
Tibor Sarlos	Business Manager
Cathy Schieffer	Controller
Martha Speck	Associate Director, Purchasing and Distribution
Don Taylor	Director, Loss Prevention
Donna Tusack	Chief Administrative Officer
Barbara Van Meter	Accounting Manager
Jennifer Virgin	Sales Audit Assistant
Virginia Weckbeck	Accounts Payable Technician
Cheri Witchell	General Manager, Convenience Stores
Debra Woodman	Accounts Receivable Technician

ASSOCIATED STUDENTS, SAN DIEGO STATE UNIVERSITY

Rebekah Bulette	Ticket Office Supervisor
Cheryle Conelly	Accounts Payable Clerk
Dan R. Cornthwaite	Executive Director
Jennifer Marie Esquivel-Parker	Assistant to the Executive Director
Israel Garza	Accounting Manager
Vicki Greene	Member Services Coordinator
Frances S. Hasterok	Accounts Receivable Clerk
Lana Heck	Government Business Office Supervisor
Susan Heiser	Associate Director
Sandra E. Keshka	Controller
John Kolek	Cox Arena Director
Ismael Lopez	Accounts Payable Assistant
Brenda Plasencia	Accounting Clerk
Laurie Prettyman	Cashier
Rosa Ramos	Payroll Supervisor

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 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 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.



San Diego State University
5500 Campanile Drive
San Diego, CA 92182-8000
Tel: 619 594-5201
Fax: 619 594-8894

THE PRESIDENT

January 25, 2005

Mr. Larry Mandel
University Auditor
The California State University
401 Golden Shore, 4th Floor
Long Beach, CA 90802

RECEIVED
UNIVERSITY AUDITOR

JAN 24 2005

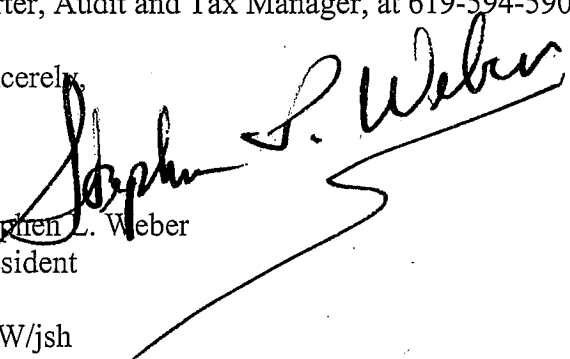
THE CALIFORNIA STATE
UNIVERSITY

Dear Mr. Mandel:

Enclosed is San Diego State University's response to the audit recommendations referenced in Report Number 04-48, *Auxiliary Organizations*. Documentation of policy and control changes will follow under separate cover.

Should you have any questions or require additional information, please contact Valerie Carter, Audit and Tax Manager, at 619-594-5901.

Sincerely,


Stephen L. Weber
President

SLW/jsh

Enclosure

- c: Sally F. Roush, Vice President, Business and Financial Affairs
Ellene J. Gibbs, Associate Vice President, Financial Operations
Dan R. Cornthwaite, Executive Director, Associated Students
Larry Marmon, Chief Executive Officer, Aztec Shops, Ltd.
Frea E. Sladek, Chief Executive Officer, SDSU Foundation
Allan Bailey, Chief Financial and Information Officer, The Campanile Foundation
Valerie J. Carter, Audit and Tax Manager

**AUXILIARY ORGANIZATIONS
SAN DIEGO STATE UNIVERSITY
Report Number 04-48**

CAMPUS

OPERATING AND ADMINISTRATIVE AGREEMENTS

Recommendation 1

We recommend that the campus establish specific written agreements with the Foundation that clearly define the responsibilities of each of the respective organizations regarding campus supervision of auxiliary employees.

Campus Response

We concur. The campus will establish specific written agreements with the Foundation that clearly define the responsibilities regarding campus supervision of auxiliary employees. This will be completed by April 30, 2005.

CAMPUS OVERSIGHT AND CONTROL

Recommendation 2

We recommend that the campus:

- a. Institute procedures requiring a specific financial review and analysis by campus fiscal administration during the establishment of campus centers, institutes, and similar organizations and programs.
- b. Establish procedures to ensure that all of these organizations and programs were included among approved centers, institutes, and similar organizations reported to the chancellor's office.
- c. Document agreement between responsible campus departments regarding the evaluation and oversight risks associated with campus centers, institutes, and similar organizations and programs.
- d. Clarify responsibility for evaluating and overseeing risks associated with campus centers, institutes, and similar organizations and programs.
- e. Ensure that funds generated by state organizations and programs are maintained and administered as in state accounts.

Campus Response

We concur. The campus will strengthen its procedures regarding centers, institutes, and similar organizations and programs. Revised procedures will require an appropriate level of financial review and analysis by campus fiscal administration. As part of the review, funds generated by specific programs will be evaluated and administered in the appropriate accounts. In addition, procedures will include an evaluation and oversight of risks which will include adequate documentation. Annually, all centers and institutes will be reported to the Chancellor's Office. Revised procedures will be completed by April 30, 2005.

AUXILIARY PROGRAMS**Recommendation 3**

We recommend that the campus review the current royalty arrangements between academic departments and the Shops and take appropriate action to ensure compliance to administrative and academic/professional responsibility policies regarding instructional materials publishing and related/required reimbursements to the General Fund.

Campus Response

We concur. The campus will review the current arrangements between academic departments and Aztec Shops regarding the publishing of instructional materials and take appropriate action to ensure compliance with administrative and academic/professional policies. This review will be completed by April 30, 2005.

SAN DIEGO STATE UNIVERSITY FOUNDATION

CORPORATE GOVERNANCE

Recommendation 4

We recommend that the Foundation redraft its corporate dissolution clause in accordance with Title 5 and appropriately reflect this change in its Articles of Incorporation.

Campus Response

We concur. The Foundation will redraft its corporate dissolution clause in accordance with Title 5. Board approval for the change will be completed by March 15, 2005.

OPERATIONAL COMPLIANCE

Recommendation 5

We recommend that the Foundation include within its written personnel policies and procedures standards for evidencing its analysis of the comparability of salaries, working conditions, and benefits for its full-time employees in relation to those provided campus employees performing substantially similar services.

Campus Response

We concur. The Foundation will revise its procedures to provide evidence of its analysis of salaries, working conditions, and benefits for its full-time employees in relation to those provided campus employees performing substantially similar services. Procedures will be revised by March 31, 2005.

SEGREGATION OF DUTIES

Recommendation 6

We recommend that the Foundation properly segregate accounting functions for personnel and payroll or institute mitigating procedures approved by the campus CFO.

Campus Response

We concur. The Foundation will request that its mitigating procedures are approved and documented by the Vice President for Business and Financial Affairs by March 15, 2005.

PURCHASING AND ACCOUNTS PAYABLE

CONSTRUCTION POLICIES AND PROCEDURES

Recommendation 7

We recommend that the Foundation develop procurement policies and procedures specific to its major capital construction projects to address, among other things:

- a. The project and contract prebid, bid, and award processes, including the bid proposal package, bid documentation, prequalification of bidders, withdrawal of bids, bid rejection, bid acceptance, and award of contract.
- b. Project oversight, including progress schedule and contract cost breakdown, contractor's payment requests, and safety compliance.
- c. Contract change order procedures, including normal change orders, change order proposal procedures, contract change orders, emergency change orders, disputed work issues, and requests for time extensions.
- d. Contract compliance and monitoring, including final inspections, project completion reports, and work performed under local jurisdictions and reconciliation of contract time.

Campus Response

We concur. The Foundation will develop procurement policies and procedures specific to its major capital construction projects to address the project and contract prebid, bid, and award process, project oversight, contract change order procedures, and contract compliance and monitoring. Procedures will be documented by April 15, 2005.

VENDOR SELECTION

Recommendation 8

We recommend that the Foundation, in the future, refrain from awarding all construction management services contracts to the same company that is to provide services as the master project manager.

Campus Response

We concur. For future construction projects, the Foundation will refrain from awarding construction management services contracts to the same company that will provide services as the master project manager.

THE CAMPANILE FOUNDATION

CORPORATE GOVERNANCE

DISSOLUTION CLAUSE

Recommendation 9

We recommend that The Campanile Foundation redraft its corporate dissolution clause in accordance with Title 5 and appropriately reflect this change in its Articles of Incorporation.

Campus Response

We concur. The Campanile Foundation will redraft its corporate dissolution clause in accordance with Title 5. Board approval for the change will be completed by April 1, 2005.

BOARD COMPOSITION

Recommendation 10

We recommend that The Campanile Foundation coordinate with the AS to ensure that student board representation is maintained in accordance with Title 5 and CSU policy.

Campus Response

We concur. Student board representation has been coordinated with Associated Students to ensure compliance with Title 5 and CSU policy.

PUBLIC MEETINGS

Recommendation 11

We recommend that The Campanile Foundation comply with requirements to set meeting schedules by resolution as established within its bylaws or amend its bylaws in accordance with practice and in compliance with Education Code §89921.

Campus Response

We concur. The Campanile Foundation Board will by “resolution” establish in advance the schedule for regular board and annual meetings at its annual meeting held each November.

AZTEC SHOPS, LTD.

OPERATING AND ADMINISTRATIVE AGREEMENTS

Recommendation 12

We recommend that the Shops perform only those functions listed in Title 5 or obtain approval for variances from the Office of the Chancellor.

Campus Response

The campus was unaware of an existing policy for approval of variances as suggested by the auditor. The campus will notify the Office of the Chancellor of the activities performed by Shops and will outline the bases for these activities.

CORPORATE GOVERNANCE

Recommendation 13

We recommend that the Shops revise its bylaws to include recent changes adopted by its board.

Campus Response

We concur. Shops will revise its bylaws by April 30, 2005 to include recent changes adopted by its board.

FISCAL COMPLIANCE

Recommendation 14

We recommend that the Shops update its written reserve policy to reflect current practice on the allocation of surplus funds/reserves.

Campus Response

We concur. Shops will update its written reserve policy by March 31, 2005.

OPERATIONAL COMPLIANCE

Recommendation 15

We recommend that the Shops revise its non-discrimination policy to include discrimination based on pregnancy.

Campus Response

We concur. Shops non-discrimination policy has been revised.

PROPERTY AND EQUIPMENT

Recommendation 16

We recommend that the Shops reconcile its fixed asset inventory listing to the general ledger on a timely basis.

Campus Response

We concur. Shops will reconcile its fixed asset inventory to the general ledger on a timely basis.

LOSS PREVENTION

Recommendation 17

We recommend that the Shops maintain documentation of loss prevention audits and similar analysis of operations for management's review.

Campus Response

We concur. As of October 1, 2004 Shops has maintained documents for loss prevention audits and analysis of operations for management's review.

ASSOCIATED STUDENTS, SAN DIEGO STATE UNIVERSITY

OPERATING AND ADMINISTRATIVE AGREEMENTS

Recommendation 18

We recommend that the AS ensure that business arrangements with a local community service non-profit corporation are properly supported by appropriate and current, written agreements.

Campus Response

We concur. Business arrangements between AS and a local community service non-profit corporation will be properly supported by written agreements.

CORPORATE GOVERNANCE

Recommendation 19

We recommend that the AS redraft its corporate dissolution clause in accordance with Title 5 and appropriately reflect this change in its Articles of Incorporation.

Campus Response

We concur. AS will redraft its corporate dissolution clause in accordance with Title 5. Board approval for the change will be completed by April 30, 2005.

OPERATIONAL COMPLIANCE

Recommendation 20

We recommend that the AS ensure compliance with conflict-of-interest policies and procedures by:

- a. Reporting conflicts of interest to the vice president of business and financial affairs at the end of each calendar year.
- b. Requiring all board members sign a statement to evidence that they had read, understood, and would abide by the conflict-of-interest policy or clarifying policies by indicating that only voting board members are required to file statements.
- c. Developing a policy requiring the AS to retain prior year conflict-of-interest statements to evidence the implementation of conflict-of-interest policies and procedures.

Campus Response

We concur. AS has complied with its conflict-of-interest policies and procedures by:

- a. Reporting to the Vice President for Business and Financial Affairs at the end of each calendar year.
- b. Requiring all voting board members to sign statements.
- c. Retaining prior year statements.

PROPERTY AND EQUIPMENT

Recommendation 21

We recommend that the AS conduct a physical inventory of fixed assets annually and that it be performed by independent personnel.

Campus Response

We concur. AS will conduct an inventory of fixed assets, in a three-year cycle, performed by independent personnel. A full count of items over \$5,000 will be completed by April 30, 2005.



THE CALIFORNIA STATE UNIVERSITY

 OFFICE OF THE CHANCELLOR

BAKERSFIELD

February 22, 2005

CHANNEL ISLANDS

CHICO

MEMORANDUM

DOMINGUEZ HILLS

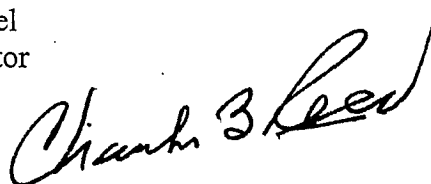
FRESNO

FULLERTON

TO: Mr. Larry Mandel
University Auditor

HAYWARD

FROM: Charles B. Reed
Chancellor



HUMBOLDT

LONG BEACH

SUBJECT: Draft Final Report Number 04-48 on *Auxiliary Organizations*,
San Diego State University

LOS ANGELES

MARITIME ACADEMY

MONTEREY BAY

In response to your memorandum of February 22, 2005, I accept the response as submitted with the draft final report on *Auxiliary Organizations*, San Diego State University.

NORTHRIDGE

POMONA

SACRAMENTO

CBR/amd

SAN BERNARDINO

Enclosure

SAN DIEGO

cc: Ms. Ellene J. Gibbs, Associate Vice President, Financial Operations
Dr. Stephen L. Weber, President

SAN FRANCISCO

SAN JOSE

SAN LUIS OBISPO

SAN MARCOS

SONOMA

STANISLAUS