

Youngsville 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

June 10, 2014

CHAIRMAN:
JAMES C. GARDNER

Youngsville ABC Board
Mr. Jim Underwood, Chairman
PO Box 387
Youngsville, NC 27596

COMMISSIONERS:
JOEL L. KEITH
Wake Forest

KEVIN M. GREEN
Greensboro

Dear Chairman Underwood,

ADMINISTRATOR:
MICHAEL C. HERRING

We are pleased to submit this performance audit report on the Youngsville 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.

LOCATION:
400 East Tryon Road
Raleigh NC 27610

The report consists of an executive summary, background information, operational findings and recommendations. This report will be posted on the Commission's public web site.

MAILING:
4307 Mail Service Center
Raleigh, NC 27699-4307

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 anticipate you implementing the recommendations outlined in the report to hopefully improve operations and increase efficiencies.

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Moniqua S. McLean
ABC Board Auditor

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 2012;
- Visited the store;
- Interviewed key ABC board personnel.

BACKGROUND INFORMATION

Chapter 328 of the 1971 Session Law authorized the town of Youngsville to hold an election for an ABC store upon a petition of at least fifteen percent (15%) of registered voters. The referendum was held on June 15, 1971 and passed 104 to 80. The first retail sale occurred on August 2, 1971.

Upon election of an ABC store, the town of Youngsville was authorized to create an ABC Board consisting of a chairman and two members. Current board members are Jim Underwood, board chairman, Linda Lemar and Robert Bridges, Jr, board members.

The Youngsville ABC Board operates one retail store. The board staffs three employees consisting of one full-time general manager and two part-time clerks. The general manager is responsible for the overall operations of the store including providing friendly customer service, maintaining sufficient inventory, supervision of personnel, and store upkeep. The board has hired the town's finance officer to handle financial duties as required. Clerks are primarily responsible for providing friendly customer service and stock maintenance.

OPERATIONAL OBSERVATIONS, FINDINGS, AND RECOMMENDATIONS

On May 23, 2013, ABC Board Auditor, Moniqua S. McLean, visited the Youngsville ABC store and interviewed Laurie Leedy, general manager, and Bill Tatum, finance officer. The following are the findings, observations, 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 2012, the Youngsville ABC Board had gross sales of \$768,419; income from operations was 37,381, a 4.86% profit percentage to sales.

Factors affecting sales and profitability:

- US Census Bureau reports an estimated population of 1,157 in 2010;
- Surrounding towns with ABC stores include Louisburg, Bunn, and Franklinton;
- Sales increased 1.07% over previous fiscal year;
- Growth and development in surrounding, more heavily populated areas has led to a shift in shopping patterns away from small towns.

RECOMMENDATIONS

1. Refer to recommendations under store appearance for methods that will increase profitability.

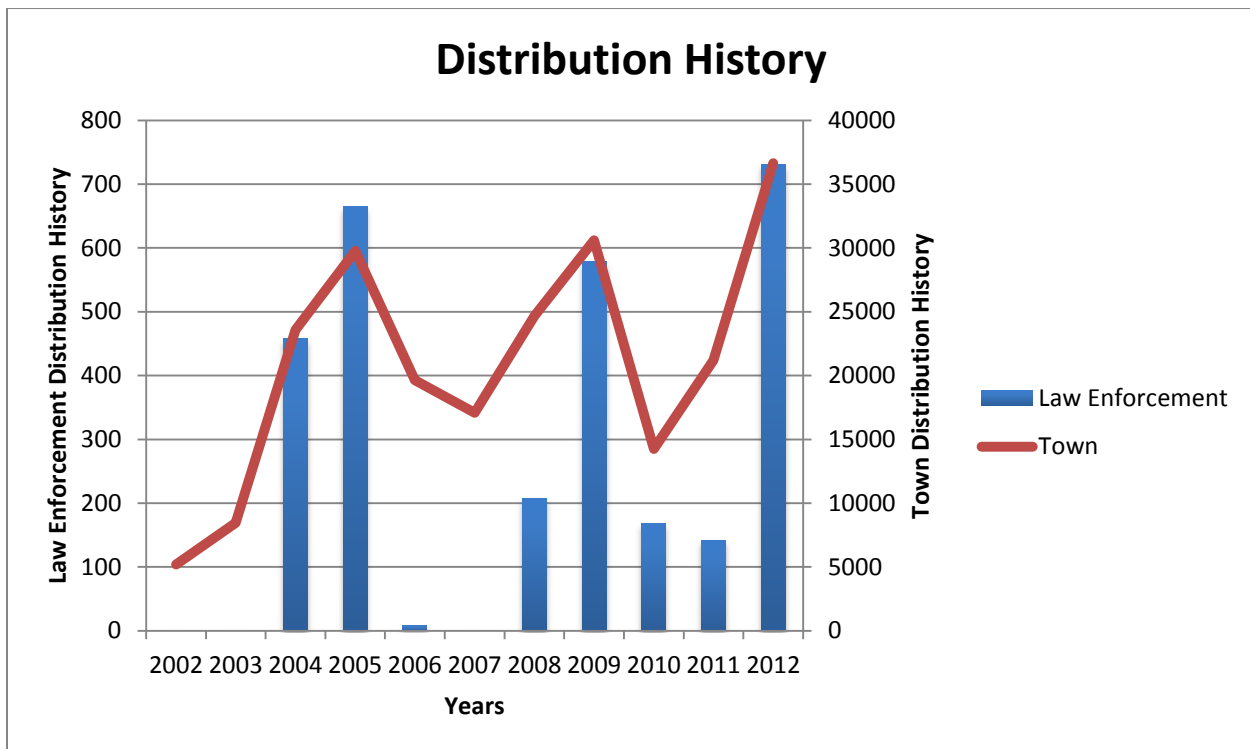
DISTRIBUTIONS

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 3 ½% markup rate to the appointing authority. In FY2012, Youngsville ABC made the minimum distribution to the town totaling \$22,794, plus additional distribution of \$36,651. \$173,219 in excise and other taxes were paid to the NC Department of Revenue, the Department of Health and Human Services, and the town.

G.S. 18B-805 (c)(2) and (3) requires the board to distribute at least five percent of profits to law enforcement and at least seven percent (7%) for alcohol education. Alcohol education distributions are not required by the board's enabling act. The remaining profits are to be distributed to the Town of Youngsville General Fund.

In FY2012, Youngsville ABC distributed to the town \$730 toward law enforcement

Below is a distribution chart analyzing the high-low trend of the Youngsville ABC Board for the past ten years.



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 FY2012, Youngsville ABC had a working capital of \$33,617 which is equivalent to less than four months gross sales and is within the limits of NCAC 02R .0902.

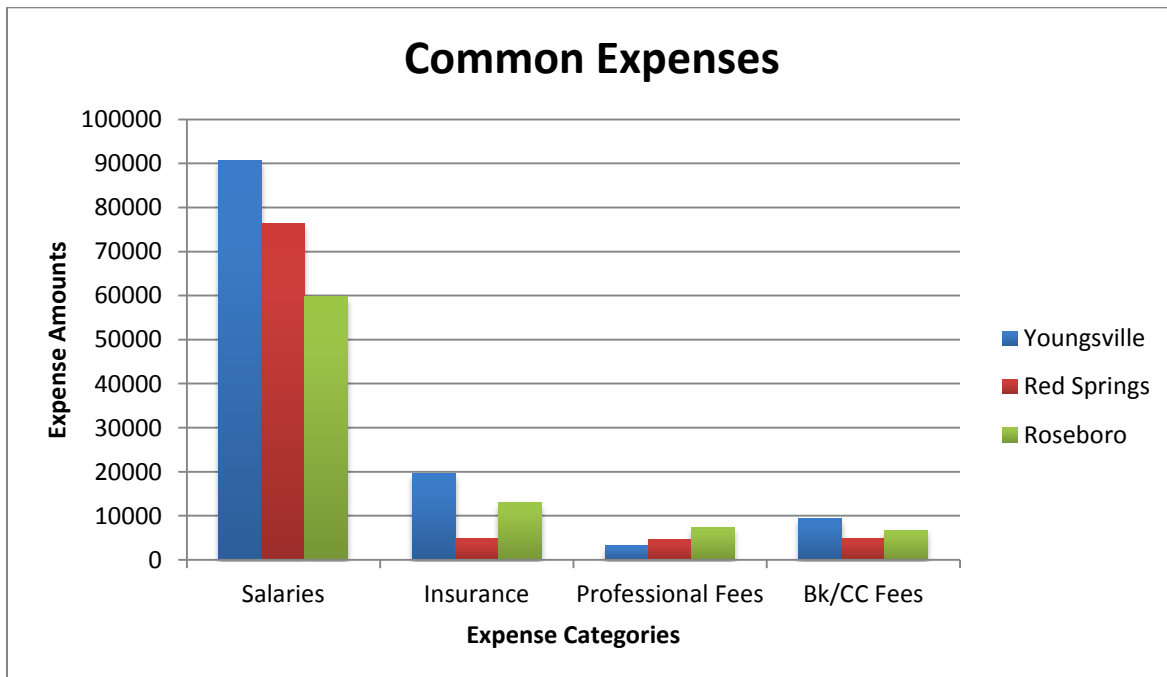
OPERATING COST RATIO

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 Youngsville ABC Board operates one retail store without mixed beverage sales; the operating cost ratio is 0.78. In fiscal year 2012, sales increased 1.08% over fiscal year 2011 while overall expenses decreased 7.61% over the same time period. The board contributes to significant savings in overhead expenses as a result of owning the store.

A common expense analysis indicates that expenses are relatively higher than that of other boards. However, salaries have decreased 4.2% since FY2011 and bank/credit card fees increased due to increase credit card transactions. Note: Insurance expenses include all insurance.



RECOMMENDATIONS

1. Closely monitor monthly overhead and business expenses. Request bids from vendors to ensure that the best price is offered for services provided, such as insurance, professional fees, some utilities, and bank/credit card charges.

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 Youngsville ABC Board receives deliveries twice a month: the inventory turnover rate is 6.8. The average inventory turnover rate for similar boards with the same delivery schedule is 5.6

NO RECOMMENDATIONS

STORE APPEARANCE AND CUSTOMER SERVICE OBSERVATIONS

The Youngsville ABC Board operates one retail store with shelf space of approximately 500 linear feet and carries approximately 700 product codes. *Refer to pictures in Appendix B.*

- Although dated, the store was clean and well-lit. Bottles were fronted and dusted. Counter areas were free of clutter and supplies were easily accessible.
- Recent improvements have been made to the parking area and to the interior, the lighting has been replaced and the store has been repainted.
- Exterior signage and landscaping around the store was clean and free of trash. The Fetal Alcohol Syndrome poster is displayed.
- Current product placement generally follows the highest priced premium product on the top shelves and lowest priced or valued product on the bottom shelves. Product displays are used where space permits and exhibit a variety of bestselling products. *Refer to pictures on page 12.*
- Security systems are in place and functional.
- The state price book is available along with monthly sales lists.
- Sales clerks' interaction with customers was attentive, courteous, and eager to meet the needs of customers.

RECOMMENDATIONS

1. Consider modernizing the store to increase shelf space and encourage impulse shopping and will in turn increase profitability;
2. Consider developing a strategy for product placement utilizing the marketing and industry standards. An efficient shelf management plan focuses on the growing market. Recommended practices are as follows:
 - a. Brand blocking products with bottles with mid-price, or premium products, at eye level, high-priced, or ultra-premium products, on top shelves and lower priced, value products, on lower shelves;
 - b. 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;
 - c. Reallocating shelf space from declining categories to those showing growth;
 - d. Allow more space for your more popular brands and re-allocating space when eliminating underperforming brands.
3. Contact other boards and suppliers for additional ideas that may be implemented in areas of shelf management and marketing techniques.

PERSONNEL AND TRAINING

- Two out of the three board members, general manager, and finance officer have attended the initial mandatory ethics class.
- 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 customer service issues, RASP training, and etc.
- Cross training opportunities have not been extended to key employees in the event the general manager was suddenly unavailable. Management has created a training notebook detailing various troubleshooting and end of the month instructions.

RECOMMENDATIONS

1. Bring all board members into compliance with the state ethics requirement. All newly appointed board members must receive ethics education within 12 months of appointment. *Refer to Appendix B (1) for statute.*
2. 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
 - Travel Policy (State Travel Policy)
 - FY2012 Annual Audit
 - FY2013 Budget (Proposed and Adopted)
 - FY2014 Budget (Proposed)

- Policies not adopted and submitted to the Commission include:
 - Law Enforcement Contract
 - Price Discrepancy Policy
 - Employee Handbook

RECOMMENDATIONS

1. Have an agreed upon law enforcement contract and submit to the Commission. All local boards are required to have an agreement, even if the agreement results in no enforcement activity without pay. *Refer to Appendix B (2) for statute.*

2. Adopt a price discrepancy policy that incorporates customer friendly practices. *Refer to Appendix B (3) for rule.*

3. Update employee handbook to reflect current practices and policies expected and outlines the duties and responsibilities of each employee, board policies, and benefits offered, if any. Forward copies to all employees and request a signed acknowledgement of receipt from every employee to be filed in the designated personnel files. Once adopted, submit to the Commission. *Refer Appendix B (4) for rule.*

INTERNAL CONTROLS

- Physical inventory counts are performed monthly by general manager only. Spot checks are conducted often by everyone. If discrepancies occur, the general manager will investigate and recount for accuracy and verification. Once completed, only the general manager will adjust the system to match with the actual store counts. Unsalable items are adjusted immediately.
- Cash drawers are counted by all clerks. All clerks are responsible for their own cash drawer. However, there is no written policy should any cash discrepancies occur. When initiating sales transactions, all clerks utilize one clerk number throughout the day.
- 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 general manager and verified by the finance officer.
- Payroll documentation is completed by the general manager and forwarded to the finance officer for payments. The master payroll activity report is verified by the general manager. Payroll software calculates tax and other withholdings.

RECOMMENDATIONS

1. To strengthen inventory controls, consider implementing procedures that would segregate duties. Physical inventories should be performed by someone other than the person(s) responsible for that inventory on a daily basis. When this is not possible, the physical inventory should be spot-checked by the bookkeeper, a board member, and/or finance officer (someone not handling the inventory daily).
2. Adopt a written cash shortage and overage policy. While this is understood, it is good business practice to have written procedures in place for current and future employees. Once adopted, submit a copy to the Commission and include in the employee personnel manual.
3. To strengthen controls on sales transactions, consider assigning each clerks a unique clerk number so as to have a better documentation on potential unusual transactions.

ADMINISTRATIVE COMPLIANCE FINDINGS AND OBSERVATIONS

- Past board meeting minutes were not available. However, current minutes were viewed, followed the order of proceedings, but did not reference the conflict of interest statement.
- Board member appointment dates and compensation amounts are 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).
- Nepotism – The board is in compliance with G. S. 18B-700 (k).
- Each board member is bonded for \$50,000. However, the general manager and finance officer are not bonded.
- Orders for liquor and other common orders do not bear the pre-audit certificate as required by G.S. 18B-702 (m).
- All checks bear the approved certificate and are signed by the finance officer and the general manager.

RECOMMENDATIONS

1. Have the board chairman read the 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 (5) for rule.*
2. Follow the Records Retention Schedule that explains how long to keep the documentation of board meeting minutes, liquor invoices, etc.
3. Update the bonding insurance to include the general manager and the finance officer as bonded for \$50,000 along with all board members. *Refer to Appendix B (6) for statute.*
4. 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 (7) for statute.*

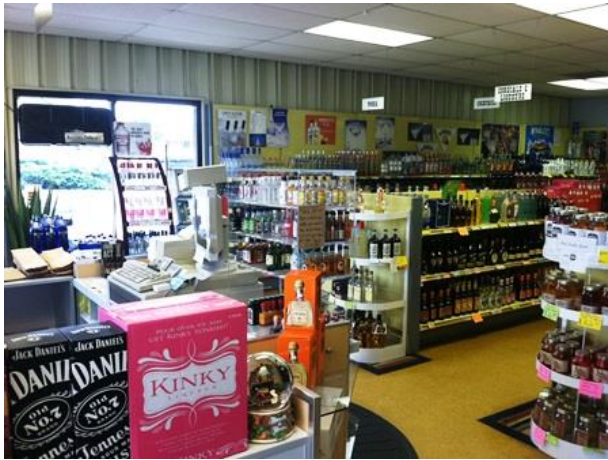
AUDITOR'S SUMMARY

ABC Board Auditor, Moniqua S. McLean, presented to the board the performance audit recommendations on January 15, 2014. However, a response detailing what policies and procedures the board and management have implemented has not been forwarded to the Commission. Therefore, this audit is being submitted without a response from the board. A follow up visit will be scheduled within six months of the final audit submission to determine whether the recommendations have been addressed. The Commission encourages the Youngsville ABC Board to address the areas of improvement noted in the audit in order to fully realize the opportunities for improved performance.

APPENDIX A



Interior view



Interior view with counter view



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) *18B-203 (f) states, "Instead of hiring local ABC officers, a local board may contract to pay its enforcement funds to a sheriff's department, city police department, or other local law enforcement agency for enforcement of the ABC laws within the law enforcement agency's territorial jurisdiction. Enforcement agreements may be made with more than one agency at the same time."*
- (3) *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."*
- (4) *NCAC 02R.1009 (a) states, "Each local board shall establish policies and rules governing each of the following:*
 - (1) Initial employment of employees, including qualifications and requirements for new employees;*
 - (2) Compensation and benefits;*
 - (3) Hours and days of work, holidays, vacation, sick leave and other matters pertaining to the conditions of employment;*
 - (4) Promotion, transfer, demotion and suspension of employees;*
 - (5) Separation or termination of employees;*
 - (6) Granting of salary increases;*
 - (7) Employee grievance procedures; and*
 - (8) Any other programs or procedures as may be necessary to promote efficiency and to provide for a fair and reasonable system of personnel administration.*
- (5) *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.'"
- (6) *G.S. 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 (\$50,000) secured by a corporate surety, for the faithful performance of his duties.*

(7) 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)