

UC MERCED INTERNAL AUDIT ANNUAL REPORT

Fiscal Year 2013–2014 in Review

Contents of Annual Report

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Overview and Highlights

The mission of UC Merced Internal Audit is to help UC Merced fulfill its mission of teaching, research, and service, by:

- Providing value added services that assist management in meeting their responsibilities and achieving established goals;
- Collaborating with internal customers so that services strengthen controls in order to mitigate risks and improve process efficiency and effectiveness; and,
- Ensuring compliance with University policies and external regulations.

Overview and Highlights

During FY 2013-2014, Internal Audit:

- Completed 4 audits and 9 advisory services projects
- The projects evaluated departments from all campus divisions
- Worked with employees during audits and advisory services to identify distinct actions to strengthen internal controls and to improve the efficiency of processes. 21 management corrective actions were set up to be tracked until completion.

Overview and Highlights

The following are some details related to the department:

- During the year, UC Merced Internal Audit was made up of one employee (the Audit Director). In July 2014, the department increased to two employees with the hiring of a new audit analyst.
- The Audit Director represents UC Merced at UC Audit Director meetings, IT Audit meetings, and other systemwide audit related discussions.

Overview and Highlights

The following is a high level overview of how employee and consultant time was utilized by UC Merced Internal Audit during FY 2014. A much larger percentage of time was spent on advisory service projects during FY 2014 compared with FY 2013.

	FY 2014 Hours	% of Time FY 2014	% of Time FY 2013
Time spent on Audits	772	36%	68%
Time spent on Advisory Service Projects	853	40%	7%
Time spent on Audit Support Activities (e.g. Audit Risk Assessment, Quality Assurance Review, etc.)	<u>109</u>	<u>5%</u>	<u>5%</u>
Total Direct Time	1,734	81%	80%
Administrative, Professional Development, Training Employees, and other Indirect Hours	418	19%	20%
Total hours available	2,152	100%	100%

Annual Audit Risk Assessment

In planning for the FY 2013 – 2014 audit plan, risks and inefficient processes were discussed with employees from many departments during the Annual Audit Risk Assessment

To evaluate potential areas for audit, Internal Audit considers five characteristics of an area or process:

- **Quality and Stability of Control Environment** *(Does the area have effective management? Have problems been noted in this area in the past? Have there been changes in this area that might increase risk?)*
- **Business Exposure** *(Based upon revenues and expenditures, how large is the potential loss in this area?)*
- **Public and Political Sensitivity** *(What is the potential for bad or embarrassing publicity that would hurt the University's reputation?)*
- **Compliance Requirements** *(Is the area subject to external policies and regulatory matters which could result in monetary losses, litigation or the loss of funding sources?)*
- **Information Technology and Management Reporting** *(Is the University's IT able to provide information that is accurate, available, timely, and useful for management?)*

Projects Based upon Audit Risk Assessment

Based upon the Audit Risk Assessment, systemwide requirements, and special requests, the following Audits and Advisory Services were completed:

Audits

- Purchasing
- Housing 4 and Student Services Building Construction Projects
- Audit of Grants (Including ARRA Grants)
- Control Over Cash and Payments

Projects Based upon Audit Risk Assessment

Advisory Service Projects

- Review of Development and Gift Accounting
- IT Operations Assessment
- Limited Scope Review of Student Business Services
- Review of the Graduate Division

Projects Completed because of Special Requests from Leadership

Advisory Service Projects

- Early Childhood Education Center
- Center for Educational Partnerships Travel Reimbursements
- Budget Roles and Responsibilities
- Background Checks
- Associated Students of UC Merced

Purchasing Audit

The purpose was to evaluate the adequacy of internal controls related to purchase order processes and practices.

Areas for improvement included:

- Additional procedures should be implemented to identify potential conflicts of interest
- Processes for reviewing and updating Certificates of Insurance should be improved
- Background checks should be completed for contractors filling sensitive positions
- Purchases in violation of policy should be reported to the Ethics and Compliance Program Management Council
- Segregation of duties related to vendor masterfiles should be improved

Housing 4 and Student Services Building Construction Projects

The purpose was to ensure that the Housing 4 and Student Services Building Construction projects were properly awarded and effectively managed.

Areas for improvement included:

- Documentation which provides evidence of fair processes in the competitive selection of contractors and professional firms
- Review that contractors and professional firms have adequate insurance coverage
- Review of Change order costs

Audit of Grants (Including ARRA Grants)

The purpose was to evaluate controls over grant processing from the point that a proposal is prepared and submitted until a final closeout of the award.

The following area for improvement was identified:

- To improve operations, data related to proposals and awards should be collected and analyzed

Control Over Cash and Payments

The purpose was to review control over cash and payments received by the University.

Areas for improvement included:

- Bank reconciliations should be completed in a timely manner
- Variances from policy should be reviewed by the Campus Cash Handling Coordinator
- Petty cash utilization should be reviewed
- Establish a plan for complying with PCI DSS 3.0
- Document changes of safe combinations
- Improve the safeguarding of cash at after-hours events

Review of Development and Gift Accounting

The main purposes were to evaluate gift recording and accounting processes and to identify potential improvements in the management and stewardship of gifts and endowments.

Areas for improvement included:

- Development Services should work with departments to improve accountability over gifts and endowment payouts
- Donor information could be better protected by utilizing electronic files rather than having paper files with duplicate information in different departments
- There could be more written guidelines related to gifts and fundraising with additional written campus procedures
- Knowledge gaps and beneficial training should be periodically reviewed

IT Operations Assessment

The project evaluated UC Merced's information technology operations and governance practices as a means to improve the overall performance of the University's IT functions.

Areas for improvement included:

- Improving governance and alignment
- Improving communication
- Security management
- Aging technology infrastructure
- Change and release management process
- Disaster recovery process
- Resource management
- Performance measurement and metrics
- Risk management

Limited Scope Review of Student Business Services

The purpose of the review was to assess risks related to student accounts and to identify whether internal controls have been set up to mitigate the risks.

The following area for improvement was identified:

- Review e-mail, computers, and shared drives for banking information

Review of the Graduate Division

The purpose was to analyze policies, forms, and processes that relate to the “lifecycle” of a graduate student at UC Merced in order to identify difficult processes and areas for potential improvement.

Areas for improvement included:

- Graduate students are required to utilize paper forms and to obtain written signatures.
- There are delays in processes related to graduate student employment and fee remissions.
- Other UC campuses provide services to graduate students which might be considered here at UC Merced.
- The website was sometimes difficult to navigate as changes in other sites created many broken links (“Page Not Found” warnings).
- The Graduate Division should provide leadership towards achieving the expected growth in the number of graduate students.
- With the limited staffing in the Graduate Office, for a long time there has been one employee handling each of the Office’s main functions. This can cause difficulties in maintaining service levels if one employee is out of the office.
- Graduate Office employees have had to manage IT-related projects or work with systems for which they’ve received little training.
- Exceptions to written policies are very common.

Early Childhood Education Center

The purpose was to determine whether proper policies and procedures were followed after the Center's first Type A Licensing Violation.

No areas of noncompliance with written requirements, policies, and procedures related to notifying parents and campus leadership, and employee disciplinary actions were identified.

Center for Educational Partnerships Travel Reimbursements

The purpose was to verify that the Center for Educational Partnerships (CEP) was accurately reimbursing for travel costs and to review the timeliness of reimbursements.

Areas for improvement included:

- Required approvals should be based upon risks
- Travel documented in the CEP timesheet system should be periodically reviewed to verify that employees have submitted reimbursement requests

Budget Roles and Responsibilities

Internal Audit facilitated a team of independent members with non-UC Merced campus expertise in UC fund mechanisms and fund management, accountability and controls, and budget management.

Results of Review

- The team put together recommendations regarding the appropriate roles and responsibilities of Accounting, Budget and departments to ensure proper financial controls and effective management of campus funds.

Background Checks

The purpose was to evaluate current compliance with UC Policy and written campus procedures related to background checks.

Areas for Improvement included:

- Improving review and monitoring of background checks of employees in critical positions
- Formalize background check procedures and requirements for contractors

Associated Students of UC Merced

The purpose was to review that ASUCM's expenditures were consistent with the purposes for student governments.

The following area for improvement was identified:

- Access to ASUCM funding

Significant and Recurrent Issues

From audits, advisory services, the annual audit risk assessment, and discussions with employees, significant and recurrent issues were noted in the following areas:

1. Human Resources responsibilities related to managing hiring practices, compensation, performance management, and training
2. Aging and obsolescence of IT infrastructure
3. IT Security
4. Wasteful Spending (excessive purchases of computer equipment and supplies)
5. Laboratory Safety

Significant and Recurrent Issues (cont.)

The significant and recurrent issues should be considered with the recurrent issues noted during prior years. The following are from FY 2013:

- Inadequate governance over information technology (i.e. the determination of the use of IT resources) results in campus units unable to get the IT support they need, insufficient backup of information, and little oversight of IT practices and security in some IT areas
- Laboratory safety processes and documentation make it difficult to verify that all Principal Investigators are fulfilling lab safety requirements.
- There is inadequate security over laptop computers, theft sensitive equipment, and mobile devices. The information on these devices could be at risk.
- Inconsistent hiring practices by campus units put the campus at risk of an audit by the Office of Federal Contract Compliance Program (OFCCP).
- Some departments were not fulfilling the administrative responsibilities assigned to them. Sufficient resources and training were not dedicated to the areas resulting in poor performance.

Significant and Recurrent Issues (cont.)

The significant and recurrent issues should be considered with the recurrent issues noted during prior years. The following are from FY 2012:

- Poorly designed systems result in departments inefficiently utilizing technology. The lack of effective interfaces between different systems results in employees having to complete manual “work around” processes.
- Departments handle financial information without adequate guidance. Accounting Services doesn't appear to have sufficient resources to work closely with departments.
- Lack of campus resources has resulted in some areas being understaffed. In some areas, poor segregation of incompatible duties has resulted.

Management Corrective Actions

Management Corrective Actions (MCA's)

Internal Audit monitors the progress of actions taken by management to address control deficiencies and operational issues identified during audits and advisory services. The follow-up process, which includes confirming agreed upon actions have been taken, is critical as it assists University leadership in ensuring appropriate work is completed to address and mitigate risks.

Management Corrective Actions

The following is a summary of the Management Corrective Actions (MCA's) during FY 2014:

	Total
MCA's outstanding after completion of FY 2013 projects	28
Additional MCA's added from FY 2014 projects	21
MCA's completed and closed during FY 2014	29
MCA's outstanding after the completion of the FY 2014 projects	20

Significant MCA's Completed

Of the 29 MCA's completed and closed during FY 2014, the following were some of the MCA's completed:

- A grant management system began to be implemented
- Human Resources began requiring the disposition process to be completed in the hiring system before offer letters are approved
- The IT Security Officer function became the full-time responsibility of an employee rather than just a part-time role.
- A campus safety specialist was hired to administer the campus Illness and Injury Prevention Program (IIPP).

Status of Past Due MCA's

UC Merced is still working to complete past due management corrective actions related to the Telecom Building Data Center. During early 2010, an IT audit report was issued that included MCA's related to fixing the cooling in the data center and fixing wiring necessary for adding an uninterruptible power source.

A building project which will fix the audit issues was in the design phase at the end of the year and is scheduled to be completed during 2016. The campus has decreased the reliance upon the data center to keep the data center from heating up.

Training in Controls

Throughout the year, Internal Audit was involved with training UC Merced employees and others regarding ways to improve internal controls. The following presentations were completed:

Monthly MSO Meetings

Monthly presentations to department MSO's regarding issues noted and ways to improve controls as part of the monthly "Internal Audit Director's Corner"

Financial Management Certification Program (FMCP)

Completed presentations in the following areas:

- The Control Environment, Internal Controls, and Monitoring
- IS-3 – Information security and confidentiality
- "Audit-Proofing Your Department" – Overview of Audit Process

Fraud Risk Workshop

Educated employees from various departments about fraud risks in Higher Education

Increased Benefit from Internal Audit

The following are some ways that Internal Audit will strive to benefit UC Merced during the years ahead:

- Internal control presentations to schools and departments in order to establish control self assessment
 - Enabling campus units to properly evaluate their own controls will improve the overall control environment
- Continue to improve collaboration between Internal Audit, Risk Management, and Compliance to improve how the campus identifies and mitigates risks
- Train employees in the Controller's Office in the use of data analytics software to be used for continuous monitoring