

Audit and Advisory Services
401 Golden Shore, 4th Floor
Long Beach, CA 90802-4210

562-951-4430
562-951-4955 (Fax)
lmandel@calstate.edu

December 6, 2018

Dr. Jeffrey D. Armstrong, President
California Polytechnic State University, San Luis Obispo
1 Grand Avenue
San Luis Obispo, CA 93407

Dear Dr. Armstrong:

**Subject: Audit Report 18-24, Cal Poly Corporation,
California Polytechnic State University, San Luis Obispo**

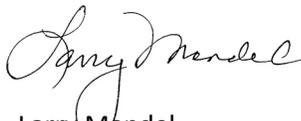
We have completed an audit of *Cal Poly Corporation* as part of our 2018 Audit Plan, and the final report is attached for your reference. The audit was conducted in accordance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*.

I have reviewed the management response 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 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

CAL POLY CORPORATION

**California Polytechnic State University,
San Luis Obispo**

Audit Report 18-24
November 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 Cal Poly Corporation (Corporation); 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 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 Corporation as of September 21, 2018, taken as a whole, provided reasonable assurance that risks were being managed and objectives were met.

In general, we noted that the Corporation had an appropriate framework for the administration of the auxiliary; however, we identified some areas needing improvement, and we found that two observations related to cash handling and timely execution of Corporation agreements were similar to observations in the prior auxiliary organizations audit conducted in 2014.

Administration of cash handling needed improvement related to segregation of duties, cash-handling training, safeguarding of funds, and endorsement of check payments, and administration of cash disbursements for hospitality expenses needed improvement related to maintenance of supporting documentation.

In addition, we found that fund-raising events were not always properly and timely approved and signed third-party agreements were not always maintained. Also, proper documentation was not always maintained to show that employee background checks were performed, and campus catering did not always obtain the required form for all catering events where alcoholic beverages were served. Further, a purchasing process did not follow Corporation procedures, and Corporation agreements with a third party and related parties were not always timely executed.

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

OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

1. CASH HANDLING

OBSERVATION

Administration of cash handling needed improvement related to segregation of duties, cash-handling training, safeguarding of funds, and timely endorsement of check payments.

We visited ten Corporation cash-handling locations, including four dining locations and four agricultural units, and we found that:

- One location lacked adequate oversight of cash handling and receipt-of-goods activities, primarily because the unit manager position was vacant. A campus department administrative support coordinator was assigned at the location but was unable to perform all of the unit manager position's duties.

At this location, new student cashiers did not receive formal or consistent training. There was also a lack of mitigating controls to ensure accuracy of transactions in the shared cash register, as cashiers did not have individual user log-ins to the register, and the register was closed out only once daily, at the end of the day. Also, cashiers selling products offsite at a farmers' market were allowed to give customers arbitrary discounts and did not timely record their cash sales in the point-of-sale system. In addition, receipts for hand-delivered products, such as floral and plant arrangements, did not always include the type of product sold and payment received. Further, the administrative support coordinator was not always notified of all deliveries received at this location.

- One location did not have adequate segregation of duties. Specifically, one individual sold products, received payments, and prepared deposits without secondary review. Also, customers were not always provided receipts at this location.
- One location had a single cash register that was used by up to ten student cashiers on busy days. Each cashier was assigned a unique log-in; however, the cash register was closed out only once a day, at the end of the day. As such, in the case of a shortage or overage, it would be difficult to identify where the error occurred. In addition, during a separate review of ten cash overages and shortages from various locations, we found one cash overage of \$32 at this location that did not have documented support showing that the overage had been researched and investigated.
- Three locations accepted check payments but did not timely endorse the checks and did not have an endorsement stamp.
- Two locations did not change the combination on their safes after turnover in personnel who had safe access.
- One location did not maintain a listing of individuals who had access to the safe or a record of when the safe combination was last changed.

We noted that cash locations cited above make up of a small percentage of the Corporation's total revenues. However, we noted similar cash-handling observations in a prior auxiliary audit conducted in 2014, where one location did not have adequate segregation of duties, safeguarding of funds, timely deposit of funds, and endorsement of check payments.

Adequate segregation of duties and proper administration of cash handling helps to ensure that employees are properly trained and aware of auxiliary policies and procedures and reduces the campus exposure to risk related to loss, theft, or misappropriation of funds.

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation, reiterate cash-handling policies and procedures and provide training to personnel involved in cash-handling activities, including adequate segregation of duties, safeguarding of funds, endorsement of checks, and other areas identified above.

MANAGEMENT RESPONSE

We concur. The Corporation will reiterate cash-handling policies and procedures to existing staff on a regular basis. The Corporation will provide additional training to any new personnel involved in cash-handling activities, including adequate segregation of duties, safeguarding of funds, endorsement of checks, and other areas identified above.

Anticipated implementation date: April 30, 2019

2. CASH DISBURSEMENTS

OBSERVATION

Administration of cash disbursements for hospitality expenses needed improvement related to maintenance of supporting documentation.

We reviewed hospitality expenses made between January 2016 and August 2018, and we found that in six of ten hospitality expenses reviewed, totaling \$15,686, hospitality justification forms had not been completed. Also, a hospitality justification form had not been completed for one campus program account expense of \$4,380. The hospitality justification form includes required information such as a description of the event and listing of attendees and official guests.

Maintaining supporting documentation for hospitality expenses reduces the risk of errors, irregularities, and misappropriation of funds.

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation, complete and retain a completed hospitality justification form for all hospitality expenses.

MANAGEMENT RESPONSE

We concur. The Corporation will update its disbursement processes to ensure that a hospitality justification form is completed and retained for all hospitality expenses. The Corporation will provide training and reminders to staff of the updated processes.

Anticipated implementation date: April 30, 2019

3. FUND-RAISING EVENTS

OBSERVATION

Fund-raising events were not always properly and timely approved, and signed third-party agreements were not always maintained.

We reviewed five fund-raising events with gross receipts greater than \$5,000 during fiscal year 2016/17, and we found that:

- In four instances, the fund-raising event was approved by the former university advancement chief operating officer (COO). However, fund-raising event administration procedures require events to be approved by the associate vice president (AVP) for advancement operations. We noted that at the time, the AVP for advancement operations position was vacant and the former university advancement COO took over the responsibility of approving fund-raising events, but the campus and auxiliary could not provide us with documentation showing this further delegation.
- In one instance, the fund-raising event approval form was signed after the date of the event.
- In two instances, the event took place at an offsite location, and the campus department holding the event did not maintain a signed agreement with the third party.

We noted that the campus department or unit holding the fund-raising event is responsible for processes that take place before the event, including obtaining approval for the event and executing third-party agreements, while the Corporation is responsible for post-event processes, including accounting and reporting of applicable IRS requirements.

Proper administration of fund-raising events helps to effectively allocate resources, coordinate events, and assess and mitigate any risks associated with these events.

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation:

- a. Determine whether someone other than the AVP for advancement operations can approve fund-raising events, and if so, update the fund-raising event procedures or provide a written memo indicating further delegation of authority.

- b. Ensure that fund-raising events are timely approved by the delegated authority.
- c. Reiterate the fund-raising event administration procedures to personnel involved with fund-raising events, including obtaining approval prior to the event and maintaining signed third-party agreements.

MANAGEMENT RESPONSE

We concur. The Corporation will coordinate with university advancement operations to review and update fund-raising event procedures to ensure approvals obtained are appropriate and timely. The Corporation will reiterate fund-raising event administration procedures to personnel involved with fund-raising events, including obtaining approval prior to the event and maintaining signed third-party agreements.

Anticipated implementation date: April 30, 2019

4. BACKGROUND CHECK

OBSERVATION

Background check documentation was not always maintained.

We reviewed the records for 15 conference and event-planning transactions and noted that four events involved minors. As such, we reviewed the records for 12 of the employees who worked at these events to verify that the required background check had been performed.

For seven employees, we found that the record showing that a background check had been completed and the employee had been cleared was not maintained. Instead, the human resources (HR) department had maintained a manually updated spreadsheet that listed employees and the date that a background check was performed.

Maintaining proper background check documentation helps to ensure compliance with CSU requirements and reduces the risks of legal liability.

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation, maintain background check documentation in employee HR files.

MANAGEMENT RESPONSE

We concur. The Corporation updated its HR recruitment processes to ensure background check records are retained in employee HR files.

Implemented: November 20, 2018

5. CATERING

OBSERVATION

University catering did not always obtain the required form for catering events where alcoholic beverages were served.

We reviewed ten catering contracts dated from June 2016 to June 2018, and we found that the alcohol service request form was not obtained for three events where alcoholic beverages were served.

Obtaining required alcohol request forms ensures compliance with campus and auxiliary requirements and reduces the risks associated with events serving alcoholic beverages.

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation, obtain the alcohol service request form for all catering events where alcoholic beverages are served.

MANAGEMENT RESPONSE

We concur. The Corporation will update its catering processes to ensure that alcohol service request forms are obtained for catering events where alcoholic beverages are served.

Anticipated implementation date: April 30, 2019

6. PURCHASING

OBSERVATION

A purchasing process did not always follow Corporation procedures.

We reviewed ten purchase orders (PO), and we found that an \$87,500 PO for an equipment purchase did not have formal bidding documentation as required by the Corporation's purchasing policy. Instead, the requesting department provided written quotes. We noted that the Corporation business office approved this PO request. According to the Corporation's *Purchasing Policy* for purchases exceeding \$25,000, an authorized signer on an account is required to submit a request for a PO and attach a minimum of three formal bids based on the same written specifications that provide competitive price, responsiveness to specifications, and reputation of vendors.

Obtaining formal bids for purchases exceeding \$25,000 ensures compliance with auxiliary procurement requirements and reduces the risk of errors, loss, theft, or misappropriation.

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation, determine whether the above-mentioned purchasing process is appropriate, and if so, update purchasing procedures to reflect the process and remind appropriate staff of the revised requirements.

MANAGEMENT RESPONSE

We concur. The Corporation will review and update, as appropriate, its purchasing policies and procedures. Processes will be updated to reflect any changes to policies and procedures. The Corporation will provide training and reminders to staff of the revised requirements.

Anticipated implementation date: April 30, 2019

7. AGREEMENTS

OBSERVATION

Corporation agreements with a third party and certain related parties were not always timely executed.

We reviewed 15 agreements, and we found that one agreement with a third party and three agreements with related parties were signed after the agreement effective date. These execution delays ranged from 48 to 346 days. We noted the same observation in the prior auxiliary organizations audit conducted in 2014.

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

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation, ensure that all agreements with third parties and related parties are timely executed.

MANAGEMENT RESPONSE

We concur. The Corporation will enhance its agreement renewal processes to ensure that agreements with third parties and related parties are timely executed.

Anticipated implementation date: April 30, 2019

GENERAL INFORMATION

BACKGROUND

Auxiliary organizations are separate business and legal entities that perform activities essential to the educational program of a 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 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 auxiliary organizations.
- Implement financial standards that will assure the fiscal viability of 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 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 (EO) 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 Polytechnic State University, San Luis Obispo (Cal Poly San Luis Obispo) has three separate auxiliary organizations, each of which provides a function that contributes to the educational mission of the university. The Corporation is a non-profit public benefit corporation established in 1940 and is the primary entity responsible for commercial operations of the campus. These operations include, among others, campus dining and catering, conference and event planning, the outsourced Cal Poly University Store, print and

copy services and a separate university graphics systems, sponsored programs, and housing for faculty and staff.

In cooperation with the appropriate campus administrative offices, the Corporation provides fiscal services to instructionally related programs, conferences, workshops, and institutes as requested by the university. In addition, the Corporation provides accounting and business administration services for the other campus auxiliary organizations, the California Polytechnic State University Foundation and the Associated Students, Incorporated of California Polytechnic State University at San Luis Obispo. The Corporation is governed by a board of directors composed of representatives from the faculty, staff, community, and student body.

SCOPE

We visited the Cal Poly San Luis Obispo campus and the Corporation from August 13, 2018, through September 21, 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 Corporation. The audit focused on procedures in effect from January 1, 2016, to September 21, 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, conflicts of interest, 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, personnel and payroll, and a limited review of investments and long-term debt.
- Gifts administration, including, but not limited to, fund-raising events, pledges receivables, cash and non-cash gifts, matching gifts, and endowments.
- Auxiliary enterprise unit administration, including, but not limited to, campus dining and catering, conference and event planning, the outsourced Cal Poly University Store, print and copy services and university graphics systems, housing for faculty and staff, agricultural units, and campus program accounts.

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.

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
- EO 1059, *Utilization of Campus Auxiliary Organizations*
- ICSUAM §1301.00, *Hospitality, Payment or Reimbursement of Expenses*
- ICSUAM §8000.00, *Information Security*
- ICSUAM §15000, *University Advancement*
- ICSUAM §13680.00, *Placement and Control of Receipts for Campus Activities and Programs*
- Coded memorandum Human Resources 2017-17, *Background Check Policy*
- CSU *Auxiliary Organizations Compliance Guide*
- CSU *Auxiliary Organizations Sound Business Practices Guidelines*
- *Corporation Cash Receipts*
- *Corporation Management Guidelines for Implementation of the Corporation Purchasing Policy*
- *Corporation Policy for Payment or Reimbursement of Hospitality Expenses*
- *Corporation Purchasing Policy*
- *Cal Poly San Luis Obispo Alcohol Service Request*

AUDIT TEAM

Audit Manager: Joanna McDonald
Senior Auditor: May Flores