

Audit and Advisory Services
401 Golden Shore
Long Beach, CA 90802-4210

March 6, 2024

Dr. Cynthia Teniente-Matson, President
San José State University
One Washington Square
San José, CA 95192

Dear Dr. Teniente-Matson:

Subject: Audit Report 23-03, Endowment Management, San José State University

We have completed an audit of *Endowment Management* as part of our 2023-2024 Audit Plan, and the final report is attached for your reference. The audit was conducted in accordance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

I have reviewed the management response and have concluded that it appropriately addresses our recommendations. The management response has been incorporated into the final audit report, which will be posted to Audit and Advisory Services' website. We will follow-up on the implementation of corrective actions outlined in the response and determine whether additional action is required.

Any observations not included in this report were discussed with your staff at the informal exit conference and may be subject to follow-up.

I wish to express my appreciation for the cooperation extended by the campus personnel over the course of this review.

Sincerely,



Vlad Marinescu
Vice Chancellor and Chief Audit Officer

c: Mildred García, Chancellor
Yammilette Rodriguez, Chair, Committee on Audit
Jean Picker Firstenberg, Vice Chair, Committee on Audit

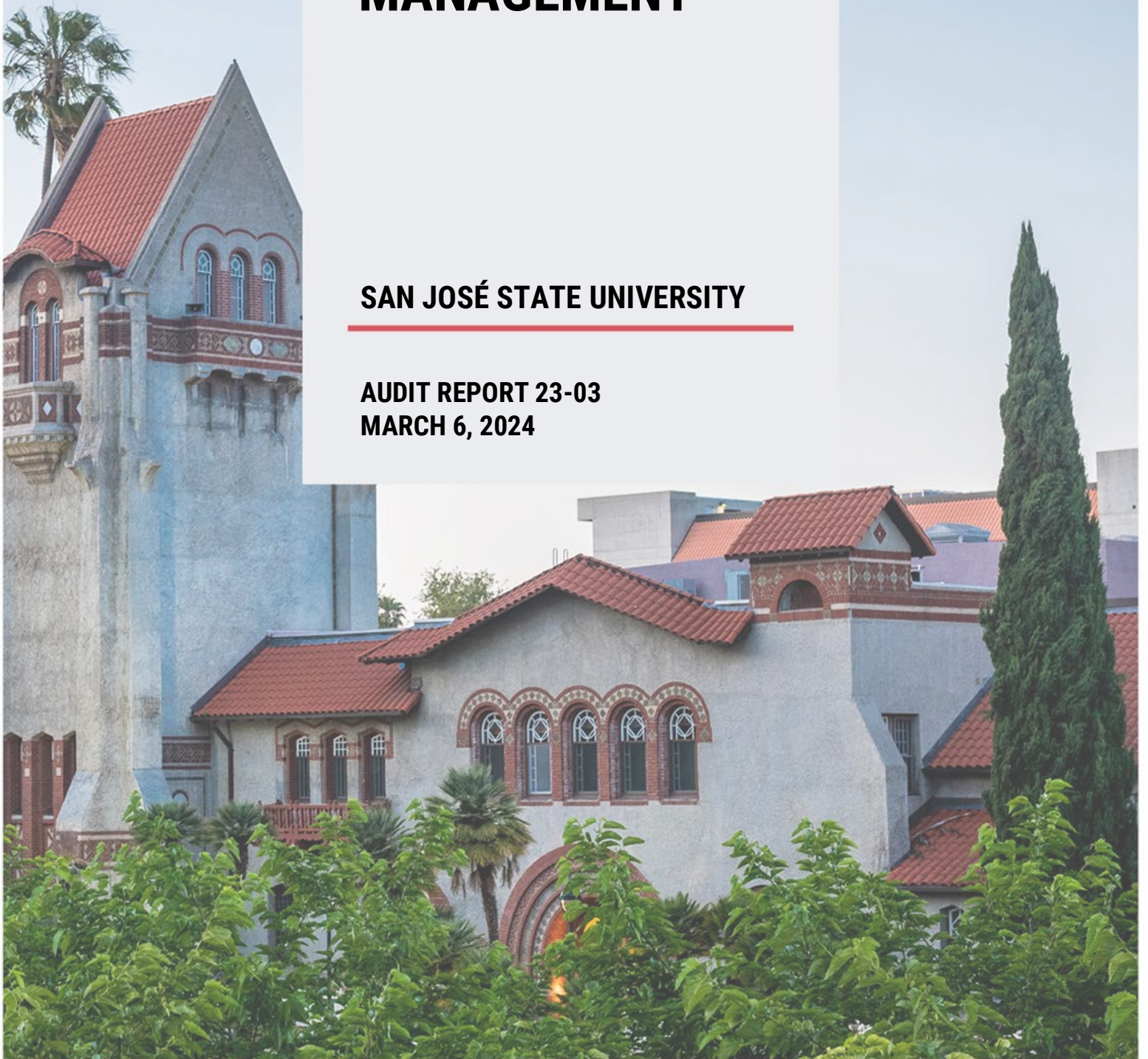
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ENDOWMENT MANAGEMENT

SAN JOSÉ STATE UNIVERSITY

**AUDIT REPORT 23-03
MARCH 6, 2024**



EXECUTIVE SUMMARY

AUDIT OBJECTIVES AND BACKGROUND

In accordance with the fiscal year (FY) 2023/24 Audit Plan, as approved by the Board of Trustees, Audit and Advisory Services performed an audit of endowment management at San José State University (SJSU).

The objectives of the audit were to ascertain the effectiveness of operational, administrative, and financial controls related to endowment management and to ensure compliance with relevant federal and state regulations, Trustee policy, Office of the Chancellor (CO) directives, and campus and auxiliary procedures.

University endowments are made up of financial assets donated to the institution to support the teaching, research, and public service missions of colleges and universities. Endowment funds, the principal of which cannot be expended by the university, are generally established with a donor-directed designation for the spending of the proceeds. The market value of endowments for SJSU at the end of FY 2022/23 was \$182.6 million. Endowment funds are held at The Tower Foundation of SJSU (Tower Foundation), and administrative and investment oversight is provided by the Tower Foundation board of directors.

OVERALL CONCLUSION

Based upon the results of the work performed within the scope of the audit, except for the weaknesses described below, the operational, administrative, and financial controls for endowment management as of November 30, 2023, taken as a whole, provided reasonable assurance that risks were being managed and objectives were met.

AUDIT SCOPE AND RESULTS

In general, we found that endowment management operations were effective and services were provided in compliance with California State University (CSU) policies and procedures. We did not note any issues related to the core function of endowment management at SJSU in our review. Although there had been recent changes in Tower Foundation executive leadership, we found that the auxiliary had maintained strong oversight of the endowment investment portfolio. The Tower Foundation finance and investment committee monitored and evaluated fund performance and regularly consulted with Beacon Pointe, the third-party investment advisor, during quarterly committee meetings.

However, our review did note a few areas for improvement related to account and expenditure documentation and review of user access to Financial Edge, the Tower Foundation accounting system. Specifically, we found that some endowment account authorization forms did not include required campus signatures or had not been updated when there was a change in an account signer. We also noted missing approvals for endowment expenditure requests. Additionally, we found instances where terminated employees retained view-only access to Financial Edge, as well as instances of employees with inappropriate levels of access given their roles and responsibilities. A summary of the observations noted in the report is presented in the table below. Further details are specified in the remainder of the report.

Area	Processes Reviewed	Audit Assessment
General Environment	Oversight of endowment program, outside reporting, policies and procedures, relationships and agreements with other entities (internal and external), financial statement recording	<i>Effective – no reportable observations noted</i>
Endowment Gift Processing	Endowment gift acceptance, creation, and recording; gift system access; gift agreements	<i>Observation noted in user access to the accounting system</i>
Distributions	Distribution calculation and approvals, endowment account setup and recording of distributions, endowment spending rate	<i>Observation noted in administration of account authorization forms</i>
Expenditures	Administration, review and approval of expenditures, dormant accounts, spending/expenditure policies and procedures, compliance with donor intent	<i>Observation noted related to missing approvals for endowment expenditure requests</i>
Investments	Investment manager and administrative fees, investment performance reporting, investment policies and procedures (such as return objectives, investment asset allocation, and rebalancing), allocation of investment gains and losses, investment reconciliations	<i>Effective – no reportable observations noted</i>

The audit focused on procedures in effect from July 1, 2021, through November 30, 2023. Our audit and evaluation included the audit tests we considered necessary in determining whether operational, administrative, and financial controls are in place and operative. Our review was limited to gaining reasonable assurance that essential elements of endowment management were in place and did not examine all aspects of the program.

OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

1. ENDOWMENT ACCOUNT AUTHORIZATION FORMS

OBSERVATION

Administration of account authorization forms needed improvement.

We reviewed endowment account authorization forms for 35 endowments and found that:

- In 19 instances, endowment account authorization forms had not been signed by the account holder and reviewed by a campus approver (such as the department chair, college dean, or vice president). Endowment account authorization forms specify the purpose of the endowment account and establish the individuals who are authorized to approve spending from endowment funds. In our discussions with the Tower Foundation, we learned that account holders are not required to sign the forms to become authorized account signers. Instead, Tower Foundation will designate an employee with appropriate authority from the department or college receiving the endowment funds to be the account signer.
- The Tower Foundation could not locate the account authorization form for one endowment established in 2017.

We also reviewed 25 non-scholarship expenditures from 12 endowment accounts and found that:

- For 23 expenditures from 10 endowment accounts, the expenditure was approved by an individual who was not the authorized signer for the endowment account. For these 10 accounts, we noted that the individual has the required authority, however the account authorization forms had not been timely updated.

Adequate administration of account authorization forms increases accountability and oversight for endowment management and decreases the risk of misappropriation of endowment funds and exposure to litigation.

RECOMMENDATION

We recommend that the campus, in conjunction with the Tower Foundation, develop and implement policies and procedures that address the completion and approval of account authorization forms for new endowments, as well as the process to update forms when there are changes in authorized signers.

MANAGEMENT RESPONSE
<p>We concur. SJSU and Tower Foundation will develop and implement policies and procedures that address the completion and approval of account authorization forms for new endowments, as well as the process to update forms.</p> <p>Expected completion date: May 31, 2024</p>

2. ENDOWMENT EXPENDITURES

OBSERVATION

Tower Foundation review of endowment expenditures needed improvement.

We reviewed 25 non-scholarship endowment expenditures and found that:

- In two instances, expenditure requests had missing approval signatures from authorized account signers. The expenditures related to salaries and supply reimbursement requests from the campus. We reviewed the expenditures with management and noted the expenses were appropriate and disbursed in accordance with the terms of the endowment.
- Tower Foundation requires all endowment expenditure requests to be reviewed and approved by endowment accounting staff prior to being processed for payment. In 11 instances, we found that there were missing documented approvals from endowment accounting to process salary, supply, professional membership, travel, equipment, and service expenditures. We reviewed the expenditures with management and noted that the expenses appeared to be appropriate and related to the endowment purpose.

Proper review and approval of expenditures reduces the risk of errors, irregularities, and misappropriation of funds.

RECOMMENDATION

We recommend that the campus, in conjunction with Tower Foundation communicate and provide training regarding procedures on the expenditure review and approval process, including the review process for expenditures relating to campus reimbursements requests, to appropriate auxiliary personnel.

MANAGEMENT RESPONSE
We concur. SJSU and Tower Foundation will communicate and provide training regarding procedures on the expenditure review and approval process to appropriate auxiliary personnel. Expected completion date: May 31, 2024

3. USER-ACCESS REVIEW

OBSERVATION

Administration of user access for Financial Edge needed improvement.

We reviewed a listing of all active users in Financial Edge and noted the following:

- Five active view-only user accounts belonged to terminated employees and should have been deactivated and removed from Financial Edge. However, we confirmed that campus active directory access is required to log-in to Financial Edge, and that upon separation, employees are removed from active directory when their SJSU ID is terminated, preventing access to the financial system.

- Six university advancement (UA) staff members were granted an inappropriate level of access to the accounting system, which provided them with the ability to record journal entries in Financial Edge. UA employee access had been changed from “view-only” to “accounting” in 2022 due to proposed reorganization plans that would have impacted these individuals’ responsibilities and necessitated an elevated level of access to Financial Edge. The Tower Foundation decided not to move forward with the reorganization, but UA employee access to the accounting system was not changed back to “view-only.” During fieldwork, the Tower Foundation adjusted the access level for the six UA staff members to “view-only.” Based on review of a Financial Edge report that detailed all changes made by users during the audit period, we also confirmed that the six UA staff members did not post, modify, or approve any journal entries within the accounting system.

Periodic review of employee access and timely removal and modification of access based on such review decreases the risk of unauthorized or inappropriate activity and ensures compliance with California State University (CSU) and campus policies.

RECOMMENDATION

We recommend that the campus:

- a. Develop and implement a procedure for periodic review of user access to Financial Edge, including a process to remove or adjust access when employees separate or there is a change in job responsibilities.
- b. Remove access to Financial Edge for the separated employees noted above.

MANAGEMENT RESPONSE

We concur. SJSU and Tower Foundation will:

- a. Develop and implement a procedure for periodic review of user access to Financial Edge, including a process to remove or adjust access when employees separate or there is a change in job responsibilities.
- b. Remove access to Financial Edge for the separated employees noted above.

Expected completion date: May 31, 2024

GENERAL INFORMATION

ADDITIONAL BACKGROUND

The state of California adopted the Uniform Prudent Management of Institution Funds Act (UPMIFA), the standards of care for both managing and investing endowments, in 2009. UPMIFA and its predecessor, the Uniform Management of Institutional Funds Act (UMIFA), clarified and revised historic interpretations of income from endowment funds and provided both a duty to ensure the growth of the principal to maintain spending power and a right to distribute from the corpus when the actions taken are prudent for the purposes for which the fund was established. UPMIFA also imposed a duty to diversify; allowed for the delegation of investment decisions to an outside professional entity; and suggested a percentage limit for annual spend that beyond which any spending would be presumptively imprudent.

In FY 2021/22, the value of CSU endowments reached \$2.3 billion. During that FY, the CSU received \$108 million in additional endowment funds and distributed \$76 million from proceeds. Endowment funds, the principal of which cannot be expended by the university, are generally established with a donor-directed designation for the spending of the proceeds. More than half of the CSU's endowments are designated for student scholarships; others support academic programs, such as nursing and agriculture, and student enrichment programs, such as study abroad.

At SJSU, the campus distributed \$5 million from endowment proceeds in FY 2022/23 for scholarships and various programs such as honoraria for participants of the visiting professionals program, support of a faculty professorship for the school of business, and contributions to faculty research and professional development. The Tower Foundation board of directors has established policies that govern the investment activities carried out by an outside investment firm, and the fund distributions are calculated and processed by Tower Foundation operations. Once the annual distributions are made to designated campus departments, it is the responsibility of the departments to ensure that expenditures align with the donor intent for the endowment.

CRITERIA

Our audit was based upon standards as set forth in federal and state regulations and guidance, Trustee policy, Office of the Chancellor directives, and campus procedures, as well as sound administrative practices and consideration of the potential impact of significant risks. This audit was conducted in conformance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

This review emphasized, but was not limited to, compliance with:

- Probate Code §18501-18510, *Uniform Prudent Management of Institutional Funds Act*
- CSU *Delegation of Gift Evaluation and Acceptance*
- CSU *Utilization of Campus Auxiliary Organizations*
- CSU *Placement and Control of Receipts from Campus Activities*
- CSU *Information Security Policy and Standards*
- CSU *Auxiliary Organizations Compliance Guide*
- CSU *Auxiliary Organizations Sound Business Practices Guidelines*
- Council for Advancement Support of Education Guidelines
- SJSU *University Gift Acceptance Standards*
- SJSU *Gift Agreement Guidelines*
- Tower Foundation *Endowment Investment Policies, Guidelines, and Objectives*

- Tower Foundation *Employee Handbook*

AUDIT TEAM

Audit Manager: Kyle Ishii

Senior Auditor: Janaki Nakum