California State Auditor

BUREAU OF STATE AUDITS

Investigative Report:

The California State University at Fullerton Mismanaged Trust Accounts, Contracts, and Donated Funds

December 1999

I970051

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CALIFORNIA STATE AUDITOR

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December 14, 1999

Investigative Report I970051

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

Pursuant to the Reporting of Improper Governmental Activities Act, the Bureau of State Audits presents its investigative report concerning California State University, Fullerton. This report concludes that the campus mismanaged trust accounts, engaged in improper contracting and questionable hiring practices, improperly created and transferred funds to a nonprofit organization, used some donated funds inappropriately, and violated its fiduciary trust over other donated funds.

Respectfully submitted,

KURT R. SJOBERG
State Auditor

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SUMMARY

Audit Highlights . . .

A manager engaged in numerous improper and questionable activities, including the following:

- ☑ ***Deposited more than $800,000 into trust accounts and used the funds for unauthorized purposes.***
- ☑ ***Repeatedly circumvented controls over contracting and hiring.***

Other employees also engaged in improper and imprudent activities, including the following:

- ☑ ***Created an unauthorized auxiliary and transferred million of dollars in donations to it.***
- ☑ ***Spent $100,000 in donations on entertainment, flowers, gifts, and other questionable items for themselves and other campus employees.***
- ☑ ***Violated their fiduciary duties over endowment funds.***

RESULTS IN BRIEF

We received allegations under the Reporting of Improper Governmental Activities Act (act) that the California State University at Fullerton (campus) illegally established an all-purpose trust account, used funds in that account to pay for many types of expenditures, and diverted surplus funds to the account.[1] Also, the allegations stated that an official in the campus's Business and Financial Affairs division (business division) improperly spent her division's fee revenues and also improperly engaged in contracting and hiring. Finally, the allegations stated that the campus improperly created an auxiliary organization to which it transferred donated funds along with the power to invest and manage them.

We investigated and substantiated these allegations and also uncovered additional improper activities. Although many of the problems we identified may not seem significant in isolation, collectively they demonstrate serious mismanagement at the campus. Based on the evidence we reviewed, we concluded the following:

- The campus acted without statutory authority when its business division improperly established an all-purpose state trust account, known as the University Trust Project account, and deposited more than $683,000 into it from July 1994 through August 1998.

- During the same period, the business division improperly used more than $628,000 from this all-purpose account to pay for campus expenditures not authorized by state laws and, in January 1995, illegally diverted more than $219,000 of its unspent utilities funds to the account. The unspent utilities funds should have been returned to the State's General Fund.

- The business division improperly directed to an account it controls $15,000 in reimbursements that should have gone to the State. In addition, the business division official named in

[1] For a more detailed description of the laws and regulations discussed in this report, see Appendix A.

the allegations improperly used funds from this account to pay for consulting services supplied by acquaintances and former business division employees.

- The business division apparently charged other campus departments too much for administrative services and improperly used $197,000 in surplus fees to pay for costs unrelated to providing administrative services. According to the state law cited by the campus as its authority to make such charges, the funds should only be used to pay for the costs of providing those services.

- The business division official named in the allegations circumvented official contracting policies and procedures when she authorized more than $158,000 worth of work through contracts and service orders, at times without any contractual documents, with her acquaintances and former business division employees.

- The same business division official engaged in questionable personnel practices when she reassigned two of her staff to management positions instead of recruiting for the best candidates, hired an employee who did not meet the minimum qualifications required for the job, placed a contractor in a management personnel plan position on an emergency basis and subsequently hired her as a manager at a higher level than the previous position, and hired another consultant as a management employee on a temporary basis without recruiting for the post.

- Campus officials participated in the creation of an auxiliary organization known as the University Advancement Foundation (UAF) and transferred to this organization the investment and management of millions of dollars donated to the campus.

- From July 1994 to June 1998, campus officials inappropriately authorized payments of about $104,000 from nonstate accounts maintained at the California State University, Fullerton, Foundation (campus foundation) and the UAF for food, entertainment, flowers, gifts, and other questionable expenditures for themselves and other campus employees.

- The campus violated its fiduciary duty over funds designated for President's Scholars by transferring the funds to other accounts and commingling them with funds that can be used for other purposes.

- The campus led donors to believe that it had raised more than $1 million for scholarships at its Front and Center fundraising events in 1995, 1996, and 1997 when, in fact, it set aside only $556,000 for that purpose.

AGENCY COMMENTS

Because campus employees told the campus president about some of the improprieties before we began our investigation, and because he participated in the creation of the UAF, we submitted our report to the chancellor of California State University (CSU). The chancellor responded that CSU's review of our report and their further investigation did not find any serious mismanagement at the campus. He concluded, "there were errors of judgment and mistakes in some instances." Nevertheless, he reported that, with the full support of the campus, he has initiated an evaluation of the campus's fiscal management to ensure that appropriate internal control systems are in place. ■

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INTRODUCTION

BACKGROUND

The Bureau of State Audits administers the Reporting of Improper Governmental Activities Act (act), which is contained in Section 8547 et seq. of the California Government Code. The act defines an improper governmental activity as any activity by a state agency or employee during official duties that violates any state or federal law or regulation; is economically wasteful; or involves gross misconduct, incompetence, or inefficiency.

Whistleblower Hotline
(800) 952-5665

To enable state employees and the public to report improper governmental activities, the state auditor maintains a toll-free whistleblower hotline at (800) 952-5665. The Bureau of State Audits receives and investigates these complaints.

ALLEGATIONS

We received the following allegations:

- The California State University at Fullerton (campus) illegally established an all-purpose trust account and used funds in that account to pay for many expenditures not allowed by state law.
- The campus also illegally diverted surplus funds to this all-purpose trust account and used them to benefit the campus. These funds should have reverted to the State.
- An official in the campus's Business and Financial Affairs division (business division) improperly used revenues generated from services her division provides to other campus departments.
- The same official also engaged in improper contracting and hiring.
- The campus improperly created an auxiliary organization and transferred the investment and management of funds donated to the campus to this organization.

BACKGROUND

In December 1996 and January 1997, several campus employees met with the campus president to express their concerns regarding management of the business division. Some of the considerations expressed during those meetings are similar to some of the allegations we received, including improper contracting and hiring. The president told us that not long after meeting with the employees, he met with the business division official several times over a few months to discuss and address the employees' considerations. The president stated that because the official assured him she had addressed those concerns, and because he did not hear any further employee complaints, he thought the business division had dealt with the concerns. To document the interview, we gave the president a written summary of his statements and asked him to make any necessary changes. We also requested that he sign the statement under penalty of perjury to ensure its accuracy, but he refused. Although we report our understanding of what he told us, we have less confidence in the accuracy of our understanding because of the president's unwillingness both to confirm the statements and to certify them under penalty of perjury. Even though the president refused to sign a statement regarding the actions he took as a result of the employees' complaints, he did provide us with a summary of the complaints.

SCOPE AND METHOD OF INVESTIGATION

To investigate the allegations, we reviewed the state accounts controlled by various campus officials and their staff. We also evaluated the California State University, Fullerton, Foundation (campus foundation) accounts controlled by these officials and their staff. The campus foundation is a nonprofit auxiliary that supports the campus's educational programs and provides financial management services for discretionary accounts and self-supporting programs. This foundation was established in accordance with state requirements. Further, we reviewed the University Advancement Foundation (UAF) accounts controlled by the same officials and their staff. Created by the campus president and a group of individuals to support the campus's educational programs, the UAF is a nonprofit organization created without the approval of the California State University Chancellor's Office (CSU chancellor). As one of its functions, the UAF provides financial management services for campus gifts and donated funds.

To determine their propriety, we assessed contracts and service orders requested by the business division official named in the allegations. In addition, we examined personnel records related to management employees this official hired to ascertain the propriety of the appointments. Finally, we interviewed the campus president, the president of the UAF's board of directors, and other campus employees.

After we sent our draft report to the CSU chancellor, CSU reviewed our workpapers and collected more information from the campus. We met several times with CSU representatives and reviewed additional documents provided by them.

Table 1 describes the various state and nonstate accounts referred to in this report.

TABLE 1

Accounts Discussed in This Report

Account	Type of Account	Intended Purpose	Responsible Party
University Trust Project	State Trust	All	Business Division Official
Business Division UAF	Nonstate*	All	Business Division Official
Alumni Relations	Nonstate*	Alumni programs	University Advancement Office
Costs	State Trust	To pay for the costs of providing accounting and administrative services	Business Division
Fees	State Trust	To pay for the costs of providing budget and payroll services	Business Division Official

* We define an account as nonstate when the account is located outside of a state entity and when expenditures from the account do not go through the normal state claim review process.

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CHAPTER 1

The Campus Has Violated State Laws by Mismanaging Various Accounts

CHAPTER SUMMARY

The California State University at Fullerton (campus) has disregarded state laws and budgetary provisions in its management of state-appropriated funds. Specifically, the campus illegally established an all-purpose trust account, made illegal deposits of over $683,000 to it, and improperly used more than $628,000 of its funds. Also, the campus failed to comply with state laws when it diverted surplus funds that should have been returned to the State, and improperly directed reimbursements for state expenses to a nonstate account. In addition, the campus's Business and Financial Affairs division (business division) used fees charged to other campus departments for its administrative services for purposes not allowed by law.

State law makes each California State University (CSU) president responsible for the proper spending and accurate financial reporting of all funds received by the campus, including state funds, gifts, bequests, trust funds, grants, and loans. Also, campus officials such as the president and the chief fiscal officer have a responsibility to collect and spend money in accordance with state law and policies of the California State University Board of Trustees (CSU trustees), and for the best interest of the campus.

THE CAMPUS HAS DISREGARDED STATE LAWS AND BUDGETARY PROVISIONS IN ITS MANAGEMENT OF STATE-APPROPRIATED FUNDS

Through its business division, the campus illegally established an all-purpose trust account, called the University Trust Project account, to receive revenues from any source and pay campus expenditures of any kind, and used its funds to pay for many campus expenditures not allowed by state laws. The campus also improperly diverted surplus utilities funds to this account rather than returning them to the State. In addition, the business division failed to comply with state law when it directed a reimbursement for state expenses to a nonstate account it controls, the business division's University Advancement Foundation (UAF) account.

The Campus Improperly Established an All-Purpose Trust Account and Used It for Purposes Not Authorized by Law

The campus deposited over $683,000 to the improperly established account.

The campus acted outside of its statutory authority to establish trust accounts at state colleges when its business division set up the University Trust Project account, an all-purpose trust account, to collect revenues and pay for expenses related to any and all campus activities.[2] From July 1994 through August 1998, the campus improperly deposited more than $683,000 into this account, including transfers of $219,000 in unspent utilities funds and $86,000 from another trust account, and a deposit of $82,000 in private grant funds. During the same period, the business division used more than $628,000 of the all-purpose trust account's money to pay for a variety of expenditures, including corporate membership fees in a private club; travel to Washington, D.C. by the campus's baseball team; and rent for the campus's university advancement office. These expenses were not improper in themselves because they could have been paid out of other accounts if properly authorized. However, these payments were improper because the campus lacked authority to establish the all-purpose trust account in the first place and, in many instances, the transferred funds were not authorized for those purposes.

By transferring money from general fund accounts, whose spending is generally subject to time limits, into the all-purpose trust account, whose funds are not subject to time limits, the business division retained funds for its future use and circumvented state laws on using appropriated funds within a time limit. In addition, the business division deprived several campus departments of money for their programs by transferring funds from those departments' general fund accounts or depositing funds due the departments into this trust account. In spending the University Trust Project's revenues for a variety of purposes, the business division also bypassed budgetary controls for the use of those funds.

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[2] State law specifies the purposes for which state trust accounts can be created. All-purpose trust accounts are not among those permitted. For details about which trust accounts are authorized at state colleges and the laws and regulations discussed in this report, see Appendix A.

As of March 1997, the business division official named in the allegations was the sole signatory authorized to disburse funds from this all-purpose trust account. (We could not determine when the business division established this account.) The document renewing the University Trust Project account indicates that its purpose is to pay for various types of university activities and that revenues for the account are to come from administrative charges and from collections for university activities.

The University Trust Project account had a balance of more than $641,000 at the end of fiscal year 1993-94, but we could not determine all sources of those funds. From July 1994 through August 1998, the business division deposited more than $683,000 into the account. Table 2 gives the dates, amounts, and sources, if known, of this revenue.

TABLE 2

Revenues Deposited Into the University Trust Project Account From July 1994 Through August 1998

Date	Amount	Source
January 1995	$219,705	Unspent utilities funds
February 1995	60,000	Utilities rebate
April 1995	100,000	Unknown
June 1995	80,622	Unknown
July 1997	15,000	Utilities rebate
March 1997	25,781	Private grant
September 1997	28,125	Private grant
December 1997	28,125	Private grant
August 1998	86,185	Costs account
Various	39,476	Various
Total	**$683,019**	

In 1997 the business division deposited more than $82,000 in private grant funds into the all-purpose trust account. According to the business division, when it received the grant money in 1997, it could not determine where the funds should go. Eventually, in 1998, the business division determined the appropriate accounting for these funds and deposited additional money received for the same grant into a different account in order to reimburse expenses associated with the grant. However, it failed to reclassify to this new account the earlier $82,000 deposit into the University Trust Project account.

In 1998, the business division transferred to the all-purpose trust account more than $86,000 from another state trust account, referred to here as the "costs account," partly to fund the construction of two new computer classrooms and a self-help area in the campus library. Although the funds were used to fund a campus construction project, it was improper for the business division to use this account because it can only be used to meet the business division's costs for providing accounting and administrative services to other campus departments.

Other improper deposits into the all-purpose trust account include the improper transfer in 1995 of more than $219,000 in unspent utilities funds, a transaction we discuss fully in the next section. The business division was unable to explain the source of other sizable deposits it made in April and June of 1995.

The law does not authorize the creation of trust accounts to pay for a variety of expenses, yet the business division used more than $628,000 from the all-purpose trust account to cover all kinds of university expenses. For example, in addition to the construction projects mentioned above, from July 1994 to August 1998, the campus used $5,000 from this account to pay for a nontransferable corporate membership in a private club; $20,700 for the baseball team to travel to Washington, D.C.; $63,000 for rent for the campus's university advancement office; and $278,000 to pay off loans for its stadium and baseball scoreboards. As of August 1998, the all-purpose trust account had a balance of more than $452,000. In September 1998, the business division committed the account to fund construction of two new computer classrooms and a self-help area in the campus library as part of the campus's library seismic upgrade project.

Although the business division spent this money for justifiable purposes, it circumvented required budgetary controls and processes. If the business division determines the need to procure services or equipment to benefit the campus, it should request funds through the appropriate channels instead of using revenue belonging to other accounts.

The Campus Illegally Diverted and Retained Surplus Funds That It Should Have Returned to the State

As noted above, the campus illegally diverted more than $219,000 of its unspent utilities funds to the University Trust Project account. These funds should have reverted to the State's General Fund. By transferring the surplus funds into the all-purpose trust account, the campus not only failed to return the funds to the State as required by law, but also improperly generated additional funds for campus use. It appears that the campus controller's office knew it was improper to transfer such money, because it quickly corrected a later improper transfer of $192,000 in unused utilities funds.

The campus did not return more than $219,000 in unused utilities funds to the State's General Fund.

Every year CSU receives its funding allocation from the State's General Fund. According to the Department of Finance, a state agency must commit its appropriated funds for expenditure within one year and pay for the commitment within two years, or those funds revert to the State. Nevertheless, through the State's annual budget act, the Legislature generally appropriates CSU's general support funds from the previous year to allow the university two additional years to commit the appropriated funds. This, in effect, allows CSU a total of three years to commit the funds it receives for general support of CSU before they revert to the State.

In May 1994, the campus controller's office identified more than $219,000 it had overcommitted for utilities for fiscal year 1992-93. That surplus should have been committed during fiscal year 1994-95 or returned to the State by the end of that fiscal year. However, on January 31, 1995, the campus controller's office transferred the $219,000 into the University Trust Project account in violation of state laws.

The Business Division Improperly Directed a Reimbursement for State Expenses to a Nonstate Account

In another misuse of state funds, the business division improperly directed a reimbursement of $15,000 for its postage expenses to a nonstate account, its UAF account, for its own benefit. The business division official named in the allegations then improperly used funds from this nonstate account to pay for consulting services supplied by acquaintances and former business division employees and for a holiday party for her staff.

On December 1, 1996, the campus's alumni relations office requested that the UAF transfer $15,000 from a nonstate alumni relations account to the business division's UAF account for reimbursement of state postage expenses, although the business division UAF account is not a state account. The alumni relations official who requested the transfer said she needed to pay the campus for postage expenses; however, if the campus mailroom charged her office for postage, she would have to set up a state account on campus and pay an 8 percent administrative fee to the business division. According to this official, the business division's budget office suggested a swap—she would transfer the $15,000 into the business division UAF account in exchange for a waiver of the 8 percent fee.

The business official deposited $15,000 into a discretionary account she controlled rather than return it to the State's General Fund.

According to the business division official, the transfer was not to cover the alumni relations office's postage and miscellaneous expenses, but to provide the business division with a source of nonstate funds to be used for discretionary purposes. However, we conclude that the transfer of $15,000 was for state postage expenses and thus the transfer was contrary to the state law requiring that reimbursement for state services be credited to the appropriate state account.

The business division official and her secretary are the two authorized signatories for the business division UAF account, which was established in October 1996. According to the document establishing this account, its funding source was to be private gifts and sponsorships and its purpose to be unrestricted. However, the only source of revenue for this account was the $15,000 transfer from the alumni relations office and a reimbursement of an overpayment to a contractor. As we discuss in the following section, the business official used funds from this account for improper payments for consulting services. In December 1997, the official also authorized payment of more than $800 from this account to pay for a holiday party at a local restaurant for her staff. As of February 1999, the account had a balance of more than $5,800.

THE BUSINESS DIVISION USED EXCESS FEES FOR PURPOSES NOT ALLOWED BY LAW

The business division official named in the allegations and her staff used at least $197,000 in excess fees charged to campus departments to pay for costs unrelated to providing services, although state law requires this division to use those fees only to meet the cost of providing administrative support to campus departments.[3] Since the costs charged to campus departments for business division services should equal the fees collected for them, no excess fees should exist. The business division's over-charges reduce the money campus departments have for their educational programs. Also, the business division official violated state laws governing her division's fees and circumvented budgetary controls.

The business division established two trust accounts to receive fees it charged other departments for accounting, administrative, payroll, and budgeting services. These two accounts—the "costs account" and the "fees account"—divide the fees among the three major offices of the business division: the budget, payroll, and controller's offices.

The business division deposits trust management fees into the costs account. Through agreements with some departments, the business division assesses an administrative fee on the monthly gross receipts of those departments' trust accounts. For departments with no fee agreements, the business division retains as compensation the entire interest earned on those departments' trust accounts. In addition, the business division has agreements with the campus's extended education, housing services, and parking divisions for reimbursements of administrative support services from the budget and controller's offices, which share in the revenues. The business division deposits the share for the controller's office into the costs account and the share for the budget office into the fees account.

From July 1995 to August 1998, the business division deposited into the costs account about $1.4 million in fees for administrative support services and about $666,000 into the fees account for payroll and budgeting services to campus departments. However, instead of using all revenues in these two accounts to meet the valid expenses of providing services to other campus departments, the business division official and her staff improperly used around $197,000 for purposes unrelated to those

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[3] The campus cited this state law as its authority for charging the fees and depositing them in a state trust account.

services. For example, from July 1995 to June 1997, the official used around $9,000 from the fees account to pay for business travel for her and her staff. As described more fully later, she also used more than $102,000 from this same account to pay for computer consulting services from her acquaintances and former business division employees. We could find no evidence that these expenditures were related to providing the services for which the division charged other units. As of August 31, 1998, the fees account had a balance of more than $78,000.

In addition, from July 1995 to August 1998, the business division official and her staff improperly transferred more than $86,000 from the costs account to another state trust account, the University Trust Project account, to cover a contract change order related to the campus's library seismic upgrade project. Moreover, as of August 31, the balance of over $263,000 in the costs account appears to be more than the total amount the business division should have charged other campus departments. However, the business division does not have a cost accounting system that would allow it to determine how much it costs to provide services to other departments.

The business division official repeatedly circumvented restrictions and budgetary controls for the use of state funds.

In addition to depriving campus departments of money, the business division is manipulating campus budget procedures to control how these service revenues can be used. If the business division determines a need for services or equipment to benefit itself or the campus, it should request these funds through the appropriate budgetary process instead of using the service fees. ■

CHAPTER 2

The Campus's Business Division Engaged in Improper Contracting and Questionable Hiring

CHAPTER SUMMARY

The business division official named in the allegations contracted improperly with an acquaintance and former colleagues, violating California State University (CSU) policies on competitive bidding for contracts and on using service orders. Further, she engaged in questionable hiring practices that prevented competition for open positions and abused the standard hiring process at California State University, Fullerton (campus). As a result, this official acted unfairly, misused state funds, and violated the public trust.

A BUSINESS DIVISION OFFICIAL CONTRACTED IMPROPERLY WITH ACQUAINTANCES AND FORMER COLLEAGUES

The business division official named in the allegations circumvented official CSU policies and procedures on contracting. In 1996 and 1997, she improperly paid acquaintances and former business division employees more than $158,000 for consulting services to her division. She skirted formal CSU contracting policies in several ways: (1) she hired these contractors without competitive bids; (2) she authorized payments to them without written agreements for the work and, in one instance, no invoices; (3) she authorized payments when charges were beyond the maximum contract amount, were inappropriate, and were not in compliance with contractual terms; and (4) she authorized duplicate payments to two contractors.

BACKGROUND

State law gives the CSU Board of Trustees (trustees) the authority to enter into contracts for services and exempts these contracts from the supervision and approval of the Department of General Services.[4] The trustees in turn delegate to each campus the authority to execute and administer certain contracts, including consulting services contracts, in conformity with legal requirements and CSU policy.

CSU's policy required competitive bidding for most contracts.

State law requires state agencies to secure at least three competitive bids or proposals for each contract, except where a contract is necessary for the immediate preservation of public health, welfare, or safety, or for protection of state property. Although CSU is exempt from this law, its written policy supports the objectives of state procurement laws and it has adopted competitive bidding requirements for most contracts. The contracts discussed here were not excepted from these requirements.[5] CSU intends to ensure full compliance with the intent of competitive bidding laws designed to protect the public from the misuse of state funds in paying more than might be necessary for labor contracts. CSU also intends to eliminate favoritism, fraud, and corruption in the awarding of state contracts, thus providing all qualified bidders a fair opportunity to enter the bidding.

In addition, official CSU policy in effect before April 1997 stated that except in emergencies, work on any contract could not begin until the contract had been approved by the appropriate authority. Any work done before that approval is considered as having been performed at the contractor's own risk and as a volunteer. Service orders could be used instead of a contract when timing or circumstances made a contract impractical; for example, in such cases as film rentals, memberships, newspaper advertisements, and some equipment repairs. However, service orders could not be used to circumvent competitive bidding

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[4] For a more detailed description of the laws and regulations discussed in this chapter, see Appendix A.

[5] CSU's internal auditor told us that although the official, written policy in effect before April 1997 was as we have described, CSU was informally allowing more freedom in the use of service orders, as reflected in the policy issued in April 1997. For example, the April 1997 policy did not require competition for services costing less than $50,000. In addition, this newer policy allowed the use of service orders to obtain various kinds of services on a less formal basis. Nevertheless, the April 1997 policy still stated that "transactions made under the CSU procurement authority shall be designed to encourage active competition among vendors wishing to become providers of services."

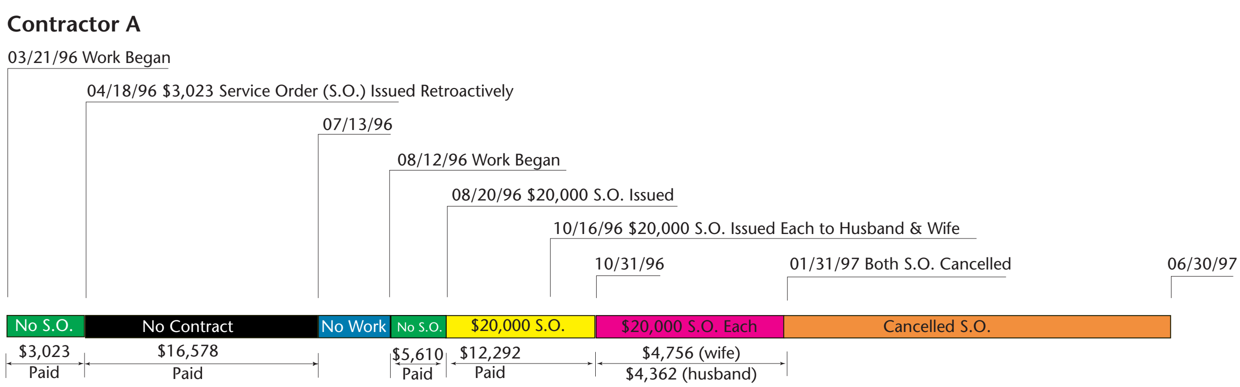
requirements, and so required written justifications when a sole source was to provide the work. Regardless of the services obtained, no service order could exceed $20,000. In addition, the service order could not be used for consulting services, or services of personnel who should be hired through normal recruiting or through temporary appointment procedures.

Contractor A

In April 1996, the business division official named in the allegations hired contractor A to do consulting without seeking competitive bidding for the work. From March 1996 through January 1997, the official authorized payments of $46,623 to contractor A and its owners. Contractor A, however, never had a formal contract, but provided services under a series of service orders the official approved. In fact, the business official at times approved payments to contractor A for work done before a service order was issued, approved a duplicate payment, and once even paid contractor A without having invoices to support the payment. Figure 1 shows contractor A's dates of work, service orders, and payments.

FIGURE 1

The Business Division's Transactions With Contractor A and Its Owners March 1996 Through June 1997



Contractor A is an Internet consulting company owned by an acquaintance of the official and the acquaintance's husband. In April 1996, the business division official requested the campus purchasing office, which was under her supervision, to prepare a service order for contractor A to provide Internet consulting services that the company had already performed in March and April without any type of contract, a violation of official CSU policies. On April 18, the same day of the official's request, the campus purchasing office issued the requested service order. The official's division then issued state checks totaling $3,023 to contractor A from the fees account, controlled by the official.

From April through mid-July, contractor A continued to provide Internet consulting services to the official's division without a contract or service order. For that period, the official approved, and her staff paid, contractor A's invoices totaling more than $10,400. These invoices included $100 for five campus parking tickets that the acquaintance received. Also, the official's staff paid contractor A another $6,100 on July 19 at the official's request, even though the campus had not received any invoices to support the payment. Although her staff repeatedly requested invoices to support the issued check, the official had not produced them as late as October 25, 1996. We do not know when the official provided contractor A's invoices to her staff, but the business division produced copies of the invoices for this payment in April 1999.

Contractor A repeatedly worked without any contract in effect.

On July 30, 1996, the official approved her own request, submitted to the campus purchasing office, to prepare a service order for contractor A to provide the campus with Internet and intranet development services for August through October, beginning August 12. But the service order was not issued until August 20, and once again, the contractor began working with no written agreement in place. The campus paid contractor A's invoices out of the fees account controlled by the official; however, those invoices indicated that $5,610 of the work was done before the service order was issued.

On October 16, 1996, the official requested two separate contracts for additional consulting services to be provided by contractor A's owners individually. On the same day, the campus purchasing office issued two service orders for Internet consulting services for the maximum amount of $20,000 each from October 15, 1996, to June 30, 1997; but one had already begun working on September 30 without any written agreement and completed part of the consulting on October 11, according to his invoice. Yet, the campus paid him $965 on November 5, 1996, from the state account of a unit under the official's supervision.

The official authorized a duplicate payment of $647 to contractor A.

After allegations regarding the business division's improprieties arose in December 1996 and January 1997, the official requested the purchasing office to cancel the remainder of the service orders awarded to contractor A's owners. On January 31, 1997, the purchasing office canceled the service order for the official's acquaintance and all but $965 of the service order for the acquaintance's husband. Prior to the cancellation, however, the campus paid the spouse another $3,400 and paid the official's acquaintance more than $4,700. These payments included a duplicate payment of $647. The official's acquaintance submitted two invoices for the same services, which the official approved and the University Advancement Foundation (UAF) paid. The official authorized these payments to her acquaintance and her acquaintance's spouse with funds from the business division's UAF account under her control.

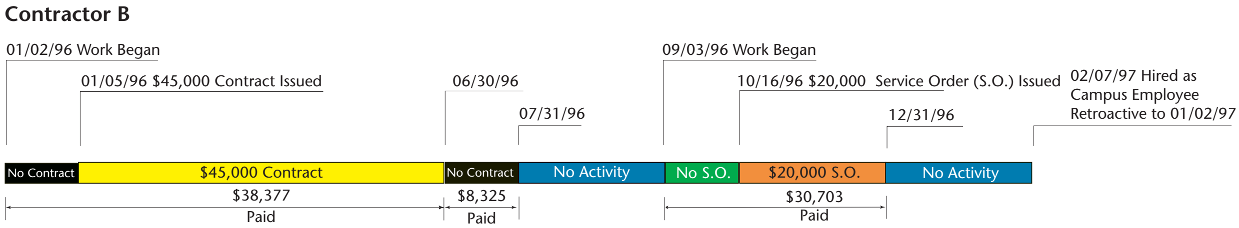
As stated earlier, CSU's internal auditor told us that CSU was informally allowing more flexibility to campuses in procuring services and the use of service orders, as reflected in the formal policy issued in April 1997. For example, the newer policy did not require competition for services costing less than $50,000. In addition, this newer policy allowed the use of service orders to obtain various kinds of services on a more informal basis. For example, the newer policy allowed campuses to use service orders when timing or circumstances made it impractical to employ a formal agreement. However, because the business division official consistently requested service orders in the amount of $20,000, we believe that she was not exercising informal latitude. Instead, it appears that she consistently circumvented the formal requirements in effect at the time.

Contractors B and C

In 1996, the business division official improperly contracted with contractor B, who gained the job without having to compete for it. The official approved payments for work done with no written agreement, payments that were $10,000 over the maximum amount allowed by CSU written policy, and a duplicate payment. The business division official authorized total payments to contractor B of $72,680 and later hired her for a management personnel plan (management) position in the business division. Figure 2 shows contractor B's dates of work, contracts, service orders, and payments. A more detailed description of the transactions with contractor B can be found in Appendix B.

FIGURE 2

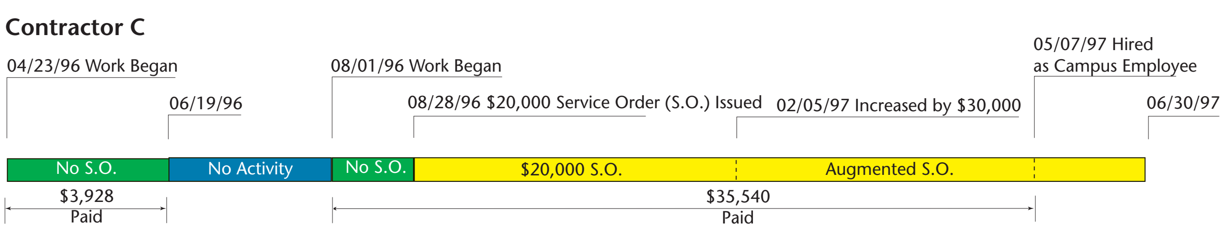
The Business Division's Transactions With Contractor B
January 1996 Through March 1997



In 1996, the business division official also hired contractor C without seeking other candidates for the work; in the next two years, the official paid contractor C a total of $39,468 with funds from the fees account, which she controls. Twice, contractor C began work before the campus issued service orders. Also, when invoices exceeded the $20,000 maximum on a 1996 service order, the official violated CSU written policy by increasing the total service order amount by $30,000. Figure 3 shows contractor C's dates of work, service orders, and payments. A more detailed description of the transactions with contractor C appears in Appendix B.

FIGURE 3

The Business Division's Transactions With Contractor C
April 1996 Through June 1997



THE BUSINESS DIVISION OFFICIAL ENGAGED IN QUESTIONABLE HIRING PRACTICES

The business division official named in the allegations did not follow the campus's standard practices when hiring management employees. She failed to recruit for the most qualified candidate when hiring several management employees. In addition, she also used the temporary hiring process as a back door for employees to move into long-term temporary jobs or into permanent positions. While these actions did not violate laws or regulations, they further illustrate the manager's willingness to disregard or manipulate established management practices. Moreover, by her questionable hiring practices, the official denied other persons who were eligible for the positions the opportunity to compete for them.

Inappropriate Reassignments Prevented Competition for Positions

The business division official circumvented campus policies by promoting two individuals without providing others the opportunity to compete for the positions. By reassigning employees A and B to higher-level positions under the context of a reorganization, the official did not have to recruit for the positions and was able to skirt campus policies. As a result, the official did not allow other qualified candidates to apply for these jobs.

Employees A and B did not have to compete for their management positions.

In April 1997, the business division official decided to reorganize her division. As part of the reorganization, on October 24, 1997, the campus president reassigned two of the official's employees. Both reassignments were to be retroactive to June 1, 1997.

CSU's management personnel plan, contained in state regulations, governs the employment rights, benefits, and conditions of CSU management employees, such as the ones discussed here. The regulations allow the appointing power to assign a management employee to different duties in the same position or to reassign the employee to a different position. However, the campus has a policy that when a management position of director or higher is to be filled, a search committee should be established to consider all qualified applicants, except when the president and the executive committee of the Academic Senate decide a search committee is not needed.

When the business official was considering the reorganization, the campus human resources office advised her that she could reassign employees A and B if the campus president approved an exception to the job posting requirements specified in the campus's affirmative action plan. Although the campus president signed the letters authorizing the reassignments, we found no evidence that he specifically approved exceptions to the posting requirements. Moreover, the former chair of the executive committee of the Academic Senate stated that the campus's policy on establishing a search committee would apply to the positions to which employees A and B were reassigned.

Further, the official's original hiring of employee A in 1988 for an administrative position in her division was improper because employee A lacked the required qualifications. The job announcement for this administrative position stated that graduation from a four-year university and the equivalent to two years of progressively responsible professional experience were required.[6] However, at the time she applied, employee A did not have a four-year degree and fell short of the required education and experience qualifications.[7] Despite this, the official hired employee A over other candidates who met the announced qualifications.

The Official Used Temporary Hiring to Inappropriately Advance Some Employees

The business division official also placed employees in management positions by unfairly manipulating the temporary appointment process. She hired several employees in temporary positions or as consultants, either hiring someone not fully qualified or hiring without considering other candidates. She then extended the temporary position instead of recruiting for a permanent employee or used the consultant's experience as a main qualification for a permanent position.

The official hired employee C, who lacked sufficient qualifications, over qualified candidates.

The business division official hired employee C to a temporary administrative position in management information systems, even though the employee did not meet the advertised

[6] Although the position announcement specified these minimum qualifications, the CSU classification and qualification standards for this classification did not require graduation from a four-year university.

[7] Employee A now has both bachelor of arts and master of arts degrees in political science.

minimum qualifications of a bachelor's degree or equivalent and two years journey-level experience performing analytical studies of management information systems.

When reviewing the applications, the business division determined that seven individuals, not including employee C, met the criteria for the position. Employee C did not have a bachelor's degree but stated in her application that she had four years of experience in systems analysis and several years of accounting experience, including specific experience at CSU. Her application also indicated that her college education had primarily focused on chemistry, English composition, and accounting, and did not indicate that she had taken any classes in management information systems. It is doubtful that employee C met the minimum qualifications for the position even considering her four years' experience in systems analysis.

One of the individuals hired by the official through a temporary appointment was also among the contractors to whom the official gave work through improper contracting arrangements.

Despite her shortcomings, the campus scheduled employee C for an interview, along with four other candidates who met the minimum qualifications. The official determined that two of the four were strong candidates for the position. Nevertheless, in May 1996, the official hired employee C.

About five months after she hired employee C, the official requested that employee C be appointed to an acting management position for November 1, 1996, to June 30, 1997. As a result, employee C's salary increased 43 percent from $3,784 to $5,416 per month. On three subsequent occasions, the official requested that employee C's acting appointment be extended. As of February 1999, according to the human resources office, the business division had not begun recruiting to fill the position permanently.

The official also hired two other management employees by abusing the contracting and temporary appointment processes. Without seeking other applications, she hired employee D, who earlier worked for the official as contractor C, to provide process mapping and business reengineering services to the official's division. On the same day employee D billed her final services as a contractor, the campus offered employee D a management position for a four-month period. Three extensions of this position let employee D work as a full-time manager through December 31, 1998.

In October 1998, after recruiting for other candidates, the official hired employee D for a higher-level position. One of the main reasons cited for employee D's selection over other qualified candidates was her experience working at the business division as a contractor and a manager. Thus, the official's manipulation of the temporary hiring system allowed employee D to obtain a permanent position as a director in the business division.

This same employee gained a permanent management position because of her experience in a temporary job she did not have to compete for.

The business division official also used contracts and the temporary appointment process to hire employee E as a manager without recruiting for her position. In March 1998, the official contracted with employee E as a special consultant from March to June 1998 to assist in the reengineering, design, and implementation of systems and procedures for various tasks in a unit of the division. On June 24, the official requested the campus's human resources office to offer employee E a temporary, full-time manager position for one year. The employee accepted this position on June 30. ■

CHAPTER 3

The Campus Should Not Have Transferred Donated Funds to a Nonprofit Organization That Officials Improperly Established

CHAPTER SUMMARY

California State University at Fullerton (campus) officials violated state laws and regulations when they improperly participated in the creation of, and transferred funds to, an auxiliary organization not approved by the California State University Chancellor (CSU chancellor).[8] Beginning in June 1994, the campus improperly transferred scholarship, endowment, and restricted gift funds from its officially recognized auxiliary—the campus foundation—to a newly created auxiliary organization, the University Advancement Foundation (UAF). When the campus created the UAF, it ignored legal requirements to seek the CSU chancellor's approval and to secure a written agreement between the chancellor and the UAF about how the organization would function. The composition of the UAF's board of directors also did not comply with legal requirements.

The Campus Improperly Created and Transferred Funds to the UAF

In June 1993, the campus president and a group of community business leaders signed papers to incorporate a nonprofit organization known as the UAF. The UAF's articles of incorporation state that it was organized to further the educational purposes and objectives of the campus. The campus president and the community business leaders composed the UAF's board of directors (board), and one of the community business leaders serves as board president.

[8] For a more detailed description of the laws and regulations concerning the creation of university auxiliaries, see Appendix A.

In establishing the UAF, the campus president did not seek the CSU chancellor's approval, as required by state regulations. Also, the UAF did not have the required written agreement with the CSU chancellor. Further, the composition of the UAF's board, with no campus staff, faculty, or students, violated state regulations.

In May or June 1994, the campus vice president for university advancement and the campus foundation's executive director signed a memorandum to transfer to the UAF more than $2 million in scholarship, endowment, and restricted gift funds administered by the California State University, Fullerton, Foundation (campus foundation). Further, the memorandum stated that the UAF would play a vital role in both raising and administering all gifts and donations to the campus. Because the memorandum transferred all responsibilities of administering and investing money raised by the campus to the UAF, the campus foundation relinquished all its responsibilities pertaining to gift funds. On June 15, 1994, the campus foundation's board of directors approved the transfer of these funds to the UAF. As of June 1998, the UAF was administering more than $7.7 million. However, the campus had improperly transferred its gift funds and the responsibilities for administering them.

The campus transferred all gift funds to the UAF, an improperly created auxiliary organization.

In September 1998, after we brought these issues to the attention of the board's president, the board amended its articles of incorporation to state that it shall be an auxiliary organization of CSU and conduct its operations in conformity with state laws and regulations governing auxiliary organizations. Further, it followed state regulations in amending its articles of incorporation to include the approval of the trustees for distribution of its remaining assets to one or more nonprofit organizations upon the UAF's dissolution.

In addition, the board brought its composition in line with state regulations. Specifically, the board amended its bylaws to state that the campus president, or his designee, will be a voting director and that the campus president will appoint a faculty member and a student member to the board. The board will then select the remaining directors.

As of March 1999, the UAF was finalizing an operating agreement with the trustees to enable it to administer gifts, bequests, devises, endowments, trusts, and similar funds. ■

CHAPTER 4

Campus Officials Inappropriately Authorized Payments for Food, Entertainment, and Other Questionable Costs

CHAPTER SUMMARY

California State University at Fullerton (campus) officials inappropriately authorized funds from accounts under their control—campus foundation and University Advancement Foundation (UAF) accounts—to pay for various non-educational expenses they and their staff incurred. From July 1994 through June 1998, these officials authorized payment of at least $104,000 for food, entertainment, flowers, and other questionable expenses for themselves and other campus employees. Specifically, they authorized around $29,800 for food and meals they and their staff had with other campus employees, $43,760 for employee entertainment and parties, $5,400 for flowers to staff, $8,600 for gifts to other campus employees, and $16,400 for additional unjustified expenses. These uses of state funds do not appear to support the educational mission of the campus; instead, they seem to be for personal benefit.

BACKGROUND

The source for most of the campus foundation and UAF money that the officials inappropriately spent was private donations to the campus. The campus trustee may accept on behalf of the State any gift, bequest, devise, or donation of real or personal property whenever the gift and terms and conditions of the gift will aid in carrying out the primary functions of the California State University (CSU). The primary mission of CSU is undergraduate and graduate instruction through the master's degree.

State regulations require that auxiliary organization accounts be used for purposes consistent with CSU trustee and campus policies. Because the campus is a public trust, it has a responsibility to prudently spend its funds to achieve the campus's goals and auxiliary organizations classified as foundations must expend discretionary funds in a manner consistent with the educational mission of the CSU. Further, state law requires the campus president to ensure all auxiliary organization expenditures are proper and in accordance with the trustees' policies.

The CSU policy on business-related meals states that for an employee to claim reimbursement, the circumstances surrounding the meal must be beyond the employee's control and completion of the business during normal work hours must be impractical. CSU policy further states that its intent is to allow reimbursement in the few instances where conducting official university business requires employees to pay for meals.

Imprudent and Excessive Payments for Food

From July 1994 through June 1998, various campus officials and their staff imprudently authorized or claimed reimbursements from campus foundation and UAF accounts of about $29,800 for breakfasts, lunches, dinners, and refreshments that they or their staff had with other campus employees. These expenses included meals at outside restaurants and refreshments during staff meetings.

The president's and university advancement offices used donated funds to pay for at least 134 meals for themselves and other campus employees.

The president's office and the university advancement office incurred most of these food expenses. For example, UAF and campus foundation accounts paid for at least 134 meals attended only by an employee of the president's office and other campus employees. At one of these meals, on July 31, 1997, a manager of governmental relations from the president's office met with the president over lunch in Brea, three miles away from the campus, to discuss governmental relations. And, on August 4, 1997, the manager of governmental relations discussed alumni events over lunch at a restaurant in Placentia, only two miles away, with one official from university advancement for alumni relations and another official from alumni programs and services.

On a number of occasions, the campus president also took his staff to lunch. For example, on August 26, 1997, the president took his staff to lunch at a nearby restaurant. Two months later, he again took his staff to lunch in Brea, and on December 10, 1997, he took them to a restaurant in Tustin. These three lunches totaled about $515.

In addition, one university advancement official and his staff often met with each other or with other staff members over lunch to discuss university advancement issues. For example, on February 4, 1997, two officials from corporate relations had lunch in Fullerton for a department meeting. A week later, they had lunch in Brea for another department meeting. Besides meeting together over lunch, these two officials also had lunch with other staff from the university advancement office. For example, on March 25, the two officials had lunch in Brea, four miles from the campus, with an alumni relations official. Besides these two individuals, other university advancement office staff also took each other out to lunch to discuss business. On at least 50 occasions in fiscal year 1997-98 alone, university advancement staff took each other out to eat and were reimbursed from UAF accounts.

Other campus officials also met with other campus staff over breakfasts and dinners, although less frequently than the university advancement and the president's office, For example, on August 20, 1997, the student health center spent $700 on a dinner in Fullerton for 16 of its staff and contractors to discuss the health center's plans and goals for the coming school year.

We could not understand why campus officials and their staff so frequently had to conduct university business over meals paid for with donated funds.

INAPPROPRIATE PAYMENTS FOR ENTERTAINMENT AND PARTIES

From July 1994 through June 1998, campus officials inappropriately spent about $43,760 on entertainment expenses for staff members and their spouses or guests. Officials from the president's office, the vice president for administration's office, the university advancement office, the student health center, and the business and financial affairs division authorized or claimed payments for these expenses from campus foundation and UAF accounts. Entertaining campus employees with money from these auxiliary organization accounts does not advance the school's educational goals or fulfill a purpose consistent with CSU trustees' policies, as required by state regulations. We believe the campus would derive greater benefit from hosting academically related meetings or entertaining official guests or potential donors than from entertaining employees.

The student health center paid $2,500 to rent a yacht at Newport Beach for a staff Christmas party.

These expenses included holiday, farewell, birthday, and thank-you parties, as well as an annual staff appreciation event for campus employees. For example, on December 13, 1996, the student health center held a Christmas party for its staff and their spouses. It rented a yacht at Newport Beach for more than $2,500 and spent more than $1,600 on food and beverages for the party. According to the acting administrator for the student health center, the center only collected funds to pay for some spouses and other guests of its staff to attend the party.

Campus officials also held retirement and farewell parties for their employees. For example, in January 1997, the president's office held a retirement dinner for the vice president for student affairs and paid more than $1,200 for the dinner catered by the campus foundation's dining services, and for entertainment. In August 1996, the vice president for administration's office spent more than $1,100 on a retirement luncheon for one of its employees, again catered by the campus foundation's dining services. In March 1997, the university advancement office spent more than $100 on a going-away luncheon at a local restaurant for one of its employees.

The president's office and other campus officials also held birthday parties for their employees. For example, in July 1995, the president's office spent more than $120 to cater a birthday party for a campus employee's 50th birthday. Further, in August 1996, the university advancement office spent more than $150 on two of its employees' birthdays.

Campus officials spent considerable money to recognize and appreciate their employees. From July 1994 through September 1997, the campus spent more than $11,400 on food, flowers, entertainment, gifts, and supplies for an annual staff appreciation day to recognize campus employees. We agree it is important for an organization to recognize its employees for their contributions and that it costs the campus to purchase the awards and gifts for its employees. State law even provides that state agencies may award its employees upon completion of 25 years of state service or at retirement; however, it does not allow for gifts to employees in other situations.[9] Though this law does not apply to CSU employees, we believe it provides prudent guidance. We also believe the campus could have spent these funds more wisely to support the educational mission of the campus. For example, for the 1996 staff appreciation day, the

[9] The cost of each allowed award may not exceed $75.

campus spent at least $3,500 to hold the event, including more than $1,400 on food and entertainment and about $100 on breakfast and refreshments for the staff appreciation committee. After the 1997 staff appreciation day, the campus even spent around $239 on a "debriefing luncheon" for the staff appreciation committee. Presumably the campus "appreciated" twice the employees who served on the committee.

Further, in July and October 1995 and in January 1996, a university advancement executive hosted three thank-you parties for his staff at a total cost of more than $400. Also, in September 1996, the university advancement office spent more than $4,400 on an overnight river rafting retreat down the Kern River for 25 of its staff. According to the university advancement executive, the river-rafting trip was a team-building opportunity to bring his unit into a more collegial and productive mode.

INAPPROPRIATE PAYMENTS FOR FLOWERS

From July 1994 through June 1998, campus officials authorized or claimed payments for around $5,400 in flowers they sent to other campus employees on special occasions. Specifically, officials from the president's office, the vice president for administration's office, the university advancement office, and the student health center authorized or claimed payments for these expenses from campus foundation or UAF accounts. While flowers were often sent in the name of a particular office or multiple employees of a campus office, sometimes the flowers were sent in the name of an individual. In no case did we see an inscription indicating the flowers were sent from university donors or from the California taxpayers. These exchanges of flowers between individual employees of the campus do not further the educational mission of the school and thus appear to be another inappropriate use of donated funds for personal benefit rather than the educational mission of the CSU.

Campus officials claimed payments for flowers they sent to other campus employees.

These expenses included flowers campus officials sent to various campus employees on special occasions, such as illnesses of employees or their relatives, and employee birthdays. For example, on September 12, 1997, the university advancement office spent more than $90 from a UAF account to send get-well flowers to two university advancement employees. On January 17, 1997, the president's office spent around $120 from a campus foundation account to send birthday flowers to an employee of the president's office and to the director of alumni programs and services. The president's office staff also purchased balloons for the president's birthday in May 1996 and sent flowers to the president for "Bosses Day" in October 1995 with funds from a campus foundation account.

Questionable Payments for Gifts

From July 1994 through June 1998, campus officials imprudently authorized or claimed payments of more than $8,600 in gifts to other campus employees from campus foundation or UAF accounts. These expenses included farewell, birthday, Christmas, and appreciation gifts given to campus employees by the officials. Again, we fail to see how these uses of donated funds support the educational mission of the campus. If government officials make personal gifts, they should do so at their own expense.

One campus executive spent $6,000 in donated funds to buy a laptop computer for another campus executive's retirement gift.

In January 1997, a campus executive purchased a $6,000 laptop computer using campus foundation funds as a farewell gift to a retiring student affairs executive. In addition, in October 1994, a campus executive used about $105 in campus foundation funds to purchase a gift of clothing for the newborn son of an employee at his campus residence. In December 1994, the same executive also used campus foundation funds to purchase $125 in gift certificates for two employees at his campus residence. Besides these gifts, officials from the president's office, vice president for administration's office, the university advancement office, and the student health center also gave farewell, birthday, Christmas, and appreciation gifts to other campus employees.

Other Questionable Payments

From July 1994 through June 1998, campus officials authorized payments for around $16,400 in other inappropriate or questionable expenses. Specifically, officials from the president's office, the vice president for administration's office, and the university advancement office authorized or claimed payments for these expenses from campus foundation or UAF accounts. These expenses included car washes for an official's personal car, late and finance charges on the officials' university credit cards, and tuition and registration fee payments for university advancement office employees.

One campus official regularly paid for washing his personal car with funds from his accounts at the campus foundation and UAF. For example, for fiscal year 1997-98, he spent about $150 to have his car washed 12 times and to have a lube and oil change once. He said that on some occasions he got his car washed after running errands for the university advancement office to make corporate calls, to attend development appointments, and to pick up donors and guests of the university.

Campus officials used donated funds for car washes, late payment fees on credit cards, and other perquisites for subordinate staff.

The campus also paid a substantial amount in late fees and finance charges on university credit cards held by campus officials. For fiscal years 1994-95 to 1997-98, the campus paid more than $2,600 in late fees and finance charges for credit cards held mainly by employees in the university advancement and president's offices.

In addition, the university advancement office reimbursed several of its employees for tuition and registration fees they paid for taking classes on campus. For fiscal years 1994-95 to 1997-98, one university advancement official authorized about $5,500 in tuition and registration fees for seven staff in his office to take classes on campus during the spring and fall semesters and summer sessions. This was over and above the fee waiver and reduction program for eligible CSU employees and thus inconsistent with CSU policy. ■

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CHAPTER 5

The Campus Violated Its Fiduciary Trust and Misled Donors

CHAPTER SUMMARY

The California State University at Fullerton (campus) violated its fiduciary trust over funds donated for its President's Scholars scholarships. In addition, it led donors to believe that it had raised $1.4 million for scholarships at its Front and Center events from 1995 through 1997. However, the amount reported was inflated because it included funds simply transferred from other accounts at the campus foundation and the University Advancement Foundation (UAF). In addition, of the amount the campus claimed it raised for scholarships, as of November 1998, it had set aside only $556,000 for that purpose. In addition, it has not yet used most of the $556,000 for its students' benefit. Although the campus claims that it has already committed the funds to President's Scholars, as of the last time we met with California State University (CSU) representatives, the campus had provided no evidence that it has reserved the funds for that purpose.

The campus is a public trust with a fiduciary responsibility to the public to spend its funds prudently and in the best interests of the campus. Further, state law requires the campus president to be responsible for the propriety of all expenditures and the integrity of the financial reporting of all funds the campus receives, including gifts. By not adhering to restrictions placed on the use of donated funds and by not distributing the scholarship money it raised, the campus has violated the public trust and sabotaged its own mission.

THE CAMPUS HAS VIOLATED ITS FIDUCIARY TRUST DUTIES FOR THE PRESIDENT'S SCHOLARS ENDOWMENT ACCOUNT

In June 1994, the UAF created the President's Scholars endowment account. Endowments are permanently invested and income from the investment is used for the purposes specified by the donor. For this particular endowment, the campus foundation and the President's Associates Scholarship Endowment Committee established these investment terms:

- The principal amount is completely restricted.
- The interest is used for scholarships.
- Interest earned in one fiscal year that is not used in the following fiscal year will revert to the endowment principal.

In July 1994, the campus transferred $99,532 to the new UAF account. Since then, over $370,000 has been deposited into this endowment account, including transfers from other campus accounts and donations from individuals. The UAF invests the various funds under its control. Because only the interest earned on endowments can be spent, each endowment account has a corresponding account to which the UAF pays the interest on the endowment principal. As of June 30, 1999, the UAF has paid $59,596 in interest to the President's Scholars endowment interest account.

Even though the funds could only be used for scholarships, the campus transferred $43,500 to other accounts used for other purposes.

Although not all of the funds deposited to the account came from sources that required the same terms, some donors did make endowments and specify that any interest earnings could be used only for scholarships given to President's Scholars. However, the UAF and the campus have not adhered to restrictions on endowments and have violated their fiduciary trust. Although interest income from the President's Scholars endowment account may only be used for scholarships, interest income of about $43,500 has been transferred to a number of other accounts and commingled with funds used for other purposes. This is about 73 percent of all the interest paid to the account by the UAF. For example, on November 1, 1996, a campus employee requested UAF to transfer $3,000 from the endowment interest account to another restricted account. She specified that the campus president would use the funds "for costs related to President's Scholars and special projects."

Although the campus has paid for numerous scholarships out of this restricted account, it can and has spent funds from the account for other purposes as well, including more than $16,000 for campus dining and catering charges and $12,750 for cash awards to employees. In addition to violating the terms of the endowment, the campus violated its fiduciary duty and state law when it commingled restricted funds with funds used for purposes other than those specified by the trust agreement. From documents provided by the campus, it is also unclear whether the employee who requested the transfer was authorized to make expenditures from the interest account.

In April 1997, the same campus employee directed UAF to transfer $4,400 from the interest income of the President's Scholars endowment account to the President's Associates campaign account, which is an unrestricted account. Funds in that account can and have been used for purposes other than scholarships. In June 1997 another individual transferred $3,486 from the interest income account to this campaign account. We could not determine from campus documents whether this individual was authorized to spend the endowment's interest. And, although the campus provided documents indicating that these two transfers were made to the unrestricted account, accounting records do not verify that the funds were ever deposited there.

In June and July 1998, an employee in the campus's annual giving office requested UAF to transfer $17,788 and $4,523 respectively, of interest income from the President's Scholars endowment account to the annual fund account, another unrestricted account. In April 1999, another campus employee requested that about $10,300 of interest income be transferred to the same unrestricted account. The campus claims that ultimately it transferred all these funds to the restricted account and used them for scholarships. However, it had no convincing explanations for the transfers and, because the funds were commingled with funds used for other purposes, it had no evidence of the use of the funds. The campus also had no credible explanation for why it transferred the money instead of simply writing the scholarship checks directly from the endowment interest account. Such transfers violate the terms of the endowment and the campus's fiduciary duty as established by state law.

THE CAMPUS HAS NOT ENSURED THAT THE UAF PAYS ITS ENDOWMENT FUNDS AN APPROPRIATE INTEREST RATE

To be sure a trust continues to fulfill its purpose, the campus has a fiduciary duty to make trust property productive. A trustee, such as the campus and the UAF, must act with the skill, prudence, and diligence of a prudent person when investing and otherwise managing university trust assets to accomplish the purposes of the university. As stated in Chapter 3, the campus transferred to the UAF responsibility for administering and investing the campus's endowment, scholarship, and other restricted funds in 1994. However, the campus did not ensure that the UAF paid appropriate interest rates to the President's Scholars endowment account. It appears that rather than paying endowment accounts the income they actually generate, the UAF periodically sets interest rates it will pay to the various accounts it administers. For example, in June 1996, the UAF decided to pay endowment accounts 3 percent interest. Later, in 1997, the UAF raised the interest rate it paid to endowments to 5 percent. From July 1994 through June 1999, the UAF paid this account $59,596 in interest. We do not know if the investment of these funds actually generated more revenue for the UAF. However, if the campus had merely invested the endowment funds in the state treasurer's pooled money investment account, the endowment would have earned $16,474 (27.6 percent) more. Because the campus allowed the UAF to pay low interest on its endowment accounts, less money was available to scholarship students. The campus also did not ensure that unused interest income reverted back to the principal in the endowment account. Because the UAF paid no interest on the endowment's income, the scholarship program lost additional interest.

The UAF paid endowment funds a low interest rate.

THE CAMPUS FALSELY ADVERTISED THAT IT HAD RAISED OVER $1 MILLION FOR SCHOLARSHIPS AT FRONT AND CENTER EVENTS

In January 1996, the campus held a unique benefit dinner known as Front and Center. The cost to the public for a floor table was $5,000, while one seat cost $500. According to its promotional and solicitation materials, the campus claimed that it raised more than $450,000 for scholarships during that event. The campus held two more benefit dinners in 1997 and 1998.

Besides charging admission to the event, the campus solicited public donations for scholarships. The campus reported that these three events grossed more than $1.4 million. However, because some of the events' operating income consisted of tickets or tables purchased by campus employees using campus foundation or UAF funds, the campus inflated the revenues actually earned. For example, in 1998, more than 11 percent of the events' gross receipts came not from outside donors, but from these employees. Thus, campus officials inflated the income from these events by using money from one account to buy tickets and depositing the receipts in another account.

For the 1996 Front and Center event, the office of the vice president for administration paid $1,000 out of its campus foundation account for two tickets. For the same event, the university advancement office spent $1,000 in UAF money on two seats and the president's office purchased five seats using $2,500 in UAF funds.

The campus inflated the amount of money it claimed it raised by simply moving money from other campus accounts to the Front and Center accounts.

Although we were not able to determine the total purchases by campus officials for the 1996 and the 1997 events, many other campus officials also used campus foundation and UAF funds to purchase seats. We do know that for the 1998 Front and Center event, campus officials used more than $56,400 from campus foundation or UAF accounts to purchase event tickets or floor table seats for themselves and their guests.

In addition, although the campus claimed that it had raised more than $1 million for scholarships from these events, it has failed to use any substantial percentage of this money on scholarships. As of November 1998, the campus had transferred only $556,000 to scholarship accounts and had used no more than $35,320 of Front and Center revenue for scholarships. Besides misleading its donors on the money's use, the campus is depriving deserving students of educational opportunities by retaining this fundraising money.

Table 3 shows the amounts the campus raised, allocated, and distributed for the three events.

TABLE 3

**Scholarship Allocations and Disbursements of Funds
Front and Center Events
1996 Through 1998**

Year	Amount Raised	Amount Allocated for Scholarships	Amount Disbursed for Scholarships
1996	$ 415,000	$151,000	$ 0
1997	498,000	215,000	13,708
1998	500,000	190,000	21,612
Total	**$1,413,000**	**$556,000**	**$35,320**

The campus categorized the money it grossed from the three Front and Center events as follows: $427,000 was operating income, which was receipts from ticket and table sales, and patrons' advertisements during the events; and more than $986,000 was donations from sponsors or ticket holders.[10]

By November 1998, the campus had deposited only 40 percent of the $1.4 million it claimed it grossed from these events, into scholarship and endowment accounts.[11] After the 1996 event, the campus transferred about $151,000 (36 percent) of the total gross revenues from the Front and Center account, in which it deposited the proceeds, to two accounts for scholarships. The campus also transferred $30,000 to a president's discretionary account and about $8,000 to a university advancement discretionary account. The campus claims that the $30,000 transferred to the president's discretionary account was repayment of seed money provided earlier. The campus also claims that the $8,000 transferred to the university advancement discretionary account was merely a loan that was subsequently repaid. However, the campus could not produce evidence that the president's discretionary account ever provided $30,000 in seed money, or that the university advancement discretionary account ever repaid the $8,000. The rest of the revenues were apparently used for event expenses.

In May, June, and October 1997, the campus transferred around $215,000 (43 percent) of the gross revenues from that year's event into four accounts for scholarships.[12] In August and October 1996, before the 1997 event, the campus transferred $30,000 to various discretionary accounts. Although the campus transferred the money before the actual event, it charged these transfers against the 1997 event. Again, the rest of the funds were apparently used for event expenses.

In June and October 1998, the campus transferred about 38 percent of gross receipts from the 1998 event to four scholarship accounts. The remaining money apparently was used to pay event expenses.

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[10] We believe that the figure for the operating income may be low because it appears that the campus may have misclassified the income received in 1996.

[11] In 1999, after we completed our fieldwork, the campus transferred another $30,000 to accounts for scholarships.

[12] Initially, the campus deposited $175,000 of this amount in a university advancement discretionary account. Later, in March 1998, the campus transferred the funds to the Front and Center scholarship account.

Even though the campus set aside $556,000 of the $1.4 million it raised for scholarships, as of the completion of our fieldwork, it had only disbursed $35,320.

Even though about $556,000 had been transferred to the Front and Center scholarship account and other scholarship endowment accounts since March 1996, the campus had disbursed from these accounts only about $35,320 in scholarships to students as of November 1998, when the Front and Center scholarship account had a balance of more than $417,000.[13]

According to the vice president for university advancement, the campus does not view Front and Center exclusively as a fundraising event. He stated that the primary purpose of the Front and Center event is to build the campus's image and to generate prospective donors within the regional and corporate community, with raising funds for scholarships being a secondary purpose. Contrary to this statement, the campus touted in its promotional and solicitation materials for the 1998 Front and Center event that it had raised more than $1 million for scholarships in 1996 and 1997.

The Campus Claims That It Has Committed Front and Center Funds for Scholarships

Although, by the end of November 1998, the campus had distributed only 6.4 percent of the funds it set aside from the Front and Center events in scholarship accounts, it estimates that it has about $409,000 in scholarship commitments through the President's Scholars program. The campus president makes commitments to certain incoming students to pay their tuition costs and a $500 book stipend for each of four years. Because the president has made commitments to students extending into 2002, and because other resources used in the past have dwindled over time, the campus claims that it will use Front and Center scholarship funds to meet these commitments.

The campus, however, provided no evidence that it has formally reserved its Front and Center scholarship funds for the President's Scholars. Moreover, as we reported earlier, the campus has already violated the terms of the endowment regarding donations made specifically for the President's Scholars program. Instead of using interest income from the President's Scholars endowment account to award scholarships, the campus has transferred most of the income to other accounts and commingled the funds with other funds that are

[13] In 1999, after we completed our fieldwork, the campus paid another $29,406 for book stipends out of the Front and Center scholarship account.

used for a variety of purposes. Moreover, the campus has failed to ensure that the endowment funds earn as much income as prudent. In view of the campus's failure to keep its formal commitments to the President's Scholars endowment fund, we are not confident that the campus will, in fact, use the Front and Center funds as it claims. Nevertheless, we agree that it is important to plan for how the campus will meet its scholarship commitments.

We conducted this investigation under the authority vested in the California State Auditor by Section 8547 of the California Government Code and in compliance with applicable investigative and auditing standards. We limited our review to those areas specified in the scope of the report.

Respectfully submitted,

KURT R. SJOBERG
State Auditor

Date:	December 14, 1999
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APPENDIX A

State Laws and Regulations

This appendix provides more detailed descriptions of state laws and regulations governing employee conduct and prohibiting the improper governmental activities detailed in this report.

RESPONSIBILITY FOR PROPRIETY OF EXPENDITURES

Section 89756 of the California Education Code states that the president of each California State University (CSU) campus is responsible for the propriety of the expenditure and the integrity of the financial reporting of funds received by the campus.

ESTABLISHMENT AND USE OF STATE TRUST ACCOUNTS

Section 89721 of the Education Code requires the chief fiscal officer of each CSU campus to deposit and maintain in trust accounts money received in connection with the following sources or purposes:

(a) Gifts, bequests, devises, and donations.

(b) Student loan or scholarship funds.

(c) Advance payments for anticipated expenditures or encumbrances in connection with federal grants or contracts.

(d) Room, board, and similar expenses of students enrolled in the CSU international program.

(e) Cafeteria replacement funds.

(f) Miscellaneous receipts in the nature of deposits subject to return upon approval of a proper application.

(g) Fees and charges to persons for services, materials, and facilities provided to the persons by the campus which fees and charges shall be used solely to meet the costs of providing the services, materials and facilities.

(h) Fees for instructionally related activities as defined by the trustees and authorized by Section 89700 and revenues derived from the conduct of such instructionally related activities.

(i) Fees for parking, health services, and other self-supporting instructional programs.

(j) Revenue from the state lottery.

(k) Money received by the trustees for research, workshops, conferences, institutes, and special projects.

None of the enumerated sources or purposes allows a campus to establish an all-purpose trust account.

LIMITS ON TIME APPROPRIATIONS ARE AVAILABLE FOR EXPENDITURE

Section 16304 of the California Government Code states that an appropriation shall be available for encumbrance, which is a commitment for expenditure, during the period specified therein, or, if not limited by law, for three years after the date upon which it first became available for encumbrance. The same section of the code further states that an appropriation shall be deemed to be encumbered at the time and to the extent that a valid obligation against the appropriation is created. Further, Section 16304.1 of the California Government Code states that payments fulfilling these obligations may be made before or during the two years following the last day an appropriation is available for encumbrance. Upon the expiration of the two years, following the last day of the period of its availability, the unused balance of any appropriation shall revert to, and become a part of the fund from which the appropriation was made.

REQUIREMENT THAT STATE FUNDS BE DEPOSITED IN THE STATE TREASURY

Section 16301 of the California Government Code requires that, among other things, all money belonging to the State received from any source whatever by any state agency be paid into the Treasury and credited to the State's General Fund, provided that amounts received as partial or full reimbursement for services furnished shall be credited to the applicable appropriation.

LIMITS ON ASSESSMENT AND USE OF ADMINISTRATIVE FEES

Section 89721(g) of the Education Code authorizes the chief fiscal officer of each CSU campus to deposit and maintain in trust accounts fees and charges for services, materials, and facilities it requires from persons who, at their option, use the services or facilities, or who are provided the materials, for which the fees or charges are made. This code section also requires that such fees and charges be used solely to meet the costs of providing such services.

CONTRACTING

Section 10340 of the Public Contract Code requires state agencies to secure at least three competitive bids or proposals for each contract. According to the law, three competitive bids or proposals are not required, among other things, in cases of emergency where a contract is necessary for the immediate preservation of the public health, welfare, or safety, or for protection of state property. Although CSU is exempt from this law, as a matter of policy CSU supports the objectives of state procurement laws and has adopted competitive bidding requirements for most contracts, regardless of monetary amount.

HIRING

Section 4(h) of Article VII of the State Constitution exempts all CSU officers and employees from the State's civil service system. However, Section 89030 of the California Education Code requires the CSU's board of trustees (trustees) to adopt rules and regulations that are consistent with state laws, including laws governing the appointees and employees of the trustees and the CSU.

Article 2.2, Title 5, of the California Code of Regulations, known as the management personnel plan, governs, among other things, the employment rights, benefits, and conditions of covered CSU management employees. Specifically, Section 42725, Title 5, of the California Code of Regulations allows the appointing power to assign a management personnel plan (management) employee to different duties in the same position or may reassign a management employee to a different position either within or outside of the grade level or management plan. However, the campus has a policy that when a management position of director or higher is to be filled, except where the president and the executive committee of the academic senate deem it not to be of faculty concern, a search committee should be established to consider all qualified applicants.

Moreover, the campus advocates an affirmative action policy that states that it is committed to ensure equal opportunities in its employment. The policy encourages all campus departments to make good faith efforts to vigorously recruit to increase the number of qualified women and minority applicants.

CREATION OF UNIVERSITY AUXILIARIES

Section 42407 of the California Code of Regulations, Title 5, states that no new CSU auxiliary organization shall be established unless a recommendation accompanied by a justification is submitted by the president of the campus and approval is given by the CSU chancellor. According to Section 89901 of the Education Code, the term "auxiliary organization" includes, among other things, any entity in which any official of the CSU participates as a director as part of his or her official position. In addition, Section 89903 of the same code requires each auxiliary organization formed to have a board of directors composed, both as to size and categories of membership, in accordance with regulations established by CSU trustees. Further, Section 42400 of Title 5 of the California Code of Regulations states that, among other things, an auxiliary organization is any organization using the name of the State or a campus, or representing an official relationship with a campus, or in which any campus official participates as a director as part of his or her official position.

Moreover, Section 42501 of the California Code of Regulations, Title 5, requires a written agreement on behalf of the State by the CSU chancellor and an auxiliary organization for the performance of its functions as allowed by law. Section 42602 of the California Code of Regulations, Title 5, also requires the governing board of an auxiliary organization to consist of voting membership from the following groups: administration and staff, faculty, noncampus personnel, and students.

In addition, Section 89720 of the Education Code states that the trustees may accept on behalf of the State any gift, bequest, devise, or donation of real or personal property when that gift and the terms of the gift will further the primary functions of the CSU, that is undergraduate and graduate instruction. Further, Section 89750 of the Education Code requires the trustees to control and expend all money received as donations pursuant to Section 89720. The trustees are required to prescribe the rules and regulations covering the collection, custody, and disposition of any money collected by any state college. Moreover, according to Section 89756 of the Education Code, the chief administrative officer is then responsible for the propriety of any expenditure of gift funds. Section 89904.6 of the Education Code requires the trustees to develop and implement guidelines to ensure that auxiliary organizations classified as foundations for sponsored programs, workshops, and institutes, expend discretionary funds in a manner consistent with the educational mission of the university.

Finally, Section 89900 of the Education Code requires that the auxiliary expenditures and operations are in accordance with the policies of the trustees. Section 42403 of Title 5 of the California Code of Regulations also requires that donations and gifts to auxiliary organizations be accepted and maintained in accordance with policies and regulations established by the trustees.

FIDUCIARY DUTIES OVER TRUST FUNDS

The California Probate Code requires that trust funds be administered with reasonable care, skill, and caution that a prudent person acting in a like capacity would exercise to accomplish the purposes of the trust as determined in the trust instrument. The acceptance of a gift with restrictions establishes a trust relationship between the trustor (donor) and the trustee (recipient). In addition, the California Probate Code applies restrictions to the use of donated funds, whether or not the donors restrict their donations. According to Section 16000 of the Probate Code, on acceptance of the trust, the trustee has a duty to administer the trust according to the trust instrument, and except to the extent the trust instrument provides otherwise, according to the laws governing trusts. This means that the trustee has a duty to carry out the terms of the trust according to the expressed intent of the trustor. Also, Section 16002 states that the trustee has a duty to administer the trust solely in the interest of the beneficiaries, and Section 16007 states that the trustee has a duty to make the trust property productive under the circumstances and in furtherance of the purposes of the trust. Further Section 16009 states that the trustee has a duty to keep trust property separate from other property not subject to the trust and to see that the trust property is designated as property of the trust. Furthermore, the trustee is bound to act in the highest good faith. Section 18506 of the Probate Code requires the campus, when delegating investment management for the benefit of the institution, to act with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of like character and with like aims to accomplish the purposes of the institution.

Section 16400 states that a violation by the trustee of any duty the trustee owes a beneficiary is a breach of trust. A breach of trust is any act by a trustee contrary to the terms of the trust or in excess of this authority and to the detriment of the trust, or the wrongful omission by a trustee of any act required of him or her by the terms of the trusts. Every violation by a trustee, whether willful and fraudulent, done through negligence, or arising through negligent oversight and forgetfulness, is a breach of trust.

APPENDIX B

Contractors B and C

This appendix provides a more detailed description of the business division's transactions with contractors B and C.

CONTRACTOR B

On January 2, 1996, the business division official requested the campus purchasing office to draw up a contract for contractor B, a former business division employee, to provide computer support services for new computer projects in the official's division. With no attempt to seek competitive bidding for this work, the official requested the contract to be effective from January 2 to June 30, for a total project cost not to exceed $45,000, and the purchasing office executed such a contract on January 5.

However, according to contractor B's invoice, she started providing computer support on January 2, and, by the time the contract was issued, had already provided more than $1,000 in services. The official authorized payments for contractor B's time and expenses to attend an annual CSU financial officers' association conference in Palm Springs and to assist in the selection and hiring of a technical employee for the official's division, although these activities were not specified in the contract. Despite the contract conclusion date of June 30, the campus paid contractor B $8,300 for her services in July. And despite the contract limit of $45,000, the campus paid contractor B approximately $46,700 for work from January through July of 1996.

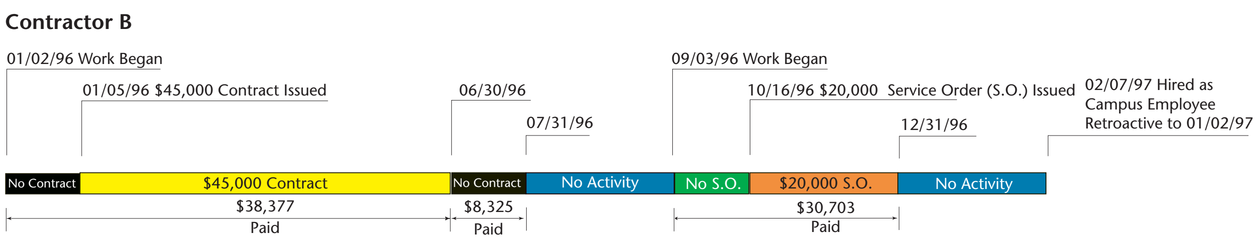
On October 16, 1996, the official requested the purchasing office to issue a service order for $20,000 for contractor B to provide computer support for her division from September through December. The campus issued such a service order that same day. Again, contractor B had already begun providing computer support to the official's division in September, prior to the service order, and charged the campus more than $11,100 for those services. The official approved the improper payment of this amount from the fees account, which she controls.

The official authorized payments that were about $10,700 over the October service order amount. This amount included over $1,000 in payments the official authorized for contractor B's time to attend a three-day information technology conference to gather information for the official's division. The amount also included a duplicate payment of $4,635 for services already paid with state funds, that the official authorized to be paid from the University Advancement Foundation (UAF) account she controls. Contractor B later reimbursed the duplicate payment.

In October 1996, the official indicated that she would soon hire contractor B as an employee in her division. In February 1997, the campus officially offered, and contractor B accepted, a temporary management position with a January 2, 1997, retroactive start date. Because contractor B actually began her job on the retroactive date, she was working and being paid as an employee without having been formally appointed to her temporary management position. Subsequently, in May 1997, through a recruitment to fill the management position, the official permanently hired contractor B. Figure 4 shows contractor B's dates of work, contracts, service orders, and payments.

FIGURE 4

The Business Division's Transactions With Contractor B
January 1996 Through March 1997



CONTRACTOR C

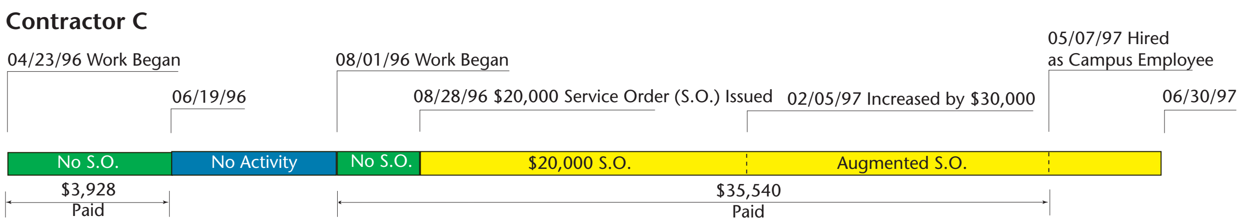
On August 1, 1996, the business division official requested the purchasing office to prepare a contract for contractor C, also a former business division employee, to conduct process mapping and provide business reengineering services for the business division from July 1, 1996, to June 30, 1997. On August 28, the campus purchasing office issued a $20,000 service order, but with a starting date of August 1.

However, contractor C started her work before the service order was issued, billing the campus more than $3,900 for services from April 23 to June 19. The campus paid for this work, even though it was performed when no written work agreement was in effect. The campus also paid contractor C $2,460 for services performed in August 1996. Because she did not break down the charges by dates, we could not determine how much of the work was performed prior to the service order.

From September 1, 1996, to January 31, 1997, contractor C charged the campus another $17,180 for her services, bringing the total billings to more than $3,500 over the approved limit on the service order. On February 5, 1997, the official directed the purchasing office to increase the total amount of contractor C's service order by $30,000, which the purchasing office did on the same day. For the period from February 1 to May 6, the campus paid contractor C another $15,900, which included payments for contractor C's time and expenses to attend an information technology conference and a process mapping seminar to gather information, although these activities were not specified in the service order. Figure 5 shows contractor C's dates of work, service orders, and payments.

FIGURE 5

The Business Division's Transactions With Contractor C
April 1996 Through June 1997



AGENCY RESPONSE

Because California State University, Fullerton (campus) employees told the campus president about some of the improprieties before we began our investigation, and because he participated in the creation of the University Advancement Foundation (UAF), we submitted our report to the chancellor of California State University (CSU) for corrective action. CSU reviewed our report and supporting documents and conducted its own investigation. CSU concluded that the issues we reported did not collectively demonstrate serious mismanagement at the campus. Instead, CSU believes that the issues we reported are examples of errors of judgment and mistakes in some instances. Nevertheless, CSU reported that the campus has established, or is in the process of establishing, policies to ensure that all funds received are properly spent and accurately reported, and that all hiring practices comply fully with CSU and campus policies. Also, CSU reported that it and the campus have initiated an external evaluation of the fiscal operations and management of the campus. CSU will "direct an evaluation of the overall adequacy and appropriateness of the management of fiscal operations as well as an evaluation of the same, relating to general financial internal control systems and of underlying central office and university-wide fiscal operations and management."

Specifically, in response to our findings in Chapter 1 regarding the campus's mismanagement of various accounts, CSU stated that, while the title and purpose of the all-purpose University Trust Project account could have more accurately defined its purpose, the expenditures from the account were legitimate expenses that advanced the educational mission of CSU. CSU concluded that the deposit of $219,000 in unused utilities funds into the all-purpose trust account was made in error, but that the campus spent the funds for legitimate purposes in accordance with established procedures. CSU reported that the campus will use only properly established trust accounts to receive and expend trust funds in an appropriate manner. Further, the campus will commit and spend its appropriated funds or return them to the State's General Fund.

Also in response to Chapter 1, CSU acknowledged that the business division's deposit of $15,000 in postage expense reimbursement into a nonstate account did not meet campus standards and said that the campus will take appropriate measures to correct the transaction. However, CSU believes that charges to internal departments for administrative services are not limited to reimbursement for direct expenses. In fact, CSU reported that the practice of retaining unused funds in cost recovery accounts from year to year is well established within the higher education environment. CSU also believes such practices are critical to ensure that ongoing operations can be carried out effectively, given the cyclical nature of campus appropriations. However, CSU reported that the campus will evaluate alternative means of recovering the full cost of providing services, and will periodically review the amounts charged to campus departments.

In response to Chapter 2, CSU agreed that the consulting contracts were not managed in accordance with campus standards, but concluded that no benefit was received by any individuals beyond that allowed by law or established by the contracts. CSU reported that the campus will contract in accordance with CSU guidelines.

In response to our findings concerning questionable personnel practices, CSU stated that campus management believes that it made personnel decisions consistent with regulations and that it has made a good faith effort to vigorously recruit to increase the number of qualified women and minority applicants.

Concerning Chapter 3, CSU acknowledged that UAF was not initially established as an officially recognized CSU auxiliary, but stated that it is now an official auxiliary in good standing. CSU had planned before we conducted our investigation to conduct a review of all campus auxiliaries. It is now conducting their review.

For Chapter 4, CSU concluded that expenditures by campus employees of donated funds for food, entertainment, flowers, gifts, and other items for themselves and other campus employees were legitimate and advanced the educational mission of CSU. Nevertheless, it concluded, "there were some expenditures for which the judgment could be questioned."

As for the improprieties related to endowment funds reported in Chapter 5, CSU stated that UAF has voluntarily submitted its scholarship fund accounting records to CSU for review. The campus supports the CSU's ongoing evaluation of the accounting records of the campus's auxiliaries. CSU stated that the campus's promotional materials reflected gross receipts when net receipts would have better represented the results of the Front and Center events. However, CSU did not address the inflation of proceeds from Front and Center events caused by the campus simply taking money from other campus and auxiliary accounts and depositing it into the Front and Center accounts. Further, CSU did not address the transfers from the Front and Center accounts to discretionary accounts. As we report on page 42, the campus could not provide evidence that these transfers were made to pay for legitimate event expenses.

Finally, CSU believes that we should not have asked the campus president to sign a statement under penalty of perjury and that his refusal to do so was a matter of principle. CSU characterized our interview with the president as an informal discussion that was not taped or recorded by a court reporter. Our interview with the president was not an informal discussion; it was a scheduled interview. Because campus employees had earlier complained to the president about several of the activities we substantiated, we believed it was important to ask the president, and have him go on formal record, about what action he had taken in response to the complaints. It is true that the interview was neither taped nor recorded by a court reporter. That is why, as we report on page 6, we asked the president to review our written summary of his statements and asked him to make any changes necessary to make it accurate. In fact, the president could have rewritten the statement. At no time did we tell or imply to the president that we wanted him to sign under penalty of perjury the statement as we had written it.

cc: Members of the Legislature
Office of the Lieutenant Governor
Attorney General
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
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