Venture Development Center

Audit Report No. R2504 | *November 7, 2024*

Executive Summary

Audit Objective

To evaluate the financial and accounting processes, internal controls systems, and the effectiveness and efficiency of related operations and controls in the Venture Development Center (VDC).

Primary Risk Types

Finance, Research, Enterprise Activities

Controls and Strengths

New leadership was put in place during FY23 and has worked on making changes to improve overall operations throughout the course of this audit.

Overall Conclusion

During the audit of the VDC, it was noted that with prior management in place, there was a significant lack of management oversight of the VDC's operations. Opportunities exist to enhance controls in the areas of management oversight, contract compliance, financial and management operations, conflicts of interest and commitment, property management, and lab safety.

Observations by Risk Level

Management has reviewed the observations and has provided responses and expected implementation dates. Detailed information is included in the attached report.

Recommendation	Risk Level	Management's Implementation Date
1. Improve Controls over Contract Compliance	**High**	Implemented per Management
2. Strengthen Financial and Management Operations	**High**	April 1, 2025
3. Monitor Conflicts of Interest and Commitment	**Medium**	December 10, 2024
4. Strengthen Controls over Property Management	**Medium**	August 1, 2025
5. Implement a Formal Lab Safety Program	**Medium**	June 1, 2025

For details about the audit procedures, explanation of risk levels, and report distribution, please see Appendices A, B, and C, respectively, in the attached report.

Detailed Audit Results

Overall Summary

During the audit of the VDC, it was noted that with prior management in place, there was a significant lack of management oversight of the VDC's operations. The absence of proper managerial oversight led to various issues regarding contract compliance, financial and management operations, conflicts of interest and commitment, property management, and lab safety that have affected the effectiveness and efficiency of operations within the VDC. Minor recommendations related to operations were shared verbally with management.

Prior to the audit, there was a different managerial structure in place where only one employee was involved in the day-to-day operations which resulted in the bypassing of controls and a lack of policies and procedures that ultimately led to fraud. As a result, leadership within the Office of Research and Innovation made changes to the overall structure, adding new management oversight.

Current management has made improvements, but there are still opportunities to enhance overall operations and ensure the VDC is operating efficiently and effectively as outlined in the observations below.

1. ***Improve Controls over Contract Compliance***

High Risk: By not monitoring the license agreements, residents may not be abiding by the terms of the contract as required and the VDC will not recover their costs. An outdated rate study may not reflect the current costs associated with the program.

As part of the process to join the VDC as a resident, a fully executed license agreement is required to be signed by UTD and the incoming resident. Prior to the audit, previous management did not ensure all residents had a fully executed license agreement in place and did not monitor the agreements for compliance. The license agreements outline the cost of the rent, when it is due, and other guidelines they must abide by as a resident at the VDC.

In testing for contract compliance, the following was noted:

- The rate study for the VDC is outdated and may not be accurate to reflect current costs associated with the program.
- Residents are not invoiced monthly for their rent payments and are responsible on their own to send in the payment on time. The VDC does not assess a late fee as stated in the agreement in the event the resident is past due.

- Several residents were either late making rent payments, had not paid at all, or were paying amounts that were not reflected in their license agreement. As of November 15, 2023, the VDC was owed $23,801 in rent from multiple residents. The VDC made changes throughout the audit to collect these payments and as of July 18, 2024, the VDC was owed $4,225 in rent from two residents. As a result of this collection process, some rent payments had to be written off due to resident non-payment.

Recommendation:
Conduct a new rate study and update periodically as needed to reflect current costs to ensure costs associated with the program are recovered. Monitor the license agreements and invoices to ensure the residents are abiding by the terms of the agreement.

Management's Action Plan:
1. VDC and IQ external rate studies were completed in July 2024.
2. The VDC began invoicing tenants monthly in July, 2024, and began enforcing late fees at the same time. As of October 2024, all VDC residents were current on their VDC payment obligations. Note: Occasionally, on a case-by-case basis, late fees may be waived with approval of the OTC Senior Director.
3. Prior to the start of the audit, it was determined that a). some VDC residents, primarily those at the Richardson IQ, did not have a fully-executed VDC license agreement in place, and b). some VDC license agreements were outdated and did not accurately reflect the then-current space utilization of the resident. Essentially, VDC license agreements and amendments were not being processed on a timely basis. During the period of October 2023 through March 2024, the VDC transitioned the residents to a new and updated VDC license template (which included a variety of updates including the University's ability to unilaterally terminate, language around the appointment of a company safety officer, and the added requirement of business liability insurance), thereby ensuring all the VDC license agreements were updated and current.
4. Prior to the start of the audit, it was determined that the ORI financial team was not being provided copies of VDC license agreements, amendments, terminations, and the like, and therefore was not being made aware of when new residents were onboarded and when monthly amounts owed would change. As of March, 2024, the ORI finance team was proved copies of all then-existing VDC license agreements (all of the "updated" agreements) and a process is in place wherein they are provided copies of all new agreements, amendments, terminations, etc., so as to ensure they are able to track the residents' financial obligations accurately.
5. In parallel to the financial team's payment tracking, in July 2024, the VDC implemented its own resident payment tracking system (the ORI financial team remains the system of record for VDC tenant payment data).

Responsible Party Name and Title:
Brent Schultze, Senior Director, Office of Technology Commercialization

Estimated Date of Implementation:
All of the above has already been completed/implemented.

Note: Audit and Consulting Services will conduct follow-up testing during the third quarter of FY25.

2. *Strengthen Financial and Management Operations*

High Risk: Without strong controls over financial and management operations, the risk of fraud and error, noncompliance, and operational inefficiencies is increased.

Policies and procedures surrounding financial and management operations are generally outlined within university policies and procedures; however, departments should also have their own procedures that outline various responsibilities and procedures unique to operations. In testing internal controls over financial and management operations, the following was noted:

- Department-specific policies and procedures do not exist.
- Several expenditures tested did not have the proper approval and supporting documentation as required by UTD policies. Audit and Consulting Services requested supporting documentation for some of the expenses tested, but they may have been lost or did not exist.
- Lack of segregation of duties within processes in the VDC. With prior management in place, there was a significant lack of management oversight. One employee was responsible for handling all day-to-day operations within the VDC from collecting rent payments, making purchases, and managing the administrative functions of the center. This ultimately led to a fraud occurring within the VDC and the employee being terminated.
- Inconsistent approval of cost center reconciliations by department personnel involved in the day-to-day operations. We found in testing, that roughly 30% of the time, the Associate Vice President for Research and Innovation approves the cost center reconciliations for the VDC even though there is no involvement in the day-to-day operations.

- Compliance issues with catering policies, as several events did not have itemized receipts as required. The previous Business Manager used her own catering company for events within the center which created a conflict-of-interest issue.

Recommendation:

Management should strengthen financial and management operations by developing department-specific policies and procedures that will improve controls over expenses, cost center reconciliations, segregation of duties, and accountability.

Management's Action Plan:

1. Regarding the expenditures that were found to not have "the proper approval and supporting documentation as required by UTD policies," it was determined that *most* of them related to the IQ cost center and the use of the VDC cost center to cover parts of the IIE's GCEC event. SOPs for the VDC and IQ will be developed/implemented to define expenditure processes and policies. **Estimated implementation date: 4/1/2025**.
2. In contrast to ACS's conclusion, the fraud that occurred did <u>not</u> result from one employee being responsible for handling all day-to-day operations within the VDC. The actual cause of the fraud was an employee's failure to disclose that they had a financial conflict of interest with a vendor that ORI had used multiple times for a variety of events. This type of fraud – a failure to disclosure an outside interest - cannot be reasonably mitigated by segregation of duties.
3. Regarding inconsistent approval of cost center reconciliations; the SOPs referenced in item 1, above, will define primary and backup cost center reconciliation approvers and approval procedures.

Responsible Party Name and Title:

Brent Schultze, Senior Director, Office of Technology Commercialization

Estimated Date of Implementation:

April 1, 2025

3. *Monitor Conflicts of Interest and Commitment*

UT Dallas conflict of interest (COI) and commitment policies for all employees is outlined on the Office of Institutional Compliance, Equity, and Title IX Initiatives website.[1] All UTD employees are required to disclose potential conflicts of interest and any outside activities. If any conflicts are noted, a management plan must be in place with appropriate approvals from both the School and University management.

> **Medium Risk:** Noncompliance with conflicts of interest and commitment policies could result in misuse of university funds, noncompliance, fraud, and reputational harm.

The previous Business Manager for the VDC had policy violations that included conflicts of interest reporting related to failure to disclose a personal business relationship with a catering company that was used for several events within the VDC. This employee did disclose that they had their own company in the same industry, but a conflict management plan was not on file and management was not monitoring activities to ensure no conflict of interest existed. The Business Manager was responsible for handling all day-to-day operations within the VDC, including making purchases and setting up catering for events. Ultimately, this led to the employee terminating employment with the University.

Recommendation:
Remind employees and require conflicts of interest and commitments be reported in compliance with university policies and monitor the reports for completeness. Monitor for potential COI during the cost center reconciliation review and approval process.

Management's Action Plan:
1. VDC and IQ employees will be reminded that any and all potential conflicts of interest must be reported in compliance with University policies. Note that annual compliance training reminds all employees of same. **Estimated implementation date: 12/1/2024**
2. All VDC and IQ cost center approvers will be made aware of all COI management plans on file for those employees routinely responsible for processing expenses for those cost centers. **Estimated implementation date: 12/10/2024**
3. And again, in contrast to ACS's conclusion, the fraud that occurred did <u>not</u> result from one employee being responsible for handling all day-to-day operations within the VDC. The actual cause of the fraud was an employee's failure to disclose that

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[1] https://institutional-compliance.utdallas.edu/compliance/conflicts-of-interest/

they had a financial conflict of interest with a vendor that ORI had used multiple times for a variety of events. This type of fraud – a failure to disclosure an outside interest - cannot be reasonably mitigated by segregation of duties.

Responsible Party Name and Title:
Brent Schultze, Senior Director, Office of Technology Commercialization

Estimated Date of Implementation:
December 10, 2024

4. *Strengthen Controls over Property Management*

According to [UTDBP3066 - Property Administration](), "each department head is responsible for the proper custody, maintenance and safekeeping of UTD property assigned to his/her department."

In testing expenses, we found an asset that was purchased that was not properly tagged. In discussing the issue with management, it was noted that there are no formal procedures within the VDC for the accounting of property.

Medium Risk: Without strong controls and formal procedures over property, including periodic inventories, the risks are increased that can lead to the loss or misuse of assets and can result in financial losses, reputational risks, and noncompliance with State and University regulations and policies.

Also, due to its unique nature, assets are not assigned to the VDC; instead, they are assigned to the Office of Research and Innovation. As a result, it is difficult to determine for which assets the VDC should be responsible and accountable.

Recommendation:
Strengthen controls over the VDC's property by developing internal procedures and separately tracking and conducting periodic inventories of the VDC's assets.

Management's Action Plan:
1. The VDC and IQ will develop/implement a property inventory management system – this system will track information including, but not limited to, the asset tag number and location of VDC/IQ assets. Periodic inventories will be performed. SOP(s) will be drafted to cover this process. Estimated implementation date: 8/1/2025

Responsible Party Name and Title:
Brent Schultze, Senior Director, Office of Technology Commercialization

Estimated Date of Implementation:
August 1, 2025

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5. *Implement a Formal Lab Safety Program*

The VDC does not have a formal lab safety program. The VDC is a unique center in that it rents space to residents that may not be current students or employees of the University. To be part of the VDC, it requires that one person be a sponsor and have been associated with UTD (or any UT System school) in some way in the past, such as a previous student or alumni.

The lab safety program at UTD is designed for areas with UTD students, faculty, staff, and researchers. As a result of the unique structure, Institutional Risk & Safety does not provide lab safety services for the VDC.

> **Medium Risk:** Without a proper lab safety program, risks are increased related to safety incidents and increase the likelihood of accidents, spills, and exposure to hazardous materials, that could potentially result in injuries. Failure to maintain adequate safety measures may lead to reputational risks, potential loss of revenue, or legal actions against UTD.

Recommendation:
Management should work closely with Institutional Risk & Safety to ensure a proper lab safety program is implemented that outlines protocols for handling hazardous materials, emergency response procedures, and regular safety training for all personnel in the VDC, including residents.

Management's Action Plan:

1. The VDC will engage Institutional Risk & Safety to develop and implement a VDC lab safety program which outlines protocols for handling hazardous materials and emergency response procedures, includes regular safety training for all personnel in the VDC (including residents), and tracks chemical inventories. Note: it would not be feasible for the VDC to implement a lab safety program that is separate and apart from Institutional Risk & Safety. SOP(s) will be drafted. Estimated implementation date: 6/1/2025.

Responsible Party Name and Title:

Brent Schultze, Senior Director, Office of Technology Commercialization

Estimated Date of Implementation:

June 1, 2025

Overall Conclusion

During the audit of the VDC, it was noted that with prior management in place, there was a significant lack of management oversight of the VDC's operations. Opportunities exist to enhance controls in the areas of management oversight, contract compliance, financial and management operations, conflicts of interest and commitment, property management, and lab safety.
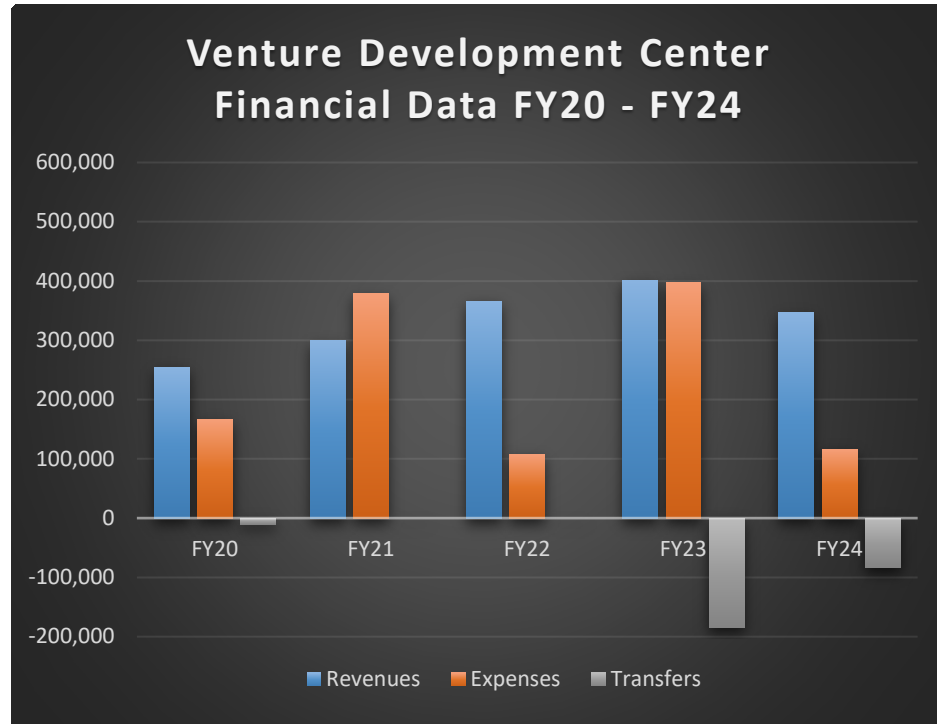
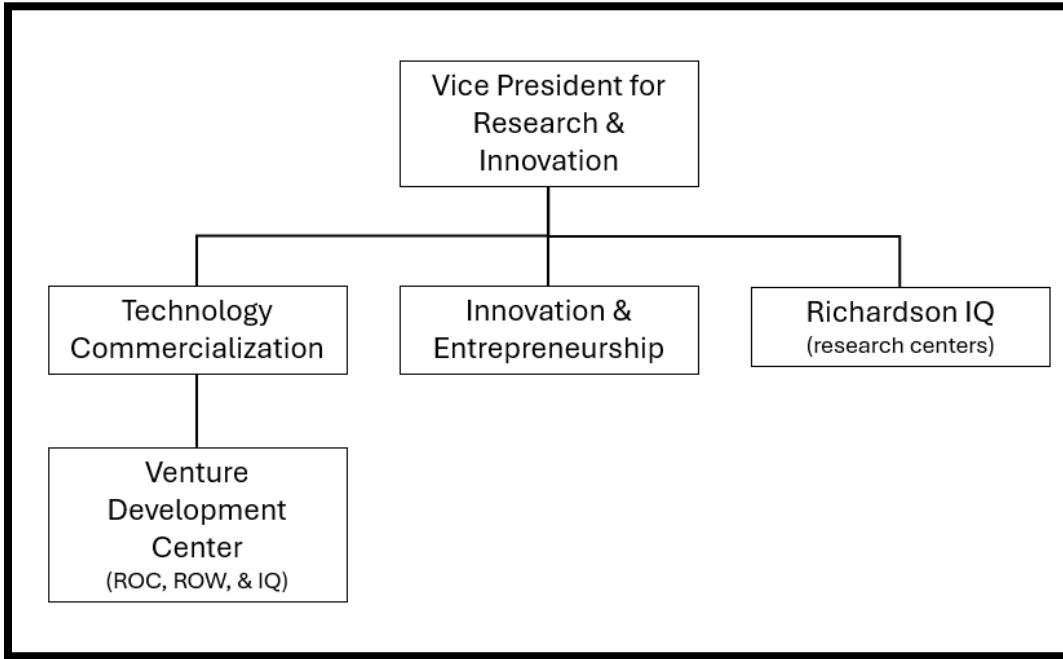# Appendix A: Information Related to the Audit

Background

According to their website, "The University of Texas at Dallas Venture Development Center (VDC) is a leading incubator designed to help students, faculty, and alumni commercialize their ideas and inventions. It does this through targeted, one-to-one support, enabling ventures to identify and build relationships with key industry partners, investors, entrepreneurs, and others to help them succeed. The VDC offers 20,000 square feet of state-of-the-art dedicated office, lab, and meeting space, as well as shared business services and equipment. We help companies build out their teams, protect their Intellectual Property (IP), and connect with expert advisors. We work to get minimum viable products (MVPs) into customers' hands and prove a viable, scalable business model."[2]

Operational data from FY20 – FY24 is shown in the table. Revenues include rents received from the license agreements.[3]

Venture Development Center Financial Data FY20 - FY24 (bar chart showing Revenues, Expenses, Transfers for FY20–FY24)

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[2] https://innovation.utdallas.edu/venture-development-center/
[3] Source: Reporting Console in PeopleSoft.

As shown in the organization chart, the Venture Development Center is led by the Senior Director for Innovation & Commercialization and reports to the Vice President for Research & Innovation. The Center is in the process of rebuilding its staff.

Objective

To evaluate the financial and accounting processes, internal controls systems, and the effectiveness and efficiency of related operations and controls in the Venture Development Center (VDC).

Scope

The scope of the audit was FY23 and FY24 to date. Fieldwork began in September 2023, and the audit concluded in July 2024.

The audit was conducted in conformance with the Institute of Internal Auditors' *International Standards for the Professional Practice of Internal Auditing*. Additionally, we conducted the audit in accordance with generally accepted government auditing standards (GAGAS). Both standards are required by the Texas Internal Auditing Act, and they require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. The Office of Audit and Consulting Services is independent per both standards for internal auditors.

Our audit methodology included interviews, observations of processes, reviews of documentation, and testing. The following table outlines our audit procedures and overall controls assessment for each of the audit area objectives performed.

Audit Area	Methodology	Observations Related to the Audit Area
Gaining an Understanding of VDC Operations	• Gained an understanding of operations by conducting interviews with VDC personnel. • Performed a risk assessment to identify areas of high risk within operations, and focused audit procedures on those risks. • Conducted physical walkthroughs of the VDC and Richardson IQ to observe strengths and weaknesses which assisted in the risk assessment process.	N/A

Audit Area	Methodology	Observations Related to the Audit Area
Financial	• Evaluated processes and tested expenses to ensure proper controls over authorization, compliance with policies and procedures, compliance with applicable gift/grant restrictions, segregation of duties, documentation, and business purpose. • Determined if cost center reconciliations were performed in a timely manner by authorized employees. • Determined if conflicts of interests and commitments had been disclosed in accordance with university policies.	Observation # 2, 3, 4
Operations	• Determined if physical access controls within the VDC were appropriate. • Evaluated the Lab Safety Program to ensure the proper safety protocols were in place and that tenants were aware of their responsibilities under the agreement.	Observation # 5
Contract Compliance	• Evaluated and verified contract compliance to provide reasonable assurance that the tenant license agreements were being followed and that the residents were paying amounts as indicated in the agreements.	Observation # 1

Follow-up Procedures

Though management is responsible for implementing the course of action outlined in the response, we will follow up on the status of implementation subsequent to the anticipated implementation dates. Requests for extension to the implementation dates may require approval from the UT Dallas Audit Committee. This process will help enhance accountability and ensure that timely action is taken to address the observations.

Appendix B: Observation Risk Rankings

Audit observations are ranked according to the following definitions, consistent with UT System Audit Office guidance.

Risk Level	Definition
Priority	If not addressed immediately, a priority observation has a significant probability to directly affect the achievement of a strategic or important operational objective of UT Dallas or the UT System as a whole. These observations are reported to and tracked by the UT System Audit, Compliance, and Risk Management Committee (ACRMC).
High	High-risk observations are substantially undesirable and pose a high probability of adverse effects to UT Dallas either as a whole or to a division/school/department level.
Medium	Medium-risk observations are considered to have a moderate probability of adverse effects to UT Dallas either as a whole or to a division/school/department level.
Low	Low-risk observations are considered to have a low probability of adverse effects to UT Dallas either as a whole or to a division/school/department level.
Minimal	Some recommendations made during an audit are considered of minimal risk, and the observations are verbally shared with management during the audit or at the concluding meeting.

Appendix C: Report Submission and Distribution

We thank the VDC management and staff for their support, courtesy, and cooperation provided throughout this audit.

Respectfully Submitted,

Toni Stephens

Toni Stephens, CPA, CIA, CRMA, Chief Audit Executive

Distribution List

Members and ex-officio members of the UT Dallas Institutional Audit Committee

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Other Interested Parties
Ms. Sanaz Okhovat, Associate Vice President for Research and Innovation and Chief Compliance Officer
Ms. Katherine Lowrey, Business Administrator, Venture Development Center

External Parties
- The University of Texas System Audit Office
- Legislative Budget Board
- Governor's Office
- State Auditor's Office

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