CAPITAL PROGRAMS

MATTERIALS AND EQUIPMENT MANAGEMENT

AUDIT REPORT #16-2102

Audit & Advisory Services

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# Background

In accordance with the Campus fiscal year 2015-16 audit plan, Audit & Advisory Services (A&AS) conducted an audit of internal controls and associated procedures governing materials and equipment management business practices within the UCLA Capital Programs (CP) department.

*Capital Programs Overview*

The CP department is responsible for conceptualizing, planning, designing, and constructing major capital construction and renovation projects at UCLA. Projects having total costs of $750,000 and above are considered major capital construction. CP develops financial strategies, obtains project approvals, reviews plans and specifications, completes environmental reviews, prepares and negotiates construction contracts, coordinates staging plans, and serves as a repository for project records and as-built plans.

The department’s mission is to create projects that “support the instruction and research mission of the University by providing a physical campus environment that fosters excellence, creativity, and a sense of community.” Capital projects are developed to take into account UCLA land use priorities, established physical designs, University policies and procedures, environmental and regulatory requirements, and community interests.

The CP department consists of the following three areas:

*Capital Planning and Finance* – responsible for planning, environmental assessment, project budgeting, and project financial services including contracts administration. This area is led by an Associate Vice Chancellor who reports to the Vice Chancellor and Chief Financial Officer.

*Design and Construction* – responsible for project design, engineering, permitting and inspection services, project management, and construction management activities. This area is led by an Associate Vice Chancellor who reports to the Vice Chancellor and Chief Financial Officer.

*Administrative Services* – includes building operations, information technology, and personnel, and is overseen by a Director who reports to the Vice Chancellor and Chief Financial Officer.

Purpose and Scope

The primary purpose of the review was to ensure that CP’s organizational structure and controls surrounding its materials and equipment management processes and procedures are conducive to accomplishing its business objectives. Where applicable, compliance with campus and University requirements was also evaluated. The scope of the audit included:

* Materials and Equipment Purchases
* Equipment Inventory and Disposals
* Asset Management System
* Physical Security

The review was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing* and included such tests of records, interviews, and other auditing procedures considered necessary in achieving the audit purpose.

Summary Opinion

Based on the results of the work performed within the scope of the audit, CP’s organizational structure and controls are generally conducive to accomplishing its business objectives related to materials and equipment management activities. However, controls and business practices could be further strengthened by implementing the following:

* Ensure that purchases are coded to the most appropriate sub and object codes during the purchasing process.
* Utilize established vendor agreements to purchase goods and services.
* Process inventorial equipment disposals within the equipment inventory system on a timely basis and ensure that departmental disposal logs are accurate and complete.
* Use Security Tracking of Office Property (S.T.O.P.) plates to strengthen control over laptop and tablet computers.
* Repair or replace the CP server room air conditioning unit and improve the water-based fire sprinkler system.

The audit results and corresponding recommendations are detailed in the following sections of the report.

Audit Results and Recommendations

Materials and Equipment Purchases

Interviews were conducted with CP management and staff to obtain an overview of departmental purchasing procedures, processes, and controls. A judgmental sample of materials and equipment purchase transactions was selected for testing from the General Ledger covering fiscal year 2014-15. The sample transactions were evaluated to verify that they were approved prior to purchase, based on a justified need, accurately coded to the General Ledger, and appropriately entered into the campus Asset Management System (AMS) on a timely basis. Equipment purchases related to capital projects were reviewed to ensure that they are properly and timely transferred to the appropriate client’s custody code. Supporting documentation and other relevant information was obtained and evaluated to verify adequacy and accuracy. A judgmental sample of Low Value Orders (LVOs) was tested to verify appropriate use and that delegation limits were being complied with. Post Authorization Notifications (PANs) related to equipment purchase transactions were examined to assess timeliness of review. Separation of duties related to purchasing processes was also evaluated to determine their adequacy. The following were noted:

A. Equipment Purchases

A&AS generated a query report from the Detail General Ledger to identify equipment items purchased for the CP department in fiscal year 2014-15. The resulting report listed 121 items. Upon grouping the data by BruinBuy ID number and then sorting by purchase amount, seven of the highest cost items were selected for testing. The individual cost for these items varied from $5,000 to over $37,000. Purchases of equipment costing $5,000 or more are considered inventorial equipment. The sample items were tested for General Ledger coding accuracy. General Ledger coding is performed by the CP Accounting unit based on the type and cost of the item per campus-defined accounting codes.

Two items (Dell Power Edge server and an HP Color Printer) have a cost of greater than $5,000 but do not appear on the inventorial equipment list. In addition, these items were coded to the General Ledger using sub-object code 05 (special items) instead of the more appropriate sub-object code 04 (equipment and supplies). Two additional items reviewed (annual maintenance agreements for Cisco servers and Canon copiers) had incorrect object codes. All four test items were found to have the improper object code of 4380 (computing supplies or hardware < $200). The more appropriate object codes for all four test items should have been 9110 (inventorial equipment-computer hardware), 9111 (inventorial equipment-copying equipment), 3100 (maintenance service agreement-computer hardware), and 3110 (maintenance service agreement-copying equipment) respectively. By not properly identifying and distinguishing items during the purchase process, inaccurate General Ledger coding may cause inventorial equipment items not to be properly capitalized or recorded into the AMS. Additionally, miscoding errors could result in non-equipment items not being properly accounted for in the General Ledger.

Recommendation: Management should ensure that all purchases are coded to the most appropriate object code during the acquisition process. Purchases of inventorial equipment (as defined in UC Policy BUS-29, Management and Control of University Equipment), should be coded using sub-object code 04, and maintenance service agreements should be properly coded with object codes 3100, 3110, etc. By properly coding purchases at the point of acquisition, the validity, accuracy and reliability of accounting records and financial reports is strengthened.

Response: Capital Programs agrees that the coding of expenditures is important. Expenses for the current fiscal year are being reviewed and will be corrected via NPEAR prior to March month-close. More stringent reviews in regards to object codes will be conducted when reviewing PANs. At the end of each month, Capital Programs will review the monthly activity to see if there are any object code corrections that need to be made that may have been missed on PAN review.

B. Low Value Orders (LVOs)

To evaluate whether LVOs are being used appropriately and in compliance with University policy 741 (Low-Value Purchases), A&AS accessed the Table of Funds by Department report from the UCLA Online Financial System. Using Capital Programs department code 2700 and fund number 66105, a Fund Balances Report was generated to identify all accounts and cost centers associated with the fund. Transactions from the Detail General Ledger for account number 661500 were sorted to highlight LVOs for review for the period of July 1 through October 20, 2015. From the resulting 37 LVOs identified, 5 sample transactions were selected for testing. Based on the review, it was disclosed that CP processed a non-inventorial equipment purchase and three payments for repair services with LVOs instead of using established vendor agreements. Purchase preparers appear to be unaware of established campus-wide vendor agreements and/or the process of searching for established agreements. Utilizing a vendor agreement provides service standards and pricing that have been reviewed and negotiated by the Campus Purchasing Department. Additionally, using a vendor agreement captures relevant transaction information within the purchasing system for control and historical purposes. By not fully utilizing established vendor agreements, the University may not receive the most favorable pricing terms and conditions or other negotiated protections that may be included in these agreements.

Recommendation: Management should utilize established vendor agreements to ensure purchases of goods and services by the University are at the best overall value, maximize protection of the University's interests by applying appropriate terms and conditions, and help facilitate compliance with University policy.

Response: Management agrees with this recommendation. A reminder will be sent to the Capital Programs Financial Services staff to ensure that established vendor agreements are utilized when appropriate.

Equipment Inventory and Disposals

A&AS interviewed selected CP management and staff to gain an understanding of departmental equipment inventory and disposal processes, procedures, and controls. A judgmental sample of inventorial equipment items was identified for testing from AMS as of October 12, 2015. Selected equipment items were physically located to verify their existence and property tag number, and to evaluate the accuracy of property descriptions within AMS. An additional judgmental sample of inventorial equipment disposals was selected from AMS as of December 2, 2015. Supporting documentation for the selected disposal items was reviewed for adequacy, including timely processing within AMS, and that an appropriate audit trail is maintained. A&AS evaluated processes over ensuring that any hard drives were “wiped” prior to the equipment being disposed. Compliance with campus and University policies and procedures governing equipment disposals, including separation of duties, was also assessed. The following was noted:

A. Equipment Disposals

Disposal of inventorial equipment is not always being processed in AMS on a timely basis. One of four equipment disposals tested disclosed that in January 2013, an equipment item (Catalyst 6000, asset #24003181) was traded-in with the purchase of new equipment. However, the disposal item was not processed in AMS until May 2015, 29 months after the trade in occurred. Additionally, one of four equipment disposal test items does not appear on Capital Programs’ disposal log. The equipment item (tape library, asset #44002991) was one of several pieces of equipment that were disposed of in bulk. However, the serial number and/or asset number was not recorded on the log as items were being picked-up for disposal. Additionally, the disposal log was not signed and dated by the preparer(s), or by Capital Programs management, attesting to the log’s accuracy.

Recommendation: Management should ensure that inventorial equipment disposals are appropriately and timely processed in AMS at the time of disposal. By doing so, management will be more effectively accounting for the asset’s final disposition and maintaining prudent control of the property. Additionally, management should ensure that relevant equipment information is accurately recorded on its departmental disposal log to maintain an adequate audit trail. Lastly, the equipment disposal log should be signed and dated by both the preparer and authorized reviewer at the time of disposal to strengthen accountability for the disposal process.

Response: Management agrees with the recommendations and is reviewing reconciliation steps to ensure accuracy between the campus logs and our own inventory logs.

Asset Management System

Interviews were conducted with selected CP management and staff, and the campus Equipment Management Administrator to obtain an overview of AMS, including controls over assigning system access rights, departmental user structure, and the roles of each authorized CP system user. AMS reports and other relevant supporting documentation regarding access rights granted were evaluated for adequacy and to verify that proper separation of duties is being maintained.

Test work indicated access to CP custody codes is appropriate. For each custody code, there is a custodian, department approver and a department representative.  The equipment custodian has full edit rights and is responsible for updating information within AMS. The department representative serves as the custodians back-up and the department approver is responsible for approving transactions within AMS. Access to AMS is controlled by UCLA Equipment Management and the department approver is controlled by the Departmental Security Administrator (DSA).

No significant control or operational concerns were found in this area.

Physical Security

Discussions were held with CP management to ascertain the departmental business practices and controls over inventorial equipment inventory and non-inventorial theft-sensitive equipment such as laptop and tablet computers. Observations were conducted of areas where equipment is installed, maintained and stored. During our physical observation of selected test items described in the “Equipment Inventory and Disposals” section of this report, we also evaluated the areas in which those items reside for any conditions that pose a risk to the security of the asset(s). Additionally, we inspected non-inventorial theft-sensitive equipment such as laptop and tablet computers to determine if S.T.O.P. plates are being utilized.

A. Security Tracking of Office Property (S.T.O.P.) Plates

Laptop and tablet computers do not have UC Police Department (UCPD) asset protection S.T.O.P. plates. The S.T.O.P. plate program is offered as part of a crime reduction initiative and theft deterrent system for highly portable and easily re-sellable electronic devices.

Recommendation: Management should consider utilizing the S.T.O.P. plate program to strengthen its control over laptop and tablet computers, and discourage opportunistic theft of such items.

Response: Laptops and tablet device have software tracking installed on devices in case of thefts. Management will continue to evaluate various options to assist with equipment security.

Audit Observation

An additional observation regarding Capital Programs’ server room was identified during the review as described below.

A. Server Room Environment

During a site visit to the CP server room, A&AS observed that the air conditioning unit has a leaking condensation pan. The pan has a temporary fix in place comprised of fabricated sheet metal, a garden hose, and a bucket. The existing condition within the server room creates a risk for potential water damage to the servers and related equipment. Additionally, the air conditioning unit appears to be old and may be approaching the end of its useful life. A partial or complete failure of the air conditioning unit may cause excessive heat to build up in the server room resulting in damage to the server equipment or fire. Should excessive heat accumulate or a fire ignite, the fire sprinklers mounted in the room’s ceiling would likely be triggered. The risk of water damage will remain as long as sprinklers continue to be utilized for fire suppression in the server room.

Recommendation: Management should consider repairing or replacing the CP server room air conditioning unit as soon as possible to adequately maintain and safeguard its essential business systems. Additionally, management should consider installing an alternative non-water fire suppression system to avoid potential water damage in the event of a fire, accidental triggering of the traditional water based fire sprinklers, or malfunction. By doing so, management will further safeguard the physical environment where its valuable server equipment resides, and reduce the risk of business interruption and diminished productivity in the event of an emergency.

Response: The server room air conditioning unit repair has been completed. Other server room safeguards include: Over the door backup air conditioner and a temperature probe with automatic email alerts of unacceptable server room temperatures. A non-water fire suppression system is also being evaluated by management.

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