Edgecombe Co ABC Board

Performance Audit Report

Alcoholic Beverage Control Commission
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ABC COMMISSION NORTH CAROLINA

Alcoholic Beverage Control

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Chairman, Raleigh

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October 24, 2011

The Honorable Leonard Wiggins, Chairman
Edgecombe Board of County Commissioners
P.O. Box 10
Tarboro, NC 27886

Dear Chairman Wiggins,

We are pleased to submit this performance audit report of the Edgecombe County 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.

This report consists of an executive summary, background information and operational findings and recommendations. The General Manager of the Edgecombe County ABC Board reviewed a draft copy of this report and her written comments are included.

We would like to thank the ABC Board and their staff for the assistance and cooperation provided to us during the audit and we hope you and your County Commissioners will find the report informative.

Respectfully,

Michael C. Herring
Administrator

CC: Lorenzo Carmon, Edgecombe County Manager
Edgecombe County ABC Board

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EXECUTIVE SUMMARY

By state law, the ABC Commission shall ensure that all local ABC Boards comply with established performance standards by conducting regular audits 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 financial audit for the fiscal year 2010;
- Visited the stores;
- Interviewed key ABC store personnel.

The Edgecombe County ABC Board has responded to the performance audit recommendations and has taken steps toward becoming more profitable by minimizing costs. Internal controls have been modified to maintain proper segregation of duties and to adhere to statutes. Due to these efforts, the 2011 financial audit showed a profit of $115,028.

BACKGROUND INFORMATION

Edgecombe County is located in the eastern part of North Carolina. While maintaining its famous charm and hospitality, Edgecombe County is home to historical sites in Tarboro and Town Common. It is home to the city of Rocky Mount which is split between Edgecombe and Nash counties. The current population is approximately 56,552.

Chapter 493 of the 1935 Pasquotank Act authorized Edgecombe County to hold an election. The referendum was held on June 22, 1935. The vote for an ABC store passed 2,845 to 332. The first retail sales date was July 3, 1935.

A mixed beverage election was held for the following:

- Edgecombe County on July 17, 1984 and did not pass,
- Tarboro on June 4, 1985 and passed 1,697 to 1,411, and
- Rocky Mount on May 14, 1985 and passed 6,512 to 5,555.

The Edgecombe County ABC Board operates six retail stores including two mixed beverage locations. The administrative office staffs one full-time and four part-time positions consisting of finance officer, office manager, and two assistants. The general manager is responsible for the efficient operation of all Edgecombe County retail stores and personnel. The finance officer provides the general manager/budget officer with fiscal management, administrative support and assists with the day-to-day operations of the Edgecombe County system. The stores are staffed with seven full-time and fourteen part-time rotating employees.

Profitability

For fiscal year 2010, the board showed a profit; total liquor sales were $3,716,450, profit before distributions was $148,207 resulting in a profit percentage to sales of 3.92%. Sales through May 2011 have dropped from last year. However, current year sales indicate that Edgecombe County is in line with sales of similar size boards. In comparing sales of the past ten years of similar boards, sales for the Edgecombe County board have increased following the state's 56% increase. *See Chart 1 and 2.*

Factors affecting sales and profitability:

- Total population for Edgecombe County has decreased 6% over the past ten years
- Adult working population has decreased 4%
- Poverty levels within the county have increased 19%
- 15.1% unemployment rate in Edgecombe County

Distribution Schedule

G.S. 18B-805 (c) (2) (3) requires that the Board expend quarterly at least 5% of profits for law enforcement. The enabling act requires an annual distribution to Tarboro Public Libraries of $15,000 and an annual $5,000 distribution to Rocky Mount Public Libraries. Of the remaining net profits, twenty-five percent is allocated to the municipalities where stores are located. Six-hundred twenty five dollars ($625) is to be distributed quarterly to the municipalities with the remainder divided proportionately based on profits. Any remaining profits go to the Edgecombe County General Fund.

In 2010, Edgecombe County made distributions to the county totaling $83,107. Law enforcement distributions totaled $20,100. Over the past ten years, distributions have dropped. *See Chart 3.*

FINDINGS AND RECOMMENDATIONS

On June 22, 2011, ABC Commission Auditor, Moniqua S. McLean, visited the Edgecombe County ABC board administrative office and stores, and interviewed Linda Rogers, General Manager, Ronnie Lewis, Office Manager, and Rebecca Webb, Finance Officer. Following are the findings relating to the performance audit:

1. Inventory Turnover

The inventory turnover rate is calculated by dividing the cost of goods sold by the average inventory in the system. The Commission has set goals for determining an effective rate based on the frequency of deliveries. Below are the turnover rates based on a delivery schedule:

- Daily/weekly deliveries target at 6 times per year
- Bi-weekly deliveries target at 5 times per year
- Monthly deliveries target at 4.5 times per year

Edgecombe County ABC has a weekly delivery schedule. The inventory turnover rate for Edgecombe Co ABC Board is 5.7 and does not meet the target rate set by the Commission.

Recommendations:

- Explore different strategies for eliminating slow moving products.
- Ask for price reductions for discontinued products.
- Move stock around within and between stores to increase visibility.
- Monitor store inventories to avoid overstocking.
- Continue to take advantage of SPA's and quarterly price reductions whenever possible.
- Continue the use of recipe cards, displays, and other marketing techniques to increase sales.

2. Operating Costs

Operating costs are calculated by dividing total operating expenses less depreciation by the gross profit on sales. Below are the average cost ratios for boards with and without mixed beverage sales.

- Boards with 3 or more stores with MXB – cost ratio .67 or less
- Boards with 3 or more stores without MXB – cost ratio .94 or less
- Boards with 2 stores – cost ratio .83 or less
- Single store boards with MXB – cost ratio .77 or less
- Single store boards without MXB – cost ratio .93 or less.

The Edgecombe Co ABC board has an operating cost ratio of .80 while the average for similar sized boards is .67. To meet the goal of .67 or less and remain at current revenue levels, operating

expenses must be reduced to less than $600,000. To meet the goal and remain at current operating expenses levels, revenue must be greater than $7 million. *Refer to Charts 4 through 7 for analysis of operating expenses.*

Recommendations:

- Because salaries and benefits are the largest segment of operating expenses, analyze personnel hours to assess efficient personnel usage.

- Request bids annually from various vendors to get the best rates possible on audit, credit card processing fees, and insurance and bonding rates.

- Reduce travel expense by sending just one board member to annual conferences on a rotating basis and having that person report back to board on topics covered; stay at a alternate location where room rates are closer to the state per diem.

- Request reimbursement from NC Association of ABC Boards for travel expenses incurred while attending meetings of the Association's Board of Directors. These expenses should not be paid with public funds.

- OPEB expenses will continue to rise. Discuss long-term expense implication with CPA and if the board has not already done so, consider cancelling this benefit for future employees.

3. <u>Profit percentage to sales</u>

The profit percentage to sales is calculated by dividing the total profit before distributions by gross sales. The Commission has set efficiency 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%

The Edgecombe ABC board has a profit percentage to sales of 3.92% and does not meet the targeted rate set by the Commission.

Recommendations:

- Analyze and reduce operating expenses to increase profits. Refer to above recommendations.

- Increase sales using the strategies recommended under inventory turnover and store appearance.

- Rocky Mount and Tarboro stores generate 78% of the profit. Closely monitor revenue and expenses for Princeville and Macclesfield where the profit margins are extremely low.

4. <u>Working Capital</u>

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:

- 4 months for boards with gross sales less than $1.5M
- 3 months for boards with gross sales less than $50M and greater than or equal to $1.5M
- 2 months for boards with gross sales equal to or greater than $50M

The Edgecombe County ABC board has a working capital of $744,687 and meets the goal set by the Commission.

5. Store Appearance

The linear footage of the Edgecombe County stores range from 1200 to 3700 feet of shelf space. All stores average approximately 763 SKU's. Refer to Appendix A for photos.

- Although all stores were clean, the lighting in Whitfield and Princeville stores was dim.
- The shelf management system is not consistent. Some products are shelved in code number order, other products are displayed left-to-right with largest size on the left and others are right-to-left with largest size on the right. Some products were displayed with all 375ml's on one row, 750ml's on another, and 1.75L bottles on another.
- Shelves were empty giving the appearance that there were not enough products available for sale.
- Some high demand products are given additional facings.

Recommendations:

- Improve the lighting for stores mentioned.

- Develop an effective and efficient shelf-management system that better utilizes the spacing areas. Shelf management needs to be consistent and easily understood. *Refer to Appendix B (1) for rule.*

6. Policies and Procedures

- Board does not have price discrepancy policy on file.

- The board has three credit cards, AMEX, Wal-mart, and Sam's Club, for board and store expenses. The general manager is the only authorized person to use the AMEX card. The office manager is authorized to use the Wal-mart and Sam's Club credit cards. All credit card expenses were supported by original receipts.

Recommendations:

- Adopt a price discrepancy policy. While it is true that the State has uniform pricing requirements, if a shelf tag is incorrect and shows a lower price than the register, it is good customer relations to honor it and just book the difference to cash over/short. The Commission will provide a sample policy upon request. *Refer to Appendix B (2) for rule.*

- Adopt a credit card use policy. Include a maximum limit allowed on purchases before a board member is notified for approval. Board approval is required for all purchases over the limit. All purchases must be pre-approved by the finance officer. Once adopted, submit a copy to the Commission. Procedures for the usage of the credit card shall include:

- What types of items the card may be used for,
- Personal usage is not allowed,
- A detailed receipt for every transaction is required,
- Who has authority to use the card.

7. Administrative Compliance

- Board meeting minutes were viewed and followed the order of proceedings for conducting business meetings. Minutes should reflect that the meeting has been called to order, a record of attendees, approval of the minutes of the last meeting, any votes taken and how members voted, policies adopted, and any other business presented in sufficient detail so that anyone reading the minutes can understand what transpired.

- Law enforcement contract has not been adopted and filed with the Commission.

- Board information on the Commission website does not reflect board members' latest appointment date. Board member compensation meets the current statutory requirements.

- When approving for store and office supplies, purchase orders are not used. The pre-audit certificate is placed on all liquor bills.

- Nepotism – The board does not employ immediate family members.

- All board members have attended the mandatory ethics training.

Recommendations:

- Adopt a law enforcement contract and file with the Commission.

- Update board information on the Commission website to reflect current appointment dates.

- Use purchase orders for ordering all store and office supplies. Purchase orders are required to have the pre-audit certificate signed by the finance officer. *Refer to Appendix B (3).*

- Affix pre-audit stamp to liquor order, not invoices. Approval should take place before the liability is incurred.

8. Personnel/Training Compliance

- Training is conducted when need arises and whenever new information is available.

Recommendations:

- Attend annual training, such as the Responsible Alcohol Seller Program, offered by the Commission and other approved venues. Create a checklist for use in training new and existing employees and have each employee sign it once training is completed.

9. Internal Controls

- Employees refer to a calendar made by the office manager for scheduling purposes. The finance officer and general manager rely on the calendar to determine when employees have signed in or out for work. The procedure for verifying time entries is for all employees to sign the calendar. Often times, the employees do not sign.

- A deputy finance officer has not been appointed.

Recommendations:

- Have employees review and sign all time records to verify accurate time worked. To ensure better internal controls, have the manager and finance officer sign time sheets.

- Appoint a deputy officer to aid in the duties of the finance officer when he/she is absent.

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Chart 1

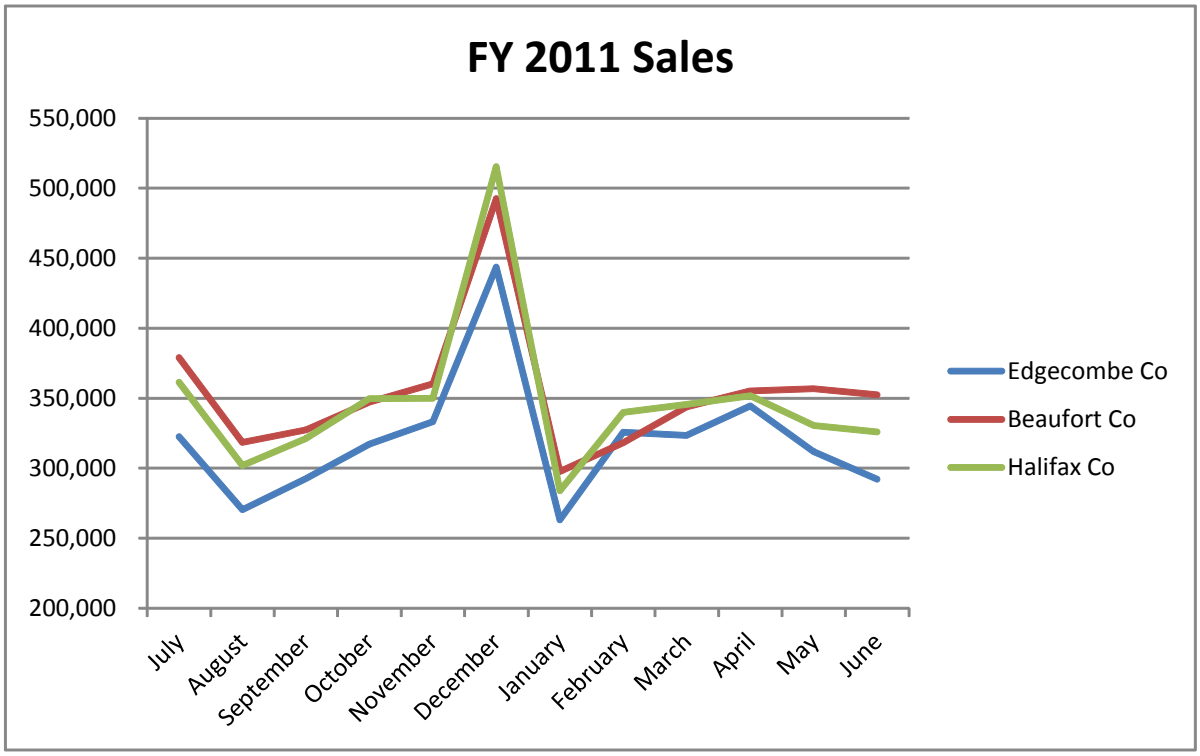

Chart 1 shows current year sales for similar boards

Chart 2

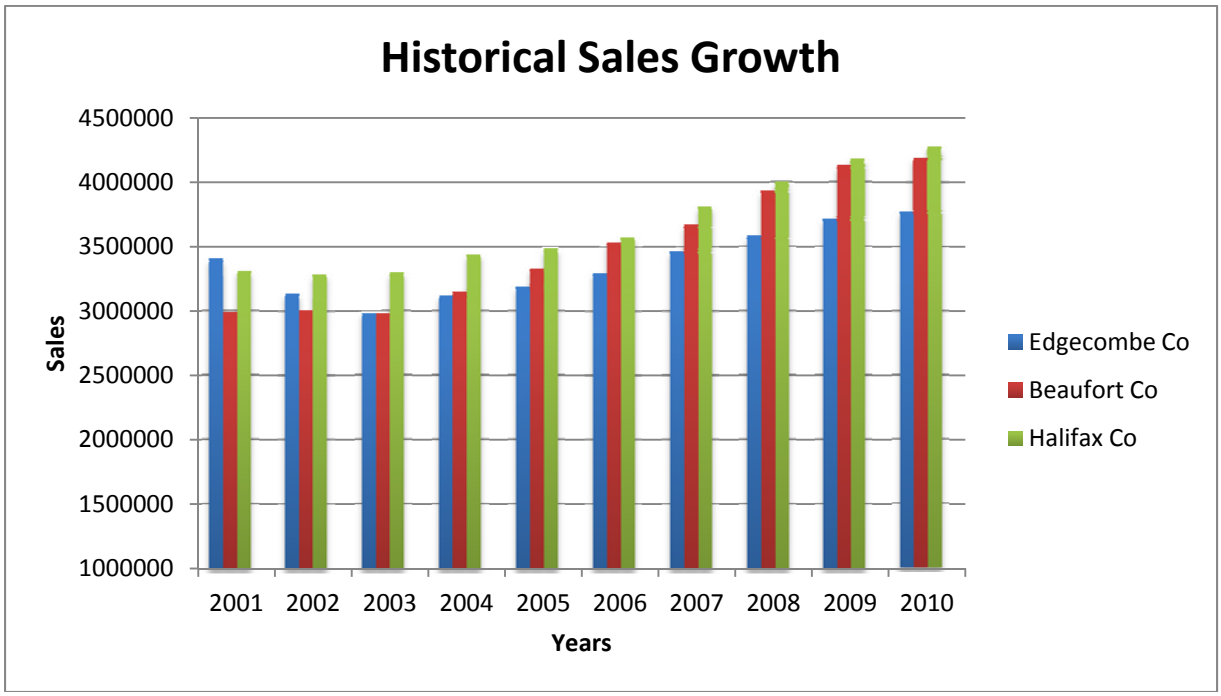

Chart 2 reflects the historical sales growth for similar boards for the past ten years.

Chart 3

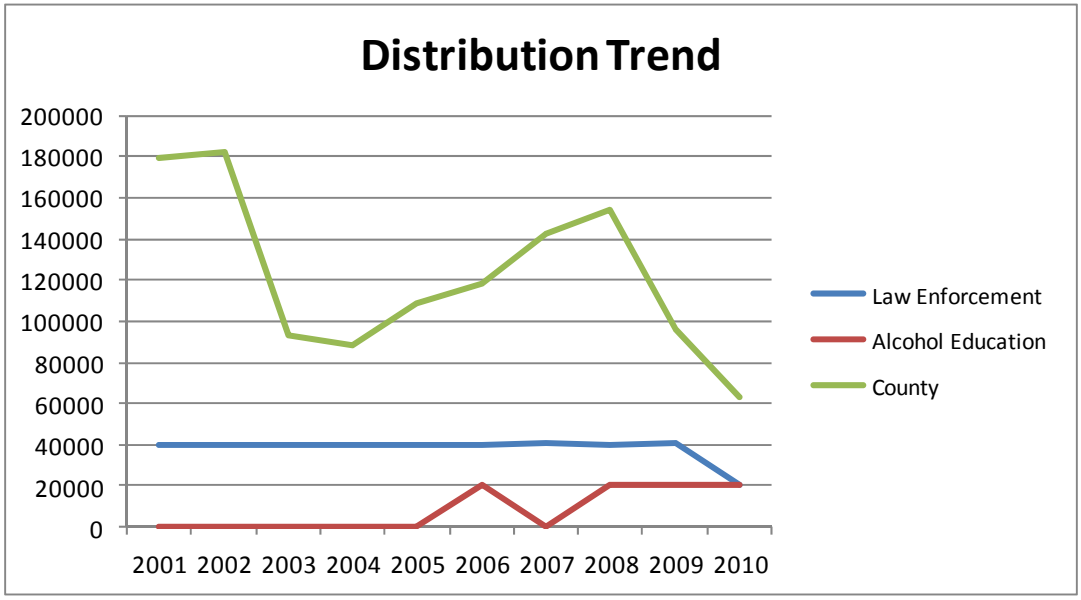

Chart 3 shows the downward trend of profit distributions to the appointing authority, law enforcement, and alcohol education.

Chart 4

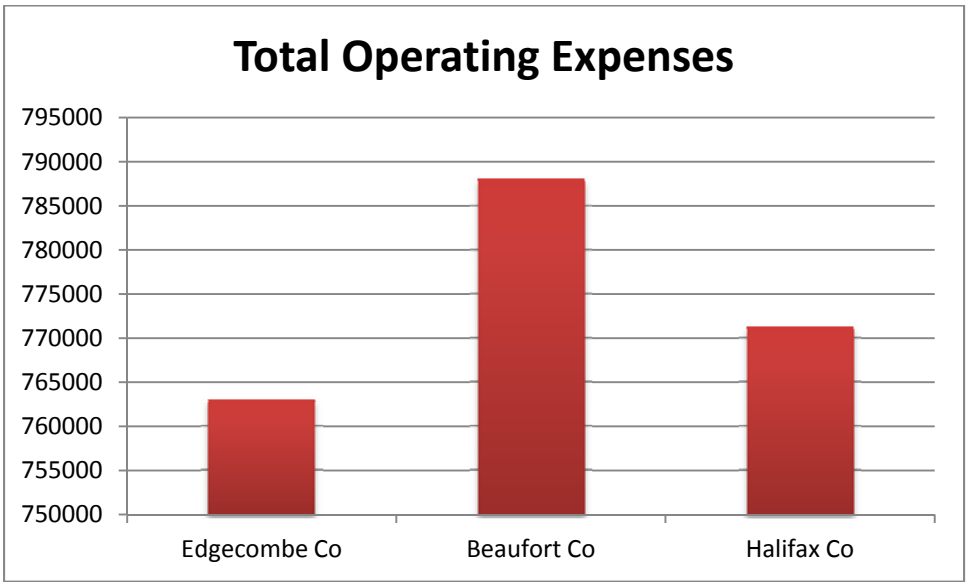

Chart 4 reflects total operating expenses for similar boards.

Chart 5

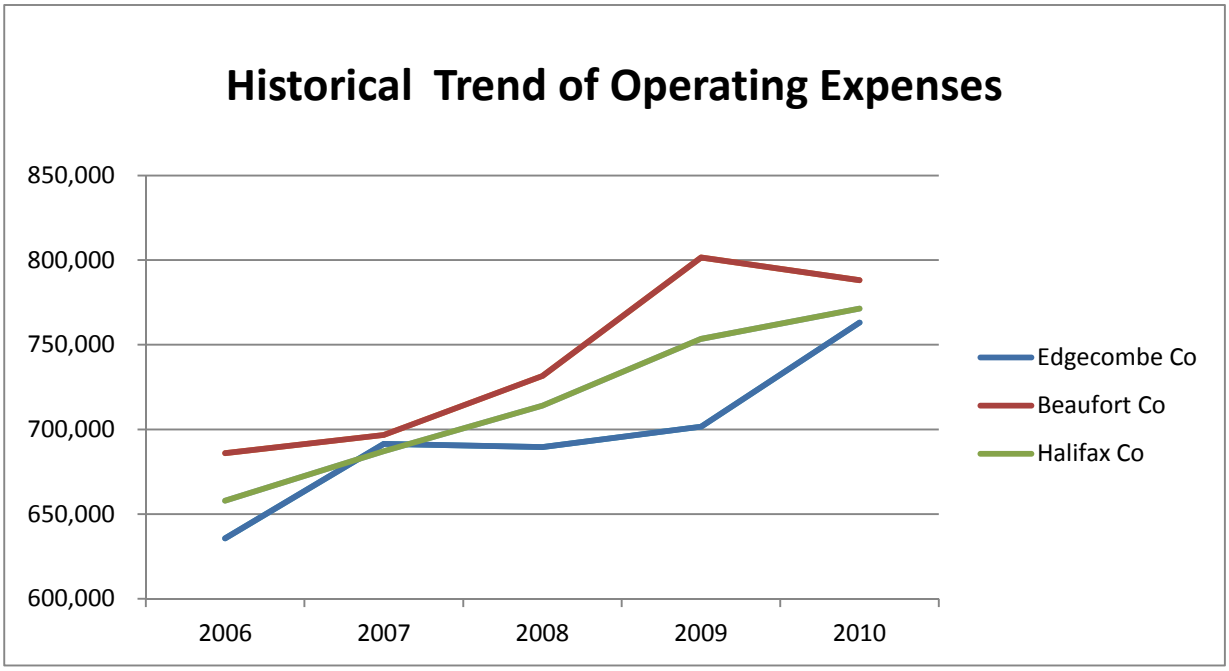

Chart 5 reflects the historical trend of operating expenses for similar boards.

Chart 6

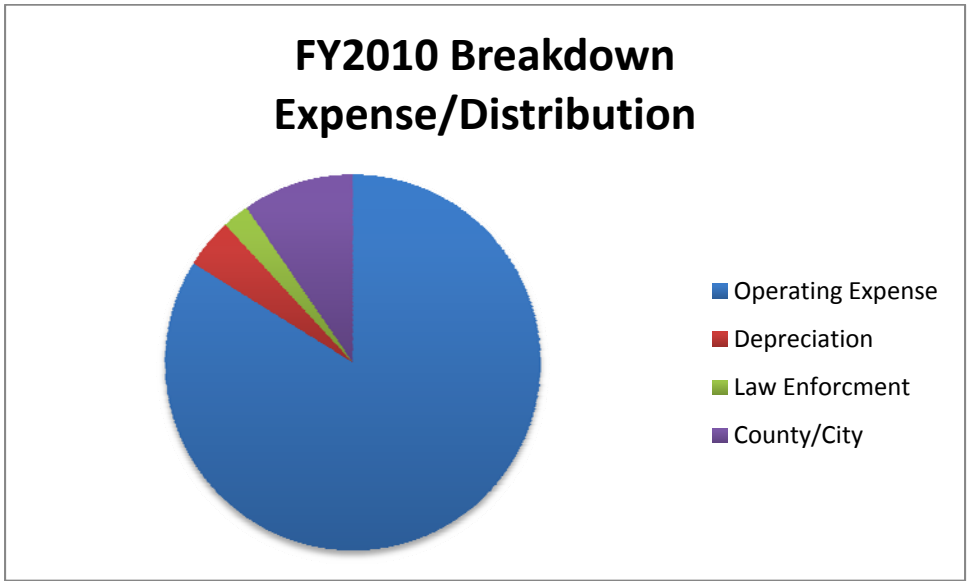

Chart 6 reflects the percentage of operating expenses from gross profit of sales.

Chart 7

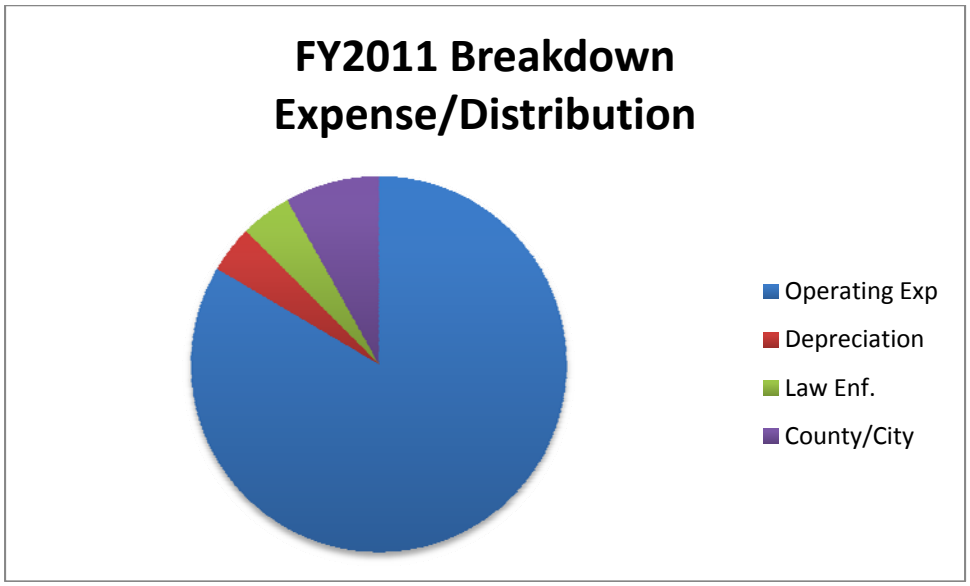

Chart 7 reflects operating expenses and distributions from gross profit of sales.

APPENDIX A

Picture 1

Illustration of parking lot in Rocky Mount, NC.

Picture 2

Illustration of shelf management system.

Picture 3

Illustration of shelf management system.

Picture 4

Illustration of high demand for products.

APPENDIX B

(1) NCAC 02R.1711(a) states "Each local board shall establish and maintain a shelf management plan. The board shall establish policies within its plan that govern the following concepts:

(1) Set the higher price items on the upper shelves at eye level and set the lower price items on the bottom shelves;
(2) Block categories in vertical sets per their category;
(3) Arrange bottle sizes so they increase left to right of the same item;
(4) Create brand billboard by stacking all brand sizes together;
(5) Set the shelf space for a product equal to market share for the individual store after the product has been carried for a year;
(6) Set and maintain all bottles at the front of the shelf; and
(7) Discontinue low profit slow moving items.

(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-audit in the manner required by GS 18B-702."

_____

(Signature of finance officer)

EDGECOMBE COUNTY ABC BOARD
P. O. DRAWER 398
TARBORO, N .C. 27886

Moniqua McLean
ABC Board Auditor
ABC Commission
North Carolina

RE: Performance Audit Response

Dear Ms. McLean,

It was with much pleasure to meet you as the State of North Carolina's ABC Commission's board auditor. We feel that we have learned a lot about the structure and the organizational expectations of the ABC boards in the state of North Carolina.

I would like to address your recommendations as listed in your audit.

- Inventory Turnover - Weekly deliveries for target at 6 times per year and Edgecombe County turnover rate was 5.7. This is partially due to the fact that this is a geographically large county and we have 6 stores to accommodate the public. When our stores were established, they were located conveniently for public access by the small towns and also one store in the Tarboro and East Rocky Mt. None of these stores are located near a by-pass or interstate highway to pick up out of town sales. We serve our public and none of the stores are in the red.
- Operating Costs – The board operating cost ratio of .80 compared to the average of the similar sized boards that we were compared to with a .67 ratio does not sound like a fair comparison as we stated to you at our board meeting. Edgecombe County has very little mixed beverage, no mall or brand name stores, limited restaurants and no major tourist attractions as the counties we were compared to. We think this figure would be better compared to some other counties with more similarities. Salaries have been the same for 4 years in this county. We are diligent in pricing our supplies and operational needs. Our board does not allow all members to attend the conferences and conventions, one or two is the absolute most that ever travel. Our board has stated their position to you that the small cost of travel for the NC Association of ABC Boards is minimal and the same as other boards that have board members on the association board. The board has agreed with you totally and has voted to cancel the OPEB benefits for future employees and was effective July 1, 2011. As for the profit percentage to sales, this figure has dropped during the slump in the economy over the last 5 years. Edgecombe County has maintained one of the highest unemployment

rates during this time. Businesses have closed and many have been laid off and no work is available.

- Profit Percentage to sales - As for sales strategies, Edgecombe County has surpassed the imagination of many with the strategies that we have used to promote our products, advertising for requesting of products, recipes, buying small quantities of most new brands to appeal to the public, decorating our stores with seasonal decorations and keeping adequate stock. We recognize that the Rocky Mt. and Tarboro stores are our most profitable stores, but the other stores are not losing money, or in the red, and it would be devastating to the small towns to close these stores and put even more of a burden on the local residents. This would be bad for our sales and a hardship for our small communities.
- Working capital - met the goal set.
- Store Appearance – The message to ABC Boards at the supervisor meeting introduced the shelf management plan in March of this year. With all the incoming mails and demands on supervisors with the changes in operations, the shelf management program had been started in this county but was not completed. This was only about two month's time between learning of the program and having the audit. Lighting in the stores was recommended but the cost of that project is more than this board wanted to spend at this time due to some repairs that are necessary.
- Administrative Compliance – Minutes were in good order, but the law enforcement contract is being negotiated between the board and the sheriff. Board appointments dates have been updated on the state web page. A price discrepancy policy was approved by the board and noted in the minutes as now board policy. The board also adopted a credit limit, without their approval, of $500 for supplies and $1000 for equipment and documented it in the minutes and accepted as policy.
- Personnel Training - Ms. Rogers said she had talked with the state and was planning a training session for all employees in the fall.
- Internal controls – Ms. McLean provided a blank form for purchase orders that Ms. Rogers accepted at the purchase order form for the office. The timesheets and store schedules are not being singed by each employee and approved by the manager before being turned in to the office. This problem has been corrected and time sheets and schedules are now being signed by employees and the store manager. Ms. Peggy Hyde was appointed as the deputy finance officer at the July meeting and documented in the minutes.

Having completed these requests by Ms. McLean at the July board meeting and documented in the minutes, the only item outstanding is the contract renewal between the Edgecombe County ABC Board and the Edgecombe County Sheriff's department. The board attorney is writing the contract when negotiations are completed.

Ms. McLean also visited the six stores in Edgecombe County and talked with our employees. We would like to also share some the stories of the history and survival of this ABC board over the last 12 years and the hardships and successes that we have had:

The flood in Edgecombe County in 1999 completely flooded the Tarboro store, the warehouse and the office and all products, supplies, vehicle and equipment. It was the diligent employees that valued their jobs that worked hours, days and weeks to help this county's ABC board survive. Senior employees retired and were not replaced, warehouse manager was not replaced and the duties were taken over by the office staff and a part time delivery helper. The six stores, office and warehouse were then operated by 8 full time employees and 14 part time employees with the office staff working some shifts to manage the stores. The board had previously operated with 20 plus full time employees.

The Princeville store was a rental building and because of the flooding was not opened again for a few years. The shelving and counters were purchased and installed in the store by ABC employees and part time help was hired for clerking and reopened in 2003.

Edgecombe County has suffered, as all counties, with the economy and declining sales. Any and every idea that could be thought of was used to improve the quality of shopping experience, the appearance of the grounds and inside the stores and training personnel to display their southern hospitality to all individual that frequented or passed through our stores. We provided slide shows on a television in each of our stores to show the bottle and sale price of each SPA sale price on a monthly basis until the number of products increased so much that our program would not accommodate the load. We also made generic recipes and printed them for the customers to enjoy, especially around the holidays. We have an upside down Christmas tree that is displayed in our Tarboro store every year that is always recognized by the local newspaper as a front page item during the week of Christmas and loved by our patrons.

The Pinetops store has recently been remodeled because of wall and floor deterioration. The shelving and flooring were contracted out, but the floor repairs, all tearing down old shelving, woodwork, painting, staining and moving the products around during the job was handled by one part time contractor and ABC employees. In the two months that it took to accomplish this job, the store was never closed one business hour. Many nights and weekends of hard work was accomplished by the employees. The Pinetops store has been a special project for the past two years. Many new products have been added, a few bottles at the time, many VAP products have been ordered and stocked and at lease one or two bottles of all new products are always placed on special display area to make customers more away of their available products. This has been very successful and has gained some new customers and also made the locals want to shop in their hometown. This is now our project in all our small stores to increase the products, manage the inventory levels well, and improve the appearance as best we can with the least cost.

We appreciate the opportunity to have worked with this audit and learn what we can do to improve the Edgecombe County ABC Board and appreciate your approach that we had helped you in future audits by listening to us and our views of the struggles with small boards and making profits in this difficult time.

Thank you for your time and you are always welcome to visit with our ABC system and hope you can understand the time and effort we put in to surviving our difficult times.

Sincerely,

Linda Rogers
General Manager
Edgecombe County ABC Board

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OCT 06 2011
NC ABC COMMISSION

RECOMMENDATION	REQUIRED BY STATUTE	IMPLEMENTATION STATUS
Store Appearance – Improve lighting in Whitfield and Princeville stores. Develop an shelf management system that adheres to current marketing strategies of the industry.	☐ **Yes** ☑ **No**	(Please provide documentation supporting implementation status.) ☐ Fully Implemented ☑ Partially implemented 50% complete. (Explain below.) ☐ Not implemented (Explain below.) The Board is in the process of implementing a shelf management system in all the stores. The cost of implementing new lights for the mentioned stores is more than what the board is able to spend.
Policies and Procedures – Adopt a price discrepancy and a credit card policy.	☐ **Yes** ☑ **No**	(Please provide documentation supporting implementation status.) ☑ Fully Implemented ☐ Partially implemented _____% complete. (Explain below.) ☐ Not implemented (Explain below.) The Board has adopted a price discrepancy policy and a credit card policy. Both have been noted in the minutes.

RECOMMENDATION	REQUIRED BY STATUTE	IMPLEMENTATION STATUS
Administrative Compliance – Adopt a law enforcement contract and submit to the Commission. Update board member appointment dates on the Commission website. Use purchase orders when ordering store and office supplies	☑ **Yes** ☐ **No**	(Please provide documentation supporting implementation status.) ☐ Fully Implemented ☑ Partially implemented 50% complete. (Explain below.) ☐ Not implemented (Explain below.) The Board is currently negotiating a law enforcement contract with the sheriff. Board member appointment dates have been updated. *(Fully implemented)* Purchase orders provided by the auditor have been used for ordering supplies. *(Fully implemented)*

Personnel Training – Have employees attend annual training.	☐ **Yes** ☑ **No**	(Please provide documentation supporting implementation status.) ☐ Fully Implemented ☑ Partially implemented 50% complete. (Explain below.) ☐ Not implemented (Explain below.) A training session has been scheduled in Fall 2011.

RECOMMENDATION	REQUIRED BY STATUTE	IMPLEMENTATION STATUS
Internal Controls – Have all employees verify and sign time sheets before submission to the finance officer.	☐ **Yes** ☑ **No**	(Please provide documentation supporting implementation status.) ☑ Fully Implemented ☐ Partially implemented _____% complete. (Explain below.) ☐ Not implemented (Explain below.) Time sheets are currently signed by all employees and verified by store managers of hours worked.
Internal Controls (continued) - Appoint a deputy finance officer to aid in duties of finance officer whenever he/she is absent.	☑ **Yes** ☐ **No**	(Please provide documentation supporting implementation status.) ☑ Fully Implemented ☐ Partially implemented _____% complete. (Explain below.) ☐ Not implemented (Explain below.) The Board has appointed a deputy finance officer and was verified in the August board meeting minutes.