UNIVERSITY OF CALIFORNIA, DAVIS
AUDIT AND MANAGEMENT ADVISORY SERVICES

Receivable Reconciliations
Audit and Management Advisory Services Project #16-12

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Receivable Reconciliations

MANAGEMENT SUMMARY

This review of internal controls over Accounts Receivables (AR) owed to UC Davis was included in our 2016 Audit Plan. Our review focused on campus units that process and collect their own receivables. It excluded the contracts and grants and student accounting receivables processed through Accounting & Financial Services (A&FS). Staff from A&FS supported our work throughout the project.

The objectives for this review were to evaluate compliance with applicable university policies in the recording, review, and collection of accounts receivables; and the sufficiency of the controls and practices in place to properly collect funds due to the university in a timely manner and to record those accurately in the general ledger.

We conducted interviews with staff in 12 selected units that represent a cross section of the types of units that process accounts receivable on campus. We interviewed staff from the Veterinary Medical Teaching Hospital, the California Animal Health & Food Safety Laboratory, the Veterinary Genetics Laboratory, the Center for Comparative Medicine, UC Davis Extension, the campus bookstore, and other smaller departments.

We surveyed another 28 AR account managers, such that our review examined units that accounted for 88% of AR balances within our scope at fiscal year end June 30, 2015 (FYE15).

Revenues from external sources for our selected units were $126 million in FY15. Of those dollars, $96 million were processed through the AR systems we examined. At June 30, 2015, the aggregate AR balance for our selected units was approximately $10.3 million.

We observed that most units are generally compliant with policy and that controls are adequate to ensure timely collection of receivables overall. This is evidenced by the fact that the aggregate AR balances at FYE15 were approximately 11% of revenues processed through these AR systems in FY15. We found—as expected—that our campus is rich with diversity of high quality activity, fulfilling our mission to teach, to learn, and to serve the wider community in a myriad of ways. We also learned that the diversity of products and services provided by the units we reviewed creates a challenge for the campus. Each unit must find a way to document and preserve the data from their work, create specialized bills for their customers, and record their transactions to the campus general ledger.

We believe the campus will improve the AR function if it invests in effective, efficient billing technology, increases centralized oversight, strengthens the integration between independent departments and central units, and documents associated accounts receivables procedures. Our detailed observations and recommendations are presented below along with corresponding management corrective actions.

We will communicate with the appropriate Deans and Vice Chancellors regarding our recommendations for specific individual units. Additional operational information obtained during this project is included in Appendix A.

OBSERVATIONS, RECOMMENDATIONS, AND MANAGEMENT CORRECTIVE ACTIONS

A. Inadequate billing systems reduce efficiency and delay the timely collection of receivables.

We reviewed AR processes in units that provide:

- veterinary care to small and large animals
- consultations to animal shelters
- radiography & irradiation services
- chemical analysis
- writing workshops
- pollution toxicology studies
- child welfare training to counties
- the development & application of atmospheric particulate matter

These units are providing valuable mission-related services to the university in addition to generating millions of external revenues annually.

We observed inefficiencies due to inadequate information systems in nine of the 12 units we interviewed. That is, extensive manual processes or duplication of efforts or both are required to regularly perform basic AR functions: billing, review of AR aging, recording and reconciliation to the campus general ledger (gl), and documentation of collections efforts.

Five of the 12 units we interviewed use three systems to get from their core business activity to the gl: their business data system, a separate billing software, and then the Kuali Financial System (KFS) which houses the gl. In four interviewed units we found billing software systems that cannot produce effective reports. These four units are all self-supporting units that make the decision independently to invest—or not—in information technology upgrades or repairs. While one is small enough that its systems function reasonably well, the other three suffer from notable deficiencies that require staff to perform inefficient manual processes regularly. Manual processes are not only a waste of valuable staff time, but they increase the risk of error.

Most of the units we surveyed process fewer invoices annually and have simpler businesses than the larger units we interviewed. Twenty-four of 28 of these surveyed units (86%) use the KFS AR module to create invoices and record activity directly. We do not believe the kinds of difficulties we observed in certain larger units are present in the smaller, less complex units. However, based on interviews with staff who use KFS, we know that the limitations of this system can result in duplication of effort and other inefficiencies. Three of the units we interviewed are manually entering invoices in KFS, when those same invoices have already been created in another system. This may be taking place in other departments using KFS as well.

While we cannot accurately quantify the economic impact of inefficiency without further study, we can comment generally by giving a dollar value to two of the processes we observed as follows: We estimated the salary and benefits costs for a staff person spending four hours per month entering duplicate invoices. We estimated the cost of a supervisor spending eight hours per month on a manual reconciliation process. We then multiplied these amounts by the number of units within our scope that are likely to have similar inefficiencies. Our calculations result in an estimated inefficiency cost somewhere in the range of $175-220,000 per year.

While we acknowledge that the complexity inherent to our enterprise creates challenges in billing for, recording, and collecting receivables, we know that corporate entities of excellence meet this challenge every day. An investment in improved information technology would align with the objectives of the UC Davis Financial Sustainability Action Plan (FSAP) as it would support more efficient collection of external revenues.

Recommendations

Invest in effective, efficient billing technology that will serve the campus as a whole.

Management Corrective Actions

A&FS will meet with the larger and mid-sized departments to assess the invoicing and AR needs of the department and discuss potential system solutions to allow for more efficient and accurate processing of Revenue/AR. These meetings will be completed by March 15, 2017.

B. There is wide variation in the level of business expertise among the staff who process revenues and receivables in the independent units. This along with other factors can result in suboptimal functioning in AR processes.

A typical model in the units we examined is subject-matter experts producing the service offered, with staff supporting their effort by performing business functions. Unit size varies from the Veterinary Teaching Hospital (VMTH) with 55,000 visits per year to departments that may have only two invoices annually. Staff expertise in accounting and controls varies widely and generally is not at a specialized professional level, particularly within the smaller units.

We observed that the majority of units function well, with an AR at year end below 10% of annual revenue. They have AR aging distributed across the aging groups as would be expected in a healthy business—the bulk of receivables in the 0-60 days category with diminishing totals as the groups age.

We also observed the following:

- A unit with a $1 million AR balance at FYE15 that was equivalent to 56% of its revenues for the year. Upon investigation it was discovered that it had not consistently pursued collections such that some of the receivables on its books were as old as 2009. Although the scope of our audit excluded recharges, it came to our attention that the unit had not billed an internal customer timely, resulting in an unexpected recharge to the other department of $60,000 at year end. Recharge and external billing are processed through the same system within this unit.

- A unit responsible for billing time-sensitive receivables which had not adequately pursued collections. At the time of our interview, 49% of its $412,000 receivables were older than six months and thus likely to prove uncollectible.

- Three of the 12 units we interviewed are unable to reconcile their AR aging to the balance in the general ledger. Only 39% of our survey respondents indicated that they were able to perform this reconciliation. For some, this is related to problems with the central reports and data which will be addressed in Observation C below. For others, this is a training and/or dedication of resources issue.

- The responses to our survey indicated actual or potential risks due to lack of separation of duties issues in 11 of the 28 units surveyed (39%). Risks related to separation of duties existed in 3 of our 12 interviewed units.

- Several units requested additional detailed guidance and training on the collections process, including training regarding collections documentation.

These examples and observations demonstrate that there is a risk that losses and errors in financial reporting can take place in the current model of operations without central oversight of the function. Even units that are functioning well could experience turnover or other staffing issues that could cause the management of these revenue streams to deteriorate to an unacceptable level without this being noticed centrally.

Recommendations

Increase centralized oversight of and support for AR processing by independent departments.

Management Corrective Actions

1. By July 15, 2016, A&FS will provide KFS AR aging reports to the Deans' and Vice Chancellors' offices. The report will detail out the customer balances by organization and by aging category. A&FS will provide instructions for reviewing and analyzing the report, as well as provide a roadmap of how to obtain more details from the system to analyze the balances. There will also be references to policies and instructions on how to write off balances, if deemed necessary. This process will be completed on an annual basis.
2. By March 15, 2017, A&FS will augment online training resources related to collections and collections documentation.

C. Problems with central reports and processes reduce AR functionality and decrease efficiency. Units using Banner invoicing may not be aware that they must include a review and approval step within their department before posting to the gl.

We observed the following:

- Forty-eight percent of the units we contacted reported that they can agree their Aging report to the general ledger, but audit work did not include reconciling these balances. There are known problems with the KFS AR Aging report (FIS409). Many units state that they either do not know how to do this reconciliation or are unware that it needs to be completed. Other units have department-specific problems that prevent the reconciliation.
- Only 32% of surveyed units reported that they regularly reconcile unapplied balances.[1] Additional survey comments noted that there are problems with the FIS407 Unapplied report, a comment we also heard during our interviews.
- The MyInvoice (Banner) system used by 47 departments on campus has no routing for review and approval of invoices. Departments are responsible for creating a review process within their unit before posting. We found one department that was unaware of this and had been relying upon Student Accounting to provide review. There is risk that other departments are similarly unaware.
- The current system does not allow for central documentation of collections efforts. These records are kept in manual systems—paper files or Excel spreadsheets--or within unit billing systems. This information is lost when accounts are sent to collections through Student Accounting. Meanwhile units lose direct access to information regarding collections efforts made by Student Accounting on these accounts once they turn an account over to that unit.

Recommendations

Improve integration between independent departments and central units.

Management Corrective Actions

1. By July 15, 2016, A&FS will repair the KFS AR Aging report (FIS409) and the Unapplied report.
2. By January 15, 2017, A&FS will notify the 93 account managers currently using MyInvoice/Banner that their departments are responsible for a review and approval process for invoices before those invoices are posted in Banner.
3. By March 15, 2017, A&FS will provide online training to units for the regular reconciliation of AR to gl and regular review of the Unapplied report. This will include training on how to analyze accounts receivable balances and determine when a reserve/write off is necessary.
4. By March 15, 2017, A&FS will evaluate the feasibility of documenting collections efforts centrally.

[1] Unapplied amounts are payments received by the Cashier’s office that have not been applied to a customer account.

D. Many units extend credit beyond the 30 days stated as campus policy. Most units do not have written AR procedures documents.

Sixty percent of surveyed units reported that they consider an account overdue 30 days after the first invoice or statement has been provided to the customer. Twenty-eight percent reported 60 days and twelve percent reported 90 days, despite the fact that campus policy is 30 days (PPM 330-90, *Accounts Receivable*).[2] Many units surveyed and interviewed noted that collections from international customers are expected to be slower.

Seventy-four percent of the surveyed units state that they do not have written account receivables procedure documents. This creates risk and potential inefficiency for departments when there is staff turnover.

Recommendations

Communicate the 30-day campus policy to independent units that process AR. Document accounts receivables procedures for independent departments.

Management Corrective Actions

1. By July 15, 2016, A&FS will communicate the policy to all units in this group, and will update the A&FS website to clearly state that accounts are overdue 30 days after the first invoice or statement has been provided to the customer. A&FS will remind units that they have the option to require prepayment from international or recalcitrant customers in order to increase policy compliance.
2. By March 15, 2017, A&FS will develop a departmental process template for accounts receivables that by reference adopts campus policy, but allows for tailoring to a department's unique processes.
3. By March 15, 2017, A&FS will post the template on its website, notify departments that the template is available, and will assist them in developing and documenting their procedures upon request.

[2] Thirty-two percent of survey respondents indicated that they send regular monthly statements. Sixty-eight percent report that they do not. These units generally provide customers with an initial invoice and then resend if the account becomes overdue per the unit's internal policy.

APPENDIX A

We sent survey invitations to selected account managers who were in the scope of our project but had not been selected for interviews. We sent reminder invitations and followed up with units that did not reply before closing the survey with 28 completed surveys out of 36 requests (78%).

The following is information obtained via our survey that does not directly pertain to our recommendations for improvement or has not been included in the body of our report. It has been provided as supplementary information that may benefit some readers.

- Most of the responding units (89%) report that most or all of their customer payments are received by the Cashier's office.
- A name was provided by 83% in response to our question asking who reviews the AR Aging report. Sixty-one percent indicated a monthly review.
- The majority of the units (96%) are responsible for their own collection activities.
- Most (64%) consider all accounts on their books to be collectible.
- The majority (83%) report that they do not provide any good or service without charge.
- The majority are aware of (82-96%) and have used (73-88%) online AR processing resources and training.
- Most (74%) are not interested in using centralized services for accounts receivables processes.