

April 16, 2015

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***Subject: Graduate Programs – Rady School of Management
Project 2015-37***

The final audit report for Graduate Programs – Rady School of Management, Audit Report 2015-37, is attached. We would like to thank all members of the department for their cooperation and assistance during the audit.

The findings included in this report will be added to our follow-up system. We will contact you at the appropriate time to evaluate the status of the corrective actions. At that time, we may need to perform additional audit procedures to validate that actions have been taken prior to closing the audit findings.

UC wide policy requires that all draft audit reports, both printed (copied on tan paper for ease of identification) and electronic, be destroyed after the final report is issued. Because draft reports can contain sensitive information, please either return these documents to AMAS personnel or destroy them. We also request that draft reports not be photocopied or otherwise redistributed.

David Meier
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Attachment

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AUDIT & MANAGEMENT ADVISORY SERVICES

Self-Supporting Graduate Programs – Rady School of Management
April 2015

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Project Number: 2015-37

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I. Background

Audit & Management Advisory Services (AMAS) has completed a review of Self-Supporting Graduate Degree Programs (SSGDPs) in the Rady School of Management (RSM) as part of the approved audit plan for Fiscal Year 2014-15. This report summarizes the results of our review.

In an effort to increase degree program funding and accommodate new groups of students, the University of California (UC) adopted the Policy on Self-Supporting Part-Time Graduate Professional Degree Programs in 1996. The policy was revised in 2011 to provide additional guidance and distinctions between self-supporting and state-supported programs. While SSGDPs are expected to adhere to the same UC academic standards as other graduate degree programs, they may not be supported by state general funds. SSGDPs also differ from state-supported programs in a number of other ways. SSGDPs are primarily directed at non-traditional student populations including full-time employees, employer-supported students, and international students. Additionally, programs may be offered during evenings, weekends, or summers.

Per UC's 2011 policy guidelines, SSGDPs are expected to become fully self-supporting within three years, meaning that SSGDP student tuition and fees should be sufficient to cover all direct and indirect costs associated with the program. While these programs do not receive state support, they may be subsidized with non-state funds to cover deficits or meet strategic needs. Any excess revenue generated from SSGDPs may be used to support the University's core academic mission.

Each year SSGDPs must submit a Cost Analysis report to the University of California Office of the President (UCOP) Budget and Capital Resources office in addition to an annual program tuition and fees request. The Cost Analysis demonstrates whether program tuition and fees are sufficient to fully cover direct and indirect expenses related to the program.

RSM was founded with the intent of being a fully self-supporting activity and did not receive permanent funding at inception. Therefore, its funding model has evolved over the years to comply with changing SSGDP reporting requirements.

For Fiscal Year 2014-15, RSM offered two SSGDPs: the Flex MBA and the Master of Finance (MF). Established in 2004, the Flex MBA is intended for working professionals with a focus on innovation. Students choose between a weekend or evening program. Both program options require the completion of 92 academic units for graduation and are typically completed over 24 to 30 months. Program fees include textbooks, parking, meals, and lodging. Flex MBA program enrollment and financial activity for Fiscal Years 2010-11 through 2012-13 were as follows:

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| Flex MBA Program | FY 2010-11 | FY 2011-12 | FY 2012-13 |
|---|-----------------------|----------------------|----------------------|
| Average FTE Program Student Enrollment¹ | 180 | 156 | 149 |
| Average FTE School Student Enrollment¹ | 605 | 922 | 879 |
| Program Fee¹ | \$32,635 ² | \$1,025 ³ | \$1,065 ³ |
| Program Revenues¹ | \$5,866,132 | \$5,669,163 | \$5,796,068 |
| Total Cost per FTE student¹ | \$23,721 | \$36,778 | \$37,388 |
| Program Surplus (Loss) | \$1,596,352 | \$(68,205) | \$228,256 |

The one-year MF program is RSM’s newest SSGDP addition, admitting its first cohort of approximately 50 students in fall 2014. The MF program aims to provide hands-on training with an emphasis on quantitative and analytical skills. The program requires the completion of 52 academic units, culminating in a final capstone project.

II. Audit Objective, Scope, and Procedures

The objective of our review was to evaluate RSMs practices for the management of revenue generating graduate degree programs. The scope of the review included the Flex MBA and MF programs.

In order to achieve our objectives we completed the following:

- Reviewed the 2011 Policy of Self-Supporting Graduate Degree Programs;
- Interviewed the RSM Assistant Dean of Finance and Administration and the Assistant Dean of the MBA program;
- Interviewed the Campus Budget Office Assistant Budget Director;
- Reviewed the RSM, Flex MBA evening, and MF proposals;
- Reviewed the Flex MBA Cost Analysis reports for 2010-11 through 2014-15;
- Reviewed and evaluated the direct expense index list and direct cost allocation percentages for the Flex MBA, as provided by RSM;
- Examined RSM’s reconciliation between the financial activity posted to the Integrated Financial Information System (IFIS) Flex MBA funds and financial information on the Cost Analysis report for Fiscal Year 2012-13;
- Evaluated the methodology used by RSM to allocate Flex MBA program costs to the appropriate IFIS fund; and
- Reviewed RSM and MF program financial accessibility goals.

¹ Source: Annual Cost Analysis reports submitted to UCOP

² Annual fee per student (average)

³ Annual fee per unit

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The scope of this review did not include a detailed review of MF program revenues and expenditures, as the program enrolled its first cohort of students during our review, in fall 2014. Consequentially, we were not able to conclude as to the effectiveness of practices in oversight of that program.

III. Conclusion

Based on our review, we noted opportunities for improvement in RSMs practices for the management of the revenue generating Flex MBA graduate degree program. While the Cost Analysis reports submitted to UCOP reported that Flex MBA program revenues were sufficient to fund program expenses, expenses included on the Cost Analysis report could not be readily reconciled to IFIS at the fund level. We identified opportunities to improve the RSM model by utilizing additional Flex MBA sub funds for allocating Flex MBA direct costs to provide greater visibility and reconciliation at the fund level to the Cost Analysis report. This observation is discussed in further detail in the balance of this report.

IV. Observation and Management Corrective Actions

A. Program Cost Allocations

Direct expenses reported on the Fiscal Year 2012-13 Flex MBA Cost Analysis report did not agree to expenses posted to the Flex MBA IFIS fund.

As mentioned above, a Cost Analysis report must be submitted to UCOP annually to report the financial activity of the program. Ideally, revenues and expenses reported on this annual Cost Analysis report materially agree to revenues and expenses posted in an IFIS fund that has been established to account specifically for the financial activity of the program.

Determining the Flex MBA's use of resources can be challenging at the fund level. In addition to the Flex MBA self-supporting program, RSM also administered undergraduate, full-time MBA, and PhD programs during FY 2012-13, which are state-funded. However, all of RSM's programs share particular resources (e.g. admissions and career staff, certain supplies and expenses, and travel). Because these expenses are not uniquely identifiable to the Flex MBA program, these costs are considered allocated costs.

Due to the number of programs RSM manages and the complexity in isolating Flex MBA expenses, expenses associated with the Flex MBA have been charged across index codes specific to general funds, state-funds, and the Flex MBA fund. This makes it difficult to extract Flex MBA-specific expenses from IFIS. The majority of Flex MBA program expenses, including direct and indirect expenses,

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were recorded in the Flex MBA fund 20228A. However, RSM also posted shared direct costs to full-time MBA fund 20225A, general fund 19900A, non-resident tuition fund 19942A, as well as to various fellowship funds for financial aid expenditures.

Due to the amount of intermingling of shared state-supported and Flex MBA costs in IFIS at the fund level, RSM extracts operational data from IFIS by index into several Microsoft Excel worksheets to calculate and organize direct and indirect expenses in the UCOP Cost Analysis reporting format. The worksheet formats separate IFIS indexes from the funds listed above into seven different cost pools, and assign percentages to each cost pool to calculate costs allocable to the Flex MBA program. The cost pools, and percentages assigned to each pool, were as follows:

- Instructional – 100%
- Other Direct Costs – 100%
- MBA Programs – 41.27%
- MBA Career Services – 20%
- Faculty Startup – 28.76%
- PhD Programs – 24.54%
- School IDC – 20%

In accordance with the UCOP Cost Analysis format, all costs calculated using the above percentages were reported on the Cost Analysis report as total direct costs. The percentage allocations are based on RSM's best estimates of effort or resources devoted to the Flex MBA program. **Attachment A** compares the expenses posted to the Flex MBA fund to the direct expenses shown on the Fiscal Year 2012-2013 Cost Analysis, and includes a general explanation for the methodology used to determine the finalized amounts on the Cost Analysis.

During our review, RSM provided documentation of their Excel reporting worksheets, which were used to calculate direct expenditures for the Flex MBA Fiscal Year 2012-2013 Cost Analysis report submitted to UCOP. Based on our review of the Cost Analysis reports and the IFIS funds used to account for Flex MBA program financial activity, we identified opportunities for RSM to improve accounting practices to provide greater visibility for program expenditures at the fund level. The areas of potential improvement are summarized in **Attachment B**.

One additional best practice is to establish a separate sub fund to account for the use of surplus balances, and transfer surpluses to this fund on an annual basis. RSM did not have a separate fund to account for the use of surplus balances.

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Management Corrective Actions:

RSM has created fund 20228B to separately account for all Flex MBA direct expenses and fund 20228C to account for all Flex MBA indirect expenses.

In order to strengthen the accounting practices for the Flex MBA program, RSM will:

1. Use the newly created Flex MBA fund (20228B) to post direct expenses. Expenses unrelated to the Flex MBA program will not be posted to this fund.
2. Account for all indirect expenses in IFIS funds other than 20228B. On a regular basis (monthly, quarterly or annually), RSM will transfer indirect expenses to fund 20228C using a reasonable and supportable cost allocation methodology.
3. Allocate a portion of 19900A Flex MBA program faculty salaries to fund 20228B on at least an annual basis.
4. Utilize fund 20228A or create another Flex MBA sub fund to account for the use of surplus balances in funding non-program related costs.
5. Continue to expand the use of IFIS funds, as described in this review and consistent with current practices, to existing and new RSM programs.

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AMAS Reconciliation of the 2012-13 Flex MBA Direct Expenses

| | Per IFIS (Fund 20228A) | Cost Analysis Report | Difference |
|-----------------------------------|---------------------------|--------------------------|------------------------|
| Total Faculty Salaries | \$ 2,069,252 ¹ | \$1,718,351 ² | \$(350,901) |
| Total Staff Salaries | 2,509,701 | 402,012 ³ | (2,107,689) |
| Faculty and Staff Benefits | 1,571,358 | 490,851 ⁴ | (1,080,507) |
| General Assistance | 155,255 | - | (155,255) ⁵ |
| Supplies and Expenses | 2,462,789 | 145,081 ⁶ | (2,317,708) |
| Equipment | 32,732 | - | (32,732) ⁷ |
| Travel | 428,485 | 124,929 ⁸ | (303,556) |
| Financial Aid | - | 285,081 | 285,081 ⁹ |
| Other | - | 825,178 | 825,178 ¹⁰ |
| Total | \$9,229,572 | \$3,991,483 | \$(5,238,089) |

¹ Includes Flex MBA temporary faculty, teaching assistants, faculty startup, and PhD program operations salaries.

² Flex MBA ladder rank faculty (LRF) salaries are calculated at 20% of one FTE per course, plus any offload salaries. In general, these salaries are charged to general fund 19900A and are not allocated to fund 20228A. Offload salaries are charged to fund 20228A. The figure also includes temporary faculty salaries posted to fund 20228A.

³ Includes staff salaries for MBA programs, MBA career services, PhD program graduate student researchers (GSRs) and teaching assistants (TAs), and Flex MBA TAs charged to funds 19900A, 19942A, 20228A, and 20225A. Various percentage allocations are then applied to each index pool within these funds to determine the Cost Analysis figure.

⁴ Includes faculty and staff benefits charged to funds 20228A and 20225A, LRF benefits charged to general fund 19900A, and some PhD program GSR benefits charged to the general fund and non-resident tuition fund. Various percentage allocations are then applied to each index pool within these funds to determine the Cost Analysis figure.

⁵ General assistance expenses are for student workers. These costs are included in staff salaries on the Cost Analysis report.

⁶ Supplies and Expenses (S&E) are charged primarily to funds 20228A and 20225A. While a portion of LRF (NGN/GL) is charged to the general fund, the balance of LRF S&E are charged to fund 20228A. Various percentage allocations are then applied to each index pool within these funds to determine the Cost Analysis figure.

⁷ Equipment expenses are included in S&E on the Cost Analysis report.

⁸ Travel expenses are charged to funds 20228A and 20225A. Various percentage allocations are then applied to each index pool within these funds to determine the Cost Analysis figure.

⁹ Financial aid is charged to various fellowship IFIS funds. Private donor fellowships reported on the Cost Analysis report are not transferred into the Flex MBA IFIS fund.

¹⁰ Other expenses (student meals/lodging, parking, graduation events, etc.) are included in S&E in IFIS. Per the UCOP cost analysis reporting instructions, this cost is segregated to account for student related expenses (student meals/lodging, parking, graduation events, etc.) covered by the program.

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Program Costs: Historical Practice vs. Best Practice

| Program Costs | Historical Practice | Best Practice |
|--------------------------------------|---|--|
| Direct Non-Payroll Expenses | Expenses are charged primarily to the Flex MBA fund, the school's original fund source, and the full-time MBA fund, with additional funds charged in certain instances. Pre-determined percentages are applied to specific indexes to determine the Flex MBA's share of costs. Costs not associated with the Flex MBA program were not transferred out to the associated IFIS fund. | Expenses that directly benefit the program should be posted as a direct expense to the Flex MBA fund. All other costs should be posted to other RSM IFIS funds. |
| Indirect Non-Payroll Expenses | Expenses are charged primarily to the Flex MBA fund and the full-time MBA fund, with additional funds charged in certain instances. Pre-determined percentage allocations are applied to index pools in each fund to determine the Flex MBA's share of costs. These expenses are reported as direct expenses on the Cost Analysis report. | Indirect expenses should initially post to a non-Flex MBA IFIS fund or a Flex MBA sub fund. RSM should periodically transfer the Flex MBAs share of these costs to a Flex MBA IFIS indirect cost fund via an electronic journal entry. These expenses should be reported as indirect costs on the Cost Analysis report. |
| Faculty Salaries and Benefits | <p>Ladder rank faculty (LRF) salaries and benefits, excluding summer ninths and overload teaching, are charged to the general fund. The charges were never allocated to the Flex MBA fund. Temporary faculty salaries are charged to the Flex MBA fund.</p> <p>RSM is not allocated faculty lines in the same manner as other campus entities and earns core funds to support faculty salaries through matriculation into the full-time MBA and undergraduate minor programs.</p> <p>Benefits for teaching assistants and PhD program operations are charged primarily to the Flex MBA fund and the general fund. Pre-determined percentages are applied to specific indexes in each fund to determine the Flex MBA's share of costs.</p> | Faculty salaries and benefits posted to the general fund that benefit the Flex MBA program should be transferred to the Flex MBA fund on a periodic basis via an electronic journal entry. All other TAs and faculty salaries and benefits that directly benefit the Flex MBA fund (such as offload teaching payments) should continue to be posted directly to the Flex MBA fund. |
| Staff Salaries and Benefits | Staff salaries and benefits for MBA programs, MBA career services, the PhD program, and Flex MBA teaching assistants are primarily charged to the general fund, Flex MBA fund, or the full-time MBA fund. Pre-determined percentage allocations are applied to index pools in each fund to determine the Flex MBA's share of costs. | Only staff salaries and benefits that directly benefit the Flex MBA program should be posted to the Flex MBA fund via an electronic journal entry. If these are indirect costs, expenses should be periodically transferred to the Flex MBA indirect fund. |