Prepared by:
Julie Chung
Senior Auditor

Reviewed by:
Mike Bathke
Audit Manager

Reviewed by:
Bent Nielsen
Director
May 29, 2012

ANDREW J. POLICANO
DEAN
PAUL MERAGE SCHOOL OF BUSINESS

RE: Paul Merage School of Business
    Report No. 2012-108

Internal Audit Services has completed the review of the Paul Merage School of Business and the final report is attached.

We extend our gratitude and appreciation to all personnel with whom we had contact while conducting our review. If you have any questions or require additional assistance, please do not hesitate to contact me.

Bent Nielsen
Director
UC Irvine Internal Audit Services

Attachment

C: Audit Committee
    James Pavelko, Assistant Dean for Finance and Administration
    James McKenzie, Director of Finance
I. **EXECUTIVE SUMMARY**

In accordance with the fiscal year 2011-12 audit plan, Internal Audit Services (IAS) reviewed the adequacy of internal controls, policy compliance, and information technology (IT) operations for the Paul Merage School of Business within the University of California, Irvine (UCI). Business risks and control concerns were identified. Specifically, the following issues were noted.

**Conflict of Commitment and Leave of Absence/Travel Authorization** – Travel, including those associated with outside professional activities, were not properly authorized and reviewed. IAS also noted that travel reimbursements were not submitted in a timely manner. These observations are discussed in section V.1.

**PACoR Transactions** – The transactions were not authorized prior to purchase and proper supporting documentation was not maintained on file. In addition, the business purpose for the purchase was not documented. These observations are discussed in section V.2.

**Ledger Review/Reconciliation** – The ledgers were not properly reviewed and reconciled per policy. This observation is discussed in section V.3.

**Traveler/Host Certification** – Travelers did not comply with the travel policy regarding the "Traveler Certification signature". This observation is discussed in section V.4.

**Disaster Recovery Plan** – The disaster recovery plan should be further developed and enhanced to minimize risks. This observation is discussed in section V.5.

II. **BACKGROUND**

The Graduate School of Management at UC Irvine was founded in 1965. The school was renamed the Paul Merage School of Business (School of Business) in 2005, and in 2008 the undergraduate business major was introduced. Currently, the School of Business is home to seven centers, eight academic areas, and offers four MBA programs in addition to the doctorate and undergraduate business degree programs, which serve 2,000 students annually.

While the School of Business is relatively young, it has quickly gained in its ranking in the U.S. News & World Report, #40 in the U.S. for the Full-Time MBA Program and #17 among U.S. public universities in 2011.

The School of Business employs over 380 faculty, staff, and students and has annual operating budget over $35 million.
III. PURPOSE, SCOPE AND OBJECTIVES

The purpose of the audit was to review internal controls, policy compliance, and IT operations from January 2010 to present. Based on the assessed risks, the following objectives were established:

1. Verify whether the required general, confidential, payroll, and medical documents are properly maintained and filed in personnel records;

2. Determine whether the following aspects of employee time reporting: overtime approval, payroll ledger reconciliations, and sick and vacation balance tracking comply with University policy;

3. Review non-payroll expenditures for proper approval and supporting documentation in compliance with University policy;

4. Evaluate whether there are adequate controls over budgeting and accounting;

5. Determine whether the annual conflict of commitment disclosure report and corresponding forms were completed properly and submitted in a timely manner; and

6. Review selected IT operations.

IV. CONCLUSION

In general, internal controls and processes reviewed appear to be functioning as intended. However, business risks and control concerns were identified in non-payroll expenditures, conflict of commitment/compensated outside professional activities, ledger review/reconciliation, and disaster recovery planning.

Observation details and recommendations were discussed with management, who formulated action plans to address the issues. These details are presented below.

V. OBSERVATIONS AND MANAGEMENT ACTION PLANS

1. Conflict of Commitment and Leave of Absence/Travel Authorization

   Background

   Official University travel must be properly authorized, timely reported, and reimbursed in accordance with Business and Finance Bulletin G-28, Policy and
Regulations Governing Travel (G-28). Authorization is to be obtained prior to undertaking University travel.

**Observation**

An adequate mechanism is not in place to properly authorize and monitor academic personnel’s travel, including those activities likely to raise a conflict of commitment and/or require a leave of absence form.

IAS reviewed a sample of academic personnel PayQuest travel reimbursements and related leave of absence forms (UCI-AP-76) and reports of compensated outside professional activities (UCI-AP-3/APM 025), and noted that none of the travel reimbursements reviewed had been pre-authorized (no AP-76 leave of absence form or any other type of travel authorization form). Further review revealed that some of the travels related to compensated outside professional activities had not been properly pre-approved and/or reported.

In addition, IAS noted that none of the travel reimbursements reviewed had been submitted within 21 days of the end of trip as required by policy.

Proper authorization and timely submission of travel expenses reduces the risk of inappropriate/unauthorized/inaccurate expenses.

**Action Taken**

IAS discussed the conflict of commitment/compensated outside professional activities issues with the Vice Provost for Academic Personnel and the Assistant Vice Chancellor of Academic Personnel. Academic Personnel will work with the School of Business Dean and Senior Associate Dean to address the issues noted.

**Management Action Plan**

The School of Business Finance office (Finance) will notify all employees via email regarding the 21-day requirement for submitting travel reimbursements. This information will also be posted on our financial services website, as well as added to the faculty/lecturer handbook. The School of Business Finance Director will also meet with his staff to ensure that they include this point in their document review, and require exceptional approval if this policy is not followed.

Finance will update the internal travel form (currently used as a post-travel document) to act as a pre-authorization document, to be completed, signed, and dated before trips of less than seven days. All employees will be notified via email, and the information and new form will be posted to the financial services website. The Finance Director will also meet with his staff to ensure that they
include this point in their document review, and require exceptional approval if this policy is not followed.

Finance will work with the School of Business Academic Personnel office to have faculty complete leave of absence forms when required, and to track conference/professional business days. In addition, Finance will add the leave of absence form (AP-76) to the financial services website, and all faculty and faculty assistants will be notified via email. The Finance Director will also meet with his staff to ensure that they include this point in their document review, and require exceptional approval if this policy is not followed.

2. **PALCard Transactions**

**Background**

The UCI purchasing card (PALCard) is used by faculty and staff who have buying responsibilities to purchase equipment, supplies and services. UCI PALCard policies require supporting documentation for each transaction. UC purchasing policies require purchases to be pre-authorized either through a purchase requisition or some other form of documentation, such as an email. In addition, a reviewer must review the PALCard supporting documentation and account/fund for appropriateness in a timely manner and attach appropriate reviewer documentation.

**Observation**

IAS analyzed PALCard transactions from January 1, 2011 through December 31, 2011 and selected a sample for further review, and noted the following:

- For all transactions reviewed, an authorization was not obtained prior to purchase;
- For the majority of transactions reviewed, a packing slip was not maintained on file for review.

In addition, for the majority of the transactions reviewed, the business purpose for the purchase was not documented. As a best business practice, the internal requisition should state the actual business purpose of the expense. This allows the approver the ability to question a purchase before approving funds to be spent. This would also aid the mandatory reviewer in approving the purchase for upload to the general ledger, especially since the reviewer is not in the same unit as the buyer.
Internal controls, such as obtaining authorized requisitions prior to purchase and proper documentation, need improvement to reduce the risk of error, inappropriate, and unauthorized use of University funds.

Management Action Plan

Finance will work with the School of Business IT office to implement an electronic pre-authorization document and/or email. In addition, Finance will inform employees via email to include packing slips as well as the business purpose of the expense on the PALCard form. The Finance Director will also meet with his staff to ensure that they include this point in their document review, and require exceptional approval if this policy is not followed.

3. Ledger Review/Reconciliation

Background

University policy states that each manager, who is directly responsible for the financial affairs of a school, department/unit, or office, is required to monitor and verify transactions in order to reconcile balances monthly to the general ledger. This procedural requirement ensures the appropriateness and accuracy of all financial transactions applied to the ledger. In addition, the unit has the obligation of maintaining signed documentation of this review to ensure that they adhere to internal control procedures.

Observation

After discussions with management and reviews of the current reconciliation procedures, it was determined that the ledgers were not properly reviewed and reconciled.

Performing timely reconciliations are integral to ensure that financial information is complete, accurate, and valid. Failure to perform reconciliations may result in undetected errors or unauthorized use of University funds.

Management Action Plan

Finance will change reconciliation procedures so that when reviewing the scanned supporting documentation, the file will be opened and the critical information is matched to the ledger download. In addition, Finance will start a reconciliation log complete with dates and signatures of the reviewers.
4. **Lack of Traveler/Host Signature on PayQuest Cover Sheet**

**Background**

The traveler must sign the travel expense voucher certifying that the amounts claimed are a true statement of the expenses incurred and that the original of all required receipts has been submitted. Internal departmental expense claim forms are not an acceptable alternative for obtaining the traveler’s signature on the travel expense voucher (or electronic equivalent), unless approved as an exception to this policy.

**Observation**

The majority of travel reimbursements reviewed lacked the traveler’s certification on the PayQuest cover sheet. The non-compliant PayQuest cover sheets contained “see attached” notations on the traveler certification signature line, which then referred to/relied upon the signature noted on a previous version or the internal request for reimbursement as the traveler’s certification.

Allowing preparers to use “see attached” notations on the traveler certification line weakens the control structure and reduces the ability to detect inaccuracies.

**Management Action Plan**

All employees will be notified via email regarding signing the PayQuest cover sheet. The information will be posted to the financial services website, and the Finance Director will also meet with his staff to ensure that they include this point in their document review, and require exceptional approval if this policy is not followed.

5. **Disaster Recovery Plan**

**Background**

Appropriate measures should be in place to enable IT to respond to incidents and disruptions in order to continue operation of critical business processes and required IT services and maintain availability of information at a level acceptable to the Department and the University.

**Observation**

Discussions with the School of Business IT management indicate that they have developed a disaster recovery (DR) process that includes performing regular back up of their critical data. However, backup data are currently not sent to offsite
storage but are stored in servers in two different locations within the UCI campus. We suggest that management consider enhancing their DR by considering the following:

- Store offsite all critical backup media, documentation and other IT resources necessary for IT recovery and business continuity plans;
- Ensure that offsite arrangements are periodically assessed, at least annually, for content, environmental protection and security; and
- Ensure compatibility of hardware and software to restore archived data, and periodically test and refresh archived data.

Without a comprehensive DR plan, a disruption affecting the campus may affect the department’s ability to recover their systems, data, and normal operations.

**Management Action Plan**

School of Business IT management agrees with the observation and has explored external services such as the Amazon and Microsoft Windows Azure cloud services but believed the pricing for these external services did not present the best value. They are currently discussing options with OIT, who is in the process of setting up offsite storage at the UC San Diego supercenter, to store their critical data in an offsite location. By December 2012, School of Business IT management plans on purchasing space from OIT for offsite backup needs and should be able to implement the comprehensive DR soon after.