

Office of the
LEGISLATIVE AUDITOR GENERAL
State of Utah

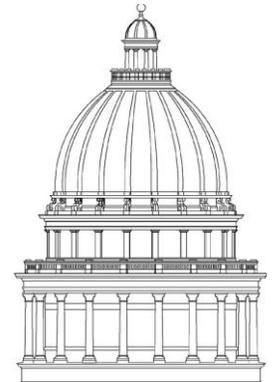
REPORT NUMBER 2012-04
January 2012

A Performance Audit of DABC Oversight of Package Agencies

This report addresses the management of package agencies by the Department of Alcoholic Beverage Control (DABC). This audit was requested in response to the audit released in May, 2011 regarding a \$300,000 loss from a closed package agency in Eden, Utah (Eden audit report). We found that the problems associated with the Eden Package Agency were not isolated, but DABC has strengthened controls over package agencies since the Eden audit. DABC can further improve the oversight of package agencies by formalizing its new practices into written procedures and considering some other changes. Because of the risks associated with DABC operations, we recommend that an internal audit division be established at the department.

Package Agencies Are Retail Liquor Outlets

Package agencies are retail liquor outlets operated by private persons under contract with DABC for the purpose of selling packaged liquor or wine to the general public for off-premise consumption. This audit focuses on package agencies that are on consignment, meaning the state owns all or part of the inventory the package agency sells. Non-consignment package agencies purchase their own inventory and are not subject to DABC audits. Currently, there are thirty-one package agencies on consignment in Utah. The



The problems associated with the Eden Package Agency were not isolated, but DABC has strengthened controls over package agencies since the Eden audit report.

Package agencies are retail liquor outlets approved by the DABC Commission.

total consignment value for these package agencies is \$1,059,748. This represents a substantial liability to the state if package agencies are not managed correctly.

Package agencies are approved for the purpose of selling alcohol by the DABC Commission. *Utah Code 32B-2-601(1)(a)* states:

The commission may, when the commission considers proper, issue authority to operate as a package agency by directing the department to enter into a package agency agreement with a person to sale, offer for sale, or furnish liquor in sealed containers from premises other than those owned or leased by the state.

Package agencies are further categorized by the DABC Commission in administrative rule. The five types of package agencies are defined in Figure 1.

Figure 1 There Are Five Types of Package Agencies in Utah.

Administrative Rule R81-3-1 defines the five types or classifications of package agencies.

There are five types of package agencies. This audit focused on type-2 and -3 consignment agencies.

Type 1	A package agency under contract with the department which is operated in conjunction with a resort environment (e.g., hotel, ski lodge, summer recreation area).
Type 2*	A package agency under contract with the department which is in conjunction with another business where the primary source of income to the operator is not from the sale of liquor.
Type 3*	A package agency under contract with the department which is not in conjunction with another business, but is in existence for the main purpose of selling liquor.
Type 4	A package agency under contract with the department which is located within a facility approved by the commission for the purpose of selling and delivering liquor to tenants or occupants of specified rooms which have been leased, rented, or licensed within the same facility. A type 4 package agency shall not be open to the general public. A type 4 package agency may also sell liquor other than in a sealed container (i.e. by the drink) as part of room service.
Type 5	A package agency under contract with the department which is located within a winery, distillery, or brewery that has been granted a manufacturing license by the commission.

* Type-2 and -3 package agencies may operate with liquor that is on consignment from DABC.

State law and DABC Commission rules allow DABC to supply initial or base inventory (consigned inventory) to a type-2 or -3 package

agency. Package agents use the funds generated from the sale of merchandise in the base inventory to purchase replacement stock.

Oversight of Package Agencies Has Improved Since Eden Audit

Although problems existed in other package agencies besides Eden, we found that oversight has improved since our May 2011 audit report. It should be noted, however, that the problems at other package agencies were not as serious as those at the Eden package agency. In the Eden audit report, we concluded that DABC exercised poor management and contributed to the state’s financial loss.

Problems Existed With Package Agencies Other Than Eden

In addition to Eden, other package agencies were experiencing on-going problems. Consignment package agencies are required by rule to have a biannual audit by DABC personnel. These audits identify whether a package agency can fully account for its consignment inventory. The combined value of a package agency’s liquor inventory and agency funds must equal or exceed its consignment value; if it does not, the audit will identify a shortage amount. Prior to the Eden audit, there were a number of package agencies whose audits reported shortages, yet DABC failed to take appropriate action. Five of these agencies are shown in Figure 2.

In addition to Eden, other package agencies were experiencing on-going problems, but none were as significant as Eden.

Figure 2 Audit Shortages Reported at Five Package Agencies Between January 2007 and April 2011. Prior to the Eden audit, DABC audits frequently found shortages at some other package agencies, but no immediate action was taken by DABC.

Package Agency Number	Number Short / Total Audits	Average Amount Short
102	6 / 10	\$ 6,728
123	6 / 8	5,695
151*	4 / 7	2,318
166	7 / 9	7,373
173	5 / 10	8,152
Average		\$ 6,053

* Agency 151 is a type-2 consignment package agency while the others are type-3 consignment package agencies.

Despite repeated shortages found in some package agencies, we could not identify any immediate corrective actions taken by DABC to control for shortages before the Eden audit report.

As shown in Figure 2, several package agency audits reported shortages on multiple occasions between January 2007 and April 2011. Despite the repeated shortages found at all five package agencies, we could not document any immediate corrective actions taken by DABC to control shortages. The recurring nature of the shortages highlights the importance of developing written policies and procedures to identify actions that should be taken to remedy current shortages and prevent future problems.

Figure 2 shows that the average shortage amount among select agencies over this period, ranged from \$2,318 to \$8,152. The range of individual agencies was even greater, with one package agency reporting shortages that ranged from \$8 to \$39,718. This wide range in shortages suggests that DABC's written procedures should indicate when shortages are significant enough to warrant corrective action by DABC. Figure 2 also shows that some package agencies did not receive their biannual audits as required by rule. For example, from January 2007 through April 2011 each package agency shown should have had at least eight to nine audits, but package agency 151 only had seven audits. Despite the continued absence of written policies for handling shortages following the Eden audit report, DABC has made a number of positive changes that have strengthened package agency oversight.

DABC Has Improved Oversight of Package Agencies Since the Eden Audit Report

Since the Eden audit report, DABC has assigned responsibility for oversight of all type-2 and -3 package agencies to an audit manager (instead of regional managers who also oversee the state liquor stores). Among other duties, this individual is responsible for ensuring that biannual audits are conducted in accordance with rule and that audit results are acted upon.

New Practices Have Been Implemented Regarding the Oversight of Package Agencies. DABC has instituted many new practices to help reduce the potential risk of the state losing money due to package agency shortages. According to DABC, if a package agency is found short in an audit, the DABC director is notified and a follow-up audit occurs in the next few weeks. If there is still a shortage after the second audit, then the following occurs:

- All shipments and transfers to the package agency are stopped until the shortage is resolved
- A letter is sent to the package agency alerting the operator that shipments have been stopped and stating the amount of payment required
- The package agency's consignment amount is reduced by the amount of the audit shortage
- The DABC Commission is notified at the next commission meeting.

We believe the new practices reported by DABC provide a much better response to audit shortages than have previously occurred. However, these policies must still be formalized in written policies and procedures.

We are concerned about one of the new practices regarding the reduction of consignment. Reducing consignment forces a package agency to either purchase inventory itself or reduce the inventory available to patrons. A lower consignment reduces the state's risk, but it could hinder the package agency's ability to operate efficiently and provide product to the public. Rather than reducing the consignment allowance for every shortage, the DABC Commission may need to develop procedures to address agencies with chronic shortages that may include possible replacement of the agency operator. In fact, current policies state that DABC may close substandard package agencies based on an annual review that includes a number of factors including compliance with state laws, rules, and procedures.

A Recent DABC Audit of a Package Agency and Subsequent Actions by the Department Show Improvements. The more assertive actions taken following a recent audit of one package agency illustrate the strengthened controls over consignment package agencies. As shown earlier in Figure 2, agency 123 was short on six of eight audits from January 2007 through April 2011, yet no action was taken to correct for these shortages. Figure 3 shows the results of the most recent audit conducted in November 2011.

Since the Eden audit report, DABC has implemented new practices to improve the oversight of package agencies.

The DABC Commission may want to consider terminating contracts with vendors that are chronically short instead of reducing consignment for isolated incidents.

Figure 3 A November 2011 Audit of Package Agency 123 Found a Shortage of Over \$12,500. The recent audit resulted in immediate action to correct the shortage.

Inventory in stock	\$ 36,085.24
Amount in bank, agency, credits, transfers	46,105.96
Subtotal	\$ 82,191.20
Less Outstanding Shipments*	(43,753.64)
Total	\$ 38,437.56
Less Consignment	(51,000.00)
Shortage	\$ 12,562.44

* Outstanding shipments accounts for inventory orders (since their initial consignment) that the package agency has not paid the DABC for.

A November 2011 package agency audit and subsequent actions taken by DABC illustrates oversight improvements.

Unlike prior practice where shortages were not followed by action from DABC, this recent audit provides an example of how package agency oversight has been tightened. When agency 123 was found to be short by \$12,562 in an audit dated November 29, 2011, DABC stopped all inventory shipments to the agency until December 12, 2011 when the debt was paid in full by the agency’s operator. DABC resumed inventory shipments, but reduced the agency’s consignment level from \$51,000 to \$38,438, the same amount as the shortage. These tightened practices have been consistent in every audit where shortages were found since the Eden audit report was released in May 2011.

In total, six different package agencies had an audit shortage since the Eden audit report. As previously noted, however, none of these audit shortages compare to the severity of the Eden package agency in the amount of money involved. Furthermore, in all instances, except for one \$479 shortage, DABC took immediate steps to stop shipments and resolve the shortage. DABC now has practices in place to take corrective action when a package agency is found short, but it needs to formalize and adopt these oversight mechanisms in written procedures.

Oversight of Package Agencies Could Further Improve

DABC’s oversight of package agencies has improved since the Eden audit report, but oversight weaknesses still exist. Five issues are discussed in this section. First, a number of instituted oversight practices need to be stipulated in written policy or procedure. Second,

DABC needs to clarify and enforce its ongoing reporting requirements from package agencies. Third, DABC should consider a written procedure for how it establishes and adjusts consignment levels for package agencies. Fourth, DABC should consider extending the covert underage buyers program, currently used at state liquor stores, to package agencies. Fifth, we evaluated the feasibility of requiring package agencies to remit funds daily, but determined that the current consignment structure would not be amenable to daily remittance.

Package Agency Policies and Procedures Need to Be Updated for New Practices

As previously discussed, DABC has instituted many new practices to help reduce the potential risk of the state losing money due to a package agency's failure. These new practices need to be formalized into written policies and procedures to help ensure that they continue and are consistently applied.

These practices were primarily developed by the audit manager who previously oversaw package agencies. This employee is no longer with DABC and we are concerned that the current controls may be diminished if the next audit manager operates differently. The DABC Commission should ensure that the department stipulates in policies and procedures the requirements for consignment package agencies' oversight to ensure consistent application, regardless of employee turnover. This would also help communicate to package agencies what is expected of them.

The policies and procedures for type-2 and type-3 package agencies need to be updated. Type-2 package agencies' policies and procedures have not been updated since 2005; the same documents for type-3 package agencies have not been updated since 2009, even though substantial changes were made to oversight practices after the Eden audit report was issued in May, 2011. DABC should keep these documents up-to-date and ensure that package agencies have the latest versions.

DABC Should Clarify and Enforce Reporting Requirements from Package Agencies

DABC staff recently sent a letter to all consignment package agencies, changing some important reporting requirements. The audit

The DABC Commission should ensure that the department stipulates in policies and procedures the requirements for consignment package agencies' oversight to ensure consistent application, regardless of employee turnover.

A DABC employee changed reporting requirements for package agencies without the consent of the commission or director.

manager told us he canceled the reporting requirements because the information submitted was not being used by DABC. We are concerned both because the individual did not have the authority to cancel the requirements and because the reports provide valuable information that DABC could use to help ensure package agencies are effectively managed.

The former audit manager responsible for overseeing package agencies sent a letter to all consignment package agencies stating that the following reports were no longer required to be submitted to DABC:

- Quarterly inventory counts
- Daily sales record of all liquor sales
- Licensee sales log

It is concerning that this change was sent to package agencies without the knowledge of the DABC director or the commission. The change is especially concerning because the daily sales record is required in the package agencies' contract in order for them to be covered by Risk Management. Furthermore, the daily sales record is required by DABC Commission rule. DABC staff does not have the discretion to ignore a commission rule.

Discontinuing the required reports reduces the information available to help DABC manage consignment package agencies effectively. Discussions with DABC personnel revealed that quarterly inventory counts and daily sales records, two reporting requirements canceled by the previous audit manager, help maintain oversight between audit visits and track daily sales.

For example, according to existing policy, the quarterly inventory count must be taken after the close of business on the last Saturday of designated months. This inventory report could be used in conjunction with a complete bank statement (which is required at the end of each month) to determine whether a package agency may have a potential shortage. If it appeared that a shortage might exist, DABC could take steps to ensure there was not a serious problem.

We think DABC needs to clarify what reports it needs from package agencies and how they will be used by the department.

DABC needs to clarify what reports are required from package agencies and how they will be used by the department.

Clearly, DABC should not require reports that are not useful, but it appears to us that reviewing reports that have long been required could help DABC ensure a level of control between audit visits. Rather than cancelling reports, DABC needs to develop procedures for using them.

DABC Commission Should Consider Formalizing Consignment Practices for Package Agencies

The DABC Commission should consider formalizing its practices for establishing and adjusting consignment amounts. Current policy provides that consignment amounts should be based on average monthly sales. DABC staff told us the target consignment amount was a six-week supply based on annual sales. We found that consignments varied widely from the six-week target. However, we question whether a target based on annual sales adequately accounts for the seasonality of package agency business.

The current DABC practice for maintaining consignment has not been consistently applied. We evaluated current consignment levels compared to average sales and found wide variation among package agencies. Figure 4 shows a sample of package agencies whose consignment levels, maintained by DABC, are currently above and below the six-week threshold.

The current DABC practice for maintaining consignment has not been consistently applied.

Figure 4 Package Agency Consignment Amounts Vary Widely. Some package agencies have much more than a six-week consignment inventory while other have much less.

Package Agency Number	Current Consignment Amount	FY 2011 Sales	Calculated Weeks of Consignment
144	\$ 24,000	\$ 86,055	14.50
130	70,000	445,782	8.17
147	82,000	527,065	8.09
139	40,000	322,291	6.45
120	45,000	382,111	6.12
152	25,000	299,445	4.34
150	25,000	307,397	4.23
166	35,000	433,952	4.19

We question if the current consignment practice of a six-week supply based on annual sales adequately accounts for the seasonality of package agency business.

Our second concern is that a formula based on annual sales does not account for fluctuations in package agency sales. Some of the package agents we spoke with said their sales vary by season. For example, summer or December sales may be much higher than other seasons. Given this fluctuation in sales, DABC should consider whether the current formula is sufficient. Other factors might also be important to consider. For example, the frequency of deliveries from the warehouse or the type and volume of liquor sales could affect the length of consignment a package agency needs.

DABC's consignment practices should provide package agencies the product they need to be successful without unduly placing the state at risk. The DABC Commission should formalize the methods for determining how consignment values will be established and maintained in package agency policies and procedures and ensure that this method is applied consistently.

DABC Commission Should Consider Monitoring Whether Package Agencies Sell to Minors

DABC has a program to test whether state employees in state liquor stores are selling alcohol to minors. This program is called the Covert Underage Buyers (CUBs) Program. The CUBs program is used in all state liquor stores but not currently used in package agencies. Since DABC is charged with ensuring that minors do not have access to alcohol, the DABC Commission should consider extending the CUBs program, on a limited basis, to package agencies.

The DABC Commission should consider extending the department's program for monitoring illegal sales to minors.

We were told that prior DABC management did not extend the CUBs program to package agencies because DABC had no way to reward or penalize package agencies for passing or failing a CUBs test. We think DABC should consider extending this program to package agencies because it is charged in *Utah Code 32B-1-103 (4)(b)(i)* to "promote the reduction of consumption of alcoholic products by minors." Currently, local law enforcement may investigate possible sales to underage buyers on their own, but there is no comprehensive program. DABC management told us they felt the CUBs program could be extended to package agencies at little additional cost.

Daily Remittance May Be Unnecessary Under Current Structure

We also reviewed the feasibility of having consignment package agencies transfer their sales receipts to DABC on a daily basis. A daily remittance system would be appropriate because the proceeds of consignment sales are state funds. However, there are two obstacles to daily remittance. First, many package agencies have a mix of consignment and additional inventory they have purchased. Second, package agencies do not have a point-of-sale inventory system that would allow an automated calculation of the amount due. Given these obstacles, existing practices seem reasonable.

DABC currently requires package agencies to pay for inventory ordered 30 days from the previous month (e.g. the package agency pays for the previous month's shipment on a set date the following month). Using 30 day payment terms or "net 30" is a standard practice that is widely used among businesses.

Consignment package agencies are able to use the proceeds of their consignment sales to purchase additional inventory. However, some package agencies invest their own funds to supplement the consignment inventory provided by the state. This dual ownership of inventory would make a daily remittance system more complicated.

Other control states we reviewed were able to require their package agencies to remit funds daily. But, in order to do so, all inventories were on consignment from the state and all agencies used a point-of-sale system. As described above, many Utah's package agencies own inventory in addition to their allotted state consignment amounts, creating a complication. Another complication is that package agencies do not use a point-of-sale system that could accurately account for product ownership. In fact, although package agency policies "strongly suggest that each package agency maintain some type of inventory control system," it is not required.

While adopting a daily remittance payment schedule has the potential to reduce taxpayer liabilities, the present conditions make it impractical. For now, strengthening other controls such as formalizing oversight and audit procedures and enforcing needed reporting requirements should help to mitigate taxpayer liability.

Internal Audit Function Would Enhance DABC Oversight of Operations

DABC currently has an operating budget of \$29.6 million and reported inventory in the warehouse and stores in excess of \$46.6 million.

An internal audit function is warranted at DABC given the risk associated with the operations of this department. DABC currently has an operating budget of \$29.6 million and reported inventory in the warehouse and stores in excess of \$46.6 million. The total annual sales for DABC in fiscal year 2011 were \$296 million. Given the financial liability associated with the operations of DABC, we believe that an internal audit function is warranted.

DABC once had an internal audit function. A 1988 organization chart showed an internal audit division that reported to the director. The most recent organization chart shows that the audit division has been eliminated. Although several finance personnel perform limited auditing duties, these limited audits do not provide sufficient controls over major risk areas such as warehouse, retail, and transportation operations. We believe that reinstating an internal audit division would provide much needed oversight and protect those resources that pose the greatest risk of loss to the state.

An Internal Audit Division Is Warranted, Given the Potential for Loss to the State

Given the potential risk of loss in state resources and the need to reduce the health and social harm associated with irresponsible use of alcohol, an internal audit division at DABC is warranted. According to *Utah Code 63I-5*, entitled *Utah Internal Audit Act*, an agency head may establish an internal audit program if the agency administers programs that:

- 1) might pose a high liability risk to the state; or
- 2) are essential to the health, safety, and welfare of the citizens of Utah.

DABC meets the above criteria. The agency manages large volumes of valuable goods and resources on behalf of state taxpayers and is entrusted to mitigate the potential dangers of alcohol, which can have a profound impact on the health, safety, and welfare of Utah's citizens. Despite these risks, DABC is not included among Utah state agencies required by statute to have an internal audit program, Figure 5 lists these agencies.

Given the potential risk, an internal audit division at DABC is warranted.

Figure 5 State Agencies Required to Have Internal Audit Programs. According to the *Utah Internal Audit Act* these agencies shall conduct various types of auditing procedures as determined by the agency head or governor.

• Administrative Services	• Health
• Agriculture	• Human Services
• Commerce	• Natural Resources
• Community & Culture	• Public Safety
• Corrections	• Transportation
• Workforce Services	• State Tax Commission
• Environmental Quality	• Utah Courts

We believe the Legislature should consider adding DABC to the list of agencies in *Utah Code 63I-5-201* that are required to have an internal audit function. However, if DABC establishes an internal audit division, then its auditors must have sufficient independence and authority in order to be effective. DABC staff told us that the department director made the decision to eliminate the internal audit division that existed in the past. If DABC were to reestablish an internal audit division, then it could be structured to have more independence by reporting functionally to the commission. We think it is important that the commission direct audit activities. However, since the commission is part time, the auditor would need to report administratively to the department director.

Other liquor control states have successfully implemented internal audit programs. For example, Virginia has an internal audit division that is responsible for identifying risk, developing an internal control environment, and recommending business solutions that improve agency practices and enhance policies. Pennsylvania’s audit division reports directly to the Liquor Control Board, and is separate from the accounting department.

Most Resources for an Internal Audit Division Are Already Present at DABC

DABC already has most of the resources needed for an internal audit division. Under the current division of finance, DABC has a store auditing function, with four positions that hold the job title of auditor, but limited audit work is done outside of package agencies. It

We believe the Legislature should consider adding DABC to the list of agencies in *Utah Code 63I-5-201* that are required to have an internal audit division.

While most resources for an internal audit division are already present at DABC, DABC would need to ensure competency, independence, and adequate coverage of significant risks areas.

is conceivable that few, if any, additional resources would be needed to establish a formal internal auditing division if these positions were transferred. However, some structural changes would be necessary for such a transition to occur.

- A qualified director of internal auditing would be needed.
- The audit division will need to report directly to the commission.

Another important structural change will be to have the current scope of audited operations expanded. Although several personnel perform limited auditing tasks, these audits do not review major areas of risk. Retail liquor stores, warehouse, and transportation operations present significantly larger control risks than do package agencies, yet have minimal audit review. These risk areas should receive sufficient and ongoing audit review to ensure that potential control weaknesses are well managed.

Recommendations

1. We recommend that the DABC Commission ensures that the department updates its package agency policies and procedures to include:
 - Newly implemented oversight practices for conducting package agency audits and acting upon audit shortages
 - Clarifying on-going reporting requirements of package agencies and processes for enforcing them.
2. We recommend that the DABC Commission review and consider the following options to further strengthen package agency oversight:
 - Formalizing their process for establishing and adjusting consignment amounts
 - Monitoring possible violations of the law relating to selling to minors

3. We recommend that the Legislature consider adding the Department of Alcoholic Beverage Control to the *Utah Internal Audit Act* in *Utah Code 63I-5-201*.
4. We recommend that DABC develop an internal audit division that reports functionally to the Commission and administratively to the department director.

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Agency Response

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January 9, 2012

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Re: Report No. 2012-04, A Performance Audit of DABC Oversight of Package Agencies

Dear Mr. Schaff:

I have sincerely appreciated the continued presence of your audit team at DABC and the professional way they have performed this and previous audits. This audit makes some sound recommendations, and I am committed to moving forward the ones I can and working with the Legislature on the issues that require their action.

I have said many times that I believe the DABC should operate as a public trust to carry out Utah's alcohol policies and to safeguard the associated revenues. It is unfortunate that this audit was necessary after the recent incident involving the Eden package agency where the DABC did not safeguard those revenues. I am pleased that this new audit has identified some of the improvements we have already instituted and laid a framework to continue moving forward.

I recognize that the audit recommendations are directed to the Legislature and the Commission, and I cannot speak on behalf of either of those entities. However, I will address what has been done, and will be done, internally within DABC operations to address these issues.

For recommendation #1, I appreciate the work of the auditors in discovering the unauthorized changes to package agency reporting requirements that were made by a former DABC employee. When we learned of the unauthorized changes we immediately started a plan to correct them. DABC is in progress of informing package agencies they are again required to submit quarterly inventory counts and daily sales records, including licensee sales logs. In addition, agencies will be required to submit quarterly bank statements which will allow the Department to conduct informal audits to determine shortages and identify red flags. This will all

supplement the on-site audits that occur twice per year. Written notifications to package agencies of these policies and procedures will go out during the second week of January. These written policies and procedures should reduce the risk of future unauthorized procedural changes by employees and provide a reference point for continued future review and revision.

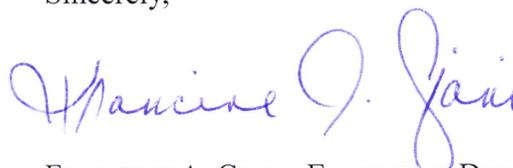
For recommendation #2, one aspect of that is already in progress. Package agencies were notified by letter in December 2011 that in 2012 the Covert Underage Buyer (“CUB”) program is being extended to package agencies. All type-2 and type-3 package agencies will receive CUB visits in 2012.

The issue of a more formal process for establishing and adjusting consignment amounts is an area where I am committed to help the DABC Commission in their discussion. Commission members have been discussing this issue for months. I believe the current Department practice of reducing consignment inventory based on shortages has established a good starting point, and I look forward to further discussions with the Commission to continue to refine the policies.

I agree with recommendation #3, and I hope the Legislature makes that change to add the DABC to the Utah Internal Audit Act. In connection with that, I also agree with recommendation #4, that the DABC Commission develop an internal audit division. However, this is the only area where I have a minor difference of opinion with the auditors. I cannot agree that “most” resources for an internal audit division are already present at DABC. While resources exist to put some personnel in place for that function, my opinion is that some additional resources are necessary to get personnel with the proper skills and abilities. In all of my assignments in state government I have believed in doing things in a fiscally sound way, but with enough resources to be successful. I hope to work through the necessary structural and budget issues during this next Legislative Session so that we will be able to report back on full implementation of this recommendation.

I have said before that I am honestly optimistic about the DABC’s future, and I believe this and other legislative audits are helping build that future. I appreciate the audit team’s work to help the DABC operate in a more transparent and accountable way.

Sincerely,



FRANCINE A. GIANI, EXECUTIVE DIRECTOR
DEPT. OF ALCOHOLIC BEVERAGE CONTROL

cc: Commission Chair Richard J. Sperry
Commission Vice-Chair Jeffrey Wright
Commissioner Kathleen McConkie Collinwood
Commissioner David L. Gladwell
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January 9, 2012

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Re: Report No. 2012-04, A Performance Audit of DABC Oversight of Package Agencies

Dear Mr. Schaff:

I am responding as the Chair of the Alcoholic Beverage Control Commission to Report No. 2012-04. Since the body of the Commission was not allowed to review the protected copy of the audit, they have not contributed to this response and all statements should be attributed to me.

As an introduction to my comments about the audit, I offer as background some history of DABC operational oversight by the current ABC Commission. Three members of the current Commission were also junior members of the preceding Commission. At least two of the three had significant concerns that the Commission was not adequately performing the operations oversight role anticipated by statute and expressed to us at the time of our appointment to the Commission. We discussed these concerns with each other but did not elevate our concerns to the entire Commission at the time. Our concerns were amplified after the revelations of the Eden package agency audit in May, 2011.

When I was named the Commission Chair on July 27, 2011, I resolved to do everything possible to ensure that an "Eden" event would not happen under my watch. The Commission was fully supportive of the resolve to renew its oversight over DABC operations – we understood this to be our statutory responsibility and our charge from Governor Herbert. However, our resolve to provide oversight was nullified after the department was reorganized three weeks into my tenure as Chair on August 17, 2011.

As the Legislature considers the future organization of the DABC, I think one question is paramount: Is an informed, empowered and engaged Alcoholic Beverage Control Commission in

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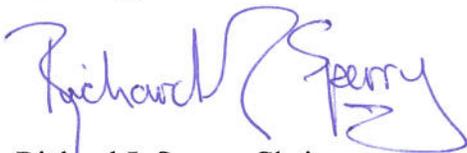
the best interest of the Citizen's of the State of Utah? If you answer affirmatively, then at a minimum two actions are required:

1. The role of the Commission must be clarified so that there is no confusion about the right, authority and obligation of the Commission to provide oversight over DABC operations.
2. Infrastructure must be created giving the commission a mechanism to gather information about DABC internal operations.

Responsibility for oversight cannot be divorced from enabling infrastructure. No oversight body can discharge its responsibilities without reliable and timely information. The current audit recommends creating an internal audit division within DABC that reports its findings directly to the Commission. I concur with this recommendation.

Finally, the Commission will work with the Department to implement the other recommendations of the audit regarding the establishment of written policies applicable to package agencies and will happily ensure that these agencies are included in the Covert Underage Buyers Program.

Sincerely,



Richard J. Sperry, Chair
Alcoholic Beverage Control Commission