UNIVERSITY OF CALIFORNIA
ETHICS, COMPLIANCE AND AUDIT SERVICES
OFFICE OF THE PRESIDENT
INTERNAL AUDIT SERVICES

University of California
Washington Center Audit Report
Audit No. P21A010
January 2022

Work Performed by:
Baker Tilly US, LLP

Work Reviewed by:
Systemwide Deputy Audit Officer Hicks
Executive Summary

Introduction and Objectives

In accordance with the annual audit plan, Internal Audit initiated an audit (IA) of key internal controls and processes at the University of California Washington Center (UCDC). The objectives of this audit were to:

- Confirm the extent to which management implemented its action plans from Advisory Services Project No. P12C010, University of California Washington Center (prior review)
- Evaluate the alignment with University policies and procedures of UCDC internal controls and processes for financial planning and budgeting, maintaining reserves and fund balances, invoicing internal and external parties, and compensation and salary setting
- Assess whether internal controls within high risk areas are operating effectively

Scope and Approach

Internal Audit performed the following activities to meet the project objectives related to this audit:

Preliminary Analysis (“Phase 1”)

- Performed a preliminary risk assessment to evaluate risks related to the following areas:
  - Financial planning and budgeting (e.g., budgeting process, financial projections, analysis of revenues and expenditures) (see Appendix A)
  - Reserves (e.g., status of reserve balances, process for designating reserve balances)
  - Fund balances (i.e., designated and restricted)
  - Budgetary communications (e.g., communication of budget to actuals within UCDC, as well as between UCDC and UCOP offices)
  - Creation and use of internal and external rates for invoicing (e.g., recharge rates, event rates)
  - Compensation and salary setting (e.g., salaries for incoming hires, raises and bonuses, parity with UC guidance)
  - Planning for continued COVID-19 programming impacts

- Based on the preliminary risk assessment, refined the scope and selected specific areas to review utilizing the following procedures:
  - Interviewed key UCDC and UCOP stakeholders responsible for the selected
operational activities to assess current processes
  o Reviewed policies, procedures, and other process documentation related to the in-scope areas
  o Evaluated whether action plans from the prior review were implemented in the following areas:
    • Safety and security
    • Receivables management (e.g., invoicing other institutions, recharges for schools)
    • Handling of cash and cash equivalents
    • Reconciliations
    • Events (e.g., timely invoicing, use of established rates)
    • Payments to lecturers
  o Assessed whether current processes for the selected operational activities align with University policies and procedures, and identified any potential control gaps and recommendations

Data Analysis and Sample Testing Review (“Phase 2”)

Based on observations identified during the preliminary risk assessment and interviews performed, Internal Audit performed data analytics (see Appendix B) on accounts payable, vendor, and employee data to identify the following:

• Potential duplicate transactions or payments/reimbursements
• Payments near approval limits
• Unexpected payment amount or reimbursement amount trends (i.e., Benford’s Law analysis)
• Potential personal spending
• Reimbursements to suspicious vendors or merchants
• Top spend by vendor or department
• Potential fictitious vendors (e.g., compare vendor master file to employee master file, missing or false tax IDs, etc.)
• Duplicate vendors and employees

Additionally, Internal Audit tested a sample of transactions and records based on the analytics performed to determine the appropriateness of the transactions.¹

¹ Internal Audit initially selected 40 samples of accounts payable transactions and vendor/employee records. However, we subsequently discovered one of the data populations provided by the UCOP Business Resource Center mistakenly included non-UCDC transactions. Three samples Internal Audit selected for testing were not UCDC transactions, therefore, we tested 37 samples.
Conclusion

As a result of our audit work completed during our preliminary review, we noted areas for improvement related to UCDC's fiscal processes, including the necessity to strengthen fiscal oversight and the visibility to accurate and updated financial information at the leadership level within both UCDC and UCOP. Some of the issues noted can be attributed to unique challenges associated with UCOP’s recent implementation of new budgeting and financial accounting systems. Other issues appear to be attributed to turnover and insufficient staffing to support financial management at UCDC. Accordingly, we recommend that UCDC leadership seek guidance from UCOP’s budget and financial accounting offices and consider assistance from external service providers to address issues related to reserve levels and accuracy of budget line items, account balances, accounts receivable, and accounting for restricted funds.

The eleven observations below were a result of Internal Audit’s preliminary review (“Phase 1”) performed during the period of September 2020 – February 2021. Based on the results of our Phase 1 review, Internal Audit identified high-risk areas to perform more detailed audit procedures, including data analysis and transaction sample testing to complete this audit.

Internal Audit’s second phase of review (“Phase 2”) performed during the period of February 2021 – August 2021, identified several areas for UCDC Business & Information Services and UCOP Budget and Finance personnel to perform further review, Appendix B.

Contextual information on key revenue and expense flows for UCDC is provided in Appendix A.

Opportunities for Improvement and Action Plans

Below is a summary of observations and actions plans from Internal Audit’s work.

1. Inadequate Accounts Receivable Policies and Procedures

Observation as of February 2021:

As of the end of Phase 1, UCDC did not have a collections policy and efforts to reconcile and follow up on accounts receivable were ad hoc and inconsistent. The UCDC Accounts Receivable Aging Detail as of February 29, 2020 from QuickBooks showed $666,053.29 in past due amounts outstanding for 91 or more days, with some amounts dating back as early as October 2012. It was not readily discernible how much of this is receivable from within the University versus externally. UCDC indicated this balance did not accurately reflect the status of past receivables.

Additionally, UCDC did not record receivables in its financial system, making it more difficult to project and accurately assess UCDC’s financial position. For receivables, UCDC used QuickBooks for invoicing other institutions (e.g., universities that have agreements with UCDC to use classroom and residential space) and entities (e.g., groups using UC facilities for events); however, QuickBooks did not interface with the financial
system. UCDC did not record receivables in the financial system based on invoices generated in QuickBooks; instead, UCDC recorded the payments in the financial system when received.

Collecting outstanding invoices is key to maintaining UCDC’s incoming revenue. Additionally, out-of-date reports lead to challenges with following up on outstanding receivables, and a strategy for write-offs and collectibles is key to an accurate understanding of UCDC’s financial position.

September 2021 Update:

Per UCDC management, UCDC has implemented the Oracle Financials Cloud (OFC/FIS) to handle accounts receivable collections, and only uses QuickBooks for recharge transactions. Additionally, UCDC management indicated it is now abiding by UCOP’s collections policies.

Internal Audit will validate these actions as part of its standard follow-up process to verify implementation of corrective actions resulting from this audit.

Action Plans:

Following UC Policy and Procedures, the Assistant Director-Admin (AD) will complete the following:

- Formally establish and document a collections policy, including how to evaluate and possibly write off uncollectible amounts,
- Implement processes for recording and tracking receivables in the Oracle system,
- Transition invoicing and invoice follow-up to the Finance team to enable appropriate recording, reconciliation, and follow-up,
- Set a materiality threshold, reconcile, and write off uncollectible accounts receivable amounts, and
- Create unit specific procedures and staff will be trained and acknowledge full understanding of relevant policies.

Target date: 3/31/22

2. Inconsistent Budget to Actual Reporting and Monitoring

Observation as of February 2021:

As of the end of Phase 1, budget to actual reporting and monitoring was not consistently performed at UCDC, with turnover continuing to occur in a key financial role typically responsible for this aspect of operations. Processes and escalation protocols for overall financial management were not formally defined, such as processes for periodically escalating detailed budget to actual information throughout UCDC (e.g., up to the Executive Director) and to other parts of the organization (e.g., up to the Vice Provost for Academic Personnel and Programs).
**Action Plans:**

The Assistant Director-Admin will start a procedure of monthly monitoring of budget to actual reports using the Oracle system. The Director will receive a monthly report.

**Target date:** 3/31/21

3. **Lack of Guidance and Formal Processes for Monitoring the Use of Designated and Restricted Funds**

**Observation as of February 2021:**

As of the end of Phase 1, formal processes for administering and monitoring the use of designated and restricted funds were not in place at UCDC. Internal Audit was unable to obtain descriptions of UCDC fund designations. Although UCDC had a relatively small volume of funds with a total of 18 designated and six restricted funds, the risk existed that funds were inappropriately commingled rather than managed in a separate account, or potentially used in a manner that did not align with the fund’s designated purpose or the donor’s intent, particularly if UCDC is able to grow its fundraising activity in the future.

For example, UCDC staff described a situation in which an organization called Partnership for Public Service wished to pay UCDC students as interns and paid the amount to pass through UCDC, with UCDC then providing students with checks for their payment amount. It is unclear whether this was recorded and taxed appropriately.

**September 2021 Update:**

Per UCDC management, since the conclusion of Phase 1, UCDC personnel have collaborated with UCOP to create a consolidated use fund.

Internal Audit will validate this action as part of its standard follow-up process to verify implementation of corrective actions resulting from this audit.

**Action Plans:**

In addition to the actions taken subsequent to Phase 1, the UCDC Assistant Director-Admin will complete the following actions, in consultation with and would like additional implementation guidance from UCOP Budget and Finance:

- Establish formal processes that are consistent with the UCOP Budget Manual for classifying and monitoring designated and restricted funds, including defining:
  - How restricted funds will be maintained in separate accounts,
  - How restrictions and donor intent information will be maintained and periodically updated, and
  - How use of funds will be monitored to confirm compliance with donor intent and any relevant restrictions.
• UCDC will follow UCOP policy. Staff will be trained and acknowledge understanding of policy and procedure.

**Target date:** 3/31/21

4. **Inaccurate Data Transfer into Oracle Planning and Budgeting System**

**Observation as of February 2021:**

As of the end of Phase 1, opening budget line item amounts and account balances in the new Oracle Planning and Budgeting System (PBS) did not appear to have correctly transferred amounts or mapped accounts from the previous system, resulting in inaccurate account balances for UCDC and contributing to challenges with financial monitoring. For example, PBS showed $1.2 million in Office Supplies and $919,000 in Fines, Penalties, and Disallowances for FY 2019-2020, and it was unclear to UCDC staff what previous amounts resulted in these balances.

**September 2021 Update:**

Internal Audit reviewed the year-to-date information in PBS for FY 2020-21 and noted some changes to the account descriptions from the prior year. For example, the account with the description of “Fines, Penalties and Disallowances” in FY 2019-20 now has the broader description of “Other Operating Expenses.” Per UCOP Budget and Finance, this account had a mapping error that was subsequently fixed. Further, per UCOP Budget and Finance, there have been some data and mapping issues across UCOP related to the conversion from the old budgeting system (BDS) to PBS due to the differing ways the two systems handled object codes and expense accounts. This was further complicated by a change to the chart of accounts effective July 1, 2020.

**Action Plans:**

The Assistant Director-Admin will collaborate with UCOP Budget and Finance to research and correct any discrepancies, and verify that account mapping and transfer of funds occurred correctly for UCDC accounts. Activities may include the following:

- Select a sample of accounts and reconcile the account to supporting documentation
- Determine the point in time in which management is comfortable with the accuracy of financial data within the financial systems, and confirm whether the account mapping and transfer of funds occurred correctly for UCDC accounts
- Determine how UCDC develops its annual budget, including forecasting revenues and expenses, expected budget line items, interdepartmental communications regarding budgetary needs, and allocation of funds for budgeted amounts

**Target date:** 06/30/2022
5. **Lack of COVID-19 Financial Scenario Plans**

*Observation as of February 2021:*

As of the end of Phase 1, UCDC reported on the impact of COVID-19 on its overall revenue and operations to senior leadership. However, it had not yet created formal financial scenario plans for how to specifically adjust expenses and activities in different COVID-19-related operational and financial circumstances.

*September 2021 Update:*

Per UCDC management, subsequent to Phase 1, UCDC personnel developed numerous financial scenarios plans and submitted them to UCOP Operations for review.

Internal Audit will validate this action as part of its standard follow-up process to verify implementation of corrective actions resulting from this audit.

*Action Plans:*

The Assistant Director-Admin, on an ongoing basis, will formalize key scenarios by analyzing the specific impacts on revenue, expenses, and operations and documenting potential measures and their impact to enable continued fiscal resiliency.

*Target date: 12/31/22*

6. **Employee Salary Ranges Below Market Salary Ranges**

*Observation as of February 2021:*

As of the end of Phase 1, UCDC compa-ratios appeared to be below market salary ranges based on UCOP salary bands, which may result in recruitment and retention risks. In fiscal year 2020-2021, adjusting for the Washington, DC, area, three salaries were below the minimum annual salary grade, and 31 of 44 salaries (70 percent) were below market salary (i.e., have a compa-ratio of less than one). Nine employees were above market, with compa-ratios ranging from 1.01 to 1.35.

According to UCOP Human Resources’ compensation team, there may be appropriate reasons for salaries to be below the midpoint. For example, some UCDC positions are intentionally graded lower because they receive the benefit of a housing allowance. Other reasons for lower compa-ratio salaries include salary compression, years of

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2 Human Resources uses minimum, midpoint, and annual salary bands to evaluate compa-ratios for UCDC. Salary bands are based on divisions and job codes (e.g., Facility Manager 1, Administrative Assistant 3, UCDC Educator).

3 Based on guidance from UCOP Human Resources, Internal Audit adjusted compa-ratios to be 5 percent greater than those calculated by Human Resources to account for the difference between salaries in the Washington, DC, area and the Bay Area.

4 Note that in FY 2020-2021, five academic non-faculty salaries did not have associated salary ranges or compa-ratios and these positions are excluded from the analysis.
experience, and the salary levels of peer groups within UCOP. A comprehensive equity analysis for UCDC would help identify positions that would be candidates for an equity adjustment.

**Action Plans:**

The UCDC Executive Director and Assistant Director-Admin will request UCOP Human Resources to perform an equity analysis for UCDC staff and will use the results of that analysis to inform any necessary equity adjustments to staff salaries.

**Target date: 03/31/22**

7. **Lack of Formalized Processes to Evaluate Recharge Rates**

*Observation as of February 2021:*

As of the end of Phase 1, formal processes did not exist for periodically evaluating recharge rates internal to the University and confirming they are aligned with expenses and positioned to break even. UCOP Rate and Recharge Guidelines require units to undertake annual self-certification of their rates following initial review and submit biennial rate updates. Recharge rates should be submitted to a Recharge Committee tasked with reviewing biennial rate adjustments submitted by existing recharge activities, evaluating recharge methodologies, and reviewing plans for addressing substantial surpluses and deficits.

*September 2021 Update:*

Per UCDC management, subsequent to Phase 1, the Executive Director and former Business Manager discussed the need to look at other UC locations in an effort to standardize the process of establishing event rates across the system.

**Action Plans:**

Per UCOP Rate and Recharge Guidelines, the Assistant Director-Admin (AD) will implement a process for formally evaluating internal recharge rates on a biennial basis to compare the actual costs with the anticipated revenue, including evaluating how large of an increase may be necessary. Adjustments to the rates and methodologies should be reviewed by the UCOP Recharge Committee. UCDC will review policy across the UC system and align best practice accordingly. We will update biannually and submit to UCOP Recharge Committee for approval. All contracts will be approved by the AD prior to being executed.

**Target date: 06/30/2022**
8. **Outdated Event Rates**

*Observation as of February 2021:*

As of the end of Phase 1, UCDC event rates had not been updated since fiscal year 2014-15 and therefore may not have been reflective of current costs for executing an event.

*September 2021 Update:*

Per UCDC management, subsequent to Phase 1, the Executive Director and former Business Manager discussed looking at other UC locations in an effort to standardize the process of establishing event rates across the system.

*Action Plans:*

The Assistant Director-Admin (AD) will implement a process to periodically (e.g., every two years) review, update, and approve its event rates. UCDC will review policy across the UC system and align best practice accordingly. We will update biannually and submit to UCOP Recharge Committee for approval. All events will be approved by the AD prior to executing any contract.

*Target date: 06/30/2022*

9. **Reserve Needs for UCDC Have Not Been Determined**

*Observation as of February 2021:*

UCDC has not conducted an adequate analysis to determine appropriate reserve levels. It is therefore unclear whether its fund balances are appropriate, excessive, or inadequate.

As of the end of Phase 1, UCDC had approximately $2.3 million in carry-forward balances allocated to various accounts, including reserves for building maintenance and information technology, parking, events, and lease accounts. While these carry-forward balances may serve as an important operational reserve in an environment with the COVID-19 pandemic and limited increases to tuition, there may be opportunities to make current investments using these funds or formally designate the funds for future priorities.

The Operations & Management Advisory Committee (OMAC) identified in 2015 that reserves for non-residential (i.e., auxiliary areas such as parking, research, and academic spaces) major maintenance and technology renewal were not sufficient for the next ten years, with an anticipated excess of expenses over reserves in 2021 and 2026. UC policy requires UCDC to maintain building and capital asset reserves. This results in a risk that funds are not available in the future to appropriately maintain part of the building, as reserves for the residential portion may not be sufficient for both residential and non-
residential long-term maintenance and renewal.

UCDC leadership reports receiving differing guidance regarding whether UCDC is a profit center and should increase certain rates (e.g., parking) to generate revenue. Carry-forward balances currently serve as a reserve to mitigate the risk of increasing costs and relatively stagnant tuition revenue.

September 2021 Update:

Per UCDC management and UCOP Budget and Finance, UCDC worked out an arrangement with UCOP Operations to use its fund balances to cover operational expenses in lieu of lost revenue from the COVID-19 pandemic, thereby reducing a portion of its carry-forward fund balances.

Action Plans:

The Assistant Director-Admin will work with UCOP Budget and Finance and the UCDC Governing Council to:
- Clearly establish that UCDC is a self-supporting entity
- Work with similar UC organizations and UCOP to explore ways to meet financial reserve positions
- Conduct an analysis to determine appropriate operational, building, and capital asset reserve targets
- Manage its fund balances against the reserve targets and invest excess reserves into current operational needs

Target date: 06/30/2022

10. Inconsistently Recorded Accruals

Observation as of February 2021:

As of the end of Phase 1, accruals (i.e., revenue and costs based on amounts earned or owed) were not recorded consistently for UCDC. Although some accruals may have been recorded periodically in coordination with UCOP, formal processes were not in place to regularly accrue significant revenue and costs.

Action Plans:

The Assistant Director-Admin will work with the Business Resource Center to establish processes and expectations for regularly accruing significant revenue and expenses, in line with University policy. Processes should define what items should be accrued and how, and who will be responsible for recording accruals going forward.

Target date: 03/31/2022
11. Monthly Bank Deposits

*Observation as of February 2021:*

As of the end of Phase 1, bank deposits were made monthly rather than weekly, as required by UC policy.

*September 2021 Update:*

Per UCDC management, subsequent to Phase 1, UCDC personnel have implemented a process for regular, weekly bank deposits.

Internal Audit will validate this action as part of its standard follow-up process to verify implementation of corrective actions resulting from this audit.

*Action Plans:*

Internal Audit will validate implementation of the process for regular, weekly bank deposits.
Appendix A: Summary of Key Revenue and Expense Drivers at UCDC

Key Revenue Drivers

- Internal sources (i.e., funds coming from within the University)
  - Allocation of funds through UCOP based on the quota of students each UC institution committed to sending to UCDC each year (i.e., annualized bed commitments) and an established academic/educational rate for UCDC
    - These funds are allocated by UCOP in a lump sum as part of the budgeting process
  - Transfers of funds for student housing from UC institutions based on the number of students each campus sent to UCDC, the housing rates established by UCDC, and the dates for moving in and moving out of residential facilities specific to each student
    - The Building & Housing Manager generates a schedule and invoices each institution’s housing office within QuickBooks; invoicing for this is transitioning to the Finance team within UCDC
  - University-affiliated individuals or groups who use UCDC facilities (e.g., short stays, events, meetings, leases by University organizations)
    - These invoices are generated in QuickBooks and UCDC collaborates with the campuses or through UCOP to transfer the appropriate funds to UCDC
  - Payments by UCDC students by credit card, check, or cash for trips or events, lost items, etc.

- External sources (i.e., funds coming from outside of the University)
  - Payments for events held at the UCDC building hosted by non-UC affiliated institutions
    - UCDC generates an invoice for these organizations; invoicing for external parties will transition from QuickBooks to Oracle moving forward
  - Housing and leases paid by non-UC institutions for classroom space, students living in the UCDC residence hall, and information technology and mental health services fees per student based on agreed-upon rates
    - The Building & Housing Manager generates a schedule and invoices each institution within QuickBooks; invoicing for this is transitioning to the Finance team within UCDC

- Funds
  - State funding
  - Donor gifts (e.g., scholarships or fellowships, emergency grants to students)

- Carry-forward balances from past years
  - Carry-forward balances from past years can exist in a variety of accounts, such as events, parking, leases, and building accounts

- Reserves
  - UCDC has reserves required by UCOP for operations, information technology, and building maintenance
  - UCDC also has an external, interest-bearing reserve account that is part of UCOP’s investment portfolio
Key Expense Drivers

- Debt service for the UCDC mortgage, paid largely by UCDC, with a smaller portion paid by UCOP for the government relations activities occurring on the second floor of the building
- Salaries and benefits for UCDC employees
- Building operations, including monthly payments to an outside vendor maintaining the building (e.g., security, housekeeping)
Appendix B: Summary Data Analysis Results

The following is a summary analysis of transactions during the period July 1, 2018 – June 30, 2020 (prior to the implementation of the new financial system).

<table>
<thead>
<tr>
<th>TMA Analyses</th>
<th>Output of Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>Potential duplicate transactions or payments/reimbursements</td>
<td>284 transactions</td>
</tr>
<tr>
<td>Payments near approval limits ($5,000 threshold)</td>
<td>• 151 transactions over threshold</td>
</tr>
<tr>
<td></td>
<td>• 3,107 transactions under threshold</td>
</tr>
<tr>
<td>Unexpected payment amount or reimbursement amount trends (i.e., Benford’s Law analysis)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The transactions during this period are generally aligned with the Benford’s prediction; however, there are a few notable outliers for transaction dollar amounts starting with 27, 30, and 43</td>
</tr>
<tr>
<td>Top Spend by Vendor</td>
<td>1. AAA Complete Building Services Inc. - $2,447,424.96</td>
</tr>
<tr>
<td></td>
<td>2. Potomac Electric Power Company - $386,373.95</td>
</tr>
<tr>
<td></td>
<td>3. CDW Government Inc. - $306,046.92</td>
</tr>
</tbody>
</table>

The following is a summary analysis of transactions during the period July 1, 2020 – April 30, 2021 (subsequent to the implementation of the new financial system).

<table>
<thead>
<tr>
<th>TMA Analyses</th>
<th>Output of Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>Potential duplicate transactions or payments/reimbursements</td>
<td>104 transactions</td>
</tr>
<tr>
<td>Payments near approval limits ($5,000 threshold)</td>
<td>• 97 transactions over threshold</td>
</tr>
<tr>
<td></td>
<td>• 385 transactions under threshold</td>
</tr>
<tr>
<td>Unexpected payment amount or reimbursement amount trends (i.e., Benford’s Law analysis)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The transactions during this period are generally aligned with the Benford’s prediction; however, there are a few notable outliers for transaction dollar amounts starting with the numbers 16, 18, 21, 22, 23, 28, 30, 35, 40, 58, 64, 81, and 83</td>
</tr>
<tr>
<td>Top Spend by Vendor</td>
<td>1. AAA Complete Building Services Inc. - $73,397.26</td>
</tr>
<tr>
<td></td>
<td>2. Potomac Electric Power Company - $42,354.63</td>
</tr>
<tr>
<td></td>
<td>3. Hann &amp; Hann Inc. - $27,297</td>
</tr>
</tbody>
</table>

Internal Audit selected samples for testing from these outputs. The details of this output were shared with UCDC management so that they can perform additional follow-up procedures as needed.
<table>
<thead>
<tr>
<th>TMA Analyses</th>
<th>Output of Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>Potential Personal Spending</td>
<td>13 transactions</td>
</tr>
</tbody>
</table>