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July 12, 2019

Dr. Eduardo M. Ochoa, President
California State University, Monterey Bay
100 Campus Center, Administration Building
Seaside, CA 92955-8001

Dear Dr. Ochoa:

**Subject: Audit Report 19-33, University Corporation at Monterey Bay,
California State University, Monterey Bay**

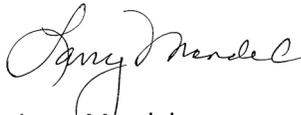
We have completed an audit of *University Corporation at Monterey Bay* as part of our 2019 Audit Plan, and the final report is attached for your reference. The audit was conducted in accordance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal 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

**UNIVERSITY CORPORATION
AT MONTEREY BAY**

California State University, Monterey Bay

Audit Report 19-33
June 6, 2019

EXECUTIVE SUMMARY

OBJECTIVE

The objectives of the audit were to confirm compliance with regulatory requirements for the establishment and governance of auxiliary organizations; ascertain the effectiveness of operational, administrative, and financial controls for the activities conducted by the University Corporation at Monterey Bay (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 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 Corporation as of April 25, 2019, taken as a whole, provided reasonable assurance that risks were being managed and objectives were met. However, we found that improvement was needed in the administration of conference and event services at California State University, Monterey Bay (CSUMB) @ Salinas City Center (SCC), and in other Corporation areas such as property and equipment, purchasing, procurement cards, commission receipts, accounts receivable collection and write-offs, and campus program accounts. We also found repeat observations from the prior audit of the Corporation regarding segregation of duties at the Camp SEA Lab and commission receipts. In addition, we found that the current service agreement between the campus and the Corporation did not include all required provisions.

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

OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

1. CONFERENCES AND EVENTS

OBSERVATION

Administration of conference and event services at CSUMB @ SCC needed improvement.

We found that a fee schedule for conference and event services was only recently established, in May 2018, and in many instances, clients were given various discounts without written justifications since 2016, the inception of CSUMB @ SCC. For example, in fiscal year 2018, clients were given discounts totaling \$303,093, and the discount percentages ranged from 10 to 100 percent. The *CSUMB @ SCC Event Procedures* allows for one type of discount: 20 percent, for non-profit organizations.

In addition, we reviewed ten conferences and events held at CSUMB @ SCC from January 2017 to December 2018, and we found that:

- For two events, facility rental applications were not submitted by the clients.
- For one event, a facility rental contract was not executed.
- For ten events, deposits were not made before the events, and the remaining balances were not collected 14 days before the event, as required by the *CSUMB @ SCC Event Procedures*.
- For nine events, contracts did not include appropriate indemnification provisions.
- For one event, a non-profit organization was given the 20 percent discount but did not provide the required documents, such as a W-9, non-profit exemption letter, or sales tax exemption letter from the state of California.

Proper administration of conference and event services provides greater assurance of financial stability and customer service, and compliance with current policies and procedures helps to reduce risk related to loss, theft, or misappropriation of funds.

RECOMMENDATION

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

- a. Evaluate the discounts given to clients since 2016 and update the *CSUMB @ SCC Event Procedures* accordingly, and require documented justifications for any exceptions to the discounts outlined the procedures.
- b. Provide training and guidance to key personnel involved with conferences and events on requirements to obtain facility rental applications and contracts, deposits and payments before the events, and required documentation and documented justifications for discounts.

- c. Update the contract template to include appropriate indemnification provisions.

MANAGEMENT RESPONSE

We concur with items a, b, and c in the above recommendation. The campus, in conjunction with the Corporation, will evaluate the discounts given to clients since 2016 and update the *CSUMB @ SCC Event Procedures* accordingly and require documented justifications for any exceptions to the discounts outlined in the procedures; provide training and guidance to key personnel involved with conferences and events on requirements to obtain facility rental applications and contracts, deposits, and payments before the events, and required documentation and documented justifications for discounts; and update the contract template to include appropriate indemnification provisions.

Expected completion date: August 30, 2019

2. PROPERTY AND EQUIPMENT

OBSERVATION

Administration of Corporation property and equipment needed improvement.

We found that physical inventory counts were not documented and reviewed by the management. Also, although non-capitalized sensitive equipment was tagged and tracked in the asset management system, the Corporation did not have policies and procedures for periodic physical inventories of non-capitalized sensitive equipment, and physical inventory counts were not performed.

Additionally, we reviewed ten capitalized and ten non-capitalized sensitive equipment acquisitions, and we found that:

- For four non-capitalized sensitive equipment acquisitions, the Corporation did not obtain approval from information technology (IT) before making the purchase.
- There was no process in place to ensure that non-capitalized sensitive equipment was accurately recorded in the asset management system. We noted that one non-capitalized sensitive equipment acquisition was recorded in the asset management system with a value that represented the invoice total, including service charges not related to the purchase, resulting in an overstatement of the asset's value.

We also reviewed ten capitalized and ten non-capitalized sensitive equipment deletions, and we found that:

- For five capitalized equipment deletions, the Request for Property Survey form was not signed by the authorized signers.
- For ten non-capitalized sensitive equipment deletions, the Request for Property Survey form was not signed by the authorized signers.

- For two lost equipment items, Equipment Loss Report forms were not completed.

Proper administration of property and equipment decreases the risk that property and equipment may be lost, stolen, or misrepresented in the financial statements.

RECOMMENDATION

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

- a. Develop and implement a process to ensure that physical inventory counts are documented and reviewed by management.
- b. Develop written policies and procedures for periodic physical inventory of non-capitalized sensitive equipment, and perform physical inventory counts accordingly.
- c. Develop and implement a process to ensure that non-capitalized sensitive equipment is accurately recorded to the asset management system.
- d. Provide training and guidance to key personnel regarding obtaining IT approval before purchasing non-capitalized sensitive equipment, obtaining approval from authorized signers on property survey forms, and completing equipment loss report forms for any lost equipment.

MANAGEMENT RESPONSE

We concur with items a, b, c and d in the above recommendation. The campus, in conjunction with the Corporation, will develop and implement a process to ensure that physical inventory counts are documented and reviewed by management; develop written policies and procedures for periodic physical inventory of non-capitalized sensitive equipment and perform physical inventory counts accordingly; develop and implement a process to ensure that non-capitalized sensitive equipment is accurately recorded to the asset management system; and provide training and guidance to key personnel regarding obtaining IT approval before purchasing non-capitalized sensitive equipment, obtaining approval from authorized signers on property survey forms, and completing equipment loss report forms for any lost equipment.

Expected completion date: December 16, 2019

3. PURCHASING

OBSERVATION

The Corporation did not always obtain a minimum of three formal bids for purchases that exceeded \$50,000, and exceptions to the bidding process were not always documented with proper approval.

The Corporation *Procurement Guidelines and Procedures* requires at least three formal bids for purchases of \$50,000 or more, unless there is a written justification by the authorized

signer and approval by the executive director. We reviewed nine purchases above \$50,000, and we found that:

- In two instances, two formal bids were obtained, rather than three, and there was no written justification with approval from the executive director.
- In one instance, written justification for the sole source was obtained 149 days after the service agreement was executed.
- In one instance, written justification for the sole source was signed by the associate executive director instead of the executive director.

Competitive bids provide transparency, mitigate favoritism toward certain vendors, and increase the chance of obtaining the best process.

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation, provide training and guidance to key personnel involved with purchasing on current requirements regarding obtaining formal bids, documenting written justification for exceptions such as sole source purchases, and obtaining proper approvals.

MANAGEMENT RESPONSE

We concur with the recommendation above. The campus, in conjunction with the Corporation, will provide training and guidance to key personnel involved with purchasing on current requirements regarding obtaining formal bids, documenting written justification for exceptions such as sole source purchases, and obtaining proper approvals.

Expected completion date: August 30, 2019

4. SEGREGATION OF DUTIES

OBSERVATION

Camp SEA Lab duties and responsibilities related to cash receipts were not adequately segregated.

We found that one employee opened the mail, received and reconciled payments, maintained custody of the payments, and prepared and made deposits. There were no mitigating controls in place, such as secondary reviews or verifications. This is a repeat observation from the prior Auxiliary Organizations audit.

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 Corporation, adequately segregate duties and responsibilities related to cash receipts or institute mitigating procedures.

MANAGEMENT RESPONSE

We concur with the recommendation above. The campus, in conjunction with the Corporation, will adequately segregate duties and responsibilities related to cash receipts or institute mitigating procedures.

Expected completion date: August 30, 2019

5. PROCUREMENT CARDS

OBSERVATION

Administration of Corporation procurement cards needed improvement.

We reviewed five cardholders' procurement card applications and all ten reconciliations for November and December 2018, and we found that:

- For one cardholder, a procurement card application and travel needs statement were not on file; a Corporation Procurement Card Alteration Request form to update the approving official had not been submitted; hospitality expenses for business lunches were not supported by documented business purposes; and payments to official guests were not supported by an agenda, invitation, or a similar document.
- For one cardholder, a temporary monthly increase from \$5,000 to \$20,000 had been issued, but the card had not been reset to its normal limit after two weeks, as required by the Corporation *Procurement Card Manual*, and had remained at \$20,000 since October 2017.
- Three reconciliations were submitted from 14 to 47 days after the due date.

Adequate administration of procurement cards decreases the risk that errors, irregularities, misunderstandings, and misappropriation of funds will occur.

RECOMMENDATION

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

- a. Obtain the procurement card application and travel needs statement, update the approving official for the cardholder noted above, and provide training and guidance to the cardholder on requirements for hospitality-related expenditures.
- b. Develop and implement a process to ensure that temporary increases are reversed after two weeks.

- c. Remind cardholders to timely prepare and submit procurement card reconciliations.

MANAGEMENT RESPONSE

We concur with items a, b and c in the above recommendation. The campus, in conjunction with the Corporation, will obtain the procurement card application and travel needs statement, update the approving official for the cardholder noted above, and provide training and guidance to the cardholder on requirements for hospitality-related expenditures; develop and implement a process to ensure that temporary increases are reversed after two weeks; and remind cardholders to timely prepare and submit procurement card reconciliations.

Expected completion date: August 30, 2019

6. COMMISSION RECEIPTS

OBSERVATION

The Corporation did not have written policies and procedures to periodically audit third-party sales commissions to ensure that commission receipts were in accordance with contractual requirements, and there was no documented review of commission receipts.

Specifically, we reviewed 11 commission receipts from outsourced operations, and we found that:

- For one vendor, the vending agreement had not been updated to include the current commission rate, and as a result, commission receipts were not calculated based on the commission rate stated in the vending agreement dated October 20, 2008.
- For another vendor, commission receipts were not calculated based on the commission rate stated in the agreement dated June 1, 2018.

This is a repeat observation from the prior Auxiliary Organizations audit.

Proper administration of third-party sales commission receipts provides greater assurance that receipts will be accurately calculated and collected.

RECOMMENDATION

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

- a. Develop and implement policies and procedures to periodically audit third-party sales commission receipts to ensure that commission receipts are in accordance with contractual requirements, including documenting review of commission receipts, and communicate the new policies and procedures to key personnel.
- b. Update the vendor agreement to reflect the current commission rate.
- c. Verify the commission rate for the vendor noted above.

MANAGEMENT RESPONSE

We concur with items a, b and c in the above recommendation. The campus, in conjunction with the Corporation, will develop and implement policies and procedures to periodically audit third-party sales commission receipts to ensure that commission receipts are in accordance with contractual requirements, including documenting review of commission receipts, and communicate the new policies and procedures to key personnel; update the vendor agreement to reflect the current commission rate; and verify the commission rate for the vendor noted above.

Expected completion date: October 30, 2019

7. ACCOUNTS RECEIVABLE AND WRITE-OFFS

OBSERVATION

Administration of collection and write-off of accounts receivable at the Corporation and KAZU needed improvement.

We reviewed five long-outstanding KAZU accounts receivable and two KAZU write-offs, and we found that the KAZU written policies and procedures for underwriting receivables and write-offs did not address time frame and documentation requirements for follow-up activity for outstanding accounts receivable and write-offs.

Additionally, we reviewed five long-outstanding Corporation accounts receivable and three Corporation write-offs, and we found that for one long-outstanding account receivable and two write-offs, documented sequential collections efforts were not made as required by the Corporation *Accounts Receivable Procedures*.

Adequate control and properly defined policies and procedures for accounts receivable improve the likelihood of collection and positively impact cash flow.

RECOMMENDATION

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

- a. Update the current KAZU underwriting receivables and write-off policies and procedures to include a time frame and documentation requirement for follow-up activity for outstanding accounts receivable and write-offs.
- b. Provide training and guidance to key personnel involved in the accounts receivable process to ensure that sequential collection efforts are made and documented in accordance with established policies and procedures.

MANAGEMENT RESPONSE

We concur with items a and b in the above recommendation. The campus, in conjunction with the Corporation, will update the current KAZU underwriting receivables and write-off

policies and procedures to include a time frame and documentation requirement for follow-up activity for outstanding accounts receivable and write-offs and provide training and guidance to key personnel involved in the accounts receivable process to ensure that sequential collection efforts are made and documented in accordance with established policies and procedures.

Expected completion date: September 30, 2019

8. CAMPUS PROGRAM ACCOUNTS

OBSERVATION

The campus had not developed written policies and procedures for campus program accounts.

We found that the campus had not developed written policies and procedures to provide specific guidance and documentation requirements for campus program accounts, including procedures to address cash receipts and deposits, purchases and disbursements, non-active or discontinued accounts, and deficit accounts.

Complete and comprehensive policies and procedures for campus program accounts provide a standard reference for campus programs and enhance compliance with systemwide requirements.

RECOMMENDATION

We recommend that the campus develop written policies and procedures that include the specific requirements outlined above and communicate these requirements to key personnel.

MANAGEMENT RESPONSE

We concur with the recommendation above. The campus will develop written policies and procedures that include the specific requirements outlined above and communicate these requirements to key personnel.

Expected completion date: December 16, 2019

9. CAMPUS SERVICE AGREEMENT

OBSERVATION

The current service agreement between the campus and the Corporation did not include all provisions required by systemwide policy.

Specifically, the service agreement between the campus and the Corporation did not include the following provisions:

- Indication of full reimbursement to the campus for services performed by state employee(s).
- The specific services to be provided by state employee(s).
- The specific performance measures used by the Corporation to measure or evaluate the level of service.
- Acknowledgment that the Corporation does not retain the right to hire, supervise, or otherwise determine how to fulfill the obligations of the campus to provide the specific services.

Proper administration of service agreements and inclusion of required terms and provisions helps to ensure compliance with systemwide requirements and reduces the risk of misunderstanding of responsibilities and liabilities.

RECOMMENDATION

We recommend that the campus, in conjunction with the Corporation, update its current service agreement to include all required provisions as noted above.

MANAGEMENT RESPONSE

We concur with the above recommendation. The campus, in conjunction with the Corporation, will update its current service agreement to include all required provisions as noted above.

Expected completion date: September 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.

CSUMB contracts with three separate auxiliary organizations, each of which provides a function that contributes to the educational mission of the university. The Corporation was established in 1994 as a non-profit public benefit corporation and in coordination with campus administrative offices, provides fiscal and administrative support services for post-award administration of sponsored programs, student housing, and conference and event services. The Corporation is responsible for commercial operations and outsources the management and operations of the bookstore, campus dining, east campus student and

employee housing, child development center, real estate sales and purchases, capital and operating lease, and the KAZU radio station. The Corporation also provides accounting and administrative support services to the Foundation of CSUMB and Otter Student Union at CSUMB under an administrative services agreement. The Corporation is governed by a board of directors composed of a representative from the community and the student body, CSUMB administration, and faculty.

SCOPE

We visited the CSUMB campus and the Corporation from March 18, 2019, through April 26, 2019. 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, 2017, to April 26, 2019.

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, budget, 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, purchasing, disbursements, personnel and payroll, and campus program accounts.
- Outsourced commercial operations, such as the bookstore, vending, dining, and property management services.
- Auxiliary enterprise unit administration, including, but not limited to, conference and event services, the KAZU radio station, student and employee housing, real estate sales and purchases, capital and operating leases, and facility rentals.

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.

We did not review the sponsored programs area as it was reviewed and reported separately.

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
- Education Code §89905
- 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*
- *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*
- *CSUMB Property Department Policy and Procedures*
- *Corporation Accounts Receivable Procedures*
- *Corporation Capital Asset Procedures*
- *Corporation Hospitality Expense Guidelines and Procedures*
- *Corporation Procurement Card Manual*
- *Corporation Procurement Guidelines and Procedures*
- *Corporation Procurement Policy*
- *Corporation CSUMB @ Salinas City Center Event Procedures*
- *KAZU Underwriting Billing and Recording Procedure*
- *KAZU Procedure to Write Off Membership and Underwriting Past Due Receivables*

AUDIT TEAM

Audit Manager: Caroline Lee
Internal Auditor: Leslie Rodriguez