



City of Madison Finance Department
ALCOHOL LICENSE REVIEW
INTERNAL AUDIT REPORT

Audited Entity: Cheba Hut Restaurant

Fieldwork Completion Date: July 8, 2025

Date of Report: August 4, 2025

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EXECUTIVE SUMMARY

BACKGROUND

At its meeting on May 29, 2025, the Alcohol License Review Committee (ALRC) requested that the City Finance Department conduct a comprehensive compliance review of Cheba Hut to determine their adherence to the City of Madison General Ordinance (MGO) Sec. 38.05(10)(b). This ordinance stipulates that alcoholic beverage sales must constitute no more than 50% of a restaurant's total gross receipts. The ALRC requested that this financial audit review sales for the period of January 2023 through May 2025.

In addition, MGO Sec. 38.05(1) requires that a license, permit, or other formal authorization be obtained by any individual or organization intending to sell, manufacture, brew, rectify, or engage in any activity regulated under Wisconsin Statutes Chapter 125.

As part of the licensing process:

- All applications must be filed by April 15 of each year.
- The ALRC reviews and approves applications at its first meeting in June.
- Licenses and retail permits to sell alcoholic beverages expire on June 30 annually.

This audit was conducted in alignment with the ALRC's oversight responsibilities and the City's commitment to ensuring compliance with applicable ordinances and licensing conditions.

OBJECTIVES

This engagement aims to determine whether Cheba Hut Restaurant complied with Madison General Ordinance 38.05(10)(b), which requires that no more than 50% of a restaurant's gross receipts derive from alcoholic beverage sales.

SCOPE AND METHODOLOGY

The audit covered a period of 29 months ending May 31, 2025. Audit procedures included:

- Review of income statements and monthly sales reports.
- Analysis of POS itemized sales data.
- Reconciliation to bank statements and sales tax filings.
- Evaluation of internal controls over sales classification.
- Sampling of daily sales to verify the correct categorization of alcohol vs. food.

FINDINGS

Compliance with the Madison General Ordinance (MGO)

Based on the financial and sales data provided by the establishments, the audit found that Cheba Hut was in compliance with the provisions of MGO Sec. 38.05(10)(b) throughout the entire review period. The business reported an overall alcoholic beverage sales ratio of 14.94% relative to its gross receipts, well below the 50% threshold required for restaurants.

Reconciliation of POS Total Sales to other Financial Records

The review of the financial statements, Point-of-Sale (POS) system reports, and supporting documentation revealed a discrepancy in the reported income figures, specifically, variances between POS sales data and the sales tax returns submitted to the City of Madison by one of the restaurant operators. This observation suggests a potential underreporting of taxable sales.

RECOMMENDATIONS

The Alcohol License Review Committee (ALRC) and the Office of the City Attorney will determine the appropriate course of action to address these findings, in accordance with the protocols established under the Madison General Ordinance (MGO).

Note: See findings and recommendations beginning on page eight (8) for more detail.

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INTRODUCTION

Pursuant to City of Madison General Ordinance (MGO) Chapter 38.05(10)(b) and in support of the City's commitment to regulatory compliance, the Internal Audit Unit conducted a compliance review of one of its licensed restaurant establishments - Cheba Hut.

This audit was conducted in accordance with the Generally Accepted Government Auditing Standards (GAGAS) and the International Standards for the Professional Practice of Internal Auditing issued by the Institute of Internal Auditors (IIA). These standards require that audits be properly planned and executed to obtain sufficient and appropriate evidence to support the findings and conclusions, in alignment with the defined audit objectives. This report presents the findings and conclusions derived from the audit work performed, including any control or procedural deficiencies determined to be significant in the context of ordinance compliance. Please note that the report does not reflect or incorporate any findings or assessments from external agencies.

BACKGROUND

As requested by the Alcohol License Review Committee (ALRC), the Internal Audit Unit has conducted a comprehensive compliance review of Cheba Hut—to assess adherence to the City of Madison General Ordinance (MGO) Sec. 38.05(10)(b). This ordinance stipulates that, for any business licensed as a restaurant, alcoholic beverage sales must not exceed 50% of total gross receipts.

In accordance with MGO Sec. 38.05(1), a license, permit, or other formal authorization must be obtained by any individual or organization intending to sell, manufacture, rectify, or brew alcohol, or to engage in any activity regulated under Wisconsin Statutes Chapter 125.

Applications for such licenses are filed through the Office of the City Clerk (as amended by ORD-18-00001, effective January 10, 2018). The City Clerk provides specific application forms for each license type or amendment, which must be completed and signed by the applicant. Each application is required to include, at a minimum, the following information:

1. The address of the building for which the license is desired, and the description includes the overall dimensions, seating arrangements, capacity, bar size of the premises therein, and any outside areas where alcohol beverages are to be sold (Am. by Ord. 9719, 3-2-89).
2. A statement that the applicant is an individual or a domestic corporation. Where the applicant is a limited liability company, the identity of the company members, managers and agent. (Am. by Ord. 10,883, Adopted 4-5-94).
3. A statement that the applicant has resided continuously in Wisconsin for not less than ninety (90) days prior to the date of such application.
4. A statement as to whether applicants have ever been convicted of a felony or of a violation of any Federal or State act, or ordinance of the City of Madison, regulating or prohibiting the sale of intoxicating or non-intoxicating liquor, and if so, the number and dates of such convictions and the penalty imposed.
5. A statement as to whether the applicant holds or has applied for any other Class A or Class B licenses for any other location within the State and, if so, the number of such licenses held or applied for by such applicant.
6. A statement as to whether any other business other than the sale of alcohol beverages as herein defined is to be conducted on the premises ought to be licensed, and if so a description of the nature of such business.

7. A statement that the applicant is not acting as agent for or in the employ of another.
8. If the application be for an operator's license, it shall state the age and sex of the applicant.
9. A statement as to whether any brewer, bottler, wholesaler, or corporation, a majority of whose stock, or if the entity is a limited liability company, a majority of which is owned by any brewer, bottler or wholesaler, has or intends to supply, furnish, lease, give, pay for, or take any chattel mortgage on any furniture, fixture, fittings, or equipment to be used in or about the premises covered by the application. (Am. by Ord. 10,883, Adopted 4-5-94).
10. A statement as to whether any brewer, bottler or wholesaler has advanced, paid or furnished the money for license fee, or intends to do so.
11. A statement as to whether any brewer, bottler, or wholesaler is financially interested in, directly or indirectly, the license for which application is made.

This regulatory framework supports the City's oversight of alcohol licensing and ensures businesses operate within the bounds of the law.

All license applications must be filed with the City Clerk's Office on or before April 15 of each year. Applications are subsequently reviewed and approved by the Alcohol License Review Committee (ALRC) during its first meeting in June.

While the City Clerk may conditionally accept late renewal applications, any application that contains deficiencies or fails to meet the required criteria will not be forwarded to the ALRC or the Common Council for consideration until all deficiencies are resolved.

In accordance with the ordinance, a late filing fee of \$250 must be paid prior to the Common Council granting a license in the following circumstances:

1. For each renewal application received after April 15, and
2. For each application in which deficiencies are corrected after April 15.

This late fee is intended to recover the administrative costs incurred in processing noncompliant applications. However, payment of the late fee does not exempt an applicant from any additional penalties prescribed by the ordinance for failing to obtain or maintain a valid license.

All licenses and retail permits to sell alcoholic beverages in the City of Madison expire on June 30 of each year.

SCOPE

The scope of this audit was limited to reviewing business activities related to the sale of alcoholic beverages, with a specific focus on evaluating each establishment's compliance with the Madison General Ordinance (MGO) Sec. 38.05(10)(b).

The audit covered the period from January 1, 2023, through May 31, 2025, providing a comprehensive twenty-nine-month review window. This timeframe allowed the Internal Audit Unit to:

- Assess historical sales data
- Identify potential patterns or trends in alcohol sales

- Evaluate the impact of past practices on current compliance
- Determine whether alcohol sales exceeded the 50% gross receipts threshold during any part of the review period

This focused scope ensured that the audit findings were relevant, timely, and aligned with the ordinance's intent to maintain appropriate licensing standards for establishments operating as a restaurant.

AUDIT OBJECTIVES AND METHODOLOGY

The primary objective of this audit engagement was to determine whether Cheba Hut restaurant complied with the requirements of Madison General Ordinance (MGO) Sec. 38.05(10)(b), which mandates that no more than 50% of a restaurant's gross receipts may be derived from the sale of alcoholic beverages.

To support this objective, the audit focused on assessing the effectiveness of operations and compliance controls within the following key areas:

1. Revenue Classification and Reporting Accuracy

- Verification of how sales were categorized between alcoholic and non-alcoholic items
- Review of consistency between financial statements, POS data, and tax records

2. Sales Tracking and Reconciliation

- Analysis of Point-of-Sale (POS) reports to ensure an accurate recording of daily sales by category
- Reconciliation of POS records to bank statements and general ledger data

3. Compliance Monitoring

- Determination of whether each restaurant continuously monitored its alcohol sales ratio
- Review of efforts to correct or maintain compliance over the review period

This structured approach allowed the Internal Audit Unit to form a well-supported conclusion on each establishment's level of compliance with the ordinance.

The Internal Audit conducted interviews with stakeholders and performed reviews of requested documents to determine if:

1. Financial records were obtained from the owners and analyzed to confirm consistency across all sources. The following procedures were implemented to ensure consistency across all sources:
 - Reviewing monthly income or annual income statements (Jan 2023 to May 2025) and sales tax returns for the audit period (2023 and 2024).
 - Reviewing POS (Point of Sale) system reports detailing sales by category (alcohol, food, non-alcoholic beverages).
 - Reviewing bank statements and deposit records.
 - Reviewing general ledger or trial balance (where applicable).
2. Analytical procedures were performed on the financial documents received to substantiate the validity of the financial records:
 - Comparing monthly trends in alcohol vs. food sales to identify spikes or anomalies.
 - Calculating the percentage of alcohol sales to gross receipts (total sales) for each period.
 - Selecting a sample of daily or weekly sales reports and reconciling totals to bank deposits.
 - Matching POS alcohol sales with liquor purchase records to verify reasonableness.
 - Verifying that any "bundled" promotions (e.g., drink + meal) are appropriately split in the accounting records.

3. The Internal Audit unit performed other tests for revenue classification accuracy. The tests performed included:
 - Selecting a sample of daily sales reports and trace to POS data to confirm correct classification of items (e.g., ensuring beer/wine/liquor are recorded under alcohol).
 - Checking whether combo meals or discounting schemes misallocate revenue (e.g., improperly assigning alcohol revenue to food).
4. Reconcile Records:
 - Reconciling total sales from POS systems to bank deposits and financial statements.
 - Investigating discrepancies or unrecorded cash sales (where applicable).

The following section contains a detailed listing of each audit finding and applicable internal audit recommendations.

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FINDINGS AND RECOMMENDATIONS

Reference 1: Compliance with the Madison General Ordinance (MGO)

Finding

To assess compliance with Madison General Ordinance (MGO) Sec. 38.05(10)(b), the Internal Audit Unit reviewed financial records submitted by each establishment for the audit period, including:

- Point-of-Sale (POS) reports
- Sales Tax Returns
- Monthly Income Statements

Based on our analysis of the financial and sales data provided by the establishments, we observed that Cheba Hut demonstrated compliance with the provisions of MGO Sec. 38.05(10)(b) by maintaining alcoholic beverage sales at less than 50% of its total gross receipts in each month reviewed. The average percentage of alcohol sales relative to gross receipts over the twenty-nine-month period was 14.94%, well below the regulatory threshold.

The table below summarizes Cheba Hut's monthly alcoholic beverage sales as a percentage of gross receipts:

Year	Month	% of Alcoholic Sales to Gross Sales
2023	January	16.89303601
	February	15.85271733
	March	16.56541876
	April	14.52274794
	May	17.99506496
	June	20.37929825
	July	20.62958356
	August	16.4795017
	September	16.35175346
	October	15.74641861
	November	14.96487888
	December	14.84435751
2024	January	11.09790127
	February	11.28842789
	March	12.26255785
	April	12.28613212
	May	15.75247808
	June	14.04144991
	July	14.92693442
	August	15.95265979
	September	14.09781865
	October	13.87904879
	November	10.89255698
	December	12.04034575
2025	January	10.74745924
	February	13.32717719

	March	15.1519228
	April	16.43149128
	May	17.40086313
Monthly Average		14.94%

Recommendation

The Alcohol License Review Committee (ALRC) and the Office of the City Attorney will determine the appropriate course of action to address these findings, in accordance with the protocols established under the Madison General Ordinance (MGO).

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Reference 2: Reconciliation of POS Total Sales to other Financial Records.***Finding***

As part of our review, the Internal Audit Unit examined the financial statements, Point-of-Sale (POS) system reports, and supporting documentation submitted Cheba Hut restaurant for the audit period to confirm consistency and accuracy across all sources.

During this review, we identified discrepancies in reported income figures—specifically, variances between POS sales data and the sales tax returns submitted to the City of Madison by the restaurant operators. This observation suggests a potential underreporting of taxable sales.

While this issue falls outside the originally defined scope of this audit engagement (focused on compliance with MGO Sec. 38.05(10)(b)), it is being disclosed in this report to ensure compliance with the Institute of Internal Auditor Professional Practice Framework (IPPF) and Standards. Accordingly, this matter has been referred to the appropriate City and State agencies responsible for overseeing sales tax reporting and compliance through the ALRC in a separate memo for further investigation and resolution.

Recommendation

The potential underreporting of taxable sales has been referred to by the appropriate City and State agencies for further review to determine whether restaurant operators may be deliberately understating their income to reduce their reported taxable sales.

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CONCLUSION

To the best of our knowledge and based on the information and documentation made available during the audit, the findings outlined above represent a fair and accurate assessment of sales activity and revenue classification for Cheba Hut.

As of the conclusion of this review, this establishment is currently in compliance with the requirements of Madison General Ordinance (MGO) Sec. 38.05(10)(b), which limits alcoholic beverage sales to no more than 50% of a restaurant's gross receipts.

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ACKNOWLEDGEMENT

The Alcohol License Review

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Signing below certifies that you have received, read, and acknowledge the audit report prepared above.

David Schmiedicke

David Schmiedicke, Director Finance

August 12, 2025

Date

Jennifer Zilavy

Jennifer Zilavy, Assistant City Attorney

August 12, 2025

Date