

Office of the Attorney General Hector Balderas



Report On The University of New Mexico's Financial Risk Areas

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INTRODUCTION

As chief law enforcement officer for the State of New Mexico, Attorney General Hector Balderas and the New Mexico Office of the Attorney General (“NMOAG”) have a duty to protect the legal rights of New Mexicans and to ensure that public entities are accountable to the taxpayers and students who support them. The NMOAG became concerned about the University of New Mexico’s (“UNM”) finances starting in 2017 after public disclosures surfaced related to UNM’s Athletic Department misappropriation of public funds by Athletics Director Paul Krebs and its complete failure to manage and collect hundreds of thousands of dollars from the sale of the suites and club seats at Dreamstyle Arena (“PIT”), dating back to the 2010-2011 Men’s Basketball season. These public disclosures of misappropriation prompted the New Mexico Office of the State Auditor (“SAO”) to conduct a Special Audit of UNM Athletics, which concluded that UNM’s financial structure lacked adequate transparency and accountability. The audit found a number of specific financial issues, including no clear lines of accountability, misuse of public funds, and misuse of donor funds contrary to donor intent. The Special Audit also raised issues regarding the problematic circular flow of money between the UNM Athletics, the UNM Foundation, and the Lobo Club. The NMOAG became further concerned with the controls and oversight at UNM when multiple other allegations of state law violations reported were by employees and students at UNM.

As a result, in January 2018, the NMOAG initiated a multidisciplinary team to collect a broad range of information to understand more concretely the financial architecture and controls at UNM, its protocol for handling misconduct complaints, and the workplace environment at the managerial level. Throughout the course of the broad multidisciplinary review, the NMOAG discovered a lack of internal control components, standards, process, and structure regarding UNM’s financial oversight, numerous transparency violations, and credible violations of state law

by UNM employees. The NMOAG's own review of the finances at UNM concluded that the problematic circular flow of money between UNM Athletics, UNM Foundation, and the Lobo Club, and the lack oversight and accountability of UNM's financial structure identified previously, remain and make it difficult for UNM to fulfill its duty to properly safeguard the public funds. Based on the findings of its initial review, the NMOAG initiated a formal inquiry into the UNM's finances.

FORMAL INQUIRY INTO UNM

On May 25, 2018, the NMOAG began its formal inquiry into the financial transactions of UNM's Athletic Department that allowed for: 1) UNM employees and private donors to expend public funds to attend a Scotland Trip to play golf; and, 2) the failure to collect hundreds of thousands of dollars from the use of the PIT suites and club seats. The NMOAG identified numerous areas where lack of financial controls and accountability created an environment ripe for fraud, waste, and abuse. In some of these areas, criminal charges for such fraud and abuse were developed. However, there remain areas where the lack of financial control and oversight are so prominent, it is not possible to develop criminal intent or pinpoint with certainty, culpable individuals.

What is clear, is that the culture and environment at the management and oversight level of UNM during this time created a situation ripe for public employees to violate state laws and abuse public resources, without any ability to be tracked, identified or ultimately held responsible. What is so alarming about UNM's lack of financial oversight of UNM Athletics and its prolonged mismanagement of the PIT Suites is that many of the risk areas identified by the NMOAG were known to UNM, as they were detailed in multiple audit reports dating back to 2010, but UNM and

its management failed to address these areas, which created an environment that would allow for fraud and abuse to occur.

The NMOAG has identified particular areas of risk in the course of our formal inquiry. Our expectation is that UNM will take steps to address these areas to ensure that public dollars and public property are not misappropriated to personally enrich public employees. Ultimately, oversight and compliance with state law and regulations is the responsibility of UNM senior leadership and they must establish a tone and commitment to maintain effective internal controls over compliance to address these deficiencies and prevent their replication.

RISK AREAS IDENTIFIED

Initially, it is crucial that all UNM employees understand their ethical responsibilities under the Governmental Conduct Act, NMSA 1978, Chapter 10, Article 16, (“GCA”), as well as the specific prohibitions and limitations that ensure that public employees conduct themselves solely in the interest of the public. Section 10-16-3 of the GCA provides:

B. Legislators and public officers and employees shall conduct themselves in a manner that justifies the confidence placed in them by the people, at all times maintaining the integrity and discharging ethically the high responsibilities of public service.

C. Full disclosure of real or potential conflicts of interest shall be a guiding principle for determining appropriate conduct. At all times, reasonable efforts shall be made to avoid undue influence and abuse of office in public service.

I. Misappropriation of Public Funds - Scotland Golf Trip

Synopsis: The first basis of the NMOAG’s formal inquiry was the allegations of financial mismanagement that allowed for UNM employees and private donors to expend public funds to attend a Scotland Trip to play golf. Then Vice President of Athletics, Paul Krebs, signed a contract with an out-of-state entity, Anthony Travel, and directed the Lobo Club to pay a deposit for twenty-

four golf packages to Scotland. All payments made to Anthony Travel were made on the UNM Athletics Department purchasing card. The descriptions listed for the Scotland golf trip expenditures were misleading and did not accurately reflect the actual use of the funds. The expenditures were made in multiple small increments to evade the requirement to ask for a spending limit increase and other financial oversight controls. This was all able to be accomplished, and evaded detection initially, because UNM Athletics lacked a dedicated CFO position for the Athletics Department and did not have an established control environment that would allow for a truly independent audit of the Athletic Department. The lack of a proper control environment and CFO oversight also allowed Mr. Krebs to use any purchasing card within the Athletics Department to make a purchase whether he had proper access to the use of the purchase card or not.

The NMOAG also identified potential conflicts of interest related to working for the Lobo Club and being a public employee of UNM. The NMOAG found that Mr. Krebs separated UNM Athletics finances into a separate fund for each sports team. Mr. Krebs then made head coaches responsible for raising funds for their respective teams. Head coaches solicited and delivered cash, check, or credit card information from the donor directly to the Lobo Club. This caused a conflict and a lack of segregation of duties as coaches were responsible for both initiating, receiving, and delivering financial transactions. This creates an environment in which funds can easily be misappropriated without detection.

Current Risk Areas:

- The lack of a financial control environment dedicated to accountability
 - The lack of a dedicated CFO position for the Athletics Department created an inadequate segregation of duties and true oversight of its financial behavior.
 - Currently, the internal audit function of UNM does not have a desirable reporting structure to maintain the independence needed for a strong

internal audit function. The internal auditor reports to President and Board of Regents but also works at the discretion of the EVP/CFO/COO. The EVP/CFO/COO has the potential to direct internal audit away from potential violations.

Recommendations

- UNM must establish a control environment that mandates compliance, welcomes oversight, and allows for a truly independent internal audit process of UNM finances. UNM should consider establishing an Office of Inspector General (“OIG”) or an office of ombudsman for ethics and compliance that would offer a solitary independent oversight arm for UNM.
 - UNM needs to establish a control environment that ensures all contracts submitted on behalf of UNM Athletics are properly reviewed, signed and executed.
- Inappropriate use of out-of-state travel agency
 - Lobo Club fronted money for what was ultimately a UNM expenditure.
 - An out-of-state travel company was only assigned to UNM Athletics for the Scotland golf trip and was not utilized for all Athletics’ travel arrangements.

Recommendations

- Lobo Club is responsible for planning, directing, coordinating, and conducting activities for fundraising. UNM Athletic “trips” should be coordinated by Lobo Club or UNM Foundation, not UNM Athletics.
 - Multiple out-of-state travel agencies should not be used for trip planning and purchasing.
- Lack of procurement card procedures and oversight
 - UNM lacks a dedicated CFO in the Athletics Department who approves transaction before expenses are incurred and audit purchase card use regularly.

Recommendations

- Hire or establish a CFO position in the Athletics Department who will maintain the proper internal financial controls necessary so UNM can properly safeguard its funds, approve transactions before the expenses are incurred to ensure procurement is proper, and audit employee purchase card use regularly, at least monthly if not more frequently.
- There is a need to monitor split transactions or expenditures to the same company to ensure procurement is compliant with state law.

II. Failure to Collect Hundreds of Thousands of Dollars From the PIT Suites

Synopsis: The second basis of the NMOAG's formal inquiry was the allegations of financial mismanagement that allowed for the failure of UNM to collect hundreds of thousands of dollars from the use of the luxury suites and club suites at the PIT ("PIT Suites").

The PIT is a publicly owned facility. However, UNM relies on the Lobo Club to manage the sale of the suites and club seats. The Lobo Club does not have its own agency financial account and deposits all funds it receives in agency accounts controlled by the UNM, except for operating expenses funds. The Lobo Club's deposited funds are then invested by UNM Athletics and all interest earned is allocated to the Lobo Club. The Lobo Club consults with UNM Athletics to establish a schedule for transferring funds received by the Lobo Club to UNM Athletics.

UNM Athletics had unpaid accounts for the use of the PIT Suites dating back to the 2010-2011 Men's Basketball season. The NMOAG formal inquiry uncovered a poor and incomplete accounting procedure for PIT Suites sales between the Lobo Club, who manages the sale of the PIT Suites, and UNM, who owns the PIT. UNM's minimal documentation of the transactions between the Lobo Club and UNM led to loosely managed financial accounts, contracts, if there were contracts at all, and employees in charge accountability. For instance, UNM Athletics failed to maintain numerous contracts between UNM and PIT Suite holders that would detail at least the purchase and total cost of the assigned PIT Suite and the agreed upon payment schedule for the use of the PIT Suite. The ultimate result of this poor and incomplete accounting procedure was that UNM Athletics had at least \$432,000 in uncollected revenue from use of the PIT Suites. What is particularly alarming is that the problems identified by the NMOAG regarding UNM's prolonged mismanagement of the PIT Suites, is that many of these weaknesses have been identified by previous independent audits of UNM, and UNM still has not chosen properly address

these weaknesses. As a result, it is likely that UNM Athletics and the Lobo Club do not have accurate financial statements because they cannot accurately reflect how much money they truly have spent or received from the use of the PIT Suites dating back to 2010.

Additionally, upon executing a search warrant at the Lobo Club, NMOAG Agents observed game tickets and parking passes in plain view and they appeared to be accessible to anyone with no control over disbursement. In addition, the NMOAG investigation found several computer systems in place that do not communicate with one another, making accounting challenging to track.

Finally, multiple allegations were reported that Mr. Krebs provided tickets to donors without seeking payment at his own discretion. These allegations however, cannot be confirmed because UNM Athletics and the Lobo Club did not have a formalized process to track sales and the collection of revenue for the PIT Suites before tickets are distributed. If such gifts or perks were given out as described, violations of the Anti-Donation Clause of the New Mexico Constitution would be implicated. Further it was found that between 2013 and 2014, at least 15 individuals and/or business did not pay for their use of the PIT Suites. This cost UNM Athletics approximately \$206,014.

Previous PIT Suites Audit Findings Regarding PIT Suites:

Outside Audit Firm Issues:

In 2011, KPMG found that the contract retention for the use of PIT Suites was an issue and listed it as an audit finding. Lobo Clubs response was, “The Lobo Club Financial Coordinator will ensure all supporting documentation is well maintained in a consistent manner and organized in files and stored in a secure location. To avoid future exceptions, the Donor Services Coordinator will be more vigilant in obtaining hard copies of all contracts that designate moneys to be given to

the Lobo Club and updating that file throughout the year. The Donor Services Coordinator will also ensure that the PIT Suites contracts are received and filed at the time of purchase and entry into the Titan System.” In 2012, KPMG claimed the issue had been resolved and has not been addressed since the 2011 audit finding.

In addition, during the Special Audit the OSA found that “[c]ontracts were not complete or maintained” and “this lack of record retention has lost the University money.” Going further, the Lobo Club manages the PIT so poorly that the SAO was unable to complete any documentation test work on the PIT Suite sales, contracts, and collections. The SAO noted in the audit, “We quickly realized that the data was very incomplete and highly inaccurate. The work we did on 50% of the population (20 of 40 suites) was so incomplete that we realized additional testing would not give us any more assurance (or lack thereof) and we terminated the testing.” NMOAG confirms that these risk areas have not been addressed.

Internal Audit Issues:

During conversations with UNM Internal Audit staff, it appeared that the UNM Internal Audit Staff was not independent from UNM. The staff were told what groups they could audit and when by UNM Staff.

Current Risk Areas:

Ineffective Management of PIT Suites

- Ticket sales for the PIT Suites began during the 2010-2011 school year. The Lobo Club was responsible for the sale of the suites and club seats. There are 40 suites, however only 37 are sold to the general public and there are approximately 150 club seats. Each suite is comprised of at least: in-suite catering, flat screen TV, 20 tickets, 5 parking passes, and early entry passes. During the 2010 - 2013 contract year the PIT Suites were sold for \$45,000 per year. Due to low sales the cost was lowered to \$42,500.

Recommendations

- UNM must develop a formalized process to track sales and collection of revenue for the PIT Suites before tickets are

distributed. The Lobo Club alone should be responsible for booking a PIT Suite and issuing tickets.

- UNM must develop a policy to track and oversee its cash accounts related to the PIT Suites use.

Lack of Segregation of Duties

- The problematic circular flow of money and oversight between the UNM Athletics, the UNM Foundation, and the Lobo Club leads to mismanagement of the PIT Suites revenue.
- Paul Krebs restricted contact with a specific list of donors in the Lobo Club database. The Lobo club employees were advised not to contact these individuals for any reason.

Recommendations

- Lobo Club manages the sale of the PIT Suites, but UNM owns the PIT. The Lobo Club should be the exclusive facilitator of suite booking. One hundred percent of the net income is ultimately transferred to the UNM Foundation for the building fund. This revenue is important because debt service payments of \$3,000,000 a year are being incurred for the renovation.
- The use and collection of payment for the PIT Suites should be handled in the same manner as general admission tickets and season tickets, which require payment prior to receiving tickets.
- UNM must require that transfers from the Lobo Club to UNM Athletics are segregated.
- Ensure that benefits intended for donors or prospective donors are paid with appropriate funds.
- UNM must formalize all agreements and contracts between the UNM Foundation and Lobo Club. UNM Foundation has currently transferred all donor funds to the Lobo Club but there is little to no oversight or transparency of the spending of those funds. The formalization process should include recognition of pertinent laws, rules and regulations that govern each of the entities. This will create greater accountability and oversight between the agencies.

Lobo Club's Incomplete Accounting Procedure Leads to Financial Mismanagement

- UNM and the Lobo Club's poor and incomplete accounting procedure make it difficult for UNM officials to be held responsible for financial mismanagement.

Recommendations

- A financial officer for the Lobo Club should be solely responsible for managing records, receipts, and reconciling.
- UNM and Lobo Club need to formalize the process regarding the PIT suite costs, contracts, invoicing, and collections; as well as a GAAP and/or GASB approved method of recording and monitoring all contracts and transactions regarding PIT suite activity.
- Lobo Club need an agency financial account that is managed solely by the Lobo Club and not UNM.

- The Lobo Club needs to follow its policy that states that they need to have an annual audit performed by an independent CPA firm in accordance with GAAP.
- Lobo Club should ensure contracts and payments are completed before tickets are distributed.

Anti-donation Violation for Gifting Access to Suites

- The New Mexico Constitution prohibits the state from directly or indirectly donating to or in aid of a private entity. N.M. Const. art. IX, § 14. The Constitution also prohibits loaning or pledging of credit to a private entity.
- The allegation that public employees would take or give out tickets to unpaid suite holders under the assumption the "donor" was going to give a larger donation to a different part of athletics could violate the Anti-Donation clause of the Constitution.
- The Memorandum of Agreement between Lobo Club and UNM Athletics describes funds transferred to UNM by the Lobo Club as "public funds." Lack of safeguarding these funds and/or the donation of any of these funds could amount to Anti-Donation violation.

Recommendations based on Ethical Considerations Regarding Mismanagement

- UNM must establish a tone at the top committed to compliance with the ethical standards contained in the GCA namely that "employees shall conduct themselves in a manner that justifies the confidence placed in them by the people, at all times maintaining the integrity and discharging ethically the high responsibilities of public service."
- The Lobo Club should not to take financial donations from employees being investigated or from any source for a use which is inconsistent with goals and policies of UNM.
- Lobo Club needs to be audited for donor intent, ensuring that the financial donations given were applied to what the donor specified.
- A formal written policy regarding donor solicitations for sports teams needs to be developed. As well as formalized, written segregation of duties for collecting pledges and collecting funds.

III. Use of University E-Mail

Synopsis: Through the course of our formal inquiry, it became obvious that former employees still had access to their UNM email account after their separation. There are also multiple documented emails in which Mr. Krebs instructed current UNM employees to delete public records. This behavior is a clear violation of state law and the ethical principles of the GCA.

Current Risk Areas:

- Allowing former UNM employees to have continued access to UNM email accounts.

Recommendations

- Once employment with UNM ceases so too must access to the former employee's email account. Documents created using a UNM-issued email account belong solely to UNM and are not personal documents of former employees. Under the Public Records Act, NMSA 1978, Sections 14-3-1 to -23 (2018), UNM is responsible for proper retention of public records and UNM cannot effectively manage the retention of its public records if former employees can access and manipulate public records contained in their former email account.
- UNM should immediately disallow account access to former employees the day they separate. This would ensure that public records are safeguarded from destruction. This would also insulate UNM from liability from former UNM employees who may continue to represent themselves as UNM employees.

CONCLUSION

Based on documentation, interviews, and other information received throughout the NMOAG's involvement with UNM and its finances, it is clear that UNM has created a financial control environment ripe for public employees to violate state laws and abuse public resources, without any ability to be tracked, identified, or ultimately held responsible. UNM must establish a control environment that mandates compliance, welcomes oversight, and allows for a truly independent internal audit process. UNM must engage New Mexico oversight agencies regarding the risk areas identified above and report on immediate fixes it is implementing to ensure that public funds are being adequately safeguarded and not being used to personally enrich UNM employees and donors.

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