



STATE OF MISSISSIPPI
OFFICE OF THE STATE AUDITOR
STACEY E. PICKERING
AUDITOR

January 9, 2018

Limited Internal Control and Compliance Review Management Report

Dorothy Ennis
President, Mississippi State Board of Cosmetology
P.O. Box 55689
Jackson, MS 39296

Dear Ms. Ennis:

Enclosed for your review are the Limited Internal Control and Compliance Review Findings for the Mississippi State Board of Cosmetology (Cosmetology) for Fiscal Year 2016. In these findings, the Auditor's Office recommends the Board:

1. Strengthen Internal Controls Over Bank Accounts and Cash Receipts to Ensure Compliance with State Law;
2. Issue Licenses Timely and Accurately;
3. Strengthen Board Oversight;
4. Strengthen Controls to Ensure Compliance with State Law over Travel;
5. Strengthen Controls to Ensure Compliance with State Law over Accrued Leave;
6. Strengthen Controls to Ensure Compliance with State Law over Procurement Card Purchases;
7. Ensure Board Meetings are Held and Recorded in Compliance with State Law.

It is our understanding that the Executive Director for the period of audit has been replaced and that the new Executive Director has begun implementing policies and procedures to correct the issues raised in this report. To that end, please review the recommendations and submit a plan to implement them or a description of corrective action that has already been implemented by February 1, 2018. The enclosed findings contain more information about our recommendations.

During future engagements, we may review the findings in this management report to ensure procedures have been initiated to address these findings.

This report is intended solely for the information and use of management, individuals charged with governance and Members of the Legislature and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

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I hope you find our recommendations enable the Mississippi State Board of Cosmetology to carry out its mission more efficiently. If you have any questions or need more information, please contact me.

Sincerely,

STEPHANIE PALMERTREE, CPA, CGMA
Director, Financial and Compliance Audit
Office of the State Auditor

The Office of the State Auditor has completed its limited internal control and compliance review of the Mississippi State Board of Cosmetology for the year ended June 30, 2016.

Our procedures and tests cannot and do not provide absolute assurance that all state legal requirements have been met. Also, our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be weaknesses. In accordance with Section 7-7-211, Miss. Code Ann. (1972), the Office of the State Auditor, when deemed necessary, may conduct additional procedures and tests of transactions for this or other fiscal years to ensure compliance with legal requirements.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

We identified certain deficiencies that we consider to be *material weaknesses* in internal control and certain deficiencies that we consider to be *significant deficiencies* in internal control. These matters are noted under the headings **MATERIAL WEAKNESSES**.

In addition, while performing our review, we noted certain instances of noncompliance with State laws that require the attention of management. These matters are noted under the heading **INSTANCES OF NONCOMPLIANCE WITH STATE LAW**.

MATERIAL WEAKNESSES AND INSTANCES OF NONCOMPLIANCE WITH STATE LAW

Finding 1: The Mississippi Board of Cosmetology Should Strengthen Internal Controls Over Bank Accounts and Cash Receipts to Ensure Compliance with State Law.

Executive Summary: The former Executive Director and employees under his purview did not deposit any license or fee revenue from approximately October 2016 until approximately June 2017. Cash, money orders, checks, etc. had been held by employees of Cosmetology for months without any accurate logs, receipts, etc. Additionally, when Investigators from the Office of the State Auditor arrived to ensure that cash receipts were counted and deposited, they found numerous receipts without cash attached. Temporary employees were hired to help count the cash receipts and these temporary employees were often left with cash with no supervision or controls. The office space was not adequately monitored or locked during off business hours.

The amount of loss of cash receipts and license revenue due to fraud, waste, abuse and additional potential criminal activity is unquantifiable without a detailed, exhaustive forensic audit of Cosmetology.

Cosmetology did not properly abide by state laws regarding bank accounts and also did not report bank information to the Office of the Treasurer timely.

In order to ensure that State assets (i.e. cash) are effectively and efficiently managed, timely and adequate supervision and control of those assets must be implemented.

Recommendation: We recommend the Mississippi Board of Cosmetology implement controls, policies, and procedures over cash to ensure compliance with laws over their bank accounts and assets. Stringent record keeping should be implemented to ensure that cash is not misappropriated or misplaced.

Additionally, account balances should be maintained as authorized by the Department of Finance and Administration (DFA) and the Office of the State Treasurer (Treasury), and transfers to the State Treasury should be made timely in accordance with state law.

Lastly, we recommend that the Investigations Division at the Office of the State Auditor review activity regarding cash receipts at the Mississippi Board of Cosmetology to determine if criminal activity regarding theft of funds has occurred. Further, we recommend Cosmetology secure the services of a forensic auditor to determine the amount of misappropriated assets.

Detailed Analysis:

Mississippi Annotated Code (1972) Section 7-9-21, requires agencies to transfer monies deposited in agency clearing bank accounts to the State Treasury within two days and requires public funds to be deposited into the state treasury by the end of the next business day following the day that funds are collected.

Mississippi Annotated Code (1972) Section 7-9-12, allows agencies to request authorization from the Department of Finance and Administration (DFA) and the Office of the State Treasurer (Treasury) to open a bank account to serve as a collection or clearing account. Each account established shall have a maximum balance to be fixed by the Treasury.

Mississippi Annotated Code (1972) Section 27-105-5(6)(b), requires a public depositor to notify the State Treasurer, no later than thirty days after the end of the fiscal year, of its bank accounts that it has with a qualified public depository, including the balance in the accounts as of the fiscal year end.

Good internal controls require cash receipts to be deposited into the agency's bank account on the day of receipt to reduce the likelihood of loss or theft. Failure to deposit receipts daily could result in the loss of receipts and interest revenue by the state and increases the risk of theft and/or misplacement of funds and noncompliance with State law. Good internal controls also require documentation of cash received so that an adequate audit trail is in place.

Finding Detail:

During our review of internal controls over bank accounts and cash receipts at Cosmetology, we noted the following problems:

- Cash receipts totaling over \$368,000 had not been deposited by employees of Cosmetology for approximately nine months. Cash, money orders, checks, etc. were found stuffed in drawers and filing cabinets. Receipts, with money attached, were left unsecured on desks and were not logged or accounted for when received. When questioned by auditors as to why cash receipts had not been deposited, employees indicated that a new system was in place and that no employee knew how to enter the receipts in the system.
- Cash appeared to be missing from several receipts. Staple holes indicated that money had been initially stapled to the receipt and removed subsequently. Employees could not account for the whereabouts of the missing funds.
- Checks were often months old and some were past expiration dates. When the checks were deposited into the bank account, a large number were returned with non-sufficient funds. Cosmetology received over \$10,000 in returned checks resulting in unnecessary penalties.
- Receipt log books were lost or destroyed. Employees could not account for the whereabouts of all receipt books. Cash receipts that arrived through the mail were not logged at all by employees of Cosmetology. The logs that were able to be examined did not agree to the customer payment receipts maintained by Cosmetology. Auditor was unable to vouch these receipts and payments to confirm accuracy.
- There were no internal controls in place over cash receipts – amounts were not logged, no audit trail was maintained, cash was not timely deposited. There is no assurance that the amounts deposited by Cosmetology accounted for all the cash receipts received by the agency. Additionally, the same employee who opens the mail is responsible for the bank reconciliations and the preparation of the deposit slip.
- Of the deposits that were made to Treasury, 20 were not made timely. Deposits ranged from 3 to 188 days late.
- Of the deposits that were made to the clearing account, 20 were not made timely. Deposits ranged from 3 to 38 days late.
- The agency failed to comply with a requirement of the MSBC Bank Authorization Form requiring checks written from the clearing account to have two authorized signatures. Checks written from the clearing account during FY2016 had one (1) authorized signature on each check.
- The agency failed to comply with the maximum allowed balance of \$1,500 as approved by the Department of Finance and Administration (DFA) and the State Treasurer. The bank account maintained month ending balances that ranged from \$3,401.48 and \$50,897.36 for 11 out of the 12 months of the fiscal year.
- The agency submitted the Public Depositor Annual Report to the State Treasurer on September 1, 2016, or 32 days after the due date. The due date was 30 days from the end of the fiscal year, or July 31, 2016.
- Auditor noted two (2) instances where checks from the clearing account were used to purchase commodity items.
- While performing bank reconciliation testwork auditor noted the agency does not

keep a separate record of the ending monthly book cash balance. Without proper documentation on the agency books, there are not sufficient records to agree the reconciliation balance. Auditor also noted that changes in cash are not accurately reflected in agency's MAGIC records.

Failure to deposit receipts daily and to keep adequate records of cash received could result in the loss of receipts and interest revenue by the state and increases the risk of theft and/or misplacement of funds and noncompliance with State law.

Additionally, failure to properly account for revenue in the correct fiscal year could result in a misstatement of Cosmetology's financial statements and the State of Mississippi's Annual Financial Report.

Finding 2: The Board of Cosmetology Should Issue Licenses Timely and Accurately.

Executive Summary: The Mississippi Board of Cosmetology (Cosmetology) was created and has the responsibility for issuing licenses to cosmetologists, hair-braiders, manicurists, estheticians, salons, and instructors. Per inquiry with licensees and observation of the operations of Cosmetology, auditors noted that Cosmetology has a severe backlog of licenses remaining to be issued. In some cases biennial licenses are sent to licensees 12 months after license fees have been paid. The backlog of license issuance resulted in employees working past business hours and often on weekends unsupervised. The neglect from the employees and the Board Members amounts to dereliction of duty in regards to the cosmetology profession.

Lack of timely issuances of licenses can undermine the authority of the Board of Cosmetology in regards to their established purposed and mission.

Recommendation: We recommend that licenses be issued timely and that the Board of Cosmetology and its employees strive to maintain an up to date licensing system.

Detailed Analysis: During the audit of Cosmetology, auditors inquired of several Cosmetologists, manicurists and estheticians about the status of their license renewals. Often the questions were met with derisive comments about Cosmetology, their purpose and the license renewal process. In one instance, auditors were told that it was vital to keep the receipt given to you by Cosmetology because it was often the only proof that you had submitted a license renewal if investigated. While this information is anecdotal, it supported the observations made by auditors that cash receipts had not been deposited and that employees stated that they often worked overtime to clear up the backlog of licenses needing to be issued.

The untimely issuance of licenses can be indicative of waste, fraud and abuse. Additionally, it can result in lack of confidence in the licensure process and circumvision of it by licensees.

Finding 3: Board Oversight Should Be Strengthened.

Executive Summary: The Mississippi Board of Cosmetology (the Board) was created and has the authority to make rules and regulations as are reasonable and necessary for the orderly

regulation of the cosmetology profession. The Board is tasked to set reasonable license fees; to make rules and regulations and to promote said regulations; to hire and retain staff as necessary to conduct business; and to hold investigations, hearings, etc. to provide disciplinary provisions in accordance with Sections 73-7-1 through 73-7-71 of *Mississippi Annotated Code (1972)*.

During our review, we noted a complete absence of Board oversight regarding the daily operations of the employees of the Board of Cosmetology (BOC). The former Executive Director was neither appropriately monitored nor did the board members take an active role in reviewing financial information, purchases, travel, etc.

Lack of appropriate oversight and appropriate “tone at the top” leadership can lead to fraud, waste, and abuse.

Recommendation: We recommend the Board Members of the Mississippi Board of Cosmetology provide more effective and appropriate oversight of the Director of the Mississippi Board of Cosmetology. We recommend the implementation of new controls, policies, and procedures where necessary. We wish to place emphasis on the importance of appropriate “tone at the top” leadership.

Detailed Analysis: The Mississippi Board of Cosmetology (Cosmetology) is comprised of five Board members (The Members) appointed by the Governor. The Members employ several staff members and investigators charged with carrying out the duties of Cosmetology as statutorily prescribed. The Members also employ an Executive Director tasked with running the day to day operations of Cosmetology as well as supervising the other staff members. As evidenced by the actions of the Executive Director and staff during the fiscal year under audit, the Executive Director operated with complete autonomy and was not overseen by the members.

These actions and findings noted in this report indicate a lack of appropriate oversight and tone at the top leadership when considered in the aggregate.

The Board Members of the Board of Cosmetology should implement processes to better regulate and oversee the Executive Director and staff.

Finding 4: The Mississippi Board of Cosmetology (Cosmetology) Should Strengthen Internal Controls Over Travel to Ensure Compliance with State Law.

Executive Summary: Employees from Cosmetology have not properly documented justifications for travel, travel reimbursements, mileage, etc. As detailed in the findings below, Cosmetology has not implemented or is not abiding by policies and procedures to ensure the reasonableness and necessity of travel and its proper reporting.

Recommendation: We recommend the Mississippi Board of Cosmetology implement controls over travel and travel reimbursements. We also recommend that the Board Members at Cosmetology review all travel reimbursements for the Executive Director and review all appropriate evidence of justification of travel.

Further, we recommend that the Investigations Division at the Office of the State Auditor review any and all travel reimbursements to ensure that all reimbursements are proper, necessary and valid.

Detailed Analysis:

Mississippi Annotated Code (1972) § 25-3-41 establishes guidelines for travel reimbursements of officers and employees of the State of Mississippi, and of any department, institution, board or commission thereof. It also establishes that the Mississippi Department of Finance and Administration (DFA) shall promulgate rules and regulations regarding State Travel Policy.

The State Travel Policy Rules and Regulations available on DFA's website is a travel manual that serves as a quick reference for the provisions and rules of Section 25-3-41 and other relevant statutes, as well as rules promulgated by DFA in accordance with State Law.

Rules established by the State Travel Policy Rules and Regulations set out the following requirements:

- 1) Department Directors will be responsible for ensuring compliance with § 25-3-41 by providing adequate internal controls over employee travel;
- 2) Travel Vouchers include a signature that verifies that all reimbursed expenses are actual expenses and that they are valid business expenses;
- 3) Travel in a privately owned vehicle must only include mileage between points of travel made from the most direct, practical route;
- 4) Business travel and personal travel may be combined when all of the following conditions are met:
 - a. The primary purpose of the trip is official state business;
 - b. The employee uses his approved leave for the personal part of the trip; and
 - c. The state agency incurs no expenses beyond what it would have incurred had there been no personal travel in the trip.
- 5) The State does not reimburse private vehicle mileage for optional travel.
- 6) The individual agency requesting reimbursements has the responsibility to maintain all documentation for audit purposes supporting rates reimbursed.

Section 9.1 C of the Mississippi State Personnel Board Policy and Procedures Manual states that falsification of travel vouchers is considered a "Group Three Offense" that may result in a written reprimand, suspension without pay for up to thirty working days, demotion, or dismissal.

Additionally, good internal controls dictate that adequate separation of duties exists over the areas of preparing travel reimbursement claims, approving reimbursement claims, and reviewing reimbursement claims.

Finding Detail:

During our testwork performed at Cosmetology related to travel, we noted the following:

- The Executive Director's travel has not been properly reviewed or approved. Reimbursements to the Executive Director were approved by the Executive Director and did not appear to have any additional approval from the Members.

- Out of a sample of 10 travel vouchers examined, two (or 20%) of the reimbursements could not be justified with proper support or documentation.
- Items that should have been purchased using procurement cards or other procurement methods were purchased and reimbursed via a travel voucher. These purchases, because of the use of incorrect procurement methods, were charged sales tax and resulted in lost revenue to Cosmetology.
- Out of a sample of 10 travel vouchers examined, two employees submitted incorrect information on their travel vouchers resulting in overpayment of travel reimbursement. Both travel vouchers were reviewed and approved by employees of Cosmetology before submission.
 - One voucher claimed reimbursement for in state mileage at the incorrect rate of \$0.575 cents per mile rather than the rate in effect during that time period which was \$0.54 cents per mile.
 - One employee claimed differing mileage amounts for the same route on multiple days.
- Travel reimbursements appear excessive when compared to the relative size and budget of Cosmetology. Cosmetology reimbursed travel expenditures in excess of \$141,000 for the fiscal year under audit. This amount was over 18% of the total expenditures (\$749,995) of the Agency.

Finding 5: The Mississippi Board of Cosmetology (Cosmetology) Should Strengthen Internal Controls over Leave Policies to Ensure Compliance with State Law.

Executive Summary: Adequate source documentation could not be provided for beginning and ending leave balances at Cosmetology. Leave balances were considered not auditable due to the lack of an audit trail or any documentation.

Recommendation: We recommend the Mississippi Board of Cosmetology implement controls over personal, sick, and compensatory leave. Further, we recommend that the Investigations Division at the Office of the State Auditor and the Mississippi Public Employees Retirement System review the accrued leave balances to ensure that all leave has been recorded in accordance with state law. We also recommend that the Board Members of Cosmetology implement written policies regarding leave, and that the Board Members review and approve leave of the Executive Director.

Detailed Analysis:

Criteria:

Mississippi Annotated Code (1972) Sections 25-3-93(4) and 25-3-95 states (in part) “Employees are encouraged to use personal leave. Personal leave may be used for vacations and personal business and shall be used for illnesses of the employee requiring absences of one (1) day or less.”

Section 7.5.1 of the Mississippi State Personnel Board Policy and Procedures Manual states “Regular attendance is a basic condition of employment with the State of Mississippi and shall be considered among the essential elements for all permanent position classifications. All employees must report to and leave work at the time designated by their employer. Anticipated absence from work is to be arranged with the employee’s supervisor in advance, and unexpected

absences are to be reported promptly to the employee's supervisor prior to the beginning of the employee's work period."

Section 9.1 C of the Mississippi State Personnel Board Policy and Procedures Manual states that falsification of leave records is considered a "Group Three Offense" that may result in a written reprimand, suspension without pay for up to thirty working days, demotion or dismissal.

Additionally, good internal controls dictate that written policies over leave policies exist to prevent fraud, waste, and abuse.

Finding Detail:

During our review of vacation, sick, and compensatory leave for fiscal years 2016 we noted that no supporting documentation regarding leave was maintained. Agency personnel could neither support beginning or ending balance, nor could evidence be found that appropriate approvals were obtained before employees used leave.

It is the understanding of the auditors that, subsequent to the audit, the Board Members hired a replacement for the Executive Director. The new Executive Director has indicated that new policies and procedures have been implemented regarding leave and that one employee was terminated due to falsification of leave records for herself and other employees.

Failure to adequately record leave can indicate potential criminal activity and can result in overstated liability.

Finding 6: The Mississippi Board of Cosmetology (Cosmetology) Should Strengthen Internal Controls over Procurement Card Purchases to Ensure Compliance with State Law.

Executive Summary: Lack of written policies and procedures regarding internal procurement procedures, lack of adherence to state mandated procurement procedures and lack of adequate internal controls led to improper use of the procurement card and violation of state law.

Recommendation: We recommend the Mississippi Board of Cosmetology (Cosmetology) implement controls over procurement card purchases. We also recommend that Cosmetology implement written policies regarding these purchases and that at a minimum the statements are reviewed and approved by Board Members of Cosmetology.

Further, we recommend that the Investigations Division at the Office of the State Auditor review any and all procurement card purchases to ensure that all payments were made in accordance with State Law and that all purchases were for business purposes.

Detailed Analysis:

Criteria:

Mississippi Annotated Code (1972) Section 31-7-9(1b) states (in part) "The Office of Purchasing, Travel, and Fleet Management may adopt purchasing regulations governing the use of procurement cards to be used by state agencies."

Mississippi Annotated Code (1972) Section 31-7-303 states (in part) "The requisition for payment of an invoice submitted to a public body and required by law to be filed with the State

Fiscal Management Board shall be filed with the State Fiscal Management Board not later than thirty (30) days after receipt of the invoice and receipt, inspection and approval of the goods or services, except that in the case of a bona fide dispute the requisition for payment shall contain a statement of the dispute and authorize payment only in the amount not disputed.”

The State of Mississippi Procurement Manual 10.111.02 states “the various state agencies may make purchases under the Small Purchase Procurement Card Program provided, however, that all such purchases shall be made in compliance with the minimum policies and procedures established by the Office of Purchasing, Travel, and Fleet Management.

The State of Mississippi Procurement Manual 10.111.03 states “government entities may use the Procurement Card to make purchases which are bona fide needs of the entity.”

The State of Mississippi Procurement Manual 10.112.01 states “balances on credit cards shall be paid at the receipt of the monthly statement, once the statement has been reconciled for accuracy.”

Additionally, good internal controls dictate that duties should be segregated in order to limit the same individual from purchasing, reconciling, and paying invoices.

Finding Detail:

During our review of procurement card purchases for the Mississippi Board of Cosmetology, we noted the following:

- Seven out of ten invoices tested had untimely payments made. Per state law payments must be made within 30 days of receiving the invoice.
- One invoice out of ten tested was paid an incorrect amount.
- Procurement cards were used for inappropriate purchases such as monthly utility payments and contractual expenditures.
- Procurement card balances were not paid in full each month and carried a large outstanding balance. This balance resulted in unnecessary expenses of interest and late fees.

Failure to appropriately monitor purchases can lead to waste, fraud, abuse, and potential criminal liability. Failure to pay balances in full each month can result in unnecessary interest expenses, late fees and penalties.

INSTANCES OF NON COMPLIANCE WITH STATE LAW

Finding 7: Mississippi Board of Cosmetology Should Ensure Board Meetings are Held and Recorded in Compliance with State Law.

Executive Summary: During the review of Board Minutes for the fiscal year under audit, auditors noted that Board Minutes were not properly signed and approved by the Chairman of the Board. Additionally, we noted that Minutes of the Board Meeting were not properly recorded and posted in accordance with state law.

Recommendation: We recommend the Mississippi Board of Cosmetology Board Meetings are reviewed and approved by the Chairman of the Board and that minutes are posted in accordance with State Law.

Detailed Analysis:

Mississippi Annotated Code (1972) Section 25-41-11, states, "Minutes shall be kept of all meetings of a public body, whether in open or executive session, showing the members present and absent; the date, time and place of the meeting; an accurate recording of any final actions taken at such meeting; and a record, by individual member, of any votes taken; and any other information that the public body requests be included or reflected in the minutes. The minutes shall be recorded within a reasonable time not to exceed thirty (30) days after recess or adjournment and shall be open to public inspection during regular business hours."

End of Report