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STATE AUDITOR

STATE OF NORTH CAROLINA
Office of the State Auditor

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**SPECIAL REVIEW
MANAGEMENT LETTER**

WINSTON-SALEM STATE UNIVERSITY

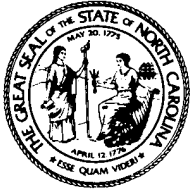
WINSTON-SALEM, NORTH CAROLINA

AUGUST 1999

OFFICE OF THE STATE AUDITOR

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July 16, 1999

Dr. Alvin J. Schexnider, Chancellor
Winston-Salem State University
601 Martin Luther King, Jr. Drive
Winston-Salem, North Carolina 27110

Dear Chancellor Schexnider:

The Office of the State Auditor received complaints through the State Auditor's Hotline alleging misuse of funds and violations of purchasing procedures at Winston-Salem State University (WSSU). We conducted a Special Review of these allegations in accordance with G.S. §147-64. In conducting this review, we examined WSSU and WSSU Foundation records and conducted interviews with individuals internal and external to WSSU. Our Special Review resulted in the following findings and recommendations to WSSU Management and the University of North Carolina General Administration (UNC-General Administration).

1. Disbursement from Discretionary Funds

In fiscal year 1997-98, WSSU's Internal Auditor conducted a review of expenditures incurred by the Chancellor from January 1996 through May 1998. We reviewed the Internal Auditor's workpapers as well as the expenditures incurred by the Chancellor from July 1998 through April 1999. Our review revealed that the Chancellor used discretionary funds to pay for some items that could be viewed as more personal than university related. Such items included travel expenses for his children, flowers for his wife, and membership in a fitness center. Although there are no general written guidelines for spending discretionary funds, these funds should be spent on items related to the University. To ensure protection for all parties concerned and an understanding on the part of the general public, UNC-General Administration should consider defining the utilization of discretionary funds.

2. Expenditures for Transporting Children to School

The Chancellor used State funds to pay mileage to a house worker from January 1998 through March 1998 to take his children to school. The total reimbursement for mileage was \$416.62. On May 20, 1998 the Chancellor reimbursed the University this amount. According to the Chancellor, he reimbursed the University after being told that

the expenditures were inappropriate. He did not reimburse the University, however, for the house worker's time spent to transport his children. Based on estimates received from the Chancellor of the time it would take to perform this task, the Chancellor should reimburse WSSU an additional \$495. The Chancellor said he thought he had already reimbursed the University for the house worker's time.

3. Outside Contractors Clean the Chancellor's Residence and Maintain His Yard

The Chancellor's residence, located 8.5 miles from campus, is owned by the University. According to the Chancellor, the former Vice-Chancellor for Finance and Administration recommended outsourcing the housekeeping duties which had been done in the past by a university housekeeping employee. Outsourcing the housekeeping duties at the residence cost WSSU \$92.50 per week for three hours of work.

WSSU incurs a similar cost by using an outside contractor for landscaping tasks. The Associate Vice-Chancellor for Facilities recommended outsourcing the landscaping duties. Currently, the contractor mows the lawn once a week, performs minor landscaping duties and cleans away ice and snow for an agreed upon contract of \$7,385 per year.

WSSU should conduct a cost benefit analysis to determine the feasibility of continuing these contracts versus using university staff.

4. Some Items Purchased for the Chancellor's Residence Are Not On the University's Inventory System

A large screen television, a pool table, and a fax machine were purchased for the Chancellor's residence but do not show-up on the University's Fixed Asset Inventory. WSSU's inventory policy states that all purchases in excess of \$500 must be recorded for inventory control purposes.

5. Invoices Are Not Always Paid on Time

We examined one hundred checks paid in September 1998 and one hundred checks paid in February 1999 to determine if they were paid by the due dates. In September 1998, WSSU wrote twenty-two checks out of the one hundred examined after the due date on the invoice. In February 1999, the number of late payments increased to thirty out of the one hundred examined. According to WSSU's Accounts Payable Supervisor, she and her staff were employed within the last year. The constant turnover of the staff in the finance area has resulted in the need to constantly train new employees. The Accounts Payable Supervisor said she is writing new procedures for her section, effective July 1, 1999, that should eliminate late payments, as well as any duplicate payments.

We are presenting these findings and recommendations for your review and written response. The purpose of the response is to allow you the opportunity to outline any corrective actions taken or planned. We request that your written response be delivered to us by July 30, 1999.

Dr. Alvin J. Schexnider, Chancellor

July 16, 1999

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While we have addressed the issues at WSSU in this management letter, it seems prudent for General Administration to review the need for developing policies and guidelines for the spending of discretionary funds. Adherence to such guidelines would ensure consistency and benefit all the chancellors within the system.

We wish to thank you and your staff for the cooperation extended to us during this review. If you have any questions do not hesitate to contact this office at 919/733-3217.

Sincerely,

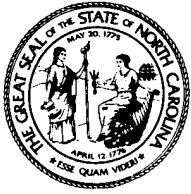
A handwritten signature in black ink that reads "Ralph Campbell, Jr." in a cursive script.

Ralph Campbell, Jr., CFE
State Auditor

RCJr:dj

cc: Dr. Molly C. Broad, President
UNC General Administration

Management letters and responses receive the same distribution as audit reports.



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Auditor's Note

August 19, 1999

In accordance with our statutory mandates, we reviewed allegations of fraud, waste and abuse at Winston Salem State University and reported those findings along with our recommendations for improvements. The results of our review were presented in a management letter, in accordance with our procedures, because the findings were not significant enough to warrant a full report. We asked Chancellor Schexnider and President Broad to respond. Those responses are included herein as is our practice.

The Chancellor's response¹ contains various assertions and insinuations that require a reply on our part. In summary, we have thoroughly reviewed that response and stand behind the findings and recommendations in the management letter. We also stand behind the procedures used to conduct the special review as being appropriate, straightforward and professional. In that regard, and as an example, the response states we did not return a telephone call from the Chancellor's attorney inquiring about a scheduled meeting with the Chancellor. In fact, we did return the call, leaving a message with the attorney's secretary and discussing the meeting with the attorney's partner.

The management letter recommends that General Administration for the University of North Carolina review the controls over the expenditures of discretionary funds. The President of the University System has assured us that this matter will get immediate attention. The Chancellor, however, has chosen to challenge the findings at great length. Based on all the audit evidence available, we stand behind the finding that there were expenditures that could be viewed as more personal than university related and that General Administration should review this area.

The remainder of the response continues to challenge not only the findings of the management letter, but also the methods and motives of the special review. We believe that it is extremely unfortunate that a leader at one of the state's institutions of higher learning has reacted so personally to a special review of expenditures at an institution which, by his own admission, and also the admission of General Administration for the University of North Carolina, has financial control issues that need to be resolved and that have already occasioned personnel changes. The Chancellor's reaction to what was intended to be constructive criticism is troubling to this office.

Mr. Grace, in the response letter indicates that he represents both the chancellor and the university. Until that notification, we understood that Winston Salem State University was represented by Alice C. Bynum, Esq., the University Attorney and the Office of the North Carolina Attorney General and that Mr. Grace represented the chancellor personally.

¹ Note: As of the date of printing we had only received a facsimile of the response that did not include the cited exhibits.



The University of North Carolina

GENERAL ADMINISTRATION

POST OFFICE BOX 2688, CHAPEL HILL, NC 27515-2688

MOLLY CORBETT BROAD, *President*

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Appalachian State
University

East Carolina
University

Elizabeth City
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Agricultural and
Technical State
University

North Carolina
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North Carolina
School of
the Arts

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North Carolina
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at Pembroke

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North Carolina
at Wilmington

Western Carolina
University

Winston-Salem
State University

An Equal Opportunity/
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July 30, 1999

The Honorable Ralph Campbell, Jr., CFE
State Auditor
State of North Carolina
300 N. Salisbury Street
Raleigh, North Carolina 27603-5903

Dear Mr. Campbell:

Thank you for the opportunity to respond to your proposal that UNC General Administration review the need for developing policies and guidelines for the spending of discretionary funds. Certainly, the availability of funds for discretionary purposes is critically important to each of our chancellors, who have an inherent responsibility to exercise the highest professional judgement to ensure that these funds are used in the best interest of the University.

Each month I meet with the chancellors as a group, and I will place a discussion of responsible discretionary spending on our next agenda. In addition, I will ensure that our Finance Division discusses discretionary spending in all future training sessions with new chancellors and that the topic is addressed at the next systemwide meeting of UNC chief financial officers.

Financial responsibility is essential to the integrity and reputation of our University, and I assure you that we will give your proposal immediate attention.

Sincerely,

Molly Corbett Broad

MICHAEL A. GRACE, P.A.
ATTORNEYS AND COUNSELLORS AT LAW
102 WEST THIRD STREET, SUITE 522
WINSTON-SALEM, NORTH CAROLINA 27101-3915

MICHAEL A. GRACE
CHRISTOPHER R. CLIFTON

TELECOPY COVER SHEET

(336) 725-9428

TELECOPIER
(336) 721-1176DATE: 8-13-99

TIME: _____

PLEASE SEND THE FOLLOWING PAGES TO:

NAME: Mr. Rufus WilliamsCOMPANY: State Auditor's OfficeTRANSMITTAL TELEPHONE NUMBER: 919-733-8443FROM: Mike
MICHAEL A. GRACE, P.A.TOTAL NUMBER OF PAGES SENT (INCLUDING COVER SHEET): 10RESPOND TO MICHAEL A. GRACE, P.A. AT FAX NUMBER 336-721-1176.
IF YOU DO NOT RECEIVE ALL PAGES PLEASE CALL 336-725-9428.

COMMENTS: Response to Audit report
per our conversation regarding and exhibit
posted this day to your system
Shap
MAG

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AT THE ADDRESS SHOWN ABOVE. THANK YOU.

Response to Special Review
Winston-Salem State University
Dr. Alvin Schexnider

TO: Mr. Ralph Campbell, Jr.
State Auditor

FROM: Michael A. Grace, Esq.

DATE: August 13, 1999

Please accept the following as the response of Dr. Alvin Schexnider and Winston-Salem State University to the findings of the Special Review done by your office as contained in your correspondence dated July 16, 1999.

By way of background for the uninformed, your office contacted the Chancellor and the University sometime in June of this year and informed same that your office had received several calls on the Auditor's Hotline of complaints and possible abuses of financial practices by the Chancellor and the University. The Chancellor and the University were informed that a Special Review would be conducted by the Auditor's Office to investigate those alleged abuses. On June 13, 1999 the Chancellor received a call from the Auditor's staff to arrange an interview concerning these issues. Prior to the meeting this writer, counsel to the Chancellor, contacted Mr. Rufus Williams of the State Auditor's Office and left a voice mail inquiring as to the subject matter of the scheduled June 15th meeting. That request was made to allow the Chancellor to prepare for the meeting and to arrange to have such members of the University staff in attendance as necessary to fully answer the questions of the Auditor's staff. Instead of returning the call to

counsel, Mr. Rufus Williams contacted the Chancellor directly and informed him there was no need for the Chancellor to prepare for the meeting and no documentation that he need bring, but that the Auditor's staff only wanted to clear up a few areas of concern.

The purpose of the call by counsel was to give the Chancellor an opportunity to talk to University staff members who were responsible for areas of concern to the Auditor's Office. It was an effort to make sure the Chancellor was fully apprised of matters that he would not ordinarily be familiar with in great detail. It was against this backdrop that the Chancellor, along with counsel, met with three members of the Auditor's staff on June 15, 1999.

In addition to the matters contained in the Auditor's Review, the Chancellor was interrogated concerning: the lease on the apartment the Chancellor resided in prior to moving into the Chancellor's residence; the cost of the Christmas decorations at the Chancellor's residence; the bathroom accessories at the Chancellor's residence; the cost of tickets purchased for functions that the Chancellor attended in his official capacity as Chancellor; nominal expenditures from the discretionary funds for donations to local charitable institutions and events; various gifts, such as a book for a benefactor of the University; and the sales price of the former Chancellor's residence. As the Chancellor informed the Auditor, he is acutely aware that he is ultimately charged with responsibility for the running of the University in each and every detail. However, he informed the Auditor's staff that he did not have specific knowledge at hand concerning every detail and about every check written from the University or discretionary accounts. Nevertheless, the Chancellor did answer all questions openly and to the best of his ability given his limited opportunity to prepare.

Notwithstanding an attempt by the Chancellor to be completely candid, the State Auditor chose to offer a very limited context for the matters reported. For instance, when asked about

payment of travel expenses for the Chancellor's children out of discretionary funds, the Chancellor informed the Auditor's staff that such an expenditure was occasioned by an instance in March of 1997 where the Chancellor was the speaker at an alumni event in Raleigh, North Carolina. The Chancellor's wife was also in attendance at that event. The Chancellor and Mrs. Schexnider were unable to secure childcare services. Consequently, as the Chancellor informed the staff, the minor children traveled with the Chancellor and Mrs. Schexnider to Raleigh. The event lasted late into the evening and resulted in the Schexnidrs obtaining accommodations at a local motel. The Chancellor's room was, according to the Chancellor, paid for out of the University operating account and the Chancellor's children's hotel room paid for out of the Chancellor's discretionary account. All of this was explained to the Auditor's staff who chose only to report in its Special Review that the Chancellor had paid for the travel expenses for his children out of discretionary funds and further reported that same could be viewed as more personal than University related. Given the proper context coupled with the fact that there are absolutely no rules governing the use of the discretionary account, it is clear that such an expenditure was indeed related to Dr. Schexnider's duties as Chancellor and not some personal matter for which the discretionary account was abused.

Also in Paragraph 1 of the Special Review, the Auditor goes on to say that the purchase of "flowers for his wife" could also be viewed as a personal expenditure. This item in question relates to an entry from an invoice from a local florist in the amount of \$30.00, which listed the recipient as Virginia Schexnider. Said invoice is attached hereto and marked as Exhibit A. The Chancellor was unable to specifically remember for what event the flowers were purchased, but informed the Auditor's staff that on numerous occasions flowers were ordered for the chancellor's residence when special events and functions were hosted there which related to

University business. The Chancellor was able to recall one such occasion during Commencement of 1998 where a reception was held at his private residence. Flowers were ordered for centerpiece and table decorations and were paid for out of discretionary funds. The Auditor's Office was provided copies of the invitation to that event which occurred one day after the purchase of the flowers along with Mrs. Schexnider's handwritten note requesting that the Chancellor order flowers. Both are attached as Exhibits B and C, respectively. Notwithstanding the Chancellor's open and honest efforts to answer the questions the matter was presented in the Special Review without any context, which makes it appear that the Chancellor had abused the discretionary account by purchasing flowers for his wife. The Chancellor unequivocally informed the Auditor's staff that he had never purchased flowers for his wife out of University or discretionary funds. Without any proof to the contrary and notwithstanding the Chancellor's denial, the Auditor has created the perception of improper activity when none exists. If in June of 1999 the Chancellor is supposed to remember one 1997 \$30.00 purchase out of thousands of transactions, then clearly the Auditor's Office has no grasp of all of the duties and responsibilities of a University Chancellor.

The last matter in paragraph one of the Audit Report which is taken out of context and which raises an inference that the Chancellor abused his discretionary account is the question of the Chancellor's membership in a local fitness club. The Chancellor informed the auditors that he often used the fitness club as a place to meet University friends and benefactors to discuss University business while exercising. He even informed the staff that he had been able to secure several donations and one scholarship through contacts and connections made at the fitness club. The Chancellor further drew the analogy of his membership in the fitness club to the membership of other Chancellors in local country clubs. The audit staff failed to report any of this and chose

to simply state that the Chancellor had purchased a membership in the local fitness club without further explanation or discussion. It appears that the Auditor's position is that membership in a local fitness club, purchased with discretionary funds, is, in and of itself, an abuse of that account. The Auditor is challenged to canvas the University System to determine how many other Chancellors have memberships to local fitness, country and/or dining clubs which were paid for out of discretionary accounts.

In Paragraph 2 of the Special Review the Auditor's Office revisits the question of reimbursement by the Chancellor for mileage paid to the house worker who is employed in the Chancellor's residence. The Auditor again fails to put this matter in the proper context and to the uninformed raises an inference that the Chancellor has done several things improper or illegal. The Auditor fails to state that the house worker who was employed in the Chancellor's residence was properly employed and paid for out of State funds. The Chancellor mistakenly believed that since the worker was properly employed in his residence that it would be proper to pay that person mileage for transporting the minor children out of State funds. An internal audit by the University determined that mileage payments to the worker from State funds was inappropriate and suggested that the Chancellor reimburse the State for those mileage payments. The Chancellor did so on May 20, 1998, all of which was the subject of much local publicity and as stated above an internal audit by the University.

The Auditor further states "he did not reimburse the University however for the house worker's time spent to transport his children". The statement is, in and of itself, is true. However, the State Auditor fails to include that at no time was the Chancellor informed that the University should be reimbursed for the actual time expended by that employee transport the children. The Auditor phrases the report to insinuate that the Chancellor had refused to

reimburse the State for that worker's time, when in fact, the internal auditor was unable to determine what monies, if any, would be appropriate for that employee's time. In the June meeting, the State Auditor's staff asked the Chancellor how long he estimated it would take the worker to drive to and from the residence and the children's school and the market where the worker sometimes traveled. From that very rough estimate by the Chancellor, the Auditor determined that the Chancellor should reimburse the University an additional \$495.00. The Chancellor informed the Auditor's staff that he thought the money that he had paid included everything he was required to pay and that he would be more than happy to pay the additional fees. Again, to the uninformed, the Auditor, while stating the facts, has very cleverly worded this matter and put it in a context to suggest that the Chancellor was not entitled to have a house worker and that he, when asked to pay back travel expenses improperly paid, refused to do so.

Paragraph 3 of the Special Review contains many of the same tactics by the Auditor's Office. While reviewing what by any standards is a totally innocuous practice on behalf of the University, the Auditor raises the specter of some wrongdoing by the University and especially the Chancellor in outsourcing services for the Chancellor's residence. The Special Review to the uninformed public would seem to question whether or not the Chancellor is entitled to either or both housekeeping services and lawn care services at the Chancellor's residence. There can be no question by anyone that these are proper expenditures of State funds and is a practice that is University wide. The Special Review properly states that the Chancellor was informed by the Vice Chancellor for Finance and Administration that outsourcing should be done in these two areas. Never did the Special Review Auditors contact or question the Vice Chancellor to determine if some cost analysis had been done before outsourcing took place. The Chancellor informed the staff that he felt like such had been done but could not unequivocally state that

same was true. If the Auditor had in fact spoken with Mr. Irvin M. Hodge, Associate Vice Chancellor for Finance they would have been informed that such an analysis had been done. Furthermore, the Auditor's Office was provided a handwritten note, which is marked as Exhibit D and which was provided to the staff as an attachment to a preliminary answer to this audit review from the Vice Chancellor for Finance and Administration. The note contained the analysis for the outsourcing of the lawn care services. I have also enclosed herewith a memo dated August 11, 1999 from Mr. Hodge to the Chancellor, marked as Exhibit E, which indicates the disparate pricing between using in-house personnel and outsourcing the housekeeping services at the Chancellor's residence. Had the Auditor's staff taken the time to ask someone other than the Chancellor for this information or had the Chancellor had the opportunity to bring the right people to the meeting this answer would have been readily available to the Auditor's Office. The Chancellor questions how the outsourcing of services could be the subject of a Fraud and Abuse review when the General Administration by way of a memo under cover of the signature of Mr. William O. McCoy, former Vice President for Finance of the University System. I have attached a copy of that memo as Exhibit F. Said Exhibits were provided to the Auditor's Office in an earlier version of this response.

The matters contained in Paragraphs 4 and 5 of the audit review probably best reflect how far the Auditor's Office is prepared to reach to raise the inference of some impropriety on behalf of the Chancellor. In the meeting of June 15th the first question asked of the Chancellor concerned the inventory of fixed assets and what person or persons within the University were responsible for compiling that inventory. The Chancellor informed the staff that Ms. Pitt of his office was responsible for the inventory. The Chancellor was then immediately questioned about a large screen TV, a fax machine and copier, along with two routers not being on the inventory

sheet. The Chancellor informed them that he felt confident that those matters had been properly tagged and inventoried. Of note is the fact that in the audit report of the University finances there are listed several thousands of dollars of assets that the Auditor determined were not properly tagged and inventoried. One can but question why the Auditor sought to single out these three items that happened to be in the Chancellor's residence to include in this Special Review of Fraud and Abuse. The answer would suggest that the Auditor's Office attempts to raise a specter of some misconduct by raising the inference that the Chancellor in some way misappropriated these items for his own use. When in fact these items were properly tagged and inventoried; proof of same was offered to the Auditor's Office by way of memo dated May 14, 1998 and submitted to the Campus Controller by Mr. Marlowe Foster and attached hereto and marked as Exhibit G. These items are accounted for and have been accounted for through proper tags and inventories for some several months, and notwithstanding any inference the Auditor attempts to make, are properly recorded as University property.

The Chancellor has at all times acknowledged that some of the University's internal financial practices have been sub-par and has had his staff working very diligently to bring those practices up to par. There is no question that in the past there has been late payment of some invoices due to these lax practices. The Chancellor strongly suggests that the handling of late payments by the University would be more properly covered in the University Audit Review, which is a separate review from this special Fraud and Abuse review. The Auditor even states in his finding that the supervisor responsible for writing of checks and payment of invoices has placed into effect new practices which would eliminate the late payments as well as any duplicate payments. Why the Auditor chose to include this finding in this particular review is a question only the Auditor's Office can answer. If this particular matter is a proper subject for a Fraud and

Abuse Review then most everything in the annual audit report of the University could be included. It appears to be one further attempt to suggest that the Chancellor has personally abused the rights and privileges of his office or has been lax in the personal handling of the day-to-day finances of the University.

In closing and on behalf of the Chancellor this response is the second such response submitted to the State Auditor's Office. The first response was an attempt by the Chancellor to urge the Auditor to include in his Special Review findings all of the facts surrounding the various circumstances examined. It was an attempt by the Chancellor to gain a fair treatment of the facts rather than the one-sided and often erroneous approach made by the Auditor's Office. The Chancellor and his staff are at the disposal of the Auditor's staff to answer any questions they may have or to clarify any information contained herein.

This is respectfully submitted on behalf of the Chancellor and the University.

Michael A. Grace
Counsel to the Chancellor

As required for disclosure by G.S. §143-170.1, 275 copies of this public document were printed at a cost of \$60.50, or 22¢ per copy.