

UC RIVERSIDE: AUDIT & ADVISORY SERVICES

December 16, 2011

To: Laurie Gustafson, Chief Financial & Administrative Officer

Subject: Internal Audit of School of Business Administration

Ref: R2012-C

We have completed our internal audit of School of Business Administration in accordance with the UC Riverside Audit Plan. Our report is attached for your review.

We will perform audit follow-up procedures in the future to review the status of management action. This follow-up may take the form of a discussion or a limited review. Audit R2012-C will remain open until we have evaluated the actions taken.

We appreciate the cooperation and assistance provided by you and your staff. Should you have any questions concerning the report, please do not hesitate to contact me.

Michael R. Jenson
Director

xc: Audit Committee Members
Interim Dean Wang

UNIVERSITY OF CALIFORNIA AT RIVERSIDE
AUDIT & ADVISORY SERVICES
MEMBER OF ASSOCIATION OF COLLEGE & UNIVERSITY AUDITORS

INTERNAL AUDIT REPORT R2012-C
SCHOOL OF BUSINESS ADMINISTRATION

DECEMBER 2011

Approved by:

Laura Bishin
Principal Auditor

Toffee Jeturian
Assistant Director

Michael R. Jenson
Director

**UC RIVERSIDE
SCHOOL OF BUSINESS ADMINISTRATION
INTERNAL AUDIT REPORT R2012-C
DECEMBER 2011**

I. MANAGEMENT SUMMARY

Based upon the results of work performed within the scope of the audit, it is our opinion that the system of internal controls over School of Business Administration (SoBA) processes, with the exception of the issues noted in the Observations section (Section III), is generally adequate and in compliance with applicable University policies and procedures.

SoBA management has taken a proactive approach and made progress in enhancing controls as evidenced by the following positive observations:

- 1) The unit has implemented the recommendations in the prior SoBA audit R2008-07.
- 2) During the audit, management was receptive to suggestions to improve segregation of duties and internal controls and they made several adjustments to application level security as a result.

However, we observed some areas that need enhancement to strengthen internal controls and/or effect compliance with University Policy:

- 1) SoBA Deficit Projections (Observation III.A).
- 2) Supplies & Equipment Inventories – Segregation of Duties (Observation III.B).
- 3) Travel Vouchers (Observation III.C).

These items are discussed below. Minor items that were not of a magnitude to warrant inclusion in the report were discussed verbally with management.

II. INTRODUCTION

A. PURPOSE

UC Riverside Audit & Advisory Services (A&AS), as part of its Audit Plan, performed an audit of SoBA to determine the adequacy of internal controls and evaluate compliance with applicable University policies and procedures.

Included in the review were consideration and evaluation of significant processes and practices employed in the management of SoBA, specifically addressing the following components:

1. Management philosophy, operating style, and risk assessment practices;
2. Organizational structure, and delegations of authority and responsibility;
3. Positions of accountability for financial and programmatic results;
4. Process strengths (best practices), weaknesses, and mitigating or compensating controls; and
5. Information and communications systems, applications, databases, and electronic interfaces.

B. BACKGROUND

In September of 2011, the Executive Vice Chancellor/Provost appointed Yunzeng Wang Interim Dean through June 30, 2013.

SoBA currently offers MBA, executive MBA (EMBA), and Ph.D. programs, as well as an undergraduate major in Business Administration. In Fall 2011, there were 158 MBA, 20 EMBA, 6 Ph.D., and 2,309 undergraduate students in Business Administration (including the Pre-Business students). SoBA charges a Professional Degree Fee (PDF) for the graduate level programs in addition to student fees. PDF annual fees are \$21,354 per student.

The undergraduate major was formerly under the College of Humanities, Arts, and Social Sciences (CHASS). Starting in FY 2009, it is managed and funded entirely by the SoBA primarily through General funds.

The self-supporting EMBA program, which started in FY 2009 and offered at the UCR Palm Desert Graduate Center, is expected to be discontinued. The last class of students will graduate in June 2013.

SoBA plans to introduce three new self-supporting programs in the coming years: 1) a one year Masters of Professional Accountancy (MPAc) starting Fall 2012, 2) a Fully Employed MBA (FEMBA) program, and 3) a Masters in Finance.

Presently, SoBA has a faculty complement of 25 (with 43.58 lines). They have EVC approval to hire seven more faculty in FY 2012. They have an administrative staff of 22 (five are funded on General State funds and the rest are primarily funded through Professional Degree Fees).

Relevant SoBA financial information for FY 2009 – FY 2011 follows.

SoBA Revenues and Expenditures (in thousands)						
Summary Account	FY 2009	FY 2010	FY 2011	% Total Rev/Exp	Inc/(Dec) FY2010 - FY2011	% Inc/(Dec) FY2010 - FY2011
Student Fee	2,200	3,110	3,530	80%	420	14%
Restricted Gift	504	473	727	16%	254	54%
Sales & Service Educ Act	13	70	160	4%	90	129%
Revenues Total	2,717	3,653	4,417	100%	764	21%
Academic Salaries & Benefits	7,996	7,481	7,819	68%	338	5%
Staff Salaries & Benefits	2,073	2,075	2,141	18%	66	3%
General Supplies & Expenses	1,221	1,163	1,469	13%	306	26%
Equip/Other Inventorial	148	135	73	1%	(62)	(46%)
Facilities	172	29	32	0%	3	10%
Expenditures Total	11,610	10,883	11,534	100%	651	6%
Net Income/(Loss)	(8,893)	(7,230)	(7,117)		113	2%

The largest expenditure category within General Supplies & Expenses for FY 2011 is Travel & Entertainment (\$520K). Academic and Staff Salaries & Benefits make up 86% of total expenditures for FY 2011.

Following is the SoBA Permanent Budget beginning of the year allocation (in thousands).

Fiscal Year	Amount
FY 2009	6,406
FY 2010	7,943
FY 2011	7,490
FY 2012	7,573
Increase FY 11 to FY 12	83
% Increase FY 11 to FY 12	1%

Following are the carry forward balances by Fund Group (in thousands).

Fund Group	FY 2009	FY 2010	FY 2011	FY 2012	Increase FY 2011 to FY 2012	% Increase FY 2011 to FY 2012
Core	932	820	147	213	66	45%
Endowment	26	17	15	22	7	47%
Gifts	1,524	440	727	1,124	397	55%
Sales & Service	45	5	10	28	18	180%
Fee	307	225	536	526	(10)	(2%)
Total	2,834	1,507	1,435	1,913	478	33%

Most of the increase in gifts carry forward from FY 2011 to FY 2012 pertains to Gary A Anderson foundation, which increased from \$286,000 to \$464,000.

SoBA expects to take approximately \$451,000 in permanent budget cuts in FY 2012. Projections have them going into deficit starting FY 2012 through the end of their projection period FY 2016. They are also entering into a reaccreditation period with the Association to Advance Collegiate Schools of Business (AACSB). See Observation III.A – SoBA Deficit Projections.

C. SCOPE

The audit included evaluating whether organizational procedures comply with UC and UCR policies and procedures, and good business practice. The audit was principally limited to the following areas:

- a. General Overview and Risk Assessment
- b. General Control Environment
- c. Business Processes
- d. Information and Communication Systems

We evaluated administrative and accounting procedures, and internal controls based on management responses to the internal control questionnaire and verification of selected areas.

The audit included, but was not limited to the following areas:

Analytic Review

We reviewed financial activity for FY 2009 through FY 2011 and obtained explanations for any unusual variances and significant fluctuations by Budget Category, Fund, and Activity Codes.

Fund Carry Forward and Deficit Balances Review

We reviewed the Resource Planning & Budget (RPB) Carry Forward Analysis (CF) for FY 2011 & FY 2012 for SoBA to verify accuracy of the analysis, look for unusual changes or deficits in core CF fund balances, core permanent budget beginning balances, endowment & gift balances, and C&G overdrafts.

Financial Management Review

We reviewed FY 2011 SoBA management reports (which included Actual, Budget and Projections through FY 2016), and Faculty Commitments Analysis. We reviewed the timeliness and evidence of Ledger Reconciliation Storage System reviews and certifications for three months in FY 2011. We also reviewed Budget Cuts taken in FY 2010 and FY 2011 and anticipated for FY 2012.

Distribution of Payroll Expenses and Leave Accounting

We downloaded the Distribution of Payroll Expenses (salary portion) for FY 2009 – FY 2011 and reconciled to the General Ledger. We reviewed unusual changes between Fiscal Years by employee.

Selected nine individuals for detail leave testing (e.g. vacation, sick, overtime, comp time, etc.). Examined their monthly timesheets for proper approval and accuracy of leave balances in the Personnel Payroll System.

The review did not include the determination of the propriety of vacation and sick time use and whether all leave taken had been reported in the Time Records. Therefore, there is a risk that opinions stated in this report could prove to be inaccurate since we did not test these areas.

Travel & Entertainment

We reviewed procedures over processing travel vouchers and entertainment and performed an analytic review of such activity from FY 2009 through FY 2011. Reviewed travel by account, vendor, cost center and source code. We judgmentally selected and reviewed 37 travel and entertainment invoices over three FYs (\$286,000 or 55% of population for FY 2011) for proper documentation, authorization, and Full Accounting Unit (FAU) coding.

Purchasing/Accounts Payable & Purchasing Card Disbursements

We performed an analytic review for FY 2009 through FY 2011 of purchasing card (Pro-Card) transactions (approximately \$285,000 for FY 2011) and Accounts Payable invoices paid (approximately \$593,000 for FY 2011) to identify unusual transactions, vendors, or FAU coding.

In addition, we judgmentally selected and reviewed 15 Pro-Card transactions (\$173,000 or 61% of total population) and 11 Accounts Payable invoices paid (\$184,000 or 31% of total population) between July 1, 2010 and June 30, 2011 for proper documentation, authorization, and FAU coding.

Contracts and Grants

SoBA has minimal Contract & Grant activity. As such, we limited our review to an evaluation of administrative and accounting procedures and internal controls based on management responses to the internal control questionnaire and limited substantive tests of transactions.

Access Control

We reviewed the Enterprise Access Control System (EACS) and Payroll access in SoBA to identify any improper or unauthorized access.

Executive MBA Profitability Review

We reviewed SoBA's profitability analysis and projections (FY 2009 – projected FY 2013) for accuracy and reasonableness, and funding sources for compliance with applicable campus Policies & Procedures.

Faculty Conflict of Commitment & Class Reductions

We reviewed for possible faculty Conflict of Commitment. We verified class reductions for a sample selection of five faculty to ensure they were properly authorized and documented.

Cellular Phone Expenses

We performed an analytic review of cellular phone expenses for FY 2009 – FY 2011.

D. INTERNAL CONTROLS AND COMPLIANCE

As part of the review, internal controls were examined within the scope of the audit.

Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the achievement of objectives in the following categories:

- Effectiveness and efficiency of operations
- Reliability of financial reporting
- Compliance with applicable laws and regulations

Substantive audit procedures were performed from September through November 2011. Accordingly, this evaluation of internal controls is based on our knowledge as of that time and should be read with that understanding.

III. OBSERVATIONS, RECOMMENDATIONS, AND MANAGEMENT RESPONSES

A. SoBA Deficit Projections

SoBA projects to incur annual net losses of between \$750,000 to \$1.5 million per year from FY 2012 through FY 2016 (the end of their projection analysis).

COMMENTS

Although SoBA is currently in a minimal surplus position, projections have them incurring deficits starting FY 2012 through the end of their projection period FY 2016. Several factors are placing downward pressure on their budget:

- 1) SoBA was allocated \$451,000 in permanent budget cuts in FY 2012.
- 2) The EVC/Provost has authorized SoBA to hire seven ladder rank faculty, increasing the faculty from 23 to 30 (43 lines are authorized). Although Central funds will be allocated for these positions, SoBA's unfunded cost will be approximately \$720,000.
- 3) SoBA is planning to launch a new self-supporting program (Masters of Professional Accountancy) in Fall 2012 and two more self-supporting programs in the coming years. The plan is to initially launch these programs with existing faculty, staff, and classes; however, there will be some pressure on the budget in the early years of these programs.
- 4) SoBA is also entering into a reaccreditation period with the Association to Advance Collegiate Schools of Business (AACSB), which has put pressure on them to fill faculty lines and improve student services, which comes at a cost.

RECOMMENDATIONS

Management should address the discrepancy between the established plan and available resources by continuing to prioritize its programs and optimally allocate its present/future resources to meet its objectives and the University's mission.

SoBA should continue to pursue possible additional permanent funding and alternative funding for the self-supporting programs during their initial start-up period, determine where additional cuts can be made while not jeopardizing reaccreditation, and obtain documented support for any verbal commitments from the EVC/Provost.

MANAGEMENT RESPONSE

The SoBA Interim Dean and Executive Assistant Dean/CFAO are working with the EVC/Provost, Vice Chancellor for Finance & Business Operations and Associate Vice Chancellor for Resource Management to identify the resources necessary to maintain an accredited School of Business at UCR. Commitment Date: April 1, 2012.

- B. **Supplies & Equipment Inventories – Segregation of Duties**
SoBA's Supplies & Equipment inventories functions are assigned in a manner that does not provide appropriate segregation of duties.

COMMENTS

Supplies Inventory - One individual performs the following conflicting duties:

- Orders
- Receives
- Compares the supplies inventory listing to the inventory on hand

Equipment Inventory – One individual performs the following conflicting duties:

- Physical count of equipment inventory
- Maintains the equipment inventory records

Sound internal controls require that accounting responsibilities be assigned to personnel in such a manner that no one individual controls all aspects or the aspects listed above of processing a transaction.

RECOMMENDATIONS

Supplies Inventory – The staff that orders supplies inventory should not be the same employee that receives and compares the supplies inventory listing to the inventory on hand.

Equipment Inventory – The staff that performs the physical count of equipment inventory should not be the same employee that maintains the equipment inventory records.

MANAGEMENT RESPONSE

We agree with the auditor's recommendations and have reassigned duties to meet the segregation of duties standards for Supply and Equipment Inventory. Commitment Date: January 1, 2012.

C. Travel Expenditures

We noted three travel expense vouchers (TEVs) lacking sufficient explanation/documentation, one TEV incurring excessive costs for late booking, and one TEV mileage reimbursement covering six months.

COMMENTS

Some travel-related concerns are as follows:

- a. **Flight and ground transportation cost comparison** - Supporting documentation for a TEV did not include explanation or cost comparison between the reimbursed travel cost of \$2,000 for a multi-leg flight (LAX to Amsterdam on June 5, 2011, and Copenhagen to LAX on June 15, 2011) for \$1,422; and car rental, gasoline, and parking expenses of \$578 versus a direct round trip flight from LAX to the destination conference in Hamburg, Germany (June 9-11, 2011) and the corresponding travel cost from the airport to the hotel and back.
- b. **Transportation cost comparison** - Supporting documentation for a TEV did not include an explanation or cost comparison between the reimbursed rental car expense of \$1,296 versus a flight from Brussels, Belgium to Bellagio, Italy.
- c. **Flight Upgrade** – There is inadequate explanation or documentation to enable us to determine in one TEV whether a traveler used personal funds or miles to upgrade his flight or if the University paid for such upgrade.
- d. **Extra costs for late reservation** - One traveler was reimbursed an exceptional hotel charge of \$319 per night for three nights because all conference hotel rooms were full by the time registration was completed. The traveler was also reimbursed \$50 for a late conference registration penalty.
- e. **Timeliness of travel claims** - One traveler submitted a TEV covering six months of mileage reimbursement.

RECOMMENDATIONS

We recommend that SoBA management review travel Policies and Procedures with faculty to enhance documentation of cost comparisons for travel reimbursements, avoid additional costs for late reservations, and ensure timely submission of expense reimbursements.

MANAGEMENT RESPONSE

We agree with the auditor's recommendations. We will review our internal Policies and Procedures to include documentation of cost comparisons for travel reimbursements, avoid additional costs for late reservations, and ensure timely submission of expense reimbursements.

An e-mail will be sent to SoBA faculty and staff to share the audit comments and emphasize the importance of following UCR travel policies and procedures and providing adequate documentation in a timely manner.

Commitment Date: January 15, 2012.