

A Follow-Up Audit Report on

Internal Controls and Financial Processes at the Cosmetology Commission

February 2005

Report No. 05-027



**State
Auditor's
Office**

**John Keel, CPA
State Auditor**

Internal Controls and Financial Processes at the Texas Cosmetology Commission

Overall Conclusion

Additional improvements are needed for the Texas Cosmetology Commission (Commission) to discharge its fiscal obligations in a timely manner, properly manage its assets, and keep adequate fiscal records. The Commission has shown minimal improvement in addressing the findings identified in *An Audit of Internal Controls and Financial Processes at the Cosmetology Commission* (SAO Report No. 04-019, February 2004). The Commission has a number of control weaknesses in its financial systems that allow errors and violations of laws and regulations. Additionally, data integrity issues and missing data fields in the Commission's computer system hamper the Commission's efforts to capture reliable information. Although the Commission has implemented a number of recommendations, the ones that have been minimally implemented significantly affect its operations.

Implementation Status

The status of the 13 prior audit recommendations is as follows:

- Three have been **implemented**. All actions have been taken to implement the recommendations.
- Two have been **substantially implemented**. The majority of actions necessary to implement the recommendations have been taken.
- Seven have been **minimally implemented**. Some action has been taken to implement the recommendations, but the action is not sufficient to show substantial progress toward completion.
- One prior recommendation has no implementation status.

Because of the significance and persistence of the issues and the Commission's inability to develop a long-term financial plan, we recommend that the Commission outsource all of its financial processes if it continues to exist in whole or in part. The Commission can outsource these processes to another state agency, such as the Office of the Comptroller of Public Accounts, or to a private accounting firm.

Key Points

The Commission has not discharged its fiscal obligations in a timely manner.

- The Commission is consistently paying bills late, resulting in the accrual of prompt payment interest on these outstanding encumbrances for fiscal years 2004 and 2005. In addition, 74 percent (20 of 27) of vouchers tested for January 2005 were overdue.
- The Commission has not tracked or recorded any leave activity for fiscal year 2005, nor did it track leave balances in fiscal year 2004 as required by the Texas Government Code, Section 661.908. This resulted in an employee being paid for leave that should have been recorded as leave without pay.
- The executive director's mother was hired through a temporary service to work at the Commission in violation of nepotism provisions of Government Code, Section 573.041.



The Commission should improve controls over its assets.

- The Commission does not have an adequate process for securing funds because numerous employees have access to the key to the safe where checks and cash are stored.
- Due to the extraordinarily high error rate for purchase transactions, the Comptroller of Public Accounts (Comptroller) canceled the Commission's post-payment contract. This means that the Commission has to submit all purchase vouchers with supporting documentation to the Comptroller for approval before the expenditures are entered into the Uniform Statewide Accounting System. The Comptroller stated that as of February 2005 the commission frequently submits purchase transactions without the required supporting documentation and continues to have difficulty in entering information into the system correctly.
- The Commission's computer system contains significant vulnerabilities.

The Commission should improve its maintenance of adequate fiscal records.

- The Commission did not reconcile cash listed in its computer system to the State Treasury for fiscal year 2004. It has partially reconciled its cash recorded in the computer system to the State Treasury for the first four months of fiscal year 2005.
- The Commission is not reporting the correct amount for accounts receivable. We estimate that accounts receivable could be as high as \$1.4 million. However, the Commission reported accounts receivable of only \$9,800, and it could not provide supporting documentation for 16 percent of that amount.
- Weaknesses in the Commission's computer system prevent it from being able to effectively use the system and rely on the data for decision making.

The Commission has made improvements to its enforcement program.

The Commission has begun taking cases to the State Office of Administrative Hearings to aid in the collection of penalties. It also updated its computer system to ensure that it is fining licensees the correct amount. Additionally, the Commission began blocking licenses from being renewed for individuals who have not paid their administrative fines.

Summary of Management Responses

The Commission generally agrees with the implementation status of the recommendations. The Commission disagreed with the implementation status of Recommendation 2, and it disagreed with a portion of Recommendation 9. The information provided by the Commission does not change the State Auditor's findings or recommendations. (See Appendix 2 for the Commission's responses.)

The Commission's responses also include assertions about numerous observations it believes state auditors made during the audit. However, these observations were not made by state auditors. Only the body of this report contains the actual observations that the state

auditors made and verified. The State Auditor's Office cannot attest to the accuracy of the numbers contained in the Commission's responses.

Summary of Information Technology Review

A number of changes need to occur for the Commission to be able to effectively use the computer system and rely on the data in the system. The computer system is made up of several modules that capture information, including a cash module, a licensing module, and an enforcement module. These modules are not configured to relate to one another for the best use of the system. For example, the Commission's enforcement and cash modules are missing a number of critical fields that would allow them to share information with each other. Furthermore, the enforcement module does not capture reduced fine amounts, and the Commission does not appear to have adequate input edit controls over the enforcement module.

Additionally, our review of the Commission's computer system revealed significant vulnerabilities in the system, which we discussed with management. The Commission has developed a number of manual processes to address these issues; however, not all of them address the deficiencies.

Recent SAO Work		
Number	Product Name	Release Date
04-019	An Audit of Internal Controls and Financial Processes at the Cosmetology Commission	February 2004

Detailed Results

Chapter 1

The Commission Minimally Implemented Recommendations that Address the Deficiencies It Needed to Correct Immediately

Follow-up work identified additional improvements that are needed for the Texas Cosmetology Commission (Commission) to discharge its fiscal obligations in a timely manner, properly manage its assets, and keep adequate fiscal records. Although the Commission has implemented a number of recommendations, the minimally implemented recommendations significantly affect the management of the Commission.

As stated in the February 2004 audit report, correcting the issues identified required the Commission to (1) take immediate action to correct certain deficiencies and (2) implement a long-term financial remediation plan. The tables below discuss the actions the Commission has taken to implement the recommendations it needed to address immediately and the implementation status for each.

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 1</p> <p>Complete enforcement authority should be used to collect penalties, including continuing the hearings process at SOAH and consistently blocking the renewal of licenses for individuals who have not paid administrative penalties.</p>	<p>The Commission has substantially implemented this recommendation.</p> <p>The Commission indicated that as of October 2003, cases were taken to the State Office of Administrative Hearings (SOAH). All fiscal year 2004 cases resulting in a fine or penalty were scheduled for a SOAH hearing for the sample tested.</p> <p>Testing also identified instances in which the Commission blocked licenses from being renewed for individuals who have not paid their administrative fines. However, it is not possible to determine whether the Commission consistently blocks licenses because its licensing and enforcement system does not have the fields to collect the appropriate data.</p>
<p>Recommendation 2</p> <p>Controls over the receipt of funds should be implemented.</p>	<p>The Commission has minimally implemented this recommendation.</p> <p>The Commission does not have adequate processes to ensure the security of funds. All fees and fines paid to the Commission are kept in the safe. The Commission indicated that only two people have access to the safe. However, the safe is a key safe rather than a combination safe, and all accounting staff members have access to the key for the safe.</p> <p>While the auditors observed that that Commission did have two employees present in the mailroom while opening the mail, the written mailroom procedures do not require this. The Commission indicated that it developed procedures for this recommendation in February 2004.</p>
<p>Recommendation 3</p> <p>A process to ensure compliance with capital budget restrictions in the General Appropriations Act should be enforced, and documentation to support compliance should be retained.</p>	<p>There is no implementation status for this recommendation.</p> <p>The Commission did not have a capital budget for fiscal year 2004. Therefore, we could not test to determine whether the Commission was in compliance with the capital budget restrictions in the General Appropriations Act.</p>

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 4 TexasOnline subscription fees should be paid on time and in the proper amount.</p>	<p>The Commission has implemented this recommendation. The Commission has successfully paid its TexasOnline subscription fees. The sample of transactions tested after the implementation date of February 2004 showed that the Commission paid all its TexasOnline subscription fees accurately and within the time allowed by statute.</p>

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 5 A process to ensure that revenue is deposited within three business days of receipt should be implemented.</p>	<p>The Commission has substantially implemented this recommendation. The Commission has a process in place to ensure that revenue is deposited within three days of receipt. However, the Commission identified three instances in which deposits were not made within three business days. The Commission stated that these were deposited late because the Commission was short of staff, and in one instance, the computer system was down. Testing did not identify any other instances in which the Commission had not made deposits within three days.</p>
<p>Additional Revenue Issue The Commission could not accurately monitor the amounts of fines collected. This is because the report used to collect this information was not capturing all necessary data. As a result, the fines collected were understated by \$181,000 (15 percent) for fiscal year 2004.</p> <p>Subsequent Event Based on information provided to the Commission by the State Auditor's Office, the Commission was able to correct the report so that it would capture all necessary information.</p>	

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 6 A monthly process to perform cash reconciliations to the State Treasury account balance should be implemented.</p>	<p>The Commission has minimally implemented this recommendation. The Commission did not successfully reconcile cash listed in its computer system to the State Treasury for fiscal year 2004. The Commission requested data for the reconciliations in April 2004 from the vendor that maintains its computer system. The information was received in October 2004. The Commission asserted that it could not make the adjustments because it was after the close of the fiscal year and the cash accounts had been swept by the Uniform Statewide Accounting System (USAS). However, adjustments can be made quarterly to cash balances through the Commission's appropriations control officer. The Commission has partially reconciled its cash recorded in the computer system to the State Treasury for the first four months of fiscal year 2005. The Commission has not made any of the necessary adjusting entries for the reconciliation. Of the total \$3.1 million in revenues tested, the Commission was able to reconcile all but \$16,000, which represented only 0.5 percent of the total revenues tested. The discrepancy occurred from revenues collected in previous fiscal periods.</p>

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 7</p> <p>Written procedures to ensure that all transactions are accurate, properly authorized, and properly documented should be implemented. These procedures should address:</p> <ul style="list-style-type: none"> ▪ Adequate segregation of duties between the payroll function and release of payroll into the Uniform Statewide Accounting System (USAS). ▪ Supervisory review of payroll information and processing. ▪ Adequate staff training in the preparation of financial transactions. ▪ Periodic review and revision of USAS user access capabilities, including whether user access is appropriate for current job responsibilities. 	<p>The Commission has minimally implemented this recommendation.</p> <p>The Commission is not consistently following its policies and procedures because all transactions are not accurately documented.</p> <p>In October 2004, the Comptroller of Public Accounts (Comptroller) canceled the post-payment contract with the Commission after a follow-up demonstrated that the Commission continued to have an extraordinarily high error rate for purchase transactions (32 percent compared with the state average of 0.594 percent for purchases). This means that the Commission has to submit all of its purchase vouchers with supporting documentation to the Comptroller for approval before the expenditures are paid and entered into USAS. As of February 2005, the Comptroller stated that the commission frequently submits purchase transactions without the required supporting documentation and continues to have difficulty in entering information into the system correctly.</p> <p>The Commission is not accurately recording or monitoring its purchase transactions to ensure they are paid in a timely manner. As a result, the Commission is consistently paying bills late. Examination of expenditures made by the Commission for fiscal year 2004 and fiscal year 2005 showed that it is consistently accruing prompt payment interest on these outstanding encumbrances. In addition, we tested a selection of purchase vouchers processed in January 2005, and 74 percent (20 of 27) of vouchers tested were overdue.</p> <p>The Commission is not in compliance with the Texas Government Code, Section 661.908, because it is not consistently obtaining time and attendance records for each employee, recording employee leave accruals, and recording leave taken. Specifically, we found the following:</p> <ul style="list-style-type: none"> ▪ The Commission could not locate 30 percent (24 of 79) of the timesheets requested. ▪ Twenty-five percent (14 of 55) of timesheets tested were not appropriately approved. ▪ The Commission has not tracked or recorded any leave activity for fiscal year 2005, nor did it track leave balances in fiscal year 2004. The majority of leave balances for fiscal year 2004 were entered at one time in November 2004. As a result, one employee was paid for leave that should have been recorded as leave without pay in fiscal year 2005. The Commission also cannot determine whether any of its employees' compensatory balances earned have exceeded the one-year threshold. If an employee does not use his or her compensatory balances within one year after it is earned, it expires. <p>To address the prior audit recommendation:</p> <ul style="list-style-type: none"> ▪ The Commission has written procedures that require a supervisory review of payroll information and processing. In addition, testing verified that the employee who prepares payroll does not have the ability to release it into USAS. ▪ The Commission asserts that it reviews USAS access every six months. The State Auditor's Office noted that access was removed within the required timeframe for an employee who left the Commission during fieldwork. ▪ The Commission staff attended training at the Comptroller's in fiscal year 2004 and has a training schedule for fiscal year 2005.
<p>Additional Issue in Expenditures</p> <p>The executive director's mother was employed through a temporary service to work at the Commission for six months. This violates the nepotism statute in Government Code, Section 573.041, which states that "a public official may not appoint, confirm the appointment of, or vote for the appointment or confirmation of the appointment of an individual to a position that is to be directly or indirectly compensated from public funds or fees of office" if the individual is related to the public official within the third degree by consanguinity or within the second degree by affinity.</p> <p>Attorney General Opinion DM-163 interprets this section of the nepotism statute as applying only to officers who have the authority to hire personnel. The Commission's enabling statute (Government Code, Section 1602.102) allows the executive director to employ personnel necessary to administer the functions of the Commission.</p> <p>Subsequent Event</p> <p>The executive director terminated her mother's employment at the Commission in January 2005 after the auditors raised this issue.</p>	

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 8</p> <p>A process should be implemented to ensure that the Commission's reports and records present a complete and accurate picture of its financial activities and position. This includes the implementation of:</p> <ul style="list-style-type: none"> ▪ A quality control process for preparing financial statements. A process should be developed for examining financial data before it is submitted to the contractor that prepares the Commission's annual financial statements. ▪ A quality control examination on the completed financial statements to detect and prevent errors. ▪ Processes to ensure that supporting documentation for financial activities is maintained in accordance with the state records retention policies. 	<p>The Commission has minimally implemented this recommendation.</p> <p>The Commission is not reporting the correct amount for accounts receivable. Currently accounts receivable captures only book sales. It should include administrative penalties as well.</p> <p>We estimate that accounts receivable could be as high as \$1.4 million. The Commission reported only \$9,800 in accounts receivable, and it could not provide supporting documentation for 16 percent of that amount. The estimate is difficult to obtain because the Commission's computer system does not capture the date on which the Commission's governing board approves the penalties, which is the action that makes a penalty legally collectible. We calculated the \$1.4 million estimate by adding total fines assessed through the SOAH process and the fines assessed through the informal executive director process. However, it is unclear if these cases have been approved by the board.</p> <p>According to Governmental Accounting Standards Board (GASB) Statement No. 33, the Commission's accounts receivable should include administrative penalties once the agency goes through due process and the fines become legally collectible.</p> <p>To address this recommendation, the Commission developed policies and procedures in December 2004 that require the chief financial officer to review supporting documentation and authorize information contained in the financial statements.</p>

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 9</p> <p>Certain collection accounts and processes should be established. These include an allowance for doubtful accounts, a bad debt expense account, criteria defining uncollectible accounts, and procedures to age accounts receivable to determine which accounts receivable are not likely to be collected.</p>	<p>The Commission has minimally implemented this recommendation.</p> <p>The Commission does not have a procedure for budgeting bad debt expense and monitoring bad debt expense through its financial accounting system. It also does not have criteria for defining uncollectible accounts or a procedure to age accounts receivable.</p> <p>Additionally, the Commission is reducing some fines unnecessarily. The Commission indicated that it reduces the amount of fines it assessed for a violation for a number of reasons, one of which is that the Commission cannot prove that the licensee received the executive director notification. The Commission does not have to reduce the fines in this situation. An executive director notification is a letter sent to a shop/licensee from the executive director summarizing the violations noted and the penalty amount and informing the shop/licensee of the right to a hearing. The licensee technically received notification when the inspector conducted the inspection and issued the citation. Any additional communication only provides options to the licensee, and lack of this documentation should not be used as a reason to reduce the fine.</p>

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 10</p> <p>A process should be implemented to ensure that the correct penalty amounts are assessed for all violations.</p>	<p>The Commission has implemented this recommendation.</p> <p>The Commission's computer system contains the correct penalty amount to assess fines. The assignment of penalty amounts is an automatic process performed by the Commission's computer system. The Commission updated the computer system in September 2003 to include the latest fine changes. Testing identified no errors.</p>

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 11</p> <p>A process should be established to ensure that adequate server backups are tested and performed regularly.</p>	<p>The Commission has implemented this recommendation.</p> <p>The Commission has an adequate process in place to ensure that backups are performed daily. The Commission was able to successfully restore data from a backup in December 2004.</p>

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 12</p> <p>Controls should be implemented over the licensing and enforcement system to ensure accurate information and compliance with regulations.</p>	<p>The Commission has minimally implemented this recommendation.</p> <p>The Commission improved the enforcement module of its computer system by adding a field assigning a unique number to each inspection report. This was done to prevent duplicate inspection reports from being entered. However, this does not prevent duplicate violations from being entered for any inspection report.</p>
<p>Additional Computer Related Issues</p> <p>A number of changes need to occur for the Commission to be able to effectively use its computer system. The Commission's computer system is made up of several modules that capture information, including a cash module, a licensing module, and an enforcement module. These modules are not configured to relate to one another for the best use of the system. Testing identified the following:</p> <ul style="list-style-type: none"> ▪ The Commission's enforcement and cash modules are missing a number of critical fields. For example, the modules are missing a common field that would allow them to share information. Because of this missing field, the cash module and the enforcement module do not reconcile. This means that the system cannot apply the cash amounts paid to the individual violations. ▪ The enforcement module of the computer system does not capture any reduced fine amounts. Therefore, the paid status of the violation incorrectly indicates that the full amount is paid rather than the reduced amount. ▪ The Commission does not appear to have adequate input edit controls over the enforcement module of its computer system. As a result, there are a number of fields with invalid entries. For example, the current system will allow letters to be entered in a field that should contain the number of times a violation has occurred. This affects the system's ability to accurately track fine amounts. <p>Our review of the Commission's computer system revealed significant vulnerabilities in the system, which we have discussed with management.</p>	

Recommendation

Because of the significance and persistence of the issues and the Commission's inability to develop a long-term financial plan (see Chapter 2), we recommend that the Commission outsource all of its financial processes if it continues to exist in whole or in part. These processes may include preparing cash receipts, deposits, and disbursements; purchasing services, supplies, and equipment; documenting claims for payment; preparing and processing payrolls; performing reconciliations; and preparing financial reports.

The Commission can outsource these processes to another state agency, such as the Office of the Comptroller of Public Accounts, or to a private accounting firm.

The Commission Minimally Implemented the Recommendation Related to Developing a Long-Term Financial Remediation Plan

The February 2004 report stated that correcting the Commission’s financial deficiencies would require long-term actions in addition to the short-term actions discussed above. The Commission only recently developed the long-term financial remediation plan.

Recommendation from SAO Report No. 04-019	Status as of January 2005 and Action Taken by the Commission to Implement Recommendation
<p>Recommendation 13</p> <p>To fully address financial management and internal control weaknesses, the development and implementation of a long-term financial remediation plan also is necessary. This plan should ensure that the Commission's financial management system supports:</p> <ul style="list-style-type: none"> ▪ The fiduciary role of management and the Commissioners. ▪ Compliance with legal and regulatory requirements. ▪ Ongoing fiscal and budgetary monitoring. ▪ The capturing of financial information required to measure performance. ▪ The Commission's strategic plan. ▪ The safeguarding of resources against waste, loss, and misuse. 	<p>The Commission has minimally implemented this recommendation.</p> <p>The Commission developed a plan in January 2005. The plan contains the recommended points, but the plan was not tested because it has not been fully implemented. However, the plan appears to be more of a status report than a long-range plan that addresses areas that need improvement at the Commission.</p>

Appendices

Appendix 1

Objective, Scope, and Methodology

Objective

The objective of this audit was to determine what corrective action the Texas Cosmetology Commission (Commission) has taken to address the findings identified in *An Audit of Internal Controls and Financial Processes at the Cosmetology Commission* (SAO Report No. 04-019, February 2004).

Scope

We reviewed each recommendation based on the date the Commission stated it had been implemented. The Commission implemented recommendations throughout fiscal years 2004 and 2005.

Methodology

The audit methodology consisted of collecting information and documentation, performing selected tests and other procedures, analyzing and evaluating the results of the tests, and conducting interviews with the Commission's management and staff. We collected financial and operational information. We also obtained various databases from the Commission. We tested revenues, expenditures, journal vouchers, and various financial statement accounts to ensure accuracy. We also reviewed selected controls over the Commission's automated systems and performed some tests to verify the data. We did not perform an applications review of the system.

Project Information

Our fieldwork was conducted from October 2004 to January 2005. This audit was conducted in accordance with generally accepted government auditing standards. The following members of the State Auditor's staff conducted the audit:

- Stacey Williams (Project Manager)
- Nick Ballard
- Anthony Patrick, MBA
- Stephanie Sherrill
- Michael Yokie, CISA
- J. Scott Killingsworth, CIA, CGFM (Quality Control Reviewer)
- Verma L. Elliott, MBA (Audit Manager)

Management's Response

HELEN QUIRAM, CHAIR
Waco
PHILIP LAPP
Weatherford
LUCINDA SANDOVAL
Edinburg
ESTHER CAMACHO
Austin

TEXAS COSMETOLOGY COMMISSION
FRANK JOSEPH COSMETOLOGY BUILDING
5717 BALCONES DRIVE, AUSTIN, TEXAS 78731-4203
P. O. Box 26700, Austin, Texas 78755-0700
www.txcc.state.tx.us



HELIANA KIESSLING
Friendswood
LEIF CHRISTIANSEN
Houston
ELIDA ZAPATA
Lubbock

ANTOINETTE FONTENOT HUMPHREY
Executive Director

February 21, 2005

State Auditor's Office
John Keel
P.O. Box 12067
Austin, TX 78711

Re: Texas Cosmetology Commission's Management Response to State Auditors Follow-up Audit on Internal Controls and Financial Processes

Dear Mr. Keel,

I appreciate the opportunity to respond to the follow-up audit prepared by your office.

Commission staff has worked diligently to implement the audit recommendations identified in the initial audit and to improve communication with Commission members by reporting financial activities and status.

The follow-up audit indicates that the Commission has implemented three of the 13 recommendations included in the initial audit, and has substantially implemented two other recommendations. This achievement has been accomplished without additional staff or funding, and has cost the Commission greatly in other areas of operation.

Since the completion of the initial audit, the Commission has directed most of its financial and human resources toward implementing systems to address the Auditor's two most significant findings: the Commission had not collected \$2.8 million of the \$4.8 million in penalties it assessed from September 1999-June 2003 and had not followed statutory and regulatory requirements for the collection of administrative penalties. As the follow-up audit indicates, the Commission has significantly implemented the recommendation to collect penalties by reinstating the State Office of Administrative Hearings (SOAH) process previously funded through the Office of Attorney General. In FY 2004 the Commission processed 3,000 cases through SOAH and collected more than \$1.3 million in fines assessed during the time period in question. The Commission is on target to eliminate the backlog of cases pending from fiscal years 2000-2004 by the end of the current fiscal year. This accomplishment consumed more than \$100,000 of the Commission's limited resources (primarily Northrup Grumman costs to upgrade an antiquated computer system).

At this time, seven SAO recommendations have been assessed as minimally implemented, and the Commission concludes that management has addressed as many of the recommendations from the prior audit as is considered practical given the current computer system, funding level, and severe understaffing. Additional staffing and financial resources are needed to address concerns that simply cannot be corrected otherwise.

★ (512) 380-7600

★ (800) 943-8922

★ FAX (512) 454-0339

★ Web: www.txcc.state.tx.us

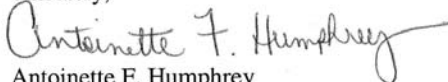
Also, I would also like to provide an update on audit findings that had not been addressed in the initial audit but have been included in this follow-up report. On February 4, 2005 (a week after the discussion conference had taken place) SAO auditors returned on-site, interviewed the temporary employee, pulled timesheets and found deficiencies in this area. To date, eighty percent of the timesheets have been entered into USPS for fiscal year 2004. On Wednesday February 23, 2005 leave activity for fiscal year 2004 will be closed out in USPS and leave activity for 2005 will be entered.

Concerning the finding of nepotism, at the time of the audit, the Human Resource/Accounts Payable Accountant relied on information obtained from the State Auditor's website and the Texas Building and Procurement Commission (TBPC). The Commission's requests to hire temporary employees must be initiated through a contract with TBPC. Based on their information, it was determined that the proposed selection of temporary employee through an approved temporary service would not present a problem. On January 28, 2005, when auditor's questioned me concerning this matter, the HR coordinator immediately discontinued the services of the temporary employee in question and on the next day provided auditors with the appropriate documentation that the temporary employee was no longer working at the agency.

Inadequate staffing levels and antiquated computer systems severely limit the Commission's ability to address identified deficiencies more quickly. At present, the 23 employees located in Austin central office are charged with providing services to individual cosmetologists and cosmetology establishment owners who hold **262,754** licenses; these services include scheduling more than 18,000 students for examinations and issuing over 25,936 students permits. Three employees are charged with answering an average of 1,100 telephone calls per day. The Human Resource Coordinator/Accounts Payable employee receives more than 1,200 calls per month related to personnel issues, and hundreds more each month from vendors, auditors, and other state agencies who request information. The Human Resource Coordinator also functions as the Accounts Payable Accountant, Risk Manager, Workers Compensation Coordinator, Safety Officer and Payroll Officer.

Again, the Commission appreciates the assistance provided by your office. I hope you can see that the Commission is committed to creating positive change and we look forward to continuing to work you're your office.

Sincerely,



Antoinette F. Humphrey

The Commission agrees that Recommendation 1 has been substantially implemented.

The Agency is working with Northrup Grumman to extend the system in order to finalize a triggering mechanism in the enforcement database so that, in a case where no payment activity has occurred, a license number is automatically blocked from renewal 30 days following the date the agency's Commissioners enter an order against a licensee by signing the Proposal For Decision.

Estimated time of implementation is March 31, 2005 .

The Commission does not agree that Recommendation 2 has been minimally implemented.

The initial audit reported that all accounting employees had access to a safe in which payments (including unendorsed checks for the payments of administrative penalties) are stored until they are deposited. Historically, critical understaffing in the Accounting Department, there have been instances where every accountant at some point in time may have needed access to the safe in order to secure checks. Although the auditors determined during the follow-up audit that all of the accounting staff at one point had access to the safe key, they also observed that the Commission has implemented procedures that ensure all checks are endorsed prior to being placed in the safe.

The auditors also observed in the follow-up audit that the Commission implemented control procedures requiring the presence of two employees in the mailroom while mail was being opened. This new process was implemented a year ago, in February 2004. The agency's written mailroom/cash control procedures were updated after the procedures were implemented. As evidenced in the initial audit, the Commission does not accept cash payments.

Therefore, we believe that this recommendation has been substantially implemented.

The Commission agrees that Recommendation 3 has no implementation status.

The Commission agrees that Recommendation 4 has been implemented.

The Commission agrees that Recommendation 5 has been substantially implemented.

The Commission agrees that Recommendation 6 has been minimally implemented.

Although the Commission provided documentation that a process had been implemented to perform reconciliations to the State Treasury, at present the cash system (IMPALA) erroneously changes prior year balances. Until this necessary program has been performed to correct this problem, the Commission's Appropriations Control Officer cannot make quarterly adjusting entries to reconcile the balances. The Commission has contracted with Northrup Grumman to perform the necessary programming. Reconciliations will be accomplished at that time.

The Commission agrees that Recommendation 7 has been minimally implemented.

The Commission has developed written procedures based on auditor recommendation to address segregation of duties, staff training, and access to USAS. The auditors observed that the new procedures and practices have adequately addressed their concerns. While the commission has made significant strides in strengthening controls and procedures, it's error rate for purchase vouchers continues to be high. The workload is overwhelming for the accountant who is charged with processing all payments and addressing all human resource needs for 43 full-time employees. Therefore, we continue to appreciate the assistance provided through the Office of the Comptroller.

Another concern arose subsequent to the follow-up audit after auditors had facilitated a Status Update meeting on January 28, 2005. On February 4, 2005, an audit of employee timesheets and leave activity was initiated and it was found that leave balances had not been updated in USPS. This area had not been included in the initial audit. The Commission employed the services of a temporary employee to begin an internal audit of time and leave balances prior to the start of the follow-up audit.

Although time sheets had not been submitted, the Commission's two division managers were monitoring attendance for all staff under their supervision. The Commission has continued to work with the Accounts Payable Accountant/Human Resource Coordinator and the temporary employee to calculate timecards, prepare timesheets, and to enter information into USPS. In addition, a new timekeeping system has been purchased which will automate the time keeping process and interface with USPS. The new system is scheduled for installation on February 22, 2005. The Commission has also implemented a policy to ensure that time sheets are collected and submitted in a timely manner.

The Commission agrees that Recommendation 8 has been minimally implemented.

No supporting documentation concerning accounts receivable for fines can be produced or reported to the Comptroller's Office until critical problems within the Commission's computer system have been resolved.

The Commission agrees that Recommendation 9 has been minimally implemented.

As stated in response number 8, at this point, the Commission's computer system is unable to verify fine information. A bad debt account, doubtful account, and criteria for defining uncollectible accounts will be established when this situation is rectified.

However, the Commission does not agree with the audit finding that the Commission is reducing some fines unnecessarily. It is within the discretion of the agency to reduce fines in instances where (1) the licensee testifies that they were not provided proper notice of an alleged violation against them, (2) documentation is presented to the commission suggesting that the licensee did not work in the salon at the time the violation was issued, (3) the Commission cannot document that a letter was sent prior to fiscal year 2003 indicating that a violation occurred as far back as the year 1999, and (4) the licensee's signature does not appear on the Inspection Report.

The Commission agrees that Recommendation 10 has been implemented.

The Commission agrees that Recommendation 11 has been implemented.

The Commission agrees that Recommendation 12 has been minimally implemented.

The Commission has used substantial resources to attempt to correct system deficiencies; however, additional employees and financial resources are needed in order to move forward with correcting the deficiencies identified.

The initial audit reported the following information technology control weaknesses: the system allowed the duplication of data entry for inspection reports and violations; lost financial information; statutory revisions to fine amounts were not updated in the system resulting in the assessment of incorrect penalty amounts, and the need to perform server backups on a regular basis.

During follow-up the Auditors observed:

- *The Commission corrected the violation code table using spreadsheet provided by State Auditors Office. The corrected table was submitted to auditors. Correct penalties are being assessed.*
- *Enforcement screens have been enhanced to display more violation information, including an amount field. This screen displays more records to reduce the occurrence of duplicate entries.*
- *New fields have been added to the Enforcement Sheet-Entry Screen so that the last 4 inspections can be displayed, and so that a Report Number can be entered to prevent duplicate entry of inspection report data.*
- *Procedures have been established to ensure adequate backup of servers is performed and tested regularly. Veritas Backup Exec software is used to perform backup of all departmental files and folders located on the Agency's server on Monday thru Friday at 10:00 p.m.*

Additional Computer Related Issues

Our primary goal is to improve the interface between the Commission's Enforcement and Cash modules, specifically:

- *Establish a link between a fine payment and the violation;*
- *Establish a unique identification number for each violation to be used for tracking and reporting;*
- *Establish new data fields for each violation that capture pertinent information, such as the actual fine and agreed-to penalty amounts;*
- *Develop new programs to process fine payments, allocating payments to the violation the payment;*
- *Establish a reporting mechanism that produces pertinent reports such as tracking delinquent violation activity, accounts receivable aging and a bad debt account;*
- *Track the history of events for each violation;*

- Automate the process of capturing “grouped” violation events, such as SOAH hearings and TCC Commission Proposal For Decision (PFD) approvals;
- Enable the system to automatically block license renewal if no payment activity has been made within thirty days after PFD approval;
- Improve program edit checking and installing entry safeguards and controls;
- Improve database integrity checks;
- Enhance staff access security and establish audit trails, and
- Provide restricted access through the TCC website for violators to review violation information and provide access to the general public to review violations by licensee.

The Commission agrees that Recommendation 13 has been minimally implemented.

The Commission developed a plan as recommended in the initial audit. Although the Commission began working on a long-range plan in FY 2004, efforts have been hampered by the fact that the position of Chief Financial Officer was vacant for most of FY 2004 and is currently vacant.

Copies of this report have been distributed to the following:

Legislative Audit Committee

The Honorable David Dewhurst, Lieutenant Governor, Joint Chair
The Honorable Tom Craddick, Speaker of the House, Joint Chair
The Honorable Steve Ogden, Senate Finance Committee
The Honorable Thomas “Tommy” Williams, Member, Texas Senate
The Honorable Jim Pitts, House Appropriations Committee
The Honorable Jim Keffer, House Ways and Means Committee

Office of the Governor

The Honorable Rick Perry, Governor

Cosmetology Commission

Ms. Helen R. Quiram, Board Chair
Ms. Esther Camacho, Board Member
Mr. Leif Christiansen, Board Member
Ms. Heliana Kiessling, Board Member
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