

**UNIVERSITY OF CALIFORNIA, DAVIS
INTERNAL AUDIT SERVICES**

**University of California, Davis Health System
UC Davis Extension
Internal Audit Services Project #13-32**

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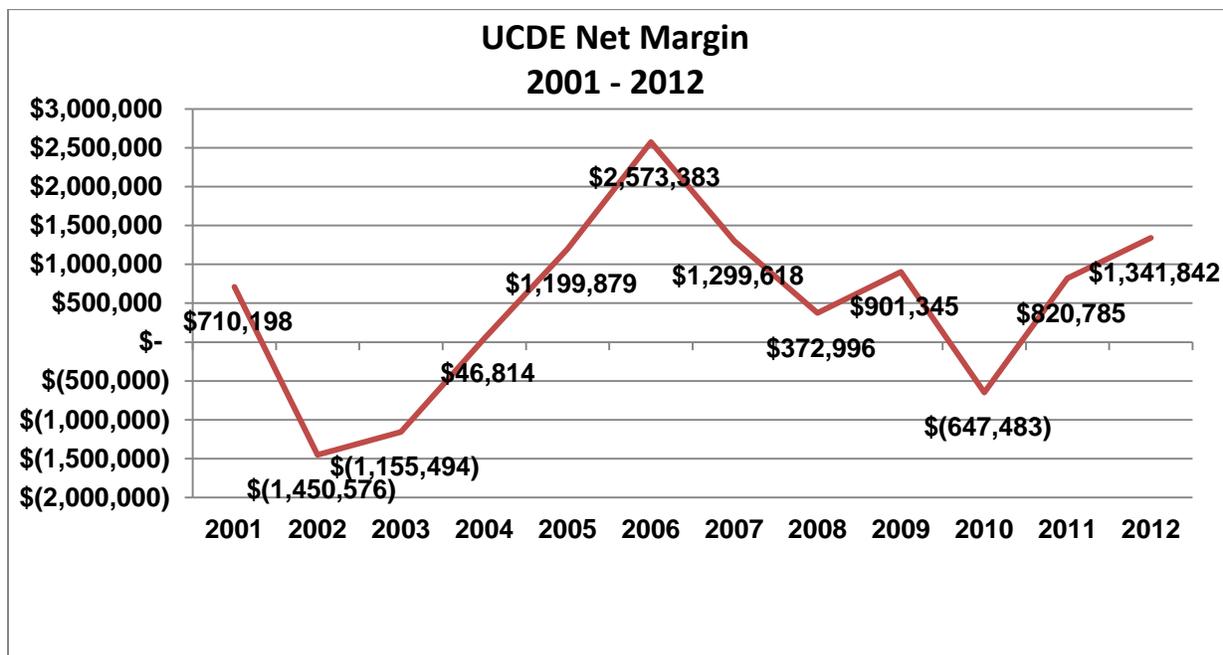
MANAGEMENT SUMMARY

BACKGROUND

UC Davis Extension (UCDE) is a large, diverse organization. In FY2012, UCDE offered 1,340 unique courses in subjects from Equine Event Management to International Commercial Law. UCDE has five academic departments, one administrative department, three independent special programs, 230 FTE staff and enrolled over 52,000 students in FY2012. The financial structure supporting UCDE is equally large, with 221 separate organizations, 394 OP funds and 803 accounts as of June 30, 2012.

There are three types of students enrolled at UCDE. Open enrollment students enroll in UCDE classes or training programs that are open to the public. Through UCDE's Open Campus Program, students take UC Davis classes on a space-available basis without formal admission to UC Davis. Open Campus students typically are completing academic preparation for graduate school, improving their G.P.A. for readmission to UC Davis, or exploring advanced classes beyond the high school curriculum. UCDE also serves students through programs supported by contracts and grants with federal, state and other agencies, as well as corporations and non-profit organizations that provide specialized education and training, consultation, and program development. Any contract or grant project UCDE undertakes must align with its core mission of providing continuing and professional education.

UCDE is a totally self-supporting entity. It relies solely on enrollment fees, gifts, contracts and grants to cover all costs. The range of UCDE's business model has allowed it to rebound from a deficit in FY2010 and succeed in FY2011 and FY2012 despite a difficult financial environment. UCDE has had positive net results in nine of the last twelve years, and has built up a healthy reserve of over \$8 million.



In FY2012, 43% of UCDE revenue came from contracts and grants and 57% from open enrollment. During this period, UCDE reported \$34.5 million in total revenue, direct expenses of \$28.3 million, and a net increase to the reserve of \$1.4 million after deducting \$4.8 million in administrative expenses and campus overhead. However, two of its five academic departments, as well as two small independent programs, were in deficit at the end of the year. UCDE's positive net proceeds were primarily the result of an exceptional year for its International Programs Department, which netted \$1.9 million. The year-to-year performance by department varies, which underscores the value of UCDE's diverse portfolio. For example, International Programs experienced significant deficits during 2001-2003. However, the impact was mitigated by the strong financial performance of other programs.

There is a detailed system of operational control used at UCDE. Managers continually evaluate risks, formulate strategies and priorities and monitor program results. The UCDE Management Council (MC), composed of the Dean, the Assistant Dean/COO and the five academic department chairs, meets biweekly. The MC discusses the operations of each program as well as new campus initiatives and external events that will affect UCDE. The MC also has an annual retreat, during which the members consider strategy and mission for the organization as a whole, as well as its strengths, weaknesses, opportunities and threats.

UCDE uses its business information system, TUBS, for financial information such as enrollment fees and accounts payable and for operational information related to enrollments, course descriptions, and curriculum. UCDE Financial Services extracts financial data from DaFIS to TUBS nightly, and uses the data to prepare and distribute reports on the revenue and expenses of each program to the program managers periodically based on each manager's requirements. Most managers review this report at least quarterly. The program directors and chairs have developed their own reports to monitor their programs on a more frequent basis. These reports track expenses as well as class enrollments and/or expected contract revenue.

Management at UCDE uses both goal-setting and strategic planning processes to plan, direct organize and control operations. During their annual evaluations, department chairs prepare goals for each of their programs for the following year. Actual performance is then reviewed with the Dean at the end of the subsequent year. The goals are general, but include specific metrics to measure success. Additionally, department chairs prepare a formal Strategic Plan which covers the strengths, weaknesses, opportunities, and threats for each of the programs in their department. The plans are also reviewed with the Dean and updated annually.

PURPOSE AND SCOPE

We reviewed the financial and operational management processes of the UCDE as part of our FY2013 audit plan. The purpose of the audit was to identify significant strengths, weaknesses and risks related to the fiscal and operational management processes within UCDE and to look for opportunities to improve its economy and efficiency.

We reviewed financial reports and results for all UCDE departments for FY2008-FY2012 and reconciled the FY2012 financial results to the results in DaFIS. We examined the financial and operational reports and metrics UCDE managers use to plan and monitor programs. We interviewed staff members from various UCDE departments and units and reviewed relevant policies. We tested a sample of accounts payable transactions from FY2012 for compliance with University policies and procedures. We also tested a sample of FY2012 grant transactions for compliance with the grant purpose. Finally, we examined departmental business plans, and the goals and objectives of a selection of UCDE staff members.

CONCLUSION

We concluded that the UCDE has suitable processes in place to manage its diverse operations and move the organization toward success through an ongoing assessment and response to risks, threats and opportunities. We also concluded that opportunities exist for improvement in budgeting and monitoring fiscal results, reconciliation of financial transactions, General Ledger review, and separation of purchasing duties.

Our observations and recommendations are presented in the body of this report along with corresponding management corrective actions.

OBSERVATIONS, RECOMMENDATIONS, AND MANAGEMENT CORRECTIVE ACTIONS

1. FINANCIAL MONITORING

The process for establishing and monitoring budgets and financial targets should be strengthened.

UCDE program managers and department chairs use the results of the previous year and their own calculations and experience to informally monitor the financial performance of their areas of responsibility. However, UCDE has not prepared a formal budget for all programs and departments since 2010. Rather than formulating budgets to facilitate monitoring and promote accountability, UCDE prepares projections of year-end results in the middle of the fiscal year using data queried from the DaFIS data warehouse. However, there is no documentation of how the projections are calculated and the projections are not saved for comparative purposes.

The UCD *Administrative Responsibility Handbook* requires the use of sound financial management principles, including the establishment of a budget, which allows management to prioritize its goals and the use of its resources, measure current financial performance, compare actual to expected results and review variances to detect errors or changes in business conditions. Furthermore, the UCDE document, *Organizational Values for Financial Management*, requires frequent financial updates and transparent planning. Failure to employ these financial management principals increases the risk of program deficits by impeding management's ability to monitor program performance in an efficient and effective manner. That said, the overall financial performance of UCDE should be considered commendable over the last 12 years.

Recommendations

UCDE should prepare an annual financial budget for each program and department, and monitor the actual financial results against expectations on a regular basis.

Management Corrective Actions

UCDE will resume formal program and departmental budgets and monitor the actual financial activity to predict financial results and detect variances and trends potentially requiring remedial action by June 15, 2013 for FY2014.

2. FINANCIAL STRUCTURE

UCDE Chart of Accounts contains unused accounts and organizations

There were 304 (30%) active accounts in UCDE's financial structure reflecting no transactions during FY2011 or FY2012. In 2009, UCDE requested the assistance of KPMG to restructure the UCDE Chart of Accounts. KPMG recommended and helped

implement a chart of accounts structure that has 11 different types of accounts. Each UCDE grant or contract now has its own fund and two to four types of accounts associated with it. However, UCDE did not establish a systematic method for closing accounts as activities or agreements end.

As the UCD *Administrative Responsibilities Handbook* states, University policy requires administrators to manage resources in an efficient and cost-effective way. All financial systems must be reliable, responsive, and accessible and meet the user's needs, including sufficient and useful financial reporting.

The detail in UCDE's chart of accounts allows the division to determine precisely the income and expenses associated with each of its contract and grant agreements and open enrollment courses. However, failure to close out accounts on a timely basis increases the risk of errors and/or inappropriate transactions.

Recommendations

UCDE should close all unnecessary accounts in its chart of accounts and establish a process for doing so on a timely basis.

Management Corrective Actions

UCDE will close all unused organizations, funds and accounts in its chart of accounts by June 15, 2013.

3. RECONCILIATION OF FINANCIAL DATA

Procedures to reconcile TUBS data to DaFIS should be strengthened

As with other campus units, DaFIS is UCDE's financial system. UCDE uses its own business system (TUBS) to break down financial information for internal allocations, reporting and decision-making. The UCDE Chief Financial Officer indicated that he reconciles TUBS to DaFIS on a monthly basis by comparing a download from TUBS to the DaFIS 193 report. However, UCDE does not maintain documentation demonstrating completion of the reconciliations, and the reconciliations are not independently reviewed and approved by management.

University policy, as summarized in the UCD *Administrative Responsibilities Handbook*, requires any department using a financial system outside of DaFIS to reconcile that data to DaFIS on a monthly basis to ensure accuracy and validity of all data. The reconciliation should determine and document the cause of significant deviations.

UCDE managers rely on TUBS data provided by Financial Services to monitor program activities and make programmatic decisions. Regular reconciliations between TUBS and DaFIS are essential to ensure that undetected discrepancies between the actual and reported income and expenses are identified. Review and approval of the reconciliation by management ensure that the reconciliation is completed as scheduled and that any discrepancies are properly resolved in a timely manner.

Recommendations

UCDE Financial Services should document the monthly reconciliation process between TUBS and DaFIS and submit the reconciliation to management for review and approval.

Management Corrective Actions

UCDE Financial Services will prepare instructions and a schedule for performing the monthly reconciliation between TUBS and DaFIS. The reconciliation, including any variances and their resolutions, will be forwarded to the Assistant Dean/COO or their designee for review and approval by January 31, 2013.

4. SEPARATION OF DUTIES

Internal purchasing controls should be strengthened.

UCDE Facilities has not maintained a proper separation of duties between ordering and receiving functions. Facilities made purchases exceeding \$1.7 million during FY2012. Facilities is responsible for ordering and receiving, including purchasing using University purchase cards. However, Facilities staff were not requiring that someone other than the person placing the order receive the items purchased. In addition, UCDE procedures for payment approval did not include ensuring that ordering and receiving was performed by different staff. UCDE advised that the person placing the order sometimes received the delivery to expedite distribution when no one else was available.

UCD PPM 330-11, *Departmental Financial Administrative Controls and Separation of Duties*, requires departmental financial administrative duties to be separated so that one person's work routinely serves as a complementary check on another's work, and no one person has complete control of a financial transaction. It specifies that the person receiving and verifying purchased items should not be the person who placed the order.

Failure to properly separate duties in a purchasing function increases the risk of waste, fraud and abuse. This risk increases with the use of purchasing cards because pre-approval for the purchase is not required.

Recommendations

UCDE should assure that separation of duties is maintained for all ordering and receiving activities.

Management Corrective Actions

UCDE will inform the staff members in the Facilities unit of the necessity to maintain separation between the person placing the order and the person receiving and verifying the goods. Additionally, the approval process for invoice payment will include a determination that the order was placed and received by different staff members by December 31, 2012.

5. GENERAL LEDGER REVIEWS

Ledger reviews should be performed more consistently.

UCDE is not reviewing general ledger accounts on a timely basis and some UCDE Principal Investigators (PIs) are not reviewing the transactions posted to their contract and grant accounts in accordance with University policy. The delay in the General Ledger reviews was reportedly caused by turnover in Financial Services, and the UCDE PIs were reportedly not aware of the requirement for performing monthly ledger reviews on their grants.

PPM 330-11 requires all departments to review their general ledgers monthly using the General Ledger Review function online in Decision Support. PPM 330-31, *Administration of Contracts and Grant Projects*, also requires that PIs review the transaction listing monthly and make adjustments as necessary.

Failure to perform monthly general ledger reviews increases the risk that charges and credits are invalid. Failure to confirm that the expenses meet grant restrictions and regulations, and are allowable, allocable, reasonable, and specifically benefitting the contract or grant, increases the risk of misused funds and could jeopardize further funding.

Recommendations

UCDE should ensure that all General Ledger reviews are certified monthly and work with PIs to review the transactions posted to their grants and contracts on a monthly basis.

Management Corrective Actions

By January 15, 2013, UCDE will implement procedures to ensure that all General Ledger reviews are performed within 15 days of the previous month fiscal close.

By June 15, 2013, UCDE will educate PIs about the importance of reviewing transactions posted to contract and grant accounts within 15 business days of the monthly close and provide support and data to significantly increase their compliance.
