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INDEPENDENT STATE AUDITOR'S
DETERMINATION ON THE
UNIVERSITY OF MASSACHUSETTS AMHERST
PROPOSAL TO PRIVATIZE MANAGEMENT AND
OPERATION OF THE UNIVERSITY STORE

OFFICIAL AUDIT REPORT

JUNE 1, 2000

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INTRODUCTION

Background

Chapter 7, Sections 52 through 55, of the Massachusetts General Laws, the Commonwealth's privatization law, outlines the process that must be followed by agencies and applicable Authorities seeking to contract for a service that is presently performed by state or Authority employees. The law, which became effective December 15, 1993, applies to contracts that have an aggregate value of \$100,000 or more.

Pursuant to this law, a specific process must be followed to demonstrate and certify to the State Auditor that (a) the agency complied with all provisions of Chapter 7, Section 54, of the General Laws and all other applicable laws, (b) the quality of the services to be provided by the designated bidder is likely to equal or exceed the quality of services that could be provided by regular employees, (c) the total cost to perform the service by contract will be less than the estimated in-house cost, (d) the designated bidder has no adjudicated record of substantial or repeated noncompliance with relevant federal and state statutes, and (e) the proposed privatization contract is in the public interest in that it meets applicable quality and fiscal standards. The State Auditor has 30 business days to approve or reject the agency's certification, and may extend the review for 30 additional business days.

The process that the agency must follow includes preparing a detailed written statement of services, estimating the most cost-efficient method of providing those services with agency employees, selecting a contractor through a competitive bidding process, and comparing the in-house cost and the cost of contract performance. The agency must also ensure that the private bids and private contract, if ultimately awarded, contain certain provisions regarding wages, health insurance, the hiring of qualified agency employees, nondiscrimination, and affirmative action.

The University of Massachusetts-Amherst (UMA) has a University Store (US) located in the Campus Center/Student Union Complex. The complex contains 36 meeting rooms, 116 hotel rooms, and a variety of food and retail services to meet the needs of the campus community and visitors. The operation of the

facility is the responsibility of UMA under a management and service agreement with the University of Massachusetts Building Authority.

The US is an auxiliary unit within UMA, an agency of the Commonwealth of Massachusetts. In addition to the students, faculty and staff, the US annually serves in excess of 100,000 visitors and serves approximately 1,000 students that attend the University through the Division of Continuing Education.

The US is currently located in 14,994 square feet of space on the concourse level of the Campus Center/Student Union Complex and has an additional 3,489 square feet of storage space in the building. Its textbook operations (Textbook Annex) are located in 16,494 square feet of space in the Physical Plant Annex Building, which consists of 8,222 square feet of retail space, 1,702 square feet of office/service space, 2,840 square feet of locked storage area, 3,227 square feet of receiving space, 313 square feet of utility closet/restroom space, and 190 square feet attributable to common areas (hallways). A point-of-sale financial management system was installed in 1994 allowing for quicker cashier service (scanning) and better control of inventory. The store employs 27 full-time employees, 12 part-time seasonal employees, and 75 students annually.

The US activities proposed by UMA for privatization include: managing all aspects of the operation of the US, including personnel, merchandising, marketing, purchasing, security, administration, and maintenance. On March 21, 2000 (later resubmitted on April 25, 2000), the University notified the State Auditor of its intent to award a privatization contract for these activities. As required by law, the notification was accompanied by a certification signed by the President of the University and the Commonwealth's Secretary for Administration and Finance and by documentation subject to review and determination by the State Auditor in accordance with state laws and applicable guidelines issued by the State Auditor.

During the performance of our review, UMA made several revisions to its previously submitted documentation. Accordingly, we redirected our review to UMA's resubmission, which we received on April 25, 2000.

Scope, Objectives, and Methodology

The objectives of this review were to determine whether UMA has complied with Chapter 7, Sections 52 through 55, of the Massachusetts General Laws, including the quality and compliance requirements of the law, and whether the revenue accruing to UMA from contractor management of the US would be more than the estimated loss of income forecast by UMA for performing US activities in-house with UMA employees.

To meet these objectives, we examined the written statement of services performed by the US, the management studies of the present in-house functions, the Request for Bids (RFB), the summary of bids received, the successful proposal, and the proposed privatization management agreement. We also examined the cost forms and supporting documentation submitted by UMA and compared the estimated revenue to be realized from contract management with the estimated revenue (loss) to perform the services in-house with UMA employees. We traced and verified cost elements listed in the cost forms to the supporting documentation, and reviewed contractor compliance documents provided by regulatory agencies. We also interviewed UMA management officials and toured the facility where the functions proposed to be privatized are presently performed. While our review was in progress, we also met with a group of employees who were representing the three union groups affected by the proposed privatization.

DETERMINATION

Based on our review, we have concluded that the University of Massachusetts-Amherst (UMA) has complied with Chapter 7, Sections 52 through 55, of the Massachusetts General Laws, as amended, in reaching its decision to award a privatization contract for the management of its University Store and Textbook Annex (US), a service which had previously been performed in-house with UMA employees.

UMA certified that the quality of services to be provided by the contractor is at least equal to or greater than that which had been provided by UMA employees, that the designated contractor has no adjudicated record of noncompliance with relevant statutes, and that the revenue enhancement of having the work performed under the management agreement will exceed the estimated revenue of having the work performed in-house with UMA employees. In our opinion, these certifications comply with Section 54, Paragraph 7, of the cited statute. We therefore approve UMA's certification in each of these required areas.

As summarized in Exhibit A, the revenue to be obtained from the five-year period of the management agreement is estimated to be \$879,268, which offsets the estimated loss of \$441,023 to perform the work in-house with UMA employees, for a total revenue enhancement of \$1,320,291.

We also reviewed UMA's compliance with certain other statutory provisions of the privatization law, as follows:

- (1) Section 54(2) of the law contains certain requirements related to the wages to be paid by the contractor to individuals who will be employed under the contract. Our review determined that the UMA wage requirements contained in the Request for Bids and the proposed management agreement were in compliance with the law.
- (2) Section 54(3) requires the contractor to offer available positions to qualified UMA employees who are being terminated as a result of the privatization. The management agreement provisions require the contractor to offer employment to qualified regular employees at the US. The management agreement further provides the affected employees the option of remaining UMA employees or becoming employees of the contractor at their current UMA salary and years of service for purposes of computing vacation and sick leave, as well as short-and long-term disability.
- (3) Our review also determined that the contractor intends to comply with the health insurance requirements of Section 54(2).

EXHIBIT A

UMA

Privatization of Operation of the University Store and Textbook Annex
Revenue Comparison
Five-Year Period Ending June 30, 2005

| | |
|---|--------------------|
| Management Agreement Performance Revenue, as Adjusted (see Exhibit C) | \$ 879,268 |
| In-House Cost Estimate (see Exhibit B) | <u>(441,023)</u> |
| Estimated Revenue Enhancement over Five-Year Period | <u>\$1,320,291</u> |

EXHIBIT BUMA

Privatization of Operation of the University Store and Textbook Annex
In-House Cost Estimate
Five-Year Period Ending June 30, 2005

| | <u>Cost</u> <u>Estimate</u> | | <u>Audit</u> <u>Adjustments</u> | <u>Adjusted</u> <u>Cost</u> <u>Estimate</u> |
|-------------------------------|--------------------------------|---------|------------------------------------|---|
| University Store Revenues | <u>\$61,257,361</u> | (1) | <u>\$ 988,973</u> | (2) <u>\$62,246,334</u> |
| Direct Costs: | | | | |
| Personnel | \$ 8,096,721 | | - | \$ 8,096,721 |
| Cost of Goods Sold | 43,694,315 | (3) (4) | \$874,717 | (2) 44,569,032 |
| Other Direct Costs: | | | | |
| Travel | 82,026 | | - | 82,026 |
| Administrative Expense | 1,531,155 | | - | 1,531,155 |
| Energy and Space | 293,459 | | - | 293,459 |
| Consultant Services | 136,710 | | - | 136,710 |
| Operational Services | 5,468 | | - | 5,468 |
| Equipment | 54,684 | | - | 54,684 |
| Lease, Rent, and Repair | 180,458 | | - | 180,458 |
| Capital Investment | <u>800,000</u> | (5) | <u>-</u> | <u>800,000</u> |
| Total Other Direct Costs | <u>\$ 3,083,960</u> | | | |
| Total Direct Costs | <u>\$54,874,996</u> | | <u>\$874,717</u> | <u>\$55,749,713</u> |
| Indirect Costs: | | | | |
| Departmental Executive Office | | | | |
| (Auxiliary Services) | \$ 3,918,776 | (6) | - | \$ 3,918,776 |
| University Central Services | <u>3,018,868</u> | | <u>-</u> | <u>3,018,868</u> |
| Total Indirect Costs | <u>\$ 6,937,644</u> | | <u>-</u> | <u>\$ 6,937,644</u> |
| Total In-House Costs | <u>\$61,812,640</u> | | <u>\$874,717</u> | <u>\$62,687,357</u> |
| Net Estimated Loss- | | | | |
| In-House Performance | <u>\$ (555,279)</u> | | <u>\$114,256</u> | <u>\$ (441,023)</u> |

(See Notes in Exhibit B-1)

EXHIBIT B-1UMAPrivatization of Operation of the University Store and Textbook AnnexNotes on In-House Cost EstimateFive-Year Period Ending June 30, 2005

NOTE 1:

A five percent (5%) textbook purchase rebate policy was instituted during fiscal year 1999 for student participation. According to a University spokesperson, the rebate policy was factored into the bookstore's textbook pricing. Although this rebate policy was not addressed by the successful bidder, the University's spokesperson expects the successful bidder to either continue the rebate policy or to price items net of an allowance for rebates, which during fiscal year 1999 totaled \$37,703.

NOTE 2:

These upward adjustments (\$988,973 and \$874,717) represent the extension over a five-year period of the University's recent (April 21, 2000) update to its fiscal year 2000 levels of revenue and cost of goods sold (1.6% and 2%, respectively) used for its five year in-house cost estimate, as follows:

| <u>Revenue</u> | <u>As Submitted</u> | | <u>Current Update</u> | |
|---------------------|---------------------|-------------------------|-----------------------|-------------------------|
| | <u>Amount</u> | <u>Percent Increase</u> | <u>Amount</u> | <u>Percent Increase</u> |
| Base Year 2000 | <u>\$10,927,201</u> | - | <u>\$11,100,000</u> | 1.6% |
| Five-Year Forecast: | | | | |
| 2001 | \$11,274,516 | 3.18 | \$11,452,980 | 3.18 |
| 2002 | 11,757,722 | 4.29 | 11,944,312 | 4.29 |
| 2003 | 12,280,888 | 4.45 | 12,481,806 | 4.45 |
| 2004 | 12,741,849 | 3.75 | 12,949,873 | 3.75 |
| 2005 | <u>13,202,386</u> | 3.61 | <u>13,417,363</u> | 3.61 |
| Total | <u>\$61,257,361</u> | | <u>\$62,246,334</u> | |

| <u>Cost of Goods Sold</u> | <u>As Submitted</u> | | <u>Current Update</u> | |
|---------------------------|---------------------|-------------------------|-----------------------|-------------------------|
| | <u>Amount</u> | <u>Percent Increase</u> | <u>Amount</u> | <u>Percent Increase</u> |
| Base Year 2000 | <u>\$7,883,424</u> | - | <u>\$8,041,092</u> | 2.0% |
| Five-Year Forecast: | | | | |
| 2001 | \$ 8,107,331 | 2.84 | \$ 8,269,459 | 2.84 |
| 2002 | 8,411,830 | 3.76 | 8,580,391 | 3.76 |
| 2003 | 8,752,790 | 4.05 | 8,927,896 | 4.05 |
| 2004 | 9,057,097 | 3.48 | 9,238,587 | 3.48 |
| 2005 | <u>9,365,267</u> | 3.40 | <u>9,552,699</u> | 3.40 |
| Total | <u>\$43,694,315</u> | | <u>\$44,569,032</u> | |

EXHIBIT B-1 (Continued)SUMMARYAs Submitted:

| | | |
|--------------------|-------------------|--------------|
| Revenue | \$61,257,361 | |
| Cost of Goods Sold | <u>43,694,315</u> | |
| Difference | | \$17,563,046 |

As Revised:

| | | |
|-------------------------------|-------------------|-------------------|
| Revenue | \$62,246,334 | |
| Cost of Goods Sold | <u>44,569,032</u> | |
| Difference | | <u>17,677,302</u> |
| Net Decrease to In-House Cost | | <u>\$ 114,256</u> |

NOTE 3:

We noted a difference between the provisions of the Request for Bids (RFB) and the Proposed Management Agreement with regard to the purchase of credit memos valued at approximately \$500,000. Specifically, the RFB states:

The Bidder will purchase from and pay to the University the total amount of unapplied credit memos still due to the University from publishers and other vendors on the date the contract commences, provided that the publishers and other vendors will transfer these unapplied credit memos to the Bidder's account. Payment estimated to be in the range of \$500,000 to \$600,000. [Underscoring added.]

The Management Agreement does not contain the RFB's qualifier of "provided that." Instead, it states definitively that:

Follett will also purchase, upon verification, outstanding credits the University has with publishers or vendors.

NOTE 4:

The RFB, in addressing the potential sale of inventory to the successful bidder, specifies that "The successful Bidder will be liable for all outstanding invoices." Although neither the successful bidder's bid package nor the Proposed Management Agreement further addresses this matter, we believe that the payment of these invoices is contingent upon whether the inventory sales price includes the value of goods acquired by these "outstanding invoices." If included, the University would be expected to pay; if not, the successful bidder would be expected to pay.

EXHIBIT B-1 (Continued)

NOTE 5:

The financial pro forma submission made by the University assumes that the main store located in the Murray D. Lincoln Campus Center and the Textbook Annex will undergo a renovation during the fiscal year ending June 30, 2002 at an estimated capital expenditure of \$800,000. Improvements in the lighting and permanent display cases and painting, carpeting and other architectural finishes are contemplated projects. To accomplish these projects, the University estimated an \$800,000 total project cost, which includes remodeling, design fees, and other project management costs. Although the contemplated renovations have been neither approved nor authorized by the University's Facilities and Planning Division, the need for such renovation is indicated by the successful bidder's contractual requirement to commit \$875,000 to that purpose.

A management study performed by Campus Bookstore Consulting Corporation (CBC) at the University's request confirmed the need for facility renovations, which CBC estimated at \$800,000. The bookstore privatization bid proposal submitted by the UMA Labor Coalition estimated renovation costs at \$235,000 during the first year of a privatization contract to be followed by a \$500,000 bond issue during the second year, if awarded the contract, for a total \$735,000 renovation expenditure.

NOTE 6:

Responding to questions raised by the UMA Labor Coalition relative to potential course packet production revenue losses by the Campus Center Print Shop if the successful bidder "operates an in-house course operation," the University's spokesperson stated:

It is premature to assume that Follett (the successful bidder) will not utilize existing campus printing operations. In fact, Follett has indicated to us that they will work with the student-run business, Campus Design and Copy. Faculty will continue to have the right to have their course packets prepared at any establishment they choose.

EXHIBIT CUMA

Privatization of Operation of the University Store and Textbook Annex
Management Agreement Performance Revenue Estimate
Five-Year Period Ending June 30, 2005

| | Management Agreement Performance Revenue <u>Estimate</u> | | Audit <u>Adjustments</u> | | Adjusted Management Agreement Performance Revenue Estimate |
|---|--|-----|-----------------------------|-----|--|
| <u>Management Agreement Revenue:</u> | | | | | |
| Commission Receipts | \$5,078,792 | (1) | | | \$5,078,792 |
| Utilities | 274,677 | | (\$274,677) | (2) | - |
| Scholarships | 50,000 | | - | | 50,000 |
| Capital Investment | 875,000 | (3) | - | | 875,000 |
| Total Management Agreement Revenue | <u>\$6,278,469</u> | | <u>(\$274,677)</u> | | <u>\$6,003,792</u> |
| <u>Transition Costs:</u> | | | | | |
| Vacation Benefits | (\$ 163,642) | | - | | (\$ 163,642) |
| Sale of Inventory | 1,280,000 | (4) | (\$1,280,000) | | - |
| Total Transition Costs | <u>\$1,116,358</u> | | <u>(\$1,280,000)</u> | | <u>\$ 163,642</u> |
| <u>Other Revenue:</u> | | | | | |
| State Income Tax | \$ 89,891 | | - | | \$ 89,891 |
| Sales Tax | 97,477 | | (\$ 61,784) | (5) | 35,693 |
| Total Other Revenue | <u>\$ 187,368</u> | | <u>(\$ 61,784)</u> | | <u>\$ 125,584</u> |
| Total Management Agreement Performance Revenue | <u>\$ 7,582,195</u> | | <u>(\$1,616,461)</u> | | <u>\$ 5,965,734</u> |
| <u>Deduct - University Continuing Costs:</u> | | | | | |
| Auxiliary Services | \$2,067,598 | (6) | | | \$ 2,067,598 |
| Central Services | 3,018,868 | | | | 3,018,868 |
| Total University Continuing Costs | <u>\$5,086,466</u> | | | | <u>\$ 5,086,466</u> |
| Net Management Agreement Performance Revenue Enhancement | <u>\$2,495,792</u> | | <u>(\$1,616,461)</u> | | <u>\$ 879,268</u> |

(See Notes in Exhibit C-1)

UMA

Privatization of Operation of the University Store and Textbook Annex
Notes on Management Agreement Performance Revenue Estimate
Five-Year Period Ending June 30, 2005

NOTE 1:

The contract (management agreement) fiscal arrangement are set forth in Section VII of the agreement, as follows:

VII. FISCAL ARRANGEMENTS

A. Revenues

Follett will be responsible for the collection of all revenue generated by the Bookstore. Follett shall deposit the revenues in a bank account located in Massachusetts, separate from any other accounts which it may have and under its own Tax Identification Number, which shall be for the exclusive use of making deposits and disbursements related to this Agreement. No such revenues will be used, either directly or indirectly, to pay any principal of, premium or interest on, any bonds of the UMBA (University of Massachusetts Building Authority), or for making deposits in any reserve with respect thereto.

B. Definitions and Payment Terms

1. The term "Gross Revenue" is defined as all sales in a Fiscal Year (retail, e-Commerce, or otherwise) less refunds, sales taxes, computer hardware sales, and interdepartmental, faculty, staff and student sales at a discount.
2. In return for the management services provided in this Agreement, the University agrees to pay Follett Ninety and Nine Tenth Percent (90.9%) of all gross revenue up to \$15,000,000, Eighty-Nine and Nine Tenth Percent (89.9%) of all Gross Revenue between \$15,000,000 and \$17,500,000 and Eighty-Eight and Nine Tenth Percent of all Gross Revenue above \$17,500,000. In the event that 9.10% of all Gross Revenue up to \$15,000,000, 10.10% of all Gross Revenue between \$15,000,000 and \$17,500,000 and 11.10% of all Gross Revenue over \$17,500,000 does not equal or exceed \$800,000 in Year 1 of the Agreement, \$825,000 in Year 2 of the Agreement, \$850,000 in Year 3 of the Agreement, \$875,000 in Year 4 of the Agreement, and \$900,000 in Year 5 of the Agreement, then the payment to Follett shall be reduced by the difference between said amounts and the aggregate of the three latter percentages of the applicable amount of Gross Revenue. It is understood that \$800,000 in Year 1 of the Agreement, \$825,000 in Year 2 of the Agreement,

EXHIBIT C-1 (Continued)

\$850,000 in Year 3 of the Agreement, \$875,000 in Year 4 of the Agreement, and \$900,000 in Year 5 of the Agreement is the absolute minimum that the University shall retain of the Gross Revenue regardless of the results of operation of the Bookstore.

3. The term "Fiscal Year" means the twelve months beginning on a July 1 and ending on the next June 30.

The \$5,078,792 shown as commission receipts represents 9.1% of total commission sales estimated to be \$55,810,900 over the five-year management agreement period, none exceeding \$15 million during any one fiscal year.

NOTE 2:

The University's in-house cost estimate (Exhibit B) identified \$293,459 as a utility cost that would be avoided upon privatization. Although those costs would continue to be incurred by the University upon privatization, the contractor has contractually agreed to reimburse the University for those utility costs (heating, air conditioning, water and sewer) estimated to be \$274,677 for the five-year contract period. However, inasmuch as the contractor's payments merely represent a reimbursement to the University for its continuing utility expenditures, those reimbursements cannot be deemed to be income to the University. Accordingly, we have adjusted the University's claimed income projection to exclude therefrom the \$274,677.

NOTE 3:

As explained in Exhibit B, the University's in-house cost estimate (Exhibit B) identified \$800,000 for contemplated renovations to the US that would be avoided upon privatization. Although these contemplated renovations have been neither approved nor authorized by the University's Facilities and Planning Division, the need for renovations is indicated by the successful bidder's contractual commitment to expend \$875,000 for that purpose.

Section VII, Paragraph D, of the proposed management agreement states that ownership of the furniture, fixtures, and equipment (FFE) portion of the \$875,000 renovation cost will remain with Follett, the successful bidder, which Follett estimates at \$425,000. However, Follett, in responding to an April 11 University inquiry, proposed adding the following provisions pertaining to FFE ownership be inserted into the management agreement at Section VII, Paragraph D:

Insert at the end of Paragraph 6: Upon the expiration of the full term of this Agreement, or the earlier payment of any unamortized amount pursuant to termination of this Agreement other than for cause, the University and/or UMBA will become the owner of all furniture, fixtures and equipment provided by Follett pursuant to this Section VII, and Follett will execute and deliver any and all instruments necessary to effect same.

EXHIBIT C-1 (Continued)

Insert at the end of Paragraph 7: Upon the expiration of the full term of this Agreement, or the earlier termination of the Agreement for cause, the University and/or UMBA will

become the owner of all furniture, fixtures and equipment provided by Follett pursuant to this Section VII, and Follett will execute and deliver any and all instruments necessary to effect same.

We believe the contractual insertion of these clarifying provisions establishes ownership of the FFE to be with the University upon completion of the management agreement.

NOTE 4:

As of the date of our review, agreement had not been reached on the purchase price of the inventory to be acquired by the contractor. Section IV, Paragraph D, of the management agreement provides:

On a date which is mutually agreeable to the University and Follett (Contractor), but in no event later than July 31, Follett shall purchase the University's inventory of books, school supplies, apparel, gifts, and other similar items retailed by the Bookstore . . .

The management agreement further provides that Follett will use various guidelines in pricing the bookstore inventory, pertaining, respectively, to New Textbooks; Used Books; Trade, Reference and Technical Books; and General Merchandise.

Notwithstanding that the University does not presently know whether it will realize a profit or loss on the inventory sale, the University nevertheless has identified the total estimated value (\$1,280,000) as a gain on its sale without considering its acquisition cost.

The various books and merchandise were acquired by the University at a cost to be recovered by subsequent sale. The difference between purchase cost and sales price represents either the profit or loss to be realized. The University's assumption that the sales price to be paid by the contractor for purchasing these books and merchandise represents a profit to the University, without factoring for the acquisition cost, is neither supportable nor rational.

The University cites the following Section 4-c.3 of the Auditor's Guidelines for Implementing the Commonwealth's Privatization law as justification for its position:

3. Gain or Loss on Disposal of Assets: A decision to contract out a function may eliminate the need for all or some of the assets for that function. The disposal value of these assets should be included in the cost comparison. The estimated disposal value, minus the estimated cost of disposal, would be treated as a gain and would reduce the cost of contracting.

However, the cited section is not intended to apply to an activity's end product, which in this case consists of the saleable books and merchandise. Rather, it pertains to those assets (capital or minor)

EXHIBIT C-1 (Continued)

supporting the function, such as furniture, fixtures, equipment, vehicles, and other fixed asset types that at best have a salvage or disposal value.

The finished product, however, was not contemplated as "disposal" if a market existed for its sale. The student body and others comprise the market for the Bookstore's products. The contractor's purchase of the inventory products rather than by sale to the student body and others, does not lessen the need to offset the sales price by the inventory's acquisition cost.

Due to the uncertainty of the extent of gain or loss resulting from the future sale of inventory to the contractor, an accurate assessment cannot be made at this time of the effect thereof on the revenue enhancement shown on Exhibit A as \$1,320,291. However, we believe that the \$1,320,291 provides sufficient margin to absorb any inventory sale loss.

The following analysis of year-end inventory values provided by the University for 1998, 1999, and 2000 does not indicate that any significant loss will result from the sale of the June 30, 2000 inventory to the successful bidder:

| | <u>Fiscal Year Ended June 30</u> | | |
|-----------------------------|----------------------------------|--------------------|-------------------|
| | <u>1998</u> | <u>1999</u> | <u>2000</u> |
| | <u>Actual</u> | <u>Actual</u> | <u>Estimated</u> |
| June 30 Inventory | \$2,036,316 | \$2,031,801 | \$1,848,000 |
| Deduct Textbooks | <u>991,851</u> | <u>1,002,188</u> | <u>909,000</u> |
| Remaining Inventory at Cost | <u>\$1,044,465</u> | <u>\$1,029,613</u> | <u>\$ 939,000</u> |
| Inventory Reduction (10%) | <u>\$ 104,447</u> | <u>\$ 102,961</u> | <u>\$ 93,900</u> |

NOTE 5:

This \$61,784 adjustment pertains to estimated sales tax collections for nontaxable transactions such as textbooks (new and used) and tradebooks that were inadvertently included as an element of revenue enhancement. University personnel agree with this adjustment.

Section VII, Paragraph L.1 of the Proposed Management Agreement provides:

Follett (the successful bidder) may acquire goods and services from the University as would typically be provided to any University department. Such goods and services will be made available to Follett at the same price as would be charged by the University to its departments.

Although the University does not pay sales taxes on these interdepartmental transactions, a similar exemption may not pertain to the successful bidder for its purchases from University departments. The University spokesperson stated that should the successful bidder exercise the above-cited option, the University "would ask the Department of Revenue whether sales tax applies."

EXHIBIT C-1 (Continued)

NOTE 6:

The University's revised in-house cost estimate of April 25, 2000 increased its December 3, 1999 Auxiliary Services cost avoidance from \$503,422 to \$1,851,219, as follows:

| | |
|--|--------------------|
| Salaries and Fringe Benefits | |
| (8 positions and student payroll) | \$1,697,222 |
| Maintenance of Riverview Point of Sale System | <u>153,997</u> |
| Total Auxiliary Service Avoidable Cost, as Revised | <u>\$1,851,219</u> |

These Riverview maintenance costs (\$153,997), are exclusive of the ongoing day-to-day maintenance of the system costs that were included in the in-house cost estimate as part of the cost category Lease, Rent and Repair. The \$153,997 avoidable cost identified as Auxiliary Services pertains to the following expenditures that, according to the University's spokesperson, would be necessary to upgrade this five-year old system should the University continue to operate the store.

| | |
|---|------------------|
| Replacement of 40 cash register terminals | \$ 80,000 |
| Replacement of 25 PCs | 37,500 |
| Training | 10,997 |
| Server upgrade | 20,000 |
| Upgrade of printers | <u>5,000</u> |
| Total | <u>\$153,997</u> |