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September 14, 2018

Dr. Joseph I. Castro, President
California State University, Fresno
5241 N. Maple Avenue
Fresno, CA 93740

Dear Dr. Castro:

Subject: Audit Report 18-22, *Agricultural Foundation*, California State University, Fresno

We have completed an audit of *Agricultural Foundation* as part of our 2018 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, which includes the campus' decision to accept the risk inherent in not adequately segregating duties and responsibilities related to cash receipts and purchasing, and have concluded that it appropriately addresses our recommendations. The management response has been incorporated into the final audit report, which has been posted to the 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,



Larry Mandel
Vice Chancellor and Chief Audit Officer

c: Timothy P. White, Chancellor

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The California State University
Audit and Advisory Services

AGRICULTURAL FOUNDATION
California State University, Fresno

Audit Report 18-22
August 7, 2018

EXECUTIVE SUMMARY

OBJECTIVE

The objectives of the audit were to confirm compliance with regulatory requirements for the establishment and governance of auxiliary organizations; ascertain effectiveness of operational, administrative, and financial controls for the activities conducted by the Agricultural Foundation of California State University, Fresno (Ag Foundation); evaluate adherence to auxiliary policies and procedures and applicable Integrated California State University Administrative Manual (ICSUAM) policies, or, where appropriate, to an industry-accepted standard; and to ensure compliance with relevant governmental regulations, Trustee policy, Office of the Chancellor directives, and campus procedures.

CONCLUSION

We found the control environment for some of the areas reviewed to be in need of improvement.

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 the Ag Foundation as of June 22, 2018, taken as a whole, provided reasonable assurance that risks were being managed and objectives were met.

In general, we noted that the Ag Foundation had an appropriate framework for the administration of the auxiliary; however, we identified a few areas needing improvement. As noted in the prior auxiliary audit conducted in 2014, the duties and responsibilities related to cash receipts and purchasing at some Ag Foundation units lack adequate segregation of duties, primarily due to limited staffing. The campus has elected to accept the inherent risk in not taking corrective action on this item; details are provided in their response in the report. Also, the Ag Foundation was not maintaining supporting records when units directly received gifts-in-kind (GIK), nor was it conducting periodic reconciliations of GIKs posted to the University Advancement gifts system and the Auxiliary accounting system. Written procedures for GIKs also needed improvement. In addition, Ag Foundation agreements with third parties and a related auxiliary were not always executed in a timely manner.

Specific observations, recommendations, and management responses are detailed in the remainder of this report.

OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

1. SEGREGATION OF DUTIES

OBSERVATION

Duties and responsibilities related to cash receipts and purchasing at some Ag Foundation units were not adequately segregated.

We visited six Ag Foundation units and noted that most had limited staff, consisting of student employees under the direction of the unit manager, which sometimes resulted in a lack of proper segregation of duties. For example, one individual:

- Sold products, received payments, and prepared deposits without secondary review.
- Placed orders, received goods, approved reimbursement requests, and was in charge of production and inventory.

We noted the same observation in a prior auxiliary audit conducted in 2014. Specifically, certain duties and responsibilities related to cash receipts, purchasing, and accounts payable were not adequately segregated at three Ag Foundation units.

Adequate segregation of duties is an essential internal control that can provide the necessary oversight and review to catch errors and prevent theft or fraud.

RECOMMENDATION

We recommend that the campus, in conjunction with the Ag Foundation, adequately segregate duties and responsibilities related to cash receipts and purchasing, or institute mitigating procedures.

MANAGEMENT RESPONSE

We do not concur. The campus president and campus chief financial officer agree to accept the level of risk associated with cash handling and purchasing responsibilities being performed within the enterprise units on the farm laboratory consistent with current policies and procedures as approved by the Ag Foundation. A letter of acknowledgement will be communicated to Audit and Advisory Services by September 30, 2018.

The Ag Foundation has mitigating procedures in place to reduce the potential for theft and fraud, such as monthly physical inventory reconciliation, monthly review of revenue and expenses, balancing and preparation of bank deposits by the auxiliary revenue technician, and approval of purchase orders and accounts payable warrants by the auxiliary controller.

2. GIFTS

OBSERVATION

Administration of gifts-in-kind (GIK) at the Ag Foundation needed improvement.

We reviewed ten Ag Foundation GIKs, and we found that:

- In three instances, the Jordan College of Agricultural Sciences and Technology (JCAST) development office did not maintain required documentation for GIKs, including a GIK form, gift receipt transmittal form, tax receipt, and thank you letter acknowledging the gift.

We noted that although these GIKs were received directly by Ag Foundation units and documented on a standard receipt/form (referred to as UARCO by the Ag Foundation), unit managers did not collect, maintain, or submit the required forms noted above to the JCAST. In each case, we found that the appropriate accounting documentation was obtained by auxiliary accounting, which then timely notified the JCAST office of the gifts.

- In one instance, an auxiliary unit did not inform auxiliary accounting about a GIK; auxiliary accounting learned of the GIK during the unit's annual inventory. As such, no supporting documentation was initially provided by the auxiliary unit, and auxiliary accounting did not timely notify the JCAST development office.
- In one instance, the JCAST development office did not send the customary thank you letter to the donor.

We also found that the Ag Foundation did not perform periodic reconciliation of GIKs posted to the University Advancement gifts system and the auxiliary accounting system, and the Ag Foundation GIK procedures did not address the reconciliation process.

In addition, the Ag Foundation did not have written procedures regarding the acceptance of certain cash gifts, including the types of cash gifts that are accepted, where gifts are accepted, and how they are processed. As a result, there was some confusion regarding processing for these gifts. According to the Ag Foundation executive director, the JCAST development office was the only place cash gifts could be accepted, and only the Fresno State Foundation could accept matching gifts. However, in our review of five Ag Foundation cash gifts, we found that:

- One check of \$3,000 was accepted by an Ag Foundation unit and deposited by the Ag Foundation instead of being processed by the JCAST development office.
- Three checks totaling \$547 related to matching gifts were received and deposited by the Ag Foundation rather than the Fresno State Foundation.

Sufficient oversight and administration of Ag Foundation gifts helps to ensure proper processing and recording and reduces the risk of errors, misplaced gifts, misappropriation of funds, and noncompliance with donor terms.

RECOMMENDATION

We recommend that the campus, in conjunction with the Ag Foundation:

- a. Maintain required documentation for all Ag Foundation GIKs, including, but not limited to, a GIK form, gift receipt transmittal form, tax receipt, and thank you letter acknowledging the gift.
- b. Perform periodic reconciliation of GIKs posted to the University Advancement gifts system and the auxiliary accounting system, and update the Ag Foundation GIK procedures.
- c. Determine whether the Ag Foundation should continue to receive cash gifts. If so, develop written procedures, including the types of cash gifts that are accepted, where gifts are accepted, and how they are processed.

MANAGEMENT RESPONSE

We concur.

- a. By September 30, 2018, the campus chief financial officer and Ag Foundation executive director will remind university advancement of its responsibility to maintain copies of all GIK documentation for the Ag Foundation, consistent with current university advancement procedures.
- b. Beginning in fiscal year 2018/19, auxiliary accounting will begin performing quarterly reconciliations of all GIK donations between the university's ADVANCE database and the Ag Foundation general ledger. University advancement's procedures will be updated accordingly. The first reconciliation will be completed by October 15, 2018.
- c. In accordance with its operating agreement, the Ag Foundation will continue to receipt cash gifts. By October 15, 2018, university advancement will advise Ag One and auxiliary accounting staff as to how cash gifts are defined, where they are to be accepted, and how they are to be processed. Gift processing is managed by university central development.

3. AGREEMENTS

OBSERVATION

Ag Foundation agreements with third parties and a related auxiliary were not always timely executed.

We reviewed 15 agreements, and we found that three agreements with third parties and one with a related auxiliary were signed after the agreement effective date. These execution delays ranged from 14 to 47 days.

Timely execution of written agreements reduces potential misunderstanding of the agreement terms, conditions, rights, and responsibilities, and reduces the CSU and auxiliaries exposure to potential loss and liability.

RECOMMENDATION

We recommend that the campus, in conjunction with the Ag Foundation ensure that all agreements with third parties and auxiliaries are timely executed.

MANAGEMENT RESPONSE

We concur. By October 15, 2018, auxiliary staff counsel will issue a reminder to all university agricultural laboratory staff that all agreements with third parties require prior legal review and must be submitted at least 30 days prior to the contract execution date.

GENERAL INFORMATION

BACKGROUND

Auxiliary organizations are separate business and legal entities that perform activities essential to the education program of each campus that cannot be legally or effectively administered using state funding. California Code of Regulations (CCR) Title 5, §42401 states that auxiliary organizations provide the fiscal means and the management procedures that allow the campus to carry on activities providing those instructional and service aids not normally furnished by the state budget.

Education Code §89900 states, in part, that the operation of auxiliary organizations shall be conducted in conformity with regulations established by the Trustees, and CCR Title 5, §42402 confirms the campus president's authority and responsibility for auxiliary organization operations. Campus 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.

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.

Executive Order 1059, Utilization of Campus Auxiliary Organizations, dated June 6, 2011, represents Trustee policy addressing appropriate use of CSU auxiliary organizations. This EO requires CSU auxiliary organizations to operate within the regulations and oversight of the campus. The EO reiterates that the campus president is responsible for ensuring the fiscal viability of auxiliary organizations and their compliance with applicable CSU policies, and it further designates the campus chief financial officer as the individual responsible for administrative compliance and fiscal oversight of auxiliary organizations.

California State University, Fresno (Fresno State) has six separate auxiliary organizations, each of which provides a function that contributes to the educational mission of the university. In 1954, the Ag Foundation was established as a non-profit public benefit corporation to provide the financial resources, land, animals, orchards, and vineyards for students to receive practical experience in the field of agriculture that reinforces their classroom instruction. The Ag Foundation is governed by an appointed board of directors, which is composed of university administrators and leaders from the San Joaquin Valley's agricultural community. The

California State University Fresno Association, Inc provides accounting and administrative support services and is referred to as auxiliary accounting.

SCOPE

We visited the Fresno State University campus and the Ag Foundation from May 21, 2018, through June 22, 2018. Our audit and evaluation included the audit tests we considered necessary in determining whether operational, administrative, and financial controls are in place and operative at the Ag Foundation. The audit focused on procedures in effect from January 1, 2016, to June 22, 2018.

Specifically, we reviewed and tested:

- Timely and proper execution of agreements, contracts, and memoranda of understanding.
- Fiscal, operational, and program compliance, such as reserve provisions, unrelated business income tax, conflict of interests, and risk management practices.
- Internal controls and segregation of duties over fiscal administration of areas such as cash receipts, accounts receivables, property and equipment, procurement, disbursements, and personnel and payroll.
- Gifts administration including, but not limited to, review of timely receiving, recording, and safeguarding of gifts-in-kind.
- Auxiliary enterprise unit administration including, but not limited to, review of budget, inventory, and cash handling.

As a result of changing conditions and the degree of compliance with procedures, the effectiveness of controls changes over time. Specific limitations that may hinder the effectiveness of an otherwise adequate system of controls include, but are not limited to, resource constraints, faulty judgments, unintentional errors, circumvention by collusion, and management overrides. Establishing controls that would prevent all these limitations would not be cost-effective; moreover, an audit may not always detect these limitations.

Our testing and methodology was designed to provide a review of key operational, administrative, and financial controls and included testing of a limited number of financial transactions and operational procedures.

CRITERIA

Our audit was based upon standards as set forth in CSU Board of Trustee policies; Office of the Chancellor policies, letters, and directives; campus procedures; and other sound administrative practices. 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:

- Education Code §89720
- Education Code §89756
- Education Code §89900

- Education Code §89904
- CCR Title 5, §42401, *Declaration of Policy*
- CCR Title 5, §42402, *Authority of Campus President*
- CCR Title 5, §42500, *Functions of Auxiliary Organizations*
- RFIN 7-81-4
- Executive Order (EO) 676, *Delegation of Gift Evaluation and Acceptance to Campuses*
- EO 1059, *Utilization of Campus Auxiliary Organizations*
- *CSU Auxiliary Organizations Compliance Guide*
- *CSU Auxiliary Organizations Sound Business Practices Guidelines*
- ICSUAM §1301.00, *Hospitality, Payment or Reimbursement of Expenses*
- ICSUAM §13680.00, *Placement and Control of Receipts for Campus Activities and Programs*
- ICSUAM §15000, *University Advancement*
- *Ag Foundation Cash Handling Policy and Procedures*
- *Ag Foundation Gifts-in-Kind Policy*
- *Fresno State Advancement Services Policies and Procedures*

AUDIT TEAM

Audit Manager: Joanna McDonald
Senior Auditor: May Flores