

Chowan County ABC Board

Performance Audit Report



Alcoholic Beverage Control Commission
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ABC
COMMISSION
NORTH CAROLINA

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ABC

COMMISSION
NORTH CAROLINA

Alcoholic Beverage Control

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JAMES C. GARDNER

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Moniqua S McLean
ABC Board Auditor
919-779-8365

December 16, 2014

Chowan County ABC Board
Mr. Haywood Coston, Chairman
PO Box 88
Edenton, NC 27932

Dear Chairman Coston,

We are pleased to submit this performance audit report on the Chowan County ABC Board. The objective of this audit is 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 General Manager's 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 along with your efforts to maintain profitability and reduce expenses.

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

Respectfully,

Robert A. Hamilton
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 2014;
- Visited the store;
- Interviewed key ABC board personnel.

BACKGROUND INFORMATION

Chapter 49 of the 1937 Session Law authorized Chowan County to hold an election for an ABC store. The referendum was held on July 6, 1937 and passed 756 to 575. The first sale occurred on September 2, 1937. A mixed beverage election for Chowan County was held on May 5, 1992 and did not pass. However, a city mixed beverage election for the City of Edenton was held on May 3, 1994 and passed 632 to 473.

Upon election of an ABC store, the county 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 Haywood Coston, board chairman, Andy Hare and Garris Perry, board members.

The Chowan County ABC Board operates one retail store. The board staffs two full-time and four part-time employees. The general manager is responsible for the oversight of all daily operations pertaining to the store, inventory management, human resource organization, and other administrative decisions for the board. The finance officer is responsible for accounts payable functions, financial reporting activities, and other duties as required by the ABC Commission statutes and rules. Store employees are primarily responsible for providing friendly customer service to all customers, general store upkeep, and stock maintenance.

OPERATIONAL OBSERVATIONS, FINDINGS, AND RECOMMENDATIONS

On August 6, 2014, ABC Board Auditor, Moniqua S. McLean, visited the Chowan County ABC store and interviewed Lewis Waters, general manager, and Michael Brown, finance officer. Below is a financial analysis followed by operational observations, findings, and recommendations related to the performance audit.

FINANCIAL ANALYSIS

PROFIT PERCENTAGE TO SALES

The profit percentage to sales is calculated by dividing the total income from operations by the total liquor sales (Total Income from Operations/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 2014, the Chowan County ABC Board had gross sales of \$1,301,888; income from operations was \$55,421, a 4.3% profit percentage to sales.

Factors affecting sales and profitability:

- Population of Chowan County is approximately 14,726 in 2013, a 0.5% decrease since 2010;
- ABC stores within a twenty mile radius include Bertie and Hertford counties and the Town of Hertford (Perquimans County);
- A decrease in population has shifted growth and shopping patterns away from the county to more heavily trafficked urban areas;
- Debt for new store construction was paid off in January 2014.

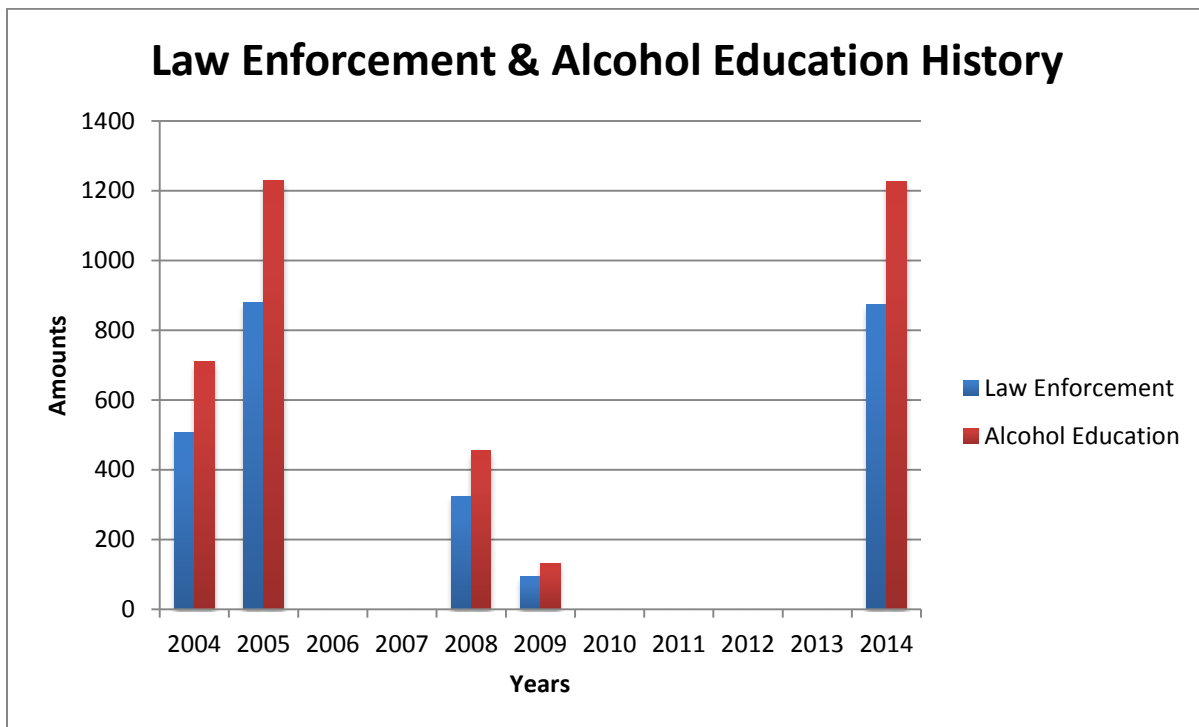
DISTRIBUTIONS

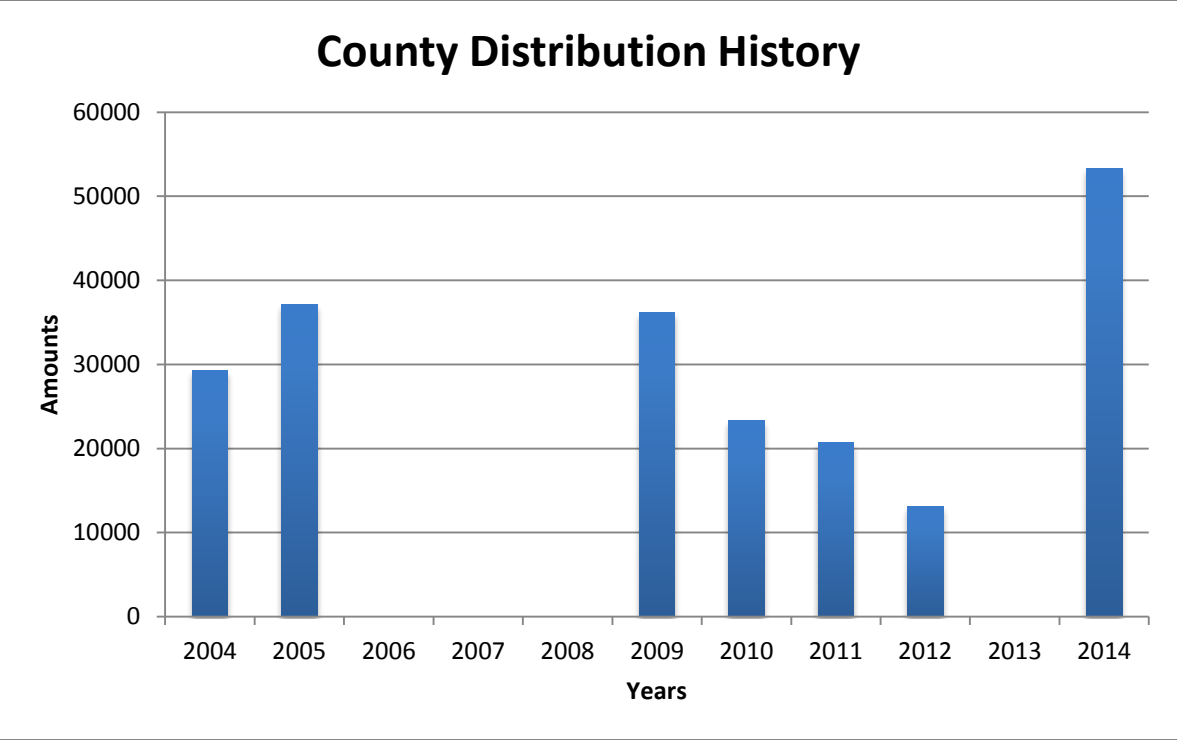
G.S. 18B-805 (b) requires the board to pay from gross receipts, all expenses, excise, mixed beverage, and bottle tax. G. S. 18B-805 (c) (1) requires the board to make a minimum quarterly distribution of the 3½% markup rate to the appointing authority. In FY2014, Chowan County ABC made the required distribution to the county totaling \$37,913, plus additional distribution of \$15,407. \$298,260 in excise and other taxes were paid to the NC Department of Revenue, the Department of Health and Human Services, and the county.

G.S. 18B-805 (c) (2) requires the board to distribute at least five percent (5%) of profits to law enforcement and at least seven percent (7%) to alcohol education/rehabilitation. The remaining profits are to be distributed to the Chowan County General Fund.

In FY2014, the Chowan County ABC Board distributed to the county \$875 to law enforcement. A law enforcement contract has been established with the Chowan County Sheriff's Department. Alcohol education/rehabilitation distributions total \$1,226.

Below are distribution charts analyzing law enforcement/alcohol education and county distributions high-low trends of the Chowan County ABC Board for the past ten years.





WORKING CAPITAL

G.S. 18B-805 (d) allows the board to set aside a portion of the remaining gross receipts, within the limits set by the rules of the Commission, as cash to operate the ABC system. 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 FY2014, the Chowan County ABC Board had a working capital of \$32,777, which is less than the minimum amount allowed of \$38,786. The FY2014 financial audit includes the OPEB liability that decreases the working capital. When excluding the OPEB liability, the calculation for working capital is \$157,366, which is less than the maximum allowed to retain of four months gross sales (\$334,511) and is within the limits of NCAC 02R .0902.

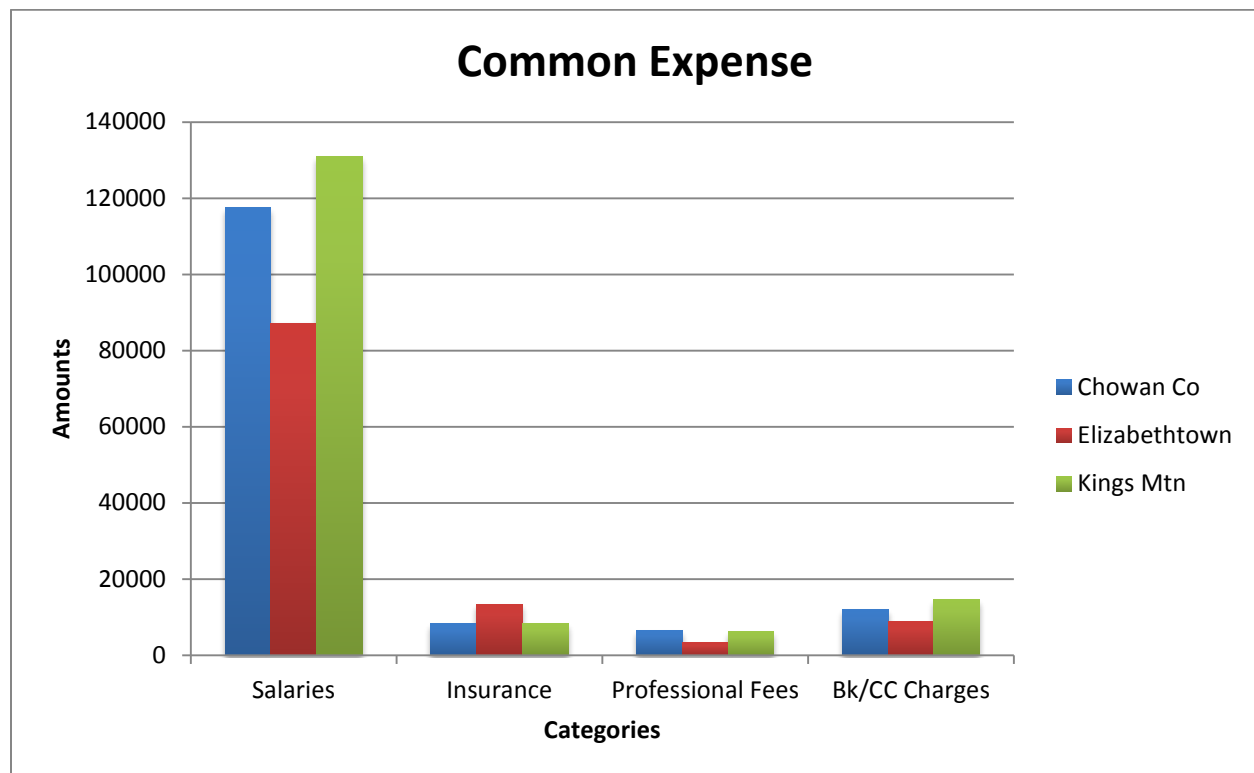
OPERATING COST RATIO

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 Chowan County ABC Board operates one retail store with mixed beverage sales: the operating cost ratio is 0.76. Mixed beverage sales make up 4.4% of total gross sales. In fiscal year 2014, sales increased 4.5% over fiscal year 2013, while expenses decreased 7.5% over the same time period.

A common expense analysis shows that Chowan County ABC Board expenses compared to other similar size boards are not out of line. Note: Insurance expense for Elizabethtown includes health insurance. Salaries are determined by the number of full-time and part-time employees for each board and longevity. Chowan County has two full-time and four part-time employees. Elizabethtown has three full-time and three part-time employees. Kings Mountain has two full-time and four part-time employees.



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 Chowan County ABC Board receives deliveries two times a month: the inventory turnover rate is 5.0. The average inventory turnover rate for similar boards with the same delivery schedule is 5.6.

RECOMMENDATIONS

1. Consider the following to increase inventory turns:
 - Incorporating a shelf management plan that analyzes sales data to targeted shopping patterns;
 - Utilizing end caps and empty shelf space as much as possible to highlight slow moving and new products;
 - Moving stock within the store to increase visibility and to encourage more impulse shopping;
 - Splitting cases with other boards or taking advantage of the Special Purchase Allowance and the Boutique collections to increase variety;
 - Eliminating poor performing items to drive category sales and increase shopper satisfaction;

STORE APPEARANCE AND CUSTOMER SERVICE

The Chowan County ABC Board operates one retail store with approximately 1,000 linear feet of shelf space and carries approximately 1,200 product codes.

- The store appeared clean and free of trash. Counter areas were neat making supplies easily accessible to staff.
- Exterior signage and landscaping around the store was well-manicured and neat. Interior signage was neat and visible. The Fetal Alcohol Syndrome poster was displayed.
- Security systems are in place and functional in all designated areas.
- A basic shelf management plan is utilized/in use that exhibits a strategy following the highest priced product on the top shelves and lowest priced product on the bottom shelves. Product placement is consistent with sizes going from largest on the right and smallest to the left.
- 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. Monthly sales information is shared with mixed beverage and retail customers on a consistent basis.
- Sales clerk's interaction with customers is attentive, courteous, and all are eager to meet the needs of customers.

RECOMMENDATIONS

1. Consider developing a strategy for product placement utilizing up-to-date marketing and industry standards. An efficient shelf management plan focuses on the growing market. Consider the following practices:
 - Brand blocking products with higher priced at eye level, premium products on top shelves, and value priced items on lower shelves;
 - Cross-merchandising by placing products that mix together on the same shelves. Intermingle North Carolina products within their specific category as well as having a designated area;
 - Reallocating shelf space from declining categories to those showing growth;
 - Optimizing the floor space and end caps to incorporate valuable displays;
 - Allowing more space for your more popular brands and re-allocating space when eliminating underperforming brands.

PERSONNEL AND TRAINING

- Two out of three board members, general manager, and the finance officer have completed the initial ethics training. One board member has since been appointed to the board and has not completed the ethics training.
- Cross training opportunities have been extended to key employees in the event the general manager is suddenly unavailable. The general manager has recently been hired and is undergoing training by the previous general manager who now serves as the finance officer.
- As new information comes available, training is provided to new and existing staff on key areas, such as product knowledge, customer service, and clerk responsibilities on a continual basis.
- Personnel files are available and contained human resource documentation and other personnel information as needed.

RECOMMENDATIONS

1. Consider additional training opportunities through the Commission and the ABC Officers Association on specific areas. The Commission offers Responsible Alcohol Sellers Program, RASP, training for ABC boards and mixed beverage permit holders.
2. Board members are required by statute to receive a minimum of two hours of ethics education within twelve months after initial appointment. *Refer to Appendix B (1) for statute.*

ABC BOARD POLICIES

- Policies adopted and submitted to the Commission include:
 - Code of Ethics
 - Law Enforcement Contract
 - Travel Policy (County approval submitted for FY2015)
 - Employee Handbook
 - FY2015 Budget (Proposed and Adopted)
 - FY2014 Annual Audit
 - Mixed Beverage Policy

- Policies not adopted include:
 - Price Discrepancy Policy

RECOMMENDATIONS

1. Adopt a price discrepancy policy that incorporates customer friendly practices. Once adopted, communicate to all employees should the need arise. *Refer to Appendix B (2) for rule.*

INTERNAL CONTROL PROCEDURES

- The general manager schedules all employees for work shift hours. Time cards are used by all clerks. During payroll processing, the general manager will verify time cards and enter all employee hours worked into the accounting/payroll software for processing.
- Cash drawers are counted by all clerks. All clerks are responsible for their own cash drawer. Management has implemented procedures on handling cash drawer overages/shortages.
- Bank deposits are made regularly as required by the ABC Commission rule. Bank notifications are received and matched with corresponding daily register reports. Bank reconciliations are completed by the general manager/finance officer.
- Physical inventory counts are completed quarterly by whoever is scheduled to work. Once the initial count is completed, management reviews and investigates variances. Once variances are checked and verified, management will adjust the inventory management system for the exact inventory held in the store. Breakage adjustments are included in this process.
- Credit cards are issued to the board with the general manager and other board members as users. The chairman views and reconciles all transactions purchased with the card. A credit card policy has not been implemented.
- Out of approximately 1,200 product codes, approximately 80 codes were sampled to ensure accurate pricing and one was incorrect.

RECOMMENDATIONS

1. To ensure correct pricing on the store shelves and in the computer system, audit shelf tags on a regular basis by incorporating this practice during or in between the regularly scheduled inventory counts.
2. To ensure strong internal controls for credit card purchases, adopt a written credit card usage policy. Document procedures for the usage including:
 - Who has authority to use the card,
 - What types of items the card may be used for,
 - Personal usage is prohibited;
 - An itemized receipt for every transaction is required,
 - Maximum limit allowed on purchases before approval is needed from the finance officer,
 - Receipts are to be submitted within 15 days of the purchase;
 - Have someone other than the persons authorized to make purchases reconcile the credit card statements.

ADMINISTRATIVE COMPLIANCE FINDINGS AND OBSERVATIONS

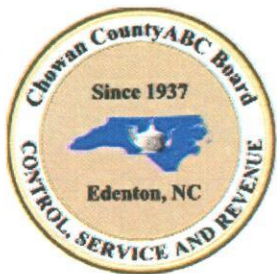
- Board meeting minutes were viewed and followed the order of proceedings, providing sufficient detail that a reasonable person would be able to follow what transpired. Board meeting minutes included a conflict of interest statement asking board members if conflicts existed with items on the meeting agenda.
- Board member appointment dates and general manager compensation is current on the Commission website.
- 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).
- The board is in compliance with G.S. 18B-700 (k); there are no immediate family members employed related to board members or the general manager.
- All board members, the general manager, and the finance officer are bonded for \$50,000.
- Orders for liquor and other miscellaneous orders do not bear the pre-audit certificate as required by G.S. 18B-702 (m).
- The board pays all bills using an Automated BillPay system with the bank. All documentation is verified by the general manager and signed by the finance officer.

RECOMMENDATIONS

1. 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 (3) for statute.*

AUDITOR'S SUMMARY

ABC Board Auditor, Moniqua S. McLean, presented the performance audit recommendations on October 13, 2014. The board has since responded to the performance audit recommendations and continues to implement strategies to maintain profitability while maintaining and reducing current costs and meeting budget appropriations. 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.



Chowan County Alcoholic Beverage Control Board
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Moniqua McLean
ABC Board Auditor
4307 Mail Services Center
Raleigh, NC 27699-4307

Ms. McLean,

The Board and Management team wishes to thank you for your help and input as to the recommendations produced by the performance audit. We have implemented them and will continue to monitor and enhance those areas. We are striving to improve our financial position and have done so with regard to working capital requirements and improving sales thru closer scrutiny of our inventory turn over. Improving on our shelf management and minimizing poorly performing products will be an ongoing part of our training routines.

Once again, Thank you for your time and efforts to help us improve and move forward.

With Regards,

Lewis Waters
General Manager

A handwritten signature in black ink that reads "Lewis Waters".

Michael Brown
Finance Officer

A handwritten signature in black ink that reads "Michael Brown".

APPENDIX A

Illustration 1



Exterior view

Illustration 2



Shelf management view

Illustration 3



Interior view

APPENDIX B

- (1) *G.S. 18B-706 (b) states, "Each member of a local board shall receive a minimum of two hours of ethics education within 12 months after initial appointment to the office and again within 12 months after each subsequent appointment to the office."*
- (2) *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."*
- (3) *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 | REQUIRED BY STATUTE | IMPLEMENTATION STATUS |
|---|--|--|
| <p>ABC Board Policies:</p> <p>Adopt the following policies and forward to the Commission:</p> <ul style="list-style-type: none"> • **Price Discrepancy Policy • Credit Card Usage Policy | <p><input checked="" type="checkbox"/> Yes</p> <p><input type="checkbox"/> No</p> <p>**Note: Required by Commission 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 copies have been submitted to the Commission.</p> |
| <p>Administrative Compliance: Affix the pre-audit certificate on orders before the transaction occurs.</p> | <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 implemented procedures to incorporate this practice.</p> |