



UCSB Audit and Advisory Services

Internal Audit Report

**University Inventories
Phase 2 Final Report**

June 23, 2014

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Report No. 08-14-0002 – Phase 2

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AUDIT AND ADVISORY SERVICES
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June 23, 2014

To: Jim Corkill, Controller and Director
Business and Financial Services

Re: **University Inventories - Phase 2 Final Report
Audit Report No. 08-14-0002 (Phase 2)**

As part of the 2013-14 annual audit services plan, Audit and Advisory Services has completed Phase 2 of our audit of University Inventories. Enclosed is the audit report detailing the results of our review.

The primary purpose of this audit was to ensure that University of California, Santa Barbara campus inventories (and non-inventoried stock) such as supplies and equipment are properly controlled and safeguarded from loss, and to assess whether processes and procedures implemented by campus departments are in compliance with University and sponsor regulations and policies.

One of the objectives of this project was a campus-wide inventory risk assessment to identify the types, locations, and value of campus inventories (and non-inventoried stock). Following that work, we performed the detailed audit fieldwork in two phases, covering four areas of focus in each phase. The audit objectives for each area of focus included an assessment of the effectiveness of processes, policies and procedures, and controls in place for receiving, issuing, safeguarding, and accounting for inventories of various types.

Our Phase I work included the campus-wide inventory risk assessment, and detailed audit fieldwork in Facilities Management, Central Stores, the Police Department, and the Department of Music. Areas of focus for Phase 2, addressed in this report, included:

- Housing and Residential Services
- Transportation and Parking Services
- Chemistry and Biochemistry
- Intercollegiate Athletics

Our work identified opportunities for potential improvements in central department and campus-wide processes that may help campus departments safeguard and account for items that are valued below dollar thresholds for tracking as property or inventorial supplies, but that nevertheless represent substantial value and cost campus-wide. Potential measures include establishing more restrictive local policies and procedures, or providing additional campus-wide guidance, for certain types of property, including theft sensitive items such as computers and tools. Our work in both phases of this audit also identified opportunities for improvement in department practices for

ensuring that certain supplies, materials, substances, and non-inventorial equipment are properly controlled and safeguarded from loss.

Detailed observations and management corrective actions are included in the following sections of the report. The management corrective actions provided indicate that each audit observation was given thoughtful consideration and that positive measures have been taken or planned to implement the management corrective actions. The cooperation and assistance provided during the review by personnel in Business and Financial Services, Housing and Residential Services, Transportation and Parking Services, the Department of Chemistry and Biochemistry, and Intercollegiate Athletics was greatly appreciated. If you have any questions, please feel free to contact me.

Respectfully submitted,



Robert Tarsia
Director
Audit and Advisory Services

Enclosure

cc: Chancellor Henry Yang
Senior Associate Vice Chancellor Marc Fisher
UCSB Audit Committee
Senior Vice President and Chief Compliance and Audit Officer Sheryl Vacca

Administrative Services

Acting Associate Vice Chancellor Pam Lombardo
Willie Brown, Executive Director, Housing & Residential Services
Martin Shumaker, CFO, Housing & Residential Services
Robert Silsbee, Interim Director, Transportation and Parking Services
John Behlman, Fleet Manager, Transportation and Parking Services
Leslie Griffin, Associate Director, Business & Financial Services
Jacob Godfrey, Associate Director and Materiel Manager, Business & Financial Services
Vaughn Boyle, Equipment Manager, Business & Financial Services

Department of Chemistry and Biochemistry

Katie Wright, Management Services Officer
Kathy Allain, Finance Manager
Cabe Fletcher, Research Storeroom Manager

Intercollegiate Athletics

Mark Massari, Director of Intercollegiate Athletics
Carlos Garcia, Coordinator of Team Services
Lauren Carter, Director of Ticket Operations

PURPOSE

The primary purpose of this audit was to ensure that University of California, Santa Barbara (UCSB) campus inventories (and non-inventoried stock) such as supplies and equipment are properly controlled and safeguarded from loss, and to assess whether processes and procedures implemented by campus departments are in compliance with University and sponsor regulations and policies. This audit, which was performed in two phases, is part of UCSB's 2013-14 annual audit services plan.

SCOPE, OBJECTIVES AND METHODOLOGY

The scope of this project included campus inventories of equipment, supplies, materials, and substances, regardless of whether the amounts involved meet applicable dollar thresholds that would require tracking the items as property or accounting for the items as inventorial supplies.

We narrowed the scope of our detailed fieldwork based on risk. One of the objectives of this project was a campus-wide inventory risk assessment to identify the types, locations, and value of campus inventories (and non-inventoried stock). After completing that phase of the work, we performed the detailed audit fieldwork in two phases, covering four areas of focus in each phase. The audit objectives for each area of focus included an assessment of the effectiveness of processes, policies and procedures, and controls in place for receiving, issuing, safeguarding, and accounting for inventories of various types.

Data Gathering and Risk Assessment

We performed extensive background and data gathering work to inform the risk assessment phase of this project, including:

- An assessment of policies and procedures that included:
 - Reviewing and evaluating federal regulations and University of California (UC) and UCSB policies and procedures relevant to the audit, including those that address what goods must be accounted for as inventory; what goods should be tracked even if below the inventory threshold; special requirements for different categories and types of equipment, supplies, and other inventory; and other potentially relevant areas.
 - Identifying UCSB *departmental* policies and procedures that are possible campus best practices.
 - Internet research to identify common policies and procedures other institutions have in the functional areas in the scope of the audit.
- Review of other audits and reviews relevant to this audit, including work by UCSB Audit and Advisory Services, other UC campuses, and other universities and institutions.
- Interviews, brainstorming sessions, and a survey of Academic Business Officer Group (ABOG) members to solicit concerns and more fully develop the risk areas that should be considered for coverage.

- Walkthroughs of select campus inventory locations to gain an understanding of campus purchasing, receiving, stocking, distribution, and safeguarding processes.

Based on our background and data gathering work, we prepared an extensive preliminary list of inventory risk areas that included:

- Campus-wide or central inventories of specific equipment, supplies, materials, substances, etc.
- Specific departments.
- Specific storerooms and storage locations.
- Other auditable inventory areas.

To complete an effective risk assessment, we found it useful to categorize campus inventories to take into consideration:

- *Inventorial vs. Non-Inventorial Equipment* – As discussed later in the Background section of this report, University policies establish inventory and other requirements for property defined as University Inventorial Equipment, Government Inventorial Equipment, Other Government Property¹, and Other Inventorial Items. The applicability of the specified requirements for the different categories of inventory, and the risks of non-compliance with these requirements, were considered particularly relevant in our assessment of risk.
- *Inventorial vs. Non-Inventorial Supplies* – University policies also establish a general threshold that specifies that supplies inventories exist when the combined inventory value of new and unissued material in a department exceeds \$50,000 at one or more locations on a campus, or exceeds \$50,000 at an off-site campus location.
- *Special/High Compliance Inventories* - Inventory requiring special handling and/or that are subject to rigorous compliance requirements, such as firearms, controlled substances, precious metals, cadavers, and vehicles. We used this “catch-all” category for risk assessment and audit planning purposes to identify higher-risk inventories, departments, programs, or other auditable areas, regardless of dollar value.

Other factors considered in completing the risk assessment included:

- Inventory levels and dollar value.
- Equipment, supplies, materials, substances, etc. considered at higher risk for loss or theft.
- Highly specialized inventory.
- Inventory types and/or organizational units for which there has been little or no prior campus audit coverage.

Some of the risk areas we identified or documented, such as controlled substances, were excluded from the potential scope of our detailed fieldwork because, in our judgment, they should be considered for separate, future audit coverage due to the specialized nature of applicable compliance requirements.

¹ *Government Inventorial Equipment* is defined as equipment to which the Government holds title but which is held in custody by the University, which is non-expendable, tangible, personal property acquired for \$5,000 or more, which is freestanding, complete in itself, does not lose its identity or become a component part of another piece of equipment when put into use, and which has a normal life expectancy of more than one year. *Government Property* is defined as all property owned or leased by the Government; it includes both Government-furnished and Contractor-acquired property.

Areas of Focus

As a result of our campus-wide assessment, we selected the following departments for detailed audit work:

Audit Phase 1:

- Facilities Management
- Central Stores
- Police Department
- Department of Music

Audit Phase 2:

- Housing and Residential Services
- Transportation and Parking Services
- Chemistry and Biochemistry
- Intercollegiate Athletics

Our work in these departments included:

- Gaining a fuller understanding of the types of inventories the department is responsible for (e.g. inventorial vs. non-inventorial equipment and supplies, government inventorial equipment, special/high compliance inventories, etc.), and their volume and value.
- Gaining and documenting an understanding of departmental inventory processes, policies and procedures, and use of systems such as the Capital Assets Tracking System (CATS) and Grand Unified System (GUS), a widely used campus shadow system.²
- Performing walkthroughs with knowledgeable personnel of departmental processes for receiving, issuing, safeguarding, and accounting for inventories of various types.
- Detailed testing, as considered necessary, to determine whether departmental processes are in place and operating as intended, including sample inventory counts and testing of purchase, receiving, issuing, disposal, and adjustment transactions.

Table 1 lists the specific types of inventories we selected for review, based on our judgment of risk and the available audit resources. The results of our work for Phase 1 departments are addressed in *University Inventories - Phase I Interim Report*, issued February 7, 2014.

This audit was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*.

² A shadow system is any application or database used for business processes that is not provided and supported centrally.

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Table 1		University Inventories Audit – Areas of Focus	
Department		Inventory Reviewed	
Audit Phase 1*			
Facilities Management		Equipment, tools, parts, materials, and supplies	
Central Stores		Surplus/disposed equipment from other departments	
Police Department		Firearms stored in armory, evidence room, bicycles	
Department of Music		Pianos, other musical instruments, and production equipment	
Audit Phase 2			
Housing and Residential Services		Dining – Food, appliances, and equipment Lodging – Furniture, appliances, supplies similar to Facilities Management	
Transportation and Parking Services		Vehicles, gasoline, equipment (e.g., smog testers), parts	
Chemistry and Biochemistry		General lab supplies, chemicals, compressed gas cylinders	
Intercollegiate Athletics		Inventorial Equipment and Non Inventorial Equipment (Laptops and video cameras distributed to ICA personnel) Ticket Office – Merchandise for resale Team Services – Team uniforms, equipment	

Source: Auditor Analysis

* Work performed and issues identified for Phase 1 departments are addressed in *University Inventories - Phase I Interim Report*, issued February 7, 2014.

BACKGROUND

Campus operations include a wide variety of inventorial and non-inventorial equipment, supplies, materials, substances and other items located at, and utilized by, a wide range of facilities, including offices, labs, garages, machine shops, and other facilities. The scope and decentralization of UCSB's operations increase the likelihood that University resources will be used for non-UC business, otherwise misused, or stolen. We included this project in UCSB's 2013-14 annual audit services plan due to these factors.

Regulations and Policies

Table 2 outlines the principal regulations, policies, and procedures we considered most relevant to the scope of this audit. These include:

- OMB Circular A-110, *Uniform Administrative Requirements for Grants and Other Agreements with Institutions of Higher Education, Hospitals and Other Non-Profit Organizations*, sets forth uniform standards governing management and disposition of property furnished by the Federal Government whose cost was charged to a project supported by a Federal award. Among other requirements, A-110 requires physical inventory of equipment at least once every two years, and requires the institution to maintain a control system to ensure adequate safeguards to prevent loss, damage, or theft.
- OMB Circular A-21, *Cost Principles for Educational Institutions*, establishes principles for determining costs applicable to grants, contracts, and other agreements with educational institutions. A-21 includes various provisions relevant to the scope of this audit, especially provisions related to equipment and supplies. Among other requirements, A-21 specifies that purchased materials and supplies are to be charged at their actual prices, and that withdrawals from general stores or stockrooms should be charged at their actual net cost. Only materials and supplies actually used for the performance of a sponsored agreement may be charged as direct costs.
- BFB BUS-29, *Management and Control of University Equipment*, establishes inventory and other requirements for property defined as University Inventorial Equipment, Government Inventorial Equipment, Other Government Property, and Other Inventorial Items. Although there is a general cost threshold of \$5,000 for equipment to be inventorial, the actual requirements depend on the property category and specific requirements to which the property is subject. For example, the Other Inventorial Items category includes firearms, as well as items acquired under extramural awards that set a dollar limit of less than \$5,000 for inventorial items. BFB BUS-29 also specifies that each University location may establish more restrictive local policies and procedures, for example, for Other Inventorial Items or items that are theft sensitive.
- BFB-BUS-54, *Operating Guidelines for University Supply Inventories*, establishes a general threshold for supply inventories that specifies that supplies inventories exist when the combined inventory value of new and unissued material in a department exceeds \$50,000 at one or more locations on a campus, or exceeds \$50,000 at an off-site campus location.
- BFB-BUS-38, *Disposition of Excess Property and Transfer of University Owned Property*, addresses the disposition of all University-owned personal property (vs. real property) that has been determined to have no continuing value to the University. It includes requirements to ensure proper protection, accounting for, and disposition of University-owned excess property, including specifying acceptable methods of disposition and restrictions on the disposition and use of property. BFB BUS-38 also specifies that each University location may establish more restrictive local policies and procedures

Phase 2 Departments

Housing and Residential Services - Housing & Residential Services is a campus auxiliary department reporting through the Division of Administrative Services. The department provides housing, hospitality, and related residential life services for UCSB's undergraduate and graduate student population.

Transportation and Parking Services - Transportation and Parking Services is a self-supporting auxiliary enterprise that operates campus parking facilities, manages the campus fleet of vehicles, and operates the Transportation Alternatives Program for the campus community.

Chemistry and Biochemistry - Chemistry and Biochemistry is a department within the College of Letters & Science focused on teaching and research in the areas of Biochemistry, Inorganic/Analytical Chemistry, Materials Chemistry, Organic Chemistry, and Physical/Theoretical Chemistry. In support of these activities, the department operates NMR spectrometer, X-ray crystallographic, and materials characterization facilities, and maintains a machine shop, glass shop, and two stockrooms.

Intercollegiate Athletics - Intercollegiate Athletics operates UCSB's NCAA Division I athletics program, offering ten sports for men (baseball, basketball, cross-country, golf, soccer, swimming, tennis, track and field, volleyball, and water polo) and nine for women (basketball, cross-country, soccer, softball, swimming, tennis, track and field, volleyball, and water polo).

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Table 2 Principal Regulations, Policies, and Procedures Applicable to Inventories	
Federal	
OMB Circular A-110 <i>2 CFR, Part 215</i>	Uniform Administrative Requirements for Grants and Other Agreements with Institutions of Higher Education, Hospitals and Other Non-Profit Organizations
OMB Circular A-21, <i>2 CFR, Part 220</i>	Cost Principles for Educational Institutions
OMB Circular A-133	Audits of States, Local Governments and Non-Profit Organizations
University of California	
BFB BUS-29	Management and Control of University Equipment
BFB-BUS-38	Disposition of Excess Property and Transfer of University Owned Property
BFB BUS-43	Materiel Management
BFB BUS-54	Operating Guidelines for University Supply Inventory
UCSB	
Purchasing/Equipment Management <i>Procedure Issued October 2003</i>	Reporting the Loss or Theft of Inventorial Equipment
Purchasing/Equipment Management <i>Website Content</i>	Physical Inventories
Accounting Manual <i>P-415-2</i>	Plant Accounting: Costing and Reconciling Inventorial Equipment Acquisitions

Source: Auditor Analysis

SUMMARY OPINION

Our work identified opportunities for potential improvements in central department and campus-wide processes that may help campus departments safeguard and account for items that are valued below dollar thresholds for tracking as property or inventorial supplies, but that nevertheless represent substantial value and cost campus-wide. Potential measures include establishing more restrictive local policies and procedures, or providing additional campus-wide guidance, for certain types of property, including theft sensitive items such as computers and tools.

Our work in both phases of this audit also identified opportunities for improvement in department practices for ensuring that certain supplies, materials, substances, and non-inventorial equipment are properly controlled and safeguarded from loss.

DETAILED OBSERVATIONS AND MANAGEMENT CORRECTIVE ACTIONS

A. Potential Improvements in Central Department and Campus-wide Processes

We have identified two areas for potential improvements in central department and campus-wide processes.

1. Theft-sensitive Equipment Under \$5,000

The results of this audit, as well as the results of prior work by Audit and Advisory Services, suggest a need for better campus guidance for controlling and safeguarding equipment and other property that is not inventorial under existing policies. As outlined in the Background section of this report, BFB BUS-29, *Management and Control of University Equipment*, establishes a general cost threshold of \$5,000 for equipment to be inventorial, along with some additional requirements that depend on the property and the specific requirements to which the property is subject. BFB BUS-29 also specifies that each University location may establish more restrictive local policies and procedures.

Based on our work on this and prior projects, we believe it would be prudent for Business and Financial Services to establish more restrictive local policies and procedures, or at least provide additional campus-wide guidance, for certain types of property that cost less than the general cost threshold of \$5,000 for equipment to be inventorial – in particular, theft sensitive items such as computers and tools.

2. Tracking and Disposal of Equipment Under \$5,000

Central Stores accepts for disposal or sale excess furniture, computer equipment and electronics, and other property, with the majority of the items valued under the \$5,000 threshold for inventory recording purposes. There are no campus-wide requirements in most cases for documenting the release to Central Stores, and the subsequent disposal of, property under the \$5,000 threshold. Although current practices are consistent with existing policies, it is our opinion that the practices lessen accountability for this property and further increase the likelihood of theft, especially for theft sensitive items such as computers and tools. Based on our work on this and prior projects, we believe it would be prudent for Business and Financial Services to establish more rigorous practices in this area.

Management Corrective Actions

Business and Financial Services will address these issues by communicating specific guidance for campus departments for tracking and safeguarding property valued below the \$5,000 threshold, including theft-sensitive items such as computers and tools. This guidance will include recommendations about department tracking and record-keeping requirements for disposal of these items. This guidance will be distributed to the campus via an email memorandum and supported by enhanced content on the BFS website.

Business and Financial Services will also reach out to the Business and Financial Bulletin Property (BFB 29 & 38) policy owner to request that a systemwide team be convened to explore expanding the scope of those policies to include additional guidance on non-inventorial assets.

Audit and Advisory Services will follow up on the status of this issue by December 31, 2014.

B. Improve Controls with Perpetual Inventory Records for Housing and Residential Services

Housing and Residential Services dining and lodging operations include substantial investments in furniture and equipment, much of which falls below the general cost threshold of \$5,000 for items to be inventorial. Some of these items, such as refrigerators, microwave ovens, and some furniture items, may be considered theft sensitive. The department does not currently have a perpetual inventory system to track these items, nor in most cases does it maintain detailed inventory lists that could be used for comparison with on-hand quantities to detect missing items.

Housing & Residential Services should evaluate the costs and benefits of implementing a perpetual inventory system to track furniture and equipment, and implement such a system if determined to be cost-beneficial. Regardless of the results of this analysis, we recommend maintaining detailed inventory lists for theft-sensitive items, and periodic (at least semiannual) comparison of the lists with on-hand quantities.

Management Corrective Actions

Housing and Residential Services will:

- Evaluate the costs and benefits of implementing a perpetual inventory system to track furniture and equipment, and implement such a system if determined to be cost-beneficial.
- Establish and maintain detailed inventory lists for theft-sensitive items, and document and follow a procedure requiring periodic (at least semiannual) comparison with on-hand quantities.

Audit and Advisory Services will follow up on the status of this issue by December 31, 2014.

C. Transportation and Parking Services Should Validate Campus Vehicle Inventory

Transportation and Parking Services is responsible for directly or indirectly managing all UCSB vehicles registered with the California Department of Motor Vehicles (DMV) in the name of The Regents of the University of California. Some of these vehicles are under the custody of Transportation and Parking Services, and some are under the custody of other UCSB departments.

Transportation and Parking Services performs periodic reconciliations between the department's vehicle inventory records and the campus Capital Assets Tracking System (CATS). However, the decentralized nature of campus operations, and the variety of funding sources used to purchase vehicles, make it possible for departments to purchase and register vehicles that are not reflected in campus records, and which do not meet campus insurance and other requirements. This could expose the campus to risk

We recommend that Transportation and Parking Services consult with the California DMV to determine the availability of reporting that would identify all vehicles registered to campus entities or with campus addresses. On at least an annual basis, Transportation and Parking Services should obtain DMV reports, reconcile them with campus inventory records, and follow up on any discrepancies.

Management Corrective Actions

Transportation and Parking Services concurs with this recommendation, and will:

- Consult with the California DMV, as well as the UC Police Department, to determine the availability of reporting that would identify all vehicles registered to campus entities or with campus addresses.
- On at least an annual basis, obtain DMV reports, reconcile them with campus inventory records, and follow up on any discrepancies.

We will complete the first reconciliation after we are able to obtain the necessary reporting.

Audit and Advisory Services will follow up on the status of this issue by August 31, 2014.

D. Enhanced Processes Implemented by the Department of Chemistry and Biochemistry

We reviewed reports from the perpetual inventory system used for the department's storeroom and performed random counts of selected items, and noted the following:

- Physical counts for three of five inventory items did not agree with the quantities on hand reflected in the system.
- The system currently allows negative inventory balances. These negative balances are not correct, and in the cases observed were caused by student employees entering quantities incorrectly.

During the course of our audit, we recommended that the department conduct periodic cycle counts and perform timely follow-up and correction of inventories with negative balances. The department has taken corrective actions to address the audit findings by revising its processes and the written procedures that outline them.