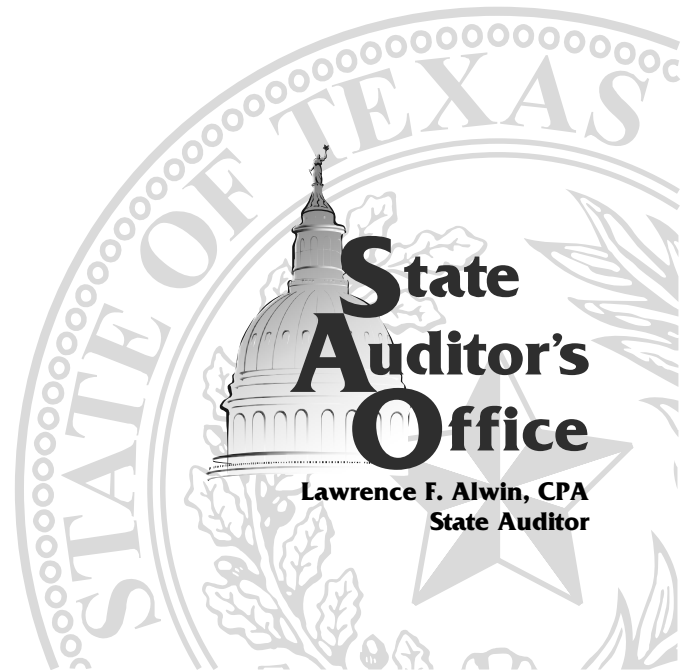


An Audit Report on

Cash Controls at the University of Texas Health Science Center at Houston

October 2004

Report No. 05-006



Cash Controls at the University of Texas Health Science Center at Houston

Overall Conclusion

The University of Texas Health Science Center at Houston (Health Science Center) has significant weaknesses in controls over the receipt and disbursement of cash, which increases the risk of financial reporting errors, fraud, and theft. We concentrated on those areas where staff physically handle checks and currency and process related transactions, making them vulnerable to fraud, theft, and abuse. We did not review controls related to major cash receipts such as state appropriations, Medicare, and research grants because those revenues are typically subject to significant external controls. Although our assessment covered a relatively small number of clinics and departments (5 clinics and 13 departments), we found control weaknesses and errors at each one, which appears to indicate institution-wide problems. The Health Science Center does not have accurate and complete recordkeeping for cash collection, revenues, receipts, or disbursements. In addition, it does not consistently comply with cash management laws and regulations or internal policies and procedures, and its information system security controls need improvement.

The Health Science Center is a large, decentralized, and complex organization that serves many functions, including education, research, public service, and medical care. Many of the clinics and departments, which are relatively autonomous, have responsibilities relating to cash management. The Health Science Center's decentralized nature makes it important for management to develop and implement comprehensive policies and procedures that can be applied in all clinics and departments. In addition, management should oversee and enforce these policies and procedures to ensure compliance. Although the Health Science Center has a handbook of operating procedures, the cash handling policies and procedures are not an adequate source of guidance for individual departments.

Key Points

Several clinics and departments tested do not have adequate controls for safeguarding cash.

We found that, in at least nine clinics and departments, some staff members performed at least two steps in the cash collection process, such as receiving cash and preparing deposits. We also found that six of the clinics and departments evaluated had inadequate physical security for safeguarding checks and currency. These problems increase the Health Science Center's risk of theft. In some cases, the weaknesses may allow losses to go undetected.



The Health Science Center's accounting reconciliations are not adequate to ensure that cash is properly deposited and recorded.

The Health Science Center's reconciliations are not sufficient to ensure that all cash receipts are properly deposited and accounted for. Consequently, the Health Science Center cannot be sure that its financial information is complete and accurate.

The General Accounting Department does not reconcile the Health Science Center's three primary bank accounts in a timely manner and does not resolve differences identified. For example, the bank's outstanding check list for one account was overstated by \$4.1 million as of August 31, 2003.

Two clinics and departments tested did not reconcile their stand-alone accounting systems to the Health Science Center's accounting system. As a result, in one of these departments, we identified \$1 million in transactions that were recorded in the Health Science Center's accounting system but not in the department's system.

Clinics and departments do not have adequate controls to ensure that receivables and revenues are accurately collected and recorded.

Because of inadequate controls over receivables and revenues, financial information generated from the accounting system is not accurate. We identified departments that do not report receivables accurately and completely. In one instance, this caused Student Receivables in the Health Science Center's financial statements for fiscal year 2003 to be understated by at least \$535,000.

In addition, we tested three clinics and found that all three had errors in the amounts charged for services. One of these clinics did not consistently collect required co-payments from patients.

The Health Science Center does not have adequate controls over documenting, approving, and recording employee and petty cash reimbursements.

Our testing of employee and petty cash reimbursements identified state funds that were spent for inappropriate items, such as alcohol, and expenditures that were incorrectly coded, such as food purchases. Forty-six percent of the petty cash vouchers and 31 percent of the expenditure vouchers we tested contained errors such as these.

Health Science Center clinics and departments do not consistently comply with cash management laws and regulations or internal policies and procedures.

Some clinics and departments did not deposit funds in a timely manner, which puts funds at risk of loss or theft. In addition, late deposits represent noncompliance with state laws and Health Science Center policies that are in place to help maximize interest and investment income.

Also, clinics and departments do not always report donations they receive to the Office of Development. Health Science Center policy requires this reporting so that it can comply with University of Texas System policies and tax regulations related to reporting donations. For the six months tested, we identified donations of \$389,000 that had been received by departments but not reported to the Office of Development.

Summary of Management's Response

Management generally agrees with our recommendations.

Summary of Information Technology Review

The Health Science Center has not yet fully implemented access controls for its Financial Management System (FMS), which it began using in September 2003. FMS accumulates and processes all accounting information for the Health Science Center. We also found access and other control issues in the Student Information System (SIS), which processes transactions such as tuition and fee billings for students.

Network security has improved overall since our previous assessment in 2002. However, our scanning identified some unauthorized and inappropriately configured wireless access points. We also found that the Health Science Center could improve its arrangements with the entities it regularly conducts business with (hospitals and libraries) to ensure that security weaknesses at these entities do not compromise the Health Science Center's network.

Our IT work included a review of security controls for FMS. In addition, we performed a limited assessment of controls over SIS and another system called IDX, which is used to handle billings and receivables for the Health Science Center's medical practice plan. Finally, we tested network security and wireless access over the servers on which these systems reside.

Summary of Objectives, Scope, and Methodology

The objectives of the audit were to determine whether (1) controls for receiving, safeguarding, and disbursing cash are adequate; (2) accounting and record-keeping of collections and of state revenues, receipts, and disbursements are accurate and complete; and (3) the Health Science Center complied with cash management laws and policies. We also reviewed safeguards over the information technology resources associated with the areas covered by these objectives.

The scope of this review included the accounting records and transactions for September 1, 2003, through March 31, 2004, and the related review of the fiscal year 2003 financial statements and bank reconciliations.

The audit methodology consisted of interviewing staff and reviewing policies, procedures, and information systems. We tested departments' and clinics' cash receipts, reconciliations, student waivers, refunds and exemptions, employee reimbursements, and petty cash accounts.

Recent SAO Work		
Number	Product Name	Release Date
04-049	An Audit Report on Cash Controls at the University of North Texas	August 2004

Contents

Detailed Results

Chapter 1 Several Clinics and Departments Tested Do Not Have Adequate Controls for Safeguarding Cash	1
Chapter 2 The Health Science Center’s Accounting Reconciliations Are Not Adequate to Ensure That Cash Is Properly Deposited And Recorded	4
Chapter 3 Clinics and Departments Do Not Have Adequate Controls to Ensure Receivables and Revenues Are Accurately Collected and Recorded	9
Chapter 4 The Health Science Center Does Not Have Adequate Controls Over Documenting, Approving, and Recording Employee and Petty Cash Reimbursements	14
Chapter 5 Some Health Science Center Clinics and Departments Did Not Consistently Comply with Cash Management Laws and Regulations or Internal Policies and Procedures	15
Chapter 6 Security Controls for Selected Information Technology Systems Need Improvement	17

Appendix

Objective, Scope, and Methodology	21
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Detailed Results

Chapter 1

Several Clinics and Departments Tested Do Not Have Adequate Controls for Safeguarding Cash

In several clinics and departments we tested, controls were not adequate to safeguard funds from the risk of theft. In some cases, the weaknesses could make it difficult or impossible to detect the losses. Specifically, nine clinics and departments have not adequately separated cash handling duties among employees, and six do not provide adequate physical security for checks and currency.

Chapter 1-A

In at Least Nine Clinics and Departments, Responsibilities for Handling and Processing Cash Are Not Adequately Segregated Among Employees

Nine clinics and departments we evaluated have not adequately segregated cash handling responsibilities.

Seven of the nine clinics and departments allow staff members to perform at least two steps in the cash collection process. The steps in this process include receiving cash, creating receipts, preparing deposits, entering data, and reconciling cash receipts. The possibility of loss through fraud or theft is significantly increased when one person receives, deposits, and records revenues.

Segregation of Duties

Separating duties so that no one employee has the authority to handle all aspects of a transaction is one of the most basic and effective controls for managing assets.

For example, both the Bursar's Office and the Student Accounts department have at least one employee who receives funds, prepares deposits, and records revenue. In addition, they do not require that two individuals be present to verify when cash is removed from the safe, during daily opening or closeout of cash drawers, or when deposits are prepared. During our audit, staff of both departments began implementing procedures to ensure that a second verification occurs on the daily cash counts. Furthermore, Student Accounts staff are allowed to post transactions to the Student Information System (SIS) and reconcile the same information to the Health Science Center's accounting system.

The Harris County Psychiatric Center, the Print Shop, the Mental Sciences Institute, the Dental Branch Clinic, and the Bookstore had similar problems related to the segregation of cash collection duties. These inadequately segregated duties create a risk that employees could commit fraud or theft without being detected.

The Bursar's Office and the Student Accounts and Parking departments share the same "cashiering" area. Ensuring accountability is therefore difficult because employees from each of these departments often perform duties for the others. If discrepancies occur, it may not be possible to determine which employee was responsible.

Two of the nine departments do not adequately segregate duties related to cash disbursements. These duties include initiating payments, granting approvals, recording transactions, and reconciling accounts. For example, we found that in

Student Accounts, one employee processes refunds through SIS and also reconciles refund payments to students' accounts in the system. Furthermore, one employee in the Housing department can prepare and sign checks against Housing's bank account and also either reconciles or supervises the reconciliation of the bank account. These inadequately segregated duties create an opportunity for employees to issue and approve checks for their personal gain.

Recommendation

Health Science Center management should develop, implement, and enforce comprehensive policies and procedures to ensure that departments and clinics:

- Rearrange duties among employees to ensure proper segregation between accepting cash receipts, preparing the deposits, and recording the information in the accounting systems used. When staffing is limited, the clinics and departments should incorporate and document an independent review of cash receipts functions.
- Segregate responsibilities for the preparation and approval of disbursement transactions, including requiring that individuals with the authority to sign checks do not reconcile or approve the reconciliation of the related bank accounts.

Management's Response

In general, UTHSC-H agrees with the auditors' findings and recommendations.

By way of background, we note that the bulk of the auditors' work coincided with the implementation of our PeopleSoft 8.4 enterprise-wide financial management system, which went "live" in September 2003. This is the first new financial information system at UTHSC-H in nearly 20 years.

We note that 90 percent or more of the Health Science Center's annual revenues result from processes not the subject of this audit (i.e., lock-box, wire transfer or other more centralized and automated processes) such as state appropriations; Medicare, Medicaid and managed care payments; and sponsored research support.

The auditors have raised important concerns about cash controls and related matters, and we either have addressed, or are in the process of addressing, these concerns. In addition, we have asked our internal audit department to validate the implementation of all the cash control improvements described in the responses that follow, and to report back to executive management by February 1, 2005. Executive management will, in turn, follow-up with departments and clinics, to ensure that necessary improvements to cash controls have been implemented.

Although a vacancy in the Bursar's Office during the audit period contributed to these segregation of duties issues, we believe that numbered receipts, reconciled daily deposit summaries, pre-employment screening and manager review did mitigate this risk significantly. The recent filling of this vacancy has further addressed these specific segregation of duties concerns.

The Parking department has been relocated from the Bursar's Office space to another floor, and the Loan Collections and cashiering areas have recently been physically separated. An adequate separation will be completed here by December 1, 2004.

Bookstore, Print Shop and certain clinics' segregation of duties issues are being resolved by "local" managers increasing their review and oversight of such matters. These changes will be in effect by December 1, 2004.

Overall, UTHSC-H is undertaking a comprehensive review of policies and procedures regarding separation of duties within departments and clinics. This review will be completed, and changes implemented and enforced, by February 1, 2005.

Chapter 1-B

Physical Security Is Not Adequate to Safeguard Cash in at Least Six Clinics and Departments

Six of the clinics and departments we evaluated had inadequate physical security for safeguarding cash. Without adequate physical security for safeguarding checks and currency, the Health Science Center's funds are at risk of theft. The most significant examples were in the three departments that share the same cashiering area: the Bursar's Office, Student Accounts, and Parking. In our observations of clinics and departments, we found that:

- Funds are kept in unlocked cash drawers, and checks held for pick-up by students or staff are accessible to all staff working in or passing through the shared cashiering area.
- The Bursar's Office's safe is used for overnight storage of deposits and other cash items for a number of departments. Departmental deposits stored in the safe overnight are not counted to verify the amounts held. Furthermore, funds stored in the safe for the Bursar's Office, Student Accounts, Parking, and the Registrar's Office are not stored in individually secured bags to keep funds from being inadvertently mixed together.
- Departments carrying cash and checks to the Bursar's Office for deposit do not transport the items in a secure manner, such as in a locked bag. The departmental deposits of cash and checks are left on a desk in the Bursar's Office for the individual who later prepares the institution's deposit. This desk is accessible to all staff working in or passing through the cashiering area.

Recommendation

Health Science Center management should develop, implement, and enforce comprehensive policies and procedures to ensure that departments and clinics:

- Establish a secure environment for the storage of checks and currency, including measures to prevent unauthorized access to funds.
- Ensure that deposits are transferred in a secure manner.

Management's Response

In general, UTHSC-H agrees with this audit finding and related recommendations. As noted above, we have recently relocated Parking from the Bursar's Office and Student Accounts areas. Thus, the number of personnel with access to this area has declined from 14 to six.

Bursar's and Student Accounts' offices are within an electronic identification card, access-controlled area. During this audit, we did install an access-controlled door between the Bursar's and Student Accounts areas, to further secure this area.

We have begun the process of "bagging" and identifying the funds of different departments (i.e., Bursar's, Student Accounts', Registrar's) within the area's safe. This will be completed by November 1, 2004.

Some clinics, departments and other personnel do carry cash and checks to the Bursar's Office in containers other than locked bags. We have initiated a training and communication effort, to remind personnel to use more secure methods of containing and delivering cash and checks to the Bursar's Office. This effort will be completed by December 1, 2004.

Overall, UTHSC-H is undertaking a comprehensive review of policies and procedures regarding physical security for safeguarding cash within departments and clinics. This review will be completed, and changes implemented and enforced, by February 1, 2005.

Chapter 2

The Health Science Center's Accounting Reconciliations Are Not Adequate to Ensure that Cash Is Properly Deposited and Recorded

The Health Science Center's accounting reconciliations are not sufficient to ensure that all cash receipts are properly deposited and accounted for. At the Health Science Center, the most significant reconciliations occur at two levels:

- The General Accounting Department is responsible for reconciling the deposits recorded in the general ledger to the bank statements for the Health Science Center's three primary bank accounts. (The general ledger is a record of all the financial accounts for an entity.)
- Individual departments and clinics are responsible for reconciling their detailed financial data, which is often recorded in a stand-alone information system, with (1) their source documents, such as deposit logs, and (2) the information posted to the Health Science Center's general ledger.

However, our testing of reconciliations identified several weaknesses, such as the failure to complete a timely resolution of differences between amounts recorded in the general ledger and the bank statement or departmental information systems. Consequently, the Health Science Center cannot be sure that its financial information is complete and accurate.

The General Accounting Department Does Not Perform Complete and Timely Bank Reconciliations

General Accounting does not perform adequate reconciliations of the Health Science

Why Are Bank Reconciliations Important?

Complete and timely bank reconciliations provide assurance that all cash receipts have been properly deposited into bank accounts and properly recorded in the accounting records. They also help to identify transactions used to conceal fraud or theft, especially counterfeit and altered checks.

Center's accounting information with bank statements. Timely resolution of any problems is critical due to the large amount of cash flowing through the Health Science Center's three primary accounts. For example, in May 2004, transactions totaling approximately \$88.7 million flowed through these bank accounts.

As of August 31, 2003, the bank's outstanding check list for the Health Science Center's Demand Account was overstated by \$4.1 million. There was a \$4.1 million difference between the Health Science Center's "positive pay list," which is provided to the bank to identify all checks issued and approved for payment, and the

Health Science Center's general ledger as of August 31, 2003. The Health Science Center canceled 1,200 checks from its general ledger but failed to do so on the positive pay list. When used properly, the positive pay list is an effective means to help protect the Health Science Center from fraud. For example, if someone tries to cash a check that does not match an entry on the positive pay list, the bank will not honor it. As a result, this overstated positive pay list creates the following problems for the Health Science Center:

- The bank will cash checks listed on the positive pay list. The Health Science Center has canceled checks within its accounting system, but it has not canceled the same checks on the positive pay list. By having these canceled checks on the positive pay list, the Health Science Center decreases the usefulness of the list as a fraud prevention tool. It creates an opportunity for someone with knowledge of which checks have been canceled in the general ledger to create a fraudulent check that matches one on the positive pay list.
- These 1,200 checks that are still on the positive pay list increase the complexity of and time required to complete bank reconciliations because staff must first verify the check list each month to ensure that those checks have not been cashed in error. Then, they must monitor the addition of new checks to the list.
- Bank reconciliations are the only control point to identify cases where the bank erroneously cashes a check that was not on the positive pay list. If General Accounting does not identify these and fails to notify the bank in a timely manner, the Health Science Center may not be able to hold the bank liable for the loss of funds.

General Accounting does not perform bank reconciliations in a timely manner. As of March 11, 2004, the latest reconciliations for two of the three primary bank accounts were for the month ending August 31, 2003, and the latest reconciliation for the third primary account was for the month ending September 30, 2003. As a result, the Health Science Center does not have an accurate assessment of the availability and usage of funds it manages and cannot safeguard itself against undetected fraud. Furthermore, departments and clinics do not receive timely feedback on issues that affect their accounts and may not be able to detect the failure to deposit funds or incorrect postings to accounts.

A reconciliation for one of these accounts was prepared and dated on February 29, 2004, and approved by the General Accounting supervisor on April 12, 2004. However, the reconciliation identified numerous discrepancies that General Accounting did not resolve. Consequently, we were unable to determine whether the reconciliation was materially accurate and complete.

Reconciliations of the credit card merchant account do not ensure that the Health Science Center receives timely and complete payments for all credit card transactions. The credit card merchant account contains deposits from credit card companies for payments made to the Health Science Center. We identified a large number of unmatched transactions between the Health Science Center's general ledger and the bank's credit card merchant account. The dollar amounts and the large number of unmatched transactions increase the risk that errors made by the bank, the credit card merchants, or the Health Science Center will go undetected for extended periods of time.

For example, we identified the following problems with the account:

- Of the transactions that occurred between August 1, 2003, and March 31, 2004, approximately 27.5 percent were listed either in the general ledger or on the bank statements but not both. These transactions totaled approximately \$2 million.
- For the credit card merchant account, the general ledger reflected nearly \$65,000 more than the bank account's cash balance as of August 31, 2003. According to the Health Science Center, this difference has accumulated over several years.
- As of March 31, 2004, the Health Science Center had not recorded approximately \$24,000 in credit card service fees, which the credit card companies had deducted from the bank account. Therefore, cash is overstated and expenses are understated by this amount in the general ledger.
- Credit card terminals in several departments were not closed out each business day, and credit card payments in some departments were not recorded in FMS for up to three weeks. This not only causes delayed receipts to the Health Science Center but also makes matching a transaction to the corresponding entry in the general ledger difficult at a later date.

Recommendations

General Accounting should immediately complete all reconciliations of Health Science Center bank accounts. All differences should be fully investigated and corrected.

Health Science Center management should:

- Develop, implement, and enforce comprehensive policies and procedures to ensure that General Accounting researches and resolves all reconciling items to make the bank reconciliations an effective control. Resolution of the reconciling items should include identifying the cause and correcting any related procedural or system problems.

- Reiterate to departments the policy for credit card terminal close-out and recording in the general ledger, and periodically review departmental deposit documentation to determine whether departments are adhering to this policy.

Management's Response

While UTHSC-H agrees, in general, with most of the auditors' findings and recommendations in this area, we believe several points require clarification.

Regarding the \$4.1 million of outstanding checks in our demand account:

- *No misstatement of cash resulted from these checks remaining on the bank's positive pay list (i.e., they did not affect the reported, August 31, 2003 cash balance).*
- *None of these 1,200 checks have cleared the bank.*

We agree that this matter does contribute to additional, unnecessary complexity in the performance of bank reconciliations. The greater security and assurance afforded by removing these checks from the bank's positive pay list is desirable and is in process.

Effective immediately, the Financial Administrative Team will enter all stop payments directly into the CheckMate system, which will process a reversal on the positive pay file ensuring that such checks will not be cashed and will not appear as outstanding on the monthly report from our bank.

We agree with the comments about timeliness of bank reconciliations and note that we are current with reconciliations as of the August 31, 2004 fiscal year-end date.

We further note that no significant or unusual adjustments resulted from our completion of these delayed reconciliations. We will remain current with these reconciliations going forward.

Regarding the credit card merchant account, we have reconciled the differences noted to just under \$21,000 as of the date of this response and will reduce this further by December 1, 2004.

We have resolved the nearly \$65,000 of older, ledger-to-bank differences noted by the auditors.

All credit card service fees have been recorded in the general ledger as of August 31, 2004 and will be recorded on a monthly basis in the future.

We agree that regularly used credit card terminals should be closed out daily. We will reiterate to departments the policy for credit card terminal close-outs. This will be accomplished by December 1, 2004.

Not All Clinics and Departments Reconcile Their Financial Information to the Health Science Center's Accounting System

Three of the clinics and departments we evaluated do not perform accurate and timely reconciliations of their individual accounting systems to the Health Science Center's accounting system. Reconciliations help clinics and departments ensure that all revenue and cash receipts recorded in their stand-alone systems are properly recorded in the Health Science Center's accounting system.

For example, the Office of Development (Development) did not detect improperly recorded donor transactions because it failed to reconcile its system to the Health Science Center's accounting system. For 43 percent of the Development accounts we tested, the amounts recorded in Development's internal system differed from the amounts recorded in the Health Science Center's accounting system. Transactions totaling \$1 million in the Health Science Center's accounting system for these accounts could not be traced to the Development system. Conversely, transactions totaling approximately \$736,000 recorded in the Development system could not be identified in the Health Science Center's system.

Based on our expanded testing and analysis of the total receipts recorded in Development's system and total deposits recorded in the Health Science Center's system, it does not appear that funds were misappropriated. However, failure to properly reconcile these accounts on a regular basis increases the risk that fraud may be committed and not detected. Additionally, the incorrect postings make it difficult for the Health Science Center to ensure that it has met its obligations to donors.

Some of the differences we noted were related to donations that other departments in the Health Science Center received and posted to Development accounts in the Health Science Center's accounting system without notifying Development. Consequently, donations were not recorded in Development's system. Because Development did not reconcile its accounts in the Health Science Center's accounting system, it was not aware that these departments were not adhering to the Health Science Center's policy for the acceptance of donations (see Chapter 5).

Our testing of other areas' reconciliations identified other weaknesses:

- Student Accounts does not have documentation to show that student accounts receivable amounts reported in SIS were reconciled to the Health Science Center's accounting system as of the end of fiscal year 2003.
- The Harris County Psychiatric Center does not always resolve the differences it identifies through its reconciliations.
- The Dental Branch clinic does not have documented procedures for reconciling its system to the Health Science Center's accounting system.

Recommendations

Development should completely reconcile all gift accounts in its internal accounting system to the Health Science Center's general ledger. All differences should be fully investigated and corrected.

Health Science Center management should develop, implement, and enforce comprehensive policies and procedures to ensure that departments and clinics:

- Perform timely reconciliations of their internal systems to the Health Science Center's accounting system and make any necessary adjustments.
- Perform a supervisory-level review and approval of these reconciliations.

Management's Response

In general, UTHSC-H agrees with the auditors' comments and related findings.

The Development Office has begun reconciliations of its records to the Health Science Center's, effective October 1, 2004. Also by this date, Development has ensured that all checks are deposited within three days of receipt. By November 1, 2004, Development will send out an institution-wide communication, reminding departments and operating units of the institutional policy that all gifts must be processed through the Development Office.

The Student Accounts, Dental Branch and HCPC areas agree that their documentation of reconciliation process can be improved, and have all committed to do so by December 1, 2004.

Overall, UTHSC-H is undertaking a comprehensive review of policies and procedures regarding reconciliations within departments and clinics. This review will be completed, and changes implemented and enforced, by February 1, 2005 and will include more central oversight and assurance as to timeliness and completeness of reconciliations.

Chapter 3

Clinics and Departments Do Not Have Adequate Controls to Ensure that Receivables and Revenues Are Accurately Collected and Recorded

Because of inadequate controls over receivables and revenues, financial information generated from the accounting system is not accurate. Specifically, four departments tested did not report receivables accurately and completely. In addition, all three clinics at which we tested revenue collections had errors. These errors included charging patients the wrong amount for the services provided and not consistently collecting required co-payments. The types and number of errors that we found during the tests of these clinics may indicate that the organization does not have

adequate policies and procedures to ensure the accurate collection and recording of revenue.

Chapter 3-A

At Least Four Departments Do Not Consistently Report Accurate Amounts for Receivables

Four of the departments that we reviewed do not consistently report complete information from their individual systems to the Health Science Center's accounting system. For example, Student Accounts reports the total amount of tuition and fees

Receivables

Receivables represent amounts owed but not yet paid to an entity for goods and services it has provided.

owed by sponsored students. (Sponsored students are those whose tuition and fees are paid by a third party such as a corporation or the military.) A receivable is recorded in the accounting system as soon as notification of the sponsorship is received. However, Student Accounts does not report the total amount of tuition and fees owed by non-sponsored students into the accounting system. Instead, it reports only the revenues for amounts students have actually paid; it does not report receivables for amounts still owed.

The Financial Reporting Department uses the accounting system and additional information from the clinics and departments to prepare the Health Science Center's financial statements. Because of incomplete and inaccurate information, the fiscal year 2003 financial statements contained the following errors:

- The \$1.4 million balance reported for Student Receivables was incorrect because it did not include amounts owed by non-sponsored students, resulting in an understatement of at least \$535,000.
- The Allowance for Doubtful Accounts in Loans and Contracts was reported as \$0 when it should have been approximately \$594,000. This amount includes loans that were past due by at least a year; some were more than 10 years past due.
- Current Assets was overstated by \$10.4 million because it included student loans that did not come due within the next fiscal year. These loans should have been classified as Non-Current Assets.
- The balance listed for Loans and Contracts did not match the contracted collection agency's end-of-year balance. The difference between the two was approximately \$9,600.

The Health Science Center's financial information is incorporated into the Annual Financial Report (AFR) of the University of Texas System (System). Therefore, these misstatements resulted in the misstatement of the System AFR for fiscal year 2003. However, because of the magnitude of the System AFR, which incorporates all University of Texas institutions, it is unlikely that the statements were misleading.

Additionally, we noted other issues with student accounts receivables:

- Student Accounts does not evaluate how long receivable balances have existed to determine which accounts to write off.

- Student Accounts does not monitor how payments of tuition and fees are applied to sponsored accounts. For example, payments on past due balances may be applied to current balances.

We also noted that the Bookstore did not report its receivable balances of approximately \$7,300 to the Health Science Center's accounting system. In addition, Print Shop receivable balances of nearly \$40,000 were past due by more than 150 days. Our testing also identified two customers to whom the Print Shop continued to extend credit although their accounts were delinquent.

Furthermore, the Health Science Center does not have an adequate process for monitoring the collection of non-sufficient funds (NSF) checks. The clinic or department that accepts the check is responsible for collection efforts, which it may or may not pursue. For example, the Bookstore's records show 21 outstanding returned checks worth \$3,700 that date as far back as 1996. The delay in collection increases the risk that the Health Science Center will never get paid for the associated goods or services. In addition, the Health Science Center does not have a system in place to track individuals who submit NSF checks. As a result, departments may continue to accept checks from individuals with previous NSF checks.

Recommendations

Health Science Center management should:

- Develop, document, and implement comprehensive policies and procedures to govern clinics' and departments' management and reporting of all accounts receivable.
- Ensure that all accounts receivable and their related allowance for doubtful accounts include appropriate amounts that are accurately classified and reported in the accounting system and on the financial statements.
- Ensure that the balance in the general ledger for Loans and Contracts agrees with the balance listed in the contracted collection agency's records.
- Analyze accounts receivable to determine how long these balances have existed, write off uncollectible balances, and ensure that customers with delinquent accounts are not extended credit.
- Monitor payments received to ensure correct application to accounts.
- Review the effectiveness of its collection policies and procedures.
- Establish centralized monitoring, collection, and tracking of NSF checks, and document policies and procedures relating to writing off NSF checks that are not collectible.

Management's Response

In general, UTHSC-H agrees with this audit finding and related recommendations.

We agree that at August 31, 2003, the Student Receivable balance was understated by approximately \$535,000. Non-sponsored student tuition was, in effect, recognized through the year on an "as received," cash basis, instead of an accrual basis. We note that tuition and fees are less than 2% of total revenues at UTHSC-H.

We agree also that the Allowance for Doubtful Accounts in Loans and Contracts was understated by approximately \$594,000 at August 31, 2003. Thus, this receivable balance was overstated (though cash balances were unaffected).

Both of these account balances have been corrected and are now being maintained on an accrual basis. We have instituted a review of Student Accounts financial information by Finance personnel, effective October 1, 2004.

We agree that UTHSC-H's Current Assets were overstated by \$10.4 million, due to the inclusion of loans not due for more than one year (Non-current Assets were thus understated by the same amount). We note that this did not affect cash balances and had no "income statement" impact on UTHSC-H's financial statements.

Effective November 1, 2004, Student Accounts will utilize agings of receivables as a part of account write-off determination. Additionally, Student Accounts is monitoring the application of tuition and fee payments to sponsored accounts.

The Bookstore does not accrue small dollar accounts receivable. These amounts do not have a material effect on the Health Science Center's financial statements (i.e., cash basis accounting is acceptable, for smaller dollar activities).

The Print Shop's past due receivable balances noted by the auditors resulted from billing issues with these customers, not customer's failure to pay. These receivables have subsequently been resolved and collected.

It is true that Bookstore staff did accept a second check from an individual a year after an earlier NSF check. This is the only such occurrence (i.e., accepting an individual's check after a previous NSF check) at the Bookstore in more than a decade.

The Bookstore's new WinPrism point of sales/inventory system now tracks NSF checks and prompts personnel – before accepting a check – when "prior offenders" are noted. This system was implemented in August 2004.

Overall, UTHSC-H is undertaking a comprehensive review of policies and procedures regarding reporting of receivables within departments and clinics. This review will be completed, and changes implemented and enforced, by February 1, 2005.

At Least Three Clinics Had Errors in the Amounts They Charged for Services

We tested revenues and cash collections at three medical clinics and found errors at all three. We selected the clinic that collected the most cash, the clinic that had the largest number of cash transactions, and one clinic that did not use the Health Science Center's automated billing system. Our testing identified the following:

Revenues

Revenues are funds received in exchange for goods, services, or other benefit. For the Health Science Center, they include tuition and fees, payments for medical services, and donations.

- When we compared a random sample of appointment documentation (encounter forms) with the billing system, we identified two clinics that charged patients the wrong amount for the services provided (such as charging for a 15-minute appointment when they should have charged for a 30-minute appointment). While the number of transactions in error was small, when we project error rates of incorrect charges made to total activity for the two clinics identified, we estimate that approximately \$50,000 in billing errors occurred during the five months we tested.
- A third clinic did not consistently require that patients make the required co-payments, and they did not have a uniform and documented policy for forgiving these payments. Again, the number of transactions in error was small, but when we project the error rate, we estimate that the clinic failed to collect approximately \$8,000 during the five months tested. This clinic also used the wrong rate to charge for a particular service, resulting in the loss of \$2,856 in revenues.

Recommendations

Health Science Center management should ensure that clinics:

- Provide training for staff to ensure that procedure codes for services provided are accurately recorded and that the related charges collected are correct.
- Develop, implement, and enforce comprehensive policies and procedures for collection or forgiveness of co-payments.

Management's Response

In general, UTHSC-H agrees with this audit finding and related recommendations. We note that the error rate in one of the clinics under audit was approximately 1%. Also, the extrapolated "\$50,000 in billing errors" could be misunderstood: Given significant differences between gross (or "list") prices billed and net collectible amounts typically found in healthcare, plus the significant indigent care we provide (more than \$160 million, on a revenue basis, in FY 2004), actual collectible revenue involved here would be much less than \$50,000.

The Health Science Center is in the midst of a major initiative to improve collections of co-pays at clinic locations. Policy and procedure enhancement is a major part of

this undertaking. New policies in this area will be completed and published by December 1, 2004.

Chapter 4

The Health Science Center Does Not Have Adequate Controls over Documenting, Approving, and Recording Employee and Petty Cash Reimbursements

The Health Science Center does not have adequate controls for documenting, approving, and recording disbursements relating to employee and petty cash reimbursements. As a result, the Health Science Center (1) does not identify inappropriate purchases and (2) does not have correct information regarding the amount spent on particular types of goods and services.

Disbursements

Disbursements are any funds paid out. The Health Science Center's disbursements include refunds, student loans, employee reimbursements, payroll, and payments for goods and services.

The Health Science Center's automated process for making disbursements relies on the initiating department's on-line approval of the expenditure for accuracy and appropriateness. However, our testing of the initial sample of 35 petty cash fund reimbursement vouchers, reimbursing nearly \$86,000, revealed that 46 percent of the vouchers had errors including misclassified expenses, inappropriate use of funds, and incomplete documentation justifying either the amounts reimbursed or the use of state funds. Based on these results, we expanded our testing to include approximately \$13,000 in reimbursement transactions and found similar errors in 33 percent of the additional transactions tested.

In a statistically random sample of 74 employee reimbursement vouchers, 31 percent had the same type of errors as those identified in petty cash testing. Projecting this overall error rate to the total population of employee reimbursement vouchers, we estimate that approximately \$230,000 in processing errors occurred during the period we reviewed.

Misclassified expenses in both employee and petty cash reimbursements included food purchases, gift items, registration fees, travel related expenses, research study participant payments, and sales taxes. Incorrect expense codes can lead to misstated financial statements and unreliable information for administrative decision making. Furthermore, incorrect expense codes can be used to hide deliberate misuse of funds.

The inappropriate use of funds in both employee and petty cash reimbursements included awards and travel expenses in excess of allowable state rates and two purchases of alcohol with state funds. However, our test results did not identify any indications of fraud.

Recommendation

Health Science Center management should develop, implement, and enforce comprehensive policies and procedures to ensure that staff members performing data entry and individuals reviewing and approving expenditure vouchers are trained and have knowledge of account coding requirements and the appropriate use of funds.

Management's Response

In general, UTHSC-H agrees with this audit finding and related recommendations.

We note that, in the auditors' employee reimbursement testing, actual overpayments identified totaled just under \$36 (and were for hotel tax for in-state lodging). All other errors were miscodings (e.g., using the wrong expense category) or similar errors, which did not affect the total amount of cash disbursed.

All of these miscodings were corrected during FY 2004.

Overall, UTHSC-H is undertaking a comprehensive review of policies and procedures to ensure that personnel performing data entry or reviewing and approving expenditures are adequately trained. This review will be completed, and changes implemented and enforced, by February 1, 2005.

Chapter 5

Some Health Science Center Clinics and Departments Did Not Consistently Comply with Cash Management Laws and Regulations or Internal Policies and Procedures

Some of the Health Science Center's clinics and departments that we reviewed did not consistently comply with state laws and regulations or internal policies and procedures relating to depositing cash receipts in a timely manner, notifying Development of gifts received, and making use of funds available in petty cash accounts.

Timely Deposit Criteria

The Texas Education Code states that funds for deposit must be deposited within seven days from the date of collection (Title III, Section 51.003[b]). The Health Science Center's policies require departments to deposit cash with the Bursar's Office within 24 hours of receipt (Section 11.10).

Some departments and clinics did not deposit funds in a timely manner. For example, a deposit made by the Bursar's Office in December 2003 contained numerous checks that were at least 30 days old at the time of deposit. The Bursar's Office makes deposits for most of the Health Science Center's other departments, such as the Print Shop, the Pediatrics Clinic, and the Dental Branch. One check included in the above deposit from the Dental Branch was more than 60 days old. We also identified \$196,000 in delayed deposits from Development. As a result, funds are at risk of loss or theft, and cash is not available for use as quickly as it could be. In addition, late deposits represent noncompliance with state laws (see text box) that are in place to help ensure that the State and its institutions maximize available interest or investment income.

Development was not notified of gifts received. In our review of 71 Development accounts, we found that other departments had deposited approximately \$389,000 in contributions without notifying Development. According to Health Science Center policy, all gifts should be reported to Development within 24 hours of receipt.

Contributions to the Health Science Center provided approximately \$7 million in operating funds during fiscal year 2003. In order to maintain good relationships with donors, honor commitments to donors, and comply with tax regulations related to

reporting contributions and with University of Texas System requirements for reporting donations, Development must have timely knowledge of all gifts.

Some departments and clinics do not make use of their available petty cash funds. Thirty-one of 62 petty cash accounts tested had no activity from September 2003 through February 2004, representing more than \$40,000 in idle funds. These 31 accounts included the Harris County Psychiatric Center and the Housing department. Furthermore, only three of the accounts met the Health Science Center's policy recommendation of being replenished every two to three weeks. By maintaining idle fund balances, the Health Science Center increases its exposure to the inherent risks associated with petty cash accounts, such as fraud and theft of funds.

Recommendations

Health Science Center management should:

- Develop, implement, and enforce comprehensive policies and procedures to ensure that departments and clinics:
 - ♦ Deposit all cash receipts in the appropriate bank accounts within seven days as required by the Texas Education Code and, where applicable, ensure that clinics and departments provide deposits to the Bursar's Office within 24 hours as required by Health Science Center policy.
 - ♦ Forward all gifts to Development promptly so that they can be properly acknowledged and reported.
- Review petty cash accounts to determine whether accounts with little or no activity can be closed.

Management's Response

In general, UTHSC-H agrees with this audit finding and related recommendations. We understand that the auditors used the "issue date" printed on the check (or 30 days thereafter) if the receipt date was not available when assessing the "age" of a check. We know that some vendors and other payers "hold" checks or otherwise delay their issuance (occasionally, even beyond 30 days).

Some checks are sent to the wrong address within the Health Science Center. Sometimes, faculty receive checks directly, for sponsored program, philanthropic, or other purposes. All of these factors can contribute to delays in check depositing.

We have communicated to appropriate staff the importance of depositing checks within seven days of receipt. Broader communication will occur by November 1, 2004.

Overall, UTHSC-H is undertaking a comprehensive review of policies and procedures with respect to cash management. This review will be completed, and changes implemented and enforced, by February 1, 2005.

We agree with the recommendation regarding the need to notify the Development Office about all philanthropic gifts and contributions. We will remind all staff about this issue as well.

We agree that inactive petty cash funds should be closed. This will be completed by December 1, 2004.

Chapter 6

Security Controls for Selected Information Technology Systems Need Improvement

The Health Science Center has not yet fully implemented access controls for FMS, which accumulates and processes all accounting information for the Health Science Center. We also found access and other control issues in the Health Science Center's Student Information System (SIS), which is used to process billing for student tuition and fees. Although network security has improved overall since our previous assessment in 2002, we identified some network vulnerabilities that should be addressed.

Access controls for FMS have not yet been fully implemented. The Health Science Center implemented FMS as its new accounting system beginning in September 2003. However, it has not yet fully implemented the new system's available access controls, and there are other areas in which improvements can be made to better protect the FMS application and the financial information that it processes. Because FMS is the central accounting system that accumulates and processes financial information for the Health Science Center, its security is critical to ensure that this financial information is protected from unauthorized or inadvertent access, manipulation, or loss. We found the following:

- FMS servers are not located in the most protected segment of the network. In their current network location, the servers that host the FMS application and its supporting database can be accessed from any computer on the network. The most protected segment of the network allows access from only specific computers and would be a more secure location for the FMS servers. According to the Health Science Center, it plans to relocate the FMS servers to the most secure location as soon as all phases of the FMS implementation processes are complete.
- There are two system and two database administrators for FMS, and these four individuals have high levels of access to both the FMS application and its supporting database. With high levels of access to both the FMS application and the database, these individuals could process an inappropriate transaction or make a change to data and eliminate all traces of those actions in both the application and the database.
- The two database administrators also share the same administrator account and password access to the FMS database. Because they share this account, the Health Science Center would not be able to hold a specific individual accountable for making inappropriate changes in the database because it is not

possible to tell which employee was using the account when a particular change was made.

- The Health Science Center does not have a process for removing inactive FMS accounts. Our tests indicated that as of May 2004, 111 FMS user accounts had never been accessed by the owner and an additional 30 had not been accessed for more than 120 days. Inactive accounts provide opportunities for unauthorized users to access FMS without detection.

The process for updating SIS as well as access controls could be improved. Employees in the Registrar's Office update the SIS database tables while the application is processing, which may cause processing errors and out-of-balance student accounts. In addition, making changes directly to the active (production) tables without first validating and testing them increases the risk that unauthorized or incorrect changes could be made. The accuracy of these tables is critical because they contain the tuition and fee information used to calculate what students owe. If there are errors, the Health Science Center may charge students the wrong amounts for tuition and fees. Such changes should be made in a test environment where they can be validated and approved before they are applied to the production environment. Registrar's Office staff members also share the same account and password when they make changes to the SIS tuition and fee tables. Because they share this account, the Health Science Center would not be able to hold a specific individual accountable for making inappropriate changes in the database because it is not possible to tell which employee was using the account when a particular change was made.

Although network security has improved, we identified some vulnerabilities to internal and external threats. The Health Science Center's network security has improved since our 2002 assessment. However, we identified the following areas where improvements can be made:

- The Health Science Center has granted seven entities with which it regularly conducts business (such as hospitals and libraries) direct access to its network. Although the Health Science Center has installed firewalls to control traffic between its network and the other entities' networks, it has not fully configured the firewalls to protect its network from weaknesses in the systems of these seven entities. This situation creates a risk of unauthorized access or disruption to the Health Science Center's network.
- Our network scans detected seven unauthorized and inappropriately configured wireless access points on the Health Science Center's network. Wireless access points are common targets of hackers, and unauthorized and inappropriately configured access points could provide a means to gain unauthorized access to the Health Science Center's network.

Recommendation

Health Science Center management should develop, implement, and enforce comprehensive policies and procedures to:

- Relocate the FMS database servers to the most protected area of the network.
- Separate system administration duties to provide control and accountability over the FMS application and its supporting database. If separation of duties is not practical, Health Science Center management should implement regular supervisory reviews of audit logs and changes to the application and the database made by the administrators.
- Ensure that system administrators and other individuals who are authorized to make changes to FMS and SIS each have and use their own accounts and passwords for system access, and establish the accounts so that they allow employees only the level of access required to perform their jobs.
- Disable FMS accounts after a predefined period of inactivity.
- Ensure that updates to SIS follow an approved change management procedure.
- Configure business partner firewalls to allow only authorized traffic access to the network.
- Regularly scan or search for unauthorized or inappropriately configured access points and either disable them or configure them appropriately.

Management's Response

The FMS database servers were not, initially, located to Zone 100. This decision was made in order to minimize potential disruption during the implementation and early production while new users were getting accustomed to the system and hardware was changing. However, we agree that the database servers need to be moved. This will occur by February 1, 2005.

The Health Science Center has two database administrators and two PeopleSoft System Administrators to support its entire HRMS and FMS application portfolio. UTHSC-H will perform a quarterly review of production application logs to identify inappropriate activities. Both the state and our internal auditors have indicated that they will assist us in determining what logs/activity will be appropriate for review. This will be completed by December 1, 2004.

The system administrators are required by PeopleSoft to utilize a particular schema ID to make database structure changes. However, individual application and database accounts have now been created for daily FMS support.

SIS production accounts, not associated with an individual, have been used for testing. The Registrar's Office will identify these accounts and request that they be deleted. This will occur by November 1, 2004.

The Registrar's Office no longer shares a password to update tables on the web-based system. Individuals now have their own passwords. All access to the web-based tables will be removed by October 1, 2004 with the implementation of mainframe downloads of table data.

A quarterly procedure to identify and remove FMS accounts with no activity for three months will be implemented by January 1, 2005.

Updates to the tuition and assessment tables in the mainframe-based SIS should be restricted to only fully tested modifications. The Registrar will remove access to these production tables and require that subsequent table changes be fully tested and signed off before asking the SIS support team to move the tables into production. This will be completed by November 1, 2004.

Access to the student and financial data residing in the web-based system will be removed with the implementation of the next phase of improvements to this system (i.e., by October 1, 2004).

Since the audit, the business partner firewalls have been reconfigured to allow only authorized traffic into the UT-H network.

Since the audit, IT Security has begun regularly scanning the network for unauthorized access points. In addition, IT Security has purchased a new wireless security hardware monitoring suite to automate the process.

Appendix

Objectives, Scope, and Methodology

Objectives

The project objectives were to determine the following:

- Whether the University of Texas Health Science Center at Houston (Health Science Center) has adequate controls for receiving, safeguarding, and disbursing cash.
- Whether the accounting and record-keeping of collections and of state revenues, receipts, and disbursements at the Health Science Center are accurate and complete.
- Whether the Health Science Center complied with state laws and regulations and its own and University of Texas System policies related to cash management.

We also reviewed the Health Science Center's safeguards over the information technology resources associated with the areas covered by these objectives.

Scope

The scope of this review included the accounting records and transactions for September 1, 2003, through March 31, 2004, and a related review of the fiscal year 2003 financial statements and bank reconciliations. We evaluated the following clinics and departments:

- Dental Branch
- Harris County Psychiatric Center
- Medical Services and Research Development Plan
 - ♦ Dermatology
 - ♦ General Pediatrics
 - ♦ Mental Sciences Institute
- Bookstore
- Bursar's Office
- Cash Management
- Employee Reimbursements
- General Accounting
- Housing
- Office of Development
- Parking
- Print Shop
- Procurement and Accounts Payable
- Registrar's Office

- Student Accounts
- Student Loan Collections

Methodology

To achieve these objectives, we:

- Interviewed Health Science Center managers and staff.
- Reviewed Health Science Center policies and procedures.
- Reviewed information systems used to collect and report financial information.
- Conducted Internet Security Scanner and wireless scans to validate the status of corrective actions and to assess the current state of network security for Health Science Center financial systems.
- Reviewed the Health Science Center's fiscal year 2003 financial statements.
- Reviewed bank statement reconciliations prepared as of August 31, 2003.
- Tested a statistically random sample of 35 student transaction detail records from the Student Information System (SIS) from September 1, 2003, through January 31, 2004, for appropriate assignment and payment of tuition and fees.
- Tested a statistically random sample of 35 student transaction detail records from SIS from September 1, 2003, through January 31, 2004, for refunds, waivers, and exemptions applied to student assessments of tuition and fees.
- Tested a statistically random sample of 74 employee reimbursement vouchers from the Financial Management System (FMS) from September 1, 2003, through January 31, 2004, to determine whether Health Science Center controls ensured that employee reimbursements were compliant with limitations on the source and use of funds, recorded in the appropriate accounts, adequately supported, approved, reasonable, mathematically accurate, and recorded within a reasonable timeframe.
- Tested a judgmental sample of 43 petty cash transactions based on the nature of expenditure coding that appeared to contradict established policy or that may have been coded incorrectly.
- Tested a judgmental sample of 35 petty cash vouchers to determine the appropriateness of using petty cash funds, whether vouchers were supported by adequate documentation, whether they had authorized approval, and the appropriate use of funds and coding.
- Tested a statistically random sample of 80 medical record numbers for time-of-service payments and services billed at each of the Dermatology and Pediatrics clinics, and tested a statistically random sample of 73 medical record numbers at the Mental Sciences Institute.
- Tested departmental cash receipts and account reconciliations for the period of September 1, 2003, through February 29, 2004.

- Tested student refunds for the period of September 1, 2003, through February 29, 2004.
- Tested a judgmental sample of 4 and a statistically random sample of 71 Development accounts for the period of September 1, 2003, through February 29, 2004.

Project Information

We conducted fieldwork between April and July 2004. This review was conducted in accordance with standards applicable to performance audits contained in generally accepted government auditing standards.

The following members of the State Auditor's Office's staff conducted the review:

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The Honorable Brian McCall, House Ways and Means Committee

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