HOUSING & HOSPITALITY SERVICES

VENDING SERVICES PROCUREMENT AND INVENTORY

AUDIT REPORT #19-2203

Audit & Advisory Services

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Background

In accordance with the UCLA Administration fiscal year 2018-19 audit plan, Audit & Advisory Services (A&AS) performed an audit of internal controls and business practices over Vending Services procurement and inventory activities.

UCLA Vending Services supplies the campus community with convenient, high-quality food and beverage selections in approximately 300 vending machines at more than 80 locations across the campus. Procurement and inventory management over the vending machines is the responsibility of the Vending Services team, which includes 11 full-time employees and four student employees. The vending manager, who reports to the assistant director of Dining Services, oversees the operation. A vendor-provided vending management system called “Vendsys” is utilized to support the operation. Vending Services is a self-supporting operation, with revenue of $2.8 million, expenses of $2.5 million, and net operating revenue of about $269,000, for fiscal year 2017-18.

Purpose and Scope

The primary purpose of the audit was to ensure that the related systems and procedures surrounding procurement and inventory are conducive to accomplishing Vending Services’ business objectives. The secondary purpose was to evaluate the adequacy and efficiency of the internal controls over procurement and inventory activities. Where applicable, compliance with campus and University policies and procedures was also evaluated.

The scope of the audit focused on the following:

* Purchasing, Receiving, and Invoice Processing
* Inventory Management

The audit was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing* and included interviews, tests, and other procedures considered necessary to achieve the objective.

Summary Opinion

Based on the results of the work performed within the scope of the audit, Vending Services' overall structure and controls are generally conducive to accomplishing its business objectives related to procurement and inventory activities. However, controls and business practices could be further strengthened by implementing the following:

*Separation of Duties*

* Due to Vending Services limited staff, a complete separation of duties with regard to ordering, receiving, physical inventories, and reconciliations is difficult to achieve. Management should designate an independent person from Vending Services to perform a periodic sample review of purchasing and inventory records as a mitigating control.

*Inventory Management*

* Vending Services should evaluate which routes may benefit from pre-kitting. In addition, management should continue with their efforts to replace or upgrade older equipment that does not DEX (a standard digital format adopted by the National Automatic Merchandising Association Technology Committee) correctly.
* Management should consider documenting the optimal inventory levels and re-order points in the event the vending manager is out of the office for an extended period.
* The Warehouse Inventory Variance Report should be reviewed and refined for improved accuracy and reliability. Guidelines and thresholds for inventory variances that warrant further review should also be established.
* Periodic physical inventory counts of the route / truck inventories should be performed jointly by two people, including an independent person. Management should continue with their efforts to replace or upgrade older equipment that does not DEX correctly, which will improve the accuracy and reliability of the route / truck inventory variance report. Management should then review the report on a regular basis.
* The requirement to log food waste on the handheld devices should be communicated to route staff. In addition, food waste reports should be regularly reviewed by management.
* To enhance security over vending inventory in the warehouse, management should consider the following:
* Install an electronic key card system, which can provide better controls over who and when access is allowed and also provide an audit trail.
* Fence off access to the areas in the warehouse where vending inventory is maintained.
* Install security cameras inside the warehouse.

*Purchasing, Receiving, and Invoice Processing*

* UCLA Vending Services should work with UCLA Campus Purchasing to:
* Request that Avendra competitively bid out the vending food and beverage items contract when the current Vistar agreement expires in August 2020.
* Identify whether there are any other vendors, in addition to Vistar, to compare pricing and provide competition. The ASUCLA Store Buyer / Manager shared a list of vendors that ASUCLA uses to purchase chips, cookies, candy, nuts, sandwiches, and other snacks. UCLA Vending Services should consider comparing the items and prices offered by these vendors to the Vistar's prices.
* UCLA Vending Services management should determine whether it would be more cost effective to obtain the safer sex health products and birth control pills directly from a vendor rather than from ASUCLA.
* Management should ensure that all mandatory reviewers are reviewing their Post-Authorization Notifications (PANs) in a timely manner, and are in compliance with the UCLA Financial Policy.

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

Audit Results and Recommendations

Separation of Duties

Due to Vending Services’ limited staff, adequate separation of duties (with purchasing, receiving, and inventory management) is difficult to achieve. The vending manager is responsible (or/and the backup) for multiple key processing functions, such as approving and placing orders; receiving items; approving invoices; physical inventory counts; reviewing inventory variances; and reviewing and approving wasted items.

Recommendation: To help minimize the risk associated with a lack of separation of duties due to staffing constraints, management should perform the quarterly review of purchasing and inventory records by someone independent from Vending Services. The independent review should include the following:

* Select a sample of purchases; obtain the supporting invoices; and verify that the purchases were authorized for business purposes.
* Verify that monthly inventories were performed for the warehouse and all of the trucks’, and inventories were conducted by two employees. Review inventory variances and ensure they have been researched to minimize the risk of inventory shrinkage and misappropriation.
* Review food waste levels to ensure that they are within expected thresholds and wasted items are appropriate and properly authorized.

This recommendation was included in our previous 2013 and 2016 audits. A mitigating control that was recommended and instituted by management was a quarterly review of purchasing and inventory records by a person independent of Vending Services. The UCLA Dining Services Assistant Director was responsible for performing these independent quarterly reviews; however, these reviews have not been conducted since the summer of 2018.

Response: Agreed, effective September 2019, the UCLA Dining Services Assistant Director will perform these reviews on a quarterly basis. In order to formalize the process, UCLA Vending Services Manager and UCLA Dining Services Assistant Director will develop a quarterly, dated checklist that will be submitted to the Senior Director of Food and Beverage by September 30, 2019.

Inventory Management

Vending Machines Inventory and Refill Routes

Discussions were held with the vending manager, vending technician, and vending route staff to determine whether vending machines are routinely checked and refilled; the refill schedule is regularly reviewed and adjusted as appropriate; the routes are efficient and multiple visits to the same machines are minimized; and inventory needed to refill machines is accurately identified.

Refill schedules have been established by the vending manager based on analysis of sales and inventory turnover per vending machine. Some machines are refilled daily, others one to three times per week, and slower selling machines once every two to four weeks. The vending manager reviews multiple Vendsys reports daily to help create and adjust the route schedules, prioritizing the vending machines that need to be refilled and collected.

* Machine Service Report – main report for printing the daily route schedules and contains pertinent information related to route scheduling.
* Asset Center Report – shows the last time each vending machine was serviced and collected.
* Machine Activity Report – revenue and units sold per vending machine.
* Machine Scheduling Report – refill schedule for vending machines.
* USAT Rollover Report – provides a breakdown of revenue (credit card, BruinCard, cash) for each vending machine.

Vending machine refill routes are primarily based on product category with separate routes for beverages, candy and snacks, food, coffee, and ice cream. Concerning organizing routes based on the geographic proximity of vending machines, the vending manager indicated the following:

* It may make more sense for organizations where vending machines are more geographically dispersed; however, the majority of UCLA vending machines are located on-campus and in close proximity to the vending warehouse and other vending machines.
* Larger vending trucks would need to be purchased to accommodate the additional inventory and product variety needed to refill the different types of vending machines.  This would be a significant expenditure, at least $300,000 to $400,000.  In addition, the existing beverage trucks were provided to UCLA free of charge as part of the Coke and Pepsi contracts.
* The route schedules vary among the different product categories based on sales and inventory turnover.  For example, a snack machine and ice cream machine may be located at the same location; however, if customers purchase more snacks than ice cream, the refill schedules for the machines would be different.

Pre-kitting

Vending route staff rely on their experience, not available Vendsys reports (such as the Route Pick Sheet Report or Driver Restock Report) to determine the amount of inventory needed from the warehouse and trucks to refill the vending machines on their assigned routes. The vending manager indicated the following about the refill process:

* The Route Pick Sheet Report and Driver Restock Report is not utilized as they are not pre-kitting, which is the pre-packing of the exact inventory needed to refill each vending machine in separate tote boxes.
* Pre-kitting is not being done because of insufficient space within the vending warehouse and trucks for all the separate tote boxes, and the vending storekeeper has been out on leave.
* Vending trucks are currently used as roving warehouses, maintaining inventory in the trucks to refill the vending machines.
* For routes that include buildings where vending machines are located on different floors, rooms, and areas, it may be helpful to rely more on the Vendsys reports to identify the inventory needed to refill the machines and reduce the likelihood of having to return to the truck to retrieve more inventory.  However, for other routes where vending staff can park their trucks right next to the vending machines, the benefits of pre-kitting would be minimal.
* Pre-kitting requires that vending machines accurately communicate sales and inventory data to Vendsys in order to generate accurate reports of inventory needed to refill these machines. The communication of these transactions is accomplished through a standard digital format adopted by the National Automatic Merchandising Association Technology Committee called DEX. According to the vending manager, as of April 2019, there were 44 vending machines that do not DEX correctly; however, they are in the process of replacing or upgrading the older equipment in these machines.

Recommendation: Vending Services management should evaluate which routes may benefit from pre-kitting. In addition, management should continue with their efforts to replace or upgrade older equipment that does not DEX correctly.

Response: Agreed, management has completed an evaluation of larger routes and has determined that one of the soda routes would benefit from pre-kitting. For this location, drivers will pre-kit from trucks for now to save time. Once all machines that do not DEX reliably have been updated, Vending Manager will identify smaller routes that could be pre-kitted from the warehouse. To ensure progress is made, Vending Manager will provide a list of all machines that do not DEX reliably to the Senior Director of Food and Beverage by September 15, 2019. Upon receiving this list, the Senior Director will outline a replacement schedule with the Assistant Director.

Optimal Inventory Levels

Audit work included discussions with the vending manager to determine whether adequate procedures are in place to ensure that optimal inventory levels are maintained. The vending manager physically checks the inventory levels in the warehouse and based on their many years of experience in UCLA Vending Services, determines which items and quantities need to be reordered. The vending manager is the only person authorized and responsible for ordering inventory items. In the rare instances that the vending manager is out of the office, he will write down what needs to be reordered and instructs another vending employee to place the order. Optimal inventory levels and re-order points have not been formally documented.

Recommendation: Management should consider documenting the optimal inventory levels and reorder points in the event the vending manager is out of the office for an extended period.

Response: Agreed, management will establish and document optimal inventory levels for the staff to follow when the Vending Manager is out of the office. Management will complete the documentation by September 30, 2019. Note – the Lead Storekeeper is aware of the proper inventory levels. Management will establish par levels based on the academic and non-academic year for items consistently sold throughout the year. The Vending Manager consistently reviews level of products based on sales and consumption and will only establish par levels once items become part of the permanent sales.

Physical Inventory Counts and Variances

A&AS selected a judgmental sample of three months (November and December 2018, and January 2019), obtained and reviewed the Warehouse Inventory Count Variance Reports and Route Stock Count Reports to verify that physical inventory counts were performed of the vending warehouse and routes / trucks, by two employees, and significant variances were researched and explained.

The following was noted:

Physical inventory counts of the vending warehouse were performed by two employees – the vending manager and vending mechanic. Physical counts of route / truck inventories were also performed.

The vending manager indicated significant inventory variances would be identified through their monthly monitoring of overall food costs compared to budget and sales revenue. For fiscal year 2017-18, the overall food costs and vending sales revenue variance compared to budget was less than one percent.

1. Warehouse Inventory Variances

Physical inventory counts of the vending warehouse were performed for the sampled months and reviewed by two employees – the vending manager and vending mechanic.

There is a monthly Warehouse Inventory Variance Report, which the vending manager indicated is reviewed; however, guidelines and thresholds for variances that warrant further review have not been defined. In addition, the report includes inaccurate data such as negative quantities, which affects the accuracy of the inventory variances calculated and reliability of the report.

Recommendation: The Warehouse Inventory Variance Report should be reviewed and refined for improved accuracy and reliability. Guidelines and thresholds for inventory variances that warrant further review should also be established.

Response: Agreed, management will re-establish the previous guideline in effect of 2.5% or $250 variance per route product group. For the record, overall over/short for each month from December 2018 through April 2019 was ($21.13), $232.05, ($55.26), ($86.29), and ($72.68), respectively. Management will tie in inventory control to Vendsys.

1. Route / Truck Physical Inventory Counts

Physical counts of route / truck inventories were performed for the sampled months reviewed. However, due to staffing limitations, route staff count their own inventory, and two people are not involved in the process. There is a route / truck inventory variance report; however, the vending manager indicated the report is not accurate and reliable due to issues with some vending machines that do not DEX properly, thus the report is not reviewed. The vending manager indicated that as of April 2019 there were 44 vending machines that do not DEX correctly; however, they are in the process of replacing or upgrading the older equipment in these machines.

Recommendation: Periodic physical inventory counts of the route / truck inventories should be performed jointly by two people, including an independent person.

Vending Services management should continue with their efforts to replace or upgrade older equipment that does not DEX correctly, which will improve the accuracy and reliability of the route / truck inventory variance report. Management should then review the report on a regular basis.

Response: Agreed, effective September 30, 2019, periodic (quarterly) physical inventory counts of route/truck inventories will be performed jointly by two people, including an independent person. Management will work to correct machines.

Food Waste Tracking and Monitoring

UCLA Vending Services has reduced food waste by finding new products with a longer shelf life, such as shelf-stable milk, and reducing products with short expiration dates, such as fresh deli sandwiches. Vending Services staff are responsible for checking and removing expired items when refilling the vending machines. Also, expired items are supposed to be logged with handheld devices; however, the vending employee responsible for checking the food and milk machines, which have items with the shortest expiration dates, has not been logging expired items because the employee thought this was no longer required with the new Vendsys system. In addition, food waste reports are available from the Vendsys system but have not been utilized.

Recommendation: The requirement to log food waste on the handheld devices should be communicated to route staff. In addition, food waste reports should be regularly reviewed by management.

Response: Agreed, all route personnel have been instructed to record food waste on their handheld devices. Note – since Vending is currently selling shelf-stable milk and frozen sandwiches with increased shelf life, food waste from vending machines is minimal. All food waste is returned to the warehouse and logged into a singular report.

Physical Security

Vending inventory items are stored in multiple locations including a warehouse, vending trucks, and vending machines. Physical security over these areas was reviewed, and the following was noted:

The UCLA Vending Services warehouse has two loading docks with pull down doors, which are only open when a delivery is being made or vending trucks are being loaded. The pull-down doors are secured with padlocks. There is a regular door for UCLA Vending Services staff to access the warehouse and office, which is open during regular business hours and locked after hours. There is another regular door in the middle of the two loading docks; however, this door is not used and is kept locked. Previously, a portion of the warehouse where the candy and snack items were stored was fenced off and locked after regular business hours. However, since the vending storekeeper has been out on leave, vending route staff need access to retrieve these items on their own to refill vending machines. As such, the candy and snack area has not been fenced off and locked. After the vending storekeeper returns from leave, they will reconsider further restricting access to these items again.

In addition, a door provides access to the vending office area, which is locked at all times and visitors must ring a doorbell and let in by UCLA Vending Services staff. There is a separate storage room in the Vending Services office area, where inventory for coffee and health products are stored. There are no external doors that provide access to this room; it can only be accessed from the Vending Services office area, through one door, that is equipped with a standard lock and key. The vending manager indicated that aside from management, the lead vending mechanic, and a vending mechanic have keys to this door. The door is locked after regular business hours. There is no security camera surveillance over this back storage room; however, there are no external doors that provide access to the room.

Two security cameras provide surveillance of the loading docks. The UCLA Access Control associate director, whose team is responsible for managing the security cameras for Housing & Hospitality Services (H&HS), confirmed the vending security cameras are functioning and there have not been any issues.

The back of the vending trucks where inventory is stored is secured with padlocks. Vending machines are locked and a key is required to open the machines. Vending keys are secured in an electronic key cabinet in the Vending Services office, which is restricted to UCLA Vending Services staff.

*Bakery Staff Access to Vending Warehouse*

Approximately 18 months ago, the bakery unit from Dining Services began sharing the freezer in the vending warehouse to store pastries. Eight baking staff members have keys to access the vending warehouse. Baking staff employees occasionally need to access the warehouse after regular business hours and weekends, to store or retrieve bakery items in the freeze, when vending staff employees are not there. The freezer is located in the main vending warehouse area, thus, bakery staff also have access to all the vending inventory items.

Recommendation: To enhance security over vending inventory in the warehouse, management should consider the following:

* Install an electronic key card system, which can provide better controls over who and when access is allowed and also provide an audit trail.
* Fence off access to the areas in the warehouse where vending inventory is maintained.
* Install security cameras inside the warehouse.

Response: Management will resume fencing off access to snack inventory. Additionally, management will explore the feasibility of utilizing electronic key card access and installing additional cameras inside the warehouse.

Purchasing, Receiving, and Invoice Processing

Competitive Bidding

Vending activity of raw food items purchased during fiscal year 2017-18 were analyzed to identify vendors, the items for which total purchases exceeded the threshold, and the vendors which would require competitive bidding. The review disclosed there were only two vendors, Coca-Cola and Vistar. Coca-Cola was awarded a 10-year campus-wide agreement based on a competitive bid process. Below is a summary of the Vistar agreement.

1. Competitive Bidding – Vending Food and Beverage Items

In the past, there were two main suppliers of vending items that UCLA Vending Services obtained bids from every three months to compare prices, Vistar and Vend Catering Supply.  However, Vistar acquired Vend Catering Supply in 2018 and since then there has only been one main supplier for a majority of the vending items purchased including candy, chips, cookies, food, beverages, and coffee products.

UCLA Dining Services, including UCLA Vending Services, has an agreement with a Group Purchasing Organization called “Avendra.”  As part of the agreement, Avendra provides a list of contracted suppliers, which Avendra states has been awarded to the lowest responsible bidder that meets specifications based on one of the following University-approved bid evaluation methodologies: cost alone, cost per quality point, or best value. Although Vistar is an Avendra-approved supplier, the Vistar agreement has not been competitively bid out since 2009. UCLA Campus Purchasing associate director indicated he expects Avendra to bid out the vending contract when the current Vistar agreement expires in August 2020.

Recommendation: UCLA Vending Services should work with UCLA Campus Purchasing to:

* Request that Avendra competitively bid out the vending food and beverage items contract when the current Vistar agreement expires in August 2020.
* Identify whether there are any other vendors, in addition to Vistar, to compare prices with and provide competition. The ASUCLA Store buyer / manager shared a list of vendors that ASUCLA uses to purchase chips, cookies, candy, nuts, sandwiches, and other snacks. UCLA Vending Services should consider comparing the items and prices offered by these vendors to Vistar's prices.

Response: Agreed, management will continue working with UCLA Campus Purchasing to identify bid products and is in the process of contacting other vendors with regard to pricing and product line. Management will work directly with Avendra and ASUCLA to determine where they purchase product to compare prices.

1. Safer Sex Health Products Prices

ASUCLA and Arthur Ashe Student Health and Wellness Center collaborated with UCLA Vending Services to make safer sex health products and birth control pills more accessible to students by offering them in a couple vending machines since October 2017. UCLA Vending Services purchases these items from ASUCLA, which charges a markup, rather than purchasing directly from a vendor.

Recommendation: UCLA Vending Services management should determine whether it would be more cost effective to obtain the safer sex health products and birth control pills directly from a vendor rather than from ASUCLA.

Response: Agreed, Vending Services recently became an Afaxys GPO member and is now purchasing sex health products direct from R&S Northeast.

Post-Authorization Notification (PAN) Reviews

Twenty purchases from fiscal year 2018-19 were judgmentally sampled and reviewed, noting that all of the purchases were authorized by the Vending manager. A&AS identified documentation and evidence of receipt of goods, and the prices on the invoices matched the agreement prices. Audit testing disclosed the following concerns.

For all UCLA Vending Services purchases, the vending manager and Dining Services assistant director have been setup as Mandatory Reviewers. For purchases exceeding $5,000, there are additional Mandatory Reviewers including the H&HS finance director, H&HS Central Services principal budget analyst, and Financial & Administrative Services executive director. For purchases exceeding $20,000, the H&HS Assistant Vice Chancellor (AVC) is an additional Mandatory Reviewer. According to the UCLA Financial Policy, Principles of Financial Accountability, “A reviewer must review a transaction within two working days of receipt.” Timely PAN reviews help to ensure that transactions are proper and appropriate. Based on our judgmental sample of 20 purchases, the following was noted:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Purchasing Mandatory Reviewer** | **Total # of PANs** | **Reviewed in 2 Days**  **or Less** | **Reviewed in 2 Days**  **or more** | **Range**  **(# of Days)** | **Average**  **# of Days Before Review** |
| Vending Manager | 20 | 15 | 5 | 0-5 | 1.6 |
| Dining Services  Assistant Director | 20 | 4 | 16 | 0-19 | 10.2 |
| H&HS Finance Director | 6 | 3 | 3 | 0-5 | 2 |
| Executive Director Financial & Administrative Services | 6 | 4 | 2 | 0-7 | 2.5 |
| H&HS AVC | 1 | 1 | 0 | 0 | 0 |

Recommendation: Management should remind mandatory reviewers to read their PANs in a timely manner to help ensure that transactions are proper and appropriate, and are in compliance with the UCLA Financial Policy.

Response: Agreed, management will remind mandatory reviewers to read their PANs in a timely manner. In the event of a leave of absence, the Assistant Director will advise the Associate Director to review PANs.

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