UNIVERSITY OF CALIFORNIA, DAVIS
INTERNAL AUDIT SERVICES

Graduate School of Management
Dean's Office Administrative Review

Project #14-14

April 2014

Fieldwork Performed by:

Tony Firpo, Principal Auditor
Victoria Owens, Principal Auditor
Man Tsui, Senior Auditor

Reviewed and Approved by:

Jeremiah J. Maher, Director

MANAGEMENT SUMMARY

BACKGROUND

As part of the Internal Audit Services (IAS) audit plan for fiscal year (FY) 2013-14, IAS conducted an administrative review of the Graduate School of Management (School) Dean's Office. The mission of the School is to be a global leader in business and management research and education, and to prepare innovative leaders for global impact. The vision for the School is to serve as an engine of economic prosperity in the region and globally.

The School has three Master of Business Administration (MBA) programs: a twenty-one month full-time program in Davis and two part-time programs, a Sacramento program that holds classes on weeknights and a Bay Area program in San Ramon with classes on weekends. In 2012, the School launched a Master of Professional Accountancy (MPAc) program, a full-time, nine-month program. The School also has an Executive Education program, which provides tailored, non-degree education for people in executive careers. The School currently has 97 students enrolled in its full-time MBA program, 218 in the part-time program in the Bay Area and 166 in the Sacramento program. The School's charter MPAc class had 29 students. The School has 29 tenure and tenure-track faculty, with an additional 35 lecturers and visiting professors.

The School and its faculty are highly regarded and ranked nationally. The 2015 Best Business Schools standings in *US News and World Report (U.S. News)* ranks the full-time program #41 nationally and the part-time programs together as #25 nationally. *U.S. News* also ranked the School #9 for MBA programs that lead to jobs. The *Financial Times* ranked the School #13 globally in faculty research productivity and *The Princeton Review* ranks the School #6 nationally in opportunities for women.

PURPOSE AND SCOPE

The objectives of our review were to assess:

- Key operational and administrative controls;
- Financial management;
- Key operating statistics; and
- The current state of operations through interviews with key administrative personnel.

To perform our review, we interviewed the Dean and administrative personnel from the School's Dean's Office, School unit managers, and personnel from other campus offices. We reviewed the School's national and faculty rankings, admissions data, and employment statistics. We also reviewed statistics and data about the School's expenditures, faculty, staff, and students, much of which is available through the Provost's Dashboard. Additionally, we obtained and analyzed reports from Davis Financial Information System (DaFIS) and other financial reports prepared by the Dean's Office and Budget & Institutional Analysis (BIA). Our review incorporated financial information for the five fiscal years, ending in FY13.

CONCLUSIONS

Financial Results:

At June 30, 2013, the School had total funds available of approximately $2.9 million. In addition to these funds, the School has $2.2 million set aside in a Fund Functioning as an Endowment (FFE).

Total fund sources increased $6.9 million (35%) from $19.7 million in FY09 to $26.7 million in FY13.[1] Degree program fee revenues represent approximately 50% of the School's annual sources, and over this five-year period, these revenues increased $4.6 million (51%) from $9 million to $13.6 million. General funds provided to the School, which represented approximately 27% of the School's current year sources in FY13, increased slightly from $6 million in FY09 to $6.2 million in FY13. For more information on fund sources, see Appendix A.

Expenditures increased $6.7 million (41%) over the five-year period. The most significant expense category is salaries and benefits, which increased approximately 50% over the five-year period and represented approximately 75% of total expenditures in FY13. For more information about expenditures, see Appendix B.

Operating Trends:

The degree program revenue increase of 51% over the five-year period resulted primarily from fee increases rather than enrollment increases, as enrollments dropped 14% for the full-time MBA program and 19% for the Sacramento MBA program, and increased 2% for the Bay Area MBA program over this five-year period. The MPAc program, which increased its enrollment 34% in its second year (FY14), also contributed to increased degree program revenues. For more information about operating trends, see Appendix C. The School faces many of the same risks as other business schools across the country, as enrollments in MBA programs have declined nationally in recent years. At the same time, the number of schools offering MBA programs has increased (especially part-time programs for working professionals).

Opportunities for Improvement:

The School's accounting procedures, chart of accounts and DaFIS organizational hierarchy do not align optimally to its programs, which impedes financial reporting, monitoring and evaluation of individual programs. The School is working with BIA to create a new chart of accounts structure that better supports financial accounting and reporting by program.

In 2011, the School developed both a long-range financial plan and a strategic plan that outlined its plans and initiatives. Since that time, the School has changed, including the launch of the MPAc program. In light of these changes, there is a need for the School to develop a long-term financial and strategic plan for financial stability. Due to planned changes in leadership, we believe this need should be communicated to leadership as deemed appropriate.

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

---

[1] The 35% increase excludes the $2 million FFE, i.e., if the School had retained the $2 million in its carryforward funds rather than establish the FFE, the increase in total sources over the five-year period would have been 45%.

I. OBSERVATIONS, RECOMMENDATIONS, AND MANAGEMENT CORRECTIVE ACTIONS

A. FINANCIAL OVERVIEW

Funds available: At June 30, 2013, the School had total funds available of approximately $2.9 million. The School also has $2.2 million set aside in a Fund Functioning as an Endowment (FFE).[2]

Sources: Between FY09-FY13, total sources increased $6.9 million (35%) from $19.7 million to $26.7 million. Degree program fee revenues represented approximately 50% of total fund sources in FY13. Over the five-year period, degree program fee revenues increased $4.6 million (51%) from $9 million to $13.6 million. Noteworthy is that much of this revenue increase resulted from fee increases rather than enrollment increases, as enrollments dropped 14% for the full-time MBA program and 19% for the Sacramento MBA program, and increased 2% for the Bay Area MBA program over this five-year period. These enrollment trends reflect national declines in MBA program enrollments. To diversify its revenue base, the School established the MPAc program which contributed $1.1 million to the overall $4.6 million increase in revenues.

General funds provided to the School, which represented approximately 27% of the School's current year sources in FY13, increased slightly from $6 million in FY09 to $6.2 million in FY13. For more information on fund sources, see Appendix A.

Uses: Expenditures increased $6.7 million (41%) over the five-year period. The most significant expense category is salaries and benefits, which increased approximately 50% over the five-year period and in FY13, represented approximately 75% of total expenditures. Academic salaries, which were approximately $8.7 million in FY13, increased 32%, reflecting primarily a new salary structure that was established to keep salaries competitive, while staff salaries, which were approximately $4.8 million in FY13, increased approximately 64%, reflecting salary increases as well as 20 new hires associated with investments in programs such as the MPAc program, the Executive Education program, and the Institute.

Facing enrollment challenges, the School recognizes that it must adjust its budget to align with its projected funding, and has reduced fixed costs, primarily through staffing reductions approximating $878,000 for FY15 on an annualized basis. The changes have led to a projected $184,000 in budget surplus for FY15. In the future, controlling costs will be important for the School's financial stability and viability, which the School recognizes. For more information about expenditures over the five-year period reviewed, see Appendix B.

Recommendation

1. The School should finalize the FY15 budget.

Management Corrective Action

1. By October 15, 2014, the School will finalize the FY15 budget.

B. CHART OF ACCOUNTS AND ORGANIZATIONAL HIERARCHY

[2] The School established this FFE in 2011 by transferring operating reserves to the FFE. As of 6/30/13, $2 million of operating reserves had been transferred into the FFE. The funds are invested like a true endowment; however, unlike a true endowment, the institution may authorize the expenditure of principal for any intended use.

The School's accounting procedures, chart of accounts and DaFIS organizational hierarchy do not align optimally to its programs, which impedes financial reporting, monitoring and evaluation of individual programs.

The School's account structure and accounting procedures do not readily foster comprehensive accounting of expenditures by program. Rather than clustering all accounts for a single program within a unique DaFIS organization, the School's accounts have subaccounts that tie a particular transaction to a specific program; thus, the expenses for an individual program are often distributed across several general ledger organizations. Also, if an expense transaction is not coded to the correct subaccount, it will not be included in the financial reports for that program. Furthermore, certain expenses that benefit multiple programs are not allocated across those programs.

Because of this accounting structure/process, creating monthly financial reports from the Kuali data requires manually moving expenses from one organization to another for reporting purposes. Also, GSM internal financial reports exclude certain accounts, such as those of the Institute, so that reports provided to the Dean are not inclusive of the entire School. A chart of accounts more directly matched to the School's programs would improve internal reporting, and enable School leaders to see the financial position of their programs and assist with making decisions. In addition, it would reduce the effort required to produce financial reports, allowing staff to spend more time on activities related to the school's goals.

Prior to the commencement of our review, the School had been aware of the need to restructure its chart of account and had been teaming with personnel from BIA on this project.

Recommendation

1. Restructure the chart of accounts and organizational hierarchy to improve financial information by program.
2. Establish procedures for allocating expenses that benefit multiple programs.
3. Provide periodic reports to the Dean and other School leaders through DaFIS Decision Support.

Management Corrective Action

1. By April 15, 2015, management will restructure the School's chart of accounts and organizational hierarchy to improve comprehensive accounting by program.
2. By April 15, 2015, management will establish procedures for allocating expenses that benefit more than one program.
3. By April 15, 2015, management will establish procedures to provide periodic reports to the Dean and other School leaders through reports available within DaFIS Decision Support.

C. FINANCIAL PLAN AND STRATEGIC PLAN UPDATES

Changes in the School's operations and management suggest the need to update the School's financial and strategic plans.

The School produced a ten-year financial plan in March 2011 and a strategic plan later in 2011. The plans were intended to guide the School in its future operations, and serve as a framework to take advantage of its strengths and align budgets with strategic priorities. Since 2011, the School has started a new program, the Masters in Professional Accountancy, and expanded the breadth of the Executive Education program. These programs, as well as increased endowment and extramural funding, create a much different situation than existed in 2011.

Updating both the financial plan and the strategic plan would help the School incorporate recent changes in its operations into its strategy for financial stability, and offer additional guidance on allocating resources. An updated and complete strategic plan can also be used as an effective marketing tool for prospective students and donors. Based on planned changes in leadership over the next few years, such updated plans may best be delayed until a permanent replacement dean is appointed, although the current and interim deans will likely have useful input with respect to these plans.

Recommendations

The current dean should memorialize input regarding key considerations for updating the School's financial and strategic plans and pass that on to the interim dean. We encourage the interim dean at the end of his or her interim appointment to do the same for the permanent replacement dean.

Management Corrective Action

1. By October 15, 2014, the current dean will memorialize input regarding key considerations for updating the School's financial and strategic plans and pass that on the interim dean and ask the interim dean at the end of his or her interim appointment to do the same for the permanent replacement dean.

D. ALLOCATION OF PURCHASING CARD TRANSACTIONS

Purchasing card expenses for FY14 have not been transferred to the proper object codes, and in certain cases, accounts.

Purchases made with purchasing cards are initially recorded to a departmental default account associated with each card and a university-established default object code (7203 – credit card expense). Departments must then distribute the expenses to the appropriate object code (and also the appropriate account, if the default account is not appropriate for a particular purchase). UCD Policy and Procedure Manual section 350-22, *Purchasing Cards*, establishes in section V.B.2 that the transfer must be made within 30 days of receipt of goods or date of the default transaction, whichever is later.

As of January 2014, GSM had not distributed approximately $190,000 of FY14 purchasing card expenses. If expenses are not distributed timely, the School cannot readily identify and analyze the nature of the purchases being made, which impedes financial analysis and reporting.

Recommendations

1. For FY14, distribute all purchasing card transactions prior to 2014 fiscal close.
2. For FY15, establish a process to transfer purchasing card expenses within 30 days as required by policy.

Management Corrective Actions

1. The School has distributed its FY14 purchasing card transactions to the proper accounts. No further actions are necessary.

2. By December 15, 2014, procedures will be developed for transferring purchasing card expenses within 30 days as required by policy.

E. TRACKING COMMITMENTS IN KUALI

The School did not record in Kuali the financial obligation for guaranteed summer support for a new faculty member.

Budget and Institutional Analysis, in an effort to better manage carryforward and reserve funds, has issued guidance concerning the use of new objects COBL and KOBL to record commitments. The School has made a commitment to a new faculty member for summer salary support totaling approximately $172,600 from FY14-16, but had not recorded this commitment in Kuali as of the date of our review.

Historically, the School did not separately track its commitments for future spending. The School compiled a list of future financial commitments as part of their effort to more closely monitor the School's budget and spending. The School does not have many commitments, and while the School does track and monitor them, the School had not recorded the commitments in Kuali as there were so few.

Recording commitments will enable both the School and BIA to better monitor and project the School's financial situation. While the School is now monitoring its commitments, previous experience demonstrates how staff turnover could cause a school to unknowingly omit these obligations in its budgeting, causing unexpected overdrafts.

Recommendation

1. The School should record its obligation for summer salary to its new faculty member in the amount of $172,600 using object code COBL.

Management Corrective Action

1. The School has recorded its obligation for summer salary to its new faculty member in the amount of $172,600 using object code COBL. No further actions are necessary.

*****

APPENDIX A

Sources of Funds, Uses, and Funds Available: FY 2009 - FY 2013

	FY 2009	FY 2013	$ Change since 2009	% Change since 2009	Enrollment % Change since 2009
SOURCES					
Carryforward funds	$ 3,652,000	$ 4,109,000	$ 457,000	13%	N/A
Degree program fee revenues					
Full-time MBA program	1,931,000	2,278,000	347,000	18%	-14%
Sacramento MBA program	3,008,000	3,916,000	908,000	30%	-19%
Bay Area MBA program	4,072,000	6,289,000	2,217,000	54%	2%
Master of Professional Accountancy	-	1,128,000	1,128,000	-	(1)
Total fee revenue	9,011,000	13,611,000	4,600,000	51%	
Non-degree program income					
(2) Executive Education program	121,000	462,000	341,000	282%	N/A
General funds					
(3) Base and current year adjustments	6,028,000	6,186,000	158,000	3%	
Other sources					
Gifts and endowment income	634,000	974,000	340,000	54%	
New contracts and grants	69,000	1,135,000	1,066,000	1545%	
Other	215,000	174,000	(41,000)	-19%	
Total other sources	918,000	2,283,000	1,365,000	149%	
Total sources	$ 19,730,000	$ 26,651,000	$ 6,921,000	35%	
USES					
Total expenditures (4)	16,409,000	23,131,000	6,722,000	41%	
Encumbered for external obligations	757,000	542,000	(215,000)	-28%	
Designated for financial end	21,000	35,000	14,000	67%	
FUNDS AVAILABLE	$ 2,543,000	$ 2,943,000	$ 400,000	16%	
COMPOSITION OF FUNDS AVAILABLE (5)	FY 2009	FY 2013			
Total available funds	$ 2,543,000	$ 2,943,000			
Less: Restricted fund sources	(991,000)	(2,484,000)			
UNRESTRICTED FUNDS AVAILABLE	$ 1,552,000	$ 459,000			

(1) Master of Professional Accountancy program began in FY 2013 with an initial class of 29 students.
(2) Executive Education program is a non-degree program; therefore enrollment figures are not applicable.
(3) General funds includes both State support for the School and a portion of student tuition.
(4) Expenditures are not comprehensively accounted for by program, and are therefore presented as a single line item.
(5) The School also has a Fund Functioning as an Endowment (FFE), which was established in 2011. As of 6/30/13, the book value of this FFE was $2 million and the market value was $2.2. million. The funds are invested like a true endowment, however, unlike a true endowment, the institution may authorize the expenditure of principal.

APPENDIX B

Summary Schedule of Expenditures (in Thousands)

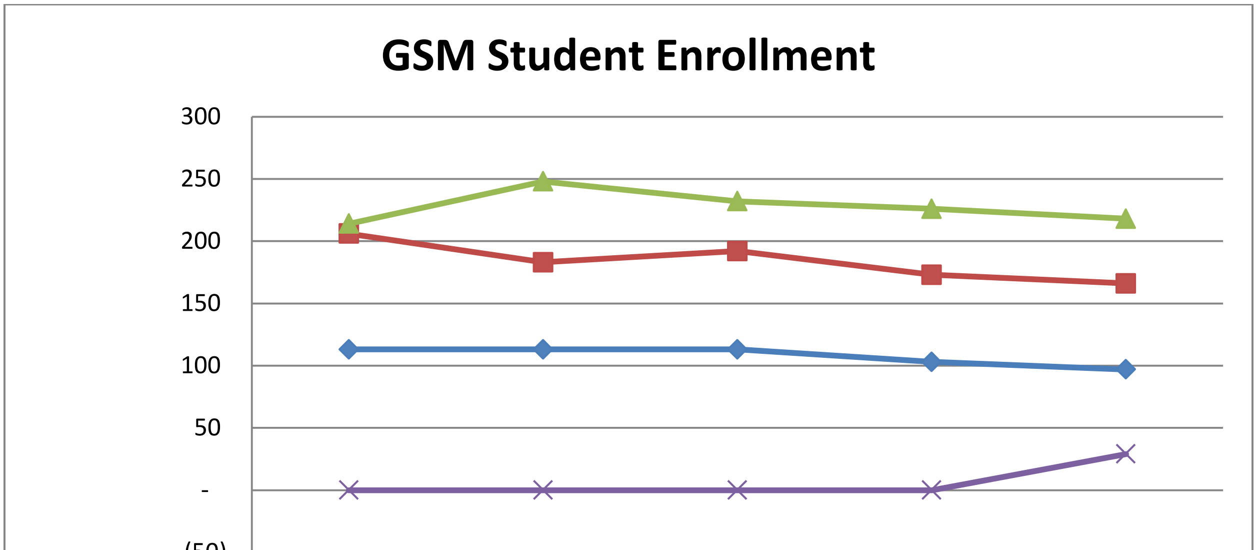
		FY 2009	FY 2010	FY 2011	FY 2012	FY 2013	Variance FY09 - FY13	Variance Explanation
EXPENDITURES								
Salaries and Benefits:								
	Academic salaries	$ 6,613	$ 6,833	$ 7,735	$ 8,148	$ 8,748	$ 2,135	See note (1)
	Staff salaries	2,959	2,984	3,365	4,173	4,844	1,885	See note (1)
	Benefits	1,832	2,067	2,535	3,038	3,614	1,782	Higher pension and healthcare costs
	Subtotal: Salaries and Benefits	11,404	11,884	13,635	15,359	17,206	5,802	
Scholarships & Fellowships		813	857	834	1,011	686	(127)	
Other Expenditures:								
(3)	Other expenditures	437	512	692	546	594	157	Growth in staffing and program expansion
(2)	Services	582	567	571	619	568	(14)	Variance immaterial for analysis
	Entertainment	526	509	574	544	563	37	Variance immaterial for analysis
	Rent	383	571	515	578	549	166	Expansion at San Ramon facility
	Advertising	259	261	410	452	508	249	Program expansion and raise enrollment
	Computer software and supplies	269	350	334	468	463	194	Growth in staffing and program expansion
	UCOP assessment	-	-	-	-	277	277	Assessment of all schools/colleges based on expenses
	Bookstore supplies	258	245	184	217	246	(12)	Variance immaterial for analysis
	Communication resources	153	226	201	214	234	81	Growth in staffing and program expansion
	Supplies	458	400	281	215	188	(270)	School-wide efforts made to reduce operational spending
	Classroom technology services	4	1	2	78	177	173	New video technology and telepresence capabilities
	Student credit card processing	145	165	145	140	144	(1)	Efforts in progress to reduce tuition from credit cards
	Equipment	290	930	156	100	128	(162)	2010 moving expenses to Gallagher Hall
	Travel	428	434	534	684	600	172	Growth in staffing and program expansion
	Subtotal: Other Expenditures	4,192	5,171	4,599	4,855	5,239	1,047	
	Total Expenditures	$ 16,409	$ 17,912	$ 19,068	$ 21,225	$ 23,131	$ 6,722	41 % increase

(1) Faculty increased by one FTE and staff increased by 20.71 FTE due to investment in program expansions such as Master of Professional Accountancy, Executive Education non-degree programs, and other mission related initiatives. New salary scale was established which increased faculty salaries to remain competitive in marketplance and improve faculty retention.

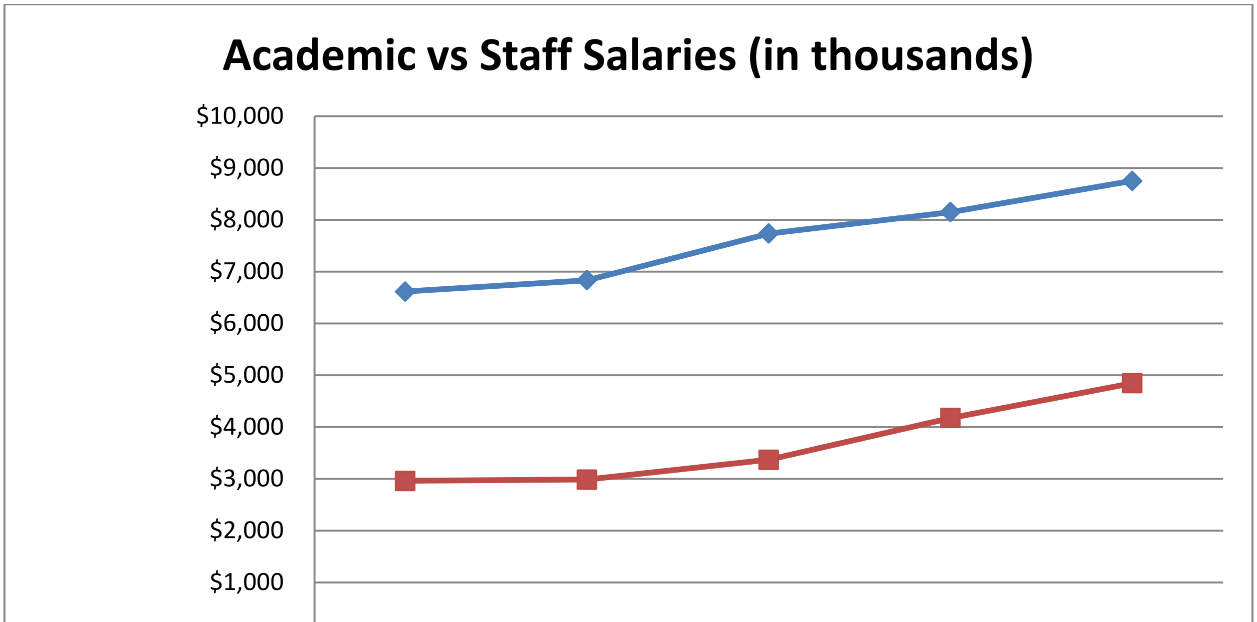
(2) Expenditures covered graphic design services, janitorial and miscellaneous services for San Ramon facility, faculty research supporting services.

(3) Includes expenditures in categories such as the following: library books, reprographic services, honoraria, equipment maintenance, liability, and membership & subscription charges, none of which individually total as much as the categories presented in the table above.

APPENDIX C
Operating Trends



	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Full time	113	113	113	103	97
Sacramento	206	183	192	173	166
Bay Area	214	248	232	226	218
MPAc	-	-	-	-	29



	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Academic salaries	$6,613	$6,833	$7,735	$8,148	$8,748
Staff salaries	$2,959	$2,984	$3,365	$4,173	$4,844