



AUDIT AND ADVISORY SERVICES
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February 24, 2020

To: Chuck Haines, Assistant Chancellor
Finance and Resource Management

Re: **Recharge Activities**
Audit Report No. 08-20-0003

We have completed a limited review of recharge activities as part of the 2019-20 annual audit services plan. The audit was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*. Enclosed is the report detailing the results of our work.

We sincerely appreciate the cooperation and assistance provided by Office of Budget and Planning and Business & Financial Services personnel during the review. If you have any questions, please contact me.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Ashley Andersen".

Ashley Andersen
Director
Audit and Advisory Services

Enclosure

cc: Chancellor Henry Yang
UCSB Audit Committee
Alexander Bustamante, Senior Vice President and Chief Compliance and Audit Officer

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UC SANTA BARBARA

UCSB Audit and Advisory Services

Internal Audit Report

Recharge Activity

February 24, 2020

Performed by:

Antonio Mañas-Melendez, Associate Director

Irene Camargo, Senior Auditor

Karen Quintana, Staff Auditor

Approved by:

Ashley Andersen, Audit Director

Report No. 08-20-0003

EXECUTIVE SUMMARY

OBJECTIVE

The purpose of the audit was to determine if adequate procedures and internal controls have been implemented to ensure that campus recharge practices are in compliance with University policies and procedures. The objective of our audit was to determine whether:

- Campus has an accurate account of income and recharge units and recharge activity postings are accurately reported.
- Income and Recharge Proposals are annually submitted.
- Recharge rates are accurately billed by the department.
- Recharges are adequately tracked for financial reporting.
- Sufficient training is provided to control points.

CONCLUSION

The audit identified a considerable lack of compliance with University recharge policies and procedures, which indicates that this key campus business process is not operating as intended or required. The results of work performed within the scope of the review identified several significant internal control weaknesses and deficiencies in compliance practices and procedures. The more significant of these include:

- Activity in 36 account-funds that were not included in the approved recharge center list.
- Eight out of ten departments tested, which were charging for services, had not submitted a recharge packet to Budget and Planning for approval.
- One department reused an existing recharge account and did not consult Budget and Planning.
- Of the ten recharge journal entries reviewed, six were using object codes for the debit transactions that did not map to recharge object code 3905; two were using recharge object codes when a transfer of expense should have been processed.

Our work further identified opportunities to improve guidance and training to ensure recharge transactions are properly classified and postings are accurately reported in the campus general ledger.

In our opinion, management should allocate the necessary resources to address the lack of compliance with policy and to ensure proper recording of recharge activities on the general ledger as to not misstate revenues or expenses in our financial statements.

OBSERVATIONS, RECOMMENDATIONS, AND RESPONSES

1. RECHARGE FACILITIES

OBSERVATION

Our limited review of recharge activity on campus found a need to enforce compliance with the Income and Recharge Program to guarantee campus recharge facilities are authorized and they operate on a break-even basis.

Inventory

The list of authorized recharge facilities managed by the Office of Budget and Planning does not reflect the real volume of recharge activity posted on campus.

We compared recharge transactions reported on the campus general ledger for departmental services during a two-year period¹ with the list of authorized recharge facilities managed by the Office of Budget and Planning, by comparing account funds². We found recharge activity in 36 account funds were not included on the mentioned list. The Income and Recharge guidelines requires that recharge transactions may be only initiated by those units with approved recharge accounts.

Annual Income and Recharge Proposals

Campus departments do not always consult the Office of Budget and Planning and/or submit income and recharge proposals on an annual basis. Additionally, the Office of Budget and Planning evaluation and approval process of income and recharge packages has suffered delays and some submitted proposals were not officially approved.

We evaluated whether annual income and recharge proposals were submitted by departments with reported recharge activity. We selected a sample of five recharge facilities³ included on the list of authorized recharge facilities managed by the Office of Budget and Planning and found:

- Two departments submitted an income and recharge proposal and did not receive formal approval from Budget and Planning.
 - Budget and Planning temporarily accepted the new rates in one proposal until they would be formally approved by the Income and Recharge Committee.
 - The department did not receive feedback from Budget and Planning in the other proposal.
- One proposal was submitted to the department's control point in 2018 for review and approved by the control point in the absence of an Income and Recharge Committee.

¹ From July 1st, 2017 to June 30th 2019.

² Account-Fund: used to identify how funds are expended and income is collected.

³ Recharge Facilities in the College of Engineering were excluded from this sample, because we performed a review of these facilities last fiscal year.

- One department's most recent approved Income and Recharge Proposal was in 2010.
- One department received a guideline and a cost sharing analysis report established by the Office of Budget and Planning in 2004, but never had a formal recharge proposal approved.

Additionally, we selected a sample of ten recharge facilities outside of the list of authorized recharge facilities managed by the Office of Budget and Planning and consulted how they were established as a recharge facility. We were informed Business and Financial Services (BFS) established recharge accounts several years ago with the exception of one department that reused an existing recharge account to process capital project services. We found:

- Eight of the ten departments had not submitted an annual income and recharge proposal to Budget and Planning.
- One department submitted an income and recharge proposal in 2018 for review and approval and received an interim approval from Office of Budget and Planning to use new proposed rates until the Income and Recharge Committee reconvened.
- One department reused an existing recharge account and did not consult Budget and Planning nor submitted an annual income and recharge proposal.

The Income and Recharge guidelines requires that income and recharge proposals be submitted by April 15th to the Office of Budget and Planning in order to be reviewed and approved for implementation in the next fiscal year.

During our review, we were informed that the Income and Recharge Committee has recently reconvened and is currently meeting on a regular basis to review proposal rates. In addition, the Office of Budget and Planning is in the process of updating the Income and Recharge policy and procedures to provide guidance for the establishment, review, and approval of income and recharge activities. This action would help to enforce compliance with the Income and Recharge guidelines.

Income and Recharge Rates

Departmental recharge billing rates matched the most recent approved income and recharge proposal rates. However, as mentioned in prior section, rates have not been annually updated and some recharge facilities rates may not be covering current operating costs.

We reviewed selected department's detailed line item billing invoices to support journal entry postings for five departments. We found recharge rates were accurately billed by departments for sales and services at the most recent approved income and recharge rate.

2. OTHER ISSUES

OBSERVATION

We found there is a need to improve guidance and training of financial reporting to ensure recharge transactions are adequately posted in the campus General Ledger.

Tracking and Financial Reporting

Recharge facilities are adequately tracking recharges for reporting purposes. However, we found that financial recharge transactions were not always adequately classified in the campus general ledger and postings did not roll up to the correct object code to offset the recharge transactions.

We interviewed five departments and reviewed their recharge activity tracking process. We determined that detail reports are generated using various systems and adequately tracked for recharge billing purposes. However, we found there was an annual recharge journal entry for a payroll cost sharing a MOU transaction that would not be considered recharge.

BFS informed us that they have discontinued including Memorandums of Understanding as a type of recharge, during fiscal year 2019-20. For these type of transactions, BFS works with departments to set up Transfers of Funds (TOF) using the TOF system⁴.

In addition, we evaluated whether ten recharge journal entries⁵ were properly recorded. We found two of the ten transactions were properly classified by selecting the correct object code⁶. We also found:

- Six sampled journal entries were classified with debit object codes that do not roll up to the correct recharge object code. Improper reporting results in a misstatement of recharge activity and an over/understatement of expenditures. Financial reporting of campus recharge activity would require a significant amount of manual review and adjustments to reclassify recharges.
- Two journal entries were classified as recharge transactions for payroll charges instead of using a Transfer of Expense⁷.

In addition, we found inconsistencies between the "Object Code Listing" posted on the BFS website with a revision date of 12/10/18 and the "Object Code Listing" categories within the general ledger Data Warehouse system. The listing posted on the BFS website should be updated when object code mapping changes in PeopleSoft so that the campus can accurately post recharge transactions.

BSF informed us that they are changing local campus object codes used, and/or mapping the rollup into UCOP object codes. The most impactful change was object code 7150

⁴ The more common solution.

⁵ Journal entries: amounts to be debited and credited in the general ledger.

⁶ Object code: Used for the classification of expenditures by object.

⁷ Transfer of Expense: a campus application allowing the transfer of expenses from one chart string to another.

used mostly by Facilities Maintenance. The recharge debit should offset the recharge credit by the same dollar amount.

Training

We found it could be beneficial for department control points to receive additional training and guidance regarding recharge activity.

We interviewed five departments and determined that departments do not have an adequate understanding of the recharge policy requirements. One of the consequences is departments are not always aware of the need of submitting annual income and recharge proposals; therefore, policy and procedures are not being followed.

Training should be performed by the Office of Budget and Planning in collaboration with BFS to control points to ensure that income and recharge proposals are being annually submitted and activities are being properly posted in the general ledger.

BFS informed us that they are working on training material and collaborating with the Office of Budget to bring campus recharge practices into compliance.

RECOMMENDATION

We recommend the Office of Budget and Planning evaluate and improve efficiencies related to recharge activities by:

- Reviewing sales and services recharge unit inventory for accurate tracking and reporting purposes.
- Evaluating whether an annual proposal is necessary for recharge units with no or minimal rate increases/decreases, in order to reduce the volume of annual reviews.
- Reviewing and approving annual income and recharge proposals and timely return signed approvals by the EVC to the department for confirmation of approved rates.
- Review recharge units surplus/deficits annually to ensure rates are covering all applicable operational costs of the recharge unit and that they are maintaining surplus/deficits within a threshold from break-even.
- Providing adequate training in collaboration with General Accounting to control points to ensure recharge activity is properly recorded.

MANAGEMENT RESPONSE

The Office of Budget and Planning has recently appointed an Associate Vice Chancellor of Budget and Planning and is engaged in recruitment activities for an Income and Recharge Analyst. The responsibilities for recharge activities fall under the AVC of Budget and Planning and will be managed on a day-to-day basis by the I&R Analyst.

Under the AVC's oversight, the Analyst will propose and implement updates to the Income & Recharge practices on campus. These practices will include:

- Review and document sales and service recharge unit inventory for accurate tracking and reporting purposes.
- Implement tiered review process to simplify and streamline of proposals with minor or no changes from previous review period, allowing the review committees to focus on larger recharge issues.
- Develop criteria to allow multi-year approvals.
- Review and approve annual Income and Recharge Proposals and timely return signed approvals by the EVC to the department for confirmation of approved rates.
- Implement an annual review of recharge unit fund balances to ensure rates are set at an appropriate level to cover expenses of the recharge operations.
- Collaborate with General Accounting to provide adequate training for control points in order to ensure recharge activity is properly recorded.

Expected completion date: June 30, 2020.

RECOMMENDATION

We recommend Business & Financial Services continue reviewing and evaluating whether recharge transactions:

- Identified in journal entries for sales and services rendered should be treated as a recharge.
- Are accurately posted in the general ledger to the correct object code and adequately roll up to University of California Office of the President account-funds for reporting purposes by performing regular reconciliations of recharge object codes.

MANAGEMENT RESPONSE

Business & Financial Services will continue reviewing and evaluating whether recharge transactions:

- Identified in journal entries for sales and services rendered should be treated as a recharge.
- Are accurately posted in the general ledger to the correct object code and adequately roll up to University of California Office of the President account-funds for reporting purposes by performing regular reconciliations of recharge object codes.

Expected completion date: June 1, 2020.

GENERAL INFORMATION

BACKGROUND

*The Office of Budget and Planning*⁸

The Office of Budget and Planning oversees annual income and recharge proposals for the campus. Recharges are recorded in the campus general ledger as direct costs. In nearly all cases, a recharge program's revenue and expenditures should be budgeted in a single restricted fund number rather than core funds (State General Funds, Opportunity Funds, Contract and Grant Overhead, and Student Fees). The segregation of recharge operations into a single fund greatly assists in monitoring departmental compliance with restrictions on the use of recharge income. It also facilitates the allocation, management, and tracking of program costs, and allows for depreciation of equipment.

The establishment of an income or recharge account is based on meeting the following criteria:

- A specifically identifiable good or service is provided.
- There exists a demand for the particular service by more than one university or non-university user.
- There will be a significant volume of activity, both in dollar amounts and in the number of transactions.
- Service will be provided on a regular and continuing basis.
- Services are unique or specialized (for example, a glass blowing shop, or a machine shop), as opposed to general administration or other institutional support services.
- Funding for the service is not part of the permanent departmental budget.

Recharge transactions may be initiated only by those units with approved recharge accounts. The Office of Budget and Planning cannot forward a request to establish a recharge account until after consultation opportunities have been provided to users, it has been reviewed by the Income and Recharge Committee, and approved by the Executive Vice Chancellor (EVC).

Recharge Unit Responsibilities:

A department that charges for services is responsible for the financial management of the account. This includes:

- Annual review of all rates - All rates must be presented to the Income and Recharge Committee at least once per year for review.
- Updating of current and permanent budgets - Income, recharge, and expenditure

⁸ UCSB Income and Recharge guidelines.

budgets (both current year and permanent) must be updated by the department via a transfer of funds within one month following approval of rates.

- Rate stability - Recharge departments are responsible for providing rate stability to the users of their services.
- Departmental subsidies - The elimination of departmental subsidies, when warranted, should be based on a phased withdrawal of funds.
- Review of services - Service providers must review their “products” at least annually in an effort to eliminate services that are seldom used, have limited benefit to the campus as a whole, and/or are available at less cost through other local providers.
- Reserves - In some cases reserves are allowed for items like depreciation and paid leave liabilities.
- Surplus or deficit condition - Rates must be constructed to recover the full costs of individual programs. Earnings (surplus or deficit) from the previous year must be taken into account in setting new rates.
- Depreciation - Any inventorial equipment assigned to the recharge program —other than equipment that has either been furnished by the federal government or has been designated as a campus cost share to a federal award — shall be depreciated.
- Off-campus rates - It is the University’s policy not to sell goods or services to outside consumers except where such goods or services are unique or where such sales would not constitute inappropriate competition with commercial sources.
- Billing & records - The service provider is responsible for all billing, including the determination of appropriate billing cycles.
- Posting of rates – All approved rates should be posted on the department web site and at the appropriate point of service location.

Budget and Planning Responsibilities:

On an annual basis, rate and recharge proposals are to be prepared for review and approval by the department chair and the control point. Upon control point approval, the proposal is forwarded to the Office of Budget and Planning for review by the Income and Recharge Committee. Based on its review, the committee prepares a recommendation for final approval of the proposal by the EVC. To effectively manage and prioritize the workload of proposal review, the committee employs three methods of approval based on a risk assessment: delegated to the Office of Budget and Planning, consent agenda item, or meeting agenda item.

*Business and Financial Services*⁹

UCSB Business and Financial Services is an integral campus and community partner. Units within Business and Financial Services include Accounts Payable, Billing, Accounts Receivable, Collections, Equipment Management, Extramural Funds, Payroll, Procurement, Travel and Entertainment, and General Accounting.

General Accounting is a unit responsible for general ledger operations, to include review, research, analysis, reconciliations and information processing; fiscal close coordination and control; financial reporting; systems development and maintenance; and Student Loan and Education Abroad Program accounting.

SCOPE

The scope of our work included an inventory of active recharge units and internal controls related to annual submissions of income and recharge proposals, accuracy of billed recharge rates, tracking and reporting of recharge activity, and adequate training to control points.

Specifically, we:

- Reviewed UC and UCSB policies, best practices, and other guidance concerning recharge activity.
- Conducted interviews with campus departments including the Office of Budget and Planning; General Accounting; Housing, Dining, and Auxiliary Enterprises; Facilities Management, Financial Aid Office, and other departments such as Physics and California Nano Systems Institute to obtain a better understanding of the process and internal controls in place and to identify areas of concern.
- Selected a sample of recharge units and determined whether:
 - Departments are annually submitting income and recharge proposals.
 - Rates charged by the department matched the most recent approved income and recharge proposal rates.
 - Tracking and reporting of recharge activity supports billing.
 - Training related to recharges to control points is sufficient.

CRITERIA

Our audit was based upon standards as set forth in the UC and UCSB policies, best practices, and other guidance relevant to the scope of the audit. This audit was conducted in conformance with the *International Standards for the Professional Practice of Internal Auditing*.

This review emphasized, but was not limited to, compliance with:

- UCSB, *Income and Recharge Guidelines*, dated July 2013.

⁹ Business & Financial Services general Accounting website.

- UC Policy, *BFB-A-56: Academic Support Unit Costing and Billing Guidelines*, dated September 2008.
- UC Policy, *BFB-A-59: Costing and Working Capital for Auxiliary and Services Enterprises*, dated October 2008.
- UC Policy, *BFB A-47: Direct Costing Procedures*, dated June 2012.

AUDIT TEAM

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