



**Internal Audit Department**

## **1899 Bar and Grill**

**November 2017  
Report Number FY 18-01**

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Northern Arizona University  
1899 Bar and Grill  
Audit Report  
November 2, 2017

## Summary

Our audit of the 1899 Bar and Grill is in the Annual Audit Plan for FY 2018, as approved by the Audit Committee of the Arizona Board of Regents. This audit supports NAU's strategic goal of sustainability and effectiveness.

**Background:** On February 28, 2011, NAU opened its historic North Union doors to a brand-new dining experience called the 1899 Bar and Grill (the Restaurant). This upscale restaurant is named after NAU's founding year and is a testament to both the university's modernization and also a nod to its history and roots. It retains features from the historic building, such as its original copper fireplace, but adds dynamic lighting and an elegant, open design to produce a kind of dining experience never seen before on the NAU campus.

The 1899 Bar and Grill features a dedicated staff of servers, many of them NAU students. The Restaurant is a valuable resource for NAU's Hotel and Restaurant program, enabling these students to learn in a real-world setting, all while the restaurant remains a full-service, independent eatery, separate from NAU's other retail outlets.

The Restaurant combines an American bistro with a contemporary Southwest steakhouse. It features many foods native to the southwest. There is both a lunch and dinner menu, with a variety of salads and desserts offered throughout the day. A full bar, with regional tap beers and wine list, complete the dining experience.

NAU's Campus Dining Services renewed its contract with Sodexo on August 28, 2015 to manage, market and operate the 1899 Bar and Grill. As part of the agreement, NAU receives an annual sales commission. The amount of sales commission is based on revenues (net of sales tax) from all food and beverage sales in the Restaurant. An addendum to the contract allows the Sodexo lease payments to be deducted from the sales commission.

The Sodexo lease payments are a result of NAU's lease agreement with Northern Arizona Real Estate Holding, LLC (NAREH). NAREH is a wholly owned subsidiary of the NAU Foundation established to construct, develop, equip, operate, maintain, lease and hold real estate investments on behalf of the NAU Foundation. During fiscal year 2011, NAREH constructed the 1899 Bar and Grill restaurant on property owned by the Arizona Board of Regents and invested in restaurant equipment for a total cost of \$3,336,733. NAREH then leased the restaurant to Sodexo under a direct financing lease over a six-year term. Because the Sodexo lease payments were deducted from the sales commissions, the direct financing lease was paid in full by NAU as of April 2017.

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Revenues as reported in Sodexo's Operating Statements for the past three fiscal years are as follows:

<b>Revenues</b>	<u>FY 2017</u>	<u>FY 2016</u>	<u>FY 2015</u>
Food Regular	\$ 250	\$ -	\$ 97
Student Dining Dollars	377,606	336,327	384,855
JacksDebit Express	17,370	16,292	14,906
Faculty and Staff Dining Dollars	16,314	8,311	7,856
Cash and Credit	659,300	656,752	664,031
Dining Charge Card Purchases	47,622	75,197	103,113
Free Meals	-	-	(80)
<b>Total Revenues</b>	<u><u>\$ 1,118,462</u></u>	<u><u>\$ 1,092,879</u></u>	<u><u>\$ 1,174,778</u></u>

Sales commission for the past three fiscal years are as follows:

	<u>FY 2017</u>	<u>FY 2016</u>	<u>FY 2015</u>
Sales Commissions	\$ 209,521	\$ 123,837	\$ -
Sales Commissions Percentage	18.73%	11.33%	0.00%

Sales commission percentages as outlined in the Contract are as follows:

- August 28, 2015 to August 27, 2016                      21.5%
- August 28, 2016 to August 27, 2017                      21.5%

The contract requires that revenue exclude concession sales as commissions on concession sales are separately calculated. Sodexo did not allocate sales commission to the Restaurant until FY2016.

**Audit Objective:** The primary objective of the audit is to determine if parties are complying with the terms of the contract with Sodexo for managing the 1899 Bar and Grill.

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**Scope:** The scope of our audit included a review of all policies and procedures governing the compliance requirements of the contract with Sodexo for managing the 1899 Bar and Grill as well as other procedures that helped us achieve our primary audit objective. We reviewed documents and system reports supporting compliance and reporting requirements that occurred from fall 2016 to spring 2017, as well as current practices and procedures. We did not audit the detailed accounting records of Sodexo America, LLC.

**Methodology:** The following procedures were performed to accomplish the audit objective:

- Reviewed the 1899 Bar and Grill website and NAU Campus Dining websites
- Reviewed the previous and current Dining Contracts as well as the addendums to the contracts
- Reviewed Sodexo and NAU policies and procedures relevant to the contract
- Interviewed Sodexo and NAU management and staff responsible for compliance and reporting requirements of the contract
- Reviewed Sodexo system reports (weekly sales summaries, credit card batch detail reports, discounts reports, voids reports, operating statements, profit and loss statements and financial activity reports) and Blackboard reports
- Reviewed sales commission calculations and documentation in support of the calculation
- Sampled and tested revenues and expenses, as reported in PeopleSoft, for the 1899 Bar and Grill restaurant
- Toured the 1899 Bar and Grill restaurant.

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

**Conclusion:** Both parties are meeting the compliance and reporting requirements of the terms of the contract with Sodexo for managing the 1899 Bar and Grill. The use of the Point of Sale system as well as the Sodexo accounting software allows for efficient capture of revenues and expenses related to the 1899 Bar and Grill. Monthly meetings between NAU and Sodexo allow for continuous communication regarding contract requirements.

**Observation:** The monthly sales summary reports inadvertently excluded the liquor sales category. However, the calculation of net sales, which forms the basis of the commission, was appropriately including liquor sales. As of August 15, 2017, the liquor sales category was reflected on the reports.

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The control standards we considered during this audit and the status of the related control environment are provided in the following table.

<b>General Control Standard</b> (The bulleted items are internal control objectives that apply to the general control standards, and will differ for each audit.)	Control Environment	Recommendation No.	Page No.
<b>Reliability and Integrity of Financial and Operational Information</b>			
<ul style="list-style-type: none"> <li>Sodexo accounting system is automated to capture revenues and expenses</li> </ul>	Reasonable to Strong Controls in Place		
<ul style="list-style-type: none"> <li>Sales commissions are calculated in accordance with the contract</li> </ul>	Reasonable to Strong Controls in Place		
<ul style="list-style-type: none"> <li>Sodexo Operating Statements include expenses allowed by the contract</li> </ul>	Reasonable to Strong Controls in Place		
<ul style="list-style-type: none"> <li>NAU's general ledger includes expenses allowed by the contract</li> </ul>	Reasonable to Strong Controls in Place		
<ul style="list-style-type: none"> <li>NAU Management reviews and verifies the revenues reported for restaurant operations</li> </ul>	Reasonable to Strong Controls in Place	1, 2	6, 7
<b>Safeguarding of Assets</b>			
<ul style="list-style-type: none"> <li>All equipment is tagged and inventoried according to NAU policy</li> </ul>	Opportunity for Improvement	3	8
<ul style="list-style-type: none"> <li>Sensitive information is adequately protected</li> </ul>	Reasonable to Strong Controls in Place		
<b>Effectiveness and Efficiency of Operations</b>			
<ul style="list-style-type: none"> <li>Policies and procedures exist for the 1899 Bar and Grill restaurant operations</li> </ul>	Reasonable to Strong Controls in Place		

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<b>General Control Standard</b> (The bulleted items are internal control objectives that apply to the general control standards, and will differ for each audit.)	Control Environment	Recommendation No.	Page No.
<ul style="list-style-type: none"> <li>Systems, processes and procedures are used to efficiently and effectively manage contract compliance and reporting requirements</li> </ul>	Opportunity for Improvement	3	8
<ul style="list-style-type: none"> <li>Satisfaction surveys are used to assess food quality and dining experience</li> </ul>	Reasonable to Strong Controls in Place		
<b>Compliance with Laws and Regulations</b>			
<ul style="list-style-type: none"> <li>The 1899 Bar and Grill complies with state statutes governing the sale and service of alcohol</li> </ul>	Reasonable to Strong Controls in Place		

We appreciate the assistance of the staff of Sodexo, Enrollment Management and Student Affairs, Contracting and Purchasing Services and the Comptroller's Office.



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**Audit Results, Recommendations and Responses**

**1. NAU management's periodic revenue reconciliations to the 1899 Bar and Grill POS reports using the Blackboard system should include all revenue.**

**Condition:** NAU does not reconcile all revenue generated by the 1899 Bar and Grill. NAU management spot checks stored value account sales only, not cash or credit card sales.

**Criteria:** Section 17.6.3 of the contract states, "All recognized sales must reconcile to the University's privilege access transaction system." NAU owns and operates a Blackboard privilege access transaction system for Point of Sale (POS) Campus Dining Services. POS terminals for the 1899 Bar and Grill are Micros terminals.

**Cause:** No formal procedures have been developed to ensure periodic revenue reconciliations are performed and documented.

**Effect:** Although spot checks are performed, there is no assurance that revenue is complete and accurate.

**Recommendation:** NAU management should periodically reconcile all sales as reported by the 1899 Bar and Grill POS system to the Blackboard system.

**Response:** The Micros point of sale system is used to recognize sales for the 1899 Bar and Grill. The contract (F17.4.2) will be amended to clarify that Micros is a transaction system and the type of terminals used. A more complete procedure will be developed to perform and document periodic revenue reconciliations. The target implementation date is Fall 2017.

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**2. Weekly sales reports should be reconciled to the profit and loss statements as required by the contract.**

**Condition:** The sum of the weekly sales reports for each month of FY 2017 do not agree to the monthly profit and loss statements.

**Criteria:** Section 17.6.4 of the contract states, "Sales reports shall be provided to the University on a weekly basis. These reports shall reconcile to the monthly profit and loss statement."

**Cause:** Different date and time parameters exist for generating the weekly sales reports and the profit and loss statements.

**Effect:** There is no assurance that revenue is complete and accurate.

**Recommendation:** Weekly sales reports should be reconciled to the profit and loss statements as required by the contract.

**Response:** NAU has compared the monthly profit and loss statements (Operating Statement) to recognized sales, periodically. With a more complete procedure being developed to document revenue reconciliation, the comparison to the profit and loss statement will follow. The target implementation date is Fall 2017.

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**3. Construction costs and restaurant equipment should be properly recorded and tagged.**

**Condition:** Construction costs and restaurant equipment to establish the 1899 Bar and Grill (the Restaurant) were not capitalized on NAU's books. The discovery of untagged equipment was made when a physical tour of the restaurant was done in July 2017. Further research revealed construction costs were not capitalized either. Capital items totaling \$254,287 at the 1899 Bar and Grill were not tagged and inventoried. Capital items include equipment such as waste extractor system, washer, broiler, freezer, burner, refrigerators, ovens, dishwasher, etc.

**Criteria:** During fiscal year 2011, NAREH constructed the 1899 Bar and Grill restaurant and purchased restaurant equipment on behalf of NAU for a total cost of \$3,336,733. NAREH then leased the Restaurant to Sodexo under a direct financing lease amortized over a 6-year term. The sublease naming Sodexo as tenant and NAREH as landlord reads, "Tenant shall pay to Landlord during the term of this Lease rental amount of \$164,175.11. Any personal property tax or cost incurred to insure the Leased Premises, or any personal property on the leased premises, shall be added to the amortized rental amount and paid by Tenant as part of the rent payment." However, Addendum 5 to the original Dining Contract states: "The University will allow Sodexo Campus Dining to reduce annual Dining Sales Commissions by the amount of the annual cost of building the new North Union Restaurant and shall begin in contract year 2010-2011 and continue for the remaining term of the Contract." The commercial lease agreement between NAU (Lessor) and NAREH (Lessee) states, "Upon placement or installation, all of the Lessee Improvements shall become the property of the Lessor".

ABOR and NAU require an annual physical inventory of all tagged assets. Tagged assets consist of capital items (those assets that have an original acquisition value of \$5,000 or more, and all computers). Accurate records of capital equipment with all pertinent information such as location, acquisition date and value and betterments or upgrades are to be maintained.

**Cause:** NAREH paid to establish the Restaurant. There was uncertainty of when ownership to the assets (leasehold improvements and restaurant equipment) transferred to NAU.

**Effect:** Capital assets, depreciation expense, accumulated depreciation, sales commission revenue, sales tax expense and interest expense were understated from FY 2011 to FY 2017.

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**Recommendation:** The Comptroller's office should record the leasehold improvements and restaurant equipment and corresponding depreciation expense.

Capital items at the 1899 Bar and Grill should be tagged and inventoried in accordance with ABOR and NAU policies.

**Response:** Comptroller's office: The Comptroller's office will record the leasehold improvements and restaurant equipment and corresponding depreciation expense. Capital items at the 1899 Bar and Grill will be tagged and inventoried in accordance with ABOR and NAU policies. The implementation date will be no later than June 30, 2018.

EMSA: Campus Services has begun working with Property Control to tag equipment in compliance with ABOR and NAU policies. The target completion date for tagging equipment is October 31, 2017.

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This report is intended for the information and use of the Arizona Board of Regents, NAU administration, the Arizona Office of the Auditor General, and federal awarding agencies and sub-recipients.