

A photograph of Anderson Hall at Kansas State University, a large stone building with a prominent tower and arched windows, illuminated by warm light. A purple vertical bar is on the left side of the page.

Kansas State University

Summary Observation Review
Internal Audit | June 30, 2017

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ANDERSON HALL
ADMINISTRATION

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Executive Summary

We have performed an analysis of 951 audit observations throughout several years to determine the frequency of certain issues across campus. These detailed observations were consolidated into overall themes, particularly those related to the control environment; risk management; the extent of compliance with the applicable regulations, policies and procedures; and whether there were adequate internal controls for the handling of funds and property. Effective control activities are designed to mitigate risk and are aligned with management’s willingness to accept weaknesses of controls and compliance. Some best practices to reduce the occurrence of these issues include:

- Establish a stronger control environment at the leadership level to foster ethical conduct, identification and management of risk, importance of compliance, adherence to internal controls and accountability.
- Enhance accountability by incorporating compliance and internal control design and implementation responsibilities into appropriate employee performance expectations.
- Update policies and procedures to ensure the university’s objectives are met and control activities are aligned with management’s risk tolerance.
- Require mandatory training of the employees who are assigned responsibilities for the business processes identified.

The detailed observations in this report provide a consolidated, detailed discussion of the weaknesses identified along with the criteria and significance.

Purpose and Scope

The purpose for the review was to identify weaknesses, and then understand and develop university mitigation efforts. The review consisted of examining more than 100 internal audit reports that included 951 observations and recommendations. The original audits included an examination of the records to determine the occurrence of observations and the associated criteria and significance of the weakness. The internal audit reports and similar observations were reviewed and entered in a database that analyzed the frequency of these observations. A report of this type is intended to be constructive in nature, provide management with an independent analysis and recommend areas for improvement. Therefore, the absence

of complimentary comments is not intended to imply the accounting procedures, operations or internal controls, in general, are deficient or unsound. The original audit examinations were based upon selected tests of accounting records, other records and related procedures; therefore, it may not have necessarily disclosed all instances of control weakness or operational inefficiencies.

General Comments

The detailed results are found in the Appendix. However, the overall theme indicates a need to improve the control environment by emphasizing the importance of controls by those in leadership at each level of the university. To implement the environment as established by management, certain control activities such as desktop procedure manuals and more extensive training should be available to the campus community. These concepts are discussed in more detail as follows:

Control Environment

Per the Committee of Sponsoring Organizations, or COSO, of the Treadway Commission, “the control environment is the set of standards, processes and structures that provide the basis for carrying out internal control across the organization.” The control environment helps establish the tone of the unit and influences the control recognition of personnel, and is the foundation for all other components of internal control by providing discipline and structure. Management reinforces expectations at the various levels of the organization. The control environment comprises the integrity and ethical values of the organization; the parameters enabling the university to carry out its governance oversight responsibilities; the organizational structure and assignment of authority and responsibility; the process for attracting, developing and retaining competent individuals; and the rigor around performance measures, incentives and rewards to drive accountability for performance. The resulting control environment has a pervasive impact on the overall system of internal control. Some of the overall trends are related to establishing a tone at the top and accountability.

Tone at the Top

Although the university executive leadership establishes the “tone at the top” for the campus community, each unit or department or subdepartment level such as academic department chairs, deans, directors, managers and supervisors influences the tone at their respective levels. Leadership positions should establish an environment that includes ethical conduct, identification and management of risk, importance of compliance, adherence

to internal controls and accountability. The tone should be communicated so that each person within the span of responsibility and sphere of influence of leadership is aware of the importance of those attributes. Soft controls such as establishment of ethical values have become more necessary because of technological advances that have enabled employees to assess large amounts of critical information and make decisions that were formerly made at higher levels within the management structure. Consideration should be given to implementing an enterprise risk management process and raising the ethical awareness of the university community.

Accountability

COSO notes that a part of the control environment component of internal control includes accountability. As such, personnel evaluation processes should include performance measures, incentives and rewards, based in part on establishing internal controls and complying with policies. Therefore, no system of policies and procedures is adequate if compliance with laws, rules and regulations, internal control design, and implementation is not accompanied by accountability. Consideration should be given to these processes as part of employee evaluations.

Control Activities

COSO states, “control activities are the actions established through policies and procedures that help ensure management’s directives to mitigate risks to achieve objectives are carried out,” and that control activities are a major component of internal control. Objectives often encompass adhering to the budget; reporting to grantors or the state, safeguarding of assets; and complying with laws, rules and regulations. Control activities are performed at all levels of the university, at various stages within business processes, as well as the technology environment. Among the broad issues made evident through this review included the need for adequate policies and procedures and training.

Policies and Procedures

Although the university has established many easily accessible policies and procedures in the Policies and Procedures Manual, or PPM, many instances were noted where departments had not complied. The PPM helps ensure compliance with federal laws, rules and regulations, thus protecting university assets.

In addition to universitywide policies and procedures, units may have additional processes that are more extensive

or detailed than the PPM. Although the PPM often provides specific processes, additional sample completed documents, often as a desktop manual, should be available to help provide step-by-step instructions to further enhance operations. Both formal and desktop procedures are invaluable when turnover occurs.

The university PPM should be periodically reviewed to ensure it is adequate and current. In certain instances, the PPM may be overly restrictive compared to state of Kansas requirements and, as part of a periodic review, there may be instances in which unneeded processes could be eliminated without creating compliance issues with the state. On the other hand, additional policies and procedures may need to be developed to assure compliance or to provide adequate internal controls.

Training

Underlying factors that could contribute to PPM noncompliance could be the result of a lack of a continuous training process by central offices. Employees should have the necessary skills, knowledge and tools to perform their responsibilities. The training process should be enhanced by implementing formal onboarding procedures for new hires as part of the required employee orientation. Moreover, consideration should be given to requiring current faculty and staff to attend periodic training sessions, including online training through a database that could monitor whether appropriate employees have completed their training. “Appropriate” faculty and staff are individuals who initiate, process or approve financial transactions and/or are responsible to maintain assets or administer processes that expose the university to risks such as, but not limited to, compliance with federal, state and university policies, procedures, rules and regulations, as well as safety, hazardous materials, animal safety, or biological/chemical materials that could pose a hazard to the university or to the community at large. Ongoing training is necessary to adapt personnel to control requirements of a changing environment.

Conclusion

Approximately 90 percent of the weaknesses identified in the reviewed internal audit reports were related to compliance with policies, procedures, regulations and adequate internal controls. These weaknesses could be improved by updating university policies and procedures, requiring job training, incorporating compliance responsibilities into employee performance expectations, and establishing a tone at the top that indicates the importance of controls.

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Inventory

Observation

Observed weaknesses in proper recording and maintenance of the fixed asset, departmental and consumable supplies and commodities/items purchased for resale inventories; authorization to use university property off campus; and in the reporting of losses.

Criteria

PPM 6510 provides university guidance on inventory including controls to fulfill the Kansas Legislature requirement for all agencies to maintain a fixed asset record based on a physical inventory for all acquisitions, including items gifted to the university of appropriate value and reduced by all dispositions of fixed assets. A departmental inventory of items not on the university fixed asset record is to be kept for internal control purposes, and annual inventory of consumable items and items purchased for resale is to be reported to the Division of Financial Services by June 30. Any university property used off campus is to have an agreement to use K-State property off-campus form on file per PPM Chapter 3030

Why is this important?

An asset record identifies university property and documents identification elements and original cost for use in the event of a loss. Inventories of consumable items and items purchased for resale identify associated costs with receipts for the period and contribute to break-even pricing calculations. Fixing responsibility for university property used off campus ensures accountability for the asset until its return and fixes liability in the case of a loss.

Expenditures

Observation

Observed weaknesses in following purchasing requirements from sources required by state statutes; competitive bidding, including splitting orders or payments to stay below bid requirements; seeking proper approval for extraordinary purchases such as building and grounds changes, official hospitality or sole source purchases; tuition payments; engaging and contracting with consultants; supervisory approval of expenditures; using proper forms; maintaining expenditure documentation; and using appropriate sub-objects to report expenditures, inventory and resale items.

Criteria

PPM 6310, 6312 and 6320 provide university guidance to ensure all payments for goods, services, equipment and capital outlay items are made in accordance with state statutes, the Kansas Department of Administration regulations and university policies in an expedient manner. PPM 7010.340 provides detailed guidance concerning consultant services and sub-recipient support for university research. PPM Chapter 3090 provides retention guidance of expenditure records that are to be retained in most cases for a minimum of five years.

Why is this important?

Abiding by state statutes and policies and procedures related to competitive bidding, purchasing and proper approvals promotes fairness, transparency, integrity, competition and increased economies and efficiencies that promote the pursuit of excellence and the best interests of the university.

Travel

Observation

Observed weaknesses in proper approval of out-of-state travel, retaining the associated travel documentation, reduction of per diem for meals included in the registration and recording annual leave taken in connection with university travel.

Criteria

PPM 6410 requires all travel to be preauthorized, travel documentation retained within the department, including the conference agenda, meeting information, meals, conference dates, lodging information and related expenses. No subsistence expense may be reimbursed when it is furnished at no cost to the employee or included in the registration fee. Annual leave taken before or after official travel is to be approved and noted on the out-of-state travel request and recorded in the HRIS.

Why is this important?

Lack of control in approval of travel, improper documentation, subsistence for meals provided and improper annual leave recording causes extra costs incurred by the university, a lack of transparency and an image of impropriety. Care must be taken to manage training and travel funds wisely to ensure future funding for an adequately trained staff, research collaborations and the transfer of knowledge to the public, as well as the university's reputation.

Telephone Use

Observation

Observed weaknesses in controlling personal usage of university-provided cellular devices and long distance calls on university equipment. Personal usage is not always noted or reimbursed as required.

Criteria

PPM 6330 advises university-provided mobile devices not be used for personal use and to be approved on the basis of work assignments. More than de minimis use may result in revocation of the device. Each payment request is to contain a statement on the invoice or payment voucher that “use is in accordance with university policy.” PPM 3310.030 advises personal phone calls on university telephones be kept to a minimum and that any personal calls requiring a toll charges be paid by the employee. Employees needing to make a personal toll call should make the call collect or charge it to a residential telephone or personal credit card. Any call inadvertently charged to the university is to be reimbursed.

Why is this important?

Inadequate internal control in personal usage of university cellular devices or telephones increases the risk of fraudulent activity going undetected, resulting in increased expenses and control efforts, and diminished production while on the phone during work hours.

Receipts

Observation

Observed weaknesses in controlling receipts and cash-handling procedures, including the use of official receipts or other approved records of prenumbered daily transactions; using proper report receipt codes; timely deposits; adequate supporting deposit records; document retention; securing of undeposited receipts; and check endorsements. Observed weaknesses in separating responsibilities, during which time an individual responsible for receiving funds, completing the official receipt and preparing the deposit slip had access to record or authorize transactions in the accounts receivable ledger and customer accounts, recording cash transactions, and/or preparing monthly reconciliations without adequate compensating controls, including supervisory review. Observed weaknesses in the use of service-clearing funds include a lack of a policy statement explaining fee structures, maintenance of a break-even pricing, and nonuniversity funds that should be deposited to a restricted fee account.

Criteria

PPM 6110 provides guidance concerning the receipts and deposits of university funds to ensure receipts are deposited in accordance with state of Kansas laws and statutes, as well as accurate accounting of receipts, including the required use of official receipts, unless an alternate procedure is approved by the assistant vice president of the Division of Financial Services, proper sub-object reporting of receipts; proper depositing of funds exceeding \$25 by the next business day, retention of supporting documentation for receipts, adequate securing of undeposited receipts and proper check endorsements. PPM Chapter 3090 provides guidance on the retention of expenditure records that are to be retained in most cases for a minimum of five years. PPM 3210 discusses adequate segregation of duties between authorization of transactions, custody of assets and record-keeping. When the work of one employee is checked by another, and when the responsibility of assets is separate from the responsibility of maintaining related records, there is appropriate segregation of duties. PPM 6085 discusses service-clearing funds used in accordance with K.S.A. 76-755, requiring self-supporting operation of each service-clearing fund. Fees are to be established in a written policy with a full cost-recovery pricing schedule in a break-even concept. Nonuniversity funds must be deposited in a restricted fee account.

Why is this important?

Inadequate internal control in the receipt and recording of funds received and improper segregation of duties increases the risk of missing objectives and increases the risk of fraudulent activity occurring undetected. Improper service-clearing fund use may result in state funds being improperly used for noncompliant finance activities, which could jeopardize state funding and the university's reputation.

Time and Leave

Observation

Observed weaknesses in reporting and recording time and time documents, requesting time away, securing and retention of time documents, changing documents and correcting time in HRIS. Observed weaknesses in compliance with the maximum work hours for students while classes were in session.

Criteria

PPM 4220 outlines the requirements for proper time recording and the completion of time documents that requires an accurate accounting of hours worked, leave used during the pay period, accurate verification and approval by the supervisor and proper error correction. PPM 3090 provides guidance on employee record retention for the typical five-year minimum. PPM 4720 states that the maximum work hours for most students is 30 hours per week while classes are in session, due to the FICA exemption. Because of immigration regulations, students holding F-1 and J-1 visa are limited to 20 hours per week. All students are limited to 30 hours per week while enrolled in four or more credit hours. Students are never allowed under any circumstances to work more than a 40-hour week.

Why is this important?

Improper reporting and recording of time could result in Department of Labor, Wage and Hour FSLA investigations and considerable penalties and liabilities related to noncompliance fines and payments for wages due. Working in excess of the maximum hours risks interfering with their education, the primary reason they attend K-State.

Foundation

Observation

Observed weaknesses in providing adequate documentation for deposits, completion of monthly reconciliations, record retention, proper signature authorization on file, authorized individual expenditures approved by higher authority, and university funds incorrectly deposited to the KSU Foundation.

Criteria

A Guide to the Kansas State University Foundation, PPM 8210 and PPM 7010 provide guidance for the deposit of funds to the foundation, adequate record-keeping, and expenditure of those funds. PPM Chapter 3090 provides guidance on the retention of accounting records that are to be retained in most cases for a minimum of five years.

Why is this important?

Improperly depositing university funds to the foundation could lead to and institutional research going unreported and conducted without proper oversight and in violation of university and federal regulations and laws. Inadequate internal control over foundation deposits and spending could lead to state law violations, including sales tax laws and reporting, Unrelated Income Tax reporting, reputational risk and the risk of undetected fraudulent activity.

Accounts Receivable

Observation

Observed weaknesses in recording, collection and reporting of accounts receivable and for the write-off of uncollectible accounts, including consecutively numbering invoices, a receivables control ledger, subsidiary records, and completion of monthly and annual accounts receivable reports.

Criteria

PPM 6210 provides guidance for management, collection and reporting of accounts receivable due from federal, state and local government; interfund; external entities; or individuals billed as a result of regular business transactions, including recording, reporting, writing off uncollectible accounts, provision of sequentially numbered invoices, maintenance of receivables subsidiary records and control ledger, and completion of monthly and annual accounts receivable reports.

Why is this important?

Improper maintenance of accounts receivable allows transactions to occur without being recorded, inaccuracy in amounts, and increases the risk of fraudulent activities to occur undetected. For example, cash received can be diverted and remain undetected.

Information Technology

Observation

The department is to develop and implement a disaster recovery plan. A regular system backup procedure is to be established where the backup files are kept at another location. Employees need to use computer security practices, including locking their computer when leaving their desks, and password protecting their screen savers. The old servers must be updated with new servers that match the specifications recommended for the software hosted on the server. The current servers could be used for development and testing.

Criteria

PPM 3438 requires all university information and technology resources to have appropriate physical and environmental security controls applied commensurate with identified risks. Kansas Information Technology Council Information Technology Policy 7230 Revision 2, referenced in PPM 3438 and others, requires entities to ensure risk assessments are performed for information systems in accordance with standards and ITEC Policy 7310, referenced in PPM 3432. The Information Technology Security Self-Assessment Policy requires all state agencies, including regents institutions, to complete an annual self-assessment of the security status of its information systems. Kansas Information Technology Executive Council Policy 5300 Revision 1, referenced in PPM 3432, requires all state entities to have business continuity plans to continue critical operations during any disruption and resume normal operations within a reasonable period of time. The Kansas Information Technology Executive Council 7230A Default Information Technology Security Requirements, Section 9, Security Requirements Document, Jan. 11, 2010, referenced in PPM 3439, requires mandatory contingency planning to address disruption to, or failure of, all information systems that house or access state-controlled information. Contingency plans are to be tested annually through the use of table-top exercises and at least every five years with a full-scale test. Keeping system backups in a separate location helps ensure availability of data for system restoration in the event of a disaster. For nonessential systems, no actions to restore functionality need be taken. PPM 3430 requires unattended university computers to have enabled password protection on the screen saver that enacts in 20 minutes or less. It is recommended computers be set to automatically logout after no more than 30 minutes idle. PPM 3439 requires appropriate security controls to be considered at all stages of an information system life cycle. Effective computing infrastructure life cycle planning ensures replacement of obsolete equipment prior to creating a security vulnerability risk.

Why is this important?

Critical information and technology resources are required for the entity to maintain functional operations. Losses of those systems can stop operations unless adequate contingency plans have been established and tested properly to restore operations of critical systems within a reasonable period of time. Password protection in conjunction with an automatic screen saver and automatic system logout helps protect against unauthorized access of data and systems. Obsolete equipment may be vulnerable to unauthorized access to sensitive information and computing infrastructure.

Change Funds

Observation

Observed weaknesses in the maintenance of the change fund with adequate security; the daily reconciliation of change funds and the record of cash long and short form; updating the DA-74 whenever there was a change in employees; the segregation of duties over the change fund; having a fund too large for the purpose; and having an unauthorized change fund.

Criteria

PPM 6120 discusses the DA-74 Application to Establish Change Fund form is to be submitted to the Division of Financial Services to request a change fund and whenever there is a change in employees. The change fund is to be reconciled daily with cash long or short and recorded on the DA-76 Record of Cash Long or Short. The fund is to be maintained by the custodian or alternate custodian with adequate security. An unauthorized change fund should not be kept in the office.

Why is this important?

Change funds are to be used only for making a change in the transaction of university business. Use of the fund outside of the purpose increases the risk for misappropriation of both the change fund and undeposited receipts.

Sales Tax

Observation

Observed weaknesses in the collection and remittance of sales tax; obtaining and maintaining the appropriate exemption certificates from customers claiming to be sales tax-exempt; and preparing and submitting monthly sales tax reports to the Division of Financial Services.

Criteria

PPM 6130 provides guidance in the collection and remitting of Kansas sales tax, including sales tax collected and remitted on the retail sale, rental or lease of tangible personal property, charges for labor services to tangible personal property and sales of admissions; the types of exempt sales relating to exempt buyers, exempt items and their uses; obtaining exemption certificates; procedures involved in collecting sales tax separately or included in the price of the item; calculations of destination-based sales tax rates; reporting sales tax on the monthly sales tax report; and maintenance of adequate records. State of Kansas Publications 1510, 1520 and 1560 may assist in understanding state tax laws and regulations. Publication 1560 “Tax Guide for Schools and Educational Institutions” provides specific guidance on tax topics related to the university. These publications are available at ksrevenue.org/forms-bustax.html.

Why is this important?

Improper collection and submission of sales tax leaves the university open to back payment, state fines and penalties and reputational risks involved in not complying with state laws, regulations and policies.

Schedule of Charges

Observation

Observed weaknesses in the completion and approval of a schedule of charges for all fees or services for which a fee is collected and related price-change updates, prices being charged consistently and in accordance with the approved schedule of charges, prices following a break-even concept or at what the market can bear when appropriate, and charging internal prices to university departments and external customers direct costs plus applicable F&A costs.

Criteria

PPM 6085 requires all activities, no matter how small, have a substantiated price; a break-even pricing schedule; abide by policies governing unfair competition; be reviewed and updated on a regular basis; and that all sponsored agreements receive the lowest rate available, as specified in CFR 2 Part 200.468. Any sale of products or services by the university, its auxiliary enterprises or university-affiliated entity is appropriate only if such sale is an integral part of, or reasonably related to, an activity which is essential to the fulfillment of the institution’s instructional, research, or public service missions.

Why is this important?

Unapproved pricing schedules may violate federal and state laws, which could result in return of funds, fines, penalties and/or debarment of the university from participation in federally sponsored research; charges of unfair competition; and other allegations of improprieties leading to reputational risk.

Vehicles

Observation

Observed weaknesses in recording the costs associated with the operation and maintenance of university vehicles, including recording mileage at fill-ups and when repairs and replacements are completed, conducting a periodic review to ensure accurate maintainence and appropriateness of expenses, and the maintenance of a vehicle use log for all trips outside the vicinity or work locations.

Criteria

PPM 6420 outlines the policies, responsibilities and procedures for the use of all state motor vehicles owned, leased or operated by the agency, officer or state employee when on official business, including maintaining vehicle travel records and expenses, which entails recording the beginning and ending mileage of trips, mileage at refueling and at service intervals, maintenance, repairs and oil changes.

Why is this important?

Inadequate monitoring of vehicle usage and expenses could result in an accident due to poor maintenance, inappropriate use and/or undetected fraud.

External Entity Contracts

Observation

Observed weaknesses in allowing the use of university resources, including hosting arrangements, by external entities without an official sponsored agreement in place. In agreements where revenue sharing is involved, the contract should include a clause which clarifies when excesses of revenues over operating expenses are to be distributed to the university. If expenditures or transfers by the university are greater than \$1 million, the Board of Regents president and CEO are to be notified in writing of the contract.

Criteria

PPM 3070 requires agreements involving the use of university resources by external entities to be processed as sponsored projects. Contracts with the expenditure or transfer of more than \$1 million require notifying the Kansas Board of Regents and CEO in writing.

Why is this important?

The use of university resources without an agreement leaves the university open to potential liabilities. Without adequate compensation and proper fixing of responsibilities, litigation may occur in case of a disagreement.

Financial Review

Observation

Observed weaknesses in setting up separate projects for determining results of operations, financial status of the unit and funds required to be in full cost-recovery/breakeven accounting in accordance with state legislation.

Criteria

PPM 6085 states all activities, no matter how small, must have a substantiated price and a break-even pricing schedule that is reviewed and updated on a regular basis. Maintenance of a separate project for those funds clarifies the accounting.

Why is this important?

Co-mingling of funds makes it difficult to document break-even analysis and could result in costs having to be reimbursed, and/or fines and penalties.

Access Controls

Observation

Observed weaknesses in monitoring of access to data, investigating security violations and subsequent actions for resolution.

Criteria

PPM 3415 responds to the Gramm-Leach-Bliley Act of 1999 that mandates protection of student financial information within the university’s policy, as well as implementing and maintaining a comprehensive information security program that contains administrative, technical and physical safeguards to protect covered information. It requires risk assessment with CISO oversight, including employee training and management, information systems designs, incident management, designing and implementing safeguards, overseeing service providers, and program evaluation and adjustment. PPM 3431

Why is this important?

Inadequate monitoring of access to data and investigating security violations without appropriate controls to address security risks and prevent violations leaves protected student financial information unsecured. This subjects the university to risks of fines and penalties as well as reputational risk.

Credit Card Processing

Observation

Observed weaknesses in credit card transactions in compliance with university policies and procedures and Payment Card Industry Data Security Standards.

Criteria

PPM 6115 provides guidance concerning the accepted use of credit cards in payment for university business and incorporates the Payment Card Industry Data Security Standards.

Why is this important?

Weaknesses in credit card processing and noncompliance with Payment Card Industry Standards leaves credit card information vulnerable to data breaches and the university at risk for fines and penalties as well as reputational risk.

Conflict of Interest

Observation

Observed weaknesses in conflict of interest and time disclosures and management plans addressing these matters.

Criteria

The University Handbook, Appendix 5, provides guidance on the management of real or apparent conflicts of interest and time commitments and consulting and other employment, with the goal of self-disclosure, discussion and negotiation to generally resolve disputes to comply with state law and mandates from the Board of Regents and federal agencies.

Why is this important?

Conflicts of interest and time call into question the professional objectivity and ethics of the individual and reflect negatively on the employing university. If not properly managed, such conflicts could lead to allegations of misconduct and debarment from federal research programs.