May 2, 2011

PETER J. FRANKS
Director, Integrative Oceanography Division
0218

Subject: *Integrative Oceanography Division*
            Audit and Management Advisory Services Project #2011-08

Attached is the final audit report for the referenced review. We would like to thank all members of the department for their cooperation and assistance during the audit.

Because we were able to reach agreement regarding corrective actions to be taken in response to the audit recommendations, a formal response to the report is not requested.

The findings included in this report will be added to our follow-up system. Management corrective actions have been included in the audit report. However, per our exit conference meeting on April 21, 2011 both findings will be closed due to completion of agreed upon management corrective actions.

UC wide policy requires that all draft audit reports, both printed (copied on tan paper for ease of identification) and electronic, be destroyed after the final report is issued. Because draft reports can contain sensitive information, please either return these documents to AMAS personnel or destroy them at this time.

Stephanie Burke
Assistant Vice Chancellor
Audit & Management Advisory Services

Attachment

cc: D. Bennett
       J. Davis
       T. Haymet
       D. Larson
       G. Matthews
       M. Nelson
       S. Vacca

AUDIT & MANAGEMENT ADVISORY SERVICES

Integrative Oceanography Division
April, 2011

<u>**Performed By:**</u>

Laurie Ward, Auditor
David Meier, Manager

<u>**Approved By:**</u>

Stephanie Burke, Assistant Vice Chancellor

Project Number: 2011-08

Table of Contents

Attachment A - Audit Results by Business Office Functional Process

I.   Background

Audit & Management Advisory Services (AMAS) completed a review of the Integrative Oceanography Division (IOD) within the University of California San Diego (UCSD) Scripps Institute of Oceanography (SIO) as part of the approved audit plan for Fiscal Year 2010-11.   This report summarizes the results of our review.

IOD has approximately 193 employees including 31 graduate students. In addition, they have 48 full or part-time volunteers. The Division incurred approximately $13million in expenditures last Fiscal Year 2009-2010. IOD is one of the oldest and largest centers for marine and earth science research, education, and public service in the world.   IOD research includes fieldwork, laboratory experimentation and computer modeling to acquire, integrate, synthesize and understand diverse data sets to expose the underlying dynamics of complex, multidimensional ocean systems.

The IOD Business Office staff support critical department business processes including academic and staff personnel management and payroll, information systems, contract and grant administration, research, recharge operations and financial analysis and monitoring. Business Office staff and Principal Investigators communicate frequently to address any issues or concerns.

The division has three recharge operations: the Hydraulics Laboratory (HLab), the Computational Infrastructure Services (CIS), and a labor clearing account.

The HLab is located at SIO on the San Diego campus. The function of the Hydraulics Laboratory is to provide expertise, space, facilities, and equipment for physical and biological oceanographic research.   CIS is IOD's physical computational infrastructure consisting of a multi-platform array of servers providing email, file, and other network services. The infrastructure team maintains the integrity of these servers and provides user support for both network and local resources.

The labor clearing account is set up for the purpose of recharging payroll costs. Effort is charged every payroll period directly to the Integrated Financial Information Systems (IFIS) clearing account. SIO personnel certify their effort monthly via timesheets, and payroll charges are then recharged by the IOD Business Office personnel from the temporary clearing accounts to the appropriate IFIS accounts based on the effort certified on the timesheets. At the end of the fiscal year, the clearing accounts are reconciled to ensure that payroll costs paid were materially consistent with costs charged to account via the recharge process.

II. **Audit Objective, Scope, and Procedures**

The objective of our audit was to evaluate whether internal control procedures in IOD were adequate to provide reasonable assurance that operations were effective, in compliance with University policies and procedures, and resulted in accurate financial reporting. The scope of the review was limited to activities and business practices for the Fiscal Year ended June 30, 2010 and for the period July 1, 2010 through January 31, 2011.

In order to achieve our objective we performed the following procedures:

- Reviewed IOD business documentation and information including the department website, the organizational structure and financial information;

- Interviewed IOD management and key personnel to discuss any potential areas of concern;

- Conferred with Personnel from the Office of Post Award and Financial Services (OPAFS), Campus Disbursements and Gift Administration;

- Evaluated IFIS electronic financial approval hierarchies;

- Evaluated business process controls, utilizing internal control questionnaires and segregation of duties matrices;

- Reviewed selected applicable federal requirements and University policies including but not limited to:

  o UCOP Contract & Grant Manual, *Chapter 7*;

  o UCSD Accounting Manual;

  o UCSD PPM 395-4.3: *Payroll Timekeeping Review of Charges;*

  o UCSD PPM 300-40 *Guidelines for Recharge and Other Income Producing Activities;*

  o UCSD PPM 510: *Use of University Property-payroll expenditure transactions;*

  o UC Business and Finance Bulletin *BUS 29: Management and Control of University Equipment;*

  o Academic Personnel Manual, Section 025: *Conflict of Commitment and Outside Activities of Faculty Members;*

  o UC Business and Finance Bulletin BUS 79*: Expenditures for Entertainment, Business Meetings and Other Occasions;*

  o UC Business and Finance Bulletin G-*28: Policy and Regulations Governing Travel;*

- o UCSD PPM 150-*35: Classification, Acceptance and Administration of Awards from Private Sources;*
- o UCSD PPM 300-*40 Guidelines for Recharge and Other Income Producing Activities;* and
- o UCSD BLINK guidance and links to policy including but not limited to express card practices, purchasing, travel, entertainment, equipment, delegation of authorities, approval hierarchies, facilities management and Statement of Auditing Standard (SAS) 112 compliance.

- Reviewed custody and accountability over IOD equipment;

- Verified the financial status of department funds and indices for the Fiscal Year ended June 30, 2010 and for the period July 1, 2010 through January 31, 2011;

- Evaluated supporting documentation and associated conflict of interest disclosures for a judgmental sample of gifts; and

- Analyzed procedures and performed limited transaction sampling in the following areas to verify that internal controls were adequate and functioning in compliance with university policy:

  - Contract and grant administration,

  - Operating ledger review,

  - Transaction sampling reports,

  - Payroll and timekeeping,

  - Payroll and non-payroll expenditures and expense transfers,

  - Travel and entertainment,

  - Express card,

  - Effort reporting/Labor Clearing Account Process,

  - Cash handling,

  - Service agreements,

  - Equipment inventory,

  - Recharge Activities,

  - Overdraft Reporting, and

  - SAS 112 compliance.

The scope of our review did not include an analysis of the information systems and processes because we recently completed a review in this area (AMAS project number 2010-10).

III.   Conclusion

Based on our review procedures, we concluded that internal controls within IOD were adequate and functioning effectively to provide a reasonable assurance that operations are effective, in compliance with University policies and procedures, and result in accurate financial reporting.

IOD management appears to have a good working knowledge of internal controls, and how they should be established. The Business Office has a strong working relationship with IOD researchers and staff.

We also noted a number of strong internal control practices that supported a strong internal control structure including but not limited to the following:

- Use of an internally developed financial reporting system, BUX, for effective communication between Principal Investigators (PI's), fund managers and the Business Office.
- Open and consistent communication between the Business Office and PI's.
- Use of Transaction Sampling.
- Use of the Overdraft Reporting System for monitoring funds in overdraft.

Attachment A provides the results of the business process review. Specific management actions planned or in process for those areas that were rated "satisfactory" or "improvement suggested" are noted in *Attachment A*.

IV.   Observations and Management Corrective Actions

A.   Approval Hierarchies

In one instance, an electronic financial approval hierarchy for travel was not appropriate.

Section IV, Approval of Travel, in Business and Financial Bulletin G-28: *Policy and Regulations Governing Travel* provides: "In order to ensure that travel is approved in an impartial manner, travelers may not approve the reimbursement of their own travel expenses. In addition, an employee shall not approve the travel expenses of an individual to whom he or she reports either directly or indirectly."

We performed a review of IOD's IFIS document approval hierarchy templates and noted the following issue. In one instance, an employee was set up to review and approve their own travel advances within the division, although the employee had not initiated any travel advances in our audit period.

IFIS document approvals should reflect current Division personnel to ensure transactions can be initiated and approved only by properly authorized personnel. Improper and unnecessary IFIS Approval Templates increase the risk that errors or irregularities could occur and go undetected.

Management Corrective Action:

IOD management deleted the hierarchy that would allow the employee to approve their own travel advance.

B.   Equipment Inventory

A physical equipment inventory count had not been conducted since 2007.

UC Business and Finance Bulletin (BUS) 29: *Management and Control of University Equipment* requires that the custodial department complete a physical inventory of all University inventorial equipment, government inventorial equipment, other government property, and other inventorial items at least every two years. The policy further states that the individual who performs the inventory may not also be assigned the responsibility for ordering or purchasing the property, maintaining the property records, or maintaining direct custody of the property.

IOD last conducted a physical inventory in 2007, in part because the division has not received information from or instructions on use of the new CAMS system to facilitate their inventory. An equipment inventory is needed to ensure that location codes are correct and that equipment that is unaccounted for is removed from inventory records. In addition, it is needed to ensure UCSD eligibility to receive federal awards by the timely submission of physical inventories.

Management Corrective Action:

Division management will continue to work with General Accounting, as needed, to obtain an equipment inventory listing, and complete an inventory as required by University policy.

Integrative Oceanography Division
Audit Results by Business Office Functional Process
Audit & Management Advisory Services Project #2011-08

Business Office Process	AMAS Audit Review Procedure				Risk & Controls Balance Reasonable (Yes or No)	Audit Conclusion[1]	Comments
	Analytical Review of Financial Data	Internal Control Questionnaire/ Separation of Duties Matrix	Process Walk-through (Ltd Document Review)	Transaction Testing (Sample Basis)			
Timekeeping & Payroll	√	√	√	Reviewed two months of timesheets, supporting documentation, recharge reports, Distribution of Payroll Expense Reports (DOPES) and performance evaluations for 10 employees.	Yes	Satisfactory	Separation of duties appeared adequate. Supporting documentation was properly maintained. Employees' evaluations were completed as required. No exceptions noted.
Transaction Processing - Non-Payroll Expenditures	√	√	√	Reviewed randomly selected transactions; traced to supporting documents.	Yes	Satisfactory	Separation of duties appeared adequate. Non-payroll expenditures appeared reasonable, and supported by documentation. No exceptions noted.
Express Card	√	√	√	Reviewed process and division management of express cards.	Yes	Satisfactory	Purchases were reasonable and appropriately authorized. No exceptions noted.

[1] Scale: Satisfactory - Improvement Suggested - Improvement Needed - Unsatisfactory

Business Office Process	AMAS Audit Review Procedure				Risk & Controls Balance Reasonable (Yes or No)	Audit Conclusion[1]	Comments
	Analytical Review of Financial Data	Internal Control Questionnaire/ Separation of Duties Matrix	Process Walk-through (Ltd Document Review)	Transaction Testing (Sample Basis)			
				Randomly selected 7 transactions; traced to supporting documentation.			We noted the Division took measures to ensure they were in compliance with policy.
Operating Ledger Review & Financial Reporting		√	√	Examined sample of operating ledgers and financial reports. Interviewed management and reviewed internal control questionnaires to determine what their process was for financial reconciliation.	Yes	Satisfactory	Operating ledgers were reviewed and reconciled by division management and PI's. They utilize Blink tools, web resources and an internal reporting system "BUX" for monthly reports to PIs.
Contract & Grant Activity (Post Award Admin.)	√	√	√	Selected three various award files and associated operating ledger detail for supply charges;	Yes	Satisfactory	Financial activity was routinely monitored for compliance with relevant agency requirements. Internal reporting and communication with Business

Business Office Process	AMAS Audit Review Procedure				Risk & Controls Balance Reasonable (Yes or No)	Audit Conclusion[1]	Comments
	Analytical Review of Financial Data	Internal Control Questionnaire/ Separation of Duties Matrix	Process Walk-through (Ltd Document Review)	Transaction Testing (Sample Basis)			
				evaluated selected journal vouchers, non payroll and payroll expenses and salary charges.			Office and PIs was consistent and thorough.
Effort Reporting (Labor Clearing Account)	√	√	√	Interviewed management, reviewed prior audits and reviewed SIO process for certifying effort. Reviewed labor clearing account year end reports for fiscal year 2009 and 2010 as well as financial activity on financial link, traced a small sample to recharge reports and DOPES.	Yes	Satisfactory	Division appears to have a strong management team that monitors and manages the labor clearing account. The process appears adequate and certification is timely and accurate by all employees. No exceptions noted.
Payroll Expenditure Transfers	√	√		Verified four adjusted payroll charges per operating ledgers & distribution of payroll	Yes	Satisfactory	Expense Transfer explanations appeared reasonable. No exceptions were noted. No

Business Office Process	AMAS Audit Review Procedure				Risk & Controls Balance Reasonable (Yes or No)	Audit Conclusion[1]	Comments
	Analytical Review of Financial Data	Internal Control Questionnaire/ Separation of Duties Matrix	Process Walk-through (Ltd Document Review)	Transaction Testing (Sample Basis)			
				expense reports (DOPE's).			exceptions noted.
Non-Payroll Expenditure Transfers	√	√		Reviewed a sample of six transfers for timeliness, business justifications and reasonableness.	Yes	Satisfactory	Separation of duties appeared adequate. Non-payroll expenditures appeared reasonable and supported by sufficient documentation. No exceptions noted.
Entertainment Expenditures	√	√		Reviewed a sample of five entertainment only expenses for business justification and timeliness in addition to other expenses for any unusual items or amounts.	Yes	Satisfactory	Selected expenses charged appeared reasonable and appropriately approved. No exceptions noted.
Gift Funds	√	√		Reviewed three gift fund files and verified proper classification, gift acceptance forms, proper use of funds,	Yes	Satisfactory	Selected funds appeared to be appropriately set up, monitored and managed in compliance with donor intent and University policy. No exceptions noted.

Integrative Oceanography Division
Audit Results by Business Office Functional Process
Audit & Management Advisory Services Project #2011-08

Business Office Process	AMAS Audit Review Procedure				Risk & Controls Balance Reasonable (Yes or No)	Audit Conclusion[1]	Comments
	Analytical Review of Financial Data	Internal Control Questionnaire/ Separation of Duties Matrix	Process Walk-through (Ltd Document Review)	Transaction Testing (Sample Basis)			
				timeliness and compliance with University policy.			
Service Agreements		√	√	Reviewed two service agreements and financial information.	Yes	Satisfactory	Service agreement process and sample reviewed appeared to be in compliance with University policy and appropriate documents maintained and approved.
Financial Overdraft Reporting	√	√	√	Reviewed and analyzed overdraft report and interviewed financial management to determine process for monitoring balances. Reviewed one balance older than 3 months over $10,000 as of January 31, 2011.	Yes	Satisfactory	Department processes were effective for preventing deficit spending. Balances were closely monitored and resolved immediately when possible. Monthly certification of review was documented. No exceptions notes.
SAS 112			√	Interviewed management and	Yes	Satisfactory	Management is well aware of the requirements and need for

Integrative Oceanography Division
Audit Results by Business Office Functional Process
Audit & Management Advisory Services Project #2011-08

Business Office Process	AMAS Audit Review Procedure				Risk & Controls Balance Reasonable (Yes or No)	Audit Conclusion[1]	Comments
	Analytical Review of Financial Data	Internal Control Questionnaire/ Separation of Duties Matrix	Process Walk-through (Ltd Document Review)	Transaction Testing (Sample Basis)			
Compliance				reviewed division process for compliance with SAS regulations.			SAS compliance. They have an internal checklist set up for monthly, quarterly and annual certification.
Cash and Recharge	√	√	√	Reviewed recharge activity reports, proposed recharge analysis worksheet, and supporting documents as well as communication with the campus recharge committee.	Yes	Satisfactory	Department does not receive cash, but they were equipped with the appropriate endorsement stamp and safe in case of the occasional check. Recharge processes appeared to be appropriately managed and monitored in compliance with University policy. IOD Management is actively managing operations and in communication with the recharge rate committee as needed.
Travel Approval Hierarchies	√	√	√	Reviewed five trips; traced to vouchers (TEV's) & supporting documents.	Yes	Satisfactory / Improvement Suggested	Travel expenses appeared to be administered appropriately and in accordance with UC Policy and Procedures. However, we did note one

Business Office Process	AMAS Audit Review Procedure				Risk & Controls Balance Reasonable (Yes or No)	Audit Conclusion[1]	Comments
	Analytical Review of Financial Data	Internal Control Questionnaire/ Separation of Duties Matrix	Process Walk-through (Ltd Document Review)	Transaction Testing (Sample Basis)			
							instance of an approval hierarchy template that needed to be corrected. *(Refer to section A of the audit report)*
Equipment Management	√	√	√	Reviewed inventory listing and equipment file for purchases, transfers, and deletes. Reviewed inventory management process and traced a small sample of equipment purchases from financial link transactions and reconciled those items to the Campus Asset Management System verifying location and existence.	Yes	Satisfactory / Improvement Suggested	The financial controls over equipment purchases appeared adequate. However a physical inventory had not been done since 2007, well over the 2 year requirement stipulated in UC policy *Section J* of **BUS 29**. *(Refer to section B of the audit report)*