

November 6, 2014

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Associate Vice Chancellor
Extended Studies
0176-O

Subject: *Service Agreements, Phase II – Extension*
Audit & Management Advisory Services Project 2015-38

The final audit report for *Service Agreements, Phase II – Extension*, Audit Report 2015-38 is attached. We would like to thank all members of the department for their cooperation and assistance during the audit.

The findings included in this report will be added to our follow-up system. While management corrective actions have been included in the audit report, we may determine that additional audit procedures to validate the actions agreed to or implemented are warranted. We will contact you to schedule a review of the corrective actions, and will advise you when the findings are closed.

UC wide policy requires that all draft audit reports, both printed (copied on tan paper for ease of identification) and electronic, be destroyed after the final report is issued. Because draft reports can contain sensitive information, please either return these documents to AMAS personnel or destroy them at the conclusion of the audit. We also request that draft reports not be photocopied or otherwise redistributed.

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Attachment

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AUDIT & MANAGEMENT ADVISORY SERVICES

Service Agreements– University Extension
November 2014

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Project Number: 2015-38

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I. Background

Audit & Management Advisory Services (AMAS) has completed a review of Service Agreements– University Extension (Extension). This report summarizes the results of our review.

A Service Agreement is a written legal agreement between the University and an external entity containing terms and conditions under which goods and/or services are provided by the University. Service Agreements may be issued for approved recharge activities for ongoing or continuous sales of goods and/or services at rates approved by the UCSD Recharge Rate Review Committee, or for services provided for non-recharge activities. A Service Agreement must be signed by persons having University of California San Diego (UCSD) contracting authority.

Extension is one of four areas of campus¹ that have the authority to execute certain incoming Service Agreements. The most common type of service provided by Extension is an agreement to provide training. The Extension Program Representatives negotiate the service with the external party and complete a draft agreement. The draft agreement is then sent to the Program Director for approval, and he forwards it to the Business Affairs unit. The Business Affairs unit reviews the agreement request and initiates the authorization through signing of the contract.

University of California (UC) Business and Financial Bulletin (BFB) A-59, *Costing and Working Capital for Auxiliary and Service Enterprises*, requires that recharge and other self-supporting activities charge the full cost of conducting business when selling to external non-University customers. These activities are supported by campus administrative offices and are generally conducted in campus funded and maintained space, so they do not pay directly for their own facility costs such as debt service, building maintenance, and utilities. As a result, the policy requires an appropriate level of campus overhead be included with the total price charged to external customers. In most cases, this is accomplished by adding a differential income overhead rate to the direct cost of the service provided, with some portion remitted back to the campus and contracting department.

In some cases, such as with Extension, an activity may have an approved exemption from remitting the differential income, because they pay for their own facility costs and many of their own administrative needs. These activities are assessed an administrative overhead recovery recharge of 4.1% for recovery of costs for central administrative support, instead of the differential income overhead assessment. Administrative overhead recovery recharge exemption requests must be submitted to the Financial Analysis Office for review and recommendation, with final approval by the Vice Chancellor of Resource Management and Planning.

¹ Other areas of campus with authority to execute Service Agreements are the Office of Contract & Grant Administration (OCGA), Scripps Institution of Oceanography (SIO) Contracts & Grants, and Health Sciences Business Contracting. These areas are addressed in separate AMAS reviews.

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Departments are responsible for establishing the appropriate accounting structure and for recording the proper entries in the financial ledger. In addition, departments are responsible for remitting differential income as part of their fiscal year end closing activities, and the Campus Budget Office (CBO) is responsible for monitoring and ensuring that the differential income is remitted properly.

In 2011, a Service Agreement Oversight Committee was convened to ensure that Service Agreement activity was properly administered across the four areas responsible for Service Agreement activity. The committee charge was to pursue delegations of authority related to Service Agreement contracting; provide policy interpretation and guidance for processing Service Agreements; and serve as a resource to resolve issues related to Service Agreement classification and responsibility.

II. Audit Objective, Scope, and Procedures

The objective of our review was to evaluate Extension's practices for executing Service Agreements with external parties and assess the overhead cost recovery process. In order to achieve our objective, we performed the following:

- Reviewed UC BFB A-59 and Blink Guidance pertaining to Service Agreements and income-producing activities;
- Reviewed relevant campus-wide reports addressing or referencing Service Agreement issues, such as the ASSA Task Group (May 2010), and the Service Agreement Oversight Group (2011);
- Reviewed documentation for Delegations of Authority for Execution of Agreements;
- Reviewed the fiscal closing instructions for Self-Supporting Activities;
- Interviewed the Extension staff responsible for Service Agreement administration;
- Evaluated the current processes for negotiating and executing Service Agreements;
- Reviewed UCSD Policy & Procedure Manual (PPM) 200-13 *Conflicts of Interest* and the Campus *Administrative Responsibilities: Principles of Conflict of Interest*;
- Interviewed the Director of the Conflict of Interest office;
- Interviewed the CBO Senior Budget Analyst regarding the monitoring and collection of differential income for contracted services;
- Interviewed the Accountant Supervisor for General Accounting regarding the accounting processes for Self Supporting activities; and
- Tested a sample of service agreements for compliance with delegation of authority, classification criteria, conflict of interest reporting, and differential income remittance².

III. Conclusion

Based on our review, we concluded that the process for executing Service Agreement contracts provided reasonable assurance that Service Agreements were appropriately

² Our evaluation of Service Agreements was limited to documentation initially submitted as part of the requisition and did not assess whether activities were consistent with final contract terms and conditions.

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classified, and received an appropriate level of review. The administrative overhead recharge of 4.1% for recovery of costs for central administrative support was administered by the CBO, and processed at the beginning of the fiscal year based on the previous year's financial information, and prorated into four quarterly installments.

We did note that internal controls related to conflict of interest reporting and delegations of authority for signing Service Agreements could be strengthened to ensure compliance with University policy and ensure that agreements are appropriately authorized.

IV. Observations and Management Corrective Actions

A. Delegation of Authority

Service Agreement contracts were executed without proper University contracting authority.

A delegation of authority specifies the scope of authority being delegated to an individual in the organization. The delegation for contracting authority is granted by the Chancellor through an official letter and is written to the title of the position to which the authority has been delegated. The authority is reassigned automatically when someone leaves the position. Letters may contain individual names, but authority always remains with the position title. A UCSD delegation of authority letter generally includes a reference to any applicable Presidential letter and any specific terms, restrictions, or requirements.

The responsibility for reviewing and approving Service Agreements for Extension resided with the Business Affairs department. The authority for the execution of Service Agreements was granted by the Chancellor to the Associate Vice Chancellor for Extended Studies and Public Programs in September 2000. In January 2013 limited authority to negotiate and enter into various types of agreements was further delegated by the Associate Vice Chancellor to the Associate Dean and Management Services Officer. However, we noted that the Business Affairs Director and Associate Director would routinely use the Associate Dean's electronic signature to authorize Service Agreements. The effect of this practice is that individuals without formal delegated authority were responsible for executing Extension Service Agreements.

Management Corrective Action:

The Associate Dean will review and approve all Service Agreements. Management may also consider the possibility of redelegating the authority to individuals in Business Affairs who provide the final review and execution for contracts.

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B. Conflict of Interest Disclosure

University Extension did not require a Conflict of Interest disclosure as part of the Service Agreement process.

A conflict of interest refers to situations in which employees may have the opportunity to influence a University's business decision in ways that could lead to personal gain or give advantage to firms in which employees have an interest. All University employees are expected to continue to separate their University and private interest in accordance with existing University policies and State law.

PPM 200-13 states that “The University's overall policy on conflict of interest is that none of its faculty, staff, managers or officials shall engage in any activities which place them in a conflict of interest between their official activities and any other interest or obligation.” The *Administrative Responsibilities for the Principles of Conflict of Interest* are guidelines to ensure a working atmosphere free of any conflicts of interest and that Employees participating in outside activities on behalf of the university must perform their functions ethically and objectively. As it relates to Service Agreements, a systematic review of financial disclosures from key personnel must disclose any financial interests prior to the acceptance of contracts from governmental and non-governmental sponsors. Both SIO Contracts and Grants and OCGA require a financial disclosure via the 700-U form for all Service Agreement requests during their initial requisition process.

During our review, we noted that Extension does not include a conflict of interest disclosure as part of the Service Agreement requisition process. The majority of Service Agreements are solicited by external companies for training services. The class specifics are initially negotiated by the Program Representative and the draft agreement is approved by the Program Representative's Director, who has overall responsibility for ensuring that direct costs associated with the classes are recouped. The draft agreement is then sent to the Business Affairs unit for review and authorization. Although there may not be a financial conflict within the Service Agreement process, there could still be a perception of a conflict, which should be addressed in the interest of transparency. Further, University officials cannot appropriately protect the University and its employees in potential conflict situations if a disclosure is not requested of personnel involved in the negotiation process.

Management Corrective Action:

Extension Management will incorporate a process for COI disclosure during the initial requisition and review of Service Agreements. In the event of a positive disclosure, a 700-U would then be required and sent to the COI office for review.