



AUDIT AND ADVISORY SERVICES

Residential and Student Service Programs Audit Project No. 12-593

August 27, 2012

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August 27, 2012

Harry Le Grande
Vice Chancellor
Student Affairs

Vice Chancellor Le Grande:

We have completed our audit of Residential and Student Service Programs (RSSP) with detailed testing in Cal Dining and Housing Operations Maintenance and Environment (HOME) Procurement as per our annual audit plan in accordance with the Institute of Internal Auditors, Inc. *Standards for the Professional Practice of Internal Auditing* and the University of California Internal Audit Charter.

The aforementioned and other observations with management action plans are expounded upon in the accompanying report. Please destroy all copies of draft reports and related documents. Thank you to the entire RSSP staff and to Cal Dining, HOME, Purchasing and Accounts Payable, specifically, for their cooperative efforts throughout the audit process. Please do not hesitate to call on Audit and Advisory Services if we can be of further assistance in this or other matters.

Respectfully reported,

Wanda Lynn Riley
Chief Audit Executive

cc: Associate Vice Chancellor LeNorman Strong
Assistant Vice Chancellor Eddie Bankston
Executive Director Shawn LaPean
Director Jeff Urdahl
Senior Vice President Sheryl Vacca
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**University of California, Berkeley
Audit and Advisory Services
Residential and Student Service Programs**

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OVERVIEW

Executive Summary

The audit objective was to assess the departmental systems of control to assure sound business practices are in place to support operational effectiveness and efficiency including compliance with University policies as well as applicable state and federal regulations in Residential and Student Service Programs (RSSP).

As a result of our assessment of current business risks, we focused the scope of the audit on two areas of Housing & Dining Services: (1) the food procurement process for Cal Dining's residential dining locations and campus restaurants and (2) the maintenance and service procurement process for Housing Operations Maintenance and Environment (HOME).

Based upon the audit procedures performed, we observed that the internal controls related to food procurement appear appropriately designed and operating effectively. We have no reportable observations related to food procurement in Cal Dining.

For HOME, we observed that internal controls related to approval and reconciliation of procurement card transactions appear appropriately designed and operating effectively. With respect to the procurement of goods and services through purchase orders (PO), we identified opportunities for improvement in the areas of contract negotiation, contract management, and in obtaining and maintaining necessary documentation for vendors to do business with the University, such as insurance. In brief, during testing we noted that terms for service and itemized costs on bids from the same vendor on multiple POs for preventative maintenance of boilers contradicted each other. As a result, it appears HOME underestimated the scope and cost of the work to be completed for the preventative maintenance project which resulted in additional costs that were billed after the fact and paid.

Source and Purpose of the Audit

The audit objective was to assess the departmental systems of control to assure sound business practices are in place to support operational effectiveness and efficiency including compliance with University policies as well as applicable state and federal regulations in RSSP.

Background Information

RSSP, in the Division of Student Affairs, provides housing, dining, residential and academic support services to 7,500 student residents. RSSP also manages six campus cafes and seven child care centers. RSSP is organized into the following departments and subunits:

- Housing & Dining Services
 - Administrative & Business Services
 - Cal Dining
 - Conference Services
 - Housing Operations Maintenance and Environment (HOME)
- Office of Student Development
 - Research and Planning
 - Residential Living
 - Academic Services
 - Family Housing
 - New Student Services
- Capital Projects
- Marketing
- Budget & Finance
- Human Resources and Organizational Services

RSSP is an auxiliary operation, with the exception of the Early Childhood Education Program, in the budget and finance unit, which receives some external funding. RSSP has over 2,000 career and student employees and an annual budget of approximately \$125 million and is one of the largest units on campus.

Scope of the Audit

As part of our audit planning we conducted interviews with management responsible for the RSSP units to obtain an understanding of management perspectives on financial, operational, and compliance risks.

Based upon these interviews and other analytical procedures we conducted which informed our assessment of current business risks, we focused the scope of the audit on two areas of Housing & Dining Services: (1) the food procurement process for Cal Dining's residential dining locations and campus restaurants and (2) the maintenance and service procurement process for HOME.

Cal Dining is the self-operated, full-service dining operation for the campus and includes the residence hall dining commons as well as campus restaurants, retail stores and catering. Their service philosophy is centered on three key principles of flavor and variety in high volume, health and wellness, and social responsibility.

HOME is responsible for all front desk, custodial, grounds, and maintenance operations in the residence halls and family, faculty and single student apartments. Their mission is to “create an environment that fosters academic success, social growth and community development by providing secure, clean, attractive and comfortable facilities and by remaining actively responsive to all clientele”.

For our detailed testing, we selected transactions from July 2011 through February 2012. We note that RSSP, including Cal Dining and HOME, was in the first cohort to implement BearBuy, the new online procurement system. HOME and Cal Dining were originally scheduled to convert to BearBuy in March 2012; however, it is our understanding that the date was extended in order for Cal Dining to resolve potential challenges with using the system for their food purchasing needs. Given the timing of the start of fieldwork for this audit and the timing of common purchasing payment terms (i.e., Net 30), we did not include transactions made in BearBuy in our testing sample. However, we expect that the controls we tested during this audit would be applicable to the new procurement system.

Procedures Performed

Our audit procedures included, but were not necessarily limited to, internal control questionnaires, process walkthroughs, physical observation, management interviews and detailed testing of sampled transactions.

For our detailed testing, we sampled 68 procurement transactions for Cal Dining totaling \$93,687 (4% of the total for the period) and 55 HOME procurement transactions totaling \$673,630 (12% of the total for the period).

Summary Conclusion

As a result of our review of food procurement practices and controls in ordering through approval of invoices, we determined that the operations at Cal Dining included internal controls such as segregation of duties, management oversight, and regular review of expenses. Based upon the audit procedures performed, we observed that internal controls related to food procurement appear appropriately designed and operating effectively.

For HOME, we observed that internal controls related to approval and reconciliation of procurement card transactions appear appropriately designed and operating effectively. With respect to the procurement of services from maintenance and service vendors we have the following observations:

- The process for negotiating and reviewing agreements for service allowed the execution of contracts with contradictory terms, which had financial implications

for HOME. The brief form agreement and POs incorporated by reference the vendor's proposals wherein the language was ambiguous about the inclusion of materials and supplies in the quoted price and they were excluded from the price breakout. When the University uses contract terms provided by third parties, greater scrutiny may be warranted to assure that terms accurately and clearly reflect the University's intention.

- We noted that contract management of the preventative maintenance project required improvement. We observed that the vendor selected for boiler maintenance appeared to conduct work between August and November 2011 and invoiced the campus the amounts detailed in their quotes and campus POs (approximately \$88,000). In December 2011, the vendor invoiced the campus for an additional \$52,000 which they represented was for additional labor and materials in excess of the initial quotes. We observed that the POs were not increased and approved to reflect the additional work but instead a fourth PO was created retroactively in January 2012 so that the invoice could be paid. We noted that there is insufficient information on the vendor's December invoice to conclude on whether the vendor's extra labor and materials charges claimed are reasonable and justifiable over and above work already invoiced and paid for. In addition, we observed that for related emergency repair work to boilers the PO was set up for an amount slightly higher than what was quoted yet the full amount of the PO was paid without documentation or justification supporting the additional amount paid.
- In our testing of the completeness of required documentation related to procurement of maintenance and services for HOME, we noted that in 20 of 45 transactions sampled, at least some of this required documentation, such as proof of insurance and completed sole source justification forms, could not be provided to us by RSSP.

The aforementioned along with management action plans are expounded upon below.

SUMMARY OF OBSERVATIONS & MANAGEMENT RESPONSE AND ACTION PLAN

HOME Service Procurement Practices: Contract Negotiation

As part of our audit testing, we selected a sample of transactions related to vendors providing services to Housing Operations Maintenance and Environment (HOME) and evaluated business processes for vendor evaluation and selection, pricing of services, and ongoing contract and vendor management.

Background/Relevant Policy

In evaluating these transactions, we recognize that it is the practice of the University to meet its need for goods and services at the lowest overall cost, while affording the maximum opportunity practicable to those who wish to become suppliers to the University.¹ In general, “service” and “maintenance” of a specific nature to be performed by an independent contractor is covered by the University’s purchase order form and standard terms and conditions of purchase.²

Furthermore, the Public Contract Code of the State of California (Public Contract Code Section 10507, et seq.) requires that all purchase contracts involving an expenditure of more than \$100,000 shall be awarded to the lowest responsible bidder meeting specifications, or else all quotations shall be rejected. The lowest responsible quote shall be determined on the basis of one of two methods: (1) cost alone or (2) on a cost per quality point basis.³

Negotiation is allowed for transactions below \$100,000 and competition is sought if the materiel manager determines that the competition is necessary to source, validate prices, or for other compelling business reasons. Negotiation may be used in conjunction with competitive quotations as well as in situations when competition is not obtainable or required. When it is advantageous to the University, all the necessary components of the order may be negotiated orally or in writing with one or more vendors. The number of vendors with whom negotiations are carried out is the responsibility of the materiel manager and will generally depend upon the size and complexity of the purchase and market conditions. Before making a commitment, there shall be a determination that the price is reasonable.

Observation

Our sample included a vendor selected to provide annual preventative maintenance and urgent repairs of boilers at RSSP facilities. There were four POs for this vendor (one for urgent repair and three for preventative annual maintenance). In three of the four quotes the terms contradicted the cost breakdown contained therein, which exposed RSSP to difficulty in

¹ Business and Finance Bulletin (BFB) BUS-43.I.A. Policy.

² BFB BUS-43.I.D. Services Provided by Independent Contractors.

³ BFB BUS-43.III.A. Common Goods, Materials, and Services over \$100,000 in Value.

adequately managing costs related to the contracts. Specifically, the proposal stated that the vendor would “supply labor, materials and equipment” to perform certain tasks that were listed. However, only the cost of labor was itemized and the line item for materials was excluded from the original proposal. An initial proposal quoted \$1,100 for labor and \$480 to \$567 for materials. Subsequent proposals quoted \$1,500 for labor and did not indicate a cost for materials and equipment. Ultimately, the vendor later billed RSSP for additional labor beyond the \$1,500 and for materials after the fact, costing RSSP an additional \$52,279 on \$87,995 of proposed work.

The negotiation and review of the agreement terms and conditions failed to identify and mitigate the risk of the noted exposure. As a result management lacked relevant information to determine that the negotiated price was reasonable.

Management Response and Action Plan

RSSP acknowledges the concerns raised in the procurement process. The lack of specificity in the project scope, the timing of POs and invoices, and the lack of detail in the vendor’s invoices give rise to the appearance of poor project oversight. HOME will put all of its project managers and maintenance management staff through a procurement training program by September 28, 2012. Emphasis will be on generating internal specifications, establishing detailed and specific vendor requirements for bids and invoices, timely completion of POs and timely submission and handling of invoices by vendors and project managers. This training program will be coordinated by RSSP’s purchasing group and conducted by Campus Purchasing with Audit and Advisory Services (A&AS) participation. We intend to track and verify effectiveness of this training through periodic peer review of contracts and POs. All participants will sign-in, indicating attendance.

HOME staff involved in establishing specifications and supervising contracts or projects have been reminded, in meetings and by email, of the necessary changes. This is to serve as a reminder until such time as the training mentioned above can take place.

In addition to confirmation with RSSP Purchasing, changes to POs or contracts in excess of 10% of the awarded amount will require the signature of the director for HOME.

Operationally, the project was managed closely. HOME staff was on site at each boiler as work was performed. This work had not been done for many years and there was a great deal of repair work required, beyond typical preventative maintenance. This work could not be determined until such time as the boilers are opened. Once the boiler was opened the work had to be completed quickly to insure a continued supply of hot water and/or heat to residents.

HOME Service Procurement Practices: Contract Management

With respect to the vendor in our sample that provided annual maintenance and necessary repairs to boilers in RSSP facilities, we observed contract management practices related to four POs that appear to have resulted in significant cost overages and retroactive payment for additional services.

On December 16, 2011 the vendor issued an invoice seeking an additional \$32,508 in labor costs stating that “supplied additional labor, above and beyond the scope of the quotations...Work consisted of performing annual preventive maintenance in excess of the \$1500 labor cap and labor to install miscellaneous materials...” This invoice also sought an additional \$19,771 in “additional materials, above and beyond the scope of the quotations...Work consisted of providing all necessary materials to perform annual preventative maintenance and supplying any additional materials per the customer’s request.” However, the support documentation provided for this additional work was an itemized proposal for 21 boilers that appears to not actually be related to the work claimed in the invoice. In addition, given that the PO was created after the invoice was submitted, it appears that the approval of additional work was not documented and/or potentially not given at the appropriate level before the work was done. A PO for the full amount of this invoice (\$52,279) was issued on January 19, 2012. This represented a 60% increase over the planned maintenance work of \$87, 995.

It was not evident that management was aware of the significant cost overruns until all related projects were at or near completion resulting in an after-the fact purchase order. A pattern of significant cost overruns may negatively impact budgets and hence operations and service level.

Based upon the descriptions on the December invoice, we noted that there is insufficient information to conclude whether the vendor’s extra labor and material charges are reasonable and justifiable over and above work already invoiced and paid.

Without the itemization of time and labor, management is disadvantaged in evaluating whether to complete boiler annual maintenance in house or outsource in the future. From a maintenance perspective, there is no information to support what work was performed on each boiler and to anticipate future repair/maintenance needs.

Management Response and Action Plan

See response above.

HOME and RSSP Purchasing have communicated to staff that language be included in all bids and contracts that requires vendors to submit detailed documentation in their invoices for time and materials on a case by case basis.

HOME Required Documentation for Procurement

We also tested for the completeness of required documentation related to procurement of vendor services including proof of insurance and completed forms for conflict of interest evaluation, basis of award, and/or sole source justification.

For 20 of the 45 transactions sampled, at least some of this required documentation could not be provided to us by RSSP.

Management Response and Action Plan

HOME will work with the RSSP Purchasing group to include this in the training program, mentioned above, to be completed by September 28, 2012. RSSP Purchasing will confirm completion of required documentation before allowing a contract or PO to be issued, this has already been instituted.

RSSP believes that following the submission of extra documentation that the count is down to four expired insurance documents out of 45 transactions still to be located.

RSSP always makes sure a vendor who provides service to RSSP possesses a current Certificate of Insurance. However, RSSP has not always maintained a copy of the Insurance Certificate once the certificate has expired, been superseded by a new current certificate, or the job has been completed without problem. Under the new BearBuy system, RSSP is attaching a copy of the applicable insurance document to the BearBuy electronic file along with other supporting documentation for that purchase. If the vendor is going to be used multiple times in a given year, the Insurance Certificate will be referenced in each purchase document and maintained in a central file in accordance with standard University document retention rules. RSSP Purchasing reviews the documents attached to BearBuy file to insure that all required documents appear in the file. This procedure has been implemented and will be reinforced in the procurement training to be conducted by September 28th.

A&AS acknowledged receipt of the additional information mentioned above.