

**REPORT TO THE
UTAH STATE BOARD OF EDUCATION**

Report No. USOR 2014-02A

**LIMITED REVIEW OF THE BUSINESS ENTERPRISE PROGRAM RULES
AND REGULATIONS**

FISCAL YEAR 2014

March 7, 2014

**Audit performed by:
Utah State Board of Education's Internal Auditors**

Table of Contents

	Page
Report.....	1
Findings and Recommendations	
1. Rules and Regulations Clarifications.....	
a. General Ledger System	2
b. Taxes	2
c. Sales Income	3
d. Reporting Basis	3
e. Payment on Delivery	3
f. Vehicle Costs	4
g. Owner Draws	4
h. Set Aside	4
i. Supervisory Visits	5
j. Authority	5
2. Other General Items	6
3. BEP Response to Findings and Recommendations.....	6

April 7, 2014

Utah State Board of Education
250 East 500 South
Salt Lake City, Utah 84114

Dear Board Members:

The Utah State Board of Education (the Board) *Administrative Rule 277-116-4(E)* authorizes the Utah State Office of Education's (USOE) Internal Audit department (IA) to perform audits of programs under the purview of the Board. The Utah State Office of Rehabilitation (USOR) Director requested that IA perform a review of the Business Enterprise Program (BEP); specifically, circumstances related to Willie B's Café and monitoring procedures conducted by the BEP staff. This report, which is in addition to the limited review of Willie B's Café (see Internal Review 14-02), includes specific recommendations to USOR related to the BEP and the BEP Rules and Regulations (R&R) to help ensure the effective and efficient administration of this program.

The procedures performed, as noted in internal review 14-02, were more limited than would be necessary to express an audit opinion on compliance or on the effectiveness of the USOR's internal control or any part thereof. Furthermore, these procedures were more limited than would be necessary to provide absolute assurance that no errors or misappropriations occurred. Accordingly, we do not express such opinions. Alternatively, we have identified the procedures we performed and the findings resulting from those procedures. Had we performed additional procedures or had we conducted an audit of the effectiveness of internal controls, other matters might have come to our attention that would have been reported.

The findings resulting from the above procedures are included in the attached findings and recommendations section of this report. This report is intended solely for the information and use of USOR management and the Utah State Board of Education and is not intended to be and should not be used by anyone other than these specified parties.

If you have any questions, please contact me at (801) 538-7813 or Deborah Davis at (801) 538-7639.

Sincerely,



Natalie Grange CPA, CFE
Internal Auditor, Utah State Office of Education

Cc Russ Thelin, USOR Director
Bill Gibson, DSBVI Director
Donna Neri-Wells, BEP Coordinator

FINDINGS AND CONCLUSIONS/RECOMMENDATIONS

1. The BEP Rules and Regulations

A. Monthly Reporting and Sound Financial Practices

The BEP R&R Section 9 outlines the monthly reporting and set-aside requirements; however, these reports do not provide the same information or accountability as a double-entry general ledger (G/L) accounting system and do not encourage the adoption and use of sound financial accounting practices. The information from a G/L system may be used to compile financial information into a monthly report; however, the opposite is not true. We also noted that the R&R do not emphasize the importance of monthly bank reconciliation.

The monthly reports do not account for all transactions that occur in the business. Presently the monthly reports omit expenditures such as owner withdrawals, bank fees, etc. These transactions are critical to understanding the financial health of the business and enable the BEP program to provide relevant and sufficient monitoring and training. The monthly reporting does not appear comprehensive enough to assess the financial health of the business or provide training, and the R&R do not require owners to adopt and maintain an accounting system.

Recommendation

We recommend that the BEP review the R&R to include guidelines on the adoption of sound financial accounting practices. At a minimum, it should require licensed managers to use a G/L system to account for all transactions; this could be Excel (if set up appropriately), QuickBooks, etc. It should also emphasize the requirement for monthly bank reconciliations to the general ledger system. As bank reconciliations are a critical internal control, the BEP should consider requiring licensed managers to submit them with their monthly report or reviewing them monthly when on-site. We also recommend the BEP review the monthly reports and modify them to include all relevant financial information so they can be used in monitoring and training.

B. Taxes

The payment of sales and use taxes is critical and may have negative consequences for the licensed manager if not paid appropriately; however, it is not currently included on the monthly report.

Recommendation

We recommend the BEP consider adding sales tax payment information to the monthly report requirement.

C. Sales Income

The net register sales amount is used as the starting point on the monthly report to calculate the set-aside that will be paid to the BEP. If a general ledger system is being used, a bank reconciliation is being done regularly, and daily deposit controls and procedures are sufficient, using the net register sales amount might be adequate; however, it would be better to use the actual revenue amount (the deposited amount reconciled to the register amount), net of sales tax paid, rather than a just the register amount, which is essentially just a paper amount.

Recommendation

We recommend the BEP consider clarifying its R&R to indicate that the net sales amount used either needs to be the register amount reconciled to actual deposits or an actual revenue amount.

D. Reporting Basis

The BEP should clarify if the expenses on the monthly report are to be included on a cash basis (when money comes in or goes out the door), accrual basis (when obligated) or allocated basis (prorated over time). Examples of the current inconsistency to this being applied at one facility include:

- Advertising is paid once a year; however, it is included on an allocated basis each month on the monthly report, not as an expense in the month it is paid.
- Payroll taxes are included on the monthly report as the obligation to pay them has been incurred, even if they have not been paid (i.e. accrual basis).
- Amounts overdue to vendors are not tracked when the obligation is made; therefore, they are only included in the monthly report as they are paid (i.e. cash basis).

As these examples show, including items on a cash, accrual, or allocated basis impacts the profit or loss and the calculated set-aside amount.

Recommendation

We recommend the BEP consider clarifying its R&R to indicate the appropriate reporting basis to use to ensure consistency and accuracy for authorized expenditures and the calculation of set-aside.

E. Payment on Delivery

The BEP R&R 7.5 and 10.1I require licensed managers to “pay on delivery for all merchandise and avoid overdue payments”, though there are exceptions to this for emergency situations and if the licensed manager establishes a 30-day deferred account. The inherent risk associated with paying on delivery (e.g. risk that the cash or check won’t actually make it to the vendor and be accounted for appropriately by both the manager and vendor) is high.

Recommendation

We recommend the BEP consider either clarifying the R&R to apprise the licensed managers of this risk and to establish internal controls accordingly or to revise the R&R to require payment by check or electronic payment to the vendor based on an invoice.

F. Vehicle Costs

Vehicle costs per the R&R Section 9.2 include that vehicles used solely for business may be itemized in deductions, or may be deducted by mileage only. Personal vehicles used for business purposes will be deducted at the standard mileage rate as allowed by the IRS. For the facility reviewed it appeared most vehicles costs reported were gas reimbursements for employees. Gas reimbursements do not track actual mileage and the tax consequences for the employer and employees are not considered.

Recommendation

We recommend the BEP consider if gas reimbursements are authorized expenses that should be included in the monthly report. Given IRS regulations (ie. tax consequences), the BEP should clarify the language in the R&R to ensure costs associated with vehicles are handled appropriately for tax, financial accounting, and monthly reporting purposes.

G. Owner Draws

It appears an owner draw may be made one of several ways as noted below:

- Paid out from the register
- Debit transaction
- Check payment
- ATM Withdrawal from bank account
- Transfer to a personal bank account

The accounting for owner draws (for financial accounting, monthly reporting, and tax purposes (self-employment income) is not explained appropriately in the R&R and there could be confusion in how these draws are to be accounted for.

Recommendation

We recommend the BEP address and clarify in the R&R each of the methods of making owner draws including their appropriateness and the required documentation if a draw is made.

H. Set Aside

Per the current R&R Section 9, set-aside payments are to be calculated based on the net proceeds of each facility. It appears in doing the year-end reconciliation that the BEP is using monthly net losses to offset monthly net proceeds which reduces the set-aside owed and could result in an overpayment. Using net losses to offset monthly net proceeds may create a disincentive to have monthly net proceeds and indirectly

penalizes managers who do have monthly net proceeds and pay the full amount of set-aside based on those amounts. It also seems illogical to have a penalty for late payment if there is a possibility of having the amount owed reduced by a subsequent net loss.

Recommendation

We recommend the BEP and the Vendor Committee review the R&R related to set-aside and consider if using net losses to offset net proceeds meets the objective of the program; clarifications to the R&R should be made accordingly.

I. Supervisory Visits

R&R Section 11 requires regular and supervisory visits to the BEP facilities. The required areas to observe include operational items, compliance with laws, and compliance with the R&R. Financial accounting related items are only indirectly included.

Recommendation

We recommend the BEP consider clarifying the R&R related to supervisory visits to include, specific financial accounting related items that should be reviewed and documented during supervisory visits, including the following documentation:

- a. Taxes paid
- b. Monthly bank reconciliations
- c. Owner draws

The BEP should also consider if internal controls are sufficient. Consequences for any inadequacies should also be detailed in the R&R.

J. Authority

While performing our review we noted that the R&R are not specific related to the relationship between the BEP and the licensed manager, particularly related to the funding of the program, including the specific circumstances, if any, when the BEP will help fund operations (product, payroll, taxes, etc.) and the documentation that needs to be available for review upon BEP request or audit to determine the financial health and operational health of the facility.

Recommendation

Per federal law (34 CFR 395.4) The R&R are to be established to “assure the effective conduct of the State’s vending facility program and the operation of each vending facility...” Therefore, the relationship between the BEP and the licensed managers should be clarified to outline the responsibilities of both parties and the authority the BEP has in performing reviews, audits, etc. related to the facility.

2. Other General Items

In addition to the clarifications and recommendations above, we also noted and recommend the following:

- A. The Client Services Manual contains a chapter and an appendix on the BEP program and its Rules and Regulations; however, it is not consistent with the current BEP R&R. We recommend that any reference in the Client Service Manual to BEP be consistent with the most current BEP R&R.
- B. BEP should consider a process for periodically reviewing and updating the R&R and having them approved. Items that are considered addenda should at that time be incorporated into the actual R&R.
- C. Licensed managers should be trained on the R&R periodically so they are continually aware of the requirements, especially if clarifications or updates are made.
- D. Given the operational and financial aspects of the BEP, the program significantly impacts all stakeholders (the BEP staff, licensed managers, facilities issuing vending/cafeteria permits and employees of those facilities that rely on the food service). Therefore, for the protection of all stakeholders, the BEP should be careful in clarifying and updating the R&R and strict and fair in enforcing the R&R with all licensed managers.
- E. USOR should consult with the State Board of Education regarding the necessity of drafting state administrative rules to govern the BEP program and its associated expenditures and monitoring obligations.

BEP Response to Findings and Recommendations

We will consider all recommendations to improve the overall BE Program Rules and Regulations. The SLA will work with the BEP Licensed Managers Vendors' Committee in developing stronger controls through the Rules and Regulations staying within the federal guidelines. We will give a presentation of the Rules and Regulations once RSA has given the final approval.

We will get the Case Service Manual updated immediately to the current Rules and Regulations and make sure that all updates are completed timely.

As we already work within the Administrative rules of USOR we will review how we can better manage or make the necessary improvements in administering the Program through those rules.