



**FINANCIAL AUDIT DIVISION REPORT**

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**Board of Barber and  
Cosmetologist Examiners**

**Internal Control and Compliance Audit**

**July 1, 2004, through June 30, 2008**

**October 23, 2008**

**Report 08-27**

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FINANCIAL AUDIT DIVISION

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## OFFICE OF THE LEGISLATIVE AUDITOR

State of Minnesota • James Nobles, Legislative Auditor

October 21, 2008

Representative Rick Hansen, Chair  
Legislative Audit Commission

Members of the Legislative Audit Commission

Mr. Frank Plant, Chair  
Board of Barber and Cosmetologist Examiners

Ms. Gina Stauss, Executive Secretary  
Board of Barber and Cosmetologist Examiners

Ms. Juli Vangsness, Administrative Director  
Health Licensing Boards – Administrative Services Unit

This report presents the results of our internal control and compliance audit of the Board of Barber and Cosmetologist Examiners (board) for the period July 1, 2004, through June 30, 2008.

We concluded that the board did not adequately control its licensing and receipt processes. The board identified and reported to us, and we substantiated, that \$10,000 in license fee receipts are missing. As required by [Minnesota Statutes](#) 2007, 3.975, we are referring this report to the Office of the Attorney General and the Hennepin County Attorney's Office.

The Health Licensing Boards – Administrative Services Unit (services unit) provides financial management assistance to the Board of Barber and Cosmetologist Examiners.

Our fieldwork ended on August 8, 2008, and we discussed the results of the audit with board staff on October 7, 2008. The audit was conducted by Michael Hassing, CPA, CISA (Audit Manager) and Tracy Gebhard (Auditor-in-Charge), assisted by auditor Alex Weber.

We received the full cooperation of the board and services unit staff while performing this audit.

*/s/ James R. Nobles*

James R. Nobles  
Legislative Auditor

*/s/ Cecile M. Ferkul*

Cecile M. Ferkul, CPA, CISA  
Deputy Legislative Auditor



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# Report Summary

## Conclusions

The Board of Barber and Cosmetologist Examiners (board) did not have adequate controls to safeguarded receipts and sensitive assets and did not properly oversee financial transactions. Approximately \$10,000 in license fee receipts are missing.

The board generally had adequate internal controls to ensure that it accurately paid employees and vendors in accordance with management's authorization, produced reliable financial information, and complied with finance-related legal requirements. However, the board did not review key payroll reports and did not comply with a key provision of the state's cell phone policy.

For the items tested, the board generally complied with finance-related legal requirements over its financial activities. However, it did not always deposit receipts daily over \$250, as required by statute.

## Key Findings

- The Board of Barber and Cosmetologist Examiners did not adequately safeguard or promptly deposit its receipts and did not reconcile receipts to licenses issued. The board could not account for approximately \$10,000 of license fee receipts. ([Finding 1, page 7](#))
- The board did not verify its payroll transactions to key payroll reports. ([Finding 2, page 8](#))
- The board did not have adequate inventory controls for its fixed assets and sensitive items. ([Finding 4, page 9](#))

## Audit Objectives and Scope

### Objectives

- Internal Controls
- Compliance

### Period Audited

July 1, 2004, through June 30, 2008

### Programs Audited

- License Revenue
- Other Administrative Expenditures
- Payroll Expenditures

## Background

The Board of Barber and Cosmetologist Examiners was established in 2004 by legislation that transferred the regulation of cosmetology from the Department of Commerce to the Board of Barber Examiners. The expanded board licenses more than 40,000 practitioners, instructors, establishments, and schools. It also sets education requirements and examination standards, standards of practice and conduct, and responds to inquiries and complaints. The board operates under [Minnesota Statutes](#) 2007, Chapter 154, and [Minnesota Administrative Rules](#) 2007, Chapters 2100, 2105, and 2110.

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# Board of Barber and Cosmetologist Examiners

## Agency Overview

The Board of Barber and Cosmetologist Examiners was established in 2004 by legislation that transferred the regulation of cosmetology from the Department of Commerce to the Board of Barber Examiners. This transition expanded the board's responsibility from approximately 4,000 licenses to over 40,000 licensed practitioners and establishments. The board operates under [Minnesota Statutes](#) 2007, Chapter 154, and [Minnesota Administrative Rules](#) 2007, Chapters 2100, 2105, and 2110.

The board consists of seven members appointed by the Governor, including three barber members, three cosmetology members, and one public member. Frank Plant has been the board chair since January 2008. The board is responsible for hiring the executive secretary. The executive secretary position was held by Maureen Tibbetts until July 2006. The board hired the current executive secretary, Gina Stauss, in August 2006; she is responsible for the daily management of the board. The board is responsible for education requirements and examination standards, standards of practice and conduct, inspections, and responding to inquiries, complaints, and reports. The board accomplishes its mission through licensing of practitioners, instructors, establishments, and schools.

Although statutes<sup>1</sup> do not consider the Board of Barber and Cosmetologist Examiners one of the health-related licensing boards, the board uses the Health Licensing Boards – Administrative Services Unit (services unit) to process its financial transactions. The services unit charges for its services based on the extent of services it provides. The services unit, located in the same building as the board, provides services in the areas of budgeting, fiscal analysis, human resources, transaction processing, purchasing, operations analysis, contracts, information technology, and policy analysis.

The Board of Barber and Cosmetologist Examiners is funded through appropriations. The revenue the board collects from barber and cosmetology licenses, renewal fees, and various other fees is deposited into the state's General Fund and are not available for the board's operations. Statutes do not require the board to set its fees to recover its operating costs. Table 1 summarizes the board's revenues and expenditures for the period July 1, 2004, through June 30, 2008.

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<sup>1</sup> [Minnesota Statutes](#) 2007, Chapter 214.

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**Table 1**  
**Revenues and Expenditures**  
**July 1, 2004 – June 30, 2008**

<b>Revenues<sup>2</sup></b>	<b>Fiscal Years<sup>1</sup></b>			
	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>
Barber Licenses & Fees	\$ 218,805	\$ 213,096	\$ 206,257	\$ 190,805
Cosmetology Licenses & Fees	<u>1,208,335</u>	<u>1,242,459</u>	<u>1,190,030</u>	<u>1,244,280</u>
Total	<u>\$1,427,140</u>	<u>\$1,455,555</u>	<u>\$1,396,287</u>	<u>\$1,435,085</u>
<b>Expenditures</b>				
Payroll and Board Per Diems <sup>4</sup>	\$ 172,571	\$ 328,080	\$ 471,007	\$ 519,472
Rent <sup>5</sup>	16,992	26,915	47,571	55,609
Supplies and Equipment	45,248	30,186	69,611	13,266
Travel	19,486	39,515	44,798	47,833
Communication	5,597	46,384	30,078	14,108
Professional/Technical				
Contracts <sup>6</sup>	292,688	29,114	165,538	10,629
Other <sup>3</sup>	<u>40,641</u>	<u>12,399</u>	<u>167,381</u>	<u>10,228</u>
Total	<u>\$ 593,223</u>	<u>\$ 512,593</u>	<u>\$ 995,984</u>	<u>\$ 671,145</u>

<sup>1</sup> The state's fiscal year is July 1 through June 30.

<sup>2</sup> The board also received appropriations of \$699,000 in 2005, 2006, and 2007 and \$829,000 in 2008. The increased appropriation was to cover additional staff and responsibilities of the board.

<sup>3</sup> Other expenditures include repairs, printing and advertising, computer and system services, employee development, and other operating costs. The board purchased a new licensing system in 2007.

<sup>4</sup> The board's staff increased from three employees in 2005 to twelve employees during 2008.

<sup>5</sup> The board moved into its current location in August 2005 and expanded its space in 2007.

<sup>6</sup> These amounts include the board's biennial payments to the services unit as professional/technical contracts.

Source: Minnesota Accounting and Procurement System as of August 12, 2008.

## Objectives, Scope, and Methodology

Our audit of the Board of Barber and Cosmetologist Examiners' licensing revenue, payroll, and other administrative expenditures focused on the following audit objectives for the period of July 1, 2004, through to June 30, 2008:

- Were the board's internal controls adequate to ensure that it safeguarded receipts and other assets, accurately paid employees and vendors in accordance with management's authorization, produced reliable financial information, and complied with finance-related legal requirements?
- For the items tested, did the board comply with significant finance-related legal requirements over its financial activities, including state and federal laws, regulations, contracts, and applicable policies and procedures?

To answer these questions, we interviewed board staff to gain an understanding of the controls related to the board's financial operations. In determining our audit approach, we considered the risk of errors in the accounting records and potential noncompliance with finance-related legal requirements. We also analyzed accounting data to identify unusual transactions or significant changes in financial operations for further review. In addition, we selected a sample of financial transactions and reviewed the supporting documentation to test whether the department's controls were effective and if the transactions complied with laws, regulations, policies, and contract provisions. We also gained an understanding of the controls provided by the services unit related to the financial activity processed on behalf of the board.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards 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 used various criteria to evaluate internal control and compliance. We used as our criteria to evaluate agency controls the guidance contained in the *Internal Control-Integrated Framework*, published by the Committee of Sponsoring Organizations of the Treadway Commission.<sup>2</sup> We used state laws, regulations, and contracts, as well as policies and procedures established by the departments of Finance and Employee Relations and Administration and the board's internal policies and procedures as evaluation criteria over compliance.

## Conclusions

The Board of Barber and Cosmetologist Examiners did not have adequate internal controls to safeguard receipts and sensitive assets. Approximately \$10,000 in license fee receipts are missing.

The board generally had adequate internal controls to ensure that it accurately paid employees and vendors in accordance with management's authorization and complied with finance-related legal requirements. However, it did not review some key payroll reports and did not comply with a key provision of the state's cell phone policy.

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<sup>2</sup> The Treadway Commission and its Committee of Sponsoring Organizations were established in the 1985 by the major national associations of accountants. One of their primary tasks was to identify the components of internal control that organizations should have in place to prevent inappropriate financial activity. The resulting Internal Control-Integrated Framework is the accepted accounting and auditing standard for internal control design and assessment.

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For the items tested, the board generally complied with finance-related legal requirements over its financial activities. However, it did not always deposit receipts over \$250 daily, as required by statute.

In addition, the services unit did not accurately record liability dates in the state's accounting system for the financial activity of the health-related licensing boards, including the Board of Barber and Cosmetologist Examiners. See Finding 2 in the report for the Board of Examiners for Nursing Home Administrators and the Health Licensing Boards – Administrative Services Unit.<sup>3</sup>

The following *Findings and Recommendations* provide further explanation about the exceptions noted above.

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<sup>3</sup> Office of the Legislative Auditor, Financial Audit Division [Report 08-26](#), Board of Examiners for Nursing Home Administrators and the Health Licensing Boards – Administrative Services Unit.

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## Findings and Recommendations

**The Board of Barber and Cosmetologist Examiners did not adequately safeguard or promptly deposit its receipts and did not reconcile receipts to licenses issued. The board could not account for approximately \$10,000 of license fee receipts.**

### Finding 1

The board had significant internal control weaknesses over license and fee receipts. These conditions set the stage for inaccurate recording of financial transactions and provided an opportunity for fraud. The board had the following weaknesses in its receipt process:

- The board did not adequately safeguard its receipts before deposit. The board held cash receipts in an unlocked box in a file cabinet until it forwarded the receipts to the services unit for entry into the state's accounting system and deposit into the bank. Although the board locked the cabinet, all staff had access to the key and had unsupervised and uncontrolled access to the receipts, including cash.
- The board did not reconcile its record of cash receipts to the deposits. Although the board used a ledger to track the movement of cash into and out of the box in the cabinet during the license application process, it did not use this record to verify that it deposited all receipts.
- The board did not reconcile receipts recorded in the state's accounting system to licenses issued, which were recorded on a subsidiary computer system. This reconciliation is necessary to ensure accurate reporting of license and fee receipts in the state's accounting system.
- The board did not always promptly deposit receipts. Statutes<sup>4</sup> require state agencies to deposit receipts greater than \$250 within one day. Of the 30 deposits tested, 25 were two days or more after the receipts were collected. The board held one receipt for 60 days before it was deposited.
- The board did not adequately secure access to the databases it previously used for cosmetology and barber applicants and licensees. The cosmetology database required a password to gain access; however, the passwords used were not secure. The barber database was not password protected. As of May 2008, the board had implemented a new computer

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<sup>4</sup> [Minnesota Statutes](#) 2007, Chapter 16A.275.

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system with adequate system security to maintain data on applicants and licensees.

Prior to our audit, the board's executive secretary discovered some errors and irregularities related to the cash receipt process. As a result, the executive secretary, with the assistance from the Health Licensing Boards – Administrative Services Unit, conducted a more detailed review of its receipt and licensing information for 2007 and 2008 and identified approximately \$10,000 of licenses issued that did not correspond to receipts deposited. Our audit substantiated that the money is missing. Because of the board's serious internal control weaknesses, we were not able to establish individual responsibility for the theft. We have referred our findings to the Office of the Attorney General and the Hennepin County Attorney's Office to consider whether sufficient evidence exists to pursue civil recovery and/or criminal prosecution.

#### *Recommendations*

- *The board should adequately safeguard receipts by keeping all receipts physically secure until deposit and limiting and monitoring access to receipts prior to deposit.*
- *The board should deposit receipts totaling \$250 or more on a daily basis, as required by statute.*
- *The board should reconcile receipts collected with deposits recorded on the state's accounting system.*
- *The board should reconcile receipts recorded on the state's accounting system with the total licenses issued.*
- *The board should work with the Office of the Attorney General and the Hennepin County Attorney's Office to recover missing funds.*

## **Finding 2**

### **The board did not verify its payroll transactions to key payroll reports.**

The board did not review key payroll reports to ensure the accuracy of wages and employee reimbursements and to verify that the accounting system posted payroll expenditures to correct accounts. State policy<sup>5</sup> requires the board to review these reports.

The board incurred about \$519,000 of payroll expenditures during fiscal year 2008, which represented approximately 77 percent of its total expenditures.

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<sup>5</sup> Department of Finance policy PAY0028.

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Because the board relied on the services unit to enter its bi-weekly payroll information, it is important that the board review the transactions to detect any erroneous or unauthorized transactions.

*Recommendation*

- *The board should review the key payroll reports to verify the accuracy of payroll transactions.*

**The board did not comply with a key provision of the state's cell phone policy.**

**Finding 3**

The board did not comply with the state's cell phone policy<sup>6</sup> requirement for departments to obtain and retain an acknowledgement of receipt form for each employee that it provided with a state cell phone. These forms give assurance to the agencies that the employees are aware of the state's policy and expectations for use of state cell phones. There were no forms on file with the board for any of its seven cell phones. The board incurred \$13,410 of cell phone expenses over the four-year audit period.

*Recommendation*

- *The board should obtain and retain written acknowledgements that employees have received a state-owned cell phone and understand state policies governing cell phone use.*

**The board did not have adequate inventory controls for its fixed assets and sensitive items.**

**Finding 4**

The Board of Barber and Cosmetologist Examiners did not conduct a physical inventory of its fixed assets or sensitive items during fiscal years 2005 through 2008. The Department of Administration's *Property Management User Guide*<sup>7</sup> requires state agencies to conduct a physical inventory of capital assets at least biennially.

The board relies on the services unit to maintain its master schedule of fixed assets. The services unit records additions and deletions to fixed asset records based on the financial activity it processes. The board, however, is ultimately responsible for its assets and to ensure the accuracy of the fixed asset schedule.

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<sup>6</sup> Department of Administration Statewide Policy: Appropriate Use of Electronic Communication and Technology.

<sup>7</sup> Department of Administration Policy ADMIN 06-03 *Property Management User Guide*.

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Without an accurate inventory of fixed assets and sensitive items, there is a greater risk that theft or errors could occur and not be detected. In addition, a regular inventory would assist the board in verifying the accuracy of the financial reporting of its assets.

*Recommendation*

- *The board should improve its security and safeguarding over its fixed assets by conducting periodic physical inventories and spot checks of fixed assets and sensitive items.*
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October 17, 2008

Mr. James Nobles, Legislative Auditor  
Office of the Legislative Auditor  
Room 140 Centennial Building  
658 Cedar Street  
St. Paul, MN 55155-1603

Dear Mr. Nobles:

This is a formal response to the Office of the Legislative Auditor audit results for the Board of Barber and Cosmetologist Examiners during the period of July 1, 2004 through June 30, 2008.

The Board acknowledges and agrees with all aspects of the audit and recognizes that it is our responsibility to implement the recommendations that your office has suggested.

The Board of Barbers merged with the Cosmetology Division of the Department of Commerce in July 2004. The Board of Barbers, with minimal increase in staffing went from approximately 4,000 licensees to 40,000 licensees. Further, the Board had a change in the Executive Secretary position that has resulted in significant changes to the Board's operations. This includes: hiring additional staff, implementing an online database, and streamline all licensing processes in order to manage the additional 36,000 licensees resulting from the merger.

The Board has addressed and made significant progress in all areas relating to the audit findings, including establishing internal controls and procedures for the safeguarding of all receipts.

The Board has responded to all of the findings and recommendations listed in the audit results. You will find these responses below.

**Finding 1**

The Board of Barber and Cosmetologist Examiners did not adequately safeguard or promptly deposit its receipts and did not reconcile receipts to licenses issues. The board could not account for approximately \$10,000 of license fee receipts.

- 1.1 The board did not adequately safeguard its receipts before deposit.
- 1.2 The board did not reconcile its record of cash receipts to the deposits.
- 1.3 The board did not reconcile receipts in the state's accounting system to licenses issues, which were recorded on a subsidiary computer system.

- 1.4 The board did not always promptly deposits receipts.
- 1.5 The board did not adequately secure access to the databases it previously used by the board for cosmetology and barber applicants and licensees.

### **Audit Recommendation**

- 1.1 *The board should adequately safeguard receipts by keeping all receipts physically secure until deposit and limiting and monitoring access to receipts prior to deposit.*
- 1.2 *The board should deposit receipts totaling \$250 or more on a daily basis, as required by statute.*
- 1.3 *The board should reconcile receipts collected with deposits recorded on state's accounting system.*
- 1.4 *The board should reconcile receipts recorded on the state's accounting system and the total licenses issued.*
- 1.5 *The board should work with the Office of the Attorney General and the Hennepin County Attorneys Office to recover missing funds.*

### **Agency Response**

The Agency agrees with the findings and has addressed each finding and recommendation below.

- 1.1 The Board has purchased and is using a safe secured in a locked office with access limited to two staff members (Program Manager and Executive Secretary) to safeguard cash. Further, the Board is ensuring that all non-cash payments received are secured at all times in a locked file cabinet when not being processed.
  - The Board has also changed the cash intake process by designing a ledger that is pre-printed with receipt numbers and fields to ensure all receipts are properly recorded.
  - The Board has separated the receipt books for cash receipts and other receipts. These books are easily identifiable by staff as they are different sizes and labeled.
  - The Board is now requiring that a duplicate copy of the cash receipt is attached to the application.
  - The Board has created specific and pre-labeled envelopes to place the cash into when receiving it.
  - The Board has created a policy for all staff to follow in the instance when the Program Manager and Executive Secretary are out of the office when cash is accepted. This includes an email notification to both the Program Manager and Executive Secretary.
  - The Board has modified the database to ensure that any type of payment received cannot be deleted by unauthorized staff.
  - The Board has modified the database to auto populate deposit numbers, rather than staff manually entering deposit numbers for each receipts.
  - The Executive Secretary will be auditing multiple applications per month to ensure that the intake process of any receipts is followed correctly.

- 1.2 The Board has already begun compliance with this statute requirement. In May 2008, the Board implemented a new database that logs receipts and applications simultaneously. Due to changes in the database, the Board had modified its receipt intake process in June 2008 to comply with this statute requirement. Funds are promptly deposited daily, if not twice per day when needed.
- 1.3 The Board currently audits all aspects of deposits against the state's accounting system. This includes verification of initial deposit by matching the receipt report, deposit detail ledger, bank deposit slip, and calculator tape. Further, the Board reconciles the daily deposits to the State's accounting system and the bank's receipt. Lastly, the Board reconciles the daily deposits to a monthly deposit report that is generated from the state's accounting system.
- 1.4 The Board will be verifying on a quarterly basis within each fiscal year the amount of receipts recorded to the total amount of licenses issued.
- 1.5 The Board is already working with the Minnesota Management and Budget Division to pursue an investigation regarding the missing funds. The Board will be contacting the Office of the Attorney General and the Hennepin County Attorneys Office to recover the missing funds.

#### **Responsible Parties**

Merrill Davis, Rebecca Gaspard, Nancy Mayberry, Kris McCarney, Deanna Porter, Laura Montez, Gina Stauss Fast

#### **Estimated Completion Date**

The Board has implemented all recommendations and is pursuing all available means to recover the missing funds.

#### **Finding 2**

The board did not verify its payroll transactions to key payroll reports.

#### **Audit Recommendation**

*The board should review the key payroll reports to verify the accuracy of payroll transactions.*

#### **Agency Response**

The board will work with Minnesota Management and Budget and the Administrative Services Unit to ensure that the Board is verifying the correct payroll reports. The Board has been verifying the Self-Service Time Entry Reports, but will verify those reports against appropriate state payroll system reports.

#### **Responsible Parties**

Rebecca Gaspard, Kris McCarney, Gina Stauss Fast

**Estimated Completion Date**

The Board will be trained by November 30, 2008 by the Administrative Services Unit and will retroactively conduct auditing as necessary.

**Finding 3**

The board did not comply with one aspect of the state's cell phone policy.

**Audit Recommendation**

*The board should obtain and retain written acknowledgements that employees have received a state-owned cell phone and understand state policies governing phone use.*

**Agency Response**

The Board has already given each employee that carries a state-owned cell phone a new copy of the Statewide Electronic Communication Policy. The Board has reviewed all aspects of the Policy that include state-cell phone usage with employees who carry a state-owned cell phone. Lastly, the Board has obtained written acknowledgements from the employees of their receipt of a state-owned cell phone and their understanding of state policies governing phone use. The signed statement is located in their personnel file.

**Responsible Parties**

Rebecca Gaspard, Kris McCarney, Gina Stauss Fast

**Estimated Completion Date**

Completed

**Finding 4**

The board did not have adequate inventory controls for its fixed assets and sensitive items.

**Audit Recommendation**

*The board should improve its security and safeguarding of fixed assets by conducting periodic physical inventories and spot check of fixed assets and sensitive items.*

**Agency Response**

The Board currently has a fixed assets inventory list that is housed in our Administrative Services Unit. The Board will request in January of each year for a list of our fixed assets and conduct a thorough physical inventory of this list.

The Board will also develop its own inventory list to conduct periodic inspections approximately twice per year. This will allow to board to ensure that fixed assets and sensitive items are safeguarded.

**Responsible Parties**

Rebecca Gaspard, Kris McCarney, Gina Stauss Fast, Administrative Services Unit

**Estimated Completion Date**

The board will conduct its first inventory in January 2009, with two additional periodic inspections each calendar year.

On behalf of the Board of Barber and Cosmetologist Examiners, thank you in advance for your attention to the Board's responses. The Board of Barber and Cosmetologist Examiners has acted quickly to resolve any findings and to implement all recommendations. The Board of Barber and Cosmetologist Examiners intends to comply with all recommendations at a minimum, if not exceed your office's expectations.

Sincerely,

A handwritten signature in blue ink, consisting of several loops and a long horizontal stroke extending to the right.

Gina Stauss Fast  
Executive Secretary