Office of the Inspector General

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Review of Suspicious Indicators at South Carolina State University Foundations

Case #2014-637 I

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I. Executive Summary

This State Inspector General (SIG) review was predicated on suspicious indicators at the Advancement Foundation (AF) raised in South Carolina State University's (SCSU) 2012 and 2013 Comprehensive Annual Financial Reports (CAFR). This led to a review of AF's financial records, which surfaced the issue of an inappropriate practice of funding the AF with revenues and rebates from SCSU vendor contracts. This funding mechanism was established in 2005 with a Memorandum of Understanding between the AF and SCSU where "certain non-state revenues, which are generated on the campus of SCSU, should be transferred to the AF." This 2005 rationale was flawed. The "non-state revenue" came directly from contracts between SCSU and its vendors for services, and thus any rebate, commission, or revenue is consideration due to SCSU, a state agency, and not a related foundation. This practice of diverting state funds, generally termed rebates, to foundations is inappropriate and needs to cease. Both the Budget and Control Board, Procurement Services Division and the SCSU President concur with this analysis.

A review of the period 2010-2013 determined SCSU's five major vendors, according to SCSU records, provided rebates of $11,131,389 during the period. Reconciliation of records to date revealed $8,831,872 (79%) and $2,299,517 (21%) were received during this period by SCSU and SCSU foundations, respectively. The foundations used the funds for salary supplements, travel, consultants, vendors, flowers, scholarships, awards, entertainment, meetings, country club memberships, and a variety of miscellaneous expenses. Regardless of the nexus these expenditures have to supporting SCSU, the issue is any consideration from a vendor contract with SCSU belongs to SCSU, not a foundation. The diversion of these funds removes transparency in the expenditure of these funds, as well as allows the use to be determined without competing in the normal university budgetary framework with other university business needs. In the very best possible light, these expenditures of vendor funds falls into the category of "nice to have" benefits, many of which were inconsistent with how the public, appropriators, and state procurement policy envisioned state funds to be spent.

The optic of SCSU executives diverting $2.29 million of vendor contract rebates, which rightfully belongs to the university, to foundations, to include discretionary expense accounts for university executives, looks highly inappropriate. Although the practice's genesis in 2005 likely started with good faith intentions, it was based on faulty legal, management, and leadership thinking. Once the process started, these revenue streams disappeared from SCSU's budgetary process. It seems the initial AF operated like a traditional foundation with some controls such as requiring SCSU executives to make funding requests in writing for the AF Board's approval. However, overtime, the entire vendor contract rebate fund stream was moved to a second foundation, the SCSU Foundation, where these funds had no policy, procedures, or oversight on expenditure decisions other than from the SCSU executives who controlled and used these discretionary accounts.

The SIG also questioned SCSU vendor contracts with rebates going directly back to SCSU. Monetary rebates are reasonable if directly connected to a profit sharing revenue stream or commissions to incentivize vendors' productivity. Additionally, capital improvement rebates with a sufficient nexus to services provided, such as refurbishing a dining hall in a food service contract, may facilitate passing costs onto students as an appropriate user type fee. However, many rebates are not much more than creative financing to create funds for special projects, many having a "nice to have" quality or create an opportunity for parochial projects. These types of rebates undermine transparency, accountability, and managing contract performance in the following areas:

- Creates potential conflicts of interests undermining rigorous contract monitoring by a state agency. As one experienced Board member commented on these rebate contract requirements, 'why would I be forceful with a vendor if I'm getting something on the backend? I am going to do a whole lot of tolerating.' One contract included a $200,000 unrestricted "partnership gift" on the first day of the contract.

- Creates hidden costs to consumers, primarily students. SCSU students annually pay an extra $343 for meals to support the food service vendor's lump sum monetary contributions back to SCSU and foundations.

- Rebate funded special projects can create a "pre-selection" inhibiting the normal comparative scrutiny projects should receive in the university, or even legislative, budgetary processes. The university component sponsoring a contract can build in rebate requirements for a parochial project, which has a value much less than other university needs. This parochial project gets funded by creating this manufactured revenue stream outside of the normal budget process. For example, SCSU's food service contract required the vendor to pay $5 million for a new wellness center. Yet, at the same time, SCSU's current fiscal year budget requested $5.1 million from the state's general fund for a boiler plant project because its current system's efficiency is less than 30% and "steam piping, traps, and condensate pumps are also in a state of disrepair."

The direction for the future should be to get back to fundamental management in these types of rebate laden vendor contracts, with emphasis on transparency and simplicity. SCSU foundations should be vehicles to support SCSU with resources from donations and gifts with a one way fund flow from the foundation to SCSU. Any university business activity generating revenue needs to stay within the institution to benefit its operations consistent with university priorities and state procurement code. Stop the practice of unnecessary rebates back to the university, which are not much more than creative financing to fund likely parochial projects outside of the normal university budgetary process. The simple analysis is to get rid of the clutter and confusion from those unnecessary rebates to focus on the contracts measurable performance, facilitate agency contract monitoring to ensure value received, and reduce distractions impacting either. In short, get back to old fashion management of driving a hard bargain and then making sure you get what you paid for.

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II. Background

A. Objectives

This SIG review was predicated on suspicious indicators at the SCSU Advancement Foundation (AF) raised in SCSU's 2012 and 2013 Comprehensive Annual Financial Reports (CAFR). Each audit report received a modified opinion because AF did not provide its financial statement of activities to the external auditor as required by the Government Accounting Standards Board (GASB). Another 2012 external audit report of Federal Awards noted a significant deficiency in internal controls in regards to the lack of financial statements for the AF, which were not provided for the period of 2005-2012.

The SIG's review focused on the following objectives:

- Determine why SCSU and its external auditors could not obtain financial information from the AF, a component unit of SCSU, as required by GASB to complete SCSU's 2012 and 2013 CAFRs;
- Gain access to AF's financial records and, based on review, assess the risk for fraud, waste, or abuse;
- Review major vendor contract rebates to SCSU and its foundations for period 2010-2013; and
- Identify opportunities to improve.

B. South Carolina State University

SCSU is located in Orangeburg and was founded in 1896 as the state's sole public college for black youth and has played a key role in the education of African-Americans in the state and nation. It consists of 107 buildings on 160 acres of land on its main Orangeburg campus. Today students are majoring in a wide range of programs that include agribusiness, accounting, art, English, and drama, as well as fashion merchandising, physics, psychology, and political science. Current enrollment is approximately 3100 students supported with a $146 million budget.

III. Diversion of SCSU Revenue and Rebates to its Foundations

The SIG's initial objective, which was to understand the SCSU external auditor's lack of access to AF financial records, started with contact with the AF Chairman and Executive Director. Both were open and transparent with AF's mission and financial records. The AF did not see the need to pay for externally audited financial statements in the recent past inasmuch as its level of foundation activity had dropped dramatically since 2010. The AF was not aware SCSU or its external auditors had issues with access to AF's records. A review of SCSU records revealed correspondence to AF regarding the need for financial records to meet SCSU CAFR requirements, as well as interviews with SCSU's external auditors indicated the same. In short, the SIG could not reconcile with interviews and records any substantive reason, other than miscommunication, as why the external auditor could not obtain AF records to support SCSU's CAFRs in 2012 and 2013. However, a subsequent review of AF's financial records to assess the risk for fraud, waste, or abuse did surface the issue of an inappropriate practice of funding the AF with revenues and rebates from SCSU vendor contracts.

The AF was established in 2004, as requested by the Board of Directors, with a goal to “serve as the repository for proceeds generated from outsourced enterprises, fund development initiatives, and other special institutional campaigns.” This was followed with a 2005 Memorandum of Understanding (MOU) between AF and SCSU where “certain non-state revenues, which are generated on the campus of SCSU, should be transferred to the AF.” The current AF officials affirmed AF’s source of revenue was designed to come from the university; the AF did not conduct traditional fundraising activities.

Sometime in 2010, there appeared to be friction between AF and SCSU executives over use of AF funds. Afterwards, these vendor contract payments, which can generally be described as contract rebates, were exclusively paid to the SCSU Foundation (SCF) into five pre-existing accounts which had also been receiving vendor contract rebates. One was titled, “Institutional Development” and the other four were “discretionary accounts” assigned to the individual SCSU positions of President, VP Finance, VP Institutional Advancement, and the General Counsel. The SCF essentially provided a ministerial function to SCSU executives use of these funds inasmuch as neither the SCF Director nor the Board had authority over these five accounts despite the accounts residing on the books and records of the SCF.

Generally, the AF seemed to focus on several major projects in the early years, such as a Presidential Debate and the Low Country Classic, and salary supplements to the SCSU President. A scan of SCF discretionary account expenditures included, travel, consultants, vendors, flowers, scholarships, awards, entertainment, meetings, country club memberships, and a variety of miscellaneous expenses. Regardless of the nexus these expenditures have to support SCSU, the issue is any consideration from a vendor contract with SCSU belongs to SCSU, a state agency, not a foundation. The diversion of these funds removes transparency in the expenditure of these funds, as well as allows the use to be determined without competing in the normal university budgetary framework with other university business needs. In the very best possible light, SCF expenditures of these vendor funds falls into the category of “nice to have” benefits, many of which were inconsistent with how the public, appropriators, and state procurement policies envisioned state funds being spent.

The SIG reviewed the five major vendors providing rebates to SCSU. A review of each vendor’s current contract along with the specific language requiring a form of rebate back to SCSU were as follows:

- <u>UGL-UNICCO (managed on-site by subsidiary DTZ)</u>: This vendor managed the physical plant of the University. The vendor agreed to pay approximately $200,000 per year ($1 million over a five year contract) to the university for special projects of the university’s choice.

- <u>Sodexo</u>: This vendor provided the food services and managed campus dining halls. Sodexo had a commission based rebate calculated on the volume of sales and type of services provided. The vendor also agreed to pay the following without any performance requirements or contingencies: $200,000 unrestricted partnership gift on the first day of the contract; $800,000 in facilities enhancement funds for on-going facilities improvements; $175,000 in-kind catering; five complementary meal entries on each student meal plan; $710,000 in construction capital investment to enhance certain food locations on campus; $5 million in investment as directed by the RFP for supporting the new campus wellness center; and $350,000 annually in a fixed contribution.

- Pearce & Pearce: This vendor provided health plans for students at the university. Pearce & Pearce had a commission based rebate, which involved SCSU collecting premiums and remitting them to the vendor and a capitation fee to the university for students seen at the on-campus wellness center.

- Follett: This vendor operated the campus bookstore. Follett had a commission rebate contract requirement based on the volume of sales. The vendor also agreed to pay the following without any performance requirements or contingencies: $100,000 to the completion of a new retail-ready Spirit Shop in or near the stadium; $66,000 upgrades to retail space; $10,000 annually in general scholarships; and $2,000 annually in textbook scholarships.

- Coca-Cola: Coca-Cola provided beverage and snack vending, as well as exclusive pouring rights in dining halls and sporting events. Coca-Cola paid a commission based on sales, as well as agreed to pay six academic scholarships each year, which were annually valued at $43,668.

The first vendor contract, UGL-UNICCO, is fee for service contract where the university pays the vendor for services provided. Any rebate, monetary or capital improvement project, from the vendor to SCSU is essentially a return of SCSU's own funds it paid for services; a classic rebate. The residual four contracts are revenue contracts where SCSU contracts the right to a vendor to provide a service. The vendor charges customers, predominately students; makes a profit; and returns a portion of the profits to SCSU. These revenue rebates can take the form of a recurring profit sharing stream, lump sums, or capital projects.

During the period under review, monetary rebates were 79% to SCSU and 21% to the foundations. The vendor contract rebates back to the foundation were inappropriate, regardless of terminology, because the funds were contract consideration back to the SCSU, a state agency, not a foundation. The Budget and Control Board, Procurement Services Division, concurred with this analysis, as did the SCSU President. Further, there was an immediate conflict of interest by SCSU executives permitting such an arrangement of diverting revenue away from SCSU, when AF's MOU specifically allows it "to offer salary supplements to key SCSU employees where appropriate." The AF's primary foundation activity provided salary supplements to SCSU Presidents.

IV. Review of SCSU Major Vendors with Contract Rebates for Period 2010-2013

To understand the scope of vendor rebates diverted to foundations, SCSU's five major vendors' with contract rebates were reviewed for the period of 2010-2013. According to the AF, SCF, and SCSU records, the below chart reflects rebates from vendor contracts to foundations at SCSU in 2010-2013:

Funds from the University's Vendors to the Foundations 2010-2013					
Vendor	**2010**	**2011**	**2012**	**2013**	**Total**
Beverage	$43,668	$0	$50,000	-	$93,668
Bookstore	$0	$500	$225	$0	$725
Health Insurance	$104,927	$82,309	$168,645	$28,386	$384,267
Food Services*	$590,057	$815,207	$0	$0	$1,405,264
Facilities	$4,994	$205,000	$0	$205,600	$415,594
Totals	**$743,646**	**$1,103,016**	**$218,870**	**$233,986**	**$2,299,518**

***Included 200,000 paid to SCSU Advancement Foundation**

The reduction in vendor rebates to foundations in 2012 was a result of interim President Cynthia Warrick discontinuing the policy of vendor rebates to foundations, which halted most, but not all, such transactions. A variety of documents surfaced identified this policy:

- In a series of June 2012 emails, the interim General Counsel stated, "It is my opinion that such funds are state funds and need to go entirely to the university, not to the foundation. It does not matter who is paying the funds. The revenue is being generated because of university activities, not foundation activities, and regardless of who is paying, the funds need to go to the university…it is my strong recommendation that no contracts be signed that provide for payments to any other entity than the university."

- The November 15, 2012, SCSU Board minutes confirmed the interim General Counsel's legal opinion, "It was noted that funds from auxiliary services (i.e., food service, facilities management, and book store) will no longer appear on this report (Private Giving Report). These funds should not be co-mingled. Auxiliary funds should come directly to the university."

- In the September 27, 2012, Board minutes, the external auditor's comments from a recent audit were noted as follows, "the University endorsed two checks over to the Foundation account in the amount of $750,000, which he recommended should have stayed with the University. Once checks are signed over to a foundation, the University does not have control over them." SCSU management provided a written response to this issue which concurred and advised the practice had "been amended."

Despite this 2012 SCSU Board policy on having monetary vendor rebates be directed exclusively to the university, the health insurance vendor commissions continued unabated to the SCF totaling $197,030 in 2012-2013. Further, in November 2013, a $200,000 vendor rebate check (UGL-UNICCO) payable to SCSU was endorsed over to the SCF into a newly established account to support the new President's inauguration activities. The President, the SCF Director, and the UGL-UNICCO on-site director all recalled the $200,000 donation was intended for the SCF with no restrictions. However, the President was not aware of the 2012 November Board minutes or the 2012 external audit finding on this issue. The reality was this $200,000 was not a donation; it was a contract required payment to SCSU. According to the contract, the $200,000 UGL-UNICCO check payable to the SCSU was to the University for special projects of the University's choice, and devoid of the words or concepts of donation or foundation. Upon learning this, the President recognized if the $200,000 was a contract requirement, then the funds should not have been diverted to the foundation.

This is just an example of the contract complexity from rebates creating the false discretion to freely spend these annual lump sums on whatever special project regardless of the university's competing general needs. It took seven years, a federal wiretap investigation, and a series of fiduciary minded analyses to finally stop diverting vendor rebates, rightfully belonging to SCSU, to foundations, which then found their way into "discretionary" accounts of SCSU executives. A year later, lessons from the past and the formal 2012 Board policy was missed, and SCSU was right back in the same predicament of an inappropriate practice which creates the conditions for fraud, waste, and abuse. Fortunately, the new SCSU President now fully recognized this legacy issue and agreed it is inappropriate going forward.

V. High Risk Financial Control Environment

During the four years reviewed, SCSU did not have a process to track the five vendors' rebates. During the majority of these four years, SCF received the vast majority of these rebates to foundations, yet until former interim President Warrick stopped this practice in 2012, SCF thought these funds were true donations rather than rebates from vendor contracts. Once SCF received these funds, it had no written policy and procedures on the movement of money within accounts controlled by SCSU executives, nor authority levels required to approve expenses. Further, these accounts controlled by SCSU executives resided inside of SCF, yet the SCF Director nor the Board had any oversight or authority over these accounts. Additional examples illustrating this high risk financial control environment over vendor rebates included:

- Two vendors inadvertently missed their annual rebate payments totaling over $280,000 without SCSU noticing, which these two vendors paid the following year based on their own initiative.

- A vendor did not pay its 2013 rebate of $43,000, and still has not, because it was uncertain as to where to send the funds; SCSU was unaware this contract term was violated.

- Despite SCSU Board policy stopping this practice in 2012, the health insurance vendor continued to send checks to a foundation totaling $197,030 in 2012-2013 and a $200,000 vendor rebate was diverted to SCF in 2013.

- A vendor provided SCSU $100,000 dedicated by contract for a Spirit Shop near the stadium that has not been started by the university. A second vendor provided over $2 million dedicated by contract for a wellness center that appears to not have been restricted and diverted to the university's general operations.

- Checks payable to SCSU were endorsed into accounts (foundations) not belonging to SCSU, which occurred even after the SCSU external auditors identified this issue in the Fall 2012 and SCSU management concurred and amended the practice.

- Some vendor rebates were split into separate checks sent directly to foundations and the university, without anyone at SCSU fusing this data together to appropriately monitor vendor compliance with contract requirements. In short, no single person at SCSU "owned" the duty to monitor vendor compliance with vendor rebate contract requirements.

In summary, SCSU had inadequate policy, procedures, and controls to manage vendor contract rebates. The practice of vendor rebates to foundations was not only inappropriate, it was poorly controlled. Although the SIG's review focused on the AF and SCF, the SIG suspects this inappropriate contract rebate practice may be taking place in other university foundations. For example, in June 2012, the interim General Counsel determined athletic game contract revenue was going to both the university and to the athletic foundation. The interim General Counsel commented, "I know what has been done in the past, but my job is to make sure that SCSU does it right going forward." The SIG agrees.

VI. Inappropriate Nature of Aspects of Vendor Rebates Direct to SCSU

Without question, vendor rebates from SCSU contracts diverted to foundations were inappropriate; this practice must cease. The SIG also challenges the general concept of vendor rebates from SCSU contracts back to the university, with two exceptions. First, contract commission revenue streams and profit sharing to incentivize a vendor to be more productive are quite appropriate. Second, a contract requiring vendor capital expenditure, such as refurbishing a SCSU dining hall in a food service contract, may have a sufficient nexus to be part of a reasonable negotiation which may also facilitate passing costs onto students as an appropriate user type fee. However, the farther capital projects stray from connectivity to services provided, the less appropriate the capital project rebate becomes.

Outside of these two exceptions, the SIG views vendor rebates as undermining transparency, accountability, and effective management of contract performance based on the following:

- Creates the potential for conflicts of interests undermining rigorous contract monitoring by a state agency. As one experienced Board member commented on these rebate contract requirements, 'Why would I be forceful with a vendor if I'm getting something on the backend? I am going to do a whole lot of tolerating.' As an example, one vendor contract included a $200,000 unrestricted "partnership gift" on the first day of the contract.

- Creates hidden costs to consumers, primarily students. SCSU students annually pay an extra $343 in meal costs to support the food service vendor's lump sum monetary contributions back to SCSU and foundations.

- Rebate funded special projects can create a "pre-selection" inhibiting the normal comparative scrutiny projects should receive in the university, or even legislative, budgetary processes. The university component sponsoring a contract can build in rebate requirements for a parochial project, which has a value much less than other university needs. This parochial project gets funded by creating this manufactured revenue stream outside of the normal budget process. For example, SCSU's food service contract requires the vendor to pay $5 million for a new wellness center. Yet, at the same time, SCSU's current fiscal year budget requested $5.1 million from the state's general fund for a boiler plant project because its current system's efficiency is less than 30% and "steam piping, traps, and condensate pumps are also in a state of disrepair."

- Creates needless complexity increasing the administrative costs and risks to ensure contract performance. The aforementioned report section titled, "High Risk Financial Control Environment," illustrates the administrative burden and the risk of significant errors in monitoring these complex contracts.

According to the Budget and Control Board, Procurement Services Division, contributions or incentive packages in contracts have a long history in South Carolina. This practice began in order to stop under-the-table incentives between agencies and prospective vendors. The argument is that now, all vendors can bid openly on both the services/products and enhancements/rebates. Those terms can also have a standardized point range as a part of the bid award. The state office sees this as increased transparency and allowing equal access by all prospective bidders. The SIG disagrees. The current rebate process creates a relaxed, tolerating, and open exchange of consideration that has no nexus to contract performance. These rebates actually can create a perception of a gift, favor, or discretionary act, as illustrated with the SCSU example above, all of which can bestow a level of relationship leverage to the vendor, when in fact the agency is just receiving money the contract provides. This complexity actually creates air cover and opportunity for anyone with corrupt intent. A better course would be to draw an absolute clear line to prohibit these rebates that decreases complexity and temptation, while promoting, both in reality and perception, a robust arms-length, performance based business relationship. What image goes through most people's minds, particularly taxpayers, when a contract term states, "a $200,000 unrestricted *partnership gift* on the first day of the contract?"

To further illustrate this point, SCSU's food service contract went into effect in August 2011, which required a $5 million investment supporting a new campus wellness center. In that same month, according to a pending November 2013 federal indictment (Count 1, overt act 54), two SCSU officials (one under indictment; one convicted) "used a cellular telephone" talked about getting a specific person work at SCSU by having this person develop a wellness center at SCSU. Later in the same indictment (Count 1, overt act 94), an SCSU official and associate (both under indictment) viewed an Atlanta Falcons Football Game in a $5000 suite; the cost was split between an SCSU vendor and a SCSU foundation. The federal indictment identified six overt acts at SCSU. Of these six overt acts, two involved foundations and five involved SCSU contracts. Three SCSU officials have pleaded guilty and one is under indictment with trial set for the Summer 2014. These examples and common sense dictate less rebates moves a contract to a greater arms-length transparent transaction, while more unnecessary, complex, and lump sum rebates creates unfavorable conditions and opportunity where other interests than agency and taxpayers' best interests can seep into the decision making.

During the review, anecdotal data from witnesses with statewide contracting experience in university settings, indicated vendor contract rebates was a common practice. One witness with broad experience said universities seem to be driving this practice rather than vendors.

The simple analysis is to get rid of those unnecessary rebates to focus on a contract's measurable performance, simplify agency contract monitoring to ensure value received, and reduce distractions impacting either. For fee for service contracts, there should be a presumption of no rebates. For revenue contracts, the revenue should optimally come back to the university's general or unrestricted funds in a systematic recurring manner, and any form of rebate, often lump sums or capital expenditures, should be viewed skeptically to avoid parochially moving contract funds away from the university's general needs. The core issue is to maximize contract revenues to the SCSU general or unrestricted funds so all projects compete with all other university needs, rather than be pigeonholed by a SCSU component for a potential parochial special project. Reducing complexity eases administrative burden, reduces costs, stops revenue bleeds to special funded projects, and allows more rigorous contract management, which are all in the direction to save money for the university.

VII. Way Forward—Transparency Prevents Problems

The optic of SCSU executives diverting $2.29 million of vendor contract rebates, which rightfully belong to the university, to foundations, to include discretionary expense accounts for university executives, looks highly inappropriate. In the best possible light, the practice's genesis in 2005 started with good faith intentions but with just faulty legal, management, and leadership thinking. Once the process started, these revenue streams disappeared from SCSU's budgetary process. It seems the initial AF operated like a traditional foundation with some controls such as requiring SCSU executives to make funding requests in writing for the AF Board's approval. However, overtime, the entire vendor contract rebate fund stream was moved to SCF where there was no policy, procedures, or oversight on funding decisions other than from the SCSU executives who used these discretionary accounts. This resulted in many expenditures inconsistent with state procurement and taxpayer standards, as well as erosion of the university's trust with stakeholders.

The direction for the future should return to fundamental management in these types of rebate laden vendor contracts, with emphasis on transparency and simplicity. SCSU foundations should be vehicles to support SCSU with resources from donations and gifts with one way fund flow from foundation to SCSU. Any university business activity generating revenue needs to stay within the institution to benefit its operations consistent with university priorities and state procurement code. Just get back to old fashion management of driving a hard bargain without convoluting rebates, making sure you get what you paid for with contract monitoring, and any revenues generated go to an agency's general or unrestricted accounts to be used in the best interests of the agency.

VIII. Findings & Recommendations

Finding #1: SCSU inappropriately diverted vendor monetary rebates from university contracts to its foundations.

> **Recommendation #1a:** SCSU should establish a policy to require all monetary vendor rebates from existing university contracts be directed towards the university and not to foundations.
>
> **Recommendation #1b:** SCSU foundations, to include, but not limited to, the Advancement Foundation and the SCSU Foundation should return all existing cash, investments, or assets that can be logically traced to vendor monetary rebates.
>
> **Recommendation #1c:** The Budget and Control Board, through its Procurement Services Division, should provide a reminder, similar to a "lessons learned," to all state agencies, particularly higher education state agencies, that all vendor monetary rebates from existing agency contracts be directed towards the agency and not to a third party, such as a foundations, unless expressly authorized by law.
>
> **Recommendation #1d:** The South Carolina legislature should consider legislation or proviso to require all state agencies examine all existing contracts with vendor revenue streams or rebates to ensure these funds are directed to the agency and not a foundation or other third party unless expressly authorized by law.

Finding #2: SCSU vendor contracts with rebates, other than of those directly connected to commissions to incentivize vendors' productivity, operational revenue generating, or capital expenditures with a nexus to the contract, undermines the transparency, accountability, and effective management of contract performance. This includes, but not limited to, creating potential conflicts of interests undermining rigorous contract monitoring; creating hidden costs to consumers, primarily students; and rebate funded special projects potentially creating a "pre-selection" inhibiting the normal comparative scrutiny projects receive in the university, or even legislative, budgetary processes.

> **Recommendation #2a:** SCSU should establish a policy for new vendor contracts to require the University' President to personally approve any rebate with the exceptions of those directly connected to

commissions to incentivize vendors' productivity, operational revenue generating, or capital expenditures with a nexus to the contract.

<u>Recommendation #2b</u>: The South Carolina legislature should consider providing a requirement, through statute or proviso, for agencies to specifically disclose revenue streams, rebates, and capital projects from vendor contracts in the budget process to add visibility of the receipt and use of these funds to facilitate analysis of these same agencies' general fund budget requests.

<u>Finding #3</u>: There exists a weak financial control environment, both in the SCSU Foundation and SCSU, in managing vendor contracts with rebates.

<u>Recommendation #3a</u>: SCSU Foundation, as well as all foundations associated with SCSU, should solely support SCSU through fundraising, gifts, and revenue developed independent of the university.

<u>Recommendation #3b</u>: SCSU Board of Directors and Executive Management should extricate the university from business ventures or complex transactions with foundations that could create real or perceived conflicts of interest or financial liability impacting their fiduciary duty and loyalty to the university.

<u>Recommendation #3c</u>: SCSU foundations should re-examine the adequacy of their respective policies and procedures to ensure adequate control over its assets and expenditures and prevent SCSU executives having unilateral access to assets without foundation approval.

<u>ADMINISTRATIVE NOTE</u>: SCSU was provided a draft and had no suggested changes or comments. The Procurement Services Division, Budget and Control Board, provided written comments which can be found at the following link: http://oig.sc.gov/Documents/PSD_BCB_Response.pdf.