June 13, 2017

Office of Internal Auditing

College and University Bookstores

Internal Control and Compliance Audit

Reference Number 2017-02

Report Classification: Public

MINNESOTA STATE

30 East 7th Street
St. Paul, MN 55101

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June 13, 2017

Dear Members of the Minnesota State Board of Trustees,
Chancellor Steven J. Rosenstone, and
Vice Chancellor Laura King

This report presents the results of our internal control and compliance audit of College and University Bookstores for fiscal years 2014, 2015, and 2016. Eight colleges and universities were selected for testing that focused on key internal controls related to safeguarding cash, riskier transactions, and textbook buyback operations.

The audit report contains six findings and related recommendations to assist college and university management in improving business processes, controls, and accountability. The results of the audit were discussed with college, university, and system office leadership on May 2, 2016.

The audit was conducted in conformance with the International Standards for the Professional Practice of Internal Auditing.

We appreciate the excellent cooperation and assistance that we received from college and university employees.

Sincerely,

David J. Pyland

Dave Pyland, CPA
Executive Director

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Report Summary

Audit Scope

We focused on current internal controls and the financial activity from fiscal years 2014, 2015, and 2016. We reviewed controls at eight institutions, which included seven colleges and one university.

Conclusion

Opportunities to improve processes and strengthen controls were identified in several areas including safeguarding and accounting for bookstore receipts (findings 1 and 2), managing point-of-sale system access (finding 3), textbook buyback programs (findings 4 and 5), and purchasing inventory and selling unneeded textbook inventory (finding 6).

Findings

1. Bookstores lacked a variety of key controls to help ensure receipts were adequately safeguarded.
2. Bookstores did not separate duties related to cashiering and certain high risk cash-related transactions. In addition, some bookstores did not retain documentation to support high risk transactions.
3. Bookstores did not adequately manage employee access to their point-of-sale (POS) systems.
4. Bookstores may be incurring additional risk when they agree to hold bookstore buyback funds for their wholesale vendors.
5. Bookstores lacked methods to adequately monitor and account for textbook buyback commissions. In addition, commission receipts were not deposited in timely manner.
6. Four bookstores have not adequately separated duties related to purchasing and five bookstores did not have sufficient controls related to selling unneeded textbook inventory to wholesale vendors.

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Background

During fiscal year 2016, 30 Minnesota State colleges and universities operated their own bookstores while six contracted with either Follett Higher Education Group or Barnes and Nobles Education, Inc. for on-campus bookstore operations. One college bookstore is operated by their foundation. Bookstores are an important part of a college campus because they have the textbooks, supplies, and other materials needed by students. Many also sell college branded clothing and gifts, snacks, and other convenience items like postage, movie tickets, or city bus passes.

Minnesota State bookstores operate textbook "buyback" programs to purchase used textbooks from students. Many offer buyback times at the end of the semester, with some also conducting them during the semester. Colleges and universities work with wholesale vendors for their buyback program. The vendors will come onto campus and purchase the used textbooks from students and pay the college or university commission. The buybacks also offer the institution an opportunity to increase its used books inventory by purchasing books from the wholesale vendor.

Minnesota State does not have a common point-of-sale (POS) system to assist colleges and universities in managing their retail environments such as bookstores. Instead, most institutions have purchased their own POS system to manage their textbook and supplies purchasing, inventory, and sales. In June 2016, we surveyed the 37 colleges and universities to determine what POS system the institutions used. Of the 30 institutions that operate their own bookstore, the majority utilized one POS system, five used another, and one use a third system. One institution did not use a POS system in its bookstore. These systems do not interface with Minnesota State's accounting system so college and university staff enter manual summary transactions into the accounting system. In addition, if students want to use financial aid to pay for books and supplies, institutions must determine a process to record student POS charges on the student's ISRS account.

We included bookstore receipts in our audit scope because of the number of past audit findings and fraud incidents.

Table 1 shows the total cash-basis receipts for college and university operated bookstores during fiscal year 2016 was nearly $60 million.

Table 1: College and University Operated Bookstore Receipts
Fiscal Year 2016

Institution	2016 Revenue	# Stores	Bookstore also Serves as Primary Collection Point for Tuition and Fees
Normandale Community College	$4,710,061	1	
Winona State University	4,473,175	1	
Anoka-Ramsey Community College	4,266,999	2	Yes (one location)
Century College	3,840,282	1	
Minnesota State Community and Technical College	3,716,645	1	Yes
Minneapolis Community and Technical College	3,383,157	4	
Rochester Community and Technical College	3,297,669	1	
North Hennepin Community College	3,058,175	1	
Saint Paul College	2,993,446	1	
Minnesota State University Moorhead	2,519,945	1	
Lake Superior College	2,375,438	1	
St. Cloud Technical and Community College	2,306,719	1	
Inver Hills Community College	2,294,903	1	
Hennepin Technical College	2,142,914	2	
Ridgewater College	1,874,792	2	
Minnesota West Community and Technical College	1,630,050	3	Yes (two locations)
Central Lakes College	1,479,010	2	Yes
Northland Community and Technical College	1,401,834	2	
Riverland Community College	1,393,923	3	Yes (backup position)
South Central College	1,240,966	2	Yes
Dakota County Technical College	981,133	1	
Anoka Technical College	946,628	1	Yes
Minnesota State College - Southeast Technical	920,280	2	Yes
Itasca Community College	689,485	1	
Hibbing Community College	526,516	1	
Mesabi Range College	449,217	1	
Fond du Lac Tribal and Community College	363,840	1	
Pine Technical and Community College	360,979	1	Yes (backup position)
Vermilion Community College	209,132	1	
Rainy River Community College	150,756	1	
Totals	$59,998,071		

Source: FY16 Financial Statements – Bookstore Fund

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Bookstore Collaboration Project

Five colleges are participating, and two more are expected to join soon, in a bookstore collaboration and shared service project. For an annual fee, college and university bookstores can join the collaboration and receive support for their bookstore operations. For example, the collaboration allows bookstores to consolidate and share a single POS system in a multistore environment and share a variety of services. The stores may collaborate on a variety of things including purchasing and textbook buyback inventory, training, marketing, ecommerce models, and use common processes for uploading student financial aid charges to ISRS. The collaboration intends to determine best practices for areas such as cash and inventory controls and then work with bookstores to implement the controls. Finally, the collaboration plans to help institutions implement new technologies such as direct digital content which allow students to access digital materials at a lower cost than traditional textbooks as well as having those materials immediately available to students versus delays that may occur when accessing financial aid funds.

Audit Objectives, Scope, Methodology, and Conclusion

Audit Objectives

The objectives for this audit were to answer the following questions:

- Did colleges and universities have policies, processes, and practices to mitigate bookstore fraud risks?

- Do opportunities exist for management to improve practices to make them more effective and efficient?

Audit Scope

Our audit reviewed current internal controls and the following activities for fiscal years 2014, 2015, and 2016. Areas of focus included:

- Controls related to safeguarding cash.
- Controls related to riskier transactions such as voids, returns, and price adjustments.
- Controls related to book buy-back programs.

Our audit did not review other aspects of bookstore operations such as purchasing or pricing practices, payment card industry (PCI) compliance, or whether bookstores were profitable. Our audit also did not include the bookstore collaboration project.

Audit Methodology

We surveyed all 37 institutions to gain an understanding of the level of participation in bookstore operations. For the eight institutions selected for review, we interviewed college staff and reviewed relevant documentation to gain an understanding of the institution's internal controls. We considered risks of fraud and errors, and potential noncompliance with finance-related legal requirements. We reviewed employee computer system access to identify the transactions staff can initiate, approve, or process to determine whether access was based on need and duties were adequately separated. In addition, we selected a sample of transactions and reviewed supporting documentation to test whether controls were effective and transactions complied with laws, regulations, policies, and contract provisions.

Audit Conclusion

Opportunities to improve processes and strengthen controls were identified in several areas including safeguarding and accounting for bookstore receipts (findings 1 and 2), managing point-of-sale system access (finding 3), textbook buyback programs (findings 4 and 5), and purchasing inventory and selling unneeded textbook inventory (finding 6).

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Audit Findings and Recommendations

1. Bookstores lacked a variety of key controls to help ensure receipts were adequately safeguarded.

Bookstores generally collect and deposit receipts on a daily or near daily basis. They also maintain starting cash balances for their cash registers and many maintain a "change fund" in case it needs to change larger bills into smaller bills or need additional coin. During our audit, we looked at physical controls related to cash receipts and noted the following.

- Security cameras: One institution did not utilize security cameras in their bookstores. Institutions were inconsistent with how long they retained security video and not always based on risks, best practices, or potential requirements. Two institutions retained security video for only seven days and one institution's retention was limited to current disk space because their system had crashed approximately six months prior to our review. The remaining four institutions retained their video surveillance for at least 30 days. Security cameras are often used in retail to deter theft of inventory and employee dishonesty and video may be helpful determining the cause of cash shortages. Minnesota State does not have a requirement related to retention of video surveillance.

- Three institutions counted cash in areas where people walking in public areas, such as the halls, could view counting activities. Institutions should count cash in areas that not visible to the public.

- Safes: One of eight institutions did not use a safe. Instead, the institution used a locked file cabinet to store bookstore cash and receipts. While the other seven used safes, practices could be improved to strengthen controls. For example, two of the safes were small and not bolted to the floor and another was kept unlocked throughout the day. The unlocked safe was stored in an office that remained locked throughout the day; however, at least six employees had keys to the room and there is not video cameras to record activity in the room and safe. In addition, six of the seven safes had not had their combination locks changed in more than five years. Safe combinations should be periodically changed, especially when an employee that knows the safe combination leaves employment.

- Shared cash drawers: None of the bookstores in our review required cashiers to use separate cash drawers. Instead, cashiers shared cash drawers throughout the day; when drawers are shared, it difficult to determine responsibility if money were to go missing.

- Cash count documentation: Three institutions did not document their denomination counts when they counted cash at the end of the day. Instead, the institution documented the total 'cash' for the day. Documenting denomination counts can assist management in looking for errors or irregularities.

- Chain of custody and starting cash: We noted cash control issues at four institutions when they did not count their cash at the beginning of the day and when it changed hands.

    - Two bookstores did not have their cashiers count their cash at the beginning of the day.
    - Two bookstores did not have their cashiers count their cash drawers at the end of day. Instead, a separate person counted their cash drawers.
    - Two bookstores did not maintain a chain of custody when the receipts given to the business office for deposit were not immediately counted by the business office staff.

  Cashiers should count and document their cash drawers at the start and end of the day to verify their cash balances, even if the drawer is given to someone at the end of the day to balance and reconcile sales activity. When cash changes hands, money should be re-counted and counts documented to verify persons agree to the amounts given. Counting cash takes a few minutes of time; however, documenting the counts at start, end, and when drawers change hands is beneficial in identifying when funds may have gone missing.

- Change funds: Five institutions maintained change funds in their bookstore and none of these were counted on a daily basis. Two counted the change fund weekly and one counted it whenever it was accessed. However, multiple persons have access to change fund throughout the day. When change funds are not counted frequently, institutions would have difficulty investigating missing funds.

- Surprise counts: Six institutions did not conduct routine surprise counts of bookstore starting cash banks and change funds. One additional institution indicated surprise counts are conducted, but it did not retain documentation related to the counts. Periodic independent surprise counts of starting cash and change funds can be effective controls in preventing theft or mismanagement of funds.

Recommendations

- *Institutions should improve physical security by:*
    - *installing security cameras in the bookstore, including every location receipts are collected, counted, and stored,*

- *reviewing risks, best practices, and any relevant requirements to establish standards and ensure video is retained for an appropriate length of time, and*
- *counting cash in areas that are not in public view.*

- *Institutions with bookstore safes should:*
  - *consider bolting small safes to the floor to increase security of safe,*
  - *determine if safe combinations can be changed and, if possible, periodically change them, especially when staff that know combination leave employment with the bookstore, and*
  - *keep safes locked throughout the day.*

- *Institutions should improve cash controls by:*
  - *maintaining separate cash drawers,*
  - *counting cash drawers at the start and the end of each day,*
  - *maintaining documentation of cash counts, including denomination counts,*
  - *counting cash when it changes hands, maintaining a record related to the chain of custody of cash, and*
  - *counting change funds daily.*

- *Institutions should perform periodic surprise cash counts of bookstore funds (including cash drawers and any applicable change funds or book buyback funds). Surprise cash counts should be performed by a person independent of the bookstore and counts should be documented and retained according to record retention schedules.*

2. Bookstores did not separate duties related to cashiering and certain high risk cash-related transactions. In addition, some bookstores did not retain documentation to support high risk transactions.

Cash operations are inherently risky but compounded when there are few bookstore employees to allow certain duties or tasks to be separated or independently reviewed. Transactions, such as refunds or voids, are considered higher risk transactions because without adequate oversight, theft can occur and may not be detected.

We reviewed controls over higher risk transactions at each of the eight bookstores. Some institutions required a second approval for transactions such as returns. However, the second approval was largely a procedural manual control rather than a system control to prevent the employee from performing the transactions without the second approval. Some institutions had staff review high risk transactions at the end of the day or the next morning. However, as noted in Table 2, evidence did not exist for some of the reviews and most of the reviews were performed by persons that were not independent of the cashiering process. At one institution, because the reviewer did not receive a system generated report related to the transactions he reviewed, he was unable to verify he had actually received documentation to support all returns that occurred that day.

Table 2: Review of High Risk Transactions

Type of Transaction	# of Institutions		
	Did not Develop Review of High Risk Transactions	Review Not Independent	Review not Documented
Refunds	4	3 (a)	0
Post sale voids	3	2	1
Price overrides	4	4	2

Source: Auditor prepared

Note (a): One institution performed an independent review of refunds issued by check. However, reviewer is unable to verify documentation for all refunds processed have been included.

Finally, during our review of risky transactions, we noted three institutions had not retained documentation to support the risky transactions we selected to review. Two institutions had not retained the bookstore's copy of the cash register slips documenting refunds that occurred on the days we selected to test. One institution did not retain a form to explain the purpose of a voided transaction.

Recommendations

- *When institutions are not able to separate duties of performing high risk transactions with handling cash, mitigating reviews should be performed by employees that are independent of the process, such as an employee in the business office or a different unit. Institutions should ensure they have methods, such as reports, to ensure they have all high risk transactions to review.*

- *Institutions should ensure that documentation exists to support high risk transactions such as refunds or voids. For example, institutions should retain the store copy of refunds slips to document the items refunded and authorization of the refund.*

3. Bookstores did not adequately manage employee access to their point-of-sale (POS) systems.

Seven of the institutions we reviewed used POS systems to process sales transactions. We reviewed access to six of the POS systems to determine if employees were provided separate login IDs to access the system, access was limited to current employees, and the roles assigned to employees were based on their job responsibilities. We noted the following issues at the six institutions we reviewed:

- None of the institutions documented periodic POS system access reviews to demonstrate access was limited to current employees and their access levels or roles were appropriate based on job duties. Institutions indicated security was generally reviewed each semester; however, documentation was not retained to document the reviews occurred.

- One college did not require cashiers to use separate logon IDs when they accessed the POS system and a second college maintained three generic login ids such as "cashier" or "manager." When separate login IDs are not used, institutions have a difficult time determining who processed specific transactions.

- One institution did not remove POS system access timely when it did not remove access for an employee who had left employment about one month prior and it did not deactivate security access for 19 temporary employees that generally return each semester.

- Two colleges assigned security roles to employees that provided more access than needed to perform their job responsibilities. The first college provided POS system access to an employee that did not use the system as part of their job responsibilities. The second college provided some employees access to process transactions they did not normally process. For example, three employees were provided access to POS system set-up that was not needed and students were provided access to process returns and book buybacks when management indicated they were not allowed to perform these tasks.

Recommendations

- *Institutions should develop procedures to ensure it:*
  - *performs periodic reviews of the POS security access,*
  - *retains documentation of their POS security reviews,*
  - *removes security access timely when employees, including temporary employees, leave employment with the bookstore, and*
  - *provides access to employees based on job responsibilities.*

- *Institutions should require that employees use separate login IDs to process POS system transactions.*

4. Bookstores may be incurring additional risk when they agree to hold bookstore buyback funds for their wholesale vendors.

As discussed earlier, institutions work with wholesale vendors for their textbook buyback programs. The colleges and universities can earn a higher commission if it utilizes college employees to operate the buyback, rather than utilizing wholesale vendor employees. During our audit, we noted that regardless of whose employees were utilized to run the buyback programs, the wholesale vendor's funds were used to fund the buybacks, and, in most cases, kept at the college or university overnight. Our institutions may be incurring a liability when they agree to hold wholesale vendor buyback funds.

As noted in Table 3, all but one institution used vendor funds for their bookstore buyback and kept the funds overnight for the vendor throughout the buyback period. The range of funds held on behalf of vendors started at $1,500 for funds held during the semester and reached $250,000 at one institution for end of semester buyback. Two institutions indicated the vendor had provided its own safe to store the end of semester buyback funds; however, college employees at one institution knew the safe combination.

Table 3: Funds used for Book Buyback Operation

Buyback Period	# of Institutions			Range of Vendor Funds
	Using Vendor Funds for Buyback	Vendor funds kept Bookstore Safe	Vendor funds kept in Business Services Office Safe	
During the semester	7 (a) (b)	6 (b) (c)	0	$1,500 - $9,500
End of semester	8	5 (c)	2	$35,000 - $250,000

Source: Auditor prepared

Notes:
(a) One institution does not operate a buyback during the semester.
(b) One institution uses vendor funds for the opening term buy but then uses their own funds for the remainder of the semester; counted as vendor funds kept in college bookstore because a portion is handled in this manner.
(c) One institution's vendor brought funds back and forth to college because the bookstore does not have a safe. Two institutions' vendors kept their own safe on the college campus; however, college employees at one of these institution knew the vendor's safe combination.

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If buyback funds were to go missing, the colleges may be liable for the missing funds. Institutions have limited employee theft insurance coverage, up to $25,000. However, as noted in table 3, the $25,000 limit is below the initial value of semester end buyback funds. Also, it is not clear whether the institution would be able to utilize the insurance coverage when non-college employees also have access to the funds. Prior to this audit, our office reviewed an incident at one college where the college realized their cash balance for their during-the-semester buyback fund was approximately $1,000 lower than it should have been; the college replaced the missing cash.

Three institutions implemented additional controls related to the handling of end of semester vendor buyback cash. For example, two vendors kept cash in locking cash bags. One institution had both a college and vendor employee count cash at the start and end of the day to jointly verify cash balances. Without verifying the vendor's cash balances, a college would likely be unable to dispute false claims of missing cash. College employee verification of cash could limit its liability if funds went missing.

Recommendations

- *Institutions should work with the system office's risk management staff to determine what circumstances crime insurance coverage may be available for wholesale vendor funds that may go missing on institution's property. After determining coverage, institutions should work with risk management to determine if they should continue to hold funds for their vendors.*

- *If institutions continue to hold funds for their vendors, they should develop procedures to:*
    - *Conduct daily cash counts of buyback funds, if applicable, and*
    - *jointly count end of semester buyback funds to verify daily cash balances.*

5. Bookstores lacked methods to adequately monitor and account for textbook buyback commissions. In addition, commission receipts were not deposited in timely manner.

Depending on contracts with their wholesale vendors, bookstores could receive a combination of textbook buyback commissions as direct payments or credit memos for future purchases or equipment upgrades. Our review noted issues related to how institutions received and accounted for buyback commission revenue.

- One institution was not aware it could obtain credit memos to be used for anything other than equipment upgrades.

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- One institution had not developed methods to track their credit memos for equipment upgrades or purchases to ensure the funds were used before they expired.
- One institution indicated that rather than receive a check, the wholesale vendor paid the college by reducing the amount the college owed the vendor for holding its buyback cash.
- Six institutions indicated their commission buyback funds are mailed to the bookstore, rather than the business office. To provide better separation of duties, commission checks should be mailed to their businesses services office.
- Five of 17 deposits were not made timely. One deposit was approximately four days after receipt of the check with the other four deposits spanning 10 to 30 days after the check was received.
- All bookstores were able to receive commission as credit memos for future purchases or equipment upgrades. All eight institutions recognized credit memos as a reduction to costs of goods sold, rather than commission revenue. Recording commission revenue in this manner understates both commission revenue and cost of goods sold.

Recommendations

- *Institutions should develop procedures to monitor textbook buyback commissions. The procedures should ensure institutions:*
    - *properly record all forms of bookstore commissions as revenue,*
    - *record and monitor credit memos to ensure they are utilized,*
    - *direct commission revenue to be mailed directly to the business office, and*
    - *deposit commission revenue in a timely manner.*

6. Four bookstores have not adequately separated duties related to purchasing and five bookstores did not have sufficient controls related to selling unneeded textbook inventory to wholesale vendors.

Four institutions did not properly separate the functions of purchasing and receiving bookstore inventory. When the functions of purchasing and receiving the inventory are not separated, institutions are at risk of processing payments for fictitious inventory, unauthorized items, or items purchased for personal use.

Five bookstores did not have a formal approval process related to selling obsolete or extra inventory to wholesale vendors. Without a formal approval process to sell inventory outside the normal retail process, the institution is at risk that items may be sold for personal gain. An independent review of inventory adjustments may identify irregularities;

however, four of the five institutions did not have a review process related to inventory adjustments.

Recommendations

- *Bookstores should separate duties for purchasing and receiving bookstore inventory. When bookstore staff is small, institutions should explore utilizing staff from other departments to assist in this process.*

- *Bookstores should develop procedures to approve the sale of textbooks to wholesale vendors.*

Management's Response

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June 5, 2017

Board of Trustees
Chancellor Steven Rosenstone
Minnesota State Colleges and Universities

The Office of Internal Auditing has completed an internal control and compliance audit of bookstores at seven colleges and one university. This work was undertaken as an approach to auditing particular business cycles across the colleges and universities. We view the completed audit as a helpful contribution to our understanding of the system and the college and university control environments.

The audit identified some instances of internal control deficiencies at some colleges and the university. Management of these colleges and the university have already addressed at least half of these findings. Additional follow up work will continue in the upcoming months, with the majority of the remaining findings to be addressed by this fall.

The colleges, university, and the system office view the completed audit as helpful and informative in better understanding institutional policies and procedures currently in place to provide strong internal controls within the bookstores.

The auditor's findings and recommendations are a welcome platform for engaging our colleges and universities in continuous improvement in the area of bookstore internal controls. The report included six audit findings, but the overall conclusion is the control environment is sufficient and serves as assurance to the Board of Trustees, Chancellor Rosenstone, and the public that care and stewardship are being exercised in the campus bookstores.

Warm regards,

Laura M. King
Vice Chancellor - CFO