

The logo for UCIrvine, featuring the letters 'UCI' in a large, bold, serif font, followed by 'RVINE' in a smaller, all-caps, serif font. A vertical line separates the 'UCI' and 'RVINE' parts.

UCIRVINE

The text 'INTERNAL AUDIT SERVICES' in a serif font, positioned to the right of the UCIrvine logo.

INTERNAL
AUDIT SERVICES

School of Physical Sciences
Internal Audit Report No. I2017-101
June 29, 2017

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INTERNAL AUDIT SERVICES
IRVINE, CALIFORNIA 92697-3625

June 29, 2017

**KENNETH C. JANDA
PROFESSOR AND DEAN
SCHOOL OF PHYSICAL SCIENCES**

**Re: School of Physical Sciences Audit
No. I2017-101**

Internal Audit Services has completed the review of the School of Physical Sciences and the final report is attached.

We extend our gratitude and appreciation to all personnel with whom we had contact while conducting our review. If you have any questions or require additional assistance, please do not hesitate to contact me.

Mike Bathke

Mike Bathke
Director
UC Irvine Internal Audit Services

Attachment

C: Audit Committee
Maria Graziano – Assistant Dean, School of Physical Sciences
Gabrielle S. Escobedo – Finance Director, School of Physical Sciences

I. MANAGEMENT SUMMARY

In accordance with the fiscal year (FY) 2016-2017 audit plan, Internal Audit Services (IAS) reviewed business operations and other financial activities within the School of Physical Sciences (SPS). In general, the review in SPS identified internal control and compliance weaknesses that should be improved to minimize business risks and ensure compliance with University policies and procedures and/or best business practices. The following concerns were noted.

Sales and Services Activities – Sales and services agreements were not obtained when SPS rendered services or provided goods to non-University entities. This observation is discussed in section V.1.

Cash Handling – Cash collections were not handled, secured, or deposited in a timely manner as required by policy. In addition, proper separation of duties was not established in the cash handling process. Further details related to these issues are provided in section V.2.

Non-payroll Expenditures – Proper supporting documentation is not always retained on file to support or justify PALCard transactions and some administrative reviews were not performed in a timely manner. These observations are discussed in section V.3.a.

Reimbursements – Proper supporting documentation and/or exceptional approval was not always submitted or obtained to justify and/or explain expenditures or missing receipts. Also, some reimbursements were not timely submitted and one of the Dean's travel reimbursements was not properly reviewed/approved. These observations are discussed in section V.3.b.

Payroll – Internal controls were not established to ensure that overtime pay and compensatory time off was appropriate and accurate. Also, prior approvals for overtime were not documented. This observation is discussed in section V.4.a.

Leave Adjustments – Concerns were also noted with vacation leave accrual (VLA) and sick leave accrual (SLA) adjustments made during the review period. Business procedures and processes were not established and implemented to ensure timely updates of accrual rates due to changes in employee's

reclassification/promotion. In addition, adjustments were made without documenting the calculation of hours or supervisory review and approval of the calculation. This observation is discussed in section V.4.b.

II. BACKGROUND

In 1965, SPS was established as one of the founding schools at the University of California, Irvine. SPS offers educational and research opportunities for tomorrow's scientists, teachers, and technical professionals in the departments of Chemistry, Earth System Science (ESS), Mathematics, and Physics & Astronomy. Approximately 1,208 undergraduate students are enrolled in Physical Sciences majors and 516 graduate students. Doctoral degrees are also granted from all four departments. In addition, SPS employs 140 faculty members, 121 researchers, 75 postdoctoral scholars, and 130 staff members.

An Associate Dean is responsible for academic oversight of undergraduate affairs, and reports to the Dean. Business operations and other financial/administrative activities are primarily the responsibility of the Assistant Dean, who also reports to the Dean. The Assistant Dean is supported by a Director of Finance, a Director of Personnel, an Information Technology (IT) Director, a Facilities Manager, and various other SPS staff members.

III. PURPOSE, SCOPE AND OBJECTIVES

The purpose of the audit was to assess SPS business risk, internal controls, and compliance with University policies and procedures. The review was designed to determine whether sufficient internal control measures are in place to prevent or detect inappropriate, non-compliant and/or fraudulent transactions, while ensuring efficiency and effectiveness in business operations. The audit scope included fiscal year 2015-2016 business operations and financial activities.

The following audit objectives were included in the review.

1. Review non-payroll expenditures for proper accountability and separation of duties, adequate supporting documentation, assurance of valid and pre-authorized transactions, as well as compliance with policies and procedures.
2. Determine whether the following aspects of payroll complied with University policy: overtime approval and sick and vacation leave accrual adjustments.
3. Review cash handling processes for compliance with policies and procedures and for assurance that collected funds are properly recorded, secured, reconciled, and deposited timely.
4. Verify if sales and services agreements between the facility centers and outside entities were obtained and reviewed by Material & Risk Management. Determine if the outside entities were properly and timely billed for sales and services activities.
5. Determine whether campus departments/units were properly and timely billed for recharge activities provided by the facility centers.
6. Evaluate the equipment inventory tracking procedures and sample inventorial items to ensure appropriate tagging, storage, and reporting.

IV. CONCLUSION

Many internal controls within SPS business operations and financial activities have been established and implemented. However, concerns were noted with the practices and processes in sales and services, cash handling, non-payroll expenditures, and payroll.

Observation details were discussed with management, who formulated action plans to address the issues. These details are presented below.

V. OBSERVATIONS AND MANAGEMENT ACTION PLANS

1. Sales and Services Activities

Background

A Sales and Services Agreement is initiated when a campus unit wishes to render a service or provide goods to a non-University user for which revenue is collected. This transaction is appropriate when the furnishing department incurs expenses to make available a product or service which is sold to the non-University user for an established price, or at a price based on an established standard pricing method.

UCI Administrative Policy, Section 703-14: Sales & Services Income Guidelines, established a mechanism for requesting, reviewing, and approving Sales and Services Agreements between the University community and a non-University entity. Also, under the policy, the campus unit should establish charges for the sale of goods and services provided to non-University users to ensure that University costs, both direct and indirect, are fully recovered.

Observation

IAS selected and reviewed the sales and services activities in the Keck Carbon Cycle Accelerator Mass Spectrometry Laboratory (Keck AMS), which has been in operation for 20 years and generated over one million dollars in income from their sales and services activities during FY 2015-2016. All sales and services activities (35 transactions, 27 different non-University entities) in the months of April and May 2016 were selected for further review to determine if the proper rates were applied during the billing process and if the invoices were billed in a timely manner.

The review disclosed that there were no sales and services agreements with any of the 27 different non-University entities and facility management could not recall if sales and services agreements were ever completed and obtained. However, IAS noted that each order form contained a current rates listing, which had been vetted through the budget office, and only two minor issues were noted when reviewing the invoice details. One entity was billed a couple

of months late another entity was charged the incorrect rate for services rendered resulting in a small under billing.

IAS performed additional testing in order to determine if sales and services agreements were completed and obtained by two other departments/units in SPS. IAS noted that there were no sales and services agreements for income generated in the Mass Spectroscopy Facility in the Chemistry department and Machine Shop in the Dean's Office.

University policy requires sales and services agreements when units wish to render a service or provide goods to a non-University user for which revenue is collected. The University may be subject to legal and financial exposure without a clearly stated sales and services agreement outlining the entire scope of the goods/services (i.e., relationship of the parties, rates charged, indemnification, etc.).

Management Action Plan

Effective immediately the Dean's Office will work with all facility managers as well as the employee in the Dean's Office who processes all invoices for the Facilities to make sure that all invoices are completed with correct rates and in a timely manner.

After speaking with multiple previous employees from SPS as well as current facility managers it has been determined that past practice has not included completing a sales and service agreement for services provided to outside entities. It has become obvious that the policy governing sales and service activities has not been enforced as well. With that said, SPS plans to partner very closely with the Budget Office as well as Risk Management to make sure that the policy is understood and enforced within SPS. IAS will follow-up on this corrective action by September 30, 2017.

2. Cash Handling

Background

University of California Office of the President policy, Business and Finance Bulletin – 49 (BUS-49) establishes the University’s policies related to handling and processing cash and cash equivalents, and defines roles and responsibilities related to receipt, safeguarding, reporting and recordkeeping for all University cash and cash equivalents. Its purpose is to ensure that University assets are protected, accurately and timely processed, and properly reported. The bulletin also establishes basic internal control principles (accountability, separation of duties, security, and reconciliation) in regard to collecting and accounting for cash and cash equivalents.

Observation

The cash handling processes in three departments (Chemistry, ESS, and Physics & Astronomy) were reviewed to determine if they were in compliance with University policy. The following is a summary of the observations.

Physics & Astronomy (P&A)

A principal investigator in P&A organized a conference. P&A was to collect a registration fee, \$200 each, payable by check or cash at the door from over 60 attendees, which included participants, speakers, and organizing committee members.

- An official University receipt was not recorded for each registration fee collected as required by policy. Instead, according to the analyst in charge of the conference registration desk, 66 attendees completed an attendance form, noting the payment amount and method, at the registration desk, but P&A did not keep a copy of the forms for their records so it’s uncertain which attendees paid and how much was collected. IAS determined that \$13,200 in registration fees should have been collected but only \$8,550 was deposited (\$4,650 is unaccounted for).
- P&A did not timely deposit the funds or use the appropriate lockable receptacles or burglarproof/fire resistant safes to store the cash and checks

as required by policy. According to the analyst in charge of the conference registration desk, the funds were stored in a lockbox and kept in the trunk of her car after the end of both conference dates until the monies were moved to her office on the following business day. In addition, the deposit was not made until three weeks after the conference and it was not validated and prepared under dual custody, which are against policy.

- P&A did not restrictively endorse the checks “for deposit only”, immediately upon receiving them. The checks, totaling \$4,300, were endorsed at the time of deposit, three weeks after the conference.
- The deposit was not transported securely to the Main Cashiering Station as required by policy using the following methods: By employees, in dual custody, transporting the deposit to the Main Cashiering Station. If the deposit is in excess of \$2,500, employees should be escorted by a Campus Security or Police Officer.

ESS

ESS has been collecting \$20 key deposits from University affiliates, such as graduate students and visiting scientists, but did not collect key deposits from University faculty and staff. However, ESS management waived key deposits for individuals they deemed to be financially unable to pay.

- An official University receipt was not recorded for each key deposit collection as required by policy. Policy states that a collection not recorded on cash register or point of sale equipment must be recorded on an official pre-numbered, multiple-part cash receipt.
- Also, a copy of the receipt was not provided to payers making an in-person payment as required by policy.
- An internal control procedure that ensures an adequate separation of duties was not established or maintained. For example, IAS noted that the ESS business manager kept the key deposit collections in a lockbox to refund key holders when they returned keys and maintained a spreadsheet of collections and refunds, but also prepared the deposit advice forms and

transported cash and cash equivalents to the Cashier's Office for deposit by herself.

- Some deposits were not validated and prepared under dual custody as required by policy.

Due to the lack of appropriate supporting documentation and lack of separation of duties, it is not possible to determine if key deposits were properly collected and deposited.

Chemistry

Chemistry has been collecting \$25 key deposits, from University employees, both faculty and staff, as well as affiliates as far back as July 2007. Chemistry management stated that cash was the preferred method of payment because it would be easier to refund key deposits to scholars from overseas when keys were returned.

- It should be noted that the practice of collecting key deposits from University employees is in violation of UCI Policy for Key Control and Access to Campus Facilities, Section 902-14, which became effective in July 2012.
- Chemistry's documentation for the reconciliation of the key deposits found that cash was not deposited in a timely manner, not weekly or when collections exceeded \$500 as required by policy. A cash count of the key deposits on July 28, 2016, disclosed that Chemistry had \$2,580 in cash. Furthermore, IAS review disclosed that the last two deposits through the Campus Online Deposit were on March 8, 2012, in the amount of \$3,050, and on July 18, 2013, in the amount of \$25.
- The key deposits were stored in a lockbox that was kept in a locked file cabinet and therefore did not use the appropriate lockable receptacles or burglarproof/fire resistant safes to store cash in accordance with the appropriate cash limits as required by policy. According to policy, cash collections from \$2,501 to \$25,000 are to be stored in a steel-door safe, with a door thickness of not less than 1 inch and wall thickness of not less than ½ inch.

The business unit head is responsible for establishing proper procedures and processes to ensure the unit is protected from loss and/or theft.

Management Action Plan

Key Deposits

Effective immediately all department managers will review section 902-14, Policy for Key Control and Access to Campus Facilities for compliance with stated policy. In addition they will also be required to review BUS-49 and implement changes to their collection of key deposits including, but not limited to, using official pre-numbered, multiple-part cash receipts, depositing cash in a timely manner, and assessing the need for more appropriate lockable receptacles. IAS will follow-up on this corrective action by September 30, 2017.

Conference Registration Fees

Effective immediately all department managers will be advised against collecting cash payments for conference registration fees. However, if it becomes necessary to collect cash payments for registration fees, as stated above, the managers will be required to review BUS-49 and implement changes to their collection of cash fees including, but not limited to, using official pre-numbered, multiple-part cash receipts, depositing cash in a timely manner, and assessing the need for more appropriate lockable receptacles. In addition, for any cash or cash equivalents collected as part of future conference registration, additional policy review and implementation will include, but is not limited to, proper endorsement of checks, dual custody when preparing deposits, and secure deposit transport.

Due to the delicate nature of handling cash or cash equivalents SPS will closely monitor the departments' efforts to comply with policy. The Dean's Office will work closely with the departments to make sure all policies are adhered to and that staff training is implemented for those who may come into contact with cash or cash equivalents. IAS will follow-up on this corrective action by September 30, 2017.

3. Non-payroll Expenditures

a. PALCard Transactions

Background

The purchasing card (PALCard) is used by staff with purchasing responsibilities to buy equipment, supplies, and services. UC purchasing policies require purchases to be pre-authorized either formally through an internal requisition or informally, such as an email. In addition, PALCard policies require an administrative reviewer to review PALCard supporting documentation and account/fund for appropriateness in a timely manner.

Observation

A sample of transactions was selected from July 1, 2015 through present for further review and the following observations were noted.

- Receipts and/or proof of delivery documentation are not always retained on file as to support the transactions.
- The business purpose for some PALCard transactions is not always clearly stated or documented.
- The administrative review was not always performed timely.

Implementation of internal controls, such as prior approval, maintaining proper supporting documentation as well as proper and timely administrative review minimizes the risks of error, fraud, waste, and improper use of University funds.

Management Action Plan

Effective immediately, all department managers will be asked to remind all faculty, students, and staff in their specific departments of the need to submit all supporting PALCard documentation as well as the business purpose to the central purchasing office in a timely manner. In addition, all PALCard reviews

and approvers will be reminded to review and approve in a timely manner as required by policy.

b. Reimbursements

Background

As of July 1, 2014, reimbursements for various transactions such as entertainment, travel, and other expenses are processed through the Kuali Financial System (KFS), a comprehensive enterprise financial system used to process most of the campus' financial transactions. Reimbursement requests pertaining to travel expenditures must comply with Office of the President (UCOP) Business and Finance Bulletin G-28 and expenditures for business meetings, entertainment, and other occasions must comply with UCOP Business and Finance Bulletin BUS-79 in addition to other applicable UCOP and UCI policies.

Observation

A sample of travel, entertainment, and disbursement voucher reimbursement transactions from July 1, 2015 to present was selected for review. The following is a summary of the observations.

Travel Expense Claims

- Some travel expense claims were not submitted in a timely manner, 45 days after the trip end date as required by policy.
- A principal investigator (PI) did not obtain prior approval for his spouse, who is not a University employee, to travel internationally to perform sampling for his research. However, exceptional approval from the Dean was obtained 90 days after the end of the trip.
- Proper supporting documentation and/or exceptional approval was not always submitted or obtained to justify and/or explain expenditures or missing receipts.

- One of the Dean's travel reimbursements was approved by his subordinate and was not reviewed and approved by the Vice Chancellor's office in accordance with policy.

Disbursement Vouchers

- IAS noted reimbursements to employees for supplies and materials expenses who lacked purchasing delegation of authority. In addition, some of the purchases were not properly supported with proof of payment documentation.

Entertainment Expense Reimbursements

- Some entertainment expense reimbursements reviewed lacked certification that the expenses were incurred for an official University business purpose. In addition, a copy of the Request to Serve or Sell Alcoholic Beverages was not submitted as proper supporting documentation.

Internal controls, such as a proper documentation, authorization, and review, reduce the potential for reimbursement of improper expenses as well as errors/inaccuracies, waste, and fraud to go undetected.

Management Action Plan

The SPS management team has already met with the Dean's Office contract and grant analysts where we reviewed BUS-28 as well as the audit review observations to determine the best way to proceed. During this meeting we carefully reviewed the observations and discussed how best to present the information to the departments, whose staff prepare all of SPS's travel expense claims, entertainment expense reimbursements, and disbursement vouchers. It has been decided that during the next several months we will be conducting meetings and/or workshops with the various departments within SPS to review policy/procedures and best practices. We will use the audit observations as examples in these meetings so that all departmental preparers will understand the importance of following policies/procedures and best practices. We expect this training to conclude on or before September 30, 2017.

4. Payroll

a. Overtime and Compensatory Time

Background

Personnel policy on overtime for staff members requires the department head to approve overtime for non-exempt employees to meet essential operating needs. The department is responsible for ensuring an employee requested advance approval for overtime work and properly report the overtime worked in a timely manner prior to compensation.

Policy also states, "A Compensatory Time Agreement form shall be used to record an employee's decision about accepting compensatory time off in lieu of premium overtime pay for hours in excess of 40 per week worked at management's request. The employee's decision to accept compensatory time off in lieu of cash overtime payment must be made freely and without coercion or pressure. The Compensatory Time Agreement form shall be used for employees who are hired, transferred, reclassified, or promoted into non-represented positions that are designated as non-exempt."

Observation

IAS reviewed 16 staff members who reported working overtime and received either compensatory time off or overtime compensation. IAS reviewed the overtime authorization and approval processes and noted that overtime authorization is not documented in writing to substantiate the need for the overtime and that approvals were obtained in advance as required by policy. One staff member, who was compensated from two federal awards, worked 1,358 hours of overtime during the award period, which exceeded his budgeted salary by \$32,380 and there is no supporting documentation to justify the need for the overtime. In addition, one staff member reported working overtime in error, and supervisors mistakenly approved the time sheets when, in fact, no overtime was actually worked for the week.

IAS noted that compensatory time agreements applicable for FY 15-16 were not obtained for seven of the 16 staff members reviewed as required by policy.

Lack of documentation to support the process of pre-authorizing and justifying overtime weakens the control structure and encumbers the review, approval, and reconciliation processes. In addition, undocumented and unjustified overtime compensation on federal awards is subject to disallowance.

Management Action Plan

The SPS management agrees that overtime on federally sponsored projects needs to be adequately documented and justified and will discuss this requirement with the related PI's and employees to ensure compliance. However, SPS management believes that the other overtime is low risk and will continue verbally approve overtime in advance since policy does not specify that it must be approved in writing. In regards to compensatory time, employees are given an opportunity each June to elect comp time off in lieu of overtime pay, however, they are not required to complete a form. If they do not indicate otherwise (via the form), they will receive overtime pay, per policy.

b. Vacation & Sick Leave Accrual Adjustments

Background

UCI departments are responsible for ensuring compliance with personnel policies for both faculty and staff. In regard to payroll and personnel processes, the department management is responsible for ensuring that all adjustments in the Payroll/Personnel System (PPS) are authorized in advance and reviewed for appropriateness and accuracy.

Observation

A total of 33 VLA and SLA adjustments for ten staff members in the Dean's Office, ESS, and Physics & Astronomy were selected for review. IAS noted that 30 adjustments were made without proper supporting documentation, such as verification of information and calculation of adjustment hours, as well as supervisory review or approval. In addition, some adjustments were made late. For example, in a letter dated March 2015, Human Resources approved the reclassification/ promotion for an employee in the Dean's Office. However,

the leave code was not updated in PPS until September 2015. In ESS, SLA adjustments were made for 10 pay periods for one employee on July 31, 2015 when the employee complained that she had not been accruing any sick leave from September 2014 to June 2015. In Physics and Astronomy, for one employee, 298 VLA and 149 SLA adjustments were made on June 30, 2016 for pay periods January 31, 2015 through June 30, 2016 because vacation and sick leaves are not accrued for this position.

Implementation of proper internal controls, such as a payroll reconciliation and prior authorization, minimizes the risks of error, fraud, and improper use of University funds.

Management Action Plan

VLA/SLA transactions processed for reclassification or promotion

Payroll Manual section 5.03 includes instructions for various fields to update, including employee relations code, next salary review date, time code, leave code, as well as vacation accrual rates that correspond to title/years of service. Once the reclassification/promotion approval has been obtained (may be several months after submission), the Payroll processor inputs the reclassification/promotion; updating various fields in PPS and processing any late time transactions (including salary, vacation accrual, etc.) to match the effective date using the approval letter from main Human Resources as our pre-approval document. In addition, Post Audit Notifications (PANs) are generated for mandatory reviewers to approve/confirm the transaction was entered correctly. Going forward steps will be taken to make sure that documentation is included for calculation of adjustments hours. IAS will follow-up on this corrective action by September 30, 2017.

VLA/SLA transactions were completed in a timely manner for the reclassifications stated, and based on approval documents received from Human Resources. Transactions can only be processed after a classification decision has been made, on occasion the classification decision happens several months after the reclassification is first requested. VLA/SLA transactions due to system error were processed based on central office instruction. In addition, all adjustments are reviewed by mandatory reviewers (via the PAN process) to approve/confirm transactions are processed correctly.