UCLA AUDIT & ADVISORY SERVICES

Edwin D. Pierce, CPA, CFE
Director

10920 Wilshire Boulevard, Suite 700
Los Angeles, California 90024-1366
310 • 794-6110
Fax: 310 • 794-8536

June 13, 2016

SENIOR VICE PRESIDENT/CHIEF COMPLIANCE AND AUDIT OFFICER SHERYL VACCA
EXECUTIVE VICE CHANCELLOR & PROVOST SCOTT WAUGH:

Re: Campus Service Enterprises – Mail, Document, and Distribution Services
     Audit Report #16-2227

Enclosed is the audit report covering our review of Mail, Document, and Distribution Services (MDDS).

The primary purpose of the review was to determine the adequacy and effectiveness of MDDS internal controls. Where applicable, compliance with University policies and procedures was also be evaluated.

The scope of the audit focused on the following areas:

- Budgeting and Monitoring
- Purchasing and Accounts Payable
- Recharge Revenue
- Mail Services
- Equipment Inventory
- Information Systems

Based on the results of the work performed within the scope of the audit, internal controls over the key areas examined were generally conducive to accomplishing the department's business objectives. However, controls and business practices could be further strengthened by implementing the following:

- Work with Campus Purchasing to establish blanket agreements with MDDS repair service providers. In doing so, MDDS will help ensure compliance with policies and procedures. Similarly, MDDS should work with Campus Purchasing when procuring alcohol.

- Develop stronger controls over postage meters, postal materials, and postal permits for campus departments with exceptions to UCLA Policy 310, or consider revising the policy to better reflect the current decentralized control environment.

- Ensure that there is a backup system administrator. Also, minimum password requirements should be implemented in compliance with UCLA Policy 401, and user access should be reset after a certain number of invalid sign-on attempts to ensure that only authorized users are accessing the system.

The corrective actions implemented by management satisfactorily address the audit concerns and recommendations contained in the report. In accordance with our follow-up policy, a review to assess the implementation of our recommendations will be conducted approximately four months from the date of this letter.

Please feel free to contact us if we can be of further assistance.

Edwin D. Pierce, CPA, CFE
Director

Enclosure

cc: S. Olsen

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CAMPUS SERVICE ENTERPRISES

MAIL, DOCUMENT, AND DISTRIBUTION SERVICES

AUDIT REPORT #16-2227

CAMPUS SERVICE ENTERPRISES
MAIL, DOCUMENT, AND DISTRIBUTION SERVICES
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Background

In accordance with the UCLA Administration fiscal year 2015-16 audit plan, Audit & Advisory Services (A&AS) conducted an audit of Mail, Document & Distribution Services (MDDS). MDDS is a department within Campus Service Enterprises, which reports to the Vice Chancellor of Finance & Budget/Chief Financial Officer. MDDS provides delivery, collection, and processing of all University mail, and manages UCLA's design, print, and distribution needs. The department strives for timely, precise, and unobtrusive service to all campus and healthcare locations, as well as many other UCLA-affiliated sites throughout West Los Angeles and Santa Monica.

The MDDS department consists of the following three units:

Mail Services

Mail Services operates five cost centers: Bulk Mail, Incoming Mail, Messenger Services, Outgoing Mail, and the Wilshire Center Contract Post Office. Mail is sorted and delivered to over 900 mail stops each business day. MDDS offers a broad range of postal services that conform to U.S. Postal Service (USPS) regulations. Standard USPS services include certified, registered, insured, priority and overnight express, as well as international services.
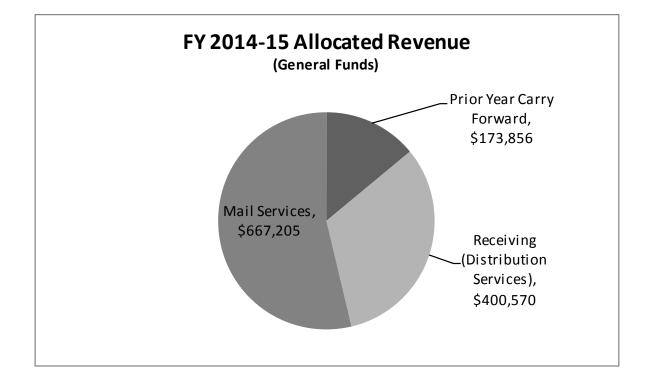
Document Services

Document Services provides a range of services to the UCLA campus, including printing, copying, document imaging/digitizing, graphic design, document planning/consultation, binding, finishing, mail merge/variable data printing, data center/system report printing, and check printing. MDDS staff are available to consult with campus customers throughout the process, from design to finalization.
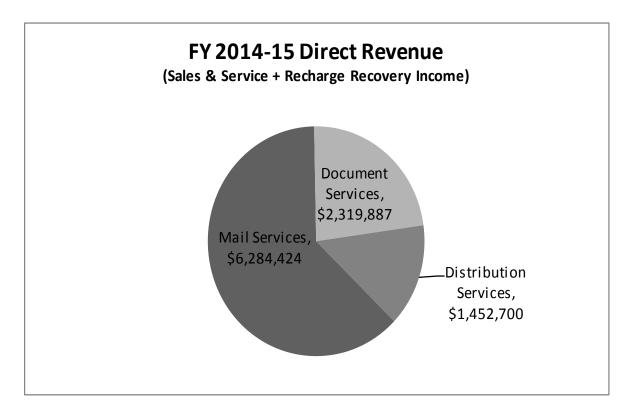
Distribution Services

Receiving, one branch of Distribution Services, provides receiving and re-delivery of inbound freight for the Center for the Health Sciences (CHS) and associated buildings. Located at CHS loading dock "A" at 650 Charles E. Young Drive South, the unit is funded through a combination of state appropriations and departmental recharges. Recharge revenue is for re-delivery services and for use of central UPS and FedEx outbound freight. According to the department, the CHS complex includes 26 miles of corridors within 13 buildings. The complex is the second-largest public building complex in the Unites States, after the Pentagon.

Cylinder Management, the other branch of Distribution Services, is a self-supporting unit that provides medical, specialty, and industrial compressed gases, as well as research alcohol, to the campus, CHS, and the Ronald Reagan UCLA Medical Center. The unit maintains an inventory of compressed gases and research alcohol in a central storage facility to provide next-day delivery to its clients. Customers can also make special orders from vendors through Cylinder Management and are recharged for products and services.

The following two charts summarize MDDS' total fiscal year 2014-15 revenue consisting of allocated funds (general funds) and direct (sales and service, recharges) income.

FY 2014-15 Allocated Revenue
(General Funds)

Prior Year Carry Forward, $173,856

Mail Services, $667,205

Receiving (Distribution Services), $400,570

FY 2014-15 Direct Revenue
(Sales & Service + Recharge Recovery Income)

Document Services, $2,319,887

Mail Services, $6,284,424

Distribution Services, $1,452,700

<u>Purpose and Scope</u>

The primary purpose of the audit was to determine the adequacy and effectiveness of MDDS internal controls. Where applicable, compliance with University policies and procedures was also evaluated. The scope of the audit included:

- Budgeting and Monitoring
- Purchasing and Accounts Payable
- Recharge Revenue
- Mail Services
- Equipment Inventory
- Information Systems

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

<u>Summary Opinion</u>

Based on the results of the work performed within the scope of the audit, internal controls over the key areas examined were generally conducive to accomplishing the department's business objectives. However, controls and business practices could be further strengthened by implementing the following:

- Management should work with Campus Purchasing to establish blanket agreements with MDDS repair service providers. In doing so, MDDS will help ensure compliance with policies and procedures. Similarly, MDDS should work with Campus Purchasing when procuring alcohol.

- Develop stronger controls over postage meters, postal materials, and postal permits for campus departments with exceptions to UCLA Policy 310, or consider revising the policy to better reflect the current decentralized control environment.
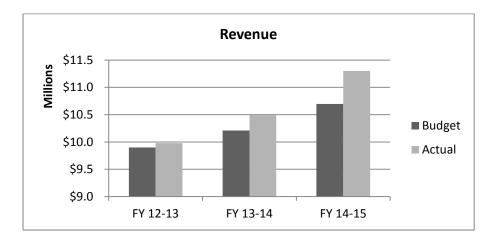
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▪ Ensure that there is a backup system administrator. Also, minimum password requirements should be implemented in compliance with UCLA Policy 401, and user access should be reset after a certain number of invalid sign-on attempts to ensure that only authorized users are accessing the system.
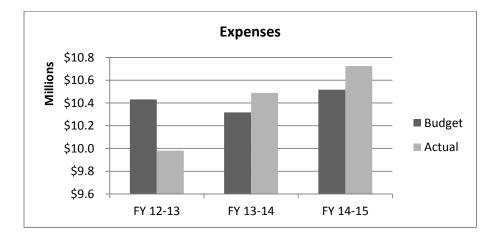
The audit results and corresponding recommendations are detailed in the following sections of the report.

<u>Audit Results and Recommendations</u>

<u>Budgeting and Monitoring</u>

<u>Budgeting</u>

A&AS compared the annual budget to actual revenue and expenses for fiscal years 2012-13, 2013-14, and 2014-15 to determine whether the department's budgeting techniques were adequate. The charts below summarize the comparisons. Year-to-year variances for revenue and expenses were no more than 10%, with most variances less than 5%. For the period reviewed, MDDS' budgeting methodology appeared to be adequate.

Revenue

(Bar chart, in Millions. Y-axis from $9.0 to $11.5. Categories: FY 12-13, FY 13-14, FY 14-15. Series: Budget, Actual)

- FY 12-13: Budget ≈ $9.9, Actual ≈ $9.98
- FY 13-14: Budget ≈ $10.2, Actual ≈ $10.5
- FY 14-15: Budget ≈ $10.7, Actual ≈ $11.3

Expenses

(Bar chart, in Millions. Y-axis from $9.6 to $10.8. Categories: FY 12-13, FY 13-14, FY 14-15. Series: Budget, Actual)

- FY 12-13: Budget ≈ $10.43, Actual ≈ $9.98
- FY 13-14: Budget ≈ $10.32, Actual ≈ $10.49
- FY 14-15: Budget ≈ $10.52, Actual ≈ $10.72

There were no significant control weaknesses noted in this area.

Monitoring

A&AS requested general ledger reconciliations, supporting documentation, and variance explanations for June and December 2015, and verified that reviews were documented and performed in a timely manner. All reconciliations were signed and dated by the preparer and reviewer. In addition, the reconciliations were all started within the month that the ledgers became available to the campus. Some reconciliations remained pending because of open purchase orders that were closed in subsequent accounting periods.

There were no significant control weaknesses noted in this area.

Purchasing and Accounts Payable

Purchasing and accounts payable policies and procedures are established at the systemwide level in UC Business & Finance Bulletin BUS-43, Materiel Management (BUS-43). Locally, UCLA Policy 740 (Purchasing Goods and Services) describes campus approval authorities, responsibilities, and restrictions for the purchase of goods and services. UCLA Policy 741 (Low-Value Purchases) provides requirements and guidelines specifically governing purchases made under low-value purchasing authority which has been delegated to employees outside of the Campus Purchasing department. UCLA departments are authorized to place low-value, N-class orders for up to $5,000 per vendor per account per day, excluding transportation costs and taxes, in BruinBuy, UCLA's web-based purchasing application.

A&AS obtained the July 1, 2014, to September 30, 2015, Detail General Ledgers for the following accounts (Table 1):

Table 1

Ledger Name	Account – Fund Number
Incoming Mail	721252 – 19900
Outgoing Mail	721254 – 66021
Bulk Mail	721253 – 66021
Messenger Services	721255 – 66021
Wilshire Center	721257 – 66021
Document Services	721211 – 66011
Receiving	721260 – 19900
Cylinder Management	721260 – 66500

Expenditures in each Detail General Ledger were analyzed and aggregated by sub code (Table 2). Based on the analysis, A&AS focused on transactions in sub codes 03 (Supplies & Expense) and 07 (Special Items). The remaining sub codes were either outside the scope of the audit, or had relatively low amounts of expenditures (or none) during the period of review.

Table 2

Sub Code	Description	Expenditures	% of Total
01	Salaries – Staff	$ 1,897,662	13.6
02	General Assistance	$ 1,809,081	12.9
03	Supplies & Expense	$ 1,699,025	12.1
04	Equipment & Facilities	$ 0	0.0
05	Special Items	$ 172,901	1.2
06	Employee Benefits	$ 2,039,175	14.6
07	Special Items	$ 6,374,606	45.6
08	Special Items	$ 0	0.0
	Total	**$13,992,450**	

A&AS selected 11 purchase orders from among the ledgers listed above in Table 1. The expenditures ranged from $9.18 to $170,000.00. The sample included the

following Order Class Codes: BruinBuy Catalog Contract Release (F), BruinBuy Low-Value Orders (N), Procurement Card purchases (Q), and Special Items (X). Because some purchase orders contained multiple invoices, the testing sample ultimately contained nine invoices.

Supporting documentation for each invoice was requested from MDDS and reviewed for appropriateness. A&AS determined that all purchases were properly authorized, invoices were approved by management, and PANs were read by all mandatory reviewers. However, the following issues were noted:

- Repair services totaling $250 for an envelope feeder were procured through a low-value order (LVO). Per Attachment A of UCLA Policies 740 and 741, a requisition is required for service, repairs or maintenance; these items may not be purchased using an LVO. In this particular situation, MDDS failed to comply with policy because of the need for timely action; departmental operations and service to campus customers might have been temporarily disrupted had a requisition, which takes at least four to five days for processing by Campus Purchasing, been properly processed. However, MDDS should strive to comply with all applicable policies to protect the University to the greatest extent possible.

- Ethanol, totaling $1,295, was purchased from Gold Shield Distributors through an LVO. Per Attachment A and B of UCLA Policies 740 and 741, ethyl alcohol (ethanol) requires a requisition and approval from the Campus Purchasing Director. MDDS, specifically the Cylinder Management unit, holds the only Industrial Alcohol User Permit from the Alcohol and Tobacco Tax and Trade Bureau for the campus. The permit allows Cylinder Management to withdraw and use alcohol free of tax. Normally, MDDS purchases research alcohols from Fisher Scientific, which has a strategic sourcing agreement with the University. However, campus customers sometimes request items that Fisher Scientific does not sell, so MDDS uses another vendor in these situations.

Recommendation: Management should work with Campus Purchasing to establish blanket agreements with MDDS repair service providers. In this way, MDDS can better ensure compliance with policies and that the University is adequately protected from liability, while still maintaining the flexibility to procure services quickly when an emergency repair is needed. Similarly, MDDS should work with Campus Purchasing to set up blanket agreements with any vendor from which alcohol is purchased.

Response: MDDS agrees that established blanket agreements, issued by UCLA Purchasing, should be in place for the following vendor types:
- Repair services that are performed onsite.
- Any purchase of Ethyl Alcohol.

MDDS will work to establish such agreements for all applicable vendors in the next 60 days. The expected completion date is August 1, 2016.

Recharge Revenue

The Policy Committee on Sales and Service Activities and Service Enterprises (POSSSE) has oversight responsibility for the campus' recharge rates and working capital issues, as well as other aspects of sales and service activities having a financial impact on the campus (e.g., submission of budgets, Short-Term Investment Pool implications, policies about who is charged and for what). POSSSE advises the Chancellor on policies pertinent to these issues and acts on his behalf by monitoring and assisting in policy implementation.

A&AS compared the department's current rates from its billing program to the POSSSE-approved rate sheets to verify that MDDS was charging customers the correct price for products and services. A total of 214 recharge rates were reviewed; all were consistent with POSSSE-approved rates for fiscal year 2015-16.

There were no significant control weaknesses noted in this area.

<u>Mail Services</u>

Postage meter machines allow MDDS to print postage indicia directly onto mail pieces. Postal materials are essentially stamps, which some departments prefer over postage printed onto the envelope. Postal permits are accounts that have been established with the USPS for a certain postage payment method for bulk and commercial mailings. A&AS interviewed the Director of MDDS to determine whether controls over postage meter machines, postal materials, and bulk mail postal permits were adequate and ensured compliance with UCLA Policy 310.

Controls over these aspects of Mail Services were adequate within MDDS. However, MDDS does not have the resources to exert effective controls over the 38 campus departments with exceptions to UCLA Policy 310, which establishes that mail services must be centralized (though MDDS) to allow UCLA to maximize volume-based postal discounts and ensure proper controls and compliance with USPS regulations. Departments with exceptions to the policy are typically off-campus locations where it would not be efficient to have a centralized model.

According to the policy, departments that have been granted an exemption to the policy must submit monthly auditable records to MDDS to ensure that adequate monitoring and controls are in place. In addition, the policy states that "annually, meter exemptions will be reviewed by Mail Services in order to ensure that information provided by campus departments is current, postage and meters are being used properly, reasonableness of dollar limits is assessed and continued justification for an exemption to policy is appropriate." Although MDDS has been reviewing monthly auditable records from these exempted departments, they do not have the resources to verify that adequate monitoring and controls are in place at remote locations, and to test the accuracy of records and the effectiveness of controls. Similarly, when it completes the annual meter exemption reviews, MDDS is unable to verify the information provided by campus departments, nor can it determine if postage and meters are being used properly at these off-campus locations.

Recommendation: Management should work with campus administration to either revise UCLA Policy 310, or to secure adequate resources necessary to ensure compliance with the current policy.

Response: MDDS agrees that UCLA Policy 310 should be revised as the original controls put in place are no longer feasible. The policy originally pertained to just 12 historical exemptions but today relates to over 32 exemptions (with most of the growth due to the expansion of UCLA Health off campus). The revised policy should:

(1) Ensure that exceptions to policy remain very limited (especially if a department is located on campus).
(2) Place the ongoing responsibility for assessing risk and ascertaining if controls are in place with UCLA Audit and Advisory (the entity with the professional knowledge and the ability to recharge for professional services provided).

The expected completion date (initial policy draft) is September 1, 2016. Timeframe for approval/acceptance of policy draft is dependent on the Office of Administrative Policies & Delegations.

Equipment Inventory

Equipment Inventory Practices

A&AS met with MDDS management to understand how the department performs its annual verification of inventorial equipment. MDDS has three custody codes, each with a different equipment custodian. After obtaining the list of inventorial equipment from the Asset Management System (AMS), the custodian physically verifies each item and confirms the asset number, description, building and room number, serial number, current user, and condition codes. The table below summarizes the number of items and total acquisition costs of the three custody codes:

Table 3

	# of Items	Total AcquisitionCost
Mail Services	18	$704,932
Document Services	10	$254,798
Receiving	7	$234,422
TOTAL	35	$1,194,152

There were no significant control weaknesses noted in this area.

Physical Verification of Equipment

A&AS selected five assets with a total acquisition cost of $375,269 from the AMS as of December 1, 2015 and verified compliance with University policies and procedures.

All selected inventorial equipment was physically located and tagged with a University property number, and item information matched AMS records.

There were no significant control weaknesses noted in this area.

Accuracy of Records

For a judgmental sample of three items selected from MDDS facilities, A&AS verified that the property number, serial number, description, manufacturer/model, location, and current user agreed with the property record maintained in the AMS. Asset records appeared to be accurate and complete for the testing sample.

There were no significant control weaknesses noted in this area.

Equipment Disposals

A&AS generated the Equipment Disposals report in the AMS from July 1, 2013 to December 31, 2015 for the entire campus, and then filtered for MDDS custody codes (0332, 0333, 0416). Based on the report, only custody code 0333 (Document Services) had five equipment disposals during this timeframe. A&AS selected a judgmental sample of two disposals, requested supporting documentation from the department, and verified that each disposal had been authorized by MDDS management and was adequately supported. Equipment disposals were authorized by management and adequately documented.

There were no significant control weaknesses noted in this area.

<u>Systems Access</u>

MDDS uses Visual FoxPro to capture billing and project information for its various units. Visual FoxPro is a data-centric, object-oriented programming language produced by Microsoft. Developers can build database applications and manage data – from organizing tables of information, running queries, and creating an integrated relational database management system to programming a fully-developed data management application for end users. Microsoft discontinued its service support for Visual FoxPro in January 2015. However, MDDS has started to migrate some of its programs to vendor-provided, web-based solutions.

A&AS met with the department to understand how MDDS controls access to its various systems through Visual FoxPro. It was noted that controls over access to Visual FoxPro itself could be improved.

- MDDS has one system administrator for all its systems. As a best practice, there should be two system administrators with exactly the same level of access and privileges in the event that one is unexpectedly incapacitated.

- There are no password requirements for users to access the systems. UCLA Policy 401, Attachment A (Minimum Security Standards for Network Devices) states that all passwords employed to authorize access to campus electronic communications systems or services must meet minimum password complexity standards. The password must contain eight characters or more, and contain characters from at least two of the following three character classes:

  - Letters (e.g., a-z, A-Z)
  - Numbers (i.e., 0-9)
  - Special characters including a space (: !@#$%^&*()_+|~-=\`{}[]:";'<>?,./)

- User IDs are not suspended after successive invalid sign-on attempts. Although a user must enter a valid password within three attempts or the system access program closes, a user who has three invalid password attempts may still click on the Systems icon and make further login attempts.

Recommendation: To strengthen internal controls management should ensure that there is a backup system administrator, minimum password requirements are implemented in compliance with UCLA Policy 401, and user access is reset after a certain number of invalid sign-on attempts to ensure that only authorized users are accessing the system.

Response: MDDS agrees that the minimum password requirements should meet UCLA Policy 401 standards including the fact that a user account should be locked after a certain number of invalid sign-on attempts. In addition, a backup system administrator should be in place. The expected completion date is August 1, 2016.