

Red Springs ABC Board

Performance Audit Report



Alcoholic Beverage Control Commission
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ABC
COMMISSION
NORTH CAROLINA

TABLE OF CONTENTS

ABC Commission Statement.....	3
Operational Observations, Findings, and Recommendations.....	6
Auditor’s Summary.....	16
Red Springs ABC Board Response.....	17
Appendices.....	18



Alcoholic Beverage Control

June 11, 2014

CHAIRMAN:
JAMES C. GARDNER

COMMISSIONERS:
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Wake Forest

KEVIN M. GREEN
Greensboro

ADMINISTRATOR:
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Moniqua S. McLean
ABC Board Auditor

Red Springs ABC Board
Mr. Malcolm Watson, Chairman
PO Box 768
Red Springs, NC 28377

Dear Chairman Watson,

We are pleased to submit this performance audit report on the Red Springs ABC Board. The objective of this audit was to examine existing policies, practices, and controls and to provide recommendations on methods to improve operating efficiency at the ABC Board in accordance with new legislative mandates.

The report consists of an executive summary, background information, operational findings and recommendations along with your response to our recommendations. This report will be posted on the Commission’s public web site.

We would like to thank you, the ABC Board and your staff for the assistance and cooperation provided to us during the audit. Additionally, we appreciate the efforts your Board has made to comply with the new performance standards and our recommendations along with your continuing efforts to reduce expenses and increase profits.

If we can be of assistance in the future, please advise.

Respectfully,

Michael C. Herring
Administrator

CC. North Carolina Association of ABC Boards

EXECUTIVE SUMMARY

By state law, the ABC Commission shall ensure that all local ABC Boards comply with established performance standards by conducting regular audit or performance evaluations. Performance standards shall include, but are not limited to, standards that address enforcement of ABC laws, store appearance, operating efficiency, solvency, and customer service. Performance audits are examinations of existing operating policies, practices, controls, and activities to determine those areas in which there may be a need for improvements. This audit was conducted in accordance with Government Auditing Standards. This report details findings and recommendations with regard to organizational and operational issues.

To achieve the objectives of the audit, ABC Commission staff

- Reviewed applicable General Statutes, ABC Commission Rules, and administrative policies;
- Reviewed applicable reports and studies of ABC boards with similar size and geography;
- Verified compliance with Commission and Board policies;
- Reviewed organizational chart and job descriptions;
- Reviewed ABC store annual audit for the fiscal year 2013;
- Visited the store;
- Interviewed key ABC board personnel.

BACKGROUND INFORMATION

Chapter 405 of the 1967 Session Laws authorized the Town of Red Springs to hold an election for an ABC store upon at least twenty-five percent (25%) of registered voters. The referendum was held on May 9, 1973 and passed 351 to 326. A mixed beverage election was held on January 11, 2005 and did not pass. The first sale occurred on August 6, 1973.

Upon election of an ABC store, the town was authorized to create an ABC board consisting of a chairman and two board members to serve for three year terms. Current board members include Malcolm C. Watson, board chairman, Alton McNeill and Crawford Garland Arrington, III, board members.

The Red Springs ABC Board operates one retail store. The board staffs two full-time and four part-time employees. The general manager manages all daily operations of the store including supervising personnel, administrative functions, inventory control, and providing customer service. All store employees extend friendly service to customers, store upkeep, and stock maintenance. The board has hired an external bookkeeper to serve as the finance officer and to provide additional checks and balances.

OPERATIONAL OBSERVATIONS, FINDINGS, AND RECOMMENDATIONS

On February 5, 2014, ABC Board Auditor, Moniqua S. McLean, visited the Red Springs ABC store and interviewed Carl Bounds, general manager. Below is a financial analysis followed by operational observations, findings, and recommendations related to the performance audit.

FINANCIAL ANALYSIS

INVENTORY TURNOVER

The inventory turnover is calculated by dividing the cost of liquor by the average inventory in the system (Cost of Liquor/Average Inventory).

The Red Springs ABC Board receives deliveries one time a month: the inventory turnover rate is 3.5. The average rate for similar boards with the same delivery schedule is 4.6.

RECOMMENDATIONS

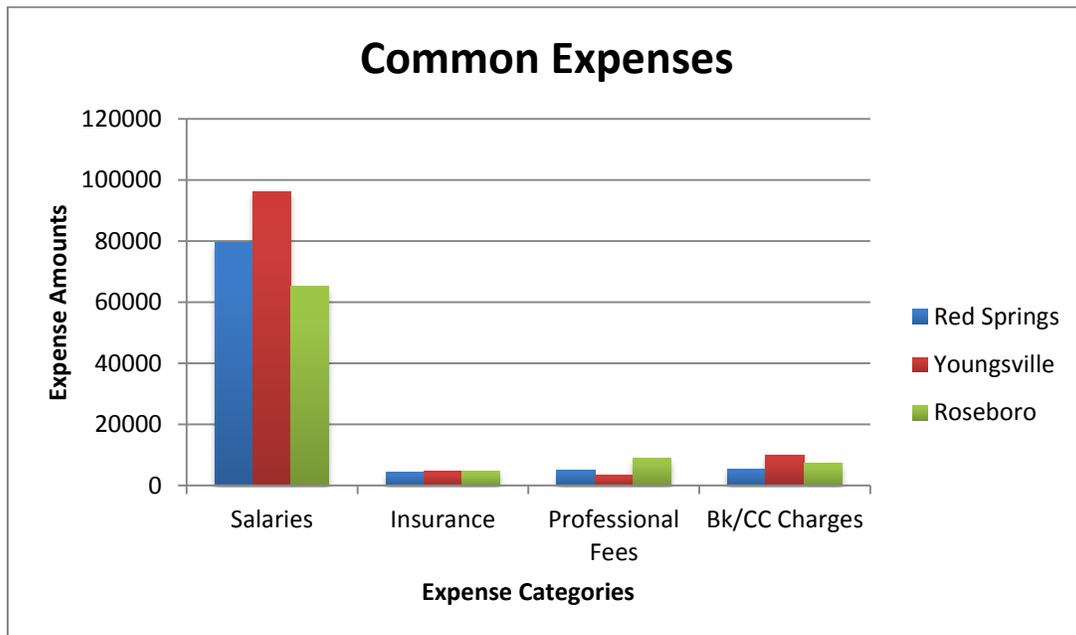
1. Consider the following to increase inventory turns:
 - Utilizing end caps and shelf space as much as possible to highlight slow moving, seasonal and new products;
 - Incorporating a shelf management plan that analyzes sales data to target shopping patterns;
 - Moving stock within store to increase visibility and to encourage more impulse shopping.

OPERATING COST RATIO

Operating costs are calculated by dividing total operating expenses less depreciation by the gross profit on sales (Total Operating Expenses less Depreciation/Gross Profit). Below are the average cost ratios for boards with and without mixed beverage sales (MXB):

- Single store boards with MXB sales that are equal to or greater than 25% of gross sales – cost ratio 0.75
- Single store boards with MXB sales less than 25% of gross sales – cost ratio 0.85
- Single store boards without MXB sales – cost ratio 0.85
- Boards with 2 stores with and without MXB sales – cost ratio 0.74
- Boards with 3 or more stores with and without MXB sales – cost ratio 0.64

The Red Springs ABC Board operates one retail store without mixed beverage sales; the operating cost ratio is 0.84. In fiscal year 2013, sales increased 4.6% over fiscal year 2012 while expenses increased 11% over the same time period. The board contributes to significant savings in overhead expenses as a result of owning the store and using local businesses to provide various services.



The data indicates that Red Springs ABC Board's common expenses are within range of other boards' common expenses.

WORKING CAPITAL

Working capital is total cash, investments, and inventory less all unsecured liabilities. Gross sales means gross receipts from the sale of alcoholic beverages less distributions as defined in G.S. 18B-805 (b), (2), (3), and (4). The Commission has set efficiency goals based on the following breakdown:

- Four months for boards with gross sales less than \$1.5M
- Three months for boards with gross sales less than \$50M and greater than or equal to \$1.5M
- Two months for boards with gross sales equal to or greater than \$50M

In FY2013, Red Springs ABC had a working capital of \$163,444, which is less than four months gross sales and is within the limits of NCAC 02R .0902.

PROFIT PERCENTAGE TO SALES

The profit percentage to sales is calculated by dividing the total income before distributions by the total liquor sales (Total Income before Distribution/Total Liquor Sales). The Commission has set goals based on the following breakdown:

- Gross sales greater than \$10M – target rate at 9%
- Gross sales between \$2M to \$10M – target rate at 6.5%
- Gross sales less than \$2M – target rate at 5%

In fiscal year 2013, the Red Springs ABC Board had gross sales of \$702,344; income from operations was \$27,263, a 3.88% profit percentage to sales.

Factors affecting sales and profitability:

- Sales increased 4.6% over the previous fiscal year;
- Surrounding towns with ABC stores within a fifteen mile radius include Pembroke, Maxton, Saint Pauls, and Lumberton;
- A neighboring store reopened after being closed since 2008;
- Population of Red Springs is estimated to be 3,428 in 2010;
- Growth and development in surrounding, more heavily populated areas has led to a shift in shopping patterns away from small rural areas.

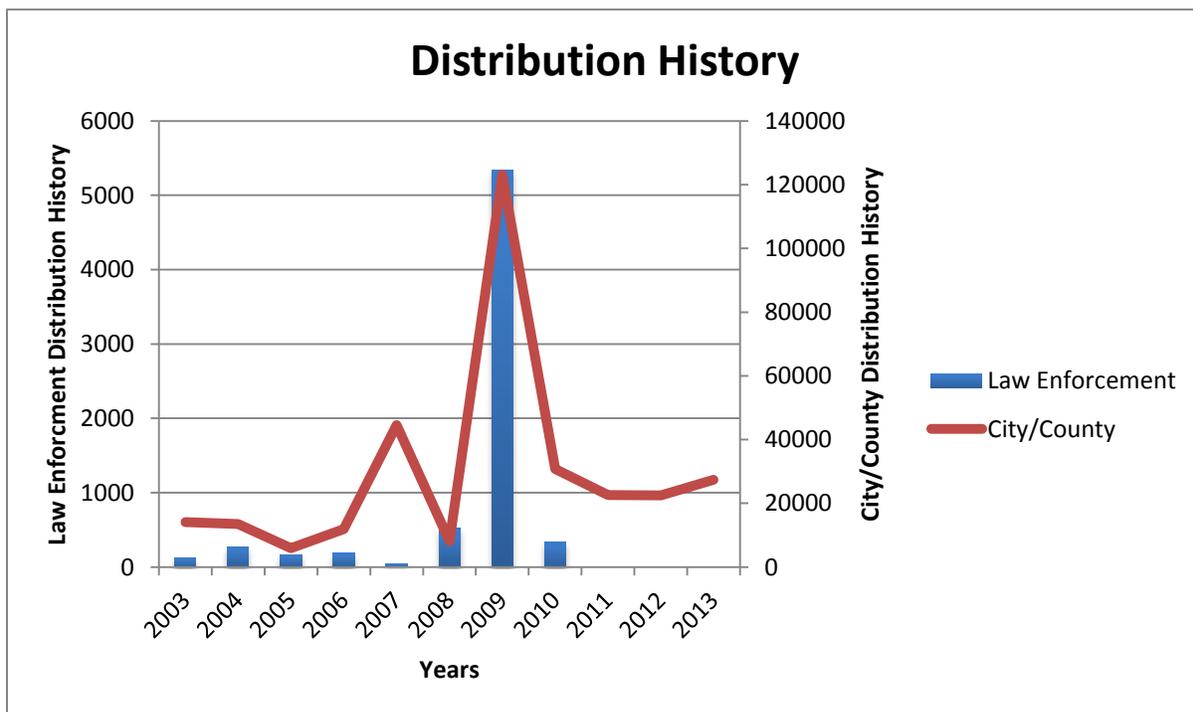
DISTRIBUTIONS

G.S. 18B-805 (c) (2) requires the board to distribute at least five percent (5%) of profits to law enforcement. Alcohol education distributions are not required under the enabling act. The remaining profits are to be distributed as follows:

- Sixty-five percent (65%) to Red Springs General Fund for any governmental, library, recreational or educational purposes;
- Thirty-five percent (35%) to Robeson County General Fund for any governmental, library, educational, or hospital purposes.

In FY2013, Red Springs ABC made the required minimum distribution to the town totaling \$21,104 plus additional distribution of \$6,327. \$158,600 in state excise and other taxes were paid to the NC Department of Revenue and the town. Law enforcement distributions were not paid.

Below is a distribution chart analyzing the high-low trend of the Town of Red Springs ABC Board.



RECOMMENDATIONS

1. Begin making the mandatory law enforcement distributions quarterly as required by G.S. 18B-805 (c) (2).

STORE APPEARANCE AND CUSTOMER SERVICE

The Red Springs ABC Board operates one retail store with approximately 800 linear feet of shelf space and carries approximately 600 product codes.

- The store appears clean; however, dust is found on bottles. Counter areas are free of clutter and supplies are easily accessible.
- Exterior signage and landscaping around the store is clean and free of trash. Interior signage is neat and visible. The Fetal Alcohol Syndrome poster is displayed and visible to the public.
- A shelf management plan is not in use. Current product placement follows the product code sequence from smallest to greatest according to category. With this strategy, sizes are going largest size to the left and smallest size to the right and vice versa. Bottles are found in other categories. Premium products are found on the lower shelves and lower priced products are found on the eye-level or top shelves. End caps and other shelves are empty and under-utilized. *See pictures on page 18.*
- The state price book is available should customers ask for specific product. Sales clerks' often refer to the price book for verification of product and pricing.
- Sales clerks' interaction with customers is attentive and courteous.

RECOMMENDATIONS

1. Dust bottles regularly. Incorporate practices within daily store activities.
2. Develop a more efficient shelf management plan that focuses on the growing market. Consider the following practices:
 - Brand blocking products with bottles with mid-price at eye level and premium products on top shelves and lower priced items on lower shelves;
 - Increasing cross-merchandising by placing products that mix together on the same shelves;
 - Reallocating shelf space from declining categories to those showing growth;
 - Aligning products by specific flavor profiles rather than code number;
 - Utilizing end caps to highlight new, seasonal, and sale products on a rotating basis.

PERSONNEL AND TRAINING

- All board members, general manager, and finance officer have completed the initial ethics training. However, one board member's term has expired and has not been reappointed.
- Cross training opportunities are being extended to key employees in the event the general manager was suddenly unavailable.
- Training has been provided to new and existing staff on clerk responsibilities. However, training has not been made available to employees on key areas such as product knowledge, customer service issues, RASP training, and etc.
- Personnel files are available and displayed documentation for tax withholdings and other personnel information.

RECOMMENDATIONS

1. Extend and provide other training opportunities that focus on those listed above to all employees. Contact the Commission and other boards who have information on these topics.

ABC BOARD POLICIES

- Policies adopted and submitted to the Commission include:
 - Code of Ethics
 - Law Enforcement Contract
 - FY2013 Annual Audit
 - FY2014 Budget (Proposed and Adopted)
 - Employee Handbook
 - State Travel Policy

- Policies not adopted and submitted to the Commission include:
 - Price Discrepancy Policy

RECOMMENDATIONS

1. Adopt a price discrepancy policy that incorporates customer friendly practices. Once adopted, communicate to all employees before the need arise so that they are informed on how to implement the changes. *Refer to Appendix B (1) for rule.*

INTERNAL CONTROL PROCEDURES

- Time sheets are used by all clerks to record hours worked. Two signatures are placed on the time sheets, that of the general manager and employee. The general manager verifies all hours reported for accuracy and manually calculates wages, tax and other withholdings as a check and balances mechanism. However, calculations are inputted in accounting software to create payroll checks. The accounting software is backed up at every use.
- Cash drawers are counted by all clerks. All clerks are responsible for their own cash drawer. Management has implemented procedures in handling shortages, whereas all shortages and overages are recorded in a daily log.
- Bank deposits are made regularly as required by the ABC Commission rule. Bank notification is received and matched with corresponding daily register reports. Bank reconciliations are completed monthly by the finance officer.
- Physical inventory counts are completed monthly by the general manager and another clerk. Spot checks are conducted if a potential loss. If discrepancies occur, the general manager investigates and recounts for accuracy and verification. Once completed, only the general manager will adjust the system to match with the actual store counts. Unsalable items are deducted from the inventory system on a monthly basis.
- Out of approximately 600 product codes, approximately ninety product codes were sampled and three were incorrect.

RECOMMENDATIONS

1. To ensure correct pricing, audit shelf tags on a regular basis by incorporating practices within spot checking or inventory checking time periods.

ADMINISTRATIVE COMPLIANCE FINDINGS AND OBSERVATIONS

- Board meeting minutes were viewed and followed the order of proceedings, providing sufficient detail that a reasonable person would be able to follow what transpired. However, board meeting minutes were not kept at the store or made immediately available. Minutes did not reference a conflict of interest statement.
- Board member appointment dates are current on the Commission website. However, compensation amounts for the general manager were not current.
- Board member and general manager compensation is in compliance with G.S. 18B-700 (g) and (g1).
- Law enforcement activity reports have been submitted to the Commission as required by G.S. 18B-501 (f1).
- Nepotism – The board employs two family members-the general manager and another employee-who were grandfathered in when the law changed. However, another employee has been employed after the enactment of the statute.
- All board members and general manager are bonded for \$50,000 as required by G.S. 18B-700 (i). However, the finance officer is not bonded under the board’s policy.
- Orders for liquor and other miscellaneous orders do not bear the pre-audit certificate as required by G.S. 18B-702 (m).
- All checks bear the approved certificate. Although the finance officer does not sign the checks, two signatures, that of the general manager and a board member, are located on the checks.

RECOMMENDATIONS

1. For transparency, have the board chairman read a conflict of interest statement to all board members at the start of each meeting. Reference the conflict of interest statement was read in the board minutes. *Refer to Appendix B (2) for rule.*
2. Update the Commission website to reflect current information on board members and the general manager. The Commission relies on information provided by boards to create reports.
3. Refrain from employing relatives. *Refer to Appendix B (3) for statute.*
4. Update the board’s bonding policy to include the finance officer as being bonded for \$50,000. *Refer to Appendix B (4) for rule.*
5. Place the pre-audit certificate with the finance officer’s signature on the order to LB&B. When ordering supplies, have a purchase order or order confirmation that will have authorization from the finance officer before the transaction takes place. *Refer to Appendix B (5) for statute.*

AUDITOR'S SUMMARY

ABC Board Auditor, Moniqua S. McLean, presented to the board the performance audit recommendations on April 24, 2014. The board has since responded to the performance audit recommendations and strives to implement strategies to maintain profitability while reducing costs and meeting budget appropriations. Economic constraints, a town re-opening an ABC store within ten miles and slow area growth, have caused the board to lose profits. Policies and procedures have been implemented to ensure compliance with statutes and Commission rules and to ensure efficient operations while maintaining sufficient checks and balances.

RED SPRINGS ABC BOARD
904 EAST FOURTH AVENUE
P. O. BOX 768
RED SPRINGS, NC 28377

May 1, 2014

Moniqua S. McLean, MAFM
ABC Board Auditor
ABC Commission
4307 Mail Service Center
Raleigh, NC 27699-4307

Dear Ms. McLean:

Thank you for attending our ABC Board meeting on Thursday, April 24, 2014. As we discussed during our meeting, the board and employees are making corrections on the areas you suggested.

Please find below, a few things that we have already done due to your audit:

- 1) We now have a price discrepancy policy which is in line with State policy.
- 2) At the beginning of our board meeting, the chairman reads G.S. 18B-201.
- 3) We have moved stock within the store to increase visibility and encourage more impulsive buying.
- 4) Checks are signed by the chairman and finance officer.

These are a few things that we are doing to help increase our sales and stay in line with the state requirements.

Thank you.

Sincerely,



Malcolm Watson
Chairman

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APPENDIX A

Illustration 1



Exterior view

Illustration 2



Interior view with shelving

Illustration 3



Product placement

Illustration 4



Counter view

APPENDIX B

- (1) NCAC 02R.1706 (b) states, "If a local board has a price discrepancy between the price on the shelf or bottle and the cash register, and the price on the shelf or bottle is lower, the local board shall sell the item at the shelf or bottle price and correct the shelf or bottle price to match the Commission's published uniform price."
- (2) OP 4.19.4 states, "In an effort to avoid possible conflicts of interest it is recommended at the beginning of each meeting the Chairman ask fellow board members if there are any potential conflicts of interest. This can be done by reading the following ethics reminder:
- 'In accordance with G.S. 18B-201, it is the duty of every Board member to avoid both conflicts of interest and appearances of conflicts. Does any member have any known conflict of interest or appearance of conflict with respect to any matters coming before the Board today? If so, please identify the conflict or appearance of conflict and refrain from any undue participation in the particular matter involved.'*"
- (3) G.S. 18B-700 (k) states, "Members of an immediate family shall not be employed within the local board if such employment will result in one member of the immediate family supervising another member of the immediate family..."
- (4) 18B-700 (i) states, "Each local board member and the employees designated as the general manager and finance officer of the local board shall be bonded in an amount not less than fifty thousand dollars secured by a corporate surety, for the faithful performance of his duties."
- (5) 18B-702 (m) states "...the contract, agreement, or purchase order shall include on its face a certificate stating that the instrument has been pre-audited to assure compliance. The certificate, which shall be signed by the finance officer or any deputy finance officer approved, shall take substantially the following form:

"This instrument has been pre-audited in the manner required by GS 18B-702."

(Signature of finance officer)

APPENDIX C

RECOMMENDATION FOLLOW UP

RECOMMENDATION	REQUIRED BY STATUTE	IMPLEMENTATION STATUS
<p>ABC Board Policies:</p> <p>Adopt the following policies:</p> <ul style="list-style-type: none"> • **Price Discrepancy Policy 	<p><input type="checkbox"/> Yes</p> <p><input checked="" type="checkbox"/> No</p> <p>**Note: Required by rule.</p>	<p>(Please provide documentation supporting implementation status.)</p> <p><input checked="" type="checkbox"/> Fully Implemented</p> <p><input type="checkbox"/> Partially implemented ____% complete. (Explain below.)</p> <p><input type="checkbox"/> Not implemented (Explain below.)</p> <p>The board has adopted the following policies and submitted copies to the Commission.</p>
<p>Administrative Compliance:</p> <ul style="list-style-type: none"> • Include the finance officer in the bonding policy to reflect a \$50,000 bond. • Affix the pre-audit certificate on all orders before the transaction occurs. 	<p><input checked="" type="checkbox"/> Yes</p> <p><input type="checkbox"/> No</p>	<p>(Please provide documentation supporting implementation status.)</p> <p><input checked="" type="checkbox"/> Fully Implemented</p> <p><input type="checkbox"/> Partially implemented ____% complete. (Explain below.)</p> <p><input type="checkbox"/> Not implemented (Explain below.)</p> <p>Management has updated and implemented policies and procedures to remain in compliance with the statute.</p>