

SPECIAL AUDIT

OKLAHOMA DEPARTMENT OF REHABILITATION SERVICES

SWANSON SERVICES, INC. CONTRACT

July 1, 2009 through June 30, 2010



*Independently serving the citizens of
Oklahoma by promoting the
accountability and fiscal integrity of
governmental funds.*



Oklahoma State
Auditor & Inspector
Gary A. Jones, CPA, CFE

OKLAHOMA DEPARTMENT OF REHABILITATION SERVICES

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Oklahoma State Auditor & Inspector

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October 18, 2011

Chairman Steve Shelton
Oklahoma Commission of Rehabilitation Services
3535 NW 58th Street, Suite 500
Oklahoma City, Oklahoma 73112

Transmitted herewith is the special audit report of the Oklahoma Department of Rehabilitation Services, Swanson Services, Inc. contract.

Pursuant to an investigative services request by the Director of ODRS, and in accordance with the provisions of **74 O.S. § 227.8**, we performed a special audit of the ODRS/Swanson Services, Inc. contract for the period of July 1, 2009 through June 30, 2010.

The objectives of our special audit primarily included, but were not limited to, the areas noted in the Director's request. Our findings and recommendations related to these procedures are presented in the accompanying report.

Because the above procedures do not constitute an audit conducted in accordance with generally accepted auditing standards, we do not express an opinion on the account balances or financial statements of Swanson Services, Inc. for the period July 1, 2009 through June 30, 2010.

The Office of the State Auditor and Inspector is committed to serve the public interest by providing independent oversight and by issuing reports that serve as a management tool to the State. Our goal is to serve the citizens of Oklahoma by promoting accountability and fiscal integrity in state and local government.

We wish to take this opportunity to express our appreciation for the assistance and cooperation extended to our office during the course of our special audit.

This report is intended solely for the information and use of the Oklahoma Department of Rehabilitation Services and its administration and should not be used for any other purpose. This report is also a public document pursuant to the **Oklahoma Open Records Act (51 O.S. § 24A.1 et seq.)** and shall be open to any person for inspection and copying.

Sincerely,

A handwritten signature in blue ink, appearing to read "Gary A. Jones", is written over a light blue horizontal line.

GARY A. JONES, CPA, CFE
OKLAHOMA STATE AUDITOR & INSPECTOR

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OKLAHOMA DEPARTMENT OF REHABILITATION SERVICES

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Introduction

Formerly a division of the Oklahoma Department of Human Services (ODHS), the Oklahoma Department of Rehabilitation Services (ODRS or Department) was created as a separate state department by legislation passed in 1993. Title **74 O.S. § 166.1 *et seq.***, which transferred the various rehabilitation functions and services from ODHS to the new department, became effective June 11, 1993.

ODRS is governed by the Commission of Rehabilitation Services (the Commission), which consists of three (3) members, appointed one each by the Governor, the President Pro Tempore of the State Senate, and the Speaker of the State House of Representatives.

Currently, the Department has divisions and programs that include:

- Division of Vocational Rehabilitation (DVR): Employment services for people with any disability, except blindness.
- Division of Visual Services (DVS): Employment and independent living services for people who are blind or visually impaired.
- Disability Determination Division: Determines medical eligibility for Social Security Disability Insurance (SSDI) and Supplemental Security Income (SSI).
- Oklahoma School for the Deaf: Educational programs for children who are deaf or hard of hearing.
- Oklahoma School for the Blind: Educational programs for children who are blind or visually impaired.
- OK Library for the Blind and Physically Handicapped: Free services to Oklahomans who are blind or visually impaired and those with learning disabilities or physical limitations that make it difficult to use standard print.

Under the Division of Visual Services, the Department operates a federal program titled the Business Enterprise Program (BEP). The Director of the ODRS made a request for “investigative services” of the Oklahoma State Auditor and Inspector, pursuant to **74 O.S. § 227.8**, and with regard to the Department’s Business Enterprise Program contract with Swanson Services, Inc. of Tuttle, Oklahoma.

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The audit period covered was July 1, 2009 through June 30, 2010. Additional information from prior and following periods is included as necessary.

In this report, fiscal years are abbreviated by using the ending calendar year. For example, the fiscal year of July 1, 2009 to June 30, 2010, will be identified as "FY10."

All dollar amounts in this report are rounded to the nearest dollar, unless otherwise indicated.

The results of the Department's special request are in the following report.

NOTE: After its initial publication, attorneys acting on behalf of Cantu Services, Inc. requested that portions related to contractual dollar amounts be redacted arguing that the information was confidential, proprietary business data and was exempted under the federal Freedom of Information Act. Acting on the advice of the Oklahoma Attorney General's Office, SAI has made the agreed upon changes.

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**General
Background**

The Randolph-Sheppard Act (the Act) was first passed by the U. S. Congress in 1936. The Act was amended and updated significantly in 1974.

The Randolph-Sheppard Act was created for the purpose of providing blind persons, as defined in the Act, with remunerative employment, enlarging the economic opportunities of the blind, and encouraging the blind to greater efforts to become self-supporting. The Act authorizes priority be given to blind persons licensed by a “State agency” for operating vending facilities on any Federal property. The Act designates the “State agency for the blind” to issue licenses for qualifying individuals to become “licensed managers.”

The Division of Visual Services (DVS) is a branch of ODRS which oversees the federally created and state administered Business Enterprise Program (BEP). BEP trains and assists people who are blind or visually impaired in establishing and operating food service businesses in public and private facilities statewide.

BEP policies define a “licensed manager” as an individual who has signed an agreement with the State Licensing Agency (SLA), in this case ODRS, to manage a Randolph-Sheppard business enterprise under the supervision of the SLA. The licensed manager oversees the operations of individual enterprises established by the BEP and receives or shares in the net profits of the operation.

The licensed managers are subject to instructions, policies, rules and regulations of the BEP, but are not employees of the program, the SLA, or the State of Oklahoma. *They do, however, have a contractual relationship with the SLA and are required to manage the business enterprise in accordance with established rules and regulations.*

On May 30, 1995, an agreement was signed between ODRS and A.B. Swanson, a licensed blind vendor. The agreement included a provision that Mr. Swanson would enter a bid for the operation of food services at the Department of Defense Army base at Fort Sill, Oklahoma.

Also, if the bid was successful, the agreement included a provision for Swanson to request contract management consulting services to ensure the continuing satisfactory performance of the contract. The terms of the agreement required that Mr. Swanson comply with all federal and state

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laws in performance of the contract, including the rules and regulations of the ODRS/BEP.

On September 27, 1999, Mr. Swanson entered into an agreement with Cantu Services, Incorporated (Cantu) to furnish the requisite expertise to assist Mr. Swanson to submit a proposal through the ODRS in response to the Department of the Army solicitation for food services at Fort Sill, Oklahoma. Under the agreement, Cantu would become the “contract management” consultant if the proposal was accepted.

Submission of the proposal to provide food services at Fort Sill resulted in the U. S. Department of the Army awarding the bid to the Oklahoma Department of Rehabilitation Services/Business Enterprise Program, with Mr. Swanson as the “licensed manager.” According to interviews with Mr. Swanson, the first year of operation for the joint ODRS/Swanson/Cantu project was the *federal* fiscal year, October 1, 2001 to September 30, 2002.

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OBJECTIVE I: *Determine if operating expenses reported on the monthly business enterprise report were allowable expenses for the purpose of calculating the set-aside fee due to ODRS.*

Background

There were three contracts involved in administering the Fort Sill, Oklahoma dining facility operations:

1. One federal contract between the Army Contracting Agency, Southern Region Contracting Center-West (Fort Sill) and the Oklahoma Department of Rehabilitation Services (ODRS or Department);
2. One state contract between the ODRS and A. B. Swanson dba Swanson Services, Inc. (Swanson Services);
3. One private sector contract between the two entities of Swanson Services and Cantu Services, Incorporated (Cantu).

Each of the three contracts played a role in the multi-level administration of the large and complex Fort Sill dining facility business enterprise operated under provisions of the Randolph-Sheppard Act (RSA or the Act). When compared to most RSA vending facility enterprises in Oklahoma, the Fort Sill dining facility operation is *very large*. As indicated in the Fort Sill/ODRS contract, the negotiated staffing bid prices were categorized into two separate types of payroll and related costs.

The larger of the two categories represented the unionized *hourly-paid* labor force and related payroll and fringe benefit costs for staffing 13 separate dining/cafeteria/“field feeding” facilities located on Fort Sill, Oklahoma. According to the Fort Sill/ODRS contract, the total amount of the dining facilities direct staffing costs was budgeted to be [REDACTED] for “Option period 1” or October 1, 2009 to September 30, 2010.

The much smaller of the two categories was titled “site management” and included non-union *salaried* positions and related fringe benefit and operating costs. According to the Fort Sill/ODRS contract, the total amount for the site management costs was budgeted to be [REDACTED] for “Option period 1.” The total contract amount including both categories of costs was [REDACTED]. The contract allowed for 3% pay increases in each

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of the following three option periods for the site management salaries, but minimal increases in the hourly based pay rates.

Both categories of costs were part of the “big picture” and were included in the monthly financial reports and calculations of various fees going to Swanson Services, to Cantu and finally to ODRS. *This report section mainly addresses the “site management” category of contract costs and the impact of those costs on the “set-aside” fee calculation, as reported to ODRS.*

Set-aside fee description:

The terms and conditions of the agreement between ODRS and Swanson Services requires the licensed manager, i.e. A. B. Swanson, to pay a set-aside charge to the Department based on a sliding scale of 0.00% to not more than 12.00% of the *net proceeds* of the business enterprise during any one month. Net proceeds are defined as:

"Net proceeds" means the amount remaining from the sale of articles or services of business enterprises and any vending machine income or other income accruing to licensed managers after deducting the cost of such sales *and other authorized expenses excluding set-aside charges required to be paid* by the licensed managers. (emphasis added)

In addition, the Code of Federal Regulations has similar wording at 34 CFR § 395.1 (k):

"Net proceeds means the amount remaining from the sale of articles or services of vending facilities, and any vending machine or other income accruing to blind vendors after deducting the cost of such sale and other expenses (*excluding set-aside charges required to be paid* by such blind vendors)." (emphasis added)

According to BEP policy #612:25-6-15 (c), the set-aside charge is “based on prior year’s performance.” Under this scale, Swanson was required to pay 12% for set-aside charges since the Swanson Services, Inc.’s net proceeds in prior years routinely placed the business in the “Class A” top level of the scale.

The licensed manager is required to submit a “monthly business enterprise report” which includes the gross receipts, business expenses and net profit,

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along with other calculations, including the one for set-aside charges due to ODRS for the reporting period.

Cantu, as contract consultant for Swanson Services, prepared the monthly business reports for the licensed manager and submitted them directly to ODRS. Diane Hanson, Cantu controller provided us with an outline of the process for preparing the Swanson Services monthly business enterprise reports.

Based on the outline, Cantu received the statements, invoices, and receipts mailed directly to their office and/or to the Swanson Services Fort Sill office. This documentation, along with payroll information, was used to compile the monthly business enterprise report and the business enterprise report spreadsheet computed the set-aside charge. The first three (3) pages of the business enterprise report were given to Cantu's payroll clerk for payment and mailing.

The payroll clerk then stamped the report with Mr. Swanson's signature stamp, issued a check for the set-aside payment to ODRS c/o "Curtis Cunningham" (an ODRS employee), and mailed the report and check to ODRS. After the Cantu's payroll clerk mailed the report and payment to ODRS, a packet containing the documentation for the expenses was mailed to Mr. Swanson. Generally, Cantu's controller faxed copies of the financial statements, monthly business enterprise report, and related documentation to the Swansons' home prior to mailing the report and set-aside payment to ODRS.

See Appendix A for the complete outline of Cantu procedures.

We obtained the monthly expense packets from Cantu in order to determine if the business expenses listed on the monthly business enterprise report were allowable business expenses for calculating the set-aside payments. The contents of the packets were reviewed to verify the expenses were supported by an itemized invoice or proper documentation and that the expenses were allowable as set-forth in the Business Enterprise Program (BEP) policies and procedures.

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Finding #1

Various operating expenses reported on the Swanson Services monthly BEP reports were not in compliance with ODRS-BEP rules and regulations and in some cases significantly overstated the operating expenses charged, as a consequence.

Any unauthorized or unallowable operating expense would impact the calculation of the 12% set-aside fee due the ODRS. By definition, any increase in operating expenses decreases the *net proceeds* amount upon which the 12% set-aside fee is calculated.

We reviewed the supporting documentation for the Swanson Services operating expenses reported for the period of July 1, 2009 through June 30, 2010. The following expenses were questioned for the purpose of calculating the set-aside payments:

Operating Expense	Amounts questioned
Telephone	\$26,467.68
Meals and entertainment	2,392.33
B & J consulting expense	268,280.00
Vehicle expense	4,416.39
Workers' comp insurance	3,914.00
General liability insurance	1,228.00
Depreciation	21,235.74
Travel	23,661.31
Interest	4,428.12
Miscellaneous	31,756.37
Fees	237,322.69
Total	\$625,102.63

The reasons for questioning the above expenses were as follows:

Telephone – The expenses listed on the monthly reports included service at Fort Sill–Building 2607, Euclid Street office, mobile service for managers at Fort Sill and mobile service for A. B. and Barbara Swanson and Adrian Villesca, a driver for Mr. Swanson. BEP policy 612:25-6-21(e) allows an expense of \$50.00 per month for “all communication devices” and the specific budgeted line item for “telephone system” was limited to [REDACTED] in the Fort Sill/ODRS contract.

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Meals and entertainment – The expenses included purchases made in Lawton, Oklahoma for meals and lodging for Swanson Services, Inc. employees. Also, included were expenses for an employees’ Christmas party. The duty station for Swanson Service, Inc. employees is Fort Sill/Lawton, Oklahoma. Internal Revenue Service (IRS) rules allow this type of expense only if travel is away from the “duty station” for a period substantially longer than an ordinary day’s work.

Except for the Christmas party, the meals and entertainment expenses were mostly transacted as credit card charges by the project manager (a Cantu employee), or by the alternate project manager (a Swanson employee), and/or by “petty cash” transactions.

B & J consulting expenses – Five invoices were submitted by B & J Activities, LLC, which according to interviews was formed by Swanson for “diverse business purposes.” *This questioned cost is discussed in detail in **Objective III** of this report.*

Vehicle expense – Expenses included fuel, service, repairs, tires, etc. for vehicles driven by Barbara Swanson, Victoria Cantu, project manager, Deborah Welch, alternate project manager, and a pick-up located at Fort Sill. BEP policies 612:25-6-21(d) disallows any vehicle expense, except for travel between two separate *approved* business enterprises, as described at 612:25-4-61(g).

Workers’ compensation insurance – This category included automobile insurance coverage for a 1985 GMC Van, a 1991 Ford F-250 pick-up, a 2008 Mercury Milan, and a 2008 Lincoln MXK, which is not allowed per BEP policy 612:25-6-21(d). Whether intentional or due to clerical error, the “coding” of these expenses resulted in charging vehicle expenses to “Workers’ compensation insurance.”

General liability insurance – Automobile insurance coverage for a 2008 Mercedes-Benz GL320 CDI, which is not allowed per BEP policy 612:25-6-21(d), and once again we noted the miscoding of vehicle expense to “General liability insurance.”

Depreciation – Depreciation expense for a 2004 Ford F-150 pickup, a 1985 GMC Van, a 1991 Ford F-250 pick-up, a 2008 Mercury Milan, a 2008 Lincoln MXK, and a 2008 Mercedes-Benz GL320 CDI. Again, using BEP policy 612:25-6-21(d), these were vehicle expenses that were

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not allowed. There was a budgeted line item in the Fort Sill/ODRS contract for “amortized items” with a parenthetical “(Equipment, Vehicles),” but the amount budgeted for “Option period 1” was only [REDACTED].

Travel – Questioned travel expenses included fuel for Swanson Service, Inc. vehicles driven by Victoria Cantu, Deborah Welch and Barbara Swanson, pike pass billing, lodging in Lawton, Oklahoma for Swanson and Cantu employees, lodging, per diem, mileage, and car rental for two (2) individuals hired by Cantu to help with problems at Fort Sill, and expenses not supported by an invoice or receipt.

The mileage and vehicle expenses were limited per BEP policy 612:25-6-21(d). Lodging and meals for Swanson Services employees at Fort Sill/Lawton, Oklahoma (duty station) would not be considered a business expense, according to IRS rules and regulations. Additionally, it appeared expenses for Cantu employees should have been covered under fees charged by Cantu to Swanson Services. Therefore, they were included as questioned business expenses.

We noted a Fort Sill/ODRS contract budgeted line item for “subcontracting plan expenses” that included another parenthetical explanation “(Travel, etc.)” However, the amount budgeted for this vague line item was [REDACTED], compared to the over \$23,000 questioned costs reported above.

Interest – There were payments to the bank for lines of credit and automobile loans for the Lincoln MXK and Mercury Milan. The interest payments on the automobiles notes were questioned per BEP policy 612:25-6-21(d). In addition to the \$130,000 annual salary for the licensed manager and the \$132,000 annual salary paid to the wife of the licensed manager, the licensed manager made varying numbers of significant “draws” on the “profits” during the month reducing the bank balances of Swanson Services, Inc. Therefore, the interest payments for the line of credit were questioned as potentially unnecessary, if there had been more attention paid to the cash flow needs of *the business enterprise itself*.

Miscellaneous – The expenses questioned included flowers and plants for employees, donations to employees, maintenance and repairs on vehicles, more Christmas party expenses, equipment purchased without prior approval, meals, and payments not supported by an invoice. The flowers,

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plants, Christmas party, and donations for employees were not considered necessary to the actual operation of the dining facilities. The vehicle expenses and equipment purchases were questioned as per BEP policy 612:25-6-21(d) and 612:25-6-21(f), respectively. Meals for employees at the Fort Sill/Lawton, Oklahoma duty station would not be considered a business expense. Unsupported expenses were disallowed per BEP policy 612:25-6-21(c).

Fees – The set-aside charges were calculated on the net proceeds of the business enterprise per BEP policy 612:25-6-15(c) and net proceeds were defined by BEP policy 612:25-2-5. The definition for “net proceeds” specifically states the set-aside charges were to be excluded from expenses when calculating those net proceeds.

The second page of the monthly BEP report form used by ODRS/Swanson/Cantu had a section “D” to calculate the 12% set-aside fee. Generally, the set-aside fee was paid to ODRS in the month following the BEP report period. For example, the set-aside fee for October 2009 was calculated to be \$16,166.36 and was paid in November 2009. The November payment for October’s set-aside fee was charged as a “fee” expense on the November report, in effect *being included* in expenses when paid in the following month.

With the lone exception of the set-aside fee for January 2010, which apparently was overlooked in some sort of clerical “error,” all payments to ODRS for set-aside fees during the audit period were subsequently *included* in expenses, which in turn reduced the amount of net proceeds for calculating *later* set-aside fees, contrary to BEP policy and CFR regulations.

Some of the above questioned expenses may be considered “discretionary,” based on auditor judgment, such as questioning the line of credit interest charges. Other questioned expenses, such as the set-aside fees being included in operating expenses in subsequent months, were clearly contrary to both ODRS and federal CFR rules and regulations.

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Finding #2

According to Swanson himself, he had no input in the preparation of the monthly reports and calculating and/or verifying the set-aside fees.

During interviews with Mr. and Mrs. Swanson, Mr. Swanson stated that he had no input in preparing the monthly set-aside reports. Cantu Services collected all the information and they prepared the monthly report. Mrs. Swanson stated that Diane Hanson would fax them a copy of the report and then FedEx them the packet containing copies of the financial reports, supporting documents, invoices, etc. The statements by the Swansons were consistent with the Cantu outline of procedures included at *Appendix A*.

Mr. Swanson stated that he mainly reviewed the amounts in the equity/profit section of the reports; that he had trusted Cantu and the "State" (ODRS); and that he had expected that if there was a problem, either Cantu and/or ODRS would contact him to have the problem(s) corrected.

Mrs. Swanson stated that she reviewed the expenses and would call Diane Hanson (Cantu controller), if there was something on the report that she did not understand. Additionally, Mr. Swanson stated that Melissa Swanson, his daughter-in-law, would go through monthly expense packets to see if the expenses "...complied with what he was being charged for." In a subsequent interview, Mr. Swanson could not think of any examples of "errors" that had been noted that could or should have been reported to Cantu following the reviews by the Swansons.

Mr. Swanson indicated that his signature on the report and on the set-aside checks was a stamp, which was applied by Cantu Services. The original BEP report and set-aside checks were mailed *direct* to ODRS. This was confirmed in the Cantu outline of reporting procedures included in *Appendix A* and by phone interview with Diane Hanson, formerly the Cantu controller and presently a Swanson Services employee.

Review of images of the set-aside checks issued to ODRS during the audit period clearly indicate at least three different "A B Swanson" signature stamps were used. By phone interview, Diane Hanson confirmed there was more than one signature stamp used by Cantu.

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Finding #3

The procedures for transaction processing and reporting by Cantu, combined with the furnishing by Swanson of his signature stamp(s), provided virtually no “segregation of duties” for internal control purposes.

We observed from the outline in *Appendix A* that Cantu:

1. Processed all payroll and operating transactions;
2. Printed and issued all checks for payment of payroll and operating expenses;
3. Performed all bank reconciliations; and
4. Prepared all financial statements and reports.

As noted in *Finding #2*, the decision by Swanson to provide Cantu with signature stamps completed the near total lack of “segregation of duties” required for an effective internal control system. We were not engaged to review the internal controls for either entity. The observation made here is that there was no segregation of duties between the two entities and that all processes and reporting were controlled by Cantu with apparently little or no *effective* review or oversight by Swanson Services.

For a *multi-million dollar federally funded contract* that has been in place for nearly 10 years, this lack of attention on the part of *both Swanson and Cantu* to produce and provide reliable reports to ODRS, or to establish and maintain a system of strong internal control, is of considerable concern. The above findings may have significant implications for the over [REDACTED] in budgeted dining facility direct staffing expenses, which greatly exceeded the “site management” expenses related to the contract, and which are *not* covered in this report. Additional implications may exist for any other federally funded contracts for which Cantu is a “consultant,” contractor, and/or subcontractor.

In addition, we observed that although Cantu prepared the reports and submitted the reports directly to the ODRS, the reports *were* in the end Swanson Services’ reports and Swanson Services’ ultimate responsibility. The lack of attention exhibited by Swanson Services in the review of *its* monthly reporting to ODRS would seem contrary to BEP policies at 612:25-6-3 that describe the “licensed manager” in terms, such as “effectively managing” or “personally operate and manage” or “actively work(ing)” in the business enterprise.

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Finding #4

There were some differences between expenses deductible for set-aside calculation under ODRS-BEP policies versus some “site management” budgeted line item expenses chargeable to the Fort Sill/ODRS contract.

For the purpose of calculating the set-aside payments, the contract between ODRS and its licensed manager limits or disallows certain business expenses, as defined by regulation. Although some business expenses were not allowed per ODRS-BEP policies, similar business expenses were “budgeted” per the contract between the Army Contracting Agency and ODRS.

For example, BEP policy “612:25-6-21 Business expenses” states:

- (a) There will be *no mileage or vehicle expense* claimed as a business expense on the monthly report except as detailed at 612:25-4-61(g). (emphasis added)

The exception “detailed at 612:25-4-61(g)” refers to travel by a licensed blind manager between a primary and a “satellite/remote business enterprise location.” That policy is for travel between two entirely separate businesses and locations.

However, the Fort Sill/ODRS contract has specific site management budgeted line items for “Option period 1” for “mileage allowance” and “vehicle maintenance” in the amounts of [REDACTED] and [REDACTED], respectively.

Another apparent difference would be section (e) of BEP policy “612:25-6-21 Business expenses,” which states:

- (e) The amount of telephone charges claimed on each monthly report will be limited to a total of \$50.00 for all communication devices.

Fifty dollars per month would amount to a \$600 annual limit, but the Fort Sill/ODRS contract specifies a budgeted line item of [REDACTED] for “telephone system.”

The above examples of differences in contracts and rules illustrated some of the more unique aspects to the complexity of the Fort Sill/ODRS/Swanson multi-level administration of the Fort Sill dining facility operations. Expenses that may have been chargeable to the Fort

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Sill/ODRS contract (and reported to the Army Contracting Agency) were not chargeable or not allowed for the set-aside calculation report that went to the ODRS. One set of numbers was reported to the federal level. A different set of numbers was likely reported to the state level.

The Fort Sill/ODRS contract for the 12 month “Option period 1” *only budgeted approximately [REDACTED] for “operating costs,”* excluding payroll expenses and a [REDACTED] profit margin for “site management.” This report questions over \$600,000, just in the various “site management” operating costs that were factored into the set-aside calculation *reported to ODRS* in FY10. Additional “site management” *payroll* costs are questioned in **Objective II**.

The above differences noted between contract provisions and financial reporting for the federal level versus state reporting requirements partially helps to explain such a wide disparity in the amounts reported and questioned.

See Appendix E for relevant BEP policies.

Conclusion

Cantu prepared the monthly business enterprise reports for Swanson Services and prepared the set-aside checks mailed to ODRS, including stamping the Swanson signature. Whatever minimal review that occurred at Swanson Services only occurred “after the fact,” and the above findings would indicate the Swanson Services review was largely ineffective.

Our review of expense records for the 12 month period ending June 30, 2010, indicated that approximately \$625,000 in operating expenses did not comply with contract terms and/or BEP policies for calculating the set-aside charges, or were at least “questionable.” These questionable operating expenses had the effect of reducing the “net proceeds” upon which the set-aside fee was calculated resulting in both the potential under-reporting and under-payment of an estimated \$75,000 in fees to ODRS.

Subsequent Events

According to interviews, following the end of the audit period, Swanson initially contracted with Arney & Associates to prepare the monthly BEP reports, but later hired Diane Hanson (former Cantu controller) in May 2011. Also, *two* Swanson signature stamps have been returned by Cantu

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to Swanson Services, and those signature stamps are now controlled by Swanson Services employees.

The Swanson Services job duties assigned to Ms. Hanson include:

1. Assist in reviewing the financial records and reports prepared by Cantu and submitted to Swanson Services;
2. Prepare the monthly BEP reports to be filed with ODRS;
3. Utilize the signature stamps (now as a Swanson employee) on checks issued and reports;
4. Receive and review copies of the bank account reconciliations, emailing any corrections noted to Cantu.

We concur with these actions taken by Swanson Services as necessary first steps towards providing some segregation of duties between Swanson Services and Cantu. However, we also observe that Swanson is currently utilizing the same individual who was supervising the previous erroneous reports filed during the 12 month audit period of this report.

Additional care should be taken to ensure corrective measures are designed and implemented. Such corrective measures should be reviewed and verified on a regular and ongoing basis by the management of Swanson Services.

- Recommendations**
1. Swanson Services should review its contracts with ODRS and Cantu, review the applicable Federal and state laws, rules and regulations for the Business Enterprise Program and take all necessary measures to improve its BEP reporting and other accounting systems and functions.
 2. Swanson Services/Cantu should review their internal control policies and procedures to determine appropriate corrective measures to ensure coding errors, such as vehicle expenses charged to “Workers’ compensation insurance” and “General liability insurance,” are identified and corrected in a timely manner.
 3. ODRS should:
 - a. Review Swanson Services’ monthly BEP reports to determine the earliest occasion of set-aside fees being included in the reported operating expenses of subsequent months, and

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- b. Calculate the additional set-aside fees and penalties that would be due for the cumulative set-aside fee reporting errors from periods prior to FY10.
4. The same should be done for other questioned operating costs in excess of the contract amounts identified in the Fort Sill/ODRS contracted option periods, including those of prior years.
5. ODRS should evaluate differences between the Fort Sill/ODRS contract language and budgeted line items versus the BEP monthly report format and design a report and adopt policy modifications that reflect the unique nature and complexity of the Fort Sill based business enterprise.
6. The proper authorities at both the Federal and state levels should review these findings to determine any further action(s) to be taken.

Subsequent Event In response to recommendations by an OSAI performance audit report published in March 2011, the Department has already taken steps to revise some of its rules and regulations, including 612:25-6-21 that defines “Business expenses.” The proposed change to 612:25-6-21 would define allowable business expenses as a “flat-rate percentage of gross sales...using historical data and industry standards.”

OBJECTIVE II: *Determine if salaries reported on the monthly business enterprise reports were allowable.*

Background

The Fort Sill, Oklahoma site management salaries and specified positions were submitted and included in the Fort Sill contract with ODRS. The salary computations were submitted for a base period and four subsequent option periods. Also, certain fringe benefits were included, calculated on the total budgeted site management salaries.

The terms and conditions in the ODRS/Swanson contract, which includes the Business Enterprise Program (BEP) policies, were *not* specific with regard to the allowable salaries for calculation of the set-aside payment.

The Fort Sill/ODRS contract *was specific* in identifying “site management” salaries and positions for the base period and four option periods. Those contract provisions were used to compare with the salaries and fringe benefits paid and reported on the Swanson BEP monthly reports, as filed with ODRS.

Cantu provided us with the payroll records for the individuals holding these positions, with the exception of the “project manager” and “human relations” positions. Those two individuals were employees of Cantu, and their salaries were reimbursed to Cantu, instead of the individuals being paid directly as employees of Swanson Services. However, the project manager was paid a clothing allowance and some bonuses directly from Swanson Services.

Based on the payroll check registers for the individuals holding specific contract positions, the invoices for reimbursement to Cantu for the two Cantu employees, and additional information on staffing supplied by Cantu, we reviewed the salaries paid for the October 1, 2009 through September 30, 2010, “Option period 1.”

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Finding #1

The site management payroll costs exceeded the amounts agreed to in the Fort Sill/ODRS contract by significant amounts.

The total paid and estimated column for the period includes regular salary, bonuses, and clothing allowances, plus a percentage estimated for employer paid FICA (7.65%) and workers' compensation insurance (5.00%). The FICA and workers' compensation insurance percentages were applied to any *excess* salary, as well as to the bonuses and clothing allowances, not specified in the contract.

The management positions and salaries specified in the Fort Sill/ODRS contract were as follows for Option period one (October 1, 2009 to September 30, 2010):

Contract position	Salary- Option period 1	Actual salary paid	Bonuses & clothing allowances paid	FICA & Workers' Comp % estimated	Total paid and estimated	Amount questioned
Project manager						
Alternate project manager						
Area manager						
*Pers mgr/sub plan admin						
Property/quality control						
Quality control						
Quality control						
*Quality control						
Office manager						
Human relations						
Payroll clerk						
Office assistant						
Payroll clerk assistant						
Office assistant						
Temporary office assistant						
Totals						

***Note:** There was no personnel manager/subcontracting plan administrator employee during the audit period and one (1) quality control position was also not filled.

****Note:** Where the "Regular salary paid" did not exceed the budgeted amount, a minimum of the "bonus and clothing allowance" costs and related fringe benefit estimates were questioned.

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Other fringe benefits included unemployment taxes, annual and sick leave. For simplicity, we made no estimates of those additional costs, but those benefits would also add to the overall amounts to be considered for exclusion and/or questioned.

Finding #2

The original contract between Swanson Services and Cantu did not include provision for certain reimbursements to Cantu and payments to two Cantu employees.

The 1999 contract between Swanson Services and Cantu had no provision or apparent amendment that described how Cantu would supply two of *its* employees to fill two of the site management positions (project manager and human relations) detailed in the Fort Sill/ODRS contract. Consequently, the amounts to be reimbursed for salaries and related payroll taxes, the availability and use of company provided vehicles, and the agreement for any bonuses and clothing allowances for the two Cantu employees were undocumented in the contract or amendments.

In a subsequent interview, Mr. Swanson indicated there had been an agreement that Mr. Swanson had signed concerning the payment of certain bonuses. The “agreement” has only Mr. Swanson’s signature. There was no Cantu representative signing. There was also no rationale or justification specified to explain the bonuses, other than “per our phone conversation of today.” There was no explanation as to how the bonus amounts had been calculated or determined.

See Appendix C for the Swanson Services/Cantu bonus “agreement.”

Mr. Swanson indicated that he had signed the document based on Cantu’s assurances that project and alternate project managers in similar situations were being paid more than what Swanson/Cantu had been paying. Consequently, Mr. Swanson signed his approval for the bonuses only to find out later that the salary comparisons apparently supplied in the “phone conversation” were inflated. The Cantu employee who was project manager at the time was also the daughter of the founder of Cantu Services, Inc.

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Finding #3

Swanson Services charged three additional salaries that were not included or described in the positions for “site management” listed in the Fort Sill/ODRS contract.

In addition to the site management positions listed in the Fort Sill/ODRS contract, we noted salaries being paid to three (3) additional individuals for positions not specified or authorized by contract. These employees included A.B. Swanson’s wife, Barbara, Kimberly Martin, and Courtney Watson. According to an early interview with Mr. and Mrs. Swanson, the duties of these individuals were as follows:

- Barbara Swanson was A.B.’s reader, driver, paid the household bills and kept the household in good order. Additionally, Mrs. Swanson stated she reviewed the monthly packet, kept everything going at the Tuttle office, which included Swanson Services and everyday life events.
- Kimberly Martin was the secretary at the office located in Swanson’s house in Tuttle, OK.
- Courtney Watson performed administrative work and odd jobs at the Fort Sill office, but was not identified for a specific “site management” position.

The following schedule summarizes payments to the three (3) employees whose positions were not authorized by the Fort Sill/ODRS contract, but were charged on the monthly BEP reports. Percentage based employer costs for payroll taxes were estimated for FICA (7.65%), workers’ compensation (5.00%).

Employee	Salary	Bonuses	FICA/W.C.	Amount questioned
Barbara Swanson	\$132,000.00	\$21,656.74	\$19,437.58	\$173,094.32
Courtney Watson	44,212.50	2,362.50	5,891.74	52,466.74
Kimberly Martin	25,200.00	1,200.00	3,339.60	29,739.60
Totals	\$201,412.50	\$25,219.24	\$28,668.92	\$255,300.66

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Finding #4

The IRS form W-2 records for calendar year 2009 did not include the value of vehicle fringe benefits provided to the project manager and alternate project manager.

The “duty station” for project manager, Victoria Cantu, and alternate project manager, Deborah Welch, was an office building provided by the Military and located at Fort Sill, Oklahoma. Swanson Services provided the project manager with a Lincoln MXK and the alternate project manager with a Mercury Milan to drive, along with credit cards to purchase fuel and maintain the vehicles.

These vehicles were driven from their residences to and from work and for business related travel in the performance of their duties on Fort Sill and in the City of Lawton. We reviewed these two employees’ 2009 W-2 forms and determined that Swanson Services/Cantu had not included the use of the vehicles as a fringe benefit, as required by Internal Revenue Service (IRS) Publication 15 Employers Tax Guide, which states in part:

“Fringe benefits. You generally must include fringe benefits in an employee’s gross income (but see Nontaxable fringe benefits next). The benefits are subject to income tax withholdings and employment taxes. Fringe benefits includes *cars you provide*, flights on aircraft you provide, free or discounted commercial flights, vacations, discounts on property or services, memberships in country clubs or other social clubs, and tickets to entertainment or sporting events. In, general the amount you must include is the amount by which the fair market value of the benefits is more than the sum of what the employee paid for it plus any amount the law excludes.” (emphasis added)

The Mercedes-Benz provided to Mrs. Swanson as a “company” vehicle should also have been reported as a taxable fringe benefit on her W-2 for 2009.

Conclusion

We estimated the salaries and fringe benefits costs exceeded the amounts for site management positions authorized in the Fort Sill/ODRS contract by at least \$277,500, with approximately \$255,300 in additional questioned costs for unauthorized, non-contract employees included in the payroll costs charged to the BEP program. If these costs were excluded from BEP monthly report amounts, the effect would be a reduction in expenses of approximately \$532,800, resulting in an additional set-aside

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fee payable to ODRS estimated to be \$63,936 for the 12 month period ending September 30, 2010.

- Recommendations**
1. As before, ODRS should:
 - a. Review monthly BEP reports and other records to determine the earliest occasion of excessive and/or non-contract payroll costs being included in operating expenses, and
 - b. Calculate the additional set-aside fees and penalties that would be due for the cumulative payroll reporting errors from periods prior to FY10.
 2. Swanson Services/Cantu should prepare and submit corrected W-2 forms to include the fringe benefit value of providing company vehicles for 2009, likely 2010, as well as prior years (as necessary) for the above employees.
 3. The proper authorities should review these finding to determine any other action(s) necessary.

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OBJECTIVE III: *Determine if a service was provided to Swanson Services, Inc. for invoices submitted and paid to B & J Activities and that the service, if any, was an allowable business expense.*

Background

B & J Activities, LLC (B & J) is a limited liability company that was originally filed for organization by Barbara J. Swanson on July 8, 2005, terminated on March 26, 2007, and then reinstated on April 29, 2010.

B & J submitted the following invoices described only as “total consulting fee” to Swanson Services for payment:

Invoice date	Invoice no.	Amount	Swanson check date
10/16/09	488	\$58,240	11/02/09
11/30/09	541	52,510	12/03/09
12/31/09	692	52,510	01/08/10
01/31/10	791	52,510	02/16/10
02/28/10	1228	52,510	03/02/10
Total		\$268,280	

The invoices submitted by B & J were not specific as to the actual product or service provided to Swanson Services. As previously noted in **Objective I**, these B & J invoices were included in the questioned operating costs identified in that section of our report.

The above invoices were reported on the five monthly BEP reports for the period of November 2009 through March 2010. All were clearly reported as a separate line-item on each of those five reports.

In the spring of 2010, the ODRS BEP operations coordinator began questioning the B & J Activities line-item expense on the monthly BEP reports filed with ODRS. A letter dated May 7, 2010, was issued to Swanson Services requesting more detail of the B & J transactions. Subsequent responses by Swanson Services included the notification to ODRS that the payments to B & J had “...been reclassified as a draw to ‘A. B. Swanson,’” in effect charging the entire \$268,280 to Mr. Swanson’s equity or profit margin, rather than to “expenses.”

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With a letter dated July 2, 2010, Swanson Services filed “amended” reports for the above time period, deleted the B & J invoice amounts on the amended reports, and issued a Swanson Services check #19431, dated June 30, 2010, in an offer to pay \$32,193.60 in additional set-aside fees (\$268,280 x 12%). The check was returned by ODRS pending additional inquiry, including this report.

Finding #1

The term “ratably” was a tacit admission on the part of the Swanson Services accounting firm that the B & J invoices were not related to specific actual goods or services supplied to Swanson Services.

To charge expenses “ratably” is terminology normally used in cost accounting for “overhead” items that are allocated based on units of production or time. General administrative salaries, utilities, general types of insurance, certain indirect materials costs, etc. are estimated and allocated on a rate per unit basis, as a matter of matching production costs to the actual production of a product or services. Although “rates” are used for allocation purposes, the expenses underlying those rate estimates are “real time” actual expenses that are accumulated, evaluated, finalized and adjusted as necessary at the end of a production run or time based project.

Both IRS guidelines and audit standards recognize that the allocated expenses are “real” with terms, such as “actual,” “documented,” “ordinary,” “necessary,” and “reasonable.” Those terms would not seem to apply in this situation.

In a two-page letter dated July 14, 2010, the Swansons’ accountant, David Arney of Arney and Associates submitted “clarification” of the B & J invoices, summarized as follows:

1. The invoices were part of a “business plan” designed to “locate possible accounting firms, business consultants, legal counsel teams, food contractors, and job specific contractors and consultants.”
2. At Arney’s suggestion, B & J billed Swanson Services “ratably,” subsequently explaining that “ratably” meant something similar to “...an individual accumulating funds to pay an annual house insurance bill or annual property tax bill.”

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3. “It was our understanding from Cantu that this was 100% AB’s expense and it would not affect their (Swanson/Cantu) profit percentage.”
4. Cantu was responsible for the “...coding decision to cause this expense to effect [sic] set-aside.”
5. There was “no intention of affecting the contract...never our intention to adversely affect the State,” i.e. by inflating expenses to reduce the set-aside payment.

The Arney letter included an attachment titled “Ledger for B&J-Swanson Services” that resembled a simple spreadsheet showing \$8,600 in four equal payments to “True Solutions” and the five deposits from the B & J invoices totaling \$268,280, leaving an ending ledger balance of \$259,680, as of “3/25/10.”

See Appendix D for the Arney letter and attachments.

A second attachment was another undated spreadsheet or table indicating the following:

Description	Projected Budget	Billed to Date	Remaining Budget
Management Consulting	\$47,750	\$29,671	\$18,079
Auditing	\$75,000	\$0	\$75,000
Systems, Tax Consulting, Business Planning	\$100,000	\$37,240	\$62,760
Specialized Business Consultants	\$275,000	\$72,428	\$202,572
Profit Margin Forecast 22%	\$138,100	\$0	\$138,100

Although there was no “total” line, the above would seem to indicate a “projected budget” of \$635,850 for the total amount to be invoiced to Swanson Services, including the projected profit margin of \$138,100 ($\$138,100 / \$635,850 = 21.72\%$). The “billed to date” column apparently represented costs billed *to* B & J, since B & J had already invoiced Swanson Services for \$268,280 by March 2010, four months prior to the July letter with the above attachment.

We also observed that based on the first five invoices submitted, the apparent intent was to bill \$52,510 per month for an additional seven months to reach the \$635,850 projected budget amount: $\$58,240 + (11 \times$

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\$52,510) = \$635,850. This was later confirmed by phone interview with Mr. Arney.

The above attachments to the Arney letter indicate that the \$268,280 in B & J “consulting services” invoiced to Swanson Services were not for actual goods and/or services “delivered,” but rather for yet mostly future “projected costs.” The term “blue sky” is sometimes used to describe this type of invoice where there are no *specific* goods or services provided that relate to the amount billed.

In a subsequent interview, in addition to using the insurance premium analogy, Mr. Arney offered that some consulting services were “ratably” billed in the “oil and gas” industry. Both analogies are irrelevant. In the government sector, goods and services are billed when rendered, not when “budgeted” or “projected.” In the Oklahoma Central Purchasing Act, 74 § 85.44B states, in part:

Payment for products or services pursuant to a contract executed by a state agency, whether or not such state agency is subject to the Oklahoma Central Purchasing Act, Section 85.1 et seq. of this title, shall be made only after products have been provided or services rendered. (emphasis added)

In addition, the BEP policies include similar language at 612:25-6-21 (c) which states, in part:

“The expense column on the monthly report should reflect the actual expenses incurred by the business enterprise.” (emphasis added)

We recognize that the Swanson/B & J transactions were technically between two private sector entities, but these transactions were directly related to the Fort Sill/ODRS/Swanson contracts and would not have occurred but for the existence of those two federal and state government contracts. Inclusion of the B & J expenses on the Swanson monthly BEP reports had a direct impact on the amount of the set-aside fee calculation for the five month period ending March 2010.

Besides the Arney letter, a letter from Swanson’s attorney seemed to confirm the invoices were at least partially for “future” services. The letter stated in part:

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"Mr. Swanson elected to have B & J Activities, LLC ("B & J") contract with Swanson Services, Inc. to enhance his ability to operate the Ft. Sill contract. As explained more fully below, *the idea is to acquire consulting services* to assist Mr. Swanson in achieving his maximum vocational potential. Doing so through B & J contains certain business advantages. *There is no doubt the acquisition of present or future consulting services is a legitimate business expense.*" (emphasis added)

The purchase of consulting services can be a legitimate business expense, but charging for "future" consulting services in the governmental sector is problematic, and the Fort Sill/ODRS/Swanson contracts were certainly in the governmental sector. B & J was a "sister" company, wholly owned by the Swansons. We consider it highly improbable that Swanson Services would pay what amounted to substantial "advances" to any other ordinary vendor that was not such a "closely related" company.

Finding #2

A certified Cantu letter dated December 31, 2009, only addressed the B & J invoices in terms of the profit split between Cantu and Swanson Services.

In early interviews, the Swansons maintained that it was not their intention that the B & J invoices affect the set-aside fee to be paid ODRS. With regard to the B & J invoices being clearly reported as a separate line-item on the monthly reports, Mrs. Swanson indicated she had seen the B & J invoice amounts on the report, but that "...it never registered." The Arney letter described in **Finding #1** placed blame squarely on Cantu's "coding decision" for the inclusion of the B & J expenses on the monthly BEP reports.

A copy of a certified letter from Cantu to A. B. Swanson was included as an attachment to a letter from Mr. Swanson's attorney to the ODRS, dated July 16, 2010. The certified letter from Cantu dated December 31, 2009, was delivered to Mr. Swanson following the payment of the first two of the five B & J invoices. Cantu sought Swanson's agreement and acknowledgement that the B & J invoices would be excluded in calculating the profit split between Swanson Services and Cantu.

The letter signed by A. B. Swanson, as of January 5, 2010, included that Swanson was accepting "any risks" associated with the Swanson Services

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payments to B & J Activities. Following that letter and agreement, Cantu excluded the next three (3) invoices from, and payments to, B & J from the calculation of the Swanson Services/Cantu profit split. From the reports we reviewed, no adjustment was made by Cantu to the profit split for the first two B & J invoices that were paid *prior* to the certified letter being agreed to by Mr. Swanson.

See Appendix B for the copy of the Cantu letter.

In a more recent interview, Mr. Swanson again maintained that there was no intention to have the B & J invoices affect the set-aside fee paid to ODRS. In addition, John Elam (dba True Solutions), a business consultant for Mr. Swanson, indicated that the Cantu letter concerning the profit split had been interpreted as implying that B & J invoices/expenses would also be excluded *from the set-aside calculation* for ODRS.

A simple, straight-forward reading of the Cantu letter indicates there were three main points or topics:

1. Cantu WAS seeking to exclude the B & J expenses “for the purposes of calculating the division of profits” (between Swanson Services and Cantu);
2. Cantu WAS NOT offering “advice as to the tax consequences,” apparently a reference to B & J Activities being described by David Arney as utilized, in part, for “tax reasons;”
3. Cantu WAS offering advice “as your contract consultant...that claiming this expense could negatively affect the status of your contract.”

The July 16, 2010, letter from Swanson’s attorney again asserted that Cantu was responsible, since they offered “...no explanation to Mr. Swanson as to how his contract would be negatively affected.”

We observe that although Cantu may have offered “no explanation,” according to our interviews, Swanson apparently made no attempt to *seek an explanation or clarification*, whether by letter or certified letter or email or any other form of written communication. The “misunderstandings” and “miscommunications” alluded to by Mr. Swanson and his representatives would seem to be more a “lack of communication” on the part of Swanson Services.

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Now, in retrospect, Swanson Services is asserting that the exclusion of the B & J expenses from the “profit split” calculation should also be interpreted to have applied to the “set-aside” calculation; and that Swanson relied upon this “implication;” and therefore, any misunderstanding or miscommunication with regard to including the B & J expenses on the ODRS monthly reports should be Cantu’s responsibility.

All of which is asserted in light of the fact that the B & J expenses were plainly reported each month as a separate line-item for five consecutive months, giving Swanson Services ample opportunity to correct Cantu’s “error” or “coding decision” in a more timely manner. We observed the attempt to correct the “error” or “miscommunication” by Swanson Services occurred only after the ODRS had raised the issue and began questioning the nature and relevance of the B & J consulting expenses.

Conclusion

Based on the information developed, B & J Activities billed Swanson Services for unspecified “total consulting fee(s)” for undocumented (except by the B & J invoices) services that at the time of billing had largely not yet been provided or rendered. Since the Swansons owned and operated both companies, it is reasonable to conclude that they were aware of these facts.

Swanson Services was notified by Cantu of a potential problem in claiming the expenses at the end of December 2009, yet allowed and/or authorized payment of three additional invoices, totaling \$157,530 through March 2010. There was also the apparent intention of billing seven more invoices at \$52,510 per month, until the planned budget of \$635,850 had been reached.

Whether by design or “error” or “miscommunication,” including the \$268,280 amount of invoices for B & J Activities on the monthly reports resulted in the underreporting and underpaying of set-aside fees to ODRS, in the amount of \$32,193.60.

We concur with one aspect of the Swanson Services/B & J Activities’ business plan. Swanson Services would benefit from the addition of more professional accounting and auditing services, and implementing the purchase of those services would likely pay for itself by reducing the need for legal services.

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Recommendation The proper legal and/or regulatory authorities should review this finding to determine whatever further action is deemed appropriate.

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OBJECTIVE IV: *Confirm that checks issued to ODRS for set-aside fees were received and deposited.*

Background

The checks issued by Swanson Services to ODRS for the monthly set-aside payments were paid to the order of:

OKLAHOMA REHAB SERVICES
CURTIS CUNNINGHAM BEP/VS33

We obtained copies of the checks issued by Swanson and a printout of the check register for Swanson vendor number "6060," "Oklahoma Rehab Services..." for the period of July 1, 2009 to August 20, 2010, the date of deposit for the June 2010 set-aside fee.

Using the monthly business enterprise business reports submitted to ODRS, we calculated the set-aside payments due, *as reported on the monthly business enterprise facility reports*. The amounts were verified to a copy of the check issued and confirmed to have been deposited into the ODRS bank account by records supplied by ODRS finance staff.

Finding

Based on the sales and expense figures reported on the monthly business enterprise reports, *prior to excluding any questioned expenses noted in Objectives 1 and 2*, the set-aside fees were properly calculated, and the Swanson checks issued for set-aside fees were received and deposited by ODRS.

Recommendation

No recommendation is provided for this objective.

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OBJECTIVE V: *Determine if fees paid to Cantu Services, as reported on the monthly business enterprise facility reports, were properly calculated in accordance with their agreement.*

Background

In September 1999, Swanson Services, Inc. entered into a “Management Support Agreement” with Cantu Services, Inc. of Wichita Falls, TX. This agreement provides that Cantu will provide “management services and administrative support necessary to ensure satisfactory performance of the contract” for the Swanson Services, Inc. food services contract with Fort Sill/ODRS.

The Swanson/Cantu contract provides that Cantu receive a fee consisting of thirty-nine percent (39%) of the *net contract receivable (profit)* and for the administrative support, general and administrative expenses, a fee of three and one half percent (3.5%) of the *contract operating cost*.

The “net contract receivable” was defined as:

“...the amount remaining of the total contract receivables after payment of all contract operating costs incurred during the contract performance period (generally 12 months, but may also include a lesser or greater period as may constitute a complete contract period.)”

The “contract operating cost” was defined as:

“...all costs directly associated with the performance of a contract including prompt payment discounts, non-performance deductions, monthly reimbursements for ADMINISTRATIVE SUPPORT SERVICES AND REIMBURSEMENT FROM G&A.” (emphasis in the original)

Finding #1

Based on the amounts reported on the monthly business enterprise reports, *prior to excluding any questioned expenses noted in Objectives 1 and 2*, it appeared the consulting/management support fees paid to Cantu, Inc. were being properly calculated, and the distribution of “net contract receivables” was consistent with the management support agreement between Swanson and Cantu.

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Finding #2 Based on the amounts reported on the monthly business enterprise reports, prior to excluding any questioned expenses noted in Objectives 1 and 2, it appeared the general and administrative fees prepared and submitted by Cantu were being properly calculated, in accordance with the management support agreement.

Recommendation No recommendation is provided for this objective.

Subsequent Events and Conclusion Concurrent with the request for this investigative report, the Department also requested an OSAI “performance audit” on its Business Enterprise Program. That report was published in March 2011.

Various issues described in that report also have some bearing on the findings in this report, as well as similarities to the problems reported here. One major difference in the Fort Sill/ODRS/Swanson business enterprise is the sheer size and complexity of the Fort Sill food services operations.

Thousands of meals per day are served at multiple locations and facilities on the base, requiring the employment and management of hundreds of unionized hourly food service employees. The management of a business enterprise of this magnitude would be challenging for any individual or company, even under the most advantageous of circumstances.

On August 5, 2011, a “Notice of Termination,” was issued by ODRS to Mr. Swanson. The notice applied to the “Business Enterprise License” of Mr. Swanson and cited various reasons for the termination.

Cantu Response The OSAI received a 4 page letter of response from Cantu Services with a request to include the response in this report. While Cantu is referred to in our report, the focus was on the ODRS/Swanson Contract, and Cantu was not a party to that contract. The Cantu response does include several points upon which we concur, as well as some on which we do not:

1. Regarding the erroneous set-aside reporting, *Cantu’s profit split was also negatively impacted* by the inclusion of the set-aside fees in the following months’ reporting, and it is reasonable to conclude Cantu Services would not have intentionally or knowingly damaged themselves with that error.

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2. While our report mentions the daughter of the Cantu Services founder, we did not report the fact that, in addition to Swanson's wife's salary reported in Objective II, other Swanson family members were *in prior periods* paid by Swanson Services and charged in the contract amounts reported to ODRS. We were made aware of that information, but did not include it due to our focus being on the FY10 audit period, with the exception of the one fiscal quarter extension (to September 30, 2010) being used for the payroll comparisons in Objective II.

However, the amounts paid to the two other family members of Mr. Swanson were significantly less than the compensation afforded to Mr. Swanson's wife and Mr. Cantu's daughter, based on the information provided. It should also be noted here that Mr. Cantu's daughter was filling an actual management position specified in the Fort Sill/ODRS contract, whereas Mrs. Swanson was not.

3. We concur that the preparation of the monthly ODRS reports was not part of the original "Manager Support Agreement" between Swanson and Cantu, and that Swanson was the ultimate party responsible for the accuracy of the ODRS reports, a point that we make clear in our report. However, we find it incredible that Cantu Services management was somehow unaware that their "comptroller" was preparing or supervising the preparation of the ODRS reports and that "Cantu Services took swift and immediate action once it knew..." that its accounting staff had been performing that function. We observe the preparation of the ODRS reports for Swanson was not a recent development, and the above lack of awareness apparently continued for years.
4. We do not concur that the vehicles provided by Swanson Services "were not actually given to the employees" and therefore were not taxable fringe benefits. The IRS rules and regulations we cited are clear in this matter. We corrected our report to include the Mercedes-Benz provided Mrs. Swanson, which was also not reported as a taxable fringe benefit on her W-2 for 2009.

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Disclaimer In this report, there may be references to state statutes, Attorney General's opinions and other legal authorities which appear to be potentially relevant to the issues reviewed by this Office. The State Auditor and Inspector has no jurisdiction, authority, purpose or intent by the issuance of this report to determine the guilt, innocence, culpability or liability, if any, of any person or entity for any act, omission, or transaction reviewed. Such determinations are within the exclusive jurisdiction of regulatory, law enforcement, and judicial authorities designated by law.

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*APPENDIX -A- Cantu Services' Outline for Preparing Swanson Services, Inc.'s
Monthly Business Enterprise Report.*

September 17, 2010

Mr. James Dickerson
Investigative Auditor

Mr. Dickerson,

Per your request, I have outlined below the expense process and how invoices are received, paid and ultimately flow to the Swanson Oklahoma Business Enterprise Report.

Swanson Services, Inc. has three accounts – Money Market, Payroll and Billing. The money market account primarily is used to receive the EFT payments from Defense Finance & Accounting (DFAS) and to transfer to the other two accounts as needed enabling the maximum amount of interest to be earned. The Payroll account is used to pay the employees their paychecks, and the Billing account is used to pay the bills. Cantu's office maintains blank Payroll and Billing checks, pays the bills for Swanson Services, Inc. and utilizes an A.B. Swanson signature stamp. Copies are provided in a packet to the Swanson's on a monthly basis. The packet includes the following items:

- Bank Statements & Reconciliations
- Copies of Other Misc Banking Transactions – i.e. Lines of credit advances,
Transfers between accounts, petty cash reimbursements
- Payroll Check Registers
- Copies of Employee Benefit Checks (pension/training/union)
- Copies of Invoices Paid with Check Stub attached
- Copies of the Semi-Monthly Invoice to DFAS for Services Performed
- Computation of Accrued Vacation & Sick Leave
- Financial Statements*
- Copy of OK Business Enterprise Report, and related documentation – i.e.
Check Register and Cantu Profit Computation*

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*These two items are also faxed to the Swanson's home generally prior to mailing the OK Business Enterprise Report with payment. Cantu's Controller, Diane Hanson, calls Mr. & Mrs. Swanson to make sure they are home prior to faxing.

The majority of Swanson's bills are mailed directly to the Fort Sill location and are then forwarded to Cantu's office for payment either by mail, or hand-carried from Deborah Welch to Robert Welch to Cantu's Payroll Clerk. Below is an outline of the monthly bills that are received for payment:

Euclid Street Office:

Monthly bills associated with the Euclid Street office are Lawton Board of Realtors, Public Service Co of Oklahoma, AT&T, and the City of Lawton. These bills are mailed to Fort Sill, and are then forwarded to Cantu for payment with the exception of the Lawton Board of Realtors. The monthly rent of \$675.00 is based upon a contract; therefore, this expense is automatically paid at month-end with no corresponding invoice.

Uniforms:

The Euclid Office is responsible for the uniforms. Cantu's office receives faxes throughout the month from the Euclid office. These are accumulated and matched up against the invoice received from Phoenix Textiles. The Phoenix Textiles invoice is mailed to the Fort Sill Office and forwarded to Cantu's office for payment.

Bank of America:

The credit card statements for Mr. & Mrs. Swanson, Deborah Welch and Victoria Cantu are mailed to the Cantu office for payment. Cantu pays the bill from the statement as there are no receipts provided from Mr. & Mrs. Swanson.

Payroll Benefits:

The Collective Bargaining Agreement (CBA) outlines the computation of benefits for union employees. The payroll clerk at Cantu's office computes these benefits in accordance with the CBA, and mails the reports and payment directly to LIUNA for Pension/Training and Union Dues.

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Petty Cash Items:

The Fort Sill Office Manager (now Shirley/prior Sue) is responsible for the petty cash. Twice a month, a spreadsheet with receipts attached is forwarded to Cantu's office for payment. A request is made to the bank for a cashier's check payable to the Office Manager. The OM cashes the check and reimburses the petty cash account.

Attorneys:

Attorney bills are mailed directly to Cantu's office and are directed to Robert Welch. Mr. Welch sends an e-mail or phones Mr. Swanson for his approval to pay.

Phones/Internet:

There are multiple companies involved including Verizon, Sudden Link and AT&T. There are two Verizon bills: one for the managers phones at Fort Sill and this bill is mailed directly to Fort Sill and forwarded to Cantu for payment. The other Verizon bill is mailed directly to Cantu's office for payment and is for Mr. & Mrs. Swanson's (and Adrian Villesca?) cell phones. Sudden Link is an internet service and is mailed to Fort Sill and forwarded to Cantu for payment.

Workers Compensation:

Fort Sill management has the ability to drug test employees who exhibit unusual behavior or have a work related accident. Allied Health Resources and AM PM Clinic provide these services. The invoices are mailed to the Fort Sill Office and forwarded to Cantu for payment. Also, Liberty Mutual is the insurance carrier for Swanson Services, Inc. Generally, all the policies are lumped together and 20% is paid down with the balance being auto-drafted over a period of months. There is a statement mailed directly to Cantu indicating that Liberty is going to auto-draft the payment.

B&J:

Mr. & Mrs. Swanson would mail an invoice to Cantu for payment.

Cantu Services, Inc.:

Cantu Services receives several checks from Swanson Services. Monthly Swanson pays Cantu for accounting services which were previously

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contracted to an outside source, Gary Wayne Crouch, P.C. Upon Cantu hiring their Controller, the preparation of the financials remained in-house and Cantu bills Swanson \$330/month, the same amount paid to the outside accountant. Swanson also reimburses Cantu for American Express charges made on behalf of Swanson by Cantu staff. These charges generally are for travel arrangements, vehicle fuel, or advertising for positions at Fort Sill. Cantu's proposal for the Fort Sill contract included a percentage for Cantu's General & Administrative (G&A) expenses. At the end of each month, Swanson pays Cantu \$21,000, and the additional G&A computed is settled up at some future date. Cantu's profit split is 39%. This amount is computed monthly by Cantu and is paid to Cantu as requested.

Swanson Dividends:

The only "scheduled" Dividends are that Swanson draws \$5,000 on the 15th and the last day of the month. A wire transfer is initiated by Cantu's payroll clerk and is wired to Swanson's bank account in Tuttle. Also, Cantu's VP of Administration, Vanessa Liston, oversees the payment of Mr. & Mrs. Swanson's personal tax estimates which are made in accordance with IRS deadlines. The tax estimate amounts are provided to Cantu's VP by either the Swanson's or their accountant, David Arney (Arney & Associates). All remaining dividends are initiated by Mr. or Mrs. Swanson calling Cantu's Controller, and instructing the amount to forward and the receiving bank.

Swanson Services Inc. financials are generally prepared prior to the close of the following month (i.e. June 30 financials are completed and faxed to Swanson's by July 31). Cantu's Controller asks Cantu's payroll clerk for the number of employees for the Business Enterprise Report. Cantu's Controller does not adjust the number of disabled employees unless notified to do so by Swanson's. Cantu's Controller reconciles the bank accounts and makes a handful of adjusting entries. These entries are accruals for payroll, payroll taxes, payroll benefits, computation sick/vacation leave estimates, depreciation etc. Cantu's Controller prints a Cash Management G/L Distribution Report on all bank accounts. This reports details the check written and to which General Ledger (G/L) account the expense is posted. This information is detailed in a Check Register spreadsheet which is linked to the OK Business Enterprise Report and the expenses flow from the Check Register spreadsheet to the Enterprise Report. Cantu's Controller then

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computes the additional G&A due to Cantu and records that entry. The additional G&A entry is added to the Check Register spreadsheet which is linked to the Business Enterprise Report. The Business Enterprise Report spreadsheet computes the Set Aside and Cantu's Controller then posts that entry to Swanson financials. Lastly, the profit computation is made and all the reports are printed. Cantu's Controller then calls Mr. & Mrs. Swanson prior to faxing the Financials, Business Enterprise Report, Check Register Spreadsheet and Profit Split Computation Spreadsheet. Cantu's Controller gives the first three pages of the Business Enterprise Report to Cantu's payroll clerk for payment and mailing. The Cantu payroll clerk for Swanson Services stamps Mr. Swanson's name on the report, writes the check to OK Rehab Services C/O Curtis Cunningham and mails.

The Cantu payroll clerk then mails the packet to Mr. & Mrs. Swanson containing the items outlined above.

Should you have any additional questions or need further clarification, please do not hesitate to contact me.

CANTU SERVICES INC
Diane Hanson, Controller

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APPENDIX B: *Letter Concerning B & J Activities, LLC.*



CANTU SERVICES, INC.

P.O. Box 8325
Wichita Falls, TX 76307

308 Mississippi
Wichita Falls, TX 76301

Phone: (940) 761-9720
Fax: (940) 761-9726

December 31, 2009

CERTIFIED MAIL
RETURN RECEIPT REQUESTED
NO. 70080500000041846441

Mr. A. B. Swanson
1059 County Street 2928
Tuttle, OK 73089

Re: Payment of Invoices from B & J Activities, Inc.

Dear Mr. Swanson:

This letter is to confirm your instruction to Cantu Services, Inc. ("Cantu") to pay invoices from B & J Activities, Inc. ("B & J") for consulting fees. It is our understanding that Cantu is to pay the invoices as submitted by B & J without prior approval from you as a regular part of the food service operations and contract at Fort Sill. The amounts paid to B & J will not be included as a regular expense for purposes of calculating the division of profits between Cantu and Swanson Services, Inc. ("SSI"). In other words, SSI will bear 100% of any amounts paid to B & J.

Cantu is not offering any advice as to the tax consequences of the transactions with B & J. However, as your contract consultant, Cantu must advise you that claiming this expense could negatively affect the status of your contract.

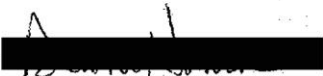
If Cantu's understanding as to the payment of invoices is correct and you are willing to accept any risks associated with these payments. Please so indicate by

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your signature below and returning the same to us in the enclosed addressed and stamped envelope. The extra copy of this letter is for your records.

Very truly yours,

CANTU SERVICES, INC.

By 
Diane Hanson, Controller

CANTU IS DIRECTED AND AUTHORIZED
TO MAKE PAYMENTS TO B & J AS SET FORTH ABOVE.
A. B. SWANSON AND SSI ACCEPT ALL RISKS
ASSOCIATED WITH SUCH PAYMENTS.



A. B. Swanson, individually and as President of
Swanson Services, Inc., an Oklahoma corporation, on
behalf of such corporation

Date: 1/5/10

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APPENDIX C: *Documentation for Bonuses Paid to Project Manager and
Alternative Project Manager.*

MAR-12-2010 12:21 From: CANTU SERVICES, INC. To: 14053812104 Page: 1/1

03/12/10


MR. & MRS. A.B. SWANSON:

PER OUR PHONE CONVERSATION OF TODAY:

VICKEY CANTU WILL BE GETTING A QUARTERLY BONUS OF GROSS \$22,000.00

DEBBIE WELCH WILL BE GETTING A QUARTERLY BONUS OF GROSS \$18,000.00

THESE BONUSES WILL BE PAID IN THE MONTHS OF MARCH, JUNE, SEPTEMBER
AND DECEMBER AND DATED THE 15TH. THERE WILL ALSO BE A YEARLY 3%
INCREASE FOR SALARIED POSITIONS.


APPROVED BY: _____

MAR 12, 2010 11:47A

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page 1

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APPENDIX D *Letter and Spreadsheets supplied by Arney & Associates*

P.O.BOX 1014
MOORELAND, OK 73852
580-994-2535,2541 OFFICE
580-994-2542 FAX
david@arney-tax.com

ARNEY & ASSOCIATES, INC.

July 14, 2010

Michael O'Brien, Ed. D.
Director, Oklahoma Department of
Rehabilitation Services

Re: A B Swanson, Ft Sill Contract Manager/ B & J Activities, LLC

Dear Mr. O'Brien:

In clarification of the B & J Activities, LLC (B&J) contract payments, I apologize for not bringing out the basic plan & purpose earlier. It is not a problem to explain this simply. AB Swanson hired our firm to take the lead on creating a business plan whereby he could better fulfill his contract as a blind vendor according to Randolph-Sheppard Act 20 (RSA) USC Sec 107 et seq. It was his belief that his teaming partner, Cantu Services Inc., (Cantu) did not communicate with him adequately and did not serve him in keeping with the RSA to become a completely independent contractor.

Specifically, he wanted us to develop this plan with categories and budgeted amounts that we deemed appropriate to achieve his ends. Through our research we ended up with four main categories. In our best effort, we assigned amounts gained from inquiry and best estimates available to those categories. In this process we began to locate possible accounting firms, business consultants, legal counsel teams, food contractors, and job specific contractors and consultants. After the initial assignment of categories and amounts, we were to monitor this process and funds to see if we need to modify the amounts or categories. In implementing this strategy, we suggested B&J bill Swanson Services Inc. (SSI) ratably so that cash flow would not be adversely affected. Also, it could decrease his normal draw from profits by that specific amount and SSI would pay its own expense, which in our view is required by the IRS. Mr. Swanson elected to contract the consulting work between the entities, B&J and SSI in an effort to fulfill his work, potential and opportunity as a Licensed Manager under the RSA. It is our opinion that as the manager of B&J and President of SSI, Mr. Swanson is fully able and


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responsible to pursue the best business practice as an independent contractor and business owner. It is our opinion that Mr. Swanson is not allowed by the IRS to deduct these reimbursable expenses personally, therefore it is correct for B&J to pay the expenses for the work that fulfills its contract with SSI.

The ratable idea mentioned above works like an individual accumulating funds to pay an annual house insurance bill or annual property tax bill. The accumulated funds were necessary for B & J in order to pay large one-time expenses forecasted to become due within the year ahead. It was our understanding from Cantu that this was 100% AB's expense and it would not affect their profit percentage. Like his usual draw from profits for estimated taxes or anything else, it was simply funds from his drawable profit to fund his business plan for the greater good of his contract which should not affect the State except eventually make them more money. Cantu, as the responsible party for overseeing and completing OKDRS monthly reports, made the coding decision to cause this expense to effect set-aside. In conversations with Cantu during this time I informed Diane Hanson that we had no intention of affecting the contract and that this decision was a business decision to benefit A.B. in pursuing his business goals. As I have stated before, it was never our intention to adversely affect the State. Cantu contracted to do reporting to the government so I make no assertion to their accuracy in that regard or what cloud their reporting might have caused on this good plan.

We will provide a spreadsheet that has our summary plan & funds broken out for your convenience and your viewing.

Sincerely,



David Arney, Vice-President
Arney & Associates, Inc

Cc: AB Swanson, Joe Walters, Scott LaBarre, Robert Humphreys, John Elam

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07-15-10 ODRS Letter
 Attachment

Ledger for B&J-Swanson Services

Check Number	Date	Transaction Description	Payment	Deposit	Balance
	11/5/2009	Deposit		\$58,240.00	\$58,240.00
3669	#####	True Solutions	\$2,150.00		\$56,090.00
	12/9/2010	Deposit		\$52,510.00	\$108,600.00
3722	1/14/2010	True Solutions	\$2,150.00		\$106,450.00
	1/15/2010	Deposit		\$52,510.00	\$158,960.00
3757	2/15/2010	True Solutions	\$2,150.00		\$156,810.00
	2/22/2010	Deposit		\$52,510.00	\$209,320.00
3774	3/25/2010	True Solutions	\$2,150.00		\$207,170.00
	3/2/2010	Deposit		\$52,510.00	\$259,680.00

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Arney & Associates, Inc.
 07-15-10 ODRS Letter
 Attachment

B & J Projection Including Profit

Description	<u>Projected Budget</u> Amounts	<u>Billed To Date</u> Amounts	<u>Remaining Budget</u> Amounts
Management Consulting: True Solutions	\$47,750	\$29,671	\$18,079
Auditing: Scott Hatch Hastch,Croke & Associates 3yr audit,specific procedures audit, and audited annual F/S	\$75,000	\$0	\$75,000
Systems , Tax Consulting and Business Planning: Payroll & Bookkeeping System Arney & Associates, Inc CSA,Tax Consulting & Plan	\$100,000	\$37,240	\$62,760
Specialized Business Consultants: Legal Team & Retainers Food Contract Consultants Job Specific Consultants	\$275,000	\$72,428	\$202,572
Profit Margin Forecast 22%	\$138,100	\$0	\$138,100

APPENDIX E *Excerpts from Oklahoma Administrative Code*
(emphasis added in yellow highlight)

612:25-1-1. Purpose

- (a) The purpose of the Business Enterprise Program Manual is to provide uniform rules and regulations for the administration of the Business Enterprise Program operated by the State Licensing Agency.
- (b) The purpose of this Chapter is to set forth the legal authority from which these rules are derived, to proclaim the mission of the Business Enterprise Program, define terms used in this body of policy, and to set forth the organization of the Business Enterprise Program.

612:25-2-2. Mission of the Business Enterprise Program

- (a) **Mission.** The mission of the Business Enterprise Program is to establish and maintain business enterprises operated by qualified individuals who are blind.
- (b) **Goals.** The goals for the Business Enterprise Program are set forth in (1) and (2) of this Subsection.
 - (1) Provide employment opportunities for qualified persons who are blind by establishing and maintaining Business Enterprise Program Facilities.
 - (2) Administer a continuing process of career development and upward mobility for qualified persons in the Business Enterprise Program.
- (c) **Objectives.** The objectives of the Business Enterprise Program are set forth in (1) through (7) of this Subsection.
 - (1) Establish and equip Business Enterprise Program Facilities.
 - (2) Assure availability of Business Enterprise Program licensed managers.
 - (3) Provide management support services to Business Enterprise Program licensed managers.
 - (4) Develop and maintain standards of conduct and a system of accountability for State Licensing Agency staff.
 - (5) Develop and maintain standards of conduct and a system of accountability for Business Enterprise Program licensed managers.
 - (6) Establish and maintain procedures for quality customer service.
 - (7) Attain the program's financial stability through its administration in an operationally efficient and cost-effective manner.

612:25-2-4. State legal authority

Rules for the Business Enterprise Program are promulgated by the Oklahoma Commission for Rehabilitation Services under the authority of 74 O.S., Section 166.1 et seq., and in accordance with the Administrative Procedures Act, 75 O.S., Sections 250 et seq.

612:25-2-5. Definitions (excerpts)

The following words or terms, when used in this Manual, shall have the following meaning unless the context clearly indicates otherwise:

"**BEP**" means the Business Enterprise Program of the State Licensing Agency which provides self-employment opportunities for qualified persons who are blind.

"**Net proceeds**" means the amount remaining from the sale of articles or services of business enterprises and any vending machine income or other income accruing to licensed managers after deducting the cost of

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such sales and other authorized expenses excluding set-aside charges required to be paid by the licensed managers.

"**Satellite business enterprise**" means a business enterprise without a permanently assigned licensed manager which is being managed by a licensed manager who is also managing his/her regularly assigned business enterprise.

"**Set-aside funds**" means funds which accrue to a State Licensing Agency from an assessment against the net proceeds of each business enterprise in the State's business enterprise Program and any income from vending machines on Federal property which accrues to the SLA.

612:25-4-1. Organization of the State Licensing Agency

- (5) **Licensed managers.** The individual enterprises established by the Business Enterprise Program are managed by licensed managers who derive their livelihood from net profits of the operations. Licensed managers are subject to instructions, policies, rules and regulations of the Business Enterprise Program, but are not employees of the program, the SLA, or the State of Oklahoma. They do, however, have a contractual relationship with the SLA and are required to manage the business enterprise in accordance with established rules and regulations.

612:25-4-4. Management services provided by the State Licensing Agency

- (a) **Overview of management services.** Management services include inspection, quality control, consultation, accounting, regulating, in-service training, and other related services provided on a systematic basis to support and improve business enterprises.
- (b) **Technical assistance services.** The SLA will provide each licensed manager with:
- (1) Recommendations for optimizing the profitability of the business enterprise.
 - (2) Recommendations and feedback on business enterprise operations including quality, service, and cleanliness.
 - (3) Possible solutions to problems recognized by the licensed manager or brought to the licensed manager's attention by BEP staff or the grantor.
 - (4) Providing upward mobility and in-service training.
 - (5) Explanation of the SLA's procedures, policies, and standards.
- (c) **Services provided by the business consultant.** Business consultants will assist licensed managers, in their assigned area, to meet Business Enterprise Program requirements through review and consultation on:
- (1) compliance with applicable laws and program regulations;
 - (2) compliance with all conditions in the manager's license;
 - (3) assuring that merchandise is:
 - (A) sold in accordance with the grantor's agreement;
 - (B) of high quality, adequately stocked, and properly displayed;
 - (4) standards for employee personal appearance and hygiene;
 - (5) quality customer service;
 - (6) maintenance of sanitation and safety standards;
 - (7) proper maintenance of equipment;
 - (8) communications and working relationships between the licensed manager and customers, purveyor, employees, grantor, and the general public;
 - (9) SLA and other agency requirements for record keeping; and
 - (10) licensed manager performance evaluations.
- (d) **Business consultants' on-site review.** Business consultants' on-site reviews will be made as often as necessary, but not less than once each month to ensure the continued success of the business enterprise.

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Each time the business consultant visits a business enterprise, he/she will document the visit on the case memorandum form.

- (e) **Inspection reports.** The business consultant completes an inspection of the facility using the Location Review form at least monthly. The report will contain at least the information in (1) - (6) of this Subsection to the extent relevant:
 - (1) Suggestions which will aid the licensed manager in the successful operation of the business enterprise.
 - (2) Violations of State or Federal Laws and the SLA's policies, rules and regulations.
 - (3) Comments on any conditions relating to any aspect of the business enterprise and recommendations for improvement.
 - (4) Follow-up action from previous inspection reports about noted discrepancies.
 - (5) Training needed or requested.
 - (6) Proper insurance, permits and license are current and posted.
- (f) **Visits by the BEP Programs Manager.** The BEP Programs Manager will periodically visit business enterprises.
- (g) **Assistance of Rehabilitation Services staff.** At the request of the business consultant or other BEP staff members, rehabilitation staff will provide necessary assistance to the program when in the best interest of the licensed manager or the SLA.
- (h) **SLA provision of training.** The SLA shall ensure that effective programs of vocational and other training services, including personal and vocational adjustment, books, tools, and other training materials, shall be provided to trainees as vocational rehabilitation services. Such programs shall include on-the-job training in all aspects of business enterprise operations for licensed managers, and upward mobility training including further education and additional training or retraining for improved work opportunities for all licensed managers. [34 CFR 395.11] Details of the BEP training provided by the SLA are presented in 612:25-4-14 and 612:25-4-15.

612:25-4-15. Training for present licensed managers

Post-employment (upward mobility) training will be provided by the SLA to encourage greater professional competence and to promote the upward mobility of licensed managers

612:25-4-25. Management of BEP equipment and fixtures

- (a) The SLA will provide each business enterprise with fixtures and equipment in such quantity and quality so as to give reasonable assurance of successful operation by the licensed manager. The SLA retains the right, title, and interest to all BEP equipment and fixtures. The SLA has the authority to direct, control, transfer and dispose of such equipment as it deems necessary. All capital equipment is purchased, inventoried, and disposed of in accordance with Department of Rehabilitation Services policy.
- (b) Equipment for new locations will be determined by the business consultant and BEP Programs Manager in consultation with an ECM member specified by the ECM Chairperson.
- (c) The licensed manager will make no additions, deletions or modifications to the business enterprise and its operation, in the form of equipment, fixtures or facilities, without first obtaining written authorization from the SLA.

612:25-4-26. Maintenance and replacement of business enterprise equipment

The SLA shall maintain, or cause to be maintained, all business enterprise equipment in good repair and in an attractive condition and shall replace or cause to be replaced worn-out and obsolete equipment as required to ensure the continued successful operation of the business enterprise. [34 CFR 395.10]

612:25-4-61. Satellite/remote business enterprise locations

- (a) A business enterprise or vending machine facility will be assigned to a licensed manager on a temporary basis when the regular selection process does not produce a permanent licensed manager, or when a

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business enterprise is vacated on short notice by a licensed manager and the time element to follow the regular selection process will cause the grantor to terminate the permit/contract with the SLA.

- (b) The BEP Programs Manager, in consultation with the Chairperson of the Elected Committee of Licensed Managers, may assign a licensed manager to a satellite/remote business enterprise on a temporary basis. The length of the agreement for a temporary assignment will be until the regular selection process can generate a permanent licensed manager to manage the vacant business enterprise with a minimum of 90 days. At the SLA's discretion, in order to achieve an equitable distribution of satellite business enterprises, a licensee that currently operates a location and a satellite will not be eligible for an additional satellite unless there are no other applicants.
- (c) After the selection process is completed, a temporary agreement will be issued for a maximum of one year, at which time the satellite business enterprise will be advertised and a permanent licensed manager selected through the normal selection process. At the end of one year, if a permanent licensed manager is not produced through the selection process, the temporary location may be closed, added permanently to another business enterprise through the selection process, or again be placed on a temporary agreement for a maximum of one year.
- (d) The temporary agreement for a satellite business enterprise may be canceled only for cause shown.
- (e) The licensed manager may resign the satellite agreement with 20 days written notice.
- (f) The satellite business enterprise will be managed as a separate business location for all purposes except for insurance and the tax permit. It is the licensed manager's responsibility to notify the Oklahoma Tax Commission and his or her insurance carrier of the addition.
- (g) When a licensed manager is managing a satellite location, travel expenses to go between the two business enterprises will be considered a business expense of the satellite/remote location at the state rate.

612:25-4-72. Audits

The SLA reserves the right to develop procedures and conduct audits including the use of third party auditors.

612:25-6-2. Standards for licensed managers

- (a) The licensed manager will agree to the terms of the licensed manager's agreement, rules and regulations governing the Business Enterprise Program, and the permit or contract governing the specific business enterprise.
- (b) The licensed manager will operate the business enterprise in accordance with all applicable health laws and regulations, safety regulations and other federal, state, county, and municipality laws and regulations applicable to the business enterprise.
- (c) The licensed manager will work cooperatively with authorized representatives of the SLA in connection with their official responsibilities.
- (d) The licensed manager will take proper care of the equipment and fixtures to minimize repair and replacement costs. The licensed manager will be responsible for repair or replacement costs when caused by the negligence of the licensed manager or his employees, repairs below \$25.00, or unauthorized repair cost. In the event of withdrawal from the business enterprise for any reason, the licensed manager will leave all equipment to the disposal of the SLA.
- (e) The licensed manager will collect and pay sales tax as required.
- (f) The licensed manager will be responsible for substitute operation.
- (g) The licensed manager will not take action inconsistent with the paramount right, title, and interest of the SLA to business enterprise equipment.
- (h) The licensed manager will accept the agreement subject to the policies, rules, and regulations of the SLA as they exist or are modified.
- (i) The licensed manager will keep daily records of gross sales, merchandise purchased, and expenses for the business enterprise.

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- (j) The licensed manager will complete and submit all necessary Federal and State reports and payments as required for each individual business enterprise.
- (k) The licensed manager will dress and maintain a level of personal hygiene which will convey a positive public image.
- (l) The licensed manager will maintain appropriate professional relationships with purveyors, customers, and building officials as in (1) through (3) of this Subsection.
 - (1) **Relationships with purveyor.** The licensed manager is free to choose the purveyor from whom he/she is to make purchases, provided, however, that such purveyor is established and reputable.
 - (2) **Relationships with customers.** To serve the best interest of the public, the licensed manager and his/her employees must provide prompt, cheerful and courteous service to all customers and accommodate, within reasonable limits, such other persons who may come to the business enterprise requesting change, information, or other services.
 - (3) **Relationships with building officials.** Units (i) and (ii) of this Subparagraph provide guidance in maintaining a productive relationship with building officials.
 - (A) The licensed manager must comply with all reasonable requests concerning the operation of a business enterprise that may be made by officials of the building in which the enterprise is located, provided that such requests do not conflict with the agreement and the rules and regulations issued by the SLA as contained herein.
 - (B) If differences should arise between the licensed manager and the grantor, the licensed manager shall bring the matter to the immediate attention of the business consultant for appropriate action.
- (m) The licensed manager will supervise employees in a manner that promotes quality customer service.
- (n) The licensed manager will maintain and display current licenses and permits, including BEP license, in the business enterprise.
- (o) The licensed manager will comply with all regulations and laws governing the possession and/or use of firearms, weapons, alcohol and other drugs.
- (p) When a licensed manager starts or buys a similar business, the licensed manager must report the nature and location of the business and make assurances to the SLA that the two businesses will not intermingle in any manner and the merchandise of the two businesses will be in separate locations. At no time will state owned equipment be used in the private business.

612:25-6-3. Grounds for suspension or termination of a license

- A BEP license may be suspended or terminated for the reasons set forth in (1) through (14) of this Subsection.
- (1) Failure to open the assigned business enterprise as stated in the permit/contract with the grantor agency, without prior proper approval from the SLA (abandonment of business enterprise).
 - (2) Defrauding any agency of the government (including the SLA) or any purveyor or **failure to pay monies due including taxes, fees, or assessments to any governmental entity or purveyor.**
 - (3) Failure to file required financial and other records with the SLA or preserve them for a specified time, and failure to comply/cooperate with audits conducted by the SLA or other State or Federal agencies.
 - (4) Failure to maintain the required insurance coverage.
 - (5) The business enterprise is not being operated in accordance with the rules and regulations, terms and conditions of the permit with the grantor agency, or the terms and conditions of the business enterprise manager's agreement.
 - (6) Intentional abuse, neglect, unauthorized use or removal of the business enterprise equipment; or failure to properly maintain the equipment in a clean and operating manner within the scope of the licensed manager's level of maintenance authorization.
 - (7) Substance abuse (alcoholic beverages, illegal drugs, etc.) while operating the business enterprise; or other substance abuse that interferes with the operation of a business enterprise.
 - (8) Operation of a business enterprise in such a way that the SLA's investment is obviously endangered.

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- (9) An attempt by a licensed manager to derive personal benefit from privileged information acquired through participation in the Business Enterprise Program.
- (10) Failure to comply with all Federal and State laws prohibiting discrimination and failure to provide services without regard to race, gender, color, national origin, religion, age, political affiliation, or disability.
- (11) Determination by the SLA that the licensed manager no longer has the necessary skills and abilities for effectively managing a business enterprise.
- (12) Use of the business enterprise to conduct unlawful activities.
- (13) Failure to personally operate and manage the business enterprise in accordance with the manager's agreement.
- (14) Does not actively work as a licensed manager or licensed employee in the Business Enterprise Program for 2 years.

612:25-6-5. Motor vehicle operation

All licensed managers, licensed employees, licensee or trainees of business enterprises will not operate a motor vehicle on any public street or highway. If it is determined that a licensed manager, licensed Employee, licensee or trainee of a business enterprise has operated a vehicle for which a state driver's license is required on any public street or highway, his/her licensed manager's agreement and/or BEP License will be subject to revocation, suspension, or termination.

612:25-6-15. Setting aside of funds

- (a) Set-aside charges paid by the licensed manager will be placed in a revolving account maintained by the SLA. Set-aside charges will be re-evaluated yearly by the SLA and the Elected Committee of Licensed Managers. Adjustments will be made accordingly in the appropriate classification, with allowances for reasonable charges for improving services, fluctuation of costs, and for program expansion.
- (b) Funds will be set aside only for the purpose of:
 - (1) maintenance and replacement of equipment;
 - (2) the purchase of new equipment;
 - (3) management services;
 - (4) assuring a fair minimum of return to licensed managers; or
 - (5) the establishment and maintenance of retirement or pension funds, health insurance contributions, or provisions for paid sick leave and vacation time.
- (c) The licensed manager's set-aside charges will be on a sliding scale of 0% to not more than 12% of the net proceeds of the business enterprise during any one month. The sliding scale will be in four classifications: Class A, B, C, and D (based on prior year's performance).
 - (1) Class A - 12% of net proceeds, \$26,000 and above.
 - (2) Class B - 10% of net proceeds, \$15,000 to \$25,999.
 - (3) Class C - 6% of net proceeds, \$4,500 to \$14,999.
 - (4) Class D - 0% of net proceeds, \$4499 and below.
- (d) When a licensed manager timely submits his/her set-aside payment to the BEP by the 25th of the month, the manager's set-aside obligation will be reduced by 1% of the set-aside amount due that month. However, if the set-aside payment is received in the BEP office ten days or more after the due date, the licensed manager will be assessed a late fee in the amount of 20% of the set-aside due for that month. If the licensed manager's set aside payment is 60 days late, the licensed manager will be placed on probation until their set aside payments to the agency are current. If the licensed manager's set aside payment is more than 90 days late his/her operating agreement will be suspended or terminated by the BEP Programs Manager.
- (e) If a business enterprise should show a marked change in net proceeds, a request for reclassification may be made by the licensed manager or the SLA after 90 days. Each licensed manager will be notified of changes in set-aside charges, and the new percentage of net proceeds will be effective at the beginning of the first

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business month following the mailing of notice to the licensed manager. The licensed manager will start paying the higher or lower percentage of set-aside with the second report due following notification.

- (f) All new business enterprises will be placed in class C for 90 days, at which time the SLA will review the business enterprise for reclassification and notify the licensed manager of changes in set-aside charges and the new percentage of net proceeds shall be effective at the beginning of the first business month following the mailing of notice to the licensed manager.

612:25-6-19. Employees of the licensed manager

- (a) The business consultant has no direct responsibility over the business enterprise employees. If, in the course of an inspection or a complaint is filed by a customer or grantor against a business enterprise employee, the business consultant will bring the complaint/problem to the attention of the licensed manager. A business consultant may make suggestions as to the action that needs to be taken, however the responsibility lies with the licensed manager as to disciplinary action toward the business enterprise employee.
- (b) In the event the grantor requests a business enterprise employee be terminated/suspended, the information will be presented to the licensed manager immediately by personal contact or phone call followed by written memorandum indicating the reason for the requested termination. If the licensed manager fails to terminate the employee, the licensed manager is subject to termination of the licensed managers agreement.
- (c) The business consultant will immediately notify the SLA state office by memorandum for insurance and retirement purposes when a licensee/licensed employee starts to work for another licensed manager or quits.
- (d) Licensed managers are to take affirmative action to employ and advance qualified individuals with disabilities on the same conditions and regulations required in Section 503 of the Rehabilitation Act of 1964 [P.L. 88-352].
- (e) Volunteer labor is permitted in a business enterprise, however the volunteer must be covered by insurance in the event of injury. This insurance coverage will be documented in the SLA state office prior to the individual's actual work in a business enterprise.

612:25-6-21. Business expenses

- (a) All business enterprises will be so designed and stocked with merchandise that a licensed manager can purchase from wholesalers that deliver products to the location, and there will be minimal travel required by the licensed manager.
- (b) All monthly report information must remain in the business enterprise during normal business hours. If a business deduction cannot be verified by the business consultant while in a business enterprise, the deduction will not be allowed, stricken from the report, and a revised report will be forwarded to the licensed manager to reflect the change.
- (c) The expense column on the monthly report should reflect the actual expenses incurred by the business enterprise. The items claimed on the report should have documentation located in the business enterprise for the business consultant to review, (merchandise receipts, salaries, copies of the quarterly IRS and social security report, insurance invoice and policies, and etc.). If it is considered by the SLA that the amount of the expenses is excessive, the SLA may audit the business enterprise to determine that the expenses are actually required for that particular location.
- (d) There will be no mileage or vehicle expense claimed as a business expense on the monthly report except as detailed at 612:25-4-61(g).
- (e) The amount of telephone charges claimed on each monthly report will be limited to a total of \$50.00 for all communication devices.
- (f) If a licensed manager rents, leases, or buys equipment to enhance the business enterprise, the cost may be deducted as a business expense. The licensed manager must have prior written approval as per Section 612:25-4-25(h) and written notice will be given to the SLA accountant.

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612:25-6-22. Monthly reports

- (a) **Content and when due.** Monthly reports are due in the business consultant's office on or before the 25th of each month. The business consultant will review each monthly report for mathematical errors, correct loan payment, correct set-aside payment, approved business expenses, and other factors that will affect the accuracy of the report. The business consultant will sign the report indicating that the report is correct and all items in question have been discussed with the licensed manager.
- (b) **Failure to file in a timely manner.** Continued late reporting may cause formal disciplinary action.
- (c) **Corrective action for late reports.** Corrective action for late reports will be taken as described in (1) through (4) of this Subsection.
 - (1) If the report is not received by the 1st of the following month (5 days late), the business consultant will call the licensed manager to remind the licensed manager that the report is 5 days past due.
 - (2) If the report is not received by the 15th of the next month (20 days late), the business consultant will send a letter to the licensed manager asking for the report.
 - (3) If the report is not received by the next report due date (25th) (one month late) the licensed manager will be placed on probation.
 - (4) If the 1st and second reports are not received by the time the 3rd report is due (25th), the licensed manager's agreement will be canceled and the BEP Licenses will be suspended.
- (d) **Fee for reports.** The Agency maintains records for its use and may charge a reasonable fee to supply copies of records to individuals. The agency will supply copies of lost reports or other documents at 25 cents per each side of a page. Copies of reports or other documents will be facsimile at a cost of \$1.00 per page.



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