

Johnston County ABC Board

Performance Audit Report



Alcoholic Beverage Control Commission
400 East Tryon Road, Raleigh, NC 27610
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ABC
COMMISSION
NORTH CAROLINA

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ABC

COMMISSION
NORTH CAROLINA

Alcoholic Beverage Control

CHAIRMAN:

A. D. "Zander" Guy, Jr.

September 9, 2020

COMMISSIONERS:

Norman A. Mitchell, Sr.
Charlotte

Karen L. Stout
Black Mountain

Steve Upton,
Chairman,
Johnston County ABC Board
P.O. Box 909
Smithfield, NC 237577

ADMINISTRATOR:

Agnes Stevens

Dear Chairman Upton,

LOCATION:

400 East Tryon Road
Raleigh NC 27610

On the following pages you will find the performance audit report conducted by the staff of the ABC Commission reviewing the operations of the Johnston County ABC Board.

MAILING:

4307 Mail Service Center
Raleigh NC 27699-4307

The report consists of an executive summary, an overview of the objective, purpose and scope, and a digest of your board's performance standards and related findings. Included in the findings are recommendations for action on the part of your board.

PHONE: (919) 779-0700

<http://abc.nc.gov/>

I encourage you to review the report and let me know if you have any questions or require assistance in implementing any of the recommendations.

On behalf of the NC ABC Commission, I thank you and your staff for your assistance and cooperation in conducting this review and in implementing the changes that will reduce expenses and increase profitability of your board.

Sincerely,

Agnes Stevens
Administrator

cc: NC Association of ABC Boards
Ted G. Godwin, Chairman Johnston County Board of Commissioners,
Swade Carroll, General Manager, Johnston County ABC Board

OBJECTIVE, PURPOSE AND SCOPE

In addition to regular and special financial audits, G.S. 18B-705(a) authorizes the NC ABC Commission to conduct performance audits of all local ABC boards in the state. Performance audits are examinations of existing operating policies, practices, controls, and activities to determine those areas in which there may be a need for improvement.

The audits are designed to ensure that all local ABC Boards comply with established performance standards pursuant to G.S. 18B-203(a)(20). The audit's scope addresses compliance with ABC laws and rules, store appearance, operating efficiency, solvency and customer service.

To achieve the objectives of the audit, auditors:

- Review applicable General Statutes, ABC Commission Rules, and Administrative Policies
- Review applicable reports and studies of ABC Boards with similar size and geography
- Verify compliance with Commission and Board policies
- Verify results of previous performance audit recommendations
- Review ABC Board annual independent financial audits
- Review ABC Board reporting and documentation reports
- Visit the store(s)
- Interview key ABC Board personnel

The initial round of performance audits for the local ABC Boards concluded in 2016 and provided a comprehensive overview of the operations of the local boards. The Johnston County ABC Board had its last performance audit back in 2012. This follow-up round of performance audits is a continuous way to provide local boards with information and best practices that target areas for improvement. Board activities that meet or exceed current performance standards are internally noted during audits but are not included in the attached summary report to focus on required or recommended corrective actions.

PERFORMANCE STANDARDS AND FINDINGS: PROFIT PERCENTAGE TO SALES AND OPERATING COST RATIO

In FY2018-2019, the Johnston County ABC Board had a profit percentage to sales of 9.6%. The NC ABC Commission profit to sales standards for ABC Boards with gross sales greater than \$10M is 9%. The Johnston County ABC Board's gross sales totaled \$18,193,694, a 12.9% increase over FY17-18.

The operating cost ratio for the Johnston County ABC Board was .54 in FY2018-2019. The NC ABC Commission standard for ABC Boards with 3 or more stores and mixed beverage sales is .63 or less. The Johnston County ABC Board met this Commission standard.

Thus, the Johnston County ABC Board met the profitability and operating cost standards set by the NC ABC Commission. Below is a chart showing expenses and income from operations for the previous two years.

	FY2019	FY2018
Expenses excluding Depreciation	\$2,436,472	\$1,987,408
Income from Operations	\$1,890,103	\$1,799,105

Factors affecting profitability and cost include:

- The ABC Board currently leases 4 of its 9 stores which increases overhead expenses
- An ABC Board's average cost of goods sold is between 52% & 54% per year. The Johnston County ABC Board's cost of goods sold was approximately 52.37% in FY19
- Mixed beverage sales total approximately 9.17% in FY19

BUDGET ANALYSIS

	FY2019 Budget Projections	FY2019 Actual	Variance	Variance %
Sales	\$17,545,329	\$18,193,694	\$126,688	0.007%
Total Operating Expenses Including Capital Outlay	\$15,806,954	\$16,501,528	\$119,521	0.007%

In reviewing the budget to actual analysis of the FY2019 financial audit, sales revenues exceeded the budgeted projections by 0.007%. Total operating expenses were within budget for the same period. The chart above shows the final budget to actual amounts and the variances.

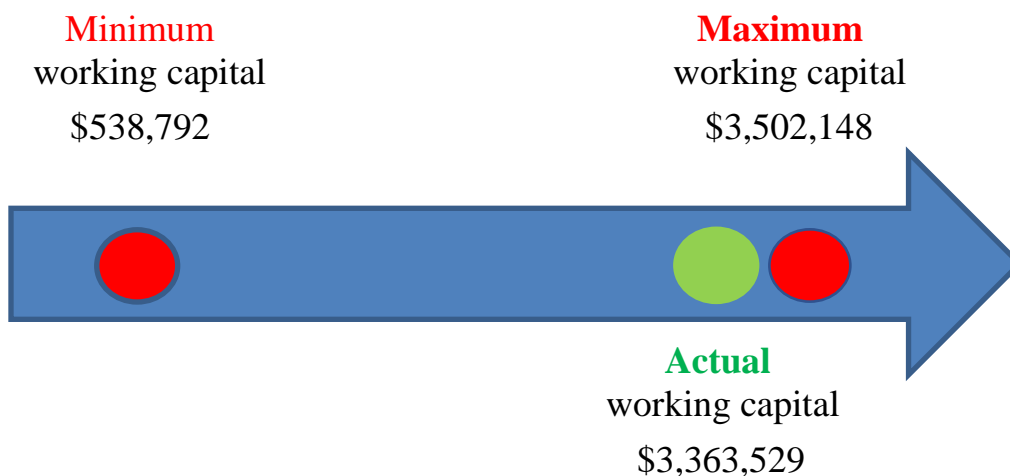
Note: In reviewing the budget to actual analysis of the FY2020 year to date budget, sales revenues are projected to exceed the budgeted projections by 12.84% or \$2,475,922. The Johnston County ABC Board is projected to reach or exceed \$21,747,202 in sales for FY20.

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. The NC ABC Commission has set a working capital standard for boards with gross sales greater than \$1.5M but less than \$50M an amount equal to 3 months of sales revenue.

Based upon the existing rules, as of June 30, 2019, the Johnston County ABC Board is required to maintain a minimum working capital of \$538,792 with a maximum working capital amount of \$3,502,148. The Johnston County ABC Board currently has a working capital balance of \$3,363,529 which falls within the Commission requirements for this section*.

FY19 -



*It is projected that at the end of FY20 the Johnston County ABC Board, especially considering the increased sales volume due to the pandemic, will exceed their statutory working capital maximum by \$400,173 and will need to make additional distributions.

Under 18B-805(d), with approval of the appointing authority for the board, the local board may also set aside a portion of the remaining gross receipts as a fund for specific capital improvements.

RECOMMENDATION #1:

- 1. That the local board consider setting aside a portion of their remaining gross receipts as a fund for the following capital improvements**
 - a. Set aside funding for the new store construction and upfit expenses (US40/42)**
 - b. Set aside funding to update, renovate and equip the current warehouses to accommodate a pallet system, converting to an automated electronic receiving and shipping system that includes scanning guns and utilizing the pallet system which will create more useable warehouse space resulting in the ability to take advantage of SPA's more often.**

CORRECTIVE ACTION TAKEN: *Management has initiated a new account for the new construction project. However, there is not a clear indication the board received approval from its appointing authority for retaining the excess working capital funds. As stated above, “the board shall receive approval from the appointing authority to set aside a portion of the remaining gross receipts for a specific capital improvement purpose.” Once approval is received, copy of the written approval shall be forwarded to the ABC Commission.*

STORE APPEARANCE

The findings for store appearance(s) are as follows:

- All 9 stores displayed the required Fetal Alcohol Syndrome poster required by G.S. 18B-808.
- North Carolina products have their own section as required by law but are also cross merchandised according to product category. Green North Carolina product tags are displayed on the shelves throughout the stores to help stimulate sales.
- Products are placed within the designated categories; premium products are found at eye-level or top shelf.
- All stores clerks were extremely professional and friendly. While observing the clerks interacting with the general public, they not only exhibited a high-level customer service excellence but a genuine friendly and helpful attitude during the encounters that I witnessed.

RECOMMENDATION #1:

1. **Maintain a consistent size flow displaying a pattern from smaller size on the left to the larger sizes on the right**
2. **Maximize store display management and ensure that proper vender products are not placed on competitor's displays**
3. **Maintain fronting practices throughout all 9 stores**
4. **Incorporate multilayered ordering and review process from store Managers, to Warehouse Manager to General Manager to maximize product availability and minimize dead/empty shelf space**
5. **Incorporate uniform practices and equipment related to table tents and out of stock signs in all nine stores**
6. **Consider utilizing resources that would create a shelf management system that is conducive to industry norms which consider sales history and trends.**

CORRECTIVE ACTION: *Management will explore alternative methods of resetting shelves that follow industry standards. With the current industry trends, effective shelf management and product placement has proven to increase sales and profits.*

OPERATIONAL AND ADMINISTRATIVE COMPLIANCE

While inspecting the stores, a random sample of 65 items was selected to determine if uniform pricing is displayed. Of those selected, 3 items were incorrect. All three items have since been corrected.

REQUIRED ACTION #1: Make corrective changes to price discrepancies noted and verify same for the other store locations. Conduct routine checks of shelf prices along with the register to ensure accuracy. All prices must match what is in the register, the shelf, and in the NC Liquor Quarterly, and/or memorandums. To further strengthen these controls, perform spot checks at random times for inventory control and price management. Refer to the ABC Commission's website to verify product pricing.

CORRECTIVE ACTION TAKEN: *Since the audit fieldwork in mid-June 2020, the price discrepancies at the specific stores have been corrected and the General Manager has taken steps to ensure that all 9 stores are in compliance with the pricing system.*

Nepotism - G.S. 18B-700(k) requires that the board does not employ members of immediate family members of the General Manager and/or Board Members.

- Upon inspection it was determined that the Board is not in compliance with this statute by which a sister of a current Board Member is employed by the Johnston County ABC Board.

REQUIRED ACTION #2: Immediately submit a waiver/exemption request to the NC ABC Commission for their review related to the nepotism issue noted above.

CORRECTIVE ACTION TAKEN: *Since the audit fieldwork in mid-June 2020, the Johnston County ABC Board submitted their exemption request and the Chairman granted approval for the exemption request. The Board is to be respectfully reminded that time is of the essence for any future occasion where this statute may apply and per North Carolina General Statute, any such request shall be made prior to employment.*

The employee manual was last updated in 2018 and reflects a vast majority of topics and information pertaining to the current practices of the board. Specific revisions relating to credit card usage and the use of Board vehicles have not been amended to cover current operating practices. A store tasting policy needs to be adopted and added to the employee manual.

REQUIRED ACTION #3: As a reminder, submit policies to the NC ABC Commission prior to adoption. NCAC 15A .1102 states, "A copy of all rules or amendments thereto that may be adopted by a local board to govern the operation of ABC stores or the enforcement of the ABC laws shall be submitted to the Commission at least 15 days prior to the date on which it is proposed that those rules or amendments are to become effective."

OPERATIONAL AND ADMINISTRATIVE COMPLIANCE CONTINUED

CORRECTIVE ACTION TAKEN: Management and the board are currently updating the employee manual to reflect current practices and laws. Once completed, the board will submit to the NC ABC Commission for review.

ABC Boards are required to remit distiller payments within thirty (30) days of receiving the product. Supplier accounts receivable departments occasionally notify NC ABC Commission staff of past due invoices for ABC Boards. The NC ABC Commission has received notifications regarding late payments specifically by the Johnston County ABC Board. These notifications are forwarded to the General Manager and in turn to the Finance Officer. The current process for disbursements is as follows:

- a. The general manager receives invoices electronically from the warehouse vendor, LB&B
- b. Invoices are printed and forwarded to the finance officer
- c. The finance officer updates the accounting records and processes invoices for payments.

Oftentimes, invoices have been paid by check and mailed approximately 3 days prior to their due date. This has caused a delay in the distiller receiving remittance within the statutory requirement of 30 days.

STRONGLY RECOMMENDED: To ensure that invoice payments are received by the vendors within the thirty (30) day statutory requirement, continue to move forward with your electronic payment system transition in order to include distilleries in your new bill pay system. Bills paid via the US Post Office should be mailed with enough time for the vendor to receive payment on or before the due date.

CORRECTIVE ACTION TAKEN: Management has implemented procedures to ensure the invoice payments are received by vendors within the thirty-day threshold.

WAREHOUSE AND ADMINISTRATIVE COMPLIANCE/OPERATIONS

During the audit, several areas related to ordering, receiving and distribution of inventory procedures and efficiency were discussed. The NC ABC Board has received several concerns from customers related to the lack of inventory on the shelves for retail or MB sales. This same concern was notated during the Auditor's field visits to several stores throughout the county. Although these concerns occurred during the Covid-19 pandemic spike in sales and with some small distiller shortages at the warehouse, not all the vacant shelf space can be attributed to these factors. Since the pandemic is reaching its six-month mark, adjustments to ordering could have been made to minimize this issue.

The current ordering process entails each store manager ordering for his/her store. This order is then sent to the board's Warehouse Manager who reviews the order and makes any known adjustments. These orders may be reviewed by the General Manager as well. Any cuts in stock during delivery from LB&B must be manually notated and there is currently no electronic back order system in place at the board level. The store managers do not know about the cut(s) in their order/stock until the arrival date. It then becomes incumbent on the Store Manager, the Warehouse Manager and ultimately on the General Manager to manually keep up with any decreased inventory orders on a weekly basis. The manual accounting process has led to a two-prong problem. The first problem that is a compounding problem relates to the consistent decrease in product inventory available to be placed on the shelf for sale which then creates unpredictable purchase of other products in an amount not normally ordered during the regular ordering or forecasted ordering requests. At best, this has contributed to lost sales, less customer satisfaction, and continued dwindling stock.

ADDITIONAL FACTORS FOR CONSIDERATION:

Johnston County ABC Board

- Is 15th out of 169 local ABC Boards in liquor sales for North Carolina (June 2020)
- 2019 population was 209,339
- Expecting a 28% growth rate in next 10 years
- Adjacent to the Research Triangle Park (30-minute commute)
- 796 square miles to service, averages 88.44 square miles per store
- As of beginning of June 2020, 15th largest ABC Board in sales

RECOMMENDATIONS FOR INDUSTRY BEST PRACTICES:

- 1. Utilization of Bulletin Board for acquisition and distribution of needed stock, reducing dead stock, and assisting in MB orders**
- 2. Holding monthly group meetings with all store managers to discuss current trends, issues and relay best practices to assist in uniformity of service throughout the Board**
 - a. Meetings will also enable transfer of product**
- 3. Updating warehouse system**
 - a. Need more warehouse space to incorporate pallet delivery/shipping system**
 - i. Pallet system decreases labor costs which pays for itself over time**

WAREHOUSE AND ADMINISTRATIVE COMPLIANCE/OPERATIONS

- ii. Current practice is to manually unload and load liquor shipments twice a week at the board's warehouse.
- iii. Warehouse deliveries currently monopolize 40% of warehouse manager's weekly time solely related to the manual labor associated with unloading and loading trucks.
 - 1. Current process using manual ordering and manual checkoff system
- iv. No board level back-order system for local stores
- v. Pallet lift system or walkie rider pallet system are a fraction of the cost of traditional fork lifts and require less operating space
 - 2. Pallet lift systems would be able to operate in current warehouse space
- b. Current system does not allow General Manager to take advantage of SPA's (Special Pricing Adjustments) which significantly decreases profitability opportunities
- c. Per Warehouse Manager, there is a current and future need for electronic inventory scanners
- d. Observed need for electronic receiving/shipping/backorder system
 - i. Currently operations use manual counts for inventory deliveries
- e. Current practice incurs increased labor expenses
 - i. Currently Warehouse Manager and 6-part time employees physically unload approximately 2,900 cases of liquor a week (approx. 98,600lbs)
 - 1. Increased risk of injuries
 - 2. Increased risk of damage/breakage
 - 3. Increased labor expenses; 6-part time employees x 10 hours x \$10 per hour x 2 days a week x 52 week per year creates a labor cost of **\$62,400 yearly**

**JOHNSTON COUNTY
BOARD OF ALCOHOLIC CONTROL**
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SMITHFIELD, NORTH CAROLINA 27577
(919) 934-7249 Ph. - Fax (919) 934-3324
jcabc@earthlink.net

To: Laurie Lee
Moniqua McLean

July 14, 2020

Subject: ABC Board Performance Audit Response

This is in response to the Johnston County ABC Board Performance Audit conducted June 15&16, 2020 by Craig Haines and Moniqua McLean. All responses will be in the form of attachments. We thank you for the opportunity to help the Johnston County ABC Board's quest for excellent customer service.

Sincerely,



Swade W. Carroll
General Manager

Johnston County ABC Board Response to June 2020 Audit

1. Working Capital-Recommendation #1
 - We will create an account to help fund the new store construction at I40/42. The Johnston County ABC Board has diligently been saving money over the last 12 months to fund lot purchase and reduce amount of loan for the building.
 - We will work with Steve Gaskins Consulting to convert receiving to utilize a scanning gun. We have already purchased an electric pallet jack to facilitate receiving pallet trucks.
 - We still have to remove items from the current warehouse in order to the room for pallet deliveries.

2. Store Appearance-Recommendation #1
 - We will look at resetting our shelves smaller size to larger size. This is not our preferred set but will look at industry standards for shelf management.
 - We already have three levels in the ordering process.

3. Operational and Administrative Compliance
 - We do not have a response to required actions 1-3 since corrective actions have already been taken.
 - Policies for vehicle usage, credit card usage and in-store tasting policy are attached.
 - Regarding invoices, as noted we are transitioning to an electronic payment system. We will mail payments earlier than the thirty-day limit to ensure receipt by vendor on a timely basis.

4. Warehouse and Administrative Compliance/Operations
 - The Johnston County ABC Board does acknowledge we have had stocking issues at several stores. Several factors are at work here. We need to have more deliveries by LB&B (if any trucks are available). We can pick up product at LB&B but new rules limit us to five pick-ups per year, and outages at LB&B have been incredible. Distillers are not stocking the warehouse as needed. Bottom line is we will do better at stocking our stores.
 - We will utilize the Bulletin Board more. Dead stock is usually reduced in price.
 - We will have monthly meetings between General Manager, Warehouse Manager and all Store Managers.

Johnston County ABC Board Response to June 2020 Audit

4. Warehouse and Administrative Compliance/Operations (Cont.)

- We already have an off-site warehouse of approximately 3500 square feet but have not utilized it to its full capacity.
- We are transitioning our warehouse at 417 S. Brightleaf Blvd., Smithfield to receive pallet loads. Loads still have to be loaded manually.
- Our back-order system is to either reorder cuts on the next truck, pull from either of our warehouses or transfer between stores.
- I disagree the current system does not allow General Manager to take advantage of SPA's. The system is there but we have to better utilize the space already available.
- Again, we will look into scanners to receive our warehouse deliveries.