Department of Rehabilitation

Audit Services Report of the Business Enterprise Program Snack Bar at the Board of Equalization Building (Location 3-764)

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INTRODUCTION

The Department of Rehabilitation (DOR) Audit Services Section has completed our audit of the October 2010 through March 2011 Monthly Operating Reports (MORs) submitted by Darren Simonds, Business Enterprises Program Vendor (BEP Vendor) to the DOR for the Snack Bar operation at the Board of Equalization (BOE) in Sacramento.

The BEP provides Department consumers, who are legally blind, opportunities to be trained in the operation of cafeterias, vending stands, and snack bars, with the ultimate goal of becoming independent food service professionals in California. The program was created through federal legislation, the Randolph-Sheppard Act of 1936, which was enacted to provide blind persons with remunerative employment, enlarge the economic opportunities of the blind, and stimulate the blind to greater efforts in striving to become self-supporting.

BEP Vendors operate their own facility and retain the profits from the facility they manage, excluding a percentage (set-aside fee) prescribed by law. This fee is placed in the Vending Facility Trust Fund, is matched with federal funds, and is then used to establish new facilities, refurbish/maintain established facilities, and pay health and dental insurance for active vendors.

State regulations require each BEP Vendor to submit a MOR by the 25th day of the following month. The MOR is a report of operations as well as the basis of calculating fees such as set-aside fees, workers' compensation and liability insurance. BEP Vendors are required to remit these fees to the BEP program each month with their MORs. As set-aside fees are the primary source of income for the Vending Facility Trust Fund, inaccurate and unsupported MORs could result in underpayment of fees which limits the amount of program funds eligible for matching federal funding and for use for the program

DOR also uses information reported on the MOR to assist BEP Vendors in making decisions on improving their locations, as a source for required Federal and State reports, and for the establishment of fees

Background

BEP Vendor Simonds began operating the GrabNGrill located in the BOE state building in November 2006. During audit fieldwork, the GrabNGrill was being remodeled and so the grill portion of the snack bar was not operational. The GrabNGrill consists of the following operations:

- A Snack Bar which includes a sit down dining area that offers hot and cold breakfast and lunch items for dine-in and take-out.
- A coffee kiosk serving hot and cold drinks as well as pastries
- Three vending machines located in the front entrance to the snack bar.

SCOPE

We conducted our audit in accordance with Government Auditing Standards for fiscal compliance as defined by the Government Accountability Office, except Standard 3.52 requiring an external peer review. These standards require that we plan and perform the audit to obtain reasonable assurance that the expenses reported on the MORs were compliant with the Vendor's Monthly Operating Report Instructions (MOR Instructions) applicable Federal and State regulations, and were supported by appropriate records. Audit fieldwork was conducted during July & August 2011.

Our audit included a limited review of the accounting systems and internal controls as they relate directly to the MORs through use of accounting system and internal control questionnaires and interviews with the BEP Vendor. We conducted additional testing, on a sample basis, of the March 2011 MOR expenses reported for sales, sales tax, purchases, inventory, payroll, operating expenses, and other income.

Our audit is subject to the inherent risk that all significant errors and irregularities, fraud, or non-compliance will not be identified.

FINDINGS AND RECOMMENDATIONS

During our review, we identified areas of non-compliance with regulations and the MOR instructions, and weaknesses in internal controls and record-keeping requirements. These deficiencies resulted in inaccurate or unsupported reporting of expenses on the MORs in the following areas:

- Gross Receipts/Sales Tax
- Cost of Goods Sold - Inventory and Merchandise Purchases
- Other Income

We recommend the BEP vendor must comply with applicable regulations and MOR instructions. Further, the BEP vendor shall strengthen controls over the operation, improve recordkeeping practices, and ensure accuracy of the MORs and fees submitted to DOR. Details on the findings and recommendations are included in **Appendix A**.

<u>GRABNGRILL'S RESPONSE TO THE AUDIT</u>

The audit of my facility has brought to light areas that need improvement. To address these issues, I am seeking the assistance of another bookkeeper with BEP experience. During the next 30 days we will be exploring the set-up of an accrual based accounting system. My current bookkeeping service is in the process of revising the March 2011 MOR. I will have this reviewed for accuracy before submitting it. The new accounting system will address all the issues listed in the findings report. Although I provided physical inventory counts to my bookkeeper, and I still have the records, I did not realize the figures were not used and was inaccurately reported.

To conclude, I am disappointed in the findings of this audit. I have in good faith provided all pertinent information to my bookkeeper. As we have discussed many issues, I now find that my concerns were not addressed.

<u>Required Action and Follow Up</u>

DOR is responsible for the proper administration and oversight of the BEP; thus, we are required to properly monitor BEP vendors to ensure their material compliance with federal, state, and DOR requirements.

1. Due to the significance of the differences identified and BEP program needs, the BEP vendor must submit amended MORs from October 2010 to current, as follows:

    - The BEP vendor will first prepare and submit an amended MOR for March 2011, to calculate the actual amounts to the affected line-items (Gross Receipts, Sales Tax, Purchases, and Other Income). The BEP vendor will also include a summary to explain the methodology used to prepare the amended MOR within 30 days of the date of this report.

    - Audit Services and BEP will review the March 2011 amended MOR submitted by the BEP vendor along with the summary provided to verify the methodology used whereupon DOR will provide feedback or approval to proceed with amending the remaining MORs.

    - The BEP vendor will submit the amended MORs for October 2010 to current to BEP for review, approval, and processing, within 60 days of the date of the DOR approval of the methodology used for the March 2011 amended MOR.

2. To ensure appropriate actions are taken to correct the findings deficiencies included in this report, a corrective action plan is required from the BEP vendor.

    - A Corrective Action Plan (CAP) will be prepared by the BEP Vendor in consultation with BEP to correct the findings identified in this report.
    - The CAP is to be submitted by the BEP Vendor to Audit Services (30 days after date of final report). Audit Services will review the CAP with BEP. The BEP vendor will be notified of the approval, or will be contacted to discuss any necessary changes as needed to ensure that taken or planned actions will satisfactorily resolve the deficiencies noted in this report.

Once the CAP has been approved, the DOR BEP will provide continued guidance and will monitor the BEP Vendor’s efforts towards completing the CAP to ensure the issues identified in the report are being corrected appropriately and timely.

APPENDIX A

DARREN SIMONDS, BEP VENDOR
BEP Location #3-764
GrabNGrill

Details to Findings

Gross Receipts

1. The BEP Vendor incorrectly reported Sales and Sales Tax, resulting in a net under-reporting of Gross Receipts on the March 2011 MOR.

   - We noted that the Gross Receipts (including Sales Tax) amount of $44,202 reported on the March 2011 MOR could not be supported. Further, the sales tax amount of $2,845 was inaccurately reported based on calculated amounts rather than the actual sales tax collected. Specifically,

     Sales
     - Coffee Cart Receipts were not included in the Gross Receipts, which resulted in the MOR amount being underreported by at least $3,400.
     - The bookkeeper missed posting receipts from the Vendor's second register on March 7, 2011 which resulted in the MOR amount being underreported by $634.40
     - Vending Machine receipts were not included in the Gross Receipts

   Based on available records for the snack bar and coffee kiosk, we were able to calculate Gross Receipts totaling $50,135, resulting in an under-reporting of at least $5,933 for the March 2011 MOR. We could not include vending machine receipts in our recalculation since the vendor did not record these amounts in his accounting records.

Sales Tax

- The sales tax collected was not used to accurately report sales tax on the MOR. Rather, we noted that the bookkeeper used an incorrect tax calculation method to report snack bar and the coffee cart taxes as follows:
  - Sales tax was reported for the snack bar sales based solely on recognizing 80% of gross sales as taxable.
  - Sales tax was reported for the coffee bar sales based solely on recognizing 33% of gross sales as taxable.

Using the snack bar Z tapes we were able to calculate the actual sales tax amount collected for the snack bar, resulting in an under-reporting of sales tax by $577.

- Applicable sales tax amounts were not reported for coffee cart sales or for the vending machine sales.

  Because the Gross Receipts and Sales Tax for the Vendor's facility were under-reported, this affects the amount reported for Liability Insurance (MOR Line 18), Profit from Operations (MOR Line 29), and to the Vending Facility Trust Fund (MOR Line 39).

  Over or understatements impact the overall BEP Vendor's profit from operations and the calculation of the set aside fee. Further, sales tax may have also been underreported to BOE. If sales tax is collected on sales transactions and not reported and remitted to BOE, it may result in penalties or administrative action by BOE.

The MOR Instructions state that the BEP Vendor is responsible for the completeness and accuracy of the report. Further, the MOR Instructions state that the Vendor must sign and date the report. The vendor's signature on the report signifies the report and attachments are a correct statement of the operation of the vendor's facility and contain only valid financial information for the location. Willful falsification of the report is legal cause for revocation of the vendor's license. The BEP Vendor is responsible for the completeness, accuracy, and submission of the report with an acceptable check or money order. The MOR Instructions also state that a copy of the instructions should be given to the vendor's accountant or any other person preparing the report. When a vendor chooses an individual to prepare MORs (DR478 reports), that person must be able to prepare legible, detailed and accurate reports.

RECOMMENDATION

To ensure accurate reporting, the BEP Vendor must report Gross Sales and Sales Tax for the snack bar, coffee cart, and vending machines and the accurate amounts must be recorded in the Vendor's Daily Cash Reports and supported by source records. Further, the BEP Vendor must ensure that all receipts from the Coffee Kiosks and Vending machine sales are included in the Gross Receipts, as well as ensuring that sales tax is properly reported based on the amounts actually collected as indicated by source records.

COST OF GOODS SOLD

2. The BEP Vendor incorrectly reported Purchases and Inventory, resulting in unsupported Cost of Goods Sold. Specifically,

- The amounts listed on line 4, Opening Merchandise Inventory ($9,908), and Line 7, Closing Merchandise Inventory ($9,046) of the March 2011 MOR could not be supported. Specifically,
  - The inventory for December 2010 cannot be fully supported because:
    - ➢ The BEP Vendor did not maintain source documentation for the December 2010 inventory summary submitted with the December 2010 MOR and used to support biannual physical inventory amounts. .
    - ➢ The BEP Vendor did not maintain supporting source documentation for the BEP Vendor's detailed Inventory Value Report.
    - ➢ There were discrepancies between the inventory summary and the inventory value report; some group totals and unit value numbers did not agree and the final inventory total reported on the summary report and the value report did not agree.

  - We were unable to determine whether the ending inventory for March 2011 was supported or reasonable because the BEP vendor does not conduct a monthly physical inventory. Rather, inventory amounts are reported based on an annualized calculation computed by the Cardinal Point (bookkeeper) computer system.

- The amount reported on Line 5 of the MOR - Merchandise Purchases ($20,500) was not supported.
    - ➢ Some invoices listed on the Accounts Payable (AP) Summary were not found among March 2011 invoices and could not be located by the vendor and bookkeeper.
    - ➢ Some invoice amounts on the AP Summary did not match the actual invoices provided by the vendor. For instance, an invoice from vendor Aramark was reported on the AP Summary as $42.35 but the actual invoice was for $42.52. Another invoice for vendor PITCO Foods was reported on the AP Summary as $244.39 but the actual invoice amount was for $241.39.
    - ➢ There were instances of double posting of invoices, e.g., an invoice for vendor Coca-Cola in the amount of $230.05 was entered twice on the AP Summary. An invoice for Quality Snacks Distributor was also entered twice on the AP Summary in the amount of $318.75.

Based on the recording errors noted, purchases for March 2011 appear to be under-reported by at least $1098. Further, the DOR has no assurance that the expenses reported on the MOR are related to the BEP Vendor's location when there is missing documentation.

The California Code of Regulations (CCR), Title 9, Section 7220 (o) requires the vendor to take and report the physical inventory of the vending facility merchandise and supplies twice annually for the periods ending June 30th and December 31st and submit the inventory reports to BEC and at other times as required by the BEP program for which previous instruction has been given.

The MOR Instructions state for Line 7 Closing Merchandise Inventory, enter the total amount of the closing merchandise inventory for the report month in the "Itemized Amount" Column. Amounts shown as inventories must be actual at least twice annually, June 30 and December 31. Additionally, MOR Instructions requires a signature certifying that the report has been reviewed and is true and correct.

The California Code of Regulations (CCR), Title 9, Section 7220 (l) requires the vendor to maintain required records on the operation of the facility for the current year plus the three preceding years. Upon written request, books of accurate account and records pertaining to a vending facility operation should be made available for examination and audit by the Department at any reasonable time and place. Such records shall include invoices from vendors.

RECOMMENDATION

The BEP Vendor must accurately calculate and report Cost of Goods Sold amounts on the MOR. We further recommend that the BEP Vendor accurately calculate and report beginning and ending inventory amounts, and document this process in order to support these figures with appropriate accounting records. Also, we recommend that the BEP Vendor make improvements to his purchasing and inventory management process by:

- Recording and reporting purchases in the month they are incurred by using an accrual based accounting system.
- Ensure that invoice amounts are accurately posted in the accounting records.
- Maintain appropriate records to support the amounts claimed on the MORs.
- Improve the physical inventory control system to be taken and reported at least twice annually as required by regulations and as often as required by the BEP program.

OTHER INCOME

3. The BEP Vendor did not report lottery commissions amounts earned during the month on the March 2011 MOR.

   The vendor's March 2011 financial statements included lottery retailer receipts and a daily cash summary that included sales of lotto tickets and lottery scratchers totaling over $9,000. Using these documents and the March 2011 MOR we found that lottery commission did not carry forward to line 32 (other income from services). As a result, approximately $1,088 should have been included on line 32 of your March 2011 MOR. This amount is the lottery commission reported on the retailer receipts.

   Vendor receives 6% commission on sales and 2% commission on winnings.

   Line 32 of the MOR states "Enter the amount of profit received from services such as video rentals, film processing, **lottery ticket sales**, etc., including sales tax in the "Itemized Amt." column.

   RECOMMENDATION
   The vendor must accurately record all lottery commissions earned timely into the accounting records to ensure proper reporting on the MOR.