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February 27, 1998

The Arizona Board of Regents

Lattie F. Coor, President
Arizona State University

Pursuant to our statutory responsibility set forth in Arizona Revised Statutes (A.R.S.) §41-1279.03, we are currently conducting a single audit of Arizona State University for the year ended June 30, 1997, and our reports thereon will be issued at a future date. As a part of that audit, we have conducted a limited investigation of improprieties found at the University's Art Museum. The purpose of our investigation was to determine what improprieties had taken place, if any, and what persons were responsible for those improprieties, and if the University's internal control structure and its operation relevant to the Museum was adequate.

Our limited investigation consisted primarily of inquiries and the examination of selected records and other documentation. Therefore, our investigation was substantially less in scope than an audit conducted in accordance with generally accepted auditing standards. Accordingly, we do not express an opinion on the adequacy of the financial records or the internal control structure of the Museum, nor do we ensure that all matters involving the Museum's internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants or other conditions that may require correction or improvement were disclosed.

Our findings and recommendations as a result of our limited investigation are set forth below.

Background

The Arizona State University Art Museum was founded in 1950. The Museum's operation is funded by an annual state appropriation. This appropriation was \$638,190 for the year ended June 30, 1997. The Museum also solicited and received grants and donations to fund other activities, such as traveling exhibits, art catalogs, receptions and dinners normally produced and held in conjunction with an exhibit, additions to the Museum's collection, and restoration of pieces already in the Museum's collection. Federal agencies, corporations, and private citizens were all sources of grants and donations to the Museum. Another source of money for the Museum is its internal store. The internal store had an average inventory of arts and crafts estimated in value at \$50,000 and sales of over \$140,000 for the year ended June 30, 1997.

The internal store was operated by volunteers and was self-supporting. The Museum used the profits generated by the store's sales to purchase additions for the Museum's art collection and for various other purposes.

The Museum's monies were deposited with either the University Comptroller's Office or with the Arizona State University Foundation (the Foundation). The Foundation is a financially interrelated nonprofit corporation controlled by a separate Board of Directors whose goal is to support the University. It was the Museum's policy to deposit all monies collected from the internal store's sales, from federal grants, and from the state apportionment with the University Comptroller's Office. All other monies the Museum received, including donations and grants from corporate or private sources, were deposited with the Foundation.

Improper Use of Public Monies

All of the monies discussed above were received in the name of ASU, by ASU employees as a part of their official duties. Because ASU is a public institution and its employees are public employees, these monies were public monies. Therefore, all of the monies described above should have been deposited with the ASU Comptroller's Office.

We found that nearly every check the Museum deposited to the Foundation was made payable to either ASU or the ASU Art Museum. These checks included payments from donations, federal grants, exhibit fees, catalog sales, and shipping reimbursements from other museums. For the period of July 1, 1995 through June 30, 1997, we determined that the Museum improperly used public monies by misdirecting \$248,184 to the Foundation.

In addition, because these monies were deposited with the Foundation and not the University Comptroller's Office they were not subject to the University's controls. Consequently, the Museum expended the monies for items such as alcoholic beverages, flowers, fines for parking violations, lost library books, and other items that would not have been allowed if the monies had been deposited with the University.

Furthermore, the Museum solicited donations through a membership drive held each fall. Previous members and other interested persons were sent a Museum membership application. Membership applications were also distributed in the Museum's quarterly newsletter. These applications contained instructions that directed applicants to make checks payable to the ASU Art Museum, and to submit payments to the Museum.

However, as stated above, the Museum deposited these monies with the Foundation and not the Comptroller's Office. We examined the Museum's records for these deposits for the period from July 1, 1995 through June 30, 1997, and determined that \$24,547 of public monies had been misdirected to the Foundation.

The Museum also solicited donations directly from Museum visitors by providing donation receptacles inside the Museum. The Museum did not maintain any records

documenting the amount of money collected in this way or how these monies were expended. However, the Museum estimated that approximately \$100 per month was collected in the receptacles. For the period from July 1, 1995 through June 30, 1997, there was only one \$100 deposit made to the Foundation. The remaining money totaling approximately \$2,300 could not be accounted for, but the director stated that on several occasions the monies collected in the receptacles were used to buy sandwiches and snacks for the Museum's advisory board meetings, and on one occasion, the money was used to purchase champagne for a reception held at the Museum. Due to the lack of recordkeeping and because the monies were disbursed directly from cash receipts, these monies were susceptible to fraud, waste, and abuse.

The ASU Comptroller's Office Policies and Procedures Manual, COM 301, contains the University's policy on cash. The policy makes the following statements:

- "Funds received on behalf of, or for the benefit of, ASU must be deposited in university area / orgs only."
- "All solicitation material for gifts to the ASU Foundation or other financially related organizations must indicate that the funds will be deposited with that organization and instruct the donor to make the check payable to that organization and not to ASU."
- "All cash receipts are to be deposited in total and may not be used for the direct payment of miscellaneous small purchases."

In misdirecting a total of \$275,131 the Museum did not comply with *The ASU Comptroller's Office Policies and Procedures Manual*, COM 301. Furthermore, by misusing these public monies, the Museum's director and employees may have violated A.R.S. §35-301, which states, "A public officer or other person . . . charged with the receipt, safekeeping, transfer or disbursement of public money is guilty of a class 4 felony who . . . knowingly fails to keep it in his possession until disbursed or paid out by authority of law." [or] "Without authority of law knowingly deposits it, or any portion thereof, in a bank, or with a banker or other person, except on special deposit for safekeeping."

Recommendations

To ensure proper control over public monies, the Museum should take the following steps:

1. All public monies received by the University must remain with the University and not be misdirected to financially interrelated corporations, like the Foundation.
2. No disbursements for unallowable items under University policy, Board of Regents policy, or state statute may be made from public monies.
3. All cash collections should be documented and deposited intact. In addition, all cash receipts should be deposited daily if significant, or at least weekly.

Transactions with Related Parties

During our examination we found that the Museum contracted with the director's son for translation and other services. The director made all decisions regarding this contract with her son, and did not file a conflict-of-interest statement with the University. On at least one occasion the son was paid in advance for his services and failed to perform them. The director made installment payments to repay the money that the Museum had paid her son.

In addition, we found three other cases in which the Museum had contracted to purchase goods and services from the spouses of Museum employees. There were multiple contracts in at least two of these cases. In one case the relative received advance payment for services to be delivered. In one case the payments to the relative were improperly classified and therefore the monies the relative received were not reported as earnings to the appropriate authorities. None of the employees whose relatives had contracts with the Museum filed a conflict-of-interest statement with the University.

*The ASU Staff Personnel Policies and Procedures Manual, SSP 802, states "Any employee who has, or whose relative has, a substantial interest in any contract with, sale to, purchase from, or service for the university or the Arizona Board of Regents shall make known that interest in the official records of the Arizona Board of Regents and shall refrain from voting upon or otherwise participating in any manner as an employee in the contract, sale, purchase, or service." Because none of the Museum employees whose relatives had contracts with the Museum had filed a conflict-of-interest statement with the University, they did not comply with *The ASU Staff Personnel Policies and Procedures Manual, SSP 802.**

In addition to not complying with University policy, the Museum's director and employees may have also violated A.R.S. §38-503(A), which has similar provisions to the ASU policy, SSP 802.

Recommendation

To comply with University policy and A.R.S., the Museum should avoid entering into contracts with relatives of its employees or director.

Lack of Accountability for Frequent Flyer Miles

Various frequent flyer accounts held by the director contained both mileage earned at the University's expense and mileage earned at the director's personal expense. From the limited records available, we determined that there were at least 94,149 frequent flyer miles available in the director's account and that 50,000 miles had been converted or used during the director's employment at ASU. Because the mileage was commingled and because the Museum's records were incomplete we were unable to reconcile any of the director's frequent flyer accounts or determine exactly what mileage

had been earned at the University's expense. When asked specifically about the use of two frequent flyer coupons, each good for one round-trip ticket anywhere in the continental United States, the director stated that she was in possession of these coupons. However, the director was unable to produce these coupons for our inspection and stated that she was unsure where the coupons were.

The ASU Comptroller's Office Policies and Procedures Manual, COM 512, states "Discounts, rebates, and/or frequent flyer coupons earned because of university travel are considered the property of ASU. Travelers who qualify for travel bonuses based solely upon university travel are obligated to deliver them to Travel Reimbursements If a traveler qualifies for free travel arrangements resulting from a combination of university and personal travel and uses the free travel arrangements for personal purposes, the traveler should reimburse the university proportionately." The director did not comply with this University policy.

Recommendations

The Museum should maintain records of all frequent flyer mileage its director and employees earned at the University's expense. These records should be reconciled periodically to the statements provided for the frequent flyer accounts.

To comply with University policy, the Museum's director and employees should deliver any discounts, rebates, or frequent flyer coupons earned solely at the University's expense to Travel Reimbursements. Furthermore, if free travel is earned through a combination of business and personal travel and the travel is made for personal use, the University employee should reimburse the University proportionately.

Lack of Controls in the Museum's Internal Store

As a part of our examination we reviewed the Museum's internal controls. We found the controls over inventory and cash receipts in the Museum's internal store were deficient. The store did not take an annual inventory. The store also did not have a perpetual inventory system or any other way of verifying inventory sold on any given day. We found that one person, a volunteer, had ordered the goods for sale, received those goods, priced them, and acted as a cashier for the store. This represented a severe lack of proper segregation of duties, and caused these public monies, and the related inventories, to be susceptible to fraud, waste, and abuse.

Recommendation

In order to gain proper control over the internal store's inventory and cash receipts the Museum should:

1. Establish an initial record of inventory by physically counting the store's inventory. The Museum should then establish procedures by which the store's inventory could be verified through the use of either a periodic or perpetual inventory system.

2. Institute a proper segregation of duties. The duties of cash handling, custody of assets, and recordkeeping should be segregated among different persons.

University Procurement Procedures Not Followed

The Museum performed its own procurement for shipping artwork and printing catalogs. Museum staff indicated their procedures were to obtain verbal or written quotes from at least three sources each time a purchase was made; however, there was not adequate documentation to support this assertion.

In two separate cases, the Museum made purchases in excess of \$25,000 without obtaining competitive sealed bids or proposals. In both cases, all or part of the purchases were made from public monies in the Museum's account at the Foundation.

The ASU Purchasing Department Policies and Procedures Manual, PUR 306-01, states "All procurements with an estimated cost of \$25,000 or more per transaction shall be based on competitive sealed bids or proposals." Because the Museum failed to obtain competitive sealed bids or proposals, the Museum did not comply with *The ASU Purchasing Department Policies and Procedures Manual*, PUR 306-01 and may have not obtained the most favorable terms possible for the University in these transactions.

Furthermore, *The ASU Purchasing Department Policies and Procedures Manual*, PUR 201-02, states "No individual other than the director of Purchasing and Business Services has the authority to place an order directly with a vendor, to enter into a contract or lease, or to obligate the university in any way unless: 1) the president of the university specifically authorizes an individual to do so in writing or 2) the director of Purchasing and Business Services delegates purchasing authority to specific individuals for a specific term or purpose." Because the Museum was not authorized by either the President of the University or by the Director of Purchasing and Business Services, the Museum did not comply with *The ASU Purchasing Department Policies and Procedures Manual*, PUR 201-02.

Recommendation

To ensure compliance with the policies and procedures of the University's Purchasing Department, the Museum should conduct all its procurement through the University's Purchasing and Business Services, unless otherwise authorized by the President of the University or the Director of Purchasing and Business Services.

Should you have any questions concerning the contents of this letter, please let us know.

Sincerely,

Debbie Davenport
Deputy Auditor General

cc: Gerald E. Snyder,
Comptroller and Treasurer,
Arizona State University

Milton D. Glick,
Senior Vice President and Provost,
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